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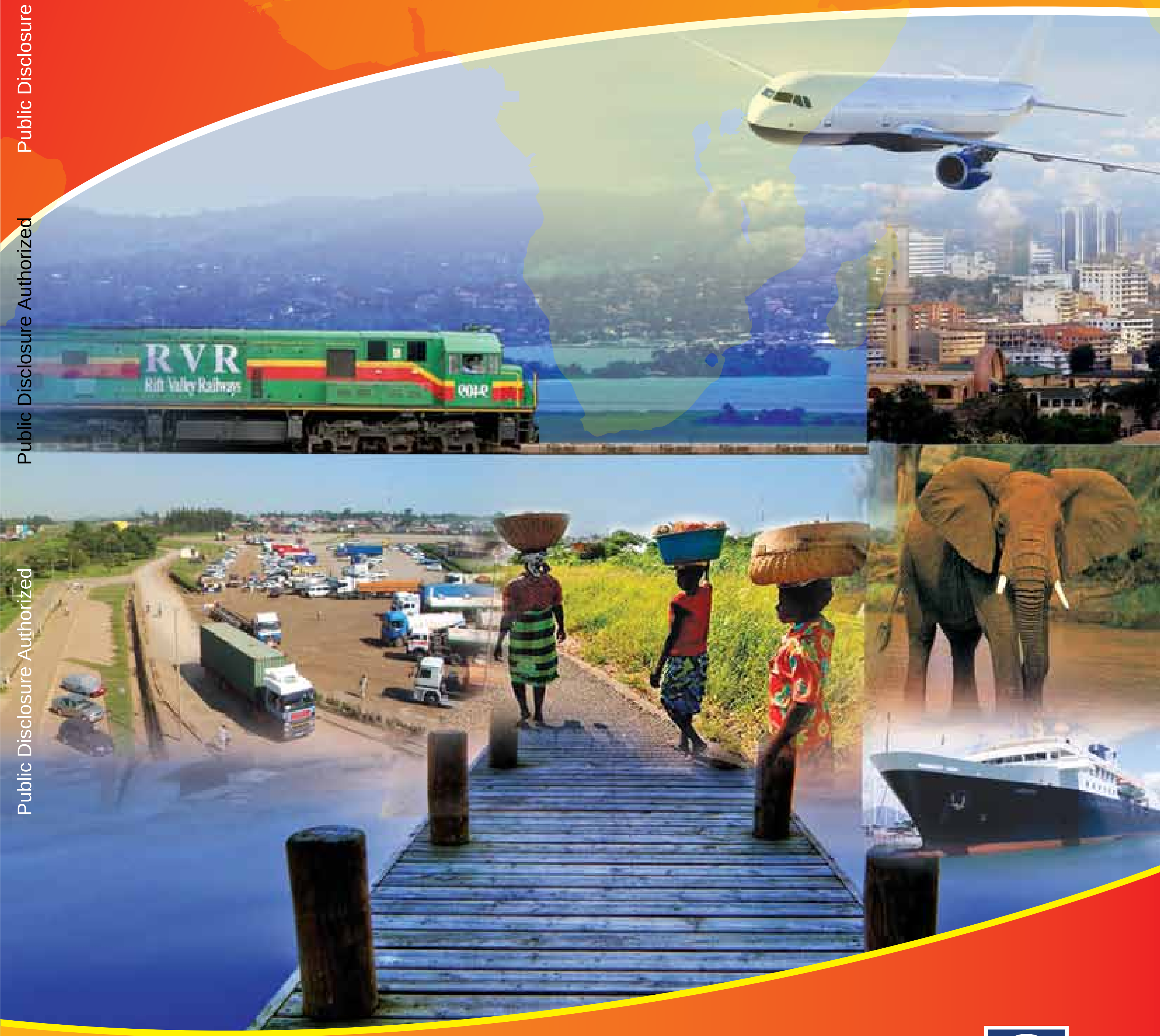
UGANDA ECONOMIC UPDATE

BRIDGES ACROSS BORDERS

Unleashing Uganda's Regional Trade Potential



February 2013 -First Edition

The World Bank

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The World Bank
1818 H Street NW
Washington DC 20433
Telephone: 202-473-1000
URL: htpp//www.worldbank.org

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Abbreviations and Acronyms

ASEAN	Association of Southeast Asian Nations
BOU	Bank of Uganda
BOP	Balance of Payments
CBR	Central Bank Rate
CET	Common External Tariff
CAGR	Compound Annual Growth Rate
COMESA	Common Market for Eastern and Southern Africa
DSA	Debt Sustainability Analysis
DRC	Democratic Republic of Congo
DTIS	Diagnostic Trade Integrated Study
EABC	East African Business Council
EAC	East Africa Community
EAPSP	East African Professional Services Platform
EU	European Union
FDI	Foreign Direct Investment
FTA	Free Trade Area
GDP	Gross Domestic Product
HIPC	Highly Indebted Poor Countries Initiative
ICT	Information and Communications Technology
IFC	International Finance Corporation
IMF	International Monetary Fund
ITC	International Trade Centre
IUCEA	Inter University Council of East Africa
LIBOR	London Interbank Offered Rate
MDRI	Multilateral Debt Relief Initiative
MFPED	Ministry of Finance, Planning and Economic Development
MTTI	Ministry of Trade and Tourism
NDP	National Development Plan
NEER	Nominal Effective Exchange Rate
NTBs	Non-Tariff Barriers
NTMs	Nontariff Measures
ODA	Official Development Assistance
RCA	Revealed Comparative Advantage
REER	Real Effective Exchange Rate
SMEs	Small and Medium Enterprises
SSA	Sub-Saharan Africa
UEU	Uganda Economic Update
URA	Uganda Revenue Authority
USAID	United States Agency for International Development
VAT	Value Added Tax
WB	World Bank
WDI	World Development Indicators
WITS	World Integrated Trade Solution
WTO	World Trade Organization

Foreword

Uganda is a reform-inclined country with a remarkable track record. More recently, the country has foundered, but shows steps towards refocusing on accelerated and sustained growth. Its ambitious target is to become a middle income country in a decade. For this to happen, however, Uganda will have to exceed its 7% growth rate of the 1990s and the early 2000s, and hit a high of 10% sustained over a period of time.

To get to this, Uganda will need the kind of resilience that has been absent in the last few years when growth rates have fallen. The keys to building resilience lie in diversifying the economic base and in appropriate use of resources, which Uganda can achieve by transforming its production and marketing value chain processes.

This is not a far-off goal for Uganda. The exploitation of oil resources is an opportunity that could transform the country through smart use of oil revenues in the non-oil sectors, and hence spur rapid and sustained growth.

Beyond national resources, Malaysia, Singapore and South Korea offer good examples of how the interplay between local productivity and external markets can lead to socio-economic transformation. The tenacity, speed, strength and determination with which these three countries pursued outward-oriented growth strategies – allowing for trade with their neighbors, yielded growth and jobs for their populations, hence their being branded "the Asian Tigers".

In similar fashion, Uganda can become the economic "Lion of Africa" if it harnesses the potential that regional trade offers. This will however only be possible if Uganda's neighbors agree to work together as a village community; open up for each other, and devise policies that enhance rather than frustrate free movements of goods, services, and people. It will take the entire region working together to realize the potential that each individual nation has. Through regional trade, Uganda can remove the obstacle of being landlocked and become integrated into a land-linked economy.

Higher productivity and better access to markets will underpin growth in regional trade. The two most critical entry points to achieve this are developing better infrastructure that will ease transportation and lower the cost of doing business, and overcoming non-tariff barriers to trade. Uganda's ambition to become a regional economic giant is therefore not far-fetched. Adopting the right policies and investments, as well as a refocusing on growth will lead to transformation. Middle income status is achievable, but it will require Uganda to work twice as hard and fast not to miss the window of opportunity.

Philippe Dongier
Country Director
Tanzania, Uganda and Burundi

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Key Messages

Despite having one of the world's highest rates of population growth, Uganda has an impressive record of economic growth and poverty reduction. Over a period of approximately 20 years, from the 1990s until around 2010, the average annual rate of economic growth stood at around 7 percent. During this same period, the proportion of the population living below the poverty line declined from 56 percent in 1992 to 24 percent in FY10.

In sub-Saharan Africa, Uganda was a pioneer of liberalization and pro-market policies in the 1980s. This established the foundation for the country's remarkable economic performance in the 1990s and the 2000s. During this period, the country diversified its exports, mainly through fisheries and tourism, with high levels of private investment. Exports of agricultural commodities (particularly innovative crops such as flowers, tobacco and maize, on top of the traditional exports of coffee, tea and cotton) grew by 16 percent per annum during most of the 2000s. Private investment, which increased to an average of 18 percent of GDP at the end of the century from 11 percent in the 1990s, was mostly driven by construction.

To harness the potential of regional trade, Uganda needs to adopt a multi-pronged approach to raise productivity and to get the products to markets. In this regard, interventions that create incentives for farmers, firms and services providers are vital measures to raise productivity.

However, in recent years, the rate of growth has slowed down and has been characterized by increased volatility. From an average of 9.3 percent per annum in the period from FY01 to FY08, the rate of growth declined to 7.2 percent in FY09 and to 5.9 percent in FY10. There was a short-lived recovery in FY11, with the rate increasing to 6.7 percent, before falling again to 3.4 percent in FY12. Developments in first half of FY13 suggest that the rate of growth will remain around 4.5 percent. Uganda, which used to have the best performing economy of the nations in the East African Community, now lags behind all the others, with all the other member nations recording rates of growth of at least 4.5 percent per annum since FY12.

The global economic crisis of FY09 and its after effects have resulted in the deterioration in Uganda's terms of trade, with commodity prices declining while oil prices increased. This had a negative impact on exports and investment, leading to a decline in the rate of growth. The prolonged drought in Uganda has had a significant negative impact on the performance of the agricultural sector. This, combined with poorly directed government spending and poor financial management, has had a negative impact on the macro environment. In turn, this has resulted in a slowing down of the services and industry sectors. The slowdown in private investment and exports was followed by a weakening external current account, driven by a dramatically increased import bill. While the combined impact of efforts to achieve stabilization, good weather and receding shocks might have facilitated a recovery in FY13, uncertainties created by governance-related aid cuts and a decline in investor confidence are continuing to stifle growth. The World Bank forecasts that the rate of growth of the Ugandan economy in FY13 will be in the range of 4.3-5.0 percent, a modest increase compared to FY12 and far lower than the country's recent historical rates. From a longer perspective, vulnerabilities have also become evident over the past five years, when public investments have become the key driver of growth. Exports remain driven by the agricultural sector, which is sensitive to climate change.

If Uganda is to achieve middle income status, it must rebuild a more resilient economy. Such resilience will be achieved through a more rapid diversification of the economic base, characterized by the production of higher value products and the judicious exploitation of the country's oil resources. This has the capacity to boost the economy, including the non-oil sector, and to close current external and fiscal imbalances. Intensified regional trade will be the catalyst for a market-oriented growth strategy to accelerate this process.

To harness the potential of regional trade, Uganda needs to adopt a multi-pronged approach to raise productivity and to get the products to markets. In this regard, interventions that create incentives for farmers, firms and services providers are vital measures to raise productivity. Farmers can then produce outputs in sufficient quantities and quality. Firms can invest in higher value export products. And service providers can invest in quality enhancement to enable Uganda to tap into the regional market. Transport costs must be reduced through the development of better quality infrastructure and improved logistics, non-tariff barriers to goods trade must be addressed, and restrictions to services trade must be eliminated. Deeper regional integration is the main means to ensure the establishment and implementation of interventions that promote a high volume and quality of trade and technology transfers.

Part I: State of the Economy: Recent Economic Developments and Economic Outlook

In FY12, Uganda experienced the double blow of a high rate of inflation and a slump in growth, with inflation averaging 23.5 percent and growth declining to 3.4 percent. These two phenomena had not occurred concurrently since 1992, when the economic stabilization and reform process begun. The causes for this double whammy were the global economic turbulence that resulted in a decline in exports and investment, higher food and oil prices, together with slippages in fiscal and monetary policy originally meant to counter the global crisis effects, the implementation of which was affected by the February 2011 elections and security spending pressures.

In FY13, tight management of monetary policy, and in support prudent fiscal policy, has stabilized the economy. The economy has also benefited from a decline in food and energy prices due to external factors, from improved weather, and from the appreciation in the value of Uganda's currency. With the combined impact of these factors, inflation came down to below the 5 percent target by the end of the first half of FY13. Fiscal adjustments that reduced the deficit by more than 3 percent during FY12 also supported efforts to reduce inflation. However, both policy measures also contributed to a slower rate of economic growth.

In FY13, Uganda had high expectations for a recovery of the economy, supported by macroeconomic stability. With the restoration of stability, both increased government spending and a moderate easing of monetary conditions were expected to stimulate overall demand in the economy. At the same time, the Central Bank Rate was cut by 8 percentage points, to 12 percent as of December 2012. As a result, the level of lending to the private sector began to gradually increase during the second quarter of FY13. The FY13 budget had demonstrated the Ugandan government's intention of utilizing spending and taxation as the main instrument to stimulate aggregate demand and supply, particularly through a large investment program. Up to 29 percent of the FY13 budget was allocated to support major road works, the rehabilitation of water ferries, the first stages of a design of a standard gauge rail, and the commencement of construction of the 600MW Karuma hydro-electricity dam.

Despite these expectations, recovery has been constrained by lower than expected expenditure resulting from failure to achieve tax revenue collection targets, budget execution problems, and the recent uncertainty arising from governance scandals and corresponding aid cuts. During the first quarter of FY13, the level of tax revenue collection was 3.8 percent below target. The rate of absorption for the development budget stood at a mere 69.6 percent, compared to 94.2 percent for the recurrent budget. This has undermined the public expenditure program, even as security and public administration budgets were overrun. Key investment projects, such as the construction of the 600MW Karuma hydro-electricity dam, have also been delayed. Finally, the governance scandals involving the Office of the Prime Minister and the Ministry of Public Service during the second quarter of the year resulted into a freeze of aid estimated at US$ 300 million (4-6 percent of the national budget or 0.9 percent of GDP). This has not only impacted fiscal operations, but it has also resulted in increased economic uncertainty, with implications for planning and investment, even in the private sector.

Uganda's external transactions position improved during FY12 on account of short term portfolio inflows and increased foreign investment in oil exploration. However, the current account position deteriorated further, following the downward trend experienced in the past five years. In FY13, the balance of payments has been threatened by lower interest rates that have reduced the short-term portfolio and by the governance scandals that have resulted in aid cuts and increased uncertainties amongst investors.

Uganda's short term economic outlook remains mixed, as the economy maneuvers the uncertainties surrounding governance-related disruptions to aid and the decline in investor confidence. Maneuvering these uncertainties is vital if the country is to sustain recovery following the dip in FY12. A positive growth outlook is highly dependent on restored macroeconomic stability, characterized by lower inflationary pressures and looser monetary and fiscal policies to stimulate aggregate demand in the short term. Favorable weather will also boost agricultural output, allowing the agricultural sector to regain its importance. However, the services sector will remain the key driver of economic growth.

The World Bank forecasts that the rate of growth of the Ugandan economy in FY13 will be in the range of 4.3-5.0 percent, a modest increase compared to FY12 and far lower than the country's recent historical rates. With curtailed momentum as a result of the governance scandals and ensuing disruptions to aid, the economy is expected to recover only modestly in the second half of the FY13 financial year. Facing these problems, the Ugandan government is expected to reduce its level of expenditure, including expenditure in the key transport sector. Hence, while agricultural output is expected to improve as projected, the reduction in government spending is expected to curtail economic activity, even if aid assistance may resume later in the year, following a government commitment to corrective actions regarding the misappropriation of funds. However, if the strategies of the medium term expenditure program and efficiency reforms are sustained and if aid disbursement resumes, economic recovery may gain momentum in FY14.

As a result of the slowdown in the global economy, Uganda's external position is expected to remain weak, with increases in exports failing to offset the rapidly increasing growth in imports. Consumer imports, mainly consisting of foodstuffs such as dairy products, fruits and vegetables from Kenya and South Africa, and clothing and household items from China, Europe and USA, are increasing. The weak external current account will also continue to reflect the large gap between the country's increasing investment needs and its low level of domestic savings, which currently stands at a value equivalent to 13 percent of GDP, compared to the average level of 17 percent for sub-Saharan Africa.

In the medium term, Uganda's economic performance is expected to improve as a result of the government's pro-growth policies, which involve reforms to enhance fiscal efficiency and to generate productivity improvements in private activities. In addition, revenues derived from the production of oil will make an increasingly significant contribution. With these factors, the growth of GDP could revert to the rate of approximately 7 percent, consistent with recent historical performance. The spending geared at alleviating constraints to growth, particularly constraints related to energy supply and transport infrastructure, should, in the medium term, revive private investments, boost agriculture production, and energize the light manufacturing sector. The new oil economy will dramatically change Uganda's economic outlook through stepped-up investment in production infrastructure. In future years, when production facilities become active, actual oil revenues could double the country's current level of fiscal revenue. The experience of other countries shows that the oil development preparation phase is often characterized by a high level of foreign investments that significantly impact economic performance, at least in the regions implementing those investments. Developing institutions to ensure transparency and the prudent management of revenue will facilitate the optimal utilization of the country's oil resources.

Uganda's economic prospects could be negatively impacted by either external or internal developments or both. In the short term, poor relations with donors, and rising food and oil prices could destabilize the domestic economy and slow down growth.

However, Uganda's economic prospects could be negatively impacted by either external or internal developments or both. In the short term, external turbulence from Europe, where the Euro Zone is struggling, instability due to the Arab Spring, poor relations with donors, and rising food and oil prices could destabilize the domestic economy and slow down growth. Government expenditure remains vulnerable to implementation constraints and lack of political will to enforce discipline in the utilization of limited financial resources. The short-term prospects for increased domestic revenue remain slim, as measures to eliminate the leakages resulting from tax exemptions are still either lacking or are poorly enforced. Uganda's large public investment program continues to be funded through external financing, as collected domestic revenue, equivalent to 13 percent of GDP, is barely enough to cover the recurrent expenditures. Furthermore, corruption and related scandals may result in the diversion of public resources and the derailment of the public investment program, 50 percent of which was expected to be financed with external resources.

In this period of transition to becoming an oil producing nation, poor relations with donors could exacerbate instability. By January 2013, the cuts in aid announced by donors amounted to 4 percent of the total FY13 budget. These cuts could be managed through cuts in some non-priority expenditures. However, lack of progress in improving spending efficiency and a failure to entrench good value-for-money practices in government operations could worsen donor relations and result in further declines in investor confidence. This in turn could result in ongoing negative impacts for Uganda, whose international rankings for transparency and good governance remain poor.

In the medium term, the challenge remains for Uganda to utilize its oil resources to create economic opportunities. The manner in which oil resources are utilized will be a major factor in mapping the country's medium- and long-term development path. Oil revenues can substitute for aid, but the transition could be a source of macro risk if these revenues are not managed properly. Elsewhere in the world, the prospect of increased revenues from oil has often been associated with increased levels of corruption. If corruption continues to increase in Uganda, further reductions in aid are likely, making the transition towards a well-managed oil economy more difficult.

Uganda will require a significantly increased rate of economic growth to achieve its vision of reaching middle income status in the next 10 years. With the medium-term projection of 7 percent, which is based on a high-growth scenario, Uganda's per-capita income could reach US$ 814 by 2025. To achieve a per capita income of US$ 1000 within a decade, Uganda must achieve a rate of growth in excess of 10 percent per year. Faster diversification of the economy and appropriate use of resources, including oil, must be the engine to facilitate the renewed growth momentum required to achieve this figure. In addition to having the potential to close the current account deficit, oil can boost the capacity of the economy, particularly the non-oil sector, enabling it to grow at a more rapid rate.

Regional trade may be the catalyst to ensure rapid economic growth. To achieve this, Uganda's economy must undergo a fundamental transformation. This transformation must affect what the country produces, how it produces it, and where it finds markets for its outputs. Policies to improve the business environment, to develop human capital, and to raise the stock of infrastructure will remain the key drivers of this transformation. To overcome implementation challenges, improving the efficiency of fiscal policy, including factors that influence it, such as good governance, cannot be overlooked, particularly when the country makes the transition to becoming an oil producer. However, international experience suggests that it is hard for a small landlocked country such as Uganda to move alone along the path of economic development. Improved levels of openness and transparency can help ensure the achievement of these goals by facilitating access to new markets (demand side) and by pushing firms to become more competitive (supply side). This leads to an expansion in production, diversification and increased employment opportunities.

Part II: Harnessing the potential in regional trade to help Uganda's economy expand and diversify.

If a typical African village is used as a metaphor for the Great Lakes region, Uganda is in the position of a typical villager who can only grow by developing deeper links with neighbors and members of surrounding communities. In Uganda's case, it must develop deeper links between domestic producers and external markets. Uganda has been at the forefront of regional integration, which is a key means of facilitating intensified regional trade. It has entered into a number of regional agreements, including the EAC and COMESA. These regional agreements have yielded significant dividends, almost doubling Uganda's regional exports over five years, to 25 percent of total exports in FY11. They have enabled Uganda to diversify its export base into industrial output such as iron sheets, cement and plastics, and to progressively reduce its imports, as it is now increasingly producing inputs that it previously imported. These achievements notwithstanding, regional integration is still in its infancy, with many benefits yet to materialize. Uganda's level of trade with its regional neighbors is still sub-optimal, with trade remaining distorted by many factors, including high transport costs, non-tariff barriers, limited currency convertibility, and failure to manage the social and political impacts of the unequal distribution of benefits and costs. At the same time, the development of new regional markets remains affected by ongoing regional insecurity.

Uganda must tap the remaining underutilized opportunities within the region. Amongst other measures, this involves exploiting its position as a land bridge linking other landlocked countries to the coastal economies; diversifying the export base within the agricultural sector and out of agriculture into higher value products; and tapping the potential of services trade. To achieve this, working together with others, Uganda has to build the bridges to facilitate intensified regional trade. While this agenda involves regional cooperation, Uganda must pursue a re-energized policy action that focuses on what the country can do on its own. Uganda cannot afford to wait. This economic update proposes an action plan to achieve these goals, as follows:

(i) Beyond the East African Community: Uganda as a land bridge for the Great Lakes region

The first opportunity to exploit the dynamic regional market lies within the EAC. However, beyond that, Uganda must position itself as a land bridge to connect other nations within the Great Lakes regions with coastal nations. In the period from 2001 to 2010, the EAC was the second-fastest growing economic bloc in the world. The Community has a rapidly expanding population and rapidly expanding levels of intra-regional trade. Uganda's level of trade within the EAC has grown more rapidly than its trade with the rest of the world. However, Uganda has the potential to almost double its trading space through an expansion of trade with nearby nations in the Great Lakes region, such as South Sudan and the Democratic Republic of Congo. In such nations, Uganda's private sector has already established trading partnerships, mainly through informal means. Building on these existing trade relations, Uganda must play a stronger strategic role in coordinating and harmonizing policies relating to trade between EAC and non-EAC Great Lakes countries, especially through the development of better infrastructure and institutions to support trade.

(ii) Boosting Uganda's regional trade by moving beyond food crops

Uganda must continue to harness its agricultural potential to feed the region. However, the full benefits of regional trade will only be realized by climbing the value export ladder and by exporting services. Facilitating intensified regional trade must involve three strategic pillars, as follows:

PILLAR 1: Harnessing the agricultural sector to feed the region: Uganda has a flexible climate and fertile soils. This gives it prospective comparative advantages as a food basket zone for the EAC, principally Kenya. Agricultural exports, particularly the export of food commodities, will buttress export growth and facilitate diversification if productivity improves to meet the rising demand associated with the growth of regional economies and the urbanization of their populations. The challenge lies in ensuring farms produce outputs in sufficient quantities and of sufficiently high quality at competitive prices and are able to

Rice Growing in Butaleja District to support food exports to the region (Great Lakes Film Production Ltd), November 2012 get this produce to markets. Recent efforts to raise productivity include the special cluster-based interventions to raise production of key commodity exports, including maize and beans, by improving access to enhanced seeds, fertilizers, mechanization and water for production. These efforts will be central to supporting Uganda's competitiveness as a food surplus producer. Beyond raising productivity on the farm, improvements in storage, transport logistics, and connectivity are urgently required to link farmers to markets and to link the domestic market to the regional market.

PILLAR 2: Climbing the export value ladder by expanding Uganda's range of outputs: This will be achieved by building on what Uganda already produces and by participating in regional production chains. Moving from low to higher value exports requires building production capabilities and capacities. In the EAC, Uganda has made the fastest transition from low value primary product exports to higher value primary products, resource based manufactures, and low technology manufactures. This has expanded its opportunities to develop other products of similar and substitutable or adaptable capabilities. Uganda can also participate in regional production chains and trade in "parts" or "tasks". For instance, by exporting plastics, Uganda has built capabilities to assemble and/or manufacture toys. It could build upon these capabilities to produce car parts or higher level outputs. Beating the stiff competition from the more economically developed Kenya will remain a challenge, given that Uganda is a small landlocked country, far from the coast, and its industrial sector lags behind Kenya's, with less established businesses and a lower level of access to technologies and skills. Better connectivity and the removal of non-tariff barriers will be vital if Uganda is to leverage these trade opportunities optimally.

PILLAR 3: Promoting the export of services: Amongst other benefits, this may be one means for Uganda to overcome distance disadvantages associated with its landlocked status. Although the services sector accounts for more than 45 percent of GDP, Uganda remains a net importer of services, with exports accounting for 9 percent of GDP while imports account for 14 percent. About 55 percent of the service imports are in the transport services sector, while 56 percent of exports are in the travel and tourism sector. This situation could improve if trade constraints are removed in strategic sectors including tourism, transport, and logistics. The situation could also improve if Uganda is able to build on recent trends that have made it a growing regional hub for education and transit for goods in the Great Lakes region.

(iii) A waiting game will be a losing game: Uganda can do a lot on its own to enhance regional trade.

Harnessing the potential of regional trade will not be easy, given that many of the constraints to such trade lie beyond Uganda's borders and are beyond its control. However, Uganda cannot afford to wait for others to act. There is still much that it can do on its own initiative. To stimulate regional trade, Uganda has to implement a multipronged approach that ranges from raising productivity to getting outputs to the market at a competitive price. Action must focus on the following three priorities:

To reduce transport costs, more efficient modes of transport will need to be developed and to become operational. Uganda has made commendable progress towards improving roads in the trade corridors. These efforts must be sustained and complemented through government-led initiatives to work with neighbors to maintain these roads and to improve ports. In the short-to-medium term, rail and water transportation systems must be made more viable through the rehabilitation of existing lines. The EAC has already committed to the installation of a standard railway gauge network. This is an important measure towards facilitating regional connectivity both within and beyond the EAC, encompassing nations including Ethiopia, Somalia, Zambia and Malawi. Improving lake transport will also improve the efficiency of railway transport, reducing distances and easing connections, compared to use of rail-road intermodal transport.

Improvements in physical infrastructure must be accompanied by improvements in logistics services. There is evidence that reductions in transport costs are driven by improving both infrastructure and transport logistics, including improvements to the trucking, freight, and storage industries. Heavy taxation and high operational costs exacerbate distance disadvantages, with Uganda still being required to import transit services, as the regional fleet is dominated by Kenya and Tanzania. Introduction of a regional customs bond will reduce constraints on forwarding businesses, especially the small freight forwarders, who form the bulk such operators. Breaking down "cartel" practices in the trucking business to improve trade competitiveness will require renegotiating road-user fees with EAC partners; accelerating improvements in key strategic border operations, including those connecting Uganda to South Sudan, DRC, and Congo; and increasing the capacity of bonded storage facilities.

A solution must be found to the problem of non-tariff barriers. The ineffectiveness of past efforts to eliminate NTBs cannot be an excuse for inaction. Efforts to intensify trade are self-defeating unless they are accompanied by efforts to reduce or eliminate non-tariff barriers (NTBs). Such NTBs are currently mainly manifested through rules and regulations. Although these rules and regulations are sometimes legitimate, they are often inappropriately implemented. Common NTBs include standards regulations and weigh bridges. In addition to creating delays for traders, NTBs also result in increased cost through the imposition of illegal fees and charges. NTBs raise the prices of traded goods in the same manner that tariffs would. Uganda and Kenya's NTBs have the most significant negative impact on regional trade. Building on previous efforts to raise awareness and improve transparency in the management of the NTBs, Uganda must enter into bilateral negotiations with strategic partners to harmonize trade policies. A strong commitment to remove its numerous trade-related rules and regulations would assist in negotiations with partner states to remove theirs. Regionally, the introduction of a mutual recognition of conformity-assessment procedures and a sanctions system of the sort implemented by other regional blocs, such as ASEAN and the EU, would help. Such measures must be accompanied by the introduction, through the EAC framework, of regional sanctions, as well as strengthened sanitary and phyto-sanitary testing and verification capabilities. In addition, efforts must be made towards mutual recognition of conformity assessment procedures.

To unleash the potential of the service exports, a number of restrictions must be eliminated. Uganda needs to prioritize specific sector interventions in the area of tourism, education and professional services, and transportation and logistics services for the greater hinterland. In the tourism sector, for instance, in addition to improving human resources, the public sector can play an important role by developing the appropriate infrastructure to reduce the cost of access to tourist centers and potential tourist attractions. In the business and professional services sector, more flexible immigration regulations are crucial to ensuring the mobility of service providers. The challenge is to develop and implement an adequate regulatory framework to support existing engagements in education, regulation, trade policy, and labor mobility.

To conclude, while developing other factors of growth, Uganda needs to sustain its efforts to deepen regional integration as a means of facilitating greater trade opportunities, but primary agenda remains it its own hands. The first point of action is to address constraints to productivity growth in sectors that have the highest potential for regional expansion, including the agriculture, manufacturing and services sectors. Uganda must 'advocate by setting an example' by removing its own NTBs as a means of encouraging neighboring countries to address theirs. However, it also needs to use its position to persuade the coastal countries to do their part, since they will also benefit from such programs. In addition, Uganda must seize every opportunity to promote peace and tranquility in the Great Lakes regions. Without peace, there can be no trade.

Deeper regional integration will facilitate the development of regional public goods such as roads and railways; reduce transaction costs and create economies of scale; provide a regulatory environment in which goods and services can flow freely; and support cross-border production networks. It will also reduce the constraints faced by many local firms in accessing the essential services and skills that are needed to boost productivity and further diversify into higher value-added production and trade. Implementing this regional agenda will not be easy. However, as a landlocked country, Uganda cannot afford to forget her neighbors. Therefore, the country must choose its strategic positioning carefully.

A solution must be found to the problem of non-tariff barriers. The ineffectiveness of past efforts to eliminate NTBs cannot be an excuse for inaction. Efforts to intensify trade are self-defeating unless they are accompanied by efforts to reduce or eliminate non-tariff barriers (NTBs). Such NTBs are currently mainly manifested through rules and regulations

Kampala is the barometer of the economy (Great Lakes Film Production Ltd), November 2012

Part 1:
State of The Economy

- Uganda's economy came under test during FY12, as growth slowed down to 3.4 percent, inflation rose to a peak of 30 percent, and both the interest rates and local currency moved up and down against a weak external balance.
- A decisive tight monetary policy and supportive fiscal restraint may have contributed to slower growth, but it gradually restored stability. This was helped by declining food and energy prices.
- In FY13, Uganda had high expectations for a recovery of the economy. Following the restoration of stability, the subsequent increase in government spending and a moderate easing of monetary conditions, were expected to stimulate the economy, while agriculture recovered under good weather.
- The short term economic outlook is mixed given the lower-than-expected fiscal spending and economic uncertainties emerging from governance scandals and corresponding aid cuts, amidst a weak external position. GDP growth may recover only modestly to 4.3 – 5.0 percent in FY13.
- In the medium term, economic performance can improve if Government's pro-growth policies realize efficiency and productivity improvements, and oil resources create economic opportunities. The main downside risks are a worsening global economy, regional insecurity, and poor fiscal management
- Uganda needs a renewed growth momentum to achieve its vision of reaching middle income status in 10 years. To achieve this, it must grow above 10 percent per annum, much higher than the impressive historical rates of 7 percent per annum.
- Regional trade can be the catalyst to spur rapid economic growth by facilitating access to new markets and pushing firms to become more productive. This leads to expansion in production, diversification and increased jobs.

1. Recent Economic Developments

Uganda's two decade record of prudent macroeconomic management and growth has recently faced significant tests. In the 2012 financial year, the rate of economic growth declined to almost 3 percent, while inflation rose to unprecedented levels. This decline was largely the result of a turbulent global economy and domestic shocks. Government's corrective fiscal and monetary stance helped to restore stability and confidence in the first few months of 2012. As a result, growth had been anticipated to recover strongly in the 2013 financial year. However, a new wave of shocks, related to corruption scandals and related aid cuts, is testing the economic momentum, which was already constrained by the slower rate of private investment and a decline in exports over the past five years.

Kampala city has been the engine of growth, (Great Lakes Film Production Ltd), November 2012

For a period of approximately 20 years, from the 1990s and into the 2000s, Uganda recorded an outstanding economic performance. During this period, up until 2010, the annual rate of economic growth averaged 7 percent. Despite an extremely high rate of population growth, per capita GDP growth accelerated from 3.4 percent in the 1990s to 4 percent in the period from 2000 to 2008. Similarly, the proportion of the population living below the poverty line declined from 56 percent in 1992 to 24 percent in FY10.

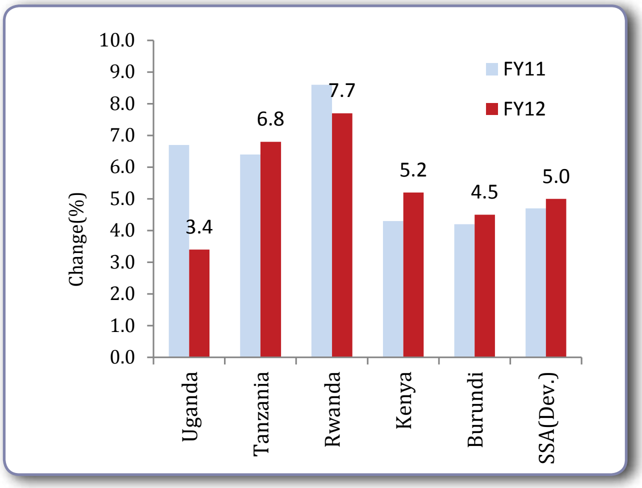
Sound macroeconomic policies accounted for Uganda's remarkable economic performance. In the 1980s, Uganda was one of the first countries in sub-Saharan Africa to implement trade liberalization and multi-sector pro-market policies. For two decades, the Ugandan government managed its fiscal and monetary policy well, while a more liberal market encouraged private local and foreign entrepreneurs to invest in the economy. The main engines of growth were exports, particularly in the fisheries and tourism sectors, and private investment. New agricultural commodities, such as flowers and maize, rather than the traditional export commodities, coffee, tea and cotton, supported a 16 percent per annum growth in exports throughout most of the 2000s. Private investment increased to an average value equal to 18 percent of GDP in the 2000s, up from 11 percent in the 1990s, with most of this investment in the construction sector.

1.1 A Dip in Growth: Global Turbulence and Other Factors

In recent years, Uganda's economy has experienced a decline in its rate of growth. The main cause for this decline has been a fall in average prices of the country's commodity exports, higher fuel prices, bad weather, and other negative effects associated with the global economic crisis. From an average rate of growth in GDP of 9.3 percent in the period from 2001 to 2008, the rate declined to 7.2 percent in FY09 and to 5.9 percent in FY10. Several factors explain this decline in growth, with these factors including the impact of the global economic crisis of 2009 and deterioration in the terms of trade as commodity prices declined while oil prices increased, which had an adverse impact on the growth of exports and investment. Domestically, the prolonged drought had a significant negative impact on the agricultural sector. Following this, fiscal and monetary slippages disrupted the macro environment which in turn resulted in a slowing down of the services and industry sectors. The declining growth of private investment and exports was followed by a weakening external current account, driven by a dramatically increased import bill.

Uganda experienced a short lived economic recovery in the 2011 financial year. Following the global turbulence and domestic shocks, including a high rate of inflation, the country experienced further declines in FY12. While the rate of growth recovered to 6.7 percent in FY11, it again declined to 3.4 percent in FY12.

Figure 1: Uganda's FY12 Growth Lowest in the Region

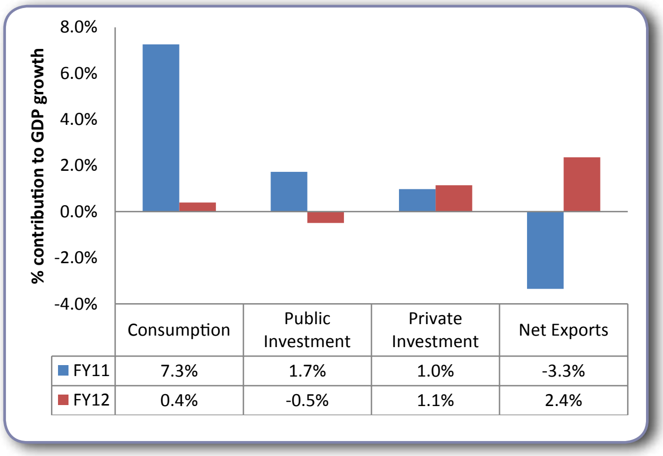


Source: Uganda Bureau of Statistics, WDI & Global Economic Prospects June 2012

This is a low rate of growth compared to other East African Community countries (EAC), all of which recorded rates at least 4.5 percent in the same period. The average growth rate in the sub-Saharan African (SSA) region in the 2012 financial year stood at 5 percent (see Figure 1). Uganda's rate of growth in 2012 was also the lowest rate recorded since 2000, and approximately 3 percent less than the average for the past decade.

The dramatic fall in the growth rate during FY12 was the result of a combination of external and domestic factors. The global crisis resulted in a decline in the demand for Uganda's exports, while rapidly increasing oil prices in the world market affected production and transport costs. As a result, the contribution of net exports to GDP growth remained negative in 2011 and 2012. This compares to the pre-global crisis period, when the trade sector contributed positively to growth every year (average of 0.1 percentage points of GDP).

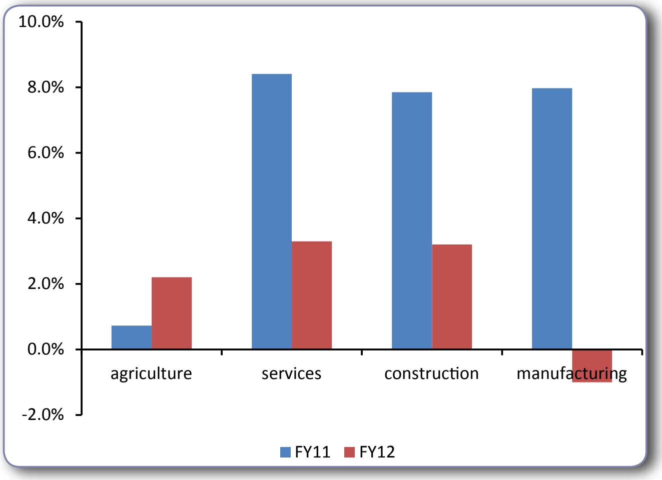
Figure 2: Squeeze in Domestic Demand as Investments Decline and Consumption Shrinks



Source: Uganda Bureau of Statistics, 2012

The decline in the rate of growth of GDP was also the result of corrective measures to fiscal and monetary policies. After several years of expansion, the government had to adjust its budget policies, leading to a severe reduction in public spending, particularly capital expenditures, in FY12. This situation was exacerbated by a slowdown in private investment and declines in consumption, resulting from higher interest rates due to tighter monetary conditions and increasing uncertainty in business environment (see Figure 2).

Figure 3: Agriculture Growth Improved While Other Sectors Decelerated



At the sectoral level, the overall weak economic growth recorded in FY12 is explained by the deceleration of the services and construction sectors, which together account for approximately 42 percent of all Uganda's goods and services. These previously booming sectors lost about 5-6 percentage points each. Financial and trade services decelerated due to increasing uncertainty in the business environment and tighter liquidity conditions that led to higher interest rates and more prudent behavior by commercial banks. Construction, including the residential houses sub-sector, grew by only 3.2 percent, which was a less than half of the growth rate reported in FY11 (7.8 percent), with the decline partially the result of the cuts in public investment.

Manufacturing faced triple jeopardy during FY12, being affected by power shortages and higher electricity prices, financing constraints resulting from tighter liquidity, and lower demand from global markets. The sector declined by 1 percent. Electricity load-shedding affected the manufacturing sector, with water levels for hydroelectricity generation remaining low due to near-drought conditions; expensive thermal generators being switched off due to insufficient funding; and construction of the Bujagali hydropower dam being delayed by almost a year.[1] At the same time, a tariff revision was required to improve the financial and operational viability of the electricity sector, pushing up businesses' operational costs[2]. Concurrently, credit became more expensive, with commercial banks tightening credit conditions.

1 By the time the first 50 megawatts unit of Bujagali, previously expected to have come on board in May 2011, was switched on in April 2012, load-shedding had reached an average of 12 -18 hours a day.

2 The industrial sector had enjoyed a subsidy of over 60 percent of the total cost of energy; a tariff increase of 68 percent for large industries and 38 percent for medium pushed up operation costs.

By contrast, the agricultural sector recorded higher rates of growth. In FY12, this sector recorded a growth rate of 2.2 percent, compared to 0.7 percent in FY11 (see Figure 3). This was principally the result of improved climatic conditions, following two years of severe droughts. Within the agricultural sector, the rate of growth of cash crops, which had declined by 6.5 percent in FY11, recovered significantly, recording a rate of growth of 16.5 percent. The level of agricultural exports, including maize, beans, and flowers, increased significantly during the first half of FY12, largely due to higher international prices and increased volume of trade. However, the rate of growth of the agricultural sector as a whole was barely above the population growth rate and insufficient to compensate for the poor performance of the services and manufacturing sectors in terms of the overall rate of growth in the GDP.

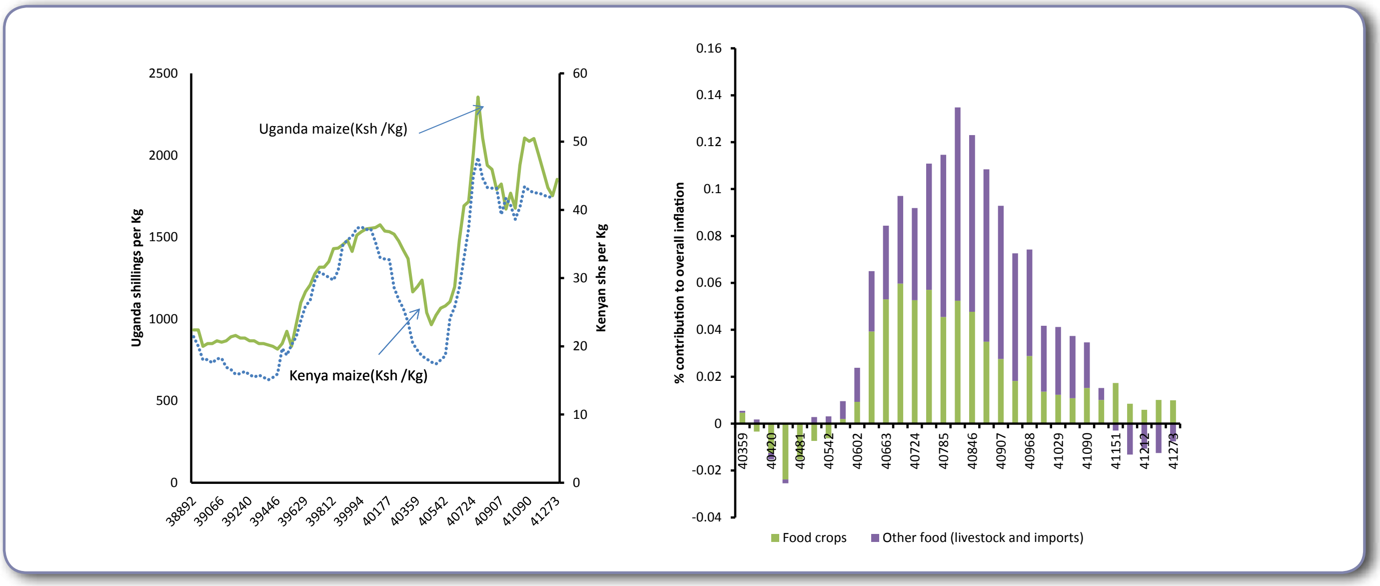
During the first half of FY13, the economy began to show signs of recovery and stabilization. Due to the fiscal and monetary adjustments implemented in the second part of FY12, the stabilization of the main key economic financial indicators, including the inflation and exchange rates, contributed to a restoration of confidence amongst most operators. Improvements in energy supply also had a positive impact on activities within the transportation and manufacturing sectors. Within the construction and manufacturing sectors, improved supply conditions were also evident, with the deceleration of producer prices and construction price indices during the first quarter. With a quarterly rate of growth of 1.8 percent during the first quarter of the year, quarterly GDP estimates had showed that overall economic growth could rebound strongly, to above 5 percent in FY13.

1.2 Tight Money Policy Restrained Soaring Inflation

During FY12, Uganda experienced its highest rate of inflation since the early 1990s, with the rate peaking at 30.8 percent in October 2011. Although this rate declined to 18 percent in June 2012, the average rate of 23.5 percent for the year was almost four times higher than recorded in FY11. Uganda recorded the highest inflation in the region: in Kenya, inflation peaked at 18 percent, but subsequently declined to 8.7 percent. In Tanzania and Burundi, inflation peaked at 19.8 percent and 25 percent respectively before declining to around 15 percent in both countries. Rwanda enjoyed the lowest rate of inflation within the EAC, with an average rate of 5.7 percent for 2012.

Higher food and energy prices were the initial main causes behind the inflation surge. Food prices rose because of higher demand from South Sudan and Kenya, while domestic harvests were reduced due to bad weather. As a result, prices of food crops, with a weight of 13.5 percent in the Consumer Price Index (CPI), increased by an average of 33 percent in the first part of FY12. Local food prices were also affected by regional factors as they followed closely regional patterns, in particular in Kenya. The subsequent decline in food prices, as the result of improved weather conditions, has been a major factor behind the gradual deceleration of inflation since November 2011 (see Figure 4).

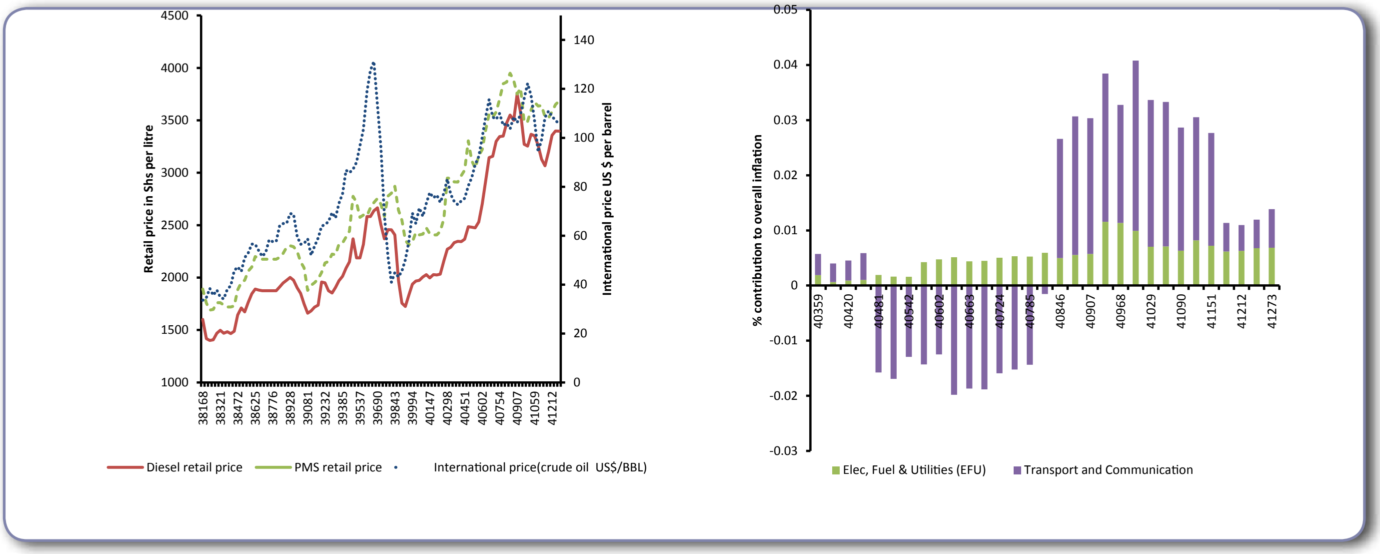
Figure 4: Uganda's Maize Price Tracks Developments in Kenya, While Contribution of Imported Food Inflation Became Important



Source: Uganda Bureau of Statistics, 2012

As usual, increases in fuel and transportation costs were the major drivers of inflation in 2012 (see Figure 5). High international oil prices were transmitted to local markets, resulting in an increase in domestic pump prices by 15 percent for petroleum motor spirit (PMS or petrol); by 26 percent for automotive gasoline diesel (AGO); and by 27 percent for kerosene (paraffin). Exchange rate fluctuations, supply bottlenecks and inefficiencies in the petroleum industry contributed to volatility in petroleum prices. [3]

Figure 5: Rapid Increase in Fuel Prices Driven by International Prices, Fed into Transport Prices



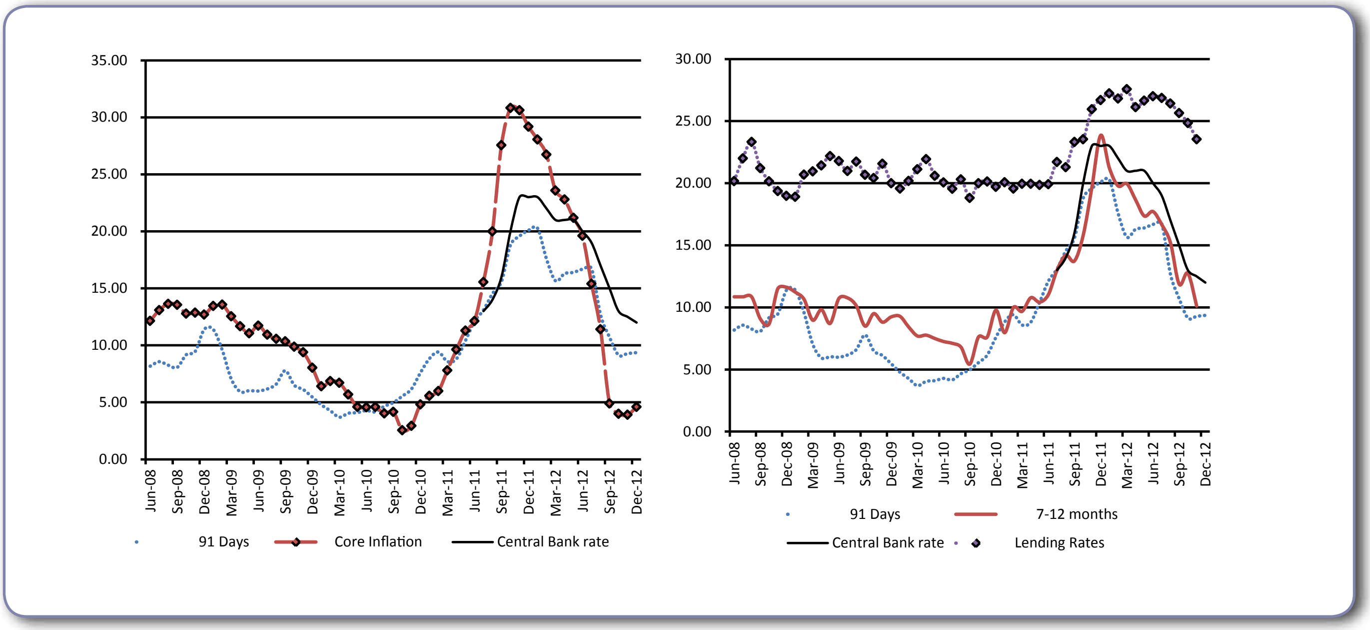
3 World Bank 2010, Petroleum Markets in Sub-Saharan Africa, Extractive Industries for Development Series No. 15, March 2010

Source: Uganda Bureau of Statistics, 2012

Other factors also influenced inflation during FY12, including local currency fluctuations and an increase in the volume of money in circulation. By September 2011, the depreciation in the value of the shilling over a one-year period reached 25 percent[4], resulting in an increased cost of imports. Concurrently, the growth in money supply reached a peak of 30 percent in July 2011, fueled by the rapid expansion of credit to the private sector, which grew at a rate in excess of 40 percent during the first quarter of the year. At this point, the Bank of Uganda adopted a tighter monetary policy, raising the Central Bank Rate (CBR). This new policy rapidly resulted in higher Treasury Bill rates and lending rates (see Figure 8).[5] The average lending rate increased from 19.9 percent in June 2011 to a peak of 27.8 percent in March 2012 before declining in the last quarter of FY12, when the tight monetary policy began to ease. The higher lending rates translated into credit expansion with a lag, with the rate of expansion declining to a mere 16 percent for the year ending in June 2012.

Inflation continued to decline through the first half of FY13, driven by lower food and oil prices and tight monetary conditions. Both core and headline inflation fell to below the target rate of 5 percent by the end of the first half of FY13. This decline in inflation gave the Central Bank confidence to gradually reduce its policy rate (CBR) to 12.0 percent by December 2012. This recent move has allowed a gradual easing of liquidity conditions, with an ensuing increase in the level of commercial banks' lending to the private sector, starting in August 2012.

Figure 6: The New Policy Rate May Have Signaled Continuous Tightening Stance Started in September 2010, but Raised Responsiveness of Commercial Banks Rates



Source: Uganda Bureau of Statistics, 2012

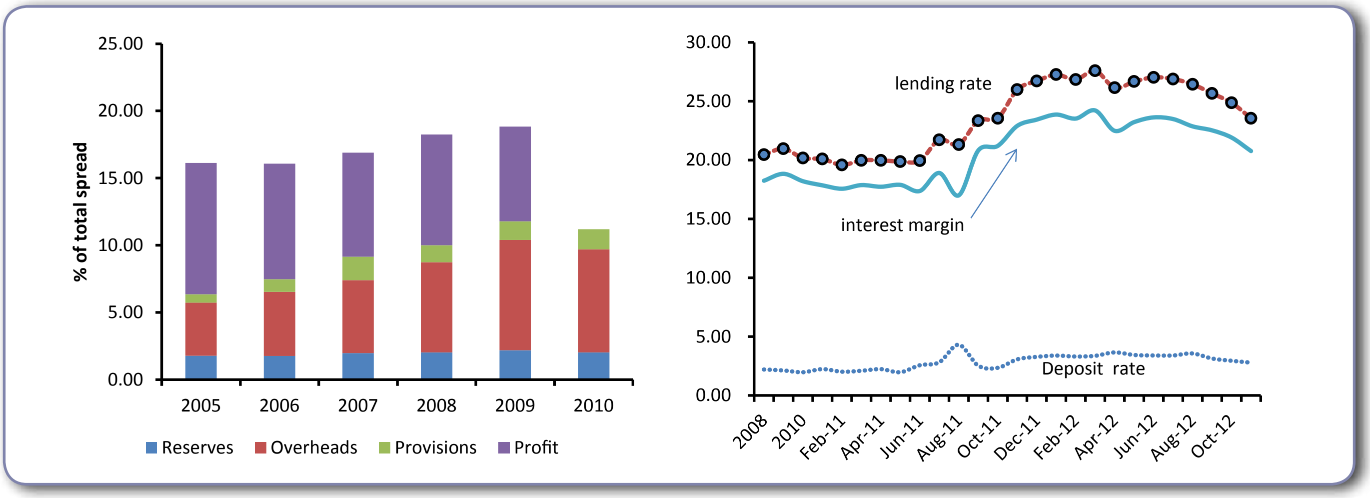
Predictably, the tight monetary policy stance contributed to a slowdown in growth during FY12, as the cost of borrowing from banks increased. Higher interest rates reduced the growth of private sector credit to 11 percent per annum during FY12, down from 44 percent in FY11, which had a negative impact on growth and the level of private investment. The decline in credit mainly impacted shilling denominated loans, which have continued to decline even further during FY13. By contrast, forex denominated loans have expanded at a steady rate since November 2012.

The negative impact of tighter monetary policy on economic growth has been exacerbated by existing structural deficiencies in the local financial system. Commercial banks continue to report high overhead costs and excessive spreads between borrowing and lending rates (see Figure 7). These deficiencies exacerbate the limited access to affordable credit for many enterprises.

4 Historically there is strong pass-through of exchange rate movements into domestic prices – for everyone percentage point depreciation of the Uganda shilling, the largest impact on prices comes in the third month after the shocks. The effects then gradually die off over about six months.

5 The correlation between BOU's policy rates and lending rates is 60 percent for Treasury Bills, 80 percent for the Bank and Rediscount Rates, and 90 percent for the CBR. ;

Figure 7: With Overheads Still Pushing Margins, Interest Spreads are Yet to Genuinely Come Down



Source: BOU and WB staff calculations

Increased transparency and innovation would improve the development of inclusive finance and reduce overhead costs. Regulatory authorities should closely monitor banks' practices and, if necessary, take punitive action to correct them. In addition, the implementation of regulatory reforms in the area of land and movable assets and the registration of companies, together with measures to streamline systems for the resolution of commercial disputes and to strengthen the court system, will improve the lending environment. In addition, authorities should devise a framework that supports the full disclosure of the cost of borrowing, improve interconnectivity of bank platforms, reform laws on sharing of customer information, and develop consumer protection laws. Finally, broader access to financial services should be encouraged through the promotion of the microfinance industry and through the development of new products that facilitate increased access, such as mobile money. While access to traditional financial services has been limited to 28 percent of the population, most of whom reside in urban areas; services such as mobile money reach demographic groups that would be unlikely to be covered by traditional banking services in the near future. By July 2011, approximately 2.4 million customers were registered for mobile money services, with up to 5 million more being expected to register in the near future. Beyond BOU's monitoring, appropriate regulation, including regulations covering non-bank correspondent networks, would support this sector's expansion.

1.3 Fiscal Adjustments to Restore Confidence

In FY10 and FY11, the government's level of expenditure increased substantially, leading to an increasing financing gap. Increased expenditures were first justified as a measure to mitigate the impact of the global financial crisis through countercyclical spending. Later, increased expenditure was related to security measures and election-related spending pressures. Election-related spending pressures were apparent with the adoption of supplementary budgets that increased public spending from 1.5 percent to 5.5 percent of GDP in FY11, leading to substantial budget re-allocation and raising questions about the credibility and sustainability of the budget.

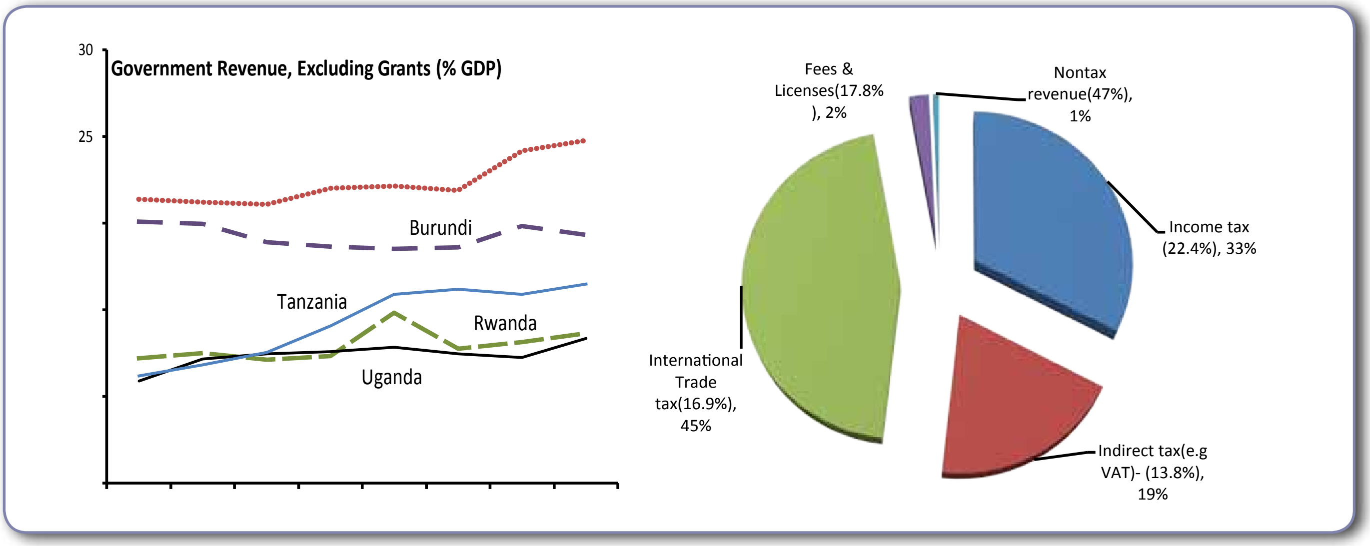
The overall fiscal deficit jumped from 4.9 percent of GDP in FY10 to 7.2 percent in FY11. While domestic revenues increased by a modest one percentage point to 13.3 percent of GDP in FY11, overall expenditure increased by 3.2 percentage points to a total value equal to 22.8 percent of GDP.6 The financial gap was closed through increased domestic borrowing, which rose from value equal to 2.1 percent of GDP to 5.9 percent, as the government drew down the Central Bank accounts. By contrast, the value of external financing (excluding grants) declined from a value equal to 2.2 percent of GDP to 1.4 percent.

6 This increase was 1.6 percentage points of GDP above the budget originally approved by Parliament, and was used for security and election-related expenditures and for subsidies directed to thermal power generation.

In FY12, the high rate of inflation and the growing imbalances in government operations were addressed through corrective fiscal measures. The government cut its fiscal deficit to a value equal to 3.9 percent of GDP by decreasing spending on exceptional security measures and power sector subsidies, which together were the main contributors to the unprecedented increase in the FY11 deficit. Such an adjustment was achieved even though development expenditures increased compared to FY12, largely as a result of the expenditure on preparations for the development of the Karuma hydro power project and a range of new road projects.

Unfortunately, increasing government expenditure was not accompanied by increased tax revenues, the level of which remains the lowest in the EAC. The composition of the collected tax revenues was characterised by a shift towards domestic indirect taxes, with the share of such taxes constituting 21 percent of total tax revenues, up from 19 percent in the previous year. However, trade taxes still constituted 45 percent of total tax revenues, a proportion unchanged from the previous year (see Figure 8).

Figure 8: : Uganda's Revenue Effort Continues to Lag, While Bulk of Revenues is from International Trade

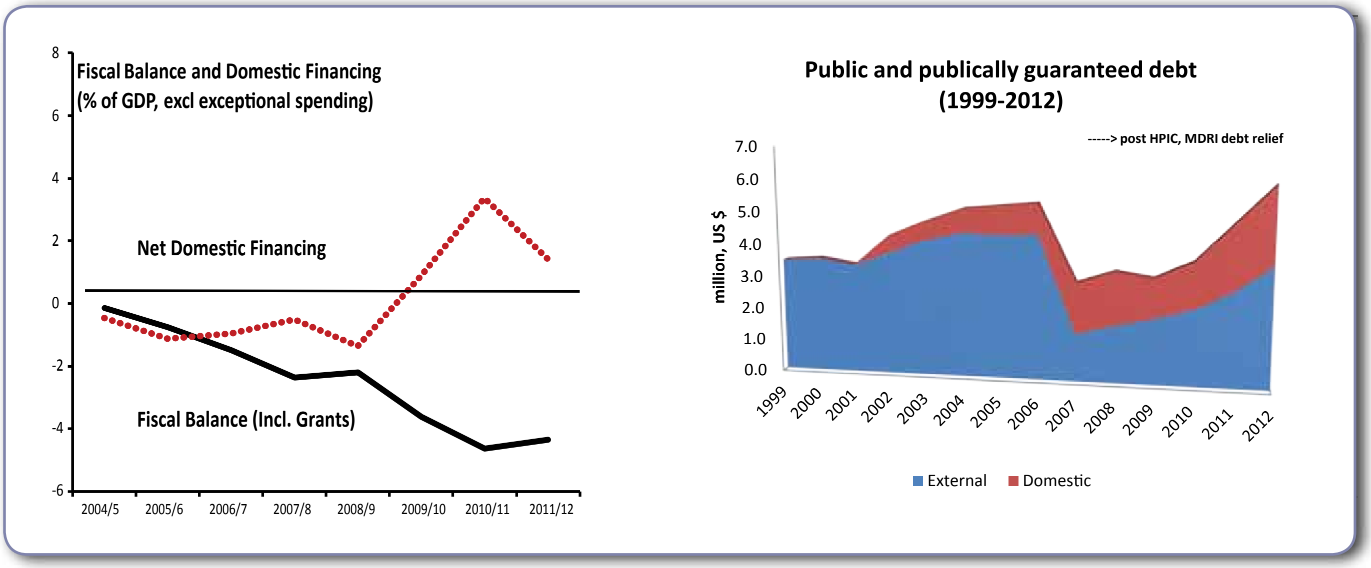


Source: Ministry of Finance Planning and Economic Development, WDI and World Bank staff calculations

In FY12, the government used external financing rather than domestic financing to close the fiscal gap. Compared to FY11, the share of external financing (excluding grants) almost doubled, reaching a value equal to 2.4 percent of GDP (or 73 percent of the overall deficit). Concurrently, the inflow of grants remained at a value equal to 2.3 percent of GDP, the same proportion as in FY11. By contrast, public borrowing on the domestic market declined to a value equal to 0.1 percent of GDP. This is a significant decrease compared to the level of public borrowing in FY11, when the value stood at 2.9 percent of GDP, with the decrease reflecting the restrictive monetary policy implemented by the Central Bank.

At the end of FY12, the government still reported low public debt ratios by both regional and international standards. In spite of increases in public expenditures in FY10 and FY11, debt management remained prudent, with new external borrowing mainly being used to finance infrastructure-related projects, including energy and transportation infrastructure. Such borrowing was contracted on highly concessional terms, with most loans sourced from the IDA (74 percent) and other multilaterals (12 percent). Hence, public and publically guaranteed external debt increased modestly from US$ 2.3 billion (equal to 15.3 percent of GDP) in FY10 to US$ 2.9 billion (19.5 percent of GDP) in FY11. Over the same period, domestic debt also increased, from a value equal to 9.5 percent of GDP to 13.4 percent. If total public domestic and external debt is estimated to have reached a value equal to 19.7 percent of GDP by the end of FY12, this remained far below the total for neighboring Tanzania, where the figure stood at close to 40 percent. The debt service ratio stood at 38 percent, while the external debt service to exports ratio stood at 3.2 percent. These figures are both far below thresholds of 35 percent and 25 percent respectively, indicating low levels of fiscal and debt distress.

Figure 9: A Shift from Domestic to External Borrowing



Source: Ministry of Finance Planning and Economic Development and World Bank staff calculations

In June 2012, following the achievement of fiscal stabilization, the government announced its intention to use fiscal policy as the main instrument to stimulate aggregate demand and supply. This policy move was demonstrated through the approved FY13 budget, which made allocations to increase overall expenditure, up by 0.2 percent of GDP compared to FY12, with a greater emphasis on capital expenditures. Almost one-third of the FY13 budget was allocated to support major road works, the rehabilitation of water ferries, the initial design of the standard gauge rail, and the construction of the 600MW Karuma hydro-electricity dam.

Nonetheless, by December 2012, the implementation of the FY13 budget had experienced a series of significant setbacks. During the first quarter of FY13, the value of collected tax revenue was below target by 3.8 percent, mainly on account of lower than expected revenues from taxes on international trade, which account for 45 percent of total tax revenue. The value of revenues derived from income taxes levied on small and medium taxpayers was also lower than anticipated. The implementation of the budget was characterized by low absorption rates, especially in terms of expenditure on capital development, where the rate stood at only 69.6 percent. This was largely due to significant delays in key investment projects, including delays to the construction of the 600MW Karuma hydro-electricity dam.

Booming activity like this in Kalerwe, a suburb of Kampala, will need to enter the tax bracket, (Sheila Gashishiri), May 2012

Table 1: Central Government Operations, 2008/09 - 2012/13

In percent of GDP	2009/10	2010/11	2011/12	2012/13 Budget	2012/13Proj.
Revenues and grants:	14.7	18.4	15.6	15.8	16.4
Domestic revenues	12.2	16.2	13.3	13.6	14.5
o/w Tax revenues	11.7	12.7	12.0	13.3	12.6
Grants	2.5	2.3	2.3	2.3	1.9
Total expenditure	19.6	22.8	18.6	20.0	19.9
Recurrent	12.3	15.3	11.2	10.2	10.3
o/w Wages	3.7	4.3	3.7	3.9	3.9
Interest payments	1.1	1.1	1.2	1.5	1.7
Development	6.6	7.1	6.9	9.7	9.4
Overall balance (including grants)	-4.9	-7.2	-3.8	-4.1	-4.8
Overall balance (excluding grants)	-7.3	-9.4	-6.1	-6.4	-6.7
External Financing	2.2	1.4	2.4	2.3	1.8
Domestic Financing	2.1	2.9	0.1	1.8	1.6
Errors & omissions	-0.5	0.0	-0.6	0.0	0.0
Memorandum items:					
Public debt stock	24.6	32.9	32.2	35.2	35.2
o/w External	15.3	19.5	19.7	24.0	24.0
Domestic	9.3	13.4	12.7	11.2	11.2

Source: Ministry of Finance, Planning and Economic Development, IMF, and World Bank Staff Estimates

The implementation of the approved FY13 budget has been affected by the governance scandals that erupted in the Office of the Prime Minister and Ministry of Public Service during the second quarter of the year. Not only did this result in the misallocation of public funds, it also resulted in a freeze in aid estimated to reach a value of US$300 million (equal to 4-6 percent of the FY13 budget or 0.9 percent of GDP).

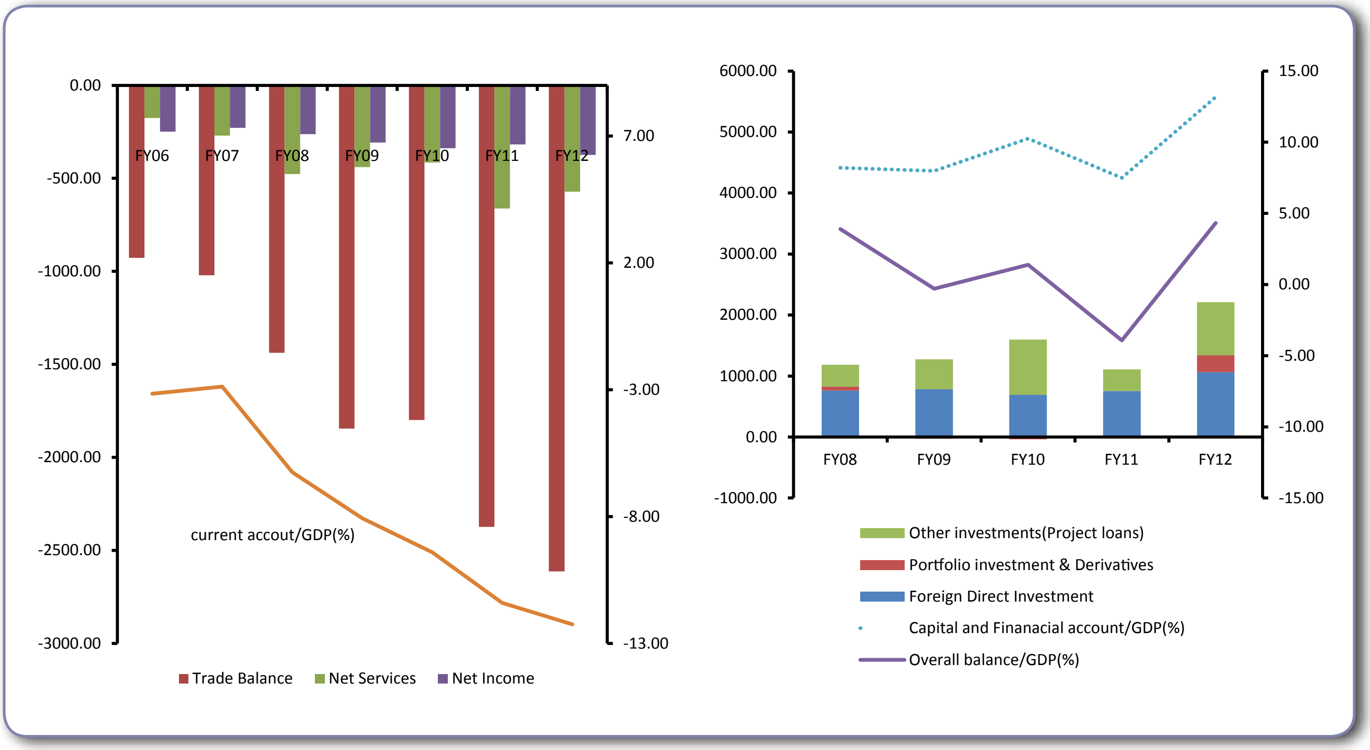
1.4 External Balance Improves, Trade Balance Deteriorates

Uganda's overall position in terms of its transactions with the rest of the world improved in FY12 on account of increased capital inflows. At the same time, the current account deficit deteriorated (see Figure 10). The meager improvement in services did not compensate for deterioration in the trade balance of goods. The volume of merchandise imports grew rapidly, largely due to higher levels of expenditure on capital goods and partly funded by increased levels of FDI in extractive industries. The volume of exports of goods rebounded from the lower levels recorded in FY11, rising by 16.5 percent as exports responded to rising commodity prices on global markets. As an example of the increasing commodity prices, the unit value of coffee rose by more than 330 percent.

Levels of FDI increased dramatically, especially in the oil exploration and tourism sectors. With these inflows, Uganda was the largest recipient of FDI among East African countries, capturing up to half of the total inflows into the region. FDI increased from US$ 719 million in FY11 to US$ 1,405 million, a value equivalent to 8.3 percent of GDP. Of the total value of FDI of US$ 1.7 billion received by East African nations by 2010, Uganda accounted for US$ 850 million. The remaining challenge for Uganda, and the other nations of the EAC, is to stimulate investment into sectors other than the natural resources sector and to generate broader linkages with the local economy.

High domestic interest rates also resulted in significant increases to short-term soft investments flows in FY12. However, these increases were temporary. Peaking in January 2012, the differential between returns on the Ugandan 91 day Treasury bill security and the LIBOR[7] rate reached 1500 basis points, compared to Kenya's security market, where the differential stood at 500 basis points. The total value of investments inflows in government securities increased to US$ 220 million in the second and third quarters of FY12, compared to a deficit position of $78 million in the same period in the previous year. However, with the gradual decline in the interest differentials between Uganda's Treasury Bill and international markets, these short-term portfolio inflows reverted to previous levels, as recently observed in FY13. It is the total value of external loans to the government that increased from US $304 million in FY11 to US$ 545 million in FY12.

Figure 10: Worsening Current Account, but Inflows on Capital Account Turned Around Overall External Position7



Source: BOU and WB staff calculations

Reflecting these movements in the country's external position, the shilling's value remained unstable throughout FY12. With the weakening of the current account during the first half of FY12, the shilling depreciated heavily against the US dollar, with the depreciation in value reaching a peak of 25 percent by September 2011. The subsequent increase in short term capital inflows helped the local currency regain its value. As a result, the nominal effective exchange rate appreciated by 4.7 percent over FY12 (see Figure 11).

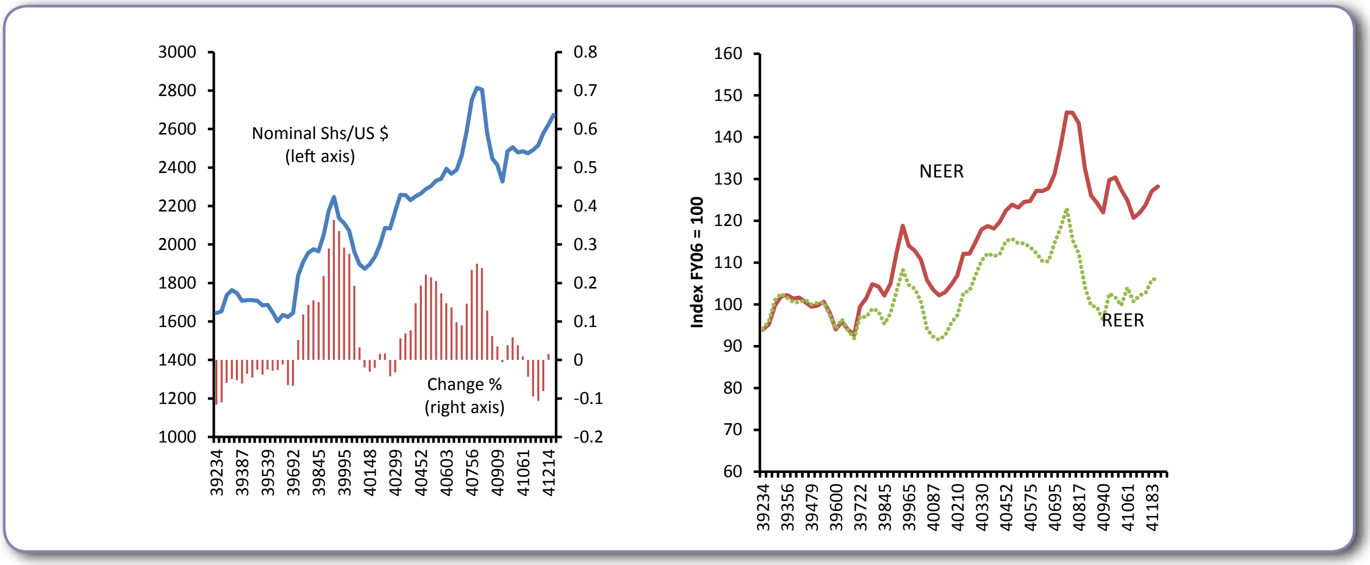
In real terms, the shilling appreciated more strongly, by 9 percent, due to a widening of inflation differentials with trading partners. It is feared that the shilling is now overvalued, eliminating any competitive advantage gains Ugandan exporters enjoyed over the last three years as the currency adjusted to the worsening current account. However, these trends are gradually reversing, with a depreciation resulting from the slowdown in short term inflows, and from the suspension of aid and the decline in confidence resulting from governance scandals.

During the first half of FY13, Uganda's overall position of transactions with the rest of the world remained weak, as short term flows slowed down and exports remain subdued. With the slight improvement in terms of trade during the first quarter,

7 LIBOR is the London Interbank Offered Rate, the rate at which banks are prepared to lend to each other at the international foreign exchange flows, and hence provides a good reference for investors considering other markets

the value of exports reached US$ 250 million per month, approximately 15 percent higher than average monthly value for exports in FY12. However, the value of imports to support investments grew at an even faster rate. As portfolio flows reversed with the declining interest rates, the overall balance of payments has remained weaker (see Table 2). The value of the shilling, which was stable through the first quarter, has also depreciated since September 2012 (see Figure 11).

Figure 11: The Shilling Recouped Value in Second Half of FY12



Source: BOU and WB staff calculations

Table 2: : Balance of Payments Position, FY10 – Quarter 1 of FY13

In millions of US $	FY10	FY11	FY12	Q1 FY13
Current account balance	-1,554.8	-1,749.0	-2,108.3	-539.5
Goods trade balance	-1,799.5	-2,373.4	-2,614.8	-521.0
Services trade balance	-536.2	-670.7	-513.5	-126.4
Income balance	-336.6	-329.3	-470.6	-193.1
Current transfers balance	1,117.6	1,624.4	1,490.7	301.1
Capital and Financial Account	1,563.7	940.6	2,404.7	597.7
Foreign Direct Investments	694.8	721.2	1,404.7	305.9
Portfolio investments	-31.3	2.1	2643.6	-66.4
Other investments	905.5	220.1	706.5	340.9
o/w Donor net disbursements	370.7	304.3	545.8	39.5
Errors & omissions	202.0	227.2	450	138.8
Foreign Exchange Reserves build-up	26	-585	741	194.2

2. Economic Outlook

Uganda's economy is expected to recover gradually in FY13 and FY14 thanks to renewed macroeconomic stability and good weather. However, the extent of recovery will depend on how the Ugandan government manages the uncertainties surrounding aid cuts and the decline in investor confidence. In the medium term, dividends from ongoing reforms; from measures to remove binding constraints to growth; and from increased investment in oil production, are expected to boost the economy, ensuring its return at least to its historical growth rates. However, risks remain. These risks include impacts from a declining or stagnant global economy, bad weather, regional insecurity, aid cuts and poor macro and fiscal management. Diversifying the economy will help to hedge those risks and to maximize the expected benefits from oil production in the longer term.

Good infrastructure, like this Masaka-Mutukula road to enable economic recovery, (Charles Kunaka) May 2011)

2.1 Growth Prospects for 2013-2014 and the Medium Term

The World Bank forecasts that the rate of growth of the Ugandan economy in FY13 will be in the range of 4.3-5.0 percent. This is a modest increase compared to FY12 and far lower than the country's recent historical rates. Contrasting developments during the first half of the year, should result in a decline in the rate of growth of GDP, at least on a temporary basis. Over the medium term, if existing uncertainties in fiscal management are resolved, Uganda's rate of economic growth should gradually increase, reverting to and perhaps even exceeding historical averages of 7-8 percent. This increased rate of growth will largely be driven by oil production and associated activities and a higher level of integration between Uganda's economy and regional and world economies.

In FY13, consistent with the pattern of the last several years, the main driver of growth will remain the service sector, contributing to approximately 8 percent of GDP. As drivers of growth, communications and finance will continue to be the most significant sub-sectors. The contribution of the tourism sub-sector will most likely also increase, although this sub-sector remains highly sensitive to security developments in the East African region. It also remained sensitive to social, health and other issues, including the impact of infectious killer diseases such as Ebola and Marburg hemorrhagic fevers. Within the industrial sector, the rate of growth of the manufacturing and construction sub-sectors are projected to recover to approximately 7 percent per annum, as financial conditions and energy provision improve. New FDI in extractive industries should boost construction activities. The rate of growth of the agricultural sector is expected to reach approximately 5 percent in FY13 as long-term weather forecasts continue to point to more favorable climatic conditions and better rainfalls than experienced in FY12.

The expected recovery in domestic economic activities has been and will continue to be driven by the renewed macro-stability, particularly a lower and less volatile rate of inflation. The gradual easing of monetary policy by the Central Bank has already led to a more rapid increase in the level of credit available to the private sector, boosting construction activities. The government has also implemented a number of measures aimed at improving the business environment, which remains one of the least conducive in the region, with Uganda being ranked 120th out of 185 countries surveyed in the World Bank's 'Doing Business' survey.8 Amongst these measures, the streamlining of business registration, the establishment of one-stop shops, and the provision of targeted assistance to SMEs should bring benefits to private investors in a relatively short time frame. As a result, private investment growth will remain robust. In spite of a deceleration from 18.9 percent of GDP in FY12 to 15.0 percent in FY13, private investment is forecast to gradually increase to 16.9 percent in FY14.

Fiscal policy remains a major source of uncertainty in the growth forecast for FY13. Initially, as described earlier, the Ugandan government had projected to stimulate aggregate demand and supply though higher overall spending and an increased emphasis on capital expenditures. The increased emphasis on capital expenditure was aimed at addressing the existing infrastructure deficits, which continue to be a major constraint to private sector development. In FY13, allocations for the development of infrastructure, particularly transportation and energy, are expected to constitute 29 percent of the budget (see Figure 12). These budget allocations have been formulated to support major road works, the rehabilitation of the water ferry system, and the initial design process for the standard gauge railway line. In addition, construction of the Karuma dam is scheduled to begin in FY13. In the same year, designs for another 600MW Ayago hydro dam will be completed and support will be provided for the development of mini hydros (125MW). The Rural Electrification Program will be expanded to improve access, with distribution losses to be addressed through the roll out of pre-paid meters. Concurrently, the authorities are placing greater emphasis on improved efficiency and effectiveness in the social sectors. Amongst the social sectors, the most significant budget allocation in the FY13 budget was for the education sector (14.9 percent), with an allocation of Shs 290 billion to raise the salaries of primary teachers and science teachers in post-O Level institutions. In addition, efficiency measures to address absenteeism continue to be implemented. In the health sector, several referral hospitals will be rehabilitated. If successful, those trends should help to improve the country's stocks of physical and human resources in the medium- to long-term.

However, capital expenditure has traditionally been constrained by the low capacity of the government to mobilize additional domestic revenues, which remain at a level equivalent to less than 13 percent of GDP, one of the lowest levels in Africa.9 In addition, the government is facing additional constraints as a result of the recent corruption-scandals-related cuts in aid inflows, currently estimated at about US$ 300 million (4 percent of FY13 budget) . In response, the authorities have prepared an action plan to strengthen the fiduciary environment, including the development of internal audit functions, to correct the misuse of the public money. The rapid and satisfactory implementation of this plan is hoped to restore confidence and to persuade donors to lift the freeze on aid. If aid continues to be suspended throughout the remainder of FY12/13, the government will need to adjust its budget targets through spending cuts and/or by accessing other sources of financing for the remainder of the financial year. The scandals underscore the need for Uganda to address her structural and other persistent weaknesses in governance, with the country ranking close to the bottom of the majority of internal transparency and government indicators over the past decade.

8 During 2012, Uganda's ranking in Doing Business improved from 123rd to 120th, on account of (i) strengthened insolvency process(i.e. rules on creation of mortgages clarified, duties of mortgagors and mortgagees established, priority rules defined, remedies for mortgagors and mortgagees provided, and powers of receivers increased), and (ii) easier processes for transferring property (i.e. title registry records digitalized, efficiency of the assessor's office increased, even though transferring property was made more difficult and time consuming with the introduction of a requirement for property purchasers to obtain an income tax certificate before registration, resulting in delays at the Uganda Revenue Authority and the Ministry of Finance)

9 Revenue targets were missed by almost 4 percent in the first quarter of FY13 as reported earlier in the update.

Box 1: Summary Assumptions for the Medium Term Outlook

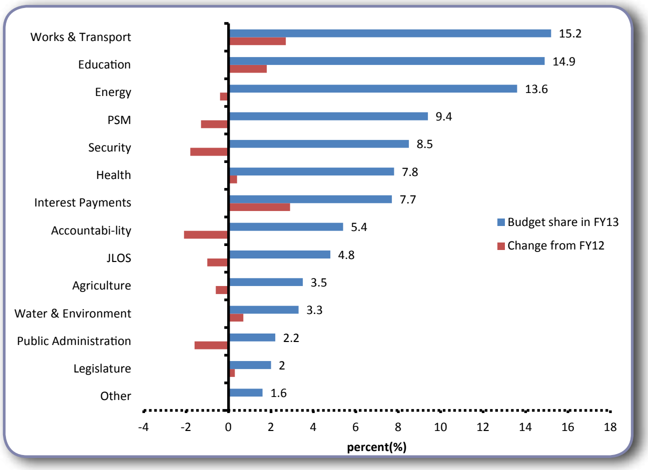
(i) Despite recent upward pressure on food prices caused by increasing international prices of food and oil and by depreciation is in the exchange rate, the inflation rate is projected to remain below 7 percent in FY13 and in FY14-15, thanks mainly to improved liquidity management and the limited financing of government activities by the Central Bank.
(ii) Fiscal policy will continue to be prudent and supportive of economic growth and poverty reduction, with improving government revenue and gradually declining public expenditure;
(iii) After a slight deterioration in FY13, mostly due to the rise in imports needed for infrastructure investments, the trade balance will improve in FY14 and beyond, reflecting the impact on exports of efforts announced by the government to raise productivity in the agriculture sector. Import growth will gradually decline from 8.4 percent reached in FY12 to an average of 4.8 percent for FY13-15; and
(v) The current account deficit will remain weak above 11.0 percent of GDP on average in FY13-15, compared to historical level of 9.6 percent in FY10;

Box Table 1.1: The Medium Term Macroeconomic Framework, Baseline Scenario

Indicator	FY12	FY13	FY14	FY15
GDP growth	3.4	4.3	6.0	6.5
Private investment (percent of GDP)	18.9	15.0	16.9	19.1
Public investment (percent of GDP)	5.8	7.6	7.5	7.7
Fiscal deficit (percent of GDP)	3.0	3.4	4.8	4.8
Revenues (percent of GDP)	13.3	14.5	13.7	14.1
Expenditures (percent of GDP)	18.6	19.9	20.3	20.2
External financing	2.4	1.8	2.6	2.9
External current account deficit (percent of GDP)	12.5	11.8	15.0	15.7
Exports growth (percent)	16.5	4.9	4.4	6.9
Imports growth (percent)	13.2	3.9	9.9	7.1
Inflation (percent)	23.5	6.2	6.7	7.1

Source: MFPED, IMF and WB staff estimates

Figure 12: Fiscal Strategy Focusing on Key Constraints



Source: Ministry of Finance Planning and Economic Development, Budget Speeches

In this year, the balance of payments is projected to remain at approximately the same level as in FY12, with increases in FDI compensating for deteriorations in the trade balance. Uganda's export earnings are expected to increase by 5 percent in FY13, driven by a modest rise in international food and fuel prices. However, the rate of growth in the volume of imports will also remain strong as a result of the need to purchase inputs to support infrastructure development. The capital balance should remain roughly unchanged, as the expected decline in official transfers following the recent governance scandals should be offset by a higher level of FDI, particularly in extractive activities. The current account deficit will remain in the range of 12 percent of GDP in FY13.

Over the medium term, the rate of growth of the economy should revert to recent historical levels. The main driving factors for improvements to the economy should be the gradual improvement of infrastructure and increased agricultural productivity (see Box 1). The rate of growth of the industrial sector could accelerate, boosted by improved infrastructure (e.g. improved energy supply) and the implementation of growth-enhancing reforms and interventions. In addition, the growth of the services sector, including growth in the banking and telecommunications sub-sectors throughout the EAC, will also contribute to the positive macroeconomic outlook. Under those conditions, the overall projected growth of the economy could rise to an average of 6.5 percent in FY14 and FY15.

It is still not clear what the extent of Uganda's oil resources is or when Uganda's production of oil will commence. However, in the long-term, it is clear that the country's production of oil will dramatically change Uganda's economic outlook. Uganda has proven oil reserves of at least 800 million barrels, although the actual figure may be closer to 3.5 billion barrels. With this level of reserves, production could reach 150,000-200,000 barrels per day over a 25-year production period. Revenues derived from oil could potentially double the government's total revenues in less than 10 years, contributing up to US$ 3 billion at current prices. At these levels, Uganda will not be totally dependent on oil revenues. They will nonetheless have a significant impact, placing considerable pressure on government regulatory and oversight systems. If current estimates of the country's oil reserves are correct, the level of Uganda's dependence on oil would place it in the company of countries such as Azerbaijan, Sudan, and Trinidad & Tobago, rather than classic petro-states such as Angola, Equatorial Guinea, and Nigeria.

The timing of the commencement of oil production is dependent on the construction of production infrastructure, including refineries and possibly pipeline. Full scale export-driven production is not expected to begin for at least five years. Although limited production of 10,000-20,000 barrels per day, primarily for domestic use, could begin within two to three years, full-scale oil production will require investments of several billion dollars in downstream infrastructure development. This will require large FDI inflows by multinational companies. This construction cycle could take up to 5-7 years, and will be influenced by recent oil discoveries in Kenya.

2.2 Risks: External Shocks, Declining Aid, Poor Weather and Political Will

Uganda is a relatively small, open economy. As such, it remains vulnerable to a number of external shocks, including fluctuations in prices of its main exports and imports. Experiences of the recent past illustrate how volatile commodity prices and financial distress in industrial countries can impact the local economy. Such risks remain, as a prolonged slowdown in the Euro zone cannot be discarded. The country's trade prospects are also influenced by the security situation in neighboring countries such as Sudan, Burundi and the Democratic Republic of Congo (DRC). Global commodity prices, including oil prices, remain volatile. A decline in the global economy could result in a corresponding decline in the volume of Uganda's trade with industrial countries, reducing its export values. It could also result in lower capital inflows, including inflows from remittances and in the form of aid. In case of such a decline in the global economy, the economic forecast will need to be revised downwards as a result of the significant additional pressures on the balance of payments, which might precipitate a depletion of reserves or the depreciation of the local currency. While a depreciating shilling would ensure exports remain competitive, it could also lead to increases in inflation.

Uganda is subject to a possible ongoing decline in official aid inflows, depending on the implementation of corrective measures to address recent corruption scandals. A significant and permanent decline in aid will require a major fiscal adjustment, particularly in the investment program, for which at least half of the funding is still externally sourced. At the same time, the short-term prospects for increased domestic revenue remain slim, as measures to eliminate the leakages resulting from exemptions are still lacking or poorly enforced. Thus, the government will have to cut both non-priority spending and planned capital investment. Such cuts will reduce aggregate demand in the short term and are likely to have a negative impact on the projected growth rate. The current temporary freeze in aid to a value of US$ 300 million by development partners is already estimated to have reduced the rate of growth in GDP by approximately 0.7 percent in FY13

The agricultural sector contributes to approximately a quarter of Uganda's total production and employs approximately three-quarters of its workforce. This sector, and therefore the overall Ugandan economy, is subject to climatic risk. Unfavorable climatic conditions, particularly poor rains, could reduce the level of agricultural production and affect the living conditions of a vast number of households in rural areas. Such negative impacts occurred during the 2010-2011 Greater Horn of Africa drought. Although this drought did not affect Uganda directly, it is estimated to have reduced food production, resulting in a decline of about three percentage points .

There are also a number of risks to the macroeconomic outlook that could arise from the government's lack of discipline in the area of expenditure, which is sometimes significantly influenced by political decisions. Firstly, fiscal discipline must be supported by the central administration to avoid any new slippages in public spending. Lack of restraint in the face of political demands, such as demands for the creation of new districts, could derail Uganda's fiscal position, resulting in shifts in expenditure to non-planned, non-priority areas. Secondly, the inappropriate prioritization of infrastructure investments and ineffective implementation could lead to a waste of public resources. There is no guarantee that a high level of development expenditure will lead to increases in the stock of physical capital. Despite the allocation of significant resources to the development budget, these will have limited benefits if those are used to finance non-capital expenditures and if the maintenance of existing infrastructure is neglected. Thirdly, corruption and theft could undermine the fiscal program, with consequences including a possible further decline in the provision of aid and other financial assistance by donors.

The rate of inflation could increase again as the result of excessively accommodating fiscal and monetary policies. This could be exacerbated by increases in food and energy prices as a result of regional and global factors. If the recent increases in global food prices persist, Uganda could face import inflation, especially if regional supply conditions deteriorate. The authorities may face a trade-off in adjusting macroeconomic policies, with the need to control the inflation rate having to be balanced against the risk of reducing the rate of economic growth.

The increased level of borrowing will support the meager savings to finance public investments. However, it will need to be accompanied by improvements in debt management. The government plans to use non-traditional sources, including Public-Private Partnerships (PPPs) and contractor facilitated financing, to finance the infrastructure development program. The government also plans to borrow on non-concessional terms for commercially and economically viable infrastructure projects for which no other source of funding is available. With such sources of financing, government debt may increase from an estimated 19.7 percent of GDP in FY12 to 24 percent in FY14, before rising to about 32 percent in the medium term. The prospects of future oil revenues may also place pressure on the government to borrow excessively in advance. The current level of debt is sustainable because of past debt relief10, and because borrowing has been concessional for the past 7 years. Nonetheless, the close monitoring of debt is warranted over the short and long terms.

Lastly, Uganda's economic performance may be affected by deterioration in the political climate. Civil unrest may undermine the economic recovery by increasing uncertainty and disrupting business, especially in urban areas, where most civil unrest occurs.

10 HIPC and MDRI, which , effectively canceled all outstanding positions up to 2007

2.3 The Need for Renewed Growth Momentum

In the past, Uganda has reaped the rewards from reforms implemented in the 1990s and 2000, which generated accelerations in economic growth that almost doubled the average per capita income. That notwithstanding, its ability to continue reaping these rewards is uncertain. With the rapid rate of economic growth, which increased from an average of 6.3 percent during the 1990s to 7.0 percent during the 2000s, Uganda's per capita income growth stood at an average of 4.0 percent per annum. This was significantly higher than the SSA average of 0.8 percent over the same period. More recently, Uganda's rate of growth has been less impressive. Since 2006, the rate of growth of GDP has decelerated gradually, converging with and eventually lagging behind SSA (see Figure 13).

The gradual deceleration in economic growth over the past few years was the result of a combination of factors. Because of negative climatic conditions, the agricultural sector grew at the slower pace of 1.6 percent per annum in the period from 2006 to 2012, less than half of the average rate of growth of 3.4 percent in the period from 1991 to 2005. Over the same periods, the rate of growth of manufacturing sector decelerated from 9.8 percent to 6.1 percent. The rate of growth of the previously booming construction sector also declined from 9.6 percent to below 7.4 percent between these two periods. The exception has been the rate of growth for the services sector, which accelerated from 7.3 percent to 7.7 percent, largely as a result of the rapid expansion of the communication and banking sectors.

The slowdown in labor-intensive sectors, particularly the agricultural sector, where more than 75 percent of the labor force is employed, has made the growth process less inclusive. Employment opportunities in the agricultural and non-agricultural wage sector grew fast, accelerating from 6-7 percent during the 1990s to approximately 12-13 percent per annum during the 2000s. The non-agricultural wage sector absorbed approximately 18 percent of the new entrants to the labor force. With the growth of labor-intensive sectors, particularly agriculture, lagging behind overall GDP growth, the economy is failing to create sufficient employment opportunities for its rapidly growing population.

On the demand side, growth is increasingly being driven by government spending, rather than by the activities of the private sector. Private sector investments have slowed down from an average of 12 percent of GDP in the period from 1991 to 2005, to 7.8 percent over the past 5 years. The widening trade deficit has increasingly drained GDP, with net exports declining from -7.5 percent to -22 percent of GDP. Consequently, the public sector has increasingly become the main driver of growth in aggregate demand, particularly through public investments, which have increased by 11 percent per annum over the past 5 years, compared to a rate of 1.4 percent per annum in the period from 1991 to 2005.

The slowdown in private investment and the decline in net exports have been accompanied by a growing imbalance between export earnings and import bills over the past few years. Driven by a rapidly expanding import bill, the weakening of the external current account also reflects the savings-investment gap. Uganda's level of domestic savings remains low, at 13 percent of GDP. This compares to the figure of 17 percent of GDP recorded by its neighbor Tanzania, which is also the sub-Saharan African average. At the same time, Uganda's patterns of consumption are increasingly involving a shift to imported goods.

These recent developments in the supply and demand sides of the economy may make it more difficult for Uganda to achieve its objective of becoming a middle-income country by 2025. At US$ 510 per person, Uganda remains a poor country, even by SSA standards. Thus, it cannot afford low growth.11 Uganda's aspirations towards middle income status, which imply a US$ 1000 per capita average income, will only be realized if it Uganda's economy grows at a rate in excess of 10 percent per year over the next decade.[12]

A more rapid diversification of the economy and the appropriate use of resources, including oil, will drive this renewed growth momentum. In addition to providing a means to close the current account deficit, the production of oil can boost the capacity of the economy through the development of backward and forward linkages and through the smart use of oil related revenues.[13] Policies to improve the business environment; to develop human capital; and to improve

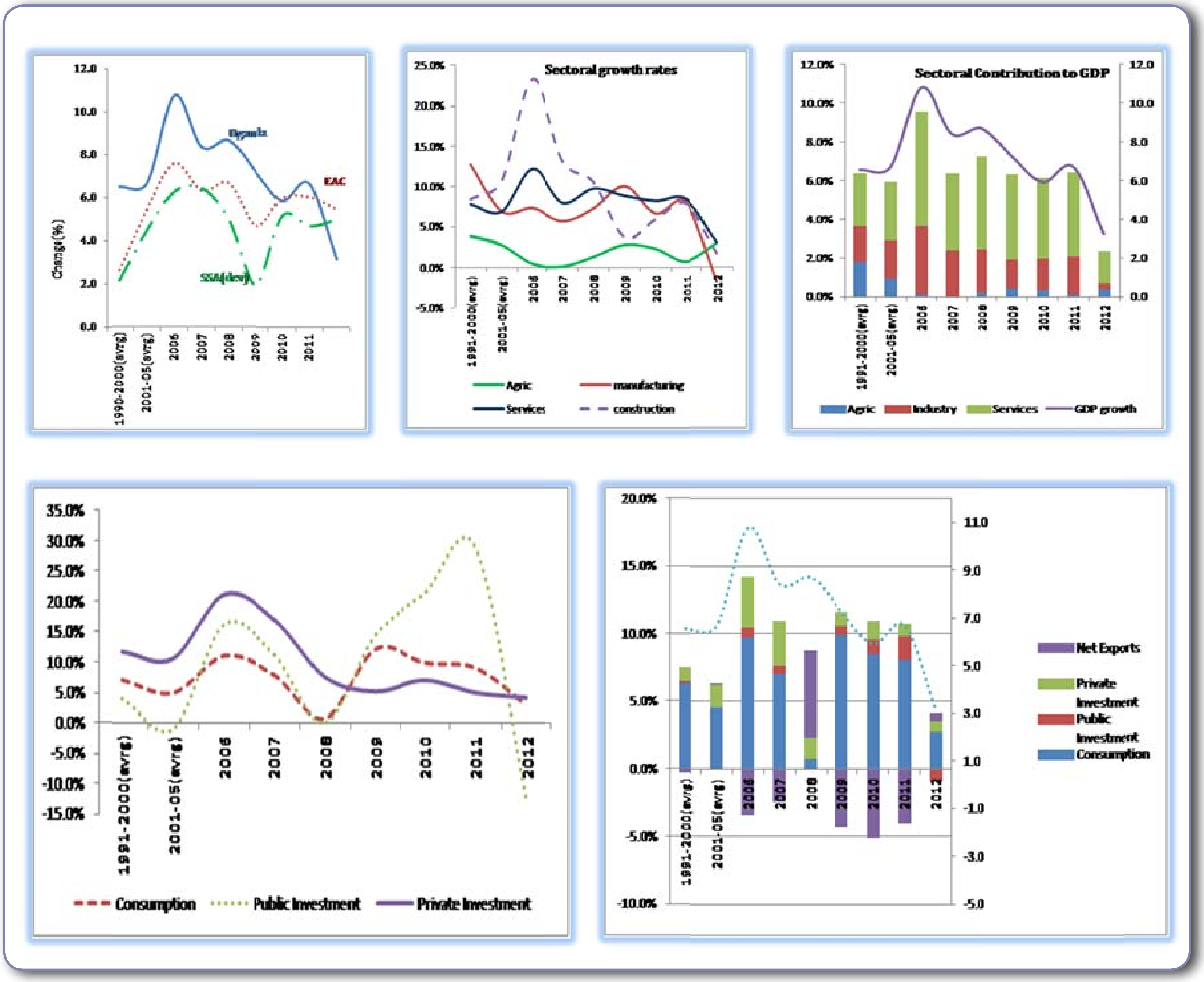
11 The lower the income, the more likely for it to grow fast, as it is starting from a low base.

12 Shanta Devarajan and Wolfgang Fengler 2012, Is Africa's Recent Economic Growth Stable at The Institut français des relations internationals (Ifri), October.

13 Even before oil revenues start to flow, private sector investment is likely to increase significantly to respond to production infrastructure needs during the preparation phase.

the stock of infrastructure, will remain key drivers of this transformation. International experience also strongly suggests that economic liberalization and integration is vital for the achievement of productivity gains and economic expansion, especially for a small landlocked country such as Uganda. Increased openness could help stimulate economic growth by providing new markets (demand side) and by encouraging firms to become more competitive (supply side). It could therefore lead to an expansion in production, increased diversification, and the creation of additional employment opportunities. Regional trade will also play a significant role in the achievement of these goals.

Figure 13: The Slide in FY12 Makes the Downward Trend Observed in Uganda's Growth in Recent Years More Pronounced



Source: Uganda Bureau of Statistics, 2012

Part 2:

Regional Trade: Harnessing the Potential

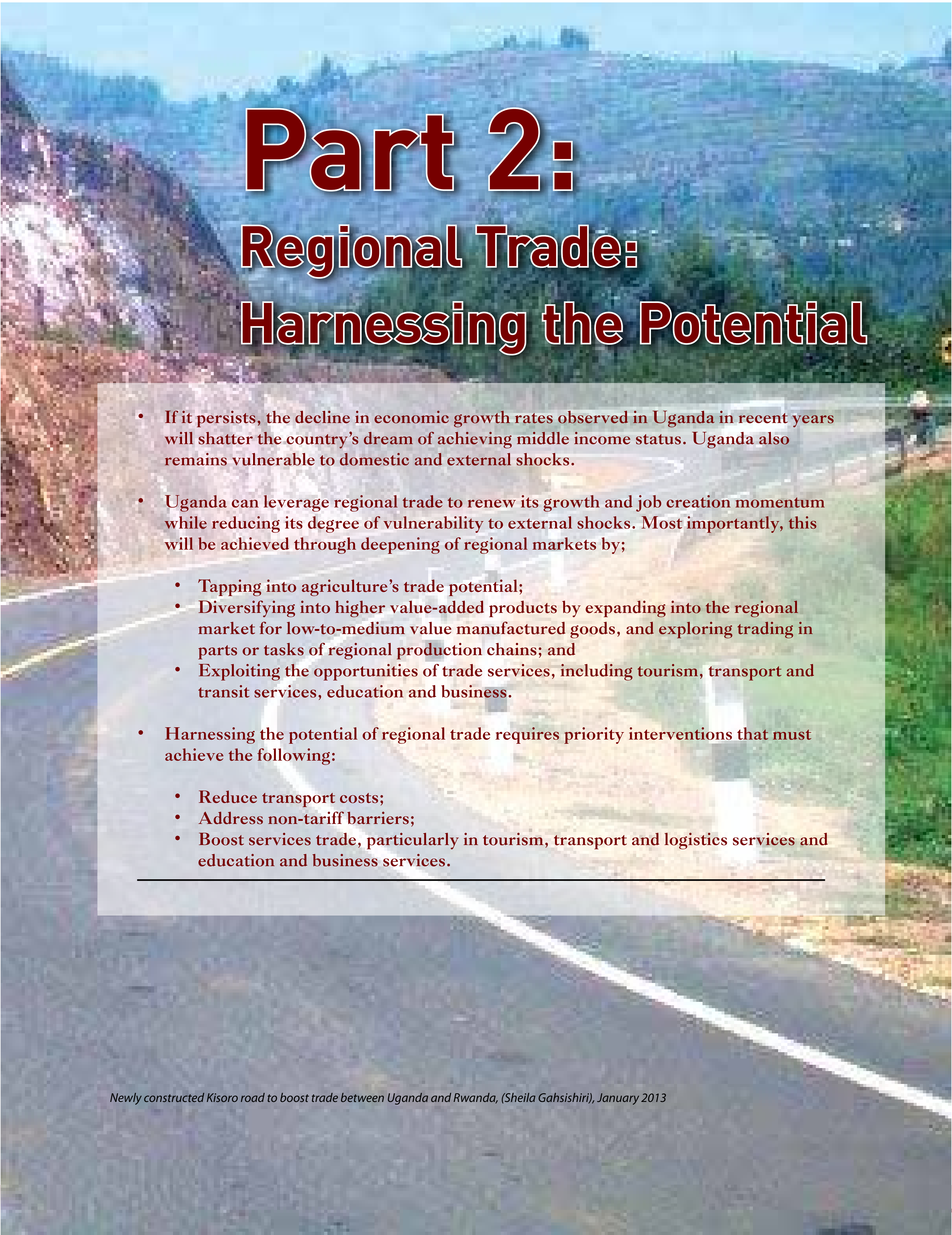
- If it persists, the decline in economic growth rates observed in Uganda in recent years will shatter the country's dream of achieving middle income status. Uganda also remains vulnerable to domestic and external shocks.

- Uganda can leverage regional trade to renew its growth and job creation momentum while reducing its degree of vulnerability to external shocks. Most importantly, this will be achieved through deepening of regional markets by;

  - Tapping into agriculture's trade potential;
  - Diversifying into higher value-added products by expanding into the regional market for low-to-medium value manufactured goods, and exploring trading in parts or tasks of regional production chains; and
  - Exploiting the opportunities of trade services, including tourism, transport and transit services, education and business.

- Harnessing the potential of regional trade requires priority interventions that must achieve the following:

  - Reduce transport costs;
  - Address non-tariff barriers;
  - Boost services trade, particularly in tourism, transport and logistics services and education and business services.



Newly constructed Kisoro road to boost trade between Uganda and Rwanda, (Sheila Gahsishiri), January 2013

3. Prospering through Cooperation and Trade with Neighbors

In a typical African village, there are specialists in different fields. There is a trader who runs the local shop, a tailor who repairs everyone's clothes, a bicycle mechanic to whom everyone runs, a nurse or doctor who will handle the simple ailments, the man who buys the local produce, and there will be a weekly market at which sales of what the village does not produce are availed in timely fashion. In the market, one person sells cassava, while another stocks bananas. There is a vegetable specialist and an elderly woman who has always sold spices. Her husband of 43 years has, from time immemorial, been the supplier of pots and pans, which he brings in from a town some 60km away. This couple's household is an epitome of class, diversifying and growing with time.

Suppose Uganda was one of the households in a typical African village, and obviously with some specialties in some areas, like producing maize or education services, and deficits in others like vehicles to transport its goods or high tech manufacturing, the optimal model of development would be to work together with other villagers. Uganda may have some natural advantages, and could be on the path of developing others, but it cannot survive for long without other villagers. Even though most of its food comes from its own farm, it also needs to buy merchandise from other villagers; and from other villages and towns very far away from it. There are also opportunities to sell its surplus to other villages as well. It cannot afford to be hostile in any way to outsiders, lest the road to the best buyer will not be fixed. It would be suicidal for the villager or the individual traders in the market to discriminate against people from the other villages or for them to declare that they will not avail certain produce because somebody's cows strayed into another person's garden. Those would be non-tariff barriers.

Warehousing services, like this depot in Nakawa to ease regional trade (Charles Kunaka), April 2011

For Uganda to achieve renewed growth momentum, it must 'think beyond its borders' and cooperate with its neighbors, just as the typical African villagers described in the story must do. However, in Uganda's case, the village is the large and expanding regional markets that exist within the Great Lakes region. Uganda must build upon its remarkable historical economic success to develop a more resilient economy. It must address its vulnerabilities to boost economic growth and create employment opportunities for a greater proportion of its population. With the current state of the village, there are both opportunities and constraints facing Uganda in its efforts to move to the next level. Uganda can achieve economic resilience and sustained growth through a higher degree of interaction between domestic producers and external markets. The successful experiences of many countries, including Malaysia, Singapore and Korea, suggest that trade openness and regional integration can drive growth and create job opportunities in small economies such as. For the spice trader to make opportunities for the growth of her business and for gainful employment for her children and grandchildren, she cannot keep doing things the way she did 30 years ago. The criticisms that have been leveled against liberalization and opening up notwithstanding, two critical questions must be addressed: (i) What has Uganda gained from trade openness so far to justify further outward orientation? and (ii) Can regional integration be the gateway for further trade?

3.1 The Benefits of Outward Orientated Policies

During Uganda's two-decade reform process, the country established a liberal environment to support the free exchange of goods, capital and ideas beyond its borders. The liberalization and reform process that began in 1993 resulted in big gains, increasing the country's openness, diversifying products and markets, and increasing FDI (see Box 2). Today, Uganda exports almost US$ 5 billion worth of goods and services each year, which represents a value equal to 27 percent of its GDP. This compares to the early 1990s, when exports accounted for only 7 percent of GDP. On the other hand, Uganda now imports goods and services worth US$ 7.6 billion, equal to 45 percent of GDP. By comparison, in the early 1990s, the total value of imports was equal to only 19 percent of GDP. Within the EAC village, Uganda's exports per capita grew faster over this period than any of its neighboring countries, at a rate of 10.2 percent per annum.14 This compares to Tanzania, where the corresponding rate was 9.7 percent, while Rwanda's stood at 5.8 percent, Kenya's at 4.3 percent, and Burundi's at 1.2 percent. During the 2008-09 global economic crisis, regional trade provided a buffer for Uganda's economic activity.

While the figures above represent a fair accomplishment, Uganda is still not achieving optimal trading results. Uganda's total trade represents approximately 59 percent of GDP. However, at its level of income, the country's openness to trade remains less than might be expected. In a number of countries with similar income levels and sizes, trade accounts for up to 80 percent of GDP. Uganda's limited success in this area is a result of under-exporting. Uganda under-exports to many countries, including its neighbors Tanzania and Kenya, and other countries including India, Brazil and US. By contrast, Uganda over-imports from most countries other than Rwanda and Burundi.15 In contrast to the situation presented in the story of the ideal African village, Uganda is dependent on merchandise from outside, while at the same time it has not fully developed productive activities where it has competitive advantages. Even though imports can bring new technology which in turn can promote productivity gains in the local firms, over-dependency creates an unhealthy imbalance.

Building on the liberal trade regime Uganda has developed, the country can still benefit from outward oriented policies that encourage farmers and businesses to make better choices regarding what to produce, how much to produce and with which inputs. In turn, this will promote improved efficiency amongst firms and farms and encourage the development of new products and services and the emergence of new markets. A higher level of integration will not be possible if Uganda continues to sell the same old products produced in the same old way.

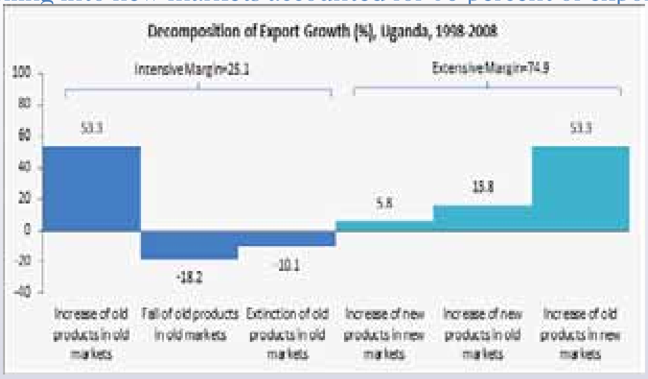
14 Growth rates calculated as the compound annual growth rate over the reference period
15 Based on gravity model allows comparing actual relationships of a country and its trading partners, with predicted values based on country characteristics.

Box 2: Uganda's Gains from Liberal Trade Environment

As a result of a liberalized trade environment:

(i) Uganda trades in a greater range of products: This is particularly true for agricultural products, but trade diversification has extended into non-agricultural products, particularly non-traditional service exports. Uganda's goods and services became more diversified as local firms became more competitive, particularly in non-traditional exports, such as processed fish, flowers and foodstuffs such as grains. Uganda's goods exports sector is dominated by agricultural produce (vegetables, animals, and foodstuffs) the share of which remained at 85 percent of total exports in the period from 1996 to 2010. However, the share of vegetables dropped from 75 to 51 percent over the period, although the share of foodstuffs and animals increased. These two products have the highest revealed comparative advantage (RCA) index. There is still a relatively high degree of concentration, with Uganda's top 10 exports of products accounting for 60 percent of the export basket. However, recently, the most important exports have included nonagricultural projects, such as cement. In addition, the services trade has experienced strong growth, supported mainly by the boom in services beyond traditional transport and travel. From increased export diversification, Uganda's exports are no longer dominated by coffee which, from contributing to 90 percent of total export earnings in the 1990s, now contributes only 25 percent. Rather, is exports include a more diversified range of products, including processed fish and sugar, among others.

Figure 3.B.1. Selling into new markets accounted for 60 percent of export diversification



(ii) Uganda has diversified markets: Uganda increased its share of the world export market in the period from 1990 to 2010, while at the same time, Kenya and Burundi's share declined. While trade beyond the continent remains very important, trade within Africa has grown at a considerably faster rate. In proportionate terms, the share of exports to the EU, the main destination for Uganda's exports, declined by 25 percent in the period from 1996-98 to 2006-10, mostly due to increased trade with the Great Lakes regional economies. As the terms of trade became favorable to Uganda in the 2000s, exporters diversified into new markets. While Uganda runs a trade deficit with its two biggest neighbors, Tanzania and Kenya, it enjoys a trade surplus with Rwanda and Burundi.

(iii) Uganda has become East Africa's most attractive investment destination: Uganda's inward flows of FDI expanded from 1.4 percent of GDP in 1990 to 5.3 percent in 2010. At US$ 755 million in 2010, Uganda received more than 50 percent of total FDI inflows to East Africa. FDI supported investments mainly in finance (30.5 percent of total flows), the manufacturing sector (11.3 percent), and mining and quarrying, including oil exploration (18.0 percent), and ICT (10.9 percent).

Source: World Bank staff calculations from World Development Indicators.

3.2 Regional Integration: To Open Up the Region

Uganda has been a pioneer in the promotion of regional integration within Africa, entering into a number of regional arrangements, including EAC and COMESA (Common Market for Eastern and Southern Africa). The rationale for its participation in these arrangements is that regional integration will help Uganda gain access to regional markets and to use these markets as a platform to expand its global import and export markets. The experiences of relatively small landlocked countries in Asia, EU, and Latin America underscore the importance of regional integration to develop regional public goods, reduce transaction costs, promote the development of a regulatory environment in which goods and services can flow freely, and to support cross-border production networks. Regional integration can also reduce the constraints faced by many firms in accessing the essential services and skills that are needed to boost productivity and diversify into higher value-added production and trade.

The EAC is the most promising regional bloc in Africa. However, while it has grown fast, efforts to achieve a high level of integration are still in their infancy. Since 1993, when the three founding countries (Kenya, Tanzania and Uganda) revived the community, the EAC has been the second-fastest growing economic bloc in the world, after ASEAN. Since that point, the EAC has doubled its GDP to US$ 79 billion. Leveraging more space for trade makes sense for Uganda. While Uganda has a very small market share, it is one of the fastest growing economies within the region in terms of trade volumes and in terms of its rate of growth of GDP. Nonetheless, the EAC faces a number of challenges in the area of policy coordination and harmonization. The Customs Union, being only at the second stage of the four planned for EAC full integration, is far from complete (see Box 3). There are a number of reasons for its slow development, including issues related to multiple trade partnerships; the lack of an effective joint revenue sharing mechanism; the persistence of multiple customs controls; and the rise in significance of non-tariff measures. Despite the 2005 adoption of the EAC Common External Tariff (CET), regional trade remains distorted by a number of factors, including numerous non-tariff barriers to trade and limited currency convertibility. While the benefits of regional integration go beyond trade (see Box 4), the EAC's efforts have so far only focused on trade of goods and services.

Political economy considerations also explain the limited progress towards a higher level of regional integration. While the benefits of such integration are clear, its achievement involves a number of challenges. In particular, these challenges relate to the unequal distribution of benefits and costs between and within member countries. In the short term, some members of the community may gain, while others will lose. While the intensified competition resulting from the development of a common market is likely to have positive effects on productivity and consumer welfare in the medium-to-longer terms, it presents a challenge for some elements within Uganda's private sector in the short term. Increased regional trade, especially in food staples, may also result in increased consumer and producer prices in Uganda. While the welfare effect of a price increase for regionally traded commodities, such as matooke, sweet potatoes, cassava, maize, millet/sorghum, onions, tomatoes, beans, and groundnuts, is positive for net sellers, it is negative for net buyers. However, on balance the benefit derived by net sellers far outweighs the loss incurred by net buyers but these asymmetries have implications on the willingness and ability of different members of the community to further develop interventions to achieve a higher level of integration.

More broadly, the lack of symmetry in regional integration becomes particularly apparent when the geographical location of businesses is considered. Economic geography16 dictates that as borders become thinner, through removal of trade barriers or as a result of other factors, businesses may seek to locate their operations to maximize their profitability and proximity to markets. For higher-end manufacturing industries aiming to penetrate global markets, this may mean locating their operations closer to the coast, as this location allows them to access larger global markets more efficiently. Otherwise, they may seek to locate their operations in a city such as Nairobi, which is the densest city in the Great Lakes region, to benefit from market size and economies of scale. Considering this, Uganda has to advocate for policies to improve regional connectivity and facilitate Ugandan firms' access to the global markets.

With no divisions and reduced distance, Uganda could start focusing on regional production chains driven by trade in parts and components ("trade in tasks"). This will contribute to export growth and diversification, increase vertical specialization, and create employment opportunities. A higher level

16 Economic geography is the branch of economics that focuses on the location, distribution and spatial organization of economic activities, and was the focus of the Bank's World Development Report (WDR) 2009.

Box 3: Status of Regional Integration Efforts in EAC

i. A Long History of EAC Integration Efforts

Kenya, Tanzania and Uganda have a long history of successive regional integration arrangements:

1927: Customs Union between Kenya, Tanzania and Uganda

1948-1961: East African High Commission

1961-1967: East African Common Services Organization

1967-1977: East African Community

1993-2000: East African Co-operation

2000: East African Community

The EAC Treaty establishing the community was signed on 30 November 1999 and entered into force on 7 July 2000 following its ratification by the original three partner states – Kenya, Tanzania and Uganda. Burundi and Rwanda acceded to the EAC Treaty on 18 June 2007. The EAC today is a regional intergovernmental organization of Kenya, Tanzania, Uganda, Rwanda and Burundi, with its secretariat in Arusha, Tanzania. South Sudan and Somalia have made applications to join.

ii Lessons Learnt from EAC Collapse in 1977

The collapse of the EAC in 1977 can be attributed to a number of reasons including governance challenges, economic imbalances (in part arising from the socialist system in Tanzania and capitalist system in Kenya), political disagreements, and an extremely limited dissemination of information. Two reasons stand out: (i) the relatively low engagement of stakeholders in civil society, the private sector and amongst EAC citizens, in the decision-making and management processes of community integration; and (ii) the lack of a dispute resolution process for sharing the costs and benefits arising out of EAC integration. Since 1977, steps have been taken to address some of these problems, including a Mediation Agreement (1984) for determining and dividing EAC assets and liabilities, and an agreement for the establishment of the Permanent Tripartite Commission for East African Cooperation (1993). Nonetheless, citizen engagement, knowledge sharing and consensus building are, and will continue to be the key components for a successful integration.

iii The EAC Today: Good Progress But Much Remains to be Done

The EAC integration is on the second stage of the four planned stages – Customs Union, Common Market, Monetary Union and Political Federation. In 2005, the EAC adopted the Customs Union protocol that established, (i) a duty-free trade between the partner states (with the successful reduction of intra-regional tariffs), (ii) common customs procedures between the partner states and a common external tariff (i.e., an identical rate of tariff is imposed on goods imported from foreign countries). The next stage came with the Common Market protocol in 2010 that established a single market allowing the free movement of goods, capital and labor within the region. Partner states have been required to review domestic rules and regulations and ensure compliance with the protocol, in order to harmonize policies and regulations within the region. This involves the removal of restrictions on the free movement of factors of production and on the right of establishment, as well as pursuing mutual recognition of academic and professional qualifications. Allowing free movement of goods, capital and labor across all partner states is more complicated than had been anticipated, and hence delays are expected.

iv. Challenges in Advancing the Regional Integration Agenda

Full implementation of a single Customs Union/Common Market (second stage) remains a challenge for the following reasons: (i) the membership in multiple regional economic communities can distort the common external tariff; (ii) customs clearance and tax collection remain destination-based while a joint revenue sharing mechanism for tariffs is absent; (iii) the persistence of various controls at customs for goods circulating within the Community; (iv) the limited institutional authority to ensure compliance with the Customs Union policy framework; and (v) the prevalence of non-tariff barriers (ASI 2012). Once the Customs Union has been established, significant efforts will be needed to progress towards the realization of the Common Market enacted in 2010 and the effective implementation of the free movement of capital, goods and labor, it entails.

Given delays in the full implementation of Customs Union and Common Market protocols, the third stage – Monetary Union – expected to bring a single currency to the region, and the fourth and final stage – Political Federation, previously anticipated for 2012 and 2015 respectively, might be postponed further.

Box 4: How Could Leveraging Regional Integration Accelerate Uganda's Competitiveness?

Landlocked Uganda has to rely on its neighbors' capacity and willingness to supply substantial services for Uganda's benefit and public goods in the form of good transit policies, regulations, infrastructure and institutional arrangements.

i. Promoting regional infrastructure projects

The disparities across countries and an unequal distribution of costs and benefits hamper the efficient supply of regional public goods. In particular, coastal countries are responsible for investments in their infrastructure that is being used by landlocked countries, creating an incentive for underinvestment. This will require the establishment at the EAC level of political and technical mechanisms to deal with the asymmetric benefits and costs of integration policies. Every strategy for addressing infrastructure bottlenecks should consider the region a single entity and seek to facilitate investments on regional rather than national lines. The benefits from better connectivity tend to be indirect and long term, and asymmetric across countries, while costs are immediate. To avoid underinvestment that can arise from this mismatch, agreement on the appropriate allocation of costs, especially for large projects, must be arrived at the regional level.

ii Improving trade facilitation

Removal of non-tariff barriers is a regional issue given the capacity and political economy of its removal. The resistance to removal of some barriers arises from the desire to protect some sectors by some countries. Coping with such vested interests will require strong political commitments at the regional level. Capacity-building programs focusing on regional integration such as the one currently being implemented. TradeMark East Africa will support trade facilitation and NTB removal.

iii. Introducing effective standards and other regulatory instruments

Regional agreements such as the EAC Common Market Protocol may also make it possible to reap scale economies in regulation and supervision, particularly where national regulatory agencies face skill and capacity constraints; they could also reduce scope for the capture of national regulation by private sector interests and reduce regulatory heterogeneity. Regional regulatory cooperation can also provide gains as a commitment mechanism to strengthen the credibility of a country's reform. Strategic regional partnerships aimed at attracting FDI will help Ugandan firms increase profitability resulting from economies of scale generated by a bigger market and better supporting services.

iv. Promoting regulatory cooperation

A good example of regulatory cooperation is in the professional services, where regional agreements on the mutual recognition of professional qualification can help with the development of adequate curricula for various professions, and provide guidance for employers, mentors and trainees regarding the practical experience requirements for professionals. Furthermore, Uganda can work with regional bodies such as the IUCEA, the EABC, or the EAPSP to undertake in-depth, cross-country comparative assessments of professional qualifications (entry requirements, education and training, and practical experience requirements) and the regulations governing the professionals in each EAC member state. This is critical for implementation of the Mutual Recognition Agreements of professional qualifications and licensing requirements (MRAs). Uganda's participation in the professional services knowledge platforms in East Africa and COMESA can help the country with the development of a meaningful reform program that includes the elimination of explicit barriers and regulatory, education and immigration reforms. Mutual recognition of educational and professional qualifications, intra-African arrangements could be more suitable than global ones for the supply of regional public goods. In tourism, Uganda can participate in EAC-wide tourism projects to increase its exports of tourism services.

of labor mobility, as envisaged under EAC's Common Market protocol, would help address critical skill gaps, while generating important agglomeration effects in the medium to long term.

Regional trade, particularly the trade of agricultural commodities, has the potential to stimulate growth and to improve the living conditions of the high proportion of the population employed in the agricultural sector. At the same time, net buyers, who are mainly residents of urban areas, may lose out, at least in the short term. The balance of costs and benefits is expected to be positive for Uganda, especially if one considers the cost of maintaining the status quo. However, there will most likely be adjustment costs, at least initially. This means that it is vital to engage in dialogue with all relevant actors in Uganda, for which the recently revived public-private dialogue mechanism offers an appropriate framework.

3.3 Is Regional Integration Working to Promote Economic Growth in Uganda?

It is a great thing for a village to have a well-constructed road. However, it could be argued that the success of the road is only demonstrated if it effectively facilitates the flow of goods, services, and people. Similarly, the success of regional integration can be determined in terms of the extent to which it has achieved the objective of improved trade and labor flows, both at the regional level and at the broader international level, following improved access and harmonized policies.

In terms of regional trade, Uganda has increased its volume within the EAC and with regional markets outside the EAC, such as DRC and Sudan, over the past five years. Uganda's exports to the four EAC partners have grown at a rate 2 percent faster than to elsewhere in the world. As a result, its share of total EAC regional exports increased from 15 percent in FY07 to 25 percent in FY11. Exports to non-EAC regional trading partners (South Sudan and DRC), grew even more rapidly, at a rate of 10 percent. For these markets, the share of Uganda's exports rose from 32 percent in FY07 to 48 percent in FY11.

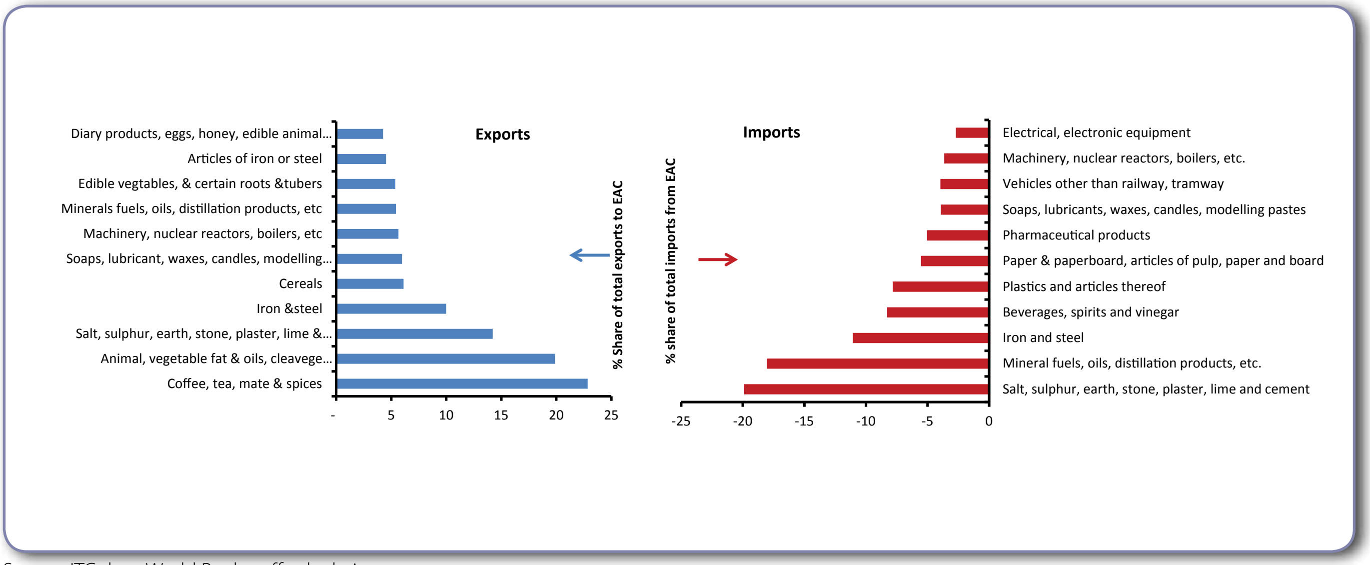
The diversification of exports has been mainly driven through exports to regional markets. At present, the bulk of Uganda's exports to the region consist of primary agricultural products and processed agro-produces. However, industrial exports, involving produce such as iron sheets, lime and cement, beverages, plastics, paper and soap, are becoming increasingly significant (see Figure 15). The level of trade complementarity[17] with Uganda's regional peers has been increasing over the last 10 years, suggesting a lessened risk of trade diverting to other non-EAC countries as the region integrates. This suggests that Uganda could satisfy a larger part of the domestic market, while also consolidating and expanding into regional markets.

Export dynamism has spread across partner states in the region with Kenya maintaining its traditionally stronger position while Uganda emerges strongest (see Table 2). Of the EAC nations, Kenya remains the strongest exporter, with more than 16 revealed comparative advantage products through the 2000s. This compares to Uganda and Tanzania, each with nine comparative advantage products. However, more recently, Uganda has had the highest number of products with revealed comparative advantage. Emerging products of this sort include dairy produce, animal/vegetable fats, sugars and confectionaries, tobacco, lime and cement, soap, base metals, and printed books and newspapers. The bulk of these are also Kenya's classic products, implying that Uganda needs to raise productivity to remain competitive.

In the short term, some members of the community may gain, while others will lose. While the intensified competition resulting from the development of a common market is likely to have positive effects on productivity and consumer welfare in the medium-to-longer terms, it presents a challenge for some elements within Uganda's private sector in the short term.

17 Trade complementarity measures the fit between one country's exports and the imports of its trading partners. It was calculated on the exports side to assess the potential market access gains on partner markets given Uganda export capabilities.

Figure 14: Uganda's Top 10 Regional Trade Goods in 2012 - Exports Concentrate in Agricultural produce, Many of the Manufactured Goods Exports are also Imported



Source: ITC data, World Bank staff calculations

Uganda's share of regional imports declined from 15 percent in 2005 to 12 percent in 2010. Uganda's imports are mainly in machinery and equipment (25 percent), and petroleum products (15 percent), the bulk of which could not be sourced from within the region. However, other imports such as chemicals, plastics and other industrial products could be sourced from the region, if they were cheaper than those from China. Informal trade, which is mainly with South Sudan, DRC and Kenya, contributes more to Uganda's exports than to its imports. The share of informal imports declined from 2.7 percent to 1.2 percent due to tougher regulations and surveillance of imports by the revenue authority. At the same time, its share of informal exports increased from 18 percent to a peak of 30 percent in FY10, before declining to 18 percent in FY11. Therefore, Uganda enjoys a relatively high regional trade surplus. However, it could reduce its import bill through import substitution and by raising productivity to compete in existing regional markets.

Petroleum imports truck their way through the Northern Corridor, (Great Lakes Film Production Ltd), November 2012

Table 3: Classification of Exports by Change of Competitive Advantage 2005-2010

	Kenya	Tanzania	Uganda
CLASSICS RCA (2005)=1 RCA(2010)=1	1. Flowers 2. Edible vegetables 3. Coffee/tea/spices 4. Animal vegetable fats 5. Sugars 6. Preparation of vegetable fruits 7. Salt/cements 8. Mineral fuels/oils 9. Inorganic chemicals 10. Pharmaceuticals 11. Soap 12. Plastics 13. Raw hides and leather 14. Paper products 15. Iron/steel & articles thereof 16. Aluminum and articles thereof	1. Fish 2. Edible fruits and nuts 3. Products of milling industries 4. Oil and grain seed fruits 5. Tobacco 6. Ores/slag/ash 7. Wood and articles thereof 8. Cotton 9. Natural pearls and stones	1. Fish 2. Coffee/tea/spices 3. Cereals 4. Cocoa and products thereof 5. Beverages/spirits/vinegar 6. Raw hides and skins 7. Cotton 8. Iron/steel & articles thereof
EMERGING CHAMPIONS RCA (2005)=0 RCA(2010)=1	1. Vegetable products 2. Beverages, spirits and vinegar 3. Electrical machinery and parts 4. Vehicles and their accessories	1. Fertilizers 2. Paper and paper board 3. Textile articles 4. Boilers and mechanical appliances 5. Electrical machinery and parts	1. Dairy produce 2. Animal/vegetable fats 3. Sugars and confectionaries 4. Tobacco 5. Salt/cements 6. Soap 7. Other base metals and articles thereof 8. Printed books/ newspapers
DISAPPEARANCES RCA (2005)=1 RCA(2010)=0	1. Raw hides and skins 2. Paper and paper board 3. Other made up textile articles 4. Articles of stone plaster	1. Cereals 2. Cocoa 3. Residues/waste from food industries 4. Other vegetable textile fibers 5. Glass and glass ware 6. Copper and articles thereof	1. Products of animal origin 2. Products of milling industries 3. Oil and grain seed fruits 4. Vegetable plaiting materials 5. Electrical machinery equipment and parts 6. Vehicle parts and accessories

Notes

1. The RCA index measures the relative advantage of a country's industry or product in trade. The RCA index above unity indicates the country's share of exports in that product/industry exceeds the global export share of the same sector. In such a case, the country has a comparative advantage in that sector. Since high export volumes can result from subsidies or other incentives provided, including under-valued exchange rates, the RCA index captures competitiveness rather than comparative advantage (Siggel, 2006).

2. ***Classics*** are those products that maintained RCA at 1, ***Emerging champions*** are those that did not reveal comparative advantage before, but do so in the latter period, while ***Disappearances*** would have revealed before, but are not competitive anymore.

Source: World Bank calculations based on Customs data, 2005-2012

4. Leveraging Opportunities in the Region and Beyond

If it proceeds appropriately, enormous opportunities lie ahead for Uganda. If it develops an increasingly outward orientation, this will allow its farms and firms to make better choices regarding what to produce, how to produce it, how much to produce and what inputs to use. This is the key benefit to be derived from the free exchange of goods, capital and ideas across borders. But this is not enough. Uganda has to adopt the appropriate strategies to sustain and grow the regional markets that it has tapped so far. The country's strategic plans must be streamlined, first, to broaden the regional market, which will require Uganda to think beyond EAC, its traditional regional market for centuries. Second, it must deepen trade by developing and exploiting a greater range of products. This will require thinking beyond food exports and low-value manufacturing exports.

Mukwano Industries in Kampala loading goods for the Juba market in Sudan, (Great Lakes Film Production Ltd), November 2012

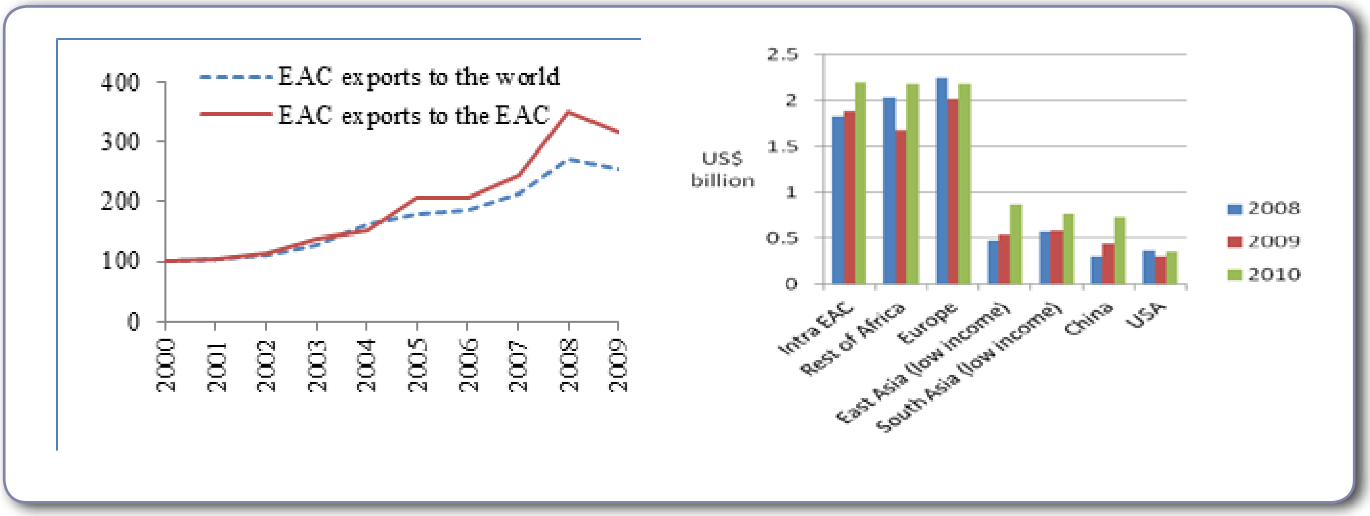
4.1 Beyond the EAC: Uganda as a Land Bridge to Connect Landlocked Nations with Coastal Regions

The EAC presents the first opportunity to leverage the dynamic regional market, with Uganda's trade with the EAC region having grown faster than that with the rest of the world. But Uganda can also almost double its trading space through the inclusion of additional neighboring markets within the Great Lakes region. These markets include countries such as South Sudan and the Democratic Republic of Congo, where the private sector has already established trading partnerships, mainly through informal means. Building on the existing trade relations, Uganda must take strong measures to coordinate and harmonize policies to facilitate trade between EAC and non-EAC Great Lakes countries, especially through better infrastructure and institutions to support trade.

As with the elderly spice trader who tapped the fast-growing incomes and population of her village through interactions with her near neighbors first, the EAC presents the first opportunity to leverage the dynamic regional market, given the fast-growing size, incomes and population of EAC members. Uganda's GDP, amounting to approximately US$ 17 billion in 2011, is only the third largest amongst EAC nations. Trailing Kenya and Tanzania, it accounts for just 21 percent of the regional economy. With the EAC regional market worth approximately US$ 79 billion, Uganda's potential market expands six-fold. In principle, this market should be relatively accessible because of its close proximity. Growing faster than the sub-Saharan African average of 2.6 percent, the EAC's population grew from 110 million in 2002 to 138 million in 2010. Of this, Uganda's population accounts for only 23 percent. Per capita incomes are also gradually increasing, with Uganda's average per capita income of US$ 500 being somewhere in the middle of the range, between the figure of US$ 795 recorded in Kenya and that of US$ 192 recorded in Burundi. Thus, there are opportunities for expanding markets and improving economies of scale. Prospects for the region are positive. Between now and 2020, Uganda, Kenya and Tanzania are expected to be among the fastest growing economies in the world, given how they have applied their productive capacities to their respective export structures.[18]

The fast expansion of trade between the EAC countries suggests that these countries have taken advantage of proximity and good neighborliness to export more within the region than to rest of the world. The value of exports from the founding members reached US$ 20 billion in 2010, following an annual average rate of growth of 16 percent in the period from 2001 to 2010. Rwanda and Burundi are also expected to increase their rate of growth of exports from 2015 onwards.[19] Intra-regional exports as a share of total exports increased from approximately 15 percent in 2000-04 to approximately 19 percent in 2009-10, and now amount to US$ 2.2 billion. Growth rates for EAC exports within the region exceed those of EAC exports to the rest of the world (see Figure 15). Unlike EAC exports to the rest of the world, which mainly consists of primary commodities, the bulk of intra-regional exports consist of semi-processed and lower value manufactured goods (e.g. food products, beverages, tobacco, cement), to which Uganda contributes significantly.

Figure 15: EAC Countries Exporting More to Each Other and Catching up with Traditional Destinations



Source: Comtrade/World Integrated Trade Statistics(WTI) and WDI

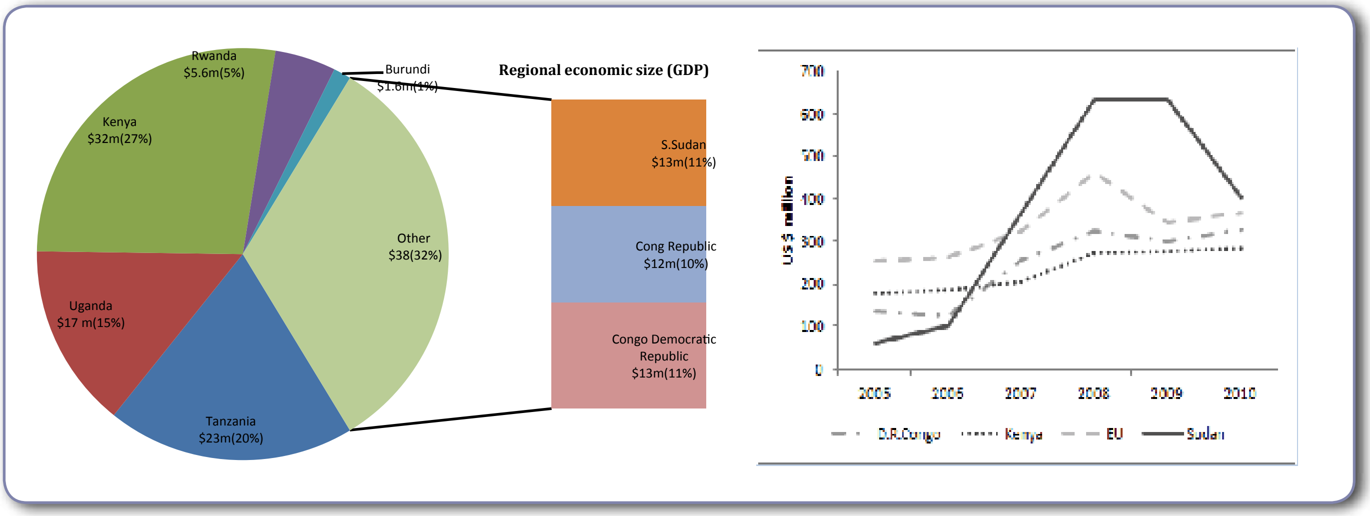
Uganda is the land bridge for the rest of the Great Lakes region, connecting a number of landlocked countries to the coastal countries. This could enable Uganda to expand its trading space by almost 50 percent, if the near markets of South Sudan, DRC and the Congo Republic are included. EAC's GDP currently stands at US$ 79 billion. With the inclusion of South Sudan, DRC and Congo Republic, total regional GDP increases by approximately 48 percent, to US$ 118 billion (see Figure 16). As political efforts to include South Sudan and Somalia into the EAC continue, the private

18 Centre for International Development Harvard University, (2012) The Atlas of Economic Prosperity: Mapping Paths to prosperity
19 Nathan Associates (2011), Corridor Diagnostic Study on Northern and Central Corridors of East Africa.

sector is trading with these countries, mainly through informal channels. At least up until 2010, South Sudan and DRC accounted for 38 percent and 20 percent of Uganda's total exports respectively. Thus, they absorb a greater proportion of Uganda's exports than Kenya, which accounted for 19 percent. In 2011 and 2012, trade to these non-EAC countries slowed down, mainly on account of the political and economic turmoil both in South Sudan and DRC. However, if the situation in these countries normalizes, trade between them and Uganda should again boom.

Building on these strong trade relationships, Uganda has an important role to play in coordinating and harmonizing policies related to trade between EAC and non-EAC Great Lakes countries. There are many impediments to trade in the region. For example, on the Uganda-South Sudan border, Ugandan traders persistently complain about mistreatment and the arbitrary introduction of new regulations. The absence of institutions to support trade is the main reason that a high proportion of trade between the countries is informal. To facilitate improved arrangements and better outcomes, Uganda should strive to broker good relations between the different countries in the region.

Figure 16: Potential Market for Uganda's Products Could Expand by 50 percent, as Sudan Becomes Largest Trading Partner During 2000s



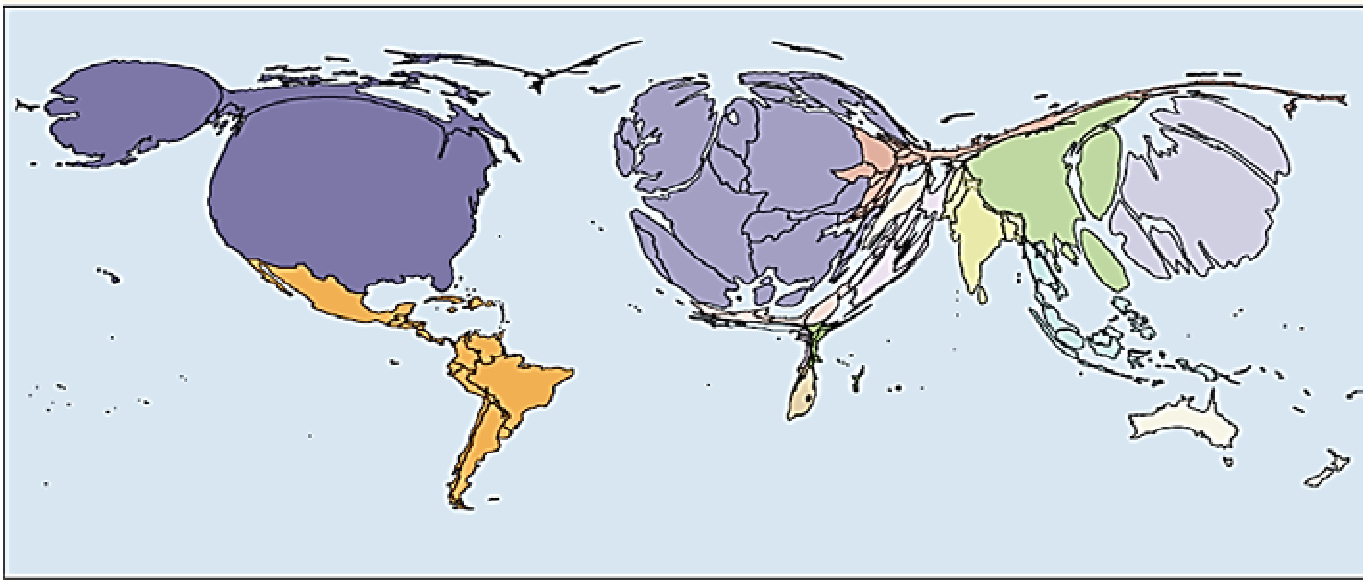
Source: World Bank staff calculations with WDI data, and Yoshino, Ngungi, and Asebe (2012), with UBOS data

Uganda's strong participation in the regional market creates increased opportunities for a higher level of trade with larger global markets. With the total value of the EAC regional market, excluding Uganda, standing at US $65 billion, existing potential is limited because of the relatively small size of this market. By way of illustration, the total value of this market is equivalent to 3.5 percent of India's GDP, which stood at US$ 1800 billion by 2010.

A market in Juba, a destination to Uganda's food and manufactured exports, (Great Lakes Film Production Ltd), November 2012

In fact, from a global perspective, the economic weight of EAC, the Great Lakes market or even the entire African market is quite limited (see Figure 17). Therefore, the regional market can be seen as a stepping stone to reach larger markets, even for prospective investors in the region who wish to take a long-term vision of markets. From a policy perspective, the isolation of regional markets is not an option. Rather, it is important to pursue policies that can minimize the disadvantages for small landlocked Uganda. These policies should include measures to reduce distance through the development of better infrastructure connectivity and better transit management and to facilitate labor mobility to support the density and efficiency of economic activity.

Figure 17: Global Perspective Dwarfs Regional Markets as Uganda Expands Trading Space



Source: World Development Report 2009

4.2 Uganda's Products: Survive, Diversify and Grow

Uganda must continue to harness its agricultural potential, given the importance of the agricultural sector to the country's trade. However, the full benefits of regional trade will be derived from deeper diversification into non-agricultural products, particularly non-traditional service exports. Uganda's goods and services have become more diversified as local firms became more competitive. This has resulted in an increased volume of non-traditional exports, such as processed fish, flowers and foodstuffs such as grains. Uganda's goods exports sector is dominated by agricultural produce (vegetables, animals, and foodstuffs), which constituted 85 percent of total exports in the period from 1996 to 2010. During this period, the contribution of vegetables to total exports dropped from 75 percent to 51 percent, while the share of other foodstuffs and livestock increased. There is still a relatively high degree of concentration, with exports of the top 10 products accounting for 60 percent of the total. However, increasingly, the most important exports include nonagricultural produce, such as cement. At the same time, trade in services has experienced a strong rate of growth, largely due to the boom in services and other than traditional transport and travel services.

4.2.1 Agriculture: Leveraging Uganda's Position as the Breadbasket of Eastern Africa

Uganda has natural comparative advantages in the form of good weather and fertile soils that support the cultivation of a range of crops and livestock. On the basis of these advantages, the country can achieve further export diversification through the development of a range of agricultural exports. Uganda's flexible climates and fertile soils support the cultivation of a range of food crops, particularly cereals and year-round drought-resistant crops. With its ability to produce a surplus of cereals for export to deficit regions, Uganda has been referred to as EAC's "food basket". In Eastern Uganda, where the cultivation of bananas and cassava ensure domestic food security, maize exports to chronically food-deficient Kenya thrive.20 In the period from 1996 to 2010, Uganda's export of agricultural products (vegetables, animal, and foodstuffs) constituted 85 percent of total merchandise exports. Of its agricultural products, Uganda had the highest rate of revealed comparative advantage for foodstuffs and animals. With the share of these products to total exports increasing, the share of vegetables declined. As the global economic crisis resulted in a decline in global demand, Uganda actively engaged in trade within the region in industrial cash crops and food staples. It conducted this trade both across borders and through the World Food Program, for which Uganda is the largest source of locally procured maize in Africa. With no established suppliers for maize, sugar, oil, or ready-to-eat meals in South Sudan, this country had to import more than 200,000 tons of grain in 2011. By 2011, 56 percent of Uganda's regional exports through customs were agricultural or agro-processed products. Of these exports, 60 percent were comprised of foodstuffs, particularly animal products, vegetables and vegetable oils and fats, and cereals. This percentage increases dramatically when informal trade is included. By contrast, only 7.6 percent of Uganda's imports from the region consist of agricultural produce.

However, relying on natural advantages alone will be dangerous for Uganda. Rather, the country needs to increase agricultural productivity and to reduce or eliminate production-curtailing regulations in order to beat competition. Uganda is not the only food producer in the region. Tanzania also often produces a food surplus: of 1.1 million tons of maize produced in Tanzania during 2011, approximately 100,000 tons were exported to the region. South Sudan, with similar vegetation and climate to northern Uganda, has the potential to grow its own food. To some extent, it is realizing its potential, as can be seen from its reduced level of imports from Uganda since 2011. Northern Zambia, Northern Mozambique, and South Africa are other food surplus producers in the region.

F**or Uganda to retain its market share, it must improve productivity.** In this regard, measures to protect domestic markets would have detrimental effects on producers and on longer term prospects for competiveness. As an example, in July 2011, when Tanzania imposed a food export ban, maize price in Dar-es-Salaam declined to US$ 284 per ton, while at the same time, Nairobi was paying almost twice the price (US$ 513 per ton), reducing incentive to produce for Tanzanian farmers. Unlike Kenya and Tanzania, Uganda had maintained a free market environment and agricultural prices were "just right". As a result, Ugandan producers received the highest pass-through of prices from the international markets in Africa, with margins reflecting competitive costs rather than resulting from government regulations. However, recent measures by the Ugandan government to ban processed maize so as to encourage value addition could create disincentives for producers in an environment where agro-processing capacity is low. At the same time, trade in food in the region remains far from free, despite efforts to achieve harmonization in policies and the regulatory environment. Despite these efforts, the arbitrary and erratic imposition of barriers undermines private sector confidence and distorts incentives, encouraging the production of cash crops while discouraging the production of food staples.

Increased trade within the region should not necessarily result in increased volatility in food prices. To prevent this, weaknesses in production structures need to be eliminated through measures to achieve a higher level of productivity and improve transportation and logistics systems. With international food prices peaking in 2009, Kenya and South Sudan responded by revising sourcing strategies, shifting focus onto Uganda where prices were relatively low. Huge price differentials, to the magnitude of 400 percent for maize or 200 percent for beans between Juba and Gulu in Northern Uganda, or 100 percentage points between Kampala and Nairobi, underpinned the food trade boom. With unstable supplies, prices for a number of foodstuffs, especially beans, have become very volatile. Uganda could enhance the productivity of its agricultural sector and improve transportation and logistics infrastructure to maintain and enhance its level of competitiveness.

With expanding populations, rapid urbanization, and increasing incomes across Africa, the potential demand for agricultural exports is virtually endless. The imbalance in food production endowment creates opportunities for Uganda as integration of regional trade links farmers to consumers across borders and mitigates the effects of periodic national food shortages and increasing global prices.

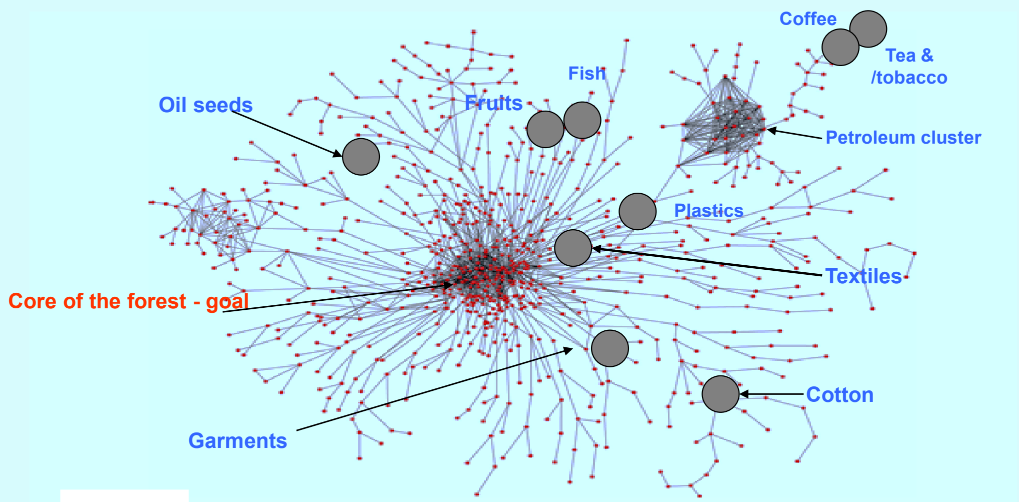
4.2.2 Climbing the Value Chain by Developing Capabilities

Uganda can export products of higher value, building on those it is already exporting within the region. Making the transition from low to higher value exports requires Uganda to build production capabilities

20 World Bank (2012), Africa Can Help Feed Africa: Removing Barriers to Regional Trade in Food Staples, Washington DC.

and capacities. However, for this to occur, Uganda's current exports must be close to a number of products already being produce by others elsewhere in the world (see Box 5).[21] By leveraging existing value exports, such as low and medium technology manufactures, Uganda can establish the basis for increasing vertical specialization. This will enable Uganda's participation in regional production chains, where trade in parts and components ("trade in tasks") may present a great opportunity. Like the spice seller who made the transition from being a producer of vegetables to selling processed spices, Uganda can build the capabilities it requires to export high value products.

Box 5: Uganda Can Move to Higher Value Exports – the Product Space View



. *Network representation of the product space. Layout uses a force spring algorithm.*

Source: Hidalgo, Klinger, Varabais, 2007

According to of Hausmann and Klinger (2006), the possibilities for export diversification in any country can be mapped in the product space. The product space is like a forest of all possible products that countries export. Each product is like a tree and a firm or country that produces the product is like a monkey located on its tree. Firms can jump from one tree to another, depending on their capabilities.
The red nodes represent a product. Similar products form a cluster. Some clusters such as those of coffee, cocoa, tea and tobacco are relatively far from the core of the product space. But products in clusters at the core are usually manufactures and make it easier for a country to jump from one to another, expand to other manufactures. Few cotton exporters export textiles or garments (distance is long). But many textiles exporters also export garments (distance is short). Uganda's manufactured exports: plastics, iron and steel products, processed foods, and fruits, place Uganda closer to the clusters.

Why shouldn't Uganda look at possibility of producing motor vehicle parts or toys (i.e. unsophisticated plastic based manufactured goods) that are being imported into the region today?

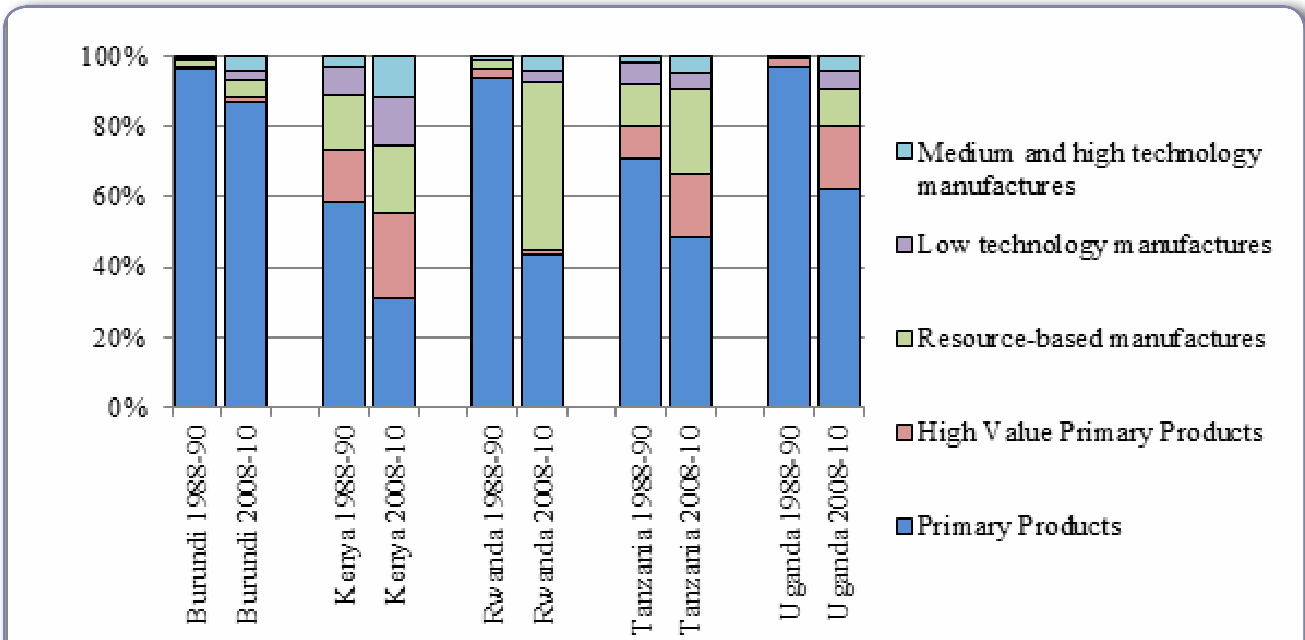
Uganda already exports manufactured produce such as plastics, iron and steel, chemicals, paints, cosmetics, construction materials, pharmaceuticals, and processed foods. It can leverage its position to export other products of similar and substitutable or adaptable capabilities. Amongst the EAC countries, Uganda has been the fastest to make the transition to higher value exports (see Figure 18). When informal exports are included in the equation, the degree to which it has made this transition becomes even more pronounced, as most ofthe informal trade

21 Hausmann R and B. Klinger (2007), The Structure of Product Space and the Evolution of Comparative Advantage, CID Working Paper No. 146, April 2007. According to this model, changes in the revealed comparative advantage of nations are governed by the pattern of relatedness of products at the global level.

involves industrial products.[22] Uganda can leverage existing exports as an entry point to higher value export products. Having particularly good potential are resource-based/agro-industrial products, with Sudan and DRC representing significant opportunities as markets. However, Uganda has the potential to exploit other products of similar and substitutable or adaptable capabilities. For example, Uganda already produces plastics and steel products. It is certainly conceivable that it could leverage these capabilities to produce motor vehicle parts and other higher-value outputs. Across the entire region, driven by external factors, the opportunities for import substitution are expanding fast. With rising labor costs, China may not retain its competitive advantages as a producer of toys or other similar low value manufactured goods beyond the next 10 years. Why can't the plastic that Uganda uses to manufacture jerry cans today be used to create products that substitute for Chinese plastic imports, thereby expanding regional markets?

With the rising regional demand for manufactured goods, Uganda has the potential to compete with more industrial Kenya. Uganda may have a lower competitive edge[23] in manufactured goods, compared to Kenya, partly because it is far from the coast. This will need to be addressed through improved connectivity to reduce the cost of imported inputs and through reducing the cost of doing business in Uganda. This will enable the country to compete with its coastal neighbors, especially for a larger share of the regional market.

Figure 18: Within EAC, Uganda and Rwanda Have Transformed Export Structures Fastest



Source: WB staff calculations based on Lall (2000); using mirror export data from Comtrade/WITS

4.2.3 The Services Sector: Where Uganda's Landlocked Status Doesn't Matter

Landlocked countries such as Uganda can overcome the disadvantages implied by their landlocked status by exporting services. In terms of accessing global markets, transportation costs will always represent a comparative disadvantage for manufacturers located at great distances from maritime port facilities. However, this disadvantage does not apply or is greatly diminished for the export of services, especially if their export is facilitated through distance-reducing technologies including mobile platforms. Uganda could be a regional hub to the Great Lakes region for the provision of services, including financial, back office functions, legal, construction, equipment leasing, medical and bio-tech research, insurance and

22 Some of the industrial products are re-exports from Kenya and China, but over 60 percent of informal exports are Ugandan made, including plastics, cement, and iron sheets

23 Kenya is at a higher level of industrialization than Uganda and hence produces most industrial goods more competitively than Uganda.

24 Paul Collier, "Uganda's structural transformation" Paper delivered at the launch of the Country Economic Memorandum 2007, September 22, 2007

trade logistics services.[24] In addition, if Uganda opens up to the import of services, this will increase the level of competition and result in the more efficient servicing of other sectors of production.

Services constitute the largest share of economic activity in Uganda and have driven the transformation of its production structure. However, Uganda still imports more services than it exports. By FY12, services accounted for 45 percent of Uganda's GDP, making it the fastest growing sector since 2002. The level of export of services has increased by 19 percent per annum over a decade, a rate exceeded only by Rwanda's, where the rate of increase stood at approximately 25 percent. By comparison, the rate of increase in Kenya was 17 percent, while in Burundi and Tanzania it stood at 15 percent. Currently, the total value of Uganda's export of services is equivalent to 9 percent of its GDP, which is three times the level at the beginning of the decade. However, the total value of its import of services in proportion to GDP has doubled to almost 14 percent over the same period, which means that the country is still running deficit services account. To achieve its full potential, Uganda must seize the opportunities created by its strong services sector. In particular, it must leverage the potential of tourism, transport and logistics, education and business services.

Table 4: A Snapshot of Uganda's Services Trade, 2010

US$ millions (and percent of total)	Exports	Imports
Commercial services	983.5 (75 percent)	1809.3 (98.6 percent)
Transport	3.7 percent	54.6 percent
Travel	55.7 percent	13.6 percent
Communications	2.3 percent	0.9 percent
Construction	..	..
Insurance	0.9 percent	12.0 percent
Financial services	1.7 percent	6.8 percent
Computer and information	3 percent	1.8 percent
Royalties and license fees	0.3. percent	0.2 percent
Other business services	7.6 percent	15 percent
Personal, cultural and recreational services	..	..
Government services	326.5 (24.9 percent)	25.9 (1.4 percent)
Total	1310.1	1835.1

Source: IMF BOP 2012.

Note: Government services includes transactions in both goods and services by international organizations, embassies, or military units and their staff in the host countries

a) Tourism: Why Don't More Tourists Visit Beautiful Uganda?

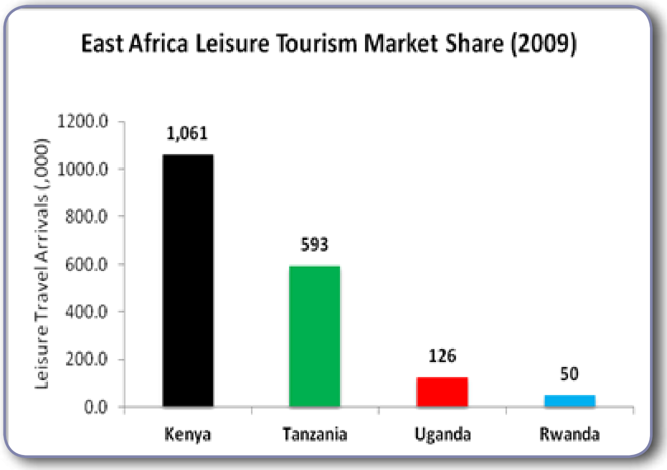
Given Uganda's large endowment of vegetation, rivers, lakes, mountains and wildlife, the fact that the tourism sector contributes a mere 3.2 percent to GDP should be considered a national embarrassment. With the number of international travel arrivals more than quadrupling in the 2000s, the sector contributed US $1.1 billion to the economy in 2012. However, less than half of this was direct tourism earnings, implying Uganda takes a meager share of the East African market for tourism. Despite a resource endowment that should facilitate its ability to create potentially highly valuable products such as wildlife safaris, primate tracking, adventure tourism, bird watching, cultural tourism, mountain ranges, and source of the Nile tours, Uganda earns only around US$ 800 million a year from such activities, lagging far behind

The Gorilla, one of Uganda's tourism attractions, (Great Lakes Film Production Ltd), November 2012

Kenya (US $3.8 billion) and Tanzania (US$ 3.4 billion) (see Figure 19).

To develop the potential of the tourism sector, it will be necessary to focus on improving human resources, implementing conservation measures to protect wild life and its habitats, developing a sound marketing strategy, and on building tourism infrastructure. The priority for the government is to facilitate the development of the necessary supporting infrastructure, while other challenges might be addressed through private-public partnerships. By far the largest potential market for tourism lies outside the region, but regional initiatives, including the development of multi-country tour packages, could help Uganda tap into this market more successfully. Uganda should also leverage its competitive edge in education services (see below) by organizing high level conferences and seminars, which will further benefit the tourism sector.

Figure 19: Uganda's Meager Share East African Tourism



Source: World Bank Sub-Saharan Africa Tourism Database (2012)

Note: Figures were taken for 2009, the last year for which complete data sets are available for all four countries; Burundi is not included, as the country has not published official arrival figures since 2006

b) Transportation and Logistics: Making the Land Bridge Pay

Uganda's central position in both northern and central corridors needs to be developed more zealously. The country must serve as a bridge to connect the traditional EAC group with a larger trading zone. At present, exports to South Sudan go through Gulu, either directly from the Kenya-Uganda border or through Kampala, rather than through the traditional Kenya-Juba route where insecurity affects the Lokichoggio-Juba segment. Similarly, traders prefer to keep their goods in bonded warehouses in Kampala to shorten delivery times into Juba. Not only have transit volumes grown, but also a distribution industry has emerged in Kampala and Jinja. Similarly, on the transit hub through the Northern Corridor linking Rwanda, Burundi, and Eastern DRC with Kenya, only the weakness of the Central Corridor through Tanzania allows Uganda to retain its competitive edge in the provision of transit services for Rwanda and DRC.

To develop Uganda's role as a land bridge, it is vital to develop its transport and logistics sectors, enabling the country to minimize its imports of these services and to export them to other landlocked countries in the region. At present, Uganda's export of transport and logistics services contributes to only 3.7 percent of its total export of services. At the same time, such services constitute 55 percent of its total import of services, with the greatest proportion of these imports coming from Kenya. While the expansion of regional trade creates opportunities for Uganda in terms of its role linking coastal countries, particularly Kenya, with inner-land landlocked neighbors (South Sudan, DRC, Rwanda, Burundi), the main transit road remains in a poor state and logistic services are undeveloped. The Kampala-Nimule-Juba road is the main corridor between Uganda and South Sudan. However, because more than half of this route is in poor state, some imports go through Oraba-Kaya for Juba. Improvement of the Nimule-Juba road (funded by USAID) is expected to greatly facilitate the flow of traffic.

In order to achieve the optimal development of the growing transit and logistics industry, Uganda must be able to provide excellent logistics and transit services. With stability restored in the border area between Kenya and South Sudan and with Kenya recently announcing its intention to develop the Sudan-Kenya corridor with support from EIB through the EAC Secretariat, Uganda must invest in infrastructure connectivity and trade facilitation to maintain its competitive edge, the shorter distance on the alternative routes notwithstanding. Moreover, the recent establishment of the Common Market for Eastern and Southern Africa free trade area (COMESA FTA) has increased Uganda's potential to serve as a transit hub between and among Sudan, Kenya, Rwanda, and Burundi. Thus, Uganda should strive to facilitate a harmonization of border policies and regulations and to address behind-the-border regulatory issues within all these countries to tap this potential market.

c) Education Services: Meeting the Needs of Foreign Students and Developing Uganda's Human Resources

There has been a dramatic growth in Uganda's exports of educational service. This growth can be sustained if Uganda works to raise awareness and to ensure that the services it provides meet the needs

Nimule Juba road constraining traders, (Great Lakes Film Production Ltd), November 2012 of non-Ugandans in terms of regulations, curriculum, and recognition of the qualifications. The dramatic increase in Uganda's export of educational services (see Box 6) has been driven by the reputation of the country's education system; the liberalization programs initiated in the 1990s; and the relative affordability of Uganda's educational services compared to regional and international institutions elsewhere. While private sector participation has helped to drive the increase in these exports, a number of significant constraints have prevented Uganda optimizing the benefits of such exports. These include a lack of awareness of the business and export opportunities, lack of a well-defined regulatory framework, inadequate marketing programs, inadequate learning facilities and limited access to ICT infrastructure, limited measures to adapt the national curriculum to international standards, and limited recognition of academic qualifications abroad.

In order to optimize the benefits to be derived from the export of educational services, the government must commit to implementing Uganda's National Export Strategy of 2007. The stated aim of the strategy is to transform Uganda into "a center of excellence for quality and affordable education in the region and beyond". Despite these laudable sentiments, five years after its adoption, it has not yet been implemented.

Box 6: Education Service Export on the Rise

Over the past decade, Uganda's education system has attracted increasingly large numbers of foreign students. While this trend is also apparent at the secondary school, it is particularly true for university education. With a total of 29 universities, 24 of which are privately-run, the total number of Uganda's University students increased by 3.4 percent, from 137,190 in 2006 to 183,985 in 2010. The number of foreign students rose from a few hundred in the early 1990s to 6,000 in 2008, then rapidly increasing to 16,000 in 2010. The contribution from these sources to educational service exports is estimated to reach a value of approximately US $ 35 million.

The greatest number of foreign students is from Kenya, with others from Rwanda, Tanzania, Sudan, Burundi and the Democratic Republic of the Congo. Beyond the East Africa region, there are also a small but growing number of students from other neighboring countries, including Somalia, Zambia, Angola and Zimbabwe. Kampala International University (KIU) has the largest number of foreign students, at 6,715 students. It is followed by the universities of Makerere (2,444), Bugema (862), the Islamic University in Uganda (767), the Makerere University Business School (MUBS) (671), and the Busoga University (575).

International students are mostly found at private universities, with many public universities lacking the capacity to accept international students. For many private universities, the international student market is a new market segment. The main comparative advantages of these educational services are affordable tuition fees, low cost of living, and the strong education system that offers a wide range of academic programs. The Uganda Exports Promotion Board (UEPB), working with 20 universities, is developing a strategy to exploit this niche in sub-Saharan Africa and to consolidate Uganda's position as a regional education hub.

Source: Commonwealth Secretariat and UEPB, 2012 and BOU

d)Business and Professional Services: Smart Money

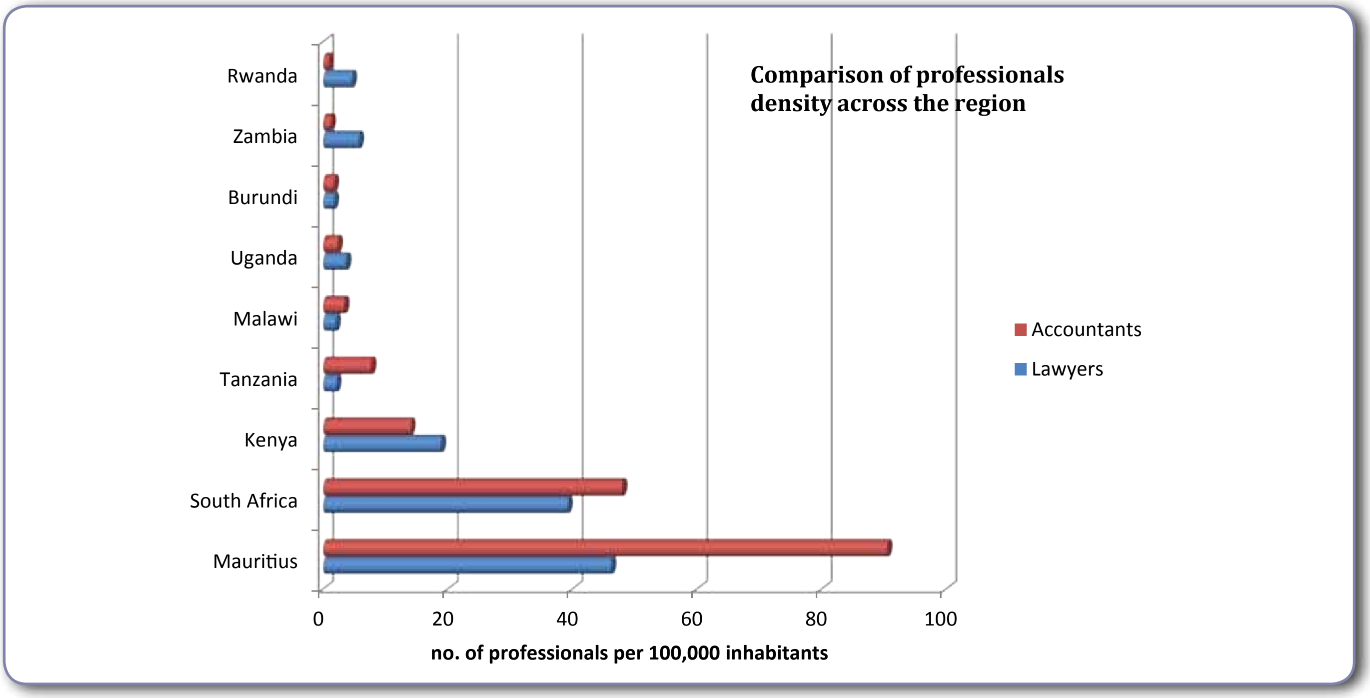
Uganda has taken the initial steps to establish trade links with other EAC countries to provide business services. Through such measures, there has been an increase in the volume of exports in virtual connectivity (computer and information technology, IT) and finance. The development of such services has been facilitated by increased rates of internet connectivity and the increasingly high level of penetration of mobile services. The most dynamic exports are in higher value-added sectors, such as information technology services and financial intermediation. The growth of the volume of exports in these areas in the period from 2004 to 2009 was more than 30 percent, compared to the rate of growth of 20 percent for services as a whole. In this area, Uganda faces strong competition from Kenya. However, even if its level of performance falls short of Kenya's, it could still gain a significant market share in this area.

In addition to exporting a significant volume of business services, Uganda is also a significant importer of such services. In particular, a large number of foreign professionals are employed in the area of accounting and auditing services, with the presence of these professionals helping to build the capacity of their Ugandan counterparts. In the period from 1994 to 2007, 17 percent of the health and social services and civil works implemented by the Rwandan government were undertaken by Ugandan firms. Over the same period, 23 percent of similar work implemented by the Ugandan government was undertaken by Kenyan firms. According to business surveys, more than 50 percent of legal services in Kenya are imported, while 25 percent are exported. By contrast, the figures for Uganda for the same services are 17 percent for import and 10 percent for export. For accounting services, Uganda imports 17 percent and exports 20 percent. The main export markets for these services are within East Africa and are related to intra-region trade. In addition, services are exported to DRC, South Africa, Mauritius, EU, China and India.

To increase the volume of exports of business services, Uganda must address the skills deficits of higher level professionals. It must also address overregulation that has in some instances segmented the domestic market. The government has declared its commitment to developing professional services as a matter of priority due to its potential to contribute to exports. Other priority areas identified by the government include information technology, education and construction. However, the development of all of these areas is constrained by a skills shortage, with a lack of highly skilled higher and middle level professionals in the legal and accountancy professions, amongst other areas (see Figure 20). In addition, undeveloped and segmented domestic markets and excessive regulation undermine Uganda's competitiveness. Skills shortages act as a constraint not only for the export of business services, but also for other types of services, such as business outsourcing. Under the common market, free movement of factors of production, most probably from Kenya's surplus market, could partially alleviate this problem.

Overall, despite private-sector efforts to develop exports, most service sectors remain undeveloped on account of existing barriers to entry. Despite dynamic growth rates, performance indicators for many backbone services in Uganda are below the level of their peers in the EAC, affecting competitiveness. Compared to its neighbors, Uganda has more significant restrictions to exporting services. In a recent World Bank survey of applied trade policies in five services sectors (banking and insurance, telecommunications, retail distribution, maritime transport, and professional services) in more than 50 countries, Uganda's overall restrictiveness index of applied services policies, which measures explicit market access and national treatment barriers in addition to selected discriminatory regulatory measures, is higher than its landlocked neighbors, Rwanda and Burundi. Reducing this at least to the level of these neighbors would be a key target to increase the volume of export of services (see Figure 32). The restrictions are most evident in the areas of retail, professional and financial services.

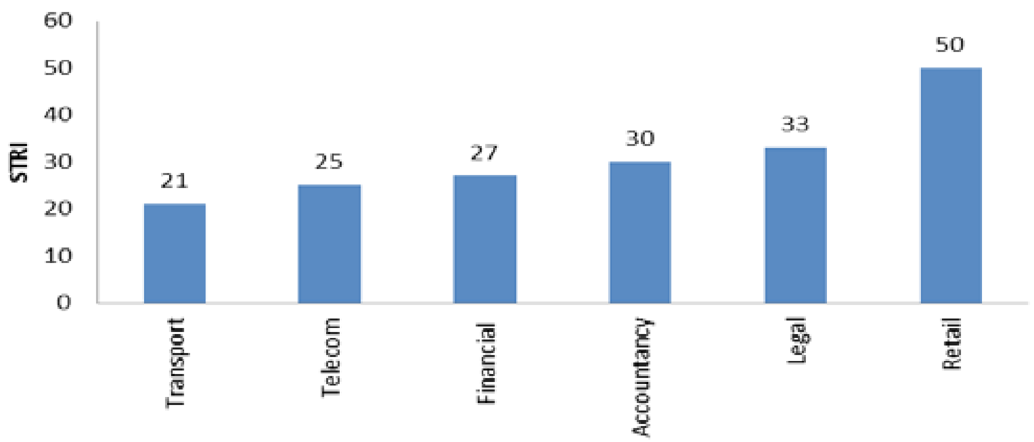
Figure 20: Uganda Still Needs Skills Capacity



Source: World Bank (2010) and Niyongabo(2011)

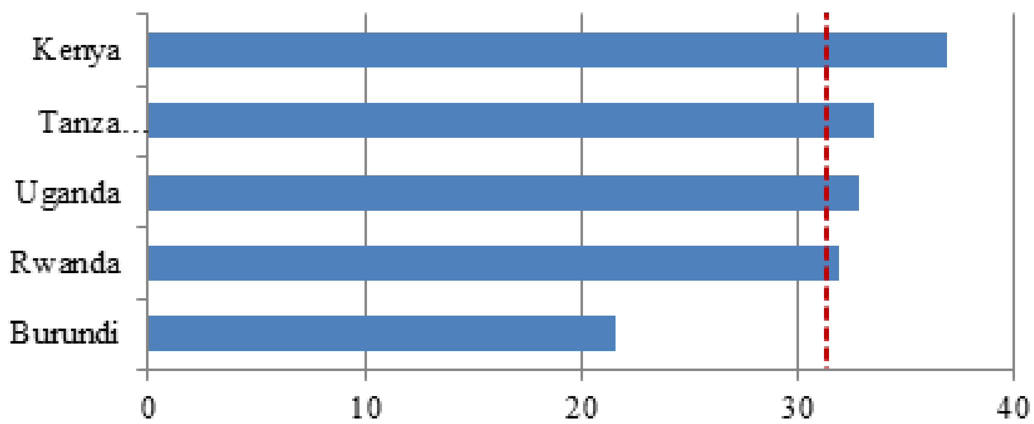
Furthermore, because of the large deficit in technical and institutional capacities, no coherent and effective regional integration policy has been formulated or implemented. Promoting the export of educational services will have wider spill-over effects, given that the skills deficit is a major constraint in many potential service export sectors. The education system needs to prepare itself not only to provide world class services that meet the needs of foreign students, but also to produce world class graduates that have the necessary skills to support the service sector, especially tourism and professional services.

Figure 21: Uganda's Services Trade Restrictiveness in Comparison to EAC Countries and Across Sectors



Source: Borchart, Gootiliz and Mattoo, "policy Barriers to International Trade in Servicves: New Empirical Evidence". World Bank, 2012

Note: STRI = Services Trade Restricveness Index. Sectoral STRI scores are averages across subsectors and modes of supply



Source: World Bank (2012), Services Trade Restrictions

5. Building Bridges to Deepen Regional Trade

It will not be easy for Uganda to harness the potential in regional trade. With the majority of constraints lying outside Uganda's borders, it must strive to raise productivity and deepen regional integration. Firstly, government policies should focus on facilitating the modernization and diversification of the agricultural sector to improve its productivity and competitiveness. Recent efforts to raise productivity include the special cluster-based interventions to raise production of key commodity exports, such as maize and beans, by improving access to improved seeds, fertilizers, mechanization and water for production. These efforts will also support Uganda's competitiveness as a food surplus producer. However, incentives for farmers to produce outputs in sufficient qualities and of sufficiently high quality, must be improved through pricing regulations that allow good quality to be rewarded appropriately. They must also be supported through the provision of better training and improved access to finance for farmers to improve cash flow management and to enhance access to ware-housing systems. Beyond raising productivity on the farm, issues related to storage, transport logistics, and connectivity must not constrain the movement of goods from farms to markets. With the majority of farms small and scattered, load consolidation could go a long way to improving access to markets.

Malaba Border post will need to maintain efficiency to support Uganda build land bridges to the other countries, (Great Lakes Film Production Ltd), November 2012

Second, for firms to diversify into a wider range of products, particularly higher value exports, constraints to investment must be addressed. Uganda's non-conducive legal and regulatory regime remains one of the greatest constraints against private sector growth. In the Global Competitiveness Index 2010, Uganda ranked 118 out of 139 countries measured, down from 108 in 2009. The country also performs poorly in the World Bank Doing Business (DB) report, ranking 123 out of 183 economies overall in 2012. In particular, the difficulties involved in establishing a business and acquiring licenses are among the major constraints affecting businesses. An improved business registration process could stimulate the formalization of MSMEs. In turn, this could reduce poverty through expanded employment, increase access by MSMEs to financial and technical services and increase tax revenue.

Beyond production, access to markets is crucial. Uganda should take measures to reduce transport costs, redress non-tariff barriers and remove barriers to services trade. Given that these measures will require cooperation with neighboring countries, Uganda must strive to promote deeper regional integration, which will provide a basis of cooperation.

5.1 Lower Transport Costs: The Key to Increasing Trade

Transportation costs remain a major challenge for land-locked Uganda. Uganda's transportation system remains characterized by poor roads, limited compatibility between different modes of transport, and poor logistics systems, including at ports of entry at Mombasa and Dar-es-Salaam. While Uganda is striving to improve trade logistics, high transportation costs resulting from poor infrastructure and logistics systems constrain the trade of goods and services and prevent Uganda from exploiting its revealed strategic position as a transit hub.[25] The high cost of transport is largely due to poor roads that are badly maintained, overloaded, and poorly managed. Trade logistics systems are characterized by high berth and yard congestion at ports, slow customs clearance at some border posts that have not been modernized, excessive dwell times for ships, limited compatibility between different modes of transport, low quality of services, low operating efficiency, and ineffective regulation. High transport costs also constrain production.

5.1.1 The Vital Need for Revamped Infrastructure

Being in poor condition, both the Northern and Central corridors that connect Uganda to coastal regions are expensive to use. Cost inefficiency is exacerbated by poor governance, organizational deficiencies, revenue inadequacy, and underinvestment, all of which have led to deficient and dilapidated regional infrastructure networks. The Ugandan trader faces freight costs that are 30 percent higher than their counterparts in Southern Africa and 60-70 percent higher than their counterparts in the United States and Europe. For landlocked Uganda, transport costs can constitute up to 75 percent of the value of exports.

The Northern Corridor is shorter and more competitive that the alternative Central route. However, with the lack of efficient railway services, it is still expensive by any international standard. Connecting Kampala to Mombasa in Kenya, the Northern Corridor is about 500km shorter than the only alternative route through Northern Tanzania to Dar-es-Salaam port. It has three modes of transport: the Mombasa-Malaba-Kampala highway; the railway; and a multi-modal water/rail route connecting Mombasa to Kampala through Kisumu and Port Bell or Jinja. Presently, with the relatively good condition of roads and plans for further rehabilitation, road transportation is the preferred option. Such transportation provides the quickest link to Kampala. Ideally, rail transportation would be a more efficient long haul transport mode to connect landlocked Uganda to the coast. However, limited rail transportation capacities have led to a modal shift towards road transport, which costs far more than a well-managed rail transportation system would. The transportation costs for containerized imports to Kampala are on average US$ 2500 per 20ft container for road transport, compared to costs for rail transportation of US$ 1920. Rail rates are not necessarily cost-based, but are priced just below road transport. This is because rail transport does not have current surplus capacity. Overall, transport prices of about US$ 0.08 per km compare unfavorably with the cost of US$ 0.06 per km between Durban and Lusaka, US$ 0.05 per km in China, and US$ 0.04 per km in USA.

Use of the lower cost rail transportation system has remained limited because the service is slow and unreliable. This results in a costly imbalance between import and export trade. Only 16 percent of Uganda's trade is transported using the rail/water alternative on this corridor, given the lack of services. Apart from the slow rehabilitation of the network, since the joint concession Uganda-Kenya Railway began operations in mid 2000s, the bulk of the remaining wagons operate in Kenya. Indeed, while merchandises take less than 24 hours to move from Mombasa to Nairobi, they take an additional 7 days to get to Kampala, with water transportation services through Lake Victoria being very limited. New high-value non-traditional exports are transported out by air. However, the aircraft used to facilitate this transportation arrive half-empty, meaning the cost of air freight is borne disproportionately by exporters. On the other hand, trucks are often empty or carry less than their

25 The World Bank's Logistics Performance Index (LPI) is a benchmarking tool to help countries identify the challenges and opportunities they face in their performance on trade logistics, based on a worldwide survey of operators on the ground - global freight forwarders and transporters. It is based on a survey of nearly 1,000 logistics professionals (international freight forwarders) across 155 countries to assess status of trade logistics, including customs efficiency, infrastructure quality, ability to track and trace shipments, timeliness in reaching a destination, competence of the domestic logistics industry in the country, and the ease of arranging and managing international. Uganda moved to 66th position out of 155 countries surveyed in 2010.

full capacity on the route to Mombasa, meaning that the cost of the two-way trip is borne by importers.

The Central Corridor alternative could be more competitive. However, this requires cheaper water transportation services on Lake Victoria and more efficient railway services to support a more efficient multi-modal regional transport system. At present, only 2 percent of Uganda's international trade uses the Central Corridor. In fact, the dependency on a single transportation route could render trade vulnerable to unexpected events, as demonstrated by events during Kenya's post-election violence in 2008. The additional distance involved in the use of the Central Corridor need not necessarily render it uncompetitive. Factors such as shipping and line connectivity, the availability of return loads, and short border crossing times are vital in determining trader references in this regard. With the right supporting factors, the Durban-Lusaka Corridor in Southern Africa is 2400km long but is preferred to other, shorter routes to ports in Mozambique. The Central Corridor could also be competitive, distance notwithstanding, if Dar-es-Salaam port becomes more efficient and if road conditions improve. However, the most critical factor is the establishment of reliable water/rail services. In addition to the recent commissioning of the MV Kaawa, RVR's plans to rehabilitate carriers, wagons and locomotives, is a move in the right direction.

Uganda's role as a land bridge and transit point is also highly dependent on the quality of the two corridors. Being positioned at the central point on both corridors, Uganda will benefit from improved connectivity. Improved connectivity will enhance Uganda's potential as a transit point between markets in the Great Lakes region and markets and port facilities in the coastal areas.

Beyond the trade corridors, limited connectivity between areas of production and markets within and outside the country remains a major constraint to producers. The poor quality of roads in Kampala acts as a significant constraint against the efficient transportation of goods and agricultural products transiting the capital and against production and processing in Kampala. With feeder roads in a sorry state, high transportation costs are one of the major beyond-the-farm gate constraints to productivity and commercialization (World Bank 2012).[26]

26 World Bank 2012, Uganda Promoting Inclusive Growth – Transforming Farms, Human Capital and Economic Geography

The government's effort to improve road infrastructure on the main trading corridors is commendable. However, it must also strive to develop a multi-modal transportation system to reduce logistical costs. The government has made the rehabilitation of the national roads that form an integral part of the corridors a top priority. The Kampala-Masaka-Mbarara-Kabale-Kisoro corridor has just been completely rehabilitated, while the Kampala to Malaba road is due for rehabilitation and expansion through the development of an express highway that will improve trade traffic flow. Despite these initiatives to support regional trade, the Ugandan government must address the following:

a. **Road transportation:** It is vital to ensure connectivity with areas of production. The establishment of connectivity across Uganda's borders will need to involve regional cooperation. The national roads that are part of the corridors must be prioritized for rehabilitation and maintenance, while connectivity between producing areas and markets has to be improved to boost agricultural exports. Beyond its borders, Uganda must negotiate with its neighbors to ensure that roads servicing the corridors are maintained. This should entail upgrades of road capacity through the addition of lanes to roads with heavy traffic; the rehabilitation of paved roads whose poor condition affects the flow of traffic along the corridors; and the upgrading of key feeder roads connecting producers to the corridors from gravel to paved standards.

b. **Rail transportation:** In the short to medium term, action must be taken to make rail/water transportation systems more viable. With transportation costs almost doubling the price of transported goods, the development of the railway transportation system makes economic sense for traders and consumers. It also makes long term economic sense as the most viable basis for regional connectivity. The EAC has already decided to install a standard gauge, with the system extending beyond the EAC to other African countries including Ethiopia, Somalia, Zambia and Malawi. As these plans progress, the rehabilitation of existing lines will be critical to support regional trade over the next 5 to 10 years.

c. **Water transportation:** Rail transportation can be made even more efficient if combined with well-developed water transportation systems. Given the huge untapped potential of Lake Victoria, improving transportation on the lake by refurbishing wagon ferries is an important measure. The government must support measures to enable the private sector to develop facilities and offer services in the medium to long term, with public procurement of roll-on roll-off facilities on Port Bell vessels and load-on/load-off facilities at Mwanza and Port Bell to ease connectivity between water and other modes of transport.

Since infrastructure investments can be costly, financing this infrastructure development strategy without a financial market will be a significant challenge. Before oil resources increase the government's available revenues, one means of overcoming this challenge could be through the use of PPPs. However, when the oil revenues begin to flow, the careful prioritization of investments will be even more important if the country is to boost regional trade and maximize returns.

5.1.2 Beyond Infrastructure: The Hidden Costs of Under-developed and Dysfunctional Logistics

Uganda must undertake strategic investments to close gaps and constraints across the entire transport chain. These investments must address pressing constraints affecting the trucking, freight and storage industries. Transportation in Uganda is expensive because of bad infrastructure, congestion and taxation policies. With 4 of the top 10 taxed activities being in the transport sector, taxation places a heavy burden on agriculture and on regional trade. Vehicle operating costs account for 50 percent of transport costs in Uganda. This is significantly higher than in most countries, with the international average running at around 30 percent due to high fuel costs, with the high cost being largely due to high fuel taxes and inefficient fuel use. In turn, the average age of the vehicle fleet exacerbates inefficiencies. Transporters tend to import older and less fuel-efficient vehicles, because the cumulative burden of import duties and withheld VAT makes the importation of newer vehicles uneconomic. [27]

Ugandan traders continue to import a significant proportion of trucking services from Kenya and Tanzania. This is mainly because Uganda's trucking industry is constrained by the country's taxation and transport policies and by regional infrastructure access fees that put Uganda's truckers at a disadvantage. On the Central Corridor, 50 percent of the trucks are Tanzanian-registered. On the Northern Corridor, approximately 90 percent of the trucks are Kenyan-registered. While there are no direct restrictions in the Tripartite Agreement that governs road transport, Uganda's trucking industry is heavily constrained by high operational costs resulting from the countries transportation policies and by infrastructure access fees, which favor coastal countries. In 2011, a move to standardize the fee for the 'transit goods' license at US$ 200 per annum across EAC countries and to facilitate mutual recognition helped Uganda's trucking industry. However, additional country-specific charges remain. For example, Tanzania imposes a US$ 20 per truck entry fee, a US$ 5 fuel tax, and a road user fee of US$ 10 per 100 km. In addition, a large number of informal charges are imposed, as in the case of weigh bridges, which are more prevalent in Kenya and Tanzania.

Secondly, if Ugandan trucking businesses were to engage in the more lucrative import business, they would still receive lower margins, given that with the low volume of exports, vehicles en route to ports in Mombasa and Dar-es-Salaam would be mostly empty. Operators would also face much higher fuel costs. Internal taxation policies and a harmonization of infrastructure access fees are required in order to make running a freight business from Uganda more competitive.

Freight forwarding businesses are constrained by difficulties in the establishment of customs bond guarantees; the low level of ICT access; and the lack of an accreditation system. With bonds organized on a national basis, cooperation between forwarders in both transit and destination countries is required. For the majority of small freight forwarders, who account for more than 80 percent of the registered association members in Uganda, this issue is a real constraint, resulting in increased operating costs. Because of the lack of regulation at entry, facilities for submitting customs documents are poorly developed and badly managed. Private sector associations, including transporters' associations (such as the Tanzania Truck Owners Association and Uganda Truck Owners Association), freight forwarders (such as the Tanzania Freight Forwarders Association), chambers of commerce and others, can contribute to the development of these logistic services. Recently, the government, clearing and forwarding agents and major importers in Uganda came together to establish the Uganda Shippers Council. The council seeks to support cargo owners in the negotiation of freight rates and provides advice on international shipping. An interim executive committee has been formed and other institutional structures are being

27 World Bank 2007, Country Economic Memorandum Uganda Moving Beyond Recovery: Investment and Behavioral Change

established. At a more strategic level, there is need to better regulate freight services and to provide training in matters related to logistics for both government and private sector services providers in the trade facilitation industry.

If existing inland bonded storage facilities have a larger capacity and were more efficiently managed, they could attract a high volume of business through the hub. As part of Uganda's strategy to develop Kampala as a regional logistics hub, it is necessary to increase the number and capacity of bonded storage facilities. Presently, Uganda businesses own and operate storage facilities in Mombasa, Nairobi and Dar-es-Salaam. This indicates that the management of their inventories relies to some extent on coordination with operators in the neighboring countries. The availability of storage facilities largely influences the choice of routes and corridors for Ugandan trading firms. In fact, while enterprises with storage facilities in Dar-es-Salaam are more likely to use the Central Corridor, those with storage facilities in Mombasa and Nairobi prefer the Northern Corridor. Over the years, Ugandan clearing and forwarding agents have developed their own infrastructure or established relationships with businesses in Kenya to provide temporary storage facilities in Mombasa. However, the number of such relationships with Tanzanian businesses remains limited, although increased utilization of the corridor should encourage their development. Nonetheless, to reduce the reliance of trading firms on storage facilities in Mombasa and Dar-es-Salaam, the capacity of existing storage facilities in Uganda needs to be expanded and their management improved.

In some areas, progress has been made towards improving customs clearance and border management systems. However, such improvements need to be implemented at all border posts. When URA introduced the Malaba one-stop border post in 2009, border crossing times were reduced from 1-2 days to 1-2 hours. URA's improved risk management, the vetting of clearing agents and the streamlining of traffic and parking rules for truck drivers have decongested the customs-controlled zones. Nonetheless, the EAC Customs Management Act, which provides a basis for the full implementation of one-stop operations, has not yet been fully implemented. There are plans to develop a one-stop border post at Gatuna-Katuna (Uganda-Rwanda). However, similar plans need to be developed for other border posts across the region. Moreover, despite formal support for 24-hour operations, such operations are constrained by a lack of supporting services such as banking services, which means that goods arriving at the border outside normal working hours are not processed.

To improve trade logistics, the government should implement the following:

(i) Introduce a regional customs bond that would reduce the cost and time of transacting business. This will ease constraints on the freight forwarding business, particularly for smaller freight forwarders who make up a majority of such operators. An accreditation system would promote professionalism in an industry which is currently open to all, irrespective of the level of knowledge and skills of operators;

(ii) Improve market access and break down trucking industry cartels by renegotiating road-user fees with EAC partners. This may be politically difficult, but it is nonetheless a necessary measure;

(iii) Accelerate improvements in border operations at Malaba, Mutukula and Katuna and initiate improvements at other posts, including Nimule, Oraba, and Bunagana;

(iv) Improve border management through measures to facilitate interaction with strategic agencies in neighboring countries, including agencies in Rwanda, Sudan, and DRC;

(v) Increase the capacity of bonded storage facilities by supporting private investors in this area;

(vi) Reform regulations and institutions to enable transportation and logistics service providers to deliver high quality, competitive and efficient services along trade networks. Top priority should be placed on the regulatory reform of logistics services, including trucking, warehousing, customs clearing, and freight forwarding services;

(vii) Review taxation of the transportation sector in the context of Uganda's public finances, particularly if alternative sources of revenue could be found that would permit the reduction of the taxes on freight vehicle imports. Not only would this reduce capital costs, it would also serve to reduce operating costs by permitting the import of newer vehicles.

5.2 Non-Tariff Barriers: Stop NTBs from Undermining Trade Liberalization

Tariff reform has drastically reduced restrictive trade protection. However, numerous behind-the-border barriers in form of non-tariff measures (NTBs) continue to constrain intraregional trade. Adoption of the EAC Customs Union could have made Uganda's tariff regime more restrictive. However, this is not as significant a constraint for regional trade and hence not an immediate challenge (see Box 7). NTBs must be addressed if regional trade is to prosper.

NTBs inflate transport costs by causing long delays, the imposition of inappropriate payments and increased levels of uncertainty. Thus, NTBs work against the positive effects of trade liberalization and under-mine efforts to deepen regional trade. Whether NTBs take the form of restrictions relating to rules of origin, import/export bans, or costly import licenses (see Box 8), these barriers result in a high level of additional cost due to: (i) lost man-days during transit and clearance; (ii) non-official expenses related to corruption in policy implementation; (iii) official payments; and (iv) lost business opportunities. Differences in regulation and immigration procedures limit services. Sometimes procedures and rules in the different countries are caused by the limited dissemination of information on harmonizing regulations to all the implementing agents involved in cross-border transactions. It also appears that many NTBs could be sustained for protectionist purposes and to offset the negative impact of EAC tariff liberalization on member countries.

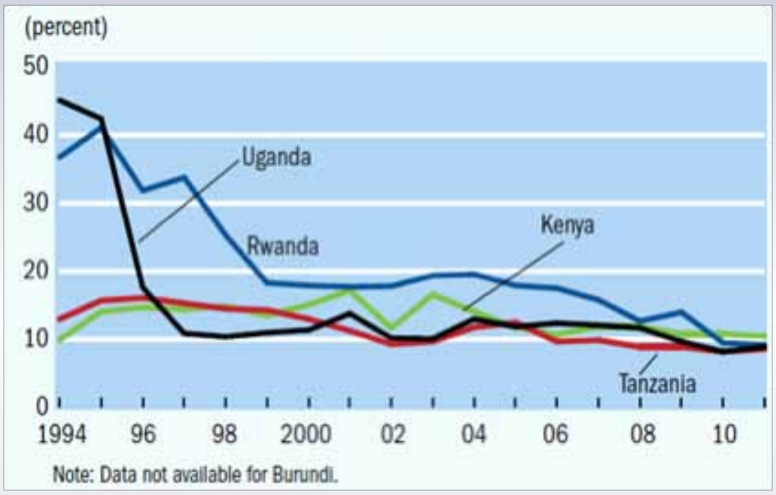
Due to these barriers, the prospects for the development of regional production chains driven by trade in parts and components ("trade in tasks") remain limited. The removal of such barriers would facilitate an increase in the volume of Uganda's existing exports, including the export of low and medium technology manufactures. It would also facilitate an increase in vertical specialization. Over the long-term, it could enable Uganda's participation in regional production chains that create employment opportunities and promote export diversification. Conversely, the removal of NTBs could also render domestic industries/services vulnerable to competition, at least in the short run. This may be compensated for by medium to long term gains, but it makes decisions on how to implement their removal sensitive. In light of such sensitivities, a gradual approach to their removal may be the preferred option.

A traffic jam as trucks wait to get onto the weigh-bridge on Mombasa Kampala road, delaying traders, (Great Lakes Film Production Ltd) November 2012

Box 7: Tariff Regime is not an Immediate Challenge

Uganda has dramatically reduced tariffs over the past two decades (see Box Figure 4.1). During the early 1990s, Uganda cut its trade tariffs by more than 75 percent. In January 2005, adoption of the EAC Common External Tariff (CET), which has three bands (0 percent, 10 percent and 25 percent for capital goods, intermediate goods and finished goods respectively), increased the highest rate from 15 percent to 25 percent.

Box Figure 4.1: Uganda Reduced Tariffs Faster than EAC Counterparts



Source: Winston and Castellanos, IMF 2011

Uganda's trade regime is more restrictive than before CET, raising questions whether it could have reduced efficiency of Uganda's trade policy and hence should reviewed. Uganda is ranked 116th out of 125 countries on the World Bank's Trade Tariff Restrictiveness Index.

Justification to review the tariff structure is distributional since the adverse trade effects of a higher tariff have washed away. The higher external tariff following CET adoption created some trade diversification, though there was also sluggish growth of tariff revenues, rising intra-EAC trade, and reduced growth of imports from outside EAC. However, these effects were not as big as would have been expected given the change in valuation to CIF Mombasa after the CET adoption, and simultaneous elimination of 4 percent withholding tax and 2 percent environment tax. Furthermore, the effects have weakened as firms seem to have gradually learnt to work with the CET through the CET remission system. CET remission distorts the market structure, but has also contributed to revenue losses). Customs firm level data suggests that by 2011, very few Ugandan firms importing from non-EAC countries were paying the CET – in FY11, these losses are estimated at US $ 147 million (equivalent to 7.3 percent of total revenues or 50 percent of budget support), the bulk of which under minerals and prepared foodstuffs. The firms benefitting from remissions are large firms, implying that the tariff structure promotes larger firms to export more and grow faster, but not small firms, which account for most Ugandan businesses. For the consumers, the CET remains as regressive as the tariff structure was earlier, as goods consumed by the poor pay the highest tariffs, raising the cost of living for the bottom of the income distribution by 12 percent, compared to 6 percent for the top (World Bank 2012).

Box 8. Non- Tariff Barriers: What are they?

Non-tariff barriers (NTBs) are any form of government or government backed non-tariff measures to protect a domestic market. Legitimate (e.g. food safety regulations to protect consumers), or otherwise (e.g. as substitutes to tariff to protect some domestic products), private-sector surveys have repeatedly shown that NTBs can raise trade costs, divert managerial attention, and penalize especially the small exporters and those located in low-income countries, where access to legal and regulatory information is difficult. The elimination of the NTBs that are applied in a trade-restrictive manner is a major dimension of multilateral and regional trade negotiations. This objective is explicitly stated in the EAC Customs Union Protocol (Art. 13) but limited progress has been achieved by member states since the establishment of the Customs Union.

A wide range of NTBs and regulatory measures restrict intra-regional trade in East Africa. These include restrictions relating to rules of origin, import and export bans, and costly import licenses. The main NTBs limiting intra-EAC trade concern the following categories:

1. Customs and administrative entry and passage procedures (number and effectiveness of institutions involved, arbitrary use of rules of origin, excessive verification of transit cargo, etc.). Complex, opaque and country-specific rules continue to add to monetary costs and loss of time. Unequal treatment according to the country of origin of the goods and/or truck and opportunities for fraudulent behavior remain frequent.
2. Government participation in trade and restrictive practices tolerated by it (ports and internal container freight station operations, delays at the numerous weighbridges and non-harmonization of authorized weight per axle, etc.).
3. Distribution restrictions (multiple police roadblocks causing delays and rent extortion, prohibition on transportation of locally produced goods by returning trucks, etc.).
4. Specific limitations (use of immigration and visa procedures, business registration, etc.).

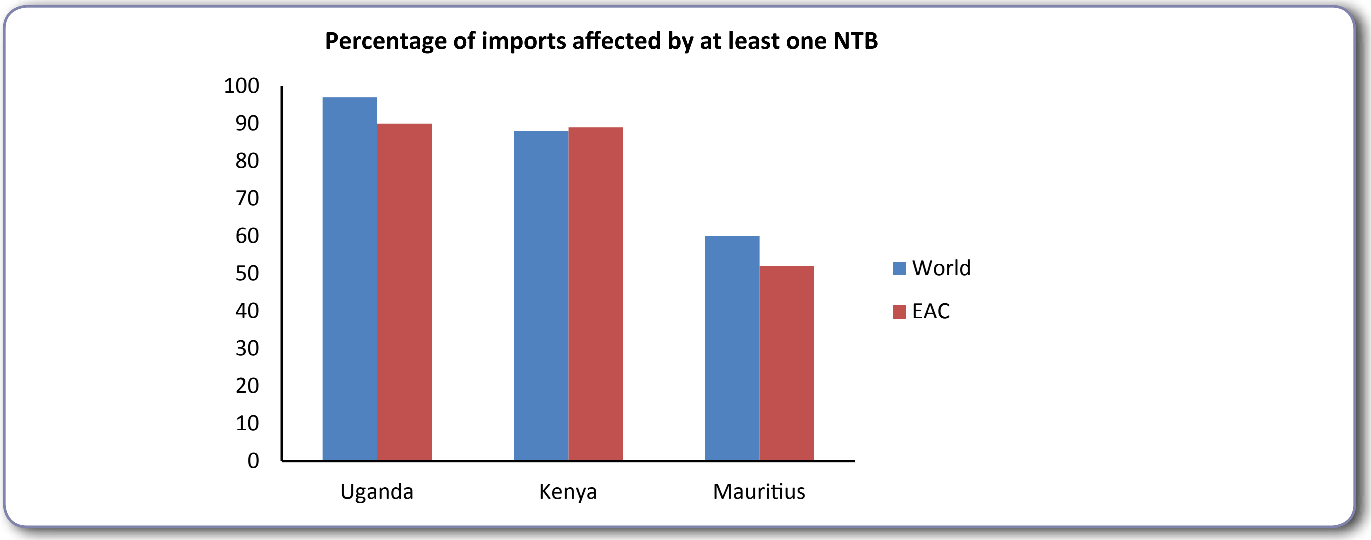
Technical barriers to trade and sanitary and phyto-sanitary measures.

Kito kya polici (road block) in Kasingada in Tanzania, are some of the sources of nontariff barriers

5.2.1 Over-Regulation as a Constraint to Regional Trade

If an African village creates an even greater number of restrictions on trade between residents of the village than on trade with those outside the village, something is wrong. However, the EAC is doing exactly that. Of EAC members, Uganda has the largest number of NTBs, followed by Kenya.[28] These two East African countries impose significantly more NTBs on their imports than do any other surveyed sub-Saharan African country (see Figure 22). Kenya imposes more restrictions on imports from its EAC partners than on imports from the rest of the world. This contrasts to the situation in all other SSA countries, all of which impose more NTBs on imports from the rest of the world. With these NTBs, Uganda and other EAC countries face more significant constraints when exporting to Kenya than they do when exporting to other non-EAC counterparts.

Figure 22: Uganda and Kenya Have Largest Number of Barriers, Even for Intra-regional Trade



Source: Cadot and Gourdon, World Bank 2012

Uganda's and Kenya's regulations on safety, and technical inputs into products could be considered cases of over-regulation. The frequency29 and coverage30 ratios of key types of NTBs constraining trade in five African countries suggest such rules and regulations in Uganda and Kenya are considerably more restrictive than in other selected African countries (see Figure 23). The categories of rules and regulations include rules related to the following issues: (i) sanitary and phytosanitary (SPS), (ii) technical barriers to trade (TBT), which arise when standards, regulations, and assessments systems intended to ensure safety are not applied uniformly, (iii) pre-shipment, (iv) price controls, and (v) quantity controls.

Concrete examples of the impact of such regulations are not hard to find. In 2009, one of Uganda's largest milk processors complained that the Kenya Bureau of Standards established a new quality standard for imported milk powder. The standard imposed a minimum level of 34 percent protein in cream powder, even though cow milk cannot have a protein level in excess of 25-26 percent. Fully documented Ugandan milk consignments were also allegedly held at the border for more than two weeks without justification. This led transporters to refuse to carry Ugandan products. Dairy processors in Uganda and Tanzania complained that Kenyan authorities had a pattern of imposing these NTBs as a means of protecting local dairy producers. Conversely, Kenyan exporters complained that Uganda requires advance laboratory analysis of every single shipment of dairy products, in violation of the mutual recognition of conformity assessment procedures in the EAC.

28 Based on a World Bank survey of a group of Sub- Saharan Africa countries, including Mauritius, Senegal Madagascar, Kenya and Uganda

29 The frequency ratio shows the percentage of import transactions covered by a selected group of NTMs for an exporting country. It accounts only for the presence or absence of an NTM, without indicating the value of imports covered.

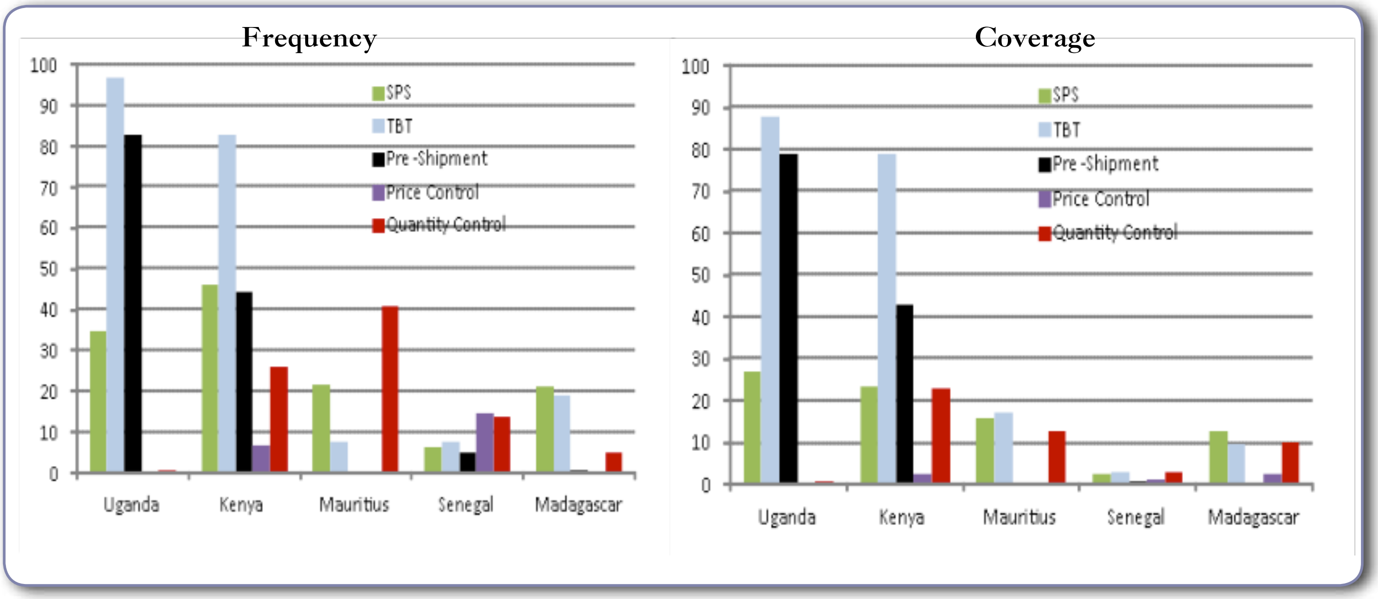
30 The coverage ratio gives the percentage of trade subject to NTMs for an exporting country at a desired level of product aggregation. It allows weighting the frequency ratio with the value of imports for the affected tariff lines.

In addition, according to Kenyan processors, Uganda imposes dairy standards on imports that are more stringent than standards that apply in domestic markets in Kenya and Uganda, which meant that they had to produce special "export-grade" produce to trade with EAC partners, even though consumers may not require dairy products produced to such stringent standards.

That rate of occurrence of such regulations significantly exceeded that in other surveyed African countries. This suggests that Uganda and Kenya may be over-regulating, irrespective of how well designed and implemented the rules and regulations could be. In effect, over-regulation is a subtle policy reversal of the trade liberalization policies that Uganda adopted two decades ago.

These regulations have raised the price of products in the same way that tariffs would have done, if tariffs had not been eliminated. The number of impact of explicitly formulated price control measures and quantitative restrictions is quite limited in Uganda. Nonetheless, just as such measures and restrictions result in increased domestic prices, SPS and TBTs raise the cost of production, resulting in increased final consumer prices and less competitive exports. Unfortunately, NTBs have the most significant impact on food products from Uganda (see Figure 23). Apart from discouraging the import of food, this also has detrimental effects on this potential food basket. SPS raise the price of rice and bread by 30 percent in Uganda, relative to the average price for such products in countries surveyed (see Figure 24).[31] With their limited production levels, the benefits to domestic producers are minimal and consumers lose out.[32] On the other hand, corruption, roadblocks, customs procedures, and harassment or discrimination in the granting of licenses and municipal or council permits account for more than 50 percent of total maize transfer costs in Uganda, compared to nearly 35 percent in Kenya.[33]

Figure 23: Uganda and Kenya are the Most Affected by NTMs Relative to Other SSA Countries[34]



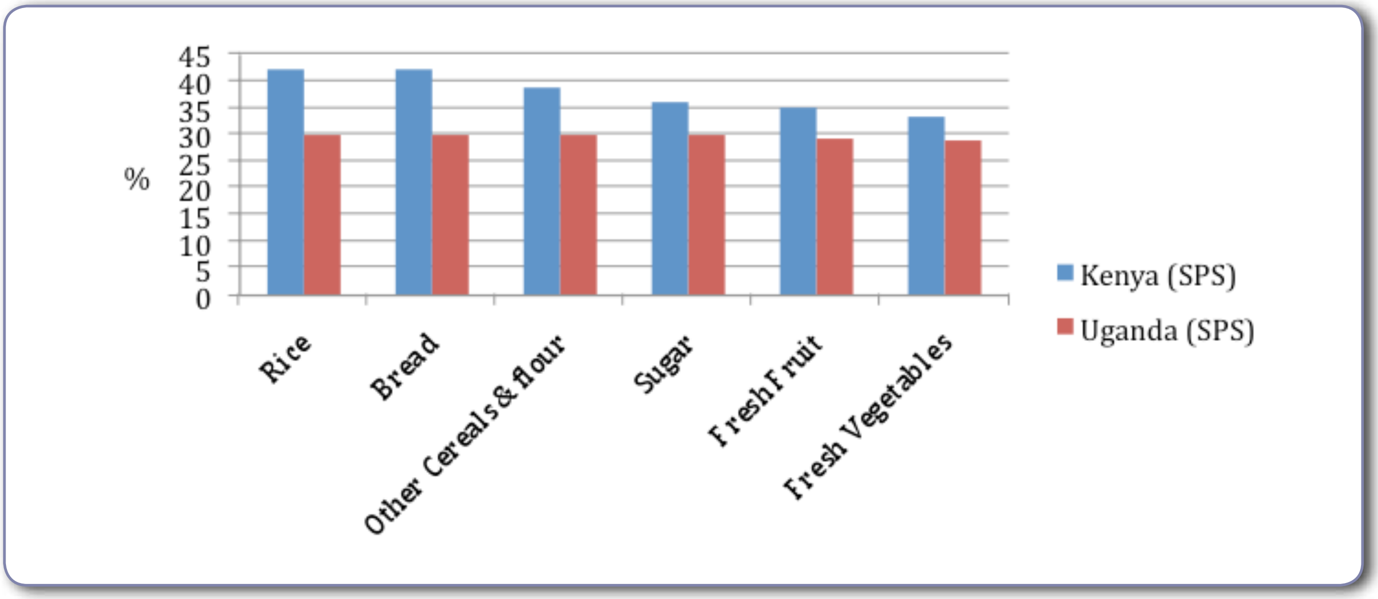
Source: Cadot and Gourdon, World Bank 2012

31 The estimated "price gaps" refer to the difference between domestic prices and the sample average at the product level.
32 Annex 1 sets out in more detail the estimated price-raising effect of NTMs, by product, for Kenya and comparator countries (percent)
33 Karugia et al, 2009, A Study on the Impact of Maize and Beef Cattle Cross Border Trade in the East African Community

34 Sanitary and Phytosanitary (SPS); Technical Barriers to Trade (TBT)

Inappropriate standards can stifle trade. Standards may be desirable at the regional rather than the national level, in order to exploit economies of scale in regulatory expertise; to prevent fragmentation of the market resulting from varying standards; and to limit the scope for regulatory capture. However, it is important to tailor regional standards to the specific preferences, needs and capacities of regional actors in order to avoid non-compliance and unnecessary implementation costs (see Box 6). Failure to do this partly explains the challenge in implementing the standards that have so far been developed.

Figure 24: Significant Price-raising Effect of NTBs on Food in Kenya and Uganda



Source: Cadot and Gourdon, World Bank 2012

Non tariff barriers imposed on products like maize have raised prices, (Great Lakes Film Production Ltd), November 2012

Box 9: The Case of Harmonized EAC Standards Becoming Potential Trade Barriers

Dairy sector: In 2006, the EAC adopted harmonized dairy standards for eight categories of product. These standards followed the international Codex Alimentarius standards for dairy products almost verbatim. EAC standards therefore assume that consumer incomes and the quality of production infrastructure in East Africa are equivalent to Western levels, which is obviously not the case.

Consistent with developed country norms, the new EAC standards focus on pasteurization as the key to ensuring product safety. This technology is widespread in developed countries but it is difficult and expensive to apply in the context of smallholder dairying, which is the dominant form of production in East Africa. While smallholders in Africa can and do supply perfectly good raw milk for pasteurization, the infrastructure and quality control systems needed for delivery of smallholder supplies to a processing plant results in consumer prices that are four to five times higher than for raw milk traded through informal channels.

Moreover, East African consumers have found an alternative to reducing health hazards not recognized in the EAC standards, which is to consume raw milk after boiling. This practice reduces the otherwise high bacteria levels found in East African milk to safe levels, a point not recognized during the harmonization process because the Codex standards were developed for Western countries that consume pasteurized milk.
As a result of setting the regional standards too high, the EAC's harmonized dairy standards have been difficult to implement and provide little practical guidance for farmers, dairy traders, and large processors on how to upgrade their operation. According to the letter of the law, more than 95 percent of the EAC's milk supply is technically illegal because it does not comply with the new standards requirements. Thus, regional trade could be stopped as a result of non-compliance at any time.

Maize sector: A similar situation is emerging with maize. The newly developed EAC standards for maize are more stringent with respect to levels of discolored and immature/shriveled grains than either the Codex standard or the existing national standards of Burundi, Tanzania, and Uganda. Given that compliance with the EAC quality standards will be mandatory, the newly harmonized EAC standards will not only result in additional certification costs, they will also make it difficult to find smallholder supplies of maize that are of suitable quality.

Ugandan butter in Rwanda: A good example of how quality standards and laboratory testing requirements can act as a constraint to formal sector trade is the story of Uganda's exports of butter to Rwanda. In this case, Rwanda's only credit license to import butter into the country decided to stop imports because of difficulties in the recognition of Ugandan quality certificates and demands for additional laboratory tests by the Rwanda Bureau of Standards (RBS). According to the importer, this was because the batch numbers were not identical throughout each consignment, since the butter was manufactured on different days. This problem also meant the trader could not obtain pre-clearance for the goods. As a result, the importer decided it would be easier to stop trading in butter and cancelled all orders with the Ugandan supplier.

Despite this move, Ugandan butter remained on store shelves in Kigali. As explained by border officials, it is impractical to stop small consignments from crossing and many dairy products are brought into Rwanda in small quantities, sometimes in cool boxes but otherwise with no refrigeration or any other kind of quality control. Just as formal sector dairy chains have a difficult time competing with informal milk vendors in domestic markets, this story shows that formal traders also have a difficult time competing with informal traders in the international market.

While the efforts to regulate the dairy trade and to harmonize regional standards may seem like an obvious step towards improving the trade regime, such moves can actually have negative consequences for formal sector operators. While it is important to have a well-regulated trade system, the system must be cost competitive and simple to use in order to avoid creating further constraints on formal dairy operators.

Source: World Bank (2012), Africa Can Help Feed Africa, Jensen and Keyser (2012), p. 191.

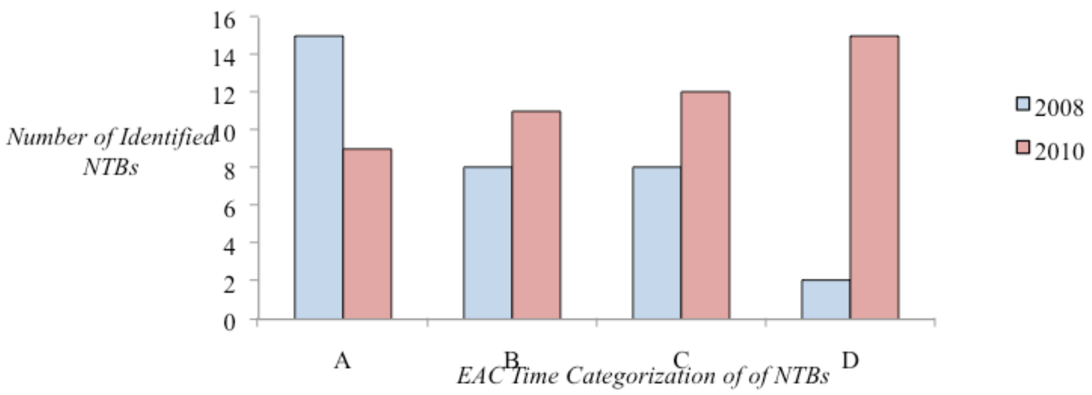
5.2.2 How Can Uganda Address the Constraints Created by NTBs?

Over the past five years, efforts to eliminate NTBs have been largely ineffective. It is clear that the successful removal of NTBs will depend on the level of commitment of all the EAC trader partners. However, Uganda should commit to doing its part. Rules and regulations still affect many sectors. Some of these rules and regulations, such as some governing food safety, have been implemented for legitimate reasons to protect consumers. However, when they are unduly restrictive or poorly designed and implemented, they become a barrier to trade. Over the past 5 years, in cooperation with the East African Business Council, the EAC has put in place a mechanism involving National Monitoring Committees to report, monitor and publicize NTBs.[35] A Time-Bound Program for the Elimination of Identified NTBs sought to identify NTBs that could be easily eliminated in order to generate a growing consensus for further reform. So far, the results have been dismal. Since the establishment of these mechanisms, there has actually been an increase in NTBs, suggesting possible increased political resistance (see Figure 25).

Cases of recurring NTBs, particularly in the dairy and poultry sectors, are common, while reporting did not deter from cost rising for the trader. An example of this is the cash bond introduced by the Kenya Revenue Authority in August 2012 on Ugandan goods destined for transit through Kenya. The bond was imposed suddenly and without prior warning, significantly altering procedures related to the taxation of transit goods. Prior to the measure, importers and exporters were required to procure an insurance bond. The policy was applied only on sugar and cars and was intended to prevent the practice of dumping transit goods on the Kenyan market without paying dues and thereby undercutting local vendors and denying the two states much-needed revenue. The policy shift has had a significant impact on trade in the short term, with approximately 2000 vehicles and 600 containers being stranded in Mombasa. It will also have medium- to long-term ramifications, resulting in increased consumer prices and a decline in demand. This is exacerbated by a policy which means that traders will now have to wait to get their cash bonds refunded, running the risk of tying up capital.

It is acknowledged that the 'Time Bound' program has been largely unsuccessful. In response, more time has been allocated for the removal of NTBs. Only around 50 percent of the NTBs identified in 2008 and 30 percent of the NTBs identified in 2010 in the EAC were eliminated within the agreed timeframe (see Figure 24). There have been very few such "quick wins"[36] and it was just as difficult to move goods across borders in 2010 as it was in 2005,[37] except at a few border points where joint clearing has been implemented.

Figure 25: More NTBs Identified, and More Time Given for Removal



Source: World Bank analysis of Draft EAC Time bound Programme for Elimination of Identified versions 2008 and 2010

35 In cooperation with the East African Business Council, the EAC Secretariat has set up a mechanism to identify and monitor the elimination of NTBs (EAC / EABC 2008), which has since then been completed by an online reporting and monitoring mechanism at the COMESA-EAC-SADC Tripartite level (see: www.tradebarriers.org).
36 Kirk 2010
37 World Bank / IFC 2011

The removal of NTBs is influenced by political economy considerations. To address these considerations, it is vital to take into account who wins and who loses as measures to eliminate them are formulated. For instance, some studies[38] have showed that in the case of maize, the elimination of NTBs would reduce the high transfer cost in the region and would cut maize producer prices by about 9 percent and consumer prices by about 3 percent in Kenya. On the other hand, it would raise producer prices in Uganda by 20 per cent and consumer prices by 24 per cent. This would result in a 2 percent rise in Uganda's maize consumption and a 3 percent rise in production. Thus, the biggest winners from the elimination of NTBs in East Africa would be Uganda's maize producers, while the biggest losers would be maize producers in Kenya.

Raising awareness and improving transparency are necessary steps. However, the voluntary and unilateral removal of NTBs by each partner state, without any sanctions for non-compliance, is proving to be ineffective. Bilateral negotiations such as those being conducted between Uganda and Rwanda can help, but a sanctions system would support the achievement of better results through such efforts. Strengthening the existing monitoring system would also help authorities to gain a good understanding of the most detrimental measures faced by Ugandan operators and to adopt a proactive attitude in negotiations on NTBs.

Uganda needs to cooperate with its EAC partners to improve the regulatory environment by eliminating NTBs, amongst other measures. Priority action areas include, amongst others:

- Strengthening SPS testing and verification capabilities and involving private labs in the process;
- Working with EAC partners toward the mutual recognition of conformity-assessment procedures;
- Relentlessly working with the EAC Secretariat to strengthen the EAC NTB monitoring mechanisms and enabling it to act upon identification of barriers.

38 W Karugia et al, 2009, A Study on the Impact of Maize and Beef Cattle Cross Border Trade in the East African Community

5.3 The Services Sector: Turning Opportunities into Gold

A strategic approach to promoting the growth of the priority service sectors of tourism, transport and logistics, education and business services will help unleash their potential.

In tourism, beyond capacity and skill development, the public sector will play an important role by developing the appropriate infrastructure to reduce the cost of accessing tourist centers. The Hotel and Tourism Training Institution should be revamped and provided with equipment and staff to raise skills. However, access to tourist sites should not be constrained by bad roads. Working closely with the private sector, new innovations must be developed to create niche markets, given the stiff competition from Kenya and Tanzania for traditional game tourism.

In the transportation sector, the development of the appropriate infrastructure and improvements to logistics systems should be the top priority. Beyond that, the development of a level playing field could be facilitated by removing charges that raise the cost of entry for Ugandan truckers and freight services providers into the regional transport market. This will support the growth of the industry.

In professional services, beyond capacity and skill development, restrictive immigration rules need to be relaxed to facilitate the improved mobility of providers. The challenge is to institute an adequate regulatory framework to support implementation of existing engagements in education, regulation, trade policy, and labor mobility. At the national level, a regulatory assessment mechanism covering all professional and education services sectors should be instituted and a roadmap for action with concrete objectives developed. Domestic policy reform should be complemented through intensified international and regional cooperation involving the participation of WTO, EAC and COMESA and other entities. For instance, sectoral agreements on the mutual recognition of professional qualifications could help with the development of adequate curricula for various professions. Such agreements could provide guidance for employers, mentors and trainees regarding the practical experience requirements for professionals. The Ugandan government should work with regional bodies such as the IUCEA, the EABC, or the EAPSP to undertake in-depth, cross-country comparative assessments of professional qualifications, including entry requirements, education and training, and practical experience requirements, and of the regulations governing professionals in each EAC member state. Such benchmarking exercises are necessary tools for the appropriate implementation of the negotiated Mutual Recognition Agreements of Professional Qualifications and Licensing Requirements (MRAs). Uganda's participation in the Professional Services Knowledge Platforms in East Africa and COMESA can help the country with the development of a meaningful reform program that includes the elimination of explicit barriers and the implementation of necessary regulatory, education and immigration reforms.

Trade reform to eliminate explicit trade barriers needs to be integrated with an open and transparent process of regulatory reform. Under this process, decisions on the nature and pace of reform need to be based on careful analysis and an understanding of good practices. Regulatory frameworks should not restrict competition or slow down expansion. Taking the example of professional services, the regulation affecting the conduct and the operations of professional firms tends to be more restrictive than in several neighboring countries. This is apparent in price regulations covering legal services, in prohibitions on certain forms of advertising and in restrictions on the form of permitted businesses in both accounting and legal services. An equally important problem is the absence of regulation, which can create a legal vacuum that actually constrains business growth and creates opportunities for unfair competition and corruption.

The key challenge to reforming services in Uganda relates to the coordination of regulatory reform with liberalization. Reforms need to focus on incremental, qualitative improvements in domestic regulation. Disproportionate cumulative entry requirements need to be relaxed. For example, narrowing the scope of exclusive tasks in certain professions would contribute to this goal. Exclusive rights can lead to increased specialization amongst professionals and guarantee a higher quality of service. However, if these exclusive rights result in the establishment of monopolies, they can have adverse price and allocation impacts, especially when granted for services for which adequate quality can be provided at a lower cost by less-regulated middle-level professionals. Disproportionate restrictions that limit competition need to be eliminated. Price regulations affecting legal services and public procurement contracts in engineering are supported by professional associations or the government, who claim that they are useful tools to prevent adverse selection problems. However, less restrictive mechanisms, including mechanisms to facilitate the improved access to information related to services and services providers, would accomplish the same goals at a lower economic cost. On the other hand, allowing advertising by accounting and legal services would facilitate competition by raising the awareness of consumers regarding different products. As such, they could be used as a competitive tool for new firms entering the market.

It is not less regulation that is required, but better regulation. 'Better regulation' can be defined as regulation that facilitates the achievement of policy objectives without unduly escalating cost of services. Policy makers need to assess whether existing or new regulation facilitates the achievement of sector-specific public policy objectives without hindering market openness. Box 10 presents some experiences with regulatory tools from which Uganda can learn.

Business services like computer use to boost more trade, (Sheila Gashishiri, October 2012

Box 10: Services Regulatory Initiatives

The OECD principles on key market-oriented and trade-and-investment-friendly regulation could offer guidance to the regulation of services sectors in Africa. Furthermore, the APEC-OECD Integrated Checklist on Regulatory Reform (adapted to developing countries' needs) could provide further guidance on how to undertake such a combined assessment of regulatory and competition policies, and market openness policies. The Checklist highlights key issues that should be considered during the process of development and implementation of regulatory policy and could be useful in building domestic capacities for quality regulation.

The APEC-OECD Checklist is a voluntary tool that Uganda and other EAC economies may use to evaluate their respective regulatory reform efforts. The checklist has four sections including 40 specific open questions in total. The first is a horizontal questionnaire that deals with the degree of integration of regulatory, competition and market openness policies across levels of government, and on the accountability and transparency mechanisms needed to ensure their success. The second is on regulatory policies which are designed to maximize the efficiency, transparency and accountability of regulations based on an integrated rule-making approach and the application of regulatory tools and institutions. The third is on competition policies which promote economic growth and efficiency by eliminating or minimizing the distorting impact of laws, regulations and administrative policies, practices and procedures on competition, and by preventing and deterring private anti-competitive practices through effective enforcement of competition laws. The fourth is on market openness policies which aim to ensure that an economy can reap the benefits of globalization and international competition by eliminating or minimizing the distorting effects of border as well as behind-the-border regulations and practices.

Other regulatory experiences such as the ASEAN Mutual Recognition Arrangement Framework on Accountancy Services, the ASEAN Mutual Recognition Arrangements on Engineering Services and on Architectural Services could provide further guidance to the Uganda and the EAC countries which are willing to engage in mutual recognition discussions. Furthermore, the experience of the EU with the internal recognition of professional qualifications as well as the regulatory dialogues and regulatory platforms established with third countries could give additional guidance to Ugandan policy makers.
Sources: OECD, APEC, ASEAN

Makerere University Kampala to tap into more education exports through quality and standards enhancement, (Great Lakes Film Production Ltd), November 2012

6. Summary and Concluding Remarks

In recent years, Uganda has experienced a slowdown in economic growth and increased vulnerabilities. The country faces the challenge of achieving sustainable growth at a rate sufficiently high to keep pace with the rapid rate of growth of the population, to create enough employment for its citizens and to fulfill its aspirations of becoming a middle-income country. Amongst other means, Uganda may achieve this by harnessing the potential of expanding regional trade to renew growth and to expand employment opportunities. Uganda can harness the potential of regional trade by: (i) leveraging its agricultural exports, particularly the export of foodstuffs within the region; (ii) diversifying Uganda's export base into higher value exports while also promoting trading in tasks or parts to establish regional production chains; and (iii) diversifying more deeply into services. The priority interventions to achieve this are two-fold:

Improved water transport to remain the key to lowering transport costs (Charles Kunaka), April 2011

i. Addressing constraints to business growth, agricultural transformation and to raising overall productivity;

ii. Easing access to markets by, amongst other measures:

   a. Measures to reduce transportation costs involving both improvements to infrastructure and improvements to trade and transport logistics,

   b. Addressing non-tariff barriers to trade to allow the free flow of goods and services, and

   c. Accelerating reforms in regulations and service restrictions.

On the issue of access to markets, deeper regional integration will be the key means to achieve progress over the long-term. However, Uganda must move to address issues under its own control without waiting for its neighbors to act. As a landlocked country with relatively limited capacities and resources, Uganda will benefit if deeper integration reduces trading costs by providing the regulatory environment for trade to flow freely and for cross-border networks to flourish.

This integration should also be leveraged to reduce constraints faced by firms in accessing key inputs for productivity and diversifying into higher value-added production and trade. Beyond promoting trade, deeper regional integration will facilitate the development of regional public goods, reduce transaction costs, provide a regulatory environment in which goods and services can flow freely, and support cross-border production networks.

Uganda must define its strategic positioning. The integration of the Ugandan economy with larger and more competitive economies creates a number of opportunities, but it also means that Uganda has to build competitive advantage. However, trade agreements among a smaller set of partners are more likely to facilitate deeper integration, involving differentiation and diversification, leading to welfare gains.

Progress towards deepening integration and boosting regional trade are highly dependent on regional peace and security. Instability in the Democratic Republic of Congo, South Sudan or any other country in the sub-region has a negative impact on trade between Uganda and these neighbors and prevents Uganda from benefiting from growth in regional trade. Accusations that Uganda has supported the insurgency in Eastern Congo (see recent UN Report) could create uncertainty within the private sector and impact its efforts to expand to new regional markets. President Museveni currently presides over three regional organizations, including the East African Community, the International Conference for Great Lakes Countries (ICGLC), and the African Union. With this position, he has a strategic opportunity to facilitate regional peace and stability. A lasting solution to conflict in the region will boost regional trade growth, much to the benefit of regional economies, including the landlocked but land-bridged Uganda.

Public awareness and stakeholders support for regional integration appears to be limited in Uganda. Arguably, efforts to mobilize public and the support of key groups at the onset of the EAC integration process have been too limited. For example, consumers have not been involved in the EAC and COMESA integration process, despite the critical importance of their participation. Similarly, there is a need to consult private sector organizations and to take into account their interests. Special attention should also be given to small and medium-sized enterprises (SMEs) and informal traders. All this matters, because commitments made without proper consultations with the stakeholders concerned are likely to exacerbate the political economy challenges and to constrain implementation. In the long term, consumers are likely to benefit from the regional integration of goods and services markets. Involving them and other key stakeholder groups in the process will help to build support for the measures that will allow Uganda to achieve its aspirations.

Statistical Annex

Annex Table 1: Key Macroeconomic Indicators

Indicator	Unit measure	2005/6	2006/7	2007/8	2008/9	2009/10	2010/11	2011/12
Population	Millions	26.7	27.6	25.6	29.6	30.7	31.8	32.9
GDP	USD	9,957.99	11,902.81	14,440.13	15,596.12	15,245.68	14,790.53	16,903.84
Per capita income	USD	372.40	430.79	564.51	527.07	497.25	465.40	513.17
GDP growth	%	10.8	8.4	8.7	7.2	5.9	6.7	3.4
Gross Domestic Savings	as % of GDP	13.2	16.0	15.9	12.2	12.2	11.3	10.2
Gross Investments	as % of GDP	21.2	23.6	23.0	23.5	24.2	24.7	25.2
Inflation (period average)	%	6.6	6.8	7.3	14.2	9.4	6.5	23.4
Exchange Rate (period average)	UGX/USD	1825.10	1777.99	1696.45	1904.70	2029.90	2323.40	2568.83
External Sector								
Exports - Goods and Services	Million USD	1,041.2	1,473.8	2,073.0	2,216.4	2,317.3	2,297.8	2,676.9
Imports - Goods and Services	Million USD	-1,969.0	-2,495.2	-3,510.4	-4,062.2	-4,116.8	-4,671.1	-5,289.7
Current Account Balance	Million USD	-314.5	-342.0	-902.7	-1,258.6	-1,435.0	-1,686.3	-2,070.5
Balance of Payments (overall balance)	Million USD	198.23	703.85	562.99	-45.70	210.89	-581.22	731.37
Foreign Reserves	Million USD	1408.3	2090.8	2684.4	2442.0	2384.7	2044.0	2346.1
External Debt	Million USD	4464.4	1466.8	1687.0	2046.4	2343.4	2904.9	3254.1
Foreign Direct Investment	Million USD	512.04	718.28	760.58	785.22	692.72	755.07	1065.34
Tourism Earnings	'000 USD		449	590	564	662	805	
Monetary Sector								
Average Deposit Rate	%	2.6	2.2	2.2	2.1	2.0	2.6	3.3
Average Lending Rate	%	16.1	16.9	18.2	18.8	18.2	19.2	23.0
Growth in Money Supply	%	16.4	17.4	31.1	25.0	31.7	25.9	15.7
Government Finance								
Total Domestic Revenue	as % of GDP	12.5	12.6	12.8	12.5	12.2	13.3	13.1
Tax Revenue	as % of GDP	11.8	11.9	12.3	11.8	11.7	12.7	12.5
Non Tax Revenue	as % of GDP	0.7	0.7	0.5	0.7	0.6	0.6	0.6
Total Expenditure	as % of GDP	18.6	18.6	17.9	17.3	19.6	22.8	19.4
Recurrent Expenditure	as % of GDP	12.3	11.5	11.8	10.9	12.3	15.3	11.1
Development Expenditure	as % of GDP	6.0	6.1	5.6	5.6	6.6	7.1	7.9
Grants	as % of GDP	5.4	4.5	2.7	2.6	2.5	2.3	2.6
Fiscal Balance (after grants)	as % of GDP	-0.8	-1.5	-2.4	-2.2	-4.9	-7.2	-3.8

Source: IMF, UBOS

Annex Table 2: Growth and Structure of Uganda's Economy

Economic Activity	2005/6	2006/7	2007/8	2008/9	2009/10	2010/11	2011/12
Real GDP Growth Rates (%)							
Agriculture	0.5	0.1	1.3	2.9	2.4	0.7	2.2
Industry	14.7	9.6	8.8	5.8	6.5	7.9	2.4
o/w manufacturing	7.3	5.6	7.3	10.0	6.6	8.0	-1.0
o/w construction	23.2	13.2	10.5	3.7	5.9	7.8	3.2
Services	12.2	8.0	9.7	8.8	8.2	8.4	3.3
GDP at market prices	10.8	8.4	8.7	7.2	5.9	6.7	3.4
Shares of GDP (%) 2002 Prices							
Agriculture	24.1	22.3	21.4	23.1	23.6	22.7	24.4
Industry	22.8	25.2	25.8	24.7	24.9	25.3	26.4
o/w manufacturing	7.1	7.1	7.3	7.9	7.7	8.6	8.3
o/w construction	11.7	13.1	13.6	12.3	12.7	13.0	13.0
Services	47.2	47.0	46.9	46.4	45.5	46.2	44.3
FISM and net taxes	5.9	5.6	6.0	5.7	6.0	5.8	4.9
Contribution to Real GDP Growth (%)							
Agriculture	0.1	0.0	0.2	0.5	0.4	0.1	0.4
Industry	3.5	2.4	2.2	1.5	1.6	2.0	0.3
o/w manufacturing	0.5	0.4	0.5	0.7	0.5	0.5	-0.1
o/w construction	3.0	1.9	1.6	0.6	0.9	1.2	0.3
Services	6.0	4.0	4.8	4.4	4.2	4.4	1.6
Shares of GDP by type of expenditure (%)							
Final Consumption Expenditure	91.9	89.7	84.7	88.2	89.5	93.5	92.3
Households	77.8	76.9	73.5	78.1	79.8	83.6	83.6
Government	14.1	12.7	11.2	10.1	9.7	9.8	8.7
Gross Capital Formation	21.2	23.7	23.0	22.0	23.5	25.0	24.4
Gross fixed capital formation	21.0	23.4	22.7	21.7	23.2	24.8	24.1
Charges in inventories	0.2	0.2	0.2	0.3	0.2	0.2	0.3
Net exports	-13.1	-13.3	-7.7	-10.1	-12.9	-18.5	-16.7
Gross domestic saving (% of GDP)	13.2	16.0	15.9	12.2	12.2	11.3	10.2
Public	-1.2	-0.8	-0.1	0.9	-0.4	-5.3	-0.3
Private	14.3	16.8	16.0	11.3	12.6	16.6	10.5

Source: IMF, UBOS

Annex Table 3: Quarterly GDP Growth Rates FY2008/9 - 2012/13

Year	Quarter	Agric	Live-stock	Fishing	Industry	Manu-facturing	Electric-ity	Con-struc-tion	Ser-vices	Whole-sale & retail	Hotels & restuar-ants	Transport & com-munica-tions	Finan-cial services	Real estate activi-ties	Other busi-ness	Public admin-istra-tion	Educa-tion	Health & social work	Other ser-vices	FISIM	Taxes on prod-ucts	GDP at basic Cost	GDP at market prices
2008/9		1.7	0.1	-0.5	3.6	6.4	5.4	2.0	3.7	6.3	1.3	2.9	11.2	3.8	3.5	1.8	1.9	1.1	2.4	14.9	2.5	3.2	3.1
2009/10		0.6	0.9	1.1	0.4	-0.7	2.3	1.1	1.5	-0.2	3.1	5.1	3.0	-1.3	4.4	5.6	-1.2	-0.5	3.4	9.1	0.3	0.8	0.8
2010/11		-1.1	0.7	0.6	2.7	4.1	2.4	2.2	2.3	0.7	0.3	3.4	6.1	3.4	-0.2	-1.3	5.9	3.9	3.9	7.3	2.5	1.7	1.8
2011/12		1.4	0.8	0.4	1.0	-1.4	2.6	2.1	0.2	-0.8	5.0	2.4	-5.9	0.2	1.5	-2.3	-0.9	-0.4	3.1	-5.9	1.5	0.7	0.8
2007/8	Q4	0.6	-1.6	-2.0	-4.8	-8.1	2.7	-3.3	-4.0	-12.3	0.1	1.1	0.4	-2.5	-0.4	-1.4	-2.0	-5.5	4.3	-5.3	-0.4	-3.4	-3.1
2008/9	Q1	3.2	-1.4	-0.7	13.0	16.9	4.3	11.9	8.8	21.7	2.0	10.3	-0.7	-2.9	6.6	2.5	9.3	6.4	4.0	3.0	-1.3	9.0	7.9
	Q2	-6.0	1.7	-0.4	-2.5	-2.8	7.6	-2.6	-0.3	-2.5	-0.2	-5.5	22.5	-1.7	5.9	4.5	0.2	-0.9	3.1	12.1	9.4	-2.0	-0.9
	Q3	3.6	-0.4	-1.5	0.2	2.1	-7.5	-0.4	3.9	-0.6	0.3	5.5	19.8	20.6	0.3	-0.9	-1.4	-7.3	1.7	41.3	4.5	2.4	2.6
	Q4	6.1	0.3	0.5	3.5	9.6	17.1	-0.8	2.5	6.7	3.2	1.2	3.2	-0.9	1.3	1.3	-0.6	6.1	0.7	3.2	-2.7	3.4	2.7
2009/10	Q1	-10.6	1.5	1.1	6.9	2.6	0.9	10.3	3.3	-4.3	4.9	14.8	7.7	2.1	8.5	8.3	1.2	0.3	4.2	29.1	5.9	1.5	2.0
	Q2	14.5	0.6	1.1	-3.3	-7.4	0.4	-1.1	-0.3	-2.3	1.7	-1.9	2.3	-0.8	-0.4	0.6	2.3	2.4	2.7	6.5	-3.3	1.0	0.5
	Q3	-2.9	0.7	2.5	1.6	6.6	3.5	-1.9	1.9	6.4	9.5	-0.9	4.1	-7.8	5.2	6.4	-3.7	-3.4	5.7	7.6	-1.2	0.9	0.6
	Q4	1.3	0.7	-0.5	-3.3	-4.6	4.3	-3.0	1.0	-0.7	-3.6	8.5	-2.0	1.4	4.1	7.0	-4.7	-1.2	1.1	-6.9	-0.5	0.0	0.0
2010/11	Q1	-6.0	1.0	-0.6	9.7	0.1	0.2	16.3	2.2	-5.2	-4.2	5.0	8.9	4.5	5.2	8.0	10.0	3.0	1.0	20.5	8.9	2.5	3.1
	Q2	11.6	0.4	-0.8	2.8	15.1	4.3	-2.9	3.8	13.1	-0.9	-2.4	10.7	1.9	0.1	-0.3	0.6	1.5	3.8	11.7	2.0	4.6	4.3
	Q3	-4.9	1.0	4.6	-2.4	-3.4	2.3	-2.7	1.4	-2.9	1.9	9.2	-2.4	4.8	-3.3	-5.8	4.8	3.1	0.5	-3.2	-3.6	-0.6	-0.9
	Q4	-5.1	0.5	-0.8	0.7	4.6	3.1	-1.9	1.9	-2.1	4.4	1.9	7.1	2.2	-2.6	-7.2	8.3	8.2	10.2	0.0	2.8	0.5	0.8
2011/12	Q1	9.6	0.9	-0.2	1.2	-5.6	-0.6	5.4	0.7	6.5	6.7	5.1	-9.1	1.3	7.9	1.2	-17.8	-14.5	3.7	-6.5	1.4	2.3	2.2
	Q2	-5.0	0.5	-0.4	-0.2	-1.9	1.3	0.4	-1.2	-2.6	5.6	-3.0	-5.1	1.0	-0.1	-4.8	2.9	6.2	-7.1	-5.6	-0.7	-1.4	-1.3
	Q3	1.3	1.0	1.8	1.8	1.6	4.3	2.0	0.6	-2.6	4.6	5.3	-7.4	-2.8	-4.2	-7.3	8.1	3.5	9.5	-5.6	7.2	1.2	1.8
	Q4	-0.3	0.8	0.5	1.3	0.3	5.5	0.7	0.7	-4.4	3.2	2.4	-1.9	1.3	2.6	1.7	3.3	3.2	6.2	-5.6	-1.8	0.9	0.6
2012/13	Q1	3.1	1.0	1.4	-1.2	-4.0	-1.8	0.3	3.4	-7.0	1.9	7.5	9.0	7.8	14.9	15.6	5.4	6.8	-5.2	2.7	-0.5	2.1	1.8

Source: UBOS

Annex Table 4: Fiscal Framework (as percent of GDP)

	2005/6		2006/7		2007/8		2008/9		2009/10		2010/11		2011/12	
	Budget	Actual	Budget	Actual	Budget	Actual	Budget	Actual	Budget	Actual	Budget	Actual	Budget	Outturn
Total revenue and grants	19.7	17.8	17.4	17.1	17.1	15.5	17.2	15.1	16.6	14.7	16.0	15.6	15.6	14.8
Revenue	13.1	12.5	12.1	12.6	13.0	12.8	13.1	12.5	13.0	12.2	13.1	13.3	12.6	12.3
Tax	12.5	11.8	11.9	11.9	12.6	12.3	12.8	11.8	12.8	11.7	12.9	12.7	12.4	11.8
Nontax	0.6	0.7	0.2	0.7	0.5	0.5	0.3	0.7	0.2	0.6	0.2	0.6	0.2	0.5
Grants	6.6	5.4	5.3	4.5	4.1	2.7	4.1	2.6	3.6	2.5	2.9	2.3	2.9	2.6
Budget support	3.9	4.1	2.6	3.7	2.1	1.9	1.6	1.8	1.7	1.3	1.6	1.3	1.3	1.3
Project grants	2.6	1.3	2.6	0.9	2.0	0.8	2.5	0.9	1.9	1.1	1.3	1.0	1.7	1.3
Total Expenditure	21.0	18.6	20.1	18.6	19.3	17.9	20.4	17.3	20.3	19.6	19.1	22.8	19.8	19.5
Recurrent	11.8	12.3	11.2	11.5	11.1	11.8	10.5	10.9	10.3	12.3	11.7	15.3	10.0	11.3
Development	8.4	6.0	8.2	6.1	7.8	5.6	9.0	5.6	9.9	6.6	7.1	7.1	9.4	7.6
Overall balance														
Including grants	-1.9	-0.8	-2.7	-1.5	-2.2	-2.4	-3.1	-2.2	-3.7	-4.9	-3.1	-7.2	-4.2	-4.7
Excluding grants	-8.5	-6.1	-8.0	-6.0	-6.3	-5.1	-7.2	-4.8	-7.3	-7.3	-6.0	-9.5	-7.2	-7.2
Financing	1.9	0.6	2.7	1.7	2.2	2.0	3.1	0.3	3.7	4.4	3.1	7.3	4.2	4.7
External financing (net)	2.7	1.7	2.5	3.3	3.1	2.5	2.1	1.7	3.0	2.2	1.9	1.4	2.4	2.7
o/w Budget support	0.6	0.4	1.2	1.9	0.8	0.9	0.6	0.8	0.7	0.7	0.1	0.6	0.7	0.8
Domestic financing (net)	-0.8	-1.1	0.2	-1.7	-0.9	-0.5	1.0	-1.4	0.6	2.1	1.2	5.9	1.9	2.0

Source: IMF, MFPED

Annex Table 5: Balance of Payments (percent of GDP unless otherwise stated)

Variable	2005/6	2006/7	2007/8	2008/9	2009/10	2010/11	2011/12
Current Account (incl transfers)	-3.2	-2.9	-6.3	-8.1	-9.4	-11.4	-12.2
Exports of goods	10.46	12.38	14.36	14.21	15.20	15.54	15.84
Imports of goods	-19.77	-20.96	-24.31	-26.05	-27.00	-31.58	-31.29
Services (net)	-1.8	-2.3	-3.3	-2.8	-2.7	-4.5	-3.4
Trade balance	-9.3	-8.6	-10.0	-11.8	-11.8	-16.0	-15.5
Income (net)	-2.5	-1.9	-1.8	-2.0	-2.2	-2.2	-2.2
Current transfers (net)	10.4	9.9	8.8	8.6	7.3	11.3	8.8
Capital and Financial Account	8.8	8.9	8.2	8.0	10.3	7.5	13.2
Capital account*	1.3	28.8	0.0	0.0	0.0	0.0	0.1
Financial account	7.6	-19.9	8.2	8.0	10.3	7.5	13.1
o/w direct investment	5.1	6.0	5.3	5.0	4.6	5.1	6.3
Overall Balance	2.0	5.9	3.9	-0.3	1.4	-3.9	4.3
Gross International Reserves (million USD)	1408.3	2090.8	2684.4	2442.0	2384.7	2044.0	2346.1
Gross international reserves in months of imports	5.1	5.6	6.0	5.1	4.2	3.4	3.6

Source: IMF, BOU

Annex Table 6: Monthly Imports of Merchandise, 2011-2012 (in USD Million)

	2011												2012										
Nature of Imports	Jan	Feb	Mar	Apr	May	Jun	Jul	Aug	Sep	Oct	Nov	Dec	Jan	Feb	Mar	Apr	May	Jun	Jul	Aug	Sep	Oct	Nov
Formal Private Sector Imports:																							
Animal & Animal Products	1.4	1.3	1.3	1.4	1.4	1.7	1.3	1.4	1.4	1.6	1.7	2.4	1.8	1.9	1.5	1.7	1.5	3.3	1.7	1.6	1.4	2.1	1.6
Veg Pdts, Animal, Fats & Oil	29.0	30.7	37.3	27.3	41.0	28.4	37.2	40.8	30.6	37.0	34.9	29.7	34.2	40.1	40.3	37.3	41.2	43.9	44.4	35.3	43.0	38.4	38.7
Prep Foodstuff, Beverages & Tobacco	14.4	11.0	12.4	12.0	12.1	12.0	12.5	16.7	19.8	21.1	39.0	40.4	36.7	28.4	25.7	22.8	25.5	19.1	16.1	18.0	14.2	16.8	16.7
Mineral Products (excl oil products)	27.1	24.8	29.2	29.5	33.1	31.5	34.5	35.4	31.8	28.5	26.2	28.2	30.0	26.4	36.5	31.5	35.1	35.7	30.9	30.9	22.0	12.7	10.2
Petroleum (Oil) Products	55.0	53.5	69.9	65.7	70.3	70.2	69.7	78.4	67.6	66.6	63.3	72.3	78.8	69.1	72.0	62.1	72.9	64.9	58.4	80.1	76.6	85.7	84.0
Chemical & Related Products	29.7	28.9	37.8	26.3	33.0	28.3	29.8	43.3	30.1	35.7	33.0	33.5	30.3	35.6	35.9	34.6	64.8	35.1	35.7	38.0	32.7	33.4	44.0
Plastics,Rubber, & Related Products	17.9	15.0	16.0	18.3	19.7	21.7	20.1	22.0	16.9	21.6	19.7	18.2	20.1	18.0	21.6	20.9	22.8	20.6	24.1	19.7	16.6	18.4	20.5
Wood & Wood Products	12.6	10.1	9.4	11.8	9.4	10.1	12.5	14.7	8.9	10.2	8.9	9.5	9.5	10.1	11.4	11.3	12.2	13.8	9.9	11.6	11.5	10.4	12.0
Textile & Textile Products	11.7	12.9	11.7	9.1	9.9	10.4	9.1	12.0	8.9	9.6	10.4	12.4	14.1	10.7	12.6	10.9	13.5	12.7	10.9	11.4	9.8	11.0	11.3
Miscelaneous Manufactured Articles	12.9	12.7	11.5	9.5	12.0	14.2	16.7	18.7	13.2	13.9	14.0	14.8	12.6	13.8	13.0	13.4	19.4	17.3	18.6	16.9	17.6	17.1	15.7
Base Metals & their Products	27.9	23.4	29.0	25.9	31.6	31.3	26.0	31.1	29.0	28.6	27.9	24.8	29.6	34.2	30.2	27.8	25.2	36.0	18.4	24.2	20.0	24.5	25.2
Machinery Equip, Vehicles & Accessories	114.7	92.7	120.8	94.3	116.5	122.0	121.1	119.1	87.5	90.7	84.3	97.8	86.2	94.2	116.3	105.3	116.2	145.6	119.4	120.3	134.6	119.7	111.0
Arms & Ammunitions & Accessories	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Electricity	0.6	0.4	0.4	0.4	0.5	0.8	0.9	0.7	0.7	0.6	0.8	0.8	1.2	0.9	1.1	0.5	0.5	0.4	0.4	0.4	0.4	0.4	0.4
Subtotal (formal private sector imports)	354.9	317.4	386.7	331.4	390.5	382.7	391.4	434.4	346.3	365.8	364.1	384.7	385.2	383.2	417.9	380.0	450.8	448.4	388.8	408.5	400.4	390.7	391.4
Other Estimated Private Sector Imports	4.5	4.4	4.2	4.1	4.4	4.9	4.8	5.7	3.5	4.0	3.9	5.5	6.2	4.0	5.4	5.0	4.6	3.3	3.0	4.1	3.8	4.6	4.1
Government Imports	19.0	40.1	120.2	20.1	12.4	51.3	11.8	45.4	55.3	28.7	46.5	40.9	66.7	50.7	31.1	29.7	19.0	55.7	11.9	44.9	14.9	20.8	43.2
Total Imports (fob)	378.4	361.9	511.0	355.6	407.3	438.9	408.0	485.5	405.1	398.5	414.5	431.1	458.1	438.0	454.4	414.8	474.4	507.4	403.8	457.5	419.1	416.1	438.7
Total Imports (cif)	461.1	441.2	626.0	434.4	495.8	534.8	497.0	593.3	493.8	487.1	506.8	521.4	561.6	535.2	556.0	507.4	581.5	623.1	493.9	560.1	511.5	508.5	537.6
o/w freight	79.2	76.0	110.1	75.5	84.8	91.9	85.2	103.3	85.0	84.8	88.4	86.5	99.1	93.2	97.4	88.7	102.6	110.8	86.3	98.3	88.5	88.5	94.7
o/w insurance	3.5	3.4	4.9	3.3	3.7	4.1	3.8	4.6	3.8	3.7	3.9	3.8	4.4	4.1	4.3	3.9	4.5	4.9	3.8	4.3	3.9	3.9	4.2
freight as % of total imports cif	17.18	17.22	17.59	17.38	17.10	17.18	17.14	17.40	17.20	17.42	17.44	16.59	17.65	17.41	17.51	17.48	17.64	17.78	17.48	17.55	17.31	17.40	17.62
insurance as % of total imports cif	0.76	0.76	0.78	0.77	0.75	0.76	0.76	0.77	0.76	0.77	0.77	0.73	0.78	0.77	0.77	0.77	0.78	0.79	0.77	0.77	0.76	0.77	0.78

Source: BOU

Annex Table 7: Monthly Exports of Merchandise, 2011-2012 (in USD Million)

		2011												2012										
ID	Nature of Exports	Jan	Feb	Mar	Apr	May	Jun	Jul	Aug	Sep	Oct	Nov	Dec	Jan	Feb	Mar	Apr	May	Jun	Jul	Aug	Sep	Oct	Nov
	Formal Exports:	162.8	174.3	191.5	165.1	187.3	194.2	191.4	184.7	174.3	167.5	177.9	192.3	181.5	197.5	204.5	181.7	216.3	221.2	216.7	220.0	208.9	182.2	197.4
	Manufactured/ Semi processed goods	44.4	43.0	48.4	47.5	53.0	53.5	42.9	46.3	47.2	48.9	54.9	56.0	53.0	54.5	55.5	52.3	63.6	64.8	57.0	64.5	53.1	47.1	51.2
1	Base Metals & Products	7.2	8.2	10.8	9.9	10.7	15.0	9.7	9.6	10.3	10.2	10.5	9.9	9.2	12.7	10.2	9.3	11.5	10.7	12.8	12.7	12.6	10.2	11.1
2	Sugar	4.5	6.5	8.2	9.6	9.0	6.1	2.7	5.3	5.1	6.7	9.1	8.3	5.9	5.7	10.3	10.7	17.4	18.0	11.0	12.7	9.3	5.7	8.8
3	Fish & its products	16.7	12.5	9.4	10.4	13.2	12.1	9.4	9.6	9.6	11.2	12.3	15.9	12.5	12.5	11.8	10.6	12.0	10.4	9.4	8.1	8.5	9.4	8.8
4	Cement	6.7	5.5	7.9	6.1	6.9	8.4	8.7	9.1	8.8	8.5	8.9	8.4	8.5	7.0	8.0	8.8	8.6	10.0	9.7	11.2	9.2	8.8	8.2
5	Edible Fats and Oils	3.6	4.9	4.7	4.3	5.1	4.2	4.5	4.5	4.9	4.7	5.5	3.5	6.2	5.1	4.6	3.2	4.4	4.3	4.4	3.8	3.8	3.2	3.5
6	Soap	2.0	1.7	1.9	2.2	2.4	1.7	2.4	2.6	2.9	2.0	2.1	2.3	3.2	3.2	3.3	2.8	2.8	3.2	2.2	2.7	2.7	2.5	2.4
7	Plastic Products	0.8	0.6	1.7	1.1	2.1	1.9	1.6	2.1	2.3	2.1	2.3	1.9	2.2	2.5	2.3	2.6	1.8	2.4	2.5	7.3	2.1	1.8	2.5
8	Beer	1.4	1.7	2.2	2.4	2.2	2.2	1.9	1.7	1.6	1.6	2.0	2.2	1.6	2.0	2.2	1.8	2.2	2.5	1.8	2.1	2.0	2.2	2.3
9	Water	0.4	0.2	0.4	0.4	0.4	0.4	0.3	0.3	0.2	0.5	0.7	1.4	1.7	2.0	1.6	1.6	1.6	1.8	1.9	2.1	1.6	2.0	2.2
10	Baker's wares	0.8	1.0	1.2	1.1	1.0	1.5	1.6	1.4	1.5	1.2	1.5	2.2	2.1	1.8	1.3	0.9	1.3	1.3	1.5	1.8	1.3	1.2	1.5
	Traditional exports	72.1	75.0	87.9	64.2	77.0	86.3	84.2	72.6	76.8	58.1	62.5	67.0	73.4	78.6	79.9	59.3	82.3	78.4	73.4	61.9	51.1	53.9	63.6
11	Coffee	30.0	27.8	34.1	26.9	40.0	57.9	54.6	44.4	48.8	30.5	34.7	37.0	33.7	36.2	30.2	21.9	35.8	36.6	40.5	31.5	23.5	23.7	28.8
12	Cotton	12.4	17.5	23.5	12.9	8.6	1.5	4.1	1.2	0.2	0.0	0.2	3.7	9.3	11.4	16.3	12.6	9.3	9.2	1.5	1.6	1.3	2.3	0.8
13	Tea	6.6	3.6	4.3	6.0	6.9	6.0	7.1	5.5	5.9	6.3	6.8	6.9	7.4	4.2	3.0	3.7	8.3	6.4	7.1	6.5	5.8	6.7	8.0
14	Tobacco	3.3	6.6	7.3	3.8	4.7	4.3	2.5	3.2	4.0	3.0	6.5	5.4	7.0	6.2	5.7	2.7	5.2	6.7	7.9	5.2	2.2	2.9	6.3
15	Maize	1.7	1.8	1.6	1.3	2.4	1.2	3.0	5.6	3.7	2.9	1.3	0.9	1.7	5.0	8.3	4.1	5.3	5.3	2.9	5.0	8.0	5.0	5.7
16	Flowers	3.9	4.5	3.9	3.7	5.5	4.9	5.5	5.2	4.6	4.0	3.6	3.3	4.7	4.9	4.4	3.7	6.1	5.6	4.8	5.0	3.7	3.6	3.3
17	Hides & skins	2.1	2.9	3.3	3.1	2.6	3.0	2.1	1.9	2.6	3.8	3.2	2.5	2.5	3.5	4.0	3.6	4.9	4.3	3.2	3.2	3.9	4.0	3.2
18	Cocoa Beans	7.4	5.0	5.7	3.7	2.7	3.2	2.1	1.1	2.0	3.0	4.2	4.0	3.8	4.1	4.5	3.1	3.0	2.0	1.1	2.2	1.0	3.0	4.0
19	Simsim	3.2	3.8	3.1	1.3	1.5	0.4	0.1	1.0	1.2	0.8	0.3	0.4	2.0	1.3	2.0	2.2	2.9	0.6	0.3	0.0	0.3	0.4	0.1
20	Beans	0.8	1.1	0.3	0.5	0.9	3.3	2.3	2.7	2.4	2.8	0.8	0.9	0.3	0.7	0.6	0.7	0.3	0.7	3.0	0.7	0.6	1.5	2.3
21	Fruits & Vegetables	0.8	0.5	0.9	1.1	1.1	0.6	0.7	0.9	1.2	1.0	1.0	1.8	0.9	1.1	1.0	1.1	1.2	1.0	1.0	1.1	0.8	0.7	1.1

Source: BOU

Annex Table 7: Monthly Exports of Merchandise, 2011-2012 (in USD Million)

	Minerals	0.9	2.1	2.1	1.9	1.9	1.9	2.4	2.0	1.5	3.4	1.9	3.2	1.5	2.5	1.4	1.7	2.2	1.4	2.1	2.8	1.5	2.6	1.2
22	Cobalt	0.5	1.6	1.8	1.6	1.6	1.6	1.6	1.6	1.0	1.6	1.6	1.6	0.5	1.6	0.5	0.5	1.1	0.5	1.6	2.1	1.1	2.6	1.1
23	Gold	0.4	0.5	0.3	0.3	0.3	0.3	0.8	0.5	0.5	1.8	0.3	1.6	1.0	0.9	0.9	1.2	1.1	0.9	0.5	0.6	0.5	0.0	0.2
	Other exports	45.5	54.1	53.1	51.6	55.4	52.5	61.9	63.7	48.8	57.1	58.6	66.2	53.5	62.0	67.8	68.3	68.2	76.7	84.1	90.8	103.1	78.5	81.4
24	Cellular Phones	7.0	10.8	10.1	9.7	9.0	9.3	15.2	14.7	6.5	11.0	10.8	14.3	9.5	6.0	10.5	7.3	10.1	12.5	13.8	13.9	17.7	17.0	19.3
25	Crude oil	3.6	1.5	3.5	4.0	4.5	3.7	4.1	5.1	3.9	3.9	4.8	3.8	6.5	5.3	3.5	5.2	4.9	4.9	4.6	5.4	16.7	6.1	4.7
26	Rice	0.8	1.0	1.3	0.9	1.5	1.5	1.8	1.7	1.4	2.0	1.8	2.6	2.1	2.4	2.4	3.9	2.8	3.8	3.0	3.7	3.7	3.4	3.7
27	Electricity	1.1	1.1	1.3	1.2	1.2	1.5	1.5	1.7	1.5	1.4	1.4	1.3	1.0	1.5	1.4	1.7	1.5	1.4	1.0	1.2	1.2	1.1	1.1
28	Oil re-exports	9.0	7.9	7.8	9.1	8.1	9.2	9.7	8.1	8.9	9.6	10.4	9.1	7.1	11.7	12.2	9.5	15.7	11.4	12.0	12.6	12.0	12.1	10.9
29	Other items	23.9	31.8	29.1	26.6	31.1	27.3	29.5	32.4	26.6	29.2	29.6	35.1	27.4	35.1	37.7	40.7	33.2	42.7	49.7	54.1	51.8	38.7	41.7
	Informal Exports (Cross Border Trade):	31.5	28.4	25.2	23.0	29.5	31.8	32.8	36.5	29.3	25.7	30.3	31.8	31.8	28.0	34.4	35.6	36.9	33.6	30.1	40.3	43.3	45.5	43.0
1	Industrial products	20.2	19.0	15.5	14.0	18.8	21.5	22.2	25.6	19.5	15.5	16.6	19.7	19.4	16.5	22.2	22.9	23.5	20.2	18.0	24.8	24.3	23.4	24.1
2	Maize	1.4	0.8	0.3	1.0	1.5	0.3	2.2	2.1	1.6	1.4	1.7	1.2	1.5	1.8	1.6	1.8	2.1	2.4	2.2	4.6	4.7	7.0	5.4
3	Fish	2.3	2.5	2.8	2.1	2.8	2.8	2.1	1.9	1.5	1.8	2.4	2.4	2.7	2.5	3.1	3.5	3.9	2.8	2.9	3.0	3.6	3.3	3.3
4	Beans	2.3	1.7	1.1	1.4	1.4	2.6	1.3	1.5	1.6	1.0	2.3	3.0	2.6	1.3	0.7	0.8	1.0	2.2	1.5	1.3	1.6	2.3	1.7
5	Other grains	0.9	0.7	0.6	0.4	0.6	0.5	0.6	0.5	0.5	0.7	0.9	0.5	0.4	0.2	0.9	0.7	0.5	0.7	0.6	0.8	0.7	0.7	0.7
6	Bananas	0.4	0.4	0.4	0.4	0.4	0.3	0.3	0.4	0.3	0.5	0.4	0.4	0.6	0.3	0.5	0.5	0.5	0.5	0.6	0.5	0.6	0.7	0.6
7	Other agricultur-al commodities	3.5	2.6	3.8	3.1	3.8	3.6	3.7	4.0	4.0	4.4	5.7	4.3	4.3	4.9	4.6	4.7	4.9	4.6	3.9	5.1	7.6	7.8	6.8
8	Sugar	0.3	0.4	0.5	0.4	0.1	0.1	0.2	0.4	0.2	0.2	0.1	0.2	0.3	0.4	0.3	0.4	0.4	0.2	0.2	0.2	0.1	0.2	0.2
9	Other products	0.2	0.1	0.1	0.1	0.1	0.1	0.1	0.1	0.1	0.2	0.1	0.1	0.1	0.1	0.5	0.3	0.1	0.1	0.3	0.0	0.2	0.1	0.1
	Total Exports	194.3	202.6	216.7	188.1	216.8	226.0	224.1	221.2	203.6	193.2	208.3	224.2	213.3	225.5	238.9	217.3	253.1	254.8	246.8	260.4	252.2	227.6	240.5

Source: BOU

Annex Table 8: Inflation Rates

Percentage Changes	2001/2	2002/3	2003/4	2004/5	2005/6	2006/7	2007/8	2008/9	2009/10	2010/11	2011/12
CPI (annual average)	-2.0	5.7	5.0	8.0	6.6	6.8	7.3	14.2	9.4	6.5	23.5
CPI (end of period)	3.5	2.4	5.0	4.7	5.2	7.8	8.0	12.5	7.8	6.3	24.3
Food (end of period)	-0.1	3.0	0.0	-6.1	-4.6	7.9	5.4	27.9	16.5	9.3	30.6
Non Food (end of period)						7.3	7.9	8.9	6.7	5.7	20.3

Source: IMF, UBOS

Annex Table 9: Quarterly Average Prices for Selected Items (UGX/Unit)

		2010				2011				2012			
Item	Unit	Q1	Q2	Q3	Q4	Q1	Q2	Q3	Q4	Q1	Q2	Q3	Q4
Sugar	Kg	2,250	2,451	2,558	2,418	2,420	2,695	4,738	5,217	3,088	2,817	2,965	3,069
Milk	Liter	854	842	1,112	1,047	1,102	1,045	1,048	1,006	1,242	1,134	1,110	1,084
Beef	Kg	5,000	5,000	5,046	5,262	5,966	6,625	7,181	7,842	8,000	8,000	7,827	7,835
Washing soap	Kg	2,227	2,300	2,307	2,572	3,138	3,477	3,673	3,895	3,906	3,874	3,740	3,720
Matooke	Kg	535	413	311	499	551	625	532	660	477	611	612	770
Maize floor	Kg	1,472	1,244	1,081	1,057	1,261	1,807	2,133	1,843	1,737	2,096	1,955	1,803
Rice	Kg	2,433	2,355	2,191	2,040	2,273	2,714	2,985	3,246	3,432	3,722	3,186	3,225
Dried beans	Kg	1,682	2,060	1,928	1,961	2,020	2,574	2,058	2,049	2,209	3,052	2,207	2,103
Paraffin	Liter	1,760	1,918	1,980	2,093	2,366	2,670	2,839	2,935	2,727	2,794	2,612	2,799
Petrol	Liter	2,471	2,936	2,970	3,155	3,264	3,557	3,805	3,860	3,483	3,667	3,529	3,668
Diesel	Liter	2,072	2,298	2,351	2,481	2,718	3,201	3,390	3,600	3,277	3,223	3,135	3,397

Source: UBOS

Annex Table 10: Inflation Rates (for selected items), 2011-2012

	2011												2012											
Items	Jan	Feb	Mar	Apr	May	Jun	Jul	Aug	Sep	Oct	Nov	Dec	Jan	Feb	Mar	Apr	May	Jun	Jul	Aug	Sep	Oct	Nov	Dec
All items	5.0	6.4	11.2	14.1	16.0	15.7	18.8	21.4	28.3	30.5	29.0	27.0	25.6	25.7	21.1	20.0	18.6	18.0	14.3	11.9	5.5	4.5	4.9	5.5
Food	3.6	8.8	23.7	30.8	35.3	33.4	40.7	42.9	50.4	45.8	40.4	34.6	27.2	27.6	15.4	15.0	13.7	12.8	5.4	4.2	-2.8	-2.5	-2.0	0.0
Food crops	1.5	6.9	29.1	39.3	44.2	39.0	42.3	33.7	38.8	35.3	25.9	20.4	13.5	21.4	10.1	9.1	8.0	11.3	7.5	12.8	6.3	4.4	7.5	7.3
Non food	6.0	5.4	5.4	6.5	7.4	7.9	9.1	11.7	18.2	22.9	22.9	22.9	24.2	24.3	23.7	22.3	21.0	20.4	19.0	16.0	10.1	8.3	8.6	8.3
Beverages and tobacco	8.9	8.3	9.3	10.3	10.8	10.6	12.1	25.2	26.1	23.3	23.8	24.6	24.1	25.0	23.6	23.2	25.1	25.5	23.6	9.9	6.1	6.2	5.2	8.5
Clothing and footwear	8.7	11.3	13.7	16.5	21.5	22.7	26.0	31.6	37.0	45.0	43.0	43.7	43.8	42.7	39.0	34.9	27.0	19.0	12.5	6.4	2.3	-2.7	-1.2	-3.9
Rent, fuel and utilities	8.7	5.7	7.1	9.5	9.9	8.9	8.5	11.9	26.1	31.8	30.3	30.9	34.5	35.0	31.8	29.1	27.0	25.7	26.9	23.3	10.3	6.0	6.4	7.4
Household and personal goods	11.5	12.8	15.7	17.7	21.0	22.8	24.9	25.9	29.6	30.5	31.8	31.0	28.0	27.3	24.5	22.3	19.4	18.2	15.9	13.1	9.7	7.6	6.3	4.5
Transport and communica-tion	-11.2	-9.7	-15.5	-14.6	-14.7	-12.4	-11.9	-11.2	-1.2	16.9	19.6	19.2	20.9	16.7	24.1	20.8	20.4	17.4	17.4	15.9	4.0	3.6	4.7	5.5
Education	6.4	5.0	5.1	5.3	5.7	8.2	8.9	9.3	10.7	10.7	10.7	10.6	10.9	14.8	14.9	14.7	14.4	18.1	16.9	16.5	16.5	16.5	16.5	16.2
Health, entertainment and others	11.7	11.8	12.8	13.1	14.3	13.0	15.3	17.3	20.0	20.2	20.2	18.7	20.9	20.6	19.2	19.5	19.0	18.0	15.9	13.9	12.3	11.2	11.5	10.2
Other goods	8.5	9.5	13.9	16.6	19.5	20.3	26.0	33.3	44.5	44.0	43.5	42.0	38.0	34.9	27.8	26.6	24.0	20.5	13.6	7.8	-1.0	-1.7	-2.2	-0.8
Services	3.1	2.8	1.7	2.1	2.5	3.2	3.7	4.8	8.5	14.0	14.3	13.7	16.6	17.8	18.9	17.9	17.5	17.7	18.0	16.7	13.5	12.5	13.1	12.8

Source: UBOS

Annex Table 11: Exchange and Interest Rates, 2011-2012

		Nominal	TBR (91)	CBR*	Deposit (LC)	Deposit (FC)	Lending (LC)	Lending (FC)
Year	Month	UGX/USD	%	%	%	%	%	%
2011	Jan	2,332.47	8.8	13.1	2.2	1.2	20.1	10.8
	Feb	2,341.93	9.4	13.9	2.0	1.7	19.6	9.5
	Mar	2,393.31	8.6	13.3	2.1	1.3	20.0	10.1
	Apr	2,367.59	8.8	13.1	2.2	1.3	20.0	9.9
	May	2,387.68	10.4	14.7	2.0	1.3	19.9	9.7
	Jun	2,461.04	12.1	16.7	2.6	1.3	19.9	9.4
	Jul	2,587.23	13.1	13.0	2.8	1.3	21.7	9.7
	Aug	2,753.23	14.5	14.0	4.3	1.2	21.3	9.8
	Sep	2,814.02	15.6	16.0	2.5	1.1	23.3	9.7
	Oct	2,805.37	18.8	20.0	2.4	1.1	23.6	9.5
	Nov	2,582.18	19.6	23.0	3.1	1.6	26.0	10.3
	Dec	2,446.91	20.1	23.0	3.3	1.3	26.7	10.1
2012	Jan	2,414.19	20.3	23.0	3.4	1.3	27.3	10.3
	Feb	2,327.97	17.6	22.0	3.3	1.3	26.8	10.4
	Mar	2,485.02	15.7	21.0	3.4	1.3	27.6	10.0
	Apr	2,506.21	16.3	21.0	3.7	1.2	26.1	8.2
	May	2,479.05	16.4	21.0	3.4	1.4	26.7	9.3
	Jun	2,484.36	16.7	20.0	3.4	1.6	27.0	8.4
	Jul	2,473.96	16.7	19.0	3.4	1.2	26.9	9.0
	Aug	2599.60	12.7	17.0	3.6	1.3	26.4	9.1
	Sep	2592.97	10.7	15.0	3.1	1.2	25.7	8.7
	Oct	2621.40	9.1	13.0	3.0	1.2	24.9	10.7
	Nov	2624.96	9.3	12.5	2.8	1.2	23.6	10.4
	Dec	2614.37	9.4	12.0				

Note: i) LC - Local Currency; FC - Foreign Currency
*ii) * bank rate to commercial banks for Jan-Jan 2011*

Source: IMF, BOU

Annex Table 12: Monetary Indicators

Indicator	2005/6	2006/7	2007/8	2008/9	2009/10	2010/11	2011/12	%
Monetary Aggregates								10.8
M3 as % of GDP	18.0	18.1	20.6	20.9	23.8	26.7	20.9	9.5
M2 as % of GDP	14.1	14.1	15.9	16.3	18.4	20.3	15.3	10.1
M3 growth rate (%)	8.7	16.4	17.4	31.1	25.0	31.7	25.9	9.9
M2 growth rate (%)	12.1	18.9	16.7	30.1	26.3	30.3	23.9	9.7
Domestic Credit								9.4
Total domestic credit (% of GDP)	6.5	4.6	7.0	10.1	13.7	18.5	16.1	9.7
Total domestic credit growth (%)	20.5	-17.6	75.4	78.6	56.9	50.5	11.4	9.8
Private sector credit (% of GDP)	8.0	8.5	11.1	11.9	12.8	16.6	14.3	9.7
Private sector credit growth (%)	28.7	23.2	51.5	32.1	25.0	44.4	9.8	9.5
Interest Rates Structure								10.3
Average TB rate (period average, %)	7.6	8.9	7.9	8.4	5.3	7.6	17.2	10.1
Average lending rate (%)	19.2	18.8	19.6	20.9	20.7	19.8	24.6	
Average deposit rate (%)	2.5	2.7	2.1	2.1	2.0	2.1	3.2	10.3

Source: UBOS

The World Bank

Rwenzori House, 4th Floor
P.O.Box 4463 Kampala, Uganda
Tel: +256 414 230094
E-mail: info@worldbank.ord