# Understanding Uganda's 2014/2015 National Budget

## Economic performance

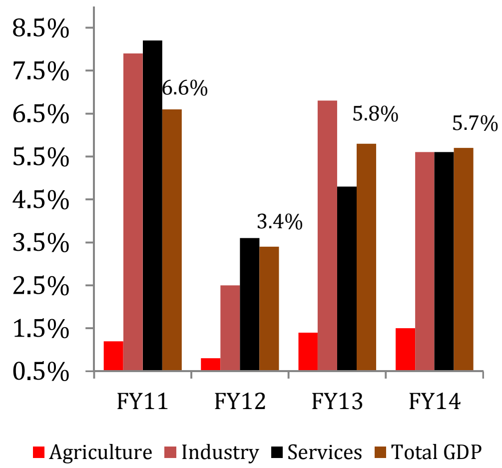
*PwC insight and analysis*

## *Macroeconomic indicators*

Through the Financial Year 2013/14 (FY14), Uganda's economy continued to grow albeit modestly at an estimated 5.7% less than target of 6.2%. The outturn depicts a steady growth given the trend from 3.4% in FY12 Despite not meeting target, the economy turned out better than average growth of 5.3% in the sub-Saharan non-oil producing economies. The growth is, however, far below the medium term target of 7% necessary to achieve socio-economic transformation.

Global economic hardships, especially slow recovery in export demand in Europe, continued to challenge Uganda's development efforts during the year. The on-going political unrest in South Sudan, one of Uganda's major trading partners, which has lasted for more than half of the budget period did not only threaten national security but adversely affected revenue streams and remittances. Proposed changes in certain legal aspects made the situation worse, with some development partners withholding funding budgeted for during the year.

Agriculture, which employs over 70% of the country's population, is the least growing. Accelerating its growth will have a significant impact on economic growth.



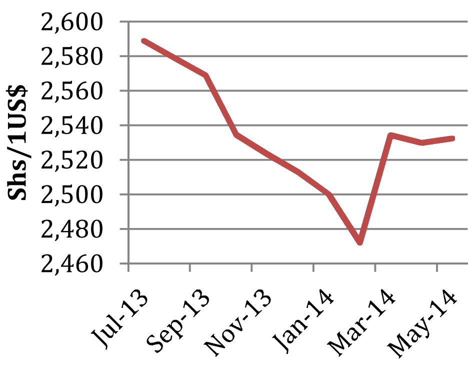

Source: MoFPED

Real GDP growth is estimated at 6.1% in FY15. Cash crop production, agro-processing, manufacturing, mining, increased electricity production, transport and communication are expected to be the main drivers of growth in FY15.

## Exchange Rate

The exchange rate, which is a key determinant of economic competitiveness, remained relatively stable over the year with overall marginal appreciation of the Uganda Shilling of about 2.2% against the US Dollar. The appreciation of the Shilling is mainly because of a weakening US Dollar on global financial markets, strong foreign inflows and foreign direct investment, the latter attracted by a stable investment climate. It is expected that the slight appreciation had a positive impact on the resource envelope given that budget planning was based on expectation of the exchange rate remaining in the range of Shs 2,600-2,700 to the US Dollar.

**Exchange rate movement**

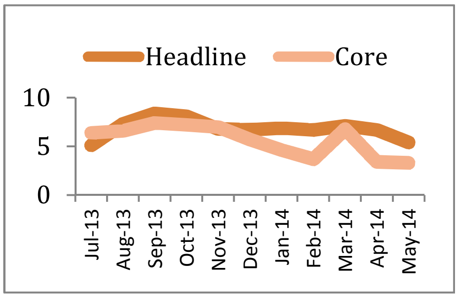



Source: Bank of Uganda

### Inflation

Inflation remained low, under single-digit, throughout the year and dropped to 5.4% in May 2014. Low inflation is a key ingredient in ensuring a stable investment climate and preserving the welfare of Ugandans. Thus maintaining low inflation continues to be a key objective of the government's macroeconomic policy. Headline inflation fluctuations were mainly as a result of movements in food prices.

A prolonged drought in the first half of FY14 caused price increases but these were largely contained. So on the whole, purchasing power of Ugandans was preserved.




### Interest Rates

Lending rates for commercial banks were on a downward trend during the year, dropping from 23.15% in July 2013 to 21.65% in April 2014, with the lowest rate since July 2011 at 20.69% recorded in February 2014. The interest rate reduction led to a slight improvement in credit growth, although not as expected given that the CBR set by Bank of Uganda was below 12% and further reduced to 11% in June 2014. This is because commercial banks focused more on quality of credit to manage credit risk that previously affected their profitability. It is projected that the credit growth trend will continue as the lending rates stabilise which should support private sector increased activity and production.

### Other indicators

Foreign exchange reserve levels slightly improved to equivalent of 4.2 months of import cover compared to 4.1 months projected a year ago. FY15 import cover is projected at 4.3 months while the medium term objective is 5 months, believed to be adequate to provide a buffer against external shocks.

Domestic revenues for the year as percentage of GDP are estimated at 13.4% compared to target of 13.9%. This rate is among the lowest in the region and is mainly attributed to Uganda's low tax effort estimated at 54-65%. In addition, domestic revenue collections during the year were 6% or Shs 475 billion off the target although revenue collection grew by 13.4% in absolute terms. To achieve the 14.2% projection in FY15, government has promised to take revenue performance enhancement measures aimed at widening the tax base and making tax administration more efficient.

**Expenditure performance in 2013/14**

Implementation of FY14 budget was challenged by significant revenue collection gaps amidst a need to undertake key infrastructure investments. To address this gap, government had to increase domestic borrowing.

Government expenditure for FY14 is projected at Shs 11.93 trillion or 99.7% of planned budget. This is a high budget execution efficiency compared to the past provided there will not be significant budget reallocations from priority sectors. The execution efficiency is in tandem with the visible implementation of prioritised projects. For example, the FY14 budget prioritised among others aggressive continued investment in infrastructure development especially transport and energy and allocated 19% and 13% respectively of budget. There is visible progress around the country in completed roads (over 830km added during the year), six new bridges, and a lot of work in progress. In the energy sector, national power generation capacity increased by over 850MW, while over 1,600km of transmission lines were added to the national grid and additional 15 districts were added to the national grid under the Rural Electrification Programme.

The good budget performance is a result of various accountability measures Government vigorously instituted and continues to implement, for example: (i) key ministries with prioritised projects report quarterly on those projects to Cabinet and are therefore regularly monitored; (ii) increased budget transparency and accountability by publishing quarterly releases to all Government departments and agencies in print media; and (iii) launching of Budget Information Website to provide all budget data which will be accessible to public.

However, performance on projects funded by external assistance was not as good. Of the external assistance budget projected at USD 1,028 million (Shs 2.5 trillion), only about 50% of the financing was realised. The slow disbursement is partly as a result of low absorption by sector ministries implementing the projects in the awake of tightened monitoring mechanisms by development partners during the year including tying disbursements to performance. Government has promised better performance in FY15 and beyond requiring all projects to be implemented as programmed.

**FY15 Resource Envelope and Application**

The FY15 budget proposals seek to sustain this growth trajectory towards social economic transformation. Indeed the FY15 budget theme "Maintaining the momentum: Infrastructure Investment for Growth and Socio-economic Transformation" is rightly so. It is worth noting that FY15 will be the final year of implementation of the first National Development Plan (NDP) which started five years ago.

FY15 budget strategy is consistent with the medium term macroeconomic objectives of achieving real economic growth of at least 7% per annum; maintaining single-digit inflation; maintain a competitive exchange rate; which can support export growth, keeping foreign exchange reserves of at least 5 months import cover; and elevating Uganda's competitiveness in the context of EAC integration. Government has more or less maintained budget priorities for FY14, re-emphasised human capital and skills development, and added maintenance of National Security and Defence.

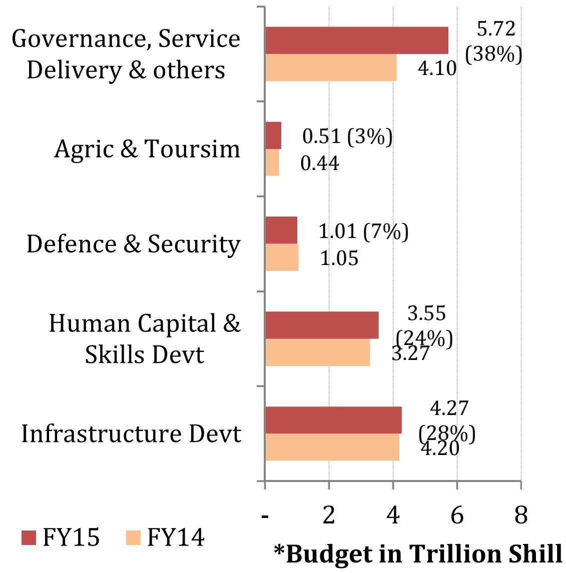
To foster growth, the budget strategy focuses on improving business climate through reducing cost of doing business. A number of reforms have been initiated or proposed including: transforming UIA and URSB into a one stop center to facilitate business registration; online business registration; automated customs clearance and electronic cargo tracking system; rolling out National Land Information System from 6 to 21 land offices; etc. Such reforms also target curbing fraud and corruption endemic in government transactions.

## Resource envelope

The total resource envelope planned for 2014/15 of Shs 15,054 billion represents 15% increment compared to FY14 budget. 15% growth is very ambitious given challenges in meeting tax revenue targets and decline in development partner financing. Domestic revenues are expected to contribute 81.8% of the resource envelope, while external financing will amount to 18.2% down from 19.5% of approved budget for 2013/14. Dependence on external financing has declined over the past years. Tax revenues, projected to grow by 20% to Shs 9,577 billion, are expected to finance 69% of the budget.

## Resource allocation

In line with FY15 budget priorities, 52% of the proposed budget will be directed to infrastructure development (especially roads and power) and human resource development (especially education and health). Budget allocation to infrastructure and human resource development has been increased by 2% and 8% respectively compared to FY14.




Source: MoFPED, *figures subject to change

Agriculture and tourism have perennially had least allocation, with 3% of FY15 budget contrary to public expectations. Allocations to agricultural sector continue to be criticised that they are too low to stimulate growth in the sector. Government's strategy, however, is not to make direct investment in agriculture but to rather create enabling environment for agricultural production and marketing such as a better road network to ease transportation. Also investments around rural electrification, provision of farm implements, irrigation and creation of youth fund are part of efforts towards an enabling environment for better agricultural production.

## Conclusion

Increased investment in the public infrastructure development, accelerated investment in the oil and gas sector, increased electricity generation, greater integration of the regional economies, and a stable investment climate supported by sustained political and macro-economic stability are recipe for accelerated growth in FY15. Last year, Uganda was ranked number one tourist destination in the world, and now is among top 10 recipients of foreign direct investment in Africa. This is a recipe for improved private sector investments. General economic outlook is good.

FY15 budget is tough and very ambitious yet attainable only if: (i) domestic revenue collection targets are met; (ii) wasteful government expenditure is significantly reduced or eliminated; and (ii) increasing unemployment problem among the youth is tackled. Strategies for a more efficient tax administration system and widening the tax base are listed in the budget. Since a number of tax exemptions especially on agricultural inputs and essential supplies have been removed, tax education will be very critical.

Government has instituted measures to curb fraud and corruption, and reduce wastefulness including: (i) implementation of the Single Treasury Account to strengthen day-to-day cash and debt management; (ii) closure of redundant government bank accounts; (iii) enforcing limits on cash withdrawals; (iii) ridding ghosts off government payroll, which exercise is expected to be completed in the first half of FY15. While Government is commended for instituting such measures, there is a lot more required in strengthening institutional governance and public service delivery.