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Uganda: Fourth Review Under the Policy Support Instrument and Request for Modification of Assessment Criteria—Staff Report; Staff Supplement; Press Release

In the context of the fourth review under the policy support instrument and request for modification of assessment criteria , the following documents have been released and are included in this package:

- The staff report for the Fourth Review Under the Policy Support Instrument and Request for Modification of Assessment Criteria, prepared by a staff team of the IMF, following discussions that ended on March 21, 2012, 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 May 18, 2012. 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.

- A staff supplement on the Joint IMF/World Bank Debt Sustainability Analysis.

- A Press Release dated June 5, 2012.

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*
Technical Memorandum of Understanding*

*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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UGANDA

Fourth Review Under the Policy Support Instrument and Request for Modification of Assessment Criteria

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

Approved by Roger Nord and Dominique Desruelle

May 18, 2012

Discussions: Held in Kampala during March 7-21, 2012. The mission met with Finance Minister Kiwanuka, Bank of Uganda Governor Tumusiime-Mutebile, Permanent Secretary/Secretary of Treasury Kassami, and other senior officials, as well as the media, representatives of parliament, the private sector, NGOs/CSOs, and development partners.

IMF team: T. Richardson (head, resident representative), G. Oestreicher and N. Mireku (all AFR), P. Wingender (FAD), and S. Wang (SPR). A. Ndyeshobola (OED) and R. Sebudde (World Bank) participated in the discussions. The mission was supported by the staff of the Kampala office of the Fund, all of whom are seconded from the Bank of Uganda.

Fund relations: The 3-year PSI-supported program was approved by the Executive Board on May 12, 2010. The Board completed the Third Review under the PSI in January, 2012, and concluded the 2010 Article IV consultations in February 2011.

Fourth Review under the PSI: All the quantitative assessment criteria were met at end-December; and most of the structural benchmarks were met. Staff is proposing modified/ new targets for end-June 2012 and end-December 2012, along with additional structural benchmarks aimed at improving budget process and tax policy.

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List of Acronyms

BoU	Bank of Uganda
CBR	Central Bank Rate
CNOOC	Chinese National Overseas Oil Company
CSOs/NGOs	Civil Society Organizations/Non-Governmental Organizations
EAC	East African Community
ENCB	External Nonconcessional Borrowing
FAD	IMF Fiscal Affairs Department
FSAP	Financial Sector Assessment Program
GAPR	Government Annual Progress Report (PRSP update)
GDP	Gross Domestic Product
HIPC	Highly Indebted Poor Country
IT/ITL	Inflation Targeting/Inflation Targeting "Lite"
MCM	IMF Monetary and Capital Markets Department
MDRI	Multilateral Debt Relief Initiative
MEFP	Memorandum of Economic and Financial Policies
MoFPED	Ministry of Finance, Planning and Economic Development
NCG	Net Credit to Government
NDA	Net Domestic Assets
NDP	National Development Plan
NFA	Net Foreign Assets
NIR	Net International Reserves
NPLs	Non-performing Loans
OECD	Organization of Economic Cooperation and Development
OED	IMF Office of Executive Director
PAF	Poverty Alleviation Fund
PAYE	Pay As You Earn
PFA	Public Finance Act (draft)
PIP	Public Investment Plan
PFM	Public Finance Management
PRSP	Poverty Reduction Strategy Paper
QAC	Quantitative Assessment Criterion
TMU	Technical Memorandum of Understanding (part of MEFP)
UBOS	Uganda Bureau of Statistics
URA	Uganda Revenue Authority
VAT	Value Added Tax

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EXECUTIVE SUMMARY

The monetary tightening initiated in July 2011 has been effective. High interest rates have strengthened the currency and led to higher reserves, while private sector credit growth and overall demand pressures are much reduced. Prices have been generally stable for the last few months and annual inflation is coming down. The deflationary effort has caused little discernable adverse effect on financial sector stability, but there has been a significant cost to the real sector, where the tighter policies combined with weaker global demand is projected to reduce growth from 6¾ to 4¼ percent. The Bank of Uganda intends to pursue a policy of cautious easing over the months ahead as inflation comes down.

Fiscal policy was very tight until the fourth quarter of the fiscal year. Cyclical weakness in revenue and rising spending pressures—motivated in large part by the deteriorating regional security situation—are now expected to lead to a ¾ percentage point of GDP deterioration of the domestically-financed deficit. Although the slippage is regrettable—particularly on budget credibility grounds—staff sees justification for this modest expansion in the deficit on counter-cyclical grounds, given the weakness in growth. Staff also finds credible the authorities' intension to have monetary policy compensate for the resulting fiscal impulse to protect the deflationary path.

The FY2012/13 budget will consolidate the fiscal position moderately, while introducing measures to place public finances on a more secure footing going forward. To this end, the authorities are initiating a number of tax policy measures to create a small revenue cushion—mostly through suspension of existing VAT and corporate income tax exemptions and holidays. These measures, to be augmented by a comprehensive reform of tax exemptions linked to a new tax procedure code now in preparation, are expected to create a foundation for improved revenue and budget performance over the medium term.

Key risks to the outlook are external. Slower than expected global growth would worsen the trade deficit, and possibly hit remittances and capital flows. Higher energy prices would dampen growth, as would a deterioration in the regional security environment.

This review includes an assessment of the authorities' poverty reduction strategy paper (PRSP) annual update. Termed the Government Annual Progress Report (GAPR), it notes areas of progress with the National Development Plan, especially with regard to infrastructure as a key bottleneck to growth and poverty reduction. A Debt Sustainability Analysis (DSA), done jointly by the World Bank and the IMF, establishes that Uganda continues to face low risk of debt distress.

All end-December 2011 quantitative assessment criteria were met, as were most of the structural benchmarks under the PSI.

Staff supports the authorities' request to complete the fourth review.

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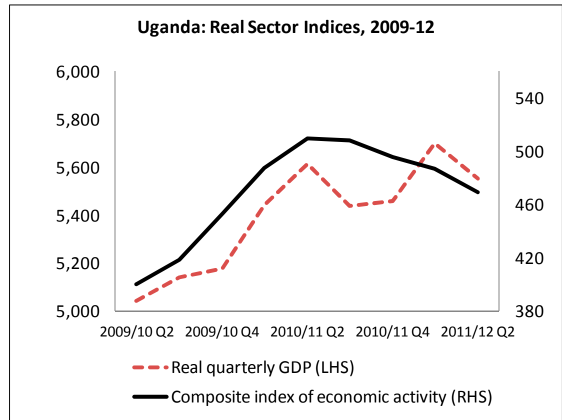
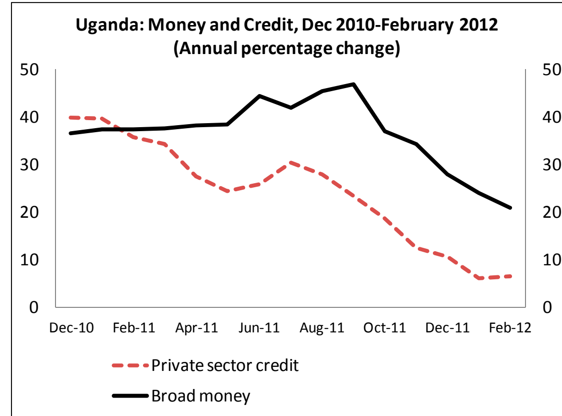
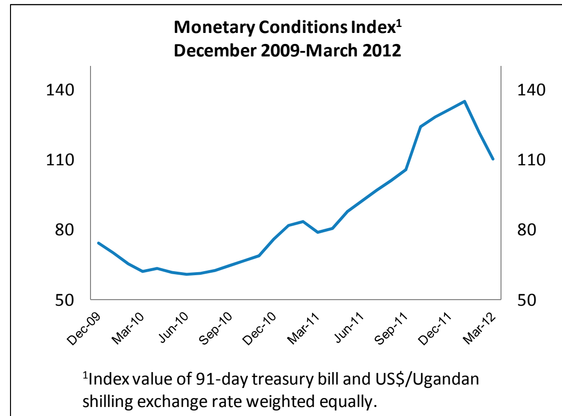
I. Recent Developments

1. **Tighter monetary conditions are having the intended effect** (Figure 1). Successive policy rate hikes and supportive liquidity management have raised the interest rate structure and significantly reduced underlying inflationary pressures. Exchange rate depreciation since January 2011, which peaked at 24 percent in September, has now been largely reversed, facilitated in part by strong non-resident demand for high-yield domestic securities. The strengthening currency moderated the rise in traded goods prices, while the dampening effect of high interest rates on money supply, credit, and private sector profits reduced demand pressure in the non-tradables sector.

2. **Growth estimates have been revised down from 5 to 4¼ percent for FY2011/12**—and from 6 to 5½ percent in FY2012/13 (Figure 2, Table 1). Weaker activity in the construction and industrial sectors reduced quarterly GDP growth in September and December, reflecting softer external demand, especially from Europe (UK), as well as demand shortfalls from monetary tightening and the effect of inflation on real incomes. Credit and monetary growth both declined since October, and there are indications of lower operations and payrolls in some industries. Public sector wages remain unadjusted for inflation and available evidence—including from real declines in VAT and excise taxes—suggest a slowing of overall consumption spending







3. **In light of the moderation in underlying inflationary pressure, the BoU has signalled a cautious easing of the monetary policy stance going forward** (Table 2). In February, the policy rate was reduced by 100 basis points, from 23 to 22 percent, and by another percentage point in early March. The policy stance nonetheless remains very tight, and capital inflows and domestic portfolio shifts from foreign to domestic currency continue to support the shilling. Inflation is expected to reach single digits by end-2012, and to approach the BoU's target range of 5 percent for core inflation by June 2013.

4. **The fiscal stance was tight for most of the year, but was relaxed somewhat in the fourth quarter, partly to compensate for underperformance of revenue** (Figure 3, Table 3). The overall deficit is now expected to

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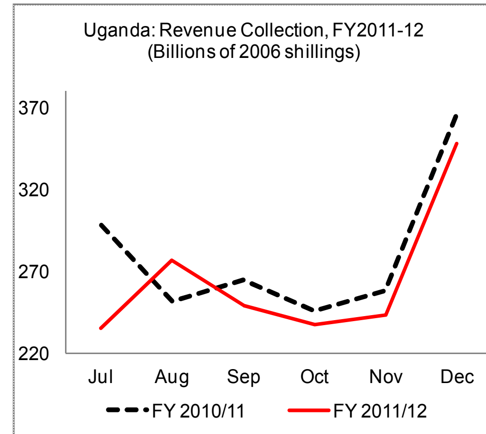
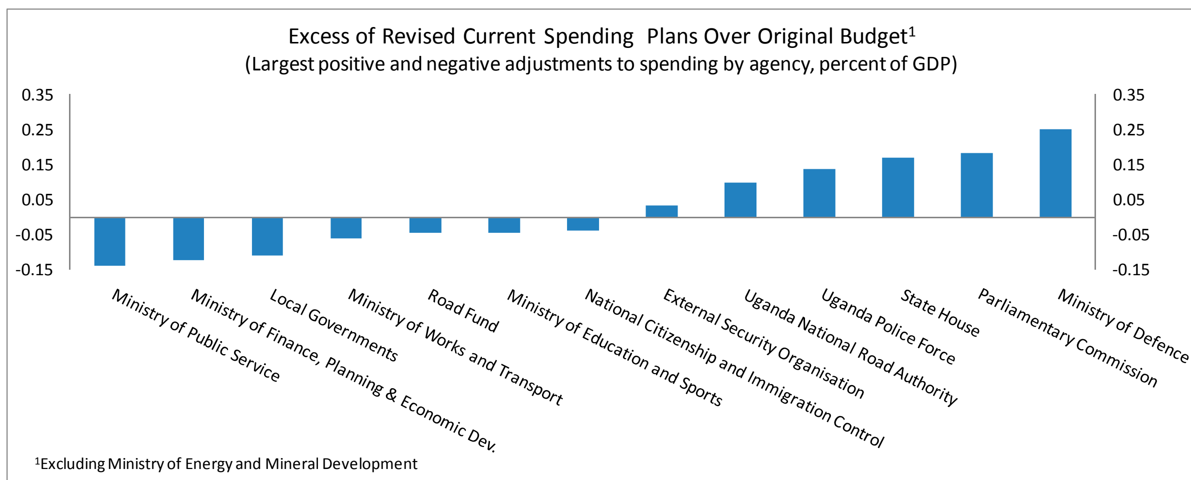
reach 4.7 percent of GDP, which is 0.9 percentage points higher than programmed, but still 2½ percentage points lower than last year. The shortfall will be financed by additional domestic borrowing.

5. **Revenue growth over the year did not keep pace with the rapid rise in inflation**. Tax collections fell by about 6 percent in real terms during the first half of FY2011/12, reflecting mainly a slowdown in growth and dislocation resulting from the high inflationary environment. End-year nominal tax revenues are expected to underperform program projections by about 0.8 percentage points of GDP.



6. **Current expenditure is being maintained at close to program targets in nominal terms**, which represents considerable restraint given that inflation has significantly eroded expected purchasing power—in real terms, total expenditure and the wage bill declined by about 11 and 8 percent. The authorities also implemented a 42 percent increase in electricity tariffs in January, which moved the sector to full cost recovery, saving about ½ percent of GDP in power sector subsidies this year, and eliminating the need for subsidies altogether in subsequent years. In addition, remaining power sector arrears are being regularized through negotiated formal repayment schedules with the generating companies.

7. **However, the composition of expenditure was significantly altered by supplementary budgets in the fourth quarter**. The authorities rearranged 1.1 percent of GDP of spending priorities, partly by increasing military and police spending in response to rising regional security concerns. Of this amount, expenditure totaling just under 0.4 percent of GDP was also diverted from originally scheduled uses to fund additional current spending of the presidential administration and the parliament. Offsetting cuts were made in other areas, chiefly transfers to local governments, resulting in an increase in current spending by ¼ percentage point of GDP at the expense of capital outlays. The authorities still hope to



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meet the indicative program floor on Poverty Action Fund spending, but have requested a modification of the end-June ceiling on net banking system claims on government (NCG) that would raise it by about ¾ percent of GDP to minimize the distortion. Staff regretted the supplementary spending because it undermines budget credibility, and expressed to the authorities serious concern about the reallocation of spending away from poverty alleviation and infrastructure investment. The authorities nevertheless considered these expenditures to be unavoidable.

8. **The current account deficit is expected to deteriorate somewhat in FY 2011/12** to about 12½ percent of GDP (Figure 4, Table 4). The deterioration was mainly due to weakened external demand, growing import bills, and lower official transfers from a delayed payment of capital gains taxes.[1] The exchange rate weakened during the first half of the fiscal year, owing mainly to nonresident concerns about the macro-outlook, but it has since recovered due to rising loan disbursements and inflows of short-term capital induced by tighter monetary policy. Gross international reserves have increased and reserve cover is expected to reach US$2.35 billion by end-FY 2011/12 (about 3.7 months of future imports).

II. Program Performance

9. **The Executive Board completed the third review under the PSI on January 13, 2012**. Six of the seven quantitative assessment criteria (QAC) were met. However, the end-June 2011 QAC on net credit to government was missed by a wide margin due mainly to overspending on wages and roads. A waiver of nonobservance for the missed QAC and completion of the review were based in part on the authorities' commitment to a number of corrective fiscal actions, including better intra-year monitoring of spending.

10. **All end-December 2011 QACs were met** (Table 5). While the indicative target on reserve money was overshot, this was due to over-performance on NIR and staff considers it did not compromise the inflation objective. Structural measures under the program were partly met (Table 6). Government is publishing release data for utilities (water and power), but sanctions are not being applied for accounting officers who run arrears. The National Identification card system is seriously delayed, but Government is committed to completing the roll-out as soon as possible.

III. Policy Discussions and Risks

A. Overview

11. **Policy discussions centered on the policy stance required to bring the disinflation effort to a successful conclusion**. Staff also reviewed the authorities' Annual Government Annual Progress Report, which constitutes the annual progress report for the National Development Plan (NDP – their poverty reduction strategy paper).

[1] The farm-down sale of Tullow Oil's stake to CNOOC and Total attracts capital gains tax, but the amount is in dispute, so payments thus far are less than previous expectations.

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12. **Progress has been made under the NDP but overall implementation has been relatively slow**. The five-year NDP, launched in April 2010, sets development objectives—including those related to poverty reduction—to be met by the end of FY2014/15. The de facto modality of progress tracking is that the annual assessment is produced in the GAPR, followed by a mid-term report by FY2012/13, and a final report at the end of the horizon. During FY2010/11, which covers the first 12 months of the NDP, the achievement rate was 60 percent for those annual targets for which data was available.

13. **Looking forward, the challenge is to fully meet all NDP objectives.** According to the GAPR, the trajectory towards achieving a large number of targets by FY2014/15 is not encouraging—48 percent of the NDP final targets are either on course to be missed or data to perform the assessment is not yet available. Based purely on the performance indicators where trend data was available for FY2010/11, 53 percent appear to be on track to achieve their targets, a further 20 percent may be achieved if implementation is accelerated, and the remaining 27 percent are unlikely to be achieved at the current rate of implementation. Staff encouraged the authorities to revive their focus on the NDP and to integrate it more efficiently with the planning of public investment projects.

B. Outlook and Risks

14. **A modest recovery in growth and continued reduction of inflation is projected for FY2012/13**. Growth is expected to be supported by a gradual easing of the monetary policy stance, an increase in low-cost electricity production from a new hydro plant, higher investment spending—particularly on the Karuma hydropower project—and by a more accelerated development of the oil sector facilitated by the recent signing of a farm-down agreement between Tullow Oil and partners Total and CNOOC. A gradual easing of monetary policy over the next year should bring inflation to single digits by December, and to the BoU's target level for core of 5 percent by June 2013. External debt will increase over the medium term with increased borrowing for infrastructure, but is expected to remain well within policy-dependent debt vulnerability thresholds.

15. **The external current account deficit will remain high over the medium term**, due to an expansion of infrastructure and oil sector investment. The start of oil sector development would imply initial deterioration in the current account during the investment phase, but such investment would carry its own financing and, over the longer term, result in a significantly improved external position after production begins. Over the medium term staff expects reserve cover and the underlying external position to improve moderately, particularly in 4-5 years when the oil sector comes on line. But downside risks certainly remain as external demand remains weak and government's capacity to manage large infrastructure investment is still nascent.

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Box 1. Key Risks to the Outlook

The main risks Uganda faces are external:

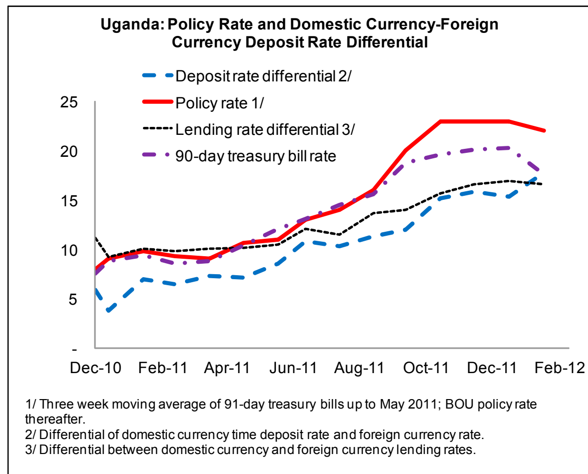
- **A global slowdown** in excess of current projections, especially for the UK and eurozone, would harm the trade balance, which is already weak. It could also affect remittance and capital flows, and possibly also reduce ODA.
- **Higher energy prices** would pass through to inflation and growth.
- **The regional security situation could deteriorate**, particularly in the Sudans. This factor, or a renewal of violence in Kenya connected with the 2013 elections, would weaken growth.

Domestic risks to the outlook would include concerns about possible budgetary expenditure arrears and potential banking system asset quality problems, given tight monetary conditions. (See below.)

C. Monetary and Financial Sector Policies

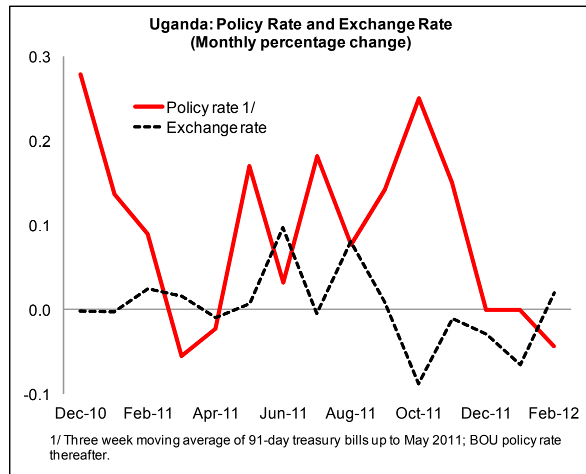
16. **The authorities intend to pursue a cautious pace of monetary easing to allow inflationary expectations to firm and avoid rekindling price pressures**. While the base effect will ensure headline inflation does not reach single digits until late 2012, underlying inflationary momentum is already waning. Monthly prices began decelerating rapidly in the last months of 2011, and are now running at an annualized rate of less than 5 percent. The rapid disinflation experienced in recent months has demonstrated that the monetary policy tools available to the BoU give it significant influence over key operational variables such as domestic interest rates and the exchange rate.

The relative rate of return on shilling-denominated assets increased with the Bank of Uganda policy rate...



1/ Three week moving average of 91-day treasury bills up to May 2011; BOU policy rate thereafter.
2/ Differential of domestic currency time deposit rate and foreign currency rate.
3/ Differential between domestic currency and foreign currency lending rates.

...leading to capital inflows and domestic portfolio shifts from foreign to domestic currency, which supported the exchange rate.



1/ Three week moving average of 91-day treasury bills up to May 2011; BOU policy rate thereafter.

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17. **The challenge facing BoU is how to ease the policy stance while anchoring inflationary expectations**, particularly to avoid a destabilizing repatriation of short-term capital flows. About 14 percent of outstanding government securities are held by nonresidents. Staff noted that maintenance of positive real interest rates at levels that pay due regard to the implicit risk premium will be key. The authorities acknowledged this factor, and expressed confidence that positions would unwind smoothly, given their intention to follow a slow and orderly transition to a lower interest rate structure. Specifically, the reserve money target for December 2012 incorporates an annualized growth rate of 16 percent, which staff considers adequate to accommodate first round effects of recent power sector tariff increases while keeping monetary conditions relatively tight, and at the same time providing the BoU with the flexibility it needs to carry out its deflationary program under uncertain conditions.

18. **The BoU remains committed to an eventual move to full-fledged inflation targeting (FFIT)**. Their current monetary policy framework remains a hybrid—a nascent inflation targeting regime, known in Uganda as "inflation targeting lite" supplemented by a reserve money program (RMP) under PSI conditionality—particularly the QAC on net domestic assets (NDA). The authorities have requested technical assistance from MCM on the design of a roadmap to FFIT, and are mindful of several areas of reform which need early attention along that roadway. These include: a clear definition of which measure of inflation to target, the appropriate legal protections and powers guaranteeing central bank operational independence, macro-modeling capacity, and production of an inflation report. In the interim, they agree it would be premature to anchor conditionality under the PSI on an inflation consultation clause, and instead have asked that the inflation corridor be added as a memorandum item to MEFP Table 1 so that they may begin building credibility in this regard.

19. **The banking system remains solvent, liquid and profitable, despite pressure associated with the recent monetary policy cycle.** Stress tests carried out during the recent FSAP mission indicated that the banking system was quite resilient to modest interest rate and growth shocks. Financial sector indicators for December offer confirmation of this assessment (Table 7). In addition, bank profits have risen sharply recently on the basis of higher interest revenue from government securities and the rapid pass through of higher rates to variable rate loans—providing an additional cushion against adverse developments. Staff nonetheless noted a small increase in nonperforming loans in December, and stressed the need for enhanced vigilance as the continued high interest rates and low rate of economic growth could result in a further deterioration in asset quality.

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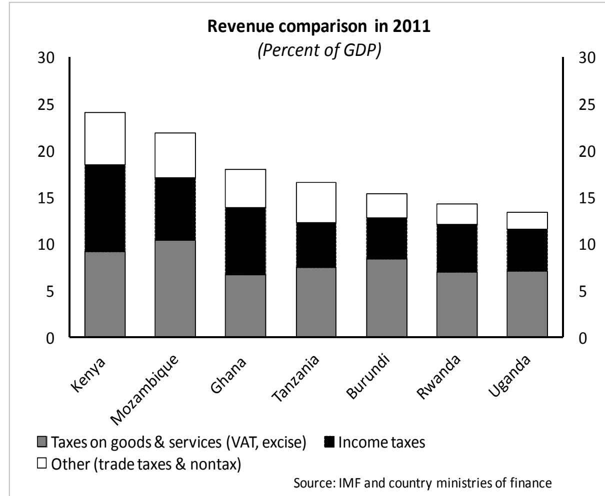
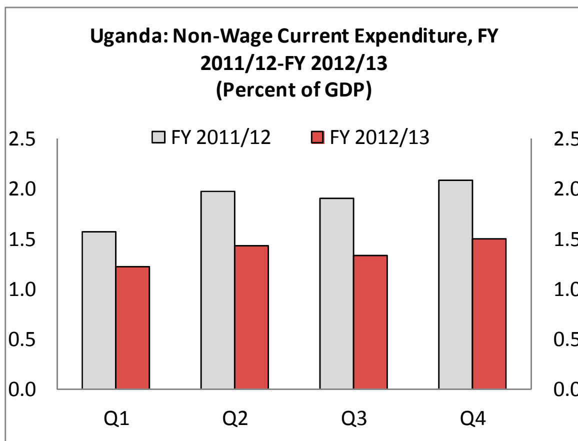
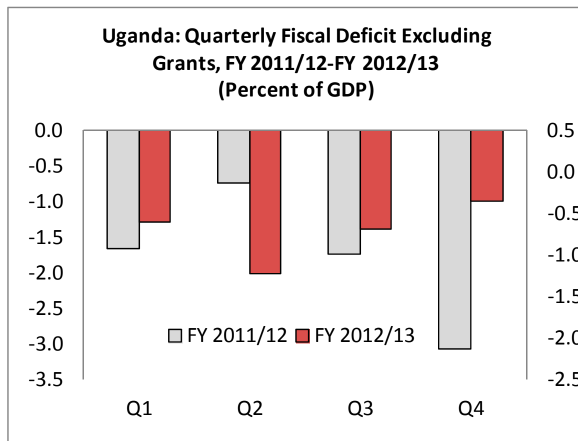
D. Fiscal Policy

20. **The fiscal program for FY2012/13 will provide some consolidation relative to the expected FY 2011/12 outturn to maintain support for disinflation**, as well as tax policy and structural measures designed to place public finances on a more secure footing going forward. The overall fiscal deficit is projected to decline by 1¼ percentage points to 3½ percent of GDP next year, while accommodating a 1 percent of GDP increase in capital spending. This adjustment is to be funded mainly by 2 percentage points of GDP of savings from compression of current expenditure—about 1½ percentage points of which will result from the cessation of one-off outlays on exceptional security procurement, power sector subsidies, and clearance of power sector arrears. Capital spending in FY2012/13 will be dominated by the start of construction of the Karuma hydropower project, which will absorb almost 2 percent of GDP (35 percent of total domestically funded investment), all of which will be funded by accumulated savings in the Petroleum Fund.



21. **Staff expressed concern about the risk of expenditure arrears or yet another supplementary budget in late FY 2012/13**, given the relatively low level of nonwage recurrent spending in the proposed budget. The authorities agreed that the required compression would require a significant effort, but saw room to effect the needed adjustment without jeopardizing spending priorities. However, they concurred with the need for realism in the budget and for risk mitigation mechanisms, and therefore proposed to set aside a contingency of about ¾ percent of GDP within the program fiscal envelope to accommodate likely spending pressures during the second part of next fiscal year. In this regard, their approach presages the draft Public Finance Bill, which would also establish an explicit contingency as part of the budget process. It was agreed that the fiscal program for FY 2012/13 would assume this contingency is activated. To further mitigate risks, the authorities will also set quarterly cash allocations in a manner that promotes a more even distribution of the deficit over the year.





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Fiscal Operations, FY 2010/11 – FY 2012/13
(Percent of GDP)

	FY 2010/11	*FY 2011/12*	*FY 2012/13*	
			Proposed Budget 1/	**PSI Program**
Revenue and grants	**15.6**	**14.8**	**15.3**	**15.3**
Expenditure	**22.8**	**19.5**	**18.0**	**18.7**
Current	15.3	11.3	9.2	9.2
Development and net lending	7.0	7.5	8.7	8.7
Other, o/w:	0.5	0.7	0.1	0.8
Contingency	0.0	0.1	0.0	0.7
Overall balance	**-7.2**	**-4.7**	**-2.7**	**-3.5**
Financing	**7.2**	**4.7**	**-2.7**	**3.5**
External	1.4	2.7	1.7	1.7
Domestic	5.9	2.0	1.1	1.8
Memo: Current including contingency	*15.3*	*11.4*	*9.2*	*9.9*

1/ Budget Framework Paper 2012/13

22. **The authorities agreed to include revenue enhancements in the draft 2012/13 Finance Bill.** These would yield about ¼ percent of GDP of additional revenue—achieved mostly through suspension of some existing VAT and corporate income tax exemptions and tax holidays (Box 2). Staff supported the implementation of these revenue measures, but saw them only as a necessary first step towards reforming the extensive system of tax exemptions that contributes to Uganda's poor revenue performance. The authorities agreed that the tax system in its present form is not delivering enough revenue to fund their planned infrastructure development, and accepted there would be benefit from streamlining exemptions. However, they considered cross-country differences in revenue performance to be closely linked to differing economic structures and variations in the efficiency of tax administration. In the latter regard, they therefore intend to carry out a systemic review of tax procedures this year to identify areas where tax yields could be increased—and will submit a draft tax procedure code to cabinet by April 1, 2013 (structural benchmark), and to parliament in June.

23. **Staff urged the authorities to address other pressing structural needs in the fiscal sector.** Improvements are needed to the budget process—for example, the FY2011/12 budget was only passed in October 2011, three months after the fiscal year began, and within-year fiscal reporting is inadequate. Staff stressed the benefits of early passage of the new draft Public Finance Act, which—if passed by Parliament in sensible form—would address a number of PFM-related concerns, including transparency and accountability in the oil sector. In this latter regard, staff urged the adoption of full transparency in the petroleum sector, including through the publication of production sharing agreements (PSAs) and making rapid progress towards becoming EITI-compliant. The authorities expressed commitment to the EITI process, but were reluctant to publish the PSAs, which they regard as confidential and market sensitive. In preparation for the commencement of oil production, staff also advised the authorities to develop greater capacity to accurately project oil revenues and monitor concession agreements. The authorities are considering requesting IMF technical assistance in this area.

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Box 2. Tax Policy Measures for FY 2012/13

Measure	Est. Tax yield (Ush bn.)
VAT	
Reinstate VAT on water	22
Terminate VAT exemption on textile sector	15
Standard rate the supply of hotels outside Kampala	7
Extend VAT to computers	30
Excise tax	
Increase excise duty on locally produced spirits from 45% to 60%	3
Change excise regime for cigarettes from specific to ad valorem at 130%	20
Impose excise duty on imported fresh juices	3
Income Tax	
Terminate exemption on agro-processing business income	2
Additional 10 percent marginal rate for top bracket of personal income tax	1
Tighten scope of exemption on plant and machinery and civil works	5
Withholding Tax for Interest and Dividends	
Increase the rate from 15 to 20%	21
Administrative Measures	
Enforce existing capital gains tax on sale of commercial building by individuals	1
Total	**130**

E. External Borrowing and Debt Sustainability

24. **The authorities have requested an augmentation of the external non-concessional borrowing (ENCB) limit under the PSI**. The ENCB ceiling was last raised from US$500 million to US$800 million in mid-2011. About US$500 million has been committed, though much less has been disbursed (under two Chinese loans for rural road construction equipment and for the Kampala-Entebbe toll road). Given that the updated DSA, carried out by staff in conjunction with the World Bank, indicates that Uganda's debt outlook would remain favorable, staff supports the request for a US$200 million augmentation of the end-June 2012 ENCB ceiling. Absent this increase, the ENCB ceiling would prevent Uganda from proceeding to contract even one more medium-sized project like the Kampala-Entebbe road (valued at US$350 million alone). The higher borrowing limit is consistent with the medium-term path of the fiscal program. At the same time, the authorities have agreed to undertake a thorough clean-up of the public investment plan as a first step to enhancing public investment management in Uganda. Staff also stressed the need for continued improvements in project identification, appraisal, and execution, and advised the authorities to seek technical assistance in improving capacity in these areas as a matter of priority.

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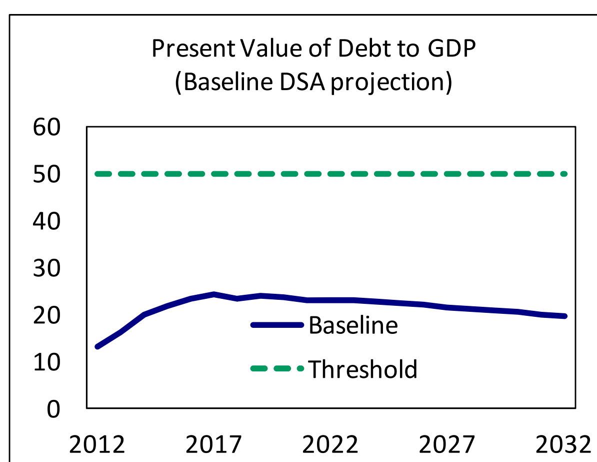
25. **The mission prepared an updated Debt Sustainability Analysis (DSA) jointly with the World Bank**. The analysis (Appendix I) indicates that Uganda remains at low risk of debt distress on existing policies, and that this conclusion would remain valid for a US$200 million increase in the ENCB limit. Staffs also considered the implications of oil sector development on debt sustainability, and developed an alternative scenario on this basis. The authorities are planning to update their debt management strategy (DMS) and have requested technical assistance from the Fund. They are also investigating alternative financing arrangements such as domestic infrastructure bonds, though not until 2013/14, when project preparation is expected to have improved. Staff also noted the uncertain international situation and advocated a continued increase in external buffers.



IV. Program Issues

26. **Revised QACs for end-June 2012 and new QACs for end-December 2012 (test dates for the fifth and sixth reviews under the PSI), and supportive structural measures, are presented in the authorities' MEFP** (Attachment I to the Minister's Letter of Intent). The revised QACs reflect the fact that inflation is declining faster than previously projected, and also a modest expansion in the fiscal deficit for FY11/12, which staff and the authorities agree is justified on counter-cyclical grounds.

27. **Risks to the program are concentrated on the external environment and on fiscal implementation capacity**. Global economic dislocation beyond that foreseen in the April 2012 World Economic Outlook would reduce growth in Uganda, as would an expansion in hostilities between the Sudans. Domestically, infrastructure investment could be further delayed by lack of capacity, and the limited ability of MoFPED to plan and execute the budget as approved by parliament.

V. Staff Appraisal

28. **The Ugandan authorities face a number of difficult challenges**. They are pursuing disinflation in the context of a weak global economy, which will lower growth somewhat. In addition, several regional security concerns have put pressure on public finances.

29. **Staff welcomes the authorities' recent efforts to restore macroeconomic stability.** Despite some fiscal slippage late in the year, budgetary policy remains under control. Monetary policy has been very tight and inflation is receding. Private sector credit growth has fallen sharply, without systemic damage to the banking system (as foreshadowed in the recent FSAP), and the exchange rate has been allowed to fluctuate.

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30. **Looking to FY2012/13, the key challenges are twofold:** first, ***revenue enhancement is urgently needed***. Staff welcomes the revenue measures to be undertaken in the FY12/13 Finance Bill, but more in the way of tax policy changes will need to be considered for FY13/14 and beyond, as low revenue is one of Uganda's key vulnerabilities. The second key challenge is to ***build realistic budgets and then to implement them as approved by parliament***, especially in the area of infrastructure investment. The key bottleneck to closing Uganda's infrastructure gap is not financing; resources are available. But line ministries and MoFPED urgently need to build capacity to manage a large, complex public investment program.

31. **In this regard, staff welcomes the authorities plans to modernize the organic budget law.** The draft Public Finance Bill now before Parliament—if it passes in sensible form—stands a good chance of materially strengthening public finance management in Uganda. Especially important are the petroleum revenue management provisions of that bill, as they should lay the groundwork for a transparent, efficient regime to convert the natural resource assets Uganda has in the ground into physical infrastructure investment assets of the state, for the benefit of current and future generations.

32. **Staff supports completion of the fourth review under the PSI.** All end-December 2011 QACs were met, and the modifications requested for the end June 2012 QACs on (i) the ceiling on the increase in net claims on the central government by the banking system and (ii) the ceiling on the contracting or guaranteeing of new nonconcessional external debt with maturities greater than one year by the public sector are consistent with reestablishment of low inflation and rapid economic growth.

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Figure 1. Monetary Developments

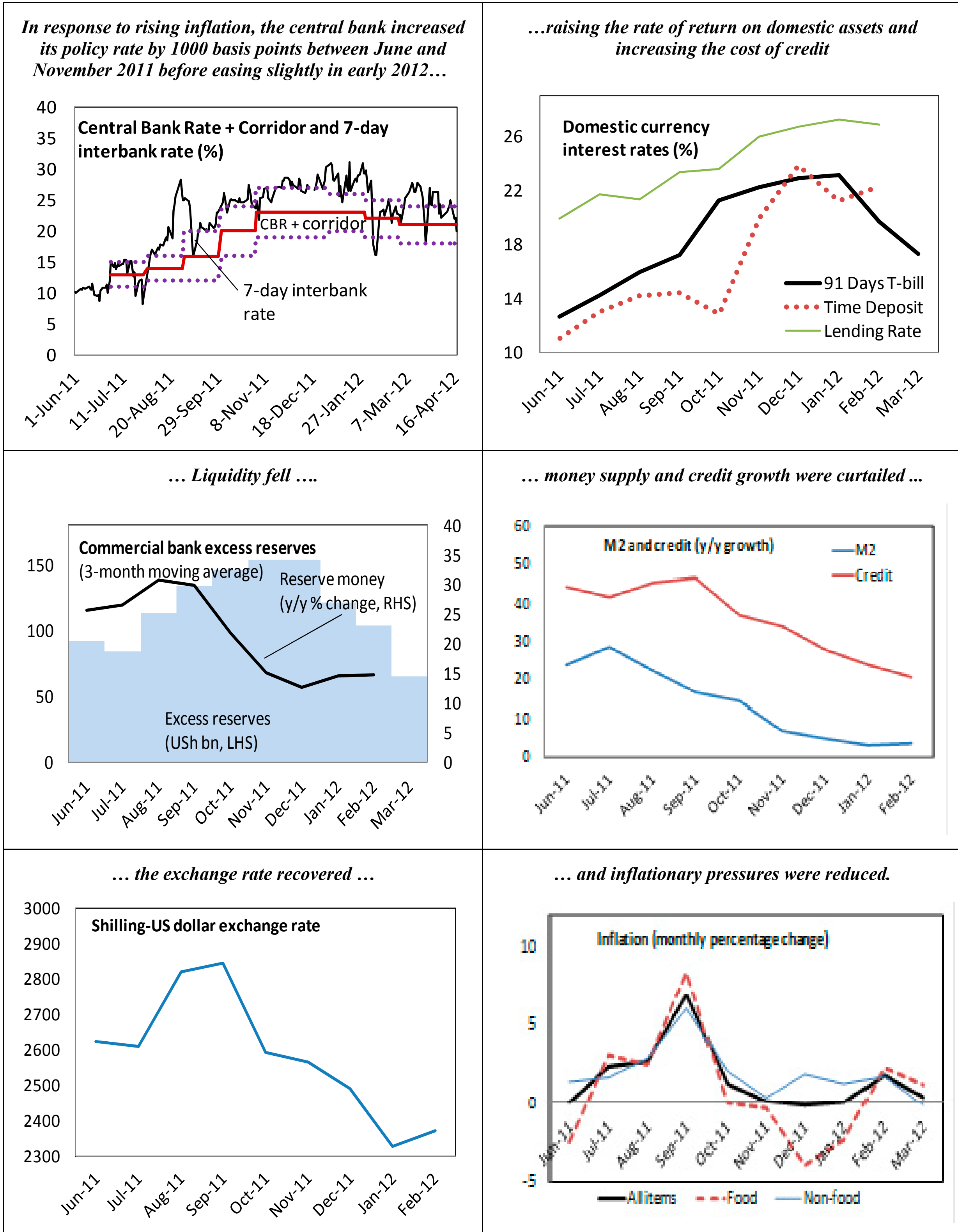

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Figure 2. Developments in the Real Sector

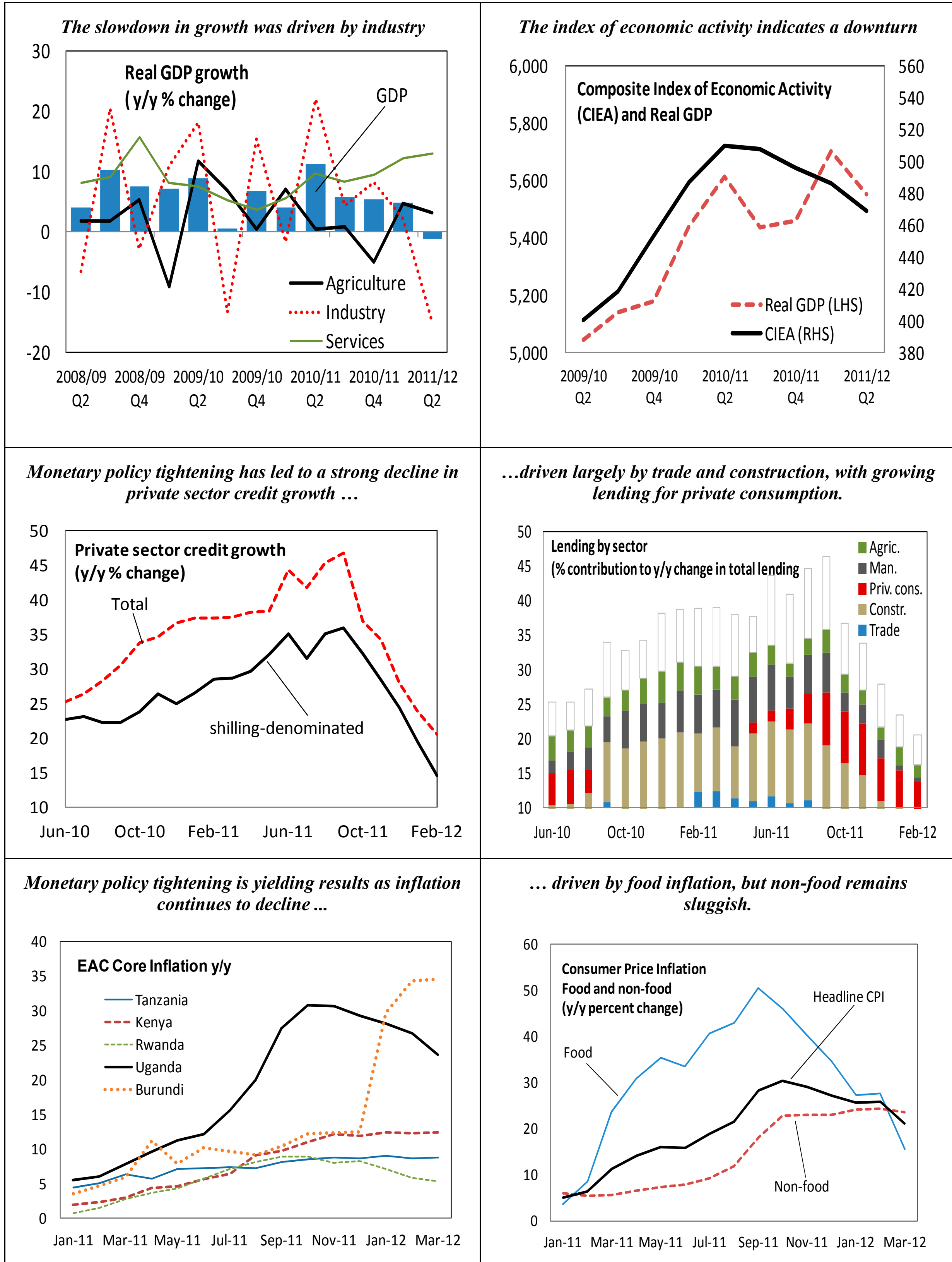

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Figure 3. Fiscal Developments

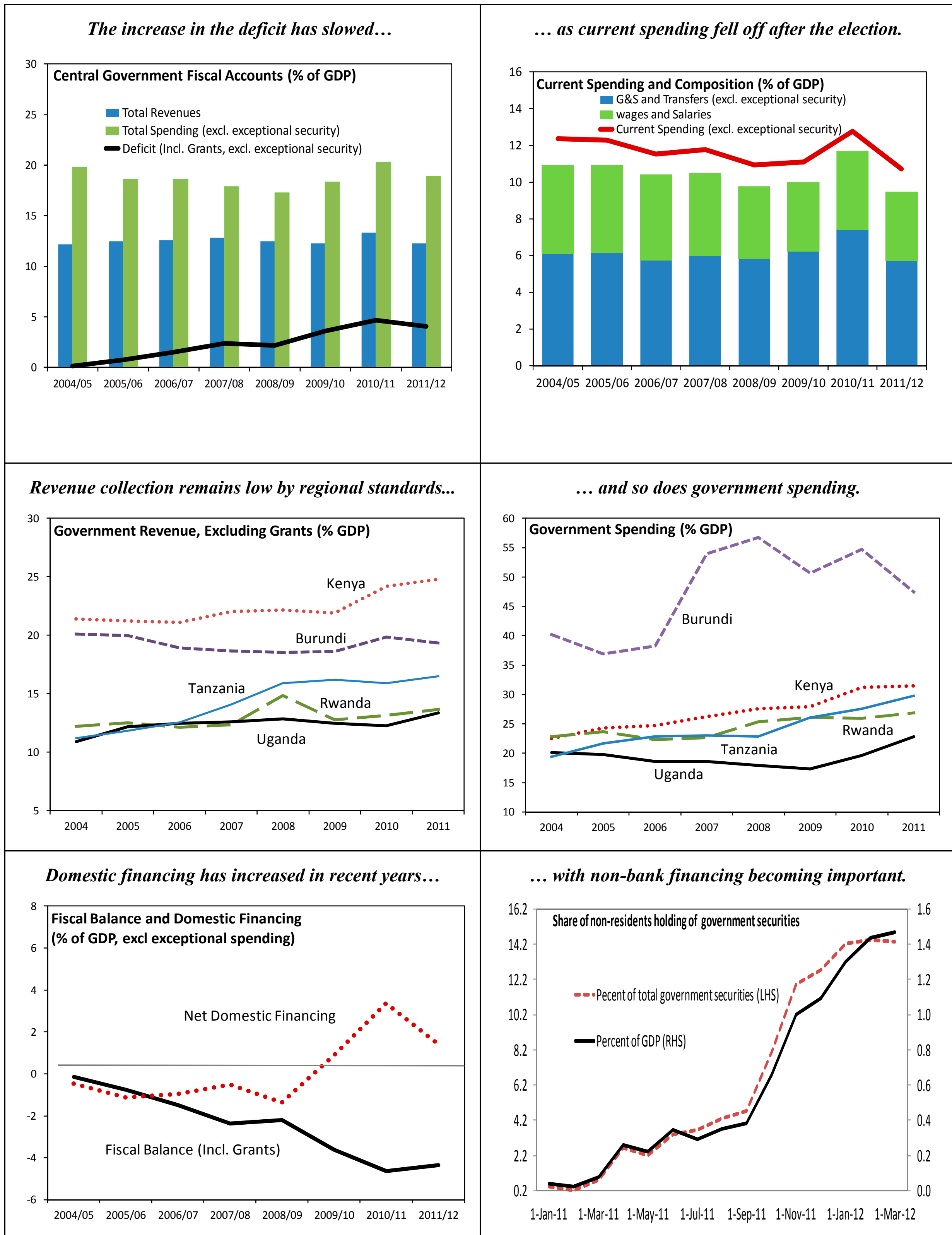

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Figure 4. External Developments

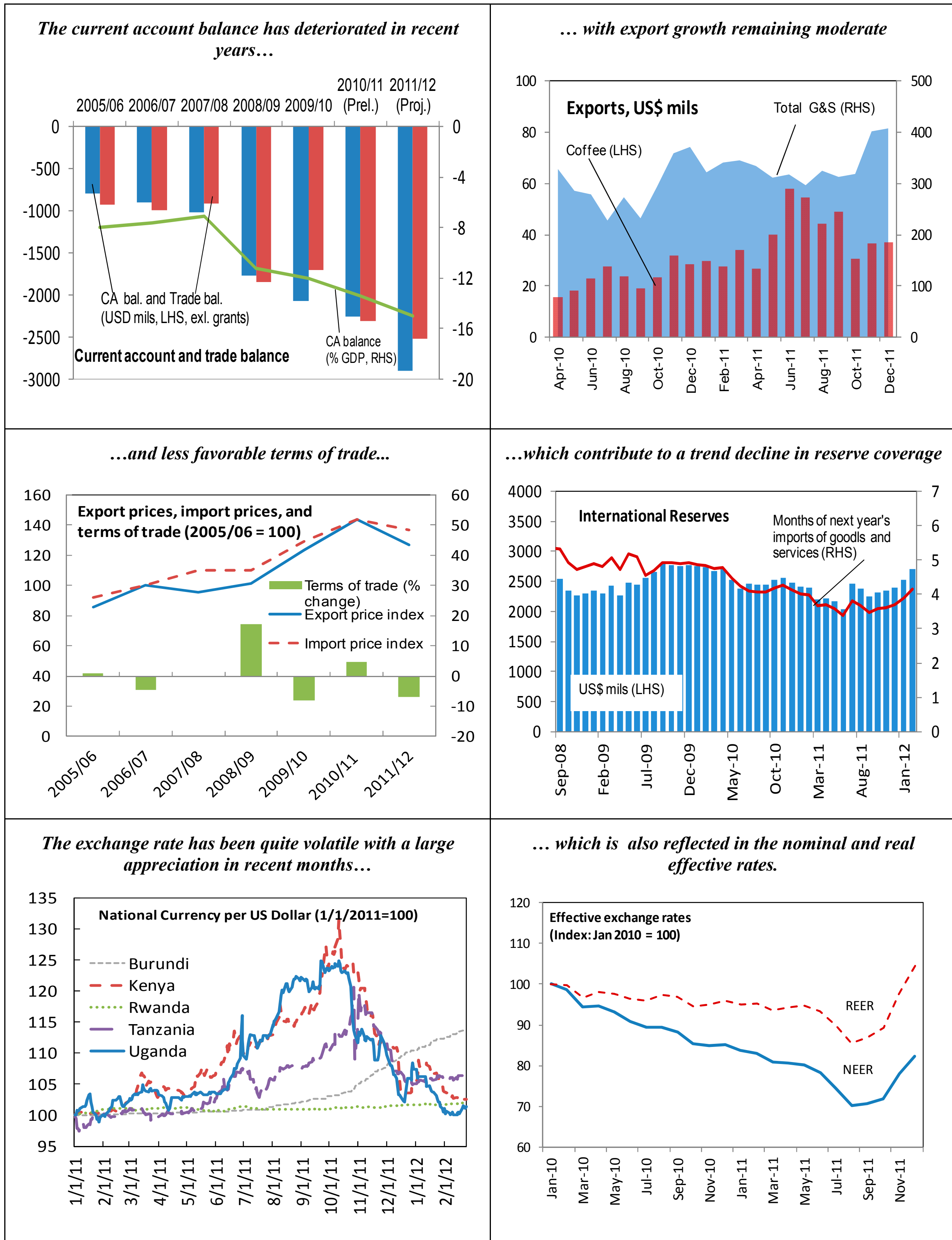

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Table 1. Uganda: Selected Economic and Financial Indicators, FY2009/10–2016/17 [1]

	2009/10	2010/11	2011/12		2012/13	2013/14	2014/15	2015/16	2016/17
	Actual	Actual	3rd Review	Proj.	Proj.	Proj.	Proj.	Proj.	Proj.
GDP and prices (percent change)									
Real GDP	5.9	6.7	5.0	4.2	5.4	6.0	7.0	7.0	7.0
GDP Deflator	9.6	4.9	24.0	22.5	5.3	4.1	6.3	6.2	6.0
CPI (end of period)	4.2	15.7	16.8	15.0	5.3	5.0	5.0	5.0	5.0
CPI (average)	9.4	6.5	23.0	23.4	7.6	5.1	5.0	5.0	5.0
Core inflation (average)	7.8	6.3	24.7	24.3	7.5	5.1	5.1	5.2	5.2
Core inflation (end of period)	4.6	12.1	20.0	17.8	5.1	5.0	5.0	5.0	5.0
External sector (percent change)									
Terms of trade (based on all exports, deterioration -)	-8.1	4.6	-0.7	-7.0	-12.7	-4.9	-5.8	-4.8	-3.0
Real effective exchange rate (depreciation –)	-4.8	-0.9	--	--	--	--	--	--	--
Money and credit (percent change)									
Broad money (M2)	30.3	23.9	15.7	1.1	23.1	23.3	22.5	20.0	15.1
Private sector credit	25.3	44.4	16.0	10.0	27.2	26.6	22.7	21.3	16.2
Savings and investment gap (percent of GDP)	-12.0	-13.4	-13.6	-15.0	-13.2	-13.6	-12.1	-10.7	-9.7
Domestic investment	24.2	24.7	25.4	25.2	26.5	26.8	26.8	26.8	25.8
Public	5.6	5.9	7.8	6.3	7.3	7.1	7.0	6.8	5.8
Private	18.7	18.8	17.6	18.9	19.2	19.6	19.8	20.0	20.0
External sector (percent of GDP)									
Current account balance (including grants)	-9.6	-11.1	-13.2	-12.4	-11.0	-12.1	-10.9	-9.6	-8.7
Current account balance (excluding grants)	-12.0	-13.4	-13.6	-15.0	-13.2	-13.6	-12.1	-10.7	-9.7
Net donor inflows	4.6	3.0	4.1	4.2	3.0	2.5	2.2	2.1	1.9
Public External debt (including Fund)	13.6	17.3	19.4	19.1	23.6	28.8	31.4	33.5	34.9
External debt-service ratio [3]	1.9	1.5	1.6	1.6	1.8	2.0	2.2	1.8	--
Government budget and debt (percent of GDP)									
Revenue	12.2	13.3	13.1	12.3	13.0	13.3	13.6	13.9	14.1
Grants	2.7	2.3	2.6	2.6	2.2	1.5	1.2	1.1	1.1
Total expenditure and net lending	-19.6	-22.8	-19.4	-19.5	-18.7	-18.5	-18.3	-18.4	-17.1
Overall balance (including grants)	-4.6	-7.2	-3.8	-4.7	-3.5	-3.7	-3.5	-3.4	-2.0
Memorandum items:									
Nominal GDP (U Sh billions)	34,909	39,056	50,857	49,833	55,287	61,029	69,447	78,892	89,455
Nominal GDP (US$ millions)	17,197	16,810	…	…	…	…	…	…	…
Average exchange rate (Ush/US$)	2,030	2,323	…	…	…	…	…	…	…
End of period exchange rate (Ush/US$)	2,283	2,623	…	…	…	…	…	…	…
Gross foreign exchange reserves (months of next year's imports of goods and services)	4.2	3.4	3.6	3.6	3.6	3.7	3.9	3.9	3.8

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

[1] Fiscal year begins in July.

[2] Percent of M3 at start of the period. Oil capital gains is included in FY10/11.

[3] Percent of exports of goods and nonfactor services.

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Table 2. Uganda: Monetary Accounts, FY2009/10-FY2016/17[1]
(Billions of Ugandan Shillings unless otherwise indicated)

	2009/10	2010/11	2011/12		2012/13		2013/14	2014/15	2015/16	2016/17
			3rd Review	Proj.	3rd Review	Proj.	Proj.	Proj.	Proj.	Proj.
					Monetary survey					
Net foreign assets	6,384	7,369	9,703	7,688	10,156	7,899	7,862	8,516	8,989	9,979
Bank of Uganda	5,741	6,874	…	6,990	…	7,413	7,248	7,892	8,368	9,360
Commercial banks	643	495	…	698	…	486	614	624	621	619
Net domestic assets	1,909	3,069	2,378	3,321	4,353	5,155	8,120	10,771	13,917	16,357
							700.4	488.7	509.3	23.7
Claims on public sector (net)[2]	284	703	-84	875	582	799	1,500	1,989	2,498	2,522
Claims on central government (net)	231	663	-123	835	542	760	1,461	1,949	2,459	2,482
Claims on the private sector	4,510	6,513	7,555	7,162	9,046	9,110	11,537	14,153	17,161	19,936
Other items (net)	-2,885	-4,146	-5,093	-4,715	-5,275	-4,754	-4,917	-5,370	-5,742	-6,101
Money and quasi-money (M3)	8,293	10,438	12,081	10,970	14,509	13,015	15,943	19,248	22,867	26,297
Broad money (M2)	6,412	7,946	9,197	8,036	11,045	9,891	12,196	14,937	17,928	20,643
Foreign exchange deposits	1,881	2,492	2,884	2,934	3,464	3,124	3,747	4,312	4,939	5,654
					Bank of Uganda					
Net Foreign Assets	5,741	6,874	8,794	6,990	9,128	7,413	7,248	7,892	8,368	9,360
Net domestic assets	-3,307	-3,906	-5,355	-3,634	-4,979	-3,594	-2,505	-2,210	-1,559	-1,483
Claims on public sector (net)[2]	-1,672	-1,578	-2,565	-1,924	-2,099	-1,999	-1,430	-1,281	-1,044	-1,352
Claims on Government (net)	-1,672	-1,579	-2,565	-1,925	-2,100	-2,000	-1,430	-1,281	-1,045	-1,352
Claims on commercial banks	-51	128	198	756	198	911	1,594	2,200	2,994	3,745
Other Items (net)[3]	-1,584	-2,456	-2,989	-2,466	-3,078	-2,505	-2,670	-3,129	-3,509	-3,876
Base money	2,434	2,968	3,439	3,356	4,149	3,820	4,743	5,682	6,810	7,877
Currency in circulation	1,739	2,190	2,535	2,593	3,058	2,763	3,407	4,030	4,820	5,550
Commercial bank deposits	695	778	904	763	1,091	1,057	1,336	1,652	1,990	2,327
					Commercial banks					
Net Foreign Assets	643	495	909	698	1,028	486	614	624	621	619
Net Domestic Assets	6,207	8,044	8,974	7,953	10,825	10,126	12,365	15,144	18,087	20,889
Claims on central government (net)	1,903	2,242	2,442	2,760	2,642	2,760	2,891	3,231	3,503	3,834
Claims on private sector	4,485	6,476	7,519	7,108	9,009	9,056	11,484	14,099	17,108	19,883
Deposit Liabilities to the Non-Bank Public	6,850	8,538	9,883	8,652	11,854	10,611	12,979	15,768	18,708	21,508
Shilling deposits	4,968	6,046	…	5,718	…	7,488	9,233	11,456	13,769	15,854
Foreign Exchange Accounts	1,881	2,492	…	2,934	…	3,124	3,747	4,312	4,939	5,654
Memorandum items:										
(Annual percentage change)										
Base money	24.8	21.9	15.9	13.1	20.6	13.8	24.2	19.8	19.9	15.7
M3	31.7	25.9	15.7	5.1	20.1	18.6	22.5	20.7	18.8	15.0
Credit to the private sector	25.3	44.4	16.0	10.0	19.7	27.2	26.6	22.7	21.3	16.2
Base money-to-GDP ratio (percent)	7.0	7.6	6.8	6.7	7.2	6.9	7.8	8.2	8.6	8.7
M3-to-GDP ratio (percent)	23.8	26.7	23.8	22.0	25.1	23.5	26.1	27.7	29.0	29.0
Base money multiplier (M2/base money)	2.6	2.7	2.7	2.4	2.7	2.6	2.6	2.6	2.6	2.6
Credit to the private sector (percent of GDP)	12.9	16.7	14.9	14.4	15.7	16.5	18.9	20.4	21.8	22.0
Gross reserves of BOU (US$ millions)	2,385	2,044	2,344	2,346	2,562	2,563	2,751	2,966	3,177	3,378
Velocity (M3)	4.2	3.7	4.2	4.5	4.0	4.2	3.8	3.6	3.5	3.5
Exchange rate (sh/US$)	2,283.3	2,623.2	…	…	…	…	…	…	…	…

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

[1] Fiscal year begins July 1st.

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

[3] Including valuation effects and the Bank of Uganda's claims on the private sector.

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Table 3a. Uganda: Fiscal Operations of the Central Government, FY2009/10–2016/17 [1]
(Billions of Ugandan Shillings)

	2009/10	2010/11	2011/12		2012/13	2013/14	2014/15	2015/16	2016/17
	Actual	Prel.	3rd Review	Proj.	Proj.	Proj.	Proj.	Proj.	Proj.
Total revenue and grants	5,136	6,100	7,964	7,397	8,446	9,044	10,303	11,810	13,552
Revenue	4,273	5,209	6,666	6,123	7,214	8,123	9,465	10,955	12,602
Tax	4,067	4,958	6,374	5,857	6,880	7,768	9,054	10,492	12,072
International trade taxes	352	455	584	493	590	664	795	937	1,065
Income taxes	1,361	1,750	2,227	2,056	2,478	2,804	3,204	3,748	4,338
Excises	1,025	1,186	1,478	1,439	1,631	1,834	2,166	2,474	2,840
Value-added tax	1,329	1,567	2,085	1,870	2,180	2,466	2,889	3,333	3,830
Nontax	206	252	292	266	335	355	411	463	530
Grants	863	891	1,298	1,274	1,232	920	838	856	950
Budget support	467	515	665	627	497	518	427	448	498
Project grants	396	375	633	648	735	402	411	407	452
Expenditures and net lending	6,836	8,900	9,876	9,717	10,360	11,275	12,741	14,492	15,339
Current expenditures	4,308	5,963	5,629	5,634	5,095	5,781	6,647	7,739	8,767
Wages and salaries	1,308	1,664	2,034	1,877	2,059	2,380	2,778	3,235	3,668
Interest payments	386	424	672	617	767	768	887	954	1,114
Other current	2,614	3,875	2,923	3,141	2,269	2,633	2,982	3,550	3,986
o/w Exceptional security	437	979	323	300	0	0	0	0	0
o/w Power sector subsidies	193	194	413	171	0	0	0	0	0
Development expenditures	2,312	2,774	3,994	3,768	4,815	5,379	5,981	6,644	6,462
Externally-financed projects	889	1,042	1,728	1,798	1,805	1,901	2,370	2,384	1,811
o/w Entebbe highway, road equipment			282	193	913	303	262	430	92
Government of Uganda investment	1,423	1,732	2,266	1,970	3,010	3,478	3,611	4,260	4,651
o/w Karuma			448	443	1,029	837	419	641	0
o/w Oil refinery			17	0	0	782	0	0	0
Net lending and investment	-37	-30	-40	-12	0	-34	-37	-40	-40
Other spending	253	194	293	327	450	150	150	150	150
Clearance of domestic arrears	84	194	293	293	50	50	50	50	50
Contingency	169	0	…	33	400	100	100	100	100
Overall balance									
Including grants	-1,699	-2,801	-1,912	-2,320	-1,914	-2,232	-2,438	-2,682	-1,787
Excluding grants	-2,562	-3,691	-3,210	-3,594	-3,146	-3,152	-3,276	-3,538	-2,737
Financing	1,532	2,862	1,911	2,320	1,914	2,232	2,438	2,682	1,787
External financing (net)	784	555	1,306	1,326	920	1,444	1,894	1,921	1,398
Disbursement	919	716	1,517	1,541	1,201	1,741	2,211	2,242	1,636
Budget support	236	237	422	390	130	241	251	265	277
Concessional project loans	683	479	813	958	810	964	1,122	1,242	1,205
Non-concessional borrowing			282	193	261	536	837	736	154
Amortization (–)	-135	-152	-197	-204	-267	-293	-312	-322	-238
Exceptional financing	-26	-8	-14	-11	-14	-4	-5	0	0
Domestic financing (net)	749	2,307	605	993	993	788	544	761	389
Bank financing	811	1,613	481	511	726	700	489	509	24
Bank of Uganda	473	1,274	281	-7	726	569	149	237	-307
o/w Petroleum fund withdrawals		0	52	0.0	982	837	428	531	0
o/w Energy Fund withdrawals		147	396	443	5.5	0	0	0	0
o/w Bank of Uganda Repayments		0	0	0	-261	-268	-279	-294	-307
Commercial banks	338	339	200	518	0	131	340	273	331
Nonbank financing	-62	694	124	482	267	87	55	252	365
Errors and omissions/financing gap (- is gap, + is surplus)	-167	62	0	0	0	0	0	0	0
Memorandum Items:									
Petroleum revenues (Ush billions)									
Inflows (including interest)		1,128	1,312	403	889	80	43	25	0
Valuation adjustment		52	…	47	10	32	49	20	0
Withdrawals		0	52	0	982	837	428	531	0
Stock at end period		1,180	2,452	1,630	1,547	821	485	0	0
Revenue, incl. petroleum revenue inflows		6,337	7,978	6,526	8,104	8,203	9,508	10,980	12,602
Overall bal, incl. grants and petr. rev. inflows		-1,673	-599	-1,917	-1,024	-2,152	-2,395	-2,657	-1,787

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

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Table 3b. Uganda: Fiscal Operations of the Central Government, FY2009/10–2016/17 [1]
(Percent of GDP)

	2009/10	2010/11	2011/12		2012/13	2013/14	2014/15	2015/16	2016/17
	Actual	Prel.	3rd Review	Proj.	Proj.	Proj.	Proj.	Proj.	Proj.
Total revenue and grants	14.7	15.6	15.7	14.8	15.3	14.8	14.8	15.0	15.1
Revenue	12.2	13.3	13.1	12.3	13.0	13.3	13.6	13.9	14.1
Tax	11.7	12.7	12.5	11.8	12.4	12.7	13.0	13.3	13.5
International trade taxes	1.0	1.2	1.1	1.0	1.1	1.1	1.1	1.2	1.2
Income taxes	3.9	4.5	4.4	4.1	4.5	4.6	4.6	4.8	4.8
Excises	2.9	3.0	2.9	2.9	2.9	3.0	3.1	3.1	3.2
Value-added tax	3.8	4.0	4.1	3.8	3.9	4.0	4.2	4.2	4.3
Nontax	0.6	0.6	0.6	0.5	0.6	0.6	0.6	0.6	0.6
Grants	2.5	2.3	2.6	2.6	2.2	1.5	1.2	1.1	1.1
Budget support	1.3	1.3	1.3	1.3	0.9	0.8	0.6	0.6	0.6
Project grants	1.1	1.0	1.2	1.3	1.3	0.7	0.6	0.5	0.5
Expenditures and net lending	19.6	22.8	19.4	19.5	18.7	18.5	18.3	18.4	17.1
Current expenditures	12.3	15.3	11.1	11.3	9.2	9.5	9.6	9.8	9.8
Wages and salaries	3.7	4.3	4.0	3.8	3.7	3.9	4.0	4.1	4.1
Interest payments	1.1	1.1	1.3	1.2	1.4	1.3	1.3	1.2	1.2
Other current	7.5	9.9	5.7	6.3	4.1	4.3	4.3	4.5	4.5
o/w Exceptional security	1.3	2.5	0.6	0.6	0.0	0.0	0.0	0.0	0.0
o/w Power sector subsidies	0.6	0.5	0.8	0.3	0.0	0.0	0.0	0.0	0.0
Development expenditures	6.6	7.1	7.9	7.6	8.7	8.8	8.6	8.4	7.2
Externally-financed projects	2.5	2.7	3.4	3.6	3.3	3.1	3.4	3.0	2.0
o/w Entebbe highway, road equipment	0.0	0.0	0.6	0.4	1.7	0.5	0.4	0.5	0.1
Government of Uganda investment	4.1	4.4	4.5	4.0	5.4	5.7	5.2	5.4	5.2
o/w Karuma	0.0	0.0	0.9	0.9	1.9	1.4	0.6	0.8	0.0
o/w Oil refinery	0.0	0.0	0.0	0.0	0.0	1.3	0.0	0.0	0.0
Net lending and investment	-0.1	-0.1	-0.1	0.0	0.0	-0.1	-0.1	-0.1	0.0
Other spending	0.7	0.5	0.6	0.7	0.8	0.2	0.2	0.2	0.2
Clearance of domestic arrears	0.2	0.5	0.4	0.6	0.1	0.1	0.1	0.1	0.1
Contingency	0.5	0.0	…	0.1	0.7	0.2	0.1	0.1	0.1
Overall balance									
Including grants	-4.9	-7.2	-3.8	-4.7	-3.5	-3.7	-3.5	-3.4	-2.0
Excluding grants	-7.3	-9.5	-6.3	-7.2	-5.7	-5.2	-4.7	-4.5	-3.1
Financing	4.4	7.3	3.8	4.7	3.5	3.7	3.5	3.4	2.0
External financing (net)	2.2	1.4	2.6	2.7	1.7	2.4	2.7	2.4	1.6
Disbursement	2.6	1.8	3.0	3.1	2.2	2.9	3.2	2.8	1.8
Budget support	0.7	0.6	0.8	0.8	0.2	0.4	0.4	0.3	0.3
Concessional project loans	2.0	1.2	1.6	1.9	1.5	1.6	1.6	1.6	1.3
Non-concessional borrowing	0.0	0.0	0.6	0.4	0.5	0.9	1.2	0.9	0.2
Amortization (–)	-0.4	-0.4	-0.4	-0.4	-0.5	-0.5	-0.4	-0.4	-0.3
Exceptional financing	-0.1	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Domestic financing (net)	2.1	5.9	1.2	2.0	1.8	1.3	0.8	1.0	0.4
Bank financing	2.3	4.1	0.9	1.0	1.3	1.1	0.7	0.6	0.0
Bank of Uganda	1.4	3.3	0.6	0.0	1.3	0.9	0.2	0.3	-0.3
o/w Petroleum fund withdrawals	0.0	0.0	0.1	0.0	1.8	1.4	0.6	0.7	0.0
o/w Energy Fund withdrawals	0.0	0.4	0.8	0.9	0.0	0.0	0.0	0.0	0.0
o/w Bank of Uganda Repayments	0.0	0.0	0.0	0.0	-0.5	-0.4	-0.4	-0.4	-0.3
Commercial banks	1.0	0.9	0.4	1.0	0.0	0.2	0.5	0.3	0.4
Nonbank financing	-0.2	1.8	0.2	1.0	0.5	0.1	0.1	0.3	0.4
Errors and omissions/financing gap (- is gap, + is surplus)	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Memorandum Items:									
Petroleum revenue fund									
Inflows (including interest)		2.9	2.6	0.8	1.6	0.1	0.1	0.0	0.0
Petroleum fund withdrawals		0.0	0.1	0.0	1.8	1.4	0.6	0.7	0.0
Stock at end period		3.0	4.8	3.3	2.8	1.3	0.7	0.0	0.0
Revenue, incl. petroleum revenue inflows		16.2	15.7	13.1	14.7	13.4	13.7	13.9	14.1
Overall bal, incl. grants and petr. rev. inflows		-4.3	-1.2	-3.8	-1.9	-3.5	-3.4	-3.4	-2.0
Nominal GDP (USh billions)	34,909	39,056	50,857	49,833	55,287	61,029	69,447	78,892	89,455

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

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Table 3c. Uganda: Quarterly Fiscal Operations of the Central Government, 2011/2012 - 2012/13
(Billions of Ugandan Shillings)

	2011/12					2012/13				
	Q1 Prov	Q2 Prov	Q3 Prov	Q4 Proj	Annual Proj	Q1 Prov	Q2 Proj	Q3 Proj	Q4 Proj	Annual Proj
Total revenue and grants	1,522	2,029	1,773	2,073	7,397	1,845	2,252	1,961	2,389	8,446
Revenue	1,371	1,601	1,485	1,666	6,123	1,591	1,883	1,745	1,995	7,214
Tax	1,314	1,535	1,416	1,592	5,857	1,522	1,786	1,665	1,907	6,880
International trade taxes	128	112	135	117	493	138	154	145	153	590
Income taxes	395	592	425	644	2,056	475	696	537	770	2,478
Excises	328	358	389	363	1,439	394	400	418	420	1,631
Value-added tax	463	472	467	467	1,870	515	536	565	564	2,180
Nontax	56	66	69	74	266	69	97	80	88	335
Grants	151	428	288	407	1,274	254	369	215	394	1,232
Budget support	93	247	134	153	627	117	166	96	118	497
Project grants	58	181	154	254	648	137	203	120	275	735
Expenditures and net lending	2,200	1,973	2,350	3,194	9,717	2,304	2,997	2,513	2,546	10,360
Current expenditures	1,220	1,431	1,398	1,586	5,634	1,133	1,326	1,236	1,399	5,095
Wages and salaries	433	448	450	546	1,877	458	536	499	566	2,059
Interest payments	119	144	181	173	617	171	200	186	211	767
Domestic	103	116	141	154	514					
External	17	28	39	18	103					
Other current	668	838	767	868	3,141	505	591	550	623	2,269
o/w Exceptional security	145	79	75	0	300					
o/w Power sector subsidies	0	50	122	0	171					
Development expenditures	749	523	948	1,549	3,768	1,071	1,554	1,168	1,023	4,815
Externally-financed projects	319	131	529	819	1,798	401	470	438	496	1,805
o/w Entebbe highway						228	228	228	228	913
Government of Uganda investment	430	392	419	729	1,970	669	1,084	730	527	3,010
o/w Karuma	0	0	0	443	443	0	1,029	0	0	1,029
o/w Oil refinery						0	0	0	0	0
Net lending and investment	-11	0	0	-2	-12	0	0	0	0	0
Other spending	242	20	4	61	327	100	117	109	124	450
Overall balance										
Including grants	-678	56	-577	-1,121	-2,320	-459	-745	-552	-157	-1,914
Excluding grants	-829	-372	-865	-1,528	-3,594	-713	-1,114	-768	-551	-3,146
Financing	566	129	579	1,045	2,320	459	745	552	157	1,914
External financing (net)	108	237	192	790	1,326	212	237	225	246	920
Disbursement	164	301	246	829	1,541	274	310	293	323	1,201
Budget support	0	126	0	264	390	29	34	32	36	130
Concessional project loans	164	176	246	565	1,151	180	211	196	222	810
Non-concessional borrowing						65	65	65	65	261
Amortization (–)	-51	-65	-50	-38	-204	-59	-69	-65	-73	-267
Exceptional financing	-5	0	-5	0	-11	-3	-4	-3	-4	-14
Domestic financing (net)	458	-108	387	255	993	247	508	327	-89	993
Bank financing	27	-458	537	405	511	162	489	176	-100	726
Bank of Uganda	344	-344	0	-6	-7	162	489	176	-100	726
Commercial banks	-317	-114	537	411	518	0	0	0	0	0
Nonbank financing	432	350	-150	-150	482	86	19	151	11	267
Errors and omissions/financing gap	-111	185	2	-76	0	0	0	0	0	0

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

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Table 4. Uganda: Balance of Payments, FY2009/10-2016/17

(Millions of US Dollars)

	2009/10	2010/11	2011/12		2012/13	2013/14	2014/15	2015/16	2016/17
	Actual	Prel.	3rd Review	Proj.	Proj.	Proj.	Proj.	Proj.	Proj.
Current account	-1,646	-1,865	-2,212	-2,409	-2,323	-2,753	-2,703	-2,578	-2,528
Trade balance	-1,698	-2,311	-2,431	-2,520	-2,512	-2,678	-2,657	-2,577	-2,516
Exports, f.o.b.	2,317	2,309	2,631	2,502	2,882	3,167	3,496	3,743	4,019
Of which: coffee	262	371	423	397	365	384	404	424	441
Imports, f.o.b.	-4,015	-4,620	-5,061	-5,022	-5,394	-5,845	-6,152	-6,320	-6,536
Of which: oil	-486	-659	-746	-735	-777	-842	-923	-910	-893
Of which: government, infrastructure related	-171	-196	-481	-466	-607	-874	-783	-650	-606
Services (net)	-533	-741	-878	-754	-841	-919	-892	-925	-954
Income (net)	-332	-321	-310	-294	-296	-338	-349	-355	-431
Of which: interest on public debt	-29	-36	-50	-41	-37	-47	-66	-69	-45
Transfers	917	1,507	1,406	1,159	1,326	1,182	1,194	1,279	1,373
Private transfers	687	833	720	773	827	989	1,041	1,127	1,211
Of which: workers' remittances (inflows)	777	825	841	863	900	1,056	1,133	1,216	1,306
Official transfers	230	674	686	386	499	193	153	152	162
Of which: budget support (including HIPC)	230	225	236	244	191	193	153	152	162
capital gains tax	0	449	450	142	308	0	0	0	0
Capital and financial account	1,811	1,072	2,523	2,722	2,553	2,959	2,932	2,789	2,729
Capital account	195	160	225	252	282	150	147	138	147
Of which: project grants	195	160	225	252	282	150	147	138	147
Financial account	1,615	912	2,298	2,470	2,272	2,809	2,785	2,650	2,582
Foreign direct and portfolio investment	871	759	1,050	968	1,221	1,356	1,389	1,431	1,889
Other investment	744	153	1,248	1,503	1,050	1,454	1,396	1,220	693
Of which:									
Public sector (net)	610	-207	769	828	106	848	828	802	455
SDR allocation	224	0	0	0	0	0	0	0	0
Build-up (-)/drawdown (+) of petroleum fund	0	-449	150	307	-252	307	148	149	0
Loan disbursements	453	308	689	600	460	650	792	762	532
Project support (loans)	337	206	289	373	310	360	402	422	392
Budget support (loans)	116	102	150	152	50	90	90	90	90
Non-concessional borrowing	0	0	100	75	100	200	300	250	50
Amortization due	-67	-66	-70	-78	-102	-109	-112	-109	-77
Commercial banks (net)	5	93	114	-76	81	-43	6	-60	-57
Other private (net)	129	266	666	750	863	649	561	478	296
Errors and omissions	47	212	0	0	0	0	0	0	0
Overall balance	212	-581	311	313	230	206	229	211	201
Financing	-212	581	-311	-313	-230	-206	-229	-211	-201
Central bank net reserves (increase = –)	-199	585	-300	-302	-217	-187	-215	-211	-201
Of which: SDR allocation	-224	0	0	0	0	0	0	0	0
Use of Fund credit	-1	-2	-2	-2	-2	-2	-1	0	0
Memorandum items:									
Gross offical reserves (BoU) 1/	2,385	2,044	2,344	2,346	2,563	2,751	2,966	3,177	3,378
Months of imports of goods and services	4.2	3.4	3.6	3.6	3.6	3.7	3.9	3.9	3.8
Net donor support	770	588	769	891	681	619	601	625	669
Of which: budget support (loans and grants)	346	327	386	396	241	284	243	243	252
project support (loans and grants)	532	366	514	625	592	510	549	560	539
Current account balance (percent of GDP)	-9.6	-11.1	-12.2	-12.4	-11.0	-12.1	-10.9	-9.6	-8.7
Current account balance (excluding grants)	-12.0	-13.4	-13.6	-15.0	-13.2	-13.6	-12.1	-10.7	-9.7
Trade balance (percent of GDP)	-9.9	-13.7	-13.5	-13.0	-11.9	-11.8	-10.7	-9.6	-8.6
Exports (percent of GDP)	13.5	13.7	14.6	12.9	13.6	13.9	14.1	14.0	13.8
Imports (percent of GDP)	23.3	27.5	28.0	25.9	25.5	25.7	24.7	23.6	22.5

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

[1] In FY 2010/11 there was a revaluation gain of US$241 million.

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Table 5. Uganda: Quantitative Assessment Criteria and Indicative Targets for September 30, 2011 and December 31, 2011 [1]
(Cumulative change from the beginning of the fiscal year, unless otherwise stated)

	September 2011[2]				December 2011			
	Prog.	Adj Prog.	Outturn	Result	Prog.	Adj Prog.	Outturn	Result
	(Ush billions)							
Assessment criteria								
Ceiling on the increase in net domestic assets of the Bank of Uganda [3]	409	592	563	Met	652	582	399	Met
Ceiling on the increase in net claims on the central government by the banking system	274	229	35	Met	119	-272	-429	Met
	(US$ millions)							
Ceiling on the stock of external payments arrears incurred by the public sector [4]	0	0	0	Met	0	0	0	Met
Ceiling on the contracting or guaranteeing of new nonconcessional external debt with maturities greater than one year by the public sector [4, 5]	800	800	450	Met	800	800	450	Met
Ceiling on new external debt with maturity up to one year contracted or guaranteed by the public sector [4 6]	0	0	0	Met	0	0	0	Met
Minimum increase in net international reserves of the Bank of Uganda (US$mn)	-66	-144	287	Met	309	344	477	Met
Share of oil revenue placed in the Petroleum Fund	100	100	100	Met	100	100	100	Met
Indicative target	(Ush billions)							
Ceiling on the increase in base money liabilities of the Bank of Uganda [3]	253	253	244	Met	253	253	322	Not met
Stock of domestic budgetary arrears under the Commitment Control System (CCS) [7]	…	…	…	…	…	…	…	…
Minimum expenditures under the Poverty Action Fund	…	…	…	…	…	…	…	…
Ceiling on the issuance of guarantees by the Government/Bank of Uganda	0	0	0	Met	0	0	0	Met

[1] Defined in the technical memorandum of understanding (TMU), all targets exclude oil revenues.
[2] Indicative targets.
[3] Based on daily average.
[4] Continuous assessment criterion.
[5] Cumulative change from May, 2010. To be used exclusively for infrastructure investment projects.
[6] Excluding import-related credits.
[7] Monitored annually.

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Table 6. Uganda: Structural Benchmarks Under the PSI—
Status of Implementation (Third Review)

Policy Measure	Macroeconomic Rationale	Date	Status
Government to begin to gazette and publish on the internet the names of beneficiaries (whether individual or corporation) of all tax expenditures.	Enforce discipline in issuance of tax exemptions.	September 30, 2011, and **quarterly thereafter**	Met.
Begin submitting to Cabinet regular quarterly reports on unpaid bills of nine Ministries based on data in the Commitment Control System (CCS) for the previous quarter of the fiscal year.	To facilitate control and elimination of expenditure arrears	June 30, 2011, for the report covering Q3 of FY2010/11, and **quarterly thereafter.**	Met.
Produce and disseminate within government a monthly index of economic activity relying on the various high-frequency indicators available.	To facilitate the conduct of monetary policy.	September 30, 2011, and **quarterly thereafter**.	Not met. Monthly index produced but not disseminated. Technical assistance has been requested to improve data quality.
BoU to include in Quarterly Report data on the net and gross positions of government in the BoU.	Enhance central bank independence and prepare Bank of Uganda to move toward inflation targeting.	September 30, 2011, and **quarterly thereafter**.	Met.
Government to publish releases by MoFPED for power and water obligations of spending ministries, and actual payments by them, with sanctions to be applied to the named Accounting Officers of agencies that run arrears on these utilities.	Help control accumulation of arrears. Replaces benchmark on "straight-through payments"	December 15, 2011 (for the previous quarter) and **quarterly thereafter.**	Partly met. Data published on web , but sanctions not applied
Government to submit to Cabinet a strategy to contain increases in power sector subsidies, including establishing the timeframe over which Energy Regulatory Authority (ERA) is to move power tariffs to a rules-based, cost-recovery level, and setting out options for the period when power demand outstrips the additional capacity coming from Bujagali hydro project.	Prevent accumulation of expenditure arrears.	April 1, 2012.	Met.
Government to submit to Parliament a supplementary budget to cover known arrears and under-budgeted spending obligations, including those for power sector subsidies which may be required in light of ERA's	Prevent accumulation of expenditure arrears	April 30, 2012.	Not met. Supplementary Budget submitted does not contain resources to settle arrears, the volume of which

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Policy Measure	Macroeconomic Rationale	Date	Status
tariff setting policy.			Government disputes. Discussions with creditors are under way.
As part of introduction of national identification system, 4 million additional citizens will have received IDs.	To support efforts to strengthen revenue collection and combat money laundering and the financing of terrorism.	June 30, 2012.	Ongoing. Projected completion date to be re-phased to December 31, 2012.

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Table 7. Uganda: Banking Sector Indicators, 2005-11
(In percent)

	2005	2006	2007	2008	2009	2010				2011			
	Dec-05	Dec-06	Dec-07	Dec-08	Dec-09	Mar-10	Jun-10	Sep-10	Dec-10	Mar-11	Jun-11	Sep-11	Dec-11
Capital Adequacy													
Regulatory capital to risk-weighted assets	18.3	17.9	19.3	20.7	20.9	22.7	21.7	21.2	20.2	21.2	19.3	18.3	20.3
Regulatory tier 1 capital to risk-weighted assets	16.8	16.4	17.7	18.7	18.7	19.9	19.2	18.8	17.5	18.9	17.3	16.2	17.9
Asset quality													
NPLs to total gross loans	2.3	2.9	4.1	2.2	4.2	3.7	3.3	2.8	2.1	2.5	1.6	1.8	2.2
NPLs to total deposits	1.1	1.7	2.5	1.6	3	2.5	2.1	1.8	1.4	1.7	1.1	1.4	1.7
Earning assets to total assets	77.6	80	79.9	75.6	78	82.4	74.9	76.7	77.1	73.6	74.8	74.3	74
Large exposures to gross loans	40.1	42.9	43.8	31	32.2	41	35.4	35.5	35.7	38.6	41.7	38.3	34.6
Large exposures to total capital	116.8	137.9	136.8	92.1	94.3	123.9	112.8	116.1	124.4	129.8	156.2	145.4	120.8
Earnings & profitability													
Return on assets	3.4	3.4	3.8	4	2	2.3	3	2.4	3	3.3	3.1	3.6	4
Return on equity	28.3	28.3	30.7	27.7	12.7	14.8	20.2	16.9	21.3	22.9	22.4	25.4	27.4
Net interest margin	10.1	10.3	10.1	11.3	10.2	…	…	…	10	…	…	…	11.7
Cost of deposits	2	2.2	2.9	2.9	3.7	…	…	…	2.9	…	…	…	3.2
Cost to income	66.7	68.3	68	69.7	75.4	…	…	…	75.7	…	…	…	68.1
Overhead to income	51.6	51.4	47.1	48.6	52.3	…	…	…	53.1	…	…	…	44.3
Liquidity													
Liquid assets to total deposits	60	50.7	46.7	48.1	44.7	45.5	41.6	40.5	39.8	40.5	35.6	36.2	37.6
Total loans to total deposits	48.5	57.5	60.2	72.5	71.7	…	…	…	68	…	…	…	78.4
Market Sensitivity													
Foreign currency exposure to regulatory tier 1 capital	-2.7	-7.4	-8.4	-1.4	-0.7	-3	-3.5	-11.8	-1.6	-2.1	-0.9	-3.4	-3.6
Foreign currency loans to foreign currency deposits	48.8	48.8	56.6	65.5	57.9	59.2	52.1	54.4	65.2	63.4	68.6	66.8	67.9
Foreign currency assets to foreign currency liabilities	102	109.5	97.4	102.7	107	101.1	98.4	96.3	98	98.1	100.1	98.1	100.2

Source: Bank of Uganda.

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APPENDIX I. LETTER OF INTENT

Kampala, Uganda
May 18, 2012

Ms. Christine Lagarde
Managing Director
International Monetary Fund
Washington, DC 20431

Dear Ms. Lagarde:

On behalf of the Government of Uganda, I would like to provide you with an update on the progress we have made under our program backed by the IMF's Policy Support Instrument (PSI).

Since the last review, tight monetary and fiscal policies have placed inflation on a pronounced downward trend. At the same time, growth appears to be weakening, both because of the policy stance and the slowing global economy. Government has steadfastly refused to succumb to the temptation to limit food prices by restricting exports, or by interfering with the exchange rate.

The attached MEFP sets out the Government's objectives and policies for remainder of this financial year and indicates our thinking for the medium term. No quantitative assessment criteria were missed for December 2011, and most of the structural benchmarks were achieved. We hereby request modification of assessment criteria for June 2012, establishment of new targets for December 2012, and completion of the fourth review. Formal targets for June 2013 will be set at the time of the 6th review, with which we expect to request a successor arrangement to this PSI.

The Government believes the policies set forth in the MEFP are fully sufficient to achieve the objectives of our PSI-supported program, but as always we stand ready to take any further measures that may become appropriate for this purpose. We consent to publication of the documents for this fourth review under the PSI. We intend to work with the IMF and

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other development partners in the implementation of our program, and will consult with Fund staff in advance should revisions to the policies contained in the PSI be contemplated by the Government.

Sincerely yours,

/s/

Caroline Amali Okao (M.P)
MINISTER OF STATE/MICRO FINANCE AND ALSO HOLDING PORTFOLIO OF MINISTER OF FINANCE, PLANNING AND ECONOMIC DEVELOPMENT

Attachments
Memorandum of Economic and Financial Policies
Technical Memorandum of Understanding

cc: Prof. Emmanuel Tumusiime-Mutebile, Governor, Bank of Uganda

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Attachment I. Memorandum of Economic and Financial Policies

May 18, 2012

I. Introduction

1. The Government is committed to ensuring macroeconomic stability is maintained as the basis for sustainable economic growth and poverty reduction as set out in the National Development Plan (NDP). This Memorandum of Economic and Financial policies gives an update on economic performance for the first half of the current fiscal year, and lays out the policies Government is undertaking over the period ahead to reduce inflation and enhance growth.

2. We have taken firm measures through a combination of both monetary and fiscal policies to address our immediate priority of reducing inflation, which accelerated to unacceptable levels over the latter half of this year. Given the weak external environment, coupled with tight fiscal and monetary policies associated with the deflationary effort, our FY 2011/12 growth forecast has been cut from 5 to 4¼ percent. The Government will nonetheless persevere in its intention to reduce inflation to single digits by end of calendar year 2012, and to bring it down to the target level of 5 percent for core inflation by the middle of calendar 2013. The tight monetary and fiscal stance will continue into FY2012/13, but priority investment programs will be maintained and measures taken to further our structural reform agenda.

A. Performance under the PSI

3. All seven Quantitative Assessment Criteria (QACs) for end-December 2011 were met. The increase in net credit to the central government by the banking system was within target by Ush 86 billion. The ceiling on the increase in net domestic assets of the BOU was also observed, and international reserves increased by US$302 million, which was slightly more than programmed. Government incurred no external payment arrears, and borrowing on nonconcessional terms remained about US$300 million below the PSI three-year ceiling of US$800 million—although we expect our pressing infrastructure needs will easily fill this borrowing space by the end of the current PSI arrangement in May 2013. All oil revenues have been placed in a dedicated Petroleum Fund in the Bank of Uganda (BOU), and have been ring-fenced for construction of the Karuma Hydropower project. The over-performance on reserves was welcome—although it did had the effect of driving base money above its indicative program target, our inflation objective was in no way compromised.

4. Most of the structural benchmarks in the program were met. The names of beneficiaries of tax exemptions were gazetted and published, we produced regular quarterly reports on unpaid bills of nine Ministries, and have developed an index of high-frequency economic indicators. We have also submitted a strategy to cabinet for a rules-based methodology of ensuring power sector tariffs are adjusted to maintain full cost recovery. Government's net and gross position in the BoU is being reported, but we have not yet

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agreed with suppliers on the volume of residual subsidies needed in the power sector (following January's tariff increase, which eliminates the need for subsidies going forward). We have published cash releases and actual payments for power and water obligations of spending ministries, although the sanctions applied to the accounting officers who allowed arrears to accumulate are not yet public.

II. ECONOMIC AND POLICY DEVELOPMENTS

A. Outturn in the First Half of FY 2011/12

Growth

5. Economic growth slowed in the first half of fiscal year 2011/12 to 1.8 percent, compared to 7.6 percent in the same period last year. For the year as a whole, the economy is expected to expand by 4¼ percent, lower than our previous projection by ¾ percentage points and 2½ percentage points lower than last year. Manufacturing and construction are leading the decline, with growth reduced to 2 and 4 percent this fiscal year from 8 percent in FY2010/11. The services sector is also projected to slow from 8.4 to 5.1 percent. However, agricultural growth showed a recovery in the first half due to a pick-up in cash crop production, and is expected to grow at an annual rate of 1.8 percent, up somewhat from the previous year.

Inflation

6. Inflation picked up sharply during the first half of fiscal year 2011/12, initially from higher food prices and the pass-through of exchange rate depreciation. However, by September, 2011, Government and the Bank of Uganda began to see signs that second round effects of this price shock were feeding through to underlying inflation. Non-food inflation rose significantly, as did core inflation. In consequence, the stance of monetary policy was tightened very sharply over the last four months of calendar 2011, with the BoU's benchmark central bank rate (CBR) rising by a cumulative 1000 basis points relative to July. Tighter monetary policy, combined with cautious fiscal policy, has begun to take effect. From a peak of 30.5 percent in October 2011, inflation has declined gradually to 21.2 percent in March 2012. Underlying price pressure is much reduced, with annualized monthly inflation now down to single digits.

Fiscal Performance

7. Revenue collections for the period July 2011 to February 2012 were lower than expected, even in nominal terms, despite inflation that was higher than forecast at the time the budget was approved. Direct taxes under-performed while indirect taxes were broadly as forecast in the budget. The major source of the underperformance was PAYE, where the shortfall was particularly marked in December 2011.

8. International trade taxes were below target despite exchange rate depreciation that would have been expected to raise the domestic currency value of revenue. Imports from

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EAC countries increased by 30 percent in the first half of the year compared to the same period last year, while imports from the rest of the world declined by 10 percent. This resulted in a slight shortfall in revenue as imports from EAC partner states are covered by the customs union agreement.

9. Grant assistance from our development partners was broadly as expected, while loan disbursements were below programmed levels for the first half of 2011/12 by about 0.4 percent of annual GDP. Project loan disbursements underperformed by more than budget support, which was close to our forecast. It is expected that donor disbursements will be broadly on target for the year as a whole.

10. Overall expenditure for the first half of the fiscal year was about 8 percent below our original projection, mainly owing to lower externally-financed project loan disbursements. As a result, the overall deficit was somewhat lower than programmed.

11. Government will this year incur about 1 percent of GDP in supplementary expenditure in order to deal with unanticipated security threats in the region, and to cater for unforeseen expenditure priorities. However, these supplementaries will be financed mainly through suppression of lower priority expenditures and a modest widening of the budget deficit for the year as a whole. There is however some risk that the target for Poverty Alleviation Fund (PAF) spending will be missed by a small margin.

Balance of Payments

12. The current account deficit has continued to widen, particularly as a result of the trade balance. In the first half of FY 2011/12, the current account deficit stood at US$972 million compared to US$720 million in the same period last year. The import bill grew strongly, in part because of higher international commodity prices. The capital and financial account surplus registered a surplus of about US$1.18 billion from July-December 2011, owing mainly to private inflows and official lending from China compared to US$605 million in the first half of FY 2010/11. Gross international reserves increased by US$476.8 million to US$2.45 billion, which is equivalent to 3.6 months of future imports of goods and services by end-December 2011.

13. The Ugandan shilling experienced significant volatility over the past year, but recovered most of its losses by early 2012. Depreciation was related to the current account deterioration and broadly followed the inflation path, beginning in June 2011 and peaking at 24 percent in September. However, it began strengthening by October as tighter policy called forth substantial capital inflows and portfolio shifts towards domestic assets, so most of the depreciation was reversed by January 2012. With policy addressing the fundamental causes of the weakness of the shilling, BoU used direct intervention only to dampen the most erratic short-term fluctuations.

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Monetary policy

14. The Bank of Uganda implemented a new monetary policy framework in FY 2011/12, termed Inflation Targeting “lite” (ITL). This framework proved effective in enhancing monetary policy communication and anchoring inflation expectations. Its centrepiece is a monthly announcement of our CBR, which targets the 7-day interbank rate within a symmetric band. During the first 9 months of the fiscal year, markets began to respond to the new framework, and interest rates on government bonds and private sector loans have so far closely mirrored changes in the CBR. Moreover, observers have generally expressed satisfaction with the greater transparency of monetary policies in Uganda.

15. The BOU used its new framework to aggressively pursue a tight monetary policy stance during the first half of FY 2011/12, as it recognized that second round effects were beginning to feed through to underlying inflation. Nonfood inflation, in particular, had been very stable for a sustained period, but in August-October 2011 it rose significantly. The objective of the tight stance of monetary policy was to curb second-round effects and anchor medium-to-long-term inflation expectations on a trajectory consistent with the BOU’s medium-term core inflation target of 5 percent. Up to February 2012, the BoU has had considerable ability to affect monetary conditions, and the growth of monetary aggregates has decelerated markedly. In the three months to February 2012, the annual growth rates of M1, M2 and M3 averaged 4 percent, 4 percent and 7 percent, respectively, compared to rates of 35 percent, 35 percent and 38 percent in the corresponding period of the previous year. Private sector credit growth is also more subdued, falling from 37 percent to 24 percent over a similar period. At the same time, tight monetary policies contributed to a strengthening of the exchange rate after September, which fed through to the price of traded goods.

16. With inflation established on a downward trajectory, the BOU began a cautious easing of its policy stance in February 2012. The policy rate was reduced by one percentage point in each of February and March, but then maintained in April at 21 percent owing to concerns about inflationary pressures over the coming months and to allow time for inflationary expectations to firm.

Financial sector

17. The Financial sector remained resilient in the first half of 2011/12, despite the sharp rise in inflation and interest rates. As noted in the FSAP of last year, the sector is well-capitalised and all banks are complying with capital adequacy requirements, registering a regulatory capital to risk-weighted asset ratio of 18.3 percent, which was well above the industry’s benchmark of 12 percent. Asset quality however declined marginally in December 2011 relative to June, as the ratio of non-performing loans to total loans rose to 1.8 percent from 1.6 percent. But bank profitability has increased substantially with higher interest income, and the system remains solvent, liquid and profitable.

18. Development of the nonbank sector has proceeded rapidly, with savings and credit cooperative associations (SACCOs) expanding rapidly throughout Uganda. Government and BoU are preparing a regulatory framework for this segment of the financial market. At the

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same time, the pension sector regulatory authority is expected to be established shortly, after which Government will begin work on a draft bill to liberalize the pension sector.

III. OUTLOOK AND MEDIUM TERM POLICIES

A. Macroeconomic Objectives and Outlook

19. Government's macroeconomic objective over the near term is to ensure macroeconomic stability and growth. Growth is expected to slow to 4¼ percent in FY 2011/12 from 6.7 percent in the previous year, both because of weaker global demand and due to the tight macroeconomic stance needed to curb inflation. However, it should recover to 5.4 percent in 2012/13 and to an average of 7.0 percent over the medium term as macroeconomic stability is restored and investments take place in agricultural production and productivity, power and roads.

Fiscal Outlook for 2012/13

20. Fiscal policy will continue to support the disinflation effort in FY 2012/13, while promoting growth and development through infrastructure enhancement. Tax revenues will be boosted by more than ½ percentage points of GDP from additional tax policy measures (see below) and natural revenue buoyancy. However, we expect this impact to be largely offset by a decline in grants. With capital spending set to increase by 1 percentage points of GDP, significant fiscal savings will be needed from a compression of non-productive expenditure. Current spending is therefore to decline by 2 percentage points of GDP, an ambitious target even though two thirds will come automatically from the end of exceptional security spending and power sector-related payments. We have, therefore, prepared for the eventuality that effecting the necessary cuts in non-priority areas might prove problematic by establishing a contingency of 0.4 percent of GDP. Fiscal policy next year will therefore give priority to infrastructure investments aimed at boosting the productive capacity of the economy. In addition to the Karuma project, this will include improving agricultural productivity and value added, providing additional infrastructure in other areas, primarily roads, and re-skilling the labour force.

21. In light of significant infrastructure and social needs, there remains a pressing need for additional fiscal space, which we will address across a broad front.

- Tax policy measures will be introduced in FY 2012/13 to boost revenue and improve the efficiency of tax collection by streamlining exemptions. Specifically, Government intends to propose in the 2012/13 Finance Bill the following measures, which are expected to yield at least Ush 130 billion (0.3 percent of GDP):

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Tax Policy measures—FY2012/13

Reinstate VAT on water;

Terminate VAT exemptions in the textile sector and for computers, software, printers;

Apply the standard VAT rate to hotels outside Kampala;

Increase the excise duty on locally-produced spirits from 45 to 60 percent;

Increase and shift the excise duty on cigarettes from specific to ad valorem;

Impose excise duty on imported fresh juices;

Terminate corporate income tax exemptions on agro-processing;

Impose an additional 10 percent marginal rate for the top bracket of PAYE;

Tighten the scope of corporate income tax exemptions for plant and machinery and civil works;

Increase the withholding tax rate on interest and dividends from 15 to 20 percent;

Enforce the existing capital gains tax on the sale of commercial buildings by individuals.

- Existing resources will be conserved through renewed emphasis on the efficiency of public spending by implementing performance-based, output-based budgeting. Efforts to synchronize quarterly spending with work plans will be strengthened; and quarterly cash releases will be phased so as to create a more even distribution of the fiscal deficit throughout the year. This is expected to lead to greater spending efficiency, as well as facilitate the more effective conduct of monetary policy.

- Moreover, government will begin to address outstanding weaknesses in tax administration. A Tax Procedure Code (TPC) is being prepared aimed at enhancing the efficiency of our revenue collection. Submission of the TPC to cabinet by the beginning of April 2012 has been set as a structural benchmark for the fifth review of the PSI-supported program. Although progress with the introduction of the National Identification Card system has been delayed, Government expects to accelerate progress over the coming months, such that 4 million ID cards will have been issued by December 31, 2012 (structural benchmark).

- Fiscal space will also be augmented by raising new sources of external financing for selected, well conceived investment projects. The existing US$800 million limit under the PSI-supported program is expected to be fully utilized. Government is therefore requesting a US$200 million increase in this limit to be effective from June 2012. Funds

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raised in this manner will be committed only on projects that have been appropriately vetted and judged to be both efficient and consistent with long-term debt sustainability, and which are "shovel ready" so as to avoid excess finance charges. Government will also investigate the feasibility and advisability of issuing long-term domestic currency denominated bonds to finance critical infrastructure projects, but will refrain from direct borrowing from the BOU for this purpose.

Monetary Policy

22. Government's overarching objective is to bring inflation down to the 5 percent target for core inflation over the medium term. The BoU will maintain its inflation targeting lite (ITL) framework, which has enhanced the transparency and effectiveness of monetary policy, and in this context will steer the CBR such that the pace of disinflation is expected to be consistent with reaching single digits late in 2012, and 5 percent in 2013. Looking ahead, if inflation is higher than forecast over the coming months, the BOU will raise the CBR, to ensure that real interest rates increase. The BOU is committed to act in a manner which will stabilise inflation, by raising the CBR by more than the change in the inflation forecast, i.e. by tightening further if the inflation outlook deteriorates.

23. If, however, price pressures continue to abate as expected, the BOU will gradually relax its policy stance in a manner and rate slow enough to keep expectations well grounded and to minimize both interest rate and exchange rate volatility. This is important not only to facilitate an orderly movement of short-term capital, but also to avoid exacerbating policy challenges stemming from global economic and financial volatility, which has led to uncertainty in regional foreign exchange markets. The flexible exchange rate regime will be maintained along with an open capital account, and the exchange rate will be allowed to fluctuate as needed to absorb external shocks—with intervention limited to smoothing short-term deviations from long-term trend.

24. BOU will continue with reforms to modernise and increase the effectiveness of its monetary policy framework. This will include settling on a definitive inflation target, enhancing the institutional and technical capacity for macroeconomic modelling and forecasting, and improving monetary policy communication in order to boost public confidence in the policy process to further anchor inflationary expectations. The BOU is also seeking to improve liquidity forecasting, develop procedures to ensure greater transparency and accountability, and enhance central bank independence. In this latter regard, and within the context of the Government's intended revision of its Debt Strategy, Government and BoU will review central bank capital arrangements and propose changes to legislation or policy as needed to ensure that the Bank is able to carry out its mandate. As a step toward full fledged inflation targeting, the BoU intends to begin publishing on its website its new monthly indicator of economic activity. It will also begin to distribute in draft form a quarterly inflation report (structural benchmark for December 2012). The BoU has requested the International Monetary Fund provide technical support to help carry out this program.

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IV. STRUCTURAL ISSUES AND REFORMS

A. Co-ordination and policy harmonization in the EAC

25. Policy coordination among the member countries is a prerequisite for deeper regional integration and a monetary union. Since the EAC countries are currently negotiating a monetary union protocol, which will pave way for monetary integration, it is important that they increase the level of macroeconomic policy harmonization.

B. Public Finance Management

26. Government has submitted to Parliament a new "Public Finance Bill" which seeks to consolidate all public finance management legislation. The proposed law consolidates the current PFAA 2003 and the Budget Act 2001 into one comprehensive law. In addition, the proposed new legislation contains provisions for the prudent management of oil revenues as well as for strengthening the management of public assets and liabilities. Moreover, it seeks to improve budget credibility by placing limit on reallocation within the budget, and by establishing a Contingencies Fund to finance supplementary spending. The proposed law is expected to be enacted by Parliament during FY 2012/13 for effect in FY 2013/14.

27. Although the new Public Finance Bill should clarify and limit the ability of government to carry forward expenditure appropriations from one fiscal year to the next, in the meantime, to limit the potential for abuse and diversion of funds, Government will take the following measures regarding unspent balances at the end of FY 2011/12: (i) publish the balances on all government accounts both in the BoU and in commercial banks as at June 30, 2012 and September 30, 2012; (ii) the Minister responsible for finance will present these accounts to parliament by July 31, 2012, and October 30, 2012, respectively; (iii) parliamentary approval, as well as supporting work and procurement plans, will be required in order to spend any balances held over from the previous year; and (iv) all unspent balances which have not been re-appropriated by parliament by end-September must be returned immediately to the Uganda Consolidated Fund.

28. Government understands that internal controls to prevent the accumulation of arrears need to be strengthened. In this context, Government will continue to report on a quarterly basis to Cabinet on all unpaid claims of spending units.

C. Improving the efficiency of cash management

29. To avoid unnecessary interest costs associated with Government borrowing from the domestic market, Government intends to implement measures aimed at improving the efficiency of cash management. One of the key reforms in this regard is the consolidation of the many fragmented Government accounts into a Single Treasury Account. This will help to bring about transparency in the interaction of fiscal and monetary policy, which may help in the appropriate pricing of Government securities.

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D. Oil Revenue Management

30. The Government in February 2012 approved a policy on oil revenue management. The policy stipulates Government's continuation with prudent macroeconomic management to ensure a sustainable path for the non-oil budget deficit, aimed at minimizing the Dutch disease risks, boom and bust cycles, and excessive borrowing. Given that oil and gas revenues are subject to price volatility, we intend to use the non-oil, non-grant budget deficit (consistent with the broader macroeconomic management objectives) as a fiscal anchor to manage this volatility and to mitigate the risks to the economy from natural resource wealth. The anchor sets out the level of oil and gas revenues to be integrated into the budget on annual basis within the overall fiscal framework in a manner that limits the impact on other sectors of the economy.

31. The collection and administration of Government revenues from oil and gas activities will be the responsibility of URA. All oil revenues will be deposited in a special Petroleum Fund at Bank of Uganda with a twin objective of financing the budget and saving for future generations.

32. In order to promote social cohesion and stable investment and production environment, 7 percent of all royalty revenues shall be set aside for sharing between local governments located in the oil and gas producing areas. The mechanism of sharing these revenues amongst the local governments will take into account intra-regional fairness, level of production and sustainability principles.

33. Tax policy and revenue administration will continue to focus on improving non-oil tax revenues, given that oil is a finite and volatile source of revenue. Government borrowing will be conducted in accordance with revised National Debt Strategy. However, no debt will be securitized on the basis of future oil and gas revenues.

E. Improving Public Investment Planning

34. The Public Investment Plan (PIP) is to be re-focused on the National Development Plan, as it does not at present fully reflect the priorities of Government. Most of the projects in the PIP have not been subjected to a critical assessment to determine their benefits and costs. As a result the PIP is bloated with too many projects which are often not adequately funded, and which are not implemented efficiently due to capacity constraints and lack of preparedness. Some projects in the PIP lack feasibility studies, which significantly delays their implementation and often leads to a waste of public funds. A review of the PIP will be carried out and submitted to cabinet by September 2012 aimed at scaling back the number of projects and aligning the remainder with the availability of resources. Going forward, new projects will all be subject to critical cost-benefit analysis before their inclusion in the PIP, and the quality of these projects will generally be improved at the identification stage. This will facilitate credible alignment of the NDP priorities with the Medium Term Expenditure Framework (MTEF) and a proper costing of Government programs and projects, and hence promote improved value for money.

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F. Power Sector Reforms

35. Government is committed to undertaking reforms that will create a more attractive business environment for private sector investment. These reforms include reducing system loses and improving financial management by rolling out prepaid meters. To this effect, Government will begin implementing its strategy for the power mix of the country. We plan to start production of heavy diesel oil which will be used to generate thermal power at a lower cost than the current private operators. The Bujagali Hydropower has come partially on stream and is expected to reach full capacity of 200 megawatts by later this year. However, in view of growing power demand as the economy expands, the additional power thus generated will only be adequate for the next two years, beyond which demand will again outstrip supply. Government is therefore exploring various financing options for new power plants, including possible issuance of Government infrastructure bonds when macroeconomic conditions improve.

V. Program Monitoring

36. Progress with implementation of the policies under this program will be monitored through quantitative assessment criteria (QACs), indicative targets (ITs), and structural benchmarks (SBs), as detailed in the attached Tables 1 and 2; and through semi-annual reviews. Modified QACs are proposed for end-June 2012 and new QACs are proposed for end-December 2012. The sixth review is expected to be completed by May 11, 2013. The attached Technical Memorandum of Understanding—which is an integral part of this Memorandum—contains definitions and adjusters. During the program period, we will refrain from imposing or intensifying exchange restrictions as well as restrictions on imports for balance of payments reasons, or from introducing multiple currency practices.

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Table 1. Uganda: Proposed Quantitative Assessment Criteria and Indicative Targets for June 30, 2012 - March 31, 2013[1]
(Cumulative change from the beginning of the fiscal year, unless otherwise stated)

	June 30 2012		Sept. 30 2012 [2]	Dec. 31 2012	Mar. 31 2013 [2]
	3rd Review	Rev. Prog.			
			(Ush billions)		
Assessment criteria					
Ceiling on the increase in net domestic assets of the Bank of Uganda	892	892	120	265	182
Ceiling on the increase in net claims on the central government by the banking system	481	537	170	683	868
			(US$ millions)		
Ceiling on the stock of external payments arrears incurred by the public sector [3]	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 [3, 4]	800	1,000	1,000	1,000	1,000
Ceiling on new external debt with maturity up to one year contracted or guaranteed by the public sector [3 5]	0	0	0	0	0
Minimum increase in net international reserves of the Bank of Uganda (US$mn)	300	300	41	83	144
Share of oil revenue placed in the Petroleum Fund	100	100	100	100	100
			(Ush billions)		
Indicative targets					
Ceiling on the increase in base money liabilities of the Bank of Uganda	471	471	156	318	400
Stock of domestic budgetary arrears under the Commitment Control System (CCS) [6]	0	0	…	…	…
Minimum expenditures under the Poverty Action Fund	1,300	1,300	…	700	…
Ceiling on the issuance of guarantees by the Government/Bank of Uganda	0	0	0	0	0
Memo item					
Upper band	…	18.0	16.0	12.0	10.0
Twelve-month consumer price inflation (percent) [7]	…	15.0	13.0	9.0	7.0
Lower band	…	12.0	10.0	6.0	4.0

[1] Defined in the technical memorandum of understanding (TMU).
[2] Indicative Target
[3] Continuous assessment criterion.
[4] Cumulative change from May, 2010. To be used exclusively for infrastructure investment projects.
[5] Excluding normal import-related credits.
[6] Monitored annually.
[7] Annual end-of-period inflation.

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Table 2. Uganda: Structural Benchmarks Under the PSI		
Policy Measure	**Macroeconomic Rationale**	**Date**
Government to begin to gazette and publish on the internet the names of beneficiaries (whether individual or corporation) of all tax expenditures.	Enforce discipline in issuance of tax exemptions.	July 1, 2012, for quarter ending March 31, 2012; October 1, 2012, for quarter ending June 30, 2012; January 1, 2013, for quarter ending September 30, 2012; and April 1, 2013, for quarter ending December 31, 2012.
Begin submitting to Cabinet regular quarterly reports on unpaid bills of nine Ministries based on data in the Commitment Control System (CCS) for the previous quarter of the fiscal year (MEFP ¶8).	To facilitate control and elimination of expenditure arrears	As for measure immediately above.
Produce and disseminate within government a monthly index of economic activity relying on the various high-frequency indicators available (MEFP ¶24).	To facilitate the conduct of monetary policy.	As for measure immediately above.
BoU to include in Quarterly Report data on the net and gross positions of government in the BoU.	Enhance central bank independence and prepare Bank of Uganda to move toward inflation targeting.	As for measure immediately above.
Government to publish releases by MoFPED for power and water obligations of spending ministries, and actual payments by them, with sanctions to be applied to the named Accounting Officers of agencies that run arrears on these utilities. (MEFP ¶4).	Help control accumulation of arrears. Replaces benchmark on "straight-through payments"	As for measure immediately above.
As part of introduction of national identification system, 4 million additional citizens will have received IDs (MEFP ¶21).	To support efforts to strengthen revenue collection and combat money laundering and the financing of terrorism.	December 31, 2012.
Government to maintain transparency over the treatment of unspent budgetary funds at the end of the fiscal year by (i) publishing the balances as at June 30 and September 30 on all government accounts in the BoU and commercial banks, and (ii) in order to spend any balances held over from the previous year beyond end June, parliamentary approval as well as supporting work and procurement plans will be required (MEFP ¶27).	To enhance budgetary discipline and promote fiscal transparency.	(i) June 30, 2012 data to be published by July 31, 2012, and September 30 date to be published by October 30. (ii) Continuous
Submit to Cabinet a new tax procedure code (MEFP ¶21).	To improve domestic revenue mobilization.	April 1, 2013
Bank of Uganda to distribute in draft form a quarterly inflation report	To improve the monetary policy framework.	December 31, 2012

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Attachment II. Uganda: Technical Memorandum of Understanding

I. Introduction

1. This memorandum defines the quarterly assessment criteria and indicative targets described in the memorandum of economic and financial policies (MEFP) for the financial program supported by the IMF Policy Support Instrument (PSI) over the period of June 30, 2012—March 31, 2013, and sets forth the reporting requirements under the instrument.

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

2. Net foreign assets (NFA) 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, excluding oil revenues in the petroleum fund. 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 referred to in the table below for the various currencies and then converted into Uganda shillings using the program average U.S. dollar-Uganda shilling exchange rate for August 31, 2011.

Program Exchange Rates

US dollar (US$)	1.0000
British pound/US$	1.6282
US$/Japanese yen	76.4600
SDR/US$	1.6094
US$/Kenyan shillings	93.8000
US$/Tanzania shillings	1,619.5000
Euro/US$	1.4398
US$/Ugandan shillings	2,821.1300

3. Net domestic assets (NDA) of the 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 paragraph 2). Based on this definition, the NDA limit for June 2012 will be a ceiling on the cumulative change from the monthly average based on daily data for June 2011 to the same monthly average for June 2012. The NDA limits for September 2012, December 2012, and March 2013 will be ceilings on the cumulative change from the monthly average based on daily data for June 2012 to the same monthly averages for September 2012, December 2012, and March 2013, respectively. NDA limits for June 2012 and December 2012 will be quantitative assessment criteria under the PSI-supported program; limits for September 2012 and March 2013 will be indicative targets.

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III. Base Money

4. Base money is defined as the sum of currency issued by the 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 limit for June 2012 will be a ceiling on the cumulative change from the monthly average based on daily data for June 2011 to the same monthly average for June 2012. The base money limits for September 2012, December 2012, and March 2013 will be ceilings on the cumulative change from the monthly average based on daily data for June 2012 to the same monthly averages for September 2012, December 2012, and March 2013, respectively. Base money limits for June 2012, September 2012, December 2012, and March 2013 will be indicative targets under the PSI-supported program.

IV. Ceiling on the Cumulative Increase in Net Claims on the Central Government by the banking system[1]

5. Net claims on the central government 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 oil revenues in the petroleum fund and 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 by the banking system will be calculated based on data from balance sheets of the monetary authority and commercial banks as per the monetary survey.

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

6. 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.

7. 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 the stock from their original currency denomination at program exchange rates (as specified in paragraph 2). The NIR limit for June 2012 will be a floor on the change of the NIR stock from June 2011 to June 2012. The NIR limits for September 2012, December 2012, and March 2013 will be floors on the change of the NIR stock from June 2012 to September 2012, December 2012,

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

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and March 2013, respectively. NIR limits for June 2012 and December 2012 will be quantitative assessment criteria under the PSI-supported program; floors for September 2012 and March 2013 will be indicative targets.

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

8. The stock of domestic payment arrears/unpaid payment claims will be monitored on a quarterly basis. Domestic payments arrears/unpaid payment claims 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 end of the quarter in question, and for which payment has not been made, under the recurrent expenditure budget (excluding court awards and pensions) or the development expenditure budget. For the purpose of program monitoring, the reports on domestic payment arrears/unpaid payment claims prepared by the Auditor General will be used to monitor this item following the end of the fiscal year. In the interim, the reports prepared by the Accountant General on unpaid claims will be monitored to gauge expenditure pressures.

VII. Expenditures under the Poverty Action Fund (PAF)

9. The indicative target on expenditures under the Poverty Action Fund is designed to ensure that resources freed by debt relief are used for additional PAF expenditures. Compliance with the indicative floor for PAF expenditures will be verified on the basis of releases (PAF resources made available to spending agencies).

VIII. Ceiling on Issuance of Guarantees by the Government or Bank of Uganda

10. The indicative target on issuance of guarantees by the Government or Bank of Uganda aims to prevent accumulation of contingent liabilities by the Government (including Government entities such as ministries, agencies and authorities). Included against the ceiling are any direct, contingent liabilities of Government (including entities that are part of government such as ministries, agencies and authorities) issued after June 30, 2011, and including any guarantees issued prior to July 1, 2011 but which are extended after June 30, 2011. This excludes guarantee programs which have explicit budget appropriations.

IX. Share of Oil Revenue Placed in Petroleum Fund

11. The purpose of this assessment criterion is to avoid a situation whereby petroleum revenues bypass the Ugandan budget framework. A petroleum fund will be created upon passage of the revised Public Finance Act; in the meantime, government has established a petroleum revenue account in the Bank of Uganda. This QAC will be deemed satisfied if 100 percent of petroleum revenues are transferred to this account upon collection by URA. These resources may then be spent or saved as governed by the organic budget law in force at the time (PFAA 2003 until the new PFA is enacted).

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X. CONSUMER PRICE INFLATION

12. Inflation is measured by the headline twelve-month rate of annual end-of-period CPI inflation published by the Uganda Bureau of Statistics (UBOS). Quarterly bands denoting the target range are specified in Table 1.

XI. ADJUSTERS

13. 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), external debt-service payments.

14. The NCG target for the banking system, 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.

15. The Uganda shilling equivalent of projected budget support (grants and loans) plus HIPC Initiative assistance in the form of grants on a cumulative basis from July 1 of the relevant fiscal year is presented under Schedule A. The ceilings on the cumulative increase in NDA and NCG for the banking system 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 (Including HIPC and MDRI)
(Ush billions)

	Jun-12	Sep-12	Dec-12	Mar-13
Cumulative change from July 1, 2011	1,017	…	…	…
Cumulative change from July 1, 2012	…	146	346	473

16. The ceiling on the increases in NDA and NCG of the banking system 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

[2] Debt service due is defined as pre-HIPC Initiative debt service due, excluding debt service subject to HIPC Initiative debt rescheduling.

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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: External Debt Service
(Ush billions)

	Jun-12	Sep-12	Dec-12	Mar-13
Cumulative change from July 1, 2011	108	…	…	…
Cumulative change from July 1, 2012	…	21	46	68

17. The ceiling on increases in NCG of the banking system will be adjusted downward (upward) by any excess (shortfall) in nonbank financing, relative to the programmed cumulative amounts in Schedule C. Non-bank financing will include any domestic debt—either in domestic currency or foreign currency— of the Government of Uganda that is held by creditors—whether resident or nonresident[3]—that is not included in the Ugandan banking system. It will include the change in government securities held by the nonbank sector as reported in the monetary survey, as calculated by data provided by the Central Depository System (CDS), plus any other claims on government, including entities of government (ministries, agencies, authorities, etc.), held outside the banking system, including those which might be held by the National Social Security Fund (NSSF).

Schedule C: Non-bank Financing
(Ush billions)

	Jun-12	Sep-12	Dec-12	Mar-13
Cumulative change from July 1, 2011	482	…	…	…
Cumulative change from July 1, 2012	…	86	105	256

18. The floor on the cumulative increase in NIR of the BOU will be adjusted downward by the amount by which foreign exchange expenditures on the Karuma hydropower project exceeds the projected amounts as set out in Schedule D. The ceiling on NDA will be adjusted upward (downward) by the amount by which the domestic currency equivalent of Karuma

[3] Non-residents holding government securities are excluded from the definition of external debt in paragraph 20.

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spending (using the annual program exchange rate) exceeds (falls short of) the projected amounts as set out in Schedule D. The ceiling on NCG will be adjusted upward (downward) by the amount by which the domestic currency equivalent of Karuma spending (using the market exchange rate) exceeds (falls short of) the projected amounts as set out in Schedule D.

Schedule D: Expenditures for Karuma Hydropower Project
(US$ millions)

	Jun-12	Sep-12	Dec-12	Mar-13
Cumulative change from July 1, 2011	157	…	…	…
Cumulative change from July 1, 2012	…	0	365	365

19. The floor on the cumulative increase in NIR of the BOU will be adjusted downward by the amount by which inflows into the Petroleum Fund falls short of the projected amounts as set out in Schedule E. The ceiling on NDA will be adjusted upward (downward) by the amount by which the domestic currency equivalent of Karuma spending (using the annual program exchange rate) falls short of (exceeds) the projected amounts as set out in Schedule E. The ceiling on NCG will be adjusted upward (downward) by the amount by which the domestic currency equivalent of Karuma spending (using the market exchange rate) falls

Schedule E: Inflows into Petroleum Fund
(US$ millions)

	Jun-12	Sep-12	Dec-12	Mar-13
Cumulative change from July 1, 2011	…	…	…	…
Cumulative change from July 1, 2012	…	308	308	308

short of (exceeds) the projected amounts as set out in Schedule E.

20. 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 re-discounting of government securities by commercial banks.

21. 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 changes 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.

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XII. 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]

22. 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 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 23.

23. 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. The ceiling also excludes nonconcessional borrowing by one state-owned bank, Housing Finance Bank, which poses limited fiscal risk and is in a position to borrow without a government guarantee.

24. 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

[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.

[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

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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, 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 sometime 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.

25. 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.

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XIII. Monitoring and Reporting Requirements

26. The Government of Uganda will submit information to IMF staff with the frequency and submission time lag as indicated in Table 1. The quality and timeliness of the data submission will be tracked and reported by IMF staff. The information should be mailed electronically to AFRUGA@IMF.ORG.

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Attachment II. Table 1. Summary of Reporting Requirements			
Reporting institution	**Report/Table**	**Submission Frequency**	**Submission lag**
I. Bank of Uganda	Issuance of government securities, repurchase operations and reverse repurchase operations	Weekly	5 working days
	Operations in the foreign exchange	Weekly	5 working days
	Interest rates (7 day interbank, commercial bank prime lending rate, government securities)	Weekly	5 working days
	Private sector credit growth by shilling and forex, and excess reserves of commercial banks	Weekly	5 working days
	Disaggregated consumer price index.	Monthly	2 weeks
	Balance sheet of the BOU, consolidated accounts of the commercial banks, and monetary survey.	Monthly	4 weeks
	Daily balances of net foreign assets, net domestic assets, and base money of the BoU (as defined in paragraphs 2, 3, and 4)	Monthly	4 weeks
	Monthly foreign exchange cash flow table of BOU.	quarterly	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.	Quarterly	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.	Quarterly	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; ((iv) new nonconcessional external borrowing; and (v) net international reserves	Quarterly	6 weeks

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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).	Monthly	4 weeks
	Summary of outstanding stock of unpaid payment claims	Quarterly	6 weeks
	Summary of contingent liabilities of the central government and the Bank of Uganda. 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 monthly central government account of disbursed budget support and project grants and loans (less change in the stock of project accounts held at the BoU and commercial banks), HIPC support, and external debt service due and paid.	Quarterly	4 weeks
	Detailed central government account of disbursed donor project support grants and loans.	Monthly	6 weeks
	Statement on new external loans contracted or guaranteed by the central government and the Bank of Uganda 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	12 weeks

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INTERNATIONAL MONETARY FUND
AND INTERNATIONAL DEVELOPMENT ASSOCIATION

UGANDA

JOINT IMF/WORLD BANK DEBT SUSTAINABILITY ANALYSIS 2012 UPDATE[1]

Prepared by the Staffs of the International Monetary Fund
and the International Development Association

Approved by Roger Nord and Dominique Desruelle (IMF)
and Marcelo Giugale and Jeffrey Lewis (IDA)

May 18, 2012

Uganda continues to be assessed at a low risk of debt distress based on the low-income country debt sustainability analysis (LIC DSA) despite recent challenges to the economy from high inflation, weakening external demand, and slower growth. Both baseline public and external DSA suggest Uganda's public sector debt is sustainable given the current size and evolution of the debt stock. Compared to the 2011 DSA assessment, overall public debt sustainability deteriorates modestly, because of a much tighter monetary policy in FY2011/12 and lower-than-expected growth. While the authorities will continue to rely primarily on highly concessional financing to fund their infrastructure investment needs, they are planning to scale up non-concessional sources for several critical infrastructure projects. The DSA hence includes an increase in the non-concessional borrowing ceiling under the PSI to US$1 billion from US$800 million. In addition, it incorporates an envisaged oil sector scenario.

The oil scenario suggests that external financing needs for oil sector development and deterioration of current account could add to medium-term debt vulnerabilities before production comes on stream in full capacity. Yet, beyond oil, downside risks on public debt cannot be ruled out, as implied by the shock scenarios of fixed primary deficits and permanently lower growth. These results highlight the need to maintain fiscal prudence and improve the efficiency of growth enhancing expenditure, particularly through improvements in investment planning, project selection, implementation capacity, and debt management.

[1] As Uganda is an IDA-only country, this DSA update is prepared jointly by the IMF and World Bank staff under the IMF-WB DSA framework for Low-Income Countries. The fiscal year of Uganda starts from July 1st.

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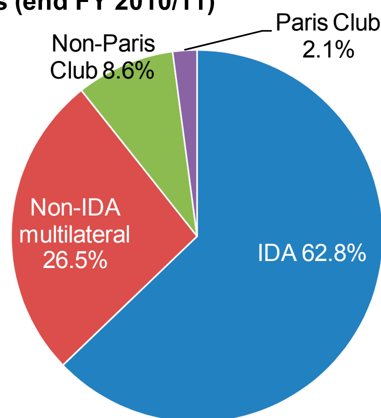
I. BACKGROUND AND RECENT DEVELOPMENTS

1. **Uganda has effectively maintained a sustainable public and external debt position over the past year amid a challenging economic environment.** The Ugandan economy suffered from rising food and energy prices, as well as adverse weather conditions in 2011. Inflation peaked at around 30 percent in last October accompanied by exchange rate depreciation, but both are now considerably improved following a decisive tightening of monetary conditions in the latter part of the year. This episode notwithstanding, Uganda's generally sound macroeconomic policies and cautious approach to public borrowing have kept the overall public debt burden manageable and sustainable, with all debt indicators well below their policy-dependent thresholds (Box 1).[2]

2. **Prudent fiscal management and modest public sector deficits helped safeguard Uganda's debt position.** Debt management has remained cautious since debt relief (HIPC and MDRI). New external borrowing was mainly used to finance infrastructure-related projects, including in energy and transportation, and was contracted on highly concessional terms, mostly from the IDA and the AfDB (text Figure 1). In mid-2011 the authorities requested an increase in the non-concessional borrowing ceiling under the PSI from US$500 million to US$800 million.[3] In light of their commitment to enhance infrastructure, the authorities recently requested a further augmentation to US$1 billion to fund additional projects. However, actual commitments and disbursements under the nonconcessional borrowing limit remain moderate, and public and publically guaranteed external debt remains low, estimated at around 19.7 percent of GDP by end-FY2011/12. Most of the external debt is owed to multilaterals on concessional terms, with IDA accounting for 62.8 percent of total debt (Figure 1). The domestic debt stock remains modest, currently at around 13percent of GDP (Table 1a).

Figure 1. PPG external debt breakdown by creditors (end FY 2010/11)



[2] Uganda is ranked as a "strong performer" under the Country Policy and Institutional Assessment (CPIA) framework of the World Bank. Accordingly, debt burden thresholds for Uganda are PV of debt to GDP ratio of 50 percent, PV of debt-to-exports ratio of 200 percent, PV 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.

[3] A contract with China was signed for US$110 million on non-concessional terms in 2010, and Parliament approved another US$350 million with China in 2011.

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Box 1. Changes in Debt Indicators since the Last DSA

- **Public and publicly guaranteed (PPG) external debt** increased from US$ 2.3 billion (15.3 percent of GDP) to US$ 2.9 billion (19.5 percent of GDP) between FY2009/10 and FY2010/11, partially due to planned non-concessional borrowings and large exchange rate devaluation (Table 1b).
- The **PPG debt-service-to-exports ratio** has remained stable at 2.7 percent over this period (Table 1b).
- Domestic debt increased from 9.3 percent of GDP to 13.4 percent in FY2010/11, contributing to the increase of **total public debt** from 24.6 percent to 32.9 percent of GDP (Table 1a).
- The PV of **PPG debt-service-to-revenue ratio** remained at 4.5-4.6 percent over this period reflecting a large portion of concessional borrowing (Table 1b).
- The **PSI ceiling** on external non-concessional borrowing is maintained at US$800 million, but is assumed to rise to US$1 billion starting from June 2012.

3. **The authorities plan to implement large-scale critical infrastructure projects to remove persistent growth bottlenecks.** Uganda's main medium-term development priorities are in the energy and transportation sectors, as described in its National Development Plan. The construction of Karuma hydropower plant is expected to commerce in FY2012/13 after some delays, and several road projects are being planned. Some of the projects will be funded through private-pubic-partnerships. Furthermore, the authorities are making progress in sorting out the development strategy for the oil sector, which has been stalled for some time. A small refinery is likely to be built starting from late FY2012/13, and there is at now some discussion of an export pipeline, possibly in the context of a regional complex involving South Sudan. In the long run, oil sector development would greatly lift Uganda's growth prospects, but its implications for medium-term fiscal and debt burdens need to be carefully examined.[4]

II. Assumptions and Comparisons with the Previous DSA

4. **Near-term projections have been revised from the previous DSA to reflect recent developments in the economy, with medium to long-term assumptions broadly unchanged.** Contrasting a resilient performance in the past two years, growth in FY2011/12 and FY2012/13 is projected to slow down to 4.2 and 5.4 percent respectively—somewhat below the historical average of 6-7 percent, due to weakening global demand and the tighter stance of monetary and fiscal policy in FY2011/12. Average inflation (GDP deflator) in FY2011/12 is projected to be 22.5 percent—almost twice as high as in the previous DSA—although the recent inflationary episode is currently under correction and the authorities aim to bring it back to its central bank's target range of 5 percent for core inflation by June 2013.

[4] An alternative scenario incorporating elements of oil sector developments is presented in the external debt sustainability analysis, and Box 3 outlines the underlying assumptions of this scenario.

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5. **The baseline scenario underlying the DSA assumes medium-term growth to rebound to 7 percent and inflation to revert to its historical average,** in line with the projections from the forthcoming IMF Staff Report for the 4th review of the PSI. Sources of growth in the medium term include services and trade recovery, as well as more public investments in roads and energy expected to begin removing capacity bottlenecks and unlock additional growth potential.[5] A sound monetary policy, supported by a prudent fiscal stance would help reduce inflation to single digit by end-2012, helped by an easing of food and fuel prices. The public sector deficit (including grants) increases slightly in the near term in response to rising public investment demand before stabilizing at about 3 percent of GDP. Compared with the 2011 Joint IMF-World Bank DSA Update, the current baseline scenario assumes a less ambitious growth path in the near term, reflecting both sluggish global demand and the back-loading of infrastructure investment (Box 2).

Box 2: Ex post analysis of the 2011 DSA update

- **Exports have under-performed since the last DSA**, as global demand remained sluggish, especially in the Euro area, which is a major trading partner.
- **With high import content in infrastructure projects, the current account balance deteriorated in FY2011/12, due also in part to depreciation in the first half of the year as well as lower official transfers** (rescheduled capital gain tax payment)**.** The Uganda Shilling depreciated more than 20 percent in nominal terms in early 2011 before rebounding to historical levels recently, resulting in rising import costs.
- **The current baseline scenario includes slightly more external borrowing** than in the previous DSA, in line with the envisaged US$200 million increase of the ceiling on non-concessional borrowing and back-loading of infrastructure projects.
- **On the fiscal side, both public revenue and expenditure have not performed as well as projected in the previous DSA**. Revenue collection is estimated to decline as percentage of GDP in both FY2010/11 and 2011/12, reflecting slower growth and delayed reforms in tax policy. Looking forward, the fiscal position would improve moderately as tax measures—such as the removal of tax exemptions—are implemented in FY2012/13.
- **The external position in the medium term is worse than in the previous DSA.** Nonetheless, reserve cover and the underlying external position are expected to improve amid downside risks including uncertainties regarding oil sector development**.**

[5] The Bujagali hydropower plant began operation in early 2012. It is expected to be fully operational by end-year and should help mitigate power shortages that have contributed to reduced growth through FY2011/12, and contain both power generation costs and power subsidies.

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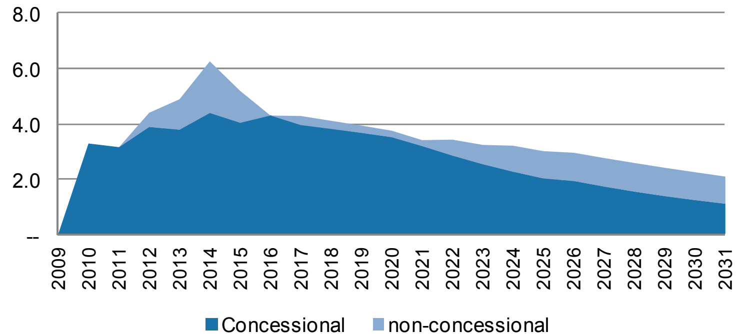
6. **External public financing continues to be dominated by concessional donor inflows, but commercial borrowing will become increasingly important.** As concessional assistance including aid inflows is projected to decline in the outer years, the use of nonconcessional resources is programmed to rise to about half the new external financing by the end of the projection period[6] (Figure 2). Despite the fact that Uganda will not graduate from IDA in the medium term, the overall grant element of new public borrowing declines gradually over time, from over 40 percent to below10 percent by 2032 (Figure 1a). Although aid flows are projected to decline as GDP per capita rises, more access to less concessional resources from both multilateral (such as IBRD) and bilateral lenders are expected to fill this gap. Public domestic debt[7] is expected to remain relatively stable from 10 to 13 percent of GDP, addressing the need for further development of domestic financial markets.

Figure 2. New concessional and non-concessional borrowing in the baseline scenario (in percent of GDP)



III. External Debt Sustainability Update

7. **Public and publicly guaranteed (PPG) external debt is assessed to be sustainable over the projection period** (Figure 1a and Table 1b), with all five debt-burden indicators staying well below their policy-dependent thresholds throughout the period. The PV of debt-to-GDP ratio is expected to rise moderately (from 13 percent in FY 2010/11 to 24.3 percent in FY2016/17) due to external borrowing for productive investment, before stabilizing at 20 percent in the outer years. Similarly, the PV of debt-to-exports ratio is expected to peak at 112 percent in FY2015/16 before going down gradually to 65.7 percent. The debt service-to-exports and to- revenue ratios remain very low, in a range of 1-2 percent, reflecting the large proportion of concessional borrowing in the debt stock.

8. **The PPG external debt position remains sustainable in the face of all standardized shocks** (Figure 1a, Tables 1b and 2a). All stress tests show a low risk of debt distress with the debt-to-GDP, debt-to-exports, debt-to-revenue, debt service-to-exports, and debt service-to-revenue indicators remaining below their indicative threshold values

[6] Nonconcessional borrowing is assumed to be contracted on IBRD-like terms with an interest rate ranging between 4 to 5 percent with10 years of grace period and 20 years of repayment.

[7] The recent increase in public domestic debt in FY2010/11 was mainly due to the much tightened monetary policy which introduced a strong appetite on domestic bonds. But the trend is assumed to revert after inflation drops to meet the annual targets.

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throughout the projection period. The most severe shocks include a further weakening of global demand and less favorable borrowing terms, which only modestly increase the external debt burden.

9. **The alternative scenario of oil sector development presents a more favorable long-run external debt path, while it has to be interpreted with caution.** Given the ongoing debates among all stake holders on the oil sector development strategy, uncertainties remain from many aspects, including modality (refinery or pipeline), revenue sharing, and export potential. This alternative scenario relies on certain normative assumptions outlined in Box 3. The key message is that, although the bulk of investments on oil sector would be financed through FDIs, external financing needs and deterioration of current account could add to medium-term debt vulnerabilities before production comes into stream in full capacity (Table 2a).

Box 3: Assumptions for the oil sector development

- **Construction of both a small refinery and pipeline** would start from late FY2012/13 and continue towards 2020, and total capital expenditure is estimated at between US$7 to 10 billion with 90 percent of import contents.

- **Small testing production of about 1,000 barrels per day begins late 2013,** and would gradually increase to full capacity by 2020 at about 100,000 barrels per day. As a result, oil products are expected to meet domestic demands before exporting to the region.

- **The current account would deteriorate significantly during the construction phase,** although such investment would carry its own financing mainly through FDIs (90 percent assumed) and ultimately result in a significantly improved external position after large-scale exports begin.

- **Real growth would pick up during the investment phase as well as the beginning of full production.** Based on the investment and production profile, real GDP growth is estimated to be 3-5 percent higher over the medium term and long-run potential growth would increase by 3 percent.

IV. Fiscal Debt Sustainability Update

10. **Both baseline scenario and stress tests suggest that the evolution of total public debt including PPG external and domestic debt is sustainable over the projection period** (Figure 1b, Tables 1a and 2b). Under the baseline, the PV of public debt to GDP and to revenue increases moderately in the medium term, mainly driven by infrastructure-related external borrowing, but both would remain at comfortable levels in the long run. It is worth noting that the implied moderate decline in domestic debt in the near term reflects higher

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domestic interest costs due to the recent monetary tightening. Similar to the stress test of the previous DSA, fixing the primary deficit at the level of FY2011/12 would show a less favorable scenario– however, under the PSI framework the fiscal stance is being tightened significantly in FY2011/12 compared to the previous fiscal year, leading to less severe debt path implied by the stress test in this DSA.

11. **Of all other alternative scenarios and bound tests, a permanent shock to growth has the second strongest impact on the public debt burden**. Under this scenario, the PV of debt-to-GDP ratio increases to 52 percent (Table 2b), illustrating the importance of ensuring the planned investments generate growth dividends to maintain a healthy debt path. The PV of debt to GDP is relatively unaffected by other bound tests, staying close to the baseline under all scenarios. Furthermore, in most cases the PV of debt and debt service to revenue ratios are broadly consistent with the baseline, with the exception of the two above-mentioned alternative scenarios of fixing primary balance and a permanent shock to growth. This reveals how critical a prudent fiscal position and careful project appraisal, selection, and execution would be to ensuring long-term debt sustainability for Uganda.

12. **The authorities broadly agree with the results of the DSA, which are consistent with the results of their own DSA exercise.** The authorities are using more conservative assumptions for non-concessional borrowing, while relying primarily on highly concessional financing in the pipeline to prioritize project needs. However, they are fully aware of the implications of non-concessional borrowing and the envisaged oil development on debt burdens.

V. Conclusion

13. **Overall, Uganda's public and external debt positions are projected to remain sustainable over the projection period**. The scenarios outlined above are consistent with the authorities' National Development Plan—which details a cautious approach combining reliance on concessional borrowing with careful selection of commercially financed infrastructure projects, and supported by a prudent fiscal stance in line with the PSI. The oil scenario suggests that external financing needs for oil sector development and deterioration of current account could add to medium-term debt vulnerabilities before production comes into stream in full capacity. To help strengthen the fiscal position and smooth the transition, tax and revenue policies should continue to focus on improving non-oil revenue, given that oil is a finite and volatile source of income. In this regard, government borrowing should be conducted in accordance with revised National Debt Strategy as well as the forthcoming PFA. Beyond oil, vulnerabilities could result from both rising deficits and a protracted negative growth shock, stressing the needs for improvement in investment planning, project selection, and implementation capacity.

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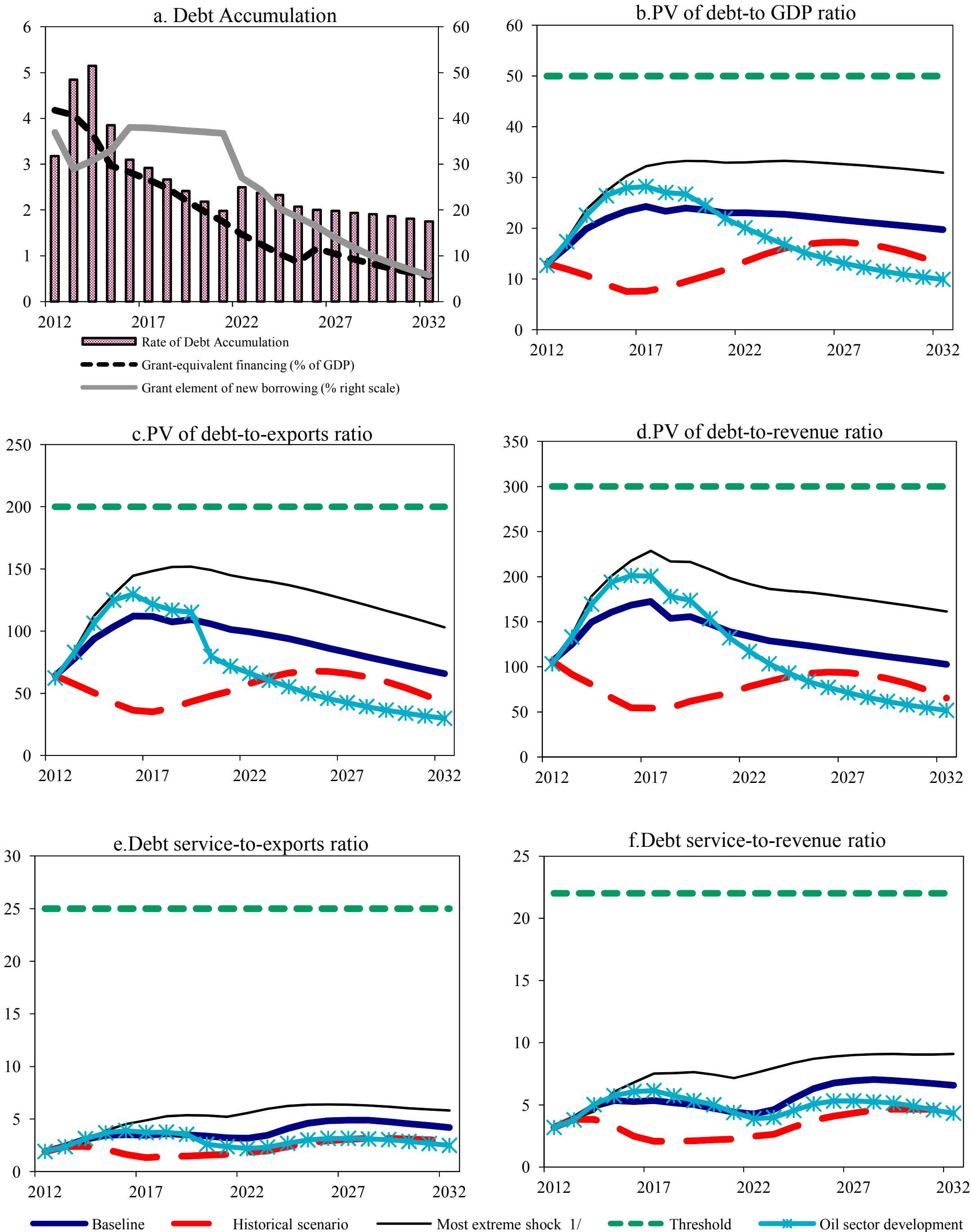
Figure 1a. Uganda: Indicators of Public and Publicly Guaranteed External Debt under Alternatives Scenarios, 2012-2032 1/



Sources: Country authorities; and staff estimates and projections.

1/ The most extreme stress test is the test that yields the highest ratio in 2022. In figure b. it corresponds to a Terms shock; in c. to a Terms shock; in d. to a Terms shock; in e. to a Terms shock and in figure f. to a Terms shock

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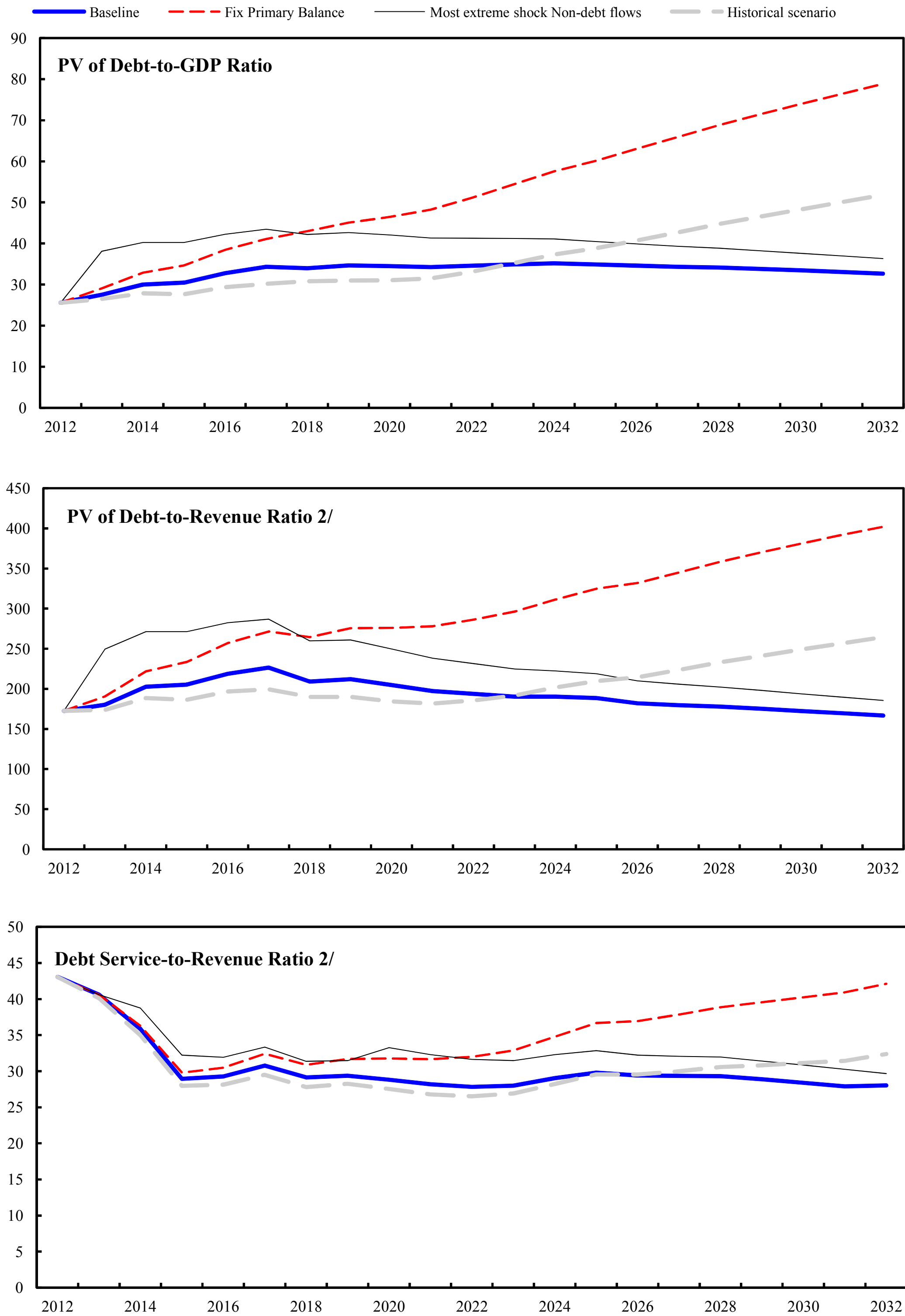
Figure 1b. Uganda: Indicators of Public Debt Under Alternative Scenarios, 2012-2032 1/



Sources: Country authorities; and staff estimates and projections.
1/ The most extreme stress test is the test that yields the highest ratio in 2022.
2/ Revenues are defined inclusive of grants.

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Table 1a.Uganda: Public Sector Debt Sustainability Framework, Baseline Scenario, 2009-2032
(In percent of GDP, unless otherwise indicated)

	Actual			Average [5/]	Standard Deviation [5/]	Estimate	Projections								
	2009	2010	2011			2012	2013	2014	2015	2016	2017	2012-17 Average	2022	2032	2018-32 Average
Public sector debt 1/	22.2	24.6	32.9			32.2	35.2	39.2	40.4	43.6	45.7		44.7	37.3	
o/w foreign-currency denominated	13.8	15.3	19.5			19.7	24.0	29.1	31.8	34.3	35.6		33.2	24.4	
Change in public sector debt	-0.3	2.3	8.4			-0.7	3.0	3.9	1.2	3.2	2.1		-0.1	-0.9	
Identified debt-creating flows	0.7	2.9	6.6			-2.3	0.3	0.8	0.0	0.3	0.1		-2.6	-3.7	
Primary deficit	1.1	3.5	6.1	1.3	2.3	3.4	2.0	2.2	2.0	1.9	2.2	2.3	0.3	-1.6	-0.4
Revenue and grants	15.0	15.0	15.6			14.8	15.3	14.8	14.8	15.0	15.1		17.8	19.6	
of which: grants	2.6	2.7	2.3			2.6	2.2	1.5	1.2	1.1	1.1		0.7	0.4	
Primary (noninterest) expenditure	16.1	18.5	21.7			18.3	17.2	17.0	16.9	16.9	17.4		18.1	18.0	
Automatic debt dynamics	-0.4	-0.7	0.6			-5.8	-1.6	-1.4	-2.1	-1.6	-2.2		-2.9	-2.1	
Contribution from interest rate/growth differential	-1.7	-0.8	-0.9			-2.7	-1.1	-1.4	-2.2	-2.2	-2.3		-2.3	-1.7	
of which: contribution from average real interest rate	-0.2	0.4	0.6			-1.4	0.6	0.6	0.4	0.5	0.6		0.6	0.8	
of which: contribution from real GDP growth	-1.5	-1.2	-1.5			-1.3	-1.6	-2.0	-2.6	-2.6	-2.9		-2.9	-2.5	
Contribution from real exchange rate depreciation	1.4	0.2	1.5			-3.1	-0.5	0.0	0.1	0.6	0.1		...	...	
Other identified debt-creating flows	0.0	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)	0.0	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	-1.0	-0.5	1.7			1.6	2.7	3.1	1.3	2.9	2.0		2.5	2.9	
Other Sustainability Indicators															
PV of public sector debt	...	...	26.4			25.6	27.5	30.0	30.4	32.7	34.3		34.6	32.6	
o/w foreign-currency denominated	...	...	13.0			13.1	16.3	19.9	21.9	23.4	24.3		23.0	19.7	
o/w external	...	...	13.0			13.1	16.3	19.9	21.9	23.4	24.3		23.0	19.7	
PV of contingent liabilities (not included in public sector debt)	...	...	...			...	...	...	...	...	...		...	...	
Gross financing need 2/	9.3	11.4	16.0			12.2	10.5	9.5	8.9	9.2	10.2		9.4	8.8	
PV of public sector debt-to-revenue and grants ratio (in percent)	…	…	169.0			172.4	180.3	202.6	205.2	218.7	226.5		193.8	166.5	
PV of public sector debt-to-revenue ratio (in percent)	…	…	197.9			208.3	211.0	225.5	223.3	235.8	243.5		201.3	170.2	
o/w external 3/	…	…	97.2			106.4	125.0	149.7	160.7	168.7	172.4		134.1	102.9	
Debt service-to-revenue and grants ratio (in percent) 4/	24.8	28.9	43.1			43.1	40.6	35.9	28.9	29.3	30.8		27.8	28.0	
Debt service-to-revenue ratio (in percent) 4/	29.9	35.3	50.4			52.0	47.5	39.9	31.5	31.6	33.1		28.9	28.7	
Primary deficit that stabilizes the debt-to-GDP ratio	1.4	1.2	-2.3			4.2	-1.1	-1.8	0.8	-1.3	0.1		0.4	-0.8	
Key macroeconomic and fiscal assumptions															
Real GDP growth (in percent)	7.2	5.9	6.7	6.9	2.5	4.2	5.4	6.0	7.0	7.0	7.0	6.1	7.0	7.0	7.0
Average nominal interest rate on forex debt (in percent)	1.4	1.4	1.6	1.1	0.4	1.3	1.7	1.9	1.8	1.9	1.9	1.8	1.9	2.8	2.2
Average real interest rate on domestic debt (in percent)	-2.4	3.1	5.6	4.4	4.9	-10.4	5.2	6.0	4.8	6.1	6.9	3.1	5.9	5.1	5.8
Real exchange rate depreciation (in percent, + indicates depreciation)	12.3	1.4	10.2	0.2	10.8	-16.5	...	...	...	...	...	...	...	...	...
Inflation rate (GDP deflator, in percent)	14.6	9.6	4.9	6.8	5.0	22.5	5.3	4.1	6.3	6.2	6.0	8.4	6.9	6.9	6.5
Growth of real primary spending (deflated by GDP deflator, in percent)	0.0	0.2	0.3	0.1	0.1	-0.1	0.0	0.0	0.1	0.1	0.1	0.0	0.1	0.1	0.1
Grant element of new external borrowing (in percent)	...	...	...	…	…	36.9	29.0	30.7	33.0	38.0	38.0	34.3	27.0	5.8	...

Sources: Country authorities; and staff estimates and projections.

1/ Public sector includes general government only and gross debt is used for all presentations.

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.

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Table 1b. Uganda: External Debt Sustainability Framework, Baseline Scenario, 2009-2032 1/
(In percent of GDP, unless otherwise indicated)

	Actual			Historical Average 6/	Standard Deviation 6/	Projections									
	2009	2010	2011			2012	2013	2014	2015	2016	2017	2012-2017 Average	2022	2032	2018-2032 Average
External debt (nominal) 1/	**21.2**	**23.0**	**27.5**			**26.7**	**30.6**	**35.3**	**37.8**	**40.3**	**41.7**		**39.6**	**31.5**	
o/w public and publicly guaranteed (PPG)	13.8	15.3	19.5			19.7	24.0	29.1	31.8	34.3	35.6		33.2	24.4	
Change in external debt	3.1	1.9	4.5			-0.8	3.9	4.8	2.5	2.5	1.4		-0.4	-0.8	
Identified net debt-creating flows	2.9	3.0	7.6			7.0	3.9	4.6	3.2	2.0	0.0		-2.8	0.9	
Non-interest current account deficit	**7.8**	**9.0**	**10.7**	**4.0**	**3.9**	**12.1**	**10.3**	**11.5**	**10.3**	**9.0**	**8.0**		**4.3**	**6.9**	5.3
Deficit in balance of goods and services	14.5	13.0	18.2			16.9	15.6	15.8	14.3	13.1	11.9		8.7	10.6	
Exports	19.6	20.4	22.1			20.4	20.9	21.2	21.1	20.9	21.7		23.2	30.0	
Imports	34.1	33.4	40.3			37.3	36.5	37.0	35.4	34.0	33.7		31.9	40.6	
Net current transfers (negative = inflow)	-7.6	-5.3	-9.0	-9.8	2.3	-6.0	-6.3	-5.2	-4.8	-4.8	-4.7		-3.7	-2.8	-3.4
o/w official	-1.7	-1.3	-4.0			-2.0	-2.4	-0.8	-0.6	-0.6	-0.6		-0.8	-0.4	
Other current account flows (negative = net inflow)	1.0	1.3	1.6			1.2	1.0	0.9	0.8	0.7	0.8		-0.7	-0.8	
Net FDI (negative = inflow)	**-4.2**	**-4.8**	**-4.0**	**-4.0**	**1.2**	**-4.5**	**-5.5**	**-5.7**	**-5.4**	**-5.2**	**-6.1**		**-5.3**	**-4.8**	-5.1
Endogenous debt dynamics 2/	**-0.7**	**-1.1**	**0.9**			**-0.6**	**-0.9**	**-1.2**	**-1.7**	**-1.8**	**-1.9**		**-1.8**	**-1.3**	
Contribution from nominal interest rate	0.8	0.6	0.4			0.3	0.4	0.6	0.6	0.7	0.7		0.7	0.8	
Contribution from real GDP growth	-1.2	-1.1	-1.6			-1.0	-1.3	-1.7	-2.3	-2.5	-2.6		-2.5	-2.0	
Contribution from price and exchange rate changes	-0.4	-0.6	2.1			…	…	…	…	…	…		…	…	
Residual (3-4) 3/	**0.2**	**-1.2**	**-3.2**			**-7.8**	**0.0**	**0.1**	**-0.7**	**0.5**	**1.4**		**2.4**	**-1.7**	
o/w exceptional financing	0.1	0.1	0.0			0.1	0.1	0.0	0.0	0.0	0.0		0.0	0.0	
PV of external debt 4/	...	...	21.0			20.1	22.9	26.2	27.9	29.5	30.4		29.5	26.8	
In percent of exports	...	...	94.7			98.5	109.4	123.4	131.9	140.8	139.9		126.9	89.3	
PV of PPG external debt	**...**	**...**	**13.0**			**13.1**	**16.3**	**19.9**	**21.9**	**23.4**	**24.3**		**23.0**	**19.7**	
In percent of exports	**...**	**...**	**58.6**			**64.1**	**78.1**	**93.9**	**103.6**	**112.0**	**111.8**		**99.3**	**65.7**	
In percent of government revenues	**...**	**...**	**97.2**			**106.4**	**125.0**	**149.7**	**160.7**	**168.7**	**172.4**		**134.1**	**102.9**	
Debt service-to-exports ratio (in percent)	**7.9**	**7.4**	**4.6**			**4.0**	**4.4**	**5.1**	**5.3**	**6.6**	**6.7**		**5.3**	**6.2**	
PPG debt service-to-exports ratio (in percent)	**2.9**	**2.7**	**2.7**			**1.9**	**2.4**	**3.1**	**3.4**	**3.5**	**3.5**		**3.2**	**4.2**	
PPG debt service-to-revenue ratio (in percent)	**4.5**	**4.5**	**4.6**			**3.2**	**3.9**	**4.9**	**5.3**	**5.3**	**5.3**		**4.3**	**6.6**	
Total gross financing need (Billions of U.S. dollars)	0.8	1.0	1.3			1.6	1.2	1.6	1.5	1.4	1.0		0.1	5.6	
Non-interest current account deficit that stabilizes debt ratio	4.7	7.1	6.3			12.9	6.4	6.8	7.8	6.5	6.5		4.7	7.7	
Key macroeconomic assumptions															
Real GDP growth (in percent)	7.2	5.9	6.7	6.9	2.5	4.2	5.4	6.0	7.0	7.0	7.0	6.1	7.0	7.0	7.0
GDP deflator in US dollar terms (change in percent)	2.0	2.8	-8.4	4.2	9.6	10.8	3.7	1.4	2.1	0.7	1.4	3.3	3.8	3.8	3.8
Effective interest rate (percent) 5/	5.1	3.2	1.6	2.6	1.2	1.5	1.7	2.0	1.8	1.9	2.0	1.8	2.0	2.7	2.2
Growth of exports of G&S (US dollar terms, in percent)	-2.7	13.3	5.9	19.7	18.3	6.2	12.0	9.2	8.8	6.7	12.7	9.3	13.4	14.4	13.4
Growth of imports of G&S (US dollar terms, in percent)	16.3	6.6	17.9	17.6	10.6	6.7	7.0	9.1	4.4	3.5	7.5	6.4	11.5	14.7	12.4
Grant element of new public sector borrowing (in percent)	...	...	...	...	...	36.9	29.0	30.7	33.0	38.0	38.0	34.3	27.0	5.8	20.8
Government revenues (excluding grants, in percent of GDP)	12.5	12.2	13.3			12.3	13.0	13.3	13.6	13.9	14.1		17.2	19.2	17.7
Aid flows (in Billions of US dollars) 7/	0.8	0.9	0.7			1.1	1.3	1.4	1.2	1.2	1.2		1.1	1.2	
o/w Grants	0.4	0.5	0.4			0.5	0.5	0.3	0.3	0.3	0.3		0.3	0.6	
o/w Concessional loans	0.4	0.5	0.3			0.6	0.8	1.0	0.9	0.9	0.9		0.8	0.7	
Grant-equivalent financing (in percent of GDP) 8/	...	...	...			4.2	4.1	3.7	3.0	2.8	2.7		1.5	0.6	1.3
Grant-equivalent financing (in percent of external financing) 8/	...	...	...			60.2	47.4	42.9	45.4	49.9	50.4		40.3	20.6	35.3
Memorandum items:															
Nominal GDP (Billions of US dollars)	15.8	17.2	16.8			19.4	21.2	22.8	24.9	26.8	29.1		49.1	139.7	
Nominal dollar GDP growth	9.4	8.8	-2.3			15.4	9.2	7.5	9.2	7.8	8.5	9.6	11.0	11.0	11.0
PV of PPG external debt (in Billions of US dollars)			1.9			2.5	3.4	4.5	5.4	6.1	6.9		11.1	27.2	
(PVt-PVt-1)/GDPt-1 (in percent)						3.2	4.8	5.1	3.8	3.1	2.9	3.8	2.5	1.7	2.1
Gross workers' remittances (Billions of US dollars)	0.9	0.7	0.8			0.8	0.8	1.0	1.0	1.1	1.2		2.0	5.1	
PV of PPG external debt (in percent of GDP + remittances)	...	...	12.3			12.6	15.7	19.1	21.0	22.5	23.3		22.2	19.0	
PV of PPG external debt (in percent of exports + remittances)	...	...	47.9			53.7	65.8	78.0	86.5	93.2	93.8		84.7	58.7	
Debt service of PPG external debt (in percent of exports + remittances)	...	...	2.2			1.6	2.1	2.6	2.9	2.9	2.9		2.7	3.7	

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).

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Table 2a.Uganda: Sensitivity Analysis for Key Indicators of Public and Publicly Guaranteed External Debt, 2012-2032
(In percent)

	Projections							
	2012	2013	2014	2015	2016	2017	**2022**	2032
				PV of debt-to GDP ratio				
Baseline	13	16	20	22	23	24	**23**	20
A. Alternative Scenarios								
A1. Key variables at their historical averages in 2012-2032 1/	13	12	11	9	8	8	**13**	13
A2. New public sector loans on less favorable terms in 2012-2032 2	13	18	24	27	30	32	**33**	31
A3. Oil sector development starting from FY2013/14	13	17	23	26	28	28	**20**	10
B. Bound Tests								
B1. Real GDP growth at historical average minus one standard deviation in 2013-2014	13	16	20	22	23	24	**23**	20
B2. Export value growth at historical average minus one standard deviation in 2013-2014 3/	13	18	24	26	27	27	**25**	20
B3. US dollar GDP deflator at historical average minus one standard deviation in 2013-2014	13	18	23	25	27	28	**27**	23
B4. Net non-debt creating flows at historical average minus one standard deviation in 2013-2014 4/	13	17	21	23	24	25	**24**	20
B5. Combination of B1-B4 using one-half standard deviation shocks	13	17	21	23	24	25	**24**	21
B6. One-time 30 percent nominal depreciation relative to the baseline in 2013 5/	13	23	28	30	32	33	**32**	27
				PV of debt-to-exports ratio				
Baseline	64	78	94	104	112	112	**99**	66
A. Alternative Scenarios								
A1. Key variables at their historical averages in 2012-2032 1/	64	57	51	42	36	35	**58**	42
A2. New public sector loans on less favorable terms in 2012-2032 2	64	85	112	129	145	148	**142**	103
A3. Oil sector development starting from FY2013/14	62	83	106	125	130	122	**66**	30
B. Bound Tests								
B1. Real GDP growth at historical average minus one standard deviation in 2013-2014	64	77	93	102	109	109	**98**	65
B2. Export value growth at historical average minus one standard deviation in 2013-2014 3/	64	93	134	144	152	150	**129**	80
B3. US dollar GDP deflator at historical average minus one standard deviation in 2013-2014	64	77	93	102	109	109	**98**	65
B4. Net non-debt creating flows at historical average minus one standard deviation in 2013-2014 4/	64	83	101	109	117	116	**102**	66
B5. Combination of B1-B4 using one-half standard deviation shocks	64	80	93	102	109	109	**98**	65
B6. One-time 30 percent nominal depreciation relative to the baseline in 2013 5/	64	77	93	102	109	109	**98**	65
				PV of debt-to-revenue ratio				
Baseline	106	125	150	161	169	172	**134**	103
A. Alternative Scenarios								
A1. Key variables at their historical averages in 2012-2032 1/	106	92	81	66	55	54	**78**	65
A2. New public sector loans on less favorable terms in 2012-2032 2	106	136	179	201	218	229	**192**	161
A3. Oil sector development starting from FY2013/14	103	133	170	194	201	200	**117**	52
B. Bound Tests								
B1. Real GDP growth at historical average minus one standard deviation in 2013-2014	106	124	152	162	169	173	**135**	104
B2. Export value growth at historical average minus one standard deviation in 2013-2014 3/	106	135	180	188	193	195	**147**	105
B3. US dollar GDP deflator at historical average minus one standard deviation in 2013-2014	106	135	174	186	194	198	**155**	119
B4. Net non-debt creating flows at historical average minus one standard deviation in 2013-2014 4/	106	132	160	170	176	179	**138**	103
B5. Combination of B1-B4 using one-half standard deviation shocks	106	131	158	169	176	180	**141**	108
B6. One-time 30 percent nominal depreciation relative to the baseline in 2013 5/	106	173	208	223	232	237	**186**	142

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Table 2a. Uganda: Sensitivity Analysis for Key Indicators of Public and Publicly Guaranteed External Debt, 2012-2032 (continued)

(In percent)

Debt service-to-exports ratio

Baseline	2	2	3	3	3	3	**3**	4
A. Alternative Scenarios								
A1. Key variables at their historical averages in 2012-2032 1/	2	2	2	2	2	1	**2**	3
A2. New public sector loans on less favorable terms in 2012-2032 2	2	2	3	4	5	5	**6**	6
A3. Oil sector development starting from FY2013/14	2	2	3	4	4	4	**2**	2
B. Bound Tests								
B1. Real GDP growth at historical average minus one standard deviation in 2013-2014	2	2	3	3	3	3	**3**	4
B2. Export value growth at historical average minus one standard deviation in 2013-2014 3/	2	3	4	5	5	5	**4**	5
B3. US dollar GDP deflator at historical average minus one standard deviation in 2013-2014	2	2	3	3	3	3	**3**	4
B4. Net non-debt creating flows at historical average minus one standard deviation in 2013-2014 4/	2	2	3	4	4	4	**3**	4
B5. Combination of B1-B4 using one-half standard deviation shocks	2	2	3	3	3	3	**3**	4
B6. One-time 30 percent nominal depreciation relative to the baseline in 2013 5/	2	2	3	3	3	3	**3**	4

Debt service-to-revenue ratio

Baseline	3	4	5	5	5	5	**4**	7
A. Alternative Scenarios								
A1. Key variables at their historical averages in 2012-2032 1/	3	4	4	3	2	2	**2**	5
A2. New public sector loans on less favorable terms in 2012-2032 2	3	4	4	6	7	8	**8**	9
A3. Oil sector development starting from FY2013/14	3	4	5	6	6	6	**4**	4
B. Bound Tests								
B1. Real GDP growth at historical average minus one standard deviation in 2013-2014	3	4	5	5	5	5	**4**	7
B2. Export value growth at historical average minus one standard deviation in 2013-2014 3/	3	4	5	6	6	6	**5**	7
B3. US dollar GDP deflator at historical average minus one standard deviation in 2013-2014	3	4	6	6	6	6	**5**	8
B4. Net non-debt creating flows at historical average minus one standard deviation in 2013-2014 4/	3	4	5	6	6	6	**4**	7
B5. Combination of B1-B4 using one-half standard deviation shocks	3	4	5	6	6	6	**5**	7
B6. One-time 30 percent nominal depreciation relative to the baseline in 2013 5/	3	5	7	8	7	8	**6**	9
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.

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Table 2b. Uganda: Sensitivity Analysis for Key Indicators of Public Debt 2012-2032

	Projections							
	2012	2013	2014	2015	2016	2017	2022	2032
PV of Debt-to-GDP Ratio								
Baseline	26	28	30	30	33	34	35	33
A. Alternative scenarios								
A1. Real GDP growth and primary balance are at historical averages	26	26	28	28	29	30	33	52
A2. Primary balance is unchanged from 2012	26	29	33	35	38	41	51	79
A3. Permanently lower GDP growth 1/	26	28	31	31	34	36	41	52
B. Bound tests								
B1. Real GDP growth is at historical average minus one standard deviations in 2013-2014	26	28	31	32	35	37	39	39
B2. Primary balance is at historical average minus one standard deviations in 2013-2014	26	29	33	33	36	37	37	34
B3. Combination of B1-B2 using one half standard deviation shocks	26	28	31	31	34	35	35	33
B4. One-time 30 percent real depreciation in 2013	26	32	34	34	36	37	37	38
B5. 10 percent of GDP increase in other debt-creating flows in 2013	26	38	40	40	42	43	41	36
PV of Debt-to-Revenue Ratio 2/								
Baseline	172	180	203	205	219	226	194	167
A. Alternative scenarios								
A1. Real GDP growth and primary balance are at historical averages	172	174	188	187	197	199	186	264
A2. Primary balance is unchanged from 2012	172	191	222	234	257	271	286	402
A3. Permanently lower GDP growth 1/	172	182	206	211	228	239	227	263
B. Bound tests								
B1. Real GDP growth is at historical average minus one standard deviations in 2013-2014	172	183	211	216	232	242	216	199
B2. Primary balance is at historical average minus one standard deviations in 2013-2014	172	192	224	226	238	245	205	172
B3. Combination of B1-B2 using one half standard deviation shocks	172	183	208	211	224	232	198	170
B4. One-time 30 percent real depreciation in 2013	172	210	227	226	238	245	207	192
B5. 10 percent of GDP increase in other debt-creating flows in 2013	172	249	271	271	282	287	231	185
Debt Service-to-Revenue Ratio 2/								
Baseline	43	41	36	29	29	31	28	28
A. Alternative scenarios								
A1. Real GDP growth and primary balance are at historical averages	43	40	35	28	28	30	27	32
A2. Primary balance is unchanged from 2012	43	41	36	30	31	32	32	42
A3. Permanently lower GDP growth 1/	43	41	36	29	30	32	30	35
B. Bound tests								
B1. Real GDP growth is at historical average minus one standard deviations in 2013-2014	43	41	37	30	30	32	29	31
B2. Primary balance is at historical average minus one standard deviations in 2013-2014	43	41	36	30	30	32	29	29
B3. Combination of B1-B2 using one half standard deviation shocks	43	41	36	29	30	31	28	28
B4. One-time 30 percent real depreciation in 2013	43	41	38	31	32	33	30	33
B5. 10 percent of GDP increase in other debt-creating flows in 2013	43	41	39	32	32	33	32	30

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.

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INTERNATIONAL MONETARY FUND

EXTERNAL RELATIONS DEPARTMENT

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IMF Executive Board Completes Fourth Review Under the Policy Support Instrument for Uganda

The Executive Board of the International Monetary Fund (IMF) has completed the fourth review under a three-year Policy Support Instrument (PSI) for Uganda. The Executive Board's decision was taken on a lapse of time basis and enters into effect today[1]. The PSI for Uganda was approved by the IMF's Executive Board on May 12, 2010 (see Press Release No. 10/195). The IMF's framework for PSIs is designed for low-income countries that may not need IMF financial assistance, but still seek close cooperation with the IMF in preparation and endorsement of their policy frameworks. PSI-supported programs are based on country-owned poverty reduction strategies adopted in a participatory process involving civil society and development partners.

The PSI-supported program with Uganda remains on track. All end-December 2011 quantitative assessment criteria were met, as were most of the structural benchmarks.

The stance of macroeconomic policy remains appropriate. Monetary tightening, initiated in July 2011 in response to rising inflation, has been effective in reducing demand and price pressures in the economy. High interest rates supported by tighter fiscal policy have strengthened the currency and raised reserve levels, while private sector credit growth and overall demand pressures are now much reduced. Prices have been generally stable for the last few months and annual inflation is coming down. The disinflationary effort has had limited effect on financial sector stability. Nonetheless, the tighter policies combined with weaker global demand are projected to reduce economic growth this year.

Looking forward, economic growth should recover significantly next year, as the expected decline in inflation will allow a phased and gradual relaxation of the monetary policy stance and a recovery of credit growth. The FY2012/13 budget aims at further moderate fiscal consolidation while increasing spending on infrastructure and other development priorities. In addition, tax policy measures will be introduced and a comprehensive reform of tax

[1] The Executive Board takes decisions under its lapse of time procedures when it is agreed by the Board that a proposal can be considered without convening formal discussions.

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exemptions linked to a new tax procedure code carried out, both aimed at improving revenue and budget performance over the medium term. While external borrowing for development is expected to increase in the years ahead, debt sustainability analysis carried out jointly by the IMF and the World Bank establishes that Uganda continues to face a low risk of debt distress.

Key risks to the outlook arise mainly from external factors. Slower than expected global growth would worsen the trade deficit and possibly reduce remittances and capital flows. Higher energy prices would dampen growth, as would deterioration in the regional security environment. However, absent these risks materializing, economic growth is expected to continue to improve, reaching 6 percent by 2013/14, and achieving its estimated potential of about 7 percent by 2014/15.

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