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THE REHABILITATION OF UGANDA -

A PRELIMINARY PROGRESS REPORT

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Eastern Africa Region
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in the Uganda Consultative Group)

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A Preliminary Progress Report

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1. This report has been prepared for submission to the Consultative Group for Uganda. It is based on the findings of two World Bank Missions which visited Uganda in July and September 1979, as well as on the report of the Commonwealth Team of Experts 1/ and on the findings of an IMF mission which visited Uganda in August/September 1979. Since the Commonwealth Report provides a comprehensive overview of the Ugandan economy, and given the short time available before the Consultative Group meeting, the World Bank has not produced a complete economic report. Instead, this report briefly analyzes the economic situation in Uganda today; describes the economic and social policy of the new Government, including its strategy for rehabilitation; outlines the steps the Government has taken since coming to power to begin the reconstruction process; suggests the remaining steps that must be taken and concludes with an indication of the role that external assistance can play in reconstruction.

I. Background

2. Since the fall of Kampala on April 11, 1979, Uganda has been governed by the Uganda National Liberation Front (UNLF), which was established by the various exile groups that met at Moshi, Tanzania in March 1979. At the Moshi meeting, it was agreed that the highest priority should be given to the rehabilitation of the Ugandan economy, and that emphasis should be placed on maintaining political unity and security during the two year interim period until elections could be held. The UNLF Government is headed by a president (since June 21, 1979, President Godfrey Binaisa), and a cabinet of ministers. A National Consultative Council (NCC) acts as a legislature during this interim period. The NCC originally comprised 30 people, mostly drawn from those who met at Moshi, but was expanded to 90 members on October 3, 1979, the additional 60 members having been drawn from within the country, with between one and three representatives (depending on population) from each of the 33 administrative districts. The expansion of the NCC is a significant attempt to make it more broadly representative and to extend its mandate. As a further step towards holding elections in about two years' time, a population census is being proposed for January 1980.

3. Shortly after taking office, the UNLF Government invited the Commonwealth Secretariat to assemble a team of experts to advise the Government on the requirements for rehabilitating the economy. Headed by Professor Dudley Seers of the Institute of Development Studies, Sussex University, the team produced a comprehensive two-volume report by the end of June 1979. The team worked in close collaboration with six technical committees of Ugandan civil servants which prepared over 100 working papers as inputs to the report. This report was reviewed at an initial donors' conference in Kampala in July 1979,

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1/ Commonwealth Secretariat: The Rehabilitation of the Economy of Uganda, two volumes, June 1979.

at which immediate short-term balance of payments assistance needs were discussed. Following discussion with the World Bank mission which visited Kampala in September, it was agreed that a second donors' meeting should be convened in early November, as a formal Consultative Group, to review the progress of the rehabilitation program.

II. The Economic Inheritance

4. As the Commonwealth Report eloquently put it: "The Government of the National Liberation Movement inherited a country in ruins." Uganda, which in 1970 had one of the highest per capita incomes in Eastern Africa, experienced a decline in real GDP estimated at about one percent per annum on average from the early 1970s through 1978. With population growth averaging more than three percent per annum, per capita GNP fell by about 25 percent. The decline was particularly severe in the modern sector, with the output of monetary agriculture, manufacturing, mining and construction all having fallen. Only subsistence agriculture achieved some growth, as farmers turned away from the production of export cash crops (principally coffee, tea, cotton and tobacco) towards essential food crops. Real investment fell sharply. From 1974 to 1978, both exports and imports fell by over 40 percent in real terms. The cumulative balance of payments deficit for the period 1970-78 amounted to over US$130 million, of which about US$100 million had accumulated as unpaid arrears. Heavy deficit financing by the Government was the main cause of a nearly six-fold increase in the money supply from 1971 to 1978. Given the severe shortfalls in domestic production and the scarcity of imports, inflation was rampant. The official consumer price index (probably understating true price inflation) rose at an annual rate of 25 percent. Despite the high inflation rate, the official minimum wage rose only 54 percent in eight years, and civil service salaries also fell sharply in real terms. These drastic declines in modern sector real incomes contributed to the development of "magendo", an extensive system of black markets, smuggling and official corruption.

5. The decline in the modern sector of the economy is reflected in the changing structure of output. In the early 1970s, about 70 percent of GDP originated in the monetary economy (including cash crop agriculture); agriculture accounted for slightly over half of GDP; (monetary agriculture 24 percent, subsistence 27 percent); industry about 11 percent; and modern tertiary sector activity about one-third. By 1978, it is estimated that the share of subsistence agriculture had increased to over one third and that the non-monetary economy accounted for nearly 40 percent. Almost all modern sector production declined. The table below compares previous production levels for selected agricultural commodities and manufactured goods with estimates for the most recent period.

TABLE 1

Production of Selected Agricultural and Industrial Commodities

	Unit	Production	
		Peak Year	Latest Year
Monetary Agriculture			
Coffee	′000 metric tons	251 (1969)	120 (1978/79)
Cotton	" " "	76 (1970)	15 (1978/79)
Tea	" " "	21 (1976)	11 (1979)
Sugar	" " "	144 (1970)	8 (1979)
Tobacco	" " "	5 (1972)	2 (1979)
Manufacturing		Average 1971-73	Latest Year
Consumer Goods			
Vegetable oil	" " "	14	1 (1978)
Cotton & rayon fabric	million sq. meters	44	25 (1978)
Blankets	million pieces	1,154	595 (1978)
Soap	′000 metric tons	11	1 (1978)
Industrial Goods			
Steel ingots	" " "	13	3 (1978)
Corrugated iron sheets	" " "	11	2 (1978)
Cement	" " "	171	50 (1978)
Hoes	million pieces	1	- (1978)

6. These output declines were largely attributable to the policies followed by the Government. In 1970, the Government took majority participation in a number of large companies. After the change in Government in 1971, this policy was first reversed but then extended, as the "economic war" was declared, and many more foreign-owned businesses were nationalized. In 1972, most Ugandans of Asian origin were expelled and their businesses allocated to Government nominees. In 1975, more foreign businesses were expropriated. Uganda did not possess the manpower resources to cope efficiently with this sudden increase in the number of businesses in the public sector or in the hands of inexperienced businessmen. No program was developed to augment the manpower resources available (in fact, Uganda lost trained manpower during this period), or to support and strengthen the newly-created parastatals and small private businesses. Only bank credit was provided -- from 1971 to 1978, credit to the private and parastatal sectors more than trebled, in many cases under pressure from the authorities to lend to unviable enterprises. As a result, many parastatals are now heavily encumbered with debt. In addition, periodic attempts to impose price control worsened the parastatals′ economic problems and stimulated the trend towards black marketeering.

7. In addition to declines in the real value of exports and imports, Uganda experienced a fall in the net capital inflow. In 1971 and 1972, net official capital inflows exceeded Shs. 200 million per year; by 1978, they had declined to Shs. 96 million, implying a much greater decline in real terms. At the same time, outflows of short-term capital increased. The increase in coffee prices during 1977 provided some temporary respite; imports increased from around Shs. 2 billion to Shs. 3.5 billion and payment arrears were reduced by Shs. 180 million. However, during 1978 the balance of payments again experienced a large deficit; by the end of the year, gross foreign assets covered less than two months' imports and net foreign assets were only marginally positive.

8. Despite the contracting real economy, the Government's budgetary operations were expansionist. Total expenditure increased from Shs. 1.9 billion in 1970/71 to Shs. 5.2 billion in 1976/77, while revenue increased from Shs. 1.3 billion to only Shs. 3.4 billion, and net foreign borrowing actually decreased. Net domestic financing, almost all through the banking system, thus increased from a little over Shs. 350 million to Shs. 1.6 billion. While the improvement in coffee prices boosted revenues significantly in 1977/78 and for a time reduced the recourse to deficit financing, the deficit and Government borrowing from the banking system both rose sharply again in 1978/79.

9. With the decrease in external assistance to Uganda after 1971, recorded external public debt outstanding, which totalled Shs. 1.5 billion at the end of 1972, rose to only Shs. 2.0 billion at the end of 1978. (The World Bank group accounts for 23 percent of total debt outstanding, the USSR for 20 percent and the UK for 12 percent.) As a result, the ratio of Uganda's debt service to export proceeds was probably less than five percent in 1978. Partly in consequence of the decline in foreign assistance, the Government's capacity to select and prepare projects declined; project selection became *ad hoc* and the normal technical requirements for project preparation were for the most part neglected.

10. By early 1979, these trends had resulted in a serious deterioration in economic and social conditions. The war with Tanzania, which resulted finally in the fall of the former regime, greatly exacerbated this situation. Following the war, shops stood looted and closed; people queued for essential commodities; industrial and repair facilities lay idle and deserted; tea and sugar estates were overgrown; the roads, the railway and its rolling stock stood in need of repair. The vehicle fleet, which numbered over 7,000 in 1970, had fallen to about 1,600 shortly after the liberation, many of the trucks having been driven to neighboring countries. There are shortages of essential drugs and medicines; diseases which had formerly been largely eliminated from Uganda (like cholera) have spread once again; schools and hospitals have been ransacked; and water and sewerage systems are in a state of severe dilapidation. The discipline and organization of the modern economy has been undermined; almost everyone, including Government officials, must participate in "magendo" to survive. The new Government thus faced a most difficult and demanding task on taking office, a fact that should be borne in mind when assessing the progress made in rehabilitation.

III. Government Policy and the Rehabilitation Program

The Economic and Social Policy of the UNLF

11. The Government has decided and announced its economic and social policy, after a careful review by all concerned ministries, and with the endorsement of the NCC. The policy statement declares the central objectives of the Government to be rapid economic growth, improved income distribution, an equitable spread of development across the entire country, and improved social services. The respective roles of the Government, the private and cooperative sectors are defined.

12. The Government will be responsible for social services and essential infrastructure (roads, power, water supply and telecommunications). In addition, the Government will, through parastatal organizations, participate in productive sectors in cases where an industry is of strategic importance, where a development need is evident (to carry out structural reform, to establish a key industry, or to carry out regional policy); or where capital requirements are too large for private enterprise. Consequently, the Government will retain a controlling interest in key industries and will continue to control the marketing of key crops and minerals. It will retain its interests in the financial, insurance and external trade fields. It recognizes the problem inherited by the parastatal organization and intends to address them; it expects such enterprises to be efficient and profitable, and has established a task force in the Ministry of Finance to recommend appropriate action.

13. The private sector, comprising both local and foreign investors, will be encouraged either to participate jointly with the Government in the enterprises in which the Government has decided to take a controlling interest, or to operate independently in those areas where the Government is taking no direct interest. Indigenous private entrepreneurs will be given certain preferences, while foreign investors will be safeguarded under the provision of the 1964 Foreign Investment Protection Act.

14. Agriculture, which is the major occupation of the people of Uganda, will receive appropriate emphasis by the Government. The Government intends to support smallholders as well as to encourage medium scale farming. It will ensure appropriate production incentives (adequate producer prices, availability of inputs, provision of training, extension services and credit). It also intends to strengthen the marketing and cooperative systems, both of which suffered under the previous regime. An outline of the Government's priorities and policies in the other major sectors -- livestock, mining, forestry, fisheries, manufacturing, tourism, housing, manpower and education -- is also presented in the policy paper.

15. The Government intends to reestablish the machinery for effective planning in Uganda. It is in the course of setting up a National Planning Commission, consisting of ministers with economic and social portfolios, served by a secretariat in the Ministry of Planning and Economic Development. A National Manpower Council is also proposed, to take stock of available and potential Ugandan manpower and to reinstitute manpower planning.

The Rehabilitation Program

16. The Commonwealth Report recommended, and the Government has adopted, a two-phase strategy to revive the economy. The priorities in the first phase (originally expected to last from July to December 1979) are to restore transportation capacity, to resume the production of building materials and key consumer goods (which have been practically unavailable since early 1979), and to restore the production and sale through official channels of export cash crops (coffee, cotton, tea, tobacco). The Report also made proposals on how to proceed on some key administrative and policy issues. To reduce the importance of "magendo", it suggested either a devaluation, or a tax equivalent to "magendo" profits, or an auction of foreign exchange entitlements. To restore export cash crop production, it proposed, in addition to improvements in transportation and marketing, an increase in producer prices for coffee, cotton and tea. To enable the cooperatives and parastatals, many of which have incurred heavy losses, to resume operation, it suggested a partial, selective moratorium on their domestic debt in parallel with the establishment of a body to review the parastatals and make recommendations on their future organization. To restore financial responsibility in the public sector, it emphasised the importance of restraining Government recourse to Ways and Means financing. A temporary external debt moratorium was suggested to give the Government time to review the debt it inherited from the previous regime. The Report estimated that imports totalling about Shs. 5 billion would be needed for this first phase, of which the main components would be agricultural and industrial inputs (24 percent), transport equipment and spares (17 percent), basic consumer goods (15 percent), petroleum (13 percent), housing (12 percent), social services and administration (11 percent). This list clearly accords with the priorities indicated above. Exports (mainly coffee) would only be sufficient to provide about one-third of the foreign exchange needed for these first six months, which was estimated at Shs. 6 billion including non-factor services and debt repayment. The balance (some Shs. 4 billion) would require financial assistance on both concessional and commercial terms.

17. The second phase (through mid-1981) calls for the initiation of a medium-term investment program directed at rehabilitating the key productive sectors and social infrastructure to the levels which prevailed in 1970. It consists of less urgently required expenditures, many of which (by contrast with phase one) may be more easily identified as discrete projects. The total cost of the second phase is estimated at Shs. 11.5 billion, of which Shs. 8.9 billion would be foreign exchange. A large proportion (36 percent) would consist of social infrastructure (including Shs. 4.1 billion for a housing program), and 15 percent for financial institutions (principally the Uganda Development Bank and the Uganda Development Corporation). The remaining expenditure would cover industry and tourism, agriculture and transport (each 14 percent of the program), and telecommunications (8 percent). The Report provides a detailed analysis of rehabilitation needs and their costs for each sector.

Progress in Rehabilitation

18. While the Government has fully accepted the general thrust of the Commonwealth Report, it has some differences on methods of implementation which it has outlined in a recent White Paper. At the same time, it has taken a number of steps to implement this strategy. The Government's position on the Commonwealth Report's recommendations and the steps it has taken are described and analyzed below.

(a) The Exchange Rate

19. A major issue of rehabilitation strategy is the exchange rate. The need for an exchange rate adjustment can be established on several grounds. First, black market exchange rates have been up to ten to twelve times the official rate. While these rates certainly exaggerate the degree of overvaluation of the Ugandan currency, the black market is at the same time far from being peripheral -- a large proportion of transactions clearly do take place at these rates. Secondly, an exchange rate adjustment could improve the balance of payments, at least over the medium term, but quite possibly within a relatively short time (say, one year). The improvement could come largely from increased export supply, provided at least part of its benefits were passed through to producers. The price increase already introduced for coffee has reportedly already has some effect in attracting production into official marketing channels and may also have stimulated some improvements in crop husbandry. Such a supply response depends partly on other factors -- improved transportation, input supply and credit arrangements. However, if these factors can be improved through the reconstruction efforts, then producer prices seriously out of line with prices obtainable for Uganda's exports in neighboring countries will only stimulate a return to smuggling.

20. Thirdly, an adjustment in the exchange rate could increase Government revenues, since it would raise the shilling value of exports and would, for any given price to the producer, increase the scope for taxation; it would also increase the shilling equivalent of external financing. Fourth, devaluation would reduce "magendo" profits since an increase in the shilling prices of consumer goods imported through official channels would probably have little effect on the much higher unofficial prices which are determined by the present supply/demand balance. In fact, if devaluation were accompanied by an increase in the total supply of goods the unofficial or free market prices should fall, thus further squeezing the margins available in the "magendo" market. Fifth, a devaluation would probably permit an increase in nominal wages. Potentially labor-intensive agricultural operations such as sugar harvesting and tobacco and tea cultivation are now constrained by a severe scarcity of labor due to the extremely low real value of the rural minimum wage. A substantial increase in the shilling value of these export crops should permit cultivators to pay higher wages.

21. In its White Paper on the Commonwealth Report the Government states that devaluation should be studied and its implications clearly assessed before a decision is made. For the reasons given, however, devaluation is

itself a key element in the rehabilitation program. Without devaluation, it is not easy to see how rehabilitation can proceed effectively. It would be unreasonable to expect imports priced far below their scarcity value to be deployed without incurring gross inefficiency and intolerable leakages. In addition, it would be very difficult to redirect exports through official channels unless producers and traders were compensated at rates also reflecting the scarcity value of foreign exchange. In our view, exchange rate adjustment should be pursued in parallel with the other measures in the rehabilitation package, notably an improvement in the flow of imports. The adverse effect on domestic prices of the devaluation could then be offset by the simultaneous increase in import supply.

(b) Fiscal Policy

22. The Government has largely followed the recommendations of the Commonwealth Report in the area of public finance. Through the end of October 1979, the Government has operated under a Vote on Account which has restricted expenditures to available revenues, and has avoided the use of Ways and Means financing through the Bank of Uganda. A budget, or financial program has, however, not yet been announced, since the Government wishes to know how much external aid it will receive before determining expenditure levels for the remainder of the fiscal year (through June 1980). However, this approach could delay the identification and implementation of rehabilitation priorities.

23. While a full fiscal year budget has not been issued, the Government has made progress in determining the likely magnitude of its revenues and its essential recurrent expenditure needs. Revenues are likely to be in the range of Shs. 3.9 billion, compared with Shs. 5.7 billion in 1977/78 and Shs. 3.2 billion in 1978/79. Development revenue (mainly foreign assistance committed or under active consideration as of October 1979), is expected to total Shs. 1.3 billion. The revenue outlook may improve somewhat if the Government succeeds in reviving the flow of imports and domestic production. However, given present inflation rates and consequent declining real incomes, there is probably little scope for additional revenue measures at this time. In addition, some needed economic measures have had adverse effects on revenues and expenditures. The increases in agricultural producer prices have reduced tax receipts in the case of coffee and will probably generate a subsidy requirement in the case of tea and cotton. The Government may also have to consider salary increases in order to improve the motivation of the civil service. Recurrent expenditure has in recent years ranged around Shs. 4.2 billion but is expected to rise to Shs. 4.9 billion in 1979/80. Development expenditure, (including ongoing projects and only minimal reconstruction) of about Shs. 1.0 billion is already committed. Thus, even before the bulk of reconstruction needs is taken into account, it would appear unlikely that expenditures can be covered from available revenue and external financing. Nevertheless, the Government should, as far as possible, limit its recourse to the banking system in order to moderate inflationary pressure and in order to accommodate the likely substantial credit needs of the private, parastatal and cooperative sectors.

24. The Government hopes that all or most of the shortfall in domestic revenues, as well as the costs of reconstruction, can be met through additional external assistance. As indicated earlier, it is still not clear how much balance of payments support or quick-disbursing project finance will be forthcoming from donors, and it will in any case take time for the various promises of aid to be finalized. This has introduced uncertainties into the planning process and made it difficult for the Government to finalize its budget as well as the allocation of foreign exchange.

25. The Government should not, however, delay further in issuing a budget and financial program for 1979/80. A full-fledged budget exercise including reconstruction is probably not possible at this time, but expenditure ceilings should be imposed reflecting the essential recurrent items and ongoing development budget indicated above. This could be followed by a supplementary authorization later in the fiscal year if the resource picture improves.

(c) Domestic Credit and the Parastatals

26. The Government has not so far imposed a moratorium on the domestic debt of the parastatals and cooperatives. The financial viability of some of the cooperatives has improved following the increase in crop producer prices, and they now appear able to obtain their credit needs on a commercial basis. The issue of parastatal indebtedness has not yet become pressing because the imports for which domestic finance will be required have not yet become available. Thus far, the Government and the banking system have applied quite strict standards of creditworthiness to applicants for credit, both from the public and private sectors. However, it may prove difficult to maintain this stance once reconstruction imports start to flow. A high priority should therefore be to develop a mechanism for quick response to financial requests by parastatals for high priority imports under the reconstruction program, with a selective debt moratorium as one of the more attractive options.

27. The Government has established a task force in the Ministry of Finance to review parastatal organizations and recommend on their future status, including the financial needs. It will however take time for this task force to complete its review, which is in any case concerned with longer term issues. A separate mechanism for deciding on short term credit allocation will, therefore, as suggested above, be needed.

(d) External Debt

28. Rather than declare a unilateral external debt moratorium, as recommended in the Commonwealth Report, the Government is examining the purposes for which debt was incurred and, in cases where legitimate obligations exist, intends to work out repayment terms with creditors.

(e) Foreign Exchange Allocation

29. The Government has started establishing a foreign exchange allocation system with the object of determining, within the limits of available foreign resources, what the import priorities should be. Individual ministries and parastatals have stated their requirements and these, together with a list of essential consumer goods, have been consolidated by the Ministry of Finance. A Foreign Exchange Allocation Committee has been set up in the Bank of Uganda, to which are referred all import licences and other applications for foreign exchange, after having been processed by either the Central Tender Board (for Government imports), or by the Uganda Advisory Board of Trade (for private and parastatal sector imports). These applications are henceforward to be allocated in accordance with the foreign exchange available from time to time, and with the Government's overall priorities (see para 16 above) as a guideline. While the system appears well designed, it could come under intolerable pressure if not reinforced by a devaluation.

(f) Agricultural Producer Prices

30. The key export crop producer prices have been raised in accordance with the recommendations of the Commonwealth Report in a commendable effort to improve the incentive to produce and market through official channels. However, as the Report points out, these price increases will take time to have an effect, and will furthermore depend on complementary developments in other areas, (e.g. input supply, transport facilities, consumer goods). Furthermore, with black market prices at several times the level of official prices, the incentive effect of the price increases will be limited. Finally, current rates of inflation will erode even the 100 percent increase in the coffee price quite quickly, and it may therefore be necessary to revise producer prices frequently in order to maintain incentives.

(g) Transport

31. Some steps have been taken to improve the transport situation. New lorries have been ordered and some are now being delivered. Limited use is being made of routes to the coast through Tanzania, which were previously not available to Uganda. Nevertheless, Mombasa still accounts for most of Uganda's export and import trade. The flow of coffee leaving the country has built up to over 10,000 tons per month, or about double the rate attained during the second quarter of 1979. Despite these improvements, the transport system remains inadequate to the task of increasing the supply of goods, especially imports and internal trade. On the external side, the railway through Kenya is far from operating efficiently, since both locomotives and wagons must be exchanged at the border. Part of the solution to this problem is the development of better working relations with Kenya Railways, to the mutual advantage of both countries. Normal international air services have still not been resumed. Internal transport bottlenecks also impede the distribution of needed inputs for agriculture and industry, as well as consumer goods, and are probably the key constraints on deliveries of coffee and other export crops to cooperatives, unions and processors, thus losing potential

foreign exchange earnings. More lorries and spares must be procured and allocated to those, especially in the private sector, with appropriate experience in haulage. Better use could probably be made of the existing fleet. The needs of the transport sector, largely as outlined in the Commonwealth Report, deserve the highest priority in the rehabilitation program.

(h) Distribution

32. The distribution system in Uganda inherited various difficulties: under the former regime, and especially after the expulsion of citizen and non-citizen Asians, businesses were allocated to many unqualified Ugandans. During and immediately after the liberation war, many of these businessmen fled and their shops were looted. The Government has made some progress in allocating these businesses, an important step in the process of reactivating the supply of consumer goods and repairing the damage done by looting. Commercial properties were gazetted for allocation by the Ministry of Commerce in August 1979, and committees have been established in each district to scrutinize applications in accordance with criteria emphasizing business qualifications and creditworthiness.

33. Assuming that the allocation of businesses proceeds as intended, the main distribution problem remaining is the widespread existence of informal or black markets ("magendo"). Goods supplied through official channels, and at the official exchange rate, are being resold on the black market from three to ten times the controlled price, and may even be finding their way to neighboring countries. Although data are not available, it is clear that the black markets are not thin; in fact, they probably account for the major part of trade in consumer goods and involve large numbers of people. Given that formal sector wages and salaries have been adjusted less frequently and to a lesser extent than the price level, many civil servants and other formal sector workers have been forced to produce for and trade in the black market in order to defend their real incomes. Furthermore, "magendo" reflects in part peoples' expectations regarding the effectiveness of Government economic policy, and it will take a long time to overcome the widespread cynicism regarding the activities of Government in general which has been inherited from the previous regime. Since the returns to "magendo" are so substantial, it is difficult to envisage any system of price control being effective.

34. The Government's strategy is to increase the supply of goods through official channels to the point where free market prices are reduced and "magendo" margins squeezed. While the supply of goods is being brought to a more normal level, the Government will be considering the exchange rate and other administered prices to see what adjustment is required. As suggested earlier, this strategy will only succeed if the exchange rate is adjusted as early as possible.

(i) Foreign Investment

35. In accordance with its policy of encouraging a mixed economy, the Government has been conducting negotiations with some former owners of agricultural and industrial enterprises in Uganda. The Government hopes this will lead to the return of these companies and individuals, and their involvement in the rehabilitation of export crop and essential consumer good production. While this matter is being dealt with on a case by case basis, a fuller statement of the regulatory framework for foreign investment should eventually be made.

(j) Government Administration

36. Finally, the Government has started the task of streamlining and improving its own administrative machinery. It has, following the recommendations of the Commonwealth Report, established an interministerial technical coordinating committee to supervise rehabilitation. And it has recently established machinery, under the Public Service Commission, to review and evaluate the performance of senior civil servants. If used to reward competent performance, this will be an important factor in restoring administrative efficiency.

Evaluation

37. The progress described above is, in our view, substantial in view of the relatively short time that the present Government has been in office, and the serious problems it inherited. The Government's economic and social policy paper and White Paper, in conjunction with the Commonwealth Report, constitute a framework for the short-term rehabilitation effort and merit the support of the international community, provided a set of policies is established which assures that foreign assistance will effectively support the reconstruction effort. The basic strategy chosen is sound, focussing as it does on the needs of the productive sectors and on the key administrative and policy questions. The priorities indicated in the Commonwealth Report for the first phase address the key areas - the transport bottleneck, agricultural and industrial input supply. The second phase understandably focusses more heavily on needed social expenditures, but there is clear recognition in the phasing itself that these are, for the time being, of lower priority. It is, however, unlikely that rehabilitation can be accomplished as rapidly as was expected by the Commonwealth team, because of the more limited availability of external resources than was anticipated, and because of absorptive capacity constraints. The Commonwealth Report assumed that Phase I -- the massive increase in import supply -- could largely be achieved during the six months ending in December 1979. Reflecting the lower rate of aid commitments than was expected, the continuation of transport bottlenecks, the need to reorganize the distribution system and political insecurity, there has been a very low level of imports since the liberation through the end of October. It is therefore necessary to revise the balance of payments forecast; since the resources available and the capacity to implement rehabilitation are probably more constrained than was hoped earlier this year, it becomes an urgent matter to establish investment priorities within an annual budgetary framework.

38. In general, Uganda has the manpower available to implement rehabilitation. While there remain specific manpower needs, the civil service has managed to retain many capable individuals. In addition some areas have already been strengthened by returning exiles. The key implementation problem is not so much a shortage of manpower as its undermotivation, especially in the public and parastatal sectors. As indicated above, the Government has started taking steps to reinstitute appropriate standards of conduct and competence among public servants. Administrative measures of this kind will however require time to take effect and will moreover require reinforcement through an adequate incentive system. As pointed out earlier, the situation inherited from the past Government has precisely the opposite effects -- the contribution of currency over-valuation, controlled prices and wages has produced rampant black-marketeering and will undermine the rehabilitation effort unless dealt with. The capacity to implement rehabilitation therefore comes down once again, at least in part, to exchange rate policy.

IV. The Next Stages

The Balance of Payments and External Assistance

39. Uganda's recent balance of payments experience is set out in Table It is evident that, with the exception of 1976 and 1977, during the peak of the coffee price boom, the balance of payments situation was characterized by trade deficits, low levels of grant and loan assistance, chronic overall deficits and the accumulation of substantial payments arrears. The experience in 1978 was particularly discouraging as, due to falling price and volume of coffee exports the total value of exports fell by 45 percent, the nominal value of imports dropped by 23 percent, and arrears on import payments rose by Shs. 560 million. By the end of 1978 net foreign assets were barely positive and cumulative arrears had risen to Shs. 759 million.

40. In 1979 the situation has only improved slightly. Export revenues, over 95 percent of which are derived from coffee, are expected to be slightly below the already depressed 1978 level. Imports are forecast to remain at roughly the same level as 1978 in nominal terms, reflecting the fact that the expansion of imports called for in the first phase of the reconstruction effort has not yet begun. The amount of official grant and loan assistance projected, roughly Shs. 370 million ($50 million) on a net basis, includes only those known commitments from EEC (STABEX) and bilateral donors which are expected to disburse during the calendar year. The change in foreign reserves figure includes the drawing of SDR 5 million (Shs. 48 million) under the IMF compensatory financing facility.

41. The outlook for 1980, given only the level of foreign assistance committed to date, is also discouraging. In making our projection for 1980 we have assumed that coffee exports will rise to 140,000 metric tons from 116,000 tons in 1979, at a price of Shs. 22 per kg. Other exports, principally tea and cotton, are expected to yield only Shs. 200 million. Three alternative scenarios for the level of imports in 1980 (cases I, II and III in Table 2) may then be considered.

TABLE 2

UGANDA: Balance of Payments 1975-80
(Millions of Shillings)

	1975	1976	1977	1978 (Provisional)	1979 (Projected)	1980 1/ (Projected) I	II	III
Trade Balance	-187.0	718.7	1,045.2	-224.0	-466.3	-1,352.0	-2,937.0	-4,368.0
Exports of Goods	1,758.3	2,707.8	4,528.0	2,484.1	2,287.4	3,322.0	3,322.0	3,322.0
Imports of Goods	1,945.3	1,989.1	3,482.8	2,708.1	2,753.7	4,674.0	6,259.0	7,690.0
Net Services	-322.0	-340.9	-459.7	-758.1	-351.3	-284.0	-284.0	-284.0
Net Transfers 2/	93.3	17.7	-21.7	-22.7	207.7	381.0	1,095.0	1,806.0
Current Account Balance	-415.7	395.5	563.8	-1,004.8	-609.9	-1,255.0	-2,126.0	-2,846.0
Private capital inflow, net	144.4	-350.9	-347.5	715.3	295.7	503.0	1,038.0	2,403.0
Net Direct Investment and Loan Disbursements 3/	(304.7)	(-198.8)	(-168.3)	(921.1)	(423.6)	(621.0)	(1,157.0)	(2,021.0)
Outflow of long term capital	(-160.3)	(-152.1)	(-179.2)	(-205.8)	(-127.9)	(-119.0)	(-119.0)	(-119.0)
Public long-term capital, net	141.2	-3.1	-47.2	95.7	101.8	485.0	1,038.0	1,747.0
Disbursements	(216.0)	(88.4)	(194.7)	(136.3)	(172.0)	(670.0)	(1,223.0)	(1,932.0)
Amortization	(-74.8)	(-91.5)	(-241.9)	(-40.6)	(-70.2)	(-185.0)	(-185.0)	(-185.0)
Other capital movements 4/	-76.8	-53.7	-	-254.5	-238.9	50.0	50.0	50.0
Overall Balance	-206.9	-12.2	169.1	-448.3	-451.3	-217.0	-	1,354.0
Accumulation of arrears (- = decrease in liabilities)	207.4	22.7	-180.2	559.0	395.1	-	-363.0	-1,154.0
Monetary authorities (net) 5/ (- = increase)	-0.5	-10.5	11.1	-110.7	56.2	217.0	363.0	-200.0

1/ See text.
2/ Includes capital grants.
3/ Includes net short term capital and net errors and omissions.
4/ Includes allocation of SDRs.
5/ Includes net use of IMF resources.
SOURCE: Bank of Uganda, IBRD staff estimates.

TABLE 3

UGANDA: External Assistance and Private Capital Inflows - 1980

	Case I 1/		Case II 2/		Case III 2/	
	Shs. m.	US$. m.	Shs. m.	US$. m.	Shs. m.	US$. m.
ODA						
Grants	385	52	1,089	146	1,800	240
Loans 3/	670	89	1,223	163	1,932	258
Subtotal	1,055	141	2,312	309	3,732	498
Private Loans and Investment	621	83	1,156	154	2,021	269
Use of IMF Resources 4/	362	48	725	96	725	96
Total	2,038	272	4,193	559	6,478	863
Memorandum Item:						
ODA per capita: (US$)		11.4		24.9		40.2

Source: Data provided by the Ugandan authorities and IBRD staff estimates.

Notes:
1/ Includes only those amounts committed or under active consideration as of September 1979.
2/ IBRD staff estimates.
3/ Includes estimated disbursements out of loans committed prior to liberation (Shs. 100 million) and an estimate for the IMF Trust Fund loan.
4/ Case I includes likely drawings under the first credit tranche and the compensatory financing facility; Cases II and III include drawings under three further credit tranches.

Case I assumes that official grant and loan assistance (included in net transfers and disbursements of public long-term capital respectively) includes only the amounts available from old (pre-liberation) loans and from known new commitments, including an IDA reconstruction credit for balance of payments assistance, which we expect to negotiate shortly after the Consultative Group meeting. We estimate that these total about $140 million, (see Table 3). Private capital inflows include anticipated bank credits and an increase in trade credits together totalling about $80 million. Account has also been taken of relatively unconditional IMF facilities -- the first credit tranche, the trust fund and additional export compensatory financing--which are under active discussion between the IMF and the Government. We have further assumed that gross foreign exchange reserves and payment arrears remain constant. Imports of Shs. 4.7 billion ($620 million) have been derived as a residual. Case I thus represents the "bare bones", a minimum import level derived on conservative assumptions regarding the availability of external assistance.

Case II differs from Case I through the inclusion of additional official grants and loans of around $170 million and $70 million of additional private resources. In addition, we have assumed that Uganda makes further drawings on higher credit tranches at the IMF; that payment arrears are reduced by about $47 million and that gross foreign exchange reserves increase slightly. This would permit imports of Shs. 6.3 billion ($840 million). As we indicate below, a conservative assessment of absorptive capacity shows that Uganda should be able to absorb this level of imports.

Case III assumes an import level close to that envisaged by the Commonwealth Report for the first full year of reconstruction (Shs. 7.7 billion or $1,030 million). We have also assumed the entire elimination of arrears and a build up in the net (as well as in the gross) reserves. To achieve this, additional finance totalling around $305 million over and above Case II would be required. For illustrative purposes, we have allocated $190 million of this increased requirement to official grants and loans, and $115 million to the private sector (Table 3).

42. The projection exercise for 1980, rough as it is, demonstrates clearly the degree of difficulty which the Ugandan Government faces in mounting the reconstruction effort. We cannot say what a "normal" level of imports for Uganda would be, based on past experience, because the past performance of the Ugandan economy has been so distorted. However, as an illustration, if we were to consider the 1977 import level to have been relatively unconstrained, even though we know that the economy was operating far below full capacity in that year, a projection allowing for 11 percent import price inflation per year would show that a nominal import value of Shs. 4,760

million ($630 million) in 1980 would be required merely to maintain the 1977 import volume. Thus, as shown in Table 4 below, the import level for 1980 assumed in Case I represents a slight shortfall from even the 1977 level. Case II imports in 1980 would represent an increase of only 30 percent over 1977 levels but would still fall short of the 1970-71 level, the last years of relatively normal economic activity and the benchmark years for reconstruction. Only Case III would permit the restoration of real imports to 1970-71 levels. There is therefore a pressing need to support the first phase of the Government's program with fast-disbursing balance of payments assistance.

TABLE 4

UGANDA: Value and Volume of Imports 1970-80

(Millions of Shillings)

	Imports at Current Prices	Indices 1/ Volume	Indices 1/ Price
1970	1,391.1	100	100
1971	2,034.0	136	107
1977	3,482.8	74	340
1978 (provisional)	2,708.1	52	378
1979 (projected)	2,753.7	47	420 2/
1980 3/ I	4,674.0	72	465 2/
II	6,259.0	97	465 2/
III	7,690.0	119	465 2/

1/ 1970 = 100.
2/ Import prices assumed to increase at 11 percent p.a.
3/ See text for explanation of assumptions.

Source: Data provided by the Ugandan authorities.

43. Since the capacity exists to absorb at least the same volume of imports as in 1977, the Case II import level of Shs. 6.3 billion ($840 million) during 1980 appears feasible. About $290 million of additional balance of payments assistance over and above present commitments would be required to attain this level. If, as indicated in Table 3, about $170 million of this were forthcoming as official development assistance, Uganda would be receiving ODA equivalent to only about $25 per capita, still less than the amounts received by neighboring Kenya and Tanzania. There is little doubt that, with an elaboration of the reconstruction policies as discussed earlier, and with improvements in transport and distribution, Uganda could absorb Case III levels of imports, implying another $190 million of ODA. Even this would leave Uganda, with $40 per capita, at about the same level of ODA as its neighbors.

The Time Frame

44. As noted earlier, it has taken longer than expected to establish the necessary machinery for reviving the supply of goods, and to activate finance for them. As suggested in para 37, it is unlikely that the first phase of rehabilitation, originally targeted for the end of 1979, can be completed before the end of 1980. Completion of the second phase will also take longer than anticipated, for the same reasons. According to the Commonwealth Report, the total foreign exchange costs of phases one and two total Shs. 13.9 billion. Assuming that rehabilitation-related imports during 1979 and 1980 reach Shs. 8 billion (Case II), this would leave Shs. 6 billion to complete rehabilitation. Given that reconstruction has started more slowly than anticipated; that the inflow of essential consumer goods and other recurrent inputs will continue to require foreign exchange; and that some lead time will be needed to prepare the projects which comprise the second phase of reconstruction, we estimate that another two years, (i.e. the end of 1982 rather than mid 1981), will be required to conclude reconstruction.

Planning

45. The Commonwealth Report provides, in general, a suitable basis on which to start building sectoral programs for medium-term rehabilitation. A start should, therefore, be made, within the framework of the new National Planning Commission, to determine a detailed medium term program of investment, and to undertake systematic preinvestment work. In the past, the Ministry of Planning and Economic Development (MPED) has not had sufficient influence on project review and selection. It is therefore especially important that this Ministry is strengthened and plays a key role in the new planning system. To assist in this, the World Bank, as executing agent for a UNDP project, will provide planning assistance to the MPED for certain key posts.

46. The priority sectors for the first phase of rehabilitation will continue to require emphasis. In particular, the productive sectors, agriculture and industry, and transport infrastructure will need continuing investment to restore 1970 production levels. Provided security improves, tourism could also revive as a foreign exchange earner. Major rehabilitation needs also confront the social sectors, especially education and water supply, but given the resource constraints, new projects in these areas should be discouraged for the next two to three years. It would be easy for the Government and the donors to start proposing new projects with heavy investment costs and heavy demands on manpower resources. The higher priority, however, is reconstruction, and attention should continually be brought back to it.

Project Development

47. The most pressing need is to support the first phase of the Government's program with fast-disbursing balance of payments assistance. Project assistance is thus of lower priority at this time. Uganda does not need additions to its productive capacity, so much as to restore capacity utilization in industries and to restore agricultural production and services to their 1970 levels. In most cases this is largely a matter of providing the

necessary inputs, raw materials and transport, and it is this that the assistance effort should focus on. However, simple projects, which can be implemented quickly, the funds for which can be disbursed quickly, and which can readily be fitted into the present scheme of rehabilitation priorities, are both very similar in effect to balance of payments support and can provide a link with more conventional project finance at a later stage. They should therefore be encouraged.

Aid Coordination

48. In addition, the mechanism for aid coordination--an essential pre-requisite for effective project assistance--is only now being developed. To obtain the maximum benefit from project assistance in the next phase, the Government should clearly determine its investment program, and coordinate its aid requests to donors. This will be the major task of the new aid coordination section in the Ministry of Finance which will require strengthening to enable it to perform its role. It is hoped that the risk of duplication and conflicting priorities can be lessened by emphasizing coordination at the early stages of rehabilitation.

Technical Assistance

49. The present situation in Uganda, with security difficulties, housing and consumer goods shortages, does not lend itself to large inputs of expatriate technical assistance. Moreover, Uganda's manpower resources, both actual and potential, are substantially greater than those of many countries at a comparable level of per capita income. At the same time, there are clear needs for technical assistance in certain specific areas which could in many cases be met on the basis of short-term assignments.

V. Conclusion

50. Uganda's case is a deserving one. It has received very low levels of assistance over the past eight years. It has been through a period of severe moral and economic decline. It has a relative abundance of skilled and trained manpower, both overseas and within the country. But these people are demoralized by the trials of the past eight years and stand in need of encouragement and support from outside. The country has a potentially rich agriculture and abundant natural resources. Its new Government has demonstrated a strong and practical commitment to the rehabilitation and development of the country, by clearly stating its economic and social policy and by adopting and starting to implement a comprehensive rehabilitation strategy.

51. The overriding need at the present time is for fast-disbursing balance of payments assistance to enable the economy to start moving again. Associated with this, a series of complementary measures on the Government's part--a budget, early action on the exchange rate, further action on transport and distribution, the establishment of planning and coordination mechanisms in the Government--are needed to facilitate the move to the next phase of development. The sooner the immediate rehabilitation needs are met, the sooner will it be possible for Uganda to start elaborating its longer term needs and priorities.

COUNTRY DATA - UGANDA

AREA
236,000 sq. km.

POPULATION
12.4 million (mid-1978)
Rate of growth: 3.3%

DENSITY
52.5 per sq. km (1978)

POPULATION CHARACTERISTICS (1977)	
Crude Birth Rate (per 1,000)	45.0
Crude Death Rate (per 1,000)	14.0

ACCESS TO SAFE WATER (Ca. 1975)	
Percent of population	35.0

NUTRITION (Ca. 1975)	
Calorie intake as percent of requirements	90.0
Per capita protein intake (grams per day)	54.0

HEALTH (Ca. 1975)	
Population per physician	28,330
Population per hospital bed	640

EDUCATION	
Adult literacy rate % (1960)	35
Primary school enrollment % (Ca. 1975)	51

GNP PER CAPITA IN 1978 a/: US$260

Gross National Product in 1978 a/ (estimates) — **ANNUAL RATE OF GROWTH** (% constant prices)

	US$ Million	%	1968-73	1973-78	1978
GNP at market prices	3,260	100.0	3.0	-0.7	-4.8
Gross fixed investment	156	4.8	-8.9	-11.1	-18.7
Gross national saving	139	4.3	0.1	-19.8	98.2
Current Account Balance	-131	-4.0	.	.	.
Export of Goods and NFS	332	10.2	-2.2	-12.4	-12.0
Import of Goods and NFS	458	14.0	-8.1	- 5.2	-30.0

OUTPUT IN 1978 a/

	US$ Million	%
Agriculture	1,842	56.5
Industry	235	7.2
Services	1,183	36.3
Total	3,260	100.0

CENTRAL GOVERNMENT FINANCE b/

	Shs. Million	% of GDP a/	
	1977/78	1977/78	1972/73
Revenue	5,856	23.4	11.7
Current Expenditure	4,113	16.4	14.0
Current Surplus	1,743	7.0	-2.3
Capital Expenditure	1,755	7.0	5.2

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a/ GNP, GDP, Per Capita GNP, investment, saving and sectoral output data have been calculated by the same conversion technique as the World Bank Atlas and are subject to review and further elaboration. All other conversions to dollars in this table are at the average exchange rate prevailing during the period concerned.

b/ Fiscal years are July 1st to June 30th.

. Not Applicable.

October 1979

COUNTRY DATA - UGANDA

MONEY, CREDIT AND PRICES

	1974	1975	1976	1977	1978	1979 June a/
	(Shs. million outstanding end of period)					
Money Supply	3,010	3,257	4,497	5,787	7,053	8,371
Net Credit to Government	2,895	3,532	4,869	5,532	7,207	8,178
Credit to Private Sector	1,570	1,681	1,912	2,834	3,207	3,334
	(Percentages or Index Numbers)					
Money as % of GDP b/	17	16	19	23	29	..
Kampala Low Income Cost of Living Index (1960 = 100)	341	410	601	1,133	1,546	..
Annual percentages changes in:						
Cost of Living Index	67	20	47	89	37	..
Net Credit to Government	35	22	38	14	30	33
Credit to Private Sector	30	7	14	48	13	3

BALANCE OF PAYMENTS

	1975	1976	1977	1978
	(Million US$)			
Export of Goods, NFS	248	333	553	332
Imports of Goods, NFS	313	281	471	458
Resource Gap	-65	52	82	-126
Factor Payments (net)	-4	-7	-11	-1
Net Transfers	13	2	-3	-3
Current Account Balance	-56	47	68	-130
Net Private Long-Term Capital	-5	-9	-15	-20
Net MLT Borrowing				
Disbursements	29	11	24	18
Amortization	10	11	29	5
	19	-	-5	13
Other Capital (net) d/	42	-36	-49	153
Increase in reserves	-	-2	1	-14
Gross reserves (end year)	28	37	38	51
Petroleum imports e/	51	55	55	39

MERCHANDISE EXPORTS (AVERAGE 1975-78)

	US$ Mln.	%
Coffee	337.3	87.9
Cotton	21.5	5.6
Tea	11.8	3.1
Copper	4.8	1.3
Tobacco	2.0	0.5
Other	6.4	1.7
Total	383.8	100.0

EXTERNAL DEBT, DECEMBER 31, 1977 c/

	US$ Mln.
Public Debt, including guaranteed, outstanding and disbursed	215.0
	%
Public Debt Service Ratio 1977 c/	3.3

IBRD/IDA LENDING (December 31) (Million US$)

	1977		1978	
	IBRD	IDA	IBRD	IDA
Outstanding and Disbursed	2.4	43.0	2.1	44.5
Undisbursed	-	4.9	-	3.2
Outstanding incl. Undisbursed	2.4	47.9	2.1	47.7

RATE OF EXCHANGE

	Annual Averages		
	1977	1978	Jan.-June 1979
US$1.00 = Sh.	8.266	7.692	7.528
Sh. 1 = US$	0.121	0.130	0.133

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a/ Provisional
b/ GDP has been estimated using the same technique as indicated in footnote a/ on page 1.
c/ External public debt data may be incomplete. The public debt service ratio is debt service as a percentage of exports of goods and non-factor services.
d/ Includes accumulation of arrears.
e/ Crude and derivatives
.. Not available
. Not applicable

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