NATIONAL PLANNING AUTHORITY

MONTHLY ECONOMIC UPDATE

Uganda Vision 2040

AUGUST 2017

Key Economic Highlights

(i) The real GDP for Q3 for FY 2016/17 grew by 1.8 percent compared to the growth of 1.4 percent registered in Q2 due to improved performance in agriculture, services and industry sectors

(ii) The overall recovery in growth is being driven mainly by the improved activity in the agricultural sector (particularly food crops) arising from better weather conditions

(iii) There was a slight decline in both headline and core inflation in the month of August and they remain within the single-digit target as reflected in NDPII

(iv) The overall fiscal operations in the month of June 2017 resulted in a larger overall fiscal deficit of UGX 619.1bn arising from a shortfall in domestic revenues and grants recorded at UGX 1,512.6bn against rising government expenditures that stood at UGX 2,131.7bn.

State of the Economy

1.1. Real Sector Developments

The recently released Quarterly Gross Domestic Product (QGDP) estimates for Q3 of FY 2016/17 from Uganda Bureau of Statistics (UBOS) indicate a pick-up in the growth of the economy. The real GDP for Q3 for FY 2016/17 grew by 1.8 percent compared to the growth of 1.4 percent registered in Q2 (see Figure1) due to improved performance in agriculture, services and industry sectors. Value added in Agriculture sector is estimated to have increased by 3.4 percent in Q3 from an earlier decline of 0.4 percent in Q2 due to improved performance of food crops activities following improved rainfall patterns.

However, there was a reduction in value added in cash crops and fishing activities. Services and industry sectors also registered improvements in their performance due to slight improvements in mining, ICT, as well as financial and insurance services.

Figure 1: Quarter-to-quarter GDP

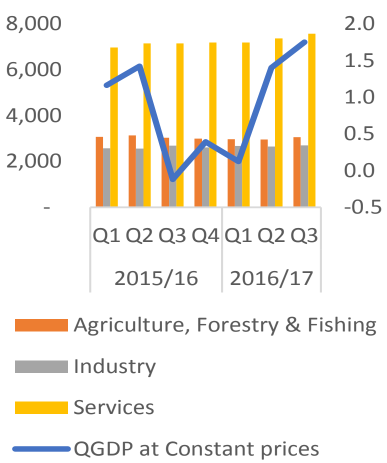
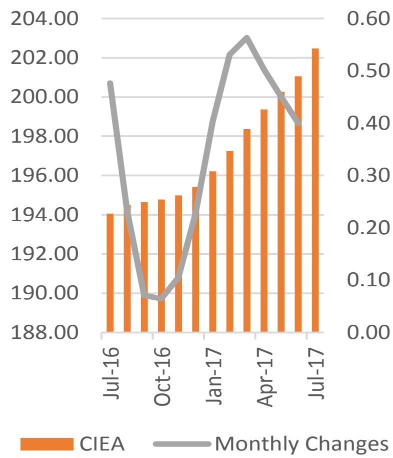
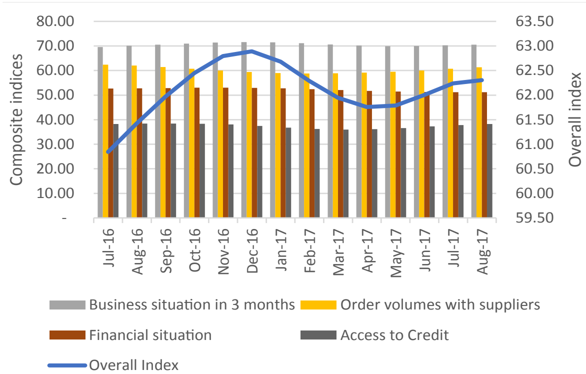


Figure 2: Monthly CIEA



Source: BOU, 2017

Figure 3: Business Tendency Indicators



Source: Bank of Uganda

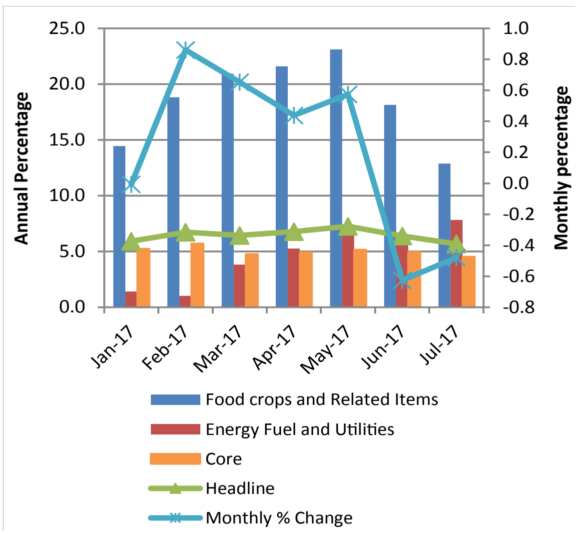
Inflation

There was a slight decline in both headline and core inflation in the month of August and both remain within the single-digit NDPII target. Headline inflation fell to 5.2 percent from 5.7 percent in July 2017 due to a decline in food crops inflation that declined to 11.8

percent from 12.9 percent in July owing mainly to a fall in prices of fruits. Core Inflation for August 2017 fell to 4.1 percent down from 4.5 percent in July owing mainly to a fall in services inflation to 3.3 percent down from 4.0 percent in July and the continued easing of the monetary policy through the Central Bank Rate (CBR). Energy, Fuels and Utilities (EFU) inflation registered remained unchanged at 7.8 percent as recorded in July 2017.

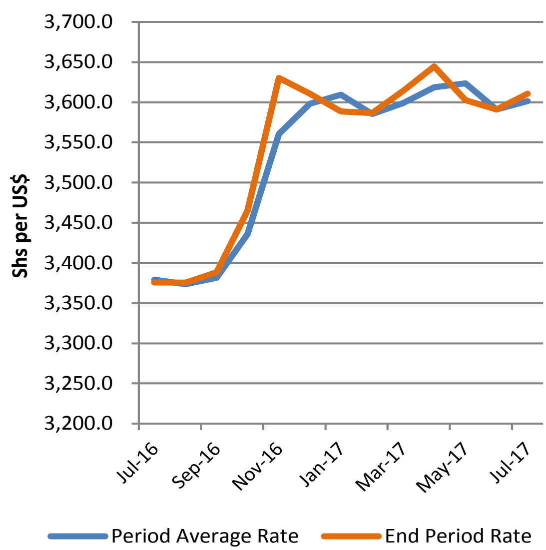
The Annual Inflation for solid fuels (charcoal and firewood) though increased to 7.1 percent compared to 6.7 percent registered in July 2017. However, Liquid Energy Fuels inflation declined to 5.7 percent compared to 6.4 percent recorded in July 2017.

Figure 4: Decomposed CPI, (Base: 2009/10 = 100)



Source: Bank of Uganda

Figure 5: Period Average and End Period Rates



Source: Bank of Uganda

1.2. Monetary and Financial Sector Developments

There is a wide disparity between the average lending rate of commercial banks (21.1 percent as at end of June 2017) at and the CBR (10 percent). Since the beginning of the year the Central Bank has cautiously and continuously been easing monetary policy in order to spur growth by lowering the CBR which currently has fallen to 10 percent up from 11.5 percent in February 2017. Also, in line with the decline in the CBR (easing of monetary policy stance) the average yields on the 91-day, 182-day and the 364-day treasury bills declined to 9.5, 9.7 and 10.4 percent respectively in July relative to 10.1, 10.8 and 12.0 percent in June.

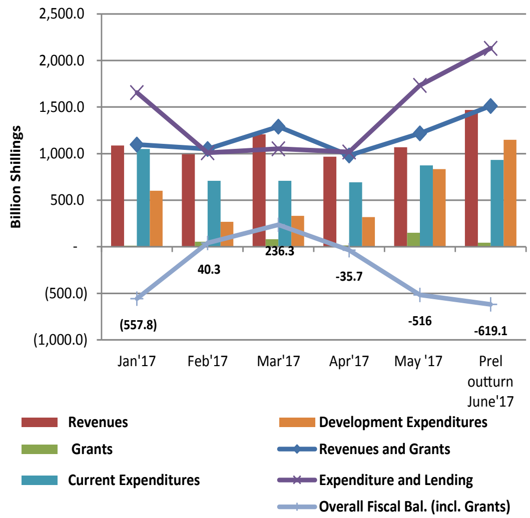
The financial market remained relatively stable in July, with mild volatility in the exchange rates supported by inflows from exports of coffee and other goods . As at the end of July, the period average exchange rate stood at UGX 3601.5 per USD while the end period exchange rate was recorded at UGX 3610.9 per USD indicating a rise of only 0.3 percent and 0.6 percent respectively (see Figure 5).

1.3. Fiscal Sector Developments

The overall fiscal operations in the month of June 2017 resulted in a larger overall fiscal deficit of UGX 619.1bn arising from a shortfall in domestic revenues and grants recorded at UGX 1,512.6bn against rising government expenditures that stood at UGX 2,131.7bn (see Figure 6) . The worsened fiscal operations were largely driven by increased development expenditures (38 percent) as a result of increased disbursement mainly for concessional projects along with the Hydro Power Projects and utilization of previously unspent funds for development projects.

The domestic revenues nonetheless rose by 37.3 percent to UGX 1,468.2bn in June 2017 while the grants declined from 70 percent to 44.4 percent. The expenditures on the other hand were marked by a moderate increase in current expenditures whereas the development expenditures increased by 38 percent.

Figure 6: Overall Fiscal Operations



Source: MoFPED

1.4. External sector Developments

Developments in the external sector point towards a narrowing of trade deficit in the FY2016/17 amounting to USD 1,391.7 million from USD 1,886.6 million recorded in 2015/16 (Table 1). This was driven by a reduced import bill and growth in the value of exports during the period, especially coffee exports. However, the monthly performance at the end June reveals a different picture, with the trade deficit widening by 11 percent to USD 134.1 million (Figure 7).

The adverse performance during the month of June was largely due to a fall in the value of exports, particularly non-coffee exports. The import bill decreased by 3.4 percent during the same period as a result of declining government project imports.

Figure 7: Monthly Trade Balance (USD millions

Table 1: Trade Balance (USD millions)

	May-17	Jun-17	FY'15/16	FY'16/17
Trade Balance	**-120.575**	**-134.125**	**-1886.640**	**-1391.759**
Total Exports	**310.23**	**282.18**	**2,687.83**	**3,168.80**
Coffee (Value)	47.57	49.59	**352.03**	**490.41**
Non-Coffee formal exports	218.72	188.06	**1,946.10**	**2,189.62**
ICBT Exports	43.94	44.53	**389.70**	**488.76**
Total Imports (fob)	**430.81**	**416.31**	4,574.47	4,560.56
Government Imports	37.57	18.99	494.18	279.22
Project	35.31	15.58	449.09	252.99
Non-Project	2.26	3.41	45.09	26.22
Formal Private Sector Imports	360.80	370.91	3,862.65	3,947.70
Oil imports	60.37	66.17	645.92	693.80
Non-oil imports	300.43	304.75	3,216.73	3,253.90
Estimated Private Sector Imports	32.44	26.40	217.64	333.64

Source: BoU

In terms of direction of trade, COMESA has the largest share of Uganda's trade exports (48 percent) mainly to Kenya and South Sudan, followed by the European Union with a share of 19.96 percent while the imports mainly come from Asia (especially China) and COMESA with shares of 47.2 percent and 14.9 percent respectively.

2.0. Other Developments in the Economy

2.1. Revisiting the Costs of Tax Incentives

Tax Incentives or exemptions are one of the issues that have dominated public discussions recently. The key issue of concern is whether issuing tax exemptions has indeed stimulated FDI or instead exacerbated the problem of domestic revenue mobilisation.

Tax incentives are deductions, exclusions, or exemptions from a tax liability, offered as an enticement to engage in a specified activity (such as investment in capital goods) for a certain period. Studies reveal that on average, UGX 75bn is spent by the government every financial year on exemptions on imports and excise duties and tax holidays. A study conducted by civil society organizations in Uganda including SEATINI and Civil Service Budget Advocacy Group (CSBAG)

reveals that UGX 77bn was spent in FY 2016/17 to pay taxes for various companies with tax exemptions and holidays like BIDCO Oil Refineries Ltd; Aya Investments Ltd; Steel and Tube; Cipla Quality Chemicals; Uganda Electricity Generation Company Ltd; and Uganda Electricity Transmission Company Ltd. The problem is that there is limited evidence of quantifiable benefits that have been derived from such tax incentives.

A 2015 joint report by the IMF, OECD, UN and WORLD BANK on effective and efficient use of tax incentives for investment by low income countries, reveals that there are many instances in which tax incentives are reported to be redundant, meaning that investment would have been undertaken even without them. Additionally, their fiscal cost can be high, reducing opportunities for much-needed public spending on infrastructure, public services or social support, or requiring higher taxes on other activities.

The study further highlights that effective use of tax incentives needs careful designing to ensure benefits by the government and an enabling environment like adequate infrastructure, and macroeconomic stability. It further reveals that governance is key in implementation of such incentives to prevent instances of corruption and rent seeking. There is therefore need to put into consideration the aforementioned issues prevent instances of redundant tax incentives that do not contribute to development of the country.

2.2. Restructuring Government Agencies to enhance Effectiveness and Efficiency of Government

The government is currently faced with unprecedented pressure to reduce public spending in order to fit government's activities into the limited resource envelope. To this effect, a directive was issued to the Ministry of Public Service to assess the impact of consolidating, rationalizing and downsizing the public service through reducing the number of government agencies. The outcome from the review should provide suitable, recommendations to restructure and disband unnecessary Ministries, Departments and Agencies (MDAs), programs and to merge duplicated functions. The directive has also been as a result of mounting dissatisfaction by the public with regard to unnecessary spending of public funds and poor public service delivery.

Many countries have indeed succeeded in improving efficiency in government spending through undertaking such transformational actions like restructuring the public service including Uganda. In 1990, a policy framework for comprehensive civil service reform was formulated by the Public Service Review and Reorganization Commission in an effort to repair the broken down civil service. Its implementation resulted in substantial real increases in salaries, a decrease in the number of ministries from 38 to 21, and the rationalization of their functions .

France also successfully undertook a civil service reform program "Révision générale des politiques publiques (RGPP)" to achieve structural reductions in the country's public expenditures. The key factors that led to the success of the reform include; the inherent will and vision by leaders at the highest level of government and invitation of public scrutiny throughout the process for transparency (Tadjeddine, 2011). The team bestowed with the duty of reviewing the various government MDAs should therefore utilise the experiences from countries that have successfully undertaken such reforms.

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Tax Incentives. (n.d.). Retrieved from Business Dictionary http://www.businessdictionary.com/definition/tax-incentive.html

The **National Planning Authority** was established by the **NPA Act (15 of 2002)** in accordance with Article 125 of the 1995 Constitution of the Republic of Uganda to produce comprehensive and integrated development plans for the country, elaborated in terms of the perspective Vision, long and medium–term plans.

NATIONAL PLANNING AUTHORITY
Planning House , Clement Hill Road Plot 17B,
P.O. Box 21434.Kampala - Uganda
Tel: +256 414 250 229 / 0312 310 730

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