Statement by Mr. Mkwezalamba, Executive Director for Uganda and Ms. Gasasira-Manzi, Advisor to the Executive Director
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The Ugandan authorities thank staff for the constructive policy dialogue during the mission on the 2017 Article IV Consultation and the eighth and final review of the economic program under the Policy Support Instrument (PSI). They broadly agree with staff's assessment of the country's macroeconomic policies and challenges in the staff report and welcome the useful analysis in the selected issues paper.

Uganda has maintained macroeconomic stability and made notable progress on the program under the PSI. However, both external and domestic challenges have contributed to disruption in trade and tightened financial conditions, while an influx of refugees from conflicts in the region has exerted significant pressure on social amenities and resources. These challenges have been compounded by subdued credit growth and the effects of climate change that resulted in a drought, which undermined agricultural production and food security. In response to these challenges, the authorities are taking deliberate measures to turn the economy around by enhancing agricultural production and accelerating the pace of industrialization.

The authorities have benefitted from the Fund's policy advice and engagement, and have implemented key recommendations from the previous Article IV consultation. They maintain their commitment to sound macroeconomic policies and seek the support of Executive Directors for the completion of the eighth and last review under the PSI. They intend to request a successor PSI arrangement in the Fall as they continue to strengthen their economic performance.

Program Performance

Performance under the current PSI has been broadly satisfactory. All end-December 2016 and continuous Quantitative Assessment Criteria (QAC) and most indicative targets were met through March 2017. The reserve accumulation floor was exceeded and the inflation consultation clause was observed. The indicative target on poverty alleviating expenditures were met. Despite a minor underperformance in revenue, owing to the slowdown in economic activity, the overall deficit remained lower than programmed at end-December 2016. There was a breach on the indicative target on the zero-ceiling for government guarantees as the government granted two guarantees to the Uganda Development Bank (UDB). This resulted from the need to recapitalize the UDB to avail affordable lending rates to priority sectors, and shore up private sector credit required to support sustained growth.

Despite some delays, the authorities continued to make progress on structural reforms. Progress was made on improving the AML/CFT regime with the approval of the Anti-Terrorism (Amendments) Bill 2017, Capital Markets Authority Act (Amendments), and the Insurance Bill, paving the way for exiting the FATF gray list. The pending reforms are related to the amendments to the Bank of Uganda (BOU) Act, publishing the report for the end-December 2016 unpaid bills, and the policy on regulation of mobile money.

Recent Economic Developments and Outlook

Growth slowed down in FY2016/17 to 3.9 percent from 4.7 percent recorded in FY15/16. The slowdown is attributed to the impact of an unusually long drought and the fall army worm outbreak that held back agricultural activity in the first part of the year, the slow recovery in private sector credit, and a slow execution of externally-financed public investment projects. Growth is expected to pick up to 5 percent in FY2017/18 with the improved weather conditions and recovery in private sector credit.

Inflation edged up, mainly reflecting the effects of the drought that affected food production in many parts of the country. Headline inflation in May 2017 was 7.2 percent and core inflation stood at 5.1 percent, in line with the BOU target of 5 percent. At its June 2017 Monetary Policy Committee (MPC) meeting, the BOU lowered its policy rate by 100 basis points to 10 percent, to ease the monetary policy stance consistent with the need to support economic growth and achieve the medium-term inflation target.

The external position was broadly consistent with fundamentals in 2016, with the current account deficit projected to narrow in 2016/17 owing mostly to increased export earnings and decreased Government and private sector imports. However, the current account deficit is expected to temporarily widen over the medium term on account of increased imports related to investments in infrastructure and the oil sector. International reserves stood at 5.1 months of prospective imports, in line with the agreed convergence criterion of 4½ months of imports in the East Africa Community (EAC) Monetary Union protocol.

Fiscal Policy

The medium term fiscal framework remains anchored to the Charter of Fiscal Responsibility (CFR). The Charter aims to achieve an overall fiscal deficit of no more than 3 percent of GDP by FY2020/21, in line with the EAC convergence criteria, and government debt below 50 percent. The fiscal deficit for FY2016/17 is expected to be lower than anticipated at about 3.6 percent, owing to the slow execution of externally-financed public investment. However, for FY 2016/17, it is expected to widen to about 5.5 percent, owing to the expansionary fiscal stance to support government's infrastructure development plan. On the other hand, the authorities remain committed to safeguarding debt sustainability. As of December 31, 2016, Uganda's external and domestic public debt amounted to about 33.8 percent of GDP, and although it is trending upwards, the authorities are committed to keeping it below the Charter's ceiling.

Progress has also been made in domestic revenue mobilization, although revenue performance remained subdued due to the slowdown in economic activity. Tax revenue is projected to reach 14.6 percent of GDP in FY2017/18 compared to 13.6 percent estimated for FY 2016/17. The authorities' revenue mobilization strategy will focus on tax administration and building a stronger compliance culture. This will be enhanced through taxpayer education, strengthening detection of non-compliant taxpayers, recovery of tax arrears, and combatting smuggling, undervaluation and under declaration. The automation of online assessments and electronic tracking of transit goods is also underway.

The authorities intend to compress current expenditure in FY 2017/18 by 0.4 percent of GDP compared to FY 2016/17, while protecting social spending. The authorities remain committed to the clearance of arrears and have earmarked resources in the FY 2017/18 budget for this purpose. In addition, the authorities are implementing measures to ensure avoidance of the recurrence of arrears. These include sanctions for all accounting officers who accumulate new arrears, withholding of future disbursements for government departments that delay payments for goods and services, use of prepaid payments for utilities, and full utilization of the Integrated Financial Management and Information System (IFMIS).

The authorities remain committed to social empowerment programs and continue to allocate resources to projects under the Youth Livelihood Program and the Uganda Women Entrepreneurship Program (UWEP). In addition, a pilot program under the Social Assistance Grant for Empowerment (SAGE), in which senior citizens receive cash transfers, is ongoing.

Under-execution of externally financed projects was largely due to capacity constraints in project implementation, land acquisition, and delays in the procurement process. Steps are being taken to eliminate delays in procurement and build capacity across government to improve project cycle management, including through amendment of the Public Procurement and Disposal of Public Assets (PPDA) Act. The authorities appreciated recent Fund Technical Assistance on Public Investment Management, and remain committed to fully implement the recommendations.

Monetary and Financial Sector Policies

The inflation targeting framework has served Uganda well. BOU continued its easing cycle that started in April 2016, and since then, the Central Bank Rate (CBR) has been reduced by 700 basis points to 10 percent, successfully containing inflation within the target. Expectations are for an increase in headline inflation in the near term and core inflation remaining within the band, around the 5 percent target. The monetary policy stance will continue to be guided by the inflation forecast as well as a careful assessment of both domestic and external risks.

The banking sector remains sound and resilient with banks well capitalized and liquid. Non-performing loans (NPLs) remain a concern as there are still many in the watch category. Following the failure of a large commercial bank last year, the BOU is stepping up measures to strengthen its supervision and monitoring framework to ensure stability, including through focusing on banks' risk management frameworks.

The authorities continue to make progress on financial deepening with the introduction of agency banking, Islamic banking, and mobile banking. They also plan to expedite the pension and insurance sector reforms to mobilize domestic savings and finance for long term capital. In addition, the Microfinance Institutions and Money Lenders Act was passed to regulate the activities of microfinance institutions, including Savings and Credit Cooperative Organizations (SACCOs), money lenders, and credit institutions, while promoting savings and enhancing inclusion. Further, to support private sector credit growth, the government plans to reduce domestic borrowing in the short to medium term. Given the implications to monetary policy management, the authorities plan to strengthen fiscal-monetary policy coordination.

Structural Reforms

The authorities are progressing with the reform agenda aimed at promoting an environment conducive for investment and private sector development. To this end, they are developing demarcated industrial and business parks; investing in infrastructure to reduce the cost of doing business, especially in the energy and transport sectors; and supporting Small and Medium Enterprises (SMEs) through skills development as well as improving access to financing.

The agricultural sector remains the mainstay of the Ugandan economy contributing significantly to food production, export earnings, and employment creation. In view of the sector's susceptibility to the vagaries of weather, the authorities plan to adopt pro-active mitigation measures, including fast-tracking irrigation and vigorously promoting agro-processing and extraction of minerals to boost industrialization. This two-pronged approach is expected to address unemployment and deliver inclusive growth and development.

The government is putting in place measures to improve public sector efficiency and eliminate corruption. The leadership code was amended to permit confiscation of properties acquired through corruption, and a directorate was established in the Inspectorate of Government to handle high profile cases. The Financial Intelligence Authority has also been strengthened to adequately enforce the AML/CFT, in collaboration with international financial intelligence authorities.

Conclusion

The authorities remain committed to reinvigorating growth and achieving poverty reduction and equality. The implementation of an economic reform program supported by the IMF's Policy Support Instrument (PSI) has been instrumental in achieving economic stability and supporting durable and inclusive growth. It has also helped catalyze support, both financial and capacity building, from other development partners towards the socio-economic transformation agenda.

Adequate support is particularly important at a time when the authorities are experiencing pressures emanating from the influx of nearly one million refugees from regional conflicts. A solidarity conference held in Uganda on June 30, 2017 raised pledges of $358 million from the international community out of the $2billion estimate required to help Uganda tackle one of the world's fastest growing refugee crises.

The Ugandan authorities continue to value the engagement with the Fund. Considering the country's satisfactory performance and strong commitment to pursue reforms, they look forward to Executive Director's support towards the completion of the eighth and last review of the PSI.