

# UGANDA

## 2017

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## UGANDA

- Growth in the Ugandan economy slowed down to 4.8% in 2016 from 5.5% the previous year but is projected to rebound strongly in 2017 to 5.1% and expand further to 5.8% the following year.
- Uganda has made limited progress in improving human development but the National Development Plan (NDP II) envisages significant investments that could contribute to increased human capital development.
- With a significant share of the active labour force (35.5%) engaged in entrepreneurship, Uganda is one of the world's most entrepreneurial nations but lacks a dedicated strategy or policy and comprehensive programme to support it effectively.

### Overview

The Ugandan economy showed remarkable resilience in achieving modest gross domestic product (GDP) growth of 4.8% in 2016 compared to 5.5% growth in 2015. Real GDP projections for 2017 AEO indicate that GDP will grow by 5.1% in 2017 and 5.8% in 2018. Headline inflation is expected to increase slightly from 5.3% in 2017 to 5.9% in 2018, owing to rising food inflation on account of unfavourable weather conditions.

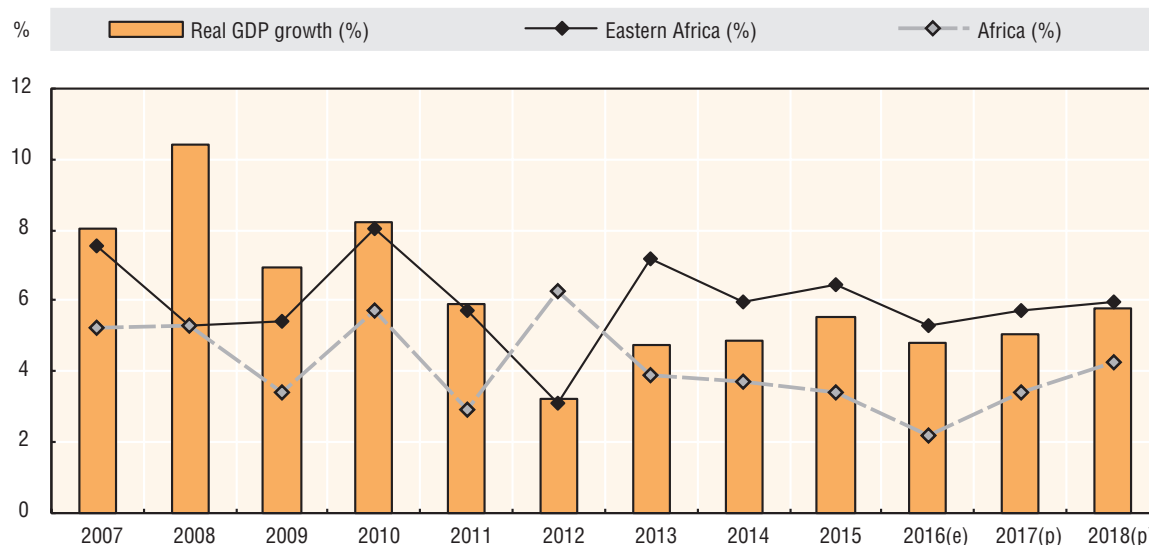
In support of macroeconomic management, the government has continued to implement large infrastructure programmes in 2016 balanced with a cautious but expansionary fiscal policy and a prudent monetary policy aimed at maintaining price, debt sustainability and exchange rate stability. The main focus has been to grow tax-to-GDP by 0.5% per annum to propel growth. However, continued institutional capacity constraints in implementing public investment projects have constrained GDP growth below the 7% full GDP potential.

The current account is expected to deteriorate from 6.5% of GDP in 2015 to 8.4% in 2016 and remain fragile in part due to the importation of inputs for large-scale infrastructure projects and a reduction in global demand for exports. According to the Bank of Uganda (BoU), the stock of foreign exchange reserves at the end of 2016 is equivalent to 4.3 months of import cover.

The country's fiscal deficit is projected to widen slightly from 4.3% of GDP in 2014/15 to 4.8% of GDP in 2015/16 and oscillate within the range of 4.9 to 5.0% of GDP between 2016 and 2018. According to the Bank of Uganda, the low levels of absorption of externally financed development expenditures resulted in a significantly lower fiscal deficit in fiscal year (FY) 2015/16 than the 7% of GDP projected at the time of the FY 2015/16 budget. The low absorption for project grants and loans is estimated at 58% and 73%, respectively.

In a bid to accelerate growth and make it more inclusive, Uganda has made industrial development an integral part of the government's overall development strategy in the NDP II period. Industrial sector development is at a nascent stage in Uganda. During FY 2015/16, the sector accounted for around 18% of GDP. The industrial sector remains largely dominated by manufacturing accounting for an average of 47% of GDP of sector, followed by construction (37%), electricity (6%), water (2%) and mining and quarrying (8%) during the period 2011-15. The relative share of industry and manufacturing has not changed over the last ten years. A large share of the active labour force is engaged in entrepreneurship mainly in the service sector. However, the country has no comprehensive policy or strategy to enhance the sector's growth. Uganda has embedded entrepreneurship development in some of its policy and strategy such as MSME Policy.

Figure 1. Real GDP growth



Source: AfDB, Statistics Department AEO. Estimates (e); projections (p).

Table 1. Macroeconomic indicators

	2015	2016(e)	2017(p)	2018(p)
Real GDP growth	5.5	4.8	5.1	5.8
Real GDP per capital growth	2.2	1.6	2.9	3.6
CPI inflation	4.0	5.2	5.3	5.9
Budget balance % GDP	-4.3	-4.8	-4.9	-5.0
Current account % GDP	-6.5	-8.4	-8.7	-8.5

Source: Data from domestic authorities; estimates (e) and projections (p) based on authors' calculations.

## Recent developments and prospects

The Ugandan economy achieved modest GDP growth of 4.8% in 2016 compared to 5.5% growth in 2015, despite a decline in growth in sub-Saharan African (SSA) countries. Continued weak external conditions, relating to fresh conflict in South Sudan, Brexit uncertainties and low global commodity prices resulted in lower exports and contributed to the depreciation of the Ugandan shilling (UGX). Internal obstacles to growth such as unfavourable weather conditions and institutional capacity constraints in implementing public investment projects have also contributed to weaker GDP growth.

The services sector remained the largest growth driver, increasing by one percentage point to 50.8% of GDP in 2016, followed by agriculture at 23% (2016), which dropped from 25% in 2013, owing to weather volatilities. Still, the census report 2014 confirmed that agriculture is the highest employer for 80% of households. The contribution of the industrial sector remained unchanged at 18.5% of GDP in 2016 due to stagnation in manufacturing and construction sectors.

The economic outlook for 2017 and 2018 will be shaped by government's aspiration to achieve a middle-income country status by 2020 with the implementation of the 2nd National Development Plan. GDP is poised to expand to 5.1% in 2017, and 5.8% in 2018, driven by continued public investment performance in the context of exchange rate stabilisation.

Figures from the national accounts for 2015 showed mixed performance. A slowdown in economic activity was registered in some sectors that in the past accounted for a significant share of GDP such as construction (7.1% of GDP), manufacturing (8.2%), food crops (11.7%), forestry (4%), financial services (4.4%), public administration (2.7%) and education (5.3%). The negative growths registered in these sectors were -0.3%, -0.3%, -1.2%, -0.2%, -0.2%, -0.2% and -0.5% respectively. The decline in the construction sector is largely explained by the under-implementation of public construction investments in roads and energy infrastructure activities. However, substantial positive growth was posted in the services sector, including trade and repair activities (13.1% from 12.3%), as well as information and communication (8.1% from 6.4%).

The economic resilience registered was due to the prudent macroeconomic policies stances implemented. On the monetary front, the depreciation of the Uganda shilling and its apparent pass through to CPI inflation was successfully contained with inflation averaging 5.2% in 2016. BoU's success in containing inflation enabled the easing of monetary policy from an average of 18% in 2012 to 14.9% in 2016, hence translating into a decline in commercial banks' lending rates, from 25.2% to 22.8% between February and December 2016. The trend signifies a recovery of private sector credit growth.

The exchange rate volatilities experienced over the previous year had been successfully stabilised in 2016. The Uganda Shilling depreciated against the US dollar by 24% in FY 2014/15 and further by 4.5% in 2015/16. The average period exchange rate of the shillings for the period July 2015 to August 2016 stood at UGX 3 434 compared to UGX 3 141 in the previous year. This depreciation has been explained by three factors: i) the decline in Uganda's exports owing to the global fall in commodity prices; ii) conflict in neighbouring countries such as South Sudan and Burundi; and iii) the strengthening of the dollar against other currencies.

The Bank of Uganda (BoU) has continued to monitor the financial soundness of the banking system, taking over the management of Crane Bank, the third largest local bank on 20 October 2016. The Bank of Uganda exercised powers under section 87 (3) 88(1)(a) and (b) of the Financial institutions Act 2004 and took over the management of Crane Bank Limited. The take-over was due to the under-capitalisation of Crane Bank, posing systemic risk to financial stability. Crane Bank management was successfully transferred to DFCU Bank in January 2017 following a competitive process. On the regulatory front, the Financial Institutions Act (FIA) 2004 was amended in 2016 with provisions for agent banking, bancassurance and Islamic banking.

On the demand side, there has been improvement in some fundamental macroeconomic variables. The current account deficit narrowed from USD 1 966 million (or -9.08% of GDP) in 2014/15 to USD 1 410 million (or -7.36% of GDP) in 2015/16, due to improvements in the trade balance from a deficit of USD 2 250 million to USD 1 870 million. Specifically, exports increased more than imports from 9.95% (of GDP) to 10.95% of GDP, while imports increased from 18.21% (of GDP) to 18.55%.

The stock of treasury bills increased from UGX 3 433 billion in 2014/15 to UGX 3 959 billion in 2015/16, while treasury bonds increased to UGX 7 654 billion in 2015/16 from UGX 6 535 billion the previous year, reflecting the impact of increased government borrowing to finance the fiscal deficit and the impact of high interest rates on domestic demand, coupled with the effects of the low global commodity prices affecting demand for exports. Consequently, private household consumption growth registered a decline from 9.8% to 4.1% of GDP, while gross capital formation expanded from -0.1% in 2014/15 to 7.4% in 2015/16 owing to heavy investments in the ongoing construction of the Karuma and Isimba hydro-power plants and roads. The AEO projections estimate a negative growth trend for exports of 1.1% in 2017, to 9.5%, with a further decline to 9.0% in 2018.



Table 2. GDP by sector (percentage of GDP at current prices)

	2011	2015
Agriculture, forestry, fishing and hunting	28.0	25.0
of which fishing	1.6	1.7
Mining and quarrying	0.8	0.7
of which oil	...	...
Manufacturing	11.2	8.9
Electricity, gas and water	2.4	2.8
Construction	7.6	7.7
Wholesale and retail trade; Repair of vehicles; Household goods; Restaurants and hotels	18.3	16.9
of which hotels and restaurants	2.6	2.7
Transport, storage and communication	7.3	11.9
Finance, real estate and business services	12.0	12.0
Public administration and defence	3.1	2.9
Other services	9.2	11.2
<b>Gross domestic product at basic prices / factor cost</b>	<b>100.0</b>	<b>100.0</b>

Source: Data from domestic authorities.

## Macroeconomic policy

### Fiscal policy

Government pursued an expansionary fiscal policy in the context of infrastructure capital expenditure as prioritised in the second National Development Plan (NDP2 2015-2020). Thus, the resource envelope was increased from UGX 15 835 trillion in 2014/15 to UGX 18 311 trillion in 2015/16, equivalent to 22.1% of GDP in 2015/16, against a target of 22.4% and up from 18.6% in the previous fiscal year. Fiscal policy was aimed at boosting domestic revenue mobilisation, and enhancing public investment efficiency while maintaining debt sustainability. The proposed budget projections for the next fiscal year indicate an increase of 10% from the approved 2016/17 budget. However, expenditure outturns could fall short owing to challenges of tax revenue collection against a backdrop of a slower global economy. The fiscal deficit is set to reach 5.0% of GDP in 2017/18 from 4.9% in 2016/17.

The NDP2 commits to mobilise the revenue to GDP ratio from 14.5% in the previous FY to 15% by 2016/17. While tax revenue improved by 0.1% of GDP in 2015/16, it missed the 0.5% annual growth target by 0.4% of GDP, due to exchange rate depreciation and weak domestic demand. According to the IMF Seventh Review, the slip in tax collection resulted in a higher underlying deficit of 2.25% of GDP. The government's fiscal policy response saw an under execution of expenditure in hydropower projects to the tune of 2.4% of GDP.

In nominal terms, tax revenue grew by 20% from UGX 9.8 trillion in FY 2014/15 to UGX 11 059 trillion in 2015/16, equivalent to 12.8% of GDP (2015/16), up from 12.7% the previous year, but notably below the 13% target. An increase in tax revenue is possible through the expansion of the tax register, and by the removal of exemptions and efficiency gains from tax administration. If achieved, this 13.4% tax-to-GDP target would still be considerably lower than for fellow member states of the East Africa Community (EAC).

In terms of fiscal sustainability, the proposed budget for FY 2017/18 will be financed up to 65% from domestic resources, and 35% from grants and loans. Although domestic arrears cleared in 2016/17 reached 0.1% of GDP, a significant stock estimated at 3.2% of GDP (or 13% of the national budget) remained outstanding as of June 2016, compared to 1.2% of GDP in 2013, thus raising the debt levels and interest payments due arising from domestic financing. Going forward, authorities



have set a target for reducing domestic arrears from 13% of government expenditure in 2015/16 to 10% (2016/17) and 7% (2019/20).

Government pursued an expansionary fiscal policy which saw an increase in the resource envelope from UGX 15.835 trillion (USD 6.239 bn) in FY 2014/15 to UGX 18.311 trillion (USD 6.5bn) in FY 2015/16. During this time, fiscal policy prioritised infrastructure and poverty alleviation in line with the second National Development Plan (NDPII) strategic priorities of reducing bottlenecks impeding growth. Fiscal policy also aimed at boosting domestic revenue mobilisation, and enhancing public investment efficiency. However, the 2015/16 expenditure outturn totalling 19.1% of GDP against a target 22.4% of GDP was slightly less than planned owing to shortfalls in public revenue collections. Hence this demonstrates that the public expenditure could easily be adjusted in response to shocks such as revenue shortfalls. Overall, this FY 2015/16 budget outturn still remains expansionary compared to an outturn of 18.5% in FY 2014/15. The expansionary fiscal stance coupled with the increased financial requirement in some sectors and revenue collections shortfall, resulted in a higher fiscal deficit (excluding grants and oil capital gains tax revenue) standing at 6.4% in FY 15/16 from the 4.5% deficit achieved in FY 2014/15. Fiscal policy has been consistent with macroeconomic stability. Real GDP growth was at 5.5% in 2015, up from 4.9% in 2014, while annual inflation averaged 5.2% in 2015, a 1.2% increase from 4.0% (2014): a notable improvement from the inflation outturn of 5.5% (2013) and 14% (2012). The 2015 inflation performance hedged slightly above the 5% medium-term target by 0.2%.

Table 3. Public finances (percentage of GDP at current prices)

	2007/08	2012/13	2013/14	2014/15	2015/16(e)	2016/17(p)	2017/18(p)
<b>Total revenue and grants</b>	<b>16.3</b>	<b>12.8</b>	<b>12.6</b>	<b>14.2</b>	<b>14.3</b>	<b>14.1</b>	<b>14.5</b>
Tax revenue	12.9	11.0	11.4	12.7	12.8	12.7	13.0
Grants	3.0	1.4	1.0	1.2	1.1	1.1	1.2
<b>Total expenditure and net lending (a)</b>	<b>18.1</b>	<b>16.2</b>	<b>16.6</b>	<b>18.5</b>	<b>19.1</b>	<b>19.0</b>	<b>19.5</b>
Current expenditure	12.9	9.1	9.5	10.2	11.0	10.8	11.6
Excluding interest	11.7	7.7	8.2	8.6	9.0	9.1	10.0
Wages and salaries	4.5	3.3	3.4	3.5	3.6	3.7	4.2
Interest	1.3	1.4	1.4	1.6	2.0	1.7	1.6
Capital expenditure	5.9	6.5	7.0	6.7	6.3	6.8	6.7
<b>Primary balance</b>	<b>-0.6</b>	<b>-2.1</b>	<b>-2.6</b>	<b>-2.7</b>	<b>-2.8</b>	<b>-3.1</b>	<b>-3.3</b>
<b>Overall balance</b>	<b>-1.9</b>	<b>-3.5</b>	<b>-4.0</b>	<b>-4.3</b>	<b>-4.8</b>	<b>-4.9</b>	<b>-5.0</b>

Note: a. Only major items are reported.

Source: Data from domestic authorities; estimates (e) and projections (p) based on authors' calculations.

## Monetary policy

The prudent monetary policy implemented in 2016 maintained inflation near the medium-term inflation target of 5% against the backdrop of a depreciating exchange rate. The monetary policy stance was tightened to 17% in October 2015 (from 16% in September) and maintained until March 2016 when it was eased. At 16% in April 2016, the Central Bank Rate (CBR) was further eased to 15%, 14% and 12% respectively, in July, September and December 2016. The gradual easing of monetary policy was meant to reverse the subdued private sector credit and bolster economic growth. The effect of easing the CBR translated into a modest decline in the average lending rate during 2016. Lending rates, however, remain sticky downwards owing to the structural rigidities in part driven by high transaction costs and prevalence of non-performing loans (NPLs).

Inflation, on the other hand, significantly reduced and stabilised throughout 2016, with the monthly CPI opening the year at 7.4% in January 2016, and declining to 5.2% and 4.1% in April and October 2016 respectively. Increases in food crop prices in the second half of 2016 increased CPI inflation upwards in December 2016 to 5.7% owing to the mild drought experienced.

The Ugandan shilling depreciated against the US dollar by 17.2% during the first half of FY 2015/16 compared to 24% during 2014/15. During the second half of 2015/16 the shilling remained stable, however, in part owing to Bank of Uganda interventions in the foreign exchange market to reduce volatilities in line with the flexible exchange rate policy. The average period exchange rate for the period July 2015 to August 2016 was UGX 3 434.46 against the US dollar compared to UGX 3 141.62 a year earlier.

With regards to the EAC monetary Union (EAMU) convergence criteria, based on the roadmap to achieve a single currency by 2024, all EAC member states concluded negotiations to establish two institutes, including the EAC Monetary Institute and Statistics Bureau. The EAC macroeconomic convergence criteria focus on the harmonisation of monetary policies, statistical frameworks, and integration of financial markets. Thus, headline inflation will apply a ceiling of 8%, fiscal deficit a ceiling of 3%, public debt a ceiling of 50% of GDP, and foreign exchange reserve cover of 4.5 months of imports.

### **Economic co-operation, regional integration and trade**

Uganda is a signatory to a number of regional trade agreements including the East African Community (EAC) Common Market Protocol, Common Market for the Eastern and Southern Africa (COMESA) Free Trade Agreement and the COMESA-EAC-SADC Tripartite Free Trade Area. With regard to EAC, significant progress has been made. The intra-EAC trade grew from USD 2 billion (2005) to USD 5.5 billion (2013). Similarly, Uganda's exports to the EAC over the decade increased four-fold to USD 667.5 million in 2015. Kenya and Rwanda have been the key export destinations for Uganda. Although exports to COMESA have stagnated at USD 1 165 million in 2014 and 2015, the intra-COMESA trade increased from USD 19.2 billion in 2012 to USD 21 billion in 2014, and are projected to reach USD 25 billion in 2017, owing to the participation of the DRC, Ethiopia and Uganda.

With regard to competitiveness, trading across borders improved to 136th position from 141st out of 190 countries in the World Bank report *Doing Business 2017* driven by the introduction of the ASYCUDA World customs electronic system easing document submission. Coupled with the completion of the One-Stop-Border to Kenya at Malaba, the time to export has been significantly reduced. Uganda is continuing to invest heavily in regional road and rail transport to facilitate regional trade and reduce trade cost across borders.

Uganda's external current account balance has narrowed due to improved exports and economic diversification. Exports increased more than imports during 2015-16, improving the trade balance. Similarly, remittances (private transfers) reached USD 1 104 million during the same period, up from USD 991 million the previous year. Notwithstanding, foreign direct investment (FDI) averaged USD 1 057m in the two years to 2016, driven by oil refinery investments. Both FDI and remittances were used for financing the current account deficit.

Table 4. Current account (percentage of GDP at current prices)

	2008	2013	2014	2015	2016(e)	2017(p)	2018(p)
Trade balance	-8.6	-8.3	-8.3	-8.8	-7.8	-9.4	-10.0
Exports of goods (f.o.b.)	10.4	10.9	9.5	10.3	10.6	9.5	9.0
Imports of goods (f.o.b.)	19.0	19.1	17.8	19.1	18.4	18.9	19.0
Services	-2.0	-1.1	-2.4	-2.1	-2.5	-2.0	-1.8
Factor income	-1.2	-2.5	-2.0	-1.4	-2.8	-2.4	-2.1
Current transfers	6.1	4.9	4.4	5.7	4.6	5.1	5.4
<b>Current account balance</b>	<b>-5.8</b>	<b>-6.9</b>	<b>-8.3</b>	<b>-6.5</b>	<b>-8.4</b>	<b>-8.7</b>	<b>-8.5</b>

Source: Data from domestic authorities; estimates (e) and projections (p) based on authors' calculations.

## Debt policy

Uganda's debt is assessed at a risk of low distress despite the sharp rise in the levels between 2014 and 2016. The total public debt increased from 34.1% (2014/15) to 37.1% (2015/16) and is projected to further rise to 38.7% in 2016/17 and peak at 43% in 2018/19. Despite the increase, debt levels are envisaged to remain well below the 50% debt-to-GDP debt sustainability threshold. In terms of the structure, external debt comprised 21.2% of the total public debt in 2015/16 (or 62% of total debt), while 12.9% was domestic debt (equivalent to 38% of total debt). In nominal terms, total public debt at end March 2016 had grown by 27% to USD 8.1 billion from USD 7.6 billion in March 2015. Of this, USD 5 billion of total external debt is debt that is disbursed and outstanding (DOD), while domestic debt is estimated at USD 3.1 billion.

Concerns remain over the rising cost of servicing domestic debt as a share of the budget, which is projected to have increased from 7% in FY 2014/15 to 10% in 2016/17. In this regard, during 2016/17, the government allocated UGX 2 91.08 billion towards interest payments, up from UGX 1 076.8 billion (15/16) and UGX 853.4 billion (2014/15). In the proposed budget for 2017/18, over UGX 2.7 billion, representing 12.2% of the resource envelope, has been allocated to interest payments due. In real terms, domestic debt stock increased from 10.9% of GDP in FY 2012/13 to 13.7% in 2015/16 also equivalent to UGX 7.05 trillion, driven by short-term government securities. According to the IMF 7th PSI, the average maturities of domestic debt is lower than one year.

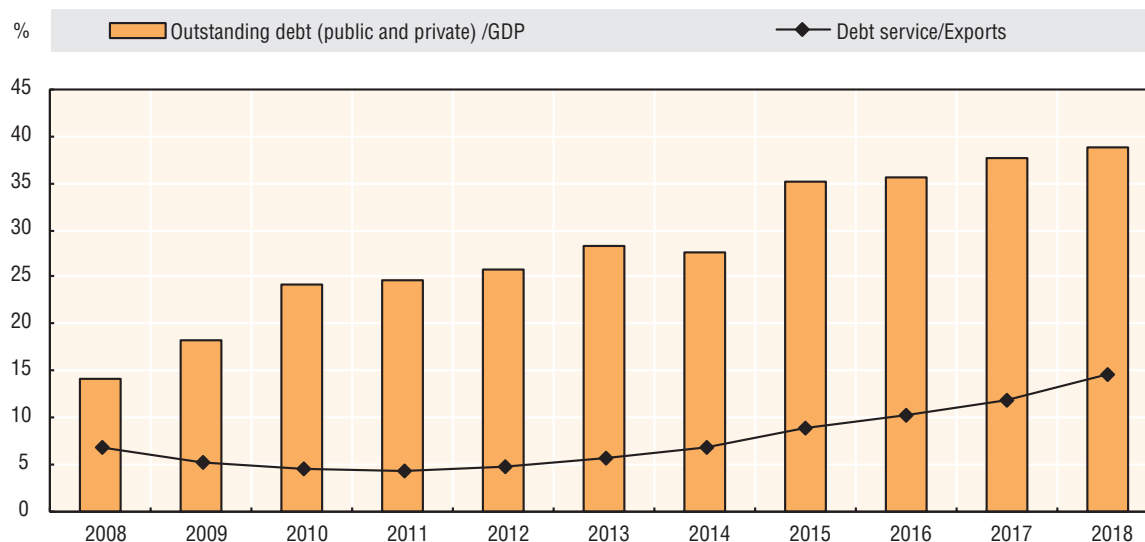
For the second year in a row, and in line with the Public Financial Management Act (PFMA) 2015, all interest payments on domestic debt repayments (securities) and maturing debts have been rolled over into the national budget for parliamentary approval. During the 2016/17 approved budget, UGX 4 977 billion, equivalent to 18.9% of the budget, has been allocated for domestic debt repayment. This item is set to increase to 28% of the national budget to UGX 6 258 billion in 2017/18.

The other indicators of debt stress remained stable; thus the PPG of debt-service-to-revenue ratio increased from 3.7% of GDP the previous year to 4.6% of GDP in 2016. Similarly, the PPG of debt-service-to-exports ratio stood at 3.4% of GDP in 2016 up from 2.7% of GDP in 2015, all indicating that debt levels are sustainable. To ensure the sustainability of the debt levels, a new medium-term Debt Strategy (2016-2021) was released in November 2016 and replaces the Debt Strategy 2013.

The sustainability of debt repayment will be underpinned by domestic revenue mobilisation against the backdrop of heavy infrastructure investment frontloading that necessitated increased domestic borrowing.



Figure 2. Stock of total external debt (percentage of GDP) and debt service (percentage of exports of goods and services)



Source : IMF (WEO & Article IV).

## Economic and political governance

### Private sector

Uganda's ranking in the World Bank report *Doing Business 2017* has improved by one place to 115th position out of 190 countries, compared to 116th/189 countries the previous year. Automation of the tax system and customs translated into a reduction in border compliance from 85 hours in the previous year to 71 hours in 2016, lower compared to the 101 hours average for SSA. Improvements were registered in five areas including: dealing with construction permits (+2); getting electricity (+7); registering property (+2); paying taxes (+1); and trading across borders (+5). Some indicators, however, declined implying the existence of challenges faced by enterprises. These include: starting a business (-3); getting credit (-2); protecting minority investors (-5); enforcing contracts (-3); and resolving insolvency (-7).

The government has continued with efforts to strengthen legislation that enhances private sector development and improves regional competitiveness. In 2015/16, various laws including the Capital Markets Authority Bill 2015, Financial Institutions Amendment Act 2004, and Public Private Partnership Bill 2014 were enacted to this effect.

Uganda's National Development Plan (NDPII 2015-2020) and Vision 2040 prioritises infrastructure development in the medium and long term; however, huge infrastructure deficits remain. The Vision 2040 projects paved roads to increase from 10% (2010) to 80% (2040). According to the *Annual Transport Sector Review Report* (2016), the percentage of the national roads network in fair to good condition stood at 78.5% for paved roads and 71% for unpaved roads. This implies that most freight is still being carried by road compared to rail freight at 3.5%, and calls for more investments in the transport infrastructure at large. Currently, Uganda spends approximately USD 1 billion per annum (or 11% of GDP) on infrastructure investments; however, huge financing deficits estimated at about USD 0.4 billion/year remain. The proposed budget for 2017/18 has allocated 35% of the budget for Transport, Energy and Mineral compared to 30% over the last FYs; however, rising concerns have been registered in relation to the persistent under execution

of public investment projects. There is need for reforms to strengthen public investment management.

## Financial sector

Uganda's financial system remained stable and resilient to shocks. According the IMF 7th PSI review of November 2016, the banking sector remained healthy, well-capitalised, and profitable despite non-performing loans (NPLs) that doubled to 8.3% in the year to June 2016, but later improved to 7.7% in September 2016. The rising NPL trajectory not only hit commercial banks, but also saw some bankrupt private businesses requesting government bailouts. Consequently, the BoU closed Crane Bank, the 3rd largest Ugandan bank due to undercapitalisation in October 2016. Similarly, private sector credit growth fell to 7.5% from 18.9% due to the low volume of loans.

Notwithstanding, the profitability of the banking sector increased by 11.5% to UGX 541.2 billion in 2015 compared to 2014, while banks' total liquid assets grew by 18.4% to UGX 6.9 trillion. Moreover, the total assets of the Credit Institutions (CIs) grew strongly by 25.3% to UGX 389.6 billion, while the ratio of liquid assets to total deposits stood at 46.6% in December 2015, up from 43.9% in 2014, almost double the 20% target. The outreach in bank branches also increased from 564 in 2014 to 573 in 2015, while automatic teller machines (ATMs) increased from 830 (2014) to 842 (2015).

Progress has been registered on the regulatory framework front following amendments of both the 2004 Financial Institutions Act (FIA) and the Capital Markets Act (CMA) in 2016. These two laws will expand financial inclusion and integration of the EAC capital markets meaning other EAC member states will now be able to trade in the Uganda securities markets. The FIA law provides for agent banking, bancassurance and Islamic banking in the same way as the Tier IV Microfinance Institutions Act 2016. It will provide oversight for Savings and Credit Cooperatives, moneylenders and microfinance institutions. More work remains to be done though to strengthen the monitoring of cross-border financial integration.

With regards to financial inclusion, improvements have been registered. Of Uganda's adult population, 85%, had access to and usage of financial services in 2013, up from 70% in 2009. The share of the population that banked with formal institutions (bank and non-bank formal) doubled from 28% (2009) to 54% (2013), while the non-banked share (such as users of mobile money services) rose from 7% to 34% during the same period.

## Public sector management, institutions and reforms

With regards to property rights and rule-based governance, various legal and regulatory reforms have been implemented since 2010 to computerise the land registry and improve the business climate. In this regard, six new zonal land offices were established in Kampala, Mukono, Jinja, Wakiso, Masaka, and Mbarara, while seven additional zonal offices are undergoing refurbishment. The computerisation process, in spite of disrupting surveys and mapping of new land titling, is expected to increase bank credit growth.

Corruption however remains a big bottleneck affecting businesses due to weak enforcement. According to Transparency International's (TI) 2016 index, Uganda's Corruption Perceptions worsened by eleven places to 151st position out of 176 countries from 2015. Similarly, the starting a business indicator declined by two places in the World Bank report *Doing Business 2017* to 165th position. This performance calls for further work on the legislative and regulatory framework to strengthen accountability. In a bid to improve the business environment, the Business Licenses (Miscellaneous Repeals) Bill 2015 was enacted in 2016 to repeal the Companies Act 2012, section 22(2), which abolishes the requirement for a statutory compliance for incorporating a company before starting a business.

The quality of public administration is improving, but a lot remains to be done to strengthen institutions. The Office of the Prime Minister, which is mandated with the co-ordination of

government programmes, continued to harmonise the programming of the legislative agenda resulting in the increased disposal of Bills in Parliament to 80% in 2016. Public financial management reforms continued to be implemented, including Integrated Financial Management Services, Treasury Single Account, and Output Oriented Budgeting. These reforms will go a long way towards strengthening the linkages between budgeting and results, as well as the quality of public administration.

### Natural resource management and environment

Uganda has lost about 14% of its forest cover between 2010 and 2015, thus a reduction from 24% in 1990 to 10% in FY 2015. The country's deforestation is estimated at about 1.8% per annum, with a cost of about 15% of GDP driven by encroachment of central forest reserves, illegal timber extraction and charcoal burning. In response, government embarked on reopening of wetland boundaries, demarcation of gazetted forest reserves, wetland restoration and re-afforestation. In 2015/16, a total of 1 341 ha 13.41 km<sup>2</sup> of wetland were restored compared to 1 802 ha 18.02 km<sup>2</sup> the previous year. Similarly, environmental policing has been stepped up since 2012/13 to enforce environmental laws and prevent the degradation of protected areas. With the commissioning of 153 officers to police lakes, forests and wetlands, a reduction in threat of forest encroachment is envisaged. Furthermore, six catchment management plans were developed in 2014 (including Mpanga, Maziba, Awoja, Ruhenzenda, Rwizi and Semiliki), while an additional 15-catchment management plans are under development. The next Forests Status report (under preparation) is due to be completed in 2017.

With regards to water and sanitation, the national access to safe water stood at 69% in June 2016 (67% rural, and 71% urban water access). Although access to rural water deteriorated by two percentage points to 86% in June 2016, urban water access registered improvements. By contrast, an improvement of two percentage points to 79% was registered in rural sanitation from last year compared to 84.6% in urban populations outside Kampala.

### Political context

The trajectory of overall governance in Uganda has improved by 3.4% over the last decade to 2016 driven by various factors. According to the Mo Ibrahim Index of African Governance (IIAG) 2016, an improvement of one and half percentage points was achieved with a score of 56.2% (out of 100) from 2015; however, Uganda's ranking remains unchanged at 19th position (out of 54) in Africa. Similarly, specific factors driving the improvements include rule of law (57.3%), participation (measured by political rights, political participation, free and fair elections, free and fair executive elections, effective power to govern and civil society participation) and human rights (59.6%). The indicator for economic opportunity (49.1%) stagnated owing to a continued infrastructure deficit. This performance not only puts Uganda above the sub-Saharan African average of 50%, but also above the EAC average score of 49%. Uganda is the fourth best EAC country after Rwanda's score (62.3%), Kenya (58.9%), Tanzania (56.5%).

The presidential and parliamentary elections held in February 2016, although well concluded, were challenged in the courts. The court, however, upheld the published results. Ethnic tensions remain in western Uganda in Kasese district, where violence erupted in the Rwenzuru Kingdom after militiamen belonging to the traditional monarchy clashed with government security agencies patrolling the district on 24 November. The clash resulted in a death toll of more than 100 people. Whereas calm is returning to the Kasese region, border conflict with DRC has also been reported recently. Uganda remains active in regional peacekeeping operations.



## Social context and human development

Uganda has made substantial progress as an early starter in the 2030 Agenda for Sustainable Development. Key highlights include: mainstreaming of the Sustainable Development Goals (SDGs) into Uganda's Second National Development Plan (NDPII), 2015/16-2019/20; alignment of Local Government Development Plans (LGDPs) to the NDPII and SDGs; ongoing alignment of sector development plans with NDPII and SDGs; and continuous dialogue with non-state actors and advocacy at various levels. This is an opportunity to finish the unfinished business of the MDG era.

### Building human resources

Uganda's population stands at 34.6 million (2014) with a density of 173 persons per square kilometre and is expected to reach 45.9 million by 2020. Of this population, 55% is below 18 years while 23% is between 18 to 30 years. The Total Fertility Rate (TFR) of 5.91 children per woman more than doubles the world average of 2.51 recorded between 2010 and 2015, and is higher than the East African Community (EAC) average of 5.14. The Human Development Index (HDI) remains low at 0.483 (2014).

Government introduced Universal Primary Education (UPE) and Universal Secondary Education (USE) in 1997 and 2007 respectively. Access to education has increased, with about 87% of children of primary school-going age (6-12 years) attending school in 2015. However, literacy improved slowly from 70% in 2002 to 72% in 2014. Literacy was lower for females (68%) compared to males (77%) and similarly lower in rural (68%) compared to urban (86%) areas in 2014.

Life expectancy improved significantly, from 50.4 years in 2002 to 63.3 years in 2014. The infant mortality rate (IMR) declined from 76 to 54 per 1 000 live births between 2006 and 2011, and declined further to 44 in 2015. Under-five mortality (UFM) declined from 137 per 1 000 live births in 2006 to 90 in 2011, and to 66 in 2015. Conversely, there has been a significant reversal in reduction of deaths due to malaria. In 2015/16, 43% of hospital-based under-five deaths were attributed to malaria, up from 23% in 2014/15 and 29% in 2013/14. Pneumonia (11%) and anaemia (11%) follow as the major causes of under-five mortality. Drug stock-outs and inadequate supply and retention of health professionals remain a problem. Uganda lacks a risk pooling mechanism, as the National Health Insurance bill has not been passed since 2007.

The Health Sector Development Plan (HSDP) 2015/16-2019/20 focuses on the development of health infrastructure and equipping and staffing health units. However, the Sector allocation has averaged 8.2% of the national budget between 2010/11 and 2015/16, below the HSDP and the African Union target of 15%. The Integrated Early Childhood Development (IECD) Policy and Action Plan was launched in 2016, and targets children up to eight years.

### Poverty reduction, social protection and labour

The Second National Development Plan (NDPII) 2015/16-2019/20 seeks to propel Uganda to a middle-income status and reduce poverty from 19.7% to 14.2% by 2020. Infrastructure investments in energy and transport will account for 32% of the five-year budget, followed by education (14.8%) and health (10.5%). Agriculture, in which 80% of households are engaged, will receive only 4.1%.

Per capita income increased from USD 715 in 2011/12 to USD 751 in 2014/15 and USD 765 in 2015/16. There is no up-to-date poverty statistics as the current poverty headcount of 19.7% is based on a 2012/13 Uganda National Household Survey (UNHS). The national poverty line is 0.53 of the international poverty line and has not been updated since 1993. Hence, it becomes a poor measure of poverty today. The Uganda National Panel Survey (UNPS) complements this information by monitoring income and service delivery dynamics annually. The chronically poor population was 9.8%, with the Northern (23.8%) and Eastern (15.5%) regions registering the highest incidence in 2015/16. About 23.4% of those without any formal education were chronically



poor compared to only 2.7% of those with secondary and higher levels. Agriculture has potential to reduce poverty significantly if transformed from being majorly subsistence. Only about 8% of agricultural households have been using improved seed since 2011/12. Irrigation usage was 1.4% in 2015/16. In 2012/13, Uganda had a working age population of 16.5 million out of which 13.9 million were actually working and 72% of them engaged in agriculture. Structural transformation has been very slow with 43% (6 million) of the working population engaged in subsistence agriculture. Overall, the proportion of females in paid employment was 37% and they are the majority (53%) for persons in self-employment.

About 93% of the labour force is not covered by the existing social protection initiatives. The Social Assistance Grant for Empowerment (SAGE) still makes up the core of Uganda's social protection system. It involves regular small transfers to persons aged 65 and over to guarantee a minimum level of income security. An evaluation of the SAGE pilot phase (14 districts) indicates that it generated positive impacts on food security, human capital development and sustaining livelihoods. The number of households eating fewer than two meals per day fell more than twice as rapidly in SAGE districts than in comparable non-SAGE districts and there were significant increases in employment and school attendance. Following the completion of the pilot in 2015, the government will roll out the grants to an additional 40 (out of 112) districts over the next 5 years. SAGE raises equity concerns since it does not cover a majority of the districts. The social protection inadequacy calls for identification of inclusive initiatives to meet human development needs of all vulnerabilities. The Uganda National Social Protection Policy was launched in 2016 and aims to increase access to social security and strengthen service delivery.

### Gender equality

Uganda has made commendable strides in reducing gender inequalities. There was near parity at primary (100%), secondary (90%) and tertiary (80%) education levels in 2015. The primary school pass rate in 2015 remained at 86% for female pupils compared to 90% for male pupils in the previous year, implying an almost equal chance of passing. There is 34% female representation in parliament, above the global (23%) and sub-Saharan Africa (24%) averages. This is attributed to the constitutional quota system for female district members of parliament. However, women are still unable to compete with men for directly elected parliamentary positions. Only 26.6% of firms have female participation in ownership. The median wage for females in paid employment has remained about half of that for males since 2005/06. In agriculture, the gender gap costs Uganda an estimated USD 67 million annually. Closing this gap would lift 119 000 people out of poverty. Eliminating these disparities requires interventions that allow women to have more access to production resources, but also engaging men in challenging social, economic and cultural gender biases.

### Thematic analysis: Entrepreneurship and industrialisation in Uganda

Industrial development is at a nascent stage in Uganda. The sector contributes on average 18% to gross GDP. The contribution of industry has been stagnating around this level for the last decade. Manufacturing accounts for 8% of GDP over the same period. The relative share of manufacturing also has not changed significantly over the last ten years. The industrial sector in Uganda is dominated by manufacturing accounting for 47% of the sector, followed by construction (37%), electricity (6%), water (2%) and mining and quarrying (8%) during the period 2011-15. The share of manufacturing declined from 49% in 2011 to 47% in 2015, while the share of construction increased from 36% to 37.0% during the same period. In terms of growth, overall industry and manufacturing grew by 4.7% and 3.3%, respectively, during the period 2011-15. Many factors constrained the performance of the sector: poor physical infrastructure, inadequate and poorly prioritised investment in research and development; limited technical and managerial skills; lack of financial infrastructure to support small and medium Enterprises (SMEs); deficiency in



technology; and lack of indigenous capability to adopt technology, which adversely affects on productivity.

Uganda has a vision to transform itself from a peasant to a modern and prosperous country by 2040. Industrial development is an integral and important part of the government's overall development strategy through, among other things, adding value by processing to reduce post-harvest losses, and by increasing exports of higher value products, especially from agricultural and mineral resources. The National Industrial Policy (2008) sets out the strategic direction for industrial development in Uganda over the next ten years. It was accompanied by the National Industrial Sector Strategic Plan (NISSP, 2010-2014/15). The policy vision is to build the industrial sector into a modern, competitive and dynamic sector fully integrated into the domestic, regional and global economies. The strategy focuses on the following key areas: i) exploitation and development of domestic, resource-based industries that use local raw materials; ii) promotion of agro-processing for value addition in niche exports; iii) encouraging knowledge-based industries such as ICT, call centres, and pharmaceuticals to exploit knowledge in science, technology and innovation, support engineering for capital goods, agricultural implements, construction materials, and fabrication; and iv) human resource development focusing on technical skills, promotion of entrepreneurship and management capacity. In addition to the overall industrial policy and strategy, Uganda developed sector specific policies and strategies such as the national textile policy; the leather policy, national sugar policy and the tea policy are in development.

Uganda is recognised as one of the most enterprising nations in the 2014 Global Entrepreneurship Monitor (GEM) report for having 35.5% of 18-65 year olds who are either nascent entrepreneurs or owners/managers of a new business. This means almost four Ugandans out of every ten are starting a business, making Uganda one of the world's most entrepreneurial nations. This is not surprising as over 73.1% of the total working population was self-employed in 2012/13. According to the same report, an average entrepreneur in Uganda is female, 18-34 years of age with at least secondary education, working in the consumer service sector largely in a small or micro business. The report further shows that women's participation rate in entrepreneurship has been steadily increasing since 2003 to the point where there are now more women than men engaged in entrepreneurship. Similarly, youth in Uganda are more engaged in entrepreneurship than adults. Ugandans have a positive attitude and less fear of failure, which are critical traits for successful entrepreneurship. Over a quarter of the businesses are discontinued for several reasons including, among others, lack of profitability, lack of finance, and personal decisions. There are still some negative perceptions, influences and attitudes towards self-employment despite higher earnings made by small entrepreneurs that are two to three times more than the official minimum wage. Despite the fact that many join the ranks of entrepreneur out of necessity rather than seeing it as a career with a promising future, many Ugandans increasingly see opportunity in starting up a business.

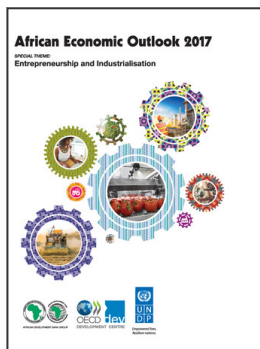
The role of entrepreneurship in industrial and private sector development is long recognised in Ugandan policy frameworks, although there is no dedicated strategy or policy towards it. In particular, the government has been promoting women and youth empowerment through entrepreneurship development. For example, the Micro, Small and Medium Enterprises (MSME) Policy (2015) embeds the objective of enhancing entrepreneurship through expanding and strengthening MSME programmes and their outreach, the integration of entrepreneurship development in vocational and technical institutions, as well as by promoting business networks. The Ministry of Trade, Industry and Cooperatives is the overall co-ordinator of industry and MSME policy. There are several initiatives aimed at promoting entrepreneurship development in the country implemented by government ministries and departments, the private sector, and public-private partnership arrangements, NGOs and UN agencies. Some of the programmes registered astonishing success. Enterprise Uganda, which is a public-private partnership organisation, offers the example of Modong Moses, a 31-year-old entrepreneur from Teso, eastern Uganda, who,

with support from a ground breaking training programme, was able to start up his own business of UGX 70 million (USD 20 000) with literally nothing but the shirt he was wearing.

Notwithstanding such anecdotal evidence, however, most of these initiatives are small in scale, fragmented, and short term, with limited impact. There has been limited co-ordination among the various actors involved in entrepreneurship development in Uganda. The Ministry of Trade and Industry and Cooperatives created a department in charge of MSMEs in 2016 with the view to co-ordinate effectively support for MSMEs. There are surveys including the Global Entrepreneurship Monitor (GEM) survey by Canada's International Development Research Centre and the Enterprise Survey by the World Bank to assess the entrepreneurship environment. Several of these surveys point out a number of constraints that needs to be addressed if entrepreneurs in Uganda are to achieve their full potential. There is inconsistency in policy direction towards entrepreneurship development, an unsupportive policy environment for business start-ups, as well a lack of co-ordination in efforts, capacity and skills gaps of entrepreneurs. Furthermore, there are limited financial services and weak linkages between small and large enterprises.

Uganda should consolidate its efforts through a coherent policy of entrepreneurship development, strengthening its capacity for implementation and co-ordination at all levels as well as consolidating the programmes that provide support to entrepreneurs in a systematic and sustained manner. The Buy Uganda Build Uganda Policy (BUBU) should be implemented more aggressively to generate demand for youth labour. It is important to note that the crippling high interest rate, above 23%, continues to pose significant challenges for business start-ups as well as growing businesses. The government, working with the private sector and other development actors, needs to seek durable solutions that provide affordable access to finance. There are promising initiatives by diverse actors from which key lessons could be drawn for scaling up support to the deserving and thriving entrepreneurs in Uganda.





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