FOREIGN DIRECT INVESTMENT IN INFRASTRUCTURE: EXPERIENCE FROM PRIVATIZATION AND UTILITY REFORM IN UGANDA

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Abstract: The convention thinking in public sector economics is that government intervention in the economy is often motivated by market failures. Unfortunately, government does not often succeed in correcting market failures. The limitation implies that government should direct its energies only at those areas in which market failures are most significant and where there is evidence that government intervention can make a significant difference. However, controversy still remains over how limited or how active the government should be, and this is very contestable within the utility sector, in which its provision is associated with high sunk cost, political economy and the welfare state. The Government of Uganda adopted economic liberalization policy in the 1990s through creating an enabling legislation for privatization and utility reform. This resulted into the privatization of the power sector with the intention of breaking the monopoly of Uganda Electricity Board in the generation, distribution and transmission of power to successor companies. The power sector restructuring and privatization were strategically intended to make power sector financially viable and efficient in order to meet the growing demands for electricity, and increase the area coverage. The improvements in viability and quality of electricity supply would mean attracting private capital into the sector, and taking advantages of the export opportunities. Generally, the power sector reform was intended to improve on attractiveness of country to influence investment decisions. Through concessions, Eskom and Umeme Companies were given up to twenty years to maintain and operate hydropower plants, and also to maintain and operate the distribution networks and collect revenues from all connected customers respectively. The government however, retains the regulatory power through its Electricity Regulatory Authority. Although foreign direct investment was assumed to replace public investment in the power sector, this however has shown little progress as private investment is strongly influenced by exogenous factors. The little progress remains because of the limited presence of public resources in the power sector. The dynamics of power deficit in Uganda's power sector is becoming chronic, and this is coupled with the increasing demand for power that exceeds the generation capacity. With the increasing power deficit, public opinion and influence are very negative towards the privatization of the power sector. The public and legislatures believe that Umeme contract must be terminated on the grounds of high tariffs, worsening load shedding, and poor customers' satisfaction. However, the contract cannot be terminated because of its nature. It is even cheaper to stay within the line of inefficiencies than terminating the contract. The government therefore has maintained that Umeme contract can only be terminated when there is evidence of not achieving the performance benchmarks such as upgrading the distribution infrastructure, reducing energy losses in transition and standardizing tariffs. Umeme defends its performance to have already achieved the reduction in power transmission losses, supplying reliable energy and also connected more new customers. The controversial issues remaining are that the UK Company (Umeme, established by Consortium, Globeleg and Eskom enterprises) is insulated from losses; if any, to be paid by the government while at same time must reclaim all core capital investments upon expiry of its contract. Also, as a respond to high tariff, the government through the World Bank support has instituted consumer subsidies to keep tariffs at affordable levels by consumers. Using economic approach of market failures, this article examines the tensions between Umeme Company, the government, the public and investors in Uganda. Few analyses have been conducted in the experience

of private sector role in the power sector in developing countries.

Keywords: (privatization, Umeme, power providers, energy shortages, and market failures)

INTRODUCTION

Public enterprises were first established by the colonial power, usually to facilitate economic development including the marketing board, railway, electricity board, and national airline. Massive expansion of public enterprises in developing countries came after independent in the 1960s, 70s and occurred in all types of economies. State owned enterprises are broadly described as state owned production which sell their output and are directly involved in the market process (Turner and Hulme 1997). A public enterprise is an organization which, is owned by public authorities – up to 50% or more. It is under top managerial control of the owning public authorities – including the right to appointing, managing and formulating critical policy decisions. It is established for the achievement of a defined set of public purposes. It is engaged in activities of business characters. It is consequently placed under a system of public accountability. It involves the basic ideas of investment and returns and services (Praxy and Sicherl 1981:24).

In fact, the growth of public was due to a number of motivating factors. Firstly, ideological development and commitment to means of ownership of production sector, in which capitalism was avoided because of its exploitation. Secondly, the growth of nationalism provided a potential political justification for government intervention. Thirdly, economic theory and the perceive role of central planning such as the Soviet Union success, Marshall Aid plan for the rehabilitation of Western Europe (Turner and Hulme 1997). Public sector enterprises were expected to generate profits that would be reinvested. Fourthly, a commitment to big government complemented the outlook – as the only organization to re-engineer necessary changes such as promoting welfare. Fifthly, local political factors have contributed to the growth. Many governments wanted to promote employment, get political support. In Malaysia, Malay politicians instituted policies to incorporate and expand the economic role of the Malay upper and middle classes. Similarly, in Thailand and Indonesia, the public sector was used to take control from local Chinese classes. The public sector was expected to contribute to increasing Gross Domestic Product through value addition, increasing total investment, offering credit systems, increasing non agricultural employment, reducing regional variations in economic development.

While there were success stories of the impacts of public sector on development, there are more considerable examples of public enterprises failing to achieve both their economic and welfare objectives. Public enterprises have not made expected profits and thus, have not been the source of capital investment, instead they had caused public deficit. Although employment was created, inadequate investment in regional infrastructure was not sufficient. There have also been management problems. There has been vagueness of goals leading to lack of strategy and the way in which organizations adapt to changing environment. Weak structures of accountability, that is, public managers were not responsible for the performance because of lack of appropriate performance evaluation. The organization of the public enterprises have been characterized by bureaucratic, emphasizing routine, rules, control and hierarchy, more rigid than flexible, and unable to cope with changing environment. Overstaffing problem – due to political patronage, managers were implementing political decisions rather than business decisions. There was wrong choice of technology and plant size, poor accountability due to politicization of public enterprises and organizational culture of un-commitment (Turner and Hulme 1997).

As a result, this calls for rethinking about the role of states. By the 1980s management problems were widely recognized (Boyle 1995; Turner and Hulme 1997). There was a fundamental questioning of the role of the state in economic development. The emerging consensus was that the state was over extended, inefficient and needed to be "rolled back." The ideological impulse came from the election of conservative governments in the United States and United Kingdom as well as other parts of Europe. They placed tight limits on state role in the economy. The United Kingdom started by privatization of public enterprises and was later supported by the "Washington Consensus" masters the World Bank and the International Monetary Fund that started helping many developing countries to privatize state owned enterprises. Development planning was judged largely to have failed (Turner and Hulme 1997). Macroeconomic crises, foreign debt and financial deficit became endemic and state intervention into the economy through Import Substitution industrialization was associated with inefficiency and resource misallocation. The end of history was later associated with the triumph of liberalism. The dominant paradigm is now a neo – classical market oriented view of development process, which seeks to realign the role of the state

and the market. Emphasis changed in favor of the private sector away from the state intervention. Then the question is what should be the role of states? Scholars have given the following: provision of public goods (enforcement of contracts and defense), provision of some merit goods – like education and heath, development of transportation, communication, and power systems, dissemination of economic information, institution of transparent and flexible regulatory framework, promotion of scientific and technological research, and provision of safety net for low income groups. Therefore, the state must relate its social and economic goals. It has set itself for consideration of whether the private sector has comparative advantage in activities which would facilitate the achievement of these goals.

Within the new policy framework, the new idea has found expression in policies of economic liberalization including removing price distortions in product, labor and capital market, reducing government expenditures, privatization of public enterprises, and creating legislative –constitutional environment conducive to the private sector have been key components of this economic liberalization. The idea of the role of the state in economic development needs rethinking. Let considers the many options around this new idea. Firstly, about the allocation efficiency of the "invisible hands" of the market, the state is regarded as predatory and all politicians, bureaucrats and organizations in civil society as exclusively driven by self interest. They advocate for the minimalist state and laissez faire capitalism where market is supreme. Hence, public sector enterprises are perceived as market distorting devices which must be privatized. Secondly, against the allocation efficiency of "invisible hand" of the market, structural changes require redistribution of assets and access to power. Government seeks to maintain support from their key base to realize the vision of their societies.

The main interest in this paper was to examine whether the privatization of the energy was a success, looking at the initiative to unbundle the institutional set up of Uganda Electricity Board. In the case of energy sector, this article explores the privatization process of utilities - the Uganda Electricity Board, considering the various kinds of initiatives taken and possibly the general impacts of the reformed process (success or a failure). To understand the process well, we shall explore the experience under the changing role of government after the concession to Umeme so as to justify the reasons why state should have led in this core sector in Uganda.

This study was based on review of legal and policy documents concerning private sector participation in infrastructure, reports of parliamentary committee on energy, government commissioned report on high electricity costs in the country. It also followed the government pronouncements on the controversial contract it signed with Umeme. This study was being conducted over a long period of time with the aim of monitoring the developments within the energy sector since 2006. Media reporting may vary in reporting information, especially on official positions of government and that of Umeme, regarding performance of the Umeme and contract related issues. To minimize errors, this study was concerned with recording official information rather than personal opinions over time with no divergence of information. Also, public relations statements and interviews conducted with government ministers and Uganda Regulatory Authority as well as Umeme Managing Director was included. Review of documents from the World Bank and other development agencies were also integrated into this article.

This article is divided into subsequent sections. It starts by introducing the historical development and rationale of the public sector and changing role of government today. Then it reviews the theoretical and ideological discourses that changed the practice and role of the public sector. It then presents the economics of market and government failures, and how the competing discourses have changed the idea concerning government role in the economy. To understand private participation in infrastructure, a section on the role of FDI in infrastructure is presented, which is then related to the process of privatization. A case study on the experience of private sector in distribution of electricity is then adequately discussed, with policy recommendations and conclusions.

THEORETICAL INFLUENCES AND THE PRACTICE OF PUBLIC MANAGEMENT

After the review of theoretical developments and influences, the privatization of utility sector in developing countries was influenced by theoretical developments such as public choice, agency theory and management theory. These theoretical underpinnings brought into practice the New Public Management (NPM) approach to organizational control and structures in the public service. This approach strives to be more like private business management and uses alternative control mechanisms such as contracting out, greater devolution, encouraging competition, and so forth.

Therefore, managerialism was adopted by the public sector, a private sector management practices that applies Public Choice Theory and Neo-Classical Economics to public sector management (Turner and

Hulme 1997). The neo-classical economists gained considerable influence within the policy circles, pointing out the inefficiency and ineffectiveness in the public sector. The focus was that the state should be 'rolled back' because the 'big government' had not been effective, and it was the time the principles of the markets be allowed to operate. The focus therefore should be on building bureaucratic capacity and efficiency and encouraging private sector growth through market mechanisms. This radical and influential approach to governance was already being implemented in countries such as the United Kingdom, Australia and the United States. The dissemination of this new model to developing countries was undertaken by the influential multilateral institutions – the World Bank and the International Monetary Fund. The support for the new approach to managing the public sector was both at the political and administrative levels. There were increased political impetus for privatization and commercialization of services. These were in the elements of quasi-markets, management by contract, and performance indicators, which became popular within the public sector (Boyle 1995). The bureaucratic, highly centralized organizations were no longer delivering in the changing environments. Societies therefore needed a flexible system, with the capacity to respond to public demands. These common issues lead us to answer contemporary questions of whether we should be moving to a more private sector ways of running public services and /or also need to rethink about the contemporary role of states therein.

The Public Choice Theory applies non economic market decision making or applications of economic to political science. It is believed that in the absence of market mechanism, public representatives, bureaucrats pursue their own interests rather than public interest. Government and politics assumed to be similar to markets. Officials, politicians, and voters are short term material self interest maximizers, seeking to benefits in the form of power, public goods among a few to mention. It is based on the assumption that humans are egoistic, rational and utility maximizers. Public choice aggregates individual preferences through voting rules. Voters engage in exchange. Individual self interest norm provides the strongest argument for the analysis of political behaviors (Boyle 1995). Public Choice Theory is based on the pluralist approach about political society being composed of organized interests, in which both the elected and non-elected officials (bureaucrats) often facilitate favored access to public goods, services and regulations (Turner and Hulme 1997).

It has been argued that public choice theory favors small organizations to reduce monopoly power, where there is need for number of organizations to inject in competition, in contract employment, and advances the need for government to primarily provide pure public goods and the private sector to provide private services. However, the theory has got some limitations, especially in non western democratic countries; the presence of cultural differences; individual behaviors deviate from self interest; choices in developing countries are institutionalized rather than being determined by market forces; and coercion shapes everyday life in developing countries (Boyle 1995). The public choice theory was based on the view that 'peoples are rational, self-interested, opportunistic, maximizers' (Larmour 1990:64). It is dominated by narrow interests and not public interest. Because it focuses mainly on economic ideas of efficiency and consumer preferences to take advantages of market opportunities, the method had been used to criticize public providers of services and looking to consumers to find what is wanted and how it could be supplied most efficiently (Meier 1991).

Like Public Choice Theory, the Agency Theory explains the contractual relationship that exists between the principal (employer) and the agent (employee). It is based on the economic assumption of self – interest. The principal agent relationship faces difficulties as the principal's and agent's interests diverge. The principal limits this divergence by establishing incentives for the agent to fulfill the contracts, and incurring and monitoring costs to limit opportunistic behavior by the agent. The problems associated with the theory are the desire or goals of principal and agent may conflict. It is also very difficult for the principal to verify what the agent is actually doing. The presence of risk sharing problem may arise when the principal and agent have different attitudes towards risks (Boyle 1995). This calls for contract knowledge to effectively determine the contract desirability, observing the behavior of an agent (behavior based control), and rewarding the agent on the basis of agreed job behavior. Because agency theory stresses the importance of contractual relationship and the alternative contractual relationship that may exist – behavior or outcome based. Hence, organizations, must invest in information management systems in order to control agent's behavior. However, it is costly to implement and it emphasizes more on contract violation rather than contract coordination.

Similar, like the public choice theory, the developments of a managerialist school of thought are among the major influences on the design of

governance and management in the public sector. The aim was to improve on efficiency and effectiveness by paying more attention to organization's mission, personnel and customers. The principles underlying managerialism were decentralization – establishing decentralized structures; deregulation – removing trade constraints within the private sector; and delegation -assigning tasks to subordinates (Boyle 1995).

THE ECONOMICS OF MARKET AND GOVERNMENT FAILURES: PUBLIC GOODS VS PUBLICLY PROVIDED PRIVATE GOODS

The central ideas of the eighteenth and nineteenth centuries have continued to shape the role of government. The Wealth of Nations (1776) by Adam Smith argued for a limited role of government in the economy. Smith's idea was against the widespread believe that achieving the best public interests required an active role of government in the economy, a view which was admired by the mercantilist school of the seventeenth and eighteenth centuries, calling for active role of government in promoting industry and trade. Smith addressed himself to the question: *Can society ensure that those entrusted with governing actually pursue the public interest?* This has been the dilemma for most governments on how they should attempt to intervene in the economy. Those in position to govern often seemed to pursue their private interests at the expense of public interest. Self-interest is much more persistent characteristic of human nature than to do well, hence, it provides a more reliable basis for the organization of society. Individuals are more to ascertain some accuracy on what it is in their own self interest compared to what is good for the public interest (Stiglitz 2000:56).

To understand the role of government in the economy, we have to understand if there are important market failures of imperfect information, imperfect competition, incomplete markets, externalities, public goods, and unemployment – based on the presumption that the market will not achieved efficiency. Some may intervene in the market to make someone better off without making any worst off is way of promoting Pareto improvements. It is also evidenced that actual political and bureaucratic structures of a democratic society are capable of correcting the market failure and achieving a Pareto improvement (Stiglitz 2000:89).

In conventional economics, public goods can be determined based on the concepts of excludability and non-rivalry. Availability of a public good to one person simultaneously makes it equally available to all others – that is, joint consumption by all. Secondly, it is impossible to exclude non payers. Therefore, it only defense that explicitly qualifies under these conditions. This leads us to consider another element of merit good, which are needed for the functioning of modern society. Under this category, you may exclude other people from consuming merit goods such as education, health, telecommunications and electricity because there are additional costs that need to be paid if accessibility is to be guaranteed. These types of goods are called publicly provided private goods.

What motivates government to take action in the economy? Governments may intervene in the economy simply due to market failures. These failures may include: (1) imperfect competition – leading to monopoly and oligopoly, (2) pure public goods; (3) presence of externality; (4) incomplete markets – in case private firms do not providing what is enough, insurance and capital markets; (5) information failures – borrowing rates, research and development; and (6) unemployment, inflation and disequilibrium. When government intervenes, it is tasked with the following activities: provision of a legal system necessary for the functioning of a market economy; providing public goods such as defense, education, telecommunications and so forth; regulation of private sector producers through subsidies, taxes, credits; purchasing goods and services from the private sector, which are then supplied by government to households; and also redistributing incomes.

While governments may intervene because of market failures, there interventions are also associated with major shortcomings. These failures have also motivated economists and political scientists to investigate government failures. Under what conditions would government programs not work well? Were these failures of government actions accidental, or did they follow predictability from the inherent nature of governmental activity? Are there lessons to be learned for the design of programs in the future? There are four major reasons for systematic failures of the government to achieve its stated objectives: Firstly, government's limited information on the consequences of its actions. In most cases, government does not have the information required on what it expects to do. Secondly, government has limited control over private responses to its actions. The government does not directly control the total level of expenditures by the private sector. Thirdly, government has limited control over bureaucracy. In most cases, after designing the legislation, implementation is delegated to bureaucratic agencies, hence, the agency is given

the discretionary responsibility of enforcing the regulations. The problem that may arise is that bureaucrats may lack the appropriate incentives to carry out the intentions of the legislatures. Fourthly, government has limitations imposed by the political processes (Stiglitz 2000:9-10). In most cases, representatives in government act for the benefits of special interest groups. Based on these four sources of government failures, they are sufficient enough to show that government should restrain from attempting to correct market failures, if the private failures are not fundamental.

All these call for the need of achieving a balance between the public and private sector. It is explicitly being recognized that markets often fail, but governments often do not succeed in correcting the failures of the market. The recognition of government limitations implies that government should direct its energies only at those areas in which market failures are most significant, and where there is evidence that government intervention can make a significant differences (Stiglitz 2000:10). But, controversy remains about how limited or how active the government should be? Then what should be the role of government? The neo-liberal economists and political scientist have common suggestions on these regards. Governments' role in the economy may now include: (1) provision of public goods (enforcement of contracts and defense); (2) provision of some merit goods – like education and health; (2) development of transportation, communication, and power systems; (3) dissemination of economic information; (4) institution of transparent and flexible regulatory framework; (5) promotion of scientific and technological research; and lastly but not least is the provision of safety net for low income groups (Turner and Hulme 1997:185).

When analyzing the public sector, we have to address four fundamental questions: Firstly, we need to know what activities the public sector engages in and how these are organized. Secondly, understanding and anticipating full consequences of government activities. Thirdly, we need to evaluate the alternative policies, and the fourth is interpreting the political process (Stiglitz 2000). More so, the public sector has been mainly associated with inefficiency that arises from two sources: the first is on organizational differences including issues of soft budget constraints (subsidies, no bankruptcy), the role of political concerns, absence of competition, and additional restrictions (personnel, procurement, and budget). The second issue arises from individual differences which may include the absence of incentive pay; difficulty of firing reduces incentives, and principal – agent problems (pursuing bureaucratic objectives and high level of risk aversion).

Publicly provided private goods are goods for which there is a large marginal cost associated with supplying to additional individuals. The costs of running a market provide the rationale for public supply. Electricity is a publicly provided private public good. The increasing number of electricity users increases the cost of providing electricity to the additional individuals. As argued by Stliglitz (2000:138), there is a marginal cost associated with each unit consumed. When there is a marginal cost associated with each individual using a good, and if the costs of running the price system are very high, it is more efficient to simply supply the good publicly and to finance the good through general taxation, even when providing the good publicly causes distortions. When the transactions costs are sufficiently high, it may be more efficient to supply the good publicly than to have the good supplies by private markets. Markets result in efficiency when they are competitive.

In the past, market failures have motivated most governments to intervene through taking charge of the industry directly, providing telecommunications or electricity as well as regulating private firms so that they do not exercise their monopoly power. At the moment, the process of privatization of utilities (telecommunications, electricity and gas) and transportation (railroads and airlines) is common in most countries (Stiglitz 2000:190). Despite the compelling argument against public production because government is an inefficient producer, the dilemma is whether the actions of profit maximizing firms will reflect the public interest. Governments may provide private goods such as electricity at the lowest cost.

In case of natural monopoly, market failure calls for public production of publicly provided private goods when the market is not competitive. This explains the reason why government should not have privatized the electricity. Electricity is an example of natural monopoly. The sector is closely associated with high sunk costs and this leads to monopoly.

The analysis of pricing decisions is concerned with the issues of efficiency and distribution considerations. Therefore, any increase in the price of electricity leads to reduction in consumption. In case of electricity sector, it has the element of price elasticity. Changes in prices may not lead to very large change in consumption. Because Umeme (Uganda Limited) is operating as natural monopoly with high sunk costs, the company is not subjected to competition, and hence, charging at a higher price.

This reminds us about the rationale for privatization. Was it about reducing monopoly or about changing management? It makes no sense when you privatized the only national company that provides publicly provided private good and then and later start subsiding on the tax payer's account, yet it should have been financed by the state through taxation since it is a natural monopoly. Anyway the argument has been that government does not perform well when it attempts to provide publicly provided private goods, and should therefore leave the production to the private sector. It should therefore regulate prices to ensure that the company does not take advantage of its monopoly position. More so, the government can use subsidies to support the company to provide services that might not be profitable privately, but are considered as socially desirable, in this case, we can say electricity for rural transformation. Regulation and subsidies are remedies for market failures based on three assumptions. Firstly, it allows a more consistent and national policy, for example, in the case of privatization policy in Uganda. Secondly, the utilization of tax and subsidies schemes allows estimation of the costs associated with pursuing a given objective. Thirdly, is a widespread belief that incentive for efficiency is greater with the private entities, including even regulation (Stiglitz 2000)? However, this perspective does not properly portray the motive of the private sector. Umeme has been demanding for increase tariffs because they are not making enough revenues from the general electricity charges. In this case, it is better to look at the other alternative. Since the Electricity Regulatory Authority is still weak and it cannot ensure that the natural monopoly abuses its monopoly power, public provision of this publicly provided private good through direct taxation serves a better option for the national interests.

FOREIGN DIRECT INVESTMENT (FDI) IN INFRASTRUCTURE

The role of FDI in infrastructure in developing countries can be channeled through greenfield, acquisition by privatization, build own – operate, build own operate transfer and build – transfer operate to reduce the risks of budgetary constraints on governments. For instances, governments of Vietnam, China and Malaysia used build operate – transfer scheme (UNCATD 1996: 20, 22 &25). However, constraints for FDI role in infrastructure are due to high sunk costs, long gestation period and possible price ceiling and regulations. More so, political risks of expropriation minimize investor's commitment. Despite the constraints, there are potentials for TNCs in infrastructure development due to its significance in meeting public demands.

FDI refers to a foreign corporation or foreign company having the essential attributes of a corporation that is chartered under the laws of a state or government other than that in which it is doing the business (Webster's Third New International dictionary, p.889). Moosa (2002) defines FDI as a 'process' whereby residents of one country acquire ownership of assets for a purpose of controlling the production, distribution and other activities of a firm in another country (Moosa 2002:1). Kehal (2004) puts it as the setting up of overseas operations or the acquisition of an existing enterprise located within another economy with investors exerting significant degree of influence on the management of the resident enterprise (Kehal 2004:14). In this article, FDI is defined as involving control of a resident entity in one economy by an enterprise resident in another economy (UNCTAD 1996:20). It can be in terms of entry through mergers and acquisitions (UNCTAD, 2000: 101), which is consistent with the World Bank definition as an investment made to acquire lasting management (usually at least 10 % of voting stock) in an enterprise operating in a country other than that of the host investors (Gillis et al. 2001:522).

The eclectic theory (OLI) developed by Dunning (1981) provides a conceptual framework for explaining FDI in Uganda. The paradigm states that a country propensity to attract inward FDI is a function of three variables: (1) existence of Ownership-Specific Advantages (O) that is based on firm's resources and capabilities; (2) host country's Location-Specific Advantages (L) comprising of both natural and created resources; and (3) is the Internalization (I) by which firms combine Ownership Advantages with Location Advantages to improve their competitiveness. Therefore, a host country will attract FDI when the three variables are fundamentally met. Scholars see the theory as significant enough in explaining the reasons for the 'why', 'how', and 'where' of the TNCs production whereas others see the explanatory importance of constituting many variables as a source of its limitations. In addition, Kehal (2004:16) found the size of the host country's market as the most popular factor influencing a country propensity to attract inward investment, and this was supported by the subsequent empirical literature he reviewed (e.g. Agrwal, 1980; Tsai, 1994; Chakrabati, 2001) that provided further justification for the market size hypothesis. The national policy changes including privatization via Merger and Acquisitions and purchases of existing projects helped in attracting foreign capital.

Foreign Direct Investment (FDI) plays a significant role in the development process of host economies. It acts as a catalyst for obtaining foreign technology and knowledge, managerial skills and capital. Official Development Assistance (ODA) which declined at the beginning of the 1990s (UNCTAD 1998:13) made many host economies to resort in attracting Foreign Direct Investment (OECD 2003; UNCTAD 2003) through: opening up the economy for FDI, active marketing investment opportunities, focused programs to target specific subsets of Transitional Corporations.

African governments have put efforts in economic reforms and liberalization (UNCTAD 1995:95), addressing investor's concerns, privatizing and actively promoted investments (UNCTAD 2003:36) to attract FDI, with 42 regulatory changes favorable to FDI by 2005 (UNCTAD 2006: 46). Privatization programs (UNCTAD 1998: 170) are common in African countries like Angola, Cape Verde, and Uganda among others. Africa typically attracts very moderate amount of investment, and the flows tend to fluctuate widely (UNCTAD 1994:62). The oil exporting countries in Africa dominated in inward FDI flows accounting for two – third of its stock and flows (UNCTAD 1995:84) and SSA continues to rely on ODA which constitutes the bulk of its external resource inflows. Despite of the effort in improving policy environments in sub Saharan Africa (SSA), its share of FDI in developing countries is declining and its inflows have been characterized by absolute progress but with a relative decline (Asiedu, 2004:41) and "it is not enough to improve on one's policy environment, but improvements need to be made in both absolute term and relative terms". This signifies the complementary role of FDI to domestic investment as a means to an end and not the end itself.

Inflows of FDI have implications for economies seeking growth and development (Enderwick, 2005:94) including careful investment in assets and infrastructure, coordinated integration of policies, and the avoidance of expensive incentive to attract FDI. The most attractive industries for FDI were telecommunications, food and beverages, tourism, mining and quarrying, textiles and leather (UNCTAD1999:50). This suggests that many African countries receive FDI in non–minerals. FDI in services is increasing particularly in telecommunications, electricity and management and trade due to the growing importance of services through privatization that has problems without regulations.

Evidence from the FDI related literature (Asiedu 2004; Kehal 2004; Bende-Nabende 2002) demonstrates that FDI play an increasing role in the economic development of host countries; mainly in terms of human development, technological transfers and capital formation, international trade, competition and enterprise development. UNCTAD (2000a: 8) gave a general contribution of FDI in Uganda in terms of capital inflows and technology transfers and export development among others. In developing countries, technology transfers occur through TNC affiliates, joint ventures, franchising capital good sales, licensing, technical assistance, sub-contracting or original equipment manufacturer (Bende-Nabende 2002:143).

The role of FDI role in infrastructure in developing countries can be channeled through greenfield, acquisitions through privatization, build own – operate, build own operate transfer and build – transfer operate to reduce the risks of budgetary constraints on host governments (UNCTAD 1996:20 &22). For instance, governments of Vietnam, China and Malaysia used build operate – transfer scheme. This solves the infrastructure problems in developing countries. Policy implications for investment liberalization are in three folds: (1) liberalization of entry and operation to increase competition and prevent anti – cartel practices; (2) limiting market power inducements; (3) minimizing anti – competition effect. As for policy makers (UNCTAD 1998:166), lessons can be learnt from African frontrunners in FDI including the need for stable and predictable policy and macroeconomic environment, further privatization program, growth oriented policies, regional integration, efficiency – seeking FDI like in Tunisia, natural resources revenue should be used to fund other assets and ignoring corruption perils the economy.

The macroeconomic reforms including liberalization and privatization of 1990s in Uganda restored hope in foreign investors (UNCTAD 2000a) and the economy has shifted from rehabilitation to expansion. Uganda Investment Authority (UIA) was created in 1991 to link investors into the economy through effective marketing, approval of projects and providing information on incentives (UCTAD 2000a; MIGA 2004:47) and is now a model in Africa. This made Uganda to be ranked among the "forerunners" of FDI in Africa and FDI average net annual inflow during 1993-1997 was around $112 million more than ever before. The privatization program in Uganda started in November 1992 to pave way for FDI into the economy (UNCTAD2000a:4).

UNCTAD (2000a) highlighted investment and policies in Uganda through the assistance from

national and foreign experts who considered firm's profiles. It stated that the economic fundamentals have been restored and public sector reforms have been implemented. However, the problems remain with how to put up the right set of policies to achieve a sustainable growth. By 1990s, macroeconomic reforms included liberalization, privatization and inviting back the former Asian investors. The political and macroeconomic stability by President Museveni (MIGA 2004:51) restored hope in foreign investors. This made Uganda to be singled out among the African most attractive destinations for FDI (UNCTAD 1999:50).

PRIVATIZATION OF THE PUBLIC SECTOR

The divestiture of public enterprises fulfils the multiple functions of reducing public expenditure, raising revenue and also promoting the development of the private sector (Turner and Hulme 1997:190). Privatization in developing countries was conducted for several reasons, including the need to reduce public expenditure, raising revenue, promoting private sector development, broadening ownership, increasing economic efficiency, reducing administrative burden, ideological argument, and lastly, but not least is to developed the capital markets. In this paper, the conceptual understanding of privatization means the transfers of operational control of an enterprise from government to private sector (Campell and Bhita 1996:11&12). The operational control to private sector can be conducted through lease and concession. Under lease, in return for an agree fee (rent), a private operator is given the custody for a specific period of time of some or all of assets of a public enterprise to employ in a productive manner. Ownership of these assets remains with the enterprise, while operation of the share remains unchanged. Temporary privatization of the business takes place and lasts as long as the lease arrangements remain unchanged. Concession – is a contractual arrangement whereby in return for a negotiated fee, a selected private operator is awarded a license to provide specific services over a period of time. Ownership of the principal assets remains with the enterprise and ownership of the share remains unchanged. Temporary privatization lasts as long as the concession lasts. Concession is awarded on a competitive basis. The definition of privatization is also extended to include: (a) equity dilutions – whereby the government has moved from the majority position to holding minority equity (b) joint ventures – whereby a government holds more than 50% of the equity and has ceded management to the private holders (c) divestiture – means transaction by which government has transferred title or sold some or all assets or share in an enterprise (d) liquidation – relates to the closure and winding up of an incorporated enterprise in accordance with the procedures under insolvency. Full divestiture is when the enterprise is wound up.

The methods for conducting privatization includes nationalization which involves selling public enterprises back to the former ownership or through a new share floating on the stock market, or by closing down the public enterprises altogether (Turner and Hulme 1997:191). There is also contracting out /leasing – enables the state to finance an enterprise using private firm to run it. Public works, urban development and water supply schemes are common examples. This is done through concession. Self management/cooperatives – involves transferring ownership and management of public enterprises to their workforces. For example, cooperatives or farmer associations may be used to take control of former state cooperatives. However, they were having the following problems: problem of management capacity to institute reform to make the enterprise efficient, lack of capital and inadequate service back up and the capture of cooperatives by local elites and this discourage innovation. Deregulation involves the abolition of statutory barriers preventing private operators from competing with state owned enterprises. For example, monopolistic marketing boards have been dissolved or forced to compete with private companies.

However, it has been noted that the Public Sector Reform Programs in developing countries have been at a low pace. This is because of economic factors, politico – administrative nature which affect content and implementation. As stated by the World Bank (1995), privatization is always political, hence, any successful reform must be: (a) politically desirable to the leaders and constituencies (b) politically feasible for leaders to implement (c) politically credible for investors and other affected constituencies (d) political transparency is another factor that assists in addressing political impediments thus facilitating the reform process - including giving to the rightful owners or buyers, respecting national autonomy, giving to minorities groups in the economy, and (e) must be supported by labor unions in an economy.

EXPERIENCE FROM PRIVATIZATION AND UTILITY REFORM IN UGANDA: THE CASE OF UMEME COMPANY (U) LIMITED

The Public Enterprise Reform and Divestiture Statue of 1993 promoted the divestiture of 117 enterprises and as well as liquidating 39 enterprises by 1998. The process of divestiture started with small enterprises and is now focused on utility and large scale sector.

The divestiture has taken the form of direct sale of government shares, wholly or partly, in public

Table 1: Percentage of respondents evaluating constraint as a major or very severe.

Constraint	Full sample	Foreign firms	Domestic firms	Exporters	Non-exporters
Cost of finance (interest rate)	60.3	54.1	62.0	62.5	60.2
Tax rates	48.3	43.3	49.6	48.9	48.4
Macroeconomic instability	45.4	57.6	41.3	64.3	41.7
Access to finance (collateral requirements)	45.0	36.5	47.7	37.2	46.6
Electricity	44.5	48.5	43.1	52.4	42.9
Corruption	38.2	55.0	33.3	56.4	35.0
Tax administration	36.1	42.2	34.5	42.9	35.1
Anticompetitive or informal practices	31.1	34.4	30.2	41.5	29.4
Skills and education of available workers	30.8	25.4	32.0	36.6	30.0
Regulatory policy uncertainty	27.6	38.1	23.7	42.9	24.6
Custom and trade regulations	27.4	38.1	23.2	33.3	26.3
Crime, theft, and disorder	26.9	37.3	23.5	36.4	25.3
Transport	22.9	28.8	20.9	36.4	20.2
Access to land	17.4	24.6	15.6	17.1	17.4
Labor regulations	10.8	12.3	10.4	14.6	10.1
Business licensing and operating permits	10.1	13.4	9.2	8.9	10.4
Telecommunications	5.2	6.2	4.9	7.0	4.5

*Differences of more than 10% between different categories are highlighted

Source: World Bank Investment Climate for Uganda 2004 Report, p.38.

enterprises, auction of debt/equity swap, joint ventures, and management contracts (Basu and Srinivasan 2002:36). Public Enterprise Reform and Divestiture was amended in 2000 to facilitate privatization process embedded with commitment and transparency in Privatization and Utility Sector Reform Project (PUSRP) (MoFPED 2003:1&2).

The Government of Uganda instituted the Power Sector Restructuring and Privatization Strategy. The intention was to make power sector financially viable and efficient, meeting the growing demands for electricity, increasing coverage, improving power supply, attract foreign capital and create export opportunities. The legal framework for privatization of electricity was provided in the Electricity Act of 1999 and Public Enterprise Reform and Divestiture Act of 1993. The Electricity Regulatory Authority was then established in 2000, issuing licenses to electricity providers, reviewing and imposing tariffs, establishing and enforcing standards. Eskom then took the maintenance and operation of Kiira and Nalubale power stations. What kind of competition was generated? It was merely a change of management. Since 2005, Eskom as remains in its monopolistic market, and the so called independent power producers joined the sector as a solution to limited power provided by Eskom.

Umeme (U) Ltd in 2004 took the distribution Company for a concession of 20 years. This was a great contribution in improving the management of power sector. However, there are other things that government does better than the private sector, especially in the energy sector that has got high sunk cost, long gestation periods plus heavy capital investment, in which cost of power if rendered by the private sector become very expensive for citizens. The Uganda Electricity Generation Company Limited (UEGCL) owns the electricity generation facilities at Nalubaale and Kiira, and concessioned to Eskom. Uganda Electricity Distribution Company Limited owns the electricity distribution network, and concessioned to Umeme; Uganda Electricity Transmission Company Limited (UETCL) and Rural Electrification Agency, under government's control (Parliament of Uganda 2007).

Before the privatization of Uganda Electricity Distribution Company Limited, the Private Investment Survey of 1998 revealed that on average, firms lost an estimated $90 millions of operating days

a year due to power cut that later translated into high cost of production, and therefore reducing the competitiveness

Table 2: The principal private enterprises' activities in Uganda.

Sector	Domestic		Foreign		Total	
	No	%	No	%	No	%
Agriculture, hunting, forestry and fishing	42	10.2	30	8.5	72	9.4
Mining and quarrying	1	0.2	5	1.4	6	0.8
Manufacturing	135	32.9	103	29.1	238	31.1
Electricity, Gas and water	4	1.0	3	0.9	7	0.9
Construction	15	3.7	26	7.3	41	5.4
Wholesale/retail, catering/accommodation	88	21.5	73	20.6	161	21.5
Transport, storage and communication	31	7.6	24	6.8	55	7.2
Financing/insurance, real estate/services	49	12.0	58	16.8	107	14.0
Community, social and personal services	14	3.3	10	2.8	24	3.1
Activities not covered in the above	31	7.6	23	6.5	54	7.1
Total	410	100.0	355	100.0	765	100.0

Source: UBOS Report 2004, p.16

of the private firms in Uganda, even though 77 % of the of the large firms, 44% of medium-sized firms, and 16%of small firms owned power generators (MoFPED 2000:3). After privatization in 2005, it now reported that the country's losses have increased to US$ 400 million in goods and services (The New Vision, Thursday, 18th August 2011).

To make matter worst, the hydro capacity of 380 mega watts on River Nile reduced in financial year 2005/06 to 135 MW because of extended regional drought (The New Vision, Thursday, 4th May 2006). Amidst power shortages, Umeme constantly demands for tariffs increment from Uganda Electricity Regulatory Authority. The hiking of power tariffs adds cost of doing business, heavy industry automatically reduces production, affects consumption capacity of the economy, and prospective investors are deter due to high cost of utility. More so, footloose industry relocates to other countries as they are more responsive policy environment than heavy industry leading to market failures amidst deepening competition.

The World Bank (2004) assessment report mentioned electricity among the top three leading constraints in the country when it comes to the ease of doing business. The 2002/2003 survey was conducted to 392 firms in the country as illustrated in table1.

This contributed to opening up of the energy sector to the private players. A survey by Uganda Bureau of Statistics (UBOS) 2004 conducted to 765 investing enterprises in Uganda showed an increment of the number of private investment in the energy sector as illustrated in table 2.

The growth in manufacturing, wholesale, catering and accommodation plus finance inclusive showed the available opportunities in the economy. In finance and real estate services, the privatization program opened up entry into the economy to rescue the ailing companies that were controlled by government including M&As and Joint Ventures.
Most important is that investor's participation in utility has been minimal since 1990. However, the private investment in energy sector increased from US$18 million in 2003 to US$ 30 million in 2011 making a total of US$1,263 million. Investment in telecom increased from US$4 million in 1994 to US$ 185 million in 2011making a total of US$ 2,567 million. In general, a total of 24 projects were registered including 16 projects in electricity, telecoms 5, water and sewage 2 and 1 in railway (World Bank 2011). Table 3 shows projects by primary sector and subsector investments.

Surprisingly, investments in the energy sector are driven more by short term objective to reduce the energy crisis in the country. There is need for a strategic point of entry into the economy given the available of various resources for energy development including solar, biomass, and fall sites. Such best practiced policy would be at the interests of Government of Uganda that is eager to promote rural electricity but constrained by limited resources. The private developers will complement Government rather than being the only consumers of energy from Government. As foreign investors have recently invested in energy sector to avoid load shedding that affects factor productivity and their competitiveness, the recent developments in telecom was due to the liberalization and removal antitrust law that inhibited

new entrance in the sector signed between MTN and Uganda Telecom in 1998. This has helped to create public good (information and communication) across

Table 3: Private Participation in Infrastructure in Uganda

Total Projects By Primary Sector And Subsector (Us$ Million)					
Sector		Sub -Sector	Number of Projects		Total Investment
Energy		Electricity	16		1,263
		Total Energy	16		1,263
Telecom		Telecom	5		2,417
		Total Telecom	5		2,417
Transport		Railroads	1		404
		Total Transport	1		404
Water And Sewerage		Utility	2		0
		Total Water And Sewerage	2		0
Total			24		4,083
Sector	Concession	Divestiture	Greenfield Project	Management And Lease Contract	Total
Energy	4	0	12	0	16
Telecom	0	1	5	0	6
Transport	1	0	0	0	1
Water And Sewerage	0	0	0	2	2
Total	5	1	17	2	25
Total Investment in Projects by Primary Sector (US$ million)					
Sector	Concession	Divestiture	Greenfield Project	Management And Lease Contract	Total
Energy	102	0	1,160	0	
Telecom	0	298	2,269	0	2,567
Transport	404	0	0	0	404
Water And Sewerage	0	0	0	0	0
Total	506	298	3,429	0	4,233

Source: World Bank Group. 2011. Private Participation in Infrastructure Projects Database

the country unlike before under the monopoly of Uganda Post and Telecommunication Limited that had been characterized by market failures including limited coverage, inefficient and lack of competition.

For illustration, the Madhvani Group has a joint venture in Nile Independent Power Consortium with initial investment plans of $400m. Also, Arabian International Construction Ltd., wholly owned by Egyptians has got $600 million in Kalangala Falls project (UNCTAD 2000a:5&7). The joint ventures in the energy and mineral explorations is a positive move to reduce risks and costs in the energy sector, acquiring technological and managerial skills, local partners and entrepreneurial class within the local firms. This reinforces the capacity to produce more power needed for maintenance in the production process. It also reduces the monopoly of Umeme which is associated with market failures. However, the limited entry in utility sector shows the risks borne by private sector's participation in the energy sector including risks in heavy capital investment and

sunk costs, government caps on prices and political economy embedded in the energy sector.

Technological transfers in developing countries occur via TNC affiliates, joint ventures, franchising capital good sales, licensing, technical assistance, subcontracting or original equipment for manufacturing (Bende-Nabende 2002:143). Investment in telecom has been highly recognized in solving the country's technology problems. MTN Uganda Ltd joined Uganda's business in 1998 through a concession of 20 years for provision of telecom services. It is now the leading mobile industry in the economy with over 70% of 350,000 lines. In addition, there is Celtel Uganda with 60,000 lines and Uganda Telecom with a network of 140,000 lines and 40,000 lines rest in the hand of Mango telecom–Uganda (www.ugandainvest.com).

Leapfrogging in telephone industry has filled the information gap in Ugandan via greenfield investments – MTN, Celtel, Uganda Telecom and Warid Telecom from Abu Dhabi. This has got multiplier effects of attracting prospective investors as competition drive utility cost of doing business down and improves on their competitiveness. In other word, Uganda benefited more from technology transfer in the telecom sector and has built the confidence in foreign investors in this sector.

The energy crisis will continue since the sector is associated with natural monopoly, characterized by heavy capital investment and sunk costs involved. Even if it is opened to private developers, the marginal cost of providing it to additional consumers is low which leads to under consumption. The government always has price ceiling and regulations in the sector. Also, most foreign investors are engaged in commercial and heavy manufacturing industry. More so, there is a persistently increasing high cost of production that affects location decisions of already existing and prospective TNCs. The power crisis is reducing the competiveness of enterprises. The persistent high cost of doing business is fueled by extra expenditures on fuel to operate private generators.

In 2005, Umeme was granted the concession to distribute electricity, which was previously managed by Uganda Electricity Distribution Company Limited (UEDCL) and the Uganda Electricity Board (UEB). On an advertorial highlight, Umeme (U) Limited pointed its factual achievements since 2005 despite the numerous challenges it faces in the sector. Umeme reported to have paid approximately, Ugandan Shillings (UGX) 65 billion in corporate tax and UGX 89 billion in Value Added Tax (VAT). Before the concession, UEDCL had losses of above 38 percent, but Umeme has managed to reduce the losses to 28 percent in 2011. As a result of loss reduction, there was a saving of UGX 343 billion. Umeme has also reduced non-collection rates of above 20 percent prior to the concession to 5 percent in 2011, achieving improved collections up to UGX 327 billion over seven years. With regards to investments in the sector, Umeme planned to invest approximately UGX 351 billion into the network and supporting business infrastructure. In the absence of the concession, this investment would probably have been financed by government cash injections. Umeme pays rental payments for the network to UEDCL, which forwards on to the government. In the past years of concession, it pays over UGX 297 in the rental payments. In terms of improvement in operational efficiencies, Umeme receives a pre-agreed amount from the tariff for its operational costs. To improve performance of business, it had to spend additional UGX 97 billion from its own resources. Prior to the concession, previous company UEDCL was experiencing problem of servicing its debts and meeting its financial obligations, primarily towards Uganda Electricity and Transmission Company Limited and Uganda Revenue Authority, and funding investments into the network and rural scheme. Since the start of the concession, the government no longer needed to contribute funds to UEDCL (Umeme 2011).

Umeme's publication also acknowledged a lot of challenges since the start of the concession. Most of these challenges arise from exogenous factors rather than endogenous factors, and these contributed to increasing the tariffs. These include: (1) load shedding. Since 2005, the energy demand in Uganda has grown by 10 per cent per year. This has been driven by economic growth and new customers being connected to Umeme's network. The new customers increased from 230,000 connections in 2005 to 450,000 in 2011. Unfortunately, the energy supply has not grown fast enough to satisfy the rising demand. Initially, in 2005, the availability of energy generation from hydro stations dropped due to drop in water level in Lake Victoria. Severe loading shedding ensued, which was only reduced with significant deployment of thermal generation by Aggreko. Other thermal projects were added later, as well as some small hydro and co-generation power plants. However, even with the new plants and strong rains, demand will outs-space power supply until Bujagali hydro station comes online; (2) high price of oil. The thermal plants currently produce almost half of the electricity supply in Uganda and run on imported diesel and heavy fuel oil. With the high prices of oil in the recent years, the cost of thermal

generation to the energy sector was very high – approximately UGX 2.8 trillion. Unfortunately, at that time it was the only available choice for keeping the lights on; (3) the depreciation of the Ugandan Shilling. Most of the costs in the electricity sector are imported and therefore denominated in US Dollars: fuel, plant and equipment, financing costs. Since Ugandan Shilling has lost value against the US Dollar, energy sector costs have gone to the sky (Umeme 2011).

These challenges have resulted in significant costs, which have put pressure on electricity tariffs. This burden has been shared between the consumers and the Government: electricity tariffs increased in 2006 and 2007 and Government contributed significant funds to prevent them from going higher. Since 2006 Government has subsidized the energy sector with UGX 1.3 trillion and the World Bank with additional UGX 465 billion. These funds have been injected into UETCL, which is owned by government. Subsidies were not given to Umeme (Umeme 2011).
Efforts to overcome these challenges are underway. Bujaali hydro station is under complete construction to start generating power, which can eliminate load shedding. The government also plans to build several generation power plans and Umeme will receive enough power from UETCL to distribute to its customers. Umeme network investment is planned to worth around UGX 920 billion to connect 550,000 new customers, extend the network, improve its reliability and reduce losses. Umeme is also committed to prepaying metering technology, in which a pilot project with 10,000 connections is at advanced level and the customers feedback to the project is very encouraging. This strong investment in technology will reduce energy losses to 20 percent (Umeme 2011).

In an exclusive interview with Luka Buljan, a consultant with Actis capital, a subsidiary of the UK common Wealth Development Corporation which owns Umeme, Umeme position was that “we are not the problem”. The interview was about Umeme’s operation and contract with the government. He hinted on the achievements of Umeme despite many challenges. He pointed that Umeme has replaced 100,000 poles out of 240,000 poles countrywide. It has also replaced 2,000 generators out of the 6,000 generators. Umeme also refurbished 1500 km network and built another 1500 km, refurbished 40 out of 60 sub counties. Buljan revealed that Uganda electricity spent US $ 1.1 billion on buying power from thermal plants from 2006 to 2011. The total subsidies injected excluding the World Bank contribution from 2006 to 2011 was more than US$ 470. Delays in Bujagali constructed was expected to cost appropriately US$ 285 million in thermal generation costs, of which US$ 175 million was to be contributed by government. Before Umeme, losses were from 38 percent to 40 percent, but have been reduced to 28 percent by 2011. On investment, Umeme has invested US$ 130 million (UGX 364 billion) in the last years since the concession agreements, and this substantially upgraded the network. As a result, it has recouped US$ 7 million (UGX 20 billion). Umeme also plans to invest again additional US$ 340 million (952 billion) or more in the next seven years. On load shedding, he maintained that it is a generational problem, not Umeme. There is high demand for electricity more than the supply. This explains the reason for load shedding. The urban centers have grown, leading to a mismatch between supply and demand. This could also be understood simply under the conventional theory of demand and supply. Tariff has increased to 98 percent since 2005 due to thermal generation. It is when Bujagali starts producing 50 MW in the first unit production then 150 MW out of the 250 MW that the problem can be brought to control. On the issues of contract clauses standing to favor Umeme than the government, especially the termination clauses that require the government to pay heavily, Buljan stated that when government defaults then Umeme gets 120 percent, but when Umeme defaults, Umeme gets 80 percent. According to Umeme, the middle range is 100 percent. If Umeme defaults, it gets less by 20 percent, and if government defaults Umeme gets more by 20 percent. This position is very contradictory. Popular opinion is that the penalty clause restricts government to stay with Umeme for the 20 years even when Umeme remains inefficient. To Umeme, the problems Uganda is facing are associated with wider energy problems of the energy sector. Load shedding, high tariff are problems Umeme cannot control (The New Vision, Thursday, 15th September 2011).

The contract between Umeme and the government was costly. A contract signed in 2004 by former Minister of Finance, Gerald Sendaula on behalf of government, Irene Muloni, now Energy Minister signed on behalf of UEDCL as the Managing Director, while former Managing Director, David Grills singed on behalf of Umeme. The concession was intended to improve on the quality of services, increase investment in the rehabilitation and expansion of the power distribution network, reduce losses, increase new connections, and provide reliable and affordable electricity to consumers. However, the objectives of the reform are far from being realized. The sector is associated with higher distribution losses, billing and collection losses, power tariffs,

poor quality services and low access levels. The 32 page report states that the agreement signed on May 17th, 2004, stipulates that the government can only terminate Umeme's contract if it paid the company a buyout amount. The government is required to pay Umeme over UGX 4.7 trillion if it defaulted on the contract, more than the country's summed budgets of energy, health, transport and education. The buyout amount is calculated against the cost of modification/investment that is not depreciated and uncovered by Umeme before the transfer of the distribution to the UEDCL. The invested amount (US$ 120 million) is multiplied by 120 percent annually from the initial period of investment (2006) up to the end of the 13th anniversary (2017). Thereafter, the money keeps on reducing every year as the percentage multiplied with the invested money also keeps on declining by 2 percent per annum up to the end of 2024. This means government is restricted or to stick with the agreement until 2024 when the contract expires. In the event of natural termination of the contract, government would pay 105 percent of the amount to Umeme invested at the time of termination, which would be over UGX 294 billion. Natural termination of contract is when the contract expires and the contractor claims they have not recouped their total investments. The agreement further reveals that incase of termination of the contract due to circumstances beyond the control of both parties (Force Majeure), government pays 90 percent of the invested money. This would not be less than UGX 252 billion. These circumstances include war, riot, strike, crime, flooding or earthquake or volcanic eruption. The contract also obliges government to pay an interest of 20 percent per annum of any outstanding portion of the buyout amount should 91 days elapse after the termination date until it clears the money in full. The report criticizes Umeme for having high initial connection costs, operation and maintenance costs and lengthy connection time, power outages and theft (The New Vision, Wednesday, 7th September 2011).

General Salim Saleh probe report on high electricity cost mentioned several irregularities by Umeme, including irregularity in setting tariffs, collection of energy bills, and the flaws in signing the concession. Umeme is blamed for putting losses at a much higher rate, to justify its higher rebates and price increases. Umeme is also blamed for issuing faulty meter reading and billing, in which customers are charged for what they have not consumed. The probe team commissioned by Government, headed Gen. Salim Saleh, the then Presidential Advisor on Defense showed a lot of contentious issues. They revealed that the contract government signed with Umeme was unfair and favor Umeme. It further showed that the deal of unbundling Uganda Electricity Board had been made hurriedly without sufficient preparation. The mistake was the main cause of the electricity crisis in the country in 2006. They suggested that the government should have negotiated with various interested companies with the view of getting a more acceptable deal. The report recommended that there is need for a better coordination between the generation, distribution, and transmission. For further illustration, one of the most the accepted reasons for government intervention in economy is when there is coordination problem, which UEB was supposed to do. The report further pointed that Umeme colluded with some officials to favor independent power providers. Umeme also factored infrastructure investment costs into tariff, the meter reading and billing process, and the number of faulty meters that were distributed to customers. The Electricity Regulatory Authority was criticized of lacking supervision capacity and was not acting as a regulator. The report also pointed that a contractual loss figure was raised to 38 percent, translating into UGX 370 billion in compensation paid by the government. Benchmarking in the contract was of two categories, one for termination, and second was for setting tariff. The 38 percent loss benchmark refers to the cap beyond which, if exceeded by Umeme, the contract would be terminated without government compensating Umeme. While Umeme maintains that losses were not considered in determining tariff, expert's opinions show that power losses are considered when determining tariffs, including other factors such as foreign exchange rates, inflation, and prices of oil. Hence, prices fluctuate as energy prices also fluctuate.

A public relations message from Charles Chapman, Managing Director – Umeme maintains before Umeme came in 2005, the national energy consisted of only Uganda Electricity Board, which generates, transmitted and distributed the national power. He stated that UEB had problem of specialization. I disagree with this idea that UEB was facing specialization problem and great inefficiency, and that the solution was privatization, out of all what the state can do to the energy sector. This was the beginning of energy sector crisis in Uganda; public interest started conflicting with private interest of profit making in a natural monopoly that should have been reformed and strengthen to lead in the process of economic transformation. In 2001, UEB was unbundled to form four companies; Uganda Electricity Generation Company Limited (UEGCL) for generating electricity, Uganda Electricity Transmission Company Limited (UETCL) for

transmission of power to distributors, Uganda Electricity Distribution Company Limited (UEDCL) distributing power, who are the network of users, Rural Electrification Agency (REA) and Electricity Regulatory Authority. In 2005, UEDCL concessionaired parts of its network to three distributors: Umeme, WENRECO (West Nile) and Ferdsult (parts of western Uganda). In the subsequent years, more distributors were admitted such as Kilembe Investment, Bundibugyo Electrical Cooperative Society, and Abim and Pader Cooperative Society. Today, the three remaining distributors are Umeme, WENRECO and Ferdsult. The Managing Director however, failed to explain the reasons why Umeme joined the sector. The purpose was correcting state failures when it engages in the economy. I agree with the argument that Umeme is not solely responsible for the power problems in the country, what I don't agree with is whether privatization of the electricity, hurriedly done was the best option for Uganda. The performance indicators identified and agreed upon, which serve as the guiding principles include: (1) level of investment; (2) bringing down energy losses; (3) growing the customer base; and (4) improving collections. On government subsidies, the actual cost producing each unit of power was UGX 697. However, government has committed to buy down to UGX 385.6 by providing subsidies to the tune of UGX 488 billion to the UETCL for power supplies (The New Vision, Thursday, 15th September 2011). On the demand-supply forecast today, the demand today is 443 MW and the total produce is averaging between 300-420 MW, giving a shortfall of 120-140MW. Out of the total power produce, 180 MW is hydro and the rest is thermal.

Electricity sector in Uganda is in a serious crisis. According to UETCL, Uganda experiences power supply shortfall of 50 MW during day and 120 MW during evening hours. It costs the economy US$ 400 million in goods and services. This has forced government to subsidize electricity users UGX 92 billion every year to cut domestic power costs. Government subsidizes electricity sector UGX 92 billion every years to cover losses and keep prices low (The New Vision, Sunday, 5th July 2009), pays Umeme UGX 92 billion annually to pay for power losses, ranging between UGX 8 billion to 11 billion a month (The New Vision, Thursday, 16th July 2009). However, subsidies have not helped in keeping prices low. Appearing before the Parlimentary Committee on Energy, Energy Minister Irene Muloni stated that government will continue subsidizing thermal electricity generation until Bujagali first and second unit projects are completed. The government since 2005 has been paying 60 percent in subsidies for electricity consume by Ugandans. Domestic consumers pay UGX 426 per unit (The New Vision, Wednesday, 10th April 2011). Bujagali power project is a project privately financed, funded by the World Bank Group, the European Investment Banks, and other European Banks such as Kfw/DEG Bank of Germany, FMO of Holland and AFD/proparco of France (The New Vision, Friday, 2nd October 2009). The government owes independent thermal providers UGX 207.5 billion and this has been accumulated due to subsidies to shield consumers from tariff shocks (The New Vision, Tuesday, 9th August 2011). Thermal power production accounts for 170 MW, Aggreko in Jinja produces 50 MW, Mutundwe 50 MW, Namanve 50 MW, and Electromaxx in Tororo produces 20 MW (The New Vision, Wenesday, 16th Feb 2011). Umeme maintains that electricity end-user tariff is mainly driven by the cost of generation such as fuel, transport and transmission costs, non-Umeme losses and exchange rate variations (The New Vision, Wednesday, 1st December 2010). In 2006, thermal power generation accounted for 23 percent of Uganda's energy. In 2011, it then accounted for 46 percent. The cost in 2011 was 85 percent compared to 73 percent in 2006. Distribution losses have reduced from 35 percent in 2009 to 27 in 2011(The New Vision, Wenedsnesday, 20th July 2011). Despite all these problems, Umeme claimed to have done some improvement in some areas. Umeme's collection rates have improved from 92.5 percent in 2009 to 96.5 percent in 2011, while consumer connections have increased from 37,000 in 2010 to 51,000 in 2011.

The private sector is failing in rural electricity program in West Nile. The West Nile Rural Electricity Company, WENRECO is ever in financial crisis. They also have very high tariffs and has failed to construct Nyagak hydro-electric power plant due to lack of finance. The thermal plants were brought to bridge power deficit occasioned by delays in commissioning the 250 MW Bujagali Project. As a result, the government must spend UGX 396 billion yearly to pay independent power generator in order to subsidize electricity consumers (The Monitor, Thursday, January 2012).The electricity subsidies are because of reliance of expensive thermal generation, coupled with increasing costs of diesel and the high inflation rate in the country. In fact, Umeme investment is not convincing since government does know about the true cost of their investment. This is a form of government failure, failure to control private sector responses on its action.

POLICY RECOMMENDATIONS

The Privatization of the energy sector, in this case the electricity in particular generates the rationale for the complementary role of the government. This is argument is based on the existence of natural monopoly in electricity sector that is associated with high costs, long gestation period if a new project is to be developed, and this has resulted into continuing state subsidies, the possible price ceiling and regulations by government.

In addition, there are both coordination problems and the divergence interests between Umeme and that of government and other stakeholders. The former is driven by profit motive, which is not in the interest of the public interest in general. This calls for the need to review entry requirements, operational conditions, incentives, and legal frameworks since the rule of the game favors Umeme despite its poor service delivery. In this case, the regulatory authority must have the capacity to address information and coordination failures. The development of private investments in dams through Greenfields and joint ventures can be maximized through the window opportunities of donor support and regional support of NEPAD in energy development projects. The south-south cooperation with South African investors can bear positive outcomes since South African companies; in this case Eskom Company is taking active role in the generation sector.

CONCLUSIONS

The government has been an admirer of free market philosophy, but has failed to accept the fact that private sector is not the best in everything. At the same time, government is not good at doing everything. There are things government does better than the private sector when all limitations are considered pragmatism. Privatization could be a good practice, but electricity sector is associated with high sunk cost, long gestation to generate when it is supposed to be done by private capitals, which are vulnerable to exogenous factors, as well as the possibility of price ceiling and regulations, by the host government. In the context of a natural monopoly in a developing country, where coordination problems are common, government should have remained to lead the energy sector in order to develop its competiveness, and achieve the goal of rural electrification program. In the past years of concession, things have gone from bad to worst. Electricity losses are not reduced to minimal, poor service delivery; billing and connection are very poor. Citizens are greatly concerned with high user charges, daily load shading, and state's subsidies to domestic consumers to keep the electricity costs low. However, subsidies are not sustainable since the burden of subsidies is spread out through taxation, especially to non users – the rural poor. Because Umeme is driven by profit motive, the quest for higher tariffs has been inevitable since 2005 to service its debt obligations and increase its investments, which has been the point of contention with the executives.

Umeme is in a state of market failure. The demand for electricity is more than the supply. The existence of subsidies to keep prices low and coordination problem are fundamental indicators for the government to intervene. Uganda Electricity Board would have been very instrumental in developing the electricity capacity of the country, a practice which is associated more with state capitalism in boosting the energy export to neighboring countries. The country just destroys its competitiveness in energy investments. What is easily noticeable is that government and the private sector have their own strengths and weaknesses. In some instances, the market is better in delivering services than government, but not in all sectors. Government has relatively higher competitiveness than the private sector when it comes to utility sector; in this case electricity, since the sector needs higher investment. Umeme demands for higher power bill to service its debt obligations in concession payment to UEDCL and also to increase its investment. The government could easily raise this money through taxation and or other means since electricity is more of merit good. When it comes to coordination problem, having one strong point was the better option than giving to different parties, motivated by profits rather than public value. This is the problem. While this argument might divert our orientation from the neo-liberal orthodoxy of judging the government engagement in the economy as a failure, the common position here is that government should have only strengthen the electricity sector. In fact, in an emerging economy, government needs to lead in providing core good such as electricity.

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