The PRGF and Fiscal Space in Uganda

A Research Commissioned by AFRODAD

African Forum and Network on Debt and Development

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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.

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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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African Forum and Network on Debt and Development
31 Atkinson Drive, Hillside,
PO Box CY1517, Causeway, Harare, Zimbabwe
Telephone 263 4 778531, 778536 Telefax 263 4 747878
E-Mail afrodad@afrodad.co.zw
Website: www.afrodad.org

Preface

The impact of fiscal space on growth and achievement of the internationally agreed development goals has featured prominently on the research agenda of government development agencies, international financial institutions, and civil society organizations. The Poverty Reduction Growth Facility (PRGF) has remained topical in the discussions around the quest by countries in the South to regain control of their own fiscal space from the International financial institutions. The controversy over IMF polices especially the PRGF boils down to a difference of opinion over how and when governments should be allowed to invest in both infrastructure and basic services. The IFIs, CSOs and the UN Development Programme (UNDP) have contrasting views on how to increase fiscal space, that is, on how to enable governments to spend and invest more. In their definition of fiscal space, the UNDP stresses the quality of public expenditure since productive expenditures will foster growth and human development, a larger 'budget pie', and more fiscal space in the long-term. On the other hand, Scholars, policy-makers and activists have focused on how to mobilize resources, or create the 'space' in national budgets, to invest in achieving the internationally agreed development goals, including the MDGs.

In efforts to recover from economic crises, most countries in sub-Saharan Africa began implementing IMF- and World Bank-led structural adjustment programmes during the 1980s. Those programmes promoted policies to expand the role of the market and reduce that of the state in economic affairs. They curtailed public spending for education and health care, privatized state-owned enterprises and liberalized trade. African governments had to cede control over their economic decision-making in order to qualify for World Bank and IMF loans. The PRGF and the succeeding Policy Support Instrument (PSI, introduced in 2005) have been nothing less than a continuation of such policies but under the guise of a new framework. The policies contained in both PRGF and PSI remains consistent with the standard IMF austerity programmes that have proved deeply controversial over the last 25 years. The only difference is that the IMF through such instruments is seeking to polish up its appalling image of being a tough lender and disciplinarian in Sub-Saharan Africa. This study constitutes one of the several PRGF researches that AFRODAD commissioned as part of its contribution to the civic call for the IMF to free policy space and enable African governments to pursue economic resuscitation of their battered economies after many years of the ill-conceived structural adjustment programs.

This study discusses the PRGF and the question of fiscal space as perceived by the citizens who are affected by IMF policy instruments. Conditions are one of the most controversial aspects of IMF and World Bank lending. Critics often claim that the institutions do not pay adequate attention to how the conditions affect people's lives or the contradictory ways in which multiple conditions interact with each other. Many governments also say that the conditions prevent them from making decisions which should rightly be made by elected leaders and that they also fail to address the basic problems that hinder economic development. The study concludes by giving recommendations to both the Fund and the government(s) on how to deal with the question of fiscal space.

Charles Mutasa
Executive Director
AFRODAD

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Abbreviations/Acronyms

AFRODAD	African Forum & Network on Debt & Development
BOU	Bank of Uganda
CCS	Commitment Control Systems
ESAF	Enhanced Structural Adjustment Facility
FY	Financial Year
GDP	Gross Domestic Product
IEO	Independent Evaluation Office
IMF	International Monetary Fund
MDRI	Multilateral Debt Relief Initiative
MEFP	Memoranda of Economic and Financial Policies
MFIs	Micro Finance Institutions
MoFPED	Ministry of Finance Planning and Economic Development
MTEF	Medium Term Expenditure Framework
NAADS	National Agricultural Advisory Services
NSSF	National Social Security Fund
PAF	Poverty Action Fund
NRM	National Resistance Movement
PAYE	Pay As You Earn
PEAP	Poverty Eradication Action Fund
PRGF	Poverty Reduction and Growth Facility
PRSC	Poverty Reduction Support Credit
PRSP	Poverty Reduction Strategy Paper
PSI	Policy Support Instrument
HIPC	Highly Indebted Poor Countries
MDGs	Millennium Development Goals
SACCOs	Savings and Credit Cooperatives
SWAPs	Sector Wide Approach Programs
UDBL	Uganda Development Bank Limited
UPE	Universal Primary Education
URA	Uganda Revenue Authority

Executive Summary

During the last two decades, there have been four consecutive Fund-supported arrangements-Structural Adjustment Facility, Enhanced Structural Adjustment Facility (ESAF 1 and 11) and Poverty Reduction and Growth Facility (PRGF). The PRGF arrangement was first approved in September 2002 and run until January 2006. It was the first country to reach Completion Point in May 2000 under the Enhanced Highly Indebted Poor Countries (HIPC) Initiative.

After the final review of the country's economic performance under the PRGF arrangement that was conducted in January 2006, the Executive Board approved a three year 16-month Policy Support Instrument (PSI) for Uganda. The PSI is intended to further support the nation's economic reform efforts. Like under the PRGF, to monitor performance under the PSI, quantitative and structural assessment criteria and structural benchmarks have been set. These quantitative conditions and structural reforms impact on the fiscal space for Uganda. They define and restrict the Government's ability to borrow from the Central Bank and banking system, to take commercial loans as well as restrictions on certain forms of expenditure, such as public administration.

The PRGF and PSI programmes emphasize poverty reduction in the context of the Millennium Development Goals (MDGs) while seeking to revive economic growth and macroeconomic stability. The program also aims to loosen fiscal space to permit higher spending on human capital and infrastructure so as to enhance the efficiency of the private sector and reduce growing donor dependence. In this context, the research aims to make an assessment as to whether the fiscal space created by the PRGF/PSI has indeed improved and contributed to the country's development strategy.

The PRGF and Uganda's Development Programme

The Government indicates that PRGF (and later PSI) is embedded in the Poverty Eradication Action Plan (PEAP). Alignment between the PRGF and Uganda's Poverty Eradication Action Plan should not be that surprising because the Poverty Eradication Action Plan is Uganda's PRSP which is partly supported by the World Bank's PRSC, which in turn is closely linked to the PRGF. However, it is important to note that there are differences of opinion within government, with many technocrats within the Ministry of Finance and the Central Bank favouring the IMF line, more to do with expediency than conviction and some politicians preferring more interventionist approaches that are perceived to deliver poverty reduction (and election votes) faster.

In terms of achievements, the IMF considers Uganda to have reduced sharply macro-economic imbalances. Uganda was one of the first African countries to adopt a stabilization programme and it has been successful. As a result, it has had 20 years of uninterrupted economic growth. The challenge now is sustaining growth over the long term; raising growth rates to 8-9% per annum and making growth more poverty reducing. While Uganda has made considerable progress in addressing poverty, regional and gender inequality remain serious challenges. Greater fiscal space is needed to address the gaps.

The PRGF and Fiscal Space

Uganda, with the assistance of IMF and other development partners, has made a lot of progress in improving domestic revenue collection, mainly through improved tax administration where it has targeted improvements of 0.5% of GDP per year. As a result, the ratios of external assistance to domestic revenue has improved from 52% in 2003 to around 34% in 2007/08 and is projected to continue the downward trend, especially with oil revenues expected to start flowing in 2009. However, because government revenues are still less than what they might be (due to tax evasion and other inefficiencies) and because political expediency opposes tax and fee increases, and because public expenditures are still high, fiscal deficit could well grow if donors were to refuse to support government.

Fiscal space has been created by the HIPC and MDRI debt relief initiatives. The fiscal space created by HIPC debt relief was used to address poverty reducing areas of government spending. Consequently, Uganda's selected expenditure in priority areas as a percentage of the budget under the ring-fenced Poverty Action Fund (PAF) has been growing from 23% in 1998/09 when it was created to around 33% per year in 2005/06. The fiscal space created under MDRI is being applied to support commercial loan for infrastructure. (Bujagali Hydro Electric Power generation).

Another source of fiscal space is budgetary expenditure reallocation. Government's four main strategic budget priorities are Rural Development, Economic Infrastructure and Development, Human Development and Security, Justice and Governance". "In FY 2008/09 there will be an even split between allocations which are aimed at strengthening the growth of the private sector in rural areas and the economy more broadly, and those which are aimed at supporting the welfare of all Ugandans".

Under the PSI, the IMF influences the decisions on government spending through its support to government in determining the aggregate resource envelop, thereby influencing the fundamentals of the economy. Analyzing the two reports that have been issued since the introduction of the PSI, it is clear that the IMF influences much of the Government budget and MTEF.

Sector ministries prepare investment plans painstakingly working out the resources needed to realise the plan. But sector ceilings constrain the full implementation of the plans. Examples are in Education's Fast Tracking programme and additional health programmes to fight malaria and HIV/AIDS that could not be accepted on macroeconomic stability reasons. This dilemma boils down to the 'logic of need' versus the 'logic of the available', leaving no room for a sector to dream.

Yes, under HIPC and MDRI, debt relief initiatives, fiscal space has expanded but the IMF policies and conditions continue to constrain Government in its utilization. If there is going to be a boost in economic growth and human development, fiscal space needs to be understood more broadly to include extra-budgetary resources and governments given greater autonomy to determine its utilization. Having played by the rule book, Uganda demonstrates that IMF conditions are not underpinning national macro-economic framework in a manner that shapes public expenditure and fiscal space to boost government's capacity to fund programs necessary to aid economic growth and social transformation.

1.0 INTRODUCTION

1.1 Uganda and the IMF: A Brief Historical Account

Since assuming power in 1986, the current government has taken important measures towards economic recovery. Recognizing the need for increased external support, Uganda negotiated a policy framework paper with the IMF and the World Bank in 1987. It subsequently began implementing economic policies designed to restore price stability and sustained balance of payments; improve capacity utilisation; rehabilitate infrastructure; restore producer incentives through proper price policies; improve resource mobilisation and allocation in the public sector.

By the 1990s, these policies began to yield positive results. Inflation dropped from 240% in 1987 to less than 30% in 1990; some prices stabilized, production increased, and consumer goods were more readily available. The Uganda government also has worked with donors to reschedule or cancel debt. It was the first country to reach Completion Point in May 2000 under the Enhanced HIPC Initiative.

After this period of recovery, the government has made significant strides in liberalization of markets and releasing government influence although some administrative controls remain. Monopolies were abolished in coffee, cotton, power generation and telecommunications sectors and restrictions on foreign exchange removed. These reforms are considered to have been the triggered for high GDP growth, improving the economy and boosting international donor and investor confidence.

The annual growth rate between 1990 and 2006 was 6.3%, higher than growth in the 1980s. Presently, Uganda is growing more slowly at 5.3% since 2006 as compared to 6.8% in 2002. On a capita basis, Uganda's average GDP in 2006 was US$314, up from US$222 in 2002. Inflation has moderated from 8% in 2005 to 6.6% in 2006. However, the economy has experienced a widening fiscal deficit estimated at 9.2% of GDP, if external assistance is not taken into account.

In terms of sectoral composition, the Uganda economy is still essentially agriculture based, with agriculture contributing about 33% of the GDP, employing over 80% of the population and generating 90% of the export earnings. The government has made effort to curtail poverty. In the 1990s and early 2000s, a coalition of interests among the presidency, technocrats, donors and civil society helped to create a strong demand for re-orientation of government policies towards poverty reduction. The 1997 Poverty Eradication Action Plan was the Uganda's first effort at a comprehensive strategy to reduce poverty. The subsequent two iterations of the Poverty Eradication Action Plan in 2000 and 2004 have also acted as the country's PRSPs. It is created within a consultative process and is performance oriented. Political ownership of the Poverty Eradication Action Plan was helped early by embodying key new political priorities such as Universal Primary Education and raising the profiles of other basic services such as health and water and sanitation.

In the last two decades, there have been four consecutive Fund-supported arrangements. The first was under the Structural Adjustment Facility, the next two under the Enhanced Structural Adjustment Facility (ESAF 1 and 11) and the fourth one under PRGF. The last three-year arrangement under the ESAF II was approved on November 10 1997 and was in December 1999 converted to a PRGF arrangement. The first full PRGF arrangement was approved in September 2002 and run until January 2006.

According to the IMF Resident Representative in Uganda, in addition to the programme mode, the IMF engages with Uganda at two other levels: Surveillance of economic policies and prospects of member countries, and technical assistance. For example in the recent past, IMF has provided technical advice to government of Uganda on non-tax revenues, and statistics. However, the reports from this technical support are mostly not published because they are deliberative rather than definitive and government is free to use them any way it likes.

Officially, the PRGF programme emphasizes poverty reduction in the context of the Millennium Development Goals (MDGs) while seeking to revive economic growth and macroeconomic stability. The program also aimed to loosen fiscal space to permit higher spending on human capital and infrastructure so as to enhance the efficiency of the private sector and reduce growing donor dependence. In addition the program placed emphasis on governance issues. Apparently the PRGF for Uganda aimed to increase real GDP growth to about 6.5 % a year on average, while holding annual inflation at about 3.5%. This baseline scenario was premised on a major investment being made in Bujagali Hydro-Electric Power project and a broad range of structural reforms to increase investor confidence and savings.

Key features of Uganda's PRGF included:

- Reducing poverty by maintaining strong economic growth and macroeconomic stability;
- Making progress toward fiscal and debt sustainability through a gradual fiscal consolidation, diversification of the export base, and enhancement of international competitiveness;
- Increasing government revenue, primarily through strengthened tax administration but also through tax policy measures, and by curbing public administration expenditures to ensure adequate financing of essential programmes to support economic growth and poverty reduction;
- Improving governance structures at all levels of government, and building an effective budget management and accounting system at the local level to ensure greater effectiveness of donor assistance;
- Deepening financial intermediation and building greater confidence in the banking system through development of long-term instruments and institutions for financial intermediation, passage and implementation of pertinent financial sector legislation, and strict enforcement of banking regulations; and
- Implementing structural measures aimed at enhancing the environment for private sector investment and growth.

1.2 Statement of the Problem

The main objective of the project is to strengthen the links between debt relief and poverty reduction policies and to demonstrate their usefulness in understanding the fiscal and macroeconomic issues that will arise from an increase in aid flows to Uganda. One of the requirements of HIPC is the Poverty Growth and Reduction Facility (PRGF), a lending arrangement of the International Monetary Fund (IMF), which is replete with structural reforms and quantitative conditions intended to improve the fiscal position of borrower governments so that more resources could be devoted to development programmes. In this context, the research aims to make an assessment as to whether the fiscal space created by the PRGF has indeed improved and contributed to the country's development strategy.

Specifically, the study seeks to

- Present the challenges and failures from the implementation of the PRGF.
- Establish how the PRGF has been underpinned within the national macro – economic framework and establish how the programs have shaped the public expenditure framework.
- Establish the linkage between the program with various national instruments including National development plans/visions/strategies, Medium term expenditure framework, National Budget, and Sector allocations.

The methodology employed for the study includes a review of documents associated with Uganda's PRGF arrangement, including Article IV consultations, reviews and memos, applications for waivers of conditionalities and staff reports; literature on PRGF obtained from the web; some AFRODAD publications and interviews with IMF and Uganda government's ministry of finance staff and some representatives of civil society.

This introduction is followed by a discussion on Uganda's relationship with the IMF. It gives an account of Uganda's history with the IMF, provides terms of the PRGF arrangement and explores the relationship between the PGRF and Uganda's poverty eradication action plan.

Following the description of the structural forms and quantitative conditions embedded in the PRGF arrangement, it gives the outcomes of PRGF reviews and indication of reforms. The third section covers PRGF and fiscal space, indicating the main sources of financing for Uganda's development programmes and discussing the impact of IMF Benchmarks and conditions in addressing the country's development priorities. The forth and last section is the key observations and conclusions which focus on social-economic impact of the PRGF.

2.0 Uganda Under the Policy Support Instrument

After the final review of the country's economic performance under the PRGF arrangement that was conducted in January 2006, the Executive Board approved a 16-month Policy Support Instrument (PSI)[1] for Uganda under the IMF's PSI framework which was cancelled almost immediately and replaced by a 3-year PSI. PSI is intended to further support the nation's economic reform efforts. According to the IMF, the PSI for Uganda is aimed at maintaining macroeconomic stability and at promoting structural reforms, as well as implementing the broader policy agenda as envisaged in the Uganda's Poverty Eradication Action Plan (PEAP). To-date there has been two reviews of the PSI – June 2007 and January 2008. The new program includes structural measures which are supposed to spur private sector activity, lower business costs, and improve the country's competitiveness. Macroeconomic policies would continue to emphasize stability and sound management of aid flows.

Like the PRGF, to monitor performance under the PSI, quantitative and structural assessment criteria and structural benchmarks have been set. Quarterly quantitative targets include ceilings on base money and net claims on government by the banking system; and a floor on net international reserves of the Bank of Uganda, as it was under the PRGF. Unlike the PRGF, the PSI is supposed to provide more timely advice on a member's economic and financial policies than is available through the regular consultation processes. In fact, the PSI is supposed to have a fixed schedule, usually semi-annually of reviews to provide timely and accurate information. In Uganda's case, as is shown in table 1, the regularity of reviews is the same (semi-annual) under both arrangements.

2.1 Terms and Conditions of the PSI

As can be deduced from Table 2.1, the terms of the PSI do not differ in substance and focus from those under the PRGF. Historically, Uganda has met most of them and those it has not, it has been able to explain or seek a waiver. The following are some of the examples of slippages acknowledged by government and waivers requested to the IMF:

Table 2.1 Slippages and Waiver Requests under the PRGF

Year	Slippage	Waiver requested
2003	Accumulation of new domestic arrears; submission of a plan to Cabinet to streamline Public Administration; submission to Parliament for a bill to repeal the National Social Security Statute; Development of a plan to clear the outstanding stock of domestic arrears including arrears on pensions; and Privatization of Uganda Development Bank.	Waiver for the missed observance of the performance criteria.
2004	Increase in base money; continuous performance on the accumulation of domestic arrears under the Commitment Control System; new lending by Uganda Development Bank; divestiture of Uganda Development Bank; increase in net claims.	Government recognises the significance of the programme slippages and will implement a range of far reaching measures to bring the programme back on track. Waivers requested for none observance of missed quantitative performance criteria.
2005	Ceiling on increase base money; ceiling on increase in net claims; accumulation of new domestic arrears; new lending by Uganda Development Bank. Accumulation of domestic arrears under the Commitment Control System	Every effort will be made to pay off the arrears with in the fiscal year. Government will implement a comprehensive set of measures to strength overall monitoring and control of domestic arrears. Government requests for a waiver for none observance of the performance criteria.

Source: compiled from letters by the Uganda Ministers of Finance in the IMF review reports 2003-2005.

In addition, in each report the government commits to consult with the IMF on its economic and financial policies, in accord with the funds policies and practices on such consultations. This commitment continues even under PSI. Table 2.2 summarises the Structural Reforms and Quantitative Conditions (Benchmarks) over the past six years of the PRGF.

Table 2.2 Description of the Structural Reforms and Quantitative Conditions (Benchmarks)

Quantitative conditions	Year	Review period
Ceiling on the increase in base money liability in the Bank of Uganda	2002/3, 2003/4	1st, 2nd, 3rd, 4th, 5th , 6th , PSI 1, 2
Ceiling on the increase in net claims on the central government by the banking system	2002/3, 2003/4	1st, 2nd, 3rd, 4th, 5th , 6th PSI 1,2,
Ceiling on the issuance of promissory notes by the government	2002/3, 2003/4	1st, 2nd, 3rd, 4th, 5th
Minimum expenditures under the poverty action fund (including the UPE component of the development expenditures)	2002/3, 2003/4	1st, 2nd, 3rd, 4th, 5th, PSI 1, 2
Accumulation of new domestic budgetary arrears of the central government	2002/3, 2003/4	2nd
Accumulation/stock of new domestic budgetary arrears under the Commitment Control System(CCS)	2002/3, 2003/4	1st, 2nd, 3rd, 4th, 5th PSI 1,2
Ceiling on public administration expenditure	2002/3, 2003/4	1st, 2nd, 3rd, 4th, 5th
New lending by Uganda Development Bank Ltd including on-lending on behalf of the government or the Bank of Uganda, pending divesture	2003/4	1st, 2nd, 3rd, 4th, 5th
Ceiling on the stock of external payments arrears incurred by the government or the Bank of Uganda	2002/3, 2003/4	1st, 2nd, 3rd, 4th, 5th, 6th , PSI 1,2
Ceiling on new non-concessional external borrowing with maturities greater than one year contracted or guaranteed by the government or Bank of Uganda	2002/3, 2003/4	1st, 2nd, 3rd, 4th, 5th,
Minimum increase in net international reserves of the Bank of Uganda	2002/3, 2003/4	1st, 2nd, 3rd, 4th, 5th 6th, PSI 1,2,
Ceiling on new non-concessional external borrowing with maturities greater than one year contracted or guaranteed by the government or Bank of Uganda – Bujagali hydro electric power/ JBIC loan guarantee to Phoenix Textile industry	2005/6, 2006/7, 2007/8	6th review, PSI 1,2
Ceiling on new external debt with maturity up to one year contracted or guaranteed by the government or bank of Uganda	2005/6, 2006/7, 2007/8	6th review, PSI 1,2

Source: Constructed by the author from PRGF and PSI Review reports

Table 2.3 Indicative Targets

Minimum expenditures under Poverty Action Fund (including the universal Primary Education component of development expenditure) Ceilings on public administration	2003/4, 2004/5, 2006/7, 2007/8 2003/4/	3rd 4th, 5th Review PSI 1,2 3rc, 4th, 5th review
Stock of domestic budgetary arrears under the Commitment Control System	2005/6, 2006/7, 2007/8	6th, PSI 1,2
Ceiling on the increase of base money liabilities of Bank of Uganda	2006/7	PSI 1

Source: Constructed by the author from IMF PRGF and PSI Review Reports

These quantitative conditions and structural reforms impact on the fiscal space for Uganda. They define and restrict the Government's ability to borrow from the Central Bank and banking system, to take commercial loans as well as restrictions on certain forms of expenditure, such as public administration.

While Review Reports suggest that assessment criteria are met, it is common knowledge that some, such as reduction in defence and public administration were regularly not met. In addition, supplementary budgets for such sectors as defence, state house and public administration were submitted and approved by Parliament, mainly as re-allocations from so-called "non-priority" spending, privatisation proceeds and higher-than-expected programme support loans. Also on occasion, there have been bail-outs of certain politically connected businessmen, which in the review reports all seem to be covered under "fully-funded supplementary budget". Oftentimes there are requests for waivers and almost always the requests are granted. In 2004, 8 of the 10 structural benchmarks were not met and some, such as the sale of Uganda Development Bank. Though a commitment was made to sell and merge with the Development Finance Department of Bank of Uganda (2004), etc. in 2005, the government of Uganda, in a letter to the Managing Director of the IMF, had reversed their decision stating that "the Uganda Development Bank will continue to function as a development bank but provide lending strictly on commercial terms".

2.2 Outcomes of PRGF and PSI Reviews

Assessing the outcomes of the PRGF reviews has to be prefaced with a highlight of the two important caveats that feature in every review report:

A disclaimer that "the views expressed in the staff report are those of the staff team and do not necessarily reflect the views of the Executive Board of the IMF" and a caveat that "the policy of publication of staff reports and other documents allows for the deletion of market-sensitive information". Because of these caveats and disclaimer, it is not at all clear how the reviews portray the realities on the ground[2]. Nevertheless they give the general trend of Uganda's economic performance. The key findings for selected periods are summarised as follows:

According to the IMF Resident Representative in Uganda, macro-economic imbalances have been reduced sharply in Uganda. Uganda was one of the first African countries to adopt a stabilisation programme and it has been successful. As a result, it has had 20 years of uninterrupted economic growth. The challenge now is sustaining growth over the long term; raising growth rates to 8-9% per annum and making growth more poverty reducing.

One major outcome of the reviews of the PRGF has been the 'graduation' of Uganda to a "mature stabiliser". Uganda is credited for having maintained a record of sustained macroeconomic stability and completed most first-generation structural reforms and began to tackle the next layer of reforms that address the business environment. It has long-standing political support at the highest level for prudent macro policies and the role of the private sector, and no balance of payments. Therefore the Ex-post Assessment of Long-term engagement with the Fund concluded that the country has no prolonged need for Fund financing, but would benefit from continued policy dialogue with the Fund that goes beyond regular surveillance relation, a purpose a PSI would serve.

Table 2.4 Selected Outcomes of PRGF and PSI

Review	Summary of findings	Proposed measures
Fifth under PRGF	• Macroeconomic performance has been good. • Fiscal programme broadly on track • Outlook for 2005/06 remains favourable • External debt close to upper bound for manageability.	• The incidence of corruption remains a serious constraint on business development that must be addressed
Sixth under PRGF	• Performance relative to the 6th and final PRGF satisfactory. • Two performance criteria not observed but slippages did not compromise programme integrity • Uganda received MDRI debt relief of SDR 87.7 • Main risk is loss of investor and donor confidence in the run up to elections	• Request for PSI to begin immediately after the expiry of the PRGF supported
First under PSI	• Uganda is weathering the electricity crisis reasonably well • Uganda's poverty indicators are improving • A robust economy and the government's negative borrowing requirement have been conducive to the development of the financial sector	• Need to fully fund statutory domestic arrears and commitment to budget principles. • While inflation risks need to be monitored, a tightening of monetary policy appears unnecessary
Second under PSI	• Uganda's impressive economic performance continues • Foreign exchange inflows intensified • Most programme targets were met • Further delays in addressing roads, power and water infrastructure could undermine medium term growth • Any revenue from oil production expected in 09 will be incorporated in the MTEF • Government's new debt strategy will govern project selection and financing	• Uganda's well-known infrastructure deficit must be addressed to ensure favourable growth prospects. • Oil must be used prudently and transparently

Source: Compiled from PRGF Review reports

3.0 The PRGF/PSI and Uganda's Development Strategy

PRGF-supported programs were framed around comprehensive, country-owned Poverty Reduction Strategy Papers (PRSPs). PRSPs are supposed to be prepared by governments with the active participation of civil society and other development actors. They are then considered by the Executive Boards of the IMF and World Bank as the basis for concessional lending from each institution and debt relief under the Heavily Indebted Poor Countries (HIPC) Initiative.

The Government of Uganda program outlined in the Memoranda of Economic and Financial Polices (MEFP) that is attached to the letter to the Managing Director of the IMF always indicates that PRGF (and later PSI) is embedded in the Poverty Eradication Action Plan (PEAP). A summary of the 2000 PEAP served as Uganda's PRSP, which was endorsed by the World Bank and Fund Directors in April 2000 as a basis for their concessional lending programs. A summary of Uganda's Poverty Eradication Action Plan (PEAP) is contained in each of the Review reports of the IMF. Some policy issues identified in the Government of Uganda 2002 progress report on the implementation of the PEAP/PRSP were also reflected in the Memorandum of Economic and Financial Policies. For example, in their joint staff assessment of the 2002 PEAP/PRSP progress report (EBD/02129:8/26/02 and IDA/SecM2002-0366; 8/15/02), World Bank and IMF staffs indicated that Uganda's efforts in the implementation of the strategy continued to provide a suitable basis for the World Bank and IMF concessional assistance.

Table 3.1 Comparison of PRGF/PSI and Uganda's Poverty Eradication Action Plan

Key features of the PRGF/PSI	Key pillars of Uganda's Poverty Eradication Action Plan - 2004/05 version
Reducing poverty by maintaining strong economic growth and macroeconomic stability	Economic management (addressing macroeconomic stability, fiscal consolidation and boost to private investment)
Making progress towards fiscal and debt sustainability; Increasing government revenue	Directly increasing the quality of life of the poor (delivery of primary education, health and water…)
Improving governance structures at all levels of government and building effective budget management Deepening financial intermediation	Ensuring good governance (human rights, democratization, elimination of corruption) and security and disaster management Enhancing production, competitiveness and incomes (agriculture, natural resources, infrastructure, business development)
Implementing structural measures to enhance private sector investment and growth	

Source: Created from various documents

Alignment between the PRGF and Uganda's Poverty Eradication Action Plan should not be that surprising. The Poverty Eradication Action Plan is Uganda's PRSP which is partly supported by the World Bank's PRSC, which in turn is closely linked to the PRGF. In fact each PRGF Review has an Appendix on Uganda's relationship with the World Bank Group and its Country Assistance Strategy (or more recently the Joint Assessment Strategy). For example in a box on Structural Measures, the PRGF review report lists 19 measures in the World Bank supported programme against 11 of the IMF's own measures. The IMF is largely responsible for the macro-economic policy measures of the government's Poverty Eradication Action Plan. Under the PSI, programme targets and structural reforms are based on a country's Poverty Reduction Strategy. Finally, Donor harmonisation and Alignment with the government's own policies is a central tenet of the Paris Declaration of Aid Effectiveness.

While it not as easy to identify which programmes derives from the other, it is possible to identify the points of convergence and divergence. Critics of the IMF and PRSPs hold that the centrality of broad participation and greater country ownership as the overarching principle is a myth. The country may seem to be in the driver's seat but the passenger reads the map. Many countries, including Uganda tolerate the IMF policy advice rather than welcoming it. This is particularly the case when the advice has political ramifications. Advice such as privatisation of state enterprises, the placement of Uganda Development Bank for sale (June 2003 review), raising taxes, reduction in public administration (June 2003 review) , restrictions in formation of new districts (June 2003 Review), advice against stepping up defence spending when the government "modernising the army" and fighting a rebellion; ceilings on new borrowing, and restrictions on government intervention to give cheaper credit to rural areas where over 80% of the Ugandan population lives, many of which feature in policy measure to maintain macroeconomic stability (and a number appear in PRGF review reports, as shown above), it is difficult for government to consider such policies as ensuing from its own Poverty Eradication Action Plan.

As the IMF Resident Representative conceded, "In the past there have been differences of opinion, but there is much more dialogue currently". Where these differences appear, the IMF "only highlights the trade-offs on the priority options government has itself identified". However, beyond a certain level, departure from the IMF advice poses big challenges for the government, as was the case in 2002 when such departure resulted in donor aid cuts to budget support.

It is important to note that there are differences of opinion within government, with many technocrats within the Ministry of Finance and the Central Bank favouring the IMF line, we think more to do with expediency than conviction (in private some of them have been known to hold contrary views) and some politicians preferring more interventionist approaches that are perceived to deliver poverty reduction (and election votes) faster. This is aptly illustrated by Semanda:

> ***Members of Parliament have powers to approve the budget. They often want to increase expenditure to their respective areas of origin and interest. They also try so much to reduce taxes in order to be popular to their voters. They want roads, schools markets, hospitals, clinics, seeds and projects for their respective constituencies well before the next election. These demands widen the budget financing gap" (which has to be financed by borrowing, thereby bringing them directly in conflict with the IMF targets for borrowing, inflation and debt (March 2007).***

3.1 Funding the PEAP

While Uganda has made considerable progress in liberalizing the economy leading to considerable economic growth, its social indicators, as is shown below, are still weak.

Table 3.2 Uganda Social Indicators

Population Life expectancy Population growth	30 million (2007 estimates) 51 years (2007) 3.4% p.a.
Adult literacy (15years and above)	66.8 % (2005)
Gross school enrolment	63%
Population using improved water Sources Health expenditure Infant mortality per 1,000 live births	60% 2.5% of GDP 79 (2005)
Maternal mortality (per 100,000)	250 (2005)

Source: Uganda National APRM Commission 2007

According to the Ministry of Finance (2008), net of arrears, interest repayment and project support by donors, the resources available to Government are Shillings 3,255 billion in fiscal year 2007/08 and Shillings 3,864.2 billion in FY 2008/09. Over the next five years, this is projected to rise to Shillings 7,577 billion in 2012/13. It is important to note that arrears and interest repayments take a first call on the Government's resources (Ministry of Finance 2008). Overall, resources available to Government are expected to increase by 10% per year over the medium term. Projections are as follows:

Table 3.3 Government of Uganda Medium Term Expenditure Projections

Sector allocations	2006/07 actual	2007/08 approved	2008/09 projected	2009/10 projected	20010/11 projected
Rural development (Agriculture, Lands, Housing and Urban Development)	158.472	214.530	233.580	273.820	277.640
Economic infrastructure and competiveness (Energy &Minerals, Works &Transport, Information &Communication Technology, Tourism, Trade and Industry)	772.063	1,100.710	1,142.815	1,165.142	1,414.943
Human development (Education, Health, Water and Environment, Social Development)	1,018.400	1,304.880	1,447.256	1,573.726	1,612.316
Security, Justice and Governance (security, Justice, Law and order, Public Sector Management, Accountability, Parliament and Public Administration)	1,459.760	1,744.180	1,770.000	1,883.411	1,992.087
Grand Total	**3,408.695**	**4,364.300**	**4,593.651**	**4,896.099**	**5,296.986**
Changes in Sector Allocations					
Rural Development			19.050	59.290	63.110
Economic Infrastructure &Competitiveness			42.105	64.432	314.233
Human Development			142.376	268.846	377.216
Security, Justice and Governance			25.820	139.231	247.907
Grand Total			**299.351**	**531.799**	**1,002.466**

Source: Ministry of Finance (2008)

As noted already, while Uganda has made considerable progress in addressing poverty, regional and gender inequality remain serious challenges. Greater fiscal space is needed to address the gaps.

Uganda, with the assistance of IMF and other development partners, has made a lot of progress in improving domestic revenue collection, mainly through improved tax administration where it has targeted improvements of 0.5% of GDP per year. As a result, the ratios of external assistance to domestic revenue has improved from 52% in 2003 to around 34% in 2007/08 and is projected to continue the downward trend, especially with oil revenues expected to start flowing in 2009.

However, because government revenues are still less than what they might be (due to tax evasion and other inefficiencies) and because political expediency opposes tax and fee increases, and because public expenditures are still high, fiscal deficit could well grow if donors were to refuse to support government. Uganda's revenue sources are as in the table below.

Table 3.4 Government of Uganda Revenues for 2005/06, 2006/07 and 2007/08 (Ush Billions)

Source	Outturn 2005/06	Outturn 2006/07	Approved budget 2007/08
Domestic revenue	2,313.9	2,710.6	3,189.8
Grants (Budget support and projects)	897.5	1,193.9	995.9
Budget support loans	76.3	394.1	198.8
Project loans	389.9	467.5	717.6
Amortisation (incl. External Debt repayment arrears)	-155.7	-113.9	-125.3
Exceptional financing	-41.3	-39.0	-31.5
Domestic financing	68.1	-357.9	-211.0

Source: Ministry of Finance 2008

Uganda's Poverty Eradication Action Plan has identified 8 strategic result areas, viz:

1. reduced income poverty and inequality;
2. improved human development where infant and maternal mortality are reduced
3. 100% net primary school enrolment
4. improved quality of primary education
5. increased post-primary and tertiary enrolment, disaggregated by gender
6. improved quality of health care
7. increased access to safe water for urban and rural areas; and
8. revitalized community development function

4.0 The PSI and Fiscal Space

4.1 Defining Fiscal Space

Fiscal space is understood differently by different actors. The IMF seems to rely on the definition developed by Peter (2005), which states that "fiscal space is the availability of budgetary room that allows a government to provide resources for a desired purpose without any prejudice to the sustainability of that government's financial position."

In defining fiscal space, the Government of Uganda seems to place more emphasis on the budgetary room and flexibility to allocate resources within the aggregate resource envelop to new (additional) priorities. Fiscal space refers to the magnitude of resources that can be re-allocated from the budget to finance additional activities without fundamentally distorting budget priorities or jeopardising budget objectives.[3] According to the official, fiscal space is realised when provisions in the budget exceed the optimal amount required for attainment of the intended objectives. "It is like cutting white fat off the meat". It is usually occasioned by the incremental approach to budgeting where a percentage is added to a sector's previous budget regardless of the level of need. The Ministry hastens to clarify that fiscal space does not refer to the resource envelop and is not new resources that were not anticipated in the budget as these would instead be saved as utilising them tantamount to fiscal indiscipline that is likely to jeopardise other macro-economic variables such as inflation, current account balances, exchange rate, and to some extent, interest rates.

Others, particularly those within civil society (e.g. Action Aid 2007) define fiscal space more broadly as the government capacity to fund economic and social infrastructure necessary to aid growth and development, without restricting it to the aggregate resource envelop. In other words, additional resources, particularly grants that are extra-budgetary, would qualify as fiscal space that could be applied to priority activities to aid development. Consequently, most criticisms about IMF's conditions that restrict government expenditure are coming at it from this understanding.

The IMF recognizes that the issues that arise in creating and using fiscal space are not new – governments have always had to judge how much scope there is to increase expenditure and how to finance and sustain their operations over time. What is new today is that as governments try to create that additional budgetary space so they can allocate it for spending priorities, they have to choose the best ways of creating fiscal space; and most importantly, they have to manage the trade offs.

The IMF lists the following as possible sources of fiscal space:

- Mobilisation of additional domestic revenue
- Borrowing from domestic and external sources
- Securing external grants
- Reprioritising expenditures (e.g. decreasing expenditures in one sector in order to increase spending in another)
- Making spending more efficient

Strictly speaking though, according to the Ministry of Finance, additional domestic revenue, borrowing from internal and external sources, external grants and even re-prioritising expenditure, as long as they do not result in additional activities, would not fit the definition of fiscal space. In this study, the more liberal definition by civil society actors is applied.

4.2 Trade-offs

IMF's October 2007 Regional Economic Outlook for Sub- Saharan Africa lists some of the trade-offs of creating fiscal space, and posits that:

- Raising taxes lessens dependence on donors, and avoids Dutch disease effects from external inflows. However, it also implies that resources the private sector might otherwise use to support consumption and investment are re-allocated to the public sector.
- Domestic borrowing can be a source of funding for government expenditures, but it has significant drawbacks. It should only be undertaken carefully with due regard for long-term fiscal sustainability. Also, the IMF warns that if credit that would normally be available to the private sector is taken out by government, then domestic borrowing potentially crowds out private investment.
- Debt relief has opened up fiscal space for many developing countries. But it can also create an appreciation of the local currency, thus decreasing the competitiveness of the export sector. In Zambia, after the getting debt relief in 2005, the government did not anymore need to purchase dollars from the local market to pay off its debt service. With no government demand for dollars, the Zambian kwacha appreciated dramatically. This is good on one hand, because it means, for example, that Zambia can import oil more cheaply. But it also means that agricultural and mining exports now delivered less to the economy.
- Concessional loans increase the resource envelope available to the economy. But due regard has to be paid to debt sustainability.
- Re-prioritising expenditures is a policy option when there is little room to increase resources generally. But it is most difficult, especially for the poorest countries that have so little that every expenditure becomes a priority.
- Making spending more efficient is most inherently desirable but the institutional reforms required takes time, in part because they often have political and distributional implications.
- Aid is a source of fiscal space but the key issue in many countries is the absorptive capacity which limits the amount of external aid they can deploy.
- National policy-makers always face a dilemma between spending for infrastructure that promotes growth and development on one hand, and social spending to advance non-income related human development.
- Having well-designed medium-term expenditure frameworks is critical for a comprehensive approach to developing fiscal space. But implementing fully fledged MTEFs is so challenging that only a few countries have done so. Uganda has moved farthest on this, complete with sectoral plans (SWAPs), which call for substantial capacity building in line ministries.

As can be seen from the discussion above, the IMF is still in a process of developing for itself a set of clear policy recommendations on fiscal space. They have started by doing case studies of the five African countries. The trickiest part is the trade-offs for which there is still no definitive analysis while policy makers in poor countries have political imperatives to consider. The IMF acknowledges that numerous governments are already re-orienting their fiscal policies toward growth and poverty reduction. For example, Uganda Government has decided that in FY 2008/09 there will be an even split between allocations which are aimed at strengthening the growth of the private sector in rural areas and the economy more broadly, and those which are aimed at supporting the welfare of all Ugandans (Ministry of Finance 2008).

Aware of the compelling temptation for Governments to contract loans on commercial terms, for the IMF, the immediate question is how much room the easing of macroeconomic and debt burden constraints provides in the short run for fiscal expansion (IMF, 2007:22).

The just-concluded G20 meeting, which was attended by the IMF, discussed the importance of creating and maintaining fiscal space. But the G20 wanted to know how a balance can be achieved between fiscal policy as a counter-cyclical macroeconomic instrument on one hand (e.g. reduced budget deficits, reduced domestic borrowing, etc.), and the best ways of creating fiscal space to finance social and economic development, on the other. While the G20 resolved to look further on how to explore lessons from its member countries, their focus would be around:

- improving the efficiency and effectiveness of government expenditure;
- developing the design of medium-term fiscal expenditure frameworks;
- coordinating long-term or inter-generational budgeting; and most importantly,
- the identification of the range of public services critical for economic development, the returns to investing in them, and the most effective ways of implementing policy and institutional solutions to delivering them.

Unfortunately, the G20 stopped short of actually recommending policy steps to take, perhaps a reflection of the internal debates that remain unresolved. However, it is quite clear that by putting fiscal space on their agenda for the first time, the G20 now acknowledges that it has become a major global policy issue to be addressed.

Aside from the G20, a number of African countries are also moving in the direction of trying to answer the question, "Where do we get the money to finance our economic and development needs?" For example, Uganda Government is concerned about declining donor support and has embarked on strengthening revenue administration and re-prioritisation of expenditures making rural development; economic infrastructure and human development (education, health, water and environment) among the top priorities.

4.3 HIPC, Debt Relief, and Fiscal Space

It follows that the government's priority expenditure should be to boost the identified strategic result areas. It is true to say that the fiscal space created by HIPC debt relief was used to address poverty reducing areas of government spending. Consequently, Uganda's selected expenditure in priority areas as a percentage of the budget under the ring-fenced Poverty Action Fund (PAF) has been growing from 23% in 1998/09 when it was created to around 33% per year in 2005/06. Selected expenditures were as shown in table 6 below.

Table 4.1 Expenditures on Poverty Action Fund Priority Areas, as % of budget 1998-2003

Priority area	1998/99	1999/00	00/01	01/02	02/03
Education	27	26	25	24	23
Health	7	7	7	9	9
Water	1	2	2	3	3
Roads and works	6	8	9	8	7
agriculture	1	2	2	2	2

Source: Background to the Budget 2005/06

It should be noted that even where the share of the budget is declining slight for education, it remains the biggest percentage. In nominal terms, the budget for health has trebled over the past four years while that of water has increased exponentially from 1% to 3% over the same period AFRODAD (2006). It should also be noted that all Quantitative Performance criteria and Benchmarks have "Minimum expenditure under the Poverty Action Fund (including the Universal Primary Education component of development expenditures)" as indicative targets (see table 2). It also has the principle of re-prioritizing expenditure (by setting a ceiling on public administration expenditures).

According to the IMF Resident Representative in Uganda, debt relief, particularly the MDRI has given Uganda some fiscal space, which has allowed it to borrow on commercial terms for the Bujagali Power project. Uganda has formulated a comprehensive and integrated debt management strategy (Uganda Debt Management Strategy 2007) designed with the following objectives:

1. Impose a five-year borrowing cap. The Minister of Finance is to announce 5-year limits on new external loans for approval by parliament each fiscal year.

2. Loan requests must demonstrate absorptive capacity, with clear procurement plans and written confirmation of counterpart funding as included in the MTEF.
3. Limit government guarantees to private creditors and individuals and increase transparency
4. Put in place statutory instrument for external debt management to clarify the 'back office', 'middle office' and 'front office' functions of different stakeholders in external debt management.
5. Define the process of issuing domestic debt, including the channel for communication between Bank of Uganda and Ministry of Finance and the system for monitoring performance.
6. Issue public debt management regulations to guide implementation of the debt strategy and harmonize relevant existing laws and regulations.

4.4 Expenditure Re-allocations

Another source of Fiscal Space is budgetary expenditure reallocation. According to the Ministry of Finance, overall, "resource allocations between themes and sectors are intended to reflect the Government's overall policy priorities as laid out in the PEAP and the NRM (ruling party) 2006 manifesto. Government's four main strategic budget priorities are Rural Development, Economic Infrastructure and Development, Human Development and Security, Justice and Governance". "In FY 2008/09 there will be an even split between allocations which are aimed at strengthening the growth of the private sector in rural areas and the economy more broadly, and those which are aimed at supporting the welfare of all Ugandans". As such, Rural Development and Economic Infrastructure will receive 30% of the budget, Human Development 32%; and Security, Justice and Governance 38%. MTEF sector shares between 2006/07 and 2012/13 as in table 7

Table 4.2 MTEF Allocation shares (% of total budget)

Sector	2006/07	07/08	08/09	09/10	10/11	11/12	12/13
Security	9.2	9.3	8.8	8.0	7.3	6.4	6.3
Works and transport	11.3	6.1	13.6	13.4	14.5	14.8	13.6
Agriculture	3.8	2.5	4.6	4.5	4.2	3.8	3.5
Education	17.6	16.1	17.5	15.4	14.1	13.6	12.9
Health	9.3	9.0	9.3	7.8	6.3	5.5	5.4
Water and environment	3.0	3.3	2.9	2.6	3.0	2.6	2.4
Justice, Law and Order	5.0	4.9	4.7	4.0	3.7	3.5	3.2
Accountability	6.8	7.1	8.2	6.5	5.7	5.1	4.8
Energy and Mineral Development	8.3	9.5	9.0	6.5	5.9	5.4	5.0
Tourism, Trade and Industry	1.1	0.9	0.7	0.6	0.6	0.6	0.5
Lands, Housing and Urban Development	0.4	0.2	0.2	0.3	0.3	0.3	0.3
Social Development	0.4	0.5	0.4	0.4	0.4	0.4	0.3
Information & Communication Technology	0.0	0.1	0.1	0.1	0.1	0.1	0.1
Public Sector Management	12.1	10.2	9.3	9.4	7.9	7.4	7.1
Public Administration	4.3	3.7	2.5	2.5	2.9	1.9	1.8
Legislature	1.3	1.7	1.5	1.4	1.3	1.1	1.1
Interest Repayment	6.2	6.1	6.6	5.0	4.0	3.7	3.3
Total	**100**	**100**	**100**	**100**	**100**	**100**	**100**

Source: Ministry of Finance 2008

From Table 4.2, the trend of increasing certain expenditures as a percentage of the national budget over the medium term is discernable only for works and transport (infrastructure). However, significant reductions are discernible in security (9.2% in FY2006/07 to a projected 6.3% in 2012/13), public administration from 4.3% to 1.8% of the national budget over the same period. The same applies to Public Sector Management

(12.1% to 7.1%) and interest repayments from 6.2% to 3.3%. This is consistent with the policy advice by the IMF under the PSI.

Within sectors, there are re-prioritisations to increase efficiency and effectiveness. For example in education, a critical feature of the Universal Primary Education initiative has been the need to address efficiency gaps. While enrolment numbers have grown significantly, completion rates are still low. Government plans to ensure that once children are enrolled, they complete the course. In agriculture, it is acknowledged the both production and productivity remain unacceptably low. Consequently, resources are being shifted towards interventions that increase production and productivity for both farm and non-farm activity. The traditional NAADS strategy has been reviewed to emphasise enterprise selection, value addition, and the like. The real contention over fiscal space is on the how additional budgetary room is deployed.

4.5 Impact of PSI on National Budget and MTEF

Under the PSI, since it is a non-financing instrument, the IMF influences the decisions on government spending mainly through its surveillance role. Firstly, through its support to government in determining the aggregate resource envelop, it influences the fundamentals of the economy. Secondly, through monitoring missions, IMF is able to determine whether the economy is deviating from the agreed path. Once there is a deviation the IMF takes it up with the Fiscal (Ministry of Finance) and Monetary (Bank of Uganda) authorities to agree measures to address the problem. These measures are then documented in a Memorandum of Economic and Financial Policies (MEFP) with Quantitative Performance Criteria and Benchmarks and qualitative Structural Performance Criteria and Benchmarks, which provide the basis for next review.

Since the introduction of the PSI, Quantitative Assessment Criteria and Indicative Targets have remained as:

- Ceiling on the increase in base money liabilities of the Bank of Uganda (as under PRGF)
- Ceiling on the increase in net claims on central government by the banking system (as under PRGF)
- Ceiling on the stock of external payments arrears (as under PRGF)
- Ceiling on new non-concessional external borrowing(as under PRGF)
- Ceiling on new external debt(as under PRGF)
- Minimum increase in net international reserves of Bank of Uganda(as under PRGF)
- Stock of domestic budgetary arrears under Commitment Control System(as under PRGF)
- Minimum expenditure on the Poverty Action Fund(as under PRGF)

Analysing the two reports that have been issued since the introduction of the PSI, it is clear that the IMF influences much of the Government budget and MTEF. In the MEFP, the Minister of Finance reports on such details as avoidance of accumulation of new arrears to domestic suppliers related to utilities, supplier credits and international subscriptions; commitment to publish notices in newspapers about honouring invoices; installation of pre-paid water meters; along with strategic economic issues such as prospects for commercial oil production; medium term electricity strategy, further development of the financial sector, including pensions and reform processes in the Revenue Authority. Simply put, PSI puts the IMF's stamp of approval on almost every aspect of the economy. (See first and second reviews under PSI).

4.6 Impact of PSI on Sector Allocations

The sector allocations are a technocratic and political function of government. While the political arm would wish to be more liberal, the technocratic arm of government, particularly in the Ministry of Finance would generally adhere and even behave in a manner which is more IMF than IMF itself, as, for example, is exemplified in the very strict definition of fiscal space. But by putting ceilings on increase in money supply, claims on the central government, new non-concessional lending, etc, the IMF directly impacts on the funds available for allocation to different sectors, and inadvertently strengthens the technocratic arm over the political arm of government.

According to the IMF Resident Representative, the IMF's role is to highlight the trade-off on priorities government has identified, prioritising expenditures that lay foundations for long term growth and which do not crowd out private investment. However, government cannot afford to disregard the advice given by the IMF and in one of the letters the Minister wrote to the Managing Director, he was requesting to be allowed to expand the aggregate resource envelop to accommodate new demand. The advice given to government on the fiscal space created by the MDRI debt relief, for example, has been wholly incorporated in the Debt Management Strategy. Henceforth, the scope to borrow on commercial terms shall be for infrastructural projects which have been jointly identified (energy, roads, water) as the "most important constraints" to Uganda's long term prospects, notwithstanding the fact that Human Resource Development is also a major constraint to the Ugandan economy.

Under the MDRI, Uganda received debt relief amounting to US$126 million, which, according to the IMF, was made available to help Uganda make progress towards its Millennium Development Goals. Now, Uganda undertook an MDG needs assessment which indicated that huge increases are needed in both aid and public, estimated in the region of US$33.5 billion for the period up to 2015. This translates into per capita requirements of US$ 92 of which US$42 would be financed domestically through household and government contributions. While PRGF-supported programmes can be said to be MDG compliant, the scale of spending needed to achieve MDGs simply cannot happen under the PRGF constraints. It is not possible to invest more and strategies for sectors such as health are becoming neither more nor less pro-poor AFRODAD (2006).

Since 2004 political arm of government has become impatient with rate of social and economic transformation of Uganda. The new minister of Finance has introduced a Rural Development Strategy operationalised under Prosperity for All Programme. While the Poverty Eradication Action Plan remains the over-arching national programme, efforts have been made to fast track the Prosperity programme, because the former does not align well with the manifesto of the ruling party. Like Zambia, the Uganda government has decided the re-introduce a Five-Year National Development Plan to replace the decade-old Poverty Eradication Action Plan. Donors have interpreted this as the desire on the part of government for greater government intervention for short-term political expediency. Observers perceive this as a government becoming more confident as its ability to raise domestic revenue becomes enhanced and in anticipation of the flow of oil revenues, expected to commence in 2009. In the context of the discussion in this paper, we can say that it is a question of who makes the choices concerning the utilization of fiscal space as it expands.

Uganda's articulation of the need for cheap credit for rural areas

Access to credit is a problem that has long bedevil Ugandan, interest rates have remained stubbornly high for many years. Nominal cost of borrowing over the last 6years has ranged between 18% and 22%. Commercial banks tend to focus on large business neglecting small farmers and business people. Even where commercial loans are available there maturities are quiet short. Women in particular have been disadvantaged.

The credit problem has become a political issue, with rural voters demanding government intervention. In 2006 general elections president Museveni made Bonna Bagagawale a frequent campaign promise which has been translated into $42 million programme to provide subsidies credit to small holder farmers through Savings and Credit Cooperatives (SACCOs), which are member-organised and owned.

In this Letter of Intent to the IMF, the government of Uganda describes one of the strategies to improve the availability of financial services in rural areas through SACCOs:

Improving the availability of financial services in rural areas is an important objective. Such services are being provided by the member-owned savings and cooperatives (SACCOs), but we are concerned that they are not adequately supervised and lack accounting skills. To safeguard member deposits in these institutions, we are considering options to regulate SACCOs. In the meantime, we will ask Postbank Uganda (PBU) to assist by bolstering accounting capabilities of SACCOs. We intend to provide UShs 8 billion (approx. US$4.3m) in the 2007/08 budget for this effort (IMF, June 2007).

According to the IMF Resident Representative, Prosperity for All is a broad-based initiative which the IMF supports. Components include:

- Better extension services (improving National Agricultural Advisory Services (NAADS);
- Water for production
- Infrastructure for rural areas where 80% of the population lives – roads and rural electrification
- Better human capital to rural areas – deploying university graduates to operate at sub-county level (Local Council 3) and
- Formation of SACCOs for accessing cheaper micro-finance in groups formed at sub-county level.

More recently the president has also initiated a programme to provide funds to 50 families per sub-county. (There are over 900 sub-counties in Uganda).

According to the IMF, it has had views on only one element of the initiative – the need to put in place an effective regulatory framework for all micro-finance providers including the Savings and Credit Cooperatives (SACCOs), arguing that, in attempting to make rural credit cheap without a regulatory framework, government will be setting interest rates outside of market operations, which deters financial services to rural areas such as those currently provided by Micro Finance Institutions (MFIs). The principle here being that while rural financial services should be affordable (government's argument), they should also be sustainable (the market argument). MFIs should be regulated and government should allow competition rather than targeted lending and setting interest rates.

Spurred by the IMF's signalling role, the World Bank supported Country Economic Memorandum warns that "Uganda's development partners have been uncomfortable with the ad hoc interventions" by the Government of "wanting faster development" and starting to intervene … "to hasten the pace of growth". Accordingly, the essence of the Economic Memorandum seeks to appease the uncomfortable development partners by pouring cold water on to the Government initiatives to revive the economy. To quote the report, "with all the global analysis and debate, and with impatience with recent growth at home, it would be tempting for Uganda's policy makers to move to a new course in pursuit of more rapid growth. …We believe that would be a mistake. Uganda does not need a fundamental change in its growth strategy". Preference is that Government stays the course on NAADS, which has had seven years to prove that it works but has, by and large, failed to do so.

The Parable of the Goats

A farmer has lost all her goats. A neighbour comes from the north and joins the farmer in the search for her lost goats. The neighbour works even harder than the farmer herself but in reality does not want her to find the goats.

This smacks of 'the Parable of the Goats' where outsiders pretend to know better than those they are supposedly assisting but seemingly with no intend of helping them find a solution. In this case, all the Country Economic Memorandum is doing is driving a wedge between the "President and the Government" on the one hand and the "technocrats and Uganda's development partners" on the other. The former are described as "impatient" and "acting in an ad hoc" manner; the latter are uncomfortable with the Government's interventions. To heighten the issue, the morning of the launch in Kampala of the Country Memorandum read on its front page, "The President suspends funding for NAADS". In the article, the President is quoted as having done this due to the outcry by the population on the ineffectiveness of NAADS which is accused of spending money mainly on seminars rather than on farmers.

If IMF's signalling role was less, the differences with government (particularly politicians) would be much more pronounced. The IMF itself contends that while many of Uganda's donors still rely on its PSI reports as input to their aid decisions, its signalling role is not as significant as is the case in other countries. In fact it argues that now other donors have more capacity for working on macroeconomic policy, and since macroeconomic imbalances have shrunk, it will move more to its surveillance role.

Sector ministries prepare investment plans painstakingly working out the resources needed to realise the plan. But sector ceilings constrain the full implementation of the plans. Examples are in Education's Fast Tracking programme and additional health programmes to fight malaria and HIV/AIDS that could not be accepted on macroeconomic stability reasons. This dilemma boils down to the 'logic of need' versus the 'logic of the available', leaving no room for a sector to dream.

While the IMF claims that it only helps government do projections to create the aggregate resource envelop, this very envelop is what Government uses to determine sector ceilings under a Commitment Control System, which the IMF monitors religiously under Quantitative Performance criteria and Benchmarks.

In response the IMF contends that it is wrong to attribute the constraints on significantly higher Government spending to IMF programmes and advice. Rather, they are imposed by "sustainability considerations" (IMF Resident Representative). According to him, there is no sustainable fiscal space to fund the MDGs as computed above because the funding required represents an additional 10% of Uganda's GDP or 50% of current total government spending, which cannot be mobilised domestically from taxation, borrowing, spending efficiency or re-prioritisation. If it were to come from external grants that would completely distort macroeconomic fundamentals.

However, concerns about the impacts of IMF restrictive fiscal and monetary policies have recently been expressed in other new reports by the Washington DC-based Centre for Global Development,[4] which examined IMF policy impacts on health efforts, and by Action Aid International Education Team,[5] which examined IMF policy impacts on education. Both reports found that the IMF's policies were unnecessarily restrictive and not facilitating "scaling-up agenda" for aid, public spending and investment in order to fight HIV/AIDS and meet the MDGs. Both reports found that wage bill ceilings could be harmful to education and health needs. The reports echoed calls by the IMF's IEO report that a broader array of fiscal and monetary policy options should be made available to policy makers in borrowing countries.

5.0 Key Observations and Conclusions

Since the 1990s Uganda has made important strides towards macro-economic stabilisation. According to the IMF, Uganda's macro-economic imbalances have been reduced sharply and the country has had 20 years of uninterrupted economic growth. Consequently, Uganda has graduated to a "mature stabiliser", no longer needing a financing programme under the PRGF but instead moving on to PSI since 2006.

However, while Uganda has played by the rule book and seemingly made considerable progress in addressing poverty, its social indicators are still weak. And while Uganda's Poverty Eradication Action Plan has identified strategic result areas to reduce income poverty and inequality and improve human development, the scale of spending needed to achieve PEAP and MDGs simply cannot happen under the PRGF/PSI constraints.

This study sought to establish how PRGF/PSI has been underpinned within the national macro-economic framework, and how IMF programmes have shaped the public expenditure framework. It has been established that the quantitative conditions and structural reforms define and restrict Uganda's fiscal space- government's capacity to fund economic and social infrastructure necessary to aid growth and development.

Debt relief under HIPC and MDRI have expanded Uganda's fiscal space. For example, the Poverty Action Fund created under HIPC debt relief initiative created fiscal space to fund selected expenditure in priority areas of government such as health and education, PAF has grown from 23% of the budget to 33% in 7 years. Additional fiscal space created under MDRI is allowing government to take loans on commercial terms to fund Bujagali Hydro Electric Power Generation. In terms of other sources of fiscal space, Uganda has mobilised domestic revenue at a growth rate of 0.5% of GDP per year. Uganda has undertaken inter and intra sectoral prioritisation and expenditure re-allocation and it has formulated a comprehensive and integrated debt management strategy.

However, there are differences of opinion between the IMF and the government and between the IMF, Government and Civil Society over who determines and controls the size and utilisation of the fiscal space a country like Uganda should have. The IMF claims that its role is to highlight the trade-off on priorities the government has identified, prioritising expenditures that lay foundations for long term growth and which do not crowd out private sector investment. Since 2004, the political arm of government has realised the folly of IMF and become impatient with the slow pace of social and economic transformation and has introduced more interventionist programmes. On some of these interventions like provision of affordable micro-credit to rural farmers, the IMF has taken exceptions, arguing that cheap credit must be sustainable spurring other development to also become uncomfortable with the ad hoc interventions. This demonstrates that IMF's surveillance and signalling remains as powerful under the PSI as it was under the PRGF.

However, if, as they do, IMF-imposed constraints impact severely the sector ministries' ability to implement their plans for health, education, HIV/AIDS, malaria and other critical areas, the "logic of the available" versus the "logic of the need" calls into question the efficacy of the IMF policy support.

Concerns about the impact of the IMF's restrictive fiscal and monetary policies are growing. If there is going to be room to boost economic growth and to finance the meeting of PEAP objectives and MDGs then the definition of fiscal space has to be broadened to include extra budgetary resources beyond the aggregate resource envelope the IMF sets for the country and flexibility for government to determine its priorities for the short, medium and long-term. After all, Uganda is a "mature stabiliser" which ought to know expenditure that lays foundation for long-term inclusive growth.

This case study clearly demonstrates that having played by the rule book, Uganda's frustration with the IMF-influenced macro-economic framework is justified and exemplifies failed policy advice.

ANNEXES

1. The Poverty Reduction and Growth Facility

What is the Poverty Reduction and Growth Facility?

In September 1999, the IMF established the Poverty Reduction and Growth Facility (PRGF) to make the objectives of poverty reduction and growth more central to lending operations in its poorest member countries. The PRGF is the IMF's concessional facility for low-income countries. PRGF-supported programs are based on country-owned poverty reduction strategies adopted in a participatory process involving civil society and development partners and articulated in a Poverty Reduction Strategy Paper (PRSP). This is intended to ensure that each PRGF-supported program is consistent with a comprehensive framework for macroeconomic, structural, and social policies to foster growth and reduce poverty. PRGF loans carry an annual interest rate of 0.5 percent, and are repayable over 10 years with a 5½-year grace period on principal payments.

Key Features of PRGF

- Budgets that are more pro-poor and pro-growth
- Ensuring appropriate flexibility in fiscal targets
- Measures to improve public resource management/accountability
- Poverty and social impact analysis (PSIA) of major macro adjustments/structural reforms
- Broad participation and greater ownership
- Embedding of the PRGF in the overall strategy for growth and poverty reduction
- More selective structural conditionality

First, the principle of broad public participation and greater country ownership is central to the PRGF. In this regard, discussions on the policies underlying PRGF-supported programs are more open, since they are based on the nationally-owned PRSP. With increased national ownership, PRGF conditionality has become more parsimonious, focused on the Fund's core areas of expertise, and limited to measures that have a direct and critical impact on the program's macroeconomic objectives.

Second, PRGF-supported programs reflect more closely each country's poverty reduction and growth priorities. Key policy measures and structural reforms aimed at poverty reduction and growth are identified and prioritized during the PRSP process, and if feasible, their budgetary costs are assessed. Countries' budgets under PRGF-supported programs reflect this analysis. Moreover, fiscal targets in PRGF-supported programs respond flexibly to changes in country circumstances and pro-poor policy priorities, while ensuring that the strategy can be financed in a sustainable, non-inflationary manner.

Third, PRGF-supported programs focus on strengthening governance, in order to assist countries' efforts to design targeted and well-prioritized spending. Of particular importance are measures to improve public resource management, transparency, and accountability. PRGF-supported programs also give more attention to the poverty and social impacts of key macroeconomic policy measures.

IMF-World Bank cooperation

PRGF-supported programs are designed to cover only areas within the primary responsibility of the IMF, unless a particular measure is judged to have a direct, critical macroeconomic impact. Areas typically covered by the IMF include advising on prudent macroeconomic and financial policies and related structural reforms such as exchange rate and tax policy, fiscal management, budget execution, fiscal transparency, and tax and customs administration.

When appropriate, the IMF draws on World Bank expertise in designing PRGF-supported programs, and the staffs of the Fund and Bank cooperate closely on conditionality.

The Bank staff takes the lead in advising the authorities in the design of poverty reduction strategies in areas such as poverty assessments, monitoring, structural and sectoral issues, social issues, and costing priority poverty-reducing spending.

How the PRGF is Financed

Concessional lending under the PRGF is administered by the IMF through the PRGF-ESF and PRGF-HIPC Trusts. The PRGF-ESF Trust borrows resources from central banks, governments, and official institutions generally at market-related interest rates, and lends them on a pass-through basis to PRGF-eligible countries. The difference between the market-related interest rate paid to PRGF-ESF Trust lenders and the rate of interest of 0.5 percent per year paid by the borrowing members is financed by contributions from bilateral donors and the IMF's own resources.

Terms of the PRGF

- As of August 2007, 78 low-income countries are eligible for PRGF assistance.
- Eligibility is based principally on the IMF's assessment of a country's per capita income, drawing on the cut-off point for eligibility to World Bank concessional lending (currently 2005 per capita gross national income of $1,025).
- Loans under the PRGF carry an annual interest rate of 0.5 percent, with repayments made semi-annually, beginning 5½ years and ending 10 years after the disbursement.
- An eligible country may normally borrow up to a maximum of 140 percent of its IMF quota under a three-year arrangement, although this may be increased to 185 percent of quota in exceptional circumstances. In each case, the amount will depend on the country's balance of payments need, the strength of its adjustment program, and its previous and outstanding use of IMF credit. The expected average access under the initial three-year arrangement is 90 percent of quota, and 65, 55, 45, 35, and 25 percent of quota for second through sixth-time users of the facility, respectively. "Low-access" PRGF arrangements with a standard level of 10 percent of quota may be used for members with little or no immediate balance of payments need. PRGF-eligible members with per-capita income above 75 percent of the cut-off for World Bank concessional lending, or members borrowing on commercial terms, may combine PRGF arrangements with lending from the IMF's non-concessional Extended Fund Facility.

2. Uganda Structural Performance Criteria and Benchmarks, and Status of Implementation Under the Program For 2003/04

PERFORMANCE CRITERIA/BENCHMARK	POLICY MEASURES
Performance Criterion	Submit to cabinet a plan to reduce government expenditures
Benchmark	Production of a business plan for the Uganda Revenue Authority
	Fiscal
Benchmark	Verify domestic budget arrears outstanding off end June 2002
Performance criterion	Develop a time-bound plan to clear outstanding stock of domestic arrears, including arrears on pensions
Benchmark	Develop the annual business plan for implementing tax administration measures in 2003/04, in accordance with the Uganda Revenue Authority's (URA) five year corporate plan, and a plan for the completion of the computerization of URA
Benchmark	Establish a unit in the office of the inspector general of Government to identify and investigate cases of improper conduct and corruption by URA staff
Performance criterion	Adoption by cabinet of a time bound plan to clear the stock of pension arrears.
Benchmark	Ensure that Internal Auditor Office of MFPED will issue a report with verified figure for the stock of non-wage/non-pension arrears to June 2003, including revised figures of arrears to date.
Benchmark	Pay off arrears accumulated under CCS in 2002/3
Benchmark	Include in the budget documents for the 2004/05 budget, and an update of plan for clearing the stock of non-pension arrears.
Benchmark	Complete initial stage of the modernisation of the URA: • award contracts to implement integrated tax administration system for domestic taxes; • rollout automated system for customs data (ASYCUDA++) to at least three stations other than the Kampala long room; • identify 75% of late filers within 45 days of the statutory filing period; and • Prepare registry of pay-as-you earn (PAYE) per employee and tax bracket.
Benchmark	
	Fiscal Decentralization
Benchmark	Produce aggregated local government financial statistics for 2001/02 fiscal year
	Financial Sector
Performance criterion	Submit to parliament a bill to repeal the National Social Security Fund (NSSF) statute to pave way for regulation of the NSSF by Bank of Uganda (BOU)
Benchmark	Ensure development of all banks of a Capital Compliance Plan detailing proposals for complying with January 2003 capital requirement for minimum paid up capital.

Benchmark	Assign the privatisation of Uganda Development Bank limited (UDBL) to the Privatisation Unit and engage a privatisation advisor to handle the privatisation
Performance criterion	Privatise the UDBL
Benchmark	Government will decide on the divesture option to follow on the UDBL based on the recommendation of the transaction advisor.
Benchmark	Submit to cabinet an anti-money laundering bill
Benchmark	Integrate and computerise debt-information management systems within the MOFPED
	Safeguards assessment report
Benchmark	Publish the audited financial statements of the BOU for the year ended June 30th 2002.
Benchmark	Publish the audited financial statements of the BOU for the year ended June 30th 2003
Benchmark	Ensure that the BOU and Ministry of Finance enter into a memorandum of understanding to ensure that unrealised gains will be excluded from the distributable profits.

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Footnotes

[1] According to the IMF, the framework for PSI

is designed for low-income countries that may not need, or want, IMF financial assistance, but still seek IMF advice, monitoring and endorsement of their policies. PSI is voluntary and demand driven.

[2] While each of the Review reports have this statement, IMF Resident Representative says that having checked all documents from Uganda on account of market sensitive information going back to at least 2003, he was not bale to trace any such deletions

[3] As defined by a senior official in the Ministry of Finance, Uganda during an interview.

[4] “Does the IMF Constrain Health Spending in Poor Countries? Evidence and an Agenda for Action,”

http://www.cgdev.org/doc/IMF/IMF_Report.pdf

[5] “Confronting the Contradictions: The IMF, wage bill caps and the case for teachers”:http://www.actionaidusa.org/imf_africa.php

—for IMF critique of report:http//www.imf.org/external/np/vc/2007/051707.htm

—for ActionAid rebuttal to the IMF:http://www.actionaid.org/main.aspx?PageID=652