

The Role Played by Microfinance Institutions on Small and Medium Enterprise Development in Uganda

Distinguished Ladies and Gentlemen

All protocols observed,

It is a privilege to speak before you this afternoon about an important topic not only for this country, but for developing countries in general. Why is this topic important? 1. Small Medium Enterprises (SMEs) are the backbone of the Ugandan economy. SMEs account for 90% of Uganda's private sector. Therefore, if Uganda is to realise the economic transformation required to achieve middle-income status by 2020, the Sustainable Development Goals by 2030 and 2040 vision, SME development must be at the core of economic strategies. 2. It's about the role MFIs, particularly those with a strong focus on technology, play in providing access to finance to SMEs to help shape Ugandans' livelihoods and exit from poverty. The financial sector, especially MFIs continue to play a critical role in bridging the gap of the "missing middle" of SMEs.

At Financial Sector Deepening Uganda we focus on making financial markets work for the underserved (many of whom are SMEs). We do so by using a market systems approach to address their needs. We seek to facilitate a shift in the way financial service providers do business so that they can develop products that are accessible, affordable and tailored for more people in the country.

We are funded by UKAid. The UK's interest in our work is to ensure that Uganda not only reduces its poverty levels, but becomes a more competitive trading partner.

Our work has allowed us to engage with policy makers, financial innovators and service providers and SMEs to encourage and adopt the use of digital financial services. We have realised that in order to adequately address poverty we need to look through a double lens of 1. the individual 2. The systems and processes needed to support individuals on their journey out of poverty.

Who is this individual?

He or she is the Ugandan citizen. The underserved mother, father, young man or young woman who needs a sustainable source of income either as a small business owner or as an employee. It is well known that Uganda has a young population with about 80% below the age of 35 years, which presents good potential for economic and social progress.

Who are the SMEs?

These are the job creators. Therefore, we need to support these SMEs to grow. MFIs have a big role to play in that growth process. Reducing unemployment rates will help address other related social problems.

Two years ago, FSDU commissioned the National Small Business Survey, with the objective of building a body of knowledge on MSMEs in Uganda.

Findings from the first survey indicated that over 15% of MSMEs are in the agricultural sector, the backbone of Ugandan economy. Access to finance continues to be a major constraint for SMEs with 7 out of every 10 identifying 'limited access to finance' and the 'cost of finance' as constraints to business growth. Commercial banks are still the dominant source of loans for these businesses with 1 out of every 2 SMEs accessing their loans from banks. Only 1 SME out of 5 SMEs indicated that they access loans from micro-finance institutions. This means there is a lot more work for MFIs to do! Uganda has several MFIs, spread across rural and urban areas and provides access to different products.

a) So the main question is, how can MFIs become more competitive than commercial banks as the lender of option for SMEs?

1. MFIs need to diversify their funding sources to development finance institutions that have lines of credit for SME on-lending. MFIs have limited access to long term sources of capital. This means that, the available sources of capital are more expensive and thus less preferred.

2. Improve their own technology and use of technology:

A) Core banking systems are expensive both as capital expenditure and to maintain it operationally (i.e. licencing, technology staff skills etc.). However, without the latest technology, it will be impossible to effectively manage clients and grow. This is a long-term investment that makes sense.

B) To be more impactful on SMEs, MFIs should leverage their interventions and support businesses that are seeking to adopt technology and innovations. If MFIs can leverage technology, such as the now ubiquitous mobile phone and mobile money, they can refine their business models, reduce the cost of credit, making their offers more affordable. With affordable capital businesses will:

- They will be more resilient during tough economic times
- Better financial reporting
- More adaptive to changing investment climate
- Better equipped for the future

Riding on this technology and the internet wave is of great necessary to improve the linkage between SMEs and MFIs, thereby enhancing affordability of finance and consequently growth of our economy and the entire country.

3. **Improve governance:** Financial systems are based on trust, I cannot stress enough how important good governance, transparency and adequate controls are. I understand there is a balance between risk management and profit maximization but we will have no financial industry if the customers do not trust us.

b. What is FSDU doing to support the financial services sector and in turn MFIs?

1. We are engaging in regulatory reform. For instance, together with government we are working on reform of regulations to allow for progressive KYC. Also, as commercial banks gear up to improve their distribution through the use of Agents the access and cost barriers that previously existent should be lowered. FSD Uganda and other development partners are working tirelessly to support the central bank and other regulators to ensure favourable regulatory landscape in Uganda. It is up to you the private sector players-with support from us-to take full advantage of these and any other developments.

2. Besides regulatory reform, like the research I mentioned above, we conduct research that helps inform policy makers' decisions about the financial sector.

3. Lastly, we provide support in the form of technical assistance to private companies that are coming up with innovative finance products that aim to improve the financial health of the masses. It is FSDU's strategic objective is to promote adoption of digital financial services by both the financial service providers and consumers.

In fact, FSDU recommends a more concerted effort by all stakeholders to embrace digital financial services. Digital financial services have made it possible to reach people who never

dreamed they could access financial services. Digital financial services is the future but the journey starts today.

Ladies and gentlemen, in closing, I would like to say that more than ever before Uganda is ripe for bigger growth opportunities, especially in financial services for products designed for the masses. With one of the youngest populations, the potential for innovations is immense, because young people are more amenable to innovation and discovery. However, we all need to play our part in helping the next generation achieve their dreams of building the businesses for tomorrow. I believe digital financial services from MFIs are going to be one of the key drivers in this quest.

We must make it work sustainably, profitably and meaningfully. Not even the sky should be the limit.

Thank You.