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REPORT AND RECOMMENDATION

OF THE

PRESIDENT OF THE

INTERNATIONAL DEVELOPMENT ASSOCIATION

TO THE

EXECUTIVE DIRECTORS

ON A

PROPOSED CREDIT OF SDR 50.9 MILLION

AND A

PROPOSED AFRICAN FACILITY CREDIT OF SDR 18.8 MILLION

TO THE

REPUBLIC OF UGANDA

FOR AN

ECONOMIC RECOVERY PROGRAM

August 19, 1987

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CURRENCY EQUIVALENTS

Currency Unit	=	Uganda Shilling (USh)
USh 1.00	=	US$0.06
US$1.00	=	USh 60
US$1.00	=	1.27802 SDR a/

ACRONYMS

APC	Agricultural Policy Committee
CIDA	Canadian International Development Agency
CMB	Cotton Marketing Board
DANIDA	Danish International Development Agency
EAC	East African Community
ICO	International Coffee Organization
LMB	Lint Marketing Board
NRA	National Resistance Army
ODA	Overseas Development Administration (UK)
OGL	Open General Licensing
PEC	Presidential Economic Council
PIE	Public Industrial Enterprise Secretariat
PFP	Policy Framework Paper
PMB	Produce Marketing Board
SAF	Special Adjustment Facility
SIDA	Swedish International Development Authority
UDC	Uganda Development Corporation

FISCAL YEAR

Government: July 1 - June 30

a/ As of June 30, 1987.

UGANDA

ECONOMIC RECOVERY CREDIT AND PROGRAM SUMMARY

Borrower: Government of Uganda

Amount: IDA: SDR 50.9 million (US$65 million equivalent)
African Facility: SDR 18.8 million (US$24 million)

Terms: Standard for IDA and the African Facility

Programme Description:

(a) Objectives. The proposed credits would support policies and measures under the Government's Economic Recovery Program. Some of the policy actions which have already been taken include: (i) a currency reform under which one new Uganda Shilling would be equivalent to 100 old Ugandan Shillings; (ii) a 77 percent devaluation; (iii) increases in producer prices including coffee robusta (182 percent), coffee arabica (158 percent), seed cotton (375 percent), green leaf tea (257 percent) and flure cured tobacco (280 percent); (iv) increase in prices of petroleum products thus establishing parity with neighbouring states and, (v) doubling of the civil service wage bill as of June 1, 1987. Future actions include those reforms agreed to in the context of the Policy Framework Paper (PFP) in the areas of fiscal management; where the restoration of financial discipline is called for; money and credit where a key objective is to reduce inflation; the exchange rate, where there is need to maintain a realistic exchange rate for the Uganda Shilling and trade policy where the main initiative will be the introduction of a limited Open General Licensing System under which import licenses and foreign exchange will be provided freely upon request. Overall, the thrust of the policy reforms over the next twelve to eighteen months will be towards stabilizing the economy and thus creating a policy environment conducive to rapid growth with an efficient use of resources.

(b) Benefits. The Recovery Programme aims at a growth rate of 5 percent per annum in the 1987-90 period. In its initial phase, the program is designed to reduce the rate of inflation significantly while referring to fiscal and external balances. The greater availability and increased efficiency in the allocation of imports will provide the main stimulus to industrial growth. In agriculture, the restoration of adequate price measures will provide the major stimulus for growth. On balance, the implementation of the Recovery Program can be expected to have a strong positive social impact and improve welfare levels in Uganda. The Government will have more resources to increase the provision of basic services, e.g. health, education and water supply.

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Risks: The Government is well positioned to implement the program. It enjoys broad based support; the security situation has improved and discipline is being restored in public administration. Moreover, there is broad consensus on the policy agenda on which the Government has embarked. This is fully supported by the Donor community as evidenced at the recent Consultative Group Meeting. Nevertheless, there are at least three risks which could debilitate the implementation of the program: (i) Government's implementation capacity; (ii) delays in supply response; and, (iii) the sustainability of the current relatively stable political situation. To offset these risks, an intensive supervision and monitoring schedule on the part of the Bank and the IMF will be maintained. On its own behalf, the Government has established a high powered Presidential Economic Council which will inter alia oversee the implementation of the Recovery Program.

Financing Plan:

	(US$ million)
IDA	65.0
SFA	40.0
TOTAL	105.0

Estimated Disbursements:

The Credits will be disbursed in two tranches. The first would amount to US$60.0 million consisting of US$30.7 million from IDA, US$13.3 million from the African Facility and US$16.0 million from Special Joint Financing (ODA, UK). The second tranche would be available following a review in 9 January, 1988.

Rate of Return: Not applicable.

REPORT AND RECOMMENDATION OF THE PRESIDENT OF THE INTERNATIONAL DEVELOPMENT ASSOCIATION TO THE EXECUTIVE DIRECTORS ON A PROPOSED CREDIT FOR AN ECONOMIC RECOVERY PROGRAM TO THE REPUBLIC OF UGANDA

1. I submit the following report and recommendation on a proposed Development Credit of SDR 50.9 million (US$65 million equivalent) and a proposed African Facility Credit of SDR 18.8 million (US$24 million equivalent) on standard IDA terms to the Republic of Uganda to support the Government's Economic Recovery Program.

PART I - THE ECONOMY

2. A report entitled Uganda: Progress Towards Recovery and Prospects for Development (Report No. 5595-UG) and dated June 5, 1985 has been distributed to the Executive Directors. A summary of social and economic data is given in Annex IV.

A. Background

3. At independence, in 1962, Uganda had one of the strongest and most promising economies in Sub-Saharan Africa. Despite the disadvantage of being a land-locked country, with favorable climatic and soil conditions, the agricultural sector was able to provide ample food to feed the population, as well as generate foreign exchange. Even though agricultural exports were dominated by coffee and cotton, rapid progress was being made on developing new export crops, such as tea and tobacco. The industrial sector, although small, supplied the economy with basic inputs and consumer goods, and contributed foreign exchange through exports of textiles and copper. Uganda's transport system was regarded as one of the best in Sub-Saharan Africa, and through common services with Kenya and Tanzania (later to be formalized in the East African Community), Uganda shared access to an effective network of railway, port and airline facilities. On the energy front, the country was blessed with an abundant potential for hydro-electric development, a potential which was already being harnessed. Although school enrollment was still low, the country had developed a reputation for the quality of its education at all levels.

4. The initial years after independence clearly demonstrated the economic potential of the country. Real Gross Domestic Product (GDP) grew by 5.8 percent per annum from 1963 to 1970, implying an increase in per capita terms of at least 2 percent per annum. The country also was able to maintain a reasonable savings rate, averaging 15 percent of GDP, and permitting the implementation of a respectable investment program without undue pressure on domestic prices or the balance of payments. Although Uganda's export volumes grew slowly, at about 3.5 percent per annum, export

earnings were more than adequate to cover import requirements and the country maintained a current account surplus in most years. The Government's budgetary position was also basically sound.

5. However, starting in 1970, a decade of political turmoil and gross economic mismanagement radically changed the situation. Many of the best trained personnel fled the country, the parastatal sector became bloated with the addition of many abandoned or confiscated industries, and professional standards within the administration were seriously eroded. On top of this, the Ugandan economy was shaken by a series of external shocks: the sharp rise in petroleum prices after 1973, and the breakup of the East African Community in 1977. As a result real GDP declined by about 20 percent during the 1972-1978 period. This era of extensive economic, social and political destruction culminated in a war in 1979 to overthrow the regime, entailing further destruction and economic decline.

B. Recent Economic Developments

6. The Ugandan economy proved to be resilient, however, and its capacity to rebound quickly from prolonged economic contraction was demonstrated in the years 1981-1984. During those years, economic growth accelerated in response to changes in economic policy, supported with considerable donor assistance, including assistance from the Association and the IMF. These changes included a major depreciation of the Ugandan shilling, the removal of most price controls, and significant real increases for the few that remained controlled, notably producer prices for export crops and petroleum prices. These measures stimulated agricultural production and export , so that real GDP grew at an average annual rate of 6 percent during the three-year period ending 1983/84. The rate of inflation declined sharply, from an annual rate of more than 100 percent in 1980 to 30 percent by early 1984. There was a significant turnaround in budgetary performance, with the overall budget deficit falling from 9 percent of GDP in 1981/82 to 3 percent in 1983/84. There was also an improvement in the external accounts. The trade and current accounts as well as the overall balance of payments swung into surplus, and by mid-1984 foreign exchange reserves had reached the equivalent of three months of imports.

7. The fragility of this recovery, however, was revealed during 1984. With increasing political and military opposition, and worsening corruption, military expenditures escalated and fiscal and monetary control weakened. Expenditure overruns were significant, leading to a rise in the budget deficit, and an acceleration of inflation. The exchange rate became significantly overvalued as the authorities intervened in the foreign exchange auction to slow the depreciation of the shilling. As a result of these developments, economic growth turned abruptly negative in 1984/85. The situation worsened further during 1985 as civil war led to a major disruption of productive activities and a severe shortage of foreign exchange. During 1985, real GDP at factor cost declined by an estimated 5.6 percent, with value added in agriculture falling by 8 percent, as the resurgence of inflation sharply reduced the producer prices in real terms.

8. At the end of the civil war in January 1986, the economy was, once again, in a critical condition. Much of the country had been devastated;

the Luwero triangle, once among the richest areas, was nothing more than a wasteland, with most of its inhabitants either dead or displaced, and all infrastructure destroyed. Countrywide, there was a major transport bottleneck; manufacturing plants were either closed or operating at very low rates of capacity; utilities such as power and water supply had severely deteriorated. Official foreign exchange reserves were only US$24 million, equivalent to about two weeks' "normal" imports of goods and services, and net foreign reserves were negative to the amount of US$254 million. The new Government also inherited a considerable external debt burden. Taking into account the debt to the IMF, the total debt service scheduled for 1986 was equivalent to one half of the 1984/85 export of goods and services. Moreover, at end-1985, the stock of external arrears on medium- and long-term debt amounted to US$63 million.

9. Since 1986, the Uganda Government has taken major steps to re-establish peace and security and rehabilitate the economy. The Government has introduced discipline both in the army and in the general administration of the country. Despite limited foreign aid, the Government's emergency relief and rehabilitation program has helped to revive economic activities in the devastated districts. As a result of these efforts, there was some recovery in real GDP in 1986, particularly during the last half of the year. There was a significant improvement in value added from the non-monetary agricultural sector, and some increase in cash crop production. Commercial activity also made some recovery, although transport services remain weak. Some trucks have been ordered and received, and some roads repaired, but on the whole, transport remains a critical bottleneck. Manufacturing output has been slow to recover, as the lack of foreign exchange sharply constricted supplies of spare parts and imported intermediate inputs. The shortage of foreign exchange has, in fact, constituted a major constraint to economic recovery, as the Government has had to use one half of its limited foreign exchange earnings to import fuels and basic essential commodities, and the other half to honor its repayment obligations.

10. Fiscal and monetary performance deteriorated in 1986. The budget for 1986/87 sought to accelerate the country's recovery effort by doubling budgetary outlays over those of the previous year. With a smaller increase in projected revenues, the budget provided for an increased deficit on a commitment basis, with most of its financing expected to come from the banking sector. In fact, the actual deficit was much larger than projected, due mainly to shortfalls in the major sources of revenue. This resulted from the mismatch between the producer price of coffee and the nominal exchange rate, in a process that severely penalized producers while dramatically reducing revenues from the export duty.

11. The Government significantly increased the producer price of coffee in May 1986. In real terms, the new price was 45.2 percent above the average for 1983/84, a peak year in terms of coffee deliveries to the marketing board. However, by April 1987, the same comparison yielded a drop in the real producer price to 58.2 percent below the 1983/84 average (see Figure 1). The real value of the unit export duty rate fell even more rapidly than real producer prices. Despite the acceleration in inflation the nominal exchange rate remained fixed, and during this period international coffee prices fell by about 29 percent (see Figure 2 and

FIGURE 1

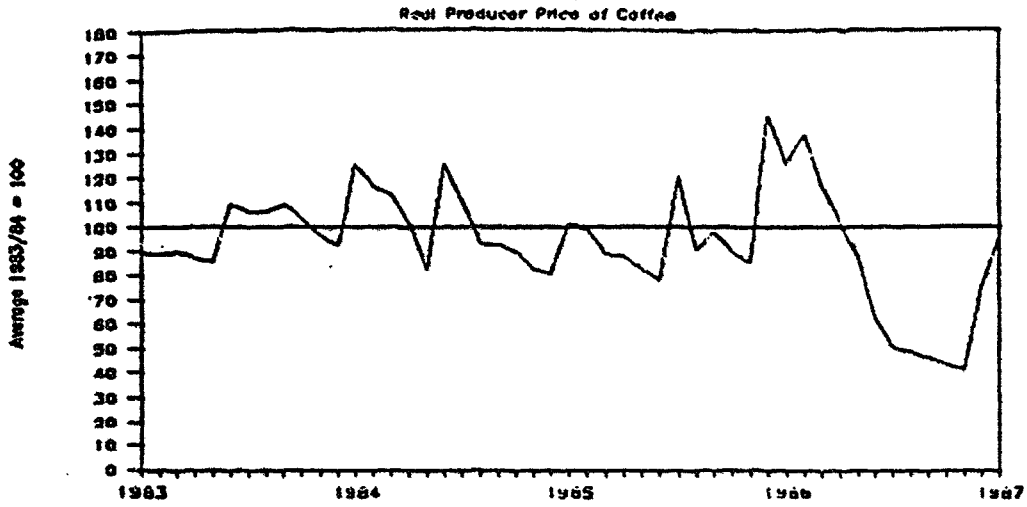


FIGURE 2

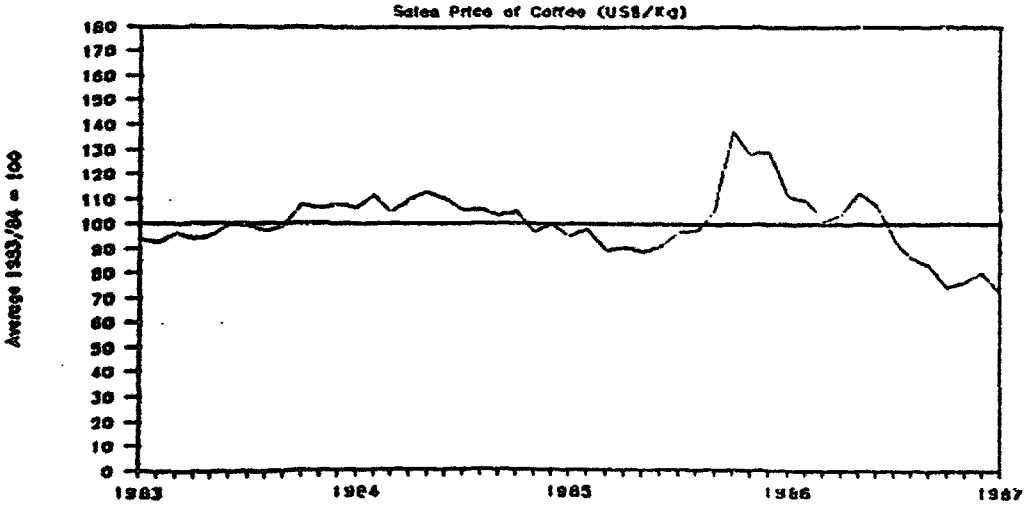


FIGURE 3

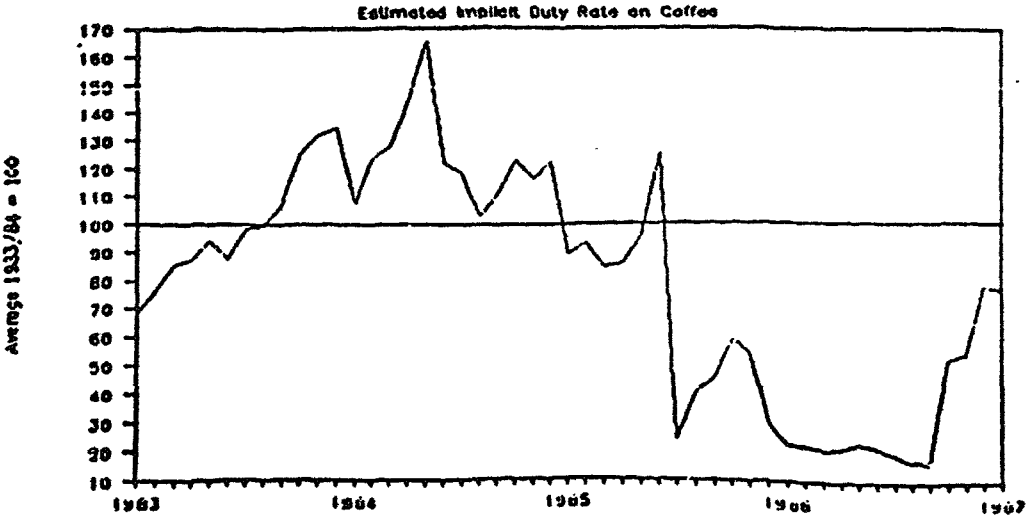


Figure 3 for the resulting value of unit export duty rate). Shrinking export volume compounded the loss in revenue. Altogether, the average real value of total export duties in fiscal year 1986/87 fell to about 20 percent of the value in 1985/86. Additional shortfalls resulted from depressed manufacturing output, which reduced sales tax and excise duty yields, and compressed import levels, which inhibited yields from import duties and sales tax on imports.

12. Despite a cut in average real expenditures to nearly two-thirds of their level in 1985/86, the budget deficit for fiscal year 1986/87 is estimated at 6.2 percent of GDP. To finance this deficit, the Government borrowed heavily from the banking system. In an economy where the total volume of credit barely reached 4.4 percent of GDP, the amount of credit outstanding to the Government at end-June 1987 measured 2.5 percent of GDP. Over the 1986/87 fiscal year, net domestic credit to the Government rose by around 230 percent. These developments, together with a rapid depreciation of the parallel market rate, led to an acceleration of inflation. At the close of the 1986/87 fiscal year, the average yearly rate of inflation approached 250 percent.

13. In 1986, the balance of payments situation also worsened. The shortage of transportation equipment severely hampered exports, particularly coffee, which accounts for about 95 percent of total export earnings. As a result, Uganda was unable to reap full benefit from the boom in coffee prices and from the suspension of the ICO country quotas in February 1986. During the year, imports increased by around 30 percent from the very low level in 1985. The Government gave high priority to the importation of those raw materials, spare parts, and transportation equipment urgently needed to restore productive capacity and facilitate the movement of goods. With the fall in international prices, the value of petroleum imports decreased. Meanwhile, imports of key consumer goods such as sugar and salt increased significantly. Despite this increase, however, the huge pent-up demand for imports could not be met, exerting considerable pressure on the parallel market. After a brief return to a dual exchange market between June and August 1986, with rates of USh1,400 and USh5,000 per US dollar, the exchange rate was unified at USh1,400 per US dollar. By early 1987, the parallel market rate for the Ugandan shilling exceeded eight times the official exchange rate.

14. The problems encountered by the Government on the economic policy front could be attributed partly to its inexperience, and partly to the difficulties involved in reaching a consensus at the political level. The present Government is broad-based, representing different power groups and economic philosophies. Initially, the views of those factions in the Government advocating stronger government controls, overvalued exchange rate, and high budgetary spending prevailed. However, the worsening economic condition throughout 1986 made it clear to the Government that a major reversal in economic policies was required. After extensive debate and study there is now a broad consensus on the direction of reform.

15. The policy agenda of the Government's Economic Recovery Program entails measures designed to restore stability in the economy, and policies to revitalize the economic recovery process and set the stage for sustained growth. The main components of this program were agreed upon with the

Government in the context of a Policy Framework Paper. The stabilization policies which are concerned with monetary and fiscal measures and with the net foreign assets position of the Bank of Uganda, are also being supported by the Fund's SAF program. As detailed in the following paragraphs, these macroeconomic measures, some of which have already been taken, will be reinforced by further measures in the productive sectors, public sector management and resource allocation. The policy reforms to be supported by the proposed credit are adjustments in agricultural producer prices, efficiency improvements in crop marketing, adjustment in the trade regime through the implementation of an open general licensing system for imports, public industrial enterprise restructuring, improved public resource management and allocation, and civil service reform. Actions outlined in this program constitute a major first step in a series of steps the Government will need to take to achieve sustained recovery and growth. Further IDA credits in support of the later stages of implementation are being planned.

PART II - THE GOVERNMENT'S ECONOMIC RECOVERY PROGRAM

16. The objectives of the Economic Recovery Program, which was formally launched on May 15, 1987, are to: (i) restore price stability and a sustainable balance of payments position; (ii) substantially improve capacity utilization in industrial and agro-processing units; (iii) rehabilitate existing infrastructure and installed capacity; (iv) restore producer incentives through appropriate price policies and the use of markets; (v) restore discipline, accountability and efficiency in the public sector; and (vi) improve public sector resource mobilization and allocation.

17. As an important first step towards these goals, the May 15th announcement included:

(a) a currency reform under which one new Uganda shilling would be equivalent to 100 old Uganda shillings;

(b) a 77 percent devaluation, in foreign currency terms, of the Uganda shilling from old USh1,400 to one US dollar, to new USh60 to one US dollar;

(c) a 30 percent currency conversion tax applicable to all cash holdings by the public; demand, savings and time deposits of households and business; all treasury bills and Government stocks held by the public; and commercial banks cash balances with the Central Bank;

(d) an increase of 182 percent in the producer prices for coffee-robusta, 158 percent for coffee-arabica, 375 percent for seed cotton (AR), 400 percent for seed cotton (BR), 280 percent for flue cured tobacco, 257 percent for fire cured tobacco, and 257 percent for green leaf tea;

(e) subsequent increases in producer prices of the five foodcrops targeted for export, ranging between 130 percent and 230 percent for beans, maize, simsim, groundnuts and soya beans;

(f) an immediate increase in the prices of petroleum products to establish appropriate parity with neighboring countries while providing net revenues to the Treasury;

(g) a doubling of the civil service wage bill effective June 1, 1987.

18. In addition to these specific actions, the President's announcement included measures that will be taken in the coming months: the setting up of an Open General Licensing (OGL) system for foreign exchange allocations and of a credit facility for local cover for imports, as well as the pursuance of fiscal and monetary policies consistent with the objective of stabilization. There would also be further actions in the productive sectors and in the area of public sector management.

19. The policies already announced by the Government have been designed to accomplish a rapid return to economic stability. The Government believes that the rate of inflation has to come down quickly to enable markets and prices to play their allocative role effectively. To sustain stability and achieve recovery, the policies aimed at restraining and controlling demand have to be supported by measures from the supply side. In the short run the Government expects an immediate supply response from improved producer price incentives in the agricultural sector, increased capacity utilization in industry, and larger numbers of road vehicles in transportation. Experience from the 1981-1984 period when the economy rebounded from prolonged contraction supports this expectation. To sustain the expected recovery, the rehabilitation of basic infrastructure in transportation and energy, as well as the restoration of productive capacity, is essential. In the longer-term, however, growth will be achieved through the implementation of policies aimed at improvements in efficiency and productivity, as well as increases in productive capacity.

A. Macroeconomic Policies

20. Macroeconomic policy concerns in Uganda are justifiably dominated by short-term problems of stabilization. Stabilization is a necessary first step towards the creation of a policy environment conducive to rapid growth with an efficient use of resources and a most equitable distribution of rewards. The Government's recent initiatives, and complementary policies to be pursued, aim at stabilizing the economy over the next 12 to 18 months. The plan restricts the expansion in broad money supply to control the growth in nominal aggregate demand. This is not, however, the only, or even the principal objective. The plan also restores the revenue base for public spending and in doing so it goes beyond a reduction in the public sector's borrowing requirements. The recovery in revenues is designed to finance a net repayment of outstanding debts to the banking system. It will therefore release resources for the expansion of non-government sectors without a parallel expansion in total credit. Revenues will increase following the substantial devaluation of the currency which produces two main outcomes. First, it results in an increase in the

"implicit" duty rate on coffee exports, the main source of public revenues. Second, with the price incentive given to producers, the devaluation leads to an increase in exports, hence in the tax base and in import capacity. Imports are the key ingredient for a short-run supply response. It is this increase in supply, partly financed by the growth in credit for non-government use, that forms the basis for a sustained, non-inflationary recovery in output.

Fiscal Policies

21. The restoration of financial discipline with price stability in Uganda depends crucially on fiscal performance. Not only must the fiscal deficit be reduced, but the financing of the deficit must also avoid recourse to monetary expansion in order to curb inflation. For the 1987/88 budget, the Government has agreed with the IMF, in the context of the SAF program, that the overall deficit of the Central Government on a commitment basis would be limited to 4.5 percent of GDP, compared with 6.2 percent of GDP in 1986/87. The deficit target will allow a 38 percent decrease in net bank credit to the Government. The SAF arrangement establishes quarterly benchmarks for the reduction in net Government credit. With this, the Government's share of total domestic credit will fall from 56 percent at end-June 1987 to a projected 31 percent at end-June 1988.

22. The planned deficit reduction will be achieved primarily through an expansion in tax revenues. During 1987/88 most of the increase will result from a sharp rise in coffee export duties, reflecting the large depreciation in the exchange rate. Despite a real increase in the producer price of 130 percent between April and June, 1987, the average unit duty rate is expected to rise from 27 percent of export receipts in 1986/87 to 51 percent of export receipts in 1987/88. (It averaged 52 percent in the period 1982-1984). The real value of total duty revenues is projected to increase by a factor of 4.5 times the value in 1986/87. Supplementing this increase is an expected improvement in tax collection and administration designed to remedy the widespread noncompliance with most other taxes. From a drop to about 3.5 percent of GDP in fiscal year 1986/87, not including the currency conversion tax, Government tax revenues will recover to 8.2 percent of GDP in 1987/88 and, stabilize thereafter to approximately 9 percent of GDP. This trend reflects first the increased revenue from export and import duties and, later, the growth in proceeds from sales and income taxes. For 1987/88, the SAF arrangement establishes quarterly benchmarks for tax revenues with a cumulative total of USh16.8 billion by end-June 1988.

23. The Government is aware of the problems caused by the current overwhelming dependence of the budget on the coffee export tax (nearly 60 percent of total revenue and more than 65 percent of tax revenue). However, before introducing additional taxes, the Government plans to assess the impact of the new measures to revitalize the administration and collection of taxes prescribed by the existing laws. A study by the IMF in 1984 concluded that, from a revenue standpoint, Uganda had an adequate tax structure. The main weaknesses have been the breakdown in collection, the fiscal drag due to high and accelerating inflation, and the fall in real taxable domestic income. Also firms, mainly parastatals, have built up a large volume of tax arrears in recent years. While full repayment of the

arrears is unlikely, a shift towards prompt current payments would have a major impact on the level of inland revenues.

24. Contributing to the deficit reduction target will be a decline in the share of recurrent expenditure to GDP, from 7.3 percent in 1986/87 to 6.9 percent in 1987/88. This will occur because of the projected recovery in real GDP growth, as real government recurrent expenditures are expected to be maintained at present levels. The composition of government expenditure will change markedly, however. As noted earlier, the Government has announced a two-fold increase in the nominal wage bill. This will increase the share of wages in recurrent expenditures from about 9 percent in 1985/86 to an estimated 15 percent in 1987/88. On account of the devaluation, payments on interest will also increase -- to an estimated 20 percent of total recurrent expenditures. Meanwhile, the Government is committed to reducing defense expenditure in real terms in the 1987/88 budget. Expenditure on subsidies and transfers, specially to parastatals, will also be scrutinized for possible reductions. In the context of the SAF program the Government has agreed to quarterly benchmarks on total recurrent expenditure with a cumulative total of USh14.2 billion by end-June 1988.

25. Recurrent revenues including grants are expected to grow more rapidly than recurrent expenditures, reversing the trend of net negative savings by the public sector. In fiscal year 1987/88 the surplus of recurrent revenue over recurrent expenditures should approach 4 percent of GDP, before reaching 5 percent of GDP in 1988/89. Part of this surplus is to be used for the necessary repayment of Treasury's debt to the banking system. However, a significant share of it will go to defray the very substantial increases in governmental development outlays. Development expenditures are expected to increase to 8.3 percent of GDP in fiscal year 1987/88, up from 3.3 percent of GDP a year earlier. They are projected to expand to 8.7 percent of GDP by 1989/90, growing in real terms by 8 percent annually in the period following the substantial recovery in 1987/88. Disbursements from foreign borrowings will finance two-thirds of total development outlays, up from about one half in the previous fiscal year. To avoid unfinanced expenditures, development outlays will be monitored closely against disbursements of external credits and capital grants.

Monetary and Credit Policies

26. Reducing inflation while increasing output is a fundamental goal of short-run economic policy. Inflation is expected to decline from an average annual rate of 250 percent in 1986/87 to about 90 percent in 1987/88, and to less than 30 percent in 1988/89. Thus the immediate objective of monetary and credit policies is to control monetary expansion without undue restraint on credit to productive activities. This is to be accomplished by reducing in real terms the overall level of credit while shifting access to credit from the Government to private and parastatal enterprises. The magnitude of this shift is to be such that credit to the private and parastatal sectors will increase in real terms.

27. In fiscal year 1987/88, total domestic credit is projected to rise by 10 percent in nominal terms, to USh10.0 billion. This compares with a 163 percent nominal increase in 1986/87. At the same time, credit to the

private and parastatal sectors is projected to increase by 72 percent during 1987/88, equivalent to a real increase of 33 percent. During 1986/87, by comparison, real credit to the non-government sectors fell by 40 percent. The monetary and credit policies will supplement the initial effects of the May 1987 currency conversion tax, which reduced most nominal money balances by 30 percent. Half of the proceeds from the tax were used to retire public debt, while the remaining half have been placed in a Special Development Fund. Disbursements from this Fund will be slow, at least initially. Therefore, revenues from the tax will be effectively sterilized while the lending capacity of commercial banks is reduced.

28. The Government is committed to contain the nominal expansion in broad money to about 40 percent in 1987/88. This expansion is consistent with the planned reduction in inflation and with the target for nominal GDP growth. The reduction in liquidity will be sharper in the initial months of the program but will be sustained by the shift in budgetary financing away from direct borrowing from the Bank of Uganda. To monitor monetary developments during 1987/88, quarterly benchmarks on the cumulative change in net domestic credit and in net bank credit to the Government have been established under the SAF program. The Government has requested and the IMF agreed to have a mid-year review of performance under the first year SAF arrangement. Following this review, corrective actions will be agreed upon.

29. Devaluation and concurrent increases in domestic petroleum prices will exert some upward pressure on prices. While it is difficult to predict to what extent the reduction in primary liquidity will counteract the inflationary pressures created by devaluation, there are additional reasons for expecting a significant fall in inflation. In the recent past, except for the price of petroleum products, prices of other imported goods were effectively set at the parallel market rate of exchange. For obvious reasons, this rate was significantly higher than the official rate -- in fact considerably higher than the new devalued official rate. The parallel rate has already begun to converge towards the new official rate, appreciating by nearly 40 percent between May 15 and June 15, 1987. This, together with the expected greater availability of goods through official channels, and an increased efficiency in the allocation of imports brought about by changes in the trade regime, to be discussed in para. 33 and 34, should lead to import price stability. It could even lead to a fall in the domestic price of some imported goods. On balance, therefore, there are strong reasons to expect a significant reduction in the rate of inflation.

30. The current level of commercial interest rates yields negative real returns. This discourages time deposits and shifts the structure of loans towards short-term, practically risk-free instruments. It is the Government's intention to move quickly to positive, market determined, real interest rates and to maintain positive real rates over the medium term. As a first step in this direction, a secondary financial market for treasury bills will be established by end-1987. However, in nominal terms current interest rates are high (for example, 35 percent for 12-months deposits). With the anticipated fall in inflation, it is expected that current nominal rates will yield positive returns for deposits of equal maturity beginning by end-1987. Therefore, considering the rapid pass-through of increases in the cost of credit to prices, the Government has

decided to maintain the current level and structure of rates until the end of 1987. It was agreed, under the SAF program, that interest rates would be reviewed by end-1987 and, if necessary, adjusted in the light of expected inflationary trends.

Exchange Rate and Trade Policies.

31. Establishing and maintaining a realistic exchange rate for the Uganda shilling has been given high priority in the Government's Economic Recovery Program. The real effective exchange rate had appreciated by 133 percent between the second quarter of 1984, when the foreign exchange auction was operating without interference, and the first quarter of 1987. After considering various options, the Government decided to maintain a fixed exchange rate, albeit at a more realistic level, to be reviewed and revised periodically. This exchange rate system is to be anchored on appropriate monetary policies with strict fiscal discipline. Experience under the previous auction system, and similar auctions in other African countries, indicated the risks in introducing such a system before the initial stabilization of the economy. Uganda presently faces both very high levels of demand for consumer and intermediate goods, including the demand for stock replacement, and a short-run speculative demand for imports. This pressure on demand for imports should decrease with the substantial increase in relative import prices, the expected rise in foreign capital inflows, and the slowdown in monetary expansion. To improve efficiency in the allocation of foreign exchange, the Government is introducing an Open General Licensing (OGL) system, the details of which are given in paras. 33 and 34. Over time the system will expand to cover nearly all imports; its continued operation will then require a market clearing exchange rate.

32. The adjustment of the exchange rate, which constitutes the centerpiece of the recently announced stabilization measures, has led to a significant and immediate increase in government revenues, essential for achieving fiscal balance. It will also help restore price incentives for the production of tradeables and re-equilibrate the trade account. Based on the second quarter of 1984 parity, when the exchange rate was market determined, the new rate represents a real effective devaluation of 43 percent. Monetary policy will play a key role in maintaining the competitiveness of the exchange rate. Nevertheless, monetary discipline alone will not suffice, and the Government is committed to an active exchange rate policy to avoid future imbalances in the external sector and to maintain appropriate price incentives for tradeables. In the present inflationary context, the Government wanted to avoid the negative impact of frequent changes in the exchange rate on current inflation and on inflationary expectations. For this reason, aside from the impact on tax revenues, a major determinant of the extent of the initial devaluation was the sustainability of the nominal rate over the following months. If foreign exchange supplies increase as projected and the effects of the reduction in liquidity are as expected, in both intensity and timeliness. the present nominal exchange rate should remain competitive for the entire second half of 1987. However, the Government recognizes that a commitment to an active exchange rate policy must be based on continuous careful monitoring of the supply and demand for foreign exchange with prompt actions to correct emerging misalignments. A major review of exchange rate

developments will be undertaken during the mid-year review of the SAF program agreed upon with the IMF.

33. The Open General Licensing System. The Government is introducing a limited OGL system, under which import licenses and foreign exchange will be provided freely upon request. Currently, the very limited foreign exchange is entirely administratively allocated. The proposed OGL system, once fully effective, will help optimize the allocation of foreign exchange among eligible importers. From the start it will facilitate the recovery of production in essential industries. Given the critical scarcity of foreign exchange, the OGL system will be introduced in stages. Initially, it will operate alongside the current administrative allocations of foreign exchange and will cover only the import of intermediate inputs and spare parts demanded by the high-priority industries. The system is expected to be in place by no later than end-September 1987. Prior to the finalization of the system, the Government will consult with the Association on the size of the system and the details to be covered, the criteria for eligibility, and the processes through which eligible importers will have access to the system. Preliminary estimates indicate that, from its inception, the system will cover around 20 percent of merchandise imports and one-half of non-petroleum, non-aid related imports. The Government will conduct regular reviews of the system with the aim of enlarging it on a quarterly basis. A condition of the release of the second tranche of the credit is that, following a review of the system, a plan of action, satisfactory to the Association, has been adopted. By end-1988 the OGL system it will extend to all capital and intermediate goods, basic necessities, and selected incentive items. The implementation of this policy will be reviewed by the Association under the proposed credit, by the IMF under the SAF agreement.

34. The Government in consultation with the Association, has worked out the basic design of the OGL system. Initially, only the primary users of imports are eligible for participation, and the system would cover eligible imports for textiles, soap, beverages and tobacco industries. Aside from sectoral criteria, conditions for eligibility are minimal and objectively stated to avoid judgmental decisions concerning firm specific eligibility. Once the eligibility of the firm is established, no special permit required to import the listed product. Recognizing the importance of a sustained and unhampered operation of the system, the Government is prepared to support it through appropriate macroeconomic policies. These include the use of monetary and especially credit policy instruments to reduce aggregate, and import demand, and/or discrete devaluations of the exchange rate to curb imports while encouraging exports. In addition, the Government is prepared to reapportion the available foreign exchange not linked to project related aid disbursements from the administrative allocation system in favor of imports under OGL.

35. The Special Credit Facility. The Government has been concerned about the ability of industrial firms to raise sufficient local currency to purchase the foreign exchange needed to import priority inputs, particularly after the devaluation and the currency conversion tax. This has been perceived as a problem not for the 50 or so firms that are already clients of commercial banks, but for potential new clients. These would be firms that are economically viable, but for special circumstances may not

be able to meet the normal lending criteria of the commercial banks. These are smaller firms that once accounted for a substantial slice of total industrial output; firms that possess plant, machinery and equipment in reasonably good operating state, and firms that have competent and proven management. Yet these firms cannot meet the cash-flow conditions for servicing short-term debt demanded by commercial banks, prior to the expansion in output and sales that could be accomplished through greater imports. Even though these firms can provide sufficient collateral in land and equipment, this would not make them fully eligible for borrowing. Understandably, banks in Uganda have been risk averse, and in the new environment of reduced lending capacity they are expected to lend to established clients, preferably in the trading sector.

36. Given the already determined quarterly credit ceilings for 1987/88, and given the probable level of credit demand by other users (crop financing, traders and major industrial firms), an estimated US$4 to US$7 million equivalent would be available from the banking system, depending on the seasonal variation in crop financing. This corresponds to about 3.5 to 6.0 percent of total bank credit in the economy. If these resources are loaned to firms in the special conditions described in the previous paragraph, they will most likely have a significant impact on total industrial supply. To induce banks to extend this credit, the authorities will set up a Special Credit Facility that will make short-term credit available for local cover of imports and related working capital requirements.

37. Commercial banks will handle all credit applications and apply normal banking criteria in deciding to extend credit. In this, they may be influenced by the special features of the facility that would lead to a reduction in the risk of the loan. First, the risk involved in lending will be shared by the commercial banks and the Government. To this end, the authorities will set aside a fixed sum of about US$6 - 8 million which would cover losses on default up to the pro-rata risk assumed by the Government. Second, credit extended will be subject to a fee over and above the going interest rate for credit of equal maturity. This will discourage those firms which can obtain normal commercial credit and dissuade the commercial banks from using the facility to secure added cover. The facility's risk fund will be escrowed with drawings made exclusively by participating commercial banks. For a fee it may provide for optional but limited discounting of the loans issued. The facility is self-liquidating; no replenishments will be made to the initial size of the Fund to cover losses on loan defaults.

38. The Government will agree with the Association on the timing for the introduction of the facility. It will also agree on the size of the fund to cover losses on default, on the fees to be charged, and on the operational details of the facility. Once the facility is operational, the Association will review its performance and agree with the Government on measures to improve its implementation, if necessary.

B. Sector Policies

39. The measures announced on May 15, 1987, and the other macroeconomic policies agreed under PFP and the Fund's SAF program, will

establish the pre-conditions for the recovery of the Ugandan economy. While the proposed credit also supports these policies, its main focus is on the supply side policies affecting the performance of the productive sectors and the public sector management. These policies which were also agreed under PFP in broader terms, call for action on a wide range of issues. However, all aspects of the Government's program have not yet been fully developed. Further analysis will be required in a number of areas to expand the understanding of the issues and formulate concrete actions. The Bank's ongoing and programmed economic and sector work would contribute to the development of this program in subsequent years.

40. The economy of Uganda is relatively free of Government intervention and control in production. Its large subsistence and small scale sectors operate freely, and their continued growth has helped avoid a catastrophic economic situation during these years of upheaval. The controls which are in effect in Uganda are mostly concerned with the marketing of key export crops, and are in the form of setting producer prices, and exporting the crops through marketing boards. These arrangements date back to the pre-independence period. Prices of a very few basic necessities which are in scarce supply, namely, sugar, salt and soap, are also regulated pending an easing in the supply situation. Finally, in the industrial sector, the Government, as a result of earlier expropriations holds majority ownership in some 56 enterprises. As discussed in para. 60 the Government is committed to a strategy of divestiture to reduce its involvement in the industrial sector. It must be emphasized that the Government's program has the long-term objective of eliminating unnecessary interventions in the market mechanism, and reducing the Government's involvement in directly productive activities. Measures already announced by the Government and the actions to be taken under the Economic Recovery Program reflect these understandings.

Agricultural Sector Policies

41. Much needs to be done in Uganda towards the rehabilitation of the agricultural sector and to realize its full potential. To encourage production and improve efficiency in the agricultural sector in the short- to medium-term, pricing, marketing, and credit issues are being addressed under the present program. In the longer term, issues concerning research, training, extension, veterinary services, and input distribution also need to be attended. To provide a sound basis for the formulation of appropriate policies, with World Bank support, the Government organized a number of Agricultural Task Forces which concluded their work in April 1987. Their recommendations cover a wide range of areas including marketing, agricultural inputs, agricultural credit, manpower and training, land tenure, and agricultural research. Some of these recommendations are already incorporated into the present program. Others, once they are translated into policy actions, may then form the basis for future IDA sector lending.

42. Producer prices of export crops are a crucial issue addressed under the Economic Recovery Program. Price incentives to produce important export crops, including coffee, tea, and cotton sharply deteriorated during the last two years. A substantial increase in producer prices was needed to restore incentives to increase output, diversify production, and

maintain real producer incomes. Such increases, as described in para. 17, were announced on May 15, 1987. These prices, which were reviewed by the appraisal mission, were based mainly on border prices, taking into account justifiable margins for transport and processing. As shown in Figure 1, page 4, for coffee the recent adjustment brings the real level of the producer price to parity with the average level in 1983-1984 (as already mentioned, a peak year in terms of total sales to CMB). Prices in foreign markets have, meanwhile, fallen abruptly. In May 1987, prices received by CMB (in US dollar terms) had fallen 35 percent from their level in March 1986, and by 20 percent with respect to the 1983-1984 average, (see Figure 2, page 4). Meanwhile, the Government is committed to maintaining, and, if necessary, increasing returns to producers. It has been agreed that producer prices would be reviewed twice a year; once prior to planting and a second time in the harvesting and marketing season. Accordingly, the Government will review, and, if necessary adjust producer prices again in October-November 1987 in consultation with the Association.

43. To improve efficiency in agricultural producer pricing, the methodology used in price decisions is currently under review. The recommendation of the Agricultural Task Forces for a revised methodology has been adopted by the Agricultural Policy Committee (APC), and is now under consideration by the Presidential Economic Council (PEC). The proposed methodology incorporates the relevant price parameters for market efficiency such as: parity prices; market exchange rates; domestic resource costs; and relative prices of competing crops. The new methodology will also encourage the production of higher quality products, and compel the unions and the marketing boards to rationalize their overhead costs. The Government will formally adopt the new methodology by September 1987. It has been agreed that the October/November 1987 price decisions will be based on the new methodology.

44. In the area of agricultural credit, the Government is aware of the need for improvement in crop financing and has recently introduced a system whereby credit is provided directly from the commercial banks to cooperative unions with satisfactory accounting and financial expertise. Once fully operational, the direct provision of bank credit to producers' cooperatives would improve the efficiency in the use of credit, and would relieve the Coffee Marketing Board and the Lint Marketing Board of the financial burden to support the cooperative unions. In addition, the government is planning to establish a monitoring and supervision unit in the Ministry of Cooperatives to assure prompt payment to farmers. The Government will review the performance of the system by December 1987, and, if necessary, will take measures to accelerate its implementation.

45. In general, the level of Government intervention in agriculture in Uganda is substantially less than in other African countries. This is particularly true for agricultural products consumed domestically. As indicated earlier, however, the marketing activities of the major export crops -- coffee, cotton, tea, and five foodcrops are handled by government export monopolies. The poor performance of these marketing boards with their high costs and monopolistic buying power is recognized by the Government. The Government's long-term objective is to gradually liberalize the marketing and exporting arrangements for all agricultural crops. In the meantime, measures are being taken to improve the

operational and financial efficiency of the marketing boards. Measures recently taken to achieve these objectives and additional measures which the Government plans to take are specified below.

46. Coffee remains the most important cash crop in Uganda's economy contributing about 95 percent of total export earnings. The main problems of coffee marketing have been the widespread corruption in the CMB and in the cooperatives, their lack of accountability, and failure to pay farmers promptly. This inefficiency is also reflected in the widespread lack of published audited accounts, alleged misappropriation of funds and inadequate procurement procedures. To address these problems, the Government has recently replaced the top management and the board of CMB, and required the cooperatives to update and publish their accounts, which were behind schedule three to five years. The Government has also recently completed a review of the coffee marketing structure, and is presently considering the recommendations of this review. Among these recommendations the most important are the introduction of a tendering system to sell arabica coffee, the rationalization of hulleries, the reorganization of CMB, and the establishment of an effective information system for monitoring coffee sales. Under this credit, the Government will review these recommendations in association with the Bank, and agree on a timetable for implementation.

47. While cotton exports are relatively small compared to coffee, there is considerable potential for increasing export earnings and meeting more of the domestic demand. However, lack of adequate producer incentives and inefficiencies in the Lint Marketing Board (LMB) have constrained realizing this potential. At present LMB is the sole buyer and exporter of lint, and it has excessively high overhead and marketing costs. In addition, its involvement in the oil and soap industry has diverted resources from the production and marketing of cotton. During the first phase of the program, the Government will take measures to improve the efficiency of LMB and revitalize the cotton industry. To this end, a decision has been made to allow cooperatives to sell directly to textile mills, and to reduce the LMB's interest in the oil and soap industry to a minority position. These decisions would be implemented before December 1987. The Government is also exploring the alternatives to improve efficiency in exporting cotton by encouraging cooperatives, textile mills and private industries to participate.

48. Uganda has the potential to produce foodcrops over and above its domestic requirements, but procedures for obtaining licenses and some restrictions on the internal movement of foodcrops have discouraged production. The Government's declared policy calls for the licensing of traders of five foodcrops with export potential (maize, beans, simsim, groundnuts and soya beans), but allows no restrictions on their free movement across districts, except in emergency situations. Licenses are liberally issued and the licensees are free to sell to the Produce Marketing Board (PMB) or other buyers anywhere within the country. However, in practice, further restrictions are imposed on free movement of foodcrops in certain districts, particularly in border areas. Under the program, the Government, through the Ministry of Cooperatives and Marketing, would monitor the free movement of foodcrops across the district lines periodically, and would take action when needed. Under the proposed

project the Association would review the progress made in this area. The Government also intends to allow private exporters to export alongside PMB as economic conditions improve.

Industrial Sector Policies

49. The macroeconomic policies announced by the Government, particularly the establishment of a realistic exchange rate, will substantially improve the policy environment for the industrial sector. In the Government's program emphasis is given tothe provision of intermediate inputs to the industrial sector because many plants are operating at extremely low capacity due to lack of imported inputs and spare parts. As additional foreign exchange and local credit becomes increasingly available, these plants will rapidly improve their capacity use, and produce goods that are in short supply. Using the OGL system for channeling imports will substantially enhance efficiency in the allocation of available foreign exchange. This will also be an important step towards the rationalization of the import regime, which is a medium- to long-term Government objective. Meanwhile, the proposed Special Credit Facility, will contribute to the recovery of the sector by qualifying firms to raise local cover for imports.

50. The Government's policy has been to permit domestic prices to be freely determined in the market. However, under the extraordinary conditions that have prevailed in Uganda, including the existence of acute shortages of some basic necessities, the authorities exercised temporary controls on prices or profit margins for certain items, mainly imports, and, in some cases, assumed their marketing. There are no laws and regulations that call for administrative approval of price changes, and currently the Government does not exercise any formal controls, except on the prices of sugar, soap, and salt. However, firms usually submit pertinent information to the Ministry of Industry and Technology or Ministry of Finance before changing ex-factory prices. This informal system appears to have no serious consequence and the business firms are unaffected by it. The Government's commitment to a policy environment free from price controls was recently evidenced by the fact that despite temporary confusion resulting from the implementation of the currency reform and devaluation, the authorities decided not to interfere with the market determined prices.

51. The Government is reviewing the regulations regarding industrial licensing and foreign investment. Currently, the administrative processes to obtain an investment license are unnecessarily time consuming, even though such licenses are granted quite liberally. More significantly, the licensing law of 1969 requires such things as the gazetting of licensing applications and inviting statements of "no objection" from existing firms. Such regulations would encourage discriminatory practices which, in turn, discourage potential investors. The Government intends to revise the Licensing Act to shorten procedures, including exempting small investments from the provisions of the Act, and encouraging potential investors. This review would be completed by December 1987. By that time, revisions to the legislation will have been drafted and submitted to the appropriate Ministerial Committee before promulgation by the Government.

Transport Sector

52. Currently, inadequate transportation is a serious bottleneck hindering rapid economic recovery. There is a shortage of trucks and road equipment for the badly needed repair of trunk and feeder roads. A large number of trucks and pick-ups have been ordered by the Government and a significant portion of them have already been received. With donor support, including IDA, major efforts are currently underway to improve the road conditions and the maintenance capacity. A Transport Needs Assessment Study has been completed by the Bank and has been discussed with the authorities and donors. This study identifies the emergency needs of the transport sector, and provides the basis for a coordinated donor effort to meet these needs. In addition, a transportation sector strategy study sponsored by UNDP is underway. These two studies will provide the basis for Government's strategy and investment needs in the transport sector, and relevant policy and institutional reforms will be incorporated into subsequent phases of the program implementation.

C. Public Sector Resource Management

53. The proposed Credit will support a number of initiatives taken by the Government which aim to improve the efficiency in public sector resource mobilization and allocation, and reform the civil service and the public enterprise sector. These initiatives represent the initial steps in a lengthy process of effecting institutional reforms in the public sector. As the underlying studies are completed the Government is expected to expand and develop its program and take further action in these areas. The Region is prepared to support the further stages of this program through policy-based lending and technical assistance.

Public Resource Budgeting and Management.

54. Given the almost complete breakdown in sales and income tax collection, improvement in tax administration is essential to achieve major increases in tax revenues. To this end, the Government will address the problems specific to each of the three revenue departments. The measures outlined here are to be monitored under the Fund's SAF program. In the Income Tax Department, priority will be placed on (i) the canvassing and identification of non-filers; (ii) the speeding up of the posting of taxpayer accounts; (iii) the initiating of distraints and court actions for the largest cases of arrears; (iv) the auditing of tax returns, with prosecution in fraud cases; and (v) the creation of an internal audit and inspection unit that would have authority to investigate all allegations of misconduct by employees. In the Customs and Excise Department, the major effort will be on (i) the continuation of the repression of large-scale smuggling; (ii) the rigid enforcement of payments of customs duties and sales tax before all goods are cleared, even for government departments and parastatals; (iii) the inspection of all customs stations and posts on a quarterly basis; (iv) the strengthening of the internal checking branch that monitors the performance of customs staff; (v) the rigid enforcement of regulations on the use of bonded warehouses; and (vi) the monitoring of the accounts of all firms producing goods subject to excise duties, and the taking of appropriate actions in cases of fraud or accumulation of tax arrears. In the Inland Revenue Department, the focus will be on (i) the

canvassing and identification of nonregistered businesses; (ii) the enforcement of the regulations requiring monthly returns and payments of tax, and the assessment of penalties for late payment; (iii) the overhaul of the Investigation Branch; and (iv) the establishment of an internal audit and inspection unit that would inspect and check staff performance. In order to help it carry out these various reforms, the Government is seeking appropriate technical assistance from external sources, including the Fund and the Bank.

55. In the area of tax policy, the Government will make initial modifications to the customs duties in the 1987/88 budget by eliminating a number of exemptions that do not concern aid-financed items. In July 1987, the Government will also abolish the current exemption from income tax on civil service emoluments. Improvements in the implementation of the existing tax laws will yield short-term results but it is also necessary to review the existing tax system to improve its buoyancy, insure that it provides adequate incentives to producers, and promote a more efficient resource allocation. To provide the basis for such revisions in the tax system, the Government is committed to initiate a comprehensive study by end-1987. In the same context, the tariff structure will also be reviewed with a view to promoting the development of efficient import substitution activities and a diversified export base. The study on taxes and tariffs is expected to be finalized by end-1988, and will provide a basis for government policies in these areas.

56. The Government is planning on taking steps to establish and maintain budgetary discipline. Accordingly, it will follow a policy of strictly limiting expenditure to achieve the overall deficit target and the target for repayment of net bank debt. The mechanisms for expenditure control were in place and operating reasonably effectively in 1982/83 and 1983/84, so it is not a matter of setting up such mechanisms, but more one of reviving them. Beginning in fiscal year 1987/88, the Government will strengthen all its monitoring and accounting procedures to eliminate the possibility of unauthorized overspending by ministries and departments. Expenditures in excess of monthly budget allocations will be adjusted against subsequent allocations, and an investigation by a strengthened Auditor General's Department reporting directly to the President will be triggered if allocations are exceeded during three successive months. In addition, the Government will be prepared to reduce expenditure as needed in the event of shortfalls in revenue or in foreign assistance. As regards development outlays, the Finance Ministry will improve its monitoring and develop more comprehensive records of foreign assistance and related expenditure. Under the SAF agreement with the IMF, the Government is committed not to incur new domestic or external arrears during the program period. The Government is also taking measures to: improve the effectiveness of the Central Tender Board and Central Clearing and Forwarding Company; set up a Central Procurement Body at the Supplies Directorate; strengthen the parastatal financial monitoring unit; and, set up a Financial Management System. The Bank would provide support for these activities under a proposed technical assistance project.

57. The Government recognizes the need to overhaul and streamline the civil service in order to increase its efficiency and limit the wage bill. As a first step, the Government will take a census of non-military

government employees, including regular civil servants, contract employees, and group (i.e., temporary) employees, with a view to eliminating all "phantom" workers from the government payroll. The Government will apply strictly the civil service regulations regarding the retirement age, attendance, and discipline, in order to prune the civil service of unproductive staff. By end-1987, the Government will also reduce significantly the number of group employees. These measures will contribute to creating the capacity to increase civil service wages for the remaining employees. However, because further gains in wages, in addition to those announced on May 15, 1987, will be accompanied by reductions in the number of employees, it is expected that the real wage bill will be kept at its 1986/87 level.

58. The Government is also undertaking a comprehensive review of the functional and staffing structures of the civil service with Bank assistance. The review initially concentrates on the Office of the President, and the ministries of Public Service and Cabinet Affairs, Planning and Economic Development, Finance, Local Government and Works, and Education, which together comprise about 60 percent of the civil service. The review will subsequently be extended to cover the entire civil service. After some delay in their initiation, all preparations are finalized for the launching of these studies, the completion of which is expected to take about eighteen months. The findings and recommendations of these studies will be incorporated in future lending operations of the Association that will address the reform of the civil service.

Public Enterprise Reform and Divestiture

59. In the short run, the recovery of industrial output depends to a considerable extent, on how quickly the public industrial enterprises can improve their extremely low capacity utilization. However, in the medium- to longer-term, restructuring and rehabilitation of the public enterprise sector is essential for sustained industrial growth, including the divestiture of a large number of undertakings. Currently the public industrial enterprise sector contains about 56 companies, most of which are operating below 20 percent capacity, and two-thirds have been making losses for an extended period of time. In addition to input shortages and deteriorated physical plant conditions, this poor performance reflects excessive political interference, lack of financial discipline, and deteriorated management quality and staff morale.

60. As a result of expropriations under previous regimes, the public sector assumed the ownership of a large number of enterprises of varying size. The present Government has a pragmatic approach to state ownership in industry, and its strategy calls for reducing the size of the sector in order to lessen the burden of management responsibility and avoiding the financial drain on public resources. Accordingly, the Government is planning to divest a large number of enterprises that can better be managed by the private sector, while taking measures to improve the efficiency and profitability of those remaining under public ownership. To achieve these objectives the Government has taken steps including: (i) the establishment of a verification committee and a board of valuers; (ii) the organization of a public enterprise sector task force by the Prime Minister; (iii) the

decision to set up a Public Industrial Enterprise Secretariat; and (iv) the preparation of a restructuring plan for the Uganda Development Corporation (UDC).

61. A task force assembled in December 1986 by the Prime Minister is to review the parastatal sector and to make recommendations for restructuring of the sector. The task force has already submitted its report to the Presidential Economic Council (PEC) last May which is currently being reviewed by a sub-committee. Before December 1987, PEC will decide on an action plan for steps to be taken to finalize the restructuring of the public enterprise sector, and identify both the industrial and non-industrial parastatals to be divested, those to be retained, and those to be closed.

62. Meanwhile, a Verification Committee has been working on resolving ownership issues on the plants expropriated earlier, and a Board of Valuers to assess the value of plants, equipment and other properties has been set up. The Government has already settled the ownership issue of some twenty-five enterprises, although the question of outstanding liabilities has not been resolved in all cases. By December 1987, the verification of the ownership of a significant number of industrial enterprises will be completed, and a plan of action drawn up for completing the verification and valuation of all properties and enterprises, subject to the Expropriated Properties Act, and for the return to former owners or sale of such enterprises or properties.

63. To facilitate the restructuring of the public enterprise sector, a decision was recently taken to set up a Public Industrial Enterprise (PIE) Secretariat under the Ministry of Industry and Technology. In addition to advising the Government on the divestiture process, the Secretariat will assume the functions of assisting the Government in restoring financial discipline, developing and implementing public enterprise institutional and policy reform, preparing management training programs, and providing a mechanism for enhanced managerial autonomy and accountability. The Bank is providing technical assistance for setting up the PIE Secretariat. By December 1987, key level staff will have been recruited and the Secretariat could be operational.

64. A comprehensive restructuring plan for the UDC is being drawn up. The plan is designed to re-establish UDC as a viable institution capable of developing enterprises in its portfolio to the stage where they can be divested, and reinvesting the proceeds in new viable enterprises. To this end, UDC's development role has been defined to entail the identification of new investment opportunities, marrying these with investors with appropriate managerial and technical skills and capital, and supporting them with risk capital. UDC's restructuring program will include the areas of portfolio strategy, financial strategy, organization, and management which will enhance its capabilities as a catalyst for new investments. The UDC is expected to close and/or divest a number of firms and reduce its share to a minority position in most others. UDC's restructuring program will have been approved by its Board by December 1987.

65. The Bank has provided extensive support to the Government with the development of detailed recommendations both for the establishment of the

PIE Secretariat and the restructuring of UDC. Both these efforts are planned to be supported by an IDA technical assistance credit, scheduled for FY88. In the meantime, bridge financing for the PIE Secretariat will be secured from the existing Technical Assistance II credit and a project preparation facility may, if necessary, be arranged for UDC.

D. Public Sector Investment Program

66. The Government has prepared a public sector investment program covering the period between 1987/88 and 1990/91. The main objective of this program is to rehabilitate and reconstruct the economic and social infrastructure so as to restore the productive capacity of the economy and the provision of basic social services. The level of expenditure in the program is relatively high, reflecting Uganda's rehabilitation and recovery needs, and the envisaged level of external financing. The projects emphasize specific goals in five areas: (i) acquisition of agricultural tools and machinery, and other essential inputs; (ii) repair and maintenance of feeder and trunk roads; (iii) acquisition of trucks and rolling stock for railroads; (iv) rehabilitation of industries manufacturing essential commodities (such as sugar, soap, and textiles); and (v) rehabilitation of basic public utilities, such as electricity and water supply. Nearly 30 percent of the planned investment will be expended on transport and communications, followed by another 24 percent on agriculture, a little over 21 percent of industry and tourism, and 7 percent on mining and energy. The remaining 18 percent will be devoted to social infrastructure and public administration.

67. This program has been reviewed by the Bank. The first year, which provides the basis for development expenditures in fiscal year 1987/88 is consistent with the adopted macroeconomic targets, and has an appropriate sectoral distribution and project content. However, the expenditure levels for the outer years of the program are excessive in view of budgetary considerations and the size of expected new external commitments. Also, the Bank has recommended that the decision on a few projects be postponed until the relevant sector studies are completed. The Government plans to have a three-year rolling investment plan. In this context, the public sector investment program covering 1988/89-1990/91 will be reviewed and reformulated by the Government in coordination with the Bank, before December 1987.

PART III - THE PROPOSED OPERATION

A. Background

68. Three reconstruction credits were made by IDA to the Uganda Government from 1981 to 1984 to support a medium-term Recovery and Rehabilitation Program, covering fiscal years 1981/82-1983/84. The program was supported also by considerable donor assistance including three successive one-year stand-by arrangements from the Fund. After some initial success, the economic recovery faltered and after the military coup of July 1985, the economic situation worsened rapidly.

69. The NRA Government which took power in late January 1986 inherited an extremely precarious economy. Despite some success in reviving economic activities in war-devastated areas, economic developments in 1986 were not encouraging. After a brief experiment with a policy based on stronger controls, a fixed exchange rate, and relatively high levels of public expenditure with bank-financed deficits, a consensus emerged for a reversal in economic policies. The Government approached the World Bank in January 1987 for help in the design of an Economic Recovery Program and to provide financial support for its implementation. The major components of this program were discussed with the Government in the context of a joint Bank-Fund mission in March 1987, when agreement was reached on a Policy Framework Paper (PFP). The PFP was approved by the Committee of the Whole on May 26, 1987. A Consultative Group met in June 1987 and gave strong support to the program. A meeting of the Paris Club was held on June 18, 1987 to consider Uganda's arrears and debt servicing due to bilateral organizations. The club responded favorably to the request for rescheduling of arrears and current debt servicing obligations. A mission to appraise this credit visited Kampala in May-June 1987 and credit negotiations were held in Washington at the end of July 1987. The Ugandan delegation was led by Dr. C.W.C.B. Kiyonga, Minister for Finance.

B. Relationship to the Government's Program

70. The proposed operation would support policies and measures under the Government's Economic Recovery Program. Some of these actions are also supported by and monitored under the Fund's SAF credit. In line with the earlier understandings, on May 15, 1987, the Government announced the policy package described above in para. 17. The actions taken up-front constitute a major effort on the part of Government and are an indication of its commitment to the implementation of the Economic Recovery Program. The proposed credit supports the actions already taken, and other actions agreed upon and described in Part II of this report. This operation will also serve the important objective of deepening our policy dialogue with the Government and helping the authorities in the formulation of economic policies.

71. The proposed credit should be seen as the first of a series of policy based operations to support the recovery and structural transformation of the Ugandan economy. Many aspects of the program related to the removal of structural constraints to sustained growth have not yet been fully developed since both the Government and the Bank have had to formulate this program in a relatively short period of time. Moreover, the changing political and economic environment in Uganda and the two-year hiatus in our operations necessitate additional analysis in a number of areas. To the extent that the structural constraints have been analysed and identified, they are addressed under the proposed credit. In some areas, however, further analysis will be required, and studies will be undertaken to underpin reform programs in subsequent operations.

C. Financing Requirements

72. To meet the import requirements of economic recovery and the investment targets, merchandise imports are projected to rise from an

average of US$407 million per annum in 1983-1986 to an average of US$605 million per annum in 1987-1990. This expansion reflects a 53 percent increase in volume and a small (1 percent) decrease in prices, mostly on account of further reductions in petroleum prices. Exports are to rise from US$382 million, on average, in 1983-1986 to US$429 million in 1987-1990, with a growth in volume of 19 percent. The trade deficit is therefore expected to grow, from US$24 million per annum on average, during 1983-1986 (US$77 million in 1986) to US$170 million in 1987, to US$193 million in 1988, and to US$186 million in 1989, before beginning to come down to US$155 million in 1990.

73. Being a landlocked country, Uganda faces high transportation costs on the export and import of goods. Moreover, despite falling interest obligations, interest payments will still account for approximately 8 percent of exports by 1990 (down from more than 16 percent in 1987). Thus, on balance, payment for services will continue to constitute a drain in the current account. This outflow is partly neutralized by inflows of private transfers, but on the whole, the current account deficit is expected to increase. From a small deficit of US$29 million in 1986, the current account in 1987 will show a likely deficit of US$176 million, expanding to US$205 million in 1988, and to US$181 million in 1989 but narrowing to US$148 million in 1990. Uganda also faces considerable repayment obligations on previous borrowing which peak in 1987. Of note is the debt to the IMF. The level of annual repurchases and charges will decline from their peak of US$102 million in 1987, nevertheless, they will average approximately US$72 million per year over the next four years, including 1987. Moreover, the country will have to replenish her foreign reserves, eliminate pending short-term obligations and make a significant effort in reducing external arrears. The figures add to financing requirements of US$400 million in 1987, US$370 million in 1988, US$329 million in 1989, and US$288 million in 1990.

74. To finance the accumulated requirements of US$1,387 million from 1987 to 1990, Uganda can count on a large backlog of undisbursed resources from previously committed grants, credits and loans. These resources are estimated at US$539 million, or about 40 percent of the total financing requirements. This leaves a financing gap of US$685 million to be filled from new sources. To meet this target, new commitments on credits and loans must reach about US$250 million in fiscal year 1987/88, while in 1988-1990, they should average nearly US$200 million per year.

75. Based on the experience of the last two years, when commitments from medium and long-term loans and credits averaged less than US$70 million a year, these requirements would seem very high. It must be emphasized, however, that the years 1985-1986 were exceptional, in that political problems in Uganda discouraged new aid commitments. A more relevant comparison is to the years 1983 and 1984, when the level of new commitments of medium- and long-term borrowing averaged US$220 million. What is proposed for the program period, therefore, is a resumption to earlier commitment levels. In fact, taking into account the significant depreciation of the US dollar in the intervening years, in real terms, the proposed level of new commitments is smaller than that in the early 1980s.

76. Disbursements from new credit and loan commitments are expected to total $510 million over the program period. To close the remaining gap three additional forms of assistance are considered. First, a total of US$84 million in disbursements from new official grants is expected between 1987 and 1990. Second, agreements recently completed with the IMF will add another US$91 million, including initial disbursements of US$57 million in 1987. This includes a total drawdown of Uganda's share in the Structural Adjustment Facility during 1987-1989, and a US$32 million drawing from the Compensatory Finance Facility in 1987. Notwithstanding the disbursements in 1987-1990, net transfer from the IMF will be negative, accumulating to US$197 million. Finally, at the Government's request, the Paris Club met on June 1987 to consider a rescheduling of external debt service obligations, including arrears. The Club agreed to reschedule all payments due in 1987/88 on medium- and long-term guaranteed bilateral debts concluded before July 1, 1981, including previously rescheduled debt, and 100 percent of arrears as of end-June 1987. The repayment period is 9 years with a grace period of 6 years. Arrears rescheduled totalled US$44.5 million and payments otherwise due in 1987/88, US$25.6 million. On the assumption that similar terms are granted for arrears (US$47.3 million) and current obligations (US$12.2 million) due to non-Paris Club bilateral creditors (Saudi Arabia, Kuwait, Lybia, India, etc.) the estimated debt relief amounts to about US$130 million. Uganda will require further rescheduling from bilateral sources in 1988/89, estimated at US$33 million. However, already in 1989/90 the country will face a sustainable balance of payments position -- without requiring further debt relief.

77. The composition of commitments is also important. In 1987, 1988, and 1989 quick disbursing balance-of-payments support will be required to sustain the recovery program and OGL. The financing plan assumes that slightly over one-half of the volume of new commitments up to 1989 will disburse by end of 1989, and that nearly two-thirds of new commitments up to 1990 will be disbursed by end 1990. Moreover, the net benefit to Uganda of higher commitments and faster disbursements of external assistance could soon be eroded if this assistance is not provided on concessional terms. The country's external debt burden has been exceptionally high over the last three years including 1987. Scheduled debt servicing obligations would have consumed over one-half of export revenues. Under current projections, 85 percent of new commitments up to 1990 would be provided on concessional terms. With this, and given the rapid repayment of previous non-concessional borrowing from IMF, the total debt service ratio is expected to fall, from 57 percent in 1987, to 39 percent in 1988, to 31 percent in 1989, and to 24 percent by 1990, when no debt relief is planned for. Without reschedulings, the ratios for 1987, 1988 and 1989 would have been, 63 percent, 46 percent and 35 percent respectively.

78. However, the down-side risks are real: Uganda's export structure is heavily dependent on coffee earnings which could be constrained by more unfavorable and unexpected price movements; the Government may find it difficult to reduce the import requirements of security related activities; and adequate amounts of assistance may not be forthcoming to support the recovery effort. Moreover, if the major assumptions underlining these projections can be realized, Uganda's creditworthiness will improve significantly over the coming years.

D. Monitorable Actions

79. The Letter of Development Policy (Annex I) describes the actions that have been taken by the Government, and the further actions that will be taken during the first phase of the Economic Recovery Program implementation. These measures are also summarized in the matrix of policy actions shown in Annex II. In addition to the overall satisfactory progress in the implementation of the program, the release of the second tranche of the credit would be contingent upon the implementation of the following actions:

(a) agreement with the Association on the three-year public investment program covering 1988/89-1990/91;

(b) agreement with the Association on a revision of the May 1987 producer prices for export crops based on a methodology satisfactory to the Association for determining these prices;

(c) adoption of the Open General Licensing (OGL) system giving eligible producers in priority industries access to foreign exchange upon request for the importation of eligible imports; and following a review of the implementation of the system, adoption of a satisfactory plan of action for expanding its coverage.

(d) finalizing an action plan for steps to be taken towards the restructuring of the public enterprise sector, and identify both the industrial and non-industrial parastatals to be divested, those to be retained, and those to be closed; and

(e) completion of the verification of the ownership of a significant number of industrial enterprises and the submission of a plan of action satisfactory to the Association, for the completion of the verification and valuation of all properties and enterprises subject to the Expropriated Properties Act, and for the return to former owners or sale of such properties and enterprises.

E. Cofinancing Arrangements

80. A total of US$105.0 million equivalent would be provided under the proposed credit to support the Government's recovery program including an IDA credit equivalent to US$65.0 million and US$40.0 million equivalent from the Special Facility for Africa, of which US$24.0 million equivalent would be in the form of an African Facility Credit, and about US$16.0 million would be from Special Joint Financing (SJF). Special Joint Financing is expected to be provided by the Overseas Development Administration (ODA) on behalf of the United Kingdom (UK) through a grant of Pounds Sterling 10.0 million. The UK expects to conclude its Grant Agreement with the Government of Uganda regarding the SJF by the end of 1987. If approved the UK funds would be administered by IDA.

81. In addition, the Canadian International Development Agency (CIDA), on behalf of Canada, is considering a grant contribution of up to Can$15.0

million (about US$11.2 million) over the next 3 years, in roughly equal amounts of Can$5.0 million per year. Canada intends to request IDA to administer the Canadian grant. The Danish International Development Agency (DANIDA), on behalf of Denmark, intends to provide Uganda with a grant of about US$5.0 million equivalent in support of Uganda's Economic Recovery Program. DANIDA also intends to request IDA to administer the Danish grant. The Swedish International Development Authority (SIDA), on behalf of Sweden, plans to extend to Uganda a grant of SKr10 million (about US$1.3 million) to support Uganda's recovery program. SIDA also intends to request IDA to administer the Swedish grant. Considering the Canadian, the Danish and the Swedish contribution, the total support for the Government's program amounts to the equivalent of US$122.5 million.

F. Procurement and Disbursement Arrangements

82. IDA and African Facility. Procurement would be limited to eligible imports on the basis of a negative list, in accordance with Bank/IDA guidelines. Private, cooperative, and public sector imports would be eligible for financing. Procurement procedures have been designed to permit rapid use of the funds while ensuring efficiency and economy. Contracts for the procurement of goods by the private sector of less than US$2 million equivalent would follow normal commercial practice. Government contracts equivalent to less than US$2 million would follow procurement procedures which are acceptable to IDA. All purchases under contracts of more than US$2 million would be procured through international competitive bidding. Certain commonly traded commodities may be purchased at prices quoted on organized international markets. Expenditures for goods covered by invoices for less than US$5,000 equivalent would not be eligible for financing. Procurement sources for the African Facility are the same as for IDA financing in this instance, since the funding for the African Facility will be financed from the IBRD's contribution to the Facility.

83. Special Joint Financing. The proceeds of the Special Joint Financing would cover only those eligible expenditures for goods produced in or services supplied from the eligible countries under the Resolution establishing the Special Facility.

84. The proposed IDA Credit, the African Facility Credit and the Special Joint Financing totaling about US$105.0 million equivalent would be disbursed in two tranches. The first tranche would amount to US$60.0 million equivalent, of which up to US$17.9 million (20 percent of the program financing) would be eligible expenditure from May 1, 1987. The first tranche would consist of US$30.7 million from IDA, US$13.3 million from the African Facility and US$16.0 million from Special Joint Financing. The second tranche would be available for disbursement following a review in January 1988 of progress made in the carrying out of the program and subject to the specific conditions outlined in para. 79.

85. To facilitate procurement and disbursement, the Government will open two special accounts in an international commercial bank, in US dollars (Revolving Funds), one for the IDA Credit and one for the African Facility and the Special Joint Financing. The initial deposit would be US$10.0 million from IDA, and US$10 million from the African Facility

Credit and US$4 million from the Special Joint Financing, representing about three months expected financing from these sources after drawdown of the retroactive financing. Applications for replenishment of the special accounts would be submitted monthly, or when withdrawals equal one-third of the amount advanced. Applications would be fully documented with respect to payments against contracts of more than US$500,000 equivalent. Reimbursements for payments against smaller contracts would be made on the basis of Statements of Expenditure (SOE) certified by the Bank of Uganda with supporting documents retained for review by visiting missions. Annual audit reports would include a separate audit of amounts withdrawn on the basis of statements of expenditure. No reimbursement would be made from imports financed from other sources. It is estimated that eligible imports in 1987/88 will total about US$200 million equivalent. The proposed credits would finance about half of this amount, thus permitting rapid disbursement. Disbursements will be completed by March 31, 1989.

G. Economic Impact of the Program

86. Stabilization of the Economy. The Government's Economic Recovery Program aims at a quick return to economic stability with growth in output. In its initial phase, the program is designed to reduce the rate of inflation significantly, while restoring fiscal and external balances. The program is based on a combination of a sizeable, initial exchange rate adjustment and strict monetary and fiscal policies with quick responding supply side measures. These comprise, mainly, a recomposition of domestic credit towards private and parastatal enterprises, an adjustment in producer prices for the key export crops, and an increase in the volume and in the allocative efficiency of imports.

87. Achieving a rapid supply response in the economy, in turn, is very much related to the availability of foreign exchange for essential imports to increase the capacity utilization in the manufacturing sector. In the short run, the Government relies heavily on additional foreign exchange from external sources. Therefore, not only the size but timely disbursement of external assistance is extremely important for the Government to succeed in its stabilization efforts. If the essential import requirements are met in a timely way, it is expected that the manufacturing plants can rapidly increase the production of goods that are currently in short supply.

88. Economic Growth. The Recovery Program aims at a growth rate of 5 percent per annum in the 1987-1990 period. Following a decline in output in 1985 and 1986, and a hesitant recovery in 1987, the industrial sector is expected to grow at 5.5 percent in 1988 and by 6.0 percent in 1989 and 1990. The greater availability and increased efficiency in the allocation of imports will provide the main stimulus to industrial output increases. Projected output levels reflect increased capacity utilization, and not additions to plant capacity through major new investments. The large-scale manufacturing firms in textiles, tobacco, beverages, wood-products, paper products, construction materials, and chemicals are prime candidates to procure their import requirements through the OGL system. While initially the sectors with the highest concentration of small scale firms are not expected to be the main beneficiaries of the OGL system, they will benefit from the increased availability of domestically produced inputs. In the

medium- to longer-term, the expansion of the OGL system to all sectors, and the Government's policy of providing an environment conducive to industrial growth, will be instrumental in maintaining relatively high growth rates in small scale industry.

89. Because of its relatively large share in output, exports, and employment, overall growth in the economy closely mirrors developments in the agricultural sector. After a slow start in 1987, when output is anticipated to expand by less than 4.0 percent, the sector is projected to grow at 5.0 percent in 1988 and at somewhat faster rates of 5.3 percent per annum in 1988-1990. In the agricultural sector, restoring adequate price incentives for both cash and foodcrops will provide the major stimulus for production in the short- to medium-term. The maintenance of peace and security and the return to productive use of areas devastated by war will also assist in achieving this objective. The Government will also continue to improve marketing arrangements to create a more competitive and rewarding environment for producers. The rehabilitation of the transport network will play a crucial rule in increasing marketable supplies throughout the country. Once the agroprocessing industries, such as sugar, beer and edible oils, start expanding their capacity use domestic demand for agricultural products will also expand. As the agricultural supply situation improves, and as processing plants, cooperatives, and credit mechanisms are rehabilitated and reformed, the export market for agricultural products will gradually be liberalized, which will give added stimulus to the production of non-traditional, exportable crops.

90. Investments, and Savings. Implementation of the Government's program calls for a major increase in the aggregate level of investment, from 14 percent of GDP in 1985/86 to about 20 percent of GDP by 1990. The Government's share in total investment will increase temporarily in 1988 and 1989, when the rehabilitation efforts will be most intensive and more than half of all investment would be undertaken by public or parastatal entities. However, already in 1990, the Government's share should decline to about one-third of total investment. While this share is still higher than the average for the early 1980s, it represents a level of public investment that is compatible with available resources, with an adequate provision of funds for recurrent expenditures, and with a reduction in the overall public sector's deficit to less than 4 percent of GDP.

91. To finance the growth in investment, in addition to a sustained high level of concessional aid flows, gross national savings are expected to increase from an average of 14 percent of GDP in 1985/86 to more than 17 percent by 1990. As discussed earlier, fiscal policy, and in particular, tax policy will play a significant role in the recovery of domestic savings. The importance of this is not only in the reduction of the overall public sector's deficit, but in the alleviation of the savings burden of the private sector. Taking into account government savings and the substantial volumes of foreign financing of development expenditures, private savings are expected to decrease from about 15 percent of GDP in 1986 to 11 percent in 1987 and 8 percent in 1988/89 before rising again to 11 percent of GDP in 1990. This movement in private savings will allow a small but sustained gain in per-capita consumption.

92. The External Sector. Under the Economic Recovery Program the volume of merchandise imports is projected to grow at an average rate of 6.1 percent per annum between end-1986 and end-1990. Taking into account the expected trend in international inflation, import growth expressed in US dollar terms will be about 8 percent per annum on average. Over one third of imports will be related to specific disbursements of medium- and long-term loans and credits, and of grants and transfers. The bulk of these will be capital goods and/or inputs directly linked with investment projects. Petroleum imports will account for about 10 percent of the total. Another 10 percent will go to imports on consignment or associated with the repayments for former joint ownership of assets of the East Africa Community. This leaves approximately 40 percent, on average during 1987-1990, for "cash" imports, including intermediate goods, spare parts and consumer goods for the private and parastatal sectors.

93. The volume of exports is projected to increase even faster than imports, growing in real terms at slightly more than 7 percent per annum on average between 1987 and 1990, nearly all of which will continue to be agricultural products. Coffee exports, which account for close to 90 percent of the total volume of exports, are expected to grow at an average rate of 4.2 percent per annum in the period 1987-1990. It is likely that coffee exports will be constrained by world demand and the possible re-introduction of the ICO quota system. However, due to the recent fall in export volume, the projected increase can be accommodated within the revised coffee quota agreed by the ICO in December 1985, following the collapse of the Brazilian crop. Historically, Uganda has a diversified agricultural export base including, in addition to coffee, major exports of cotton, tea and tobacco. For these crops the expected recovery in output levels will encourage a rapid expansion of exports, albeit from a very small basis. Altogether, non-coffee exports, including other products such as beans, groundnuts, simsim and soya beans, are expected to grow at nearly 40 percent per annum on average -- pushing their share in total exports volume from 8 percent in 1986 to 17 percent by 1990.

94. Export revenues, especially from coffee, will grow at a slower rate than the volume. Coffee prices in the world market are likely to remain depressed over the next few years. From 1987 to 1990, the US dollar value of coffee exports will expand at less than 2 percent per annum on average. In 1987, the combination of falling prices with a slow expansion in export volume will probably lead to exports of no more than US$332 million, down from an estimated US$414 million a year earlier. Coffee prices, and especially the volume of exports, will most likely rise in 1988, but it will take at least another year before revenues approach the 1986 level. By 1990 the terms of trade are expected to be 13 percent below the 1986 mark, despite a speedy recovery beginning in 1988. On the whole, exports in US dollars will be less than one-fourth larger in 1990 than in 1986, while imports in 1990 will probably exceed by one-third their 1986 level. Moreover, imports of non-factor services, mainly transport charges, will continue to exceed exports as the volume of international trade expands. The resource imbalance will therefore grow from 3.1 percent of GDP in 1986 to about 6.5 percent of GDP in 1987, reflecting both the larger trade imbalance and the valuation effect of the change in the exchange rate. For the reasons already discussed, the imbalance will expand further in 1988 and 1989 before closing to about 5.9 percent of GDP in 1990.

H. Social Impact of the Program

95. On balance, the implementation of the Economic Recovery Program is expected to have a strong positive social impact and improve welfare levels in Uganda, particularly after a transitional period. Prolonged decline in the economy through 1986 resulted in substantial reductions in both rural and urban per capita incomes. The implementation of the program will facilitate the recovery of the economy and help attain sustained per capita income. Whatever transitional costs may incur in the process, they should be evaluated in the context of the social costs of failure to achieve recovery and growth within a reasonable time period. Further declines in per capita income with economic stability would have not only economic and social but also strong adverse political ramifications.

96. In the short run, the implementation of the stabilization program will require further restraints on consumption for all segments of the economy, particularly the urban sector. Already, the imposition of the 30 percent currency conversion tax has lowered the liquidity of the public and reduced their purchasing power. The increase in the prices of petroleum products and imported items due to devaluation have also added to costs. However, as the stabilization measures take effect, the high rates of inflation would be reduced, thereby significantly slowing down the erosion of the purchasing power. With the implementation of recent measures, the pressure on prices has already eased, while prices of certain products have actually come down. The rapid deceleration of inflation will help the poor and the underprivileged more than the other segments of the society. With the enlarged inflow of foreign exchange and improved confidence in the economy, as well as with domestic supply responding to the policy changes, per capita consumption is expected to grow beginning in 1988.

97. The rural sector is expected to benefit from the implementation of the Government's program more rapidly than the urban sector. With the announcement of the new measures, prices both for export crops and foodcrops have already been raised significantly. These increases in producer prices more than compensate for the increases in agricultural input prices. It may take longer, however, for the urban sector to benefit fully from the program's implementation. The Government has raised civil service salaries by 100 percent which would help ease the economic difficulties of the salaried urban dwellers. However, urban employment will be adversely affected to the extent that public sector employment is reduced. Nonetheless, it is expected that a number of positions to be cut in regular employment will not mean a loss in actual employment, because these positions are phantomly occupied. Also, reduction in temporary group employment should be seen in the light of extremely low payments to the employees whose main livelihood depends on income from other sources. In this context, it is important to note that the distinction between urban and rural population is not sharply drawn in Uganda, and the number of people exclusively dependent on fixed salary income is small.

98. Any employment losses that may arise from the civil service reforms must be set against the prospective employment gains from the program's implementation. Improved capacity use in the public and private industrial firms through increased supply of inputs will give immediate

rise to urban employment. Improved producer incentives in industry and agriculture, as well as higher levels of public and private investment will gradually help create new jobs. The increase in transportation activities will also enhance employment opportunities. The implementation of the program, however, will have a favorable social impact beyond the creation of job opportunities and employment. The Government will have more resources to increase the provision of basic services, particularly in primary health, education, and water. These measures will, in the medium-term, help raise the standard of living of the population in general, and of urban dwellers in particular.

I. Risks

99. Uganda is relatively well positioned to implement the Economic Recovery Program. For the first time in years, the regime has considerable broad based support, has improved the security situation, and introduced some discipline in the public administration. A high-powered President's Economic Council has been set up to address all major economic policy issues, including overseeing the design and implementation of the Economic Recovery Program. There is a broad consensus on the policy agenda and the Government has already displayed its commitment to reform by taking strong macroeconomic measures. The donor community is supportive of the Government's program as evidenced in the recent Consultative Group meeting. There are, nevertheless, at least three risks associated with the program implementation and its success. These risks relate to: (i) the Government's implementation capability; (ii) possible delays in the supply response; and (iii) the socio-political situation.

100. The success of the recovery program requires astute national economic management. One of the risks concerns the inexperience of key officials in the formulation of development policy, and the weakness in the Government's implementation capacity. Even though Uganda is endowed with educated and skilled individuals, political turmoil and extremely low civil service remuneration have persuaded many to leave the government service. However, some key personnel with specialized skills has recently been recruited from both inside and outside the country. To step up these efforts, Government is considering special compensation schemes, particularly for those recruited from abroad. Technical assistance support from donors, including the World Bank, is being programmed to complement the Government's own manpower resources. Civil service salaries have recently been raised by 100 percent, and further salary increases are planned within budgetary limits. Improved remuneration would enhance the attraction of the civil service both for potential recruits and those currently employed. In the medium- to long-term, civil service reform based on the ongoing study on staffing and functional requirements, would help improve the effectiveness of the administration.

101. Economic recovery depends, to a large extent, on the speed at which a supply response is realized. One major risk originates from the fact that the increase in supply is dependent upon the availability of imports, which in turn depends on the flow of external resources, at least during the initial phase of the recovery. Without a significant increase in the available foreign exchange, output in all sectors, particularly in industry, would be severely constrained. This would not only endanger the

recovery prospects but also the stabilization efforts. In the recent Uganda Consultative Group meetings, donor representatives recognized the strength of the Government's program, and pledged financial support to match the first year's requirements both in terms of totals and quick disbursing assistance. However, there is still some element of risk associated with the timely disbursement of these commitments and the Government's procurement capability. Delays in disbursements would hamper the flow of essential imports vital for recovery.

102. Another issue related to the supply response concerns the capability of the industrial firms to recover and increase capacity utilization, even if foreign exchange is available. A smoothly functioning OGL system would facilitate the importation of strategic inputs by industrial firms, and help remove some of the uncertainty over the steady supply of certain categories of imports. A relatively large number of firms are positioned to take advantage of the new system, and may have the capacity to raise domestic resources. But a number of smaller firms may have difficulty and the Government's proposed "Special Credit Facility" would help ease this difficulty. Even though the Government is prepared to use resources from the Special Development Fund, the requirements of the stabilization program will limit the overall credit availability. Moreover, a number of publicly owned industrial enterprises need to be rehabilitated before they can efficiently engage in productive activities. The planned restructuring of the public enterprise sector would contribute to this.

103. The third potential risk is the degree of Government's political strength to carry out the reform package. Some of the agreed reforms, and the involvement of the World Bank and IMF, are contrary to earlier statements of some politicians. However, the Government has debated and experimented with a variety of policy options, and none have succeeded. The Government has learned from experience that earlier policies would not work and is ready to implement the kind of program agreed with the Bank and the IMF. This readiness will be sustained, provided the supply response is positive and quick. Without a timely supply response, the objectives of the stabilization program would be seriously jeopardized, and the Government's credibility and effectiveness would be eroded. On the security situation, there has been a vast improvement since this Government took over in January 1986. There is still, however, fighting in the northern part of the country, where remnants of the previous regimes' supporters are resisting NRA. Even though this trouble does not appear to be a threat to the stability of the Government, it remains costly for the budget and a distraction for the policy makers.

PART IV - BANK GROUP OPERATIONS

104. The International Development Association has provided three credits totalling US$192.5 million to support Uganda's reconstruction efforts in 1980, 1982, and 1984. These credits supported policy and institutional reforms, while helping meet urgent needs for rehabilitation of the economy. Through two credits (US$23.0 million) for technical assistance projects, in 1981 and in 1984, the Association has supported

rehabilitation of key government institutions. Although small in financial terms, these projects have provided essential strengthening of administrative/institutional capacity, facilitated project preparation and implementation, and supported training, both directly and through upgrading of facilities. Since 1980, fourteen credits totalling US$324.6 have assisted rehabilitation of Uganda's infrastructure, productive capacity and social services. In addition, Uganda also received 10 loans from the Bank totalling US$244.8 million for the development of common services (railways, ports, telecommunications and finance for industry) operated regionally for the three partner states of the former East African Community. The International Finance Corporation has also invested about US$12.8 million in four projects in Uganda since 1983, covering industrial finance and food production and processing (sugar and tea). Annex III contains a summary statement of Bank Loans, IDA Credits and IFC investments in Uganda as of May 31, 1987.

105. Implementation of IDA-financed projects in Uganda slowed down during the recent civil disturbances. After February 1986, implementation improved and US$77.7 million was disbursed in FY86, leaving a total of US$186.5 million undisbursed as of March 31, 1987. To expedite project implementation, and further accelerate disbursements Country Implementation Review (CIR) meetings will be convened annually.

106. The country assistance strategy for Uganda has three main elements: (a) urgent policy reform to restore macroeconomic stability; (b) rehabilitation of economic and social infrastructure; and (c) development-oriented investments and structural reforms to address longer-term growth objectives. Once appropriate policy reforms are underway, emphasis would be on the rehabilitation of the productive sectors, requisite infrastructure, and social services with the objective of restoring the economy to a fully-functioning level.

107. In terms of project lending operations, this means basically a resumption of activities in the pipeline. Project lending will continue to focus on the rehabilitation of the productive sectors and the alleviation of infrastructure bottlenecks as well as addressing the longer-term issues of agriculture research, population and natural resources management. To minimize the effects of the social costs of adjustments, we plan to increase our support for the social sectors to improve water supply, health and education services. Several operations call for financial resources well in excess of available IDA funds; coordination of cofinancing would remain a key aspect of the work program. CESW is designed to provide an analytical basis for addressing evident constraints to growth and recommending appropriate remedial action. Once clear plans of action are formulated, these would be supported through regular project activities and particularly through policy-based credits. The proposed credit would be the first of a series of policy-based credits, which have been programmed for each year through the fiscal year 1989/90. These credits, which may include sector operations, would address bottlenecks restricting the effectiveness of regular projects and rapid economic growth. Also, a technical assistance project is currently being prepared to provide assistance for the restructuring of the public enterprise sector, and the institutional changes in the Ministry of Finance.

108. At end-1986, the Bank Group accounted for 49.2 percent of Uganda's total external medium- and long-term debt outstanding and for 7.7 percent of its debt service. By 1990, the Bank Group's share in Uganda's total external debt is projected to rise to about 53 percent and its share in the debt service to about 14 percent.

109. The Bank chaired the Fourth Consultative Group Meeting for Uganda, which was held in Paris on June 11 and 12, 1987. The meeting agreed that the implementation of the Government's Economic Recovery Program would require, over the next few years, adequate levels of external assistance on concessionary terms including substantial amounts of balance of payments support. Aid indications made by members of the Group for the first year of the program exceeded initial estimates of the financing requirements for fiscal year 1987/88. The donors stressed the need to strengthen aid coordination and to closely review progress of the implementation of the Economic Recovery Program.

PART V - COLLABORATION WITH IMF

Fund Relations with Uganda

110. Between 1981 and 1984, the Fund approved three stand-by arrangements for Uganda. The last stand-by arrangement (SDR 95 million, or 95.4 percent of quota) was approved by the Executive Board in September 1983 in support of a financial program which covered fiscal year 1983/84. Uganda made three purchases totaling SDR 65 million under this arrangement before it became inoperative in March 1984. Between then and end-1986, with the exception of a few weeks in early 1986 during the civil war, Uganda maintained payments on its obligations to the Fund despite difficult circumstances and the lack of foreign assistance. As a result, during that period, Uganda reduced its net Fund credit by nearly SDR 168 million (168.7 percent of quota). As of December 31, 1986, the Fund's holdings of Uganda currency subject to repurchase totaled SDR 187.4 million (188.2 percent of quota). Between mid-January and end-April 1987, Uganda was continuously in arrears to the Fund. On May 21, 1987, Uganda settled these arrears, which, at that date, amounted to SDR 17.1 million, equivalent to 17.2 percent of quota, and has remained current in its financial obligations to the Fund since then.

111. On June 15, 1987, the Fund's Executive Board approved Uganda's request for arrangements under the Fund's Structural Adjustment Facility (SAF) and the first annual arrangement thereunder. Given present rules, total disbursements under the facility would amount to SDR 53.3 million (53.5 percent of Uganda's quota of SDR 99.6 million); the first disbursement is SDR 19.9 million, equivalent to 20 percent of quota. The first year of the program establishes quarterly benchmarks for total domestic bank credit and net bank credit to the Government. Quantitative benchmarks for the overall government budget deficit and new non-concessional foreign borrowing by the public sector have also been set. For policy benchmarks the introduction and quarterly enlargements of an OGL system, the implementation of an improved expenditure monitoring system, and the overhauling and streamlining of the civil service have been

decided. In the same meeting of the Executive Board, a purchase under the compensatory financing facility equivalent to SDR 25.0 million (25.1 percent of quota) was approved in respect of an export shortfall.

Bank-Fund Collaboration

112. The staff of the Bank have maintained close contact with the Fund staff working on Uganda, both sharing views and information, particularly on matters related to the Economic Recovery Credit and the Structural Adjustment Facility. The staff of both institutions have worked closely with each other and with the Ugandan authorities in developing the Policy Framework Paper (PFP). Missions from the Bank and Fund jointly visited Uganda in March 1987 to discuss and negotiate the PFP with the authorities, and the Fund resident representative in Kampala assisted in the appraisal mission for this credit in May-June 1987.

PART VI - RECOMMENDATION

113. I am satisfied that the proposed Development Credit would comply with the Articles of Agreement of the Association. I am also satisfied that the proposed African Facility Credit would comply with Resolution No. IDA 85-1 adopted on May 21, 1985 by the Executive Directors of the Association.

114. I recommend that the Executive Directors approve the proposed Development Credit and the proposed African Facility Credit and that the Association act as administrator of the proposed Special Joint Financing from the United Kingdom.

Barber B. Conable
President

Washington, D.C.
August 19, 1987

TELEGRAMS: "FINSEC."

TELEPHONE: MINISTER. KAMPALA 43054 & 32370.
OFFICE. KAMPALA 34700/9 (10 LINES.)

IN ANY CORRESPONDENCE ON THIS SUBJECT PLEASE QUOTE NO.....

THE REPUBLIC OF UGANDA

OFFICE OF THE
MINISTER OF FINANCE,
P.O. BOX 8147,
KAMPALA, UGANDA.

LETTER OF DEVELOPMENT POLICY

July 1, 1987

Mr. Barber Conable,
President,
International Development Association,
1818 H Street, N.W.,
Washington, D.C.
U.S.A.

Dear Mr. Conable,

The Government of Uganda requests a credit from the International Development Association (IDA) to support its Economic Recovery Program. The requested credit would enable the government to continue with various measures of adjustment already started and to undertake new initiatives. The government has already reached an understanding with the International Monetary Fund (IMF) on major macroeconomic policies. The IMF is supporting the Government's program with a Structural Adjustment Facility (SAF), which was approved by its Board on June 15, 1987. The IMF Board also approved a Compensatory Financed Facility (CFF) on the same date. It is the government's hope that additional resources from the World Bank and other multilateral and bilateral agencies will complement and hasten the pace of economic recovery now set in motion. I wish also at this juncture to complement the World Bank for convening the Consultative Group meeting for Uganda in Paris on 11th and 12th June, 1987, where Uganda's recovery program was discussed and appropriate support given. I believe that the role of the Bank as a close partner in development will continue and be enhanced.

Background

At the time of independence in 1962, Uganda was a country which seemed poised for rapid growth and expanding prosperity. As it turned out, however, none of these expectations materialised. Instead, the country has suffered a persistent and devastating process of economic decline rendering Uganda one of the poorest, least-developed countries in the World. The reasons for these disappointments have to do principally with the political mismanagement of Uganda's society and the resulting instability and violence, which since 1969, have prevailed in the country except for brief periods of respite. The result was a cumulative decline in real GDP of about 14 percent between 1970 and 1985. The manufacturing sector registered the sharpest decline of almost 60 percent over the same period making the country dependent on imports even for simple manufactured products.

When the National Resistance Movement (NRM) came to power in January 1986, the economy was in a critical condition. Much of the country had been devastated; the Luwero triangle, once among the richest areas, was nothing more than a wasteland, with most of its inhabitants either dead or displaced, and all infrastructure destroyed. Countrywide, there was a major transport bottleneck as large numbers of trucks were destroyed or stolen by the withdrawing forces of the previous regime. Roads, railways and telephone services were in a terrible state of disrepair. Manufacturing plants were either closed or operating at very low levels of capacity. Utilities such as power and water supply had severely deteriorated. Official foreign exchange reserves were only equivalent to about two weeks' "normal" imports of goods and services, and net foreign reserves were significantly negative. The new government also inherited a considerable external debt burden. Taking into account the debt to IMF, the total debt service scheduled for 1986 was equivalent to one half of the 1984/85 export of goods and services. Moreover, at end-1985, the stock of external arrears of medium- and long-term debt amounted to some US$63 million. Besides the economic breakdown, the country was faced with high degree of insecurity, and total disregard for human rights. But, however, caused, a country's socio-economic problems are primarily its responsibility and the government of Uganda is determined to undertake and is in fact already undertaking the measures needed to reverse the decline in the country's productive capacity.

Following the takeover of power therefore, the NRM Government moved rapidly to re-establish peace and security throughout Uganda, and an emergency plan was launched to bring assistance to those districts devastated by war and to assist resettling the returnees. The security situation is now very much improved in most parts of the country. The Government's relief and rehabilitation program has helped to revive economic activities in the devastated districts.

Overview of the Economic Recovery Program

Later in 1986, the Government began formulating a comprehensive program of economic recovery. The Government has had consultations on the formulation of this programme with the World Bank.

In broad terms, the objective of the Government's Economic Recovery Program is to achieve a rapid overall economic recovery and set the stage for sustained economic development. More specifically, the program aims at restoring relative price stability in the economy and a sustainable balance of payments position, improving capacity utilization in the production sectors, rehabilitating the existing infrastructure and the-installed capacity, restoring adequate incentives to producers through appropriate pricing policies and the use of markets, and improving public sector resource mobilization and allocation.

Macroeconomic Policies.

The Government has already begun the implementation of the Economic Recovery Program by introducing important policy reforms on May 15, 1987. These include a currency reform under which one new Uganda shilling replaced 100 old shillings, and a substantial depreciation of the exchange

rate to new U.Shs.60 per US dollar from the previous rate of old U.Shs.1400 per US dollar. This action is in line with the government's intention to maintain an active exchange rate management policy. This adjustment of the exchange rate has enabled the Government to restore price incentives for the production of tradeable goods and increase government revenue. With the announcement of the change in the exchange rate, the prices of petroleum products were also increased to levels consistent with world market prices. To reduce the high money supply which was in circulation a tax levy of 30 percent on cash holdings and bank deposits was applied during the currency reform exercise. Half of the proceeds of this tax will be used towards retiring the public debt while the other half will contribute to financing development projects.

The Government is committed to the pursuance of monetary and fiscal policies designed to reduce inflation and strengthen the balance of payments. To this end, the Government will reduce the fiscal deficit and restrain recourse to domestic monetary financing. The 1987/88 budget aims at a net reduction in the Treasury's indebtedness with the banking system. Interest rates would be maintained at levels reflecting the expected rate of inflation over the various loan and deposit maturities.

Sectoral Policies

We expect that the macroeconomic policies described above will establish the preconditions for economic recovery. The Government believes, that to induce a sustained supply response, these actions have to be followed by sector specific policies to address the underlying structural issues.

In the agricultural sector, the program seeks to achieve a significant expansion of production for export and domestic use. The Government believes in providing adequate price incentives to the producers of cash and foodcrops. Producer prices for coffee, cotton tobacco and tea were substantially increased in May 1987, the prices paid for robusta coffee was raised by 182 percent, for arabica coffee by 168 percent, cotton by 375 percent, tobacco by 280 percent and tea prices by 275 percent. The subsequently announced prices for major foodcrops also reflected significant increases. We intend to review agricultural producer prices next fall and, if necessary, make changes under an improved methodology to be adopted by the government.

We are also addressing the problems associated with the institutional constraints to increased agricultural production, in particular, the marketing and processing of coffee, tea, cotton, and certain foodcrops. The poor performance of the marketing boards and the irregularities in their management, have been recognized by the authorities. To improve the performance of these boards, we have recently replaced their management and improved procedures for expenditure control. The Government intends to take additional measures to improve the marketing arrangements in the country.

The Government has recently completed a review of the coffee marketing structure, and we are presently examining the recommendations of this review with a view to preparing an action plan for implementation. Among these recommendations, the most important are the introduction of a

tendering system to sell arabica coffee, the rationalization of hulleries, the reorganization of the Coffee Marketing Board, and the establishment of an effective information system for monitoring of coffee sales. In the area of lint marketing, by the beginning of the next crop season, cooperatives will be allowed to sell cotton directly to textile mills. By December 1987 Lint Marketing Board's interest in the oil and soap industry will be reduced to a minority position, thereby relieving the board from administration and management in this activity. The Government's declared policy in food marketing has been to licence the traders of five major food crops, but allow no restrictions to their free movement across the districts, except in emergency situations. Under the Program, we will monitor the free movement of foodcrops across districts. The Produce Marketing Board would continue to be the sole exporter of the five major foodcrops, but as the economic conditions improve, we intend to allow private exporters to export alongside the Produce Marketing Board.

With regard to agricultural credit, we have introduced a system of crop financing whereby credit is provided directly from the banks to those cooperatives and private buyers with adequate financial and accounting expertise. Once fully operational, this system should substantially improve the efficiency of crop financing, since the marketing boards would be relieved of the financial burden of supporting the unions and private processors and buyers. A program is in place with donor assistance to make the scheme fully operational, and we plan to review progress by December 1987 and, if necessary, take further action to accelerate its implementation.

In the industrial sector, the Government's objective is to rapidly increase capacity use through removing the import bottlenecks in the short-run, and to provide a more conducive policy environment for growth in the medium- to long-run. The improved macroeconomic policy environment, including the implementation of an active exchange rate management policy will be important to achieve this objective. However, during the early phase of program implementation, increased foreign exchange inflows are needed from external sources for the importation of essential goods, raw materials and spare parts to increase the capacity use in manufacturing plants and enable them to produce those goods currently in short supply.

To ensure a more efficient utilization of available foreign exchange, the Government has announced that the current foreign exchange allocation system which relies on administrative procedures would gradually be replaced with an Open General Licensing (OGL) system under which importers would obtain foreign exchange upon request. Because of the current scarcity of foreign exchange, however, initially the coverage of the OGL system would be limited to financing imports of intermediate goods and spare parts for priority sectors. A detailed design for OGL has been worked out and we expect the system to be in place by September 1987, when the foreign exchange scarcity should be somewhat eased. However, from the beginning OGL will cover a significant share of non-project related imports. The system would be reviewed by December 1987 with a view to expanding its coverage. We aim at extending the coverage of OGL to capital and intermediate goods, basic necessities and incentive goods by end-1988.

The Government is concerned about the ability of certain enterprises to raise sufficient working capital, particularly to raise local cover for imports, following the currency devaluation. This is especially relevant for those firms that are economically viable but for special circumstances may not be able to meet fully the normal lending criteria of commercial banks. To address this concern, the Government plans to set up a "special credit facility" to enable these firms to have access to commercial bank credit. Under the proposed facility, the commercial banks would handle all credit applications and would share the risk involved in lending with the Government. To this end, a fixed sum would be set aside by the Government to cover losses on default up to the pro-rata risk assumed by the Government. Credit extended under the facility would be subject to a fee. The facility would conform to the overall domestic credit ceilings established by the authorities and agreed upon with IMF.

The Government will continue to rely on markets and is committed to maintaining a policy environment free from unnecessary price fixing and control. Even though firms report to the Ministry of Industry and Technology for intended price changes, there are no formal mechanisms to set prices and impose price controls. The only exceptions are the prices of basic essential requirements by the population, viz, sugar, salt, and soap which, because of their widespread use and scarcity, will continue to be subject to guidelines.

The legislation regarding industrial licensing and foreign investment is currently being reviewed with the objective of avoiding delays in the procuring of applications for investment and encouraging potential investors. Even though industrial licenses for investment are liberally granted, we plan to revise the Industrial Licensing Act to shorten procedures including the exemption of small investments from the provisions of the Act, and create a more conducive environment for industrial growth. Preparations to this end will be completed by December 1987.

Public Enterprise Sector Restructuring

The Government gives primary importance to the restructuring and rehabilitation of the public enterprise sector. As a result of expropriations under previous regimes, a large number of industrial enterprises are now publicly owned. Most of these enterprises are working at less than 20 percent capacity and have incurred heavy operational losses in the past. This poor performance reflects not only the shortage of imported materials, but also lack of financial discipline, and deteriorated management quality and staff morale. The present Government's strategy is to reduce the size of the sector in order to lessen the burden of management and avoid the financial drain on public resources, while strengthening the mechanisms to improve efficiency.

More than 25 enterprises have already been returned to former owners and the government has wound up seven of its own. Currently, a Verification Committee is trying to settle the ownership conflicts, and a Board of Valuers to assess the value of plants and equipment has been set up. By December 1987, the verification of the ownership of a significant number of

industrial enterprises will be completed, and by December 1987 we will have a plan of action for the completion of the verification and valuation of all properties and enterprises, and for the return to former owners or sale of such properties. A committee recently established by the Prime Minister made its recommendations on divestiture to the President's Economic Council which, in turn, has appointed a sub-committee to prepare an action plan for divestiture. By end first quarter of financial year 1987/88, the action plan will be finalized regarding the restructuring of the public enterprise sector, and identifying both the industrial and non-industrial parastatals that would be subject to divestiture. In addition, a Public Enterprise Industrial Secretariat is being set up under the Ministry of Industry and Technology to establish mechanisms for improving the operational efficiency of the industrial sector. The key positions will be staffed and the Secretariat will be operational by December 1987.

The Uganda Development Corporation (UDC) will be reorganised and restructured to enable it to better identify new investment opportunities, bring together investors with managerial and technical skills and capital, participate in the development of these investments and support them with risk capital. As enterprises in its portfolio reach maturity, UDC will divest its ownership position and reinvest the proceeds in new ventures. By December 1987, the UDC restructuring plan, including portfolio strategy, financial strategy, organization and management, as well as a strategy for divestiture will be finalized, and approved by the UDC Board.

Public Resource Budgeting and Management.

Under the Economic Recovery Program, measures are being adopted to strengthen control over budgetary expenditures and limit the scope for unauthorized overspending. Rules are already in effect to disallow overdraft by spending ministries without authorization by the Treasury. The Government is also making plans to: strengthen the public enterprise monitoring unit in the Ministry of Finance; set up a central procurement body, improve the financial effectiveness of the Central Tender Board, and strengthen the financial management system.

Measures are being planned to increase budgetary revenues through improved tax administration, and through up-grading the staff of the three revenue departments, revamping their operational procedures and increasing the means at their disposal. In addition, a comprehensive study of the tax and tariff system is planned to determine changes that may be required to improve incentives, promoting resource efficiency. The study would be initiated by mid-December 1987 and completed by end-1988.

There is need to streamline the civil service to increase its efficiency. The salaries in the civil service, which have eroded dramatically in real terms, have been raised by 100 percent, effective June 1, 1987. Prior to the 1987/88 budget, a head count would be carried out to determine the total number of employees, including regular civil servants, contract employees and group employees, and to identify redundancies. Using the results of this census, before end-1987, we plan to significantly reduce the number of group employees. A comprehensive review of the functional and staffing structures of the entire civil service is also underway, with technical assistance from the World Bank. On the basis of this review's recommendations, there will be a major restructuring of the civil service.

Public Sector Investment Program

A medium-term public sector investment program has been prepared. The level of investment increases considerably over the next few years, and reflect Uganda's rehabilitation needs, its absorptive capacity, and the envisaged level of external financing. The emphasis in the program is on road rehabilitation and maintenance, power generation and transmission, and the provision of social infrastructure, particularly for health services. The World Bank has reviewed this program, and found the first year of the program which provides the basis for the next fiscal year's budget, consistent with resource availabilities and priorities set by the Government. The investment levels for the following three years of the program, however, are being reviewed by the Government. Agreement with the Bank on the size and composition of the public investment program covering 1988/89-1990/91 will be sought by December 1987.

Conclusion

The Government of Uganda is embarking on a major program of economic recovery. Important measures have already been taken, and in the context of the Economic Recovery Program, further policy and institutional reforms will be implemented. This program, however, can only succeed with the provision of quick-disbursing financial assistance. In this context, we are counting on World Bank assistance and requesting an Economic Recovery Credit in support of this program.

Yours sincerely,

DR. E.W.C.B. KIYONGA
MINISTER FOR FINANCE

UGANDA
MATRIX OF POLICY ACTIONS UNDER
THE ECONOMIC RECOVERY PROGRAM

Policy Area	Issues and Objectives	Measures Taken	Measures to be Taken	
			IMF SAF Program	Bank ERC
Macroeconomic Policies				
A. Exchange Rate and Trade Policies	It is essential to maintain an exchange rate policy consistent with the objectives of providing adequate price incentives for the production of tradeable goods, taking into account the exchange rate effect on the price of imported inputs and exports.	In the context of the currency reform (1 new USH replacing 100 old USh), the exchange rate was depreciated from $1 = old USh1400 to $1 = new USh60.	Mid year review of 1987-1988 program scheduled to take place before end-1987. Subsequent review in May-June 1988 during negotiations for second year program. The SAF program includes quarterly benchmarks for the build up of gross foreign reserves in 1987/88 and concomitant increases in net foreign assets of the Bank of Uganda.	Monitor developments in exchange rate in close coordination with IMF.
	Currently all foreign exchange is allocated administratively. The Government intends to optimise the allocation of foreign exchange among importers and improve the availability of imported inputs to priority sectors.	The basic design of an Open General Licensing (OGL) system has been worked out. Under OGL foreign exchange will be provided freely for eligible imports by priority industries.	Introduction and quarterly review of the OGL system with a view to enlarging it.	Introduction of a limited OGL system in September 1987 with participation open to all primary users of intermediate inputs and spare parts in high-priority industries. Initially the OGL system covers eligible imports for textiles, soap, beverages, and tobacco industries. Before second tranche, review the functioning of the OGL system with the aim of enlarging its coverage.

Policy Area	Issues and Objectives	Measures Taken	Measures to be Taken	
			IMF SAF Program	Bank ERC
B. Fiscal Policies	To restore the fiscal balance, the budget deficit must be reduced and recourse to monetary financing of the deficit must be avoided. The Government aims to limit fiscal deficit to ensure substantial repayment of net bank credit.	Adjustment in exchange rate will increase substantially revenues from export duty on coffee, despite real increase in producer's price (see below). Prices of petroleum products were increased significantly.	Overall budget deficit for 1987/88 on a commitment basis and including grants limited to USh 9.27 billion, approximately 4.5 percent of estimated GDP. Quarterly targets on net repayment of bank credit to the Government.	Initiate study on the tax and tariff system with the aim of improving incentives to producers, eliminate distortions in the structure of protection and reduce further tax dependency on duty levy on coffee exports.
	Effective expenditure controls must be established.	Spending ministries are disallowed making overdrafts without Treasury endorsement.	Ceiling of USh 14.16 billion on total recurrent expenditure in 1987/88, with quarterly benchmarks on recurrent expenditure and tax revenue. Closely follow policy implemetation ("policy benchmark") of an improved expenditure monitoring system.	Monitor implementation of fiscal policies in revenue collection and expenditure performance and monitoring.
	Revenue performance will be improved through improvement in tax administration. Overwhelming dependence on coffee export tax needs to be reduced.	Increase in the graduated tax on income; modifications to the customs duties inthe 1987/88 budget to eliminate exemptions that do not concern aid-financed items; measures to improve tax administration and to strengthen tax collection are being taken.	Increase collection of non-coffee taxes (see below). Second and third year programs to emphasize reduction of revenues on export duty on coffee, and further reductions in the share of the overall deficit in GDP.	

Policy Area	Issues and Objectives	Measures Taken	Measures to be Taken	
			IMF SAF Program	Bank ERC
C. Monetary and Credit Policies	Monetary expansion must be limited without undue restraint on credit to productive activities.	In the context of the currency reform, a 30 percent currency conversion tax on all liquidity was introduced to reduce the money supply.	Limit of USh 1 billion in the total expansion of net domestic credit between June 1987 and June 1988 (with a USh 1.9 billion cumulative reduction in net bank credit to Government). Quarterly benchmarks on net domestic credit and net bank credit to government. Consistent with the target for total domestic credit and net improvement in external assets, broad money supply is expected to increase by 40 percent from end-June 1987 to end-June 1988.	Monitor implementation of monetary policies.
	Steps need to be taken to move towards market determined interest rates.		Review current nominal interest rates. Adjust rates by end-1987 in the light of inflationary trends so as to re-establish positive real interest rates over the various loan and deposit maturities. Develop a secondary financial market for government bills, by end-1987.	Monitor trends in interest rates so as to re-establish in 1988, positive real rates over the various loan and deposit maturities. Move gradually towards a market determined interest rate, beginning with the rates in government paper.
	The Government wants to ensure that economically viable industrial firms in priority sectors are able to raise sufficient local cover for imports.	With Bank support, the design of a Special Credit Facility to provide short-term credit for local cover of imports has been worked out.		Set-up a Special Credit Facility to induce commercial banks to extend short-term import credit to economically viable borrowers who are unable to meet the cash-flow requirements demanded by commercial banks. The Facility will operate within the pre-established credit ceilings agreed upon in the SAF program. To reduce risk for banks, credit will be partially guaranteed by the Government through a specially created, non-replenishable, guarantee fund. Credit extended will be subject to a fee.

Policy Area	Issues and Objectives	Measures Taken	Measures to be Taken	
			IMF SAF Program	Bank ERC
Sectoral Policies				
D. Agricultural Sector	To encourage production and improve efficiency, pricing, marketing, and credit issues need to be addressed urgently. Incentives to produce has eroded drastically in recent years. Marketing boards for major crops have been crippled by poor management, financial indiscipline, and alleged corruption. Price incentives to the producers of cash crops need to be restored. While gradually liberalizing the marketing and exporting arrangements, efficient functioning of the marketing boards must be ensured. In the longer-term, in addition to marketing, pricing, and credit, issues related to manpower and training, land tenure, and agricultural research need to be tackled.	In May 1987, producer prices of coffee, tea and cotton were raised between 158 percent and 375 percent. Also producer prices for foodcrops were raised substantially. A new methodology for improved producer pricing has been developed by the Agricultural Task Forces and adopted by the Agricultural Policy Committee. A system for direct provision of bank credit to producers' cooperatives was introduced. The top managements of the Coffee Marketing Board and the Lint Marketing Boards werereplaced. Coffee producers' cooperatives were required to update and publish audited accounts. Agricultural Task Forces made recommendations to improve efficiency in coffee marketing.	Monitor policy implementation of reforms in the agricultural crop marketing system and maintenance of adequate producer prices for principal cash crops.	Adopt new methodology for producer pricing decisions. Review the producer prices for cash crops twice a year. The next review to take place in October-November 1987. New pricing decisions to be based on this methodology. In consultation with the Bank review and, if necessary, revise May 1987 producer prices based on new methodology. Review the performance of the system by December 1987. If necessary, take measures to accelerate implementation. Allow cotton producers' cooperatives to sell directly to textile mills, and reduce the interest of the Lint Marketing Board has in the oil and soap industry to a minority position by December 1987. Review the recommendations of the Agricutural Task Forces on coffee marketing, and prepare an action plan for implementation. Ensure the free movement of foodcrops among districts, except in emergency situations.

Policy Area	Issues and Objectives	Measures Taken	Measures to be Taken	
			IMF SAF Program	Bank ERC
E. Industrial Sector	Most plants are operating at extremely low capacity due to lack of imported inputs and spare parts. Additional foreign exchange is urgently needed for essential imports so that plants can rapidly improve capacity use and produce goods in short supply. Also the scarce foreign exchange needs to be allocated efficiently. The Government maintains a policy environment basically free from unnecessary interventions. However, industrial licensing system is cumbersome.	Preparations for OGL and the Special Credit Facility that will encourage capacity use have been underway. The regulations on industrial licensing and foreign investment are currently underway.		Formally launch the OGL system and the Special Credit Facility, and ensure their proper functioning. Maintain the present policy not to interfere with the market-determined prices. Make the necessary revision in the Industrial Licensing Act, including the exemption of small investments from the provisions of the Act.
F. Transport Sector	Improve the shortages for trucks and road maintenance equipment. Repair and rehabilitate the major roads.	Two studies on the transportation sector sponsored by the Bank the the UNDP were undertaken. Trucks and equipment were ordered, some of which have arrived.		Draw government's strategy and plans in the transport sector based on the two studies. Continue to repair and build major roads, and take further action to fill gaps in truck and road equipment requirements.

Policy Area	Issues and Objectives	Measures Taken	Measures to be Taken	
			IMF SAF Program	Bank SRC
Public Sector Resource Management and Allocation				
G. Public Resource Budgeting and Management	Given the almost complete breakdown in sales and income tax collection, improvement in tax administration is essential.		Strengthen tax administration by upgrading the staffing in the departments of Income Tax, Customs and Excise Tax and Inland Revenue, and by revamping their operational procedures. Introduce a system of merit incentives to motivate tax-collecion officers.	
	In the medium- to long-term the tax and tariff system need to be examined closely with a view to improve tax buoyancy, incentives to produce, and more efficient resource allocation.		Ensure compliance to the existing tax laws and regulations.	Initiate a comprehensive tax and tariff study by end-1987 and finalize it by end-1988.
	Budgetary discipline needs to be restored through strengthened institutions and improved procedures.	Preparations underway at the Ministry of Finance.	Strengthen monitoring and accounting procedures.	Overhaul the Central Tender Board; set-up Central Procurement body; strengthen parastatal financial monitory unit, set-up a financial management system.
	Civil service will be streamlined to increase efficiency and limit the wage bill.	Project to review functional and staffing requirements has been launched. A census of the civil service has been undertaken.	Cut the number of group (temporary) employees significantly before end-1987.	Monitoring of measures regarding the reform of the civil service. Reduction in the number of group employees.
	Functional and staffing structures of the key ministries need to be examined and reorganized.			Substantial progress on the project reviewing functional and staffing requirements in civil service. Initiate implementation of measures in those Ministries for which the reorganization proposals have been concluded.

Policy Area	Issues and Objectives	Measures Taken	Measures to be Taken	
			IMF SAF Program	Bank ERC
H. Public Enterprise and Reform Divestiture	Restructuring and rehabilitation of the public enterprise sector is essential for sustained industrial growth. Public enterprises, most of which owned by the Government as a result of expropriations under previous regimes, are operating at extremely low capacity and most have been making losses. Excessive political interference in the past, lack of financial discipline, and deteriorated management quality and staff morale are issues. Divestiture is necessary to reduce Government's administrative and financial burden. It is also necessary to improve the efficiency in those enterprises retained by the Government.	A task force on the restructuring of the public enterprise sector prepared recommendations that are currently being reviewed by the Presidential Economic Council. The ownership issue of some twenty-five enterprises was settled with former owners. Institutional mechanisms were set up to sort out the legal and financial problems associated with the divestiture process. Preparations for setting-up a Public Enterprise Secretariat have reached an advanced stage. A comprehensive restructuring plan for the Uganda Development Corporation (UDC) is underway.	Monitor policy implementation and actions towards the rehabilitation and restructuring of parastatals.	Before second tranche release finalize the restructuring plan for public enterprises, and decide on enterprises to be divested, retained, and to be closed: Also finalize the verification of the ownership of a significant number of industrial enterprises and, by December 1987, prepare a plan of action for the completion of the verification and valuation of all properties and enterprises and for the return to former owners or sale of such properties and enterprises. Finalize setting up the Public Industrial Enterprise Secretariat as an advisory agency for restructuring. Complete the recruitment of the key staff for the Secretariat, before December 1987.
I. Public Sector Investment Program	To prepare and implement a public sector investment program consistent with resource availabilities and the rehabilitation needs of the economy.	The Government has prepared a medium-term investment program covering 1987/88 to 1990/91.		Finalize UDC restructuring plan, including the portfolio strategy, financial strategy, organization and management by December 1987.

ANNEX III
Page 1 of 2

THE STATUS OF BANK GROUP OPERATIONS IN UGANDA

A. STATEMENT OF BANK LOANS AND IDA CREDITS AS OF MAY 31, 1987

Loan or Credit No.	Year	Borrower	Purpose	Amount in US$ million (Less Cancellations) Bank	IDA	Undisbursed
One (1) loan and thirteen (13) credits fully disbursed				8.40	261.45 1/	
1248-UG	1982	Uganda	Industrial Rehabilitation		35.00	25.16
1328-UG	1983	Uganda	Agricultural Rehabilitation		70.00	41.46
1329-UG	1983	Uganda	Third Education		32.00	1.34
1367-UG	1983	Uganda	Posts and Telecommunications Rehabilitation		22.00	1.30
1434-UG	1984	Uganda	Second Technical Assistance		15.00	13.70
1445-UG	1984	Uganda	Third Highway		58.00	66.91
1510-UG	1985	Uganda	Water Supply and Sanitation Program		28.00	18.98
1539-UG	1985	Uganda	Agricultural Development		10.00	11.96
1560-UG	1985	Uganda	Second Power		28.80	35.27
1561-UG	1985	Uganda	Petroleum Exploration Promotion		5.10	6.21
1803-UG	1987	Uganda	Fourth Highway		18.00	18.14
			Total	8.40	583.35	240.43
			of which has been repaid	.08	3.85	
			Total now outstanding	8.32	587.20	
			IDA amount sold: 17.50			
			of which has been repaid 17.50			
TOTAL NOW HELD BY BANK AND IDA				8.32	587.20 1/	
TOTAL UNDISBURSED				0.00	240.43	

1/ Includes exchange rate adjustment.

B. STATEMENT OF IFC INVESTMENTS

AS OF MAY 31, 1987

Fiscal Year	Obligor	Type of Business	Amount in US$ million		
			Loan	Equity	Total
1983	Toro and Mityana Tea Co., Ltd. (TAMTECO)	Food and Food Processing	1.76	-	1.76
1983	Sugar Corp. of Uganda	Food and Food Processing	8.00	-	8.00
1984	Uganda Tea Corp. Ltd.	Food and Food Processing	2.75	-	2.75
1984	Development Finance Company of Uganda	Development Finance	-	0.38	0.38
	Total gross commitments now held by IFC		12.51	0.38	12.89
	Total undisbursed (including) participants portion)		6.74	0.27	7.01

Source: IFC Disbursements Section

Table 1: Uganda - Key Indicators
(in percent or percent per year)

	Actual		Estimated		Projected			
	1983	1984	1985	1986	1987	1988	1989	1990
GDP Growth Rate 1/		3.1%	-12.4%	11.4%	3.8%	5.2%	5.0%	5.0%
GDY Growth Rate		5.0%	-14.9%	14.6%	2.0%	5.4%	4.8%	5.1%
GDY/capita Growth Rate		1.9%	-17.3%	11.2%	-0.9%	2.4%	1.8%	2.1%
Consumption/capita Growth Rate		-6.7%	-12.9%	12.6%	-0.4%	0.6%	0.4%	0.3%
Scheduled Debt Service (in US$)	-121.31	-159.06	-201.72	-223.28	-222.84	-202.53	-170.44	-128.39
Of which M&LT	-81.57	-86.28	-106.17	-115.04	-120.69	-118.47	-105.66	-92.55
Scheduled Debt Service/XGS	31.6%	35.5%	54.8%	50.8%	62.7%	46.0%	35.0%	24.3%
Of which M&LT	21.2%	19.3%	28.9%	26.2%	33.9%	26.8%	21.6%	17.4%
Scheduled Debt Service/GDP	-3.5%	-4.4%	-6.4%	-6.3%	-6.1%	-5.3%	-4.2%	-3.0%
Scheduled Debt Service/GDP-Current	-3.5%	-7.0%	-8.6%	-6.4%	-7.0%	-6.4%	-5.3%	-3.7%
Scheduled Debt Service/GDP-US$ 2/		-4.9%	-8.1%	-8.1%	-6.9%	-5.7%	-4.9%	-3.6%
Gross investment/GDP-Current	12.1%	19.6%	14.9%	13.9%	17.4%	19.3%	19.9%	20.2%
Domestic savings/GDP-Current	8.4%	19.8%	12.9%	10.8%	10.9%	11.9%	12.8%	14.4%
National savings/GDP-Current	10.2%	21.3%	14.7%	13.9%	13.2%	14.1%	15.6%	17.6%
Marginal national savings rate-Current		46.8%	7.2%	13.9%	12.8%	16.5%	21.5%	30.1%
Public investment/GDP-Current	1.7%	3.8%	2.5%	3.3%	4.2%	7.8%	7.9%	7.2%
Public savings/GDP-Current	-1.8%	-3.6%	-1.8%	-4.1%	0.4%	4.6%	5.4%	4.0%
Private investment/GDP-Current	10.4%	15.8%	12.4%	10.6%	13.2%	11.5%	12.0%	13.0%
Private savings/GDP-Current	10.2%	23.4%	14.7%	14.9%	10.5%	7.3%	7.4%	10.3%
Ratio of public/private investment	15.9%	23.8%	20.5%	30.9%	31.6%	67.6%	66.1%	55.5%
Ratio of public/total investment	13.7%	19.3%	17.0%	23.6%	24.1%	40.3%	39.8%	35.7%
Government revenues/GDP	13.0%	19.1%	14.4%	7.8%	6.7%	11.7%	11.9%	11.9%
Government expenditures/GDP	16.5%	26.5%	20.4%	16.9%	11.5%	16.2%	15.7%	15.7%
Deficit (cont.)/GDP	-3.5%	-7.4%	-5.9%	-9.1%	-4.8%	-4.4%	-3.8%	-3.8%
Govt. revenues/GDP Fiscal year 3/	15.0%	12.8%	11.0%	4.4%	10.7%	11.6%	11.0%	
Govt. expend./GDP Fiscal year 3/	17.8%	18.1%	15.5%	10.6%	15.2%	15.5%	14.3%	
Deficit (cont.)/GDP Fiscal year 3/	-2.8%	-5.3%	-4.5%	-6.2%	-4.5%	-3.9%	-3.3%	
Export growth rate (US$)		16.5%	-17.9%	19.4%	-19.1%	24.1%	10.7%	8.8%
Exports/GDP	11.0%	19.7%	15.7%	12.6%	11.2%	14.0%	15.1%	15.4%
Import growth rate (US$)		-8.6%	-8.0%	27.3%	2.4%	17.9%	5.1%	1.8%
Imports/GDP	15.8%	22.2%	19.9%	17.0%	19.1%	22.6%	23.3%	22.1%
Current Account (US$)	-44.81	39.16	-4.68	-0.99	-133.00	-162.61	-138.00	-90.65
Current Account/GDP	-1.8%	1.7%	-0.2%	0.0%	-4.2%	-5.2%	-4.3%	-2.6%

1/ Because of the weakness of GDP data, indicators expressed as ratios to GDP should be treated with caution.
2/ Using the World Development Report standard convertion formula.
3/ Fiscal year begins July 1. Entries refer to the fiscal year beginning in the reference year.

Table 2: Uganda - External Financing Requirements, 1987 - 1990
(in millions of US$)

	Actual		Estimated		Projected			
	1983	1984	1985	1986	1987	1988	1989	1990
Current account (excl/off transf)	-102.6	-29.9	-54.3	-26.4	-175.5	-205.1	-180.5	-147.6
Amortization	-64.7	-54.5	-79.2	-86.5	-91.2	-88.4	-74.7	-60.1
Change in foreign arrears	-87.8	-86.9	7.9	27.8	-28.5	0.0	0.0	0.0
Change in foreign reserves 1/	-37.6	-5.4	-0.3	0.3	-27.1	-10.0	-20.0	-50.0
Repurchases to IMF	-12.7	-38.7	-64.1	-81.5	-77.9	-66.4	-53.8	-30.1
Total financing requirement	-305.3	-215.4	-189.9	-166.4	-400.2	-369.9	-329.0	-287.8
Disbursements: Existing commitments								
Total	217.5	151.6	189.9	166.4	144.7	168.3	146.1	80.2
Official grants	37.7	69.1	49.6	25.5	38.3	29.8	21.3	11.4
MLT loans	93.4	88.2	108.1	118.9	127.6	119.4	105.6	49.6
of which: IDA	32.6	58.3	91.7	62.4	55.6	51.8	36.8	28.0
of which: Private sources	27.6	14.8	13.9	27.1	15.1	4.3	2.3	0.2
Purchases from IMF	97.2	22.3	0.0	0.0	0.0	0.0	0.0	0.0
Short term & other capital (net)	-10.9	-28.0	32.2	22.0	-21.2	19.2	19.2	19.2
Disbursements: Expected new commitments								
Total					141.5	170.4	165.3	207.9
Grants					4.3	12.8	21.3	45.6
MLT loans					80.0	140.9	127.2	162.4
of which: IDA-projects					7.7	18.9	28.6	40.2
of which: IDA-program					50.0	73.3	26.7	33.3
of which: Private guaranteed					7.3	11.9	16.2	19.7
Purchases from IMF (CFF)					32.3	0.0	0.0	0.0
SAF					24.9	16.8	16.8	0.0
Short term and other capital (net)					0.0	0.0	0.0	0.0
Total identified financing	217.5	151.6	189.9	166.4	286.2	338.7	311.4	288.1
Financing gap	87.8	63.8	0.0	0.0	114.0	31.2	17.6	-0.3
Debt rescheduling	87.7	63.8	0.0	0.0	114.0	31.3	17.9	0.0
To be financed	0.0	0.0	0.0	0.0	0.0	-0.1	-0.2	-0.3

Table 3: Balance of Payments Projections
(In millions of U.S. dollars)

	Actual		Estimated		Projected			
	1983	1984	1985	1986	1987	1988	1989	1990
CURRENT ACCOUNT	-102.6	-29.9	-54.3	-26.4	-175.5	-205.1	-180.5	-147.6
Trade balance	-60.4	36.6	7.8	-77.3	-169.9	-193.1	-185.7	-154.7
Exports, f.o.b.	367.7	407.3	341.5	414.2	332.4	416.5	462.1	503.7
Of which: coffee	339.7	374.4	321.0	386.0	302.5	363.6	384.4	403.6
tea	1.2	3.2	1.6	3.5	4.4	5.6	7.4	10.1
cotton	12.4	11.4	14.6	5.4	5.9	11.4	17.7	21.9
other	14.3	18.3	4.4	19.3	19.6	35.8	52.6	68.0
Imports,c.i.f.	428.1	370.7	333.7	491.5	502.3	609.6	647.8	658.4
Of which: oil	104.7	75.0	76.7	53.5	56.9	56.1	59.1	62.4
from loans	118.5	134.2	141.1	135.9	168.0	236.9	226.7	216.5
other imports	139.1	133.6	54.5	157.5	192.9	238.3	262.9	277.1
Services (net)	-107.9	-93.9	-104.7	-75.0	-80.6	-80.2	-77.0	-78.4
Non-factor services	-69.2	-33.1	-55.2	-32.3	-36.6	-39.5	-43.8	-49.0
Factor services	-38.7	-60.8	-49.5	-42.7	-44.0	-40.7	-33.2	-29.4
EAC interest	0.0	5.1	8.9	8.2	6.9	5.6	4.3	3.0
Unrequitted transfers	65.8	27.4	42.6	125.9	75.0	68.2	82.2	85.4
OFFICIAL GRANTS	37.7	69.1	49.6	25.5	42.5	42.5	42.5	57.0
CAPITAL ACCOUNT	17.9	5.7	61.1	54.4	95.3	191.0	177.3	171.0
Official MLT (net)	28.7	33.7	28.9	32.4	116.5	171.8	158.2	151.8
Disbursements	93.4	88.2	108.1	118.9	207.7	260.2	232.9	212.0
Existing commitments					127.6	119.4	105.6	49.6
From new commitments					80.0	140.8	127.2	162.4
Amortizations	-64.7	-54.5	-79.2	-86.5	-91.2	-88.4	-74.7	-60.1
EAC payments	0.0	0.6	18.8	18.8	18.8	18.8	18.8	18.8
Short term & other (net)	-10.9	-28.6	13.4	3.1	-40.1	0.4	0.4	0.4
Advance sales coffee (net)		-46.7	32.2	12.0	-40.4	0.0	0.0	0.0
Receipts		10.3	40.2	74.0	0.0	0.0	0.0	0.0
Payments		-56.9	-8.0	-62.1	-40.4	0.0	0.0	0.0
OVERALL BALANCE	-46.9	44.9	56.4	53.4	-37.7	28.4	39.3	80.4
FINANCING	46.9	-44.9	-56.4	-53.4	37.7	-28.4	-39.3	-80.4
External arrears	-87.8	-86.9	7.9	27.	-28.5	0.0	0.0	0.0
Monetary authorities	46.9	-21.8	-64.4	-81.2	-72.7	-76.4	-73.8	-80.1
Gross reserves change	-28.2	16.8	29.6	0.8	-27.1	-10.0	-20.0	-50.0
IMF (net)	84.5	-16.4	-64.1	-81.5	-45.6	-66.4	-53.8	-30.1
Other (net)	-9.4	-22.3	-29.8	-0.5	0.0	0.0	0.0	0.0
Financing Gap	87.7	63.8	0.0	0.0	138.9	48.0	34.4	-0.3
Debt relief	87.7	63.8	0.0	0.0	114.0	31.3	17.9	0.0
SAF					24.9	16.8	16.8	0.0
To be funded					0.0	-0.1	-0.2	-0.3
Memorandum items:								
Change in net reserves (US$mill)	-56.3	-0.5	34.5	80.7	72.7	76.4	73.8	80.1
Change in net reserves (SDR$mill)	-53.8	-0.5	31.4	65.9	55.9	58.8	56.8	61.6
Gross reserves (US$mill)	70.1	53.3	23.7	22.9	50.0	60.0	80.0	130.0
Coverage of imports (months)	2.0	1.7	0.9	0.6	1.2	1.2	1.5	2.4
Coffee exports (000 tons)	144.6	133.4	151.7	140.9	147.2	159.7	163.4	166.3
Coffee export price (USc/Kg)	235.0	280.6	211.6	274.0	205.5	227.7	235.3	242.7
Rescheduling: Amortizations	0.0	0.0	0.0	0.0	12.4	26.4	15.4	0.0
Interests	0.0	0.0	0.0	0.0	9.9	4.9	2.5	0.0
Arrears	40.9	10.9	0.0	0.0	91.8	0.0	0.0	0.0
Total	40.9	10.9	0.0	0.0	114.0	31.3	17.9	0.0
Debt forgiveness	46.8	52.9	0.0	0.0	0.0	0.0	0.0	0.0

Table 4: Investment and Savings: 1983 - 1990
(In percentages of estimated GDP at current prices)

	Actual		Estimated		Projected			
	1983	1984	1985	1986	1987	1988	1989	1990
Total consumption	91.6%	77.3%	88.5%	87.4%	89.0%	87.7%	87.0%	85.2%
Government	1.2%	18.2%	13.0%	8.9%	5.7%	6.4%	5.2%	6.3%
Private	90.4%	59.1%	75.5%	78.5%	83.3%	81.3%	81.8%	79.0%
Gross capital formation	12.1%	19.6%	14.9%	13.9%	17.4%	19.3%	19.9%	20.2%
Government	1.7%	3.8%	2.5%	3.3%	4.2%	7.8%	7.9%	7.2%
Private	10.4%	15.8%	12.4%	10.6%	13.2%	11.5%	12.0%	13.0%
Total absorption	103.7%	96.9%	103.4%	101.3%	106.4%	107.0%	106.9%	105.5%
Government	2.9%	22.0%	15.5%	12.2%	9.9%	14.2%	13.1%	13.5%
Private	100.8%	74.9%	87.9%	89.1%	96.5%	92.8%	93.8%	92.0%
Gross national savings	10.2%	21.3%	14.7%	13.9%	13.2%	14.1%	15.6%	17.6%
Domestic Savings	8.4%	19.8%	12.9%	10.8%	10.9%	11.9%	12.8%	14.4%
Of which: Government	-1.8%	-3.6%	-1.8%	-4.1%	0.4%	4.6%	5.4%	4.0%
Of which: Private	10.2%	23.4%	14.7%	14.9%	10.5%	7.3%	7.4%	10.3%
Gross foreign savings	1.8%	-1.7%	0.2%	0.0%	4.2%	5.2%	4.3%	2.6%
Net disbursements M&LT loans	0.8%	1.5%	2.1%	1.5%	5.1%	6.6%	6.0%	4.9%
Short term flows	-0.3%	-1.3%	0.6%	0.1%	-1.3%	0.0%	0.0%	0.0%
Change in net foreign assets	1.3%	-2.0%	-2.4%	-1.5%	0.4%	-1.4%	-1.7%	-2.3%
Of which: Net IMF	2.4%	-0.7%	-2.7%	-2.3%	-1.4%	-2.1%	-1.7%	-0.9%
Of which: Change in reserves	-0.8%	0.7%	1.3%	0.0%	-0.9%	-0.3%	-0.6%	-1.4%
Of which: Mon. Auth. - Other	-0.3%	-1.0%	-1.3%	0.0%	0.0%	0.0%	0.0%	0.0%
Of which: Change in arrears	-2.5%	-3.8%	0.3%	0.8%	-0.9%	0.0%	0.0%	0.0%
Of which: Excep. financing	2.5%	2.8%	0.0%	0.0%	3.6%	1.0%	0.6%	0.0%
Net transfers from abroad	3.7%	-0.2%	2.0%	3.1%	6.5%	7.4%	7.1%	5.9%
Factor service income	-1.1%	-2.7%	-2.1%	-1.2%	-1.4%	-1.3%	-1.0%	-0.9%
Current transfers & grants	3.0%	4.2%	3.9%	4.3%	3.7%	3.5%	3.7%	4.1%
Gross foreign savings	1.8%	-1.7%	0.2%	0.0%	4.2%	5.2%	4.3%	2.6%
Memorandum items:								
Real growth rates								
Total consumption		-3.9%	-10.3%	15.9%	2.6%	3.6%	3.4%	3.3%
Gross capital formation		39.9%	-29.9%	19.1%	22.4%	14.7%	7.9%	7.6%
Gross national savings		129.3%	-43.0%	6.6%	-1.9%	12.2%	15.1%	13.9%
Trends in real values (1983 = 100)								
Total consumption	100.0	96.1	86.2	99.9	102.5	106.3	109.8	113.5
Gross capital formation	100.0	139.9	98.1	116.8	142.9	163.9	176.8	190.7
Gross national savings	100.0	229.3	130.7	139.4	136.7	153.3	176.5	209.7
Marginal savings rates (in current prices with reference to GDP)								
Gross national savings		42.8%	7.6%	13.5%	12.9%	16.3%	21.6%	29.7%
Gross domestic savings		41.7%	5.5%	9.8%	11.0%	14.3%	16.2%	23.8%

Table 5: Exports, Imports and Terms of Trade: 1983 - 1990
(Bases in US$ values)

	Actual		Estimated		Projected			
	1983	1984	1985	1986	1987	1988	1989	1990
(In US$ million)								
Merchandise Exports	367.7	407.3	341.5	414.2	332.4	416.5	462.1	503.7
Coffee	339.7	374.4	321.0	386.0	302.5	363.6	384.4	403.6
Cotton	12.4	11.4	14.6	5.4	5.9	11.4	17.7	21.9
Tea	1.2	3.2	1.6	3.5	4.4	5.6	7.4	10.1
Tobacco	0.9	1.5	1.0	1.0	1.6	1.9	2.2	3.1
Other	14.5	16.8	12.9	18.3	18.0	33.9	50.4	64.9
Adjustment	-1.1	0.0	-9.5	0.0	0.0	0.0	0.0	0.0
Merchandise Imports	428.1	370.7	333.7	491.5	502.3	609.6	647.8	658.4
Petroleum products	104.7	75.0	76.7	53.5	56.9	56.1	59.1	62.4
Cash imports	146.6	143.2	110.5	157.5	192.9	238.3	262.9	277.1
Imports M&LT loans and grants	118.5	134.8	159.9	154.7	185.0	253.8	243.6	233.4
Other	53.3	17.7	-13.4	125.9	67.5	61.4	82.2	85.4
(1983 = 100)								
Merchandise Exports - Volume	100.0	94.2	103.6	97.6	102.3	115.6	123.0	128.6
Coffee	100.0	92.3	104.9	97.5	101.8	110.5	113.0	115.1
Cotton	100.0	94.7	131.5	67.2	74.7	141.9	212.8	255.4
Tea	100.0	192.3	107.7	226.1	263.0	315.6	394.5	512.9
Tobacco	100.0	186.0	118.5	128.4	204.3	242.1	279.9	378.2
Other	100.0	118.6	106.9	107.8	109.9	178.9	237.7	280.0
Merchandise Exports - Prices	100.0	117.5	89.6	115.4	88.4	98.0	102.2	106.5
Coffee	100.0	119.4	90.0	116.6	87.4	96.9	100.1	103.3
Cotton	100.0	97.3	39.1	64.8	64.1	64.9	66.9	69.0
Tea	100.0	138.7	123.4	127.8	138.2	147.1	155.9	164.7
Tobacco	100.0	88.6	89.0	88.8	87.1	87.1	87.1	89.7
Other	100.0	97.5	83.3	117.1	112.8	130.6	146.1	160.0
Merchandise Imports - Volume	100.0	88.0	79.6	118.3	135.5	151.2	152.0	150.0
Petroleum products	100.0	72.1	75.1	101.1	118.3	113.5	115.8	118.1
Cash imports	100.0	99.5	77.2	97.3	116.6	139.9	149.8	153.3
Imports M&LT loans and grants	100.0	115.8	137.3	121.4	190.1	228.1	203.3	189.4
Merchandise Imports - Prices	100.0	98.4	97.9	98.1	88.5	95.7	101.0	104.1
Petroleum products	100.0	99.4	97.5	50.5	46.0	47.2	48.8	50.4
Cash imports	100.0	98.2	97.7	110.4	112.8	116.2	119.7	123.3
Imports M&LT loans and grants	100.0	98.2	97.7	110.4	112.8	116.2	119.7	123.3
Memorandum items:								
Terms of trade index (1983 = 100)	100.0	119.4	91.6	117.7	99.9	102.4	101.1	102.3

Table 6: External Public Debt: 1983 - 1990
(US$ million)

	Actual		Estimated		Projected			
	1983	1984	1985	1986	1987	1988	1989	1990
COMMITMENTS	291.3	274.0	62.3	74.1	284.2	208.9	199.5	208.6
Concessionary	149.3	204.2	44.8	48.0	228.0	182.9	171.2	177.9
of which IDA:	120.8	148.1	44.9	33.9	143.0	100.0	85.0	105.0
of which gap financing	0.0	0.0	0.0	0.0	24.9	16.8	16.8	0.0
of which SAF	0.0	0.0	0.0	0.0	24.9	16.8	16.8	0.0
Non concessionary	44.9	47.5	17.5	26.0	23.9	26.0	28.2	30.7
Use of IMF credit	97.2	22.3	0.0	0.0	32.3	0.0	0.0	0.0
DISBURSEMENTS	190.6	110.5	108.1	118.9	264.9	277.0	249.7	212.0
Concessionary	53.6	63.0	80.6	62.2	176.6	219.3	188.2	150.4
of which IDA:	32.6	58.3	91.7	62.4	113.3	144.0	92.0	101.6
of which gap financing	0.0	0.0	0.0	0.0	24.9	16.8	16.8	0.0
Non concessionary	39.9	25.2	27.5	56.8	56.0	57.7	61.5	61.6
Use of IMF credit	97.2	22.3	0.0	0.0	32.3	0.0	0.0	0.0
From existing commitments	190.6	110.5	108.1	118.9	159.9	119.4	105.6	49.6
From new commitments	0.0	0.0	0.0	0.0	104.9	157.6	144.0	162.3
SCHEDULLED DEBT SERVICE	-121.3	-159.1	-201.7	-223.3	-222.8	-202.8	-170.9	-129.0
Principal repayments	-77.4	-93.1	-143.3	-168.0	-169.1	-154.8	-128.5	-90.2
of which IMF repurchases	-12.7	-38.7	-64.1	-81.5	-77.9	-66.4	-53.8	-30.1
Interest payments	-43.9	-65.9	-58.4	-55.3	-53.8	-48.0	-42.4	-38.8
of which IMF charges	-27.0	-34.1	-31.5	-26.8	-24.2	-17.8	-11.2	-6.1
of which interest on gap	0.0	0.0	0.0	0.0	0.0	-0.1	-0.2	-0.3
NET TRANSFER	69.3	-48.6	-93.6	-104.3	42.0	74.2	78.8	83.0
of which M&LT loans	11.8	1.9	1.9	3.9	87.0	141.7	127.2	119.4
of which IMF	57.4	-50.5	-95.6	-108.2	-69.9	-84.2	-65.0	-36.1
of which gap financing	0.0	0.0	0.0	0.0	24.9	16.7	16.6	-0.3
RESCHEDULLED DEBT SERVICE					-200.6	-171.4	-153.0	-129.0
Principal repayments					-156.7	-128.4	-113.1	-90.2
of which IMF repurchases					-77.9	-66.4	-53.8	-30.1
Interest payments					-43.9	-43.1	-39.9	-38.8
of which IMF charges					-24.2	-17.8	-11.2	-6.1
of which interest on gap					0.0	-0.1	-0.2	-0.3
NET TRANSFER					64.3	105.5	96.6	83.0
of which M&LT loans					109.2	173.0	145.1	119.4
of which IMF					-69.9	-84.2	-65.0	-36.1
of which gap financing					24.9	16.7	16.6	-0.3
MEMORANDUM ITEMS								
Debt Outstanding & Disbursed	1071.2	1084.3	1071.0	1068.3	1181.8	1358.0	1467.1	1614.4
Use of Fund credit	447.8	409.1	345.0	263.6	185.6	119.2	65.5	35.4
Undisbursed debt	449.8	569.2	541.6	450.3	419.7	297.6	259.5	230.5
Level of arrears	224.3	84.5	92.4	120.2	-0.1	-0.1	-0.1	-0.1
Schedulled Debt service ratio	31.6%	35.5%	54.8%	50.8%	62.7%	46.0%	35.0%	24.3%
of which IMF	10.3%	16.2%	26.0%	24.6%	28.7%	19.1%	13.3%	6.9%
of which gap financing	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	0.1%
Interest ratio	11.4%	14.7%	15.9%	12.6%	15.1%	10.9%	8.7%	7.3%
Rescheduled Debt service ratio					56.4%	38.9%	31.3%	24.3%

ANNEX V

UGANDA
ECONOMIC RECOVERY CREDIT

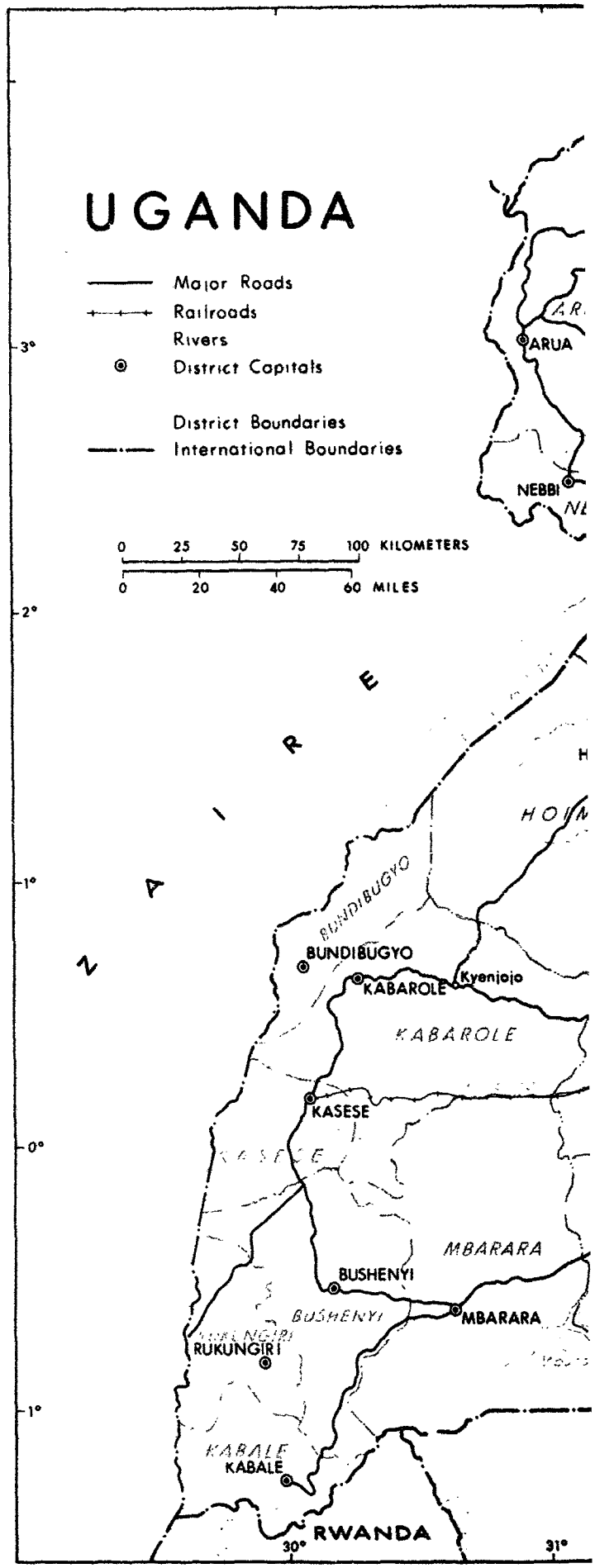
Supplementary Project Data Sheet

I. Timetable of Key Events:

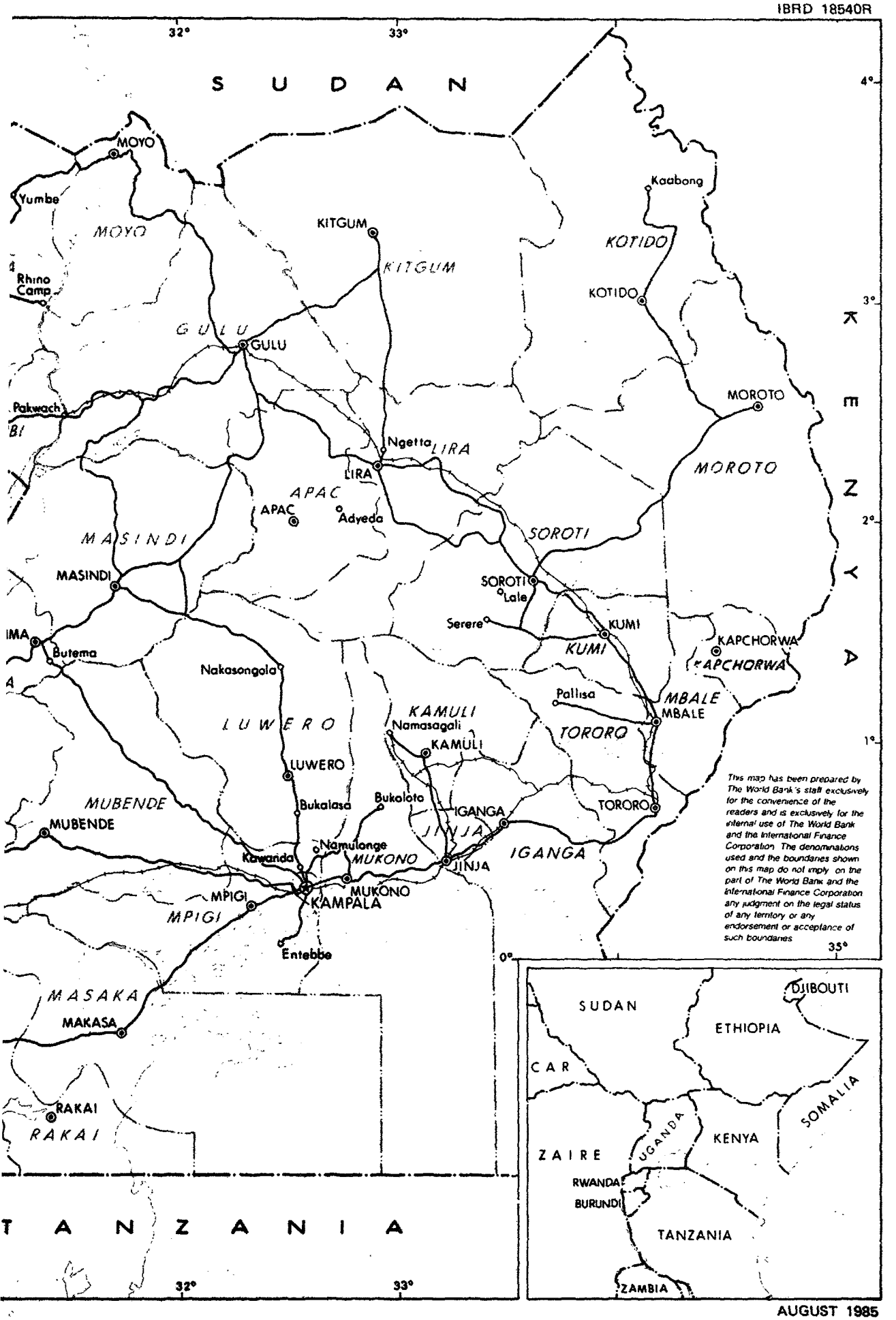
(a)	Time taken to prepare the operation:	9 months
(b)	Operation prepared by:	Ministry of Finance and Ministry of Planning and Economic Development
(c)	Project identification:	January 1987
(d)	IDA appraisal mission:	May 1987
(e)	Negotiations:	July 1987
(f)	Planned date of effectiveness:	November 1987

II. Special Conditions:

Special conditions are summarized of paragraph 79 in the text and in Annex II.


UGANDA
Major Roads
Railroads
Rivers
District Capitals
District Boundaries
International Boundaries
0 25 50 75 100 KILOMETERS
0 20 40 60 MILES
ARUA
NEBBI
3°
2°
1°
0°
1°
BUNDIBUGYO
KABAROLE
Kyenjojo
KASESE
MBARARA
BUSHENYI
RUKUNGIRI
KABALE
RWANDA
30°
31°

IBRD 18540R



AUGUST 1985