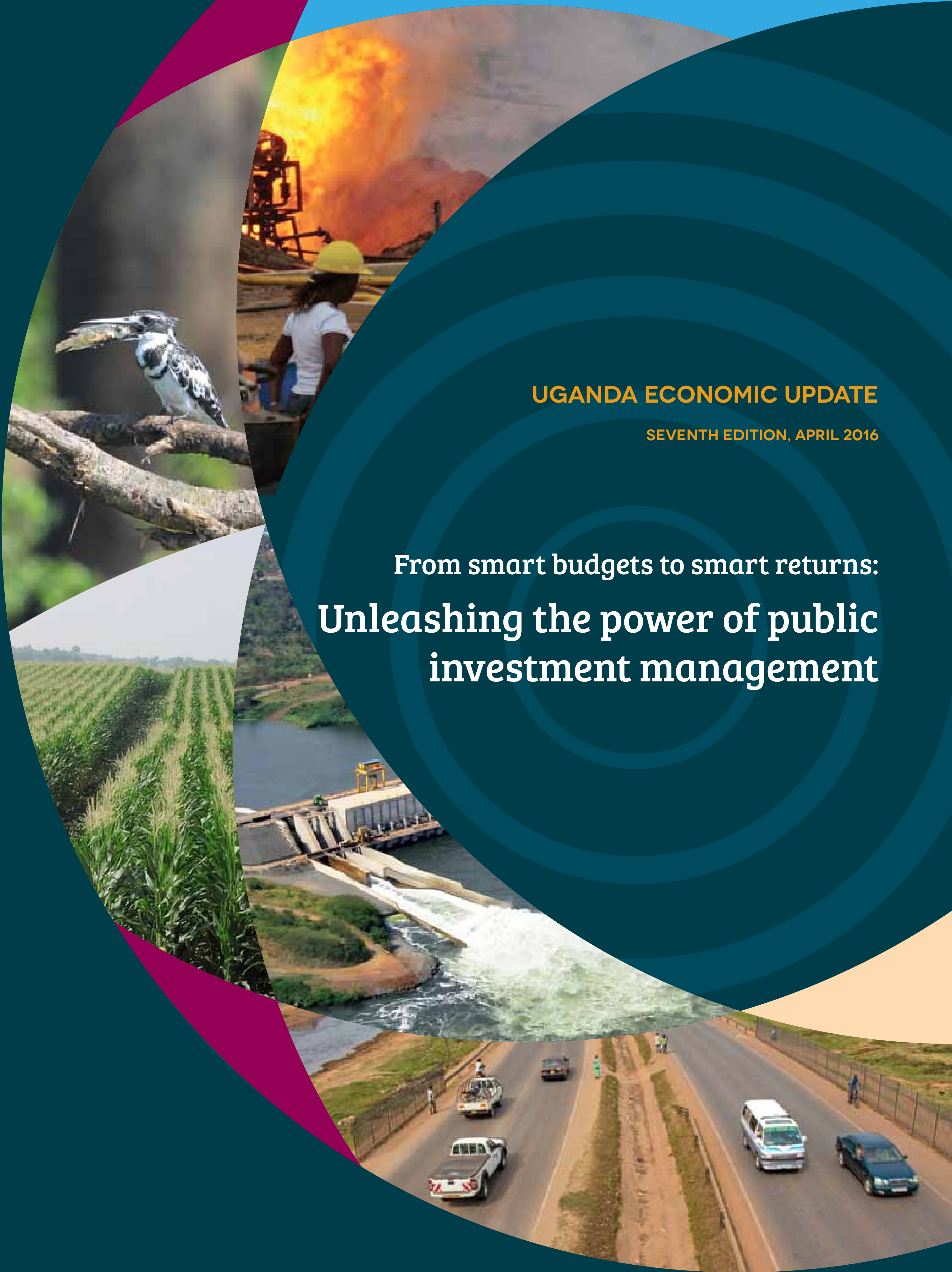

UGANDA ECONOMIC UPDATE

SEVENTH EDITION, APRIL 2016

From smart budgets to smart returns:

Unleashing the power of public investment management

THE WORLD BANK
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Additional material relating to this report can be found on the World Bank Uganda website (www.worldbank.org/uganda). The material includes a fact sheet, documentary video and a number of blogs relating to issues in the report.

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ABBREVIATIONS AND ACRONYMS

ASYCUDA	Automated System for Customs Data
BoU	Bank of Uganda
BOP	Balance of Payments
BPD	Barrels per day
CBA	Cost-Benefit Analysis
CBR	Central Bank Rate
CEM	Country Economic Memorandum
CNOOC	China National Offshore Oil Corporation
CPI	Consumer Price Index
CPIA	Country Policy and Institutional Assessment
COICOP	Classification of Individual Consumption According to Purpose
COMESA	Common Market for Eastern and Southern Africa
DRC	Democratic Republic of Congo
DSA	Debt Sustainability Analysis
EAC	East African Community
EU	European Union
FDI	Foreign Direct Investment
FY	Financial Year
GDP	Gross Domestic Product
HIPC	Highly Indebted Poor Countries
IBP	Integrated Bank of Projects
ICOR	Incremental Capital Output Ratio
ICT	Information and Communications Technology
IFC	International Finance Corporation
IMF	International Monetary Fund
KIIP	Kampala Institutional and Infrastructure Project
LIBOR	London Interbank Offered Rate
MDRI	Multilateral Debt Relief Initiative
MFPED	Ministry of Finance, Planning and Economic Development
MoLG	Ministry of Local Government Economic Development
MDA	Ministries, Departments and Agencies
MoLG	Ministry of Local Government
MTEF	Medium Term Expenditure Framework
NBFP	National Budget Framework Paper
NCN	Non-Concessional Borrowing
NDP	National Development Plan
NEER	Nominal Effective Exchange Rate
NPA	National Planning Authority
ODA	Official Development Assistance
OECD	Organization of Economic Cooperation and Development
OPM	Office of the Prime Minister
PAPP	Project Analysis and Public–Private Partnerships
PDU	Procurement and Disposal Unit
PFMA	Public Finance Management Act
PFM	Public Financial Management
PIMA	Public Investment Management Analysis
PIMAC	Public and Private Infrastructure Investment Management Centre
PIMI	Public Investment Management Index
PIMS	Public Investment Management System
PPDA	Public Procurement and Disposal of Public Assets Authority
PPP	Public-Private Partnerships
RAPs	Resettlement Action Plans
RDP	Reconstruction and Development Plan
REER	Real Effective Exchange Rate
SBFP	Sector Budget Framework papers
SMEs	Small and Medium-sized Enterprises
SSA	Sub-Saharan Africa
SWA	Sector Wide Approach
SWG	Sector Working Group
UEU	Uganda Economic Update
UBOS	Uganda Bureau of Statistics
UNHS	Uganda National Household Survey
UGX	Uganda Shillings
USA	United States of America
URA	Uganda Revenue Authority
UNRA	Uganda National Roads Authority
VAT	Value Added Tax
WB	World Bank
WDI	World Development Indicators

FOREWORD

Accelerating Uganda's structural transformation and transition towards middle income status will require facilitating higher levels of growth, improving productivity, and creating jobs for the large and growing population. Policymakers in Uganda know this well, and a key strategy that Government has pursued over the past seven years has been to adjust the fiscal policy to provide more resources for capital development. In line with the National Development Plans, this strategy is expected to be continued into the medium term in order to address a binding constraint on growth, the country's huge infrastructure deficit. The intention to increase the level of capital investment is further driven by the prospect of revenues from oil exploitation, which in turn, can generate revenues to finance infrastructure and human capital investments.

This Seventh Edition of the Uganda Economic Update discusses the importance of accompanying this fiscal strategy with sound public investment management systems. Indeed, a key risk to Uganda's fiscal strategy relates to the potential for public investments to fail to yield the expected growth and welfare dividend. Over the past decade, for every dollar invested in Uganda's capital infrastructure, only seven-tenth of a dollar has been generated. This is far below countries that have successfully undergone structural transformation. As an example, every dollar invested in the development of the interstate highway network in the United States of America between 1954 and 2001, generated six dollars' worth of economic activity. In other words, Uganda's public investments are falling short of generating the desired economic return. The good news is that by improving public investment management, Uganda can greatly increase her economic growth rate and social impact of her investment strategy.

Our forecasts show that the Ugandan economy will be growing at an average rate of about six percent into the medium term. Yet, if the country operated at a higher level of efficiency, this growth rate could increase to almost 10 percent per annum, thereby allowing Ugandans to enjoy middle income status within the next five years. Uganda, needs to invest in her ability to invest by transforming her public investment management system so that it generates more. This involves carefully scrutinizing public investments selection so that it actually improves public welfare; ensuring that investments are managed effectively and completed on schedule; and overseeing that infrastructure assets are operated and maintained efficiently and sustainably.

I am pleased to introduce this Seventh Edition of the Uganda Economic Update series. I hope that it will serve as valuable input to policy debates, and motivate a comprehensive set of actions to increase the returns on public investments to catalyze much needed transformation of the economy. This is absolutely essential for boosting inclusive growth and accelerating poverty reduction in Uganda.

Diarietou Gaye
Country Director
Eritrea, Kenya, Rwanda and Uganda
Africa Region

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KEY MESSAGES

Over the past decade, Uganda has planned an investment push intended to accelerate and sustain the high levels of economic growth and to spur transformation into a middle income country. Mandated by its National Development Plan (NDP), this move aims at addressing the binding constraints on growth, with the most significant of these being the country's huge infrastructure deficit. The intention to increase the level of capital investment has been further driven by the prospect of revenues from the exploitation of oil, which would create new opportunities to allocate additional resources to finance critical infrastructure and also invest in human capital. While the resultant expansionary fiscal strategy has squeezed the fiscal space for spending on social sectors amidst low levels of revenue, it could be justified by the potential accompanying dividends, including higher growth and higher domestic resources, which in turn can drive faster development, including human capital accumulation.

The fiscal strategy hinges on these investments generating the expected growth dividend. Is this happening? While the fiscal strategy of the early 2000s was accompanied by high growth rates, the recent increase in the size of deficits has not yet resulted in a similar acceleration to the economic growth rate. In order for capital investments to contribute to increased growth and improved productivity, they need to feed into higher public capital stock that facilitates reductions in the cost of production. This would then support the private sector to engage in higher levels of economic activity and to generate a greater number of productive jobs. This rate of economic and social return depends to a very significant extent on how effectively and efficiently public investments are managed.

Following previous editions, the seventh Uganda Economic Update presents an assessment of the current state of the economy, before addressing a specific theme of significance for the country's development. This edition focuses on how the management of public investments could be improved to maximize the economic and social value of these investments. Well-designed, well-managed, and well-implemented public investments are a sine qua non for Uganda's economic transformation. Efficient management of public investments is essential also for ensuring that oil revenues will play a positive role in the country's transformation.

Part 1: State of the economy

During FY 2015/16, the Ugandan economy faced a number of developments with anticipated challenges for economic management. This included the staging of a national election, and a slowing global economy and subsequent declining commodity prices. The latter developments were associated with policy adjustment in China and structural impediments to growth in big emerging market economies such as Brazil. During the year, the Ugandan authorities also commenced the implementation of a new NDP, which necessitated some adjustments in strategy. With such developments, some degree of macro volatility was inevitable, not least due to the uncertainties surrounding the elections, given the experiences from the 2011 elections, when inflation rose to a two decade-high. Uganda's economic policy makers focused on managing these volatilities.

Monetary policy coped well with what was anticipated. By September 2015, the Shilling had depreciated against the dollar by more than 40 percent, compared to the year before. This change in the Ugandan currency had not been experienced since the forex market was liberalized in 1994. The rate of inflation also went up to reach 8.5 percent by December 2015, with the expectation at that time that it would rise further, particularly because of the effect of the depreciating Shilling. To avoid inflation becoming embedded, the Bank of Uganda raised its policy rate by six percentage points over 12 months to October 2015. Interest rates on government securities and for lending to the private sector increased rapidly as the financial market re-adjusted to the tighter liquidity conditions.

Despite policy success in containing spill-overs, the combined effect of the resultant volatility on private investments was quite severe, through the lower access to funding from domestic banks, as well as from external sources. The rate of growth of credit to the private sector declined from 24 percent per annum during the first quarter of the fiscal year to 8.7 percent by March 2016, reflecting the tightened money conditions. Surprisingly, the volatility in the Shilling did not deter agents from borrowing in dollars, even though the bulk of them were engaged in activities that provide incomes in Shillings, thus risking increased exposure with the depreciating currency. On the part of external sources, the private sector received lower funding through foreign direct investments, which is estimated to have declined from US$ 1.1 billion to US$ 0.8 billion between FY 2014/15 and FY 2015/16, and from remittances that decreased from US$ 1.3 billion to an estimated US$ 1.2 billion over the same period. In addition, Uganda realized lower than usual receipts from export of goods and services, due to a combined effect of low demand and low commodity prices. Under these circumstances, private investments are estimated to have reached levels that are far lower than had been anticipated.

Uganda's external position remained weak, largely due to the impact of the weak global economy; the associated sustained decline in global commodity prices; and the uncertainties related to an election year. The impact of reduced cost of oil imports lowered the goods trade deficit, but this was more than offset by the increased volume of imports required to support construction. Meanwhile, the declining global incomes and commodity prices also reduced the value of total exports receipts, which led to a widening of the trade deficit, increasing from an estimated value of 8.5 percent of GDP during FY 2014/15 to 9.3 percent. With the additional negative impact of the decline in services, income and transfers, the external current account is estimated to have reached a value of 9.6 percent of GDP during FY 2015/16.

The execution of fiscal policy was generally effective, which resulted into spending closer than usual to the budgeted levels. According to figures released by the Ministry of Finance in May 2016, fiscal revenues and expenditures remained largely on target throughout the year. The anticipated fiscal expansion materialized, with the deficit remaining at high levels, at an estimated value of around 6.4 percent of GDP, which is only slightly lower than the originally expected value of 6.6 percent of GDP. Prudent fiscal management by the authorities was complemented by good performance in the area of revenue collection, for which the value reached 13.9 percent of GDP, compared to the budgeted level of 13.6 percent. With construction of two large energy projects taking off, the execution of the development budget was much better than in previous years, recording a small shortfall from the budget of 0.5 percentage points of GDP. Therefore, even though there was overspending in the recurrent budget, largely due to expenditure on election and security related measures, total expenditure is expected to have reached 22.1 percent of GDP, the level that was planned for in the budget.

The stimulus effect of fiscal expansion and the stabilization of expectations was not enough to outweigh tightened private liquidity, hence GDP growth during FY 2015/16 is estimated at 4.6 percent, more than one percentage point lower than had been forecast by the authorities. The estimated growth is also more than half a percentage point lower than the forecast in the previous World Bank Economic Update. This was the result of a stronger than anticipated impact of macroeconomic volatilities on private sector activities during the year. The main driver of growth was public investments, which however represents a smaller share of the economy where services account for close to half.

With macro-fiscal uncertainties related to elections now dissipating, the economic outlook is positive, with the rate of growth projected to reach approximately 5.9 percent in FY 2016/17, and to remain on an upward trajectory into the near future. The weak global economy will continue to affect economic activity in Uganda, as it has done during FY 2015/16. However, from this perspective, the economy will also benefit from the low energy prices, particularly if investors take advantage of the associated low cost of imported inputs. In addition, growth will also be driven by an intensification of investments by the private sector in the post-election period, particularly in oil-related activities. Yet the predominant driver of growth will be an increase in the economic activities of the construction sector, with this growth driven by Uganda's significant investments in public infrastructure projects. The stimulus effects from this large public investment program will offset those of a weak external sector on the Ugandan economy, with carry-through to FY 2017/18, when the rate of economic growth is expected to increase to above 6 percent.

Despite the generally favorable outlook, a number of risks could reduce the country's growth outcome. The risks include the low revenue base, which is being further threatened by a renewed appetite for tax exemptions; the sequencing, financing and management of the large infrastructure investment program; an increase in debt beyond the threshold of 50 percent of GDP should the investments not generate sufficient growth and revenues to service the growing debt; as well as exogenous conditions, such as bad weather, regional instability, and protracted low growth of the global economy. Policy makers must strive to ensure that the infrastructure program results in efficiency and productivity improvements and in oil production capacities to exploit oil in a manner that generates economic opportunities for the maximum possible number of Uganda's citizens. To achieve this, the appropriate selection, sequencing and good overall management of the financing and implementation of the Government's huge infrastructure development program are vital.

Part 2: Moving beyond spending to creating productive assets

Uganda's development plan and budgets clearly signal an investment-driven growth phase to enable structural transformation and development of oil resources. In line with national development objectives, the fiscal policy has been expansionary over the past five years. However, on average, up to 36 percent of the planned spending over this period did not materialize, with the bulk of this under-spending recorded in the priority sectors of energy and transport. Budget execution challenges are matched by overall inefficiencies in investments and consumption has increasingly become the largest contributor to increases in economic activity. There are also indicators that there is a decline in efficiency in utilization of public capital. Going forward, these inefficiencies in investment could limit the rate of accumulation of capital, as it has done in many other countries, thus curtailing the desired socio-economic transformation.

If such inefficiencies persist, increased investments will not be converted into productive assets to support accelerated economic growth rates. The budget process suffers from an overhang of incomplete projects, which become perpetual, with continuing demands on the budget or even requiring additional resources when poorly implemented. When budget execution struggles, there is a high risk of stop-and-go cycles in investment, which can worsen volatility, especially when oil revenues come on-stream.

Realizing the gains from the ambitious fiscal strategy will require addressing existing investment inefficiencies. The efficiency with which the capital stock is used is a powerful lever with which to increase growth. It has been estimated that if efficiency of infrastructure investments in Uganda was doubled, the economic growth rate would increase by nearly three percentage points. Therefore, it is vital that the country 'invests in its ability to invest'.

Converting investments into productive assets requires an effective management of public investments at all stages of the project cycle, from when a project idea begins to the management of the completed asset. To assess how Uganda performs in terms of public investment management (PIM), against good practices around the world, the World Bank, working with Ministry of Finance, Planning and Economic Development and other stakeholders, assessed Uganda's existing PIM system. The overall conclusion: *Uganda has made effort to build institutions, often inspired by universal best practice. While chasing best practice in every area, the focus can be placed on the essential "must have" features for sound functionality.* In fact, as a result of previous reform efforts to improve the overlapping area of public financial management, Uganda's PIM system has a number of good practice elements. Nonetheless, there is ample room for improvement, particularly in the preparation of projects, which determines projects *'quality at entry',* and their execution. In terms of the overall quality of the institutional environment underpinning PIM, Uganda ranks in the 46th place out of 71 countries, well behind good performers in the region, such as Ghana (in 27th position) and Rwanda in (12th place).

Deficiency in quality at entry explains the pervasiveness of problems from implementation delays; such as cost escalations, time-overruns; contract disputes; abandonment of projects; poor quality of some completed projects; and rapid depreciation of public capital stock. At present, the public investment practice involves ad hoc identification of projects, with project analysis only being conducted after the financing has been allocated, combined with inefficient management of the implementation and maintenance of the public assets that it produces. This Update recommends a systematic approach to building capacities along three pillars:

A. Streamlining and strengthening the institutional arrangements for the management of public investments;

B. Ensuring a shared understanding across institutions regarding what needs to be done and how it should be done by standardizing the information and documentation needed to guide the identification, formulation, preparation, appraisal, investment decision, execution, operation, monitoring and evaluation of projects across all implementing agencies; and

C. Determining where gaps in the legal and regulatory environment exist and how they should be closed to strengthen mandates and the incentive structures.

Good reforms are underway, but will need to be reinforced while building momentum to follow-through with a more sustained reform program. The Government should focus on addressing constraints that have the most significant impact on the achievement of good investments now and in the short term. At the same time, the Government should build momentum for reform actions to be implemented over a five year period. It is therefore recommended that the reform plan could move as follows:

Immediate actions to progress PIM reform

The six actions that Government can pursue immediately are:

1. **Formalize and strengthen independent review of new project proposals.** The new Project Analysis and Public-Private-Partnerships Department within the Ministry of Finance, Planning and Economic Development, can be nurtured and groomed to perform the role of an independent reviewer. This would strengthen the role of the Ministry as the gate-keeper with respect to spending of public resources to generate value. (Action A1 in the PIM Reform Action Plan below)

2. **Build the capacities of Ministries, Departments and Agencies (MDAs) and other implementing agencies, particularly in the area of project preparation, appraisal, approval and monitoring phases. I**n the short term, training should be focussed on capacitating a core group of technicians across the different MDAs involved in the preparation and appraisal of projects within their own agencies. Building and sustaining the range of skills required for effective PIM system can be accelerated through the establishment of linkages with higher education centres. Susequently, building capacities at all levels of the Government, would require developing training programs targetting officials and staff at the basic, intermediate and advanced levels for all agencies, particularly those involved in preparing and implementing projects. *(Action A2 in the PIM Reform Action Plan)*

3 **Document and implement good practice operational processes, starting with project preparation and appraisal.** These will be used by all MDAs to ensure that they implement measures to achieve economic evaluation of projects. A key component of this exercise will be to establish a set of standard national parameters, including shadow prices, unit costs, and the discount rate, as well as standard criteria for project performance indicators, aimed at ensuring that projects are aligned with national strategies priorities. *(Action B1 in the PIM Reform Action Plan)*

4. **Create a technical fund to facilitate feasibility studies during the pre-investment stage.** This is a prerequisite for ensuring that agencies can actually undertake the required feasibility studies. Similar modalities could be adopted for both GOU and externally funded projects to ensure projects are properly prepared by the MDAs before they are submitted for consideration in the medium term fiscal framework. *(Action B2 in the PIM Reform Action Plan)*

5. **Establish a standard framework for the monitoring and evaluation of all public capital investment projects under implementation.** While MDAs currently undertake this function to some extent, and monitoring and evaluation is being done both by the MoFPED and Office of the Prime Minister, there needs to be a single entity and standard framework that can ease tracking and ensure remedial actions. The immediate step under this action could be to re-assess the existing portfolio of projects already under implementation and take action where financial and technical risks are highest. *(Action B3 in the PIM Reform Action Plan)*

6. **Formulate a policy framework for PIMS**. This will create the background for overall understanding of the PIM system across the various institutions of government, including the executive, parliament and the judiciary, and will thereafter be the basis for legal and regulatory changes for its implementation. *(Action C1 in the PIM Reform Action Plan below)*

Medium term actions to progress reform of the PIM processes

In the medium term, Government should consider implementing further improvements in efficiency and effectiveness in PIM. Four actions to achieve this include:

1. **Clarify roles, mandates and responsibilities of various entities within the PIM process.** This will require re-evaluating the different entities, each of which has specific roles to play within the project cycle to remove redundant, un-coordinated, overlapping responsibilities, which leads to wastage and inefficiency. The outcome should be a mapping and re-engineering of the PIM processes to support the better implementation of projects. *(Action A3 in the PIM Reform Action Plan below)*

2. **Develop an integrated bank of projects (IBP), to constitute a central database and depository for public projects, including pipeline projects, with clear criteria and a systematic approach for their inclusion.** Such a data bank directly corresponds to the function of improving the quality-at-entry and having ready to go projects for implementation. It should contain information related to beneficiaries, sector statistics, technical parameters, demographics, information on poverty, social indicators, and other matters relevant to project formulation. In order to manage the IBP effectively, it will be necessary to build focussed systems capacity in technical (such as software management, data collection for project formulation at sector level) and in non-technical matters (such as the interpretation of information from the IBP to ensure it is used efficiently and appreciation of usefulness of the process to PIMS. *(Action A4 in the PIM Reform Action Plan below)*

3. **Enhance the legal and regulatory framework required to support PIM.** Implementation of the PIM system may expose gaps in the existing legal and regulatory framework that may warrant amendments or the enactment of new laws to strengthen the system. *(Action C1 in the PIM Reform Action Plan below)*

4. **Develop a system for monitoring and ex post project evaluation of projects.** A system to facilitate the evaluation of past project experiences and to formulate lessons learned to serve as input for future project designs and implementation is vital. To achieve this, it is equally vital to build capacities for managing the system. *(Action B4 in the PIM Reform Action Plan below)*

The PIM Reform Action Plan

IMMEDIATE ACTIONS

A. STRENGTHEN PIM INSTITUTIONS

A1 Formalize and strengthen an independent reviewer of project appraisals

A2 Build capacity of MDAs in project preparation, appraisal, and monitoring of projects.

B. STANDARDIZATION OF GUIDANCE IN PROJECT DESIGN, APPRAISAL, SELECTION, OPERATION, AND M&E

B1. Develop manuals and guidelines to implement the PIM framework

B2. Create a project preparation fund to facilitate pre-investment stage preparation

B3. Create a standard framework for M&E of on-going

C. ENHANCEMENT OF THE POLICY, LEGAL AND REGULATORY FRAMEWORK SELECTION

C1. Formulate a policy framework for PIM system

MEDIUM TERM ACTIONS (2017-2018)

A. . STRENGTHEN PIM INSTITUTIONS

A3. Clarify institutional roles, mandates and responsibilities of various entities.

A4. Develop an integrated bank of projects(IBP), including acquiring the software systems and building capacity in managing the system

B. STANDARDIZATION OF GUIDANCE IN PROJECT DESIGN, APPRAISAL, SELECTION, OPERATION, AND M&E

B4. Develop a standard framework for EX- POST monitoring and evaluation of projects, including building capacities to implement it.

FORMALIZE THE ROLE OF KEY PERFORMANCE INDICATORS

C2. Enhance the legal and regulatory framework for PIM by closing gaps that will arise as the system and processes are re-engineered.

PART 1

THE STATE OF THE ECONOMY

- *As was expected in an election year, the Ugandan economy faced volatilities - currency depreciation, inflation, and high interest rates during FY 2015/16. Real GDP is estimated to have grown by 4.6 percent, with growth mainly driven by services and construction, as two key public projects took off.*

- *The growth disappointment was due to a sizable negative impact on private investment, which declined in face of a high level of uncertainty related to the staging of the national elections, the subsequent volatilities in domestic variables as well as volatile global economic conditions.*

- *Monetary tightening achieved the objective of lowering inflation, as the cost of credit further reduced the rate of growth of credit to the private sector. Surprisingly, dollar-denominated credit remained buoyant amidst a volatile domestic currency.*

- *The upside surprise was the materialization of the planned spending, especially on the capital budget, and the deficit remaining at the expected value of around 6.4 percent of GDP. Budget re-adjustments, amounting to almost five percent of original budget, were mainly due to election related supplementary spending.*

- *Uganda's external position remained weak, largely due to the impact of the weak global economy; the associated sustained decline in global commodity prices; and the uncertainties related to an election year. The external current account deficit is estimated to have reached a value of 9.6 percent of GDP during FY 2015/16.*

- *The economy is projected to grow at approximately 5.9 percent in FY 2016/17 and thereafter to remain on an upward trajectory into the near future. This acceleration will be driven by Uganda's significant investments in a number of public infrastructure projects and an intensification of investments by the private sector in the post-election period, particularly in oil-related activities.*

- *The main risks relate to the volatility of the global economy, particularly as the Chinese economy slows down. However, if the Government's huge infrastructure development program is not implemented appropriately, it may result into low absorptive capacity; build-up of debt; and failure to achieve efficiency and productivity improvements in the economy.*

- *Poor implementation specifically threatens the ability of fiscal policy to facilitate the achievement of Uganda's development goals. It is vital that policymakers strive to achieve a higher level of efficiency in the public investment management regime.*

1. RECENT ECONOMIC DEVELOPMENTS

The Ugandan economy is estimated to have grown at a rate of 4.6 percent during FY 2015/16, which was much slower than the projected rate of 5.8 percent. With the take-off of a number of the energy projects boosting public investment, the slower than anticipated growth can be attributed to the adverse impact of both domestic and external volatilities. The tightening of monetary policy was necessary to address inflation pressures, but raised the cost of credit, which affected private consumption and investment. Fiscal policy was implemented well, keeping overall expenditure within the budgeted levels, even though there were reallocations of funds to recurrent expenditures, mainly on account of election-related pressures.

Over the past five years, the Ugandan economy recorded some positive growth, despite a number of challenges resulting from both domestic and external factors. In FY 2014/15, the rate of growth was 5.0 percent per annum. This growth rate sustained the momentum achieved after the economic growth rate had increased to 5.2 percent in FY 2013/14, from 3.6 percent recorded in FY 2012/13, according to the Uganda Bureau of Statistic (UBOS)'s revised GDP series. This recovery was mainly driven by a growth in consumption, since there was a deceleration in the rate of growth of gross investments over this period. To a certain extent, the economy stabilized, with the rate of inflation declining from 23.5 percent in FY 2011/12 to 3.0 percent in FY 2014/15, even though increasing food prices and currency depreciation began to exert an influence towards the end of the year. It was also challenging for policymakers to manage the impact of the unpredictable global environment, with Uganda's external current account deficit increasing from a value of around 7.8 percent of GDP in FY 2012/13 to 9.6 percent in FY 2014/15. In addition, Uganda's economy operated in the context of significant regional political challenges, mainly due to the unrest in neighboring South Sudan and the Democratic Republic of Congo and to isolated terrorist incidents in Kenya. All of these factors had an impact on Uganda's spending needs, exports, and remittances.

At an estimated rate of 4.6 percent during FY 2015/16, Uganda's economic growth is far lower than the rate recorded in the decades following reform. With the low per capita income and high vulnerability to poverty, the rate of economic growth is not sufficient to reach the national target of achieving middle income status by FY 2019/20. In FY 2014/15, the average per capita income is estimated to have reached US$ 740. While this is slightly higher than the average for low-income countries (US$ 629), it is less than half of the average for Sub-Saharan Africa (developing only) countries (US$ 1,638). The number of households living below the international poverty line, measured at US$ 1.9 per day in 2011 PPP terms, is expected to have declined further to about 33.2 percent in FY 2014/15, from 41.5 percent five years ago. However, despite this impressive decline in the poverty rate, 43 percent of the population continues to live just above the poverty line and therefore remains highly vulnerable and at risk of falling back into poverty in the case of economic shocks. While the structure of the economy is slowly changing, approximately three-quarters of the population still depend primarily on low paying jobs in the agricultural sector, with the majority employed in subsistence farming, which contributes to approximately 25 percent of the total value of GDP.

UGANDA RECORDED A RATE OF ECONOMIC GROWTH OF 4.6 % IN FY 2015/16. A RATE SIGNIFICANTLY LOWER THAN RECORDED IN RECENT HISTORY AND LOWER THAN THAT OF REGIONAL PEERS IN THE EAST AFRICAN COMMUNITY (EAC)

In FY 2015/16, Uganda began the implementation of its second National Development Plan (NDPII), the same year that it conducted its national elections. The NDPII, which covers the period from FY 2015/16 to FY 2019/20, is the second of a series of six five-year plans intended to facilitate the achievement of a vision for Uganda's economic and social transformation by 2040. The NDPII builds on a number of projects and initiatives implemented under the previous plan, with a particular focus on addressing Uganda's infrastructure deficit and on preparing for the production of oil. The beginning of the period of the new plan coincided with the preparations for presidential, parliamentary, and district-level election period, which took place in February-March 2016. With memories of tensions in the area of economic management during the previous election period, in 2011, there were concerns regarding the possible re-occurrence of similar events. With additional challenges created by the volatile external environment, policymakers had to manage these concerns carefully while remaining focused on an economic management drive intended to address structural issues to sustain overall growth and economic development over the longer term.

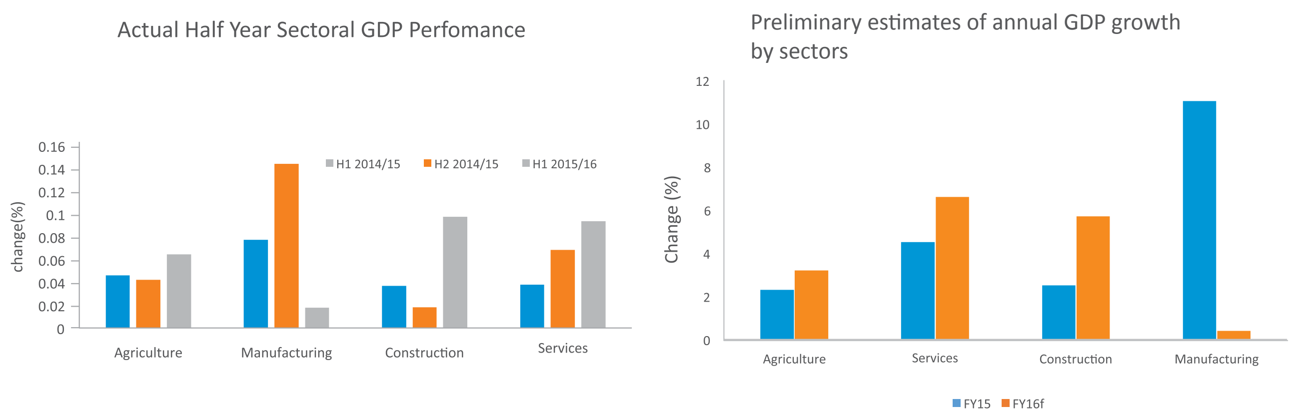
1.1 GROWTH SLOWED DOWN DUE TO UNCERTAINTIES

During FY 2015/16, Uganda recorded a rate of growth of 4.6 percent (preliminary estimate) as a result of both domestic and external uncertainties. This was lower than 5.4 percent, the rate which had been forecast in our previous economic update released September 2015, with the largest shortfall in growth coming from private investments. On the basis of revised data from the Uganda Bureau of Statistics this rate is lower than 5.0 percent recorded for FY 2014/15.

The services sector remains the main driver of growth, accounting for an estimated 52 percent of all economic activities. However, increased construction activities also significantly boosted the contribution of the industrial sector. During FY 2015/16, the services sector grew by 6.6 percent, with the bulk of this growth driven by activity in the information and technology sub-sectors. The rate of growth of the construction sector, increased to approximately 5.7 percent, more than doubling the rate recorded in FY 2014/15, when the sector grew by a mere 2.5 percent. This development is largely attributed to the take-off of large public construction works. With a deceleration in the rate of growth of all other subsectors, particularly manufacturing, the overall rate of growth of the industrial sector during the year was significantly lower than in the corresponding period in the previous year (see Figure 1).

The agricultural sector grew at a rate of 3.2 percent during the year, after benefitting from favorable weather conditions, particularly during the first half of the year. This is a higher rate of growth than the rate of 2.3 percent recorded during the corresponding period in FY 2014/15. The impact of low commodity prices at the international market, the sector's performance during the year was better than might have been expected. This is because the average global prices for Uganda's major export commodities, particularly coffee, tea, maize and fish, were generally lower than in the corresponding period in the previous year. A positive factor was the weather conditions during the first half of the year, before the El Nino set in with more volatile and unfavorable patterns during the latter part of the year.

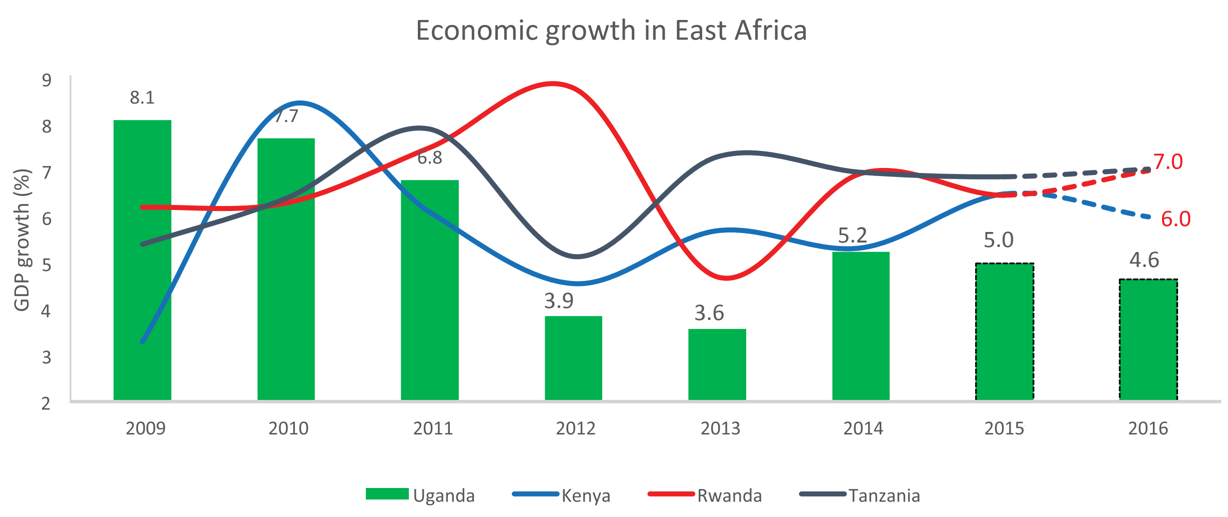
Figure 1: Construction and Services drive economic recovery



Source: Uganda Bureau of Statistics, 2012 and World Bank Staff Estimates

The economic growth recorded in FY 2015/16 was primarily driven by the accelerated rate of execution of public investments in energy infrastructure, with private investment constrained by both domestic and external factors. The value of public expenditure on energy infrastructure doubled to reach around 3.0 percent of GDP, up from 1.5 percent in the previous year. Earlier in the year, the increased availability of credit, the bulk of which went to the construction sector, is also expected to have driven an increase in the level of private investment. However, as uncertainty related to the elections increased, economic volatility, characterized by a sharp depreciation in the value of the Shilling and intensified inflationary pressures, increased. This prompted policymakers to tighten monetary policy, with the result that private sector investment did not achieve the same level of momentum as in the previous year. Economic activity was also constrained by the regional insecurity and the weak global economy which resulted into generally low commodity prices, with all these factors reducing demand for Uganda's exports, FDI inflows and remittances. In particular, Uganda's merchandise exports were adversely affected by the instability in South Sudan and the Congo (DRC); the slow recovery in Europe; and the deceleration of economic growth in China. In total, including both public and private investment, the combined value of public and private investments is estimated to have increased by 6.3 percent in FY 2015/16, compared to the increase of 1 percent recorded in the previous year.

Figure 2: Economic growth in East Africa



Source: World Bank / IMF

Overall, Uganda's economic growth in recent years has been significantly lower than the rates recorded earlier and lower than regional peers (Figure 2). As such, other countries in the East African Community (EAC) achieved significantly higher levels of growth performance from the rest of the sub-Saharan (SSA) region, which experienced a general economic slowdown, with the average rate of growth declining from 4.5 percent in FY 2013/14 to 3.0 percent during FY 2015/16.

1.2 HEIGHTENED INFLATIONARY PRESSURES INDUCED MONETARY POLICY TIGHTENING

Domestic prices tended to increase throughout the first half of FY2015/16, with the rate of inflation increasing to a peak of 8.4 percent in December 2015. In the previous year, the rate of inflation reached its lowest levels for the past five years, mainly due to low food prices resulting from bumper harvests and from low international commodity prices. Even with some pass-through effect from the depreciation in the value of the Shilling to domestic prices, the average rate of inflation for FY 2014/15 still stood at only 3.0 percent. During FY 2015/16, the annual headline inflation rate more than tripled, from 1.8 percent per annum in December 2014 to a peak of 8.4 percent in December 2015, according to the new rebased Consumer Price Index (CPI) launched in January 2016 (see Box 1). The rebasing resulted in an index that generated a slightly lower rate of inflation for this period, together with other moderating factors to the inflationary pressures during the second half of the year. By April 2016, the headline inflation rate had declined to 5.1 percent. Uganda's regional peers also experienced volatile rates of inflation over recent months. For example, Kenya recorded an average annual rate of 6.6 percent in FY 2014/15, with this increasing to 7.8 percent in January 2016, before declining to 5.3 percent in April. In Rwanda, the rate increased to an average of 6.4 percent in the first half of the financial year and had declined to 4.7 percent by April 2016. Surprisingly, Burundi, which has experienced a civil insurgence over the past two years, managed to record a rate 5.6 percent for FY 2014/15, down from 18.2 percent in FY 2011/12.

Box 1: Re-basing Uganda's CPI: What does it mean?

The Consumer Price Index (CPI) is designed to measure changes in the prices of a basket of goods and services consumed by an average household. To facilitate measurement, such prices are based on a basket of consumption goods and services commonly purchased by the households within an economic territory and in reference to a particular point in time, normally referred to as the 'base period'. The pattern of consumption is captured through weights derived from a household survey for the base period. Changes in patterns of consumption can arise due to changes in the socio-economic characteristics of the population; government policies; technological advancement; innovations; evolution in consumer products which leads to disappearance of some products and the appearance of new ones; and changes in tastes and preferences; an increase in the consumption of previously marginal products; previously dominant products slipping into decline or vanishing off the markets as a result of changes in technological innovation driving productivity and hence patterns of consumption; or new products changing these patterns. These changes require frequent adjustments in the key parameters used to measure the CPI to ensure it accurately measures consumer price movements.

What did the 2016 Uganda CPI re-basing involve?

During FY 2015/16, the Uganda Bureau of Statistics rebased the CPI to ensure it correctly measures the price movements, and to comply with international standards, including under International Labor Organization, International Monetary Fund, East African Community, Common Market for Eastern and Southern Africa and the Free Trade Area, among others. The key adjustments included:

i. Changing the base period from 2005/06 to 2009/10;
ii. Changing CPI classification from "Country Product Classification" to "Classification of Individual Consumption according to Purpose" (COICOP), in line with international good practice;
iii. Adjusting the weights of the CPI to ensure consistency with the expenditure patterns described by the 2009/10 Household Survey. This adjustment required updating the coverage of goods and services in the basket; changing the weights of the goods and services; adjusting the geographical coverage of the CPI by extracting another urban center (i.e. Fort Portal) out of western region; and stratifying the Kampala index further into low; middle and high income baskets; and changing scaling from 100 to 1000.

What are the implications of the 2016 Uganda CPI re-basing?

The rebased CPI yields an average inflation rate of 7.0 percent during the first half of FY 2015/16. This rate is only slightly lower than 7.4 percent before the rebasing. It is critical to note that the rebasing did not result into a systematic lowering of inflation. In fact the average inflation over a longer period of 12 months to December 2015 shows a figure of 5.8 percent, which is higher than 5.2 percent without rebasing. The resultant adjustment was minimal because the CPI has been aptly rebased regularly in the past.

Nonetheless, the rebasing allowed for systematic adjustments, including in the methodology to measure better movements in cost of living for individual locations and products. Key of these include education, health, transport, food; and the electricity, fuel and utilities sub-groups while locations are also better measured with Kampala divided into high, middle and low income indices.

Source: Uganda Bureau of Statistics

The inflationary pressures in Uganda resulted from both weather-induced seasonal factors and external developments. As has often been the case in the recent past, during the first half of FY 2015/16 food crop prices increased, with prolonged droughts reducing the supply of weather-sensitive agricultural food crops. At the same time, the rate of core inflation (a measure that eliminates volatile components) had remained on an upward trend since September 2014, reaching a peak of 7.7 percent in February 2016. In particular, the rate for the energy, fuel and utilities sub-category accelerated at a higher rate than the average due to inflationary pressures on components such as charcoal and firewood resulting from the prolonged spell of dry weather. Moreover, with the Shilling declining in value against the dollar by 27 percent, this depreciation had a significant inflationary impact, especially given that tradable goods contribute to up to 60 percent of the basket of goods in the CPI. The Bank of Uganda has previously estimated that a depreciation in the value of the Shilling can be transmitted into domestic inflation by a factor of 0.4 to 0.5.[1] For the same reason, there was little pass-through of the effect of low global commodity prices (particularly for oil), to domestic prices.

In an anticipated response by policy makers to these increased inflationary pressures, monetary policy was tightened to curb demand pressures, before being eased later in the year. After the experience of 2011, when elections were followed by runaway inflation, the Central Bank adopted a highly precautionary stance during the 2016 election year. During the first half of FY 2015/16, the Bank of Uganda (BOU) intensified measures to forestall the inflationary pressures that it had foreseen in its inflation forecasts. In particular, the Central Bank raised its key policy rate (CBR) from 13 percent in June 2015 to 17 percent in October 2015, a level that has been maintained until April 2016. In addition, margins on the bank rate and rediscount rate were widened to make it more difficult for commercial banks to access funds from the BOU. In addition to these interest rate actions, the BOU reduced the level of currency in circulation through net sales of its short-term instrument, the repurchase agreement security, and through sales of foreign currency to a value in excess of US$ 400 million within a period of six months, with this latter measure also relieving pressure on the Uganda shilling.

The tight monetary policy stance increased the cost of borrowing for both the Government and the private sector. However, this policy stance realized the objective of lowering inflation. Continuing the trend from the preceding year, the yields on government securities increased sharply during the first half of FY2015/16 (see Figure 2), with these increases possibly related to increases in market uncertainty in the period prior to the election. The 91-day monthly Treasury bill rate rose to 18.3 percent by November 2015, up from 12.8 percent in July 2014. While this increase may have resulted in a strengthening of Ugandan currency by attracting inward portfolio flows as a result of increased investor appetite for government securities, it also increased the cost of borrowing for the Government. As a result, the Government reduced its borrowing from the financial system by 10 percent over the first half of FY 2015/16. Commercial banks also sharply increased their lending rates as of April 2015, with the average rate reaching 25.2 percent by February 2016, compared to 20.8 percent in the corresponding period in 2014. However, these tight monetary conditions, together with the low commodity prices, reduced inflation pressure and the rate of inflation had declined to 5.1 percent by April 2016.

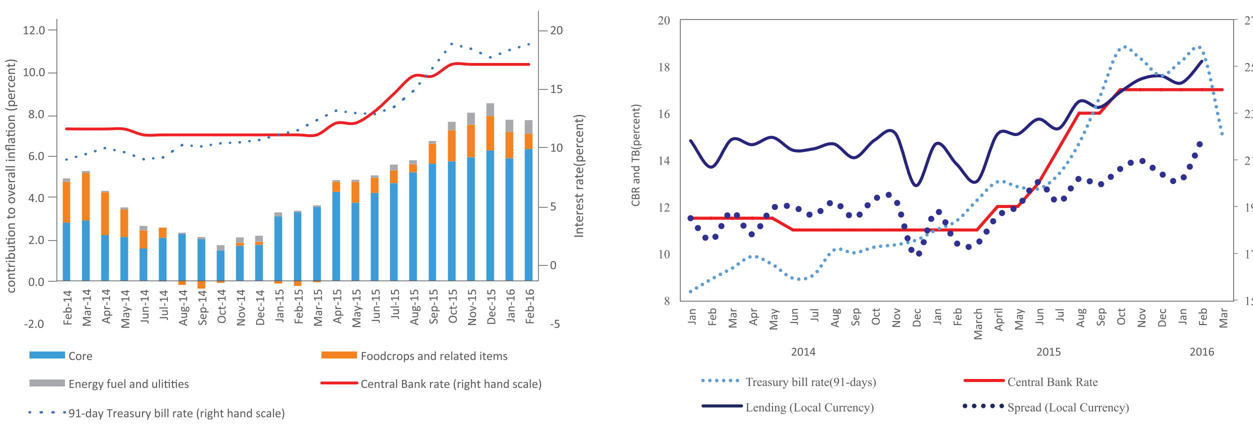
A Bank Counter at Fina Bank a commercial bank in Uganda

margins on the bank rate and rediscount rate were widened to make it more difficult for commercial banks to access funds from the BOU. The central bank also reduced the level of currency in circulation through net sales of its short-term instrument

1. Okello , A. J. and Brownbridge , M., 2013; Exchange Rate Pass-through and its implications to Monetary Policy in Uganda. Bank of Uganda Working Paper No. 10/2013,

The impact of the tight monetary policy stance on credit eventuated only much later. During the first half of FY 2015/16, financial institutions had accelerated the supply of credit to the private sector, with the rate of growth standing at an average of 24 percent, almost double the average rate of 13 percent recorded during the same period in FY 2014/15. The impact of the high interest rates began to be felt in October 2015, when the rate of growth of credit began to decelerate until it reached 8.7 percent per annum by March 2016. The largest proportion of the credit was utilized to finance activities in building, mortgage, construction and retail estate, which accounted for 23 percent. This was followed by trade, which accounted for 20 percent; by the personal and household sector (14.8 percent); and by the manufacturing sector (15 percent).

Figure 3: Inflation pressures led into tighter monetary policy and cost of credit

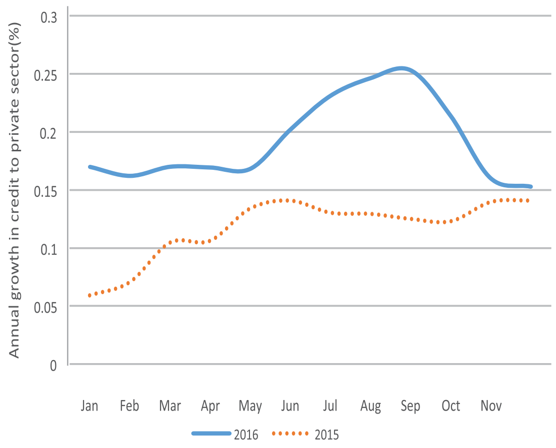


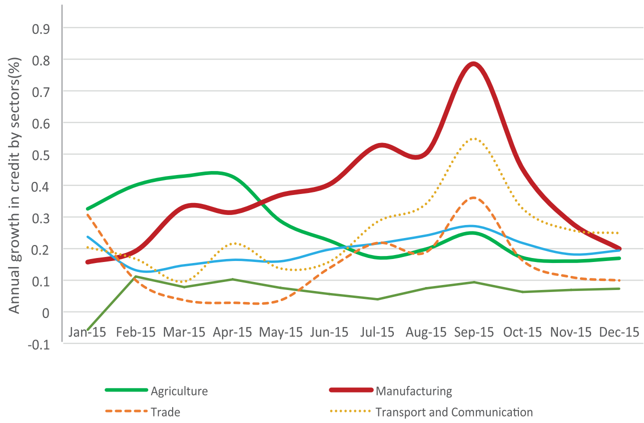
Source: Bank of Uganda

Contrary to expectations, the volatility in the value of the Shilling did not deter agents from increased borrowing in foreign currency. The total value of credit denominated in foreign currency grew by 38 percent during the first quarter of the year, compared to a growth of 21 percent during the corresponding period in FY 2014/15. This is a very significant increase, particularly when the Shilling was witnessing the highest level of volatility, with a rate of depreciation reaching 40 percent per annum in September 2015. The shilling-denominated credit recorded much lower rates of growth, increasing from 8 percent to 15 percent over the same period. With this growth, dollar-denominated credit accounted for 45 percent of the total value of credit by March 2016. Borrowing in foreign currency creates opportunities for borrowers to access lower cost credit; to diversify loan portfolios; and to hedge the risks associated with the volatility of the local currency. On the financial institutions side, prudential limits set by BOU forbid financial institutions from expanding their foreign currency denominated loan portfolios to a value in excess of 20 percent of the total value of the portfolio. This requirement has been broadly met by banks over the past two year. However, the increase in the proportion of loans denominated in foreign currencies also creates a significant exchange-rate risk for borrowers whose earnings are shilling-denominated, as would particularly be the case for entities operating in non-tradable sectors. In the case of a depreciation in the value of the local currency, it would become increasingly expensive for those sectors to service their foreign currency denominated debt.

FINANCIAL INSTITUTIONS ACCELERATED THE SUPPLY OF CREDIT TO THE PRIVATE SECTOR IN THE FIRST HALF OF FY 2015/16, WITH THE RATE OF GROWTH STANDING AT AN AVERAGE OF 24 %

Figure 4: Acceleration of credit to private sector cut short as monetary tightening catches up with financial institutions activities

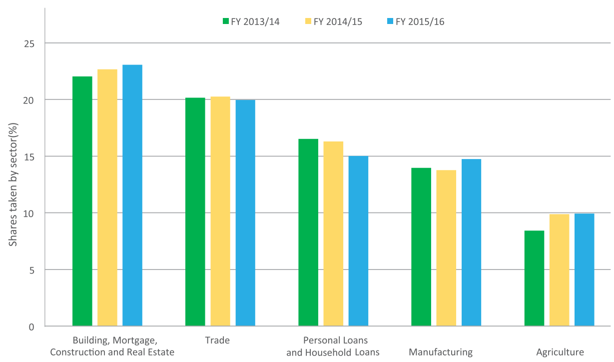


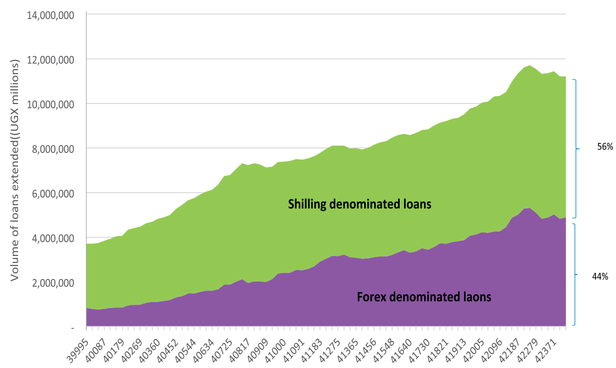


Source: BOU and World Bank staff calculations

In Uganda, the bulk of credit denominated in foreign currency is provided to businesses in the building, mortgage, construction and real estate sector and in the manufacturing sector, which combined, account for 50 percent of all of this credit. The value of the credit provided to these two sectors has grown rapidly over the first half of the year, at 57 percent in the case of the building, mortgage, construction, and real estate sector and at 53 percent in the case of the manufacturing sector. This compares to an average increase of five percent in the case of the former and a decrease of seven percent in the case of the latter compared to the corresponding period in FY 2014/15.The manufacturing sector exports some of its produce, and thus generates revenues in foreign currency, and similarly, some categories of real estate collect their rent in foreign currency. However, a significant proportion of the borrowers operate domestically and have revenues solely denominated in shillings, exposing these businesses to significant exchange rate risk.

Figure 5: Private sector credit: Construction, Trade and Personal Loans get the lion's share as borrowers prefer dollars





Source: BOU and World Bank staff calculations

Overall, the financial health of the banking sector has remained sound, despite the significant risks associated with exchange and interest rate movements. In particular, increases in interest rates could increase the risk of default on commercial bank loans, given that most loans are based on variable rates. At the end of December 2015, the banking system maintained an acceptable capital adequacy ratio, although these ratios were a percentage point lower than was the case during the corresponding period in 2014. Relative to the total value of loans, the proportion of non-performing loans momentarily decreased to 3.9 percent, but was back to 5.3 percent in December 2015, which was the same ratio reached in the corresponding period in 2014. The rate of return on assets improved to 2.7 percent, up from 2.2 percent. Liquidity indicators also improved.

1.3 CAUTIOUS FISCAL POLICY MANAGEMENT OUT PERFORMED BY ELECTION SPENDING PRESSURES

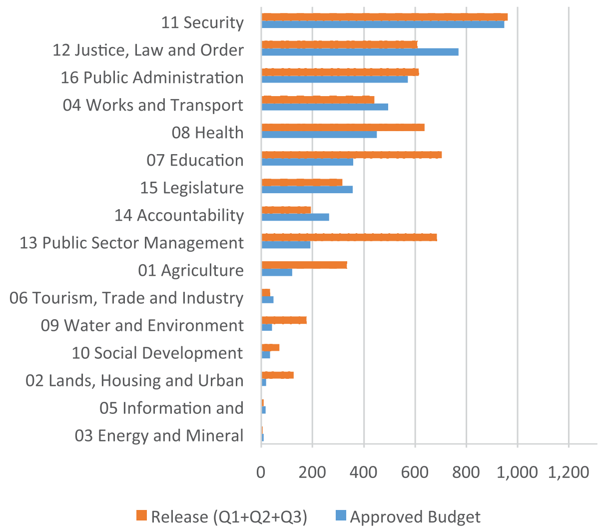
In FY 2015/16, fiscal policy managers strived to balance the achievement of a high level of prudence in the context of election-related expenditure pressures with the need to maintain efforts to boost growth. In line with the revised budget timetable mandated by the Public Financial Management Act (2015), the Parliament approved the budget for FY 2015/16 in June 2015. This represented a significant improvement in the budget process, with this expedited approval expected to contribute to a reduction in delays to the absorption of the public investments budget. While the authorities have remained committed to moving forward with fiscal policies intended to boost growth by addressing constraints on economic growth, particularly those related to Uganda's infrastructure deficit, they have also been determined to prevent the types of fiscal slippages that occurred around the 2011 election. Therefore, while the Parliament approved an expansionary budget for FY 2015/16, with a projected increase in the value of public expenditures to 22.1 percent of GDP (up from 19.4 percent of GDP in FY2014/15), the bulk of this increase was earmarked for investments in public development projects intended to address key infrastructure constraints and to establish a workable public infrastructure to facilitate oil production. This is consistent with trends observed over the past five years, during which the Government has substantially increased its allocations for the development budget, with these allocations increasing from 32 percent of total expenditure in FY 2010/11 to 51 percent in FY 2015/16.

With significantly increased expenditure and only modest improvements in revenue collections, an increase in the value of the fiscal deficit is inevitable. The value of revenues was projected to increase from 13.0 percent of GDP in FY 2014/15 to 13.6 percent in FY 2015/16, while the value of external grants was projected to increase from 1.1 percent of GDP to 1.6 percent. The revenues from external grants have been declining after Uganda achieved mature reformer status, which it has had only very limited access to grants from multilateral institutions. Revenues from external grants declined even further in 2012 following the governance-related scandals, which has resulted in a number of donors revising their overall assistance strategy to the Government over the past five years. Therefore, the value of the overall fiscal deficit was projected to increase, from 4.6 percent of GDP in FY 2014/15 to 6.4 percent in FY 2015/16. It was expected that this deficit would be partially funded by external loans, the value of which would reach 4.8 percent of GDP, and partially by domestic resources, the value of which would reach 1.6 percent of GDP.

During the first half of FY 2015/16, policy makers were assisted in their endeavors to implement prudent fiscal management by good performance in the area of revenue collection, which in turn was assisted by the depreciation in the value of the currency. The budget estimates for the first half of the year indicated that the Government had been able to collect domestic revenues which exceeded the established targets by UGX 218 billion (or 4 percent above the pro rata target for this period). While this is largely attributable to the high value of non-tax revenues, the total value of tax revenues collected by the Uganda Revenue Authority exceeded targets by UGX 59.5 billion, with all major categories of taxes delivering at least the targeted level of revenue, except in the case of indirect taxes, for which there was a shortfall of around UGX 86.7 billion in the first half of the FY 2015/16. Underperformance in the collection of excise duty and VAT on domestic products during this period was largely attributable to the slow economic activity, while collections on international trade-related activities benefited from the depreciation in the value of the domestic currency. The value of overall domestic revenues is projected to reach 13.9 percent of GDP, which is 0.4 percentage point above the original target. Uganda's level of performance in this area is still significantly lower than that of its peers in the EAC. On account of the depreciation in the value of the Shilling, the revenues from external grants are expected to reach UGX 1,461 billion during FY 2015/16. This value is equivalent to 1.7 percent of GDP, which is higher than the originally budgeted level of 1.6 percent of GDP.

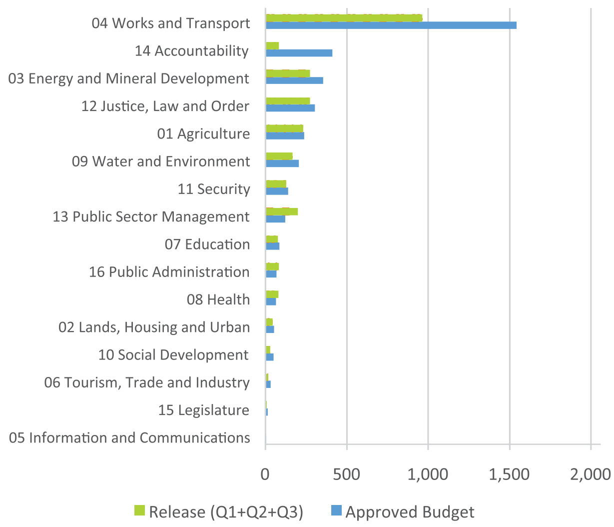
During the first half of the year, the overall government expenditure (including net lending to investment projects) was more or less on target, with the execution of some key projects progressing quickly. However, the level of expenditure later began to exceed budgeted allocations due to election related pressures and security related operations. The total value of expenditure was estimated to exceed targets by UGX 155 billion during the first six months of the financial year. The rate of execution of public investments was relatively good, with 34 percent of the budget being absorbed during these months. Some key investments, including the Karuma and Isimba hydro power projects, which had been carried over from the previous year and had been expected to be frontloaded into the first half of the year, performed well. By the end of December 2015, the rate of execution for the Karuma Hydro power dam project had reached 54 percent and the rate for the Isimba hydro power plant project had reached 89 percent, both well ahead of schedule. Meanwhile, the rate of execution for the Albertine region oil refinery has only reached 31 percent, while only 25 percent of the thermal energy subsidy has been absorbed, putting these projects significantly behind schedule. In the case of roads, execution has been affected by setbacks related to contract management and social safeguards, which meant that the sector was under-executing its budget by the end of the third quarter of the year. In contrast, most recurrent expenditures have reached levels in excess of the established targets.

Figure 6: Performance of the recurrent budget in three quarters of FY 2015/16 (approved vs. released)



Source: Ministry of Finance, Planning and Economic Development

Figure 7: Performance of the development budget in three quarters of FY 2015/16 (approved vs. released)



Source: Ministry of Finance, Planning and Economic Development

To a significant degree, overspending has been driven by expenditures related to the heightened security measures during the elections. By the end of the first half of FY 2015/16, up to 70 percent of the planned budget had been spent. While the slow execution of the development projects left space in the budget, it also heightened the risk of tilting the balance of expenditure towards recurrent expenditures, particularly in the non-wage category. Unfortunately, the spending pressures continued into the second half of the year, during which period a supplementary budget to a value of at least UGX 1,000 billion was approved by the Parliament As a result of the heightened security measures in the run-up to and during the elections in February 2016, for instance, the non-wage defense budget had been over-executed by 125 percent by the end of the third quarter of the year and required an additional UGX 253 billion in the form of a supplementary budget. It is forecast that the defense budget will be over-executed by 152 percent by the end of FY 2015/16. The restructuring of the Uganda National Roads Authority (UNRA) has been another significant cause of over-execution in the non-wage budget, with its budget having over-executed by 154 percent by the third quarter, but expected to reach 174 percent beyond the budgeted level by the end of the fiscal year.

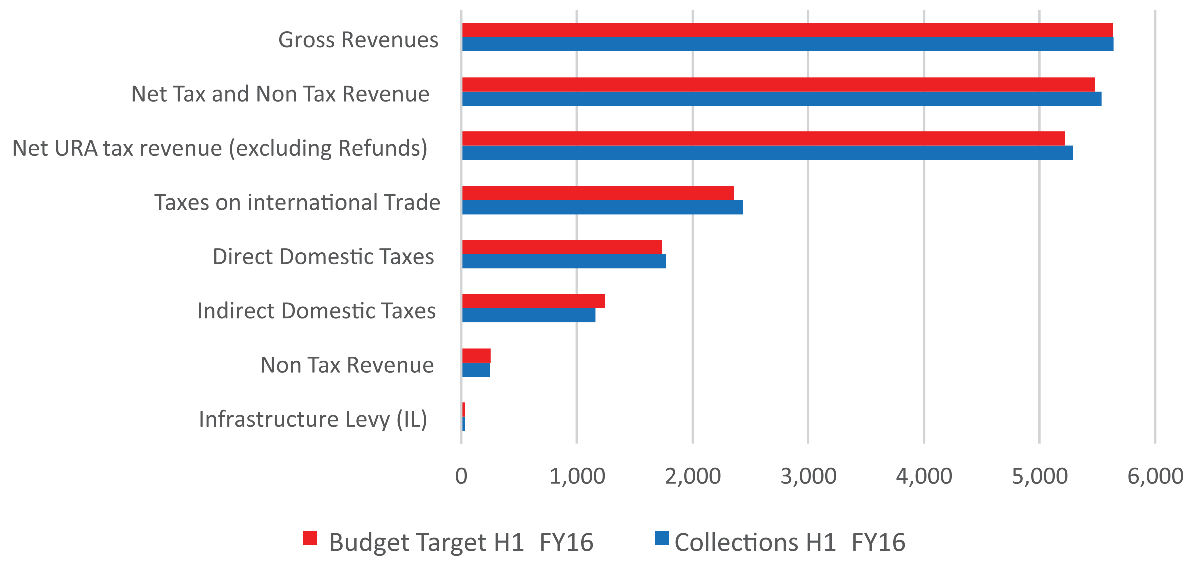
2. A supplementary budget worth a total of UGX 1,041 billions, equivalent to 4 percent of the budget, was tabled in Parliament in April 2016. The bulk (33 percent) was allocated to security spending (Defense and Police), followed by wages and pensions (15 percent), Education (11 percent), Presidency (8 percent), Parliament (6 percent) and Electoral Commission (5 percent). Except for the component for Education, which was financed by additional financing accruing to finalization of external financing project requirements, the rest of the supplementary was financed through budget reallocations within the original budget. The supplementary was largely due to weak planning as the majority of expenditures, with exception of exchange rate depreciation pressures, could have been foreseen at the time of budgeting.

Table 1: Central Government Operations: FY2010/11 – FY2013/14

In percent of GDP	FY2012/13	FY2013/14	FY2014/15	FY2015/16 App. Budget	FY2015/16 Proj.
Revenues and grants:	12.9	13.0	14.8	15.1	15.7
Domestic revenues	**11.4**	**11.9**	**13.5**	13.6	**13.9**
o/w Tax revenues	11.0	11.5	12.8	12.9	13.4
External Grants	1.5	1.0	1.2	1.6	1.7
Total expenditure	**16.5**	**17.1**	**19.4**	22.1	**22.1**
Recurrent	9.1	9.8	10.3	10.4	10.8
Development & investment	6.6	7.2	7.0	11.3	8.3
External	3.4	2.7	2.6	4.0	4.1
Domestic	3.2	4.5	4.4	7.3	4.2
Arrears & contingencies	0.1	0.0	0.3	0.2	0.1
Overall balance	**-3.6**	**-4.1**	**-4.6**	**-7.0**	**-6.4**
External Financing	2.2	1.3	1.2	5.0	4.8
Domestic Financing & residual items	1.4	2.8	3.4	2.0	1.6
o/w Petroleum Fund withdrawals	0	0	0.6	0.1	0.2
o/w Domestic Borrowing	1.2	0	1.2	1.6	...
Memorandum items:					
Nominal GDP (Shs billions)	63,905	68,371	74,765	83,596	84,984

Source: Ministry of Finance, Planning and Economic Development, IMF, and World Bank

Figure 8: Performance of the domestic revenues in the first half of FY 2015/16



Source: Uganda Revenue Authority

The overall fiscal deficit in FY 2015/16 is expected to be slightly lower than had been planned, being financed mainly with externally borrowed resources. By the end of the year, total expenditure is expected to reach a value of 22.1 percent of GDP, which was the level projected in the budget. However, the outturn for the level of collected revenues is higher than projected, and so the fiscal deficit is projected to reach 6.4 percent of GDP. This would be lower by 0.6 percentage points of GDP than the level in the approved budget, although still at the highest level in more than a decade. Originally, Uganda's authorities had planned to finance 80 percent of the fiscal deficit through external borrowing. This is consistent with the Government's policy to use external resources to finance large infrastructure projects. Hence, while the Karuma project will continue to draw on government savings accumulated from the oil related capital gains tax,[3] the value of net external financing is projected to reach 4.8 percent of GDP. With the decline in concessional donor inflows, the value of loans from commercial sources (non-concessional loans) will reach 3.6 percentage points of GDP. The value of domestic financing is forecast to decline to around 1.6 percent of GDP, compared to the budgeted level of 2.0 percent after the Government adjusted the modalities for financing its budget to manage the high cost of borrowing recorded during the first half of the year.

1.4 UGANDA'S EXTERNAL POSITION WEAKENED FURTHER

During FY 2015/16, Uganda's external position continued to weaken due to the combined impacts of the weak global economy and domestic factors. The current account deficit is estimated to have reached a value of 9.6 percent of GDP in FY 2015/16, significantly higher than the figure recorded in the previous year, when it stood at 9.2 percent. This is largely due to the continued weakness of the global economy leading into the sustained decline in commodity prices, and a decline in inflows related to exports, income, transfers, and foreign direct investment. Therefore, a stronger capital and financial position wil have been achieved only through the disbursement of public loans. Thus, the overall balance of payments deficit is estimated to have declined from US$ 353 million in FY 2014/15 to US$ 139 million in FY 2015/16, with the deficit being financed through a reduction in international reserves from US$ 2,895 million to US$ 2,745 million. This level of reserves will have been sufficient only to cover 3.9 months of import of goods and services, compared to reserves of 4.0 months of import cover in FY 2014/15.

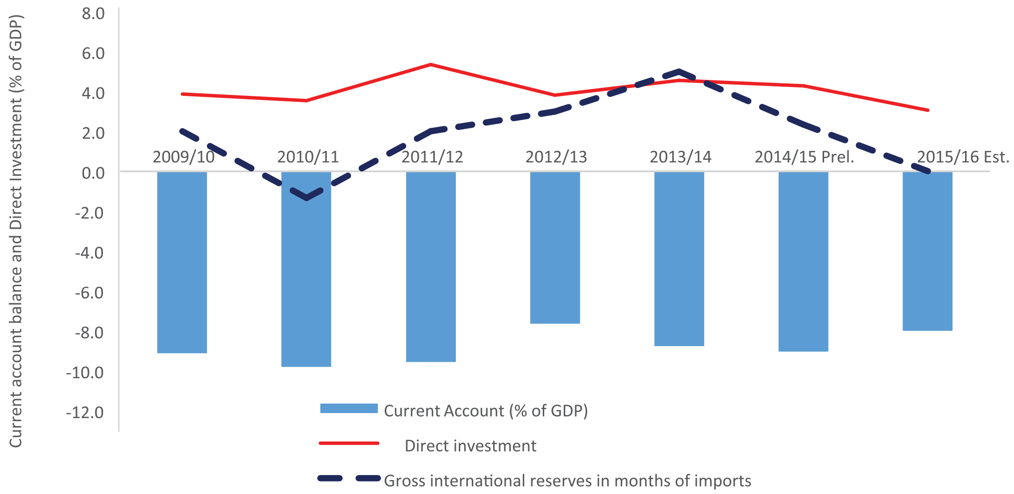
The reduced cost of oil imports should have resulted in a decline in the goods trade deficit. However, this was more than offset by the increased volume of imports required to support construction. The oil import bill is estimated to have declined to US$ 671 million during FY 2015/16, down from US$ 933 million in FY 2014/15. Even as demand for petroleum products continues to grow, particularly to support the booming construction and transport industry, the unit price of oil imports has continued to decline drastically. However, the postive impact of this decline has been more than fully offset by increases in the Government import bill, with this bill increasing by 96 percent to US$ 335 million, mainly as a result of the need for inputs for major infrastructure projects, and for security and election related materials. With a sizable decline in the prices of most of Uganda's commodity exports over the past two years, the value of exports of merchandise recorded a modest rate of growth, with this growth being primarily driven by a growth in non-traditional exports, mainly going to regional markets. At the same time, the impact of low commodity prices on Uganda's traditional commodities, including coffee and tea, was significant. These commodities remain the most significant contributors to the overall value of exports, accounting for 30 percent of the total value of export earnings during the last fiscal year. Consquently, the trade deficit is estimated to have widened, increasing from a value of 8.9 percent of GDP during FY 2014/15, to 9.3 percent in FY 2015/16.

In addition, the current account has been negatively affected by the decline in the net value of inflows of services, income, and transfers. The impact of lower oil prices on freight charges was to reduce the net value of foreign outflows related to services. However, the value of tourism receipts declined as a result of the impact of terrorist incidents on consumer perceptions; lower global incomes; and the impact of election-related uncertainties. The value of net transfers also estimated to have declined, with the value of these transfers envisaged to reach US$ 1,217 million, down from the figure of US$ 1,312 million recorded in the previous year, as income sources for these flows adjusted to the weak economic environment abroad and as domestic uncertainties increased due to the elections.

The capital and financial account is estimated to have improved by about 15 percent in FY 2015/16, mainly due to disbursements to finance public projects. In addition to almost doubling the value of disbursements for project grants to US$ 337 million, it is estimated that an additional US$ 946 million worth of funds derived from non-concessional borrowing has been disbursed to finance construction work on the Karuma and Isimba projects. Nevertheless, the value of FDI inflows is estimated to have declined to US$ 838 million, from US$ 1,153 million over the year, as investors adopted a 'wait and see' approach with respect to oil production related flows, particularly in the context of the uncertainties related to the election and its aftermath.

3. These revenues arose from the taxes levied on the US$ 1.5 billion sale of oil exploration rights between Heritage and Tullow oil companies.

Figure 9: Uganda's external current account, direct investment and international reserves worsen in the face of uncertainties



Source: IMF and bank of Uganda

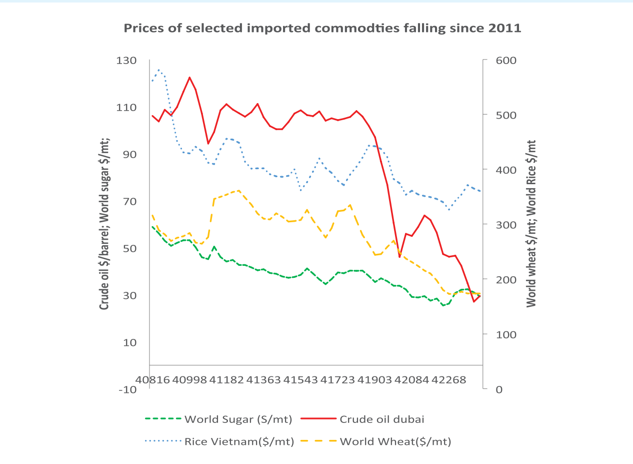
The weak external position was accompanied by depreciation in the value of the local currency, with this depreciation being marked by a significant degree of volatility. The deterioration of the balance of payments position during FY 2015/16 resulted in a continuation of the adjustments to the value of the Shilling that commenced in the previous year (in September 2014). During the first nine months of the year, the value of the currency had depreciated by an average of 24 percent. The bulk of the depreciation occurred during the first three months, with the currency losing value by 40 percent over a 12 months period, an unprecedented rate of depreciation since 1993, when the forex market was liberalized. A significant driving factor was the negative market sentiments in the run up to the elections and the related high level of currency speculation (see Box 2). These pressures on the currency were alleviated when the Bank of Uganda tightened monetary policy and as the private sector demand for foreign exchange declined as the election approached. In real terms, the value of the Shilling has depreciated at an average of 10 percent over the 10 months to March 2016, with such depreciation expected to allow for an adjustment of the real economy to the balance of payment shock.

A Total E&P fuel staition

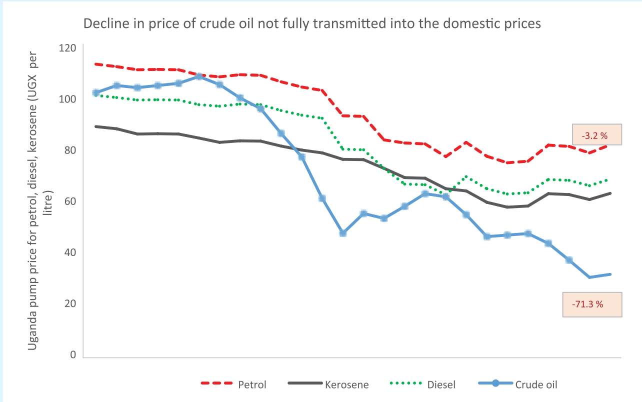
the impact of lower oil prices on freight charges was to reduce the net value of foreign outflows related to services

Box 2: Lower commodity prices is a double edged sword for Uganda

Over the past five years, commodity prices have experienced sharp swings, generally declining on account of the slowdown in the global economy. Uganda imports oil and a significant number of food items, with oil constituting 19 percent of the country's imports bill during FY 2014/15. A reduction in the unit price of these imports can result in a positive balance of payments shock. However, Uganda is also a commodity exporter, with 39 percent of the total value of its exports being derived from commodities. Thus, a decline in commodity prices may result in lower export receipts, which results in a negative balance of payments shock.



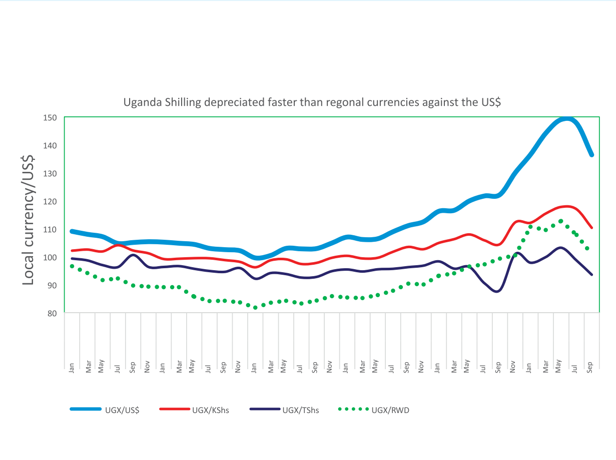
As the global price of a barrel of crude oil plummeted from US$ 108 in June 2014 to US$ 31 by end of February 2016, the oil import bill also declined from an average of US$ 90 million per month during FY 2013/14 to US$ 55 million in FY 2015/16, even though the volume of imported oil is estimated to have increased by more than 50 percent over this period. While the price of other commodity imports did not fall as steeply, they too have been on a declining trend since 2011. The decline in global commodity prices has resulted in a decline in Uganda's import bill by at least 16 percent, which is equivalent to about US$ 800 million, despite an increase in the volume of imports by 20 percent. In terms of exports, the price declines were less significant, with the price of coffee declining by 25 percent, tea by 17 percent, and maize by 21 percent, in the period from June 2014 to Febarury 2016. Thus, on balance, Uganda received an average of US$ 213 million per month during FY 2015/16, which is US$ 15 million lower than the average level recorded over the past two years. Overall, the decline in commodity prices has improved Uganda's terms of trade by about 2.5 percent.



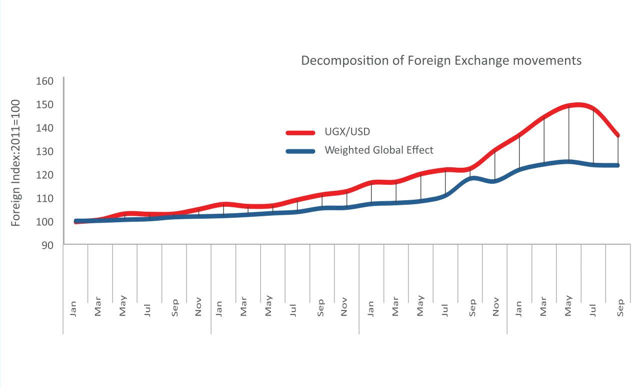
The domestic effects of lower commodity prices can be varied, depending on the transmission channels. Lower oil prices can be expected to assert downward pressure on the costs of production, particularly within the industrial and mechanized agriculture sectors. They also result in lower costs for lighting for the more than five million Ugandans who rely on kerosene for lighting; and generally reduce the cost of transporting goods and services. These effects have been less pronounced because of imperfect transmission from the international market price to the fuel pump prices. Indeed, while the average crude oil price declined by 71 percent in the period from June 2014 to February 2016, the pump prices of petrol declined by only 25 percent, kerosene by 26 percent and diesel by 30 percent over the same period (see Figure 1). The failure for the decline in fuel pump prices to reflect the decline in global crude oil prices can be partially explained by depreciation in the value of the shilling against the US Dollar, which declined by 30 percent during the first half of FY 2015/16. It is estimated that the exchange rate explains 7 percent of the variation in petrol pump prices, 11 percent in pump kerosene prices, and 12 percent in diesel pump prices. Other factors constraining this transmission include the taxation and domestic supply issues, with the latter comprising inefficiencies such as inadequate storage capacities and non-standard commercial practices due to weak regulation. According to a World Bank (2010) report, such inefficiencies contribute 50 percent of the retail price, higher than any other country included in the study, except Madagascar.

Box 3: Accounting for the Uganda shilling depreciation during FY 2015/16

By November 2015, the Shilling had lost 32 percent of its value against the US dollar relative to the position at the beginning of FY 2015/16. This rate of depreciation was far higher than the depreciation of 3.8 percent recorded over the same period in FY2014/15. Many other currencies across the world also weakened against the US dollar during this period. Within the region, the Uganda Shilling depreciated in value relative to the Rwandan franc by 25 percent; to the Kenyan Shilling by 14 percent; and to the Tanzanian Shilling by 3 percent, with these rates of depreciation being significantly higher than those recorded in the corresponding period in FY2014/15 (1 percent, 2 percent and zero percent respectively). This was because the value of Kenya's currency depreciated by 4 percent; Tanzania's by 4 percent; and Rwanda's by 8 percent against the US dollar over the same time period.



External shocks were a major driver of the currency's depreciation. As a result of the weak global economy, mainly driven by with a deceleration of growth in China, Brazil and the US, commodity prices declined and weakened the external accounts of regional economies. In the period from January to December 2015, the Food, Beverage and Agriculture raw materials price indices declined by 29 percent, 16 percent and 29 percent respectively.



Country specific, domestic shocks became even more important in the case of Uganda. It is estimated that these domestic shocks accounted for an average of 10 percent of the volatility in exchange rate in 2015, compared to about 3 percent in 2014. The most significant factors propagating these domestic shocks were the negative market sentiment and the outbreak of speculative behavior driven by memories of currency fluctuations during the previous election in 2011, even though the latter had resulted from a combination of exogenous shocks and policy slippages that also fueled inflation. This time, the external position remains weak on account of weaknesses in the global economy. Meanwhile the implementation of pre-emptive monetary policy and deflationary pressures from the external environment prevented the emergence of a vicious cycle that could have been sparked off speculative transactions and resulted in more significant depreciations in the value of the currency to levels that did not reflect the true state of the economy.

Oil mining in the Albertine region

lower oil prices can be expected to assert downward pressure on the costs of production, particularly within the industrial and mechanized agriculture sectors

2. ECONOMIC OUTLOOK

The outlook for the Ugandan economy is broadly favorable. With uncertainties arising from the February 2016 elections having dissipated, the low energy prices and the stimulus effect from large public investments intended to address infrastructure constraints and prepare Uganda for oil production should boost investment and drive an increased rate of growth, higher than those recorded over the past five years. Despite the adverse impact of a weak external sector, with the impact of low oil prices on investments in the oil sector being particularly significant, the rate of growth for the Ugandan economy is projected to accelerate to 5.9 percent in FY 2016/17 and to remain on an upward trajectory into the medium term. However, there are risks to these growth prospects, including risks related to the protracted weak global economy, volatile weather, regional insecurity, and poor implementation of the huge investment program. In particular, this latter risk could reduce the ability of the planned investments to facilitate the achievement of the intended growth acceleration.

2.1 ECONOMIC GROWTH PROSPECTS IMPROVE AS UGANDA RETURNS TO ITS INVESTMENT PATH

The World Bank forecasts that Uganda's rate of economic growth will accelerate from the estimated 4.6 percent recorded in FY 2015/16 to about 5.9 percent in FY 2016/17, as short-term domestic uncertainties recede. With the completion of the current electoral cycle, the purpose of domestic policies is expected to be to create a more conducive economic environment, as policymakers balance the need to reduce the cost of borrowing; the need to avoid exacerbating upward inflationary pressures; and the need to build the confidence of investors in the post-election period. It is envisaged that the looser monetary conditions, together with the reduced use of domestic borrowing to finance large public investments, will increase the availability of credit to the private sector and reduce the crowding out of private investment that has occurred in recent years. At the same time, there will be gains from low energy prices and from the construction boom, with this boom expected to result from the continuing high level of public investment to address infrastructure constraints and to prepare for oil production. Together, these factors should boost investment, and thereby drive a greater momentum for growth.

The domestic policies have to be managed alongside a volatile global economy, with the ongoing possibility of shocks that could have a significant negative impact on Uganda's growth outcomes. The global environment remains unstable, with a possibility that the global rate of growth will remain low, possibly lower than the 2.9 percent that has been projected by the World Bank for 2016[4] if a more protracted slowdown across large emerging markets spill over to other developing economies. Under such a scenario, Uganda's external position would be further constrained by the lower level of demand for merchandise exports, tourism, remittances and FDI. However, this forecast assumes that a modest recovery in the advanced economies will continue and that activity will stabilize among major commodity exporters, resulting in some upward pressure on commodity prices. Indeed, the World Bank is raising its 2016 forecast for crude oil prices to US $ 41 per barrel from US $ 37 per barrel in its latest Commodity Markets Outlook[5], as an oversupply in markets is expected to recede. This could resuscitate export growth and lead to an increase in FDI, especially in oil related sectors, which would compensate for the gradual decline in official aid.

4. World Bank, 2016. Global Economic Prospects 'Spillovers Amid Weak Growth'; January 2016.

5. http://www.worldbank.org/en/news/press-release/2016/04/26/world-bank-raises-2016-oil-price-forecast-revises-down-agriculture-price-projections

Table 2: Summary Assumptions for the Medium Term Outlook, Baseline Scenario

	2013	2014	2015 e	2016 f	2017 f	2018 f
Real GDP growth, at constant market prices	3.2	4.8	5.0	4.6	5.5	5.9
Private Consumption	0.1	3.2	12.3	13.2	8.7	8.8
Government Consumption	-5.1	-5.8	3.7	10.3	5.3	2.5
Gross Fixed Capital Investment	9.2	3.3	1.1	4.0	8.0	10.0
Exports, Goods and Services	6.7	0.0	-5.4	0.9	8.0	9.0
Imports, Goods and Services	0.0	-6.4	14.5	25.5	16.2	16.0
Real GDP growth, at constant factor prices	3.4	3.9	4.8	4.5	5.0	5.1
Agriculture	1.8	3.0	2.3	3.2	4.3	4.0
Industry	4.3	3.9	7.8	3.0	7.0	9.0
Services	3.9	4.3	4.8	5.7	4.6	4.1
Prices: Inflation						
Inflation (GDP Deflator)	4.1	2.3	3.5	7.6	4.2	5.0
Inflation (CPI period average)	5.5	4.3	2.7	7.7	6.3	5.0
Current Account Balance (% of GDP)	-8.1	-10.5	-9.2	-9.6	-10.0	-10.3
Financial and Capital Account (% of GDP)	6.1	7.4	8.1	7.2	8.3	9.6
Net Foreign Direct Investment (% of GDP)	4.5	4.2	4.5	3.7	4.6	4.2
Fiscal Balance (% of GDP)	-4.2	-4.2	-4.6	-6.4	-6.5	-6.3
Debt (% of GDP)	26.2	29.1	33.2	36.9	40.2	44.3
Primary Balance (% of GDP)	-2.2	-2.6	-2.8	-4.6	-4.7	-3.8
Poverty rate ($2.5/day 2005 PPP terms) [a,b,c]	33.3	33.0	32.6	32.2	31.6	30.9
Poverty rate ($5/day 2005 PPP terms) [a,b,c]	63.1	62.8	62.5	62.2	61.6	60.9

Source: Compiled by World Bank staff using historical data from official sources.

Notes: f = forecast

(a) Calculations based on 2009-UNHS and 2012-UNHS. | (b) Projection using annualized elasticity at the regional level with pass-through = 1 based on GDP per capita constant PPP. | (c) Actual data: 2012. Projections are from 2013 to 2017.

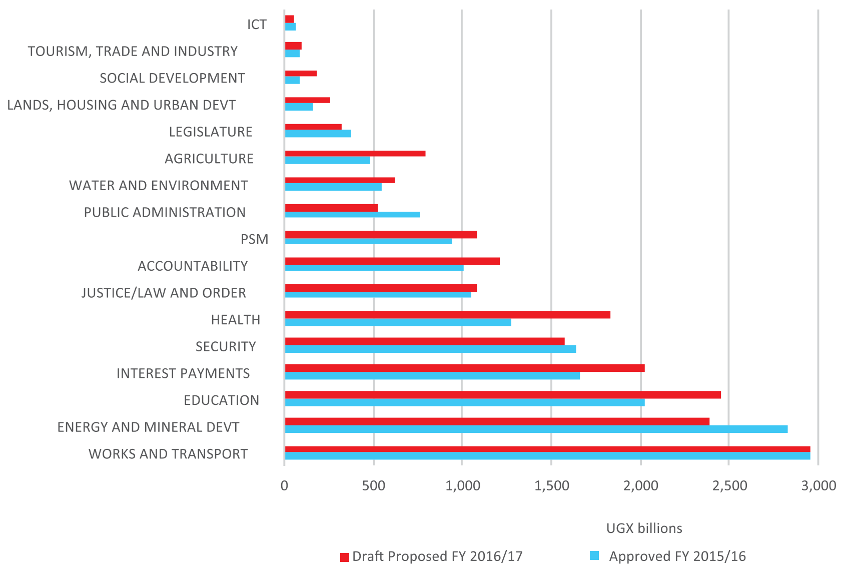
It is expected that patterns of growth will remain roughly similar to those that have characterized Uganda's economy over the past decade and a half. The predominant source of growth will continue to be an increase in the economic activity of the construction and services sectors, with manufacturing continuing to grow from a small base. Growth in the output of the agricultural sector will remain subdued, largely due to supply-side constraints. Though still accounting for only a small share of GDP, the mining and quarrying sector could be a significant source of growth in coming years, as the sector's proven potential begins to attract increased attention from investors.

Fiscal policy will continue to be used as the key instrument to stimulate growth. As mandated by the second NDP and by the resource allocation framework and the charter of fiscal responsibility required by the Public Finance Management Act (PFMA 2015), fiscal policy during FY 2016/17 will continue on an expansionary path, with the key intent being to continue with the construction of key infrastructure. At the same time, it will remain sufficiently flexible to enable policymakers to manage the impacts of exogenous shocks. According to the FY 2016/17 National Budget, the total value of expenditure is forecast to increase to 22.4 percent of GDP, up from the level of 22.1 percent recorded in FY 2015/16. The major driver of this increase is the perceived need to implement priority infrastructure projects to facilitate private sector development and to enhance the productive capacity of the economy. These projects include the Karuma, Isimba and Ayago hydro projects; a number of electricity transmission projects; the construction of a standard gauge railway; the construction of the Kampala-Jinja and Kampala-Entebbe Express Highways; and the rehabilitation of the Entebbe Airport. Among other benefits, these projects are expected to increase the rate of electrification by doubling Uganda's power generation capacity; enhancing its transmission capacity; and easing the transportation of goods, services and passengers, both internally and across borders. In total, the value of resources allocated to the transport sector will reach 19 percent of the total budget, while that to the energy sectors will be 12 percent (see Figure 10).

Meanwhile, the budget aims to continue allocating resources to improve the quality of social services, even as these are being squeezed by the increasing pressures from the security and public administration sectors. It is expected that 12 percent of the budget will be allocated to the education sector in FY 2016/17, with this allocation taking up the third largest share of the budget. With 66 percent of the allocation for education going to pay teacher salaries, a significant amount of resources will have to be sought off budget for other non-salary requirements that can support the sector's key priority of improving the quality of primary education and of ensuring a higher rate of transition to secondary education. Without this, Uganda will not be able to equip the rapidly expanding labor force with the requisite skills to facilitate the achievement of higher levels of productivity. The health sector, which takes up seven percent of the total value of the budget, has also received a large portion of its funding off budget. This trend towards off budget financing raises serious concerns regarding planning within the affected sectors. At the same time, off budget financing can enable the Government to close critical gaps in cases where it is not possible to allocate sufficient resources under the national budget. With increased regional security and terrorism concerns, the value of budget allocations to the security sector have increased rapidly over the recent past, with this allocation amounting to 8 percent of the total value of the budget in FY 2016/17. On the other hand, the wider public administration sector, including the legislature and public sector management agencies, continues to require increasingly large allocations to finance new administrative units and the increased size of parliament, amongst other perceived needs. The overall administrative burden reaches a level of 2.1 percent of GDP, which is far higher than the level recorded in most other countries around the world.

With increased pressure for exemptions in the context of modest revenue collection efforts, the authorities face a significant challenge in their endeavors to finance proposed expenditures while maintaining debt at a reasonable level. To some degree, the recently implemented measures to boost the performance of revenue collection[6] have had a positive impact, with the actual revenue collections exceeding budget for two consecutive years. However, if the Government is unable to resist a new wave of demands for exemptions, it may be difficult for the Uganda Revenue Authority to collect revenues to the budgeted value of 14.4 percent of GDP in FY 2016/17. If revenues collected fall below this level, the fiscal deficit will exceed 6.4 percent of GDP in FY 2016/17, with more than 80 percent of the fiscal deficit funded through external borrowing. The value of net external financing is projected to reach 5 percent of GDP. With the decline in concessional donor inflows, the value of loans from commercial sources (non-concessional loans) will amount to 3.9 percent of GDP. Domestic financing is forecast to amount to 1.3 percent of GDP, with the Government drawing on the petroleum fund to support and modestly increase the level of domestic borrowing, with lower interest rates reducing the Government's cost of borrowing.

Figure 10: Proposed sector allocations maintain same priorities into FY 2016/17



Source: Ministry of Finance, Planning and Economic Development

6. Government of Uganda National Budget Speech for Financial Year 2015/16

In FY 2017/18, Uganda's economic growth should increase by an additional percentage point to reach approximately 6.8 percent. Thereafter, it should remain on an upward trajectory into the medium term, perhaps facilitating a further reduction in poverty levels by around 1 to 2 percentage points per year. The negative effects of a possible protracted slowdown in the global economy notwithstanding, the continuation of a fiscal strategy focused on removing constraints to growth and proceeding with key oil projects is expected to boost economic activity, particularly in the construction sector. In addition to completing major energy and transport projects that have already commenced, a number of projects within these areas will continue to pre-occupy the Government over the next three years. And with key decisions related to the development of infrastructure to support the oil production, distribution, and the transportation of its products to the Indian Ocean having been made (see Box 3), it is expected that upfront investments to a total value of US$ 8-12 billion could be undertaken over the next five years. It is assumed that these investments will boost construction activity to accelerate the rate of economic growth in the near term, and if managed well should to be expected to lead to improvements in the productivity of the economy to sustain higher growth in the medium to long term.

The fiscal deficit is likely to remain high into the medium term, but with an increasing proportion of expenditure being allocated towards capital investments and with an increasing proportion of financing being derived from external sources. It is expected that capital expenditures will gradually increase to around 11 percent of GDP by FY 2019/20. With only modest improvements to revenue collection, the overall deficit is projected to decline only marginally, to around 6.2 percent of GDP by FY2017/18. It is then expected to remain at around the level of 6.5 percent of GDP in subsequent years. To finance the deficit, it is expected that there will be a reduced emphasis on domestic sources of financing and an increased emphasis on external sources, with most of the external borrowing contracted on non-concessional, but still favorable, terms. If the Government manages to reduce the deficit following the implementation of its planned large infrastructure projects, Uganda is likely to remain on a fiscally sustainable path, consistent with the charter of Fiscal Responsibility mandated by the PFM Act (2015).

Pregnant women attending an antenantal clinic in Mukono HC iv

the Uganda National budget aims to continue allocating resources to improve the quality of social services, even as these are being squeezed by the increasing pressures from the security and public administration sectors

Box 4: Key Decisions are Moving Uganda's oil Sector

The oil sector is a critical element in supporting Uganda attaining the key objectives of achieving middle income status by 2020 and transforming into a modern economy. Uganda's 6.5 billion barrels of proven reserves could support the proposed production of 100,000-200,000 barrel per day (BPD) over a 20 to 30 year period, depending on the speed of extraction. If oil prices remain low, the expected stream of revenues in the medium term could be lower than forecast. Nonetheless, if oil production starts in the next two years and investment accelerates over the next decade, the real rate of GDP growth is expected to reach an average of 8.8 percent annually in the period from 10 years after production starts. This is 2.2 percentage points higher than in a scenario without oil and/or with a more limited investment surge. In per capita terms, the emergence of the oil sector and the continued emphasis on public investment will allow Uganda to reach the US$ 1000 GDP per capita mark by 2019/20. This level of per capita income is 32 percent higher than for a scenario without oil and with lower levels of public investment. Realizing these impressive scenarios would depend on a number of factors:

i. Preparing for production - Infrastructure investments taking shape, must be executed efficiently

First, the construction of the refinery with an initial capacity of 30,000-60,000 barrels per day (BPD), a capacity considered sufficient to cater for the region's demand for refined petroleum products commenced in 2015. This task was assigned to a consortium led by RT Global Resources, which is owned 100 percent by Russian defence conglomerate Rostec, and including among others South Korean conglomerate GS Group. Located in Kabaale Township, in Hoima District, along the eastern shores of Lake Albert, the refinery capacity is expected to increase to 120,000 bpd in the mid-term and 180,000 bpd in the long-term, if more reserves are discovered in the country. Building a refinery in Uganda was jointly decided by the East African heads of State in the Northern Corridor infrastructure project. It is mainly aimed at boosting petroleum production in the sub-region and serving as a back-up to the aging one in Mombasa. The refinery will be funded as a Public Private Partnership (PPP) involving a 60 percent equity share by the private sector. This implies the EAC governments will be the minority shareholder with 40 percent of the equity. The Governments of both Kenya and Tanzania have proposed holdings in the project amounting to 2.5 percent and 8 percent, respectively. Rwanda and Burundi are still evaluating their position. Second, for landlocked Uganda, decisions reached in April 2016 related to the location of the export pipeline was a major milestone in terms of progress towards addressing the logistical challenges to tapping Uganda's oil resources. Issues related to the location of the export pipeline have been a source of uncertainty and delay, contributing to the postponing of the commencement of the production of Uganda's oil, with the dates for this commencement being a moving target over the past few years.

Now that Uganda has opted to use the Southern route through Tanga port of Tanzania to export its crude oil to the coast, processes to allow for the construction of pipeline should be hastened. Estimated to involve the sum of US$ 3.55 billion for its construction, the

2.2 RISKS ARE MAINLY DOWNWARD

There are several downside risks to the growth outlook, a number of which have been present for some time. The most important of these relates to weaknesses in the area of fiscal management. In the near future, fiscal policy still faces a challenge of remaining prudent in the context of political pressures to fulfill election promises related to an expanding size of parliament and to increasing emoluments for its members, both of which would significantly increase the cost of public administration. In April 2016, the Parliament hastily passed an amendment to the Income Tax Bill 2016 that exempted members of parliament from taxes on allowances. If assented to into law by the President, this amendment alone will reduce the expected tax collections by at least 0.3 percent of GDP, pushing the expected amount of taxes during FY 2016/17 down to 13.3 percent of GDP. In the short to medium term, the other source of fiscal management risk relates to the sequencing, financing and management of the public infrastructure development program. Moreover, with only meager improvements to domestic revenue mobilization and with a considerable degree of uncertainty regarding when oil production and the subsequent flow of revenues will actually commence, there remains a considerable degree of risk related to the financing of investments. Financing risks may become

Tanga port option was considered to be the least costly option, significantly cheaper than the Northern route, which would have cost around US$ 4.20 billion. The Southern route is 400 kilometers longer than the Northern route, but other factors, such as weather and environmental risks; adjustments required to the supporting infrastructure such as rail and roads; terrain; and security concerns, make the Southern route much more favorable. With financing already secured (from Total), it is expected that the construction of the pipeline could take 3-4 years, which implies that oil export revenues will start to flow no sooner than 2020 . However, at a regional level, this development distorts the original aspirations of the "Coalition of the Willing" group of countries to connect South Sudan and Kenya to Lamu, Kenya. However, if Kenya goes ahead with the construction this pipeline, it would provide an alternative route in the long run.

ii. Expanding the horizons reap further from Uganda's rich natural resource base

With more than 60 percent of the oil rich Albertine Graben region unexplored and with the formal production of other valuable minerals yet to commence, Uganda should continue its exploration efforts. In line with the new legislative and regulatory framework approved in December 2012, the Government announced its first competitive bidding round for exploration in six blocks, these being Ngassa (410 Km2) in Hoima District; Taitai and Karuka (565 Km2) in Buliisa District; Ngaji (895 Km2) in Rukungiri and Kanungu Districts; Mvule (344 Km2) in Moyo and Yumbe Districts; and Turaco (425 Km2) and Kanywantaba (344 Km2) in Ntoroko District). Together, these six blocks cover 3,000 square kilometers. A number of firms submitted bids, including Armour Energy Limited of Australia; Walter Smith Petroman Oil Limited of Nigeria; Oranto Petroleum International Ltd of Nigeria; Niger Delta Petroleum Resources Ltd of Nigeria; Rift Energy Corporation of Canada; Glint Energy LLC of USA; and Swala Energy Ltd of Australia. It is hoped that this higher level of competition in the sector will result in increased efficiency.

iii. Managing the challenges for efficiency and effectiveness of investments

Three main challenges that must be managed. First, the granting of production licenses take an abnormally long time. Given that the bidding process has already commenced, the next milestone is to issue the production licenses. Previous experience suggest that this can take an excessive amount of time. While production licenses applications that were submitted by three companies, CNOOC (1); Tullow (3); Total (5) in 2012, only one license has been issued. Secondly, projects do not seem to be properly sequenced. While efforts toward the construction of a refinery has progressed well, with the commissioning of the project to a Russian Firm, its construction also needs to be fast-tracked, as in the case of the pipeline. Third, oil development projects should be synchronized with regional development. The commitment of regional countries to take equity shares in the refinery project is critical for its viability. Rwanda and Burundi need to indicate their interests in the project while Kenya is yet to indicate whether it will increase its participation to the average 8 percent.

Source: World Bank, Country Economic Memorandum, 2015

more critical if the rapidly expanding list of investments including hydro projects, oil refineries, oil pipelines, a standard gauge railway and numerous road transport infrastructure projects, is not properly managed and sequenced. Even if these projects are taken on by the private sector, there remains risks related to the financing component expected to come from the public sector.

Uganda is currently assessed to be at a low risk of debt distress. However, continued failure to collect revenue in the context of a rapid fiscal expansion could increase this risk. The update of the Joint World Bank/ IMF Debt sustainability analysis undertaken in March 2016 confirmed that Uganda continues to be at a low risk of debt distress. Beyond the planned fiscal expansion to support the infrastructure investment program, sustainability was judged against a lower threshold, following the downgrading of the Uganda's CPIA rating from 'strong performer' to 'medium performer.' The downgrading of this rating was mainly due to the limited improvements in the areas of transparency, accountability and corruption in the public sector since 2012. The implication was that Uganda had moved into a category of countries considered to have a much lower capacity to borrow and manage their debt than is the case for strong reformers. However, based on these assumptions, including that of a growth dividend, all debt burden indicators are projected to remain below Uganda's country-specific debt burden thresholds[7] under the baseline scenario and the standardized stress tests. However, if the investments in infrastructure do not result in an improved rate of growth or if they are delayed significantly, as has been the case with several energy projects, this could also result in rapid increases to the debt-to-GDP ratio, most likely to a level in excess of 50 percent. This is a key convergence criteria agreed upon in the East African Monetary Union Protocol last December by all East African Community member states.

In terms of external risks, downside risks are becoming increasingly significant. While low oil prices are beneficial to Uganda's balance of trade in the short term, such benefits could easily be offset by the negative impact on Uganda's exports (see Box 2), which impact will be even more significant if oil prices remain at extremely low levels. Furthermore, if oil prices take a long time to recover from the current levels of around US$ 30 per barrel, compared to the estimated breakeven price of US$ 60 per barrel for production in Uganda, it may require a re-evaluation of the phasing of refinery and pipeline investments. With China still rebalancing its growth towards consumption and services, its economy may decelerate much sharper than has been forecast, leading to further declines in the commodity prices, with negative effects on exports. Furthermore, a decline in the Chinese economy could adversely impact Uganda's planned investments in its infrastructure development program generally. It is forecast that China will account for about 37 percent of Uganda's investment program in the period from FY 2016/17 to FY 2019/20. The impact would be particularly significant for investments in the development of the oil sector.

Uganda remains vulnerable to risks associated with volatile climatic conditions and volatile food prices. Although the overall rate of inflation is expected to decline gradually as a result of good macro-economic management, food prices are expected to remain volatile due to unstable food production patterns, particularly given the limited availability of mitigation measures involving irrigation systems. Thus, food price volatility is likely to remain a significant issue. Moreover, there is a strong divergence in food price developments across Uganda, largely due to the insufficient integration of food value chains. With agriculture remaining the primary source of livelihoods for more than 69 percent of the population, supply disruptions resulting from climate change could have significant negative effects on consumption and livelihoods and could complicate the management of inflation.

Lastly, the Government's enormous infrastructure development program has the potential to generate massive benefits, which justify increased levels of the fiscal deficit. However, this is contingent on the investment program delivering its intended results, which would ensure that the fiscal position can be reconsolidated and debt serviced sustainably. The increase in development expenditure can be justified on the grounds that it mainly involves one-off investments necessary to address Uganda's significant infrastructure gap. Any short-term destabilizing effects on the macroeconomy may be mitigated by the high level of import content for these planned projects, which should prevent upward pressures on domestic prices.[8] However, in the absence of improvements to public investment capabilities, the increase in expenditure on infrastructure could rapidly lead to the build up of the debt stock. The question then is whether the expansive fiscal policy intended to facilitate the building of infrastructure can generate the intended results. The next chapter turns to this questions.

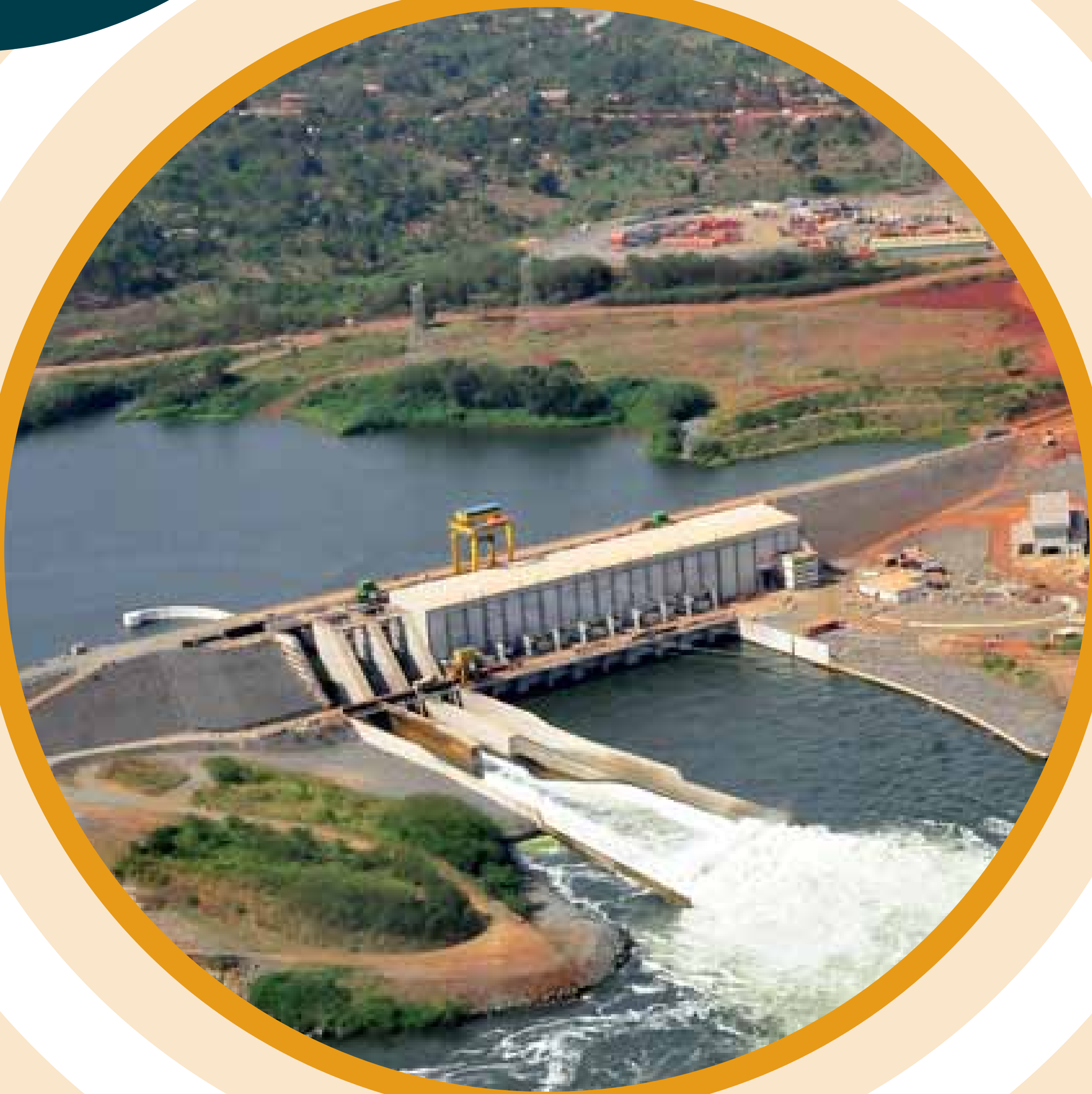
A DEBT SUSTAINABILITY ANALYSIS CONTINUES TO CONFIRM THAT UGANDA IS AT A LOW RISK OF DEBT DISTRESS UGANDA'S CPIA RATING WAS DOWNGRADED FROM 'STRONG PERFORMER' TO 'MEDIUM PERFORMER'

7. These thresholds indicate the maximum level to which a country can increase its debt with no major concern about with respect to solvency. For 'medium reformers', this suggests that the ratio of the present value of external debt should not exceed 40 percent in total exports, 150 percent in GDP, and 250 percent in domestic revenues. With respect to ability to service debt, the thresholds for this group of countries stand at a ratio of 20 percent for the debt service both in domestic revenues and in exports.

8. It is assumed that 90 percent of such projects are used to finance imports, leaving a mere 10 percent to be spent in the local economy.

PART 2

MOVING BEYOND SPENDING TO CREATING PRODUCTIVE ASSETS



- *Uganda can increase the rate of GDP growth from 6.5 percent to 9.2 percent per year, if the efficiency infrastructure investments was raised by a percentage point over the next decade.*

- *Uganda has recently pursued expansionary fiscal policies, driven by the desire to improve the country's infrastructure, increase the production of assets, and facilitate accelerated growth and productive exploitation of oil resources.*

- *Challenges related to budget execution could prevent Uganda from achieving its objective of accelerating growth in the short-term and raising productivity to be able to sustain a high rate of growth of its economy in the medium to long term.*

- *Overcoming these challenges and related investment inefficiencies will require addressing issues related to political interference, haphazard project selection, poor project preparation, and weaknesses in implementation processes such as procurement. To varying extents, all of these factors have affected Uganda's capital investment program.*

- *Uganda's public investment management system contains good elements, but needs to improve with respect to project preparation. As it is, the quality of projects at entry is poor; and project implementation is delayed ; cost escalated; resulting in the poor quality of completed projects; and poor operation and maintenance of completed assets.*

- *To convert its large investment program into productive assets, Uganda would need to strengthen the current system of PIM across all MDAs to ensure it maximizes value from public investments and eliminates waste.*

- *A systematic process of reform is required to strengthen institutions; to promote a common understanding of reforms that need to be implemented and how; and to strengthen mandates and incentives through legal reform.*

- *A sequenced action plan should first and foremost focus on the most binding constraints, namely better preparation of projects. Once this is addressed, further actions can be implemented to achieve ongoing improvements over a five year period.*

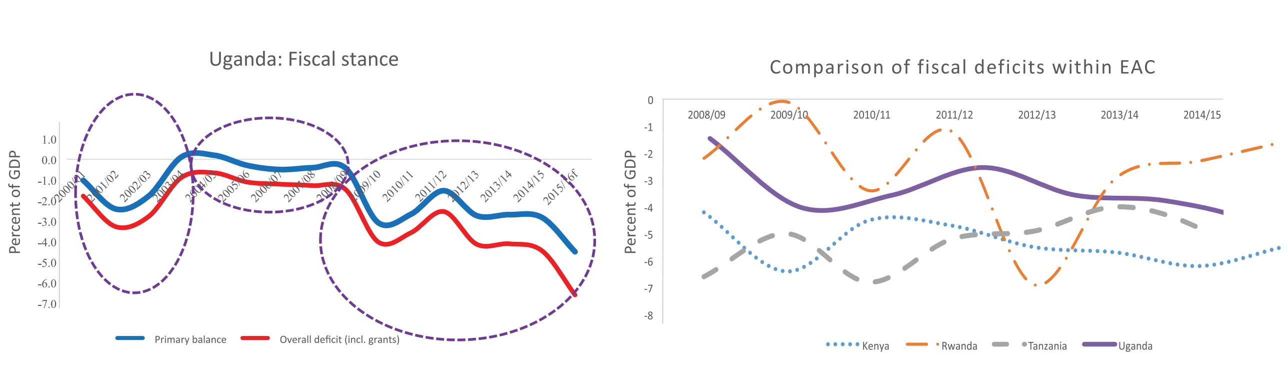
3. CAN UGANDA'S FISCAL POLICY DELIVER ITS AMBITIONS?

Uganda's fiscal policy has generally been ambitious and expansionary over the past decade in support of the National Development Plans and the Vision 2040 aimed at transforming the country to middle income status. The fiscal deficit almost reached over six percent of GDP by FY 2005/16, with over 40 percent of the resources allocated to the infrastructure sectors. The expansionary fiscal policy stance is expected to be sustained into the medium term as the Government continues its plan of addressing the key binding constraints to growth and building production capacities to exploit oil. Meanwhile, up to 36 percent of budgeted resource have not been released to the implementing agencies in the past. As a result, consumption has remained the key driver of growth in economic activity, and there are indications of a decline in the efficiency in utilization of public capital. These challenges have constrained the efficacy of fiscal policy in attaining the stated national objectives.

Over the past 15 years, Uganda's fiscal policy has passed through a number of significant transitions. Following an expansionary phase in the period from FY 1999/2000 to FY 2002/03, policies intended to facilitate fiscal consolidation were implemented in the period from FY 2003/04 to FY 2008/09, with the intention to crowd in the private sector. From the beginning of FY 2008/09, fiscal stimulus policies were implemented in order to address Uganda's significant infrastructure constraints and to mitigate the impacts of the global financial crisis that was beginning to become apparent. However, policy makers continued to implement expansionary policies, particularly during the 2011 election year, representing a departure from the principle of prudence and, in turn threatening macro stability.

The past four years, fiscal policy has been highly ambitious and extremely expansionary as also demonstrated by the significant size of both Uganda's overall and primary deficits. In fact, Uganda's fiscal policies have almost been the most expansionary of any country within the region. Uganda's fiscal deficit is estimated to have reached a value of 6.6 percent of GDP in the FY 2015/16 budget. At this level, in regional terms, the size of the fiscal deficit is second only to that of Tanzania's, which was projected to reach a value of 6.9 percent of GDP in the same year, while Kenya, which has also been in a worse position over the past five years sought to reverse it (see Figure 11). The increased fiscal deficits have come with a corresponding increase in the stock of debt, with the value of this debt increasing from 24.9 percent of GDP in FY 2009/10 to an estimated value of 37.3 percent in FY 2015/16.

Figure 11: Uganda's fiscal policy becomes one of the most expansionary within the region in recent years



Source: Ministry of Finance

Jinja Road the major gateway to and from Kampala City to the East

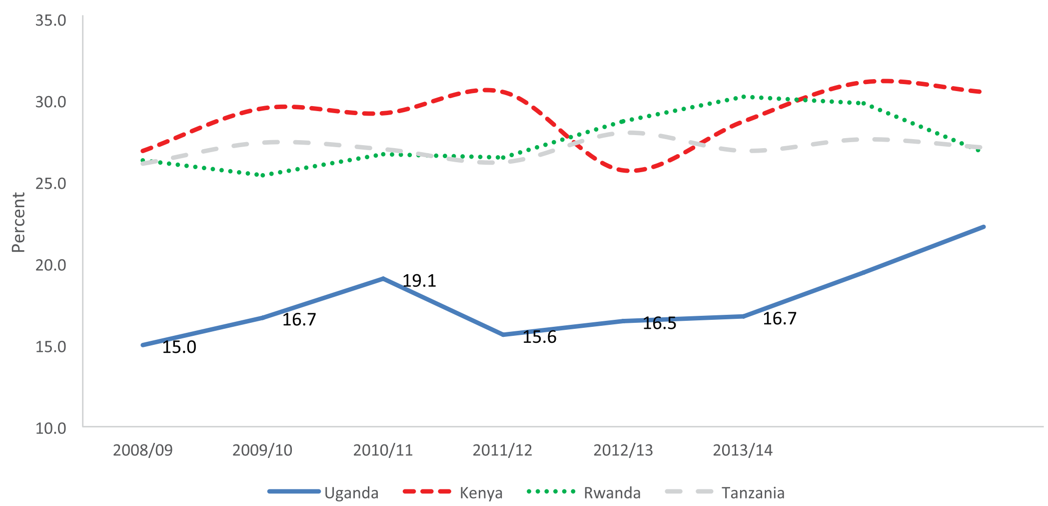
Uganda plans to increase its expenditure to support a huge public investment program to address the country's infrastructure deficit and to build production facilities to enable it exploit its oil resource

Expansionary fiscal policies are not necessarily ill-advised or unjustifiable. It is an established principle of economic theory that deficit-financed public investment projects can be justified as a corrective response, acting both as a countercyclical stimulus and potentially enhancing the stock of public assets, which in turn serves to stimulate the private sector and thus facilitate the achievement of long-term economic growth. However, to appropriately assess and provide recommendations for the Government's fiscal policy, this Economic Update discusses *how the Government is spending its resources, on what, and if this expenditure is resulting in the creation of the intended economic value.*

3.1 FISCAL STRATEGY ALMOST CONSISTENT WITH NATIONAL DEVELOPMENT PRIORITIES

Recent fiscal expansion in Uganda is largely the result of significant increases in expenditure to implement an ambitious public investment program, without corresponding increases in terms of revenue collection. Over the period from FY 2008/09 to FY 2014/15, the value of total expenditures increased from 15.0 percent of GDP to 19.4 percent. Uganda's average annual expenditure amounted to a value of 17.4 percent of GDP over this period, which was at least 10 percentage points lower than that of any of its regional peers, with Kenya's average expenditure standing at 29 percent; Rwanda's at 28 percent; and Tanzania's at 27 percent (see Figure 12). However, over the same period, the average annual value of Uganda's collected revenues amounted to only 11.8 percent of GDP, which resulted in the rapid increase in the fiscal deficit. As discussed in Chapter 2, Uganda plans to increase its expenditure to support a huge public investment program that is intended to address the country's significant infrastructure deficit and to build production facilities to enable exploiting the country's oil resource. Under this scenario, Uganda may catch up with and even surpass its regional peers before the requirement to limit fiscal expenditures, which is part of the EAC convergency criteria, is implemented.

Figure 12: Uganda lags regional peers in level of public expenditure

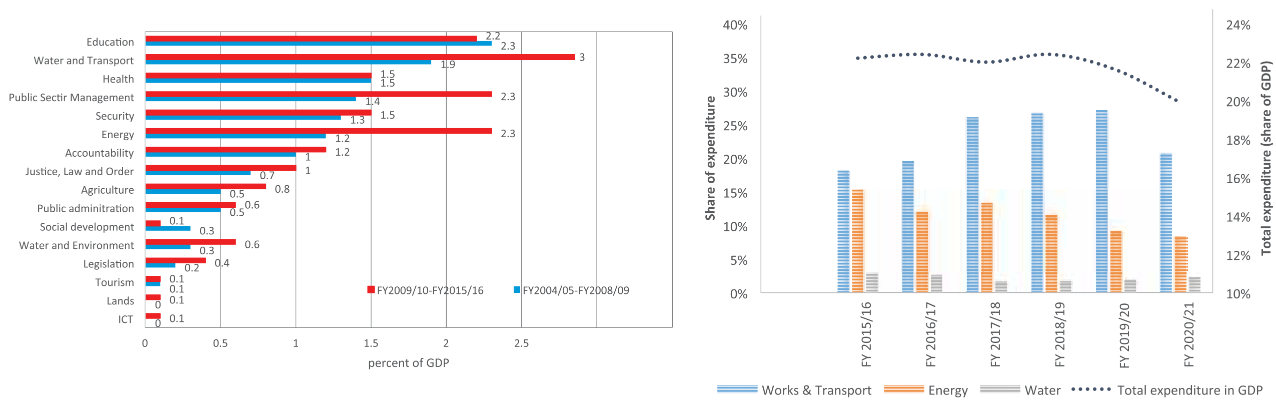


Source: IMF

The Government is increasingly emphasizing allocations to the development budget, the value of which has grown by 126 percent in nominal terms over the past four years. This shift in emphasis reflects the Government's efforts to build its capital base as a means of facilitating accelerated economic growth and transformation. Correspondingly, the share of allocations for recurrent expenditure has declined from an average value of 64.6 percent of total expenditures in the period from FY 2003/04 to FY 2007/08, to 58 percent in the period from FY 2008/09 to FY 2014/15. As a share of GDP, the value of development expenditures has almost doubled, from 4.3 percent to 7.6 percent over that period. The value of recurrent expenditure has grown at a much slower rate, increasing from 7.9 percent of GDP to 10.2 percent over the same period.

The fiscal policy implemented over the recent past is generallly supportive of the Government's Vision 2040 and the National Development Plans. Consistent with these plans, the budget framework allocates the most significant proportion of financial resources to the public works and transportation sector, and the allocation has increased from an average value of 1.9 percent of GDP in the period from FY 2004/05 to FY 2008/09 period to 3 percent over the past seven years (see Figure 13). The sector receiving the second largest proportion of financial resources is the energy and minerals sector, where the budget allocation has increased from an average value of 1.2 percent of GDP in the period from FY 2004/05 to FY 2008/09, to 2.3 percent over the seven years prior to FY 2015/16.

Figure 13: The shift in infrastructure spending has exploded and will continue to be significant



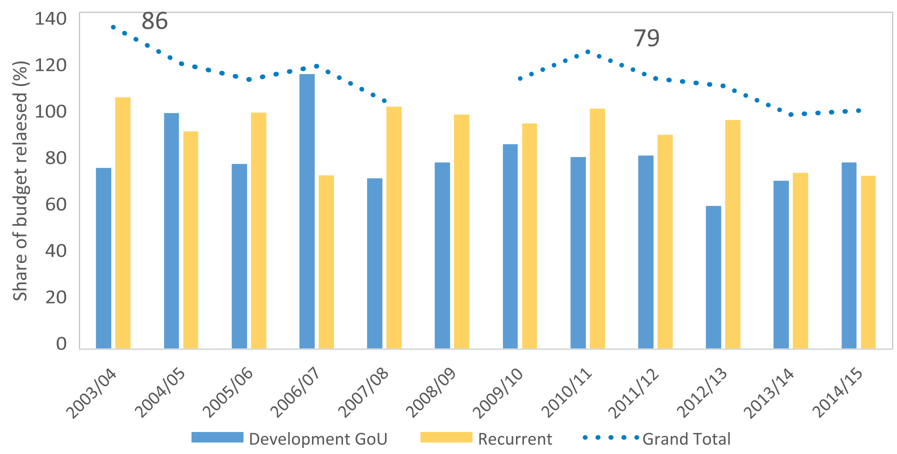
Source: Ministry of Finance

The Government's medium-term fiscal framework targets the total value of expenditures to be below 22 percent of GDP for the next five years to FY 2020/21. However, the proportion of budgetary resources allocated to the infrastructure sectors, including works and transport, and energy and water, will increase to an aggregate value of 41 percent of the total budget by FY 2017/18. It is expected that the proportion will gradually decline from FY 2018/19 back to its current level of approximately 31 percent. In nominal terms, the aggregate value of the allocation to both the roads and energy sectors will increase from the figure of UGX 4.2 trillion recorded in FY 2014/15 to UGX 38 trillion FY 2020/21 in oder to finance a number of flagship projects identified in the NDPs. Over the next five years, allocations for investments in infrastructure are estimated to reach a value of approximately US$ 9 billion. These planned projects include rehabilitation of Entebbe airport, and the construction of a standard-gauge railway line; three large dams for hydropower generation; an oil refinery; and two highways to improve the connection between Kampala and Jinja (the main eastern gateway for the country) and Entebbe (the main air gateway) respectively.

3.2 SMART BUDGETING IS UNDERMINED BY IMPLEMENTATION CHALLENGES

While Uganda's fiscal policies appear to have been well planned and appropriate, the ability of these plans to facilitate the achievement of the Government's objectives has been undermined by significant deficiencies in execution. These deficiencies have been particularly apparent in the execution of the development budget. The first measure by which the level of deficiencies can be determined is in terms of the proportion of funds released to implementing agencies. In FY 2003/04, 86 percent of overall budgeted resources to implementing agencies were released. However, this figure declined to 64 percent by FY 2014/15, even if some improvement was recorded in the period from FY 2007/08 to FY 20009/10. Furthermore, in the past, the execution of the recurrent budget was generally better than for the development budget. However, for FY 2013/14 and FY 2014/15, the level of execution seems to be roughly the same for both types of expenditure (see Figure 14).

Figure 14: The share of budgeted resources that is actually used has declined

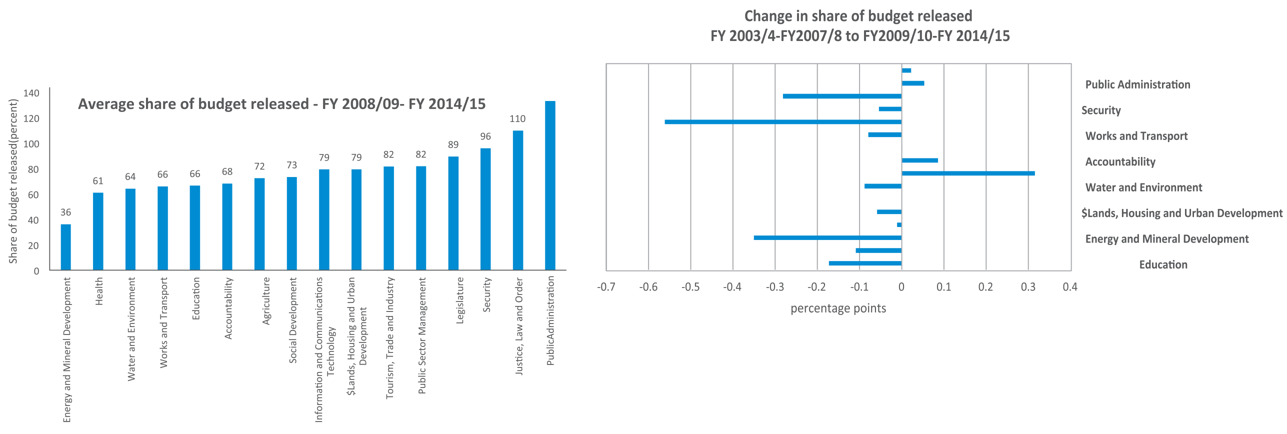


Source: MFPED BOOST Data base, 2014/15

Deterioration of budget releases has been recorded in all sectors, but it is most pronounced in the infrastructure and human capital development sectors. Compared to the level of performance in the period from FY 2003/04 to FY 2007/08, budget releases have worsened in all sectors except tourism, trade and industry; accountability; public administration; and justice, law and order (see Figure 15). If the proportion of budgeted resources released indicates the extent to which implementing agencies have actually executed planned projects, then overall implementation performance has deteriorated. For the priority infrastructure sectors, the level of budget releases has declined from an average figure of 73 percent recorded in the period from FY 2003/4 to FY 2007/8, to 55 percent in the five years to FY 2014/15. The level of performance of the energy sector has been particularly bad, with an average of 36 percent of its budget released each year in the period from FY 2008/9 to FY 2014/15. By contrast, the public administration sector, which includes Police, State House, President's Office, among others, has over-released by an average figure of 33 percent in the same period.

THE DEVELOPMENT OF INFRASTRUCTURE HAS BEEN THE GOVERNMENT'S STATED PRIORITY FOR AT LEAST THE PAST EIGHT YEARS.

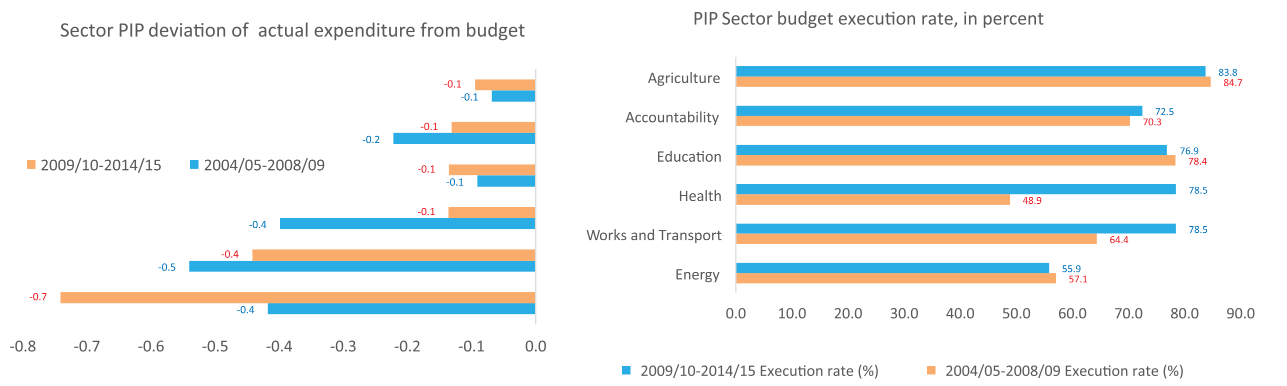
Figure 15: Worsening gap between ex post budget allocation and funds released



Source: MFPED BOOST Data base, 2014/15

Another measure by which the execution of fiscal policy may be assessed is in terms of the proportion of released resources spent to support investments that actually facilitate the achievement of the stated goals of the fiscal policy. According to data provided by Uganda's public investment plan, which maintains a data base for all projects that are publically funded, investments in infrastructure, particularly energy and transport, have been the Government's top priority for the past five years, with the value of these investments reaching an average annual value of 3.7 percent of GDP, significantly higher than the value of 2.3 percent recorded in the periom FY 2004/5 to FY 2008/09. However, these priority sectors are also the sectors in which the most significant deterioration in performance in terms of the level of execution of public investment projects has been recorded (see Figure 16). Overall, both the energy and transport infrastructure sectors have not been able to realize over two percentage points of GDP due to issues related to execution.

Figure 16: Energy and transport sectors have largest execution gaps

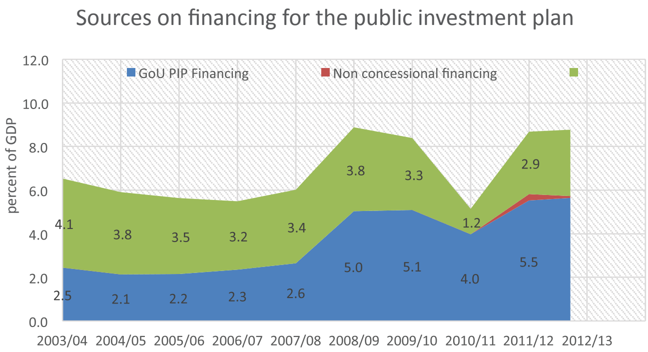


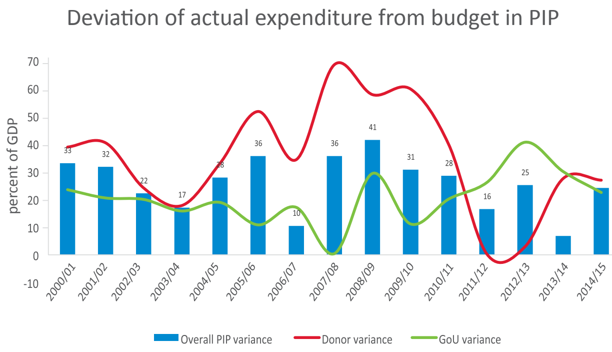
Source: MFPED BOOST Data base, 2014/15

The significant under-execution of the infrastructure budget has contributed to a huge backlog of infrastructure investments and has significantly weakened the impact of the Government's fiscal policy and overall development program. During the implementation of the first NDP from FY 2009/10 to FY 2014/15, the level of actual development expenditure remained well below the levels envisaged under the plan. According to the Public Investment Plan (PIP), only 78 percent of planned investments were actually realized in this period. While there was no change in the composition of planned expenditure over the period, domestically-financed development budgets were under-executed by an average rate of almost 30 percent. This rate of under-execution was particularly significant in the area of infrastructure investments, for which the actual average value of expenditure was lower than planned levels by around a full percentage point of GDP. As a result, the value of the backlog of planned infrastructure investments had increased by more than US$ 1 billion by the end of the first NDP. As a result of the failure of planned infrastructure investments to materialise, or at least only after significant delays, the objectives of the fiscal policy as well as its overall development objectives were not achieved.

The Government's increased use of own resources to finance public investments provides it more autonomy to make decisions, to implement projects, and to maintain them after completion. This underscores the need to build capacity to implement projects to realize full value from the investment program. The value of donor financing (excluding non-concessional loans) has declined from 3.4 percent of GDP in the period from FY 2004/05 to FY 2009/10 to 2.9 percent in the period since. The value of public investments financed by the Government's own resources has meanwhile increased from an average of 3.5 percent of GDP to 5.4 percent over the same time period (see Figure 17). A similar trend can be seen in the proportion of investments funded through the use of non-concessional borrowing (NCB), with a particularly significant increase occurring in FY2015/16. This may also be regarded as a positive development, as the use of this form of finance increases the Government's autonomy to select, appraise, manage and evaluate PIP projects. However, the capacity to implement these projects may not have increased in tandem. As such, the rate of execution of the donor-funded component of PIP improved from 46 percent to 80 percent for the periods in question, whereas the rate for the Government component deteriorated from 86 percent to 72 percent. This calls for further improving the capacities in the area of public investment management at central level as well as on local government level, given the significant value of investments managed at the local level.

Figure 17: GOU own financing of public investments increasing, as deviation of actual expenditures from budget increases



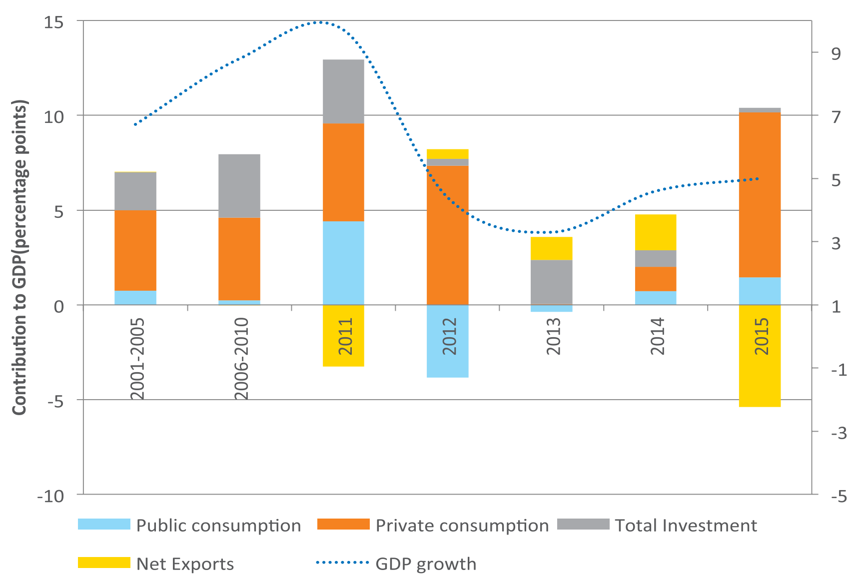


Source: World Bank Computations based on MFPED DATA

3.3 FISCAL UNDER-EXECUTION MATCHED BY INEFFICIENCIES IN INVESTMENTS AND THE ECONOMY

There is little evidence that public investments have contributed to improvements in the productivity of the economy with consumption contributing the largest share to economic growth. Over the past decade, the Government facilitated the achievement of accelerated economic growth through the fiscal policy by significantly increasing the value of its budget for investments in capital development. However, it is not clear if the invested resources are generating actual value. In fact, the rate at which the value of the Government investments are generating increases to the rate of growth of GDP is declining. In the period from FY 2010/11 to FY 2014/15, the Government's total investments contributed to 26 percent of the total rate of GDP growth. This is a much lower rate than the figure of 40 percent recorded in the period from FY 2005/06 to FY 2009/10. Instead private consumption has been the most significant contributor to increases in the rate of economic growth of (see Figure 18).

Figure 18: Uganda's investment contributing less to economic growth in recent years

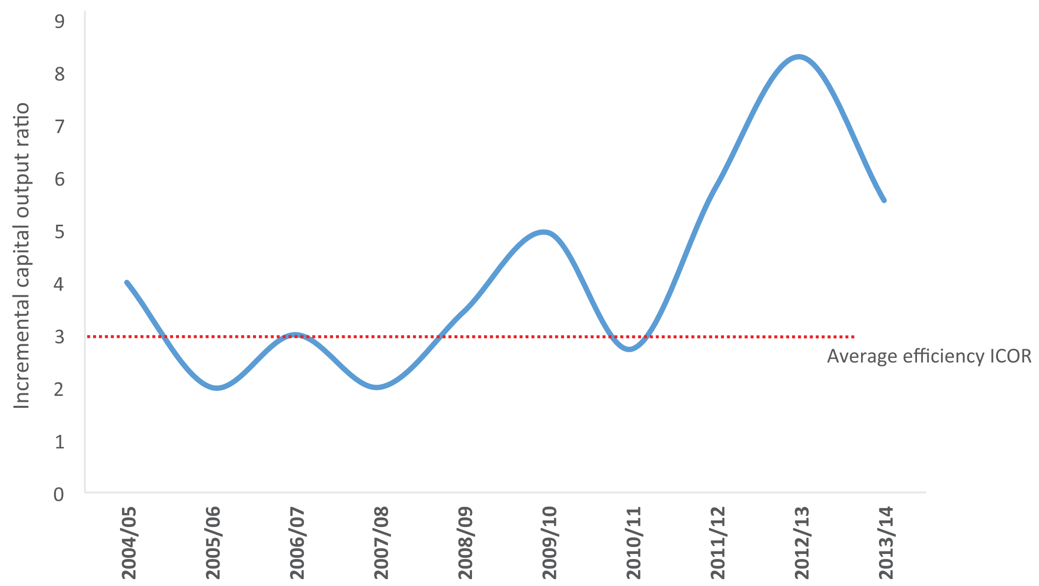


Source: World Bank staff computations, using UBOS Data

The efficiency of the Government's investments also leaves room for improvement given the value of the output that has been generated through public investment. Increases in the ratio between capital inputs and productive outputs can be seen as a measure of efficiency. Considering the recent increase in the value of the Government's investments, it is noteworthy that even when these investments have not been impacted by the execution issues described in the previous sections, they have not resulted in significant levels of increased growth. In short, these investments have not been able to leverage further private investments to generate faster economic growth. Examining the trends for Uganda's Incremental Capital Output Ratio (ICOR)[9], a rough indicator of this type of efficiency, shows that there has been a significant increase in this ratio in recent years , which suggests declining efficiency. Moreover, over the past decade, the average level of the ICOR has been significantly above the ideal average for a developing country using capital inputs efficiently (see Figure 19).

9. The incremental capital output ratio (ICOR) is defined as the ratio between investment in a period and the subsequent growth in output. The higher the ICOR is, the lower the efficiency. Since, growth in output can arise from other factors beyond investment in new capital (e.g. productivity enhancements or increased capacity utilization rate), and the lag between investment and increased output varies, reliable measure of ICOR should be over a long period of time, say three decades. Therefore, estimations over shorter periods are only rough estimates.

Figure 19: Additional capital generating less output over past decade



World Bank staff computations, using UBOS Data

The decline in the level of efficiency in the utilization of public capital is a cause of significant concern. The extent to which Uganda's public investments will contribute to increases in the rate of economic growth and productivity is determined by the extent to which they improve the level of the public capital stock, thereby reducing the cost of production for the private sector and thereby enabling it to engage in increased levels of economic activity and to create a greater number of productive employment opportunities. In the USA, for every dollar invested in the development of the interstate highway network in the period from 1954 to 2001, six dollars of economic productivity was generated. If Uganda maintains its ICOR at the levels recorded over the last eight years, then for every dollar invested in the development of public capital stock, it would generate only 0.8 dollar worth of economic activity. Thus, the rate of return (economic and social) on Uganda's public investments depends on how effectively and efficiently the public investments are managed.

Fiscal policies will only facilitate the achievement of their intended objectives and economic value if well-designed budgets are effectively executed. The challenges related to budget execution could therefore easily prevent Uganda from achieving its objective of accelerating growth in the short-term, and raising productivity to be able to sustain a high rate of growth of its economy in the medium to long term.

THE RATE OF RETURNS ON UGANDA'S PUBLIC INVESTMENTS DEPENDS ON HOW EFFECTIVELY AND EFFICIENTLY THE PUBLIC INVESTMENTS ARE MANAGED.

10. Fiscal policies will only facilitate the achievement of their intended objectives if well-designed budgets are effectively executed. It is only in this manner that the investment of resources will facilitate the delivery of the intended economic value. The issues related to the execution of the budget that have been described in this section of the update could easily prevent Uganda from achieving its objective of accelerating growth in the short-term, and raising productivity to be able to sustain a high rate of growth of its economy in the medium to long term.

4. WHY IS UGANDA NOT GENERATING GOOD RETURNS ON ITS INVESTMENTS?

Addressing the binding constraints to growth in Uganda and building production capacities to exploit oil requires managing investments effectively. Currently, the ability of the Government's fiscal policy to achieve its planned objectives is to some extent constrained by inefficiencies in public investment management. Uganda is currently ranked in 46th position out of 71 countries in terms of quality of institutions for public investment management. Among the issues affecting the effectiveness of public investments are implementation challenges that result in delays, cost overruns, and perpetuity. Based on lessons from other countries, the systems in Uganda could particularly be improved in the area of project appraisal and ex-post evaluation to establish minimum conditions to support efficiency.

The discussion above indicates that there is a clear need to enrich fiscal policies with policies and strategies that acknowledge the weaknesses in the management of public investments. It recognizes that these can derail public spending and weaken the growth process, with adverse consequences for fiscal solvency and stability. In this respect, global lessons abound, but these can only offer guidance where own capacities have been assessed and workable approaches adopted.

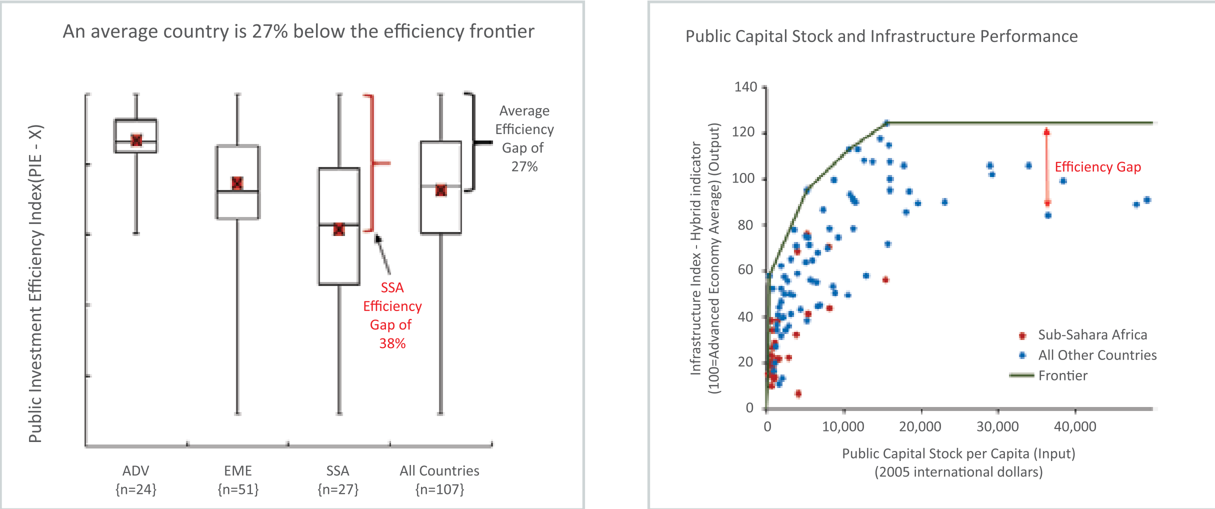
4.1 INEFFICIENCIES IN INVESTMENT RESULT IN FAILED CAPITAL ACCUMULATION EFFORTS ACROSS THE WORLD

Global evidence shows that public investments can be affected by a range of different types of inefficiencies, any one of which can have costly economic implications. The International Monetary Fund (IMF) estimates that the global average difference between the ideal value of efficiency of investments and the realized values (efficiency gap) stands at a 27 percent. The gap for countries in the Sub-Saharan Africa Region is significantly higher, with the average figure estimated to be 38 percent. At this level of inefficiency, even very high levels of investment in the development of a country's infrastructure stock will produce disappointing results (see Figure 20). In other words, whatever the level of input, the degree of inefficiency prevents the investments from being converted into productive assets and hence achieving the overall objective of an accelerated rate of economic growth. On the one hand, the selection of the investments may be based on badly formed criteria. On the other hand, implementation may be weak, characterized by waste, corruption and misappropriation. Finally, even if the investment does result in the production of a potentially useful public good, it is often not operated or maintained well, which again reduces the level of return on the investment.

Kampala CBD which houses a number of government ministry offices

there is a clear need to enrich fiscal policies with strategies that acknowledge the weaknesses in the management of public investments

Figure 20: The large efficiency gap in public investments costly to public capital



Source: IMF (2015); "Public Infrastructure Trends and Improving the Quality of Investments"

The tools to manage public investments have evolved significantly over the past decades, but this has not necessarily led to efficiently managed capital investments. In the 1970s and 1980s, the management of public investments focused mainly on Public Investment Programs (PIP). These programs were originally designed to put together capital investments intended to facilitate the construction of physical assets. However, over the past two decades, there has been a paradigm shift, with the integration of a range of projects and programs under PIPs to match them with government's medium term financial frameworks. This shift meant that the PIP became a database to organize a range of projects and programs that are not necessarily intended to build capital assets. The PIP enabled the centralized collation of plans for the development of affordable projects and programs to support the spending allocation process. Once such assets were constructed, they ceased to be part of the PIP, with the resources required for their operation and maintenance being allocated through the recurrent budget. However, because of the link between the PIP and the budget, the PIP could only include projects that had been already included in the budget. These projects could also be characterized by varying degrees of quality, depending on the prevailing regulations for appraising projects for financing. Therefore, the PIP did not fulfill the purpose of collating a bankable, ready-to-finance pool of capital projects, a process required to ease implementation and to improve the overall level of efficiency of public investments

Over the past two decades, many governments have adopted an increasingly strategic approach to both the management of public investment projects and public financial management (PFM), with these two areas being two sides of the same coin. This often involved moving towards a more integrated approach, with investment decisions increasingly delegated to line ministries. Although this approach resulted in some initial successes, especially in the area of budgeting, it did not place sufficient emphasis on the strategic importance of public investment to the economy. Thus, costly decisions with long-term implications may be undermined by short-term political considerations. The realization of the inherent dangers of this approach has led to the resurgence of a different approach to public investment management, with the more systematic identification of long-term priorities.

However, unless accompanied by measures to strengthen the framework and capacities of institutions involved in PIM, the new integrated approach did little to facilitate the achievement of higher levels of efficiency. It was expected that within the new integrated process, there would be a centralized framework to guide the management of projects, including selection and screening processes. It was also expected that PIPs would serve as a means to manage overall public expenditure. Unfortunately, there were many cases in which institutional capacities to handle these processes became overstretched, both within the Ministry of Finance and within the line ministries. This was particularly true in the case of ministries of finance and planning, which are usually expected to scrutinize all projects and programs, even when they do not include a significant level of capital expenditure. In some countries, the share of capital expenditure within the PIP is less than 50 percent. Moreover, if there is no designated process for the preparation and implementation of projects, projects are sometimes included into the PIP before these projects are ready to move to the investment phase. In some instances, this results in delays to implementation, with feasibility studies only conducted after funds have been allocated to the capital budget. In others cases, the quality of the projects may have been undermined by the failure to implement pre-appraisal or feasibility studies.

As a result of these factors, the quality of PIM has often remained poor, with many national administrations failing to realize their intended objective of developing their stock of physical capital in a manner that facilitates increased economic growth. The causes of these failures are many and varied, including undue political interference and corruption in the management of public investments; haphazard project selection, with no objective selection criteria; unclear lines of responsibility and accountability; skill and capacity gaps in the areas of project appraisal, procurement and management; perverse incentives for project managers to underestimate risk; and lack of coordination between different levels of government, across jurisdictions.

As a result of weaknesses of this nature, the level of wastage in public investments is often significant. On the one hand, there are numerous recorded cases of countries investing huge amounts of resources in "white elephants", or projects that just simply do not generate a significant return on investment. Such cases are usually characterized by significant weaknesses in the areas of fiscal and overall economic management. In particular, countries that generate significant revenues from the export of natural resources but that have weak institutional capacities may be afflicted by the so-called "resource curse," which refers to the paradox that countries with an abundance of natural resources tend to have less economic growth, less democracy, and worse development outcomes than countries with fewer natural resources. On the other hand, there are many cases of projects that run well over their planned costs and completion dates not only as a result of bureaucratic delays and the diversion of resources, but also from the underestimation of costs as a result of over optimism. In many developed nations with a high level of institutional capacity, such as the UK, the cost and duration of construction may exceed initial estimates by an average 7-10 percent. The contrast with nations with weak PIM systems can be startling. For example, in Tanzania, it is not unusual for the construction of a project to cost more than 60 percent in excess of the original estimate, or to be completed in more than twice the original planned time. In the case of Ethiopia, these overruns can be twice as high again.[10] In circumstances such as these, investments in the establishment of effective systems to manage public investment are likely to yield high returns.

While consistent data to measure sector specific waste are not available, indices that measure the overall quality of the institutional environment on which public investment management is based indicate that the management of public investments in Uganda does not facilitate the achievement of optimal value. According to the Public Investment Management Index (PIMI),[11] Uganda ranks in 46th place out of the 71 countries that were assessed. While this ranking indicates that Uganda's performance is comparable to those of its neighbors, including Kenya (which ranked in 44th place) and Tanzania (in 48th place), it places it well behind the best performers in the region, such as Ghana (in 27th place) and Rwanda (in 12th place) (see Figure 21).

Meanwhile, efficient management of public investments will become even more important for Uganda in the coming years. With the prospect of significant revenues from the exploitation of oil, Uganda is also expected to increase its investments to use these revenues for the intended purpose of transforming its economy. When oil production begins to generate substantial additional revenue for the Government, new challenges will emerge. The most critical objective may no longer be to further accelerate the implementation of public investments, but rather to slow down the growth of public spending, including public investment, in order to mitigate the negative impact of the sudden inflow of revenue from oil production. In this context, the top priority should be to increase the absorptive capacity of the Government in terms of the size of its executed public investment program and to improve the structure of this program, including through improvements to project selection processes and practices.

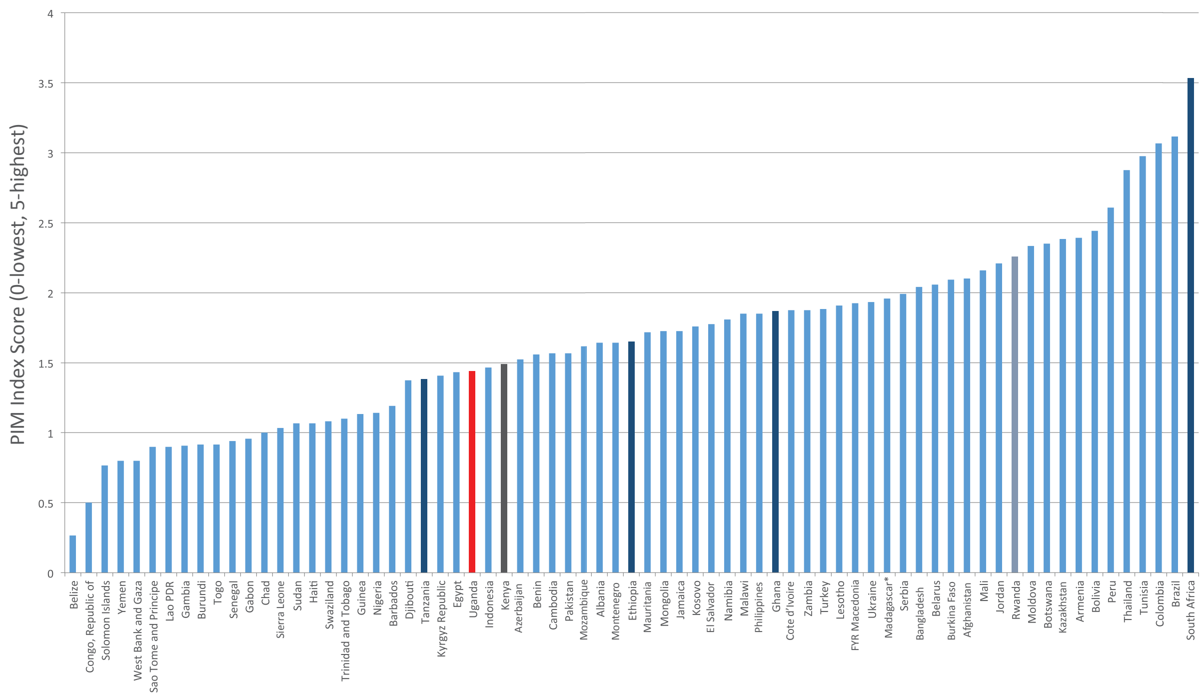
Implementation of the PIM reform program designed by the Government will develop Uganda's absorptive

10. Construction Sector Transparency Initiative (2011).

11. The PIM index is based on the four categorization of elements of public investment management: i) strategic guidance and project appraisal; ii) project selection; iii) project management and implementation; and iv) project evaluation and audit; as an attempt to measure the efficiency of the public investment management process across 71 countries, of which 40 are low-income countries.

capacity. It will also prevent overspending (at least initially), as it will take time to develop a pipeline of sound, high-priority projects and to complete all the necessary feasibility and pre-investment studies for these proposed projects. Thus, now is the critical moment for Uganda to revamp its public investment management systems, with these improvements particularly crucial for the achievement of stability and prudent management with the prospect of increased revenues.

Figure 21: Uganda fairs poorly in public investment management in relation to peers



Source: IMF (2014), The Public Investment Management Index data base

4.2 GLOBAL EXPERIENCE: HOW ARE PIM SYSTEMS BEING IMPROVED AROUND THE WORLD?

Global experience demonstrates that the establishment of an efficient PIM system involve significant challenges. In particular, it involves building institutional capacities to manage the wide range of technical aspects of investment management. It also involves coordinating these processes across many institutions in a range of different sectors to ensure the achievement of a common objective. Depending on the specific characteristics and backgrounds of the country involved, the approaches to institutional arrangements, processes and outputs expected out of a PIM system can differ. The desired outcome is to match these specific characteristics with systems to design and implement projects in a manner that will maximize economic value for each country.

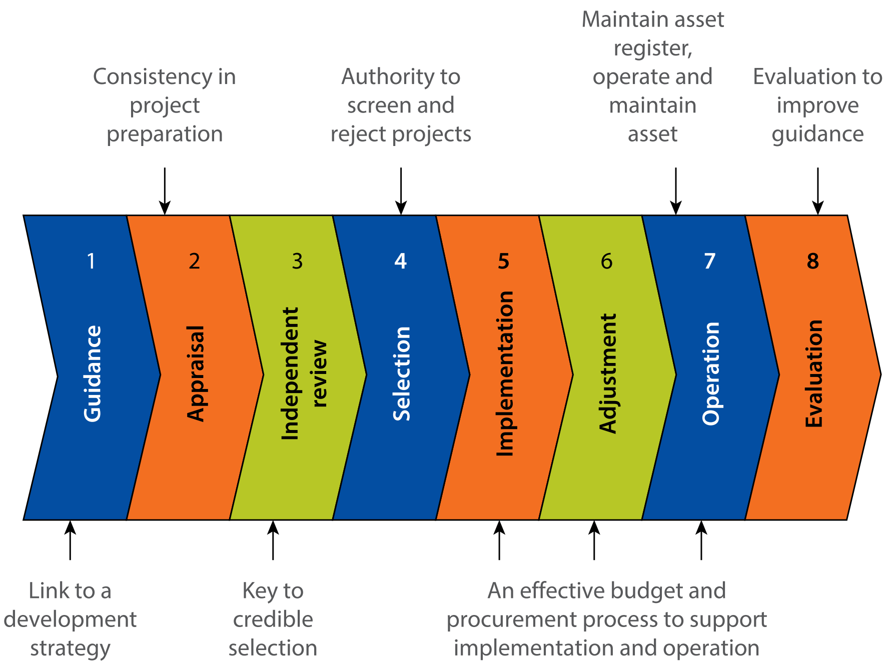
With the growing recognition of the need for the systematic identification of long-term priorities, global experience suggests that good PIM systems are characterized by a number of common features.[12] For countries in varying conditions and with varying levels of development, these features emphasize the minimum basic processes and controls that are likely to generate optimal levels of efficiency in decision-making processes related to public investments and to the implementation of these investments. In situations where traditional budgetary financing and capacity have been recognized as insufficient to meet a country's development goals, governments have developed a range of new institutions, such as private-public partnerships, sovereign funds, and others semi-autonomous entities to undertake large investments on behalf of the Government. However, it is still critically important to establish the conditions that ensure the efficiency of investments and maximize the value for money that these investments

12. Rajaram, A., Le, T.M., Biletska, N., Brumby, J. (2010). A Diagnostic Framework for Assessing Public Investment Management. World Bank Policy Research Working Paper 5397, Washington, DC.

generate. This approach focuses on the identification of the institutional features that would minimize major risks and provide an effective systemic process for the management of public investments. It also defines indicators for inputs, processes and outputs to enable a meaningful assessment of the functioning of public investment systems. These indicators are linked to institutional features with eight key stages that characterize a good practice PIM system and are intended to provide objective measures to identify sub-optimal processes (see Figure 22).

The first stage, the guidance stage, involves the provision of guidance for the development of the project concept, and the preliminary screening process. The key aim at this stage is to ensure that investment choices are justified in terms of the country's development objectives. Many countries, including most countries within the East African region, have developed both a national vision and a framework to provide such guidance. However, the challenge is to ensure that these frameworks are sufficiently specific and coherent. They should have sufficient authority to effectively guide the PIM process, including defining the criteria for the rejection of some projects at the point of preliminary screening. Chile, which has one of the most effective PIM systems in the world, uses a screening system that rejects between 5-8 percent of project proposals at this stage.

Figure 22: The Eight Stages of the Public Investment Management Cycle



Source: World Bank (2015): "The Power of Public Investment Management: Transforming Resources into Assets for Growth", Washington DC

The second stage, the appraisal stage, involves an assessment of the quality of project proposals presented for investment in terms of their social and economic value, with this assessment being used as a basis for preliminary acceptance or rejection of the concept. A key component of this assessment is a rigorous cost-benefit analysis, which ensures the cost-effectiveness of the proposed project (see Box 5). For project appraisal to be effective, technical guidance should define a clear, standardized approach to economic, social and environmental evaluations. It should also ensure that the technical capacities of the Government agencies are adequate to handle these responsibilities. The technical guidance provided should be appropriate to the scale and scope of the project, with projects of higher value requiring more rigorous tests to determine their degree of financial, economic, social and environmental feasibility and sustainability.

It is good practice at this stage to also generate an inventory of appraised projects. This inventory, with each appraised project ranked and prioritized for budget consideration, will facilitate the selection process. As has been implemented by Chile, the inventory should also be used to track projects that have been selected for implementation and enables policymakers to revisit rejected projects if underlying circumstances change so that these rejected projects become likely to generate net positive benefits. The key element of efficient PIMs is the provision of formal, standardized, clear guidance to all MDAs, with the provision of this guidance for all projects of defined economic value, including those implemented as public private partnership.

Box 5: Cost-benefit analysis is not just about the profitability of the project!

Cost-benefit analysis (CBA) assesses the costs and benefits of a project and reduces them to a common denominator. If benefits exceed costs, with both expressed in terms of present value, then the project is acceptable. If not, the project is rejected. Benefits are defined relative to their effect on the fundamental objectives, while costs are defined relative to their opportunity cost, which is the benefit forgone by not using these resources for the best alternative use. By doing so, cost-benefit analysis seeks to ensure that no alternative use of the resources consumed by the project would secure a better result from the perspective of a country's objectives.

In contrast to the concept of financial profit, this CBA seeks to measure both the economic and social profit, which in turn demonstrates the effect of the project on the fundamental economic and social development objectives. These different concepts are reflected in the different items considered to be costs and benefits and in their valuation. Thus, a money payment made for wages is by definition a financial cost, but it will be an economic cost only to the extent that the use of labor in this project implies some sacrifice elsewhere in the economy with respect to output and other objectives. Conversely, if the project has an economic cost which does not involve a financial flow—for example, because of environmental costs—this does not constitute a financial cost.

The key requirements for cost-benefit analysis are:
(i) specification of the costs and benefits;
(ii) valuation of costs and benefits;
(iii) choice and formulation of constraints;
(iv) treatment of risk and uncertainty;
(v) choice of the rate of interest for discounting future costs and benefits; and
(vi) choice of a decision rule for accepting or rejecting projects.

Economic costs and benefits are measured by "shadow prices" which may approximate market prices in well-functioning market systems. However, measuring these prices within imperfect markets-like those characterizing Uganda – can be a big challenge. This underscores the need for clear guidance on how such inputs into the CBA are derived.

Source: World Bank report "Russia: Towards Improving the Efficiency of Public Expenditures" (2001)

The third stage involves the independent review of the project appraisals. The key element of an independent review is to provide the basis for checking any subjectivity or optimism bias that may be reflected through underestimated costs or overestimated benefits. Therefore, the independent review should be conducted by an entity that is as detached and independent as possible from the entity responsible for developing the project proposal. In many countries, this function is performed by the ministries of finance or planning. However, the use of independent entities, such as research institutes or universities, can give even higher credibility to the process, and some countries also undertake public hearings (see Box 6).

Box 6: Lessons on independent review in PIM systems

The United Kingdom: Since 2001, business cases for projects have been subject to independent review under the so-called "Gateway process", which embodies a series of short, focused, independent peer reviews at key stages of a project. These reviews highlight the risks and issues that need to be addressed to ensure the successful delivery of the project. However, more attention is paid to larger projects, with Treasury approval required for road projects of a value of more than £500 million. However, the level of Treasury involvement in reviewing the appraisal of other transport projects varies widely depending on the project's scale and complexity. In addition, major infrastructure projects are subject to a public hearing before the end of the appraisal stage.

Chile: Project appraisal is conducted by the planning ministry rather than by the sponsoring ministry. To subject these appraisals to independent review, a separate unit was created within the planning ministry.

Korea: The Public and Private Infrastructure Investment Management Center (PIMAC) was established in 1999 in the Korea Development Institute (a semi-autonomous agency under the umbrella of the Ministry of Strategy and Finance) to conduct pre-feasibility studies of large projects independent of the sponsoring ministry. In practice, PIMAC conducts all appraisals for projects above a defined threshold.

Source: World Bank 2015; "The Power of Public Investment Management" Washington DC.

The fourth stage is the selection and budgeting stage, at which point a project is formally selected and entered into the budget cycle as a capital expenditure. This stage is the most critical intersection between the budget and project cycles, even though budget must be flexible to allow for recurrent expenditure incurred prior to this stage, to prepare the project, and after this stage, to maintain and operate the asset. Therefore, this stage is a key determinant of the level of efficiency of budget execution and overall fiscal policy management, and thus serves as a "gate keeping stage." At this stage, the pressures to include projects on the basis of political considerations, including pressures exerted by MDAs, development partners, private lobbyists and contractors, can be enormous, regardless of the results of an effective appraisal. Therefore, it is absolutely essential that a strong "gate keeper function" exists, with clear, formally defined criteria for the selection of projects, with such criteria legally backed and publicized amongst all stakeholders. In many countries with good practice PIM systems, including the United Kingdom and Chile, this gate keeper function is exercised by the Ministry of Finance or National Treasury.

In summary, these first four stages discussed above take place during the pre-investment phase and determine whether the projects being implemented will be executed efficiently and will deliver the expected economic value. In many countries, many of the processes that characterize the pre-investment phase, particularly those during the first three stages, are implemented haphazardly, simply not implemented, or subjected to political influence. However, these stages form a strong foundation for the effective implementation of any project. Countries such as China and Brazil have been growing fast and investing heavily, with investment rates reaching to a value of 50 percent of GDP over the past two decades. However, the weaknesses in these countries' PIM systems, particularly in the area of screening and preparing projects for investment, may negatively affect both nations' growth prospects. With the increasing tendency of governments to formulate comprehensive national development plans, many countries have in place a relatively solid basis for the identification of projects at the national level. However, despite the vital role that these plans play, they do not necessarily prevent the inclusion of poorly designed and poorly conceived projects into a public investment program nor allow for a process that scrutinizes a new concept for consideration.

The pre-investment phase is followed by the investment phase, with the first of the four stages that characterize this second phase being the project implementation stage. This stage involves the planning, procurement, fabrication, civil work construction, installation, and the formulation of the terms and conditions of contracts in order to develop detailed schedules and plans for the construction or implementation of the project. During the processes related to the execution of the project, the construction team operates on the basis of the prepared schedules, procedures and templates.

In a good PIM system, the defining characteristic of this stage is the availability of the appropriate capacities, including the capacities to disburse funding, procure materials and undertake engineering and construction works on the project. If the pre-investment phase works effectively so that projects that reach implementation are indeed 'ready-to-go', with designs that include clear organizational arrangement and a realistic timetable, implementation of such projects will be easier. However, failures can still result from weak capacities within the agencies responsibility for the implementation of a project or a failure to coordinate across many agencies. In practice, projects are implemented by a range of different MDAs or sub-governments. This calls for a clear delineation of responsibilities and functioning coordinating arrangements based on a consideration of the institutional capacities required to manage and monitor project implementation timelines, project costs, multi-year budgeting processes and effective procurement.[13]

Procurement is a core aspect of the execution of investments and is often forming the most significant challenges to the implementation of a project. In many countries, the procurement function has evolved significantly over recent years due to technological innovations, although capacity requirements can vary widely depending on the level of development of the country and the nature, size and complexity of the projects being executed. The project and procurement planning capacities necessary for the implementation of a relatively simple project, such as a straightforward road development project, will clearly be different from those required for the implementation of a project involving the development of multi-part technological systems, concessional contracts or public-private partnerships. Clearly, mechanisms for the selection and procurement of contractors can influence price and quality and can either exacerbate or mitigate the risk of fraud and corruption. On the other hand, if such mechanisms are accompanied by excessively stringent regulation or lack of capacities, they can result in delays to implementation.

In many countries, where core PFM functions such as contact management and cash management are not functioning well, procurement processes are often prone to significant efficiency losses. This is because procurement processes involve large, discrete contracts, with an associated risk of abuse and corruption, facilitated by poor accounting practices and collusion within and between political elites. A recent review of around 500 World Bank funded projects around the world concluded that unsatisfactory performance in the area of procurements

The Nothern Bypass, built to reduce traffic congestion from the city center

after a project is fully operational, the final stage involves a comprehensive process of evaluation to determine the quality of all previous phases

13. In a number of countries, including the UK and Malaysia, centralized units, known as delivery units, have been established to coordinate and monitor all processes related to implementation of priority projects or programs, including the identification of constraints and a determination of the means to address them to ensure the efficient implementation of public projects. However, even under such arrangements, the capacities of implementing agencies within the sectors remain critical.

significantly affected the development outcomes of a high proportion of these projects, with poor outcomes being three to five times more likely in cases involving unsatisfactory procurement performance. Poor procurement practices are also associated with poor design and appraisal and cost overruns. The level of implementing agencies' technical capacities can have major implications on how the project is delivered, even if these agencies are merely responsible for the oversight of the construction of projects.

Somewhat overlapping with the project implementation stage, the next stage of the investment phase is the project adjustment stage. This stage involves processes related to monitoring and adjusting implementation to ensure the achievement of development objectives. Adjustments to implementation are almost inevitable because the cost of materials may fluctuate; the cost of funding may change; physical and social conditions may evolve; providers might not perform as expected; and political demands might evolve as the project is implemented. The need for adjustment is often exacerbated if projects are not appropriately prepared and designed to standard during the initial stages. The key processes related to adjustment include project monitoring, contract management, management of contract variations, and the evaluation of budget and funding arrangements. This phase of project execution is also sometimes referred to as "project execution and control." [14] The current construction of the Karuma dam, a mega hydro project which has attracted major attention because of what appears like the construction defects in the dam walls, will provide a good example if it is handled professionally.

The next stage of the investment phase is the operation of facilities stage. The realization of value is also determined by the degree to which it is operated efficiently and effectively to deliver the intended services. Thus, it is vital that sufficient financial resources are allocated to ensure appropriate operations and maintenance of the project as a means of ensuring that it continues to deliver value.

The final stage of the investment phase involves the basic completion review and evaluation stage. After the project is fully operational, the final stage involves a comprehensive process of evaluation to determine the quality of all previous phases, with this evaluation providing inputs to policymakers for future interventions and for the development of new projects. During this stage the ex post collection of data related to the total expenditure involved in the project compared to projected expenditure at the commencement of the project and a selective evaluation of project results, all of which can serve as input for the planning and implementation of future projects.

4.3 UGANDA'S PIM SYSTEM: WORKS TO SOME EXTENT, BUT LEAVES ROOM FOR IMPROVEMENT

There is room for improving public investments in Uganda to better facilitate the achievement of increases to the rate of growth of GDP and to the achievement of the country's development objectives. A number of factors, including a non-conducive regulatory environment and external shocks, can hinder the effectiveness of investments in these terms. However, it is also clear that the public sector has not performed at optimal levels. For public investments to be considered effective, the resources invested must result in increases to the value of public capital stock, thereby facilitating improvements to the level of productivity at the national level. Public investments have this effect if they create capital that lowers the cost of production and distribution, and hence enable the private sector to achieve higher levels of productivity, thereby facilitating increased economic growth and the creation of productive job opportunities.

Over the past 30 years, the Government of Uganda has developed systems and processes to ensure a higher level of efficiency throughout its operations.[15] One measure implemented to achieve these improvements was the sector-wide approach (SWA) introduced in FY 1999/2000 to ensure that institutions delivering related services cooperated to achieve higher levels of synergy and allowed the stakeholders from cluster sectors[16], through sector working groups (SWG), to participate in decision making processes to facilitate the achievement of Uganda's strategic objectives. The SWA was implemented to improve systems to examine and review policies and plans; to identify priorities; to assess resource requirements and cost implications, including proposed medium term budget allocations; to review performance targets and outcomes; and to facilitate the identification and approval of development projects. The SWGs are accordingly responsible for the formulation and delivery of sector

14. The term "control" is utilized because execution does not refer merely to the implementation of previously formulated plans, but involves a watchful process in which the project manager should understand what is being done, how circumstances surrounding the project evolve, whether there are significant changes that require adjustments to the project and how he or she should adjust to these circumstances.

15. A detailed assessment of the PIM in Uganda along the eight stages of project cycle can be found in "Strengthening Public Investment Management in Uganda: A Diagnostic Report", an output of the technical assistance to strengthening Uganda PIM System.

16. These sectors include: Agriculture; Lands, Housing and Urban Development; Energy and Mineral Development; Works and Transport; Information and Communication Technology; Tourism, Trade and Industry; Education; Health; Water and Environment; Social Development; Security; Justice, Law and order; Public Sector Management; Accountability; Legislature; and Public Administration.

investment plans; sector budget framework papers; annual budget estimates; annual procurement plans; quarterly monitoring reports; reviews of existing/ongoing projects; annual budget performance reports; and proposals for new projects.

More recently, as Uganda has continued to streamline the national planning process to facilitate longer term planning for the country. This involved the establishment of the National Planning Authority (NPA), as mandated by the National Planning Act of 1999. The NPA is tasked with the preparation of the National Vision and an associated roadmap to guide national development. After the end of the period of the first NDP in June 2015, the NPA launched the current five-year development plan, which is intended to guide development processes for the period until FY 2019/20. The NDPs are formulated with reference to the National Vision 2040, which defines Uganda's overall development objectives, and which provides broad guidelines as to how this vision will be achieved. On the basis of lessons learnt from the implementation of the first NDP, a significantly greater emphasis has been placed on aligning the medium term expenditure framework with the priorities identified in the second NDP.

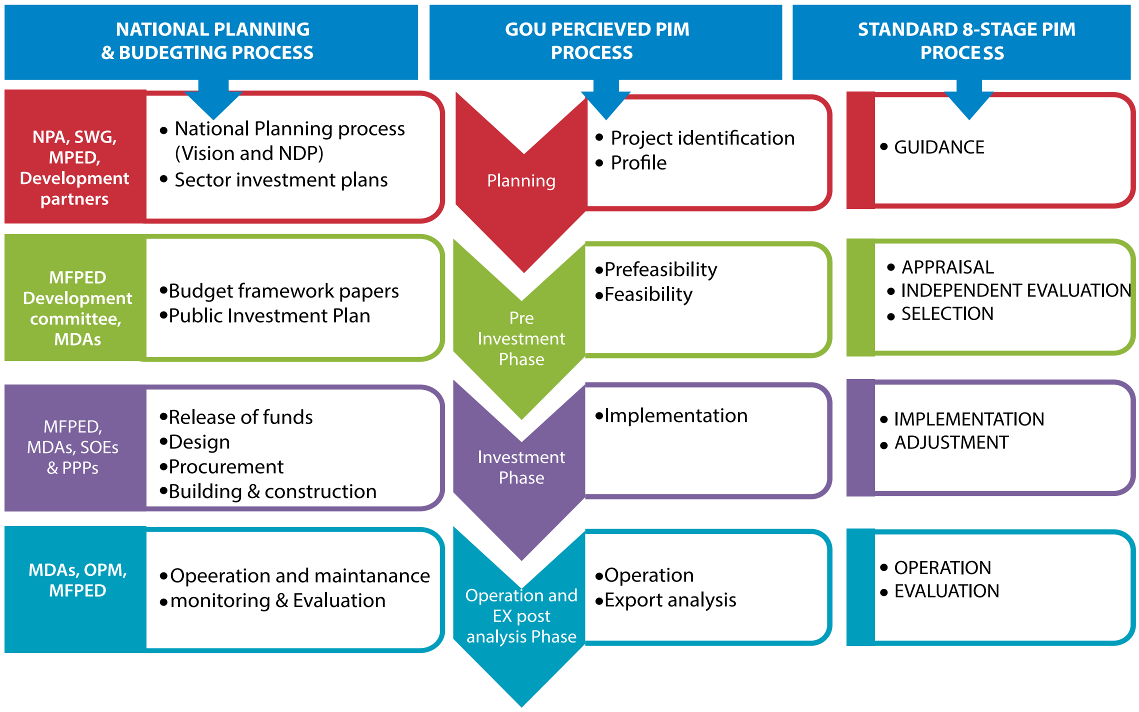
MDAs and local governments are responsible for activities related to implementation of a project in the investment phase. Depending on the modalities of execution, some or all of these responsibilities may be delegated to and/or shared with the private sector. Funding for the implementation of a project is incorporated into the Sector Budget Framework Paper (SBFP) and eventually into the annual budget. Once the funds allocated to the approved projects have been released to the MDAs, procurement and implementation processes are effected by MDAs responsible for the construction and operation of the project. In Uganda's case, this phase sometimes also includes the design of the project. In addition, the Ministry of Finance sometimes still has to make decisions related to which of the bankable projects within the PIP are to be funded and what the source of funding for these projects will be. The sources of funding could include the fiscal budget, as is traditionally the case, or other alternatives, such as PPPs.

Typically, this is the phase in which the vast majority of budgetary resources are utilized. In this regard, the Ministry of Finance ensures that allocated funds are released effectively during the budget year to ensure efficient implementation of the capital investment budget. The Ministry of Finance monitors the disbursement of allocated funds and can also provide incentives or implement penalties to ensure that there are no unused resources remaining at the end of the fiscal year. At the end of this phase, the project is commissioned and handed over. This process involves performance tests, hand-over, close down, or decommissioning and disposal.

Uganda has an elaborate procurement process, underpinned by the Public Procurement and Disposal of Public Assets Act of 1996 and as subsequently amended. The process is supervised by a semi-autonomous authority, the Public Procurement and Disposal of Public Assets (PPDA) Authority. All public projects are supposed to be handled by the Contracts Committee, which is chaired by the Permanent Secretary of the Ministry of Finance. This committee provides oversight over the entire procurement process, which starts with the implementing agency sending a statement of requirements to the PPDA. Ideally, the statement includes all information pertaining to the procurement requirements for the project, including the technical specifications of the project, the terms of reference and any other supporting information from the user department. It is this information that the Contracts Committee assesses in order to guide the agency on the most appropriate method of procurement to be used. It is then that the PPDA then, with support from the implementing agency, processes the contract by preparing the bidding document, issues solicitation documents, receives bids, nominates evaluation team, recommends award and prepares contracts for submission to Solicitor General for clearance. After the contract has been signed, it is handed over to the implementing agency for contract management. The contract manager is required to provide regular reports to PPDA on performance of the supplier/contractor or consultant, and to advise when an amendment to the contract is required. The user department is responsible for providing all the technical input throughout the procurement cycle.

Overall, Uganda's PIM system is intertwined with a number of other public processes, including planning, budgetary, procurement, and monitoring and evaluation. The institutions and processes that currently constitute Uganda's PIM closely match the country's planning and budgetary system (see Figure 23). The question is how or whether these different processes are coordinated to effectively and efficiently implement the projects. The aim is not just to align processes and institutions to design and select projects for financing by public resources, but to ensure that existing technical and administrative capacities are sufficient to implement and operate the project.

Figure 23: Uganda's PIM System closely follows the budget process



Source: Compiled from "Strengthening Public Investment Management in Uganda: Diagnostic and General Recommendations", 2015.

4.3.1 GREAT IDEAS AND PLANS UNDERMINED BY WEAK APPRAISALS AND POLITICAL CONSIDERATIONS

Uganda's current processes for identification of projects and for ensuring alignment with national priorities contain many features that characterize good practice PIM systems. The first phase of the cycle is identifying potential public sector projects, which is mandated by the NDP. The NDP applies both a bottom-up approach to capture sectoral priorities and a top-down approach that expresses national aspirations as outlined in the Vision 2040. The purpose of the processes implemented at this stage is to determine the basic desirability of a proposed project and to identify high-priority projects that are the mandated responsibility of the public sector. The NDP is required to inform and be informed by sector investment plans, defined as the detailed statement of performance, issues and opportunities, development objectives, policies and strategies that support development in specific sectors. These provide a framework, which should be aligned with the NDP, for the identification of initiatives and projects for government agencies, the private sector, civil society, development partners and academia.

Second, each sector is required to prepare and submit sectoral budget framework papers according to the budget guidelines developed by the Ministry of Finance. This is intended to facilitate the provision of public resources to fund proposed initiatives in the following fiscal year. The SBFP defines a budget strategy for a specific sector, specifying the sector's objectives and performance targets for the financial year. It defines sectoral objectives, performance targets, planned actions and outputs, strategies to improve performance and draft work plans with outputs for spending agencies. The Ministry of Finance, Planning and Economic Development (MFPED) consolidates the SBFPs from the 16 sectors and prepares the National Budget Framework Paper (NBFP), which is presented to the Parliament no later than March 31 each year. The NBFP is the Government's overall budget strategy document and is intended to link the Government's overall policies, as identified under the National Development Plan, with the annual budget. This document describes macroeconomic policy and plans; overall fiscal strategies, including revenue projections; the overall medium-term resource envelope; and priority interventions, as identified in the proposed sectoral expenditure plans.

Third, the MFPED implements a number of processes associated with the independent review stage of the public investment management system. The preparation of studies, including the profile study, the pre-feasibility and feasibility studies, and the identification, preparation and evaluation of the project, begins with the MDA submitting the proposal to the SWG to ensure it is consistent with sector investment priorities; to avoid duplication; and to develop synergies. The approved proposal is then submitted to MFPED, where the Development Committee appraises the project on the basis of established guidelines to determine the degree to which it is aligned with national priorities and to which it will generate value for money and thereby determining its suitability for inclusion in the public investment plan (PIP). The PIP is intended to serve as a central data base covering all active public investments in the development budget. The projects that meet the minimum requirements for inclusion in the PIP are also considered suitable for funding through the budget. In recent years, the composition of the Development Committee has been expanded to include the NPA and Office of the Prime Minister (OPM), to strengthen the linkage between the appraisal and planning processes and the monitoring and evaluation functions of the Government.

Fourth, the Parliament exercises its oversight role to ensure that proposed projects are consistent with national priorities and scrutinizes detailed expenditures. This process represents another layer of scrutiny to ensure that funded initiatives will facilitate the achievement of development objectives.

Meanwhile, despite the positive aspects of the process, Uganda's pre-investment phase is still affected by significant weaknesses, with severe consequences for the implementation process. First, at the project identification stage, many projects are introduced into the cycle without any process to determine whether they are aligned with national priorities or to appraise their effectiveness (see Box 7). In part, this is because projects identified under NDP are very broadly defined. This creates space for unwarranted interventions from various stakeholders during the implementation process. In addition, with the national planning process occurring only every five years, there is no systematic framework for continuously collecting project ideas and concepts in between the planning cycle. Ideally such new concepts should be submitted to the responsible MDAs for appraisal to ensure their economic viability and value to the economy, and for possible inclusion in the sector and national plans. Furthermore, it would appear that the SWGs do not perform their responsibilities in terms of scrutinizing the project proposals, due to weak capacities or as a result of political pressures. As a result, the public investment plan includes a number of projects that are poorly aligned with national priorities, including many that are also poorly planned. Other challenges are the low level of ownership by implementing agencies and the inclusion of projects not clearly aligned with normal planning process. Therefore, while the PIP plays a positive role in centralizing data related to government projects, it is not an optimally effective tool because of the poor quality of many proposed projects; because it includes projects of a recurrent nature; and because it does not provide a pipeline of ready-to-go projects (see Box 8). Moreover, given that only projects with identified sources of funding are included in the PIP, a number of potentially beneficial projects are excluded. For the purpose of this Update, it was not possible to estimate how many projects in the PIP had been subjected to an economic assessment, due to the poor quality of information.

Uganda Parliament, where most government policies are sanctioned

the preparation of studies, identification and evaluation of a project, begins with the MDA submitting the proposal to the SWG to ensure it is consistent with sector investment priorities

Box 7: Lessons of project ideas differ and projects enter budget process in variant form

1. Private sponsors, enterprises or development partners: In this case, a private partner usually proposes a specific investment project to an MDA. In most cases, this project involves a productive sector (for instance, infrastructure) rather than a social service sector (health or education). In general, these projects come with a proposal for funding by the private partner.
2. National needs identified by high level authorities: This category entails the identification of projects by executive representatives of public institutions, such as the ministries and the president's office. It includes local government agencies that have a direct contact with the area and its people. It also includes regional investment projects involving the participation of other countries, such as energy and pipelines projects.
3. National needs identified by MDAs: In this case, a technical team from MDAs identifies projects conceived as a possible solution to a specific problem and then In addition, it may include regional investment projects that might involve the participation of other countries, such as energy and pipeline projects.
4. Complement projects: This category includes projects identified by sectors that require a project to be implemented to support another, bigger project in order to optimize benefits. An example of this case is a road project (complement project) which is needed to provide connectivity to a mine project (principal

In addition to limited capacities and resource constraints, the most important weakness in Uganda's PIM system is the lack of a comprehensive framework that can be adopted across sectors to facilitate project proposal assessments. This weakens the requirement set by the Development Committee that the sectors undertake detailed pre-feasibility and feasibility studies to guide decision-making processes. Without a solid legal mandate, the Development Committee is not currently empowered to operate effectively. At present, the Development Committee derives its authority from the administrative powers of the Permanent Secretary of the Ministry of Finance, imputed from the broader aspects of the PFM Act 2015. Thus, its authority is constrained, which potentially undermines its sustainability. Without a clear, legally mandated framework, the overlapping mandates create additional confusion. Under NDP II, it has been found that there is often duplication between the roles of the NPA and the Development Committee in the identification of tasks such as project appraisal and analysis. Another source of weakness emanates from the inconsistencies between the development partner requirements and the country's PIM processes for investment projects funded by development partners.

Construction of the Malaba one border post

the key element of an independent review provides a basis for checking any subjectivity or optimism bias that may be reflected through underestimated costs or overestimated benefits

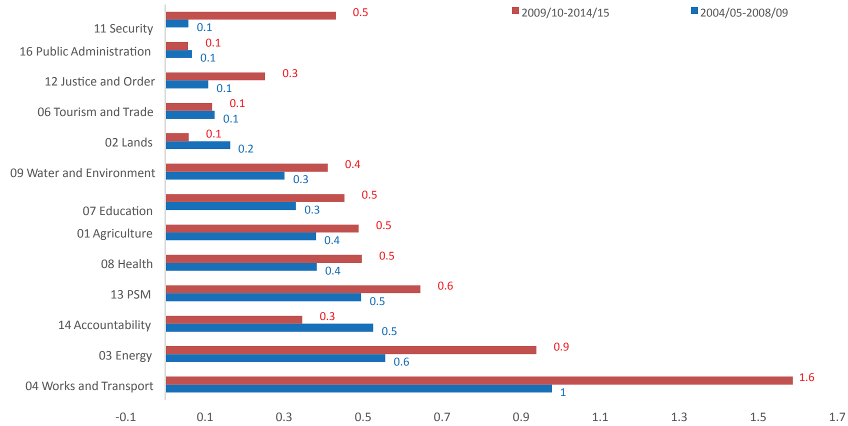
Box 8: Public Investment Plan: It should do what its name says! form

As in many other countries, the Government of Uganda maintains a public investment plan (PIP), which was first established in 1994/95 to support the management of public investments. The PIP replaced the Rehabilitation and Development Plan (RDP) Volume 11, and is intended to serv P captured only priority projects, with these being mainly donor funded projects. It is estimated that as of FY 2008/09, the PIP covered only about 30 percent of all public investments, with most of these involving counterpart funding. Later, the PIP was restructured with the intention of including all projects and programs receiving support from the development budget. However, not all expenditure included in the development budget was utilized for investment, partly because not all budgeted development expenditure is converted on a one-for-one basis into additional public investment. In addition, the development budget included some expenditure items of a recurrent (i.e. consumable) nature, with these items being included in the development budget because they were associated with specific projects. This was mainly the case for donor funded projects. The PIP also included programs that were judged to have a long term growth impact, even if their capital expenditure component was low or non-existent (e.g. National Agricultural Advisory Services). By FY 2008/9, the PIP covered 295 projects. Of these projects, 58 percent had a defined closing date, with the average lifespan of these projects being six years. The remainder had no defined closing date, suggesting they were being funded and implemented in perpetuity. In fact, the actual investment component of the PIP was still quite small, estimated at about 40 percent of all the projects.

Over the last five years, the PIP has undergone a number of refinements, including the development of clear guidelines related to the inclusion of projects. These guidelines mandate that an included project must involve a capital expenditure component of at least 70 percent for new projects and at least 50 percent for existing projects, with this provision intended to distinguish capital investments from recurrent expenditure. The assessment of projects is intended to be an ongoing process, with an annual review to exclude projects that do not conform to the requirements. As a result, while the total number of projects in the PIP increased to 410 by FY 2014/15, the investment component of the PIP had also increased to 60 percent. To improve accountability, the PIP was revised so that expenditures were tagged to vote functions. In line with the overall fiscal framework and the NDP, the bulk of investments are in infrastructure sectors.

However, the PIP still focuses on the affordability of projects, since projects that fit within the Medium Term Expenditure Framework (MTEF) ceiling are included. While this ensures that resources are not wasted on projects for which there are no MTEF allocation, it undermines the development of a culture of planning and preparing bankable projects that can be funded once resources become available. Secondly, because the process of preparing projects starts after they have been included in the budget, no feasibility and/or pre-appraisal studies are conducted for many of the projects included in the PIP. This exacerbates the low levels of budget execution and other weaknesses in the management of public investments. Thirdly, government and externally funded projects are still managed under separate data systems, leading to difficulties in timely reconciliation of the full PIP database, as well as variant quality standards for the two sets of data.

Therefore, while the PIP currently provides the most comprehensive database of public sector investment projects, it still has a long way to go before it becomes an effective tool for public investment management. Efforts ae underway to include additional project information and data to develop the list of projects that have been appraised and are bankable but that do not have allocated financing, and to subsequently introduce an Integrated Bank of Projects (IBP) will be very useful. This will furnish the PIP with information and have a priority list of future projects to be implemented. In addition the IBP will assist in tracking implementation of the project from commencement to closure, easing multi-year budgeting, cost tracking, and project adjustments monitoring, among others. So far, a manual has been development and some capacity building for preparation and appraisal of projects initiated.



4.3.2 IMPLEMENTATION CHALLENGES RESULT IN DELAYS, COST OVERRUNS AND PERPETUAL PROJECTS

In Uganda, most projects enter the investment phase before they are ready for implementation. These projects require additional time for preparation through processes such as planning and drawing designs, with these processes being conducted only after resources have been allocated or when disbursements are ready to begin. As discussed earlier, rather than start off with projects that are ready to execute, the investment phase in Uganda begins with the preparation of a full feasibility study and the drawing of designs, following which procurement, fabrication, construction, and other processes commence. Thus, Uganda's investment phase starts off on a default of a longer project life span than would be the case under a more efficient system. Within the current PIP, projects have an average life span of five years, although many of them have remained in the PIP for more than 10 years. The Karuma dam project has been budgeted to start implementation every year since 2012, but significant progress in construction was only visible starting in FY 2014/15. In some instances, implementing agencies face challenges related to inadequate funding, particularly counterpart funding for externally funded projects, acquisition of right of way, and poor quality of designs. These inevitably lead to a failure to deliver projects on time and on budget. This was in fact the experience of the Transport Corridor Project, which the Government conceived and budgeted for in FY 2008/09, but with construction only starting three years after.

The quality of projects included in the investment plan is often poor. As discussed above, because of non-adherence to the established PIM system, the quality of the projects in the PIP is generally poor. This results from poor appraisals in the pre-investment stage and the bypassing of established procedures, and also from delays that are so protracted that designs and feasibility studies become outdated.

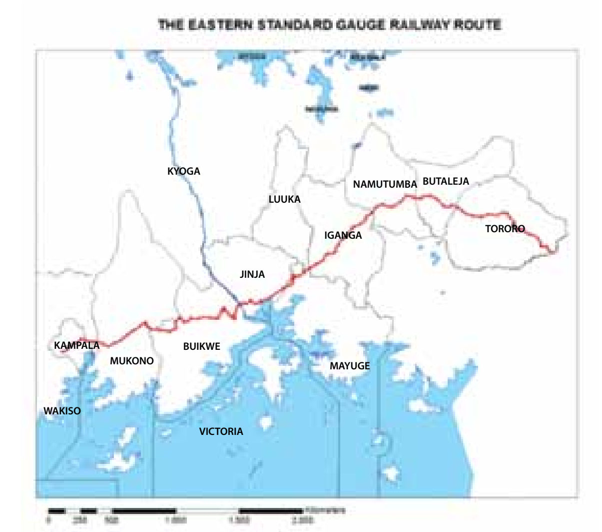
Another significant issue is the frequency of budget overruns and delays in procurement and implementation processes. Weaknesses in the project design also sometimes result into redesigning of plans or even constructing completely new works during the course of construction, resulting in the need for the allocation of additional financial resources and delays to delivery. Institutions responsible for project execution state that many construction companies involved in implementation do not have the necessary technical and financial capacities, which leads to additional implementation challenges. Due to issues related to the quality of data within the PIP, it is not possible to estimate the overall completion rate, or the extent of cost overruns and delays with public projects. Nonetheless, evidence from a sample of World Bank funded projects currently active or completed over the past 10 years confirm that significant challenges remain in project execution. World Bank projects accounts for a small proportion of (about 0.1 percent) of the approximately US $ 1.8 trillion stock of Government active infrastructure projects. However, the level of performance has been declining over the past three years to the point that out of a project portfolio of a value of US$ 2.3 billion, less than 6 percent of these funds has been disbursed. Almost all the reasons explaining the low performance relate to the ineffective PIM systems. According to this project profile, project life extends to approximately seven years, which is much longer than the average for sub-Saharan Africa. Cost overruns are frequent, partly resulting from delays to project implementation. In some cases, cost overruns amount to a value of up to 50 percent of the original cost of the projects.

National semi arid resources research institute, Serere

to ensure that investments generate better value for money, a higher level of scrutiny should be applied to ensure that these investments actually improve public welfare

Box 9: Lack of communication and coordination of public investments costly to the economy

In August 2016, Uganda expects to commence construction of its part of the more that 1300 km of East Africa's first standard gauge railway (SGR) linking Kampala to Mombasa. Work on the Kenya side began in 2013. In Uganda, the contract for the stretch covering at least 40 km between Malaba and Kampala has been awarded to China Habour Engineering Company. This portion of th SGR is expected to be completed by December 2020.



Districts traversed by SGR Eastern Route

The SGR project has broad benefits, key among which is to reduce the cost and time taken for goods to be transported between Kampala and Mombasa. This development should also enhance the potential for Uganda to leverage its unique geographical location to become a regional transport and logistics hub.

However, while the SGR project is generally viewed positively, government communication with the transport and logistics industry and coordination across the industry remains insufficient. Key stakeholders like the Inland Container Depot (ICD) at Mukono, managed by Rift Valley Railways (RVR), have limited information with respect to the SGR project, with implications that it may not sufficiently benefit from it. If the ICD Mukono is not connected to the SGR, it may become uncompetitive with the potential effect of future investment in the facility declining. This scenario cannot come to reality as is confirmed by information from the Ministry of Works and Transport. However, lack of information to key stakeholders can result in sub-optimal investment decisions. In this scenario, the container depot could still remain uncompetitive, even if it is connected to SGR, if the investors continue to base decisions on misinformation.

Source: World Bank

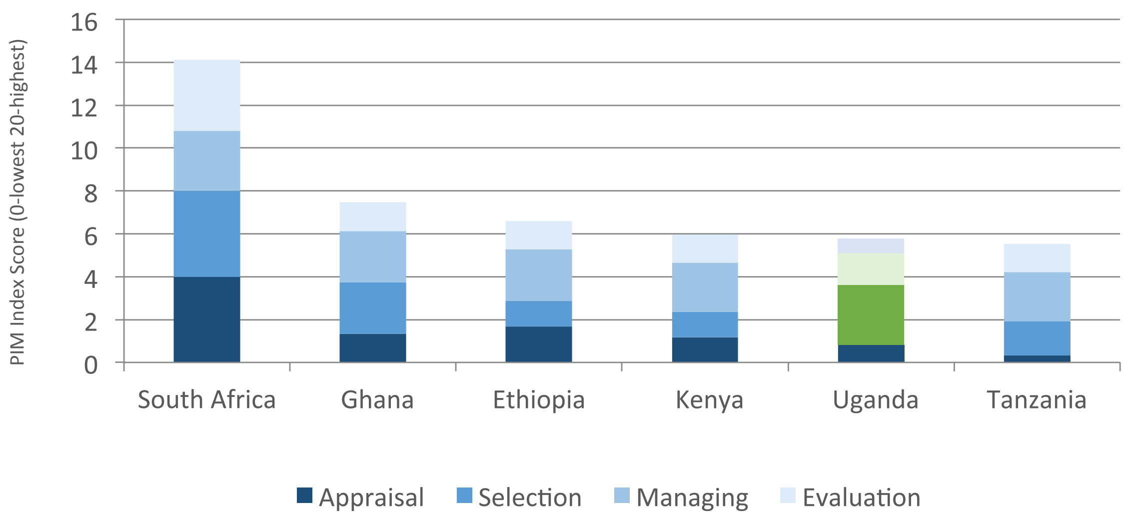
In the monitoring and ex post analysis phase, some institutions have specific units and systems to monitor progress during execution. These institutions, which exist both within the Ministry of Finance and within other line ministries, evaluate budget execution, overruns and compliance with schedules, among other matters. The operation, maintenance and ex post evaluation of the performance of the public asset is usually the responsibility of the project sponsoring agency or in other designated entity. However, a number of public sector institutions are also responsible for the evaluation of the execution process. These institutions focus on the overall progress of investment projects implemented by the Government, with examples of such institutions including OPM and NPA.

Systems for the monitoring and evaluation of service delivery quality during project operation are weak. This issue is exacerbated by a poor maintenance culture in the management of public assets, resulting from the inefficient use of available resources, capacity constraints and a failure to implement ex post evaluations of completed projects. Uganda's budget allocations to operations and maintenance have increased from about 3.4 percent of the total budget in the period from FY 2004/05 to FY 2008/09 to 8.4 percent over the past five years. However, this level of spending on operations and maintenance is still far lower than the level of 20 percent suggested by global good practice, and hence leaves many agencies with inadequate resources capacities to maintain assets.

Overall, existing processes and programs are marred by weaknesses that undermine project management and result in failures to achieve good value for money. The current public investment program involves the ad hoc identification of projects, with an analysis of projects conducted only after they have been earmarked for financing. There are insufficient mechanisms to ensure the efficient management of implementation of the construction of assets, let alone the operation and maintenance of these assets. The current process results in significant economic and social costs.

Inefficiencies resulting from poor inter-agency coordination lead to delays in evaluating projects and poor project selection, which together result in a failure to produce productive public capital. According to the IMF PIMA index, Uganda is ranked lowest among its peers in the area of project appraisal selection and ex post evaluation. While it is ranked highly for its selection of projects, the score for the management of these projects is also lower than its peers. As a result, the overall score for public investment management is worse than that for all other countries, except Tanzania (see Figure 24).

Figure 24: Uganda's largest challenge lie in appraisal, managing and evaluation of projects



To ensure that investments generate better value for money, a higher level of scrutiny should be applied to ensure that these investments actually improve public welfare. In addition, the Government should implement measures to ensure that investment projects are managed effectively and completed on schedule; that projects are operated efficiently and sustainably; that there is a process of learning to improve future project selection, implementation, and operation; and that risks are allocated appropriately to ensure efficient and effective implementation of the project, especially the risks between the public and private entities. As Uganda embarks on a road to reform the way public investments are managed, it should draw from global good practice while taking stock of its own capacities for implementation.

ACCORDING TO THE IMF PIMA INDEX, UGANDA IS RANKED LOWEST AMONG ITS PEERS IN THE AREA OF PROJECT APPRAISAL SELECTION AND EX POST EVALUATION.

5. HOW CAN UGANDA MAXIMIZE VALUE FROM ITS PUBLIC INVESTMENTS?

To convert its large investment program into productive assets, Uganda needs to improve its public investment management system. The Government has already initiated key reforms in this area, but given the complexity, particularly related to governance and political economy issues, this requires sustained efforts and commitment. The Government may therefore adopt a systematic approach to streamline and strengthen institutions for managing public investments, including building capacity of Ministries, Departments and Agencies; promote a common understanding of what is required to do through the process, and how it should be done, through clear guidance and standard criteria on key processes; and close gaps in the legal and regulatory framework to clarify and strengthen mandates and incentives.

Building effective public investment systems can be a complex undertaking, given the various institutions, processes and mandates that have to come together to form a system that is able to manage investments efficiently. If any part of it does not function properly, then the entire system can be rendered ineffective. For example, it is not sufficient to build efficient budget allocation systems, if projects being funded cannot be properly appraised to ensure that they meet criteria for economic return. Nor is it useful to build capacities for appraisal when there are no mechanisms to enforce the results of these appraisals, or if procurement challenges will raise costs well above the original estimates from the cost-benefit analysis, sometimes making the project economically unviable.

Perhaps most important to recognize is the fact that implementing changes to the PIM systems can also be affected by political and governance challenges. First, the reform of any public management function requires a protracted commitment and a high level of discipline. For reforms to succeed, the approach adopted should recognize the environment in which the reform will be implemented, including the technical feasibility of the reform, capacities to implement it, and political economy dynamics. Secondly, some parts of the project cycle, especially during the implementation phase, may generate benefits for well-connected interests. Reforms that threaten the status quo can be met with public or covert resistance. Thus, it is vital to make a careful assessment of who will win and who will lose as a result of the reforms and formulate an appropriate strategy to manage vested interests. Third, public projects present opportunities for politicians to engage in pork-barreling, which allows them to claim delivery of benefits for their constituents. Unfortunately, political pressures to locate and build projects to meet these needs are normally limited to seeing these projects commence, as opposed to following them through to completion to deliver economic value to society. Therefore, designing an effective reform strategy needs to ensure that (i) easy to implement, low-cost reforms have been identified and implemented to create a demonstration effect; (ii) timing coincides with periods within the political cycle when political leaders can push for politically challenging reforms; (iii) display a certain level of political realism by providing some visible benefits to political leaders; and (iv) identify champions, even where a reform is widely supported, while strategizing on how more difficult parts of reform can be implemented. These challenges notwithstanding, improving efficiency of public investments can bring considerable benefits to the country. It has been estimated that if Uganda increased spending efficiency in infrastructure, it could use the same amount of resources to generate a rate of growth of GDP over the next 10 years reaching 9.5 percent per annum[17] . This rate of growth is 3 percentage points higher than the forecasted rate of 6.5 percent over this period and can allow the country to reach coveted 'middle income status in much less time that what the current average rates of growth imply.

17. Agenor, P-R., and J-P. Nganou. 2014. "Expenditure Allocation and Economic Growth in Uganda: An OLG Framework." Uganda CEM Background Paper.

5.1 REFORMS TO UGANDA'S PIM SYSTEM: A GREAT START, BUT A CONTINUED EFFORT STILL NEEDED!

Recently, the Government has implemented a number of measures intended to start a reform process that may improve Uganda's PIM system. First, a number of reforms to budgeting and overall public financial management have been initiated through the promulgation of the PFM Act (2015), with these reforms expected to result in improved efficiency to the management of public finances. Second, the Ministry of Finance has embarked on measures to strengthen its gate-keeping function by creating a department in charge of Project Analysis and Public-Private-Partnerships (PAPP) in 2015. This creates a systematic structure with clearly defined mandates to manage the project cycle, and project quality assurance. Among other matters, the PAPP Department is expected to ensure that technical and economic analysis of public investment initiatives at the national and/or regional level is conducted thus acting as an independent reviewer of the projects. Therefore, it is responsible for analyzing, appraising and recommending or rejecting public investment projects for financing and execution; defining and updating general and sector rules, guidelines, circulars and norms that inform the formulation and appraisal of investment projects; providing technical support to MDAs and local government evaluation teams or planning units; coordinating the provision of nation-wide training on issues of project preparation and project appraisal; providing the secretariat to the Development Committee, with the latter mandated to approve or reject submitted projects for project execution by granting a seal of approval; and undertaking selected monitoring and ex post evaluation for selected key projects. With technical assistance, the unit has developed public investment guidelines and manuals and started building capacity in the area of project appraisal within the Ministry and in other MDAs.[18] Amongst other measures, it has developed a simplified manual for public investment appraisal. This department can indeed champion the strengthening of the overall PIM system, while remaining cautious not to overburden the MFPED with roles that should be undertaken by other agencies along the PIM cycle.

In recent years, there have also been major improvements to the procurement function. Closely following the amendment to the PPDA Act in 2014 March, the PPDA Strategic Plan 2014-2019 was developed, with this plan providing for initiatives to improve the manner in which public procurements are managed. These changes included a new audit tool and a framework that focuses on 15 critical entities to improve the efficiency of procurements. The Government also commenced the e-Government Procurement Strategy, which was launched in 2014. It also opened regional offices in two towns to place procurement services closer to the implementing entities. A Public Procurement Policy is expected to professionalize the procurement cadre and to streamline the framework for high value contracts. This policy is awaiting Cabinet approval.

5.2 MOVING FORWARD WITH REFORMS

In many cases, it is clear what needs to be done to improve Uganda's PIM systems. However, actually implementing these measures will require a strong effort, given the nature of the reforms needed. To achieve a genuine improvement in the efficiency of public investments, a systematic approach to close gaps must address the following three issues: (i) streamlining the institutional arrangements for the management of public investments across the project cycle; (ii) ensuring a shared understanding across institutions regarding what needs to be done and how it should be done. This involves standardizing the information and documentation needed to guide the identification, formulation, preparation, appraisal, investment decision, operation, monitoring and evaluation of projects across all implementing agencies; and (iii) determining where gaps in the legal and regulatory environment exist and how they should be closed to strengthen mandates and the incentive structures. The actions already implemented by the Government are a significant step forward in this regard. The establishment on a department for the appraisal and analysis of projects and measures to build capacity in project preparation and appraisal for the PAPP department and other selected MDAs, are certainly steps in the right direction. In addition, the formulation of simplified guidelines for the preparation and appraisal of projects to be used by MDAs is a good example for the drafting and formulation of other documentation that guides the PIM process. Meanwhile it is necessary to maintain momentum to address remaining challenges to make a lasting positive impact on the way public investments are managed in Uganda (see Table 3). If there is no follow through on these reforms, then issues resulting from inadequate oversight, poor projects, delayed implementation, cost overruns, neglected assets, and corruption, among others; will continue to erode value form Uganda's public investments.

18. Through funding from DfID trust fund, the World Bank provided a technical assistance to the Government of Uganda to support it to strengthen its PIM system.

Table 3: Reforms in public investment management: Addressing key gaps

PRINCIPLE	SOME REMAINING CHALLENGES IDENTIFIED	CONSEQUENCE
Institutional streamlining and strengthening along the project cycle	**Guidance:** Some projects included in the NDP are too broad and others not fully owned by sector MDAs. Some projects from sectors are weak and/or not consistent with national priorities. No process exists to ensure that new project ideas and proposals are taken through the same screening process as those in NDP to ensure consistency with the national priorities.	***Projects not aligned with national priorities***
	Appraisal: Overlapping mandates, weak capacities and the lack of coordination between the different institutions lead to poor quality projects, sometimes without pre-feasibility or feasibility studies. They also lead to major differences between donor- and government-funded projects. The NDP2 also indicates some tasks related to project appraisal and selection, which clearly overlaps the work being done in MFPED. In addition, Uganda is yet to develop a database of ready-to-go projects and is yet to decide on the model for management of PPPs.	***Poor quality projects*** ***Delays in implementation***
	Independent review: The new unit established within the MFPED to appraise and select projects for financing may in some cases serve as the independent reviewer. Lack of clarity on mandate, thresholds, and other aspects, for which projects should be subjected to independent reviews leaves different projects being subjected to different standards.	***Poor quality projects***
	Implementation: Projects are implemented by a range of MDAs with varying levels of capacity. In addition, poor project preparation, delays in the disbursement of resources, acquisition of right of way, social safeguards, and procurement, among others, lead to chronic under-execution and to cost and time overruns.	***Cost and time overruns***
	Operation and ex post evaluation: The systems for monitoring execution of projects are weak and not coordinated across different MDAs. Even after they are completed, monitoring and evaluation of value created by public investments is non-existent because Uganda does not undertake a systematic follow-up on project completion reports; it does not maintain an asset management strategy; and it does not carry out impact assessment reports. This is further complicated by the poor maintenance culture.	***No tracking of performance*** ***Inappropriate erosion of public assets*** ***Increase in cost of capital***
Document standardization	Enforcement and gate-keeping role has to be strengthened for these frameworks to be binding. In addition to the simplified manuals that have been created, other critical documents that should be prepared include: (i) Standard criteria for formulating project performance indicators, with this criteria also emphasizing the strategic fit with national priorities; (ii) Standard national parameters to use in project assessment (e.g. shadow prices, unit costs, discount rate, among others); (iii) a comprehensive framework for PPPs, SOEs and local governments; (iv) a framework for the monitoring and evaluation of all public capital assets.	***Poor quality projects*** ***High cost of projects***
Legal and Regulatory Framework	There is no explicit legal provision for a PIM framework. Clarity of mandates of institutions would require legal provisions to remove overlaps as is the case for the appraisal function within the PAPP department, but claimed by NPA.	***Political interference*** ***Poor quality project*** ***Projects not consistent with national priorities***

The strategy to reform Uganda's PIM system should prioritize addressing the most binding constraints preventing good investment. With the current poor execution of projects in Uganda, there is a temptation to apportion the problem to be solely due to the way projects are implemented and to prioritize reforms related to project execution. However, as the previous sections have made clear, most delays in the execution of projects result from the poor quality-at-entry of these projects. Moreover, as the contribution of external donors to financing of projects declines, the Government puts greater emphasis on non-concessional funding, and with the expectation that oil revenues will eventually finance a large component of projects, it becomes vitally important to improve capacities to manage investments. Building capacity is in the area of the preparation of projects and their appraisal and selection could generate the most rapid gains. Thus, the proposed action plan consists of some actions that should be implemented as soon as possible, while other actions can be implemented over the next five year period. A PIM reform action plan that has been carefully calibrated along the three dimension of strengthening institutions, document standardization, and closing the gaps within the legal and regulatory framework is summarized in Figure 25. It recommends that the reform could move as follows:

I. Immediate actions to progress PIM reform

The Government can pursue the following six actions immediately:

1. **Formalize and strengthen independent review of new project proposals** *(Action A1 in the PIM Reform Action Plan below)*

Currently, the role of independent review of project proposals is partially being handled by the PAPP Department within the Ministry of Finance, Planning and Economic Development. This department is new and would need to be nurtured and groomed to fully perform the role of an independent reviewer. This would strengthen the role of the Ministry as the gate-keeper with respect to spending of public resources to generate value. To fulfill its mandates, the PAPP department must prepare clear procedures and guidelines to define how the economic analysis of projects should be conducted, with these guidelines defining the norms, standards and rules to be followed. The unit must also determine how it will be able to provide support to other MDAs and local governments, including through training, and what criteria it will use to approve or reject projects.

2. **Build the capacities of Ministries, Departments and Agencies (MDAs) and other implementing agencies, particularly in the area of project preparation, appraisal, approval and monitoring phases** *(Action A2 in the PIM Reform Action Plan)*

In the short term, training should be focussed on capacitating a core group of technicians across the different MDAs involved in the preparation and appraisal of projects within their own agencies. Building and sustaining the range of skills required for effective PIM system can be accelerated through the establishment of linkages with higher education centres. Susequently, building capacities at all levels of the Government, would require developing training programs targetting officials and staff at the basic, intermediate and advanced levels for all agencies, particularly those involved in preparing and implementing projects.

3. **Document and implement good practice operational processes, starting with project preparation and appraisal** *(Action B1 in the PIM Reform Action Plan)*

This action relates to standardizing the information and documentation that guide the PIMs. This should focus on developing manuals that support the different processes and ensure that they are implemented. To improve the capital investment project design, appraisal and selection processes, the procedures for preparing and presenting projects for final appraisal and approval must be streamlined. To achieve this, guidelines and manuals must be prepared for MDAs and other implementing agencies to ensure that they implement the appropriate measures to achieve the meaningful economic evaluation of projects.

The integrated project appraisal can be a key technical tool to facilitate decision-making processes and to ensure the efficient allocation of public resources. To ensure that project appraisals fulfil these functions, a range of project appraisal methodologies need to be developed. This will involve the development of templates and applied case studies, with priority given to sectors and project types that have the highest budgetary impact. The process of developing these methodologies should involve periodic training activites for a range of different types of users. There is a need to develop capacities to use the various methods of analysis for all projects, incluidng those executed in cooperation with the private sector through PPP arrangements.

A key component of this exercise will be to establish a set of standard national parameters, including shadow prices, unit costs, and the discount rate, as well as standard criteria for project performance indicators, aimed at ensuring that projects are aligned with national strategies priorities. The MFPED has already begun to prepare a number of such manuals. However, it is also necessary to create incentives to ensure the compliance of all parties involved, including the MDAs, hired consultants and donor agencies. To achieve this, project profiling criteria should include qualitative criteria based on strategic priorities and linkages; a mapping with expected outcomes; a determination of the impact in terms of the achievement of final objectives; and a prioritization of projects in accordance with qualitative and quantitative criteria that stresses the achievement of efficiency and cost effectiveness in the implementation of the projects.

Furthermore, the standard framework for the management of PPPs should be documented, as should the framework for the management of projects by SOEs and local governments.

4. **Create a technical fund to facilitate feasibility studies during the pre-investment stage** *(Action B2 in the PIM Reform Action Plan)*

This is a prerequisite for ensuring that agencies can actually undertake the required feasibility studies. Similar modalities could be adopted for both GOU and externally funded projects to ensure projects are properly prepared by the MDAs before they are submitted for consideration in the medium term fiscal framework.

5. **Establish a standard framework for the monitoring and evaluation of all public capital investment projects under implementation** (Action B3 in the PIM Reform Action Plan)

While MDAs currently undertake this function to some extent, and monitoring and evaluation is being done both by the MoFPED and Office of the Prime Minister, there needs to be a single entity and standard framework that can ease tracking and ensure remedial actions. The immediate step under this action could be to re-assess the existing portfolio of projects already under implementation and take action where financial and technical risks are highest.

6. **Formulate a policy framework for PIMS** *(Action C1 in the PIM Reform Action Plan below)*

This will create the background for overall understanding of the PIM system across the various institutions of government, including the executive, parliament and the judiciary, and will thereafter be the basis for legal and regulatory changes for its implementation.

II. Medium term actions to gradually reform the PIM process

As previous sections have made clear, it will not be possible to implement comprehensive reforms to Uganda's PIM system through a single action. Rather, it will involve an ongoing process in which the most binding constraints are addressed first, with later actions intended to build and refine upon earlier achievements. In the medium term, Government should consider implementing further improvements in efficiency and effectiveness in PIM. Four actions to achieve this include:

1. **Clarify roles, mandates and responsibilities of various entities within the PIM process** *(Action A3 in the PIM Reform Action Plan below).*

To support the proposed changes, it will be necessary to determine how the new paradigm for the management of public investments can fit into the Government's existing structure. With PIM system decentralized to different entities, each of which has specific roles to play within the project cycle, it will be critical to re-evaluate the different entities to remove redundant, un-coordinated, overlapping responsibilities, which leads to wastage and inefficiency. The outcome should be a mapping and re-engineering of the PIM processes to support the better implementation of projects.

2. **Develop an integrated bank of projects (IBP), to constitute a central database and depository for public projects, including pipeline projects, with clear criteria and a systematic approach for their inclusion** *(Action A4 in the PIM Reform Action Plan below)*

Such a data bank directly corresponds to the function of improving the quality-at-entry and having ready to go projects for implementation. It should contain information related to beneficiaries, sector statistics, technical parameters, demographics, information on poverty, social indicators, and other matters relevant to project formulation. In order to manage the IBP effectively, it will be necessary to build focussed systems capacity in technical (such as software management, data collection for project formulation at sector level) and in non-technical matters (such as the interpretation of information from the IBP to ensure it is used efficiently and appreciation of usefulness of the process to PIMS.

Therefore, development of the the IBP will involve the development of software components structured around four sub-systems that regulate the entire process of public investments: (i) the identification (technical economical analysis) sub-system; (ii) the pre-investment (capital budget formulation) sub-system; (iii) the implemention (budget execution) sub-system; and (iv) ex post evaluation sub-system. As an integral part of the IBP, a data collection module should be developed to support project formulation at the sector level. The purpose of this module should be to collate information that improves project formulation at the sector level.

Capacity building should also involve training of trainers to facilitate the rapid and effective transfer of knowledge. In the medium term, selected local universities should be involved in the delivery of these courses, with training sessions open to staff of central and local government agencies.

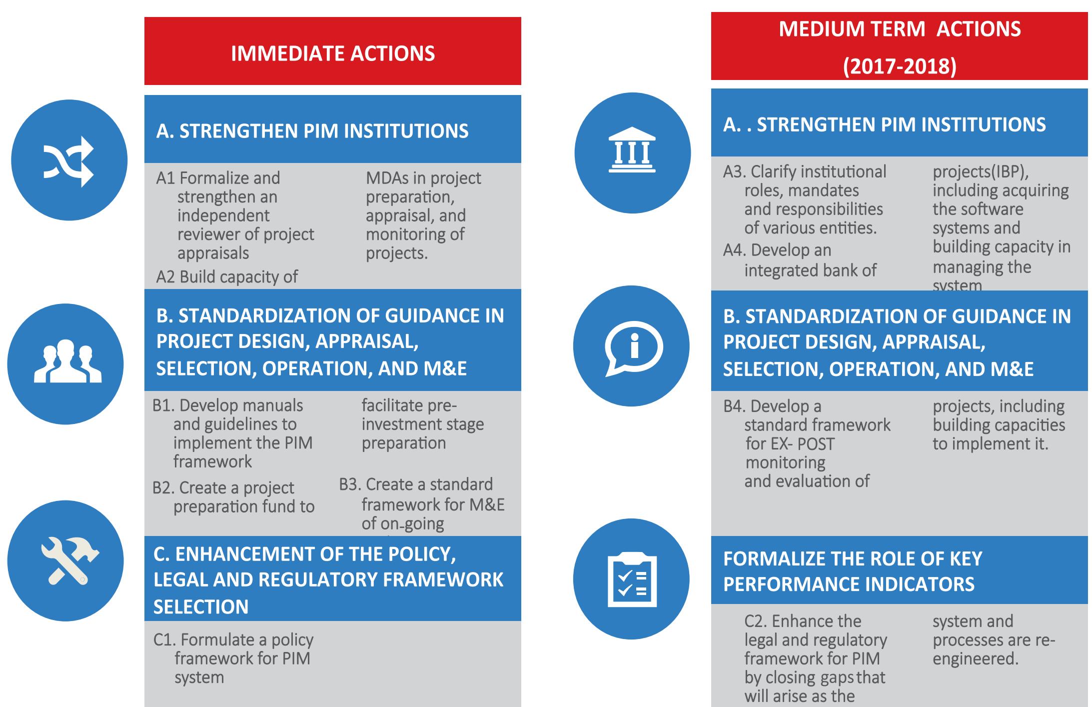
3. **Enhance the legal and regulatory framework required to support PIM** *(Action C1 in the PIM Reform Action Plan below)*

Implementation of the PIM system may expose gaps in the existing legal and regulatory framework that may warrant amendments or the enactment of new laws to strengthen the system. While this update has focused on the need to strengthen institutions and streamline their mandates, it is likely that implementation of the proposed reforms will uncover the need for changes to the legal and regulatory framework. The proposed policy framework suggested in the action 6 among the immediate actions, will provide the background for required legal reforms.

4. **Develop a system for monitoring and ex post project evaluation of projects** *(Action B4 in the PIM Reform Action Plan below)*

Usually, ex post assessment and evaluation is conducted by funding agencies as a required process for compliance with their funding arrangements. In general, particularly for projects using the Government's own funds, the ex post assessment of public investment projects is weak, with basic comparison of project costs, timelines and deliverables against budgets and plans being rarely conducted. For the development of an effective PIM system, a comprehensive system to facilitate the evaluation of past project experiences and to formulate lessons learned to serve as input for future project designs and implementation is vital. To achieve this, it is equally vital to build capacities for managing the system.

Figure 25. The PIM Reform Action Plan



ANNEXES

TABLE A1: KEY MACROECONOMIC INDICATORS

Indicator	Unit measure	2009/10	2010/11	2011/12	2012/13	2013/14	2014/15	2015/16
Population	Millions	31.0	31.9	32.9	33.9	34.9	35.9	37.0
GDP	USD millions	20,181.4	20,262.5	23,237.3	24,624.3	26,953.1	26,898.4	27,392.1
Per capita GDP	USD	578.9	562.4	652.0	670.0	709.0	748.6	740.9
GDP growth	%	5.2	9.7	4.4	3.3	4.5	5.0	5.0
Gross Domestic Savings	as % of GDP	19.7	19.5	17..7	21.7	19.9	21.9	24.3
Gross Investments	as % of GDP	12.5	12.3	28.2	29.5	29.0	31.5	24.3
Inflation (period average)	%	9.4	6.5	23.4	5.8	6.9	2.7	7.7
Exchange Rate (end-year)	UGX/USD	2,283.3	2,623.2	2,484.4	2,630.6	2,599.7	2,918.8	3,102.5
External Sector								
Exports - Goods and Services	Million USD	3,470.1	3,828.6	4,698.3	5,051.5	5,048.6	4,974.3	6,327.6
Imports - Goods and Services	Million USD	-5,757.2	-6,839.9	-7,684.4	-7,579.3	-7,745.4	-7,965.6	9,696.8
Current Account Balance	Million USD	-1,631.0	-1,984.0	-2,219.0	-1,856.0	-2,363.0	-2,430.0	-2,187.0
Balance of Payments (overall balance)	Million USD	235.0	-597.0	759.0	337.0	509.0	-356.0	-239.0
Gross Foreign Reserves	Million USD	2,384.7	2,044.0	2,643.8	2,912.3	3,394.0	2,895.0	2,645.0
External Debt	Million USD	2,343.4	2,904.9	3,067.3	3,742.9	4,339.5	5,103.1	7,058.1
Foreign Direct Investment	Million USD	693.0	719.0	1,244.0	940.0	1,225.0	1,153.0	838.0
Monetary Sector								
Average Deposit Rate	%	2.0	2.1	3.2	3.0	3.1	3.3	3.2
Average Lending Rate	%	20.7	19.8	24.6	24.8	22.1	25.2	23.7
Growth in Money Supply (M3)	%	23.6	25.7	26.1	17.4	15.7	16.6	15.2
Government Finance								
Total Domestic Revenue	as % of GDP	10.5	13.6	11.2	11.4	11.9	13.6	13.9
Tax Revenue	as % of GDP	10.3	10.9	10.1	11.0	11.4	12.8	13.4
Non Tax Revenue	as % of GDP	0.3	0.2	0.4	0.5	0.5	0.6	0.5
Grants	as % of GDP	2.1	1.9	1.9	1.5	1.0	1.2	1.7
Total Expenditure and net lending	as % of GDP	16.7	19.1	15.6	16.5	16.7	19.4	22.1
Recurrent Expenditure	as % of GDP	10.5	12.7	9.4	9.1	9.8	10.3	10.8
Development Expenditure	as % of GDP	6.1	6.1	5.8	6.6	6.9	7.0	8.2
Fiscal Balance (overall)	**as % of GDP**	**-4.0**	**-3.6**	**-2.5**	**-3.6**	**-3.8**	**-4.6**	**-6.4**

	2008/9	2009/10	2010/11	2011/12	2012/13	2013/14	2014/15	2015/16
Monetary Aggregates								
M3 as % of GDP	18.3	15.1	13.4	10.6	10.0	9.4	9.0	7.9
M2 as % of GDP	14.3	11.7	10.4	8.3	7.9	7.5	7.2	6.2
M3 growth rate (%)	25.0	23.6	25.7	26.1	17.4	15.7	16.6	15.2
M2 growth rate (%)	26.3	22.7	22.2	24.3	21.2	17.6	17.9	16.1
Domestic Credit								
Total domestic credit (% of GDP)	9.2	7.8	7.3	5.2	5.2	5.2	4.7	4.2
Private sector credit (% of GDP)	10.4	9.2	7.9	6.3	6.2	5.7	5.4	4.7
Total domestic credit growth (%)	64.1	52.4	50.6	32.7	27.8	19.7	17.8	27.9
Private sector credit growth (%)	31.3	30.7	26.8	21.5	23.9	18.6	17.3	17.0
Interest Rates Structure								
Average TB rate (period average, %)	8.4	5.3	7.6	17.2	10.3	9.3	18.7	14.0
Average lending rate (%)	20.9	20.7	19.8	24.6	24.8	22.1	25.2	23.7
Average deposit rate (%)	2.1	2.0	2.1	3.2	3.0	3.1	3.3	3.2

TABLE A2: GROWTH AND STRUCTURE OF THE ECONOMY

Economic Activity	2009/10	2010/11	2011/12	2012/13	2013/14	2014/15	2015/16
Real GDP Growth Rates (%)	**5.2**	**9.7**	**4.4**	**3.3**	**4.8**	**5.0**	**5.0**
Agriculture	3.2	2.9	1.1	1.8	3.0	3.0	2.8
Industry	7.8	11.4	3.0	4.4	3.9	7.9	7.8
o/w manufacturing	4.5	7.8	2.7	-2.5	2.2	11.0	9.7
o/w construction	12.5	15.0	3.9	10.8	5.3	2.7	5.5
Services	5.9	12.4	3.9	4.1	4.3	5.3	5.5
GDP Shares (% of constant GDP)							
Agriculture	26.2	24.6	23.8	23.5	23.1	22.6	22.1
Industry	**18.1**	**18.4**	**18.2**	**18.4**	**18.2**	**18.7**	**19.2**
o/w manufacturing	8.5	8.4	8.2	7.8	7.6	8.0	8.4
o/w construction	5.8	6.0	6.0	6.5	6.5	6.3	6.4
Services	48.5	49.7	49.9	50.3	50.2	50.2	50.4
Fish and net taxes	7.2	7.3	8.1	7.9	8.7	8.2	0.0
GDP Shares by expenditure type (% of nominal GDP)							
Final Consumption Expenditure	83.2	84.2	86.6	82.0	82.6	86.5	
Households	73.8	74.6	73.9	74.1	74.1	76.9	
Government	**9.4**	**9.6**	**12.7**	**8.0**	**8.5**	**9.6**	
Gross Capital Formation	27	27	28	28	27	24.9	
Gross fixed capital formation	26.6	26.5	28.1	27.4	26.5	24.4	
Charges in inventories	0.4	0.3	0.3	0.4	0.5	0.5	
Net exports	**-10.1**	**-11.0**	**-15.1**	**-10.3**	**-10.1**	**-11.9**	
Gross domestic saving (% of GDP)	12.5	12.3	17.7	21.7	19.9	21.9	24.3
Public	2.9	3.3	2.4	3.1	1.4	1.5	2.3
Private	9.6	9.0	15.3	18.6	18.5	20.4	22.0

TABLE A3: CENTRAL GOVERNMENT FISCAL FRAMEWORK (% OF GDP)

Ushs Billions	**Outturn**	**Outturn**	**Outturn**	**Outturn**	**Outturn**	**Outturn**	**Outturn**	**Approved Budget**	**Projection**	**Budget**
	2008/9	2009/10	2010/11	2011/12	2012/13	2013/14	2014/15	2015/16	2015/16	2016/17
REVENUE & GRANTS	**13.5**	**12.7**	**15.5**	**13.1**	**12.9**	**13.0**	**14.8**	**15.1**	**15.7**	**16.2**
Revenue	11.0	10.5	13.6	11.2	11.4	11.9	13.6	13.6	13.9	14.4
URA Revenue	10.6	10.3	10.9	10.1	11.0	11.4	12.8	12.9	13.4	13.9
Other Non Tax Revenue	0.4	0.3	0.2	0.4	0.5	0.5	0.6	0.6	0.5	0.5
Grants	2.6	2.1	1.9	1.9	1.5	1.0	1.2	1.6	1.7	1.8
Budget Support Grants	1.5	1.1	1.1	1.0	0.3	0.3	0.3	0.3	0.4	0.3
Project Grants	1.0	1.0	0.8	0.9	1.2	0.7	0.9	1.3	1.3	1.5
EXPENDITURE	**15.0**	**16.7**	**19.1**	**15.6**	**16.5**	**16.7**	**19.4**	**22.1**	**22.1**	**22.5**
Recurrent Expenditure	9.5	10.5	12.7	9.4	9.1	9.8	10.3	10.4	10.8	10.4
Wages & Salaries	3.4	3.2	3.5	3.1	3.4	3.5	3.7	3.5	3.6	3.6
Non Wage	4.4	5.4	8.2	5.3	4.3	4.9	5.0	4.9	5.2	4.7
Interest Payments	1.0	0.9	0.9	1.0	1.4	1.4	1.6	2.0	2.0	2.2
Development Expenditure	4.8	6.1	6.1	5.8	6.6	6.9	7.0	8.6	8.2	9.7
Net lending and investment	-0.2	-0.1	-0.1	-0.1	0.6	0.0	1.8	3.0	2.9	1.9
Others	0.8	0.2	0.4	0.5	0.1	0.0	0.3	2.7	0.1	0.4
OVERALL DEFICIT										
Including grants	-1.5	-4.0	-3.6	-2.5	-3.6	-3.8	-4.6	-7.0	-6.4	-6.2
Excluding grants	-4.0	-6.1	-5.5	-4.5	-5.0	-4.8	-5.9	-8.6	-8.1	-8.0
FINANCING	**1.5**	**4.0**	**3.9**	**2.0**	**3.3**	**3.6**	**4.6**	**7.0**	**6.4**	**6.2**
External Financing (net)	1.6	1.9	1.5	2.0	2.2	1.3	1.2	5.0	4.8	5.0
Domestic financing (net)	0.0	1.7	2.3	0.0	1.0	2.3	3.3	2.0	1.6	1.3
memoranda items										
GDP at market prices (Ushs billions)	**34,504**	**40,946**	**47,078**	**59,420**	**63,905**	**68,407**	**74,565**	**83,596**	**84,306**	**92,878**

TABLE A4: BALANCE OF PAYMENTS (PERCENT OF GDP UNLESS OTHERWISE STATED)

Variable	2009/10	2010/11	2011/12	2012/13	2013/14	2014/15	2015/16
Current Account (incl transfers)	**-8.1**	**-9.8**	**-9.5**	**-7.5**	**-8.8**	**-9.2**	**-8.0**
Exports of goods	11.5	11.3	11.4	11.8	10.1	10.3	10.8
o/w coffee	1.3	1.8	1.9	1.7	1.5	1.5	1.4
Imports of goods	-20.4	-23.1	-22.6	-20.4	-18.8	-18.8	-18.6
o/w oil imports	-2.5	-3.4	-4.1	-4.2	-4.0	-3.5	-2.5
Services (net)	-2.1	-3.4	-1.7	-1.7	-1.2	6.6	-2.5
Trade balance	-8.9	-11.8	-11.1	-8.6	-8.7	-8.5	-7.7
Income (net)	-1.7	-1.7	-2.0	-2.2	-2.9	-2.9	-2.5
Current transfers (net)	4.6	7.1	5.3	4.9	4.0	5.0	4.7
Capital and Financial Account	**8.8**	**5.3**	**10.1**	**7.3**	**8.4**	**6.4**	**7.1**
Capital account	1.0	0.8	0.8	1.2	0.8	0.7	1.2
Financial account	7.9	4.5	9.3	6.1	7.6	5.7	5.9
o/w direct investment	3.4	3.5	5.4	3.8	4.5	4.4	3.1
o/w portfolio investment	0.2	0.0	-1.1	0.2	0.0	-0.6	0.0
Overall Balance	1.2	-2.9	3.3	1.4	1.9	-1.3	-0.9
Gross International Reserves (million USD)	2,384.67	2,043.98	2,643.77	2,912.34	3,394.0	2,895.0	2,645.0
Gross international reserves in months of imports	4.4	3.2	4.3	4.5	5.1	4.3	3.6

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