The Challenges of Debt Sustainability in Africa

African Forum and Network
on Debt and Development

The Case of Uganda

About AFRODAD

AFRODAD Vision

AFRODAD aspires for an equitable and sustainable development process leading to a prosperous Africa.

AFRODAD Mission

To secure policies that will redress the African debt crisis based on a human rights value system.

AFRODAD Objectives include the following:

1 To enhance efficient and effective management and use of resources by African governments;

2 To secure a paradigm shift in the international socio-economic and political world order to a development process that addresses the needs and aspirations of the majority of the people in the world.

3 To facilitate dialogue between civil society and governments on issues related to Debt and development in Africa and elsewhere.

From the vision and the mission statements and from our objectives, it is clear that the Debt crisis, apart from being a political, economic and structural issue, has an intrinsic link to human rights. This forms the guiding philosophy for our work on Debt and the need to have African external debts cancelled for poverty eradication and attainment of social and economic justice. Furthermore, the principle of equity must of necessity apply and in this regard, responsibility of creditors and debtors in the debt crisis should be acknowledged and assumed by the parties. When this is not done, it is a reflection of failure of governance mechanisms at the global level that protect the interests of the weaker nations. The Transparent Arbitration mechanism proposed by AFRODAD as one way of dealing with the debt crisis finds a fundamental basis in this respect.

AFRODAD aspires for an African and global society that is just (equal access to and fair distribution of resources), respects human rights and promotes popular participation as a fundamental right of citizens (Arusha Declaration of 1980). In this light, African society should have the space in the global development arena to generate its own solutions, uphold good values that ensure that its development process is owned and driven by its people and not dominated by markets/profits and international financial institutions.

AFRODAD is governed by a Board of seven people from the five regions of Africa, namely East, Central, West, Southern and the North. The Board meets twice a year. The Secretariat, based in Harare, Zimbabwe, has a staff compliment of Seven programme and five support staff.

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Preface

The World Bank (WB) and the International Monetary Fund (IMF), as the leading lending agencies, have been under mounting pressure to deal with a wide range of debt sustainability challenges. The challenges have refused to subside. Instead they continue to stimulate urgent need for a new debt sustainability framework and debt management orientation that can allow for the borrowing economies to break the vicious circle of unending distress. The Heavily Indebted Poor Countries (HIPC) framework and the 2005 G8 Debt deal which is generally a compromise of the US and UK proposals are yet to shake down into a coherent strategic compact (with the poor countries of the borrower economies) capable of addressing unsustainability challenges facing the debt burden of all the poor economies of the South.

In the recent past; the Bank and the Fund have paradoxically demonstrated a generous willingness to admit the 'systematic over-optimism' of the previous International Financial Institutions' debt sustainability calculations and measures. From time to time, creditors have however, failed to put sufficient political will, resources and serious analysis into the debt reduction operations. Debt reduction targets are set and reset arbitrarily - writing off 30 percent, then 50 percent, and so on-rather than based on serious assessments of the needs of each country.

In order to operationalize debt sustainability existing frameworks such as HIPC and the Country institutional Policy Assessment (CPIA) need a revisit. One way of looking at resolving the Third World debts would be by first securing an agreement on the working definition of debt sustainability. This implies revisiting the concept of debt sustainability as given by the IMF, identifying its short-falls and seeking ways of redressing them so as to enable the initiative to work better for the poor countries. In so doing, the issues of both domestic and external debt, conditionalities, domestic revenue as well as the role of external shocks in the fiscal and monetary policies of the poor country become very important.

This case study looks into the debt sustainability issue taking cogniscence of the domestic debt issues facing the African government (s) at national level. It argues that debt sustainability should not be defined as just meeting the debt indicators as given by the international financial institutions, but it should help the country to break from its debt burden-both external and domestic and be on the path to development. Thus the study among other things advocates for a holistic definition of debt sustainability and the agreement on indicators that a developing country is comfortable to work with than just focusing on of exports earnings to the net present value of all future debt servicing payments. In short, Debts are should be considered 'sustainable' when the debt service burden leaves the Low income countries (LICs) with sufficient funds to meet their human rights obligations under the internationally agreed Millennium Development Goals (MDGs).

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Acronyms And Abbreviations

AGOA	African Growth and Opportunity Act
APIR	Annual PEAP Implementation Review
APRM	African Peer Review Mechanism
BoU	Bank of Uganda
CCS	Commitment Control System
CS	Civil Society
CSOs	Civil Society Organizations
EDS	External Debt Strategy
ERP	Economic Recovery Programme
FENU	Forum for Education NGOs in Uganda
GBS	General Budget Support
GDP	Gross Domestic Product
GNI	Gross National Income
GNP	Gross National Product
GoU	Gov't of Uganda
FINMAP	Financial Management and Accountability Programme
FY	Fiscal Year
HIPC	Highly Indebted Poor Countries Initiative
IDA	International Development Association
IFMS	Integrated Financial Management System
IMF	International Monetary Fund
LTEF	Long Term Expenditure Framework
MDGs	Millennium Development Goals
MFPED	Ministry of Finance, Planning and Economic Development
MTEF	Medium Term Expenditure Framework
NPV	Net Present Value
NRM/A	National Resistance Movement/ Army
NWSC	National Water and Sewerage Corporation
PEAP	Poverty Eradication Action Plan
PFAA	Public Finance and Accountability Act
PMA	Plan for Modernization of Agriculture
PPAs	Priority Programme Areas (funded under PAF in Uganda)
PPDAA	Public Procurement and Disposal of Assets Authority
PRSC	Poverty Reduction Support Credit
PRSP	Poverty Reduction Strategy Paper
SWGs	Sector Working Groups
PV	Present Value
UDN	Uganda Debt Network
UEB	Uganda Electricity Board
UShs	Uganda Shillings
UTL	Uganda Telecom
WB	World Bank

Executive Summary

Issues pertaining to debt, aid delivery and management, and debt sustainability, remain central to discourses on national, regional and global development. The poor nations of the world have had millions of their people living in poverty, partly arising out of the rise of the debt and burden of repayment. Further, repayment has been to the detriment of spending on key sectors and programmes for social (such as human development) and economic advancement of such nations.

Public debt has stifled the countries' capacity to spend on their respective national development priorities to realize poverty reduction, the Millennium development Goals and other aspirations. Effort to off-set the debt burden for the poor nations has been through schemes such as the Highly Indebted Poor Countries (HIPC) Initiative in the 1990 and 2000s, as well as the 2005 Multilateral Debt Relief Initiative (MDRI) under the auspices of the Great 8 (G8) Summit at Gleneagles.

It is through such development discourses coupled with the global aid and debt reforms that issues, which underpin debt sustainability analysis, are rooted. Debt sustainability as a concept is basically considered as the level of debt at which the debtor country is able to meet its current and future debt service obligations in full, without recourse to further debt relief or rescheduling; or avoiding accumulation of arrears, while allowing an agreeable level of economic growth and development[1]. The study, therefore, examines this spectrum with Uganda as a case.

Is Uganda's Debt Sustainable?

In an endeavour to fund her development agenda, under the Economic Recovery Programme (ERP) and the Poverty Eradication Action Plan (PEAP) priorities, Uganda attracted a lot of donor funding. While, this was good, it led to a situation of debt burden for the country. Eventually, it was one of the beneficiaries of the above debt relief initiatives. By registering 100 percent debt cancellation under the MRDI, Uganda's total external debt had sharply declined from US$4.5 billion in 2005 to about US$1.1 billion by March 2007. A 2007 Debt Strategy was instituted to provide policy guidance towards debt sustainability for Uganda. Indeed, the study established that all the debt related indicators for Uganda were below their thresholds, putting Uganda at a comfortable situation.

The full implementation of MDRI helped to deliver faster and deeper relief for Uganda and to achieve debt sustainability, after reducing the NPV of external debt to exports ratio to about 50 percent in FY 2006/07. This again was obviously well below the threshold of 200 percent. Whether Uganda is able to have a sustainable debt or not will largely be determined by the existing debt overhang and the prospective path of its fiscal deficits together with the evolution of its repayment capacity.

To determine whether Uganda's current level and rate of indebtedness is sustainable or not, requires one (within the country's macro economic framework) to note that debt sustainability is a function of cost of borrowing and performance of the economy, in particular exports. It would also be taken on from the perspective of the country's ability to continuously meet repayment obligations without compromising budget expenditure priorities. Beyond the budget, the availability of foreign exchange is also crucial, particularly for external debt. Meanwhile, domestic debt is constrained by demands on the domestic financial sector, including availability of credit to the private sector. A reflection on additional indicators yields a more precarious debt position for Uganda. The indicators for debt sustainability have to include, inter alia the debt stock in relation to GDP or domestic revenue, the Net Present Value (NPV) of debt in relation to GDP, foreign exchange reserves or exports, and debt stock in relation to private sector credit.

Challenges to Debt Sustainability

Although Uganda's debt is considered sustainable, the degree of risk (thus falling short of debt sustainability) in meeting the intended achievements seems to be high.

Uganda still experiences challenges of poor public expenditure management, lack of a strategic framework for domestic debt management and prudent policies on Government guarantees and effective monitoring of compliance to regulations.

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[1] http://siteresources.worldbank.org/INDEBTDEPT/Resources/DSAGUIDEv7.pdf

Further Government had the task of offsetting pension arrears and working against undermining the growth of the private sector through delayed payment of bills. Others included flouting and by-passing designated systems, limited institutional absorptive capacities, a huge cost for macroeconomic management and failure of Parliament to duly exercise its oversight role.

Amongst other key strategies, the above challenges also require adherence to the exiting laws, regulations and procedures on prudent public finance management. This would contribute to fostering of good governance as well as external debt and loan contraction, management, reporting and payback, as one of the mechanisms in dealing with the overall call for debt sustainability for Uganda. In a nutshell, with the MDRI, Uganda's debt remained sustainable.

1.0 Introduction

Issues pertaining to debt, aid delivery and management, and sustainability, remain central to discourses on national, regional and global development. The poor nations of the world have had millions of their people living in poverty, partly arising out of the rise of the debt and burden of repayment. Repayment has been to the detriment of spending on key sectors and programmes for social (such as human development) and economic advancement of such nations.

The debt burden can be traced from the fact that since the 1960s and 1970s, "commercial banks (London Club) began lending lavishly to the Third World countries without much thought about how the money would be used or whether the recipients had the ability to repay it. Later debts came from bilateral loans from individual Western governments (Paris Club)"[2]. Sadly, most of the resources acquired through debt went to financing military supplies to shore up oppressive regimes and large-scale development projects with minimal participation of citizens in determining the necessity and suitability of those projects. Other resources acquired were lost to corruption, misuse, waste and later on debt servicing.

> ***The West did not want to lose their loans, so they clubbed together and obtained the support of the International Monetary Fund (IMF) for a scheme to reschedule the debts. Since then the IMF and the World Bank - the two main international financial institutions - have been involved in lending money and rescheduling debt in countries that cannot pay the interest on their loans. But their loans add to the debt burden and come with conditions***[3]

The tutorship of the IMF and World Bank led to economic reforms under the Structural Adjustment Programs (SAPs)[4] since the 1980s, for the debt riddled countries. The genesis of various debt relief schemes was rooted in off-setting the debt burden of those debt riddled countries, genuinely or otherwise. The debt and aid-development paradigm has been shaped by, amongst other things, schemes like the Highly Indebted Poor Countries (HIPC) Initiative in the 1990 and 2000s, as well as the 2005 Multilateral Debt Relief Initiative (MDRI) under the auspices of the Great 8 (G8) Summit at Gleneagles. In particular, the issue of debt sustainability has been considered within the broader[5] ream of such events as the 2002 Monterrey (Mexico) summit. Others included the 2000 Millennium Development Goals MDGs) launched under the United Nations (UN), as well as the High-Level Forum (2005), which culminated in the Paris Declaration on Aid Harmonization and Effectiveness.

The HIPC Initiative was basically an agreement amongst official creditors[6], to help the poorest and heavily indebted nations to overcome unsustainable debt, to pave way for those nations to address the issues of poverty reduction and development. The Initiative is open to the poorest countries, those that: (1) are eligible only for highly concessional assistance such as from the World Bank's International Development Association (IDA) and the IMF's Poverty Reduction and Growth Facility (formerly called Enhanced Structural Adjustment Facility); (2) face an unsustainable debt situation even after the full application of traditional debt relief mechanisms; and (3) have a proven track record of implementing strategies and reforms through developing a Poverty Reduction Strategy Paper (PRSP) and building the foundation for sustainable economic growth[7]. Most of the beneficiary countries were in Africa. The IMF is the administrator of the HIPC Initiative.

While the HIPC Initiative was in place, debt still remained a challenge to a number of the beneficiaries. This further necessitated other mechanisms for debt relief, of which the MDRI features prominently. The MDRI offered 100 percent debt cancellation of the most indebted countries of the world that had graduated from HIPC Initiative, most of which are in Africa.

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[2] *http://www.uiowa.edu/ifdebook/faq/faq_docs/HIPC.shtml*

[3] http://www.uiowa.edu/ifdebook/faq/faq_docs/HIPC.shtml

[4] The SAPs were perceived to include measures for countries to repay their debts through earning more hard currency, increasing exports while decreasing imports, and fostering economic stability

[5] The agenda for the Monterrey summit was centered on financing for Development At the Summit, the greatest developed and donor nations around the world pledged to commit 0.7 percent of their GNP as aid to international development; Meanwhile, the July 2005 G8 Gleneagles summit pledged commitment to better and impact-oriented aid.

[6] They include commercial creditors (London Club), bilateral creditors (Paris Club), multilaterals (IMF, WB and AfDB)

[7] http://www.uiowa.edu/ifdebook/faq/faq_docs/HIPC.shtml

The MDRI also pledged a doubling of aid support, from about USD$12 billion in 2004 to $25 billion per year by the year 2010. This was one of the strategies to achieving the MDGs.

MDG 8 of building a global partnership for development, was in particular perceived to advantage the developing nations through 3 key elements; (a) fair trade and transparent global trading regime (b) debt relief, to capacitate funding country development programmes and (c) increased official development assistance (ODA) by the developed nations of the world, for the developing nations to hasten their effort on the road to realisation of good governance, transparency, youth employment, access to essential drugs, information and better technologies.

It is through such development discourses coupled with the global aid and debt reforms that issues, which underpin debt sustainability analysis, are rooted. Debt sustainability as a concept is basically considered as the level of debt at which the debtor country is able to meet its current and future debt service obligations in full, without recourse to further debt relief or rescheduling; or avoiding accumulation of arrears, while allowing an agreeable level of economic growth and development[8]. The study, therefore, examines this spectrum with Uganda as a case.

Uganda's history of debt was traceable from the 1970s. The emergence of the National Resistance Movement/ Army (NRM/A) government in 1986, hitherto a guerrilla force, brought to Uganda a spell of relative political and economic stability. The government then attracted substantial sums of resources for Uganda; mainly generated either through both domestic and external borrowing or otherwise. Whereas this was a good gesture, it inherently created its own predicament through increased stock of public debt. Government even guaranteed loans to the public and private sector players, some of whom subsequently failed in their obligations to pay back. Such loans were then added to the Government's overall domestic and external debt liabilities. Undertaking an analysis of debt sustainability for Uganda, therefore, looked at the cumulative debt in respect to domestic borrowing (government securities and arrears-outstanding bills beyond a given Fiscal Year, external borrowing and government-guaranteed debt (since the guarantees constituted contingent liabilities on the part of the Government).

Through the study, it was also noted that under the tutorship of the Bretton Woods institutions and other entities like the European Union, Uganda in 1987 implemented a neo-liberal coated Economic Recovery Programme (ERP). The ERP mainly depended on externally borrowed resources and so did the PEAP. The PEAP is Uganda's PRSP. The Government had perceived that continued large-scale borrowing to finance public expenditure would reduce poverty at a very fast and desirable rate. According to Government officials this desire had been achieved, even though the civil society respondents were sceptical about its extent. Uganda's sharpest debt increases in fact occurred during 1987, 1989 and 1990. Worth noting, however, was that the borrowing was, by and large, in the absence of a national debt acquisition and management strategy for both domestic and external debt.

1.1 Statement of the Problem

Debt relief initiatives, coupled with the international community having set the development goals for the new millennium, have renewed attention to the nature and quality of financing for development programmes aimed at achieving the global and national development agendas. There are, however, challenges that pertain to debt sustainability, frameworks and practices that remain apparent. The objective of this project is to identify the contribution of the HIPC and the MDRI programme in the context of assessing the debt sustainability scenarios of developing countries with a view to ascertaining whether the frameworks have been realistic in understanding both the endogenous and exogenous shocks on which these countries operate.

Specifically, the research aims to:

- Give an update of Uganda's HIPC experience and examine the nature and scope of the debt relief realized.
- Describe and critically assess the IMF's debt sustainability analysis of Uganda.

8 http://siteresources.worldbank.org/INDEBTDEPT/Resources/DSAGUIDEv7.pdf

- Ascertain as to whether the DSA calculated has taken into consideration Uganda's strategy for poverty reduction and the MDGs, and make a determination as to whether a balance has been struck between financing for development and poverty reduction that does not impair future generations with a heavy debt burden.

The methodology employed under the study included desk reviews and key informant interviews. A team of researchers, including a Principle Researcher, first discussed the Terms of Reference and also shared their expectations in undertaking the study. Draft questionnaires were developed, discussed and modified by all the researchers, for the following categories of respondents: government officials (from Ministry of Finance, Planning and Economic Development, Parliament, Macroeconomic Management Department, and the Budget office), civil society organisations, and the IMF. Details regarding respondents may be found in Annex 1.

2.0 Uganda's Experience With HIPC

Uganda, undertook a number of policies that paved way for the implementation of the Structural Adjustment Programmes (SAPs) in the early 1980s and 1990s with a view to eradicating poverty.

> ***In the quest for development, Uganda in the 1980s and 1990s adopted policies targeted at poverty eradication (or reduction). Between 1987 and 1995, poverty eradication, indeed, was the key objective of government thinking and planning. This was to coalesce into the Poverty Eradication Action Plan (PEAP) in 1997. Informed by the Millennium Development Goals (MDGs) and other national aspirations, the PEAP has since become Uganda's strategic framework and action plan for arresting poverty by 2017. This was partly the genesis of what made Uganda a darling of the western world and such institutions as the International Monetary Fund (IMF), The World Bank and the African Development Bank (AfDB). The love translated into massive donor and debt relief resources for Uganda's drive out of poverty (genuinely or otherwise).***[9]

Uganda was the first country to benefit from debt relief of the Heavily Indebted Poor Countries (HIPC) Initiative10 in April 1997, whose full maturity/ implementation came in April 1998, while Enhanced HIPC that was committed in February 2000, was fully implemented in May, 2000[11]. In FY 1996/97, the pre-HIPC nominal value of the country's external debt stock stood at US$3.7 billion. In the same period, the net present value (NPV) of debt to exports ratio was 243 percent. Under HIPC 1, during the FY1997/98, Uganda received debt relief worth US$347 million in NPV terms, of which 79 percent was from multilateral institutions (WB, IMF and AfDB); and the WB (IDA) debt relief amounted to nominal US$354 million (equivalent to US $160 million in NPV terms).[12]

Debt-service relief under HIPC 2, from all Uganda's creditors, was approximately US$1.3 billion or US$660 million in Net Present Value terms, which amounted to two-fifths of external debt stock. Including the US$650 million provided under HIPC 1, total debt-servicing under the HIPC Initiative relief harvested approximately US$2 billion[13] for Uganda. Enhanced HIPC was granted to the country arising out her declining terms of trade, a factor that had borne a negative effect on the country's NPV debt to exports ratio in the 1990s.

The World Bank's enhanced HIPC Initiative debt relief for Uganda amounted to nominal US $629 million (an equivalent of US$357 million in NPV terms), which covered about 54 percent of debt service falling due to the International Development Association each year, over the next 20 years beginning with the year 2000. The overall WB debt relief to Uganda under HIPC 1 and 2 totalled approximately US$1 billion (US $517 million in NPV terms). Meanwhile, under the IMF, Uganda was to save about US$210 million (equivalent to US$160 million in NPV terms) from debt servicing, over a 10-year period, covering about 50 percent of Uganda's existing debt-service obligations to the Fund[14].

For those countries that had reached their respective HIPC completion point, the G8 nations agreed to increase their debt relief under the MDRI in July, 2005 at Gleneagles, of which Uganda was a beneficiary. The advent of MDRI provided 100 percent cancellation of eligible debt owed to the International Development Association (IDA), the IMF and AfDB Fund[15]. IMF relief was delivered in January 2006 and included all debt contracted before 31st December 2004, while IDA relief was effective from July 2006 for all debt contracted before 31st December 2003. The African Development Fund relief also provided for all disbursed and outstanding debt owed to the ADF by end-December 2003.

[9] UDN, in an Article, MPs should not compromise their watchdog role, by Julius Kapwepwe, Policy Review Newsletter, Vol. 7 Issue 1 January, 2007

[10] www.worldbank.org/hipc

[11] www.imf.org/external/np/fin/tad/exfin2.aspx?memberkey1=990&date1Key=2008-01-31

[12] http://www.imf.org/external/np/sec/pr/2000/PR0034.HTM

[13] http://www.imf.org/external/np/sec/pr/2000/PR0034.HTM

[14] http://www.imf.org/external/np/sec/pr/2000/PR0034.HTM

[15] MDRI did not currently cover debts owed to IBRD, the AfDB or other Multilateral Banks. It differs from the HIPC Initiative, in that MDRI does not include debt relief by any bilateral & commercial creditors.

2.1 Evaluation of HIPC

For Uganda, even with the debt relief enjoyed, as discussed above, the pre-MDRI debt picture was worrisome. The contribution of HIPC, as compared to MDRI, was negligible. For instance, by end of FY 2005/06, the country's external debt amounted to approximately UShs 8,360 billion, equivalent to 79 percent of Uganda's total debt stock.

The stock itself stood at about 61 percent of GDP[16] then. Some members of the civil society also argued that under the HIPC Initiative, the creditors really experienced minimal effect from the hitherto accumulated unpaid (bills) debt by Uganda that was offset through this Initiative. The returns siphoned out of the debtor countries already, through debt servicing, even though with difficulty, were adequate profits for those creditors to negate the outstanding bills. In any case "the creditors, whether individual, private sector, commercial, bilateral or multilaterals are all a racket of individuals and agencies systematically conniving to perpetually rob Uganda and Africa as a whole of her precious resources", observed a respondent from civil society.

So, by registering 100 percent debt cancellation under the MRDI, Uganda's total external debt had sharply declined from US$4.5 billion in 2005 to about US$1.1 billion by March 2007. In-other-words, Uganda no longer had to pay hefty sums through debt servicing and amortisation to the various creditors. Rather, the country was to annually channel such funds to programmes perceived to contribute to poverty reduction and national development. Debt relief in this context was not about the country receiving funds from anywhere else, but re-channelling what it would have paid to offset debt, for funding local priorities, programmes and initiatives. More precisely, the total debt stock of Uganda at end FY 2006/07, with the MDRI taken into account, was approximately UShs 4,633 billion or 23 percent of GDP, of which approximately 12 percent of GDP was external debt[17].

Uganda channelled the debt relief resources in due of HIPC Initiative to key programmes perceived to have direct and indirect as well as short-term and long-term impact on the overall poverty reduction. Within the framework of IMF requirement for a Poverty Reduction Strategy Paper under the Initiative, Uganda implemented the Poverty Eradication Action Plan (PEAP)[18]. The Poverty Action Fund (PAF) as a special basket mainly for debt relief resources was introduced in the national budget in 1998 as a key PEAP component to operationalise programmes such as the five Priority Programme Areas (PPAs)[19] and their respective sub-programme apparatus to poverty reduction[20]. The PAF was instituted against the setting that basic services in Uganda had long been under-funded. Table 2.1 below gives a highlight of the PAF resource allocation for selected financial years.

Table 2.1 PAF) Expenditure in Uganda, between FY 2003/04 and 2007/08 (in billion UShs)

Sources	FY 2003/04	FY 2004/05	FY 2005/06	FY 2006/07	FY 2007/08
HIPC	169.62	178.89	98.98	141.84	125.22
Government own resources	233.22	445.00	619.97	741.51	858.88
General donor support	120.77	80.49	42.72	65.05	67.22
Earmarked donor support	120.24	128.13	142.37	142.74	110.54
Total PAF expenditure	743.85	832.51	903.73	1,116.85	1,178.48

Source: MFPED, Budget Speeches, for FY 2006/07 and FY 2007/08

[16] MFPED, Debt Strategy, December 2007
[17] MFPED, Debt Strategy, December 2007, p. 3
[18] PEAP is Uganda's Poverty Reduction Strategy Paper (PRSP)
[19] MFPED, Poverty Eradication Action Plan, A Summary Version, 2002, pp 3-4
[20] The programmes were Plan for Modernization of Agriculture b) Universal Primary Education c) Water and sanitation d) Primary Health Care and e) Rural feeder roads

By nature of its perceived importance to poverty reduction, the PAF was 'ring fenced' so that it does not suffer unprecedented budget cuts in any given financial year. As seen from Table 2.1, the size of PAF resource envelope had been expanding and not only benefited from HIPC and other debt relief initiatives for Uganda but also Government's own generated resources, donor grants and loans. For instance, during the FY 2007/08 PAF budget expenditure was projected at about UShs 1,668 billion (US$930 million). This constituted approximately 39 percent of the discretionary Uganda government budget, which indicated a substantial increase compared with 18 per cent in the FY 1997/98 when the PAF was established.

Beyond debt relief, the volatility of PAF resources could be explained by the country's annual increases in the volume of the domestically generated resources, grants and other bilateral and multilateral support.

The implementation of the PEAP as a whole also continued to attract funding, for example, through the PRSC of the WB. The PAF also received an increase of resources, arising out of the MDRI from US$54 million in FY 2005/06 to US$90 million in FY 2006/07[21] and was expected to keep an upward trend over the medium term (3 years). It should further be noted that in the same FY 2007/08, PAF was allocated the Universal Primary Education at 47 percent, Primary Health Care at 18 percent and, water and sanitation at 7 percent. The rest of the funds were also shared out accordingly to the PAF-supported programmes.

Uganda's pre-MDRI stock of external debt that stood at 61 percent of GDP was most probably already stifling economic growth, development and poverty reduction efforts, for example, through amortization and debt servicing. Indeed, the positive impact of debt relief may have been a key factor in the somewhat impressive growth rates that Uganda had experienced in the post-HIPC period. For instance, Uganda's GDP was estimated to grow from 5.1 in FY 2006/07 to 6.5 percent in FY 2007/08[22].

There were some concerns over the size and use of the fiscal space created by HIPC and MDRI. A rate of change of less than 1.5 percent in the growth rate for a developing country like Uganda was not sufficient to meet the expectations regarding the PEAP, MDGs and other national development expectations. Secondly, unlike debt relief for Uganda under HIPC Initiative, the relief provided through the MDRI arrangement was not targeted to necessarily be channelled into the PAF. In the absence of PAF conditionality or policy dialogue, savings from the MDRI risked being channelled to other priorities as Government may deem fit. There was a fear amongst stakeholders that this was likely to render the vitality of PAF and the whole point for equitable poverty reduction and economic development into jeopardy.

2.1.1 Debt 'Spreading Out' versus 'Front-loading'

In the context of this discussion, Spreading Out means that all debt relief resources, in this case for HIPC Initiative, are forgiven over a period of time, based on their scheduled repayment, servicing commitments. Meanwhile, Front-loading of debt infers that a country's repayment and servicing obligations are forgiven at once, where the financial resources thereof are mobilized and availed immediately and in total, say in a given fiscal year.

During the study, there were mixed views on whether Uganda would be better off with either front-loading or spreading out of debt relief. The civil society respondents suggested that with front-loading of debt relief, the county would not necessarily continue borrowing and risking falling back into debt sustainability. This is because the front-loading mechanism would enable Uganda to have a substantial amount of resources to finance her budget needs and obligations. Furthermore, beyond the fact that Uganda continued to pay large sums of funds as amortization of external debt of about US$80 million annually, [23] front-loading of debt relief would further eliminate the costs associated with debt. The saved resources then would be channelled into the development programmes of the country.

Some of the government and civil society respondents that were supportive of spreading out of debt relief were concerned that Uganda lacked a fully-functional institutional capacity to effectively manage the huge amounts of resources that would be available at once. They further argued that government had registered precedence and issues that tainted its ability since there were accountability gaps and scandals on different occasions.

[21] MFPED, Background to the Budget, 2006/07, 2006
[22] MFPED,Budget Speech, FY 2007/08, June 2007
[23] MFPED,Budget Framework Paper, FY 2007/08, April 2007

This factor was also partly attributed to weak relevant institutional, policy, implementation, investigative and judicature frameworks. One civil society respondent while citing a government source, further illustrated that while, for example, Uganda was a signatory to the principles of the Paris Declaration on Aid Effectiveness and Harmonization, where general budget support was one of the mechanisms to effect the declaration, Uganda still experienced high project funding modality to the tune of about 76 percent of external financing[24] over the medium term. According to the respondent, this was an indication of the lack of confidence in the government's capacity was less-trusted, based on its weaknesses amongst other factors.

Even though the CPIA regarded Uganda as a strong performing country, some respondents still believed that the country experienced poor absorptive capacity; where some loans, even without front-loading of debt relief, were expiring before being utilized.

This expressed weak institutional arrangements and capacity to bear the huge volumes of resources that would come with front-loading; hence, the preference for spreading out of debt relief. Other factors for spreading out of debt relief were to do with macro-economic stability, such as control of inflation and money liquidity in the economy.

Indeed a number of key players in debt relief initiatives had spread out their debt relief offers to Uganda. For instance, the WB had spread out over the next 20 years beginning with the year 2000, while the IMF was over a 10-year period, perhaps, to ensure that Uganda had resources it could ably manage over a period of time. While that could be the case, it was also possible that some of the players in debt relief such as the WB and IMF were earning interest payments through spreading out of debt relief, than if it were done through front-loading.

Meanwhile, some public investments did not have short maturity periods and the returns to plough back for self-sustenance, hence better managed under spreading out of debt relief, so that resources thereof are available over a period of time. Certainly, spreading out of debt would certainly not exert as much pressure and cost on the Central Bank in mopping up and sterilization of money in the economy. Spreading out of debt relief was further relevant in the management of the exchange rate to levels that do not cause macro economic distortions. The PAF example indicated that Uganda's share of expenditures included in the PAF in total national budget spending (excluding donor projects), increased from 17 percent in FY 1997/98 to 24 percent in FY 1998/99 and 1999/00; further growing to 31 percent in FY 2000/01 and about 38 percent in subsequent years. Clearly, therefore, the savings from debt relief were spread out as opposed to front-loading to match with the pace of improved economic capacity and development needs of the country.

Beyond the aforementioned, the spreading out of debt related resources, the civil society members mentioned that this had continued to provide a clear, monitorable and evaluative way of demonstrating the claim that the budget in Uganda was pro-poor. Such monitoring and evaluation was, for example, through the Annual PEAP Implementation Review. All in all, Uganda seemed to have more opportunities and advantages to better utilize the debt relief resources, through spreading out of debt as opposed to front-loading it.

[24] MFPED,Budget Framework Paper 2007/08, April 2007

3.0 Uganda: Debt Sustainability Analysis

3.1 The Context and Assumptions

Debt sustainability for Uganda should be viewed in the context that Uganda is a HIPC Initiative country, and of the government's projection of average annual economic growth rate of about 7 percent[25] in the 1990s and 2000s. Uganda is also under the IMF-administered Policy Support Instrument (PSI). This means that the country no longer needed financial support from the IMF but policy guidance. Uganda's second PSI was approved on December, 2006, with major focus on macroeconomic stability, financial sector deepening and debt sustainability among others.[26]

It was such policy reforms that the country was perceived to meet the said economic growth rate and spur the country on the path to debt sustainability. A closer examination of the economic growth rates, nonetheless, tells a different story. For instance, in the fiscal year 2003/04, real GDP growth for Uganda was estimated at 5.9 percent, while the population growth grew by 3.4 percent[27]. This kind of population growth is not only one of the highest in the world but also had the potential to eat up the economic gains of a country, with various spending pressures on government to meet their needs; thus, contributing to unsustainable debt levels through borrowing.

The total debt stock of Uganda at the end of FY 2006/07, with the most recent Multilateral Debt Relief Initiative (MDRI) taken into account as well, was approximately 4,633 billion shillings.[28] This is 23 percent of GDP, of which approximately 12 percent of the GDP was external debt. The external public debt alone for Uganda was about UShs 2,413 billion, while domestic arrears constituted UShs 540 billion. Government securities stood at UShs 1,680 billion.[29] The study could not easily ascertain the volume of the Government guaranteed debt. Such scenarios posed questions and challenges about Uganda's debt sustainability.

3.2 IMF Assessment of Debt Sustainability of Uganda

The IMF assessment of Debt Sustainability is based on a framework that has major four areas of focus: a) the CPIA; b) HIPC nine year forecast; c) LIC baseline; and d) Risk assessment. The framework was a basis in informing the lending policies, surveillance, policy dialogue and decisions of the creditors such as those under the Paris Club and the World Bank (WB) in determining the volumes of debt relief to accrue to a given country. The framework was also instrumental in informing decisions on the new financing that a country would be receiving through grants and/ or loans.

3.2.1 CPIA index for Uganda

The Country Policy and Institutional Assessment (CPIA) is basically used by the IMF and WB as a measure of a country's economic, institutional and governance framework that was primarily developed to allocate IDA finances.[30] The CPIA is perceived to fully assess a given country's vulnerability to debt distress and classifying a country as per the debt and debt service benchmarks, by measurement of the net present value (NPV)-that is the discounted value of future debt repayment) through a consideration of its debt-to-exports ratio and its debt-to-GDP ratio and its debt service-to-exports ratio. A country is regarded as severely indebted if the present value of total debt service to gross national income (GNP) exceeds 80 percent or if the present value of total debt service to exports exceeds 220 percent. This would imply that a big chunk of a country's revenues earned from exports is actually lost to debt servicing than being ploughed into the more deserving programmes of the economy to generate investment and growth, for poverty reduction and debt sustainability.

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[24] MFPED,Budget Framework Paper 2007/08, April 2007

[25] MFPED, Poverty Eradication Action Plan, 2004/05-2007/08, 2004, p xvi

[26] IMF, Second Review under Policy Support Instrument & Request for Modification of Assessment Criteria, November, 2007

[27] IMF, Article IV Consultation, 4th
Review under the Poverty Reduction & Growth Facility (PRGF), Jan, 2005, p. 4

[28] US$ 1.5 billion at the FY 2006/07 averaged Uganda Shilling / US$ exchange rate of 1,644

[29] MFPED, Debt Strategy, December, 2007

[30] EURODAD, Still the Point: Unpacking the new World Bank/IMF debt sustainability framework, Position paper, September, 2005, p.5

Under the CPIA, Uganda was currently rated as a "strong performer" with a sustainability NPV threshold of external debt to exports ratio of 200 percent. This also implied that the country had strong policies that supported debt sustainability.

A respondent from Ministry of Finance (MFPED) while citing a government source observed that, for countries regarded as strong performers, the debt burden threshold of NPV of debt to GDP ratio should be 50 percent, NPV of debt-to-exports ratio be 200 percent and the NPV of debt to revenue ratio be 300 percent. The debt service to exports ratio should also be 25 percent and debt service to revenue ratio be 35 percent.

With this in view, Uganda was implementing an updated 2007 Debt Strategy, to ensure that the NPV of total resulting debt stock to exports remained at 150 percent over the medium and long terms.[31] While this may be the case, macroeconomic shocks were likely to degenerate Uganda's NPV of debt-to-exports ratio. Arising out of the Kenyan political crisis, the fuel prices skyrocketed since January 2008, a factor that constrained trade transactions and escalated the prices of consumer goods and services as well as transportation. The crisis had also had a negative effect on investment and production capacity (since of the export commodities depended on imported raw materials) and the overall exports for Uganda.

So, beyond the highly rated policy and institutional leverage, Uganda remained susceptible to macro shocks at the exogenous and endogenous levels, with a possible adverse effect on debt sustainability. For this case it has been agued that, in a situation where exports were to grow less by one standard deviation during the 2007-2009 period, Uganda's NPV of debt-to-exports ratio would increase to 147 percent in 2011/12. Thus, an export shock and low growth performance would have a significant impact on debt sustainability.[32]

3.2.2 Baseline Scenario for Uganda

Table 3.1 highlights the scenarios, within the ream for debt sustainability.

Table 3.1 Uganda: DSA Baseline Scenarios

	FY 2007/08	FY 2010/11	FY 2014/15	FY 2017/18	FY 2027/28
a) NPV of debt-to-GDP ratio					
Baseline scenario	5	12	13	13	
High investment scenario	5	13	16	17	14
b) NPV of debt-to-exports ratio					
Baseline scenario	31	83	88	87	68
High investment scenario	31	89	112	118	96
c) Debt service ratio					
Baseline scenario	4	6	6	5	5
High investment scenario	4	6	11	10	7

Source: IMF, Uganda, Article IV consultations, Dec. 2006

As shown in the table above, the scenario for Uganda indicated that the debt burden indicators were below the thresholds over the period of projection. In this case, the NPV of debt-to-GDP ratio was projected to increase to 13 percent in FY 2016/17, impressively below the policy-dependent threshold of 50 percent. Similarly, the country's NPV of debt-to-exports ratio in FY 2016/17 was anticipated to be at 87 percent[33]; which was still well below the debt burden threshold of 200 percent.

[31] MFPED, Debt Strategy, December 2007, p. 45
[32] IMF, Uganda, Article IV consultations, December, 2006
[33] IMF, Uganda, Article IV consultations, December, 2006, p. 73

3.2.3 HIPC Forecast

It was clear that Uganda debt relief under the HIPC Initiative in the 1990s and 2000s, coupled with the 2005 MDRI, played a key role in causing substantial debt reduction and sustainability for Uganda. This was further reinforced by the implementation of sound/ robust macroeconomic policies. Accordingly, one government respondent shared that all the debt related indicators for Uganda were below their thresholds and expected to decline as follows:

- NPV of debt-to-exports ratio had declined from 179 percent in FY 2004/05 to 31 percent in FY 2006/07
- Debt service-to-export ratio had declined from 16 percent in 2004/05 to 4 percent in the financial year 2006/07
- NPV debt-to-GDP ratio had declined from 24 percent in FY 2004/05 to 5 percent in FY 2006/07.

3.2.4 Risk Assessment

Uganda's current risk of debt distress was rated as low and was mainly attributed to infrastructural inadequacies. These consisted of electricity supply shortages and the roads and railway networks that had a negative bearing on the production capacity and growth of the private sector. One of the debt sustainability strategies over the medium-term and long-term (but also informed by the Article IV consultations), included borrowing for the sectors that government perceived as of priority in the enhancement of asset formation, productivity, competitiveness and economic growth. Such sectors were regarded as critical to building capacity for generating resources and export earnings that were significant in debt servicing and offsetting the effect of the country's debt.

Still, over the five years, commencing with FY 2008/09, external borrowing was to be restricted to the so-called priorities such as Agriculture, Works and Transport, Water and Energy sectors. In this regard, construction of two hydro power stations at Bujagali and Karuma sites in Uganda were in the offering, as part of dealing with the risk to debt sustainability. While this was impressive, it was urgent for Uganda to scale up funding to infrastructural development to continue on the path of supporting economic growth and development. This inherently also called for reversing the country's poor culture of infrastructure maintenance.

It was from the above consideration, perhaps, that the IMF's assessment of debt sustainability for Uganda, under Article consultations, was anchored on specific measurements that included[34] quantitative performance criteria, structural assessment criteria, and structural benchmarks. Under the quantitative performance criteria for Uganda, an annual borrowing ceiling/ cap was in place to ensure that new external borrowing was consistent with Uganda's fiscal consolidation and liquidity management (achieving the money supply target) over the medium term. It was argued that, for debt sustainability to stay on course, a small fiscal deficit was required for Uganda.

Under the Structural Assessment Criteria, there was a strong element of offsetting domestic arrears, with Ushs 280 billion in FY 2007/08 and Ushs 300 billion in FY 2008/09 committed by government in the respective budgets. Domestic arrears were the focus but priority going to the verified pensions. Another criterion was on finalizing and publishing Uganda's Debt Strategy by end of December 2007. This had been finalized by the time of this study and awaited publication and formal launching. Further, there was a criterion for submitting to cabinet a policy paper outlining the establishment of a new regulatory framework for financial institutions[35] not under the statutory supervision of the Bank of Uganda. This was to be implemented by end of January 2008, but was rescheduled to end in June 2008, to allow Uganda to receive technical assistance through Bank of Uganda. The final criterion under structural assessment was for Uganda to issue a tender to select a provider for the national identity card system by end of June 2008.

[34] Data obtained from the IMF Country office

[35] They included private and public pension funds, insurance companies and Uganda Development Bank.

The Structural Benchmarks included rolling out the Integrated Personnel and Payroll System pilot[36] in three Commissions and two Local Governments by end of May 2008. It also covered Bank of Uganda and other members of the Monetary Affairs Committee of the East African Community to finalize a comprehensive draft financial market development strategy by end of May 2008. The final structural benchmark was for an update of a national energy (Oil) policy to include macroeconomic policy options during 2008.

So, from the IMF assessment above, it should be noted that the pre-HIPC (FY 1996/97) nominal value for Uganda's external debt stock stood at US$ 3.7bn, while the NPV of debt to exports ratio was 243 percent[37]. Under HIPC, Uganda received debt relief amounting to US$347m in NPV terms, of which 79 percent was due from multilateral creditors. Following the sharp post-HIPC fall in the NPV debt to exports ratio, mainly arising out of a deterioration of the country's terms of trade, Uganda qualified and received yet another debt relief under the Enhanced HIPC in 2000.

As a result of the change of the IDA Poverty Reduction Support Credit (PRSC) from loan to grant in 2003/04 and 2004/05, financing of the fiscal deficit through external loans was significantly lower than programmed. So, new external loans reduced from 4.9% of GDP in 2002/03 FY to 1.9% in 2004/05 FY. The biggest contribution to our debt was through the HIPC initiative. These amounts, which would otherwise have been spent on servicing debts, have been utilized on poverty reduction interventions by Government. The above relief led to a decline in the debt stock-to-GDP ratio from 67.0% in 2002/03 FY to 51.4% in 2004/05 FY. Combined with a rising level of export revenues, the relief also led to a decline in the Net Present Value (NPV) of debt stock-to-exports ratio, an important measure of debt sustainability, from 302.0% in 2002/03 FY to 285.0% in 2003/04 FY, and 266.0% in 2004/05 FY. [38]

The calculation of the trend for debt sustainability above was based on HIPC methodology that considers a three-year average of exports. It was clear that the country's debt sustainability around the FY 2004/05 remained way above the globally accepted upon threshold of 200 percent[39], hence unsustainable. The full implementation of MDRI, nonetheless, helped to deliver faster and deeper relief for Uganda and to achieve debt sustainability, after reducing the NPV of external debt to exports ratio to about 50 percent in FY 2006/07. This again was obviously well below the threshold of 200 percent. Table 3 indicates Uganda's Debt Stock between Fiscal Years 1997/98 and 2006/07.

Whether Uganda is able to have a sustainable debt or not will largely be determined by the existing debt overhang and the prospective path of its fiscal deficits together with the evolution of its repayment capacity. It is therefore important to take a closer look at the country's debt servicing abilities over a period of time, as highlighted in the table in Annex 1.

3.3 Is Uganda's Debt Sustainable?

To determine whether Uganda's current level and rate of indebtedness is sustainable or not, requires one (within the country's macro economic framework) to note that debt sustainability is a function of cost of borrowing and performance of the economy, in particular exports. It would also be taken on from the perspective of the country's ability to continuously meet repayment obligations without compromising budget expenditure priorities. Beyond the budget, the availability of foreign exchange is also crucial, particularly for external debt. Meanwhile, domestic debt is constrained by demands on the domestic financial sector, including availability of credit to the private sector. The indicators for debt sustainability have to include, inter alia the debt stock in relation to GDP or domestic revenue, Net Present Value (NPV) of debt in relation to GDP, foreign exchange reserves or exports, and debt stock in relation to private sector credit. Table 3.2 below, therefore, highlights some of the measurements for Uganda's debt sustainability.

3.3.1 Domestic debt stock / GDP

Uganda's current domestic debt stock was 10 percent of GDP. This was a low percentage by international standards, hence making the country's debt appear sustainable at face value. Uganda's total current debt stock, however, was approximately 28 percent of GDP.

[36] The Commissions were for Public Service, Health and Education, while the Local Governments were Lira and Jinja Districts

[37] MFPED, Poverty Eradication Action Plan, 2000-2003, 2001

[38] MFPED, Uganda Poverty Status Report, 2005, p. 19

[39] The IMF & WB use the Low Income Countries (LIC) DSA methodology based on the 3-year volume of exports for a given country and where the debt sustainability threshold is estimated at 200 percent

Worse still, the country has had a history of rapid growth of debt stock as noted earlier, where, for example, in 1999 the domestic debt stock to GDP stood at 2 percent but had increased five-fold over the last seven years to about 40 percent. The projected benchmark of 15 percent, therefore, called for more vigorous efforts for Uganda in the management of debt portfolio.

Table 3.2 Macro-level Sustainability and Cost Minimization Benchmarks for Uganda

	Suggested Benchmark	Current (FY 2006/07)
Domestic debt stock / GDP	<15%	10%
Domestic interest cost / Domestic revenue (excluding grants)	<15%	10%
Domestic debt stock / Private Sector Credit	<100%	130%
Percent maturing in 1 year	< 50%	80%
Percent maturing in any year after year 1	*< 20%*	?
Ratio of bonds/bills	60/40	43/57
Source: MFPED, Debt Strategy, December, 2007		

3.3.2 Domestic tax revenue to GDP

As seen from the table above, Uganda's domestic tax revenue to GDP remained generally low and actually lowest in the Sub Saharan Africa. While the share of revenue to GDP in FY 2005/06 was 13.7 percent of GDP, the share of total Government expenditure to GDP was 22 percent.[40] There was, therefore, a lot of effort to be undertaken in plugging issues around tax avoidance, equitable and efficient tax collections. Still, the weak financial sector in Uganda means that the ratio of private sector credit (PSC) to GDP remains very low and cannot widely and rapidly function as a big domestic revenue base. So, even a relatively low level of domestic debt to GDP causes a crowding out (credit squeeze) effect to the private sector and a room for lack of debt sustainability.

3.3.3 Domestic Interest Cost / Domestic Revenue

This benchmark captures the budget sustainability of the debt burden. Given that extension of donor grants is neither obvious/automatic nor necessarily consistent, this aspect looks at domestic debt against the budget. Here the accumulation and stock of domestic debt to GDP in Uganda are critical.

For instance, during the FY 2006/07, DFID through the Poverty Reduction Budget Support only released to Uganda £35 million instead of £70 million promised, a sum less by £55 million previously planned for use by the Government. Similarly, during the FY 2005/06, the following bilateral donors suddenly reduced their funding to Uganda's national budget a) Norway - US $4 m b) Sweden -US $8m. While the current level of the Domestic interest cost to Domestic revenue benchmark at about 10 percent and projected to 15 percent capping, the measure fell short of accounting for the extent of external debt interest cost to the economy and future possibility of a fluctuating interest rates environment. Thus, showing traces for lack of Uganda's debt sustainability.

3.3.4 Domestic Debt Stock / Private Sector Credit

Looking at Uganda's financial sector, the ratio of domestic debt stock to private sector credit had increased from approximately 50 percent six years ago to the current 130 percent. The current ratio of 130 percent also implied that the banking system loaned more money to Government than to private sector. Given that Government debt/ securities were apparently being issued purely to 'mop up' excess money supply in the economy, Uganda was seriously overlooking another opportunity of issuance to finance and stimulate economic development. Indeed, the limited supply of credit to the private sector has been identified as a significant constraint on economic growth in Uganda, yet Government could easily play a financing role.

40 MFPED, Background to the Budget, FY 2006/07, June 2006

Clearly, therefore, sharp and rapid increase in Government debt stock was susceptible to crowding out the private sector, driving up interest rates, thus jeopardizing the country's economic growth, development and poverty reduction strategies and eventual failure in debt sustainability.

In addition, the current level of domestic debt stock to Private Sector Credit standing at 130 percent certainly exceeded the proposed benchmark of 100 percent. While this was a good move in terms of, for example, regulating additions on the debt stock and reducing donor dependency, it was mainly dependant on the overall financial deepening in Uganda for private sector growth. So, Uganda could only achieve such an ambitious benchmark of 100 percent, at least in the medium-term; thus, putting debt sustainability at a precarious position.

3.3.5 Cost Minimization And Risk Management

Uganda's debt stock, contracted for monetary management purposes, continued to grow annually, due to the persistent fiscal deficit. So, also annually, the proportion of the existing debt stock matures through issuance of government securities. This was also being affected such exogenous factors such as political turmoil in Kenya during December 2007 and early 2008. The interplay of such factors implied that interest rate could easily become volatile and this was quite difficult to accurately predictable, has associated cost and consequence for debt sustainability for Uganda.

3.3.6 Ratio of Bonds to Bills

It has been noted that was not possible for Uganda to reduce the annual refunding volume to a level of less than 50 percent when the Treasury Bills comprised close to 60 percent of the country's total domestic debt stock. As seen from the table above, the benchmark 60/40 Bonds/Bills mix required a modest and viable increase in the size of monthly bond auctioning by Government, through Bank of Uganda. Even then, the respondents shared such a benchmark was likely to be realized earliest between one to two years. To the extent that this could be achieved, there was a possibility for contributing to Uganda's debt sustainability.

In a nutshell, there were possibilities that Uganda's debt was sustainable. The country was to, over the forthcoming five fiscal years, commit itself and project to maintaining an average debt/ export ratio at less than 150 percent and, at the same time trim, to borrow through capping and reduction of domestic debt, as earlier discussed under the 2007 debt strategy. Looking at the benchmarks discussed above, nonetheless, the degree of risk (thus falling short of debt sustainability) in meeting the intended achievements, seems to be apparently high.

3.4 Domestic (Public) debt and Debt Sustainability

The domestic debt for Uganda in this study considered was domestic borrowing (government securities and arrears) and government guarantees (since they constitute contingent liabilities on the part of the Government). In Uganda, domestic debt was being issued for monetary policy purposes, so as to manage inflationary pressures. Growth rates of Uganda's domestic debt stock, particularly in the 1990s, were unsustainably high, resulting in both increasing average cost of debt and excessive interest rate volatility. Still, the country's domestic debt stock had grown rapidly in the last six years, outpacing growth in both GDP and total domestic credit, from an estimated UShs300 billion in June 2000 to about UShs1.7 trillion in FY 2006/07.[41]

3.4.1 Domestic Arrears

These are basically the outstanding bills beyond a given Fiscal Year in which they were incurred. These may include utility bills and unpaid certificates after project completion. In Uganda, the arrears formed a key component of domestic public debt. This was due to the 1995 constitution provision in Article 159 (7) that considered a loan as any form of borrowing in respect to which money from the national consolidated fund or any other fund may used for payment or re-payment.

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[41] MFPED, Debt Strategy, December 2007, p. 29

Concerning efficiency, effectiveness, planning, budgeting, harmonized and accurate financial and statutory reporting, transparency and accountability (especially under procurement) in public finance management, Uganda had in the past instituted financial management reforms and processes. Such reforms were ideally equally beneficial to the management of domestic debt and debt sustainability. The reforms included a) Commitment Control System (CCS) and b) Integrated Financial Management System (IFMS). The CCS is ideally the adoption of a prepayment system for utilities. IFMS is a fiscal and financial management information system for Government that bundles all financial management functions into one suite of applications; as an Information Technology-based budgeting and accounting system for Government needs in regard to budget spending, monitoring, processing of payments, general financial management and reporting.[42]

In spite of the reforms and processes, Uganda's stock of domestic arrears continued to grow, as highlighted in Annex 2, with challenges and wider implication on domestic (public) debt and debt sustainability for the country.

3.4.2 Government Securities

From the theoretical point of view, a high externally financed deficit resulted in an annual increase in the money supply above the level of demand from the economy. To avoid a potential macro-economic distortion effect, therefore, an increase in money supply ought to be 'sterilized', mainly through either sale of foreign exchange or domestic debt through issuance of government bills/ bonds; hence, the basis against issuance and size of the Government securities in Uganda.

In the wider spectrum of Uganda's relationship and being pastured by the Bretton Woods institutions (IMF and WB) and related agencies, Uganda's key macro-economic parameters followed the neo-liberal considerations such as a) deficit reduction (maintaining small deficits) b) inflation control (monetary policy that is fixated on low inflation targets at about 5 percent annually) and c) Exchange-rate policy that was committed to full flexibility. [43] Table 3.3 below indicates the level of Government securities, as part of stock of domestic debt.

Table 3.3 Government Securities Statistics

Period (by end of FY)	Stock of public Domestic Debt (in billion UG X)	Annual % change in Public Debt	Total Domestic Credit (in billion UG X)	Cost of Public Domestic Debt (in billion UG X)	GDP	Debt/ GDP	Debt / PSC	Fiscal deficit excluding grants
1999/ 2000	319		899	30	8,950	3.60%	55%	
200/2001	545	71%	1180	59	9,971	5.50%	86%	-10.20%
2001/2002	730	34%	1392	91	10,240	7.10%	110%	-12.30%
2002/2003	997	37%	1846	118	11,771	8.50%	117%	-10.40%
2003/2004	1,163	17%	2149	193	13,190	8.80%	118%	-10.00%
2004/2005	1,472	27%	2602	174	15,176	9.70%	130%	-9.00%
2005/ 2006	1,680	14%	2977	183	17,234	9.70%	130%	-7.20%

Source: MFPED

From the table above, Government securities had continued to grow from merely 320 billion Uganda shillings during FY 1999/2000 to a considerably higher level of about 1.68 trillion Uganda shillings by end of FY 2005/2006. This deepened the predicament of debt sustainability for Uganda. The causes to such a scenario are discussed later under the challenges to debt sustainability.

[42] http://www.finance.go.ug

[43] MFPED, Poverty Eradication Action Plan, 2004/05-2007/08, 2004, pps 34-42

In a nutshell, although domestic debt had represented a relatively small portion of Uganda's total debt portfolio in the past, the recent MDRI created a situation where both the external and domestic debt portfolios were somewhat closer in size than at any other time in Uganda's history with debt. This shift represented a marked change in the composition of the public debt for Uganda, in as far as debt sustainability was concerned.

3.4.3 Government Guaranteed Debt

The contingent liabilities usually arise from explicit and implicit guarantees, including legal entitlements, policy-led commit Government to particular levels of support as well as those that have not necessarily had a designated criterion to guide their disbursement. In the case of Uganda the guarantees constituted part of domestic debt.

For instance, Government had guaranteed loans as follows a) US$5.50 million to Phenix Logistics Limited (a private company in Uganda dealing in textiles for export to the American market under AGOA) b) US$5.2 million to the Islamic University in Uganda and c) bailing out of ailing business individuals, such as one Hassan Bassajjabalaba to the tune of UShs19.9 billion.[44]

In conclusion, by FY 2006/07 Uganda's domestic arrears stood at about UShs 540 billion and Government securities at about UShs 1,680 billion. The study was unsuccessful in ascertaining the volume of the Government guaranteed debt.

3.5 Challenges to Uganda's Domestic Debt Sustainability

Poor public expenditure management: In view of domestic debt and debt sustainability for Uganda, there was general consensus that amongst the respondents of the study that the growing situation of the domestic arrears was mainly attributed to Uganda's poor public expenditure management, coupled with lack of streamlined policies or even enforcement in instances where they existed.

Lack of a strategic framework for domestic debt management: This continues to pose challenges to Uganda's development and poverty reduction since the accumulation of domestic arrears complicated budget planning and execution. It was against this backdrop that arrears constituted off-budget expenditure and were susceptible to a higher risk of channelling resources outside non-priorities and overarching national development framework priority programmes, for example under PAF, as stipulated in the PEAP. A huge stock of domestic arrears further was likely to undermine Uganda's endeavour to align the structures of the national budget to such priorities over the medium and long term (MTEF and LTEF), respectively, causing additional dilemma for debt sustainability.

Lack of policies on Government guarantees: At the level of policies, guidelines and actions on tax incentives, waivers or guarantees, every financial year, Government announced figures of how much incentives and waivers were to be extended to firms in Uganda. At times Government further extended guarantees to individuals as well. The challenge for Uganda, nevertheless, was that there was no clear and adhered to criteria on who gets what, how much or a related Government action, according to some of the civil society respondents during the study.

Lack of effective monitoring of compliance: For instance, during CHOGM[45], hoteliers abused the tax exemption plan set-up to help them build or improve hotels in time for the Commonwealth Summit. Consequently, it was not clear whether UShs 18.9 billion in taxes that the MFPED paid on behalf of hoteliers covered only the very items spelled out in this particular policy. [46] Daily Monitor newspaper, Saturday, January 26, 2008, p.1

Clearly, therefore, poor or lack of polices and enforcement was contributing to Uganda's domestic debt and posing a challenge to the country's debt sustainability. Government failure to offset pension arrears: Furthermore, the continued failure of Government to offset pension arrears was one of the major impediments to poverty reduction in Uganda, through adversely affecting the living conditions of the beneficiaries (pensioners), constraining spending (poor purchasing parity) and investment opportunities of such retired government workers who at one time paid their due diligence to national service.

[44] UDN, CS Statement on Continued Misuse and Wastage of Public Resources, May 2005, p.3
[45] CHOGM was the Commonwealth Heads of Government Meeting that was hosted by Uganda during November 2007
[46] Daily Monitor newspaper, Saturday, January 26, 2008, p.1

The non-payment also indirectly affected the livelihood and capacity of their dependants; thus, limiting the production capacity of the economy at the micro and the aggregate/ macro levels for debt sustainability.

Undermining growth of private sector: Uganda embraced neo-liberal policies which emphasized the private sector as the driver of economic growth and development. The apparent trends and stock of the domestic debt rooted in poor government behaviour such as non-payment of bills and invoices, threatened the very survival of the private sector.

This was manifested through the liquidity and cash flow squeeze arising out of delayed payments, growth and capacity constraints over and above debt accumulation of individual private sector entities that transacted business with Government.

It was, therefore, no wonder that, in terms of the cost and volume of the private sector borrowing, the deficit had increased the sector's cost of borrowing, and that it peaked at 34 percent in 2001, which reduced the resources the commercial banks had available for private sector lending by FY 2004/05.[47] So, since Government borrowing was definitely high and on an upward trend, it was contributing to crowding out private sector borrowing in Uganda, making the condition of Uganda's domestic debt contributing to the country's debt unsustainable.

Other than financial squeeze, the private sector enterprises and individuals were being forced to impose a premium on their contracts with Government or charges. This was in order to mitigate the risks associated with delayed payments. While this sounded okay in itself, it inherently increased the cost of doing business with the private sector in Uganda. Yet the sector was perceived as the engine of growth that would greatly contribute to the national capacity for expansion of economic functions and opportunities for eventual debt sustainability.

[47] MFPED, Poverty Eradication Action Plan, 2004/05-2007/08, 2004, p. xvii

4.0 Uganda's Debt Management Framework

4.1 Alignment of Uganda's Debt Management Framework

There is a linkage among debt relief, development at the level of policy and institutions. The debt management framework for Uganda was aligned to her economic objectives, development aspirations and debt sustainability strategies and institutional strengthening.

The power of the Government to borrow was enshrined in Uganda's constitution, 1995; Public Finance and Accountability Act, 2003; The Budget Act, 2001 and; Bank of Uganda Statute, 1993 and the Treasury Bills Act, 1969. These laws, accordingly, gave several institutions of Government different mandates in the acquisition of debt, aimed at debt sustainability, poverty reduction, economic growth and development for Uganda. In the Constitution, for example, Articles 159 provided for the manner in which Government could borrow and guarantee loans; authorized Parliament to scrutinize the terms and conditions of loans, etc.

At the level of policy framework, there was the 1991 External Debt Strategy that was updated into the 1995 revised External Debt Strategy. A more comprehensive framework for strategy was also put in place in 2007. Such mechanisms were expected to improve debt management and sustainability for Uganda.

Institutionally, the 1995 Constitution of Uganda vested authority for public borrowing in the Minister responsible for Finance, but working closely with the Bank of Uganda. Other relevant legal, procedural and institutional arrangements were also instituted to ensure harmonized prudent utilization of public resources (including borrowed resources), loan contraction processes. This was also aimed at beefing up the debt management policy framework in Uganda.

Furthermore, the study ascertained that Uganda's development plans and projections such as the PEAP and the debt strategies were designed within the framework of outstanding debt repayment maturities, obligations and expected and disbursed funds-mainly grants. New borrowing and domestic revenue generation were also said to be in line with economic growth and development projections. Even receiving grants had a limit due to issues of absorption and macro-economic stability against the political pressures to spend.

Uganda had in place an updated and more comprehensive debt strategy referred as the 2007 Debt Strategy. It was expected to tackle inadequacies in the previous approaches to debt management and sustainability at the level of legal, institutional and policy framework. The capture of approaches for both the domestic and external debt was also critical in the 2007 strategy. In view of debt levels that so not jeopardize national development, the Strategy provided for capping (putting a ceiling) on new borrowing and limiting project borrowing to sectors perceived by Government as priorities in championing the commitments such as the PEAP, MDGs and a sustainable debt position.

The study noted that since 1991 when Uganda developed the first External Debt Strategy (EDS), even though the ground rules at the point of implementation were increasingly not fully adhered to. Due to indiscipline on the debt strategy, the country failed to achieve debt sustainability, relief mechanisms notwithstanding. The focus of the revised EDS of 1995 on pursuance of debt relief, borrowing on concessional terms and preference to use of grant financing for national development and debt sustainability was in line with Uganda's macroeconomic choices and institutional arrangements in place, though with limitations.

Through the study, it was clear that positive steps had also been taken in the alignment and harmonization of aid (grants and loans) delivery to Uganda's systems and development strategy. The improvement steps, for instance, had streamlined the number of Sector Working Groups over the medium term from 14 to 18. Such alignment was critical in the execution of debt sustainability strategy for Uganda, in avoiding duplication, wastage and plugging loopholes that had a bearing on the national debt.

4.2 Challenges to Debt Sustainability in Uganda

Corruption: The culture of impunity, misuse and wastage of public resources in Uganda seemed to have been deeply rooted amongst a number of officials that conduct public affairs. According to a country report by the APRM, Uganda was estimated to have been annually losing a whooping US $300 million (about UG X 510 billion) to corruption since 2005, through corruption and procurement malpractices, yet procurement accounted for about 70 percent of public expenditure in Uganda[48]. This was a big threat to Government's debt sustainability strategy, since the production capacity of the economy was being undermined and/ or its proceeds dubiously being eaten away mischievously.

Flouting and by-passing designated systems: Related to corruption above, Uganda was experiencing flouting of set procedures and by-passing of systems by the constituent administrators. There were catalogues of a wide range of unethical practices that went contrary to the set laws, rules and regulations and. This resulted into shoddy and dubious transactions that compromised accountability precepts, with an eventual bearing on debt sustainability for Uganda. This was largely out of accounting officers by-passing the IFMS system, absence of adequate control procedures and poor coordination among the implementing departments in MFPED; the incidence of diversion was highest amongst the IFMS sites[49]. The following illustration indicated that the question for Uganda's prudent public finance management, as a critical factor in debt sustainability was experiencing a big challenge.

> ***A Mafia-like syndicate of civil servants, especially those who deal with payments, has been stealing public money in an elaborate scam that could cost taxpayers billions of shillings. The fraudsters have been tampering with the new payment system called the Integrated Financial Management System (IFMS) to pay out huge sums of money to fictitious suppliers. The IFMS records all government financial transactions and is managed at the Treasury in Ministry of Finance.***[50]

Clearly, therefore, Uganda was at cross-roads since the very institutions instrumental to accountability, coordination, debt processes and debt sustainability strategies were at the helm of defrauding the very systems they were custodians of. Measures were being proposed to curb errant actions and behaviour, but their success and expected impact remained to be seen.

Cases of poor verification: Through the study, it was established that Uganda still experiences instances of poor verification, a key element in dealing with debt framework and debt sustainability. For instance, ineffective implementation of the arrears strategy was due to diversion of budgeted arrears resources towards meeting current bills or settlement of both unverified and ineligible arrears. Also, "Military pensions are not fully verified, while only fifteen local governments have had some of their pension arrears verified".[51]

Inadequate budgeting and poor predictability: Beyond the violations by accounting officers and administrators, the Government still experienced limited coverage of the updated mechanisms for efficiency, effectiveness and thus sustainable debt management. This was compounded by the unpredictability of budgetary provision for emergencies (such as the floods in Eastern and North of Uganda during the second half of 2007), volume of increasing court awards and other contingencies such as the Kenyan political crisis that contributed to Uganda's monthly revenue decline[52]. The rapid creation of semi-autonomous, administrative units in Uganda was posing a big dilemma in this regard. Instances of inadequate budgeting, too, remained as inevitable outlays in pensions, utilities and rent. Others included subscriptions to international organizations and fixed cost contractual obligations under the country's development budget. Such pressures were likely to entice the Government into new borrowing, with a net effect on the country's debt sustainability. Likewise, the expected impact of the proposed interventions in these areas remains to be seen.

Limited institutional absorptive capacities: Uganda has registered instances where taxpayers were losing billions money through forfeiture of funds on expired loans that had to be paid back together with interest.

[48] MILTON OLUPOT, The New Vision, 22 January, 2008, p. 1
[49] MFPED, Debt Strategy, December, 2008, p. 10
[50] CHRIS OBORE, Sunday Monitor, 17 February, 2008, p. 1
[51] MFPED, Debt Strategy, December, 2008, p. 44
[52] a)Red Pepper in article, Reasons why Government Wants Shs 200 bn additional budget, 25th February, 2008, p.18 and b) Interviews with some officials from Government

The 2007 debt strategy had hinted on addressing capacity gaps through provision of procurement plans and implementation approaches prior to acquisition of such loans. It was, however, definite that Uganda was shouldering big debt challenges in the context of best practices, transparency, accountability and prudent use of public resources, operational management framework as well as the implementation of debt strategies, fiscal and monetary policies. In some cases, the forfeited funds were far in excess of 50 percent of the contracted loans.

> ***This happens when the period during which the loans are supposed to be utilized expires before they are used and they have to be paid back with interest. This is one of the revelations contained in the Report of the Auditor General to Parliament for the 2004 - 2005 financial year. According to the report, between 31 December 2004 and 31 December 2005, 24 loan accounts were partially drawn. As a result, the equivalent of Ushs 177,803,918,754/-, which is 28 per cent of the total account of Ushs 629,679,445,910/- was forfeited[53].***

Failure of Parliament to duly exercise its oversight role: The broad debt sustainability challenge for Uganda seemed to be out of the fact that the Legal, Policy and Institutional framework for debt procurement, management and repayment procedures bestowed a lot of authority to the MFPED/ Minister for Finance. For instance, the reality that, "In some cases, loan agreements have been signed with creditors before Parliamentary Approval…to coincide with the timing Boards of Development Finance Institutions that approve the loans"[54] indicated that some MFPED methods circumvented the Legal, Institutional and Policy processes in this respect. So, Parliaments oversight role was compromised, with a bearing on the perceived best practices, transparency and accountability, operational management framework, coordination, as well as the medium-term debt strategies and benchmarks for effective implementation and monitoring.

Contradictory Planning and Spending frameworks: The PEAP was Uganda's overarching policy framework that ideally was guiding budgetary allocations. Out of the multiparty political dispensation and related aspects, the Rural Development Strategy (RDS) and the political manifesto of the ruling NRM party with programmes such as Prosperity For All (PFA) had the potential to compromise the country's debt sustainability strategy and other legal, policy or institutional arrangements for debt management. For instance, a local tax revenue source for Local Governments was abolished by the NRM during the financial year 2006/07.

Potential for Debt Burden: Other than the above, the RDS had proposed to implement a US$ 42million subsidized credit to local savings and cooperative societies in Uganda, for poverty reduction endeavours. Under the IMF Policy Support Instrument to Uganda, this intervention particular had raised disagreements between the Government and donor community led by IMF. The donors' argument was that such a subsidy would create preferential interest rates to segments of borrowers and was a recipe for market and macro economic distortions[55]. While this may be debatable, it was clear that public spending pressures for Uganda remain high. Such tendencies if not properly and eventually harmonised with the wider policy regimes, were a potential source for poor debt sustainability for Uganda. Such scenarios indicated that external debt financing, in the short and medium term were most likely to continue as part of budget financing.

As long as domestic revenues fall significantly, the donor grants, as emphasized in the 2007 debt strategy, cannot entirely meet the shortfall and expenditure pressures. The undesirable debt burden will be shouldered by the Ugandan economy, with the consequent amortization and interest payments. Worse still, in spite of the benefits accrued from the various debt relief initiatives like the HIPC 1 in 1997, Enhanced HIPC in 2000, MDRI in 2005 and borrowing on highly concessional terms, Uganda continued to pay large sums of money as amortization of external debt to the tune of US $80 million annually. [56] Such is recipe for a new debt trap.

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[53] UDN, Policy Review Newsletter, October, 2006, Vol. 6 Issue 7, p. 1
[54] UDN, Policy Review Newsletter, March, 2008, Vol. 7 Issue 3, pp 1 & 7
[55] The East African, in an article, $42 m "Bonna' Credit Scheme for Rural-poor now draws IMF ire, 1-7 January, 2007
[56] MoFPED, Budget Framework Paper, FY 2007/08, April 2007

Huge cost for macroeconomic management: It should be noted furthermore that an increase in external borrowing would slap a huge cost for macroeconomic management, to Uganda. Certainly, a large deficit tends to appreciate the exchange rate, as more donor foreign exchange flows into the economy; and to raise interest rates, as the Bank of Uganda sells more Government securities to for inflation and liquidity management purposes. An appreciated exchange rate is damaging to export-led growth, as exporters receive fewer Shillings for each dollar they earn. High interest rates also are detrimental to private sector development, since they raise the cost of doing business and reduce access to credit[57].

Still, additional sales of Government securities increase the overall portfolio of the country's domestic debt. It also increases domestic interest payments plus the degree of vulnerability of the national budget. This is a recipe for domestic debt crisis with an adverse effect on the fiscal and monetary policies, medium-term debt management benchmarks and implementation of Uganda's debt sustainability strategies. A consistently increasing debt burden will inevitably reduce Government resources for financing the budget's poverty reduction and national development priorities.

Limited participation of key stakeholders such as Civil Society (CS): The Legal, Policy and Institutional framework for debt contraction, management, repayment and debt sustainability in Uganda did not provide a clear consideration on the level at which CS could give an input (say intellectual contribution). Yet, CS was perceived by Government officials as a critical stakeholder. According to CS respondents during the study, the debt processes were closed and in fact a domain of the government agencies. This was further confirmed by the policy and institutional set up as highlighted upon earlier. So, CS participation, in the wider spectrum of deepening country and citizens' ownership of national development programmes, transparency and accountability, and monitoring utilization of resources accruing out of loans, was not obvious but selectivity by seasonal invitation.

The media and other CSOs were believed to be one of the strong pillars of a society enjoying a democratic dispensation. In Uganda, conversely, both the print and electronic media rarely had coverage of loan contraction or debt management issues. Such documents with loan processes and debt were not readily accessible even though Uganda basted of enactment of The Access to Information Act, 2005. Thus curtailing Government the legal provisions, democratic expectations and accounting to its perceived key constituents who are the citizens.

The limitation for CS participation in debt related platforms was further a matter of weak and uncoordinated CS mechanisms and networking. Some respondents from CSOs acknowledged limited knowledge bases and capacities for CS engaging in the macro related areas such as debt stock, fiscal policies and loan processes.

[57] MFPED, Debt Strategy, December, 2007, p. 15

5.0 Conclusions and Recommendations

The chapter presents the key recommendations on debt sustainability for Uganda, within the context of debt relief initiatives and debt sustainability analysis. In a nutshell, it was noted that Uganda's debt situation was sustainable. However this sustainability is presented with challenges, that, if not addressed, risk taking the country back to its pre-HIPC Initiative and MDRI.

5.1 General Recommendations

- In order for Uganda to realize its 2007 Debt Strategy objectives in the areas grant financing as the preferred mode of aid, borrowing for priority sectors in the economy, dealing with Government guarantees, fixing an annual borrowing cap and assessing the cost and risks associated with external debt, the legal, institutional and policy framework need to be strengthened through amendments. This will help in plugging any loopholes thereof and facilitate effective implementation and monitoring of the said strategy.
- To tap into the advantages for general budget support that is inclined to grants (which is Uganda preferred aid financing modality), as well as build on the various debt relief initiatives it has benefited from, Government should discourage project financing , for it tended to come with conditionality, with implications on the debt sustainability strategy and development aspirations. This would further save Uganda the costs incurred through amortization and debt servicing.
- Enforcing adherence to the existing laws, regulations and procedures on the loan contraction, management, reporting and payback will contribute to the furtherance of debt legitimacy coupled with promotion of transparency and accountability in the management of public affairs in Uganda.
- In dealing with domestic debt, Government should develop a comprehensive taxation policy to guide taxation and increase own domestic revenue. This could be through comprehensive reviews of tax policies and regimes, by focusing on adequate revenue, economic efficiency, provision for equity, simplicity and effective tax administration and losses through corruption (avoidance and diversion). The comprehensive reviews should with a view towards de-linking from the Bretton Woods institutions that seem to hold Uganda hostage. Uganda should look more to regional integration with the wider economies of scale and opportunities available, in dealing with the exogenous factors.

5.2 Specific Recommendations

5.2.1 External Debt

- Government must enforce (with punitive measures where need be) adherence to the exiting laws, regulations and procedures on prudent public finance management, governance as well as external debt regarding loan contraction, management, reporting and payback. The provisions of Budget Act, 2001, for a presentation before Parliament of a detailed annual assessment of each loan and grant must be enforced. This will minimize the cases of expiry loans whose cost is eventually shouldered by the citizens of Uganda.
- The current loophole in the laws which provide for Parliamentary approval to all external borrowing without stating the basis against which such approval may be given or denied should be reviewed and plugged. For Uganda, external borrowing has previously been a major source for unsustainable debt and a huge macroeconomic cost.
- It is critical to adhere to capping the annual fiscal deficit (annual borrowing) to regulate debt stock, as proposed in the 2007 Debt Strategy. The Government needs to amend the existing legislation to capture this aspiration or even compel the Minister for Finance to assign external debt limits.

- Government institutions should be supported by various stakeholders in addressing Uganda's failure to utilize debt resources (particularly loans) in a timely manner and adherence (rather than flouting) to the laws and regulations and procedures. This, for example, could curtail cases of Government signing loan agreements prior to scrutiny and/ or approval by Parliament, a factor that had contributed to unwarranted debt servicing and debt accumulation.
- All aid (loans and grants) in Uganda should be aligned to loan contraction processes in Uganda. Aid by-passing such processes results into aid under-reporting and other cases of off-budget and expiry of loans before they are utilised, to the detriment of the national development and poverty reduction strategies. Government should in this case have an aid delivery and utilization policy in place.
- Likewise, the respective Government projects that need funding through external borrowing ought to be well prepared and appraised prior to signing of the loan. This will contribute to the overall borrowing that is responsible, aligned to the country's medium and long-term external debt sustainability, consistent with macroeconomic aspirations, fiscal consolidation and reduced aid dependency. At the sectoral level, the capacity to develop well-planned and absorptive projects should be enhanced through Sector Wide Approaches, polices and activities that are aligned to the budget priorities over the MTEF, to minimize delays and confusion in disbursement of loans.
- Regular, open and sincere policy dialogue between Government and stakeholders such as civil society groups, academia and donor community on utilisation of MDRI resources, since unlike previous debt regimes (say those under HIPC Initiative) that were earmarked to PAF, MDRI resources are not targeted to specific priority areas in the economy. This could provide a chance for agreeing on sectors or projects perceived by stakeholders as priorities as well as developing joint monitoring indicators, to ease future assessment.

5.2.2 Domestic Arrears

- Uganda already has in place relatively sufficient legal, policy and institutional framework within which to offset domestic arrears. The 2007 Debt Strategy on domestic arrears, therefore, should be adhered to, in dealing with the accumulation of domestic arrears.
- Government should clear the entire existing stock of verified domestic arrears as a matter of extreme urgency. They are hurting the private sector, pensioners together with their dependants and curtailing the production (consumption and investment) capacity of the economy.
- Roll out the CCS and IFMS to cover the entire Central and Local Governments' institutions, in facilitating accurate, timely transactions and reporting procedures.
- The provisions in the Constitution of Uganda of 1995, PFAA of 2003, PPDA 2003 and Budget Act, 2001 coupled with their corresponding procedures and regulations be enforced as sanctions on errant Accounting Officers who violate/ by-pass public expenditure management initiatives such as the CCS and IFMS.

5.2.3 Government Guarantees

- Develop a policy on Government guarantees to the private sector and individuals, to avoid selective guarantees that may be skewed towards favouritism, in the framework of prudent utilization of public resources and upholding equitable sharing of the national resources.

5.2.4 Government Securities

- Over recent years, Uganda's improved macro economic management had, for example, led to reduced levels of volatility interest rates and the level of interest cost to the economy. The fiscal and monetary policies, however, should be extended beyond mere management of liquidity to financing for economic development as well.

Additionally, Uganda needs to build institutional capacity for spending and making fiscal policy more expansionary and focused on financing wide-ranging public investment.

- The monetary policy should also accommodate fiscal expansion instead of restricting it through the targeting of unreasonably low inflation rates and correspondingly high rates of interest. This should be studied further in terms of how it could contribute to overall economic expansion and capacity to support debt sustainability for Uganda.

Annex 1

Debt Service, including Debt Relief (in US $ m)

Creditor Category	1996/7	1997/8	1998/9	1999/0	2000/1	2001/2	2002/3	2003/4	2004/5	2005/6	2006/7
TOTAL MULTILATERAL	107.1	111.2	110.9	98.2	114	109.9	120.6	139.1	161.7	158	
TOTAL NON-PARIS CLUB	22.25	26.32	29.64	13.86	12.16	3.53	5.37	4.88	5.45	32.25	
TOTAL PARIS CLUB	12.38	10.92	18.08	15.57	18.14	14.87	14.8	17.77	19.32	26.28	
TOTAL OTHER CREDITORS	14.16	6.24	5.11	5.8	1.77	5.3	5.16	6	6.29	5.29	-
GRAND TOTAL	155.9	154.6	163.7	133.4	146.1	133.6	145.9	167.8	192.7	221.8	-

Source: MFPED

Annex 2

Uganda Government Domestic Arrears Position Between 1997/98 & 2006/07

Fiscal Year	Court	Pensions (est.)	Gratuity	Salary (est.)	UEB	NWSC	UTL	Rent	Int	Other	Dev't	Total
	Awards								Org			
Pre-1997/98		57.00	0.00	0.00	0.00	0.00	0.00	0.50	9.90	0.30	0.00	67.60
1998/99	1.00	-	0.00	0.00	0.00	0.00	0.00	4.10	9.30	1.70	0.10	16.10
1999/00	1.80	9.40	0.00	0.00	0.00	0.00	0.00	2.00	0.40	8.90	2.30	24.80
2000/01	1.00	120.50	0.10	0.00	0.00	0.10	0.10	0.50	1.70	3.70	0.10	127.80
2001/02	2.30	-	7.70	0.00	0.10	-	0.00	1.30	-	3.90	-	15.20
2002/03	2.00	-	1.00	0.00	0.50	-	0.00	0.10	0.50	1.00	0.00	5.20
2003/04	0.60	12.50	0.00	0.00	0.10	0.00	1.30	0.20	4.70	4.80	0.10	24.30
2004/05	40.10	38.90	3.90	0.00	1.70	0.30	0.80	2.20	14.20	17.80	23.40	143.40
2005/06	15.30	38.30	2.30	4.00	5.40	0.60	0.50	4.40	13.60	30.20	3.10	117.70
2006/07 (est)	0.00	38.30	0.00	0.00	0.00	0.30	0.00	0.00	0.90	41.80	0.10	81.40
Total	64.20	314.90	15.10	4.00	7.80	1.30	2.60	15.20	55.20	114.10	29.30	623.70

Source: MFPED

Annex 3 List of Respondents

Government

Mr. Deogratius Kamweya, Economist, Aid Liaison Office, MoFPED

Mr. Denis Barigye, Senior Accountant, Office of the Accountant General, MoFPED

Mr. Tisasirana Longino, Commissioner Policy and Macro-economics, MoFPED

Mr. Mugambe, Commissioner Budget, MoFPED

Mr Muwanga Moses, Coordinator, Financial Management and Accountability Programme, MoFPED

CSOs

Julius Mukunda, Director Gender Budgeting, Forum for Women in Democracy

Ms Sarah Nakibuuka, Communications Officer, Private Sector Foundation Uganda

Ben Twinomujuni, Policy and Advocacy, African Women's Economic Empowerment Network

Ms Pauline Apolot, Programme Officer, Uganda Debt Network

Daniel Lukwago, Senior Policy Officer, Uganda Debt Network

Ms Sophie Kyagulanyi, Programme Manager, Action Aid International in Uganda

Other Agencies

Mr Jude Lugya, Sub Editor, Daily Monitor

Parliament

Samuel Wanyaka, Director, Parliamentary Budget Office

Hon. Nandala Mafabi, Chairperson, National Economy

Hon. William Oketcho, Chairperson, Budget Committee

Hon. Geofrey Ekanya, Chairperson, Local Governments Public Accounts Committee

Executive Director, East African Sub-regional Support Initiative-EASSSI

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