Statment by Mr. Willie Nakunyada and Mr. Mawek Tesfaye Mengistu on Uganda
Executive Board Meeting on September 6, 2024

Introduction

1. Our Ugandan authorities appreciate the constructive engagement with staff and share the thrust of staff's assessment of economic developments and key policy priorities.

2. The Ugandan economy continues to experience robust growth benefitting from prudent macroeconomic policies that have delivered improved socio-economic conditions. Importantly, the Fund supported Extended Credit Facility (ECF) program, approved in June 2021, helped advance the authorities reforms articulated in the third National Development Plan (NDP III) and facilitated the post-pandemic recovery. Despite the challenging circumstances characterized by tight global financial conditions which triggered portfolio reversals, continuing geopolitical tensions and the associated rise in freight costs, decline in external financing, and adverse climate shocks, the authorities made notable reform progress. That said, the authorities regret the expiry of the ECF arrangement before the sixth and final reviews, against the backdrop of program implementation challenges compounded by external funding constraints, portfolio outflows, and high domestic interest costs. That said, they have remained in reform mode to effectively consolidate the progress made under the ECF arrangement and advance outstanding reforms.

3. The authorities reiterate their strong commitment to economic reforms under the fourth National Development Plan (NDP IV), which is prepared under the theme *"Sustainable Industrialization for Inclusive Growth, Employment, and Wealth Creation."* NDP IV builds on the experience gained from NDP III, which is ending this fiscal year, and is aligned with the Uganda Vision 2040. The authorities re-affirm their resolve to pursue prudent macroeconomic management to preserve stable macroeconomic conditions, build buffers, and advance structural reforms to achieve transformative, inclusive, and sustainable growth.

Recent Economic Developments and Outlook

4. Real GDP continues to register robust growth, with an estimated increase of 6.0 percent in Financial Year (FY) 2023/24, compared to 5.3 percent growth in FY2022/23. The broad-based and strong growth performance is underpinned by a 6.6 percent expansion in the service sector, while the industry and agriculture sectors grew by 5.8 percent, and 5.1 percent, respectively. The strong growth rebound also benefitted from firm domestic demand, low and stable inflation, investment in the oil sector, favorable weather, and effective wealth and job-creating initiatives including under the *'Parish Development Model (PDM)' and 'Emyooga fund'*. In the medium term, the strong growth momentum is expected to continue, with further impetus anticipated from the commencement of oil

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production in late 2025, favorable weather conditions, and low inflation. Consequently, stronger growth is projected for 2025/26 before gradual normalization to the pre-pandemic trend of 6-7 percent in the medium term. Nevertheless, the outlook remains subject to downside risks, from still weak external demand, supply chain disruptions, and climate shocks. That said, important upside risks may arise from greater-than-expected spillover effects of oil sector investments, accelerated structural reforms, and improved external conditions. Meanwhile, headline inflation has decelerated sharply, from a peak of 8.8 percent in FY2022/23 to 3.2 percent in FY2023/24, reflecting decreasing food prices, tight monetary conditions, and relative exchange rate stability.

5. The current account deficit is expected to improve from 8.4[1] percent of GDP in FY2023/24, to 7.1 percent of GDP in FY2024/25 and gradually stabilize around 4.0 percent of GDP in the medium-term. Commencement of oil production and fiscal consolidation efforts are expected to narrow the current account deficit. Presently, despite volatility in other financial flows, oil project related FDI inflows have remained robust supporting the financing of the current account deficit. However, reflecting higher external debt service payments and global financial conditions that have limited FX net purchases, international reserves declined to an import coverage of 2.8[2] months at the end of FY2023/24, down from 3.7 months at the end of FY2022/23.

Fiscal Policy and Debt Management

6. The authorities are determined to sustain fiscal consolidation efforts to preserve debt sustainability and create fiscal space for critical social and development spending. In the near term, an increase in interest payments on domestic debt is expected to drive up the overall fiscal deficit to 5.7 percent of GDP in FY2024/25, compared to 4.8 percent in FY2023/24. However, in the medium term, the overall fiscal deficit is projected to decline steadily to 1.3 percent of GDP by FY2028/29 as domestic revenue mobilization efforts begin to bear fruit reflecting the expected additional oil revenues alongside expenditure restraint. The authorities' fiscal consolidation efforts are centered on enhancing domestic revenue mobilization, rationalizing expenditures, and strengthening budgetary and cash management practices.

7. The authorities' Domestic Revenue Mobilization Strategy (DRMS) is expected to guide resource mobilization efforts geared to raise tax revenue by 0.5 percentage of GDP annually. The implementation of the DRMS was not fully completed due to the Covid-19 pandemic. Consequently, the authorities have extended the DRMS implementation period until 2027 and are undertaking its comprehensive review. They are committed to implementing tax policy measures aimed at widening the tax base, such as introduction of

[1] The preliminary actual data for FY2023/24 shows that the current account deficit stands at 8.4 percent of GDP.

[2] The latest preliminary actual data shows that international reserves covered 3.8 months of prospective imports for FY2022/23 and 3.0 months for FY2023/24.

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a VAT on provision of taxable goods/services by an employer to an employee, a gaming tax, and increasing excise duties on petrol and diesel. Simultaneously, they are focusing on strengthening tax administration through enhanced enforcement, bolstering the capacity of the Uganda Revenue Authority (URA), and leveraging technology. The authorities recognize the potential revenue gains from rationalizing untargeted tax expenditures-estimated somewhere between 1.5 percent to 4 percent of GDP. However, they emphasize that strategies to rationalize these tax expenditures should be based on empirical analysis alongside a strong communication strategy to garner public support for the tax reforms.

8. The authorities are committed to reprioritizing spending by curbing non-essential current expenditures and focusing on growth-enhancing development and social sector spending. They continue to prioritize critical social sectors such as education and health to advance progress on Sustainable Development Goals (SDGs). Accordingly, they have allocated significant resources in the FY2024/25 budget for the rehabilitation and construction of health infrastructure, the construction of new schools, and financing for the government-funded higher education loan scheme. They also plan to undertake a diagnostic analysis of under-execution in social spending and continue prioritizing targeted support to the vulnerable segments of the population including the elderly and disabled. Their social support remains instrumental in closing gender gaps. They will continue to provide senior citizen grants and, for better efficiency, have decided to unify the Youth Livelihood Program and the Uganda Women's Enterprise Program. That said, the authorities are committed to restraining non-essential current expenditures, including reducing spending on government officials' business travel abroad, as well as on training and consultancy fees.

9. Uganda's public debt remains sustainable, and the authorities are committed to preserve debt sustainability and strengthening their fiscal framework. They emphasize that borrowed resources should continue to be invested in critical infrastructure, such as transport, energy, and industrial park development with competitive returns. As such, debt financed investments have been supporting economic growth and alleviate future debt pressures. Nevertheless, to avoid risk of debt distress they are committed to keeping the public debt below 50 percent of GDP, while prioritizing concessional borrowing. Simultaneously, the authorities are working to improve budgetary and cash management practices including by adopting a new cash management framework, expanding the Treasury Single Account (TSA) to several extra-budgetary entities, and strengthening the monitoring of SOEs. These reforms will enhance public finance management, minimize the necessity for supplementary budgets, and thereby bolster fiscal and debt sustainability. Looking ahead, they have implemented a rules-based framework for managing oil revenues. Under this framework, a ceiling of 0.8 percent of the previous year's non-oil GDP will be allocated for budget purposes, with the remaining funds directed to the sovereign wealth fund, the Petroleum Revenue Investment Reserve (PRIR).

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Monetary and Exchange Rate Policies

10. While the monetary policy stance remains broadly restrictive, the BoU's Monetary Policy Committee reduced the Central Bank Rate (CBR) by 25 basis points to 10.0 percent in August 2024. This decision reflects the continued low and stable domestic inflation over the past twelve months, up to July 2024, with annual headline and core inflation averaging 3.2 percent and 3.0 percent, respectively, both below the medium-term target of 5.0 percent. Looking ahead, BoU expects inflation to remain below target but remains attentive to upside risks, including from stronger-than-expected domestic demand, energy price hikes, and adverse weather conditions. While remaining cautious, BoU stands ready to adjust its policy rate based on incoming economic data, with the overarching goal of keeping medium-term inflation around 5.0 percent. The authorities acknowledge that lending rates remain sticky while emphasizing the robustness of the monetary transmission mechanism, including the credit channel. Nevertheless, they are working to further strengthen monetary policy transmission by improving communication, deepening financial markets, and enhancing the credit information system. That said, the authorities' decision to securitize outstanding advances from the BoU and their commitment to limit borrowing within statutory limits alongside implementation of the recommendations from the 2021 safeguards assessment will reinforce the bank's balance sheet and help enhance its operational independence.

11. The authorities attach prominence to exchange rate flexibility as a shock absorber while recognizing the need to rebuild international reserves. They continue to support full exchange rate flexibility and will limit foreign exchange interventions to smoothen disorderly market conditions. As such, they welcome the recommendations from the IMF's Integrated Policy Framework (IPF) which align with their current practices. Additionally, they emphasize that the BoU's recent foreign exchange swap with two local banks has helped rebuild reserves, enhance market confidence, and incur lower costs compared to recent market access efforts by peer countries. Going forward, the authorities are committed to rebuilding international reserves to adequate levels, including through purchases from the local FX market when conditions permit, buying gold from the domestic miners in the local currency and processing it into monetary gold, and encouraging forex inflows through export promotion and tourism development.

Financial Sector Policies

12. The financial sector remains resilient, reflecting the implementation of macroprudential measures, risk-based supervision, and key recommendations from the 2012 Financial Sector Assessment Program (FSAP). The banking system is well-capitalized, with ample liquidity buffers and strong asset quality. The BoU continues to strengthen its regulatory and supervisory framework to maintain financial stability. In 2024, the BoU liquidated EFC Uganda Limited (a deposit-taking microfinance institution) and Mercantile Credit Bank Limited due to failure to meet capital requirements, poor governance, and insolvency.

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The BoU is also working to enhance its stress-testing capabilities, including by adopting a forex stress test model developed with Fund TA. They plan to address information gaps to cover a broader range of sectors, including non-financial corporations in forex stress testing. While emphasizing the limited risk from the sovereign-bank nexus—since most securities are held to maturity and are highly liquid—the authorities remain committed to further strengthening systemic risk surveillance and taking appropriate remedial actions.

13. Over the last decade the authorities have made significant strides in promoting financial inclusion guided by its first National Financial Inclusion Strategy (NFIS I), with access to formal financial services rising from 20 percent in 2011 to 68[3] percent in 2023. Building on this progress and aligning with the NDP IV, the authorities have launched their second National Financial Inclusion Strategy (NFIS II, 2023-2028). This strategy aims to promote access to affordable and high-quality financial services to reduce poverty and promote economic growth. NFIS II seeks to further enhance access by increasing physical access points in underserved areas and leveraging financial sector innovation. Additionally, the authorities aim to address gender gaps in financial inclusion by adopting gender-sensitive regulations, promoting inclusive gender finance, raising public awareness, and offering tailored financial training and services. Further, various government initiatives, including the full rollout of the *'Parish Development Model'* and its mobile application (*WENDI*), *Emyooga* funds, and the capitalization of the Uganda Development Bank, are expected to support wealth creation initiatives and enhance inclusive economic growth, as these initiatives particularly target underserved segments of the population.

Structural Reforms

14. The authorities place a high premium on structural reforms designed to foster private sector-led development to achieve accelerated and inclusive growth. As such, they remain committed to the key objectives of the fourth National Development Plan (NDP IV) aimed at: enhancing human capital, improving public infrastructure, strengthening good governance, creating a better business environment, and generating jobs to uplift living standards. Key sectors identified for achieving these goals include agro-industrialization, tourism development, mineral development, and science, technology, and innovation. Initiatives in agro-industrialization involve investing in research and genetic development, pest control, and agricultural mechanization. In tourism, the authorities' plans include upgrading infrastructure, enhancing marketing and service quality, and increasing trained personnel. In science and technology, and mineral development, the authorities aim to expand industrial parks, improve financial access, and fast-tracking quantification and market studies for all minerals. Concurrently, the authorities are working to strengthen regional and global trade integration to unlock Uganda's growth potential. They are addressing trade barriers through implementation of the African Continental Free Trade

[3] The latest FinScope survey indicated that overall financial inclusion in Uganda, including the informally served population, increased from 77 percent in 2018 to 81 percent in 2023.

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Agreement (AfCFTA)and making substantial investments in infrastructure, including roads, railways, and air transport.

15. The authorities place climate adaptation and mitigation measures high on their agenda to enhance climate resilience. They have set an ambitious target of reducing national greenhouse gas (GHG) emissions by 25 percent below business-as-usual levels in their updated Nationally Determined Contributions (NDC) targets. To achieve this, the authorities have formulated a National Adaptation Plan (NAP) aimed at strengthening adaptation planning, governance, and coordination; developing tools for adaptation; and securing finance. Their efforts include restoring degraded wetlands, planting a variety of tree species, and building climate-resilient infrastructure in transport, energy, and agriculture. Considering significant financing required to meet their NDC targets, the authorities are working with development partners to secure the necessary resources while promoting green financing domestically, including under their NFIS II initiatives. Drawing on the IMF's C-PIMA recommendations, the authorities are also collaborating with the World Bank on the Country Climate and Development Report, which is expected to help mobilize additional climate financing.

16. The authorities place a high premium on strengthening good governance and the anti-corruption frameworks as the bedrock for their national development plan. To this end, they are working to leverage the country's strong institutional and legal frameworks, supported by the National Anti-Corruption Strategy (2029-24), to tackle attendant vulnerabilities. Further, they plan to partner civil society and expand e-government services to address enforcement gaps. They also increased budgetary resources for courts to recruit additional judges and invest in court automation to reduce the backlog of cases. Furthermore, they reiterated their commitment to implementing the Extractive Industries Transparency Initiative (EITI) by disclosing contracts related to oil and gas production. Additionally, Uganda's exit from the FATF grey-list in February 2024 demonstrates the authorities' continued efforts to strengthen the AML/CFT framework, including by enhancing access to and accuracy of beneficial ownership information.

Conclusion

17. Despite the regrettable expiry of the ECF arrangement before the sixth and final review, the authorities reaffirm their resolve to sustained implementation of prudent macroeconomic policies to preserve economic stability to support strong and inclusive growth while building buffers to withstand future shocks. They are also determined to sustain fiscal consolidation efforts to keep public finances on a sustainable footing. Additionally, they will continue to appropriately calibrate monetary policy to entrench price stability and foster financial sector stability. They are also pressing ahead with structural reforms to strengthen governance practices, improve the business climate, and unleash the country's enormous growth potential. The authorities appreciate the Fund's

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advice and technical support and look forward to Executive Directors' support in concluding the 2024 Article IV consultation.

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