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Uganda: Seventh Review Under the Policy Support Instrument, Request for a New Policy Support Instrument and Cancellation of Current Policy Support Instrument—Staff Report; Staff Supplements; Press Release on the Executive Board Discussion; and Statement by the Executive Director for Uganda.

In the context of the seventh review under the policy support instrument, request for a new policy support instrument and cancellation of current policy support instrument, the following documents have been released and are included in this package:

- The staff report for the Seventh Review Under the Policy Support Instrument, Request for a New Policy Support Instrument and Cancellation of Current Policy Support Instrument, prepared by a staff team of the IMF, following discussions that ended on March 17, 2010, with the officials of Uganda on economic developments and policies. Based on information available at the time of these discussions, the staff report was completed on April 27, 2010. The views expressed in the staff report are those of the staff team and do not necessarily reflect the views of the Executive Board of the IMF.

- Staff supplement of April 27, 2010, updating information on recent developments.

- A Press Release summarizing the views of the Executive Board as expressed during its May 12, 2010 discussion of the staff report that completed the request and/or review.

- A statement by the Executive Director for Uganda.

The documents listed below have been or will be separately released.

Letter of Intent sent to the IMF by the authorities of Uganda*
Memorandum of Economic and Financial Policies by the authorities of Uganda*

*Also included in Staff Report

The policy of publication of staff reports and other documents allows for the deletion of market-sensitive information.

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INTERNATIONAL MONETARY FUND

UGANDA

Seventh Review Under the Policy Support Instrument, Request for a New Policy Support Instrument and Cancellation of Current Policy Support Instrument

Prepared by the African Department
(In consultation with other departments)

Approved by Saul Lizondo and Dominique Desruelle

April 27, 2010

- **Fund relations.** A three-year Policy Support Instrument (PSI) was approved by the Executive Board on December 15, 2006 and extended by one year on December 21, 2009. Outstanding Fund credit amounts to SDR6 million (3.32 percent of quota). The authorities are requesting a new three-year PSI based on the reform agenda articulated in their National Development Plan (NDP)**.**

- **Staff team**. Martine Guerguil (head), Nabil Ben Ltaifa, Stella Kaendera (all AFR), Amina Lahreche (SPR), Jack Grigg (FAD), and Thomas Richardson (Senior Resident Representative).

- **Mission.** Discussions took place in Kampala during March 4–17, 2010. The mission met with the Minister of Finance, Planning and Economic Development, Ms. Bbumba; Bank of Uganda Governor Tumusiime Mutebile; and other senior officials.

- **Outreach activity**. The mission met with the press, representatives of the civil society, members of parliament, members of the business community, and representatives of the donor community.

Contents Page

Appendixes

Executive Summary

Performance under the three-year PSI has remained strong, although progress in structural reforms has been mixed. All assessment criteria for the seventh review have been met and staff recommend completion of the review.

Thanks to prudent macroeconomic policies, the global financial crisis and the regional drought have had a relatively limited impact on Uganda's economy. Activity decelerated recently but it remains robust and is expected to rebound shortly. The policy response to the slowdown has been constrained by unintended shortfalls in budget execution and a weak monetary transmission mechanism, underscoring the centrality of structural reforms for increased policy effectiveness.

Staff support the authorities' request for a new three-year PSI to anchor their near and medium-term policies. The new PSI, will supersede the current PSI, whose cancellation the authorities request. It will be more closely aligned with the budget cycle and its objectives guided by those of the recently-adopted National Development Plan (NDP). It will continue to target investment spending to address Uganda's large infrastructure gap while maintaining low inflation, a flexible exchange rate and a comfortable level of international reserves. In view of prospective declines in aid, financing will rely more on domestic revenue and additional external sources, including on less concessional terms. A reinvigorated structural reform agenda will seek to strengthen fiscal oversight, increase revenue mobilization, and deepen domestic financial markets.

The PSI-supported program will begin to lay the ground for the commercial exploitation of oil and the establishment of the East African Monetary Union (EAMU). Although dates for both are still uncertain and years away, they will raise multiple policy challenges for Uganda. More robust fiscal institutions, a comfortable reserve buffer, and scaled-up infrastructure will strengthen Uganda's competitiveness in preparation for both events.

The medium-term outlook for Uganda remains favorable but risks are on the rise. Growth is expected to rebound to its potential in the coming two years on the heels of a supportive fiscal stance and higher global and regional growth. It remains vulnerable to exogenous shocks (including unexpected shortfalls in aid) as well as election-related uncertainties. But Uganda's longstanding commitment to prudent macroeconomic policies should help mitigate their impact.

I. Background

Uganda has shown firm commitment to prudent macroeconomic policies throughout the PSI-supported program. A strong policy framework has helped make the economy more resilient to exogenous shocks; robust growth, moderate inflation, and a sustainable fiscal and external position have prevailed.

1. **The Ugandan economy performed strongly during the first three years of the PSI even in the face of exogenous shocks and the global financial crisis**. Real GDP growth averaged around 8 percent, and monetary policy was successful in containing inflation after a spike following the rise in world food and fuel prices. The fiscal position remained sound, and debt low. The external position strengthened, with international reserves growing to over $2 billion, or about 5 months of imports.

2. **Nonetheless, uneven progress in structural reforms hampered policy implementation** (Box 1)**.** An important objective of the PSI was to create the fiscal space necessary for scaling up public investment in infrastructure. Tax revenue increased, thanks to notable improvements in tax administration, but capital spending was repeatedly below budget, due to pervasive absorptive and capacity constraints. At the same time, persistent weaknesses in public financial management led to the accumulation of new domestic arrears.

3. **The authorities are requesting a new three-year PSI to support their near and medium-term policies and reinvigorate the structural reform agenda.** The current PSI was approved by the Board on December 14, 2006 and extended by one year in December 2009. The authorities are requesting the cancellation of the current PSI and the approval of a new PSI that will be more closely aligned with the budget cycle. Its objectives dovetail with those of the recently-adopted National Development Plan (NDP).[1] With its longstanding track record of prudent macroeconomic policies, ample foreign exchange reserves, and low external debt, Uganda remains well positioned for continued engagement under the PSI.

4. **The near-term political environment will be dominated by the preparations for the 2011 presidential and legislative elections**. President Yoweri Museveni and his ruling National Resistance Movement (NRM) are widely expected to win a fourth term. However, political and ethnic tensions are flaring up and governance issues are being exacerbated by the prospects of large fiscal revenues once identified oil reserves are brought to commercial use.

[1] See Uganda's *National Development Plan 2010/11-2014/15*, and the *Joint Staff Advisory Note on Uganda's National Development Plan 2010/11-2014/15* (http://www.imf.org).

Box 1. The 2006-2009 PSI—Achievements and Challenges

- **The 2006 PSI aimed to build on the achievements of an impressive decade of macroeconomic consolidation and structural reforms** supported by a series of Fund programs and HIPC and MDRI debt relief. As a "mature stabilizer" with no immediate need for balance of payments support, Uganda easily qualified for a non-financial instrument, and its PSI was one of the first in the Fund.
- **The main objectives of the 2006 PSI were to create the fiscal space to enable a rapid scaling up of public sector investment and encourage private-sector-led growth**. Fiscal policy targeted an increase in revenue and a rationalization of current spending. Monetary policy aimed at keeping inflation at around 5 percent through increased foreign exchange sales from aid inflows to reduce interest rates and encourage private sector credit growth. Second-generation structural reforms were designed to improve tax collection, strengthen public financial management (and in particular control spending arrears), and develop the financial infrastructure to support financial deepening.
- **The program was largely successful in maintaining macroeconomic stability.** Both core and headline inflation declined to 5 percent in 2008, before rising subsequently due to high world food and fuel prices, and later a regional drought. Real GDP growth peaked at 9.5 percent in 2007/08 before declining again to 7 percent the following year. Gross international reserves increased markedly, and as portfolio inflows increased, the shilling appreciated.
- **Lack of progress in public financial management and weak implementation capacity constrained the scaling up of the public investment program**. While reforms in tax administration led to a steady increase in the tax-to-GDP ratio, at least through 2007/08, execution of public investment repeatedly fell short of program targets due to a combination of persistent spending inefficiencies, operational capacity constraints and delays in donor disbursements. Weak expenditure commitment controls led to continued accumulation of arrears, undermining budget execution and efforts to strengthen implementation capacity.
- **Exchange rate appreciation raised new challenges for monetary management**. Following a surge in portfolio inflows beginning in 2007, concerns about real exchange appreciation and loss of competitiveness led to a reduction in forex sales in the monetary policy mix. The BOU maintained a relatively tight monetary stance, allowing exchange rate flexibility to dampen external shocks and using intervention judiciously to smooth exchange rate volatility. In this context, the monetary program was adjusted to allow more flexibility.
- **Observance of program conditionality was mixed.** Adherence to quantitative targets was impressive, with all the quantitative assessment criteria observed in all the six reviews—except for the ceiling on the increase in base money missed in the second review**.** Compliance with the ambitious structural conditionality weakened over the course of the program reflecting technical and political limitations as well as 'reform fatigue'. Overall compliance has declined to 40 percent, compared to 80 percent (with 70 percent on time) under previous Fund programs, and 50 percent in other PSIs. The highest number of missed conditions related to public financial management (PFM), and particularly the reforms aimed at avoiding the accumulation of new domestic arrears.

II. Recent Developments and Program Performance

Growth is slowing on account of global uncertainties and the regional drought but external and financial indicators remain robust. Structural rigidities continued to prevent delivery of the intended monetary and fiscal stimulus. All program targets have been met.

5. **The first-round impact of the global financial crisis in Uganda was relatively limited.** The sudden reversal of portfolio inflows and lower foreign direct investment in the second half of 2008 led to a tightening of liquidity conditions, a rise in interest rates and a rapidly depreciating shilling. But economic growth (7 percent in FY2008/09) remained robust by regional and international standards, buoyed in part by strong cross-border exports, particularly of agricultural products.[2]

6. **Activity decelerated more markedly this fiscal year.** Subdued import growth, underperforming VAT receipts and weakening credit growth suggest a significant slackening in private demand in the first half of FY2009/10. The sharp deceleration in core inflation (to a 12-month rate of 6.5 percent in March compared to 9.9 percent in September 2009) may also reflect falling consumer demand. Causes for the slowdown include a prolonged drought (which adversely affected agricultural output) and lingering uncertainties regarding the path of the global recovery. Growth is expected to rebound in the latter part of the year as weather conditions improve and government spending accelerates, and reach 5.6 percent for FY2009/10 as a whole.

7. **The external position has remained strong.** Exports continued to expand while import growth slowed markedly with the downturn, leading to a narrowing of the trade deficit. The small increase in the external current account (to a projected 5 percent of GDP in FY2009/10, largely on account of lower official transfers) should be readily covered by higher FDI and multilateral disbursements. The rebound in capital inflows pressured the shilling, which appreciated by 19 percent between June and November 2009. Gross international reserves (including the SDR allocation) stood at the equivalent of about 5.1 months of imports in December.

8. **The policy response to the slowdown has been constrained by pervasive structural rigidities.** Prudent economic policies of the past gave Uganda scope to implement counter-cyclical policies. From the last quarter of 2008, monetary policy was gradually eased while the fiscal authorities took steps to raise investment spending and provide a positive impulse to growth. However, in both cases the intended stimulus failed to materialize.

- *The transmission mechanism from monetary policy to real sector activity has been weak.* The large injections of liquidity by the Bank of Uganda (BOU) prompted a sharp fall in interest rates on government securities, but lending rates did not come down as banks moved to a more conservative risk stance. As a result, private credit growth slowed markedly and only trended up marginally by the end of 2009. Reserve

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[2] Uganda's fiscal year starts July 1.

money, broad money and private sector credit all grew below program levels in the year to December 2009.

- *Budget under-execution prevented the delivery of the expected fiscal stimulus.* On the revenue side, receipts from VAT, personal income taxes and import duties grew more slowly than in previous years, reflecting softer economic growth and declining import volumes. However, the stimulus effect of lower revenue collections was more than offset by significant under-execution of capital spending, due to a combination of longstanding weaknesses in investment planning and teething problems as new procurement procedures were being introduced to ensure 'value for money'.

9. **The BOU has used foreign exchange management operations more actively to smooth out excessive volatility and support activity.** While remaining committed to a flexible exchange rate, the BOU intervened sporadically in the foreign exchange market to limit volatility including at the onset of the global financial crisis. More recently, the BOU stepped up its foreign exchange purchases in response to the sudden appreciation of the shilling. It also shifted the distribution of its monetary interventions from November 2009, reducing its regular daily sales of foreign exchange while maintaining the stock of domestic securities broadly unchanged. The shilling subsequently depreciated by around 9 percent between November 2009 and March 2010.

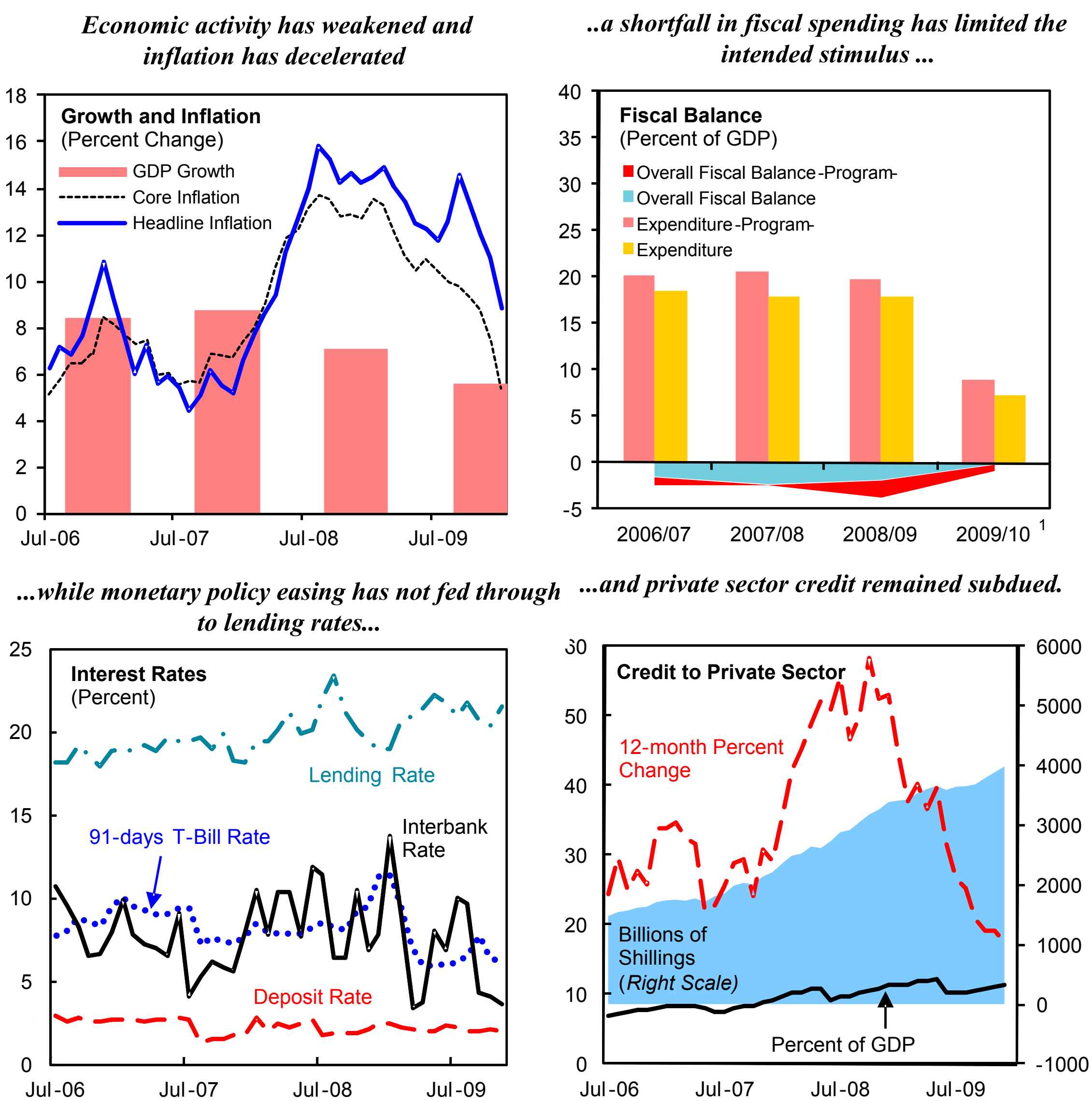
10. **The financial system remains sound, but pockets of vulnerabilities may be emerging.** In light of global and domestic uncertainties, banks have generally increased their liquidity buffers and tightened their lending standards. The system's capitalization levels remain adequate in the aggregate, and although NPLs have increased, the overall level is still low. Yet, new strains seem to have emerged, as reflected in the decline in overall bank profitability, with some banks, particularly smaller ones, registering losses and periodic liquidity stresses. Operational risks may also have increased, as new financial products such as mobile banking have spread rapidly.

11. **Financial sector structural reforms are progressing, albeit at a slow pace.** Recent advances in this area include, in particular, the near-complete rollout of the credit registry system and the development of a BOU-based settlement system to support secured transactions in the interbank market (as a way to reduce transaction costs and market segmentation). However, progress with other legal and institutional reforms has been slower and a number of laws to support the development of financial markets are yet to be enacted.

12. **Program performance in the first half of FY2009/10 has been strong in spite of a weakening of spending oversight.** All end-December assessment criteria and indicative targets have been met. No structural benchmarks were due for this review, but the authorities are making progress towards the completion of two measures: the submission to Parliament of a draft regulatory framework for pension funds and the rolling out of the Integrated Personnel and Payroll system. Latest figures from the auditor's office confirm, however, an upward drift in domestic arrears, with arrears accumulated since FY2004/05 through January 2010 estimated at around ½ percent of GDP. There is also evidence of a weakening in budget management, with unspent balances equivalent to about ½ percent of GDP being carried

forward from the previous fiscal year to the next one outside of established budget procedures.

Figure 1. Recent Economic Developments



[1] Outturn at December 2009

Source: Ugandan authorities and IMF staff estimates

III. The New PSI

The objectives and policies of the new PSI-supported program will largely be guided by those set out in the National Development Plan (NDP). Beyond maintaining macroeconomic stability, policies will continue to seek to alleviate constraints to growth through a build-up in public infrastructure while giving new impetus to structural reforms, particularly in the fiscal area. The government program will also aim at strengthening institutions ahead of expected oil production and lay down the grounds for Uganda's participation in the future East African Monetary Union.

13. **The new PSI will be guided by the objectives and policies outlined by the new NDP**. The NDP, approved by the cabinet in February 2010, broadens the policy focus from 'poverty reduction' to 'structural transformation'.[3] It gives the government a strategic role in this process through the elimination of growth constraints and the promotion of private investment in selected priority targets (Box 2). Government action is to be centered on four main areas: human resources development (health, education and skills building); physical infrastructure, particularly in energy and transportation; science, technology and innovation; and facilitation of private access to critical production inputs, particularly in agriculture.

Box 2. Uganda: Constraints to Growth

The National Development Plan identifies the following as the main impediments to economic growth and poverty reduction:

- *Weak public sector management and administration*: despite years of reforms, PFM slippages affect the efficiency in absorbing public funds. Insufficient funding of spending agencies remains a key constraint for effective performance of public institutions and delivery of public goods and services.
- *Inadequate financial services to the private sector:* availability and access to financial services is limited by the lack of financial services infrastructure across the country, high cost of financing, and an underdeveloped capital market.
- *Weak infrastructure*: with the exception of a rapidly expanding telecommunications sector, the state of Uganda's infrastructure is poor. Transport costs remain a significant trade barrier, equivalent to effective protection of over 20 percent and an implicit tax on exports of over 25 percent. Road density indicators are at par with the average for Sub-Saharan Africa but a much smaller fraction is paved. The existing railways are in poor shape and carry a negligible volume of freight. Electricity supply lags far below demand, with only 11 percent of the population having access to power from the grid. The internet infrastructure is also nascent with most concentration placed in the capital, Kampala.
- *Insufficient production inputs*: farm inputs and irrigation are costly and not widely employed, increasing agriculture vulnerabilities.

[3] Uganda's *National Development Plan 2010/11-2014/15* (http://www.imf.org) discusses in more detail the content of the NDP.

14. **Accordingly, the PSI-supported program will continue to target infrastructure development while ensuring a stable macro-economic environment**. The investment drive will maintain a focus on transport and energy. As donor assistance is likely to decline over the medium term, the increase in public spending will require higher mobilization of domestic revenue and access to new financing sources, including on less concessional terms. The fiscal and debt positions will however remain sustainable. Monetary policy will anchor inflationary expectations while a flexible exchange rate regime will help maintain competitiveness and a comfortable level of international reserves to cushion against exogenous shocks. The authorities will seek to continue to improve the living conditions of the poorest segments of the population through targeted programs in health and education as described in the NDP.

15. **The new PSI also aims at breathing new life into the structural reform agenda.** After a commendable start at the beginning of the previous PSI, progress in structural reforms has slowed and new weaknesses have emerged, particularly in public financial management. Over the last few years, the authorities embarked—with the support of donors—on a large number of initiatives in this area. The multiplicity of objectives and lack of prioritization has tended to overwhelm the local implementation capacity and at times overshadowed narrower, more functional reforms. In the event, progress in addressing longstanding problems such as the accumulation of domestic arrears and weak account management practices has been limited.

16. **Structural conditionality will be more narrowly focused on specific, incremental steps that can bring quick results in macro-critical areas and ensure a more satisfactory implementation of reforms**. It will continue to straddle the fiscal and financial sectors, both key to increase policy effectiveness and raise future growth. Staff and the authorities agreed on a set of actions to be implemented promptly and also identified follow-up and consolidation measures. The authorities noted that in many cases, external technical support would be needed to assist with implementation.

- On *public financial management*, there was broad consensus that weak implementation capacity and spending controls bear even more heavily on the public finances in the context of scaled-up infrastructure investment, and that strengthening account management and controlling the accumulation of domestic arrears—an area where performance has fallen repeatedly short—was an immediate priority.

- *Tax policy reforms*, together with continued improvements in tax administration, will raise domestic revenue and create fiscal space for the public investment push over the medium term.

- *Financial sector reforms* will continue to be two-pronged, aiming on one hand at consolidating banking stability and on the other at facilitating financial deepening, including through institutional and legal reforms.

17. **The PSI-supported program begins to lay the ground for two momentous events, the commercial exploitation of oil and the establishment of the East African Monetary Union (EAMU).** Although dates for both are uncertain and in any case still years away, both

will raise multiple macroeconomic policy challenges for Uganda. The policies in the program will help reach consistency with EAMU requirements over the medium term (including with respect to the international reserve cover and the fiscal deficit) and strengthen competitiveness and fiscal transparency in preparation for the oil era.

18. **The macroeconomic outlook over the period of the new PSI remains broadly positive although risks are on the rise.** Growth is expected to rebound to its potential in the next couple of years on the heels of the supportive fiscal stance and higher global and regional demand. Inflation is projected to hover around 5 percent and international reserves to rise above 5 months of imports. Risks, however, are mounting, mostly on the downside. The region remains vulnerable to severe security and weather-related shocks as well as unexpected shortfalls in aid. Domestically, election related tensions and resistance to the ambitious structural reform program could put pressure on Uganda's fiscal position and undermine donor and investor confidence. The authorities expressed their commitment to maintaining macroeconomic stability in the face of external and domestic shocks, as they have in the past.

A. Fiscal Policy

19. **Fiscal policy will continue to target a bold scaling up of energy and transportation infrastructure.** Public investment is targeted to increase from 6 ½ percent of GDP in 2008/09 to 8 percent by 2011/12—a path that is scaled down slightly compared to previous forecasts in view of implementation and absorptive capacity constraints.

20. **Reaching this ambitious investment target will require, first and foremost, more efficient budget execution.** Staff encouraged the authorities to step up capacity building in relevant spending agencies. Recent efforts to that end—most with support from donors—augur well for the future. The expanded use of Public Private Partnerships (PPPs) could also help alleviate implementation bottlenecks. Staff strongly support ongoing work to establish a sound legal and monitoring framework for PPPs (MEFP ¶23).

21. **Spending controls will also be strengthened.** As public investment spending is slated to increase significantly over the next three years, effective oversight mechanisms become even more critical. Procedures will be set to ensure the transparent treatment of unspent budget balances (Box 3). Regarding arrears, narrowly focused measures seem to have achieved some degree of success. For example, the establishment of a centralized payment system appears to have stemmed the increase in pension arrears. Staff and the authorities identified a set of similarly targeted actions that could be implemented quickly and complemented by follow-up and consolidation measures over the rest of the program (MEFP ¶26).

Box 3. Measures to Strengthen Spending Controls

Strengthening account management

- Report to Parliament of unspent budget balances at the end of each fiscal year will become mandatory and their subsequent use will be allowed only with new Parliamentary appropriation.
- The authorities will undertake a thorough review of all existing government accounts and close promptly those not associated with a legitimate government activity (structural benchmark).
- Relevant financial legislation will be reviewed and amended as needed to ensure it does not leave scope for diverting budgetary funds.

Controlling domestic arrears

- The centralized payment procedure will be extended to utilities and rents in the next budget cycle (structural benchmark).
- More realistic budget projection mechanisms will be introduced to prevent under-provisioning of recurrent spending in key areas, an important source of arrears accumulation in recent years.
- A mandatory rotation of accountants and procurement officers will also be introduced to reduce opportunities for collusion (structural benchmark).
- The government will continue to expand use of integrated management and payroll systems across government entities to improve oversight (structural benchmark).

22. **New financing sources will need to be tapped to fund the public investment drive.** Current financing plans show that aid flows, and particularly grants, are expected to decline in coming years. Donor support has also tended to trend down in previous election periods because of governance and transparency concerns. Under conservative projections, grants would decline to about 1½ percent of GDP by the end of the program period (from 3½ percent in FY2008/09). In that context, raising the public investment ratio to 8 percent of GDP will require mobilizing additional financing equivalent to about 3½ percentage points of GDP.

23. **There is significant scope to raise domestic revenue.** Uganda's tax-to-GDP ratio is low by international and regional standards, including in the EAC. So far, efforts to boost tax receipts have largely relied on improvements in revenue administration. The forthcoming introduction of a national identification system will also help reduce tax evasion. While welcoming these efforts, staff argued that additional tax policy measures are needed to raise the tax ratio in a more decisive manner. In view of the forthcoming elections and the still subdued level of activity, objectives for the first year of the program are relatively modest (a review of all existing tax incentives and exemptions—many of which may have been granted in *an ad hoc* fashion to individual sectors and firms—and recommendations for their streamlining) (MEFP ¶14). The authorities agreed to consider additional tax policy measures in subsequent years (MEFP ¶21).These could include broadening the coverage of taxes on property, capital gains or informal activities. The program targets an increase in tax collections of 1½ percent of GDP over the coming three years.

24. **The shortfall could be financed in part by non-concessional borrowing.** Uganda has maintained a very cautious borrowing strategy since debt relief, and its risk of debt distress is low.[4] The authorities intend to continue to rely on concessional resources to the extent possible to fund their investment program, and to rely on non-concessional borrowing only to the extent that a shortfall materializes (MEFP ¶24). The debt sustainability analysis shows that measured amounts of non-concessional borrowing could be contracted without endangering debt sustainability. Domestic financing could also be increased as long as it does not endanger monetary stability and inflation targets. In practice however, Uganda's limited absorptive capacity and its still budding procedures for public investment selection and implementation set constraints on the size of a manageable borrowing envelope.

25. **The PSI includes a ceiling of $500 million on non-concessional borrowing for the duration of the program.** This borrowing, equivalent to about 0.7 percent of GDP a year, on average over the PSI period, would leave all debt indicators well below the DSA thresholds. It is consistent with the authorities' preliminary investment program. It could be revisited once investment plans are better specified and financing options have been more closely assessed, including in particular those related to the development of regional infrastructure in the context of the EAC.

B. Monetary and Financial Sector Policies

26. **Monetary policy will aim at keeping annual underlying inflation at 5 percent on average, using base money as an operating target to that end.** The exchange rate will remain flexible, with only sporadic intervention from the BOU to smooth out undue volatility. In addition, the authorities will seek to build up international reserves in the context of the EAC.

27. **Monetary management will continue to rely on a mix of foreign exchange and domestic securities operations.** With technical assistance from MCM, the BOU will continue to enhance the flexibility of its short-term liquidity management. The absence of high-frequency activity indicators has complicated monetary decisions in the recent downturn, and staff welcome the steps taken by the authorities to fill that gap (MEFP ¶15). Staff emphasized that closer coordination with the Ministry of Finance on near-term cash flow projections is also critical to ensure the effectiveness of liquidity management.

28. **Staff support the authorities' objective of maintaining comfortable international reserves.** Uganda's vulnerability to sizable external shocks (including to aid flows) and uncertainties related to the future development of the oil sector justify keeping a solid reserve buffer. Shortfalls in donor aid, particularly in the coming election year, may dampen reserve accumulation. Also, the large public investment drive may put pressure on the reserve cover target, in as far as these investments entail a large increase in imports. Against that backdrop, reserve accumulation is projected to slow in the near term before regaining steam in the outer years. Staff continue to see merit in targeted intervention in the foreign exchange market to smooth out excessive exchange rate volatility.

[4] The detailed debt sustainability analysis is a supplement to this staff report.

29. **A new, comprehensive financial markets development plan is being prepared.** The plan, developed under a common EAC framework, aims at harmonizing the legal and regulatory infrastructure in the region. It will include a roadmap of reforms to increase access to financial services (including in rural areas) and reduce borrowing costs for smaller enterprises. A deeper financial market should make monetary policy more effective over the medium term. The plan, expected to be finalized in June 2011, could form the basis for structural reform agenda in this area to be included in the PSI's later years. The authorities indicated that external technical expertise, including from the IMF, would be desirable to assist in implementing this plan.

30. **Finalizing the reform of the pension sector remains an objective of the PSI-supported program.** The bill establishing a pension fund regulator—a key requirement for sound liberalization of the sector—was approved by Cabinet in December 2009 and is on track to be submitted to Parliament before year end. Staff welcome progress in this area and support the authorities' intent to conduct, preferably with external technical assistance, an assessment of the viability of the National Social Security Fund and other existing pension schemes (MEFP ¶25).

31. **The BOU will pursue its efforts to raise the quality of its oversight of the banking system**. A financial stability department has been established, and the first *Financial Stability Report* was published in January 2010. Steps are being taken to increase minimum bank capital requirements, in line with the practice in other EAC members, and to extend regulatory coverage to large deposit-taking microfinance institutions (MEFP ¶17). Staff welcomed these advances and recommended continued watchfulness, particularly of the few small banks that have suffered a recent deterioration of their balance sheet. Staff also encouraged the authorities to review their crisis preparedness and build capacity for contingency planning and crisis resolution, to ensure that the BOU has the legal tools and appropriate human resources to intervene quickly if the need were to arise.

C. Management of Oil Resources

32. **Large-scale oil production will pose significant macroeconomic policy challenges for Uganda.** It is not yet possible to estimate precisely the impact of oil on the Ugandan economy as the timing, scope and pace of oil production remain contingent upon the results of ongoing exploration activity and technical analyses. However, with reserves potentially as large as 2 billion barrels and oil revenues likely to exceed one third of total government revenues, oil can be expected to alter meaningfully Uganda's productive, fiscal and financial landscape (Box 4).

33. **Staff commended the authorities for their early commitment to establishing a sound legal and institutional framework for the management and use of oil revenues.** The authorities are eager to preserve Uganda's hard-won record of macroeconomic stability while maximizing the opportunities offered by oil for development and income growth. They are initiating the expert review of relevant public finance legislation and stand ready to introduce all necessary amendments to provide a robust and transparent regulatory environment for oil, preserve budget integrity and limit unintended leakages (MEFP ¶29). The authorities are appreciative of the technical assistance provided by the Fund and other

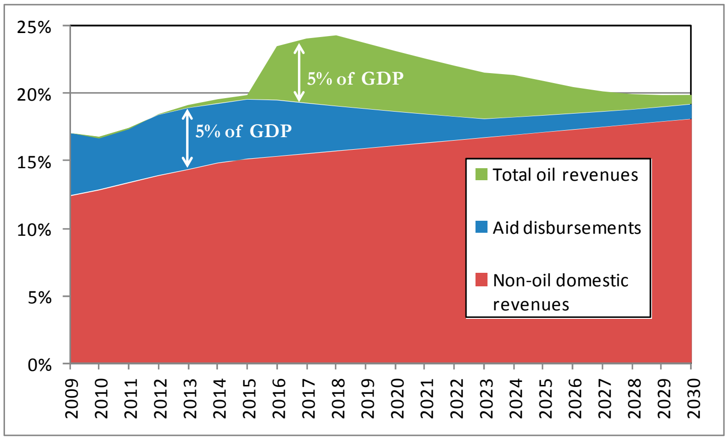
development partners in this area and hope it will be continued. Staff and the authorities agreed that a fiscal ROSC would provide a particularly timely assessment of the quality of their fiscal institutions.

34. **The PSI-supported structural reform agenda will help prepare Uganda for the oil era.** Stronger public financial management systems are crucial to the efficient spending of oil revenues. Higher non-oil tax collections will help ensure post-oil fiscal sustainability and offset any retrenchment in overseas aid. The current drive to improve public infrastructure and increase financial access will help overcome, at least in part, the strains on competitiveness that could arise from oil-related appreciation pressures. These first steps could be usefully complemented by more forceful efforts to promote a more fluid and supportive investment climate and reduce transaction costs—policies that take time to bear fruit and should be initiated now. A transparent and well-focused public communication strategy with investors, donors and civil society would also help in keeping private expectations in check.

Box 4. The Macro-Economic Implications of Oil

Preliminary estimates suggest that oil could account for around 8 percent of Uganda's GDP, and up to one third of government revenues. Oil reserves are currently expected to last for around 25 years and offer a unique opportunity to raise income levels. However, the substantial size of oil revenues combined with their short duration and inherent volatility will pose significant challenges for macroeconomic management.

Figure 2.: Uganda's oil revenue will be large but temporary (percent of GDP).



The first and most widely documented risk is to competitiveness. Demand for non-tradables can be expected to rise in line with government spending and private expectations. The resulting appreciation of the shilling (either through inflation and/or through the nominal exchange rate) cannot be avoided, but well-designed policies can increase productivity and preserve competitiveness. There is considerable scope, for example, to lower production costs through investment in public infrastructure, skills training, and reforms to land and other input markets.

Money and foreign exchange markets will also face major structural shifts. Oil export earnings will increase their size in an abrupt manner. Oil price movements will feed through the foreign exchange market and increase exchange rate volatility. Asset bubbles will be a risk as oil wealth prospects attract private financial inflows. In that context, monetary policy alone is likely to be insufficient to address both appreciation and inflation pressures stemming from oil resources, and fiscal policy will take an even more central role in maintaining macroeconomic stability.

A fiscal rule can help govern the accumulation and spending of oil wealth. The rule would respond to at least three objectives: (i) preserving a share of oil wealth for future generations; (ii) smoothing spending to insulate the non-oil economy from volatile oil revenues; and (iii) mitigating the deterioration in competitiveness (as public spending usually features a large component of non-tradables). Countries such as Timor-Leste and Chile offer examples of well functioning commodity funds underpinned by relatively complex fiscal rules. Uganda may consider a simpler fiscal rule initially, with sufficient flexibility to adapt to the country's circumstances. The authorities expressed interest in anchoring fiscal policy through a ceiling on the public spending-to-GDP ratio. Technical assistance may be useful in this respect

Box 4.The Macro-Economic Implications of Oil (concluded)

The fiscal rule should also take into account Uganda's participation in the future East African Monetary Union. Uganda is the only prospective EAMU member with large proven oil resources. In the future, its business cycle would not be fully synchronized with those of other oil-importing EAMU members. Monetary policy in the EAMU will be set based upon economic conditions in the union as a whole. It would likely be loosened during oil price booms, to support growth in oil importers, fueling further inflationary pressures in oil-exporting Uganda. The monetary union will thus place an additional burden on fiscal policy as a counter-cyclical policy instrument in Uganda. In anticipation, the authorities could consider measures to strengthen automatic stabilizers (through an increased tax effort and the development of social transfers). Consideration could also be given to a fiscal rule that weakens the link between oil prices and domestic activity—for instance, a savings rule that places a relatively low discount rate on the consumption of future generations.

IV. The Program for the Remainder of 2009/10 and 2010/11

In light of the slowdown in economic activity, near term economic policies will aim at reviving growth back to its potential. An ambitious, upfront effort at fiscal structural reforms will help address recent shortcomings and set the stage for more efficient fiscal spending in the years to come.

35. **Growth is expected to remain below potential in the near term.** After a weak first half of FY2009/10, activity is projected to recover gradually on the heels of higher public spending and a weather-related rebound in agriculture. Overall, growth in FY2009/10 will only reach 5.6 percent, rising moderately to 6.4 percent in 2010/11. Inflation is expected to ease to about 5 percent at the end of the fiscal year but pressures may arise from the recent depreciation of the shilling. Gross international reserves are projected to remain at a comfortable level, reflecting, inter alia, the positive impact of the SDR allocation, which provides an additional buffer against shocks and downside risks.

A. Fiscal policy

36. **Public spending is being accelerated in the second half of FY2009/10 to provide stimulus to domestic demand.** Expenditure worth around ½ percent of GDP is being reallocated from development to current items. Reallocated resources will be used to address humanitarian emergencies and provide for under-budgeted pensions. In addition, unspent balances from the FY2008/09 development budget are being carried forward, for an amount equivalent to another ½ percent of GDP. Assuming full execution of this revised budget, the fiscal stance will be roughly neutral for the year, but strongly expansionary in the second half (Table).

Uganda: Fiscal Impulse of the Central Government, FY2007/08–2010/11

	2007/08	2008/09	2009/10		2010/11
	Actual	Est.	6th Review	Proj.	Proj.
Overall fiscal balance (incl. grants)	-2.4	-1.9	-2.5	-2.3	-3.2
Primary balance	-1.1	-1.0	-1.5	-1.3	-2.1
Fiscal impulse (unadjusted for cyclical position) [1]	0.7	-0.1	0.6	0.3	0.8
Cyclical adjustment	0.3	0.0	-0.1	-0.3	-0.1
Fiscal impulse adjusted for cyclical position [2]	**1.0**	**-0.1**	**0.5**	**0.0**	**0.7**
GDP growth	8.7	7.1	6.3	5.6	6.4
Potential GDP growth	7.0	7.0	7.0	7.0	7.0
Gap	1.7	0.1	-0.7	-1.4	-0.6
Cyclical elasticity of primary balance	0.2	0.2	0.2	0.2	0.2

[1] The impulse is calculated as the change in the primary balance with respect to the preceding year; (-) = fiscal withdrawal

[2] The adjusted fiscal impulse is equal to the fiscal impulse, adjusted for the fiscal impact of the deviation of growth from potential; the calculation assumes an elasticity of 0.2 and a potential GDP growth of 7 percent.

37. **A range of structural measures are being introduced to ensure that the additional resources are well spent.** Staff noted in particular that the carry-forward of unspent balances from 2008/09 without Parliamentary re-appropriation creates serious potential for leakages and ineffective spending. The authorities agreed to move quickly to tighten the relevant legislation (MEFP ¶27) to avoid recurrence of this practice. Staff also underscored that reallocated items should be subject to the same budgetary discipline as items approved in the original budget.

38. **The fiscal stance will remain slightly expansionary in FY2010/11.** Investment spending is scheduled to increase by around 1 percentage point of GDP as spending agencies gain familiarity with planning and procurement procedures. Tax revenue will rebound reflecting the pick-up in economic activity together with renewed efficiency gains, but this will be insufficient to cover the expected shortfall in grants. To avoid squeezing public infrastructure investment and dent the emerging recovery, the program envisages a temporary increase in domestic financing of the government budget (0.6 percent of GDP, year-on-year) and a small dip in the reserve cover. These are upper bound estimates, as a less-than-complete execution of the budget, and higher donor disbursements, would reduce the financing needs.

B. Monetary and Exchange rate Policies

39. **Monetary policy in the near term will be cautiously accommodative.** Reserve money is projected to grow by 19 percent in FY2009/10 so as to cover shortfalls in budget financing while providing enough room for private sector credit growth. This stance is not expected to generate inflationary pressures given the weak economic activity. However, the authorities should remain vigilant to inflation risks and stand ready to tilt the policy stance as demand picks up.

40. **The monetary policy stance in FY2010/11 will be driven by the pace of the economic recovery and inflation developments.** Reserve money growth (of about 14 percent, consistent with a core inflation target of 5 percent) is predicated on a pick-up in

economic activity and full execution of the planned fiscal stance. The authorities viewed the development of high-frequency activity indicators as key to enhancing the efficiency of monetary policy.

41. **International reserves are not expected to come under strain in the near-term.** In FY2009/10, muted import growth is expected to lead to an additional build-up of reserves despite weaker capital inflows. However, the expected shortfall in budget support may constrain the authorities' ability to increase reserves further in the following year. Even though this could delay the desired accumulation path, the authorities and staff agreed that a drawdown in reserves to cushion a temporary shock was appropriate.

C. Program Monitoring

42. **For monitoring performance under the three-year PSI, quantitative assessment criteria, quantitative indicative targets, and structural benchmarks have been proposed** (MEFP Tables 1 and 2). The quantitative targets will be monitored on a semiannual basis and include net credit to the central government from the banking system, net domestic assets of the central bank, and net international reserves of the BOU. Targets to be monitored on a continuous basis include nonaccumulation of external arrears, contracting or guaranteeing of new nonconcessional external debt, and new short-term external debt. The standard provisions on the exchange system and trade issues that apply to the use of the Fund's financial resources will apply as continuous assessment criteria under the PSI. The assessment dates for the first year will be end-June 2010 and end-December 2010.

V. Staff Appraisal

43. **Prudent macroeconomic management has allowed Uganda to emerge from a succession of adverse external shocks relatively unscathed.** Although growth has slowed, it remains enviable by international standards and is set to rebound quickly. The authorities' focus on closing the infrastructure gap—one of the most binding constraints to growth—while maintaining a sound macroeconomic environment should help raise potential output and future income levels.

44. **Persistent structural rigidities continue to hamper policy implementation.** Financial sector segmentation together with fiscal capacity constraints have prevented the delivery of intended fiscal and monetary stimulus, and weaknesses in public financial management bear on the efficient use of scarce public resources. Revamping and refocusing the structural reform program on these hurdles is an important priority. Well-targeted external technical assistance can go a long way in helping the authorities reach that goal.

45. **Staff recommend completion of the 7th review under the PSI.** All quantitative assessment criteria have been met. The impact of emerging weaknesses in budget implementation and spending controls has been limited and has not jeopardized program objectives. Staff welcome the authorities' determination to take early action to address these shortcomings head-on in the requested successor PSI.

46. **Staff support the authorities' request for a new PSI.** The agreed program aims at continued infrastructure build-up to support private investment and growth. It will give new impetus to structural reforms in the fiscal and financial sectors through structural conditionality that is more narrowly focused to enhance the prospects of success. The PSI-supported program will help maintain macroeconomic stability through the forthcoming election period. It will also help Uganda prepare for East African integration and the oil era, when they come.

47. **There are risks to the program but they appear manageable.** The first would be a loss of investor and donor confidence due to uncertainties in the run-up to elections. Against that backdrop, the program is predicated on conservative financing assumptions. Regional shocks are also a risk given the fragile security situation in some of Uganda's neighbors. The authorities have a solid track record of maintaining macroeconomic stability in the face of adverse domestic and external shocks, and staff trust that they will be able to continue to do so if the need were to arise.

Table 1. Uganda: Selected Economic and Financial Indicators, FY2008/09–2013/14 [1]

	2008/09	2009/10		2010/11	2011/12	2012/13	2013/14
	Prel.	Sixth Rev.	Proj.	Proj.	Proj.	Proj.	Proj.
GDP and prices (percent change)							
Real GDP	7.1	6.3	5.6	6.4	7.0	7.2	7.4
Headline inflation (end of period)	12.3	12.2	5.0	5.3	5.2	5.3	5.5
Headline inflation (average)	14.2		9.5	4.1	5.2	5.3	5.2
Core inflation (end of period)	11.1	7.9	3.9	5.0	5.0	5.0	5.0
Core inflation (average)	12.5		7.0	4.5	4.9	5.1	4.9
External sector (percent change)							
Terms of trade (Based on commodities, deterioration –)	6.6	-2.7	5.9	-8.4	-2.4	-1.1	-1.3
Terms of trade (based on all exports, deterioration -)	11.6		7.8	-4.0	1.1	1.8	1.8
Real effective exchange rate (depreciation –)	…	…	0.3	--	--	--	--
Money and credit (percent change)							
Broad money (M2)	26.3	21.2	19.3	13.7	15.6	15.9	16.0
Domestic credit	24.1	13.7	11.3	8.8	8.3	8.2	8.9
Credit to the central government [2]	6.8	1.4	1.5	1.6	0.6	0.6	1.3
Private sector credit	31.6	21.4	17.1	12.7	13.8	13.9	14.2
Savings and investment gap (percent of GDP)	-8.1	-9.2	-7.7	-8.0	-7.9	-7.3	-7.1
Domestic investment	24.2	24.9	23.3	24.7	26.0	26.2	26.6
Public	6.2	7.2	5.6	6.7	7.9	7.9	8.1
Private	18.0	17.7	17.7	17.9	18.1	18.3	18.5
National savings (excluding grants)	16.1	15.7	15.6	16.7	18.2	19.0	19.6
Public	0.9	2.2	0.9	1.7	2.6	3.1	3.6
Private	15.2	13.5	14.7	15.0	15.6	15.9	16.0
External sector (percent of GDP)							
Current account balance (including grants)	-4.8	-6.7	-5.3	-6.2	-6.1	-5.7	-5.6
Current account balance (excluding grants)	-8.1	-9.2	-7.7	-8.0	-7.9	-7.3	-7.1
Net donor inflows	4.5	6.1	5.3	3.8	4.4	3.8	3.4
External debt (including Fund)	13.9	14.3	14.0	15.6	17.6	18.9	19.9
External debt-service ratio [3, 4]	1.6	1.0	1.1	1.0	1.3	1.7	1.6
Government budget and debt (percent of GDP)							
Revenue	12.5	12.8	12.5	13.1	13.5	14.0	14.4
Grants	3.4	2.6	2.4	1.8	1.8	1.6	1.4
Total expenditure and net lending	-17.8	-17.8	-17.2	-18.1	-18.8	-18.7	-18.9
Overall balance (including grants)	-1.9	-2.5	-2.3	-3.2	-3.6	-3.2	-3.1
Overall balance (excluding grants)	-5.3	-5.0	-4.7	-5.0	-5.4	-4.8	-4.5
Stock of domestic debt	8.4	6.7	7.6	7.0	6.7	6.6	6.5
Memorandum items:							
Nominal GDP (U Sh billions)	29,972	36,330	35,213	39,040	44,014	49,725	56,246
Average exchange rate (U Sh per US$)	1,905	…	…	…	…	…	…
Treasury bill yield (percent)	6.0	…	…	…	…	…	…
Overall balance of payments (US$ millions)	178	291	291	60	237	284	288
Gross foreign exchange reserves							
(months of next year's imports of goods and services)	4.9	4.9	5.1	4.8	4.9	5.0	5.1

Sources: Ugandan authorities; and IMF staff estimates and projections.

[1] Fiscal year begins in July.
[2] Percent of M3 at start of the period.
[3] Percent of exports of goods and nonfactor services.
[4] Including Fund obligations; reflects actual debt service paid, including debt relief.

Table 2. Uganda: Fiscal Operations of the Central Government, FY2007/08–2013/14 [1]

	2007/08	2008/09	2009/10		2010/11	2011/12	2012/13	2013/14
	Actual	Actual	Sixth Review	Proj.	Proj.	Proj.	Proj.	Proj.
	(U Sh Billions)							
Total revenue and grants	3,800	4,773	5,577	5,242	5,804	6,719	7,722	8,921
Revenue	3,145	3,758	4,642	4,408	5,106	5,929	6,938	8,116
Tax	3,024	3,560	4,439	4,186	4,856	5,682	6,659	7,805
International trade taxes	308	361	431	382	424	509	612	741
Income taxes	862	1,094	1,372	1,305	1,475	1,732	2,040	2,373
Excises	815	921	1,083	1,055	1,202	1,425	1,660	1,938
Value-added tax	1,039	1,184	1,464	1,334	1,550	1,782	2,077	2,448
Additional revenue effort	0	0	90	110	205	235	270	305
Nontax	121	198	203	222	249	246	279	311
Grants	656	1,014	936	834	698	790	784	805
Budget support	470	531	519	611	368	392	373	384
Project grants	185	484	417	223	330	399	410	422
Expenditures and net lending	4,384	5,339	6,472	6,046	7,048	8,287	9,320	10,644
Current expenditures	2,881	3,198	3,737	3,810	4,125	4,655	5,243	5,929
Wages and salaries	1,106	1,184	1,307	1,307	1,462	1,655	1,888	2,140
Interest payments	309	264	358	358	440	439	479	510
Other current	1,466	1,750	2,072	2,145	2,223	2,561	2,876	3,278
Development expenditures	1,362	1,915	2,599	1,987	2,662	3,521	3,961	4,602
Donor-supported projects	644	708	1,077	733	1,265	1,744	1,795	1,846
Domestic-financed	718	1,207	1,522	1,253	1,397	1,777	2,166	2,756
Net lending and investment	-163	-57	-40	-31	-39	-39	-34	-36
Other spending [2]	304	283	176	281	300	150	150	150
Off which: Development spending carried over [3]				174				
Overall balance								
Including grants	-583	-566	-895	-804	-1,245	-1,568	-1,598	-1,724
Excluding grants	-1,239	-1,581	-1,830	-1,638	-1,942	-2,358	-2,382	-2,529
Excl. grants and add'l energy spending	-1,120	-1,581	-1,830	-1,638	-1,942	-2,358	-2,382	-2,529
Financing	541	526	895	805	1,245	1,568	1,598	1,724
External financing (net)	618	592	863	710	1,022	1,413	1,436	1,478
Disbursement	706	746	1,044	890	1,144	1,560	1,606	1,651
Budget support	211	233	383	380	208	214	221	227
Project loans	495	513	661	510	936	1,346	1,385	1,424
Amortization (–)	-87	-126	-119	-127	-126	-139	-161	-170
Exceptional financing [2]	-13	-29	-61	-53	1	-11	-12	-4
Domestic financing (net)	-78	-66	32	94	223	155	162	246
Bank financing	-177	343	88	94	123	55	62	146
Nonbank financing	99	-409	-57	0	100	100	100	100
Errors and omissions/financing gap	43	-41	0	0	0	0	0	0

Sources: Ugandan authorities; and IMF staff estimates and projections.

[1] Fiscal year begins in July.

[2] Includes arrears.

[3] Spending related to unused balances carried over from FY2008/09

Table 2. Uganda: Fiscal Operations of the Central Government, FY2007/08–2013/14 [1] (concluded)

	2007/08	2008/09	2009/10		2010/11	2011/12	2012/13	2013/14
	Actual	Actual	Sixth Review	Proj.	Proj.	Proj.	Proj.	Proj.
Total revenue and grants	15.5	15.9	15.4	14.9	14.9	15.3	15.5	15.9
Revenue	12.8	12.5	12.8	12.5	13.1	13.5	14.0	14.4
Tax	12.3	11.9	12.2	11.9	12.4	12.9	13.4	13.9
International trade taxes	1.3	1.2	1.2	1.1	1.1	1.2	1.2	1.3
Income taxes	3.5	3.6	3.8	3.7	3.8	3.9	4.1	4.2
Excises	3.3	3.1	3.0	3.0	3.1	3.2	3.3	3.4
Value-added tax	4.2	4.0	4.0	3.8	4.0	4.0	4.2	4.4
Additional revenue effort	0.0	0.0	0.2	0.3	0.5	0.5	0.5	0.5
Nontax	0.5	0.7	0.6	0.6	0.6	0.6	0.6	0.6
Grants	2.7	3.4	2.6	2.4	1.8	1.8	1.6	1.4
Budget support	1.9	1.8	1.4	1.7	0.9	0.9	0.8	0.7
Project grants	0.8	1.6	1.1	0.6	0.8	0.9	0.8	0.7
Expenditures and net lending	17.9	17.8	17.8	17.2	18.1	18.8	18.7	18.9
Current expenditures	11.8	10.7	10.3	10.8	10.6	10.6	10.5	10.5
Wages and salaries	4.5	3.9	3.6	3.7	3.7	3.8	3.8	3.8
Interest payments	1.3	0.9	1.0	1.0	1.1	1.0	1.0	0.9
Other current	6.0	5.8	5.7	6.1	5.7	5.8	5.8	5.8
Development expenditures	5.6	6.4	7.2	5.6	6.8	8.0	8.0	8.2
Donor-supported projects	2.6	2.4	3.0	2.1	3.2	4.0	3.6	3.3
Domestic-financed	2.9	4.0	4.2	3.6	3.6	4.0	4.4	4.9
Net lending and investment	-0.7	-0.2	-0.1	-0.1	-0.1	-0.1	-0.1	-0.1
Other spending [2]	1.2	0.9	0.5	0.8	0.8	0.3	0.3	0.3
Off which: development spending carried over [3]				0.5				
Overall balance								
Including grants	-2.4	-1.9	-2.5	-2.3	-3.2	-3.6	-3.2	-3.1
Excluding grants	-5.1	-5.3	-5.0	-4.7	-5.0	-5.4	-4.8	-4.5
Financing	2.2	1.8	2.5	2.3	3.2	3.6	3.2	3.1
External financing (net)	2.5	2.0	2.4	2.0	2.6	3.2	2.9	2.6
Disbursement	2.9	2.5	2.9	2.5	2.9	3.5	3.2	2.9
Budget support	0.9	0.8	1.1	1.1	0.5	0.5	0.4	0.4
Project loans	2.0	1.7	1.8	1.4	2.4	3.1	2.8	2.5
Amortization (–)	-0.4	-0.4	-0.3	-0.4	-0.3	-0.3	-0.3	-0.3
Exceptional financing [2]	-0.1	-0.1	-0.2	-0.1	0.0	0.0	0.0	0.0
Domestic financing (net)	-0.3	-0.2	0.1	0.3	0.6	0.4	0.3	0.4
Bank financing	-0.7	1.1	0.2	0.3	0.3	0.1	0.1	0.3
Nonbank financing	0.4	-1.4	-0.2	0.0	0.3	0.2	0.2	0.2
Errors and omissions/financing gap	0.2	-0.1	0.0	0.0	0.0	0.0	0.0	0.0

Sources: Ugandan authorities; and IMF staff estimates and projections.

[1] Fiscal year begins in July.

[2] Includes arrears.

[3] Spending related to unused balances carried over from FY2008/09.

Table 3. Uganda: Monetary Accounts, FY2007/08–2013/14 [1]
(U Sh billions; end of period, unless otherwise indicated)

	2007/08	2008/09	2009/10		2010/11	2011/12	2012/13	2013/14
	Act.	Act.	Prog	Proj.	Proj.	Proj.	Proj.	Proj.
				Monetary survey				
Net foreign assets	5,087	5,711	5,508	5,893	6,370	7,169	8,115	9,130
Net domestic assets	-49	586	2,122	1,619	2,171	2,708	3,329	4,147
Claims on public sector (net) [2]	-1,026	-677	-589	-583	-460	-406	-344	-198
Claims on private sector	2,736	3,599	4,371	4,214	4,752	5,409	6,159	7,034
Other items (net) [3]	-1,759	-2,336	-1,661	-2,013	-2,120	-2,296	-2,486	-2,690
Money and quasi-money (M3)	5,038	6,298	7,630	7,512	8,541	9,877	11,444	13,277
Broad money (M2)	3,895	4,921	5,961	5,869	6,674	7,717	8,942	10,374
Foreign exchange deposits	1,142	1,377	1,668	1,642	1,867	2,159	2,502	2,903
Net foreign assets	4,351	5,119	4,737	5,221	5,501	6,174	6,979	7,837
Net domestic assets	-2,737	-3,169	-2,377	-2,897	-2,843	-3,074	-3,388	-3,671
Claims on public sector (net) [2]	-2,418	-2,277	-2,154	-2,329	-2,169	-2,228	-2,355	-2,437
Claims on commercial banks	131	124	124	124	124	124	124	122
Other items (net) [3]	-449	-1,016	-348	-692	-798	-970	-1,157	-1,356
Base money	1,614	1,950	2,360	2,324	2,658	3,099	3,591	4,166
Currency outside banks plus cash in vaults	1,230	1,469	1,779	1,752	2,010	2,352	2,725	3,162
Commercial bank deposits with BOU	384	482	581	572	649	747	866	1,004
Memorandum items:								
Base money	29.9	20.8	21.0	19.1	14.4	16.6	15.9	16.0
M3	31.1	25.0	21.2	19.3	13.7	15.6	15.9	16.0
Credit to the private sector	50.9	31.6	21.4	17.1	12.7	13.8	13.9	14.2
M0-to-GDP ratio (percent)	6.6	6.5	6.5	6.6	6.8	7.0	7.2	7.4
M3-to-GDP ratio (percent)	20.6	21.0	21.0	21.3	21.9	22.4	23.0	23.6
Base money multiplier (M2/base money)	2.41	2.52	2.53	2.53	2.51	2.49	2.49	2.49
Credit to the private sector (percent of GDP)	11.2	12.0	12.0	12.0	12.2	12.3	12.4	12.5
Gross reserves of BOU (US$ millions)	2,684	2,442	2,730	2,730	2,790	3,022	3,301	3,589

Sources: Ugandan authorities; and IMF staff estimates and projections.

[1] Fiscal year begins in July.

[2] The public sector includes the central government, the public enterprises, and the local government.

[3] Including valuation effects and the BOU's claims on the private sector.

[4] Reclassification of non-bank institutions in FY2007/08 added approximately Ush 250 bn to the stock of private sector credit. Excluding this amount, credit to the private sector grew by 40 percent.

Table 4. Uganda: Balance of Payments, FY2007/08-2013/14 [1]
(US$ millions)

	2007/08	2008/09	2009/10		2010/11	2011/12	2012/13	2013/14
	Act.	Act.	6th Rev.	Proj.	Proj.	Proj.	Proj.	Proj.
Current account	-469	-758	-1,196	-942	-1,156	-1,246	-1,283	-1,396
Percent of GDP	*-3.2*	*-4.3*	*-6.4*	*-5.3*	*-6.2*	*-6.1*	*-5.7*	*-5.6*
Trade balance	-913	-1,139	-1,294	-978	-1,140	-1,233	-1,224	-1,289
Percent of GDP	*-6.3*	*-6.4*	*-6.9*	*-5.5*	*-6.1*	*-6.0*	*-5.4*	*-5.2*
Exports, f.o.b.	2,597	3,085	3,421	3,432	3,657	3,924	4,229	4,552
Of which: coffee	349	336	314	306	319	338	359	380
Imports, f.o.b.	-3,509	-4,225	-4,715	-4,409	-4,797	-5,158	-5,453	-5,842
Of which: infrastructure related				-366	-511	-603	-650	-718
Services (net)	-555	-664	-736	-805	-894	-966	-1,007	-1,077
Income (net)	-280	-332	-488	-445	-432	-430	-490	-543
Of which: interest on public debt	-22	-24	-25	-25	-34	-45	-61	-67
Transfers	1,278	1,378	1,322	1,285	1,309	1,383	1,438	1,513
Private transfers	852	857	838	865	974	1,014	1,082	1,158
Of which: workers' remittances (inflows)		746		776	843	905	974	1,047
Of which: nongovernmental organizations (inflows)	547	454	445	454	472	484	495	506
Official transfers	427	521	484	419	335	369	355	355
Of which: budget support	232	224	219	261	126	130	114	114
project support	109	254	215	112	158	186	186	186
HIPC grants	48	44	50	47	51	53	55	55
Capital and financial account	1,139	1,434	1,487	1,234	1,216	1,483	1,567	1,685
Capital account	0	0	0	0	0	0	0	0
Of which: MDRI debt relief	0	0	0	0	0	0	0	0
Financial account	1,139	1,434	1,487	1,234	1,216	1,483	1,567	1,685
Foreign direct and portfolio investment	817	631	816	816	923	1,020	1,125	1,245
Other investment	322	803	671	417	293	463	442	440
Medium- and long-term	516	577	966	842	660	611	576	544
Of which:								
Public sector (net)	318	322	694	610	489	663	655	653
SDR allocation			224	224				224
Disbursements	369	388	756	672	550	728	728	728
Project support	292	270	341	257	450	628	628	628
Of which: new non-concessional borrowing			*0*	*0*	*0*	*178*	*178*	*178*
Budget support	2	118	191	191	100	100	100	100
Amortization due	-51	-65	-62	-62	-61	-65	-73	-75
Private sector (net)	198	255	271	232	171	-52	-79	-109
Short-term	-193	226	-295	-424	-367	-148	-135	-104
Errors and omissions	-143	-497	0	0	0	0	0	0
Overall balance	563	178	291	291	60	237	284	288
Financing	-563	-178	-291	-291	-60	-237	-284	-288
Central bank net reserves (increase = –)	-545	-163	-289	-288	-60	-232	-279	-289
Of which: gross reserve change	-545	61	-288	-288	-60	-232	-279	-289
Memorandum items:								
Coffee export volume (millions of 60-kg. bags)	3.0	3.2	3.3	3.3	3.4	3.6	3.8	4.0
Coffee price (U.S. cents per kg.)	192	178	160	180	179	180	182	183
Net donor support	708	803	1,137	987	786	982	944	941
Of which: budget support	235	342	410	452	226	230	214	214
project support	401	523	556	369	608	814	814	814
total HIPC debt relief	51	48	68	57	66	65	67	69
Residual inflows (after trade and official flows)	1,309	1,164	1,169	1,070	1,304	1,448	1,565	1,714

Sources: Ugandan authorities; and IMF staff estimates and projections.

[1] Fiscal year begins on July 1.

Table 5. Uganda: Quantitative Assessment Criteria and Indicative Targets for December, 2009 [1]
(Cumulative change from the beginning of the fiscal year, unless otherwise stated) [2]

	December 30 2009 [3]		
	Prog.	Adj. Prog.	Actual
Assessment criteria			
Ceiling on the increase in net domestic assets of the Bank of Uganda (NDA) [3]	187	288	121 ✓
Ceiling on the increase in net claims on the central government by the banking system (NCG) [3]	-59	62	-64 ✓
Ceiling on the stock of external payments arrears incurred by the government or the Bank of Uganda	0	0	0 ✓
Ceiling on new nonconcessional external borrowing with maturities greater than one year contracted or guaranteed by the government or the Bank of Uganda [4,5]			
Karuma hydropower plant	400	400	0 ✓
JBIC loan guarantee to Phenix textile factory	6	6	3 ✓
Other	0	0	0 ✓
Ceiling on new external debt with maturity up to one year contracted or guaranteed by the government or the Bank of Uganda [4,6]	0	0	0 ✓
Minimum increase in net international reserves of the Bank of Uganda (US$ mn)	263	210	241 ✓
Indicative target			
Ceiling on the increase in base money liabilities of the Bank of Uganda (BM) [3]	261	261	210 ✓
Stock of domestic budgetary arrears under the Commitment Control System (CCS) [7]	…	…	…
Minimum expenditures under the Poverty Action Fund (including the Universal Primary Education component of development expenditure)	537	537	586 ✓

[1] The assessment criteria and indicative targets under the program, and their adjusters, are defined in the TMU.
[2] Fiscal year begins on July 1.
[3] Cumulative changes are from June 2009 (averages for NDA and BM) as defined in the TMU.
[4] Continuous assessment criterion.
[5] Cumulative change from December 1, 2006.
[6] Excluding normal import-related credits.
[7] Arrears incurred after end-June 2004. Excludes new arrears accumulated during the current fiscal year.

Table 6. Uganda: Structural Benchmarks[1]

Policy Measure	Date of Implementation
Structural Benchmarks	
Implement pilot Integrated Personnel and Payroll System in four Commissions (Public Service Commission, Health Service Commission, Education Service Commission and Judicial Service Commission), Ministries (Ministry of Finance, Ministry of Health, Ministry of Public Service, Ministry of Education, Judiciary (Courts and Judicature)), and Local Governments (Lira and Jinja Districts).	End-September 2010
Submit to Parliament draft regulatory framework for pension funds.	End-June 2010

[1] Benchmarks also apply on a continuous basis to the standard provisions on the exchange and trade issues that apply to programs supported by the Fund's financial resources.

Table 7. Selected Banking System Indicators, 2006–09

	Dec-06	Jun-07	Dec-07	Jun-08	Dec-08	Jun-09	Dec-09
Return on equity	28.3	31.5	31.4	26.6	25.0	24.3	18.7
Return on Assets	3.4	3.9	3.9	3.4	3.5	3.7	2.9
Non interest income to gross income	30.6	32.0	33.0	31.4	31.9	30.5	30.3
Non interest expenses to operating expenses	75.3	72.7	69.2	68.4	69.7	72.6	69.1
Regulatory capital to risk weighted assets	16.5	18.7	17.8	19.1	18.7	19.3	18.7
Shareholders equity to total assets	11.9	12.8	12.4	13.2	15.2	15.0	15.8
Non performing loans to total advances	2.9	3.4	4.1	4.1	2.2	4.0	4.2
Earning assets to total assets	78.5	77.8	79.2	80.5	78.0	78.8	77.7
Loan loss provisions to non performing loans	74.4	69.3	71.8	73.3	120.3	71.9	79.8
Sectoral concentration of loans							
Government	0.1	0.0	0.0	0.6	0.1	0.1	0.1
Agric	6.8	6.9	6.9	6.0	6.9	4.5	5.2
Mining & Quarrying	0.3	2.5	2.5	0.4	0.8	0.3	0.2
Manufacturing	15.9	14.6	14.6	12.3	14.2	15.2	12.8
Trade & Commerce	15.6	16.1	16.1	12.2	18.2	20.6	21.6
Transport	7.7	6.7	6.7	7.7	6.9	6.4	8.1
Building	5.6	6.4	6.4	9.7	10.9	11.4	9.9
Other services	48.0	46.9	46.9	51.2	42.0	41.5	42.1

APPENDIX I. LETTER OF INTENT

Kampala, Uganda
April 25, 2010

Mr. Dominique Strauss Kahn
Managing Director
International Monetary Fund
Washington, DC 20431

Dear Mr. Strauss Kahn:

On behalf of the Government of Uganda, I wish to provide you with an update on the progress we have made under our program backed by the IMF's Policy Support Instrument (PSI). Further, I would like to request continued cooperation through a new three-year PSI.

Performance under the PSI through the 7th review has remained strong and all end-December assessment criteria have been met. Our strong policy framework enabled us to limit the impact of the global financial crisis on our economy. Growth has slowed but remains robust and is set to recover quickly, and inflation has been kept under control. Although there have been some delays in reforms, particularly in public financial management, we have made advances in other areas and we remain committed to strengthening the structural reform agenda.

We recently launched our National Development Plan (NDP) aimed at sustaining long-term economic growth, promoting economic transformation and wealth creation. To better align program targets with our medium-term development plans, the Government of Uganda wishes that the current PSI be canceled immediately upon conclusion of the seventh review, and that a new three-year PSI commence immediately thereafter.

The attached Memorandum of Economic and Financial Policies (MEFP) sets out the Government's objectives and policies derived from our NDP. Specific emphasis is placed on infrastructure investment to address critical constraints to growth in a coherent and consistent framework. The new PSI also seeks to rejuvenate the structural reform agenda.

The Government of Uganda believes that the policies set forth in the attached MEFP are adequate to achieve the objectives of our PSI-supported program but will take any further measures that may become appropriate for this purpose. We stand ready to work with the Fund and other development partners in the implementation of our program and will consult in advance should revisions be contemplated to the policies contained in the PSI.

The Government of Uganda authorizes publication of this letter, its attachments, and all reports prepared by IMF staff for the 7th review under the PSI and the request for a new PSI.

Sincerely,

/s/

Ms. Syda Bbumba
Minister, Ministry of Finance, Planning, and Economic Development

cc: The Governor, Bank of Uganda

ATTACHMENT 1. UGANDA: MEMORANDUM OF ECONOMIC AND FINANCIAL POLICIES

April 25, 2010

I. INTRODUCTION

Purpose of MEFP

1. The Government of Uganda (GOU) requests a new Policy Support Instrument (PSI) for the period 2010 to 2013, to be aligned with the recently-adopted National Development Plan (NDP). The NDP, which covers the period 2010/11-2014/15, identifies four priority objectives: human resource development through health and education; eliminating infrastructure bottlenecks to growth, particularly in energy and transportation; supporting science, technology and innovation, and facilitating private access to critical inputs to production, especially in agriculture. Economic policies under the new PSI will also be framed to be consistent with the requirements of the transition to a monetary union in East Africa.

2. This memorandum outlines the performance of the economy in the first half of 2009/10, discusses the projections and policy stance for the remainder of the fiscal year and then sets out the policy objectives for the 2010/11 fiscal year and the medium-term.

Performance under the PSI

3. All of the six quantitative assessment criteria for end-December 2009 were met, as were the two indicative targets. Both structural benchmarks under the PSI have 2010 deadlines which Government expects to meet.

II. ECONOMIC AND POLICY DEVELOPMENTS

Outturn in the first half 2009/10

4. There have been indications of slowdown of real GDP growth in H1 2009/10 because of drought in the first quarter of 2009/10, and delays in the implementation of government spending. Core consumer price inflation fell sharply in H1 2009/10, from an annual rate of 11 percent in June 2009 to 7.4 percent in December 2009, because of the slow growth in consumer spending and the exchange rate appreciation in the first half of the year. A sharp rise in food crop prices in Q1 2009/10, attributable to the drought, drove up annual headline consumer price inflation from 12.3 percent in June 2009 to 14.6 percent in September 2009, but the recovery in food supply in the second quarter together with the continued fall in core inflation brought down headline inflation to 11 percent in December 2009.

5. The fiscal stance in H1 2009/10 was tighter than programmed because of delays in implementing public expenditures, especially capital expenditures. Total expenditures were Shs 246 billion lower than budgeted in H1. Revenues underperformed by Shs 85 billion, on account of the weakness in import growth. There was, however, an over performance in several direct and indirect domestic tax handles, including excise taxes and VAT on domestic goods, as a result of stronger enforcement efforts by the Uganda Revenue Authority.

6. Monetary growth was lower than projected in H1 2009/10, reflecting weak money demand as a result of subdued private sector consumption. Reserve money was 2.4 percent lower than programmed. To stimulate stronger private spending, the Bank of Uganda (BOU) sought to boost liquidity and reduce interest rates, with the yields on 364 day Treasury Bills falling from 14 percent in June 2009 to 9 percent in December 2009. The fall in securities yields, alongside lower money market rates, reflected both the stance of monetary policy and falling inflationary expectations. However, thus far lending rates have only declined marginally, reflecting market rigidities and a tightening in lending standards.

7. The BOP, which had recorded an overall deficit in 2008/09, improved in the first half of 2009/10, with an overall surplus leading to a net accumulation of international reserves of US$ 93 million. The improvement in the BOP, which was due to weaker import growth and a recovery of foreign investment, led to an appreciation of the nominal exchange rate, which on a trade weighted basis, appreciated by 8.2 percent between June and December 2009.

Projections for the second half of 2009/10

8. Aggregate demand is projected to pick up in H2 2009/10, boosted by recovery of consumer demand and a more rapid implementation of budgeted public expenditures. This is expected to result in real GDP growth for the fiscal year of 5.6 percent, 0.7 percentage points lower than had been programmed. Despite the recovery in H2, output will remain below potential and hence inflationary trends are expected to remain subdued. Although monthly core inflation will begin to accelerate in H2 in line with consumer demand (from around zero at the end of H1), annual core inflation is projected to decelerate to 3.9 percent in June 2010. Annual headline inflation is projected at 5 percent in June 2010.

9. The fiscal outturn for 2009/10 is projected to be slightly less expansionary than projected at the time of the 6th Review, largely due to the underperformance of development expenditures (by 1.6 percent of GDP).This is for two reasons. First, reallocations from capital expenditures to current spending, including increased provision for pension payments, and for emergency spending and road maintenance through supplementary appropriations, will raise current expenditures above programmed levels by 0.5 percent of GDP. Secondly, expenditures amounting to 0.5 percent of GDP, mainly pertaining to roads projects, will be implemented from budgetary resources carried forward from the previous fiscal year. Revenues are projected to underperform but only by 0.3 percent of GDP. With grants being approximately in line with programmed levels, the overall fiscal deficit, both including and

excluding grants, is projected to be lower than programmed by 0.2 percent of GDP and 0.3 percent of GDP, at 2.3 percent and 4.7 percent of GDP, respectively. The fiscal deficit is projected to be financed by net external borrowing of 2.0 percent of GDP and net domestic financing of 0.3 percent of GDP, the latter being 0.2 percent of GDP higher than programmed.

10. Monetary policy will continue to be cautiously accommodative. Money demand is projected to pick up in H2, lifting annual broad money growth for the fiscal year to 19.3 percent and reserve money growth to 19.1 percent. Private sector credit is projected to grow at 17.1 percent in 2009/10.

11. The BOP is projected to record an overall surplus of US$ 291 million in 2009/10, in line with the programmed level. The current account deficit is projected to widen as a percentage of GDP, from 4.8 percent in 2008/09 to 5.3 percent in 2009/10, despite a lower trade deficit, because of higher services and lower official transfers.

Economic Policies for 2010/11

12. The main objective of macroeconomic policy in 2010/11 will be to support demand while maintaining macroeconomic stability. In this context, policies will aim to raise output back towards its potential level (with potential real growth estimated at 6-7 percent per annum) while maintaining core inflation at a maximum of 5 percent (barring exogenous shocks to inflation) and running a BOP surplus to accumulate international reserves. The authorities are mindful that, in an election year, private sector expenditure may increase more quickly than programmed and hence will exercise caution in implementing monetary and fiscal policies. A projected worsening of the external terms of trade will also constrain the scope for macroeconomic policy to support growth in 2010/11. On balance, real GDP growth is projected to rise to 6.4 percent in 2010/11 on the heels of a recovery in domestic demand.

Fiscal Policy

13. The fiscal strategy for 2010/11 and the medium term centers on the implementation of the capital projects and social programs in the NDP in order to boost real growth and reduce poverty. This will require the creation of fiscal space for higher public investments by curtailing growth in recurrent spending on non-productive activities. To ensure that the medium-term fiscal strategy is implemented effectively, a key goal of the 2010/11 budget is to remedy the absorption constraints in the execution of government programs through deployment of external technical assistance on contracting and procurement, and training of accounting officers on preparation of work plans, execution and reporting.

14. The fiscal balance in 2010/11 is projected to be roughly similar to the projected outturn in 2009/10, with an overall deficit excluding grants of 5 percent of GDP. Expenditure and net lending is expected to increase by 0.9 percent of GDP in 2010/11 from the outturn in 2009/10, as absorption of available resources for development expenditure improves; while

revenue is projected to increase by about ½ percent of GDP. To generate increased budget resources for allocation to priority public investments, including infrastructure, the authorities are committed to strengthening domestic revenue mobilization. However, due to the limited options with respect to new sources of tax revenue in the near term, efforts to increase revenue will focus on improving enforcement and the collection of non-tax revenues. In addition, the authorities will undertake and publish a review which costs the revenue loss and assesses the effectiveness of all existing tax holidays and exemptions, and formulate recommendations to Cabinet for their streamlining before end-June 2010.

Monetary policy

15. Monetary policy in 2010/11 will aim at supporting economic growth while being mindful of potential pressures on inflation. The operation of the BOU's monetary policy will continue to be based on the flexible implementation of the reserve money program which was developed with TA from the Fund. The BOU will review its quantitative targets for monetary aggregates on a monthly basis, taking into account the latest available macroeconomic data, and intervene on a daily basis with repos and reverse repos to ensure stability in the money markets. The intermediate target for broad money growth, which is provisionally set at 13.7 percent for 2010/11, takes into account the projected growth of potential real output, the BOU's inflation target and the projected fall in velocity of circulation. The monetary program for 2010/11 will be designed to provide room for bank lending to the private sector to grow at the same pace as nominal GDP. To enhance the efficacy of monetary policy, the BOU will develop a set of high frequency indicators designed to capture activity and demand in the formal sector of the economy by March 2011.

External Sector

16. With the external environment expected to be less favorable in 2010/11, the BOP is projected to record only a modest overall surplus of US$ 60 million in 2010/11. The exchange rate will continue to be flexible with the BOU intervening only to dampen volatility and to avoid significant misalignments arising from external capital flows.

Financial sector policies

17. The banking system remains financially sound, with aggregate tier 1 capital to risk weighted assets of 20 percent, well above the statutory minimum of 12 percent. However the BOU is concerned that the minimum paid up capital required to open and operate a bank is no longer sufficient to support new entrants in the more competitive banking markets which now prevail in Uganda, as well as being out of line with regional minimum requirements. Therefore Government intends to introduce amendments to the Financial Institutions Act (FIA) in Parliament to raise the minimum paid up capital for a bank during 2010/11. Furthermore, amendments to the FIA will also be introduced to allow commercial banks to offer insurance and Islamic banking products to their customers. The rationale of these

amendments is to improve the efficiency of banking and broaden the range of financial service products available to the public.

18. Government will prepare and implement a comprehensive strategy to deepen and diversify the financial markets. A detailed strategy, drawing on the ongoing work by the Financial Markets Development Committee Secretariat, will be prepared by June 2011 and will be included in the midterm review of the NDP. The strategy will cover all of the required reforms to the legal and institutional framework for the financial markets. The strategy will be coordinated with Uganda's EAC partner states to ensure that the legal and institutional framework is consistent with the adoption of a common market in East Africa.

19. The credit reference bureau has commenced operations, and is expected to become fully operational in the 2010/11 fiscal year. Government will also establish a Small Commercial Claims Court to speed up the resolution of small business disputes.

20. The BOU intends to strengthen the regulation of deposit taking microfinance institutions, by bringing under aegis of the Microfinance Deposit Taking Institutions Act the larger savings and credit unions (SACCOs) which are currently unregulated.

III. Medium Term Policies

21. The macroeconomic strategy for the medium term will continue to focus on maintaining a sound fiscal policy that allows Government to invest in the public infrastructure which is critical to alleviate the binding constraints to economic growth, while at the same time ensuring macroeconomic stability. To achieve this, Government aims to create fiscal space by raising the revenue to GDP ratio from the current level of about 12.5 percent to over 14 percent during the medium-term, through a combination of measures to broaden the tax base and improve tax administration.

22. Government has taken the initial step to establish the National Identification system for movement of persons within the East African community; this will also help to improve tax administration and broaden the tax base by bringing informal sector activity into the tax net. To achieve this objective, Government has procured an external firm to undertake the identification exercise.

23. Government will strengthen the prioritization of public spending and improve value for money through the implementation of efficiency measures, which aim to link public spending more closely to outputs. Public expenditure is projected to increase from 17.2 percent of GDP in 2009/10 to an average of 18.8 percent of GDP per year and a fiscal deficit (excluding grants) of 4.9 percent of GDP per year on average over the NDP period. The NDP prioritizes public investments that facilitate regional integration. To leverage private sector financing and expertise, some of the priority projects in the NDP will be executed through public-private partnerships (PPPs). Government is finalizing a PPP policy framework and

institutional arrangements to enhance the capacity of Government to analyze PPP proposals and allocate risks appropriately will be finalized during FY 2010/11.

24. Although Government will continue to rely mainly on concessional financing, it may occasionally need to mobilize nonconcessional funds to cover shortfalls in project financing and to finance its share in the equity in PPPs. Therefore, Government requests the IMF to maintain the ceiling for non-concessional borrowing at US$ 500 million in the next PSI. Government aims at using such nonconcessional resources exclusively for the financing of investment expenditures, including the Karuma hydropower dam and other high-yield infrastructure projects. In addition, Government is considering participation in regional projects to boost transportation infrastructure in the EAC, and may require an increase in the ceiling on nonconcessional borrowing to finance its share of such projects in due course.

IV. STRUCTURAL REFORMS

25. Government is advancing reforms in the pension sector. The Retirement Benefits Authorities Bill was approved by Cabinet in December 2009, together with the policy on liberalizing the sector. It is expected that the Bill will be submitted to Parliament by end-August 2010, and the new regulator put in place by 2011. Government will request technical assistance from the IMF to undertake an actuarial evaluation of the NSSF to determine its financial viability.

26. Government continues to accumulate domestic expenditure arrears, which weakens the credibility of the budget system. The Ministry of Finance, Planning and Economic Development has undertaken a verification exercise of the newly accumulated arrears during FY 2008/09, which revealed a substantial increase in non-pension arrears. Therefore, Government is implementing the following measures to curtail the accumulation of new arrears:

(i.) accounting officers will be required to provide a detailed account of how the arrears came about, and this information will be used in any independent investigation;

(ii.) all new non-statutory arrears will raise an automatic audit query and will be subjected to scrutiny by the Public Accounts Committee (PAC) of Parliament;

(iii.) the quarterly releases to spending agencies will be adjusted downwards by the magnitude of the new accumulated non-statutory arrears, starting with Q4 of fiscal year 2009/10;

(iv.) arrears will have a first call on spending agencies' resources for next fiscal year;

(v.) the "straight-through payment" system (STP) now employed for pensions will be extended to the utility sector (electricity, water, telephone, and rental payments) by July 2010; and,

(vi.) mandatory rotation of accountants and procurement officers will start July 2010, and a report on the implementation of this rotation will be completed by end-December 2010.

In addition, the Directorate of Budget of the MoFPED will undertake by end-July 2010 a review of the annual utility services consumed by government departments to ensure adequate resources are provided for.

27. Government recognizes that budgetary carry forward procedures are less rigorous than would be desirable and could pose a potential risk of abuse. Therefore, Government is taking measures to eliminate the scope for diverting budgetary funds which remain unspent at end of the fiscal year, but which, under the Public Finance and Accountability Act (PFAA), can be spent in the first quarter of the next fiscal year (beyond which time they must be returned to the Government Consolidated Fund). These measures include: (i) publishing the balances as at June 30 and September 30 of each calendar year on all government accounts at the BOU and commercial banks; (ii) the Minister responsible for Finance will present these accounts to Parliament by July 31 and October 30 of the following fiscal year; (iii) in order to spend any balances held over from the previous fiscal year beyond end-June, parliamentary approval as well as supporting work and procurement plans showing how such funds would be utilized will be required; (iv) all unspent balances which have not been re-appropriated by Parliament by end-September must be returned to the Government Consolidated Fund. Government will propose amendments to the PFAA and other relevant laws and regulations to support these measures. In the meantime, Government will undertake an inventory of existing accounts and immediately close those which are no longer justified by a current project or legitimate activity by end-December 2010. Related to this, Government will be seeking technical assistance from the Fund to assist in amending the PFAA and other relevant regulations in accordance with international best practices.

28. The implementation of the first phase of the Integrated Personnel and Payroll System (IPPS) has started with the procurement of the main contractor in October 2009, training of staff, establishment of a data centre in the Ministry of Public Service (MoPS) which also includes updating the Establishment register, job description and specification for the IPPS sites. This phase, which is scheduled to be completed by September 2010, will cover four commissions (public service, health service, education service, and judicial service), four ministries (Finance planning and economic development, Health, Public service, Education, and Judiciary (courts and judicature)), and two local governments (Lira and Jinja).

29. Government will ensure that the management of petroleum revenues is handled in a transparent manner that does not undermine the integrity of the budget framework, and that

large, volatile petroleum revenues do not endanger macroeconomic stability. And, through amendments to the PFAA, Government will strengthen the institutional and regulatory framework for petroleum revenue management ahead of the start of commercial production. Furthermore, Government requests the IMF to prepare and publish a revised *Report on the Observance of Standards and Codes* **(***ROSC), to* provide an updated assessment of Uganda's fiscal governance.

Program Monitoring

30. Progress in the implementation of the policies under this program will be monitored through assessment criteria (ACs), indicative targets (IT), and structural benchmarks (SBs) detailed in the attached Tables 1 and 2 and through semiannual reviews. Assessment criteria are proposed for end-June 2010 and end-December 2010, to be monitored respectively at the first and second reviews. The first review is expected to be completed by end-December 2010 and the second review by end-June 2011. The attached Technical Memorandum of Understanding—which is an integral part of this Memorandum—contains definitions and adjustors. During the program period we will refrain from imposing or intensifying exchange restrictions as well as restrictions on imports for balance of payments reasons, and from introducing or modifying multiple currency practices.

Table 1. Uganda: Quantitative Assessment Criteria and Indicative Targets for June 2010 - June 2011 [1]
(Cumulative change from the beginning of the fiscal year, unless otherwise stated) [2]

	June 30 2010	Sep. 30 2010 3	Dec. 31 2010	March 31 2011 3	June 30 2011 3
	Prog.	Prog.	Prog.	Prog.	Prog.
Assessment criteria	(Billions of Uganda shillings)				
Ceiling on the increase in net domestic assets of the Bank of Uganda [4]	252	54	144	181	221
Ceiling on the increase in net claims on the central government by the banking system [4]	94	31	82	103	123
	(Millions of U.S. dollars unless otherwise specified)				
Ceiling on the stock of external payments arrears incurred by the public sector [5]	0	0	0	0	0
Ceiling on the contracting or guaranteeing of new nonconcessional external debt with maturities greater than one year by the public sector [5] [6]	500	500	500	500	500
Ceiling on new external debt with maturity up to one year contracted or guaranteed by the public sector [5] [7]	0	0	0	0	0
Minimum increase in net international reserves of the Bank of Uganda (US$mn)	288	18	36	49	60
Indicative target	(Billions of Uganda shillings)				
Ceiling on the increase in base money liabilities of the Bank of Uganda [4]	373	89	213	274	335
Stock of domestic budgetary arrears under the Commitment Control System (CCS) [8]	51				51
Minimum expenditures under the Poverty Action Fund (including the Universal Primary Education component of development expenditure)	1,097.0	160.0	579.0	883.0	1,184.8

[1] The assessment criteria and indicative targets under the program, and their adjusters, are defined in the technical memorandum of understanding (TMU).
[2] Fiscal year begins on July 1.
[3] Indicative targets.
[4] Cumulative changes are from June 2009 (averages for NDA and BM) for June 2010 targets and from June 2010 for FY 2010 11 targets, as defined in the TMU.
[5] Continuous assessment criterion.
[6] To be used exclusively for infrastructure investment projects. Cumulative change from May, 2010.
[7] Excluding normal import-related credits.
[8] Monitored annually.

Table 2. Uganda—Structural Benchmarks for the First Year Under the New PSI (2010-13)		
Policy Measure	**Date of Implementation**	**Macroeconomic rationale**
Fiscal Sector		
Complete and publish a review of existing tax holidays and exemptions and formulate and submit to Cabinet recommendations for their streamlining (¶14)	June 30, 2010	Strengthen revenue mobilization
Extend the “straight-through payment” system (STP) now employed for pensions to the utility sector (electricity, water, telephone, and rental payments) (¶26)	July 31, 2010	Help control accumulation of arrears
Implement pilot Integrated Personnel and Payroll System (IPPS) in four (4) commissions four (4) ministries, judiciary (courts and judicature) and two (2) local governments (¶28)	September 30, 2010	Strengthen oversight and control of public payroll
Report on the implementation of mandatory rotation of accountants and procurement officers (¶26)	December 31, 2010	Help control accumulation of arrears
Undertake an inventory of existing government accounts and close immediately those which are no longer justified by a current project or legitimate activity (¶27)	December 31, 2010	Enhance transparency and monitoring of public finances
Financial Sector		
Submit the Retirement Benefits Authorities Bill to parliament (¶25)	August 31, 2010	Encourage development of long-term savings
Other		
Develop a set of high frequency indicators designed to capture activity and demand in the formal sector of the economy (¶15)	March 31, 2011	Enhance macroeconomic information

Attachment II. Uganda: Technical Memorandum of Understanding

A. Introduction

1. This memorandum defines the targets described in the memorandum of economic and financial policies (MEFP) for the May 2010-May 2013 financial program supported by the IMF Policy Support Instrument (PSI), and sets forth the reporting requirements under the instrument.

B. Ceiling on the Cumulative Increase in Net Domestic Assets (NDA) of the Bank of Uganda (BOU)

2. The net foreign assets of the BOU are defined as the monthly average (based on daily data) of foreign assets minus foreign liabilities, and include all foreign claims and liabilities of the central bank. The monthly average values of all foreign assets and liabilities will be converted into U.S. dollars at each test date using the average cross exchange rates for October 2009 for the various currencies and then converted into Uganda shillings using the average U.S. dollar-Uganda shilling exchange rate for October 2009.

Program Exchange Rates (US$ per currency unit, unless indicated otherwise)	
Euro	1.48164
British pound	1.61854
Japanese Yen	0.011066
Kenya shilling	0.01329
SDR	1.5896
Uganda shilling (per US$1)	1898.28

Net domestic assets (NDA) of the Bank of Uganda (BOU) are defined as the monthly average (based on daily data) of base money (defined below) less net foreign assets of the BOU (as defined in para. 2). Based on this definition, the NDA limits will be ceilings on the cumulative changes from the monthly average based on daily data for June 2009 to the same monthly average for June 2010, and cumulative changes from the monthly average based on daily data for June 2010 to the same monthly average for September, and December 2010.

(In billions of shillings)			
	June 30, 2010,	September 30, 2010	December 31, 2010
Cumulative change in base money	373	89	213
Cumulative change in NFA	121.4	34.3	69.2
Cumulative change in NDA	251.6	54	143.8

B. Base Money

3. Base money is defined as the sum of currency issued by Bank of Uganda (BOU) and the commercial banks' deposits in the BOU. The commercial bank deposits include the statutory required reserves and excess reserves held at the BOU and are net of the deposits of closed banks at the BOU and Development Finance Funds (DFF) contributed by commercial banks held at the BOU. The base money limits will be cumulative changes from the monthly average based on daily data for June 2009 to the same monthly average for June 2010, and cumulative changes from the monthly average based on daily data for June 2010 to the same monthly average for September 2010, and December 2010.

C. Ceiling on the Cumulative Increase in Net Claims on the Central Government by the Banking System[1]

4. Net claims on the central government (NCG) by the banking system is defined as the difference between the outstanding amount of bank credits to the central government and the central government's deposits with the banking system, excluding deposits in administered accounts and project accounts with the banking system, including the central bank. Credits comprise bank loans and advances to the government and holdings of government securities and promissory notes. Central government's deposits with the banking system include the full amount of resources freed by the IMF MDRI. NCG will be calculated based on data from balance sheets of the monetary authority and commercial banks as per the monetary survey. The quarterly limits on the change in NCG by the banking system will be cumulative beginning end-June in the previous fiscal year.

[1] The central government comprises the treasury and line ministries.

D. Floor on Net International Reserves of the Bank of Uganda

5. Net international reserves (NIR) of the BOU are defined for program monitoring purpose as reserve assets of the BOU net of short-term external liabilities of the BOU. Reserve assets are defined as external assets readily available to, and controlled by, the BOU and exclude pledged or otherwise encumbered external assets, including, but not limited to, assets used as collateral or guarantees for third-party liabilities. Short-term external liabilities are defined as liabilities to nonresidents, of original maturities less than one year, contracted by the BOU and include outstanding IMF purchases and loans.

6. For program-monitoring purposes, reserve assets and short-term liabilities at the end of each test period will be calculated in U.S. dollars by converting them from their original currency denomination at program exchange rates (as specified in para 2).

E. Ceiling on the Stock of Domestic Budgetary Arrears of the Central Government

7. The stock of domestic payment arrears under the Commitment Controls System (CCS) will be monitored on an annual basis. Domestic payments arrears under the CCS are defined as the sum of all bills that have been received by a central government spending unit or line ministry delivered prior to the beginning of the current fiscal year, and for which payment has not been made by end of fiscal year, under the recurrent expenditure budget (excluding court awards, subscription to international organization and pensions) or the development expenditure budget. For the purpose of program monitoring, the CCS reports, which will include arrears accumulated at IFMS and non-IFMS sites, prepared by the Accountant General, will be used to monitor arrears. Arrears can be cleared in cash or through debt swaps. According to the verified report prepared by the Accountant General, this stock of arrears, incurred after end-June 2004, is estimated at USh 99 billion as of June 2009.

F. Expenditures under the Poverty Action Fund (PAF).

8. The compliance with the indicative target on minimum expenditures under the PAF will be verified on the basis of releases (PAF resources made available to spending agencies).

G. Adjusters

9. The NDA and NIR targets are based on program assumptions regarding budget support, assistance provided under the Heavily Indebted Poor Countries (HIPC) Initiative and the Multilateral Debt Relief Initiative (MDRI), and external debt-service payments.

10. The NCG target, in addition to being based on the aforementioned assumptions, is also based on assumptions regarding domestic nonbank financing of central government fiscal operations. In addition, the NDA target depends on the legal reserve requirements on deposits in commercial banks. Finally, the NDA and NIR targets are based on program

assumptions regarding automatic access by commercial banks to the BOU's rediscount and discount window facilities.

11. The Uganda shilling equivalent of budget support (grants and loans) plus HIPC Initiative assistance in the form of grants on a cumulative basis from July 1 of the fiscal year is presented under Schedule A. The ceilings on the cumulative increase in NDA and NCG will be adjusted downward (upward), and the floor on the cumulative increase in NIR of the BOU will be adjusted upward (downward) by the amount by which budget support, grants and loans, plus HIPC Initiative and MDRI assistance, exceeds (falls short of) the projected amounts.

Schedule A: Budget Support Plus Total HIPC Initiative Assistance

(Cumulative billions of Uganda's shillings, beginning July 1 of the fiscal year)

Quarter	June 30, 2010	September 30, 2010	December 31, 2010
Budget support, including HIPC Initiative grants	991.3	105	389.5

12. The ceiling on the increases in NDA and NCG will be adjusted downward (upward) and the floor on the increase in NIR will be adjusted upward (downward) by the amount by which debt service due[2] plus payments of external debt arrears less deferred payments (exceptional financing) falls short of (exceeds) the projections presented in Schedule B. Deferred payments are defined to be (i) all debt service rescheduled under the HIPC Initiative; and (ii) payments falling due to all non-HIPC Initiative creditors that are not currently being serviced by the authorities (that is, gross new arrears being incurred).

Schedule B: Debt Service

(Cumulative billions of Uganda shillings, beginning July 1 of the fiscal year)

Quarter	June 30, 2010	September 30, 2010	December 31, 2010
Debt service due before HIPC, excluding exceptional financing	207	57	121

[2] Debt service due is defined as pre-HIPC Initiative debt service due, but from 2003/04 onwards, this excludes debt service subject to HIPC Initiative debt rescheduling.

13. The ceiling on the increase in NCG will be adjusted downward (upward) by any excess (shortfall) in nonbank financing[3] less payment of domestic arrears on pensions, to international organizations, and court awards, relative to the programmed cumulative amounts presented in Schedule C. For the purpose of this adjuster, payment of such arrears cannot exceed the programmed amount by more than Ush 45.0 billion.

Schedule C: Nonbank Financing Minus Repayment of Domestic Arrears

(Cumulative billions of Uganda shillings, beginning July 1 of the fiscal year)

Quarter	June 30, 2010	September 30, 2010	December 31, 2010
(A) Nonbank financing	0	100	100
(B) Repayment of domestic arrears on pensions, to international organizations, and for court awards	76.1	52	105.4
(C) Total = (A) –(B)	-76.1	48	-5.4

14. The ceiling on NDA of the BOU for every test date will be adjusted upward by the daily average amount of commercial bank automatic access to the BOU discount window and rediscounting of government securities by commercial banks.

15. The ceiling on NDA of the BOU for every test date will be adjusted downward/upward to reflect decreases/increases in the legal reserve requirements on deposits in commercial banks. The adjuster will be calculated as the percent change in the reserve requirement multiplied by the actual amount of required reserves (Uganda shillings and foreign-currency denominated) at the end of the previous calendar month.

H. Ceiling on the Contracting or Guaranteeing of New Nonconcessional External Debt by the Public Sector, and Ceiling on the Stock of External Payments Arrears Incurred by the Public Sector[4]

16. The assessment criterion on short-term debt refers to contracting or guaranteeing external debt with original maturity of one year or less by the public sector. Excluded from

[3] Comprising the check float and the change in government securities and government promissory notes held by the nonbank sector. The change in government securities held by the nonbank sector will be calculated from the data provided by the Central Depository System (CDS).

[4] Public sector comprises the general government (which includes the central government, local governments, and monetary authorities), and entities that are public corporations which are subject to 'control by the government', defined as the ability to determine general corporate policy or by at least 50 percent government ownership.

this assessment criterion are normal import-related credits and non-resident holdings of government securities and government promissory notes. The definition of "debt" is set out in paragraph 18.

17. The program includes a ceiling on new nonconcessional borrowing with maturities greater than one year contracted or guaranteed by the public sector.[5] Nonconcessional borrowing is defined as loans with a grant element of less than 35 percent, calculated using average commercial interest rates references (CIRRs) published by the Organization for Economic Cooperation and Development (OECD). In assessing the level of concessionality, the 10-year average CIRRs should be used to discount loans with maturities of at least 15 years, while the 6-month average CIRRs should be used for loans with shorter maturities. To both the 10-year and 6-month averages, the following margins for differing payment periods should be added: 0.75 percent for repayment periods of less than 15 years; 1 percent for 15–19 years; 1.15 percent for 20–25 years; and 1.25 percent for 30 years or more. The ceiling on nonconcessional external borrowing or guarantees is to be observed on a continuous basis. The coverage of borrowing includes financial leases and other instruments giving rise to external liabilities, not only current as defined below, but also contingent, on nonconcessional terms. External debt for the purpose of this assessment criterion means borrowing giving rise to liabilities to non-residents. Excluded from the limits are changes in indebtedness resulting from non-resident holdings of government securities and government promissory notes, refinancing credits and rescheduling operations, and credits extended by the IMF. For the purposes of the program, arrangements to pay over time obligations arising from judicial awards to external creditors that have not participated in the HIPC Initiative do not constitute nonconcessional external borrowing. Excluded from these limits are also nonconcessional borrowing within the limits specified in Table 1 of the MEFP.

18. The definition of debt, for the purposes of the limit, is set out in point 9 of the Guidelines on Performance Criteria with Respect to External Debt (Executive Board's Decision No. 6230-(79/140), as amended by Decision No 14416-(09/91, effective December 1, 2009). It not only applies to the debt as defined in Point 9 of the Executive Board decision, but also to commitments contracted or guaranteed for which value has not been received. The definition of debt set forth in No. 9 of the Guidelines on Performance Criteria with Respect to External Debt in Fund Arrangements reads as follows:

> (a) For the purpose of this guideline, the term "debt" will be understood to mean a current, i.e., not contingent, liability, created under a contractual arrangement through the provision of value in the form of assets (including currency) or services, and which requires the obligor to make one or more payments in the form of assets (including currency) or services, at some future point(s) in time; these payments will discharge the principal and/or interest liabilities incurred under the contract. Debts can take a number of forms, the primary ones being as follows: (i) loans, i.e., advances of money to the obligor by the lender made on the basis of an undertaking that the obligor will repay the funds in the future (including deposits, bonds,

[5] Contracting and guaranteeing is defined as approval by a resolution of Parliament as required in Section 20(3) and 25(3) of the Public Finance and Accountability Act, 2003

debentures, commercial loans and buyers' credits) and temporary exchanges of assets that are equivalent to fully collateralized loans under which the obligor is required to repay the funds, and usually pay interest, by repurchasing the collateral from the buyer in the future (such as repurchase agreements and official swap arrangements); (ii) suppliers' credits, i.e., contracts where the supplier permits the obligor to defer payments until some time after the date on which the goods are delivered or services are provided; and (iii) leases, i.e., arrangements under which property is provided which the lessee has the right to use for one or more specified period(s) of time that are usually shorter than the total expected service life of the property, while the lesser retains the title to the property. For the purpose of the guideline, the debt is the present value (at the inception of the lease) of all lease payments expected to be made during the period of the agreement excluding those payments that cover the operation, repair, or maintenance of the property. (b) Under the definition of debt set out in point 9(a) above, arrears, penalties, and judicially awarded damages arising from the failure to make payment under a contractual obligation that constitutes debt. Failure to make payment on an obligation that is not considered debt under this definition (e.g., payment on delivery) will not give rise to debt.

19. The ceiling on the accumulation of new external payments arrears is zero. This limit, which is to be observed on a continuous basis, applies to the change in the stock of overdue payments on debt contracted or guaranteed by the public sector from their level at end-June 2006. External debt payment arrears consist of external debt service obligations (reported by the Statistics Department of the BOU, the Macro Department of the Ministry of Finance) that have not been paid at the time they are due as specified in the contractual agreements but shall exclude arrears on obligations subject to rescheduling.

I. Monitoring and Reporting Requirements

20. The authorities will inform the IMF staff in writing at least ten business days (excluding legal holidays in Uganda or in the United States) prior to making any changes in economic and financial policies that could affect the outcome of the financial program. Such policies include but are not limited to customs and tax laws (including tax rates, exemptions, allowances, and thresholds), wage policy, and financial support to public and private enterprises. The authorities will similarly inform the IMF staff of any nonconcessional external debt contracted or guaranteed by the government, the BOU, or any statutory bodies, and any accumulation of new external payments arrears on the debt contracted or guaranteed by these entities. The authorities will furnish an official communication to the IMF describing program performance of quantitative and structural assessment criteria and benchmarks within 8 weeks of a test date. The authorities will on a regular basis submit information to IMF staff with the frequency and submission time lag as indicated in Table 1. The information should be mailed electronically to AFRUGA@IMF.ORG .

Attachment II. Table 1. Summary of Reporting Requirements

Reporting institution	Report/Table	Frequency	Submission lag
I. Bank of Uganda	Issuance of government securities.	Weekly	5 working days
	Interest rates on government securities.	Weekly	5 working days
	Operations in the foreign exchange market and daily average exchange rates.	Weekly	5 working days
	Consumer price index.	Monthly	2 weeks
	Balance sheet of the BOU, consolidated accounts of the commercial banks, and monetary survey. The Internal Audit Department (IAD) of the BOU will review the reconciliations of monetary survey data with the financial records and the audited financial statements. Any revisions to monetary survey data, in line with the recommendations of the IMF safeguards mission, will be documented and reconciled with the previous presentation to ensure accurate reporting.	Monthly	4 weeks
	Composition of foreign assets and liabilities of the BOU by currency of denomination.	Monthly	4 weeks
	Statement of (i) cash balances held in project accounts at commercial banks; (ii) total value (measured at issue price) of outstanding government securities from the Central Depository System (CDS); and (iii) the stock of government securities (measured at issue price) held by commercial banks from the CDS.	Monthly	6 weeks
	Summary of (i) monthly commodity and direction of trade statistics; (ii) disbursements, principal and interest, flows of debt rescheduling and debt cancellation, arrears, and committed undisbursed balances—by creditor category; and (iii) composition of nominal HIPC Initiative assistance, disaggregated into grants, flow rescheduling, and stock-of-debt reduction by creditor.	Monthly	6 weeks
	Summary of stock of external debt, external arrears, and committed undisbursed loan balances by creditor.	Quarterly	6 weeks
	Standard off-site bank supervision indicators for deposit money banks.	Quarterly	4 weeks
	Summary table of preliminary program performance comparing actual outcome with adjusted program targets for (i) base money; (ii) net claims on central government by the banking system; (iii) stock of external arrears; (iv) new nonconcessional external borrowing; and (v) net international reserves	Quarterly	5 weeks
	Daily average amount of commercial bank automatic access to the BOU discount window and rediscounting of government securities by commercial banks.	Quarterly	4 weeks

Attachment II. Table 1. Summary of Reporting Requirements (concluded)			
Reporting institution	**Report/Table**	**Frequency**	**Submission lag**
II. Ministry of Finance	Summary of central government accounts. Revenues shall be recorded on a cash basis. Expenditures shall be recorded when checks are issued, except for domestic and external debt-service payments, cash transfers to districts, and externally funded development expenditures. Expenditures on domestic interest will be recorded on an accrual basis and external debt service will be recorded on a commitment basis (i.e., when payment is due). Cash transfers to districts will be recorded as expenditures of the central government when the transfer is effected by the BOU. Expenditures on externally funded development programs will be recorded as the sum of estimated disbursements of project loans and grants by donors, less the change in the stock of government project accounts held at the BOU and domestic commercial banks.	Monthly	6 weeks
	Summary of outstanding stock of verified domestic arrears comprising the stock of CCS/IFMS arrears incurred after end-June 2004.	annually	6 weeks
	Summary of contingent liabilities of the central government. For the purpose of the program, contingent liabilities include all borrowings by statutory bodies, government guarantees, claims against the government in court cases that are pending, or court awards that the government has appealed.	Quarterly	6 weeks
	Detailed central government account of disbursed budget support grants and loans, HIPC support, and external debt service due and paid.	Monthly	4 weeks
	Detailed central government account of disbursed donor project support grants and loans.	Monthly	6 weeks
	Statement on new loans contracted during the period according to loan agreements.	Quarterly	6 weeks
	Updated national accounts statistics (real and nominal) according to UBOS and medium-term projections.	Quarterly	4 weeks

INTERNATIONAL MONETARY FUND

UGANDA

Seventh Review Under the Policy Support Instrument, Request for a New Policy Support Instrument and Cancellation of Current Policy Support Instrument —Informational Annex

Prepared by the African Department
(In consultation with other departments)

April 27, 2010

- **Relations with the Fund.** Describes financial and technical assistance by the IMF and provides information on the safeguards assessment and exchange system. Outstanding Fund credit was SDR 6 million (3.3 percent of quota) at end-March, 2010.

- **Joint Bank-Fund Work Program.** Describes Bank-Fund collaboration through June 2011.

Contents Page

APPENDIX I. UGANDA: RELATIONS WITH THE FUND
(As of March 31, 2010)

I. Membership Status: Joined: September 27, 1963; Article VIII

II. General Resources Account:	**SDR Million**	**%Quota**
Quota	180.50	100.00
Fund holdings of currency	180.51	100.00

III. SDR Department:	**SDR Million**	**%Allocation**
Net cumulative allocation	173.06	100.00
Holdings	143.64	83.03

IV. Outstanding Purchases and Loans:	**SDR Million**	**%Quota**
PRGF Arrangements	6.00	3.32

V. Latest Financial Arrangements:

Type	Date of Arrangement	Expiration Date	Amount Approved (SDR Million)	Amount Drawn (SDR Million)
PRGF	Sep 13, 2002	Jan 31, 2006	13.50	13.50
ESAF/PRGF	Nov 10, 1997	Mar 31, 2001	100.43	100.43
ESAF	Sep 06, 1994	Nov 09, 1997	120.51	120.51

VI. Projected Payments to Fund[1]
(SDR Million; based on existing use of resources and present holdings of SDRs):

	Forthcoming				
	2010	2011	2012	2013	2014
Principal	0.20	1.00	1.20	1.20	1.20
Charges/Interest	0.07	0.08	0.09	0.09	0.09
Total	0.27	1.08	1.29	1.29	1.29

VII. Implementation of HIPC Initiative:

I. Commitment of HIPC assistance	Original Framework	Enhanced Framework	Total
Decision point date	Apr 1997	Feb 2000	
Assistance committed			

[1]When a member has overdue financial obligations outstanding for more than three months, the amount of such arrears will be shown in this section.

by all creditors (US$ Million) [2]	347.00	656.00	
Of which: IMF assistance (US$ million)	68.90	91.00	
(SDR equivalent in millions)	51.51	68.10	
Completion point date	Apr 1998	May 2000	

II. Disbursement of IMF assistance (SDR Million)			
Assistance disbursed to the member	51.51	68.10	119.61
Interim assistance	--	8.20	8.20
Completion point balance	51.51	59.90	111.41
Additional disbursement of interest income [3]	--	2.06	2.06
Total disbursements	**51.51**	**70.16**	**121.67**

VIII. Implementation of Multilateral Debt Relief Initiative (MDRI):

I. MDRI-eligible debt (SDR Million)[4]	87.73
Financed by: MDRI Trust	75.85
Remaining HIPC resources	11.88

II. Debt Relief by Facility (SDR Million)

	Eligible Debt		
Delivery Date	GRA	PRGF	Total
January 2006	N/A	87.73	87.73

[2] Assistance committed under the original framework is expressed in net present value (NPV) terms at the completion point, and assistance committed under the enhanced framework is expressed in NPV terms at the decision point. Hence these two amounts can not be added.

[3] Under the enhanced framework, an additional disbursement is made at the completion point corresponding to interest income earned on the amount committed at the decision point but not disbursed during the interim period.

[4] The MDRI provides 100 percent debt relief to eligible member countries that qualified for the assistance. Grant assistance from the MDRI Trust and HIPC resources provide debt relief to cover the full stock of debt owed to the Fund as of end-2004 that remains outstanding at the time the member qualifies for such debt relief.

IX. Safeguards Assessments

Under the Fund's safeguards policy, assessments with respect to the PSI are voluntary. An update assessment of the Bank of Uganda (BOU) was completed on April 10, 2007 and concluded that the BOU had strengthened its safeguards framework since the 2003 assessment. The main developments included implementation of International Financial Reporting Standards, publication of financial statements, establishment of an audit committee, and strengthening of the internal audit function. Staff made recommendations to address remaining vulnerabilities in the legal and internal control areas.

X. Exchange Rate Arrangement

The official exchange rate is determined on the interbank market for foreign exchange. As of March 31, the official exchange rate was U Sh 2084.4 per U.S. dollar. The exchange system is free of restrictions on the making of payments and transfers for current international transactions. Uganda's exchange rate regime is classified as floating.

XI. Article IV Consultation

The Executive Board concluded the last Article IV consultation on January 7, 2009. The next Article IV consultation with Uganda will be held on the 24-month cycle, subject to the provisions of the decision on consultation cycles approved on July 15, 2002.

In February and April 2001, joint World Bank/Fund missions visited Kampala as part of the Financial Sector Assessment Program (FSAP). A final report was provided to the authorities in November 2001, and an MFD mission discussed the report with the authorities during the Article IV consultation discussion in November 2002; the Financial System Stability Assessment was prepared for Board discussion in February 2003. In November 2004, a joint World Bank/Fund missions visited Kampala for a FSAP update.

XII. Policy Support Instrument (PSI)

Uganda initiated a 16-month PSI with the Fund in January 2006. The 16-month PSI was replaced by a new three-year PSI in December 2006, and extended for an additional year in December 2009.

XIII. Technical Assistance

Uganda has received extensive technical assistance from the Fund in recent years.[5]

[5] For a description of technical assistance provided prior to 2006, see *Uganda—Staff Report for the Sixth Review Under the Three-Year Arrangement Under the Poverty Reduction and Growth Facility, Request for Waiver of Performance Criteria, and Request for a Policy Support Instrument* (IMF Country Report No. 06/43).

FAD has provided TA to the Uganda Revenue Authority (URA) in the areas of revenue administration and oil revenue management, with three missions from headquarters visiting Kampala during 2008. FAD—represented by three public financial management (PFM) advisors and one revenue administration advisor at AFRITAC East—continues to provide follow-up TA in several fiscal areas, such as cash management; the design of a comprehensive donor-supported PFM reform strategy; and revenue collection enhancements.

A TA mission on enhancing the effectiveness of monetary policy implementation and developing financial markets was conducted in August 2005; in April 2006 MCM and the BOU held a joint workshop on financial market development. In 2008 and 2009 MCM has provided TA to build capacity to undertake financial stability analysis and reporting; and more recently MCM has provided TA in the monetary operations area.

XIV. Future Technical Assistance Priorities

The priorities for Fund technical assistance in the next few years will be in the areas of tax administration, public expenditure management, especially control and monitoring of public arrears at both central and local government levels, monetary and exchange rate management, bank supervision, national accounts statistics, reporting standards for government finance statistics, monetary and balance of payments statistical reporting, central bank accounting, and audit and debt management.

XV. Resident Representative

The Fund has maintained a resident representative in Uganda since July 1982.

APPENDIX II. JOINT BANK-FUND WORK PROGRAM, JUNE 2010 – JUNE 2011

Title	Products	Provisional timing of missions (if relevant)	Expected delivery date
1. World Bank Work Program	The work program will continue to concentrate on areas within the existing portfolio, including infrastructure development (transport and energy), secondary education, health infrastructure, agricultural research, advisory services and training, Kampala infrastructure development, and local government service delivery (including Northern Uganda rehabilitation). In addition, the Bank project to support public service performance enhancement, Northern Uganda social protection, minerals development and environment sustainability will be maintained.		
	Public Expenditure Review on budget composition trends and efficiency in the road sector will be delivered to client. Public Expenditure Review on Investment Planning concept discussed with government and work started	 May 2010	June 2010 December 2010
	Poverty Reduction Support Credit to enhance effectiveness of service delivery, public sector management, and human development issues.	June 2010	August 2010
	Strategy paper for GOU's negotiation with other member states on the efforts towards elimination of non-tariff barriers. Follow-up work on implementation of the report recommendations with particular emphasis on adaptation of experiences from other RECs, in depth study of the		September 2010

	diary sector in the region, will be completed		
	A new study on shared/spatial growth with special focus on agriculture, labor and integration of leading and lagging areas, will be initiated.	June 2010	May 2011
2. Fund Work Program	Seventh Review and Request for a new PSI.	March 2010	May 2010
	Staff visit on the government budget	May 2010	June 2010
	First review under the PSI	September 2010	November 2010
3. Joint Work Program	Joint DSA	March 2010	May 2010
	JSAN on the NDP (new PRSP).	March 2010	April 2010

UGANDA

Joint IMF/World Bank Debt Sustainability Analysis[1]

Prepared by the Staffs of the International Monetary Fund and
the International Development Association
Approved by Saul Lizondo and Dominique Desruelle (IMF)
and Sudhir Shetty and Sudarshan Gooptu (IDA)

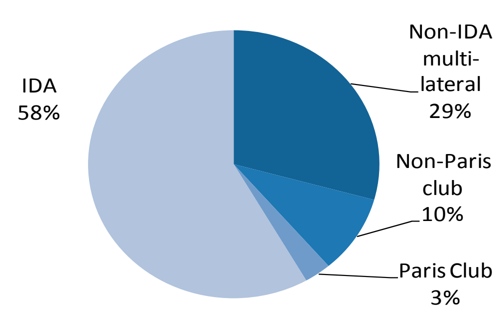
April 27, 2010

Based on the joint Low-Income Country Debt Sustainability Framework of the World Bank and the IMF, Uganda continues to be assessed as a low risk of debt distress. The authorities intend to continue to rely on concessional assistance to finance their public infrastructure investment in the coming years, but increase gradually their use of non-concessional funds as they build up their debt management capacity. Under these baseline assumptions, external debt is expected to remain well below the thresholds over the medium and long term, and public debt exhibits stable debt dynamics. The sensitivity of Uganda's debt indicators to a growth shock suggests that careful selection of public investment projects have a key role to play in the maintenance of debt sustainability over the near and medium term, requiring continued attention from the Ugandan authorities to improving investment planning processes and strengthening implementation capacity.

I. Background

1. **Sound macroeconomic policies and cautious public borrowing following debt relief have allowed Uganda to maintain a sustainable debt position**. HIPC (in 1999/2000) and MDRI (in 2005/06 and 2006/07) debt relief reduced Uganda's debt burden sharply, with all debt indicators declining to levels well below their policy-dependent thresholds.[2] Prudent fiscal management and modest public sector deficits further strengthened the debt position. Debt management has remained cautious since debt relief (Box 1). New external borrowing concentrated on financing for energy, roads and agricultural development, and was contracted on highly concessional terms, mostly from IDA and the AfDB. The authorities have guaranteed somewhat more than $100 million in private external loans over 2006-09, mostly as part of

Figure 1. Breakdown of the stock of external debt (end FY2008/09)



[1] Prepared by the IMF and World Bank staff in consultation with the authorities. This DSA replaces the one prepared in 2008 as a staff supplement in IMF Country Report No. 09/79. Its assumptions and results have been discussed with the authorities. All debt indicators refer to Uganda's fiscal year (July-June).

[2] The World Bank's Country Policy and Institutional Assessment (CPIA) ranks Uganda as a "strong performer." Debt burden thresholds for strong performers are NPV of debt to GDP ratio of 50 percent, NPV of debt-to-exports ratio of 200 percent, NPV of debt-to-revenue ratio of 300 percent, debt-service-to-exports ratio of 25 percent, and debt-service-to-revenue ratio of 35 percent.

the financing for the Bujagali hydropower dam[3] – the guarantee has remained uncalled. As a consequence, public and publicly guaranteed external debt has remained low as a percent of GDP (13.8 percent in 2008/09), and is mostly owed to multilaterals (IDA accounts for 58 percent of total debt – Figure 1). Domestic debt, issued exclusively for the conduct of monetary policy, amounts to less than 10 percent of GDP.

Box 1. Changes in Debt Indicators since the Last DSA

- **Public and publicly guaranteed external debt** increased from US$ 1.8 billion (11.8 percent of GDP) to US$ 2.0 billion (13.8 percent of GDP) between 2007/8 and 2008/09.
- **Debt service to exports**, the key indicator of external liquidity, fell from 6.0 percent to 3.5 percent over this period, partly on account of better recording of export data.
- With domestic debt declining from 10.7 percent in 2007/08 to 8.4 percent of GDP in 2008/09 (mostly on account of high growth), **total public debt** declined slightly to 22.2 percent of GDP, from 22.5 percent recorded in 2007/08. The **debt-service-to-revenue ratio** declined from 33.0 to 24.8 percent over this period.

2. **The backbone of the authorities' medium-term policies continues to be a sharp increase in public investment with a view to removing persistent growth bottlenecks.** Investment in infrastructure (mostly energy and transportation) is the main priority of the new National Development Plan, and a number of large 'flagship' projects have been identified, including the Karuma hydropower plant[4]. Capacity building is expected to raise implementation and absorptive capacity over the coming years, alleviating the main constraints to budget execution faced in the recent past.

3. **Financing is expected to come from a combination of domestic and external sources.** The authorities are committed to raise domestic revenue over the medium term, partly to make up for the expected decline in aid. While a large share of their financing needs will continue to be filled by concessional borrowing, they also intend to use limited amounts of non-concessional borrowing for large high-yield investments such as the Karuma hydropower project.

II. Assumptions

4. **Long-term assumptions are consistent with the recent performance of the Ugandan economy and only slightly different from those in the previous DSA.** Growth is

[3] The Bujagali hydroelectric plant was financed through a US $800 million private consortium with participation from multilateral lenders, with a public sector guarantee of only US $115 million.

[4] See Uganda's *National Development Plan 2010/11-2014/15*, and the *Joint Staff Advisory Note on Uganda's National Development Plan 2010/11-2014/15* (http://www.imf.org).

expected to remain below potential in 2009/10 and 2010/11 on account of the prolonged effects of the global economic slowdown and of the regional drought, but rebound to around 7 percent (about the historical average of the past nine years[5]) thereafter, while improved monetary policy management would help keep inflation around 5 percent. The public sector deficit (including grants) increases in the near term on account on the public investment drive before stabilizing at about 2.5 percent of GDP. Compared with the 2008 Joint IMF-World Bank DSA, the current baseline scenario assumes a more marked slowdown in the near term and a less ambitious growth path over the medium term, reflecting a slightly scaled-down profile of infrastructure investment in light of capacity and implementation constraints (Box 2).

Box 2. Ex post analysis of the 2008 DSA

- **Exports have over-performed compared to the last DSA**, mostly on account of better recording of informal cross-border trade and a stronger resilience to the impact of the global slowdown.

- Similarly, higher growth than initially envisaged has led to **more sustained imports**. Assumptions on the behavior of exports and imports over the long term are similar to the 2008 DSA, and the trade and current account balances are similar.

- **The current baseline scenario includes slightly less external borrowing** compared to the 2008 DSA, in line with the smoother public expenditure path.

- **On the fiscal side, both public revenue and expenditure have not performed as well as envisaged in the 2008 DSA**. They are assumed to grow smoothly over the projection period, as implementation and absorption capacity constraints are lifted and improved tax policy increases fiscal resources.

5. **The external position remains solid.** The external current account deficit widens somewhat in the early years, largely on account of the high import content of infrastructure investments, before stabilizing around 3 percent of GDP in the long run. Exports in 2009 were well above projections, largely on account of inclusion of cross-border informal trade.[6] They are subsequently assumed to grow in line with GDP before accelerating over the long term, reflecting the supply response to improved infrastructure. Imports pick up during the investment drive, reaching 35 percent of GDP before returning to their steady-state level of 30 percent of GDP over the long term. The trade deficit stabilizes over the long term at around 6 percent of GDP. Total transfers decline over time, from 9 to 4 percent of GDP.

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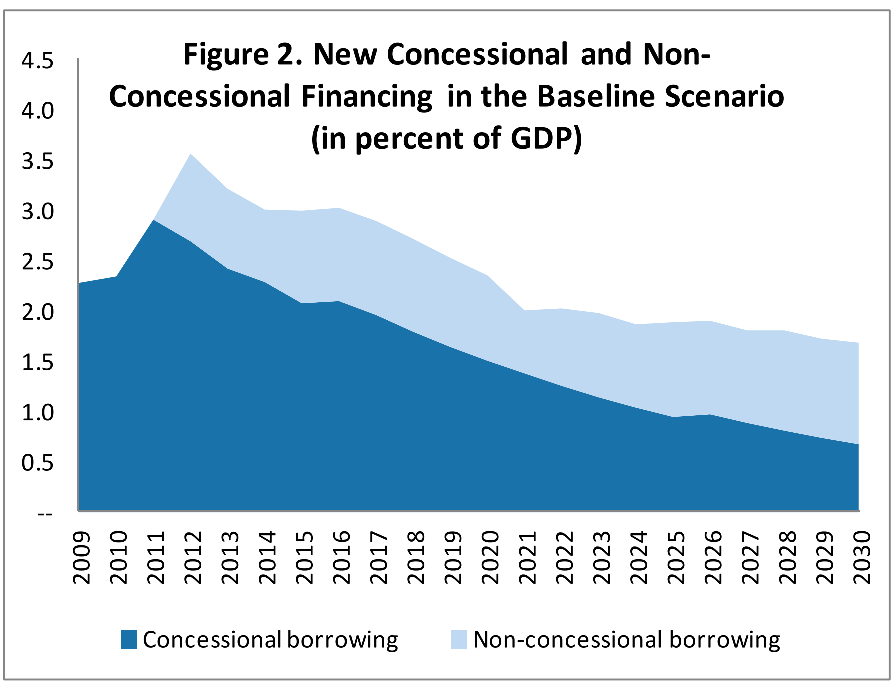
[5] Historical averages exclude FY1999/2000, where growth was abnormally high.

[6] Export grew at abnormally high levels of 57 percent and 19 percent during 2007/08 and 2008/09 as recording was adjusted to include the informal border trade that is usually not captured in the Customs data previously used to derive export figures.

Remittances are assumed to stabilize at about 3.5 percent of GDP over the long term, with a slowly declining trend, and FDI stabilizes at about 4 percent of GDP.

6. **Concessional donor inflows are projected to continue to contribute to budget financing but gradually taper off.** As concessional assistance decline, the use of non-concessional resources grows to provide about half the new external financing at the end of the projection period (Figure 2). [7] The grant element of new public borrowing declines over time, from over 40 percent to less than 10 percent by the end of the projection period. Public domestic debt grows in line with GDP, hovering over 8 percent of GDP. Financing projections are somewhat below those of the previous DSA, reflecting the slower projected growth in public investment

7. **The current scenario does not account for the impact of oil, given the uncertainties that continue to affect the medium-term prospects**. Recent oil exploration in Eastern Uganda suggest that oil will likely have a significant impact on growth as well as the fiscal and external accounts over the medium and long term. However, there remains a high degree of uncertainty regarding the scope, timing and pace of petroleum exploitation. The costs in terms of infrastructure development are also difficult to quantify at this point. Under the most recent estimates, production and commercialization cannot be expected before 2017. While the current analysis excludes oil, the next full DSA will explore this issue in detail, taking into account the additional information that will become available by then on the impact of oil on the economy.



[7] Non-concessional borrowing is assumed to be contracted on IBRD-like terms, with LIBOR rates, 10 years of grace and 20 years of repayment.

III. External Debt Sustainability Analysis

8. **The authorities agreed with the results of the DSA, which were similar to the results of their own DSA.** The authorities intend to rely primarily on concessional borrowing, and based their DSA on more conservative assumptions regarding non-concessional borrowing. They were however well aware that some non-concessional borrowing was likely and agreed that such a borrowing would remain consistent with debt sustainability under the joint IMF-World Bank DSA assumptions. In that context, the authorities are also considering the use of private public partnerships to ease pressure on government financing, and are strengthening the relevant regulatory framework to be able to better assess potential contingent liabilities.

9. **Public and publicly guaranteed external debt is expected to remain sustainable over the next 20 years** (Table 1 and Figure 3). All five debt-burden indicators remain well below their policy-dependent thresholds throughout the period. The PV of debt-to-GDP ratio is expected to rise in the first part of the period (from 8 percent in 2009/10 to 13 percent in 2014/15) in line with the public investment drive; it then stabilizes to about 14 percent in the outer years. The PV of debt-to-exports is expected to peak at 86 percent of GDP in 2019/20 before going down gradually to 70 percent at the end of the projection period. The debt service-to-exports ratio remains very low, reflecting the continued large share of highly concessional borrowing in the debt stock.

10. **External debt is expected to remain resilient to all standardized shocks** (Figure 2, Tables 2a and 2b). The stress tests point to a low risk of debt distress. Under all standardized stress tests, the debt-to-GDP, debt-to-exports, and debt service-to-exports indicators of public and publicly guaranteed external debt remain below their indicative threshold values throughout the next 20 years.

11. **Historical scenarios reflect to a large extent Uganda's uneven performance over the last ten years**, notably with respect to GDP and export growth, inflation, transfers, and FDI inflows. However, stronger performance since 2005 points to an increased resilience. In addition, Uganda has accumulated large foreign reserves in recent years – reserves stand at 5 months of imports in 2009/10 and are projected to remain close to this level providing a significant cushion in the event of a transitory foreign financing shock.

IV. Fiscal Debt Sustainability Analysis

12. **The path of total public debt, which includes external debt and domestic public debt, is sustainable under all stress tests.** (Tables 3 and 4, and Figure 4). Under the baseline, the PV of public debt to GDP and revenue increases in the medium term, but returns to a very low level over the long term. Debt service is broadly stable as a share of revenue.

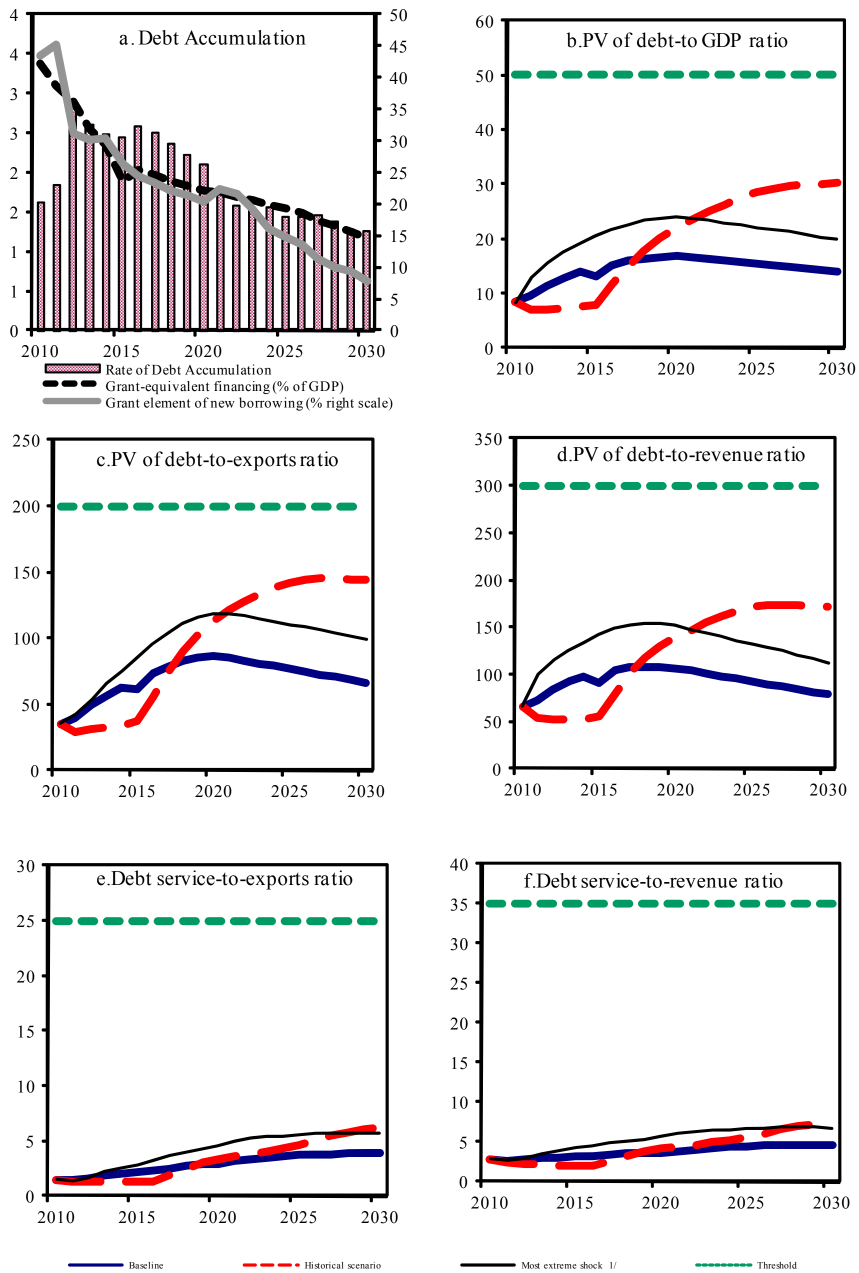
13. **Of all bound tests, a permanent shock to growth stands out as bearing the strongest impact on debt indicators.** The PV of debt to GDP is relatively unaffected by the

bound tests, and remains below 30 percent and close to the baseline under all scenarios. The PV of debt to revenue is relatively robust to most shocks, but is significantly affected by a shock to growth. Finally, a permanent shock to growth would raise the present value of the debt service-to-revenue ratio markedly, raising it to 30 percent and constraining fiscal spending significantly. This reveals how critical investment selection is to ensure long-term debt sustainability.

V. Conclusion

14. **Uganda's public and external debt are expected to remain sustainable under the baseline scenario as well as under alternative shock scenarios**, thanks to a cautious strategy that combines reliance to concessional borrowing (especially in the near future) to finance infrastructure projects and a prudent fiscal stance. Uganda's public debt indicators are however sensitive to a protracted adverse growth shock. This highlights the importance of ensuring that a shift towards non-concessional borrowing is combined with medium-term improvements in project selection, investment planning processes and implementation capacity.

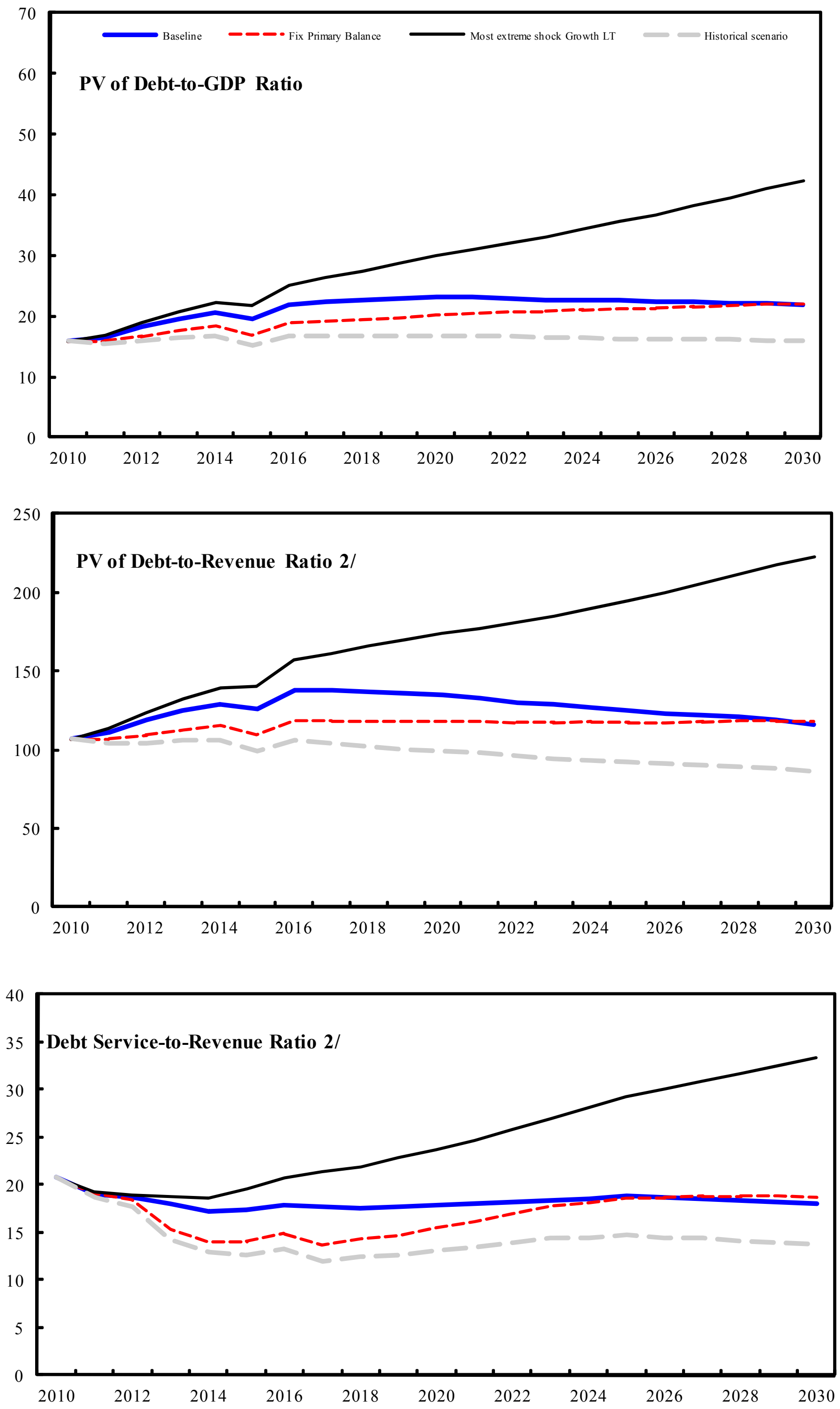
Figure 3. Uganda: Indicators of Public and Publicly Guaranteed External Debt under Alternatives Scenarios, 2010-2030 1/



Sources: Country authorities; and staff estimates and projections.

1/ The most extreme stress test is the test that yields the highest ratio in 2020. In figure b. it corresponds to a One-time depreciation shock; in c. to a Terms shock; in d. to a One-time depreciation shock; in e. to a Terms shock and in figure f. to a Terms shock

Figure 4.Uganda: Indicators of Public Debt Under Alternative Scenarios, 2010-2030 1/



Sources: Country authorities; and staff estimates and projections.
1/ The most extreme stress test is the test that yields the highest ratio in 2020.
2/ Revenues are defined inclusive of grants.

Table 1.: External Debt Sustainability Framework, Baseline Scenario, 2007-2030 1/
(In percent of GDP, unless otherwise indicated)

	Actual			Historical 0 Average	0 Standard Deviation	Projections									
	2007	2008	2009			2010	2011	2012	2013	2014	2015	2010-2015 Average	2020	2030	2016-2030 Average
External debt (nominal) 1/	**18.3**	**17.7**	**19.6**			**19.8**	**22.5**	**24.8**	**25.4**	**25.6**	**23.1**		**26.8**	**22.7**	
o/w public and publicly guaranteed (PPG)	11.4	11.8	13.8			13.3	15.1	17.2	18.7	19.9	18.2		21.8	16.2	
Change in external debt	-35.3	-0.6	1.9			0.2	2.7	2.3	0.6	0.3	-2.6		0.0	0.5	
Identified net debt-creating flows	-10.6	-5.4	-1.3			-0.2	0.2	-0.2	-0.8	-1.1	-1.8		-4.9	-4.3	
Non-interest current account deficit	**3.2**	**2.6**	**4.2**	**2.5**	**1.9**	**4.8**	**5.4**	**5.3**	**4.8**	**4.5**	**4.0**		**0.6**	**0.4**	0.4
Deficit in balance of goods and services	11.1	10.2	11.5			10.1	10.8	10.7	9.9	9.4	8.4		6.8	5.4	
Exports	16.9	21.9	23.8			23.6	23.7	23.2	22.8	22.3	21.6		19.5	21.0	
Imports	27.9	32.0	35.3			33.6	34.5	33.9	32.6	31.6	30.0		26.3	26.5	
Net current transfers (negative = inflow)	-9.0	-8.9	-8.8	-10.2	1.8	-7.3	-7.0	-6.7	-6.4	-6.1	-5.6		-5.2	-4.0	-4.8
o/w official	-3.7	-3.0	-3.3			-2.4	-1.8	-1.8	-1.6	-1.4	-1.1		-1.3	-1.0	
Other current account flows (negative = net inflow)	1.1	1.3	1.5			2.0	1.6	1.3	1.3	1.2	1.2		-1.0	-1.1	
Net FDI (negative = inflow)	**-5.8**	**-5.4**	**-4.6**	**-3.6**	**1.6**	**-4.5**	**-4.8**	**-4.8**	**-4.9**	**-4.9**	**-5.0**		**-4.8**	**-4.3**	-4.7
Endogenous debt dynamics 2/	**-8.0**	**-2.6**	**-0.9**			**-0.4**	**-0.5**	**-0.6**	**-0.7**	**-0.7**	**-0.7**		**-0.7**	**-0.3**	
Contribution from nominal interest rate	0.8	0.6	0.6			0.6	0.7	0.8	0.9	1.0	1.0		1.0	1.1	
Contribution from real GDP growth	-3.9	-1.3	-1.1			-1.0	-1.2	-1.4	-1.6	-1.7	-1.7		-1.7	-1.4	
Contribution from price and exchange rate changes	-4.9	-1.9	-0.3			…	…	…	…	…	…		…	…	
Residual (3-4) 3/	**-24.7**	**4.8**	**3.2**			**0.4**	**2.5**	**2.5**	**1.4**	**1.4**	**-0.8**		**4.9**	**4.7**	
o/w exceptional financing	-28.6	0.1	0.1			0.0	0.0	0.0	0.0	0.0	0.0		0.0	0.0	
PV of external debt 4/	...	...	13.5			14.9	17.0	19.0	19.6	19.8	17.9		21.8	20.4	
In percent of exports	...	...	56.6			63.1	71.6	82.1	86.0	89.0	83.2		112.1	96.9	
PV of PPG external debt	**...**	**...**	**7.7**			**8.3**	**9.5**	**11.4**	**12.9**	**14.0**	**13.1**		**16.9**	**13.9**	
In percent of exports	**...**	**...**	**32.5**			**35.3**	**40.3**	**49.3**	**56.6**	**63.1**	**60.8**		**86.5**	**66.0**	
In percent of government revenues	**...**	**...**	**61.8**			**66.4**	**73.0**	**84.9**	**92.3**	**97.3**	**91.1**		**106.8**	**78.4**	
Debt service-to-exports ratio (in percent)	**9.8**	**6.0**	**3.5**			**4.3**	**6.1**	**6.5**	**7.5**	**8.2**	**8.4**		**10.2**	**12.0**	
PPG debt service-to-exports ratio (in percent)	**4.0**	**2.4**	**0.7**			**1.5**	**1.4**	**1.6**	**1.9**	**2.0**	**2.1**		**3.0**	**3.9**	
PPG debt service-to-revenue ratio (in percent)	**5.4**	**4.1**	**1.3**			**2.8**	**2.6**	**2.7**	**3.1**	**3.1**	**3.2**		**3.6**	**4.6**	
Total gross financing need (Billions of U.S. dollars)	-0.1	-0.2	0.1			0.2	0.4	0.4	0.4	0.4	0.2		-1.1	-2.0	
Non-interest current account deficit that stabilizes debt ratio	38.5	3.2	2.4			4.6	2.8	3.0	4.2	4.2	6.5		0.6	-0.1	
Key macroeconomic assumptions															
Real GDP growth (in percent)	8.6	8.5	7.1	9.1	5.0	5.6	6.4	7.0	7.2	7.4	7.5	6.8	7.0	7.0	7.0
GDP deflator in US dollar terms (change in percent)	10.1	11.8	1.8	1.5	10.4	6.5	-0.4	2.4	2.4	2.4	2.7	2.7	4.2	4.2	4.2
Effective interest rate (percent) 5/	1.7	4.3	3.4	2.4	0.8	3.2	3.9	3.9	4.0	4.2	4.3	3.9	4.3	5.5	4.7
Growth of exports of G&S (US dollar terms, in percent)	30.2	57.1	18.9	19.1	19.2	11.1	6.7	7.1	7.6	7.6	6.9	7.9	10.9	12.5	11.3
Growth of imports of G&S (US dollar terms, in percent)	24.5	39.1	20.2	15.1	13.4	7.1	8.8	7.5	5.7	6.6	4.7	6.7	10.5	12.0	10.6
Grant element of new public sector borrowing (in percent)	...	...	...	...	...	43.5	45.1	31.1	30.3	30.4	26.3	34.4	20.4	7.8	17.2
Government revenues (excluding grants, in percent of GDP)	12.6	12.8	12.5			12.5	13.1	13.5	14.0	14.4	14.4		15.8	17.7	16.3
Aid flows (in Billions of US dollars) 7/	0.5	0.8	0.5			0.7	0.8	0.8	0.8	0.8	0.7		1.1	1.9	
o/w Grants	0.5	0.4	0.5			0.4	0.3	0.4	0.4	0.4	0.3		0.6	1.5	
o/w Concessional loans	0.0	0.4	0.0			0.3	0.5	0.5	0.4	0.4	0.4		0.5	0.5	
Grant-equivalent financing (in percent of GDP) 8/	...	...	...			3.4	3.1	2.9	2.5	2.3	1.9		1.8	1.2	1.6
Grant-equivalent financing (in percent of external financing) 8/	...	...	...			71.9	66.1	54.2	53.2	52.9	46.1		48.8	45.0	49.0
Memorandum items:															
Nominal GDP (Billions of US dollars)	11.9	14.4	15.7			17.7	18.8	20.5	22.5	24.8	27.4		47.3	140.7	
Nominal dollar GDP growth	19.6	21.3	9.0			12.5	6.0	9.5	9.8	10.0	10.4	9.7	11.5	11.5	11.5
PV of PPG external debt (in Billions of US dollars)			1.1			1.4	1.7	2.2	2.8	3.3	4.0		8.0	19.5	
(PVt-PVt-1)/GDPt-1 (in percent)						1.6	1.8	2.9	2.6	2.5	2.4	2.3	2.1	1.2	1.8
Gross remittances (Billions of US dollars)	0.3	0.6	0.7			0.8	0.8	0.9	1.0	1.0	1.1		1.9	5.1	
PV of PPG external debt (in percent of GDP + remittances)	...	...	7.4			8.0	9.1	10.9	12.3	13.5	12.6		16.2	13.4	
PV of PPG external debt (in percent of exports + remittances)	...	...	27.1			29.8	33.8	41.4	47.6	53.0	50.9		71.8	56.3	
Debt service of PPG external debt (in percent of exports + remittances)	...	...	0.6			1.3	1.2	1.3	1.6	1.7	1.8		2.5	3.3	

Sources: Country authorities; and staff estimates and projections.

1/ Includes both public and private sector external debt.
2/ Derived as [r - g - ρ(1+g)]/(1+g+ρ+gρ) times previous period debt ratio, with r = nominal interest rate; g = real GDP growth rate, and ρ = growth rate of GDP deflator in U.S. dollar terms.
3/ Includes exceptional financing (i.e., changes in arrears and debt relief); changes in gross foreign assets; and valuation adjustments. For projections also includes contribution from price and exchange rate changes.
4/ Assumes that PV of private sector debt is equivalent to its face value.
5/ Current-year interest payments divided by previous period debt stock.
6/ Historical averages and standard deviations are generally derived over the past 10 years, subject to data availability.
7/ Defined as grants, concessional loans, and debt relief.
8/ Grant-equivalent financing includes grants provided directly to the government and through new borrowing (difference between the face value and the PV of new debt).

Table 2a.Uganda: Sensitivity Analysis for Key Indicators of Public and Publicly Guaranteed External Debt, 2010-2030
(In percent)

	Projections							
	2010	2011	2012	2013	2014	2015	**2020**	2030
PV of debt-to GDP ratio								
Baseline	8	10	11	13	14	13	**17**	14
A. Alternative Scenarios								
A1. Key variables at their historical averages in 2010-2030 1/	8	7	7	7	8	8	**22**	30
A2. New public sector loans on less favorable terms in 2010-2030 2	8	10	13	15	17	18	**23**	21
B. Bound Tests								
B1. Real GDP growth at historical average minus one standard deviation in 2011-2012	8	9	11	12	14	15	**17**	14
B2. Export value growth at historical average minus one standard deviation in 2011-2012 3/	8	9	12	13	14	15	**17**	14
B3. US dollar GDP deflator at historical average minus one standard deviation in 2011-2012	8	10	13	14	16	17	**19**	16
B4. Net non-debt creating flows at historical average minus one standard deviation in 2011-2012 4/	8	9	12	13	14	15	**17**	14
B5. Combination of B1-B4 using one-half standard deviation shocks	8	7	6	8	9	11	**15**	14
B6. One-time 30 percent nominal depreciation relative to the baseline in 2011 5/	8	13	16	18	19	21	**24**	20
PV of debt-to-exports ratio								
Baseline	35	40	49	57	63	61	**86**	66
A. Alternative Scenarios								
A1. Key variables at their historical averages in 2010-2030 1/	35	29	31	32	34	37	**113**	144
A2. New public sector loans on less favorable terms in 2010-2030 2	35	43	54	65	75	85	**119**	99
B. Bound Tests								
B1. Real GDP growth at historical average minus one standard deviation in 2011-2012	35	38	47	54	60	66	**86**	66
B2. Export value growth at historical average minus one standard deviation in 2011-2012 3/	35	40	52	60	66	72	**92**	69
B3. US dollar GDP deflator at historical average minus one standard deviation in 2011-2012	35	38	47	54	60	66	**86**	66
B4. Net non-debt creating flows at historical average minus one standard deviation in 2011-2012 4/	35	40	50	56	63	69	**88**	66
B5. Combination of B1-B4 using one-half standard deviation shocks	35	28	23	30	36	42	**63**	55
B6. One-time 30 percent nominal depreciation relative to the baseline in 2011 5/	35	38	47	54	60	66	**86**	66
PV of debt-to-revenue ratio								
Baseline	66	73	85	92	97	91	**107**	78
A. Alternative Scenarios								
A1. Key variables at their historical averages in 2010-2030 1/	66	53	53	53	53	56	**140**	172
A2. New public sector loans on less favorable terms in 2010-2030 2	66	77	93	107	116	128	**146**	117
B. Bound Tests								
B1. Real GDP growth at historical average minus one standard deviation in 2011-2012	66	70	82	89	94	101	**108**	79
B2. Export value growth at historical average minus one standard deviation in 2011-2012 3/	66	72	87	94	98	105	**110**	79
B3. US dollar GDP deflator at historical average minus one standard deviation in 2011-2012	66	74	94	102	108	115	**123**	91
B4. Net non-debt creating flows at historical average minus one standard deviation in 2011-2012 4/	66	73	85	92	97	103	**109**	79
B5. Combination of B1-B4 using one-half standard deviation shocks	66	54	46	57	65	74	**93**	77
B6. One-time 30 percent nominal depreciation relative to the baseline in 2011 5/	66	100	116	126	133	143	**153**	112

Table 2b.Uganda: Sensitivity Analysis for Key Indicators of Public and Publicly Guaranteed External Debt, 2010-2030 (continued)
(In percent)

Debt service-to-exports ratio

Baseline	2	1	2	2	2	2	**3**	4
A. Alternative Scenarios								
A1. Key variables at their historical averages in 2010-2030 1/	2	1	1	1	1	1	**3**	6
A2. New public sector loans on less favorable terms in 2010-2030 2	2	1	2	2	3	3	**5**	6
B. Bound Tests								
B1. Real GDP growth at historical average minus one standard deviation in 2011-2012	2	1	2	2	2	2	**3**	4
B2. Export value growth at historical average minus one standard deviation in 2011-2012 3/	2	1	2	2	2	2	**3**	4
B3. US dollar GDP deflator at historical average minus one standard deviation in 2011-2012	2	1	2	2	2	2	**3**	4
B4. Net non-debt creating flows at historical average minus one standard deviation in 2011-2012 4/	2	1	2	2	2	2	**3**	4
B5. Combination of B1-B4 using one-half standard deviation shocks	2	1	1	1	1	1	**2**	3
B6. One-time 30 percent nominal depreciation relative to the baseline in 2011 5/	2	1	2	2	2	2	**3**	4

Debt service-to-revenue ratio

Baseline	3	3	3	3	3	3	**4**	5
A. Alternative Scenarios								
A1. Key variables at their historical averages in 2010-2030 1/	3	2	2	2	2	2	**4**	7
A2. New public sector loans on less favorable terms in 2010-2030 2	3	3	3	4	4	4	**6**	7
B. Bound Tests								
B1. Real GDP growth at historical average minus one standard deviation in 2011-2012	3	3	3	3	3	3	**4**	5
B2. Export value growth at historical average minus one standard deviation in 2011-2012 3/	3	3	3	3	3	3	**4**	5
B3. US dollar GDP deflator at historical average minus one standard deviation in 2011-2012	3	3	3	4	4	4	**4**	5
B4. Net non-debt creating flows at historical average minus one standard deviation in 2011-2012 4/	3	3	3	3	3	3	**4**	5
B5. Combination of B1-B4 using one-half standard deviation shocks	3	3	2	2	2	2	**3**	4
B6. One-time 30 percent nominal depreciation relative to the baseline in 2011 5/	3	4	4	4	4	4	**5**	7
Memorandum item:								
Grant element assumed on residual financing (i.e., financing required above baseline) 6/	19	19	19	19	19	19	**19**	19

Sources: Country authorities; and staff estimates and projections.

1/ Variables include real GDP growth, growth of GDP deflator (in U.S. dollar terms), non-interest current account in percent of GDP, and non-debt creating flows.
2/ Assumes that the interest rate on new borrowing is by 2 percentage points higher than in the baseline., while grace and maturity periods are the same as in the baseline.
3/ Exports values are assumed to remain permanently at the lower level, but the current account as a share of GDP is assumed to return to its baseline level after the shock (implicitly assuming an offsetting adjustment in import levels).
4/ Includes official and private transfers and FDI.
5/ Depreciation is defined as percentage decline in dollar/local currency rate, such that it never exceeds 100 percent.
6/ Applies to all stress scenarios except for A2 (less favorable financing) in which the terms on all new financing are as specified in footnote 2.

Table 3.Uganda: Public Sector Debt Sustainability Framework, Baseline Scenario, 2007-2030
(In percent of GDP, unless otherwise indicated)

	Actual					Estimate	Projections								
	2007	2008	2009	Average	Standard Deviation	2010	2011	2012	2013	2014	2015	2010-15 Average	2020	2030	2016-30 Average
Public sector debt 1/	23.6	22.5	22.2			20.9	22.1	23.9	25.3	26.3	24.6		28.0	24.1	
o/w foreign-currency denominated	11.4	11.8	13.8			13.3	15.1	17.2	18.7	19.9	18.2		21.8	16.2	
Change in public sector debt	-31.7	-1.1	-0.3			-1.4	1.2	1.8	1.4	1.0	-1.7		0.0	-0.5	
Identified debt-creating flows	-37.2	-1.0	0.4			-0.7	1.5	1.5	0.9	0.6	-1.5		-0.3	-0.5	
Primary deficit	0.0	1.1	0.8	1.2	1.5	1.3	2.3	2.6	2.3	2.1	2.5	2.2	1.4	0.7	1.3
Revenue and grants	17.1	15.5	15.9			14.9	14.9	15.3	15.5	15.9	15.5		17.1	18.7	
of which: grants	4.5	2.7	3.4			2.4	1.8	1.8	1.6	1.4	1.1		1.3	1.0	
Primary (noninterest) expenditure	17.1	16.6	16.7			16.2	17.2	17.9	17.8	18.0	17.9		18.5	19.5	
Automatic debt dynamics	-11.3	-2.1	-0.5			-2.0	-0.8	-1.1	-1.4	-1.5	-4.0		-1.8	-1.2	
Contribution from interest rate/growth differential	-5.0	-1.5	-1.8			-1.0	-0.7	-1.0	-1.3	-1.4	-1.5		-1.3	-0.9	
of which: contribution from average real interest rate	-0.6	0.4	-0.3			0.1	0.5	0.4	0.3	0.3	0.3		0.5	0.7	
of which: contribution from real GDP growth	-4.4	-1.9	-1.5			-1.2	-1.3	-1.4	-1.6	-1.7	-1.8		-1.8	-1.6	
Contribution from real exchange rate depreciation	-6.4	-0.6	1.3			-0.9	-0.1	-0.1	-0.1	-0.1	-2.5		...	...	
Other identified debt-creating flows	-25.8	0.0	0.0			0.0	0.0	0.0	0.0	0.0	0.0		0.0	0.0	
Privatization receipts (negative)	0.0	0.0	0.0			0.0	0.0	0.0	0.0	0.0	0.0		0.0	0.0	
Recognition of implicit or contingent liabilities	0.0	0.0	0.0			0.0	0.0	0.0	0.0	0.0	0.0		0.0	0.0	
Debt relief (HIPC and other)	-25.8	0.0	0.0			0.0	0.0	0.0	0.0	0.0	0.0		0.0	0.0	
Other (specify, e.g. bank recapitalization)	0.0	0.0	0.0			0.0	0.0	0.0	0.0	0.0	0.0		0.0	0.0	
Residual, including asset changes	5.5	-0.1	-0.7			-0.7	-0.3	0.4	0.5	0.4	-0.2		0.3	0.0	
Other Sustainability Indicators															
PV of public sector debt	12.2	10.7	16.2			15.9	16.6	18.2	19.5	20.5	19.5		23.1	21.8	
o/w foreign-currency denominated	0.0	0.0	7.7			8.3	9.5	11.4	12.9	14.0	13.1		16.9	13.9	
o/w external	...	...	7.7			8.3	9.5	11.4	12.9	14.0	13.1		16.9	13.9	
PV of contingent liabilities (not included in public sector debt)	...	...	...			...	...	...	...	...	...		...	...	
Gross financing need 2/	11.1	10.8	8.4			8.1	8.7	8.6	8.1	7.8	8.1		6.6	7.2	
PV of public sector debt-to-revenue and grants ratio (in percent)	71.3	69.1	101.5			107.1	111.5	119.1	125.4	129.2	126.0		135.0	116.2	
PV of public sector debt-to-revenue ratio (in percent)	96.9	83.6	128.9			127.3	126.7	135.0	139.5	142.1	135.6		146.1	123.1	
o/w external 3/	…	…	61.8			66.4	73.0	84.9	92.3	97.3	91.1		106.8	78.4	
Debt service-to-revenue and grants ratio (in percent) 4/	41.7	27.3	19.6			20.8	19.0	18.6	18.0	17.3	17.4		17.8	18.0	
Debt service-to-revenue ratio (in percent) 4/	56.7	33.0	24.8			24.7	21.6	21.1	20.0	19.0	18.7		19.3	19.0	
Primary deficit that stabilizes the debt-to-GDP ratio	31.7	2.2	1.1			2.7	1.1	0.8	0.9	1.1	4.1		1.4	1.3	
Key macroeconomic and fiscal assumptions															
Real GDP growth (in percent)	8.6	8.5	7.1	9.1	5.0	5.6	6.4	7.0	7.2	7.4	7.5	6.8	7.0	7.0	7.0
Average nominal interest rate on forex debt (in percent)	0.5	1.7	1.4	1.0	0.4	0.9	0.9	1.0	1.3	1.5	1.6	1.2	2.1	2.8	2.3
Average real interest rate on domestic debt (in percent)	3.6	3.7	-3.5	5.2	4.8	0.9	6.9	7.7	6.9	6.7	6.5	5.9	8.4	8.1	8.3
Real exchange rate depreciation (in percent, + indicates depreciatior	-15.5	-5.5	11.9	2.1	11.0	-7.2	...	...	...	...	...	...	...	...	...
Inflation rate (GDP deflator, in percent)	7.4	6.5	14.3	4.5	5.2	11.3	4.2	5.4	5.4	5.3	5.5	6.2	3.7	3.7	3.5
Growth of real primary spending (deflated by GDP deflator, in perce	0.0	0.1	0.1	0.1	0.1	0.0	0.1	0.1	0.1	0.1	0.1	0.1	0.1	0.1	0.1
Grant element of new external borrowing (in percent)	...	...	...	…	…	43.5	45.1	31.1	30.3	30.4	26.3	34.4	20.4	7.8	...

Sources: Country authorities; and staff estimates and projections.
1/ Public sector refers to general government (gross debt).
2/ Gross financing need is defined as the primary deficit plus debt service plus the stock of short-term debt at the end of the last period.
3/ Revenues excluding grants.
4/ Debt service is defined as the sum of interest and amortization of medium and long-term debt.
5/ Historical averages and standard deviations are generally derived over the past 10 years, subject to data availability.

Table 4.Uganda: Sensitivity Analysis for Key Indicators of Public Debt 2010-2030

	Projections							
	2010	2011	2012	2013	2014	2015	2020	2030
PV of Debt-to-GDP Ratio								
Baseline	16	17	18	19	20	20	23	22
A. Alternative scenarios								
A1. Real GDP growth and primary balance are at historical averages	16	15	16	16	17	15	17	16
A2. Primary balance is unchanged from 2010	16	16	17	18	18	17	20	22
A3. Permanently lower GDP growth 1/	16	17	19	21	22	22	30	42
B. Bound tests								
B1. Real GDP growth is at historical average minus one standard deviations in 2011-2012	16	17	20	22	23	22	27	28
B2. Primary balance is at historical average minus one standard deviations in 2011-2012	16	17	18	20	21	20	23	22
B3. Combination of B1-B2 using one half standard deviation shocks	16	16	17	19	20	19	23	22
B4. One-time 30 percent real depreciation in 2011	16	20	21	22	22	20	23	22
B5. 10 percent of GDP increase in other debt-creating flows in 2011	16	23	24	24	25	23	26	23
PV of Debt-to-Revenue Ratio 2/								
Baseline	107	111	119	125	129	126	135	116
A. Alternative scenarios								
A1. Real GDP growth and primary balance are at historical averages	107	104	104	106	107	99	100	87
A2. Primary balance is unchanged from 2010	107	107	109	113	115	109	118	118
A3. Permanently lower GDP growth 1/	107	113	123	132	140	140	174	223
B. Bound tests								
B1. Real GDP growth is at historical average minus one standard deviations in 2011-2012	107	115	129	138	144	143	159	147
B2. Primary balance is at historical average minus one standard deviations in 2011-2012	107	113	121	127	130	127	136	116
B3. Combination of B1-B2 using one half standard deviation shocks	107	110	115	122	126	124	134	117
B4. One-time 30 percent real depreciation in 2011	107	132	136	139	141	131	136	116
B5. 10 percent of GDP increase in other debt-creating flows in 2011	107	156	160	157	158	149	150	122
Debt Service-to-Revenue Ratio 2/								
Baseline	21	19	19	18	17	17	18	18
A. Alternative scenarios								
A1. Real GDP growth and primary balance are at historical averages	21	19	18	14	13	13	13	14
A2. Primary balance is unchanged from 2010	21	19	18	15	14	14	15	19
A3. Permanently lower GDP growth 1/	21	19	19	19	19	20	24	33
B. Bound tests								
B1. Real GDP growth is at historical average minus one standard deviations in 2011-2012	21	19	20	20	20	20	21	22
B2. Primary balance is at historical average minus one standard deviations in 2011-2012	21	19	19	19	17	18	18	18
B3. Combination of B1-B2 using one half standard deviation shocks	21	19	19	17	16	17	18	18
B4. One-time 30 percent real depreciation in 2011	21	20	20	20	19	19	20	21
B5. 10 percent of GDP increase in other debt-creating flows in 2011	21	19	21	40	19	25	18	19

Sources: Country authorities; and staff estimates and projections.

1/ Assumes that real GDP growth is at baseline minus one standard deviation divided by the square root of the length of the projection period.

2/ Revenues are defined inclusive of grants.

INTERNATIONAL MONETARY FUND
EXTERNAL RELATIONS DEPARTMENT

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FOR IMMEDIATE RELEASE
May 12, 2010

International Monetary Fund
Washington, D.C. 20431 USA

IMF Executive Board Completes Seventh Review under Uganda's PSI and Approves a Three-Year Policy Support Instrument

The Executive Board of the International Monetary Fund (IMF) completed today the seventh review of Uganda's economic performance under the Policy Support Instrument. At the request of the authorities, the Executive Board cancelled the current PSI and approved a new three-year program. Uganda's previous PSI was approved on December 15, 2006 (see Press Release No. 06/281).

The PSI for Uganda aims at maintaining macroeconomic stability and alleviating constraints to growth through a scaling up of public investment spending and structural reforms to enhance the country's absorptive capacity. It will also support the strengthening of institutions ahead of expected oil production and Uganda's participation in the future East African Monetary Union.

The IMF's framework for PSIs is designed for low-income countries that may not need, or want, IMF financial assistance, but still seek IMF advice, monitoring and endorsement of their policies. PSIs are voluntary and demand driven. PSI-supported programs are based on country-owned poverty reduction strategies adopted in a participatory process involving civil society and development partners and articulated in a Poverty Reduction Strategy Paper (PRSP). This is intended to ensure that PSI-supported programs are consistent with a comprehensive framework for macroeconomic, structural and social policies to foster growth and reduce poverty. Members' performance under a PSI is normally reviewed semi-annually, irrespective of the status of the program (see Public Information Notice No. 05/145).

Following the Executive Board's discussion on Uganda, Mr. Naoyuki Shinohara, Deputy Managing Director and Acting Chair, stated:

"Prudent macroeconomic policies have enabled Uganda to maintain macroeconomic stability despite a series of external shocks. Notwithstanding a recent deceleration, output growth has been strong and is expected to rebound quickly. Inflation has moderated, and the external position has remained solid, buoyed by robust exports and foreign investment flows. Limited central bank intervention has helped smooth excessive exchange rate volatility, and the financial sector has remained sound.

"Looking ahead, the main challenge is to accelerate infrastructure development while ensuring macroeconomic stability. The new PSI-supported program aims to support the objectives of the recently adopted National Development Plan. The authorities aim to raise domestic revenue and, if needed, use a limited amount of non-concessional borrowing to finance the increase in public spending. A cautious monetary stance, a flexible exchange rate regime, and a comfortable level of reserves will help keep the fiscal and debt positions within sustainable bounds.

"To improve efficiency and raise future growth, the government is committed to reinvigorate structural reforms. These will focus on public financial management, including strengthening spending controls and efficiency, and increasing domestic tax revenue. Financial sector reforms will seek to enhance banking stability and facilitate financial deepening.

"Large-scale oil production and the establishment of the Eastern African Monetary Union will present opportunities but also pose significant policy challenges for Uganda in the years to come. The authorities are taking steps to further strengthen their institutional and policy frameworks which, together with improving infrastructure, should help the country prepare effectively for these developments", Mr Shinohara added.

ANNEX

Recent Economic Developments

The Ugandan economy weathered the first-round impact of the global financial crisis relatively well. Despite the reversal of portfolio inflows and lower foreign direct investment, economic growth remained strong by international standards (7 percent in 2008/2009), driven in part by strong cross-border exports and recovery of private investment flows.

The slowdown was more marked this year. Economic activity decelerated due to a prolonged drought and the uncertainties about the path of global growth. Growth is expected to reach 5.6 percent for 2009/2010, but should rebound quickly over the next couple of years.

The medium-term outlook remains favorable. Looking forward, the prospect of substantial oil revenues offers an opportunity to raise growth and eliminate poverty, but also poses important policy challenges. Uganda will need robust fiscal and financial institutions, a supportive business environment and scaled-up infrastructure to prepare for this event. The fiscal policy framework must also be further bolstered in preparation for the establishment of the East African Monetary Union.

Program Summary

Uganda's PSI will be guided by the objectives and policies outlined in the new National Development Plan launched in April 2010. Fiscal policies will continue to target a bold scaling up of energy and transportation infrastructure. Public investment is targeted to increase from 6.5 percent of GDP in 2008/2009 to 8 percent in 2011/2012. Monetary policy will aim at keeping annual inflation at around 5 percent on average. The exchange rate will remain flexible and the authorities will seek to build up reserves as they prepare for the forthcoming East African Monetary Union. A financial markets development plan is being developed under the common EAC framework with a view to further enhancing banking stability and facilitating financial deepening.

Uganda: Selected Economic and Financial Indicators, FY2008/09–2013/14 [1]

	2008/09	2009/10		2010/11	2011/12	2012/13	2013/14
	Act.	Sixth Rev.	Proj.	Proj.	Proj.	Proj.	Proj.
GDP and prices (percent change)							
Real GDP	7.1	6.3	5.6	6.4	7.0	7.2	7.4
Headline inflation (end of period)	12.3	12.2	5.0	5.3	5.2	5.3	5.5
Headline inflation (average)	14.2		9.5	4.1	5.2	5.3	5.2
Core inflation (end of period)	11.1	7.9	3.9	5.0	5.0	5.0	5.0
Core inflation (average)	12.5		7.0	4.5	4.9	5.1	4.9
External sector (percent change)							
Terms of trade (Based on commodities, deterioration –)	6.6	-2.7	5.9	-8.4	-2.4	-1.1	-1.3
Terms of trade (based on all exports, deterioration -)	11.6		7.8	-4.0	1.1	1.8	1.8
Real effective exchange rate (depreciation –)	…	…	0.3	--	--	--	--
Money and credit (percent change)							
Broad money (M2)	26.3	21.2	19.3	13.7	15.6	15.9	16.0
Domestic credit	24.1	13.7	11.3	8.8	8.3	8.2	8.9
Credit to the central government [2]	6.8	1.4	1.5	1.6	0.6	0.6	1.3
Private sector credit	31.6	21.4	17.1	12.7	13.8	13.9	14.2
Savings and investment gap (percent of GDP)	-8.1	-9.2	-7.7	-8.0	-7.9	-7.3	-7.1
Domestic investment	24.2	24.9	23.3	24.7	26.0	26.2	26.6
Public	6.2	7.2	5.6	6.7	7.9	7.9	8.1
Private	18.0	17.7	17.7	17.9	18.1	18.3	18.5
National savings (excluding grants)	16.1	15.7	15.6	16.7	18.2	19.0	19.6
Public	0.9	2.2	0.9	1.7	2.6	3.1	3.6
Private	15.2	13.5	14.7	15.0	15.6	15.9	16.0
External sector (percent of GDP)							
Current account balance (including grants)	-4.8	-6.7	-5.3	-6.2	-6.1	-5.7	-5.6
Current account balance (excluding grants)	-8.1	-9.2	-7.7	-8.0	-7.9	-7.3	-7.1
Net donor inflows	4.5	6.1	5.3	3.8	4.4	3.8	3.4
External debt (including Fund)	13.9	14.3	14.0	15.6	17.6	18.9	19.9
External debt-service ratio [3, 4]	1.6	1.0	1.1	1.0	1.3	1.7	1.6
Government budget and debt (percent of GDP)							
Revenue	12.5	12.8	12.5	13.1	13.5	14.0	14.4
Grants	3.4	2.6	2.4	1.8	1.8	1.6	1.4
Total expenditure and net lending	-17.8	-17.8	-17.2	-18.1	-18.8	-18.7	-18.9
Overall balance (including grants)	-1.9	-2.5	-2.3	-3.2	-3.6	-3.2	-3.1
Overall balance (excluding grants)	-5.3	-5.0	-4.7	-5.0	-5.4	-4.8	-4.5
Stock of domestic debt	8.4	6.7	7.6	7.0	6.7	6.6	6.5
Memorandum items:							
Nominal GDP (U Sh billions)	29,972	36,330	35,213	39,040	44,014	49,725	56,246
Average exchange rate (U Sh per US$)	1,905	…	…	…	…	…	…
Treasury bill yield (percent)	6.0	…	…	…	…	…	…
Overall balance of payments (US$ millions)	178	291	291	60	237	284	288
Gross foreign exchange reserves (months of next year's imports of goods and services)	4.9	4.9	5.1	4.8	4.9	5.0	5.1

Sources: Ugandan authorities; and IMF staff estimates and projections.

1 Fiscal year begins in July.
2 Percent of M3 at start of the period.
3 Percent of exports of goods and nonfactor services.
4 Including Fund obligations; reflects actual debt service paid, including debt relief.

Statement by Samuel P. Itam, Executive Director for Uganda
May 12, 2010

Introduction

1. My Ugandan authorities have persevered with strong macroeconomic policies that have enabled them to emerge from a succession of adverse external shocks relatively intact. They are appreciative of the policy support provided under the Fund's PSI, particularly in facilitating the implementation of their structural reform agenda. Going forward, my authorities are determined to preserve Uganda's hard-earned record of macroeconomic stability, while striving to achieve key national objectives set out in their recently launched National Development Plan (NDP). The NDP will guide the policy thrust of the new PSI.

2. The authorities believe that addressing infrastructure bottlenecks—one of the most binding constraints to growth—while maintaining a sound macroeconomic environment should help Uganda attain a satisfactory sustainable growth path. It is against this backdrop, that they are requesting a new PSI to be aligned with the NDP objectives and annual budget cycles. They request the conclusion of the seventh review, a new three-year arrangement under the PSI, and cancellation of the current PSI that was due to expire at the end-2010.

Program performance, recent economic developments and prospects

3. Performance under the PSI through the seventh review has remained strong and, like in the previous reviews, all end-December assessment criteria have been met. Building on that record, the authorities affirm that all the structural benchmarks with deadlines in 2010 are expected to be met. While some weaknesses in budget execution and spending controls lingered, their impact on the program objectives has been contained.

4. Real GDP growth, which had remained broadly resilient to the global economic downturn, slowed down in the first half of 2009/10[1] due to drought and delays in the implementation of government spending. Annual consumer price inflation decelerated sharply during the same period, from 11 percent in June 2009 to 7.4 percent in December 2009, mainly due to slower consumer spending and appreciation of the Uganda shilling. The outlook on aggregate demand is projected to increase in the second half of 2009/10 on account of recovery of consumer spending and better execution of capital expenditures. Likewise, real GDP is expected to rebound towards its potential growth trajectory in the medium term.

5. The fiscal stance in the first half of 2009/10 has been tighter than programmed because of delays in the implementation of capital expenditures. Though revenue overperformed in some categories of direct and indirect domestic taxes, total revenue underperformed on account of the weakness in imports.

6. The Bank of Uganda (BOU) has pursued an accommodative monetary policy to stimulate domestic demand, especially private spending. However, due to market rigidities

[1] Fiscal year runs from July 1 to June 30.

and tightening of lending standards by commercial banks, lending rates declined only marginally. As a result credit to the private sector remained unchanged.

7. The financial sector has remained resilient to the global financial and economic crisis on account of the limited exposure of the banking system to the toxic assets and the strength of the regulatory framework. Additionally, the banks have generally increased their liquidity buffers and tightened their lending standards. These commendable developments notwithstanding, non-performing loans (NPLs) have increased -- though from a low base -- with the slowdown in economic activity. The extension of the financial sector to include mobile banking may also have created new strains and operational risks, especially those related to transfers and the regulatory framework.

Policy framework under the new PSI

Fiscal policy

8. My Ugandan authorities are resolved to maintain a modest expansionary fiscal strategy in the near to medium term, geared to scaling up infrastructure investment while maintaining spending on the MDG clusters, to boost growth and reduce poverty. To achieve these objectives, the authorities are aware that they need to create adequate fiscal space and address weaknesses in the public sector's absorption capacity. Against this backdrop, they are determined to restrain expenditure growth in non-productive activities, while at the same time focusing on revenue-enhancing measures.

9. Cognizant of limited options with respect to new sources of tax revenue in the near term, my authorities' efforts to increase revenue will focus on improving enforcement and the collection of non-tax revenues. In the same vein, they would be taking steps to strengthen budget execution (absorption) capacity through the deployment of external technical assistance on contracting and procurement, and training of accounting officers on preparation of work plans, execution and reporting.

Monetary and exchange rate policies

10. The BOU's monetary policy framework in the near to medium term will focus on supporting growth. The authorities would, however, remain vigilant and monitor the inflation risks closely and stand ready to tilt the policy stance when warranted. Lack of high frequency activity indicators has constrained the efficiency of monetary policy. In this regard, the BOU is committed to developing a set of high frequency indicators that would capture the level of activity and demand in the economy. The BOU will also continue to review its quantitative targets for monetary aggregates on a monthly basis, based on the latest available macroeconomic data, to check for stability. They stand ready to intervene on a daily basis with repos and reverse repos to ensure stability in the money markets.

11. On exchange rate, the BOU remains committed to a flexible exchange rate regime and sees it as a key line of defense against external shocks. The BOU will only intervene occasionally to smooth out excessive volatility. The authorities will also seek to accumulate a level of international reserves consistent with the East African Monetary Union convergence criteria over the medium term.

Financial sector

12. The BOU will continue to strengthen its supervisory and regulatory services to the financial institutions to stem further exposure to the new strains emanating from mobile banking and the rise in NPLs. Further, the authorities intend to strengthen the regulatory framework for financial institutions, by updating the Financial Institutions and Microfinance Deposit-taking Institutions Acts. The new framework will include an upward revision of minimum and paid-up capital requirements; provisions to cover Islamic banking products, regulations to cover insurance products offered by banks and other non-bank financial institutions, and bring the large savings and credit unions under the financial sector regulatory framework.

Structural reforms

13. Through the recently launched NDP, my Ugandan authorities have reaffirmed their commitment to the implementation of a wide range of reforms. The authorities' drive at addressing the infrastructure deficit underpins the NDP objectives and the thrust of the structural reforms in the medium term. Improving the stock and quality of infrastructure—from road and rail networks to energy and telecommunications—is a priority with the aim of enhancing productivity in the primary sectors and competitiveness of the country as a whole. The authorities are also considering participating in regional transportation projects infrastructure in the East African Community (EAC) to strengthen regional markets. To finance these investment priorities, the authorities will implement both allocative and technical efficiency improvements and other measures—including the use of PPPs—in order to create the needed fiscal space. Although they have maintained the current ceiling for non-concessional borrowing in the new PSI-supported program, the authorities may request an increase when the need arises after appropriate due diligence.

14. The authorities reaffirm that the imminent exploitation of oil and gas resources would present opportunities as well as challenges to the Ugandan economy in terms of substantive revenue base and high start-up infrastructural and operational costs. In this regard, they are focused on developing an oil and gas intervention plan, setting up a sound legal and institutional framework for the oil sector, and strengthening their resource management capacity. They also intend to foster regional cooperation in terms of key infrastructure for energy supply and security. To that end, they would welcome Fund TA and continued engagement in the assessment of the macroeconomic impact of oil and gas exploitation on the rest of the economy, including the Dutch disease effects.

15. In light of the future increase in public investments in the oil and gas sector, the authorities remain committed to fast-track the strengthening of their Public Financial Management (PFM). Also reforms will be undertaken to improve the pension sector, including liberalization to allow entry of private pension providers that will compete with the National Social Security Fund (NSSF). A Bill to establish a regulatory framework for the pension sector and other retirement benefits schemes will be submitted to Parliament at the start of the 2010/11 financial year, and the new regulator put in place soon after the enactment of the law.

16. On the regional front, the authorities consider the deepening of the EAC regional integration framework as an important catalyst to enhance Uganda's medium-term growth. They, therefore, view progress in the implementation of the Customs Union and Common Market protocols as key to advancing the EAC's integration agenda. They are committed to make progress in the harmonization of monetary and fiscal policies, and the ultimate EAC monetary union.

Conclusion

17. Uganda's strong macroeconomic fundamentals and policy framework has helped the economy to weather the storm of the global crisis. The authorities are committed to continue with the implementation of sound macroeconomic policies and a broad range of structural reforms. They also remain committed to advance the EAC integration agenda.

18. My Ugandan authorities are aware of the opportunities and challenges arising from the imminent exploitation of the oil and gas resources. They, therefore, request continuous support of the Fund, other international financial institutions, and development partners in their effort to strengthen macroeconomic stability, and restore high growth rates with low inflation for poverty reduction and the attainment of the MDGs.