International Journal of Economics, Commerce and Management
United Kingdom Vol. VI, Issue 11, November 2018
http://ijecm.co.uk/ ISSN 2348 0386

FAST-TRACKING PROCUREMENT OF LOCAL CONTENT IN UGANDA'S OIL AND GAS INDUSTRY: THE SIGNIFICANCE OF LOCAL SME'S CAPACITY AND REGULATORY ENVIRONMENT

Alinda Fred
Uganda Management Institute, Uganda
alindafred@yahoo.com

Alex Nduhura
Uganda Management Institute, Uganda

Edgar Agaba
National Gaming Board, Uganda

Abstract

Procuring local content in developing economies is on the surge. In Uganda, the oil and gas industry is pioneering this agenda. While sourcing local content is deemed a viable path to securing economic development across various sectors, in Uganda mystery exists as interventions put in place to boost capacity of local firms to supply local content are not yielding. This paper explores the capacity of local SMEs and the regulatory environment to ascertain the critical factors affecting Local content development with regard to SMEs' exploitation of business opportunities in the Oil and Gas Industry. Existing research points to local content indicates that there is opportunity for SMEs to supply requirements for the oil and gas sector in Uganda. However, research reveals that there is suboptimal exploitation of such opportunities by local SMEs. The objective of this study was to identify why such gap exists and how this gap can be bridge. Based on primary and secondary data on 80 local small and medium sized enterprises (SMEs) on Tullow prequalified list of suppliers and review of secondary data, significant capacity gaps particularly inadequate knowledge and experience on the complex bidding process for the business tenders in the industry are identified. These limit competitiveness of the firms and their capacity to compete with foreign firms. Capacity is further *constrained by the small nature of firms. These capacity gaps were found to significantly reduce the companies' chances of exploiting the business opportunities in the oil and gas industry. The findings of this study point to the need for Local companies to create long term credible partnership linkages with potential exporters so as to attract purchase of goods on credit to circumvent the huge capital requirements for supplies in the industry. To bridge the technical gap in bidding for supplies tenders, key players in capacity building for local content development such as Tullow need to re-focus trainings towards building technical competence of the local companies in the bidding process. This paper is critical in providing guidance in an era where Ugandan government and governments elsewhere over are developing and implementing procurement guidelines aimed at fast-tracking local content.*

Keywords: Local Content, Oil and Gas, Capacity, Regulatory Environment

INTRODUCTION

Like elsewhere in the World Oil exploration has triggered hope to Uganda, a country ranked the 21st poorest in the World (Aneki, 2010) and ranked 91 among 135 countries in respect to human poverty The country's oil resources endowment are deemed significantly sufficient to elevate to elevate her to the top 50 producers of oil in the world, and among the foremost African oil producers (Tullow Oil, 2012; 2014).However, to fully harness the benefits from the oil resource, local content is key. This is based on the general notion that the oil resource can realize value to a country, if only it can positively impact on the local economy and develop the industrial base of the country. Realizing this necessitates utilization of local resources or domestically produced goods and services (Seyed, 2013). This is what is on a general notion, widely defined as "Local Content". It is a complicated concept (Sigrid & Muhammed, 2011) and present slight variations in definition across authors and countries. For example in Ghana, it is defined as the level of using local expertise, goods and services people, business and financing in oil and gas activities (MOEMD, 2010; Warner, 2011). In a bid to develop local content of the Oil and Gas Industry, the Government of Uganda, through the Ministry of Energy and Mineral Development and through the National Oil Policy instituted number of measures. First, a regulatory framework for licensing interested companies was instituted with provisions to create a favorable regulatory environment and give priority to local companies for supplies to the oil industry. Secondly, partnerships of foreign companies with local companies in supplies are encouraged to bridge capacity gaps of local companies. In addition, foreign companies in the sector including Tullow Oil, CNOOC and TOTAL are required to employ local resources where available (MOEMD, 2010).

In addition to the interventions by Government, Tullow Oil extended capacity building to 140 locally-owned companies (25% of its supplier base) with closing-the-gap seminars, which entailed mainly providing information on the standards required by the oil and gas industry. And in line with enterprise and SMEs support, Tullow also established a $600,000 enterprise center where over 150 business local companies accessed training, mentoring and business advisory services. The center also provides insight into opportunities to work in Tullow's supply chain, and the wider sector. In addition, advisory services and training on agricultural productivity and postharvest handling were extended to farmers in Hoima and Buliisa districts (Tullow Oil, 2012). Consequently, over 300 local companies have either registered as potential suppliers or expressed interest to make supplies to Tullow Uganda.

Despite the efforts to develop Local Content, the current level of participation of local companies in the oil and gas supply chain remains unsatisfactorily. For example local companies represent a mere 25% of Tullow Oils local supplier base (Tullow Oil, 2012). This compromises the extent to which exploitation of the oil and gas resource can significantly contribute to poverty eradication and creation of lasting value to society. It calls for better strategic actions to foster entry of local suppliers into the oil and gas supply chain. Previous studies for example in Nigeria (Heum, et al., 2011; Muloni, 2011) associate local content development in the oil and gas contexts with capacity and competitiveness. These factors have been further linked with conduciveness of the business regulatory and infrastructural environment. This article explores the capacity of local SMEs and the regulatory environment to ascertain the critical factors affecting Local content development with regard to SMEs' exploitation of business opportunities in the Oil and Gas Industry.

LITERATURE REVIEW

This article leverages on capacity of local SMEs, the regulatory, infrastructural and Macro-economic environment visa-vis local content development in Uganda's oil and gas industry draws from empirical literature that associates these factors with local content development. This forms basis for literature presented in this section.

Local content development is believed to depend on capacity and competitive level of local companies compared to the foreign companies. It is assumed, that even in the face of the regulations favoring the local firms, the foreign oil companies will choose to engage local companies provided they offer higher value services in terms of cost-effectiveness and efficiency. This is in other words what can be referred to as the competitive advantage of local firms which partly leverages this study. The literature identifies factors that are crucial for competitiveness. These include; macroeconomic stability and predictability, adequacy and quality of infrastructure for business development including public utilities such transport modes, telecommunications, electricity, water supply; and supportiveness of institutions such as taxes, interest rates, exchange rate (Heum, et al., 2011). Capacity for Local Content has been oriented to financial soundness of SMES and supporting institutional framework.

In Uganda, Local SMESs, have been identified with inadequate institutions and regulations (Byaruhanga, 2011)and limited investment capital (Heum, et al., 2011; Byaruhanga, et al., 2013; Kasekende and Opondo, 2003)and inadequate financing including limited working capital, insufficient equity and expensive credit cost (Byaruhanga, et al., 2013; Abuka, et al., 2003) have characterize inadequate capacity. The challenge of limited capital and finance for investment has been confirmed in a recent study by (Heum, et al., 2011). It is also evident that SMEs in Uganda lack international quality certifications the procurement processes especially for transport and logistics supplies are complex where as the cost of production is high (Heum, et al., 2011).These challenges have also been stressed in the country's National Development Plan. The magnitude of challenges is likely to vary across SMEs depending on their age and size measured in terms of fixed assets value and investment capital. It is suggested that with time business enterprises tend to discover and develop long term survival strategies and advance from their capital developments over time. Business maturity reduces tendencies of risk averseness and crafting of risk mitigation procedures (Abuka, 2006; Humphrey, 2003; Mwakali, 2011). Many Private Sector Apex Institutions (PSAIs) have responded to the obvious needs for capacity building of the companies by educating best practices to the business community; training in fundamental business skills, calculating costs, keeping of proper accounting records and certification of skills (Byaruanga, 2011; Mwakali, 2011). Tullow oil, the oil extraction company, has taken lead in implementing the interventions towards promoting local content in Oil and Gas. The company has streamlined local content development in its operations (Tullow Oil, 2012). The company's interventions have focused on building a dynamic supplier base which can take part in the Uganda's oil industry's supply chain. The capacity building activities have entailed; closing-the-gap seminars and business development advisory services to local SMEs, provision of information to suppliers regarding available business opportunities in the oil and gas industry (Tullow Oil, 2012).

Generally, the literature evidences that SMEs need to be highly competitive to exploit business opportunities in the oil and gas industry. To realize the barriers highlighted must be addressed purposely to create a competitive business environment. Beyond this, there are also critical capacity gaps which should also be addressed. This is premised on a general consensus in literature that local content development necessitates building capacity of local firms to operate competitively and meet the high supply standards demanded in oil and gas supplies. However, issues of capacity of local SMEs, the regulatory, infrastructural and Macro-economic environment need to be further investigated in the context of Uganda's oil and gas industry where SMEs' access to business opportunities in the industry remains low amidst regulatory and capacity building efforts towards development of local content.

METHODOLOGY

This article leverages on findings generated from primary data collected on a sample of 80 Local SMEs including those which previously accessed business supply tenders at Tullow Oil and those which attempted but failed. The target companies were drawn from Tullow Oil's records, stratified into the two categories. Simple random sampling was applied to select the Company Heads and Managing Directors who formed the primary respondents for the study. These were administered a questionnaire to collect data on their SME's access to supplies tenders in the oil and gas industry, size of investment capital investment, knowledge of and experience in the bidding process. The analysis of capacity extended to the bidding regulations for which respondents shared their opinion on complexity of the bidding process, conduciveness of bidding terms & conditions. In addition respondents presented their perception of the business environment including supportiveness of production infrastructure (availability of quality and cost-effective raw materials, transport, water, electricity); and supportiveness of micro-economic environment (inflation rates, exchange rates, stability, predictability). This quantitative data was triangulated with the views of private sector associations and relevant ministry departments who were interviewed as key informants. In view of (MOEMD, 2011) such triangulation gives more valid evidences as the qualitative part helps to provide in-depth understanding of the study phenomena there by complementing the quantitative evidences. They shared an expert opinion on appropriateness of the regulatory environment for local content development; the capacity to exploit the oil and gas business opportunities and the supportiveness of the business environment to Local content in Uganda's oil industry.

Analysis of quantitative data was twofold. First, the percentages of respondents who agree or disagree with the statements elicited in the questionnaire were generated to which companies are capacitated to access the business opportunities in the oil and gas industry. This analysis also extended to ascertaining the extent to which Oil and Gas regulatory framework provides an appropriate regulatory, infrastructural and macro-economic environment. The next stage applied a Binary Logit Model to predict the effect of these factors on SMEs' access to business opportunities in the oil industry. For qualitative data, the initial stage was a quick analysis of transcribed notes. The hand-written notes were assembled together and typed into a word processing program-Microsoft word. The data was thoroughly read and manually analyzed for content and recurrent themes in the texts as per the themes in the objectives of the study.

FINDINGS

Characterizing capacity of Local SMEs and regulatory environment for Local Content development

The perspective of previous and potential suppliers of good and services to the oil and Gas industry was analyzed upon which a characterization of capacity and the regulatory environment for Local Content Development was leveraged. Characterization of capacity reflects on company size-investment measured in terms of investment capital, knowledge of and experience in the bidding process. On the other hand, the regulatory environment drew on to the perceptions of respondents on complexity of the bidding process as well as conduciveness of bidding terms and conditions.

SMEs' capacity for exploiting the Oil Industry business opportunities

Regarding companies' size, the majority of companies (69.2%) that accessed the supplies tenders was medium or had investment capital of more than UGX 360 million. In contrast, the majority of companies that attempted and failed were small-sized or with capital investment of not more than UGX 360 million. This implied that, company size distinguished between companies that had previously accessed business tenders from those which had attempted and failed. Size was regarded a critical constraint particularly considering the fact that more than half of the companies that expressed interest to supply the oil industry operated small businesses (UIA, 2010).The general argument was that companies with huge capital investments have a competitive and capacity advantage over the small companies. They enjoy bigger purchase discounts; operate more efficiently due to minimal costs of production or importation all of which minimize the price at which they can offer goods. Besides, they are more famous and credible hence easy to attract trust from potential suppliers of goods on credit. They are also more likely to attract high technical expertise and use their strong business linkages to build strong technical and financial proposals than the small companies. This argument is consistent with the position in previous studies regarding the effect of size on capacity and competiveness of firms (Kasekende and Opondo, 2003; Abuka, 2003; UIA, 2010).

Besides, size, limited knowledge and inexperience, capacity of local firms was found to be further compromised by unfavorable business environment as observed by the majority (over 83%) of respondents. The environment was characterized by high production costs arising from high cost of production utilities including fuel and electricity as well as high taxes. These negatively impact on the price which can be quoted for supplies in the bids for supplies to the oil industry. The price is further affected by high exchange rates and inflation rates which also increase the cost of production and affect capacity of local companies to access supplies businesses in the oil industry. Such an environment limit competitiveness of local firms limiting their capacity to exploit the business opportunities in the oil and gas industry.

SMEs' knowledge and experience in the oil and gas industry

With regard to companies' knowledge of and experience in the bidding process, the majority (66%) of companies lacked adequate knowledge on the bidding process for supplies tenders in the oil and gas sector. Specific knowledge gaps were identified in aspects of; preparing financial and technical proposals, meeting the technical and financial requirements; and ease of meeting the requirement on administrative documents as indicated by 66-71% of the respondents. Whereas SMEs require exposure to the bidding process and how to comply with the procedure, the trainings by companies like Tullow Oil advisory services and training rendered to the local companies by oil companies like Tullow have mainly focused on fundamental business skills, calculating costs, keeping of proper accounting records and certification of skills. Whereas knowledge is important and emphasized under interventions to build capacity for local content [5], the study demonstrates ineffectiveness of the trainings provided to companies. More important, the analysis identifies specific gaps in the training focus which need to be bridged to enhance Local Content. Regarding experience, the majority (67.5%) of the companies had inadequate experience in the bidding process which is consistent with the finding by (Nalumu, et al., 2014; Tullow Oil, 2014) Experience was linked with strategies for easy preparation of quality and competitive bidding proposals (technical and financial proposals). And from the perspective of the contractors in the oil industry, experience meant trust and credibility that a company bears capacity to deliver once engaged.

The significance of knowledge and experience was further underscored by the complex nature of the bidding process as observed by the majority (62.5%) of respondents. Complexity was observed in terms of the many and lengthy procedures right from preparation of bids to award of contracts. Besides, companies were observed to have limited trust in transparency along these procedures with many perceiving the entire process as prone to corruption. Consequently, many companies perceived bidding for tenders in oil and gas as a more risky investment. Similarly, (Nalumu et al. 2012) observed complexity of the procurement processes with specific reference to transport and logistics supplies in Uganda are complex which affects SME's competitiveness and investments.

The effect of capacity and regulatory environment on Local Content Development

A Binary Logit Model was fitted to predict the effect of capacity and the regulatory environment factors on Local Content expressed in terms of access to or exploitation of supplies tenders in the oil and gas industry. The model generated odds which indicated the likelihood of accessing the supplies tenders at a particular level of an independent. A summary of the model results is presented in table below.

Table 1: Binary logistic model results

Variable	B	Sig.	Exp(B)
Knowledge of the bidding process	1.489	0.136	4.432
Complexity of the bidding process	2.158	0.011	8.654
Conduciveness of bidding terms and conditions	2.079	0.012	7.997
Company age-years of operation	-0.423	0.641	0.655
Company size-capital investment	2.276	0.005	9.740
Ease of meeting technical and financial requirements	1.527	0.041	4.603
Ease of preparing technical and financial proposals	1.725	0.045	5.615
Experience in the bidding process	0.206	0.810	1.228
Constant	-5.414	0.000	0.004

χ 2 statistic= 56.089; Cox & Snell R 2=0.052

The chi-square (χ 2) statistic for the model was 56.089 and statistically significant indicating that the model was significant for predicting the likeliness of access to supplies tenders. The Cox & Snell R 2 statistic was 0.52 indicating that the variables in the model explained up to 52% of the difference in access to the supplies tenders. The model affirmed that companies' access to supplies tenders is significantly (p<0.05) influenced by capacity factors including; company size-capital investment and experience in the bidding process. Access to supplies tenders is also significantly (p<0.05) influenced by complexity of the bidding process and conduciveness of the tendering terms and conditions.

More specifically, companies with small capital investments and inadequate experience are less likely to access the supplies tenders than the ones with huge capital investments. The medium sized companies are 10 times more likely to access the supplies tenders than the small-sized companies and vice versa. In terms of experience, companies with 10 years or and more years of competitive bidding experience are 4 times more likely to access the business tenders than those with a lesser experience. Companies which experienced ease in the bidding process are 9 times more likely to access the supplies tenders than those which experienced complexities. In terms of conduciveness of the bidding terms and conditions, companies which considered the terms to be conducive were 8 times more likely to access the supplies tender than those which considered the terms and conditions to be unfavorable.

CONCLUSION

Local companies face significant capacity gaps which affect their access to supplies tenders in the oil industry. The capacity factors specifically identified to bear significant influence on companies' access to supplies tenders are company size-capital investment and experience in the bidding process. Access to supplies tenders was also influenced by complexity of the bidding process and conduciveness of the tendering terms and conditions. In light of the findings, Local companies are argued to create long term credible partnership linkages with potential exporters so as to attract purchase of goods on credit to circumvent the huge capital requirements for supplies in the industry.

Closing capacity and technical gaps can also be addressed by encouraging local firms to form joint bids. This will help to secure economies of capacity that are currently lacking. Despite lack of empirical evidence from this study, there is evidence that such practices have helped to boost capacity of local firms for instance Apple and Samsung supply chain chains have manifested the thrust of such practices (Apple Inc, 2015; Ssamsung, 2014).

To bridge the technical gap in bidding for supplies tenders, key players in capacity building for local content development such as Tullow need to re-focus trainings towards building technical competence of the local companies in the bidding process. This will enable companies overcome the complexities along the bidding process where as improving the quality of bids.

Moving forward, further studies are needed to explore effectiveness of Public Private Partnerships and how best it can be implemented in the Uganda's Oil and Gas Industry. Further studies can also explore Local Content Development in other industries rather than Oil and Gas given that the Government of Uganda is promoting the Local Content across all industries.

REFERENCES

Abuka, C.K., Egesa, C.A., Atai,A and Abeona, M. (2006). Firm Level Investment: Trends, determinants and Constraints: Research Series No.47, Economic Policy Research Centre, Kampala, 2006.

Aneki (2010). "Poorest countries in the World." http://www.aneki.com/index.html

Apple Inc. (2015). Annual Report of 2015. Accessed June, 2016

Byaruhanga, H., P. Mwakali, P. and Ekern, O.F. (2011). Enhancing Local Content in the Oil and Gas Industry in Uganda

Cresswell, J.W. and Clark, V.L.P.(2011) Designing and Conducting Mixed Methods Research. 2nd Edition. SAGE Publications, 2011

Heum, P. Kasande, R., Ole, F.E and Nyombi, A. (2011). Policy and regulatory framework to enhance local content. Yardsticks and Best Practice: Paper presented at The 5th Conference & Exhibition on the Petroleum Potential and Investments Opportunities in East Africa Revenue

Heum, P. C. Quale, J.E. Karlsen, M. and Osahon, G. (2003).Enhancement of local content in the upstream oil and gas industry in Nigeria – a comprehensive and viable policy approach, Bergen: The Institute for Research in Economics and Business Administration, SNF-Report 25/03, 2003

Humphrey, J. (2003), "Opportunities for SMEs in developing countries to upgrade in the global economy", International Labour Organization SEED Working Paper 43, Geneva, ILO

International Alert (2009). "Harnessing Oil for Peace and development in Uganda, 2009

Kasekende, L. and Opondo, H. (2003). Financing Small and Medium-scale Enterprises (SMEs): Uganda's Experience. BOU Working Paper, WP/03/0/2003

Magelah, P.G. (2014). Local content in oil and gas sector n assessment of Uganda's legal and policy regimes. ACODE Policy Briefing Paper Series, No.28, 2014

Ministry of Energy and Mineral Development (2011). "A Report on National Validation Workshops for the Oil and Gas Sector Local Content Study", Hotel Africana, Kampala 24th and 25th May 2011

Ministry of Energy and Mineral Development (2010). Paper presented at the United Kingdom/Uganda Investment Forum, London, September 2010

Muloni, A. (2011) Uganda's emerging oil and gas sector: Challenges, strategies for sustainability of the Sector. A presentation at the Oil politics in Africa conference, Coventry University, United Kingdom

Mwakali, J.A. (2011). "Local Content in the Oil and Gas Industry: Implications for Uganda", in J.A. Mwkali and Alinaitwe (eds.), Proceedings of the 2nd Conference on Advances in Engineering and Technology, Entebbe, Uganda, 31 January-1 February 2011

Nalumu, R. Kikabi, P. and Mugisha, J. (2012). Constraints and Opportunities for SMEs Investment in Uganda's Oil and Gas Sector, 2012

National Planning Authority (2014) "Uganda's National Development Plan 2010/11 – 2014/15

Samsung Electronics Inc. (2014). Annual Report of 2014. Accessed June 2016

Seyed, P.M. (2013). Local Content Strategy, solution for successful global oil and gas projects in emerging economies, Norwegian University of Science and Technology, Norway, 2013

Sigrid, D. A. G. and Mohammed, K. S. (2011). Developing local content: Knowledge

Tordo, S., Tracy, B and Arfaa, N. (2015). National Oil Companies and Value Creation, Attitudes and Practices among Ghanaian supply companies 2011. Accessed online on August, 2015.

Tullow Oil (2012).Tullow Uganda Country Report: Creating shared prosperity in Uganda, 2012

Tullow Oil (2014).Tullow Uganda Country Report: Creating shared prosperity in Uganda, 2014

Uganda Investment Authority (2010) "National Investment Database." 2010

Warner, M. (2011). Local content in Procurement, creating local jobs and competitive domestic, Industries in supply chains, Greenleaf Publishing Limited

ABOUT AUTHORS

Fred Alindais a Ugandan graduate of Master of Science degree in Agricultural and Applied Economics from Makerere University, Kampala Uganda and Master of Science in Research Methods from Jomo Kenyatta University of Agriculture and Technology, Nairobi, Kenya. Before his graduate training, Fred attained a Bachelor of Agribusiness Management from Makerere University Kampala Uganda in 2002. Fred is currently working as a Research Fellow at Uganda Management Institute in Kampala Uganda. Before this position he served as a Junior Researcher at the Institute of Policy Analysis and Research in Kigali-Rwanda and a Research Assistant at Makerere University in Kampala-Uganda. His research interests include Business development, Entrepreneurship, Consumer economics, Technology adoption and Evaluations. He has several publications to his credit.

Alex Nduhura is a Consultant in Procurement, Logistics and Marketing at Uganda Management Institute. He is member of the Chartered Institute of Procurement and Supply (CIPS). He holds Master of Business Administration Makerere University Kampala. He is holds a Certificate in Professional Marketing from The Chartered Institute of Marketing and is currently perusing a Doctorate of Philosophy(PhD) at North West University under scholarship from Uganda Management Institute and African Development Bank(AfDB) in Public Management and Governance with a bias on Public Private Partnerships (PPPs) and Competitiveness of the Hydro Electricity Energy Subsector in Uganda. He has previously worked as a Procurement Manager at Stanbic Bank, a member of Standard Bank Group, He has held procurement and administration roles in aviation, poultry processing industry. He has lectured at Mt. Kenya University-Rwanda, Makerere University Kampala, Uganda Management Institute, Makerere University Business School(MUBS), Team University and offered. He has worked as Country Manager for Singapore Institute of Purchasing and Materials Management for Uganda, Rwanda and South Sudan He has been involved in consultancy assignments ranging from developing strategic plans, feasibility studies, functional capacity assessment, procurement and value for money audits, PPP transaction advisory services and project assessments. Key organizations where he has provided team leaderships on consulting assignments have included Trocaire, Southern Africa Development Community(SADC) Secretariat, National Social Security Fund(NSSF) Rwanda, Uganda Martyrs Hospital, and Mandela National Stadium. He volunteers as a public Relations Officer for CIPS Uganda and is a part of the founding Board of Uganda Marketers Society. He has coauthored several publications.