

Covid-19 Market Diagnostics & Options for Long Term Recovery of MSEs in Uganda

Summary of a supply-side study by **M-CRIL Limited**¹

Objectives of this study: To develop practical solutions for preserving and building relevant elements of the financial system to support the survival, recovery and growth of micro and small enterprises (MSEs) in Uganda.

Core of the analysis: To understand how the supply of finance to the MSE sector in Uganda by Tier 4 institutions – referred to here as Inclusive Finance Service Providers (IFSPs) – has been impacted by the COVID-19 crisis and options to build on measures already in place to mitigate this impact.

The analysis identified the threats and opportunities for IFSPs in meeting the financing needs of Micro & Small Enterprises (MSEs) in the country.

Sample for this analysis was determined by the willingness of Ugandan IFSPs to provide information and to conduct discussions with the M-CRIL study team on issues in their operations and financial performance resulting from Covid-19.

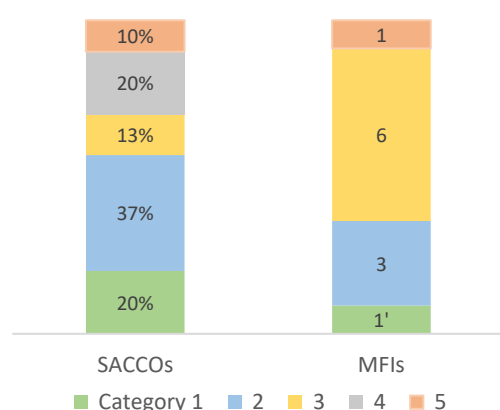
Table 1 Sample distribution – numbers of IFSPs based and operating in the Western, Central and Eastern regions – limited feedback from Northern Uganda. Two of the MFIs operate nationwide.

IFSP type	Data from...	Discussions with...
SACCOs	30	6
MFIs	11	3

With the support of AMFIU and with some direct provision of information by a few IFSPs, the M-CRIL team obtained detailed (usable) operational and financial information from 30 SACCOs and 11 MFIs.

AMFIU provided information on an anonymous basis, stating only the region in which each IFSP operates and its institutional form.

Figure 1 Distribution of IFSPs across categories



Analytical framework

M-CRIL developed a typology adapted to IFSPs from the TOR. These five categories ranged from **Category 1: Flourishing** to **Category 5: Unviable** using essentially portfolio quality and profitability as criteria. The distribution of the sample by category is presented in **Figure 1**. This distribution is indicative of the spread of the known universe of IFSPs in Uganda as shown by the extrapolated numbers in the **Annex figure** (end of page 3).

¹ This work was undertaken by M-CRIL at the initiative of and with support from Financial Services Deepening Uganda (FSDU) during August-November 2021.

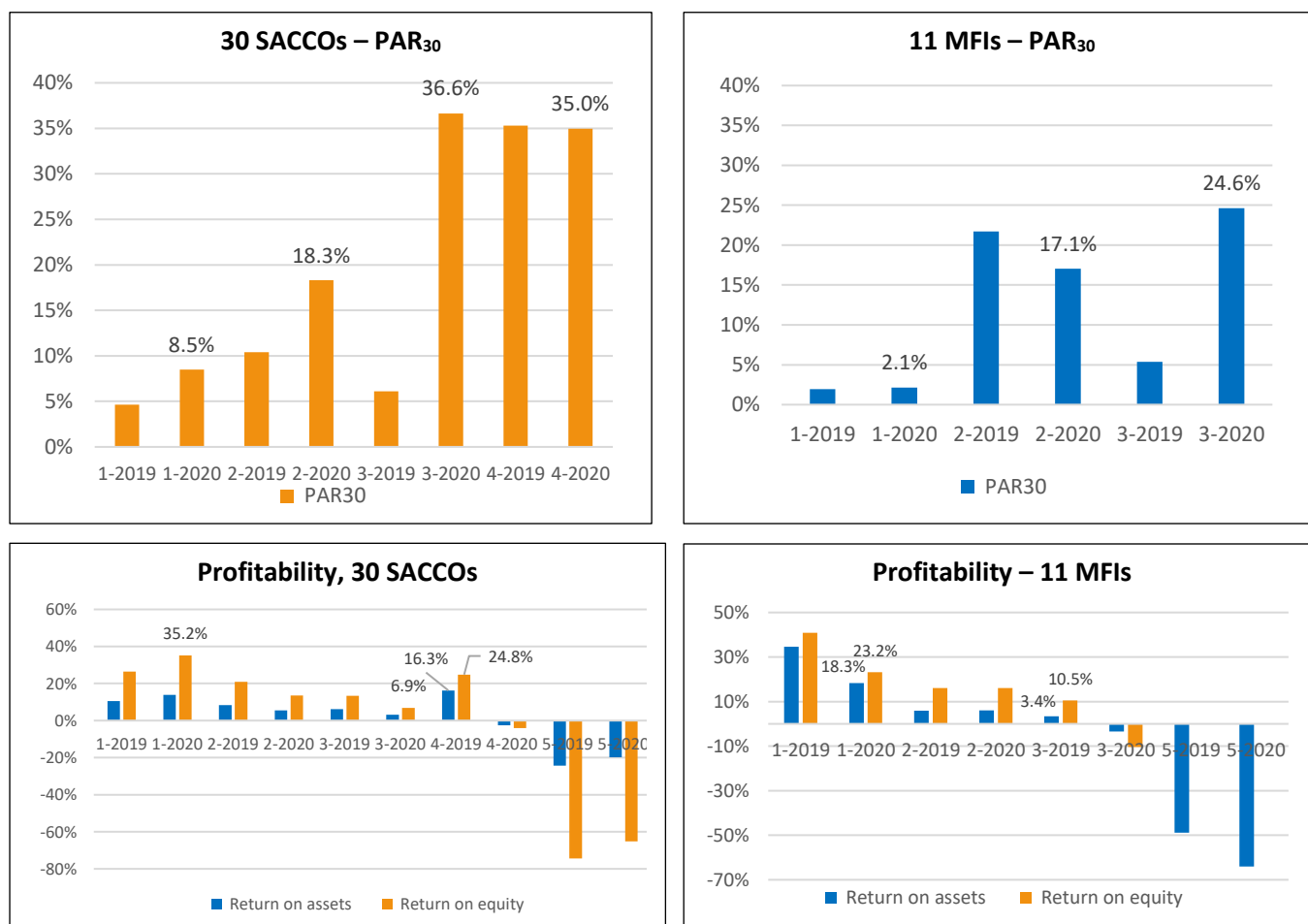
Analysis of financial performance

of sample IFSPs between pre-pandemic year 2019 and pandemic year 2020 in Figure 2 shows

- 1 Rough **doubling of portfolio at risk**, 30 days (PAR₃₀)
- 2 A **substantial reduction in profitability** as measured by return on assets (RoA)

Scattered information available for June 2021 indicates a slight improvement in performance on both ratios for SACCOs as well as MFIs.

Figure 2 Financial performance of sample IFSPs

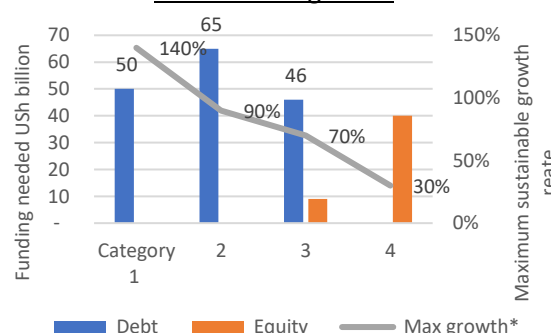


M-CRIL subjected this financial performance to a stress test for post-pandemic year 2022. Category-wise analysis of cash flows (Figure 3) shows that, at the maximum sustainable IFSP growth rates in the post-pandemic year (as determined by our stress tests)

Total borrowing requirement to support IFSPs in sustainably serving the largest possible number of MSEs would be **US\$ 160 billion** along with an **equity requirement** of **US\$ 50 billion** for some Category 3 and Category 4 IFSPs.

Total financing of **US\$ 210 bn (\$59mn)** would enable **one million MSEs to be reached by IFSPs** in a post-pandemic growth spurt **one-third of the total estimated number of over 3 million MSEs in Uganda.**

Figure 3 Funds needed by IFSPs to sustainably finance MSE growth



These estimates are based on the self-reported data available to the study team for 2019 and 2020. The likelihood of “advantageous (positive) selection” – whereby reporting to AMFIU has been by the better performing IFSPs – is quite high and may have resulted in an overestimate of the likelihood of IFSPs surviving the pandemic and an underestimate of the funds required to bring this about. It would take a more detailed assessment of individual IFSPs and better access to operational and financial information to obtain an accurate estimate of the threats to and opportunities for IFSPs in Uganda.

Conclusions and recommendations

Based on discussions with IFSP managements that interacted with the M-CRIL study team, we expect that a large proportion of the US\$59 million additional financing requirement of IFSPs will come from

- 1 **Member deposits** (SACCOs) that maintained a reasonable 9% annual growth rate during 2020
- 2 **Shareholder funds** – both SACCOs and MFIs have indicated requests to members/shareholders to increase their contributions to shore up the institution’s resource position
- 3 **Wholesale lenders operating in the local market** – Microfinance Support Centre, Soluti Finance and the Agricultural Business Initiative (ABI) have been mentioned by IFSPs as key supporters
- 4 **Wholesale lenders (international)** – Rabobank, Credit Agricole, Symbiotics – though only the best performing and managed IFSPs can expect support from them.

There is the possibility that a liquidity support facility (LSF) of the order of US\$25 million will be established under the aegis of FSDU.

Such a facility will need to be accompanied by a programme of **assessment of IFSPs for finding the right institutions to finance** and determining the right amount of financing as well as the terms of that financing by **establishing their true financial position** (rather than using the self-reported information this supply-side study has had to use).

This will include

- a **assessing the strengths and weaknesses of each potential recipient IFSP’s** governance and management capabilities
- b **designing** (if necessary) **a technical support programme** to enable the investee IFSP to improve its governance and operational functions.

To conclude, the proposed liquidity support facility from FSDU appears to have been pitched at the right size but the modalities of determining specific IFSP borrowers and designing the wholesale lending product for each one will need to be worked out carefully.

Using the funds mobilised by FSDU in an appropriately applied analytical framework is the next challenge for FSDU.

