



# Program Information Document (PID)

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Concept Stage | Date Prepared/Updated: 11-Jul-2018 | Report No: PIDC25242



**BASIC INFORMATION**

**A. Basic Project Data**

Country Uganda	Project ID P164178	Project Name Uganda Growth and Fiscal Reform Development Policy Operation (P164178)	Parent Project ID (if any)
Region AFRICA	Estimated Board Date Jan 14, 2019	Practice Area (Lead) Macroeconomics, Trade and Investment	Financing Instrument Development Policy Financing
Borrower(s) Ministry of Finance, Planning and Economic Development	Implementing Agency Ministry of Finance, Planning and Economic Development, Uganda Revenue Authority		

**Proposed Development Objective(s)**

The policy development objectives of this project are to maximize finance for development by supporting the Government efforts to: (i) enhance domestic revenue mobilization; (ii) improve the institutional framework for managing public investments and crowding in private finance; and (iii) strengthen debt management.

**Financing (in US\$, Millions)**

**SUMMARY**

<b>Total Financing</b>	200.00
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**DETAILS**

<b>Total World Bank Group Financing</b>	200.00
World Bank Lending	200.00

**Decision**

The review did authorize the preparation to continue



## B. Introduction and Context

### Country Context

Uganda is a low-income IDA country in East Africa, with GDP per capita totaling USD701 in FY16/17, and a population of close to 37 million.<sup>1</sup> Following the end of the armed conflict in 1986, the Government of Uganda, led by President Museveni, introduced stabilization and structural reforms that propelled the economy to almost twenty years of high growth: from FY93/94 to FY10/11, real GDP growth averaged 8 percent per annum, which doubled real per capita GDP, in PPP terms. Consequently, Uganda transformed from an almost failed state to one of the fastest growing economies in the world.

Over the past six years, however, real GDP growth has almost halved to about 4½ percent annually. Average real output growth decelerated as the gains from reforms waned and as constraints such as weak infrastructure and poor governance increasingly curbed the competitiveness of the private sector.<sup>2</sup> Alongside the slowdown in growth, demographic pressures have remained high. Uganda has one of the world's fastest population growth rates (3.3 percent), with almost half of its people under the age of 15. With such rapid annual population growth rate, growth in real per capita GDP slowed, on average, to 2.2 percent after FY10/11 from 3.8 percent recorded in the previous decade. As a result, Uganda's real GDP per capita is increasingly lagging those in the neighboring countries such as Kenya, Tanzania, and Rwanda.

Real GDP growth in FY17/18 is set to rebound to about 6 percent, after growing at 4.7 percent in FY15/16 and 4 percent in FY16/17. Despite the acceleration in real output growth, headline and core inflation remain well below the inflation target of 5 percent. Lower inflation allowed for an easing in the Central Bank Rate to 9 percent; the fourth reduction since March 2017 when the rate was 11½ percent, but the cost of private sector credit remains high at about 20 percent, and private sector credit growth remains sluggish at about 7 percent. The external current account deficit is expected to have widened to around 5.3 percent of GDP in FY17/18, from 4 percent of GDP a year earlier. Adjusted for net FDI inflows, however, the external shortfall is projected to total 2½ percent of GDP. Gross foreign exchange reserves stood at US\$3.4 billion in April 2018, equal to 4.7 months of imports of goods and services. The fiscal deficit is expected to have widened to 4.8 percent of GDP in FY17/18 from 3.9 percent the year before, and was characterized by an underexecution of capital spending, which offset the higher-than-budgeted current spending and the weaker revenue performance. Public debt rose, as a result, to 41 percent of GDP. This level of public debt is broadly comparable to Uganda's peers in East Africa, such as Tanzania and Rwanda, but is substantially lower than Kenya's and Ethiopia's.

The outlook for Uganda looks broadly favorable. Over the next three years, real GDP growth is expected to average around 6 percent, driven by intensified public and foreign investments in renewable energy projects (Karima and Isimba dams), and infrastructure to prepare for oil production in 2023. The scale up in public investment will go hand in hand with a rise in private consumption, as services and agriculture output are expected to remain strong, and productivity to rise. The current account deficit is projected to widen to about 7½ percent of GDP in FY18/19 and close to 9 percent in FY19/20 due to the acceleration in capital goods imports. Nevertheless, a parallel pick-up in net FDI inflows is projected as oil exports get nearer and Total and CNOOC complete building wells and other infrastructure. Foreign exchange reserves are therefore expected to remain around US\$3.3 billion (equivalent to 4.3 months of future imports of goods and services).

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<sup>1</sup> Source: UBOS, 2018

<sup>2</sup> World Bank, 2015, Uganda Systematic Country Diagnostic Report: Boosting Inclusive Growth and Accelerating Poverty Reduction, Washington DC



#### Relationship to CPF (1 para)

The operation is fully consistent with the WBG CPF 2016-20 for Uganda. The CPF was developed around three focal areas. The first of these is *'strengthening governance, accountability and service delivery'*. This DPF operation aims to support the *'enhanced economic governance and fiscal management'* objective that aims to support the public sector to become more effective in mobilizing and using public resources; including by increasing revenues to expand the fiscal space, improving debt management, and enhancing expenditure management, which in turn will be critical in achieving key indicators in the results framework. The CPF proposes DPOs as one of the lending instruments to support these interventions.

The operation will complement several WBG operations in helping to achieve the overall objectives of the CPF. These include the Uganda Competitive and Enterprise Development Project, which is supporting business environment reforms; and the Uganda Intergovernmental Fiscal Transfers Program, whose objective includes improving the adequacy of fiscal transfers to local governments for health and education services. More broadly, improved public investment management will help in closing the implementation gap, which continues to impede development impact of government projects, including Bank-financed operations. Finally, the operation will support IFCs on-going work to develop PPPs such as the Kampala-Jinja Expressway.

### **C. Proposed Development Objective(s)**

The policy development objectives of this project are to maximize finance for development by supporting the Government efforts to: (i) enhance domestic revenue mobilization; (ii) improve the institutional framework for managing public investments and crowding in private finance; and (iii) strengthen debt management.

#### Key Results (1)

Key results include raising tax revenue collections through broadening the tax base, and reducing tax exemptions, while strengthening the efficiency of the tax administration. In addition, the institutional and legal framework for undertaking PIM and PPPs is going to be strengthened, which should raise the quantity and quality of the project pipeline. At the same time, debt management functions will be enhanced to assess adequately the fiscal exposures emanating from guarantees and PPPs going forward, while in parallel reducing the stock of domestic arrears.

### **D. Concept Description (2-3)**

The proposed program is closely aligned with certain priorities outlined in the NDP II. It is designed to spur improvements in revenue mobilization through substantial tax policy reforms and improving tax administration efficiency; and to advance the implementation of infrastructure development, also through participation of the private sector via PPPs, including strengthening the governance mechanisms and structures. These strategic objectives are in part based on and are supported by other government strategies, including the PFM Reform Strategy, the Government Public Service Transformation Paper, and Public Procurement and Disposal of Assets (PPDA) Strategic Plan. An overarching objective in the NDP II is ensuring macroeconomic stability, which in the program is anchored around strengthening revenue mobilization and debt management to safeguard fiscal and debt sustainability.

Currently, tax revenues remain below the Sub-Saharan average, and a concerted tax reform effort is required over the medium term to broaden the tax base and reduce tax exemptions, while strengthening further tax administration. In addition to increasing tax revenues, restraint in recurrent outlays will create the space for augmented capital expenditure execution, which needs to be bolstered by an improved institutional setup, not only to conduct more



efficient public investment management, but also to help mobilize long-term private financing through Public-Private Partnerships (PPPs).

More tax revenue and a relative shift from recurrent to capital expenditures should help raise the growth dividend over the medium and longer term, and by doing so contribute to safeguarding public debt sustainability. Additional measures to contain debt vulnerabilities would nevertheless be needed once PPPs and accompanying government guarantees take off. These include adequate monitoring and reporting of explicit guarantees, as well as the development of a fiscal commitment and contingent liability framework to manage fiscal exposures going forward.

## **E. Poverty and Social Impacts and Environmental Aspects**

### Poverty and Social Impacts

Overall, the proposed operation is expected to have a positive impact on poverty and inequality, particularly if the spending and investment profile of Uganda going forward favors social spending and human-capital enhancing infrastructure. In the case of the prior actions under the first pillar, the direct minor adverse impact of some of the measures to increase tax revenue are likely to be offset by the benefits of increased public spending, particularly if that spending is channeled to the social sectors (such as education, health and social protection). For the second, it is expected that the prior actions will result in better and higher returns to public investment projects across sectors, particularly in the infrastructure and energy sectors (which hinge on PPPs), which in turn will help raise the incomes and wellbeing of Ugandan households. The third pillar is unlikely to have an impact on household incomes, unless it helps prevent the proliferation in guarantees and, if these were to materialize, a debt incident, which could have a severe macroeconomic impact, and in turn cause a reversal in poverty reduction.

### Environmental Impacts

The operation is not expected to have significant environmental effects. The specific reforms supported by the proposed development policy operation are not likely to have significant negative effects on the country's environment, forests and other natural resources. The tax reform aimed at broadening the environmental levy to most polluting entities (vehicles, motorcycles, factories, lumbering amongst others) will have beneficial environmental effects. Some positive effects may be realized by changes in taxation of activities that are detrimental to the environment, e.g. motor vehicles. In addition, strengthening of systems for managing public investments will minimize ad hoc investments that have not been subjected to environmental assessments, which would include risk mitigation measures.

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**APPROVAL**

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**Approved By**

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