

Document of
The World Bank

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Report No: 97145-UG

UGANDA SYSTEMATIC COUNTRY DIAGNOSTIC

***Boosting Inclusive Growth and Accelerating
Poverty Reduction***

December 4, 2015

International Development Association
Country Department AFCE2
Africa Region

International Finance Corporation
Sub-Saharan Africa Department

Multilateral Investment Guarantee Agency
Sub-Saharan Africa Department



WORLD BANK GROUP

REPUBLIC OF UGANDA - GOVERNMENT FISCAL YEAR

July 1–June 30

CURRENCY EQUIVALENTS

(Exchange Rate Effective as of *November 30, 2015*)

Currency Unit = Uganda Shilling (UGX)
US\$1 = UGX 3355.0

WEIGHTS AND MEASURES

Metric System

ABBREVIATION AND ACRONYMS

ACCS	Advisory Consortium on Conflict Sensitivity	MDG	Millennium Development Goal
AIDS	Acquired Immunodeficiency Syndrome	MoES	Ministry of Education and Sports
BTVET	Business, Technical, and Vocational Education and Training	MoESTS	Ministry of Education, Science, Technology and Sports
CEM	Country Economic Memorandum	MoFPED	Ministry of Finance, Planning, and Economic Development
COMESA	Common Market for Eastern and Southern Africa	NBI	National Backbone Infrastructure
CNOOC	China National Offshore Oil Corporation	NCD	Noncommunicable Diseases
CPIA	Country Policy and Institutional Assessment	NDP	National Development Plan
CSO	Civil Society Organization	NSSF	National Social Security Fund
EA	Exploration Area	OAG	Office of the Auditor General
EAC	East African Community	OOP	Out-of-Pocket
EPRC	Economic Policy Research Center	PEFA	Public Expenditure and Financial Accountability
FINMAP	Financial Management and Accountability Program	PFM	Public Financial Management
GDP	Gross Domestic Product	PIM	Public Investment Management
GNI	Gross National Income	PIMI	Public Investment Management Index
GoU	Government of Uganda	PPP	Purchasing Power Parity
HIV	Human Immunodeficiency Virus	SACCO	Savings and Credit Cooperatives
ICT	Information and Communications Technologies	SCD	Systematic Country Diagnostic
IFMS	Integrated Financial Management System	SDI	Service Delivery Indicators
IMF	International Monetary Fund	SSA	Sub-Saharan Africa
IPPS	Integrated Payroll and Pension System	TFP	Total Factor Productivity
JMP	Joint Monitoring Program	TFR	Total Fertility Rate
LG	Local Government	TSA	Treasury Single Account
LIC	Low Income Country	UBOS	Uganda Bureau of Statistics
LRA	Lord's Resistance Army	UN	United Nations
MacMod-UG	Macroeconomic Model of Uganda	UNHS	Uganda National Household Survey
MDAs	Ministries, Departments, and Agencies	UNICEF	United Nations Children's Fund
		WDI	World Development Indicators
		WEF	World Economic Forum

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ACKNOWLEDGEMENTS

This Systematic Country Diagnosis (SCD) was prepared by a multi-sectoral team led by Mona Prasad (Senior Economist) and Jean-Pascal N. Nganou (Senior Country Economist) with close support from Jacques Morisset (Program Leader) and Kevin Carey (Lead Economist). Core team members include Ruth Hill, Clarence Tsimpo, Anton Dobronogov, and Rachel Sebudde. The full team is listed below.

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Sincere appreciation to our peer reviewers: Abebe Adugna (Adviser, MDI), Khwima Nthara (Program Leader, AFCW2), and Kathleen Beegle (Program Leader, AFCW1).

The SCD was prepared as a joint product of IDA/IBRD, IFC, and MIGA. The work was carried out under the supervision of Philippe Dongier (Country Director, AFCE1) and Diarietou Gaye (Country Director, AFCE2), John Panzer (Director, MFM), Albert Zeufack (Practice Manager, MFM), and Ahmadou Moustapha and Christina Malmberg Calvo (Country Managers, AFMUG). Helpful comments were received from Vinaya Swaroop (Global Lead, MFM), Gallina Vincelette (Program Leader, ECCU4), Sajjad Shah (Country Program Coordinator, AFCTZ), and the SCD advisory committee. Contributions by Franklin Mutahakana (Senior Operations Officer, AFMUG), Asger Hallberg Borg (Country Officer, AFMUG), and the AFMUG team are greatly acknowledged. The team received insightful feedback from the participants of the SCD consultations and the national advisory SCD task force. Gladys Alupo (Program Assistant, AFMUG) and Damalie Nyanja (Team Assistant, AFMUG) provided operational support. Sarah Babirye (Program Assistant, GMFDR) formatted the report.

EXECUTIVE SUMMARY

1. **Following the end of the armed conflict in 1986, the Ugandan government introduced a number of structural reforms and investments, which boosted growth and reduced poverty.** The resultant macroeconomic stability, post-conflict rebound, and pro-market reforms generated a sustained period of high growth during 1987–2010. The gross domestic product (GDP) expanded at an annual average rate of 6.9 percent, one of the fastest among African countries, and Uganda transformed from a failed state to one of the fastest growing economies in the world. Per capita GDP, however, grew at a more modest pace of 3.6 percent per year during this period, essentially because of the country's high fertility rate. Growth has recently decelerated to 5.5 percent during FY2011–14, largely attributable to shocks, including the global turbulence, aid disruptions, and weather; domestic policy slippages (such as increased election-related spending); and a waning growth dividend from the first spurt of reforms. The sustained output expansion since the early 1990s had a significant beneficial impact on poverty reduction and shared prosperity. Uganda's stellar economic performance from 1987–2010 reinforces the need to maintain macroeconomic stability and continue with structural reforms. But high fertility is associated with obstacles to well-being which particularly afflict the youth.

2. **However, nearly three decades after the reforms began, Uganda still faces many challenges.** With gross national income (GNI) per capita at US\$660 in 2014 (up from US\$310 in 1987), Uganda lies below the low-income countries (LICs) average of US\$709. Many of the current development challenges facing Uganda are well-understood by the policy makers but there has not been significant progress in addressing them. These challenges include poor infrastructure, weak public service delivery, low levels of human capital, and underdeveloped institutions. These aspects, along with a host of other constraints facing Uganda are reflected in the government's National Development Plan and Vision 2040. The key challenge is, therefore, to address these constraints through a set of coordinated actions which close the large gap in implementing policies. Hence, what is really needed in Uganda is 'how to do' rather than 'what to do'.

Poverty and Shared Prosperity

3. **The proportion of the population living in poverty—whether measured using the national poverty line or the international poverty line—more than halved from 1993 to 2013.** According to the national poverty line, the proportion of the population living in poverty declined from 56.4 percent in 1993 to 19.7 percent in 2013. The incidence of extreme poverty measured by the international poverty line of US\$1.25 a day (2005 purchasing power parity [PPP]) declined from 71.9 percent in 1993 to 30.6 percent in 2013. This declining trend is confirmed when using the recently released international poverty line of US\$1.90 a day (2011 PPP) as poverty incidence declined to 33.2 percent from 68.1 percent over the same period. Over the last ten years, Uganda reduced the proportion of the population living under US\$1.25 a day faster than any other country in Sub-Saharan Africa (SSA).

4. **Moreover, prosperity was shared with the poorest segments of the population as annual consumption growth of the bottom 40 percent in the income distribution averaged around 3 percent during 1993–2013.** This was higher than most other countries in the region.

However, in relative terms, consumption growth of the bottom 40 percent was slower than the consumption growth of the top 60 percent.

5. **Within the enabling environment of macroeconomic stability, most of the progress on the twin goals was attributable to higher agricultural incomes.** Poverty reduction among households primarily engaged in agriculture accounted for 53 percent of the reduction in poverty from 2006 to 2010 and 77 percent of the reduction in poverty from 2010 to 2013. The increase in aggregate crop production came largely from the expansion of the area under cultivation, favorable weather, and high prices (in the domestic and regional markets) and marginally because of an increase in the use of modern production technologies. Improvements in access to markets and extension services also seem to have helped. The dependence of agricultural incomes on exogenous factors such as good weather and prices rather than on productivity-enhancing factors such as technology, training, irrigation, and farm-to-market infrastructure, renders it susceptible to shocks and raises concerns about sustainability. In addition, the contribution of the agricultural sector to GDP has declined over time (about 25 percent of GDP currently) and the sector has grown at an average annual rate of 2 percent over the past five years. For continued poverty reduction, there is a need to raise agricultural productivity, including through the use of modern production technologies, as well as sustainable land and water management.

6. **Growth in nonfarm self-employment, and to a lesser extent wage employment, over the past decades also raised incomes of the bottom 40 percent.** The bottom of the consumption distribution has largely transitioned into self-employment in the informal sector to supplement their incomes while those who have transitioned to wage employment have generally had higher levels of education. Improvements in infrastructure, health, and education also contributed to poverty reduction. Raising nonfarm incomes and reducing dependence on the agricultural sector will require a boost to private sector competitiveness.

7. **Despite significant progress on the twin goals, vulnerability to poverty in Uganda is high and the sparse social safety nets and limited access to finance have provided little protection.** Around 43 percent of Ugandans were insecure non-poor in 2013, defined as those living above the national poverty line but living on less than twice the national poverty line. Between 2005 and 2009, for every three Ugandans who were lifted out of poverty, two fell back into poverty, illustrating the fragility of the gains realized by the poorest households. Uganda's success in reducing poverty has resulted in many households that are living just above the poverty line remaining vulnerable to falling under the poverty line in the face of a negative shock. These shocks can take various forms such as political and regional instability, particularly in neighboring countries, unexpected health issues, and natural hazards which negatively impact agricultural incomes. When faced with such shocks, the poor have limited recourse to social safety nets (only 4.5 percent of the total population receive any kind of direct income support) or access to finance (65 percent of the population lacks access to credit). As a result, they are unable to smooth consumption or to afford health care and education, resulting in a depletion of assets. Given the high level of vulnerability, there is a need to have some basic level of social safety nets, access to savings instruments, and other means of finance and a need to improve the quality and efficiency of public services. Notwithstanding these improvements, an increase in farm and nonfarm incomes remains a prerequisite for sustained reductions in poverty and vulnerability.

8. **Inequality, as measured by the Gini index, rose from 0.36 in 1993 to 0.40 in 2013, explained by the regional distribution of poverty and conflict.** The sustained conflict in the north, which has put the region back by several years, could also have contributed to increased inequality and a slower rise in the incomes of the poor. In 2006, approximately 60 percent of the poor lived in the northern and eastern parts of the country. Seven years later, this proportion increased to 84 percent. There is therefore a need to maintain peace and stability and improve public service delivery, particularly in the north. As a result, consumption growth of the bottom 40 percent (mainly from the northern region) was slower than the consumption growth of the top 60 percent. In addition, inequality was higher in cities possibly because consumption opportunities are higher for the wealthier urban households. Nonetheless, Uganda faces moderately low inequality in comparison to other countries in the region.

9. **Poverty is more prevalent in rural than in urban areas.** In 2013, the poverty rate was 22.8 percent in rural areas compared to only 9.3 percent in urban areas. This was because income opportunities are lower in villages than in cities and access to social and infrastructure services are far more limited in rural areas. Therefore, any strategy to reduce poverty in Uganda will have to account for the large fraction of the population living in rural areas (84 percent). Hence, poverty reduction would need to entail productivity gains in agriculture together with better access to markets, further diversification in the source of income of rural households, and migration toward urban centers. This also highlights the need for increased urbanization in Uganda which remains relatively low at about 15 percent in 2013. International experience shows that urbanization, through agglomeration effects, can boost growth and the initial gains from urbanization are already evident in Uganda. More than 70 percent of manufacturing activities are conducted in urban areas while 65 percent of the new formal jobs over the past decade were created in cities and urban centers. The key constraints to urbanization in Uganda include the policy and legislative framework, the land tenure system and housing, among others.

10. **The bottom 40 percent live in larger families which erodes their ability to accumulate assets.** At 6.2 children per woman, Uganda has one of the highest fertility rates in the world. Household size in the bottom 40 percent is estimated at 6 members on average compared to 4.6 in the top 60 percent. As a result, the dependency ratio is 13 percentage points higher for those living in the bottom 40 percent. The bottom 40 percent therefore have lesser resources to invest in health and education which in turn impedes their income earning capacity. This reinforces the need to reduce fertility rates.

11. **Against this backdrop, a change in economic and social policies is required to prevent a slowdown in poverty reduction and an increase in vulnerability.** Like most countries in the world, poverty reduction in Uganda will largely be driven by the country's capacity to grow at a faster rate in the medium term and to share that growth with the population. Generating more productive jobs will be at the center of this agenda. The country will either have to raise the productivity of sectors employing the bulk of the labor force and/or shift the working force to sectors and locations of higher productivity growth following the example of China or other East Asian countries, which will eventually increase the elasticity of poverty reduction to GDP growth. A combination of these two options will be optimal and there is a need to design and implement a comprehensive growth and development strategy that will reduce poverty sustainably while addressing vulnerability concerns.

12. **In this context, a comprehensive framework based on the three interrelated blocks of growth, inclusion, and sustainability has been used to identify the challenges to and opportunities for ending poverty and boosting shared prosperity.** The first block emphasizes the development of a competitive and resilient private sector to lead the growth process by adequately capitalizing on all the available opportunities. The second block, complementary to the first one, reinforces the need to ensure a fair distribution of the growth dividend across all Ugandans, especially those living in the north and the east, by providing them with access to social and infrastructure services so that they can increase their productive capacity and income-generating opportunities. The third block emphasizes the need to undertake the inclusive growth process in a fiscally, socially, and environmentally sustainable manner. The analysis includes a macro-micro interactive approach. On one hand, it assesses macro factors such as the business environment, macroeconomic policies, public sector effectiveness, and overall institutional development which affect growth, inclusion, and sustainability. This is fused with an assessment of factors influencing the productive capacity of households to contribute to the growth process through the accumulation of assets. The income-generating capacity of individuals depends on assets such as human, physical, natural, financial, and social capital.

Growth-Poverty Links

13. **Uganda's poverty story evidences weak links with growth.** Notwithstanding its sluggish contribution to growth, the agriculture sector was the main driver of poverty reduction in the country. In addition, the amount of poverty reduction achieved in Uganda was moderate given its high rate of consumption growth over the past two decades. The growth elasticity of poverty reduction during 2000–10 was 1.09 in Uganda, lower than its Common Market for Eastern and Southern Africa (COMESA) counterparts (Kenya, 2.02; Zambia, 1.42; and Ethiopia, 1.39). However, Uganda scored a far better growth-poverty reduction elasticity compared to its East African Community (EAC) peers (Rwanda, 0.75 and Tanzania, 0.57).

14. **On the demand side, consumption was the main driver of growth in Uganda and this is likely to continue given its low level of income.** Private investment and consumption responded favorably to the pro-market reforms and the increase in incomes of the population. Given its low income level, the high share of consumption in income, and the relatively closed economy, an increase in income can produce large multiplier effects. As a result, the share of private consumption in aggregate demand has averaged around 80 percent since 1990. Public consumption also contributed, although the ratio of public expenditures to GDP decreased slightly from 23 percent in 2002 to 20 percent in 2010. There is room for further growth in consumption as the country develops. However, for this to happen, sustained growth will be crucial.

15. **On the supply side, the services sector has been driving the economy and this is unlikely to directly benefit the poor who remain in agriculture and have low levels of education and skills.** The services sector currently accounts for more than half the GDP. Growth in the sector was primarily led by communication, transport, and financial services, reflecting higher local demand and technological changes (dominated by the mobile phone revolution). Growth in these subsectors exceeded 7 percent during the last decade and is likely to continue in the future. While services-led growth has reduced transaction costs and has raised the demand for urban goods and services, it has not been a direct source of income for a majority of the population because they do not have the skills to be employed in high-end services. Poverty analysis shows

that those who have transitioned to formal wage employment generally have more years of education. Hence, building human capital by improving public health and education services will help include more of the poor people in the growth process in the future.

16. **Since 2000, the contribution of total factor productivity (TFP) to growth has declined.** TFP explained about 34 percent of Uganda's GDP growth during the period 1990 to 2000, and 28 percent over the period from 2001 to 2010, but its contribution to growth was minus 15 percent during 2011–12. The reforms in the late 1980s resulted in significant growth in TFP during the 1990s, reflecting rebound on account of post-conflict reconstruction and policy reforms, as well as transformational growth. Since then, TFP growth has slowed down indicating lower returns to investment, possibly due to suboptimal allocation of resources and limited progress on competitiveness. The decline in public investment also partly explains the lower overall returns on investment since it complements private investment.

17. **The informal sector accounted for most of the jobs created in the nonagricultural sector.** The majority of the Ugandan population is still engaged in agriculture but the sector's contribution to the GDP has been on a declining trend. The Uganda Bureau of Statistics (UBOS) estimates that 79 percent of the firms in Uganda are informal. The World Bank's 2013 Enterprise Survey, which focuses on the urban sector, also shows that only 63 percent of Ugandan firms which started their business in the past year were operating in the formal sector, which is low by regional and international standards. Most of the poor and vulnerable are typically engaged in the informal sector where they are underpaid, subject to hazardous working conditions, and unable to improve their skill base. The majority of the informal enterprises are engaged in retail sales but a large number of them are also in light manufacturing (brick making, charcoal manufacture, and beverages). Nearly 31 percent of informal sector workers receive pay only in the form of food and lodging and not cash.

18. **The bulk of jobs created in Uganda are in low-productivity sectors.** Agriculture, commerce, household-based services, and informal manufacturing are among the most common activities in Uganda, all of them being at the low end of the productivity spectrum. While the jobs are in general more productive than in subsistence agriculture, they require limited skills. The average monthly wage is estimated at UGX 85,000 in agriculture and UGX 188,000 for other services and commerce, most of which are informal activities.

19. **The waning reform dividend calls attention to the main constraints to broad based growth.** Several factors constrain growth in Uganda but a series of analytical studies and surveys have repeatedly underscored inadequate infrastructure, both electricity and roads as well as water supply. The electricity situation has improved with the commissioning of the Bujagali hydropower plant but the cost of electricity remains high and many enterprises complain about the inflated cost of electricity during peak hours (between 6 p.m. and midnight).¹ In addition, power outages or load shedding is frequent in Uganda. In the road sector, Uganda still suffers from poor transit and transport infrastructure which has raised the cost of doing business. Being a landlocked country with underdeveloped rail and inland water infrastructure, the national road networks are the main

¹ According to the 2013 Enterprise Survey

conduits to the markets and to consumers. Yet, overloading and inadequate road maintenance has resulted in the fast deterioration of the roads.

20. **Other critical constraints for firms include access to finance, skills, and business regulations.** The cost of finance is particularly high in Uganda—very few Ugandan firms have a bank loan/line of credit and the ones who have a loan get it at a high cost and huge collateral requirements. This is partly because only 20 percent of Uganda’s land is registered and most of the registered land is *mailo* (tenure) which is unsuitable as collateral since it cannot be liquidated by banks as the rights of the landowners overlap with those of the tenants (legally recognized as lawful or bona fide occupants) who enjoy inheritable and transferrable rights as landlords. With limited access to formal credit facilities, most start-up capital for firms comes from own savings or informal credit sources. On skills, although many graduates are not finding jobs, inward migration of consultants and skilled workers, especially in hi-tech financial services, telecommunications, and engineering indicates a shortage of specific skills and mismatch between demand and supply of these skills. Lastly, several business regulations, particularly those pertaining to taxes, land, buildings, construction permits, and border crossings also constrain firms.

21. **Looking forward, the oil sector, regional integration, information and communication technologies (ICT) development, and efficient urbanization offer significant opportunities to raise growth through structural transformation.** The oil sector can stimulate growth directly through increased exports and indirectly through the efficient use of public revenues and the development of linkages with the local private sector. Regional integration can facilitate access to markets and thereby boost the movement of goods, people, and capital. ICT developments can improve firms’ competitiveness and improve the delivery of public services. The urbanization process can provide new opportunities for job creation and improved living conditions as experienced elsewhere in the world and in Uganda wherein urban areas have lower poverty and high consumption levels compared with rural areas. Capitalizing on these opportunities will require the policymakers to address constraints in several areas including public financial management (PFM), governance, transport and ICT backbone infrastructure, and underdeveloped land markets.

22. **However, agriculture will continue to remain relevant in future given its impact on poverty reduction and backward and forward linkages with other sectors like agro-processing.** The productivity performance of the agricultural sector in Uganda has been rather modest and the sector has been characterized by low yields and weak value chains and market linkages. Ugandan farmers can increase their earnings through commercialization and crop and market diversification. Commercialization in Uganda will require farmers to move away from subsistence farming through improvements in productivity with the use of modern equipment and improved quality inputs (fertilizers and seeds), sustainable land and water management to address environmental concerns, improved skills, and better access to finance. However, progress within the farms will not be sufficient as linkages with markets also need to be strengthened through better transport and storage (post-harvest loss is estimated at 40 percent) infrastructure, transparent and competitive value chains, and consistent government policies (including taxation). Crop and market diversification is also important as it will help farmers to hedge the risks. A shift toward high-value vegetables or fruits can also bring additional jobs and foreign exchange.

Asset Accumulation and Inclusion

23. **To ensure that future growth dividends are enjoyed by a majority of the Ugandans, the government needs to build human and physical capital.** So far, Uganda has underinvested in its asset base, both human and infrastructure related, and this has had a significant impact on the income-generation capacity of its citizens.² For Ugandan citizens in general, and more so for the extreme poor and the vulnerable (an additional 43 percent of the population), access to social and infrastructure services is severely limited and of questionable quality. This has led to lower levels of human capital and lesser income-generation possibilities. The Ugandan population aged above 25 years has an average of 4.7 years of schooling whereas the women in this group have only 3.8 years of schooling. Currently, there are almost no students belonging to the bottom 40 percent who are enrolled in tertiary education.

24. **Gender disparities are considerable.** About 68 percent of children, especially girls, are dropping out of school to help at home or join other economic activities. While there is gender parity at the primary level, the percent of girls in total enrollment declined to 47 percent in secondary education, and 44 percent in tertiary education. The country has one of the highest fertility rates in the world and lower life expectancy at birth compared with other LICs. Malaria, maternal and neonatal disorders, Human Immunodeficiency Virus (HIV)/Acquired Immunodeficiency Syndrome (AIDS), and diarrheal diseases are the main health concerns and about 40 percent of the population report to have suffered from an illness or accident over the last 30 days.

25. **Households lack the complementary public assets and access to markets to be more productive.** Access to electricity through the grid network in Uganda is estimated at 14 percent nationally and 7 percent in rural areas, compared to the SSA average of 24 percent. Uganda's district and rural roads are in poor condition resulting in poor connectivity to markets and other services, especially for the poor. And nearly 65 percent of the population has no access to credit which together with the lack of a comprehensive social safety net, limits the ability of households to smooth consumption in the face of shocks.

26. **Public spending on education, health, and social protection, is low, even when compared with other LICs.** This has contributed to limited asset accumulation by poorer individuals which has in turn restricted their chances of moving out of poverty. With limited social protection and lack of access to credit, vulnerable families have fallen back into poverty in the event of an adverse shock and the poor have struggled to smooth consumption. In addition, children have dropped out of school to help at home or in other economic activities while the poor have not sought health care when needed. These difficulties faced by the poor highlight the need to increase public spending on social protection, education, disease prevention, and health services but along with efficiency improvements in the delivery of these public resources.

27. **There are quality concerns across the board in the delivery of public services.** These concerns reflect constraints on accountability arising from the incentive structure as well as governance challenges that Uganda faces. There are neither sufficient rewards for good performance nor sanctions for poor performance. This is coupled with a constrained frontline

² However, Uganda fares better than the SSA average on the human development index.

working environment in which there is a lack of textbooks in schools or drugs in health centers. These constraints together with a low-skilled workforce has resulted in low-quality teaching and health services. There is a need to improve the quality and relevance of health and education services by addressing sector-specific challenges. Strengthened voice and accountability, on the other hand, will raise the demand for better public services.

28. There is inequity in access to finance and in access to public services, particularly for the poor living in rural areas and in the north of the country. The poor depend on public services much more than the rich, who can afford private services, especially in health care and education. Access to infrastructure services is much more limited in rural areas where most of the poor live. Access to electricity in Uganda is one of the lowest in the world. Given the difficult working environment in the north as a result of conflicts and an influx of refugees from neighboring countries, the quality of public service delivery is much worse in the north and has resulted in poorer education and health outcomes and lower standards of living. It has also contributed to intergenerational transmission of poverty. While access to public social and infrastructure services needs to be improved throughout the country, special focus is needed in the northern region.

29. Raising the incomes of the bottom 40 percent in the medium term will require further accumulation of assets. This will require that the poor get access to quality social services (for example, education and health) to be provided mainly by the public sector. But, even if the government had the resources to spend, building human capital takes time and in the meanwhile, focused interventions in agriculture are needed to raise the incomes of the bottom 40 percent in the short to medium terms.

30. In the short to medium-term, a boost in farm incomes will require investments in infrastructure (rural roads, irrigation, and storage), natural resource management, and extension services, particularly in the north. The gains from increased agricultural income so far have largely accrued from an increased area under cultivation, favorable weather, and high commodity prices. Such gains are generally not sustainable and can easily be reversed. Moreover, there are limits to further increasing the land under cultivation except in the north. Therefore, agricultural productivity needs to be raised, which will need higher use of quality inputs, better storage facilities, improved land tenure security, and increased access to markets and inputs. This will need a strengthening of the rural and district road network, accelerating systematic land registration, developing capacity of land dispute resolution institutions, and more effective extension services to educate farmers on the advantages of using more inputs. In addition, various measures, including among others, the development of the irrigation infrastructure, improving agricultural water management, and insurance schemes will help reduce current and future weather-related risks and will also support agricultural commercialization. In the north and, to a lesser extent, in the east, where there is considerable scope to increase agricultural production through area expansion, investments and policy measures are needed to promote rental markets in communal land by formalizing landowning groups and registering their land.

Progressing Sustainably on the Twin Goals

31. It will be important to make the growth and inclusion process sustainable to avoid reversals in the gains made in poverty reduction and shared prosperity and also to make

further progress on them. This will require progress on the twin goals to be fiscally, socially, and environmentally sustainable. In this context, accumulation of wealth and effective management of resources will be crucial. In addition, addressing the large infrastructure gaps and poor social service delivery will require improvements in public sector management, particularly fiscal management and governance. Similarly, a sustained increase in per capita incomes will be aided by a reduction in the fertility rate.

32. Diversified development—in the sense of a more balanced contribution from institutions, assets, and natural resources—is the best way to sustainably achieve the twin goals in Uganda. Achieving this contribution requires a strategy articulated around four building blocks: (a) ensuring that oil revenues are able to ease the financing constraints on critical social and infrastructure investments which currently face a difficult choice between them; (b) strengthening of results orientation in the public sector to realize the benefits of existing institutional reforms; (c) a reconfigured relationship with the private sector, more focused on the enabling environment in terms of regulatory institutions, market functioning, and infrastructure; and (d) spatial policies which can calibrate a policy mix matched to the distinctive needs of rural and urban areas and the foundational market institutions for each, especially regarding land.

33. Making growth sustainable will require accumulation and conservation of wealth. Uganda's total wealth is low compared to other countries in SSA. Its total wealth per capita (excluding oil) at US\$7,190 in 2010 represented a growth of over 30 percent during the last decade. However, this was below most of its peers in East Africa, and well below the largest economies in SSA.³ In addition, the share of intangible and produced capital in the total capital was relatively low. Research has shown that across countries, the share of institutional capital tends to be lowest for oil producers. Uganda cannot afford to enter the oil era with an already low institutional base and hence there is a need to improve infrastructure, human capital, and institutions.

34. With the majority of the poor and those in the bottom 40 percent dependent on agriculture, sustainability of the natural environment is crucial for Uganda. Nearly 46 percent of the land in Uganda is severely degraded. Land is increasingly being transformed because of agricultural expansion (conversion to croplands, pastures, and so on), unsustainable agricultural practices, expansion of urban areas, and other pressures. Average soil erosion is estimated to exceed 5 tons per hectare per year, and the associated soil nutrient loss is particularly pronounced because most of the nutrients in tropical agriculture are in the top 5 to 10 centimeters of the soil. This has significant implications for future agricultural production. In addition, Uganda lost over 40 percent of its forest cover over the past two decades, largely due to fuel wood/charcoal consumption, clearing for agriculture, and timber for construction. Also, significant overharvesting, poor fishing methods, and degraded water quality have contributed to the 50 percent decline in the catch of the Nile perch in Lake Victoria since the mid-2000s peak. Given the importance of the agricultural sector on poverty reduction, improving natural resources management including land, forests, and water resources will be crucial for Uganda.

³ In the absence of oil, Uganda's total wealth per capita would have risen by only 12 percent in real terms from 2009/10 to 2014/15. If the discovery of oil is taken into account, Uganda's wealth (measured as the discounted per capita consumption expenditure over the next 25 years) grew by 26 percent in real terms during the same period.

35. **Effective public sector management is not only a sustainability concern but it also impacts growth and inclusiveness.** The key issue in the public sector is the policy implementation gap which is the result of a lack of enforcement of sanctions (mostly driven by political incentives) and a lack of capacity. Public institutions in Uganda tend to perform poorly, the acquired capacity is underutilized, and laws are not fully implemented. Uganda has one of the biggest implementation gaps in anticorruption legislation in East Africa. According to the World Governance Indicators, Uganda's government effectiveness and regulatory quality are on a declining trend. The voice and accountability environment, which improved between 2003 and 2008, has also deteriorated. Uganda's capacity to control corruption appears to have reached an all-time low and is only above that of Kenya's, East Africa's worst performer. Transparency International's Global Corruption Barometer Survey (2013) found that 61 percent of Ugandans had paid a bribe to one of the eight institutions (judiciary, education, tax services and customs, permits/registries, medical services, police, land services, or utilities) in the last 12 months. The quality of the decentralization framework has worsened since 2005 mainly due to the proliferation of districts without adequate manpower and budget. This has negatively impacted service delivery. Uganda's performance in PFM is good on transparency but weak on budget credibility, controls, and compliance, essentially highlighting implementation gaps.

36. **Addressing the large infrastructure gaps and poor social service delivery will require targeted improvements in fiscal management and governance.** Uganda ranks 46th out of 71 countries on the Public Investment Management Index (PIMI) of the International Monetary Fund (IMF), with relatively poor scores in project implementation and evaluation. An IMF report (2013) noted that Uganda's public investment performance is characterized by poor planning, delayed procurement, and under execution. The Auditor General's annual reports regularly identify weak compliance with PFM regulations, resulting in avoidable or wasteful expenditure, buildup of arrears, inadequate accountability and, in some cases, the risk of fraud or misappropriation. The unpredictability in the budget is often due to a lack of internal controls and poor planning. Some of the most significant risks of wastage, errors, delays, and fraudulent losses are found in payroll and pensions management. Around 70 percent of public expenditures go through procurement systems that are affected by poor practices. While there has been a significant improvement in the quality of audits produced by the Office of the Auditor General (OAG), there is a large backlog of audit reports that are not debated in the parliament and these reports are not published, creating a missing step in the accountability cycle. The recent adoption of the PFM Act was a big step toward alleviating some of these concerns as it introduced a contingencies fund to finance unforeseen, but urgent and unavoidable expenditures without destabilizing other components of the budget. In addition, the government is committed to rolling out the Integrated Payroll and Pension System (IPPS), introducing biometric payroll records for civil servants, and decentralization of the payroll to improve accountability.

37. **Sound oil revenue management will be critical to leverage the benefits of extractives while minimizing associated risks.** Since mismanaged natural resources can have devastating consequences, well-performing PFM systems and governance structures will be paramount to mitigate these risks. The country is also challenged by a lack of sanctions against corruption, ineffective accountability, and weak local institutions, among others. It is well-documented that natural resource-rich countries risk experiencing retarded growth and development because of the Dutch disease and other related consequences of the natural resource curse, if oil revenue is not managed properly. Uganda therefore needs to address its governance and PFM institutional

capacities including public administration to sustainably benefit from the underground resource, which entails a huge potential for its future growth and development.

38. **In the Ugandan context, social cohesion is also a crucial element of sustainability.** The significant differences in the standard of living of residents in different parts of the country, the influx of refugees from nearby countries, and a growing labor force or the youth bulge with insufficient jobs, can result in social instability. Systematic exclusion of certain groups from the growth process can exacerbate the divide within the population and this is particularly true for the Ugandans living in the north of the country who have a much lower standard of living, on average, than those in the other parts of the country. These differences highlight the need to focus public resources in the north, improve the linkage between skills development and labor market requirements, and promote job creation initiatives for the youth.

39. **The high fertility rate has stretched the limited resource base of households and the government and has lowered asset accumulation by the citizens.** A sustainable improvement in the standard of living of Ugandan citizens is unlikely with the existing fertility rate. The key to reducing fertility is to promote programs which combine education and vocational training for women together with training on family planning and health. In addition, it is also important for men to be a part of the training on family planning. However, it is also important to recognize that fertility preferences are rooted in social and cultural values and usually take time to reduce perceptibly.

Prioritizing among Constraints

40. **Achieving the twin goals in a sustainable manner will be a tall order for Uganda but business-as-usual is not an option either.** There are several binding constraints facing a poor, and landlocked country that has a deficit of infrastructure, low educational attainment, a high disease burden, and weak institutions. These constraints coupled with a limited resource base make it imperative for the government to prioritize its interventions. The prioritization of constraints in this SCD are primarily based on their impact on the twin goals of reducing poverty and boosting shared prosperity.

41. **The prioritization process included a review of the evidence, consultations with stakeholders in Uganda, and team discussions.** The starting point for the prioritization process was the evidence and analysis presented in this report. This was used to identify the key challenges in the growth, inclusion, and sustainability domains. A first round of consultations was held with the government, academia, civil society organizations (CSOs), and the private sector on the main constraints and opportunities facing Uganda. The team then used informed judgment to prioritize the constraints. A second round of consultations was also held with the stakeholders during which most of the identified constraints were reinforced. The priorities reflected in the SCD represent the collective judgment of the team which has significant institutional memory on Uganda and the process is more an art than science. These priorities are also reinforced by the existing evidence base and analytical studies.

42. **The prioritization process resulted in the identification of eight priority areas which are summarized below.** These priorities are based on their linkages with the poverty reduction story and the need to ensure continued progress on the twin goals in the future (table 1)

Table 1. Priorities for Making Progress on the Twin Goals in Uganda (not ranked in any order of importance)

Priority areas	Proposed Actions
Macro-fiscal stability	<ul style="list-style-type: none"> • Improving domestic revenue mobilization and tax administration • Strengthening the allocative and financial efficiency of the budget by implementing clear and transparent PFM rules, strengthening public investment management (PIM) and procurement, and encouraging public private partnerships to enable delivery of critical services • Strengthening debt management to ring fence rising commercial borrowing and the burden of debt service • Building awareness of need for highly resilient fiscal institutions ahead of the onset of oil revenues
Agricultural productivity and commercialization	<ul style="list-style-type: none"> • Improving land and water management (for crops, fisheries, and livestock) in a sustainable manner • Improving agricultural storage facilities • Strengthening extension services, particularly in the north and the east • Increasing the use of quality agricultural inputs • Improving rural feeder roads, particularly in the north, to reduce input costs and increase market access • Increasing agricultural access to finance • Strengthening land tenure security, rental markets, and institutions for land administration • Preventing further land degradation, deforestation, and over fishing • Addressing challenges of climate variability and change
Consumption smoothing	<ul style="list-style-type: none"> • Strengthening the social protection system • Increasing access to credit and financial services, particularly, savings instruments for individuals
Public service delivery	<ul style="list-style-type: none"> • Increasing public health and education expenditures with efficiency improvements • Increasing access to social and infrastructure services for the bottom 40 percent and for the people in the north and the east of the country • Improving the quality of public services (education, health, water supply and sanitation, electricity, roads, land, and the Internet) by addressing sector-specific challenges • Improving the demand side of good governance by promoting voice and accountability of citizens
Urbanization	<ul style="list-style-type: none"> • Improving the urban policy and legal framework, land tenure system, housing availability, and institutional capacity • Strengthening urban public transport • Preventing urban pollution
Fertility reduction	<ul style="list-style-type: none"> • Enhancing the provision of family planning services and the use of contraceptives
Private sector competitiveness and diversification	<ul style="list-style-type: none"> • Increasing low-cost access to finance for firms, including long-term finance • Reducing the administrative cost associated with taxes, lands, buildings, construction permits, border crossings, and basic infrastructure • Improving land markets by reducing the cost of transferring land

	<ul style="list-style-type: none"> • Increasing maintenance expenditures for the national road network, investing in the northern trade corridor, and developing multimodal connectivity around Lake Victoria • Expanding electricity generation, access, and usage and improving reliability and access to ICT through expanding the national broadband infrastructure • Improving district and rural roads • Promoting technical and vocational training through partnerships and targeted programs for youth and women • Increasing women's participation in the labor market • Enhancing skills for and around the oil sector and in other productive sectors such as tourism
Public sector effectiveness	<ul style="list-style-type: none"> • Instilling a delivery focus through an open and participative monitoring, evaluation, and de-bottlenecking process which draws on external inputs • Strengthening sanction mechanisms by consolidating fiduciary management systems and reinforcing central-level institutions' accountability • Improving local government (LG) accountability and horizontal equity at the local level through strengthening of the intergovernmental fiscal transfers and enhancement of own-source revenues of LGs • Continuing to build specialized capacity for the oil sector

1. INTRODUCTION

A. PROGRESS SO FAR IS THE FOUNDATION FOR THE FUTURE

1.1. **After a destructive civil war and extreme political instability, Uganda began its reconstruction process in 1987. Significant progress has been recorded since then.** Uganda's output expansion during 1987–2010, at 6.9 percent a year, was one of the highest among African countries. The sustained growth performance was the result of macroeconomic stability, post-conflict rebound, and pro-market reforms which transformed Uganda from a failed state to one of the fastest growing economies in the world. Growth in per capita GDP was however lower at 3.6 percent per year because of the high fertility rate.

1.2. **Concurrently, Uganda has made progress on some dimensions of welfare.** The primary education net enrollment rate had increased to 82 percent by 2013, from 67 percent in 1995. During the same period, the share of underweight children under the age of five reduced from 25.5 percent to 13.8 percent while mobile cellular subscriptions per 100 people increased from 0 to 44. These achievements are substantial and represent a success story in the African context.

1.3. **However, today, Uganda remains one of the poorest countries in the world.** With GNI per capita at US\$660 in 2014, Uganda ranks below the LICs' average of US\$709. The proportion of the population living under the national poverty line stood at 19.7 percent in 2013 while those under the international poverty line of US\$1.25 per day (2005 PPP) stood at 30.6 percent. Using the recently released international poverty line of US\$1.90 per day (2011 PPP), poverty incidence declined to 33.2 percent from 68.1 percent during 1993–2013. Annual consumption growth of the bottom 40 percent has averaged around 3 percent over the 20-year period from 1993 to 2013, which is higher than most countries in the region. However, in relative terms, consumption growth of the bottom 40 percent was slower than the consumption growth of the top 60 percent and inequality, as measured by the Gini index, increased from 0.36 in 1993 to 0.40 in 2013. In addition, vulnerability to poverty in Uganda is high. Around 43 percent of Ugandans are insecure non-poor, defined as those living above the national poverty line but living on less than twice the poverty line. Between 2005 and 2009, for every three Ugandans who were lifted out of poverty, two fell back into poverty, due to shocks, particularly adverse weather, illustrating the fragility of the gains realized by the poorest households.

1.4. **After two decades of strong growth, the expansion of the Ugandan economy has slowed down in recent years.** Economic growth decelerated from an average of about 6.9 percent a year during FY1987–2010 to 5.5 percent from FY2011–2014. Uganda's recent growth performance has been lower than the average of LICs, in sharp contrast to its relative performance in the earlier periods. This recent decline is partly related to the more volatile external environment and partly to domestic policy slippages. It is also attributable to the waning growth dividend from the economic reforms of the 1990s and the criticality of certain constraints like poor infrastructure.

1.5. **Looking forward, the on-streaming of oil production can have a far-reaching impact on the economy.** If managed well, oil has the potential to substantially raise government revenues, increase exports, create forward and backward linkages, and result in impressive growth rates. However, it will provide limited employment opportunities given the capital intensive nature of

the hydrocarbon industry. Hence, the role of the government will be crucial to manage resource revenues efficiently and to support the development of synergies with domestic industries. Sound oil revenue management stands on the two pillars of good governance and strong PFM. Governance, through the establishment of strong institutions and effective accountability mechanisms will be of particular importance because resource rents create perverse incentives for the elites to appropriate them. Strong public expenditure policy and management is important for every country but it assumes a more crucial role in resource-rich countries because resource revenues accrue to the government in the first instance and get transmitted to the economy through the level, timing, and composition of public expenditure.

1.6. Beyond oil, Uganda's other assets will require investment. With nearly half of its population under the age of 15 years, Uganda has one of the youngest and most rapidly growing populations in the world. This youth bulge requires investments in education and generation of more productive jobs to bring them into the mainstream of society and reduce the risk of social instability, but Uganda currently ranks 164 out of 185 countries in its human development index. Uganda can also capitalize on its tourism potential and increase mineral exports but this requires further investment in supporting infrastructure and skills. Uganda's infrastructure investment needs are estimated at US\$21 billion over the next 10 years, more than 75 percent of 2014 GDP.

1.7. Many of the development challenges facing Uganda are well-understood by policymakers but little progress has been made in addressing them. With good data availability (annex 5) and several analytical studies, Uganda's progress over the years has been well-documented. The main challenges facing the country include poor infrastructure, weak public service delivery, low levels of human capital, and underdeveloped institutions. These aspects, along with a host of other constraints facing Uganda are reflected in the government's National Development Plan and Vision 2040. The challenge is therefore, to address those constraints through a set of coordinated actions and to close the gap in implementation of policies. Hence, what is really needed in Uganda is 'how to do it' rather than 'what to do'. The key factor affecting the 'how to' is the political economy climate in Uganda, which manifests itself in public policy and public sector performance.

1.8. The political context in the country provides both opportunities and challenges. The longevity of the ruling party, which has been at the helm for 29 years has provided a sense of stability and direction to economic reforms. However, there have been relatively weak improvements in governance implementation. The new National Development Plan (NDP) provides an opportunity to consolidate reform initiatives and reap the benefits of ramped-up infrastructure investment and decentralization.

B. A FRAMEWORK TO ASSESS AND PREPARE FOR A CHALLENGING FUTURE

1.9. In this context, a comprehensive framework based on the three interrelated blocks of growth, inclusion, and sustainability has been used to identify the challenges to and opportunities for ending poverty and boosting shared prosperity. The first block emphasizes the development of a competitive and resilient private sector to lead the growth process by adequately capitalizing on all the available opportunities. The second block, complementary to the first one, reinforces the need to ensure a fair distribution of the growth dividend across all Ugandans, especially those living in the north and the east, by providing them with access to social

and infrastructure services so that they can increase their productive capacity and income-generating opportunities. The third block emphasizes the need to undertake the inclusive growth process in a fiscally, socially, and environmentally sustainable manner.

1.10. **The analysis includes a macro-micro interactive approach.** On one hand, it assesses macro factors such as the business environment, macroeconomic policies, public sector effectiveness, and overall institutional development which affect growth, inclusion, and sustainability. This is fused with an assessment of factors influencing the productive capacity of households to contribute to the growth process through the accumulation of assets. The income-generating capacity of individuals depends on assets like human, physical, natural, financial, and social capital.

C. OBJECTIVES AND STRUCTURE OF THE REPORT

1.11. **This SCD identifies the constraints to and opportunities for reducing extreme poverty and boosting shared prosperity in a sustainable manner.** The analysis is evidence based and largely draws on existing analytical work done by the Bank and other stakeholders. It will form the analytic foundation for the Country Partnership Framework of the World Bank Group. This report draws significantly from the forthcoming Poverty Assessment in Uganda. It was also informed by consultations with the government, civil society, academicians, private sector, and the international donors. These consultations were held both in Kampala and in several regions (annex 2). The SCD advisory committee, a group of experts from the government, private sector, and civil society, also provided useful inputs.

1.12. **This SCD is organized as follows.** Chapter 2 presents the profile of the poor, Uganda's performance on the twin goals, and the factors influencing this performance. Chapter 3 discusses the country's growth dynamics in the past and the potential drivers for future growth. Chapter 4 presents the inclusion story and provides details of the use and accumulation of assets by individuals and households and the opportunities to enhance inclusion. Chapter 5 discusses the concerns on sustainability and risks, while Chapter 6 presents the priorities and the process of prioritization.

2. UNDERSTANDING POVERTY IN UGANDA

A. OVERVIEW: POVERTY, SHARED PROSPERITY, VULNERABILITY, AND INEQUALITY

Uganda has been successful in reducing poverty and boosting shared prosperity but vulnerability to poverty is high and inequality has persisted.

2.1. The proportion of the population living in poverty—whether measured using the national poverty line or the international poverty line—more than halved from 1993 to 2013 but the country still has a long way to go.

The proportion of the population living under the national poverty line declined from 56.4 percent in 1993 to 19.7 percent in 2013.⁵ Similarly, the incidence of extreme poverty measured by the international poverty line of US\$1.25 per day (2005 PPP) declined from 71.9 percent in 1993 to 30.6 percent in 2013 (table 2.1). This declining trend is confirmed when using the recently released

Table 2.1. Headcount Poverty Rates from 1992/93 to 2012/13

	Proportion of the Population Living Beneath...	
	National Poverty Line*	International Poverty Line**
1992/93	56.4	71.9
1999/00	33.8	59.4
2002/03	38.8	56.6
2005/06	31.1	51.7
2009/10	24.5	37.9
2012/13	19.7	30.6

Source: Uganda Poverty Assessment using the Uganda National Household Survey (UNHS).

Note: * Ranges from US\$0.94 to US\$1.07 PPP per capita per day depending on the region of the country. ⁴

** US\$1.25 PPP per capita per day.

international poverty line of US\$1.90 a day (2011 PPP) as poverty incidence declined to 33.2 percent from 68.1 percent over the same period. Over the last ten years, Uganda reduced the proportion of the population living under US\$1.25 per day faster than any other country in SSA. The poverty gap has also fallen consistently during this period from 22 percent in 2003 to 12 percent in 2013.⁶ However, the poverty gap also indicates that Uganda is still a poor country and that it will take an average payment of US\$54.75 per capita per year to eliminate extreme poverty in Uganda.

2.2. On several other dimensions of well-being, progress has been slow. The government estimates that 61.4 percent of the population was still food insecure or poor in 2013. While primary school gross enrollment is near universal, many students do not complete primary school and

⁴ This is calculated by converting the region-specific national poverty lines to U.S. dollar PPP 2005 and dividing by the average ratio of adult equivalents to individuals (given the national poverty line is a per adult equivalent line).

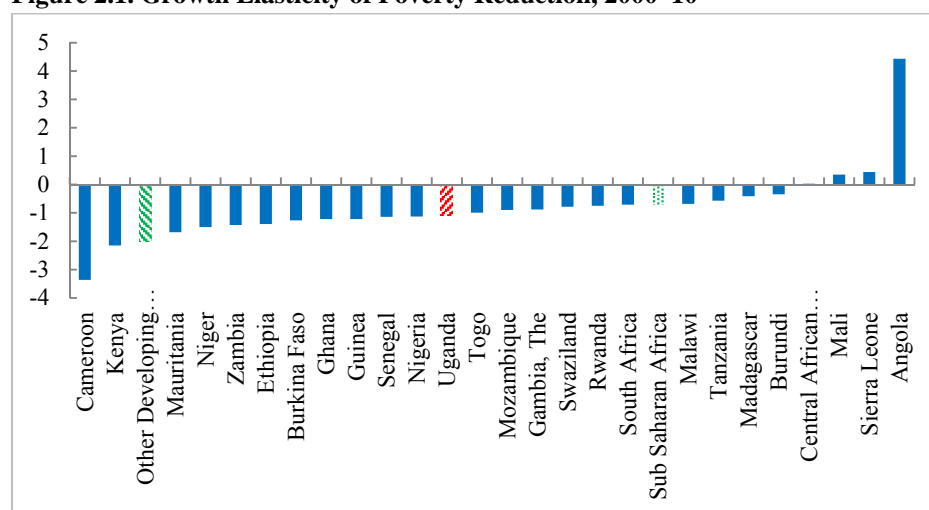
⁵ The national poverty line ranges from US\$0.88 to US\$1.04 PPP 2005 per capita depending on the region. Poverty in Uganda is calculated using a cost of basic needs approach. Consumption expenditure data is collected on food and non-food items through the UNHS conducted every 3–4 years. The poverty line was set in 1993 by calculating the cost of consuming 3,000 calories per adult equivalent and then adding an amount (the amount depending on the region) to capture non-food expenditures. The poverty line has only been updated for the cost of inflation since then and is low by international standards.

⁶ Poverty gap is the mean shortfall from the poverty line expressed as a percent of the poverty line. This measure reflects the depth of poverty as well as its incidence. The indicator is often described as the per capita amount of resources needed to eliminate poverty or reduce the poor's shortfall from the poverty line to zero, through perfectly targeted cash transfers.

secondary enrollment remains low.⁷ Life expectancy is only 51 years and the fertility rate is one of the highest in the world. It has only recently declined to 6.2 children per woman in 2013 from 6.7 in 2010.

2.3. **The amount of poverty reduction achieved in Uganda was moderate given its high rate of consumption growth over the past two decades.** The growth elasticity of poverty reduction during 2000–10 was 1.09 which compares well with the SSA average (figure 2.1), but is much lower than the global average of 2.02 in developing countries. Uganda’s performance can largely be explained by its rapid and sustained economic growth but the fruits of this expansion have not been fully shared with the poorest segments of the population, at least not in the magnitude observed in countries such as its East African neighbors (Ethiopia, and Kenya) and Vietnam in Asia.

Figure 2.1. Growth Elasticity of Poverty Reduction, 2000–10



Source: AfricaPulse 2014, underlying data from Povcalnet 2014.

Note: The bars indicate the poverty reduction achieved for each percentage point of growth.

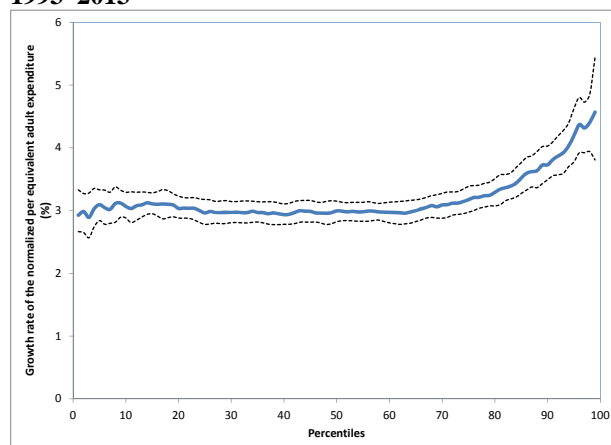
2.4. **Prosperity was shared with the poorest segments of the population but inequality increased from 1993.** Annual consumption growth of the bottom 40 percent averaged around 3 percent during 1993–2013 which was higher than most countries in the region. However, consumption growth of the bottom 40 percent was slower than the consumption growth of the top 60 percent (figure 2.2) and inequality, as measured by the Gini index, increased from 0.36 in 1993 to 0.40 in 2013.⁸ Although inequality was higher in 2013 than in 1993, it has declined since 2010 because incomes of the richest decile grew slower than the incomes of the poorest and the middle-income households. Figure 2.3 shows that Uganda faces moderately low inequality in comparison to other countries in the region, while figure 2.4 captures the inequality trend over the past two decades, including in rural and urban areas. Inequality was higher in cities possibly because consumption opportunities are higher for the wealthier urban households and social redistribution mechanisms are less vibrant than in rural areas. Sustained conflict in the north, which has put the

⁷ In 2012/13 the primary education net enrollment ratio was estimated at 82 and the secondary net enrollment ratio was estimated as 21.7.

⁸ It is worth noting that on average, the top 20th percentile was actually the main beneficiary of consumption growth over the period 1993–2003.

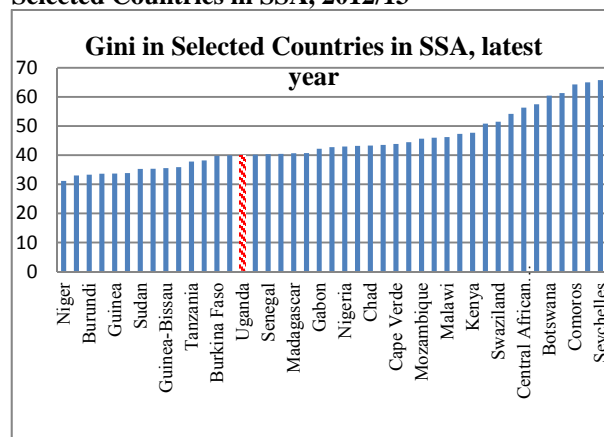
region back by several years, could also have contributed to increased inequality and slower rise in the incomes of the poor.

Figure 2.2. Consumption Growth Incidence Curve, 1993–2013



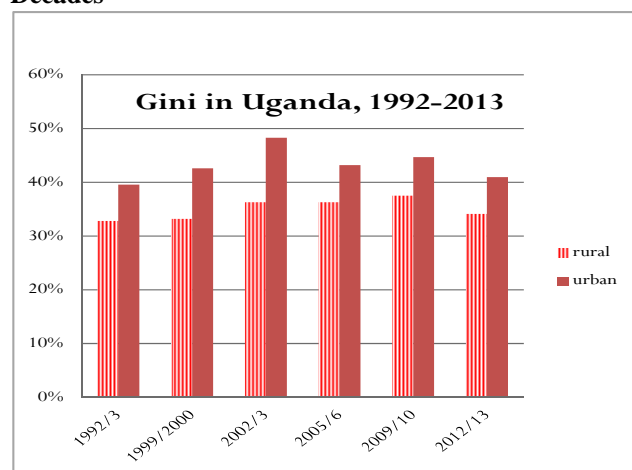
Source: Uganda Poverty Assessment using UNHS.
Note: The middle line maps the mean growth rate of incomes across different income groups while the outer lines are the standard deviation of this path

Figure 2.3. Uganda's Inequality Compared with Selected Countries in SSA, 2012/13



Source: Uganda Poverty Assessment using UNHS.

Figure 2.4. Inequality in Uganda over the Past Two Decades



Source: Uganda Poverty Assessment using UNHS.

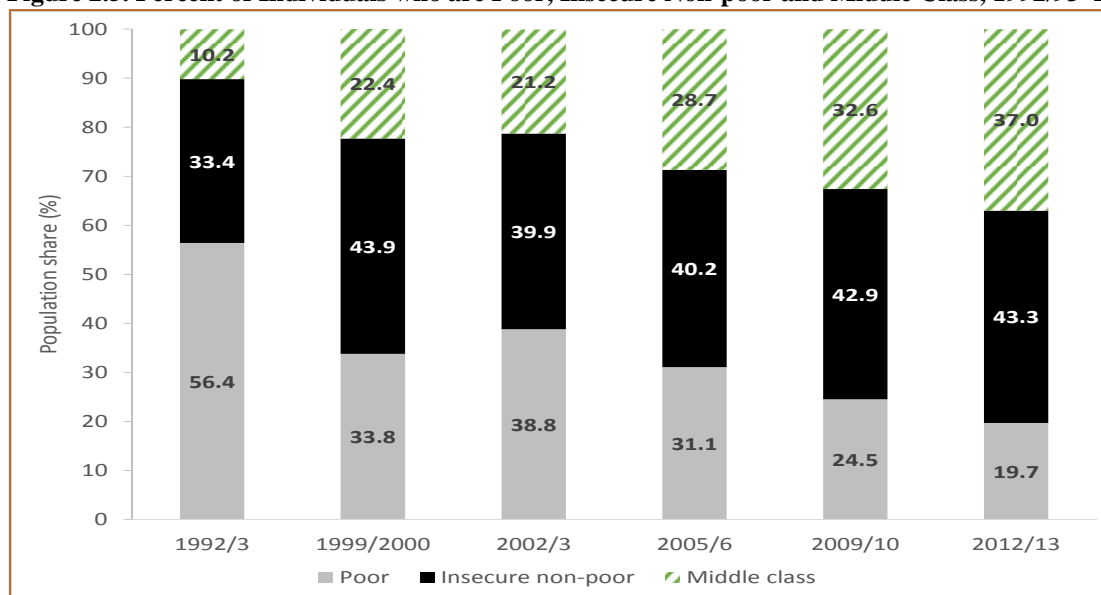
2.5. In spite of the significant decline in the poverty rate, vulnerability to poverty in Uganda is high. Nearly 43 percent of Ugandans were insecure non-poor in 2013, defined as those living above the poverty line but living on less than twice the poverty line (figure 2.5).⁹ Between 2005 and 2009, for every three Ugandans who were lifted out of poverty, two fell back into poverty, illustrating the fragility of the gains realized by the poorest households (EPRC 2013). Uganda's success in reducing poverty has resulted in many households that are living just above the poverty line who remain vulnerable to falling under the poverty line in the face of a negative shock. These shocks

could take up various forms from political and regional instability, particularly in neighboring countries (including the Democratic Republic of Congo and South Sudan), to unexpected health issues, when the key breadwinner falls sick, and to natural disasters. A large proportion of the labor force remains dependent on subsistence agriculture, which in turn is highly vulnerable to climatic conditions, crop disease, and price fluctuations. Droughts are commonplace in the northeast and floods have caused crop losses in the eastern region. Commercial commodities, such as coffee and tea, are sensitive to fluctuations in international prices. Maize and matooke (important cash crops

⁹ As per the Poverty Status Report 2014 produced by the Ministry of Finance, Planning, and Economic Development (MoFPED).

for many poor households in Uganda) are sensitive to changes in supply and demand conditions in domestic markets and importing countries, especially in Kenya and South Sudan.

Figure 2.5. Percent of Individuals who are Poor, Insecure Non-poor and Middle Class, 1992/93–2012/13



Source: MoFPED 2015.

Note: Poverty Status Report: **Poor** - living below the national poverty line; **Insecure** - living below twice the poverty line; **Middle class** - living above twice the poverty line.

B. POVERTY PROFILE: WHO ARE THE POOR AND THE BOTTOM 40 PERCENT IN UGANDA?

The poor in Uganda, live in rural areas, mostly in the northern and eastern regions, have large families, own few assets, and derive their income predominantly from farming.

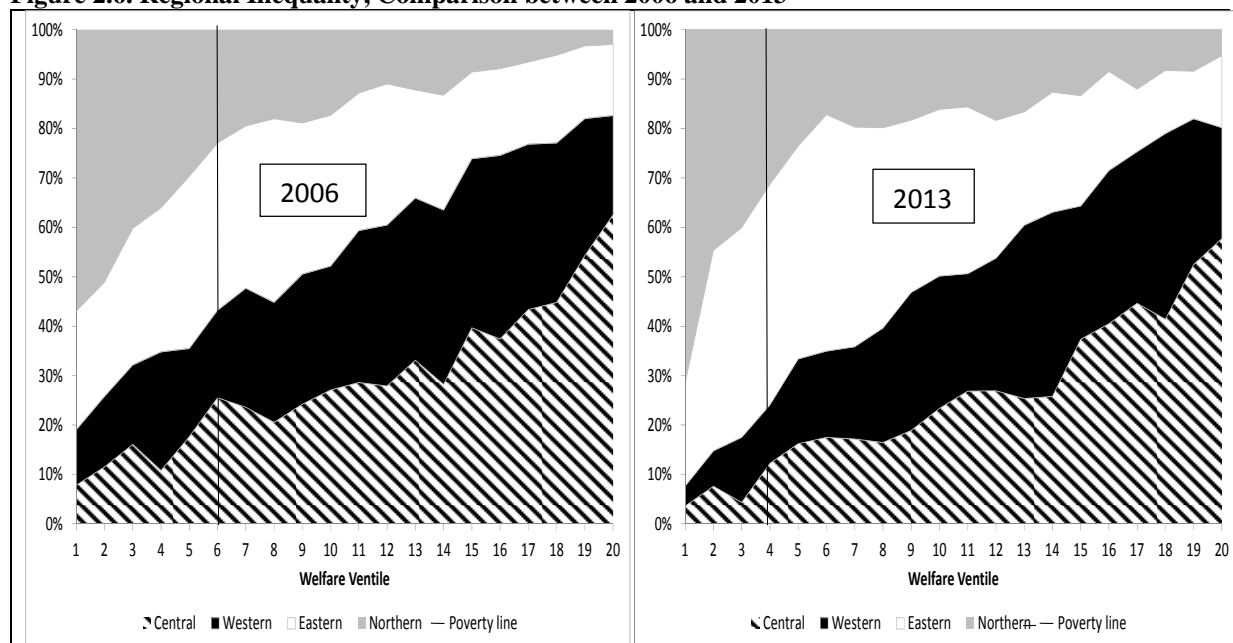
2.6. **Most of the poor in Uganda live in rural areas.** Nearly 84 percent of the population and 90 percent of the poor lived in rural areas in 2013. One in four rural Ugandans lives in poverty compared to just one in ten urban Ugandans. These statistics reveal that poverty is more prevalent in rural than in urban areas (22.8 percent in rural areas vs. 9.3 percent in urban areas in 2013) because income opportunities are lower in villages than in cities and access to social and infrastructure services are far more limited in rural areas. Therefore, any strategy to reduce poverty in Uganda will have to account for the large fraction of the population living in rural areas. Hence, poverty reduction will need to entail productivity gains in agriculture together with better access to markets, further diversification in the source of income of rural households, and migration toward urban centers.

2.7. **There are large and increasing regional variations in poverty with most of the poor concentrated in the north and the east.** In 2006, approximately 60 percent of the poor lived in the northern and eastern parts of the country. Seven years later, this proportion increased to 84 percent (figure 2.6).¹⁰ Progress, as captured by consumption levels, has been much faster in the western and southern regions, which benefited from the economic boom in Kampala and the surge in regional trade with Kenya and the global markets. Therefore, a focus on the northern and

¹⁰ About 47 percent of the poor live in the northern region and another 37 percent live in the eastern region.

eastern regions will be needed for Uganda to end extreme poverty and boost shared prosperity as well as to reduce social and political tensions that can emerge from stark differences across regions (box 2.1).

Figure 2.6. Regional Inequality, Comparison between 2006 and 2013



Source: Uganda Poverty Assessment using 2005/6 and 2012/13 UNHS.

Box 2.1. Spatial Dimensions of Poverty

Households in Uganda's northern, eastern, and western regions have much lower levels of human capital, fewer assets, and more limited access to infrastructure than households in the central region. The northern region is the worst, largely because the conflict took lives, damaged communities, destroyed assets, and had lasting effects on the aspirations of many individuals. Households in the north are larger and more likely to be headed by a woman and are also more likely to have a household head with no education (table 2.2). Most households own land but they are less likely to own other assets and have lower access to infrastructure services. The eastern region also lags behind the central and western region in nearly all of these measures.

Table 2.2. Human Capital, Asset Ownership, and Access to Infrastructure across Regions

	Central	Eastern	Northern	Western
Household size	4.2	5.4	5.0	4.8
Dependency ratio	101	130	134	116
Household is headed by a female (%)	30	30	35	31
Head has no education (%)	14	19	27	25
Head has some primary education (%)	43	50	41	41
Head has completed primary education (%)	9	7	8	11
Head has some secondary education (%)	19	15	12	11
Head has completed secondary education (%)	7	5	3	5
Head has tertiary education (%)	6	3	5	5
Literacy rate among 18+ year olds (% literate)	79	60	56	72
Owens a mobile phone (%)	82	52	35	63
Has electricity (%)	40	6	3	8
Has piped water (%)	20	5	1	6
Availability of tarmac roads (%)	53	21	19	27
No toilet (%)	5	8	29	2
Owens land (%)	59	78	80	86

Source: UBOS 2013. Report on the UNHS 2012/13.

Note: Health issues are discussed in detail in chapter 4.

Households in the northern region also have more limited access to markets and services. For households in these regions, distances to schools and health services are much larger as are distances to markets. The provision of agricultural extension and veterinary services is much lower and this is of concern given the reliance of these households on agriculture and livestock income. Rural financial institutions are almost entirely absent in the north. These constraints have limited the accumulation of human capital and the extent to which households can use their assets to earn a return in these regions.

Household income among the bottom 40 percent is low in the eastern and northern regions and heavily reliant on food crops and livestock farming. Livestock income comprises 39 percent of the agricultural income of the bottom 40 percent that live in the north. In addition, rainfall is lower and more volatile in the north increasing the vulnerability of households in this region, while households in the east are particularly vulnerable to the collapse of maize prices (annex 1).

2.8. Those in the bottom 40 percent live in larger families and have more dependents than the top 60 percent. Households in the bottom 40 percent have six members on average compared to 4.6 in the top 60 percent. As a result, the dependency ratio is 13 percentage points higher for those living in the bottom 40 percent. This gap between the bottom 40 percent and top 60 percent has remained constant between 2006 and 2013 (table 2.3). In addition, the proportion of households headed by women has increased slightly during this period but this has happened for households across all income groups.

Table 2.3. Fertility Rates and Dependency Ratios, 2006–13

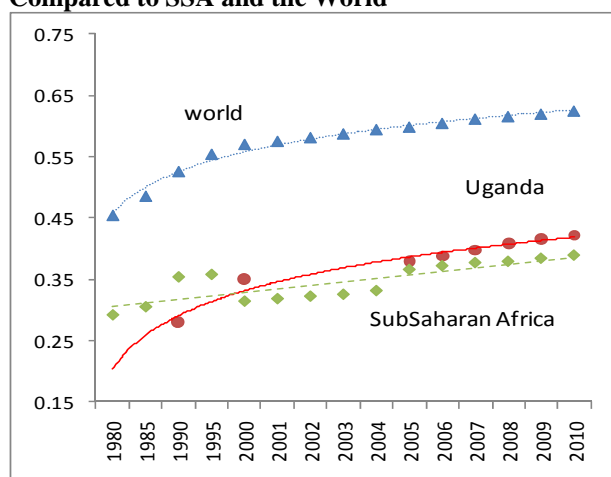
	2006			2010			2013		
	Bottom 40 percent	Top 60 percent	Wald Test (P-Value)	Bottom 40 percent	Top 60 percent	Wald Test (P-Value)	Bottom 40 percent	Top 60 percent	Wald Test (P-value)
Household composition									
Children aged 0 to 5 years	1.5	1.0	0.0000	1.4	1.0	0.0000	1.4	1.0	0.0000
Children aged 6 to 14 years	1.2	0.9	0.0000	1.3	0.7	0.0000	1.2	0.8	0.0000
Male adults aged 15 to 59 years	1.1	0.9	0.0000	1.2	0.8	0.0000	1.2	0.8	0.0000
Female adults aged 15 to 59 years	2.1	2.1	0.3966	2.0	2.0	0.0886	1.9	1.9	0.2264
Seniors aged over 60 years	0.2	0.2	0.0391	0.2	0.2	0.0001	0.3	0.2	0.0024
Household size	6.1	5.1	0.0000	6.1	4.6	0.0000	6.0	4.6	0.0000
Dependency ratio	55.4	43.5	0.0000	56.8	41.8	0.0000	56.5	43.1	0.0000
Head is female	27.4%	26.6%	0.4757	31.4%	29.5%	0.1864	31.4%	30.7%	0.6379

Source: Uganda Poverty Assessment using UNHS.

2.9. **Ugandan households have a higher level of education than in the past, but it remains low, particularly among poorer households.** Uganda has been able to increase its stock of human capital faster than the average in SSA since 2000. However, it mostly represents a catch up from a low initial level. Indeed, many working-age adults still have low levels of education—only 23.8 percent of household heads had higher than primary education. Within the bottom 40 percent of the population, this is only 11 percent.

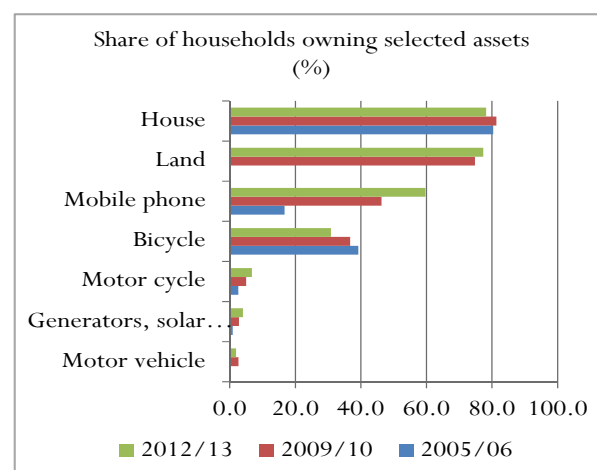
2.10. **Access to infrastructure services, particularly for the poor, remains low even by regional standards.** By 2013, more households owned land, mobile phones, and motorcycles, and also accessed electricity and piped water, compared with 2006 (figure 2.8). However, these levels of access remain relatively low by international and even regional standards, with only 12.4 percent and 6.8 percent of households having access to electricity and piped water, respectively, in 2013. In addition, there are large variations in asset ownership and access to infrastructure services between the rich and the poor. Mobile phone ownership is only 37 percent among the bottom 40 percent compared with 70 percent among the top 60. Almost no households in the bottom 40 percent have access to electricity or piped water, compared with 20 percent and 10 percent, respectively, in the top 60 (table 2.4). Interestingly, more poor households report to own land reflecting the predominance of farming as their prime occupation.

Figure 2.7. Human Capital Trends: Uganda Compared to SSA and the World



Source: Human Development Index.

Figure 2.8. Growth in Private Asset Ownership



Source: Uganda Poverty Assessment using 2012/13 UNHS.

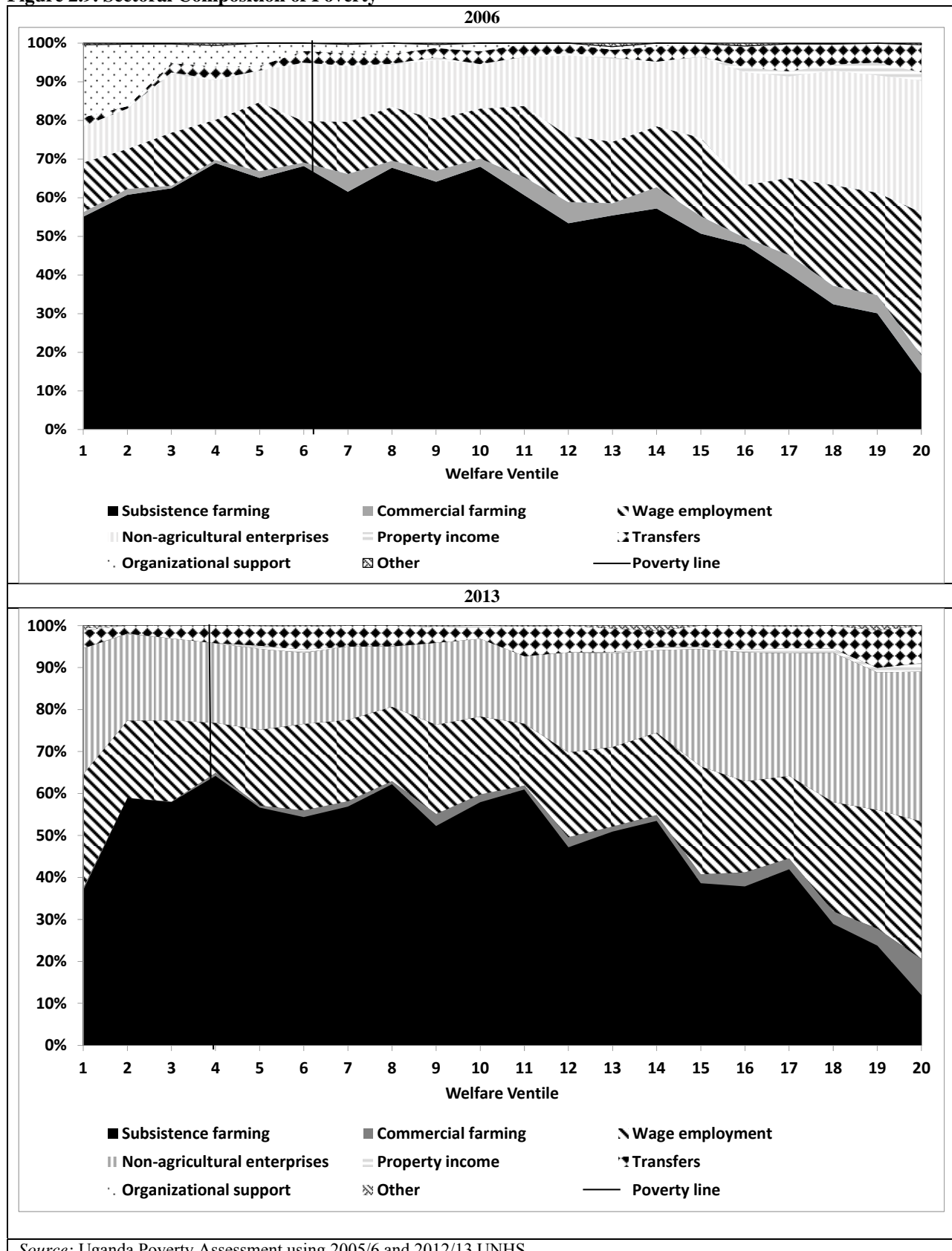
Table 2.4. Human and Physical Capital and Livelihoods among the Bottom 40 Percent, 2013

Proportion of individuals that live in a household in which...	Bottom 40 Percent	Top 60 Percent
Education level of the head of the household is:		
None	29.4	16.3
Primary	58.5	49.0
Secondary	11.4	27.3
Tertiary	0.7	7.5
The household owns the following assets:		
Bicycle	30.5	30.9
Mobile phone	36.7	70.4
Electricity	1.7	19.6
Piped water	0.4	10.2
Land	83.2	74.0
Main income source of the household is:		
Farming	52.6	38.8
Wage employment	20.4	25.4
Other source	27.0	35.7
The household owns a nonfarm business	31.6	40.0

Source: Uganda Poverty Assessment using 2012/13 UNHS.

2.11. Poorer households are more likely to report farming as their primary occupation. More than half of the households in the bottom 40 percent (53 percent) depend on agricultural production as their main source of income compared with 39 percent of those in the top 60. Wage employment and ownership of a nonfarm business is higher among the top 60 percent than among the bottom 40 percent (table 2.4). In addition, although crop income is becoming less important over time it is still the main source of income for most households at the bottom of the consumption distribution, with richer households reporting higher levels of wage employment income and income from nonfarm household enterprises (figure 2.9).

Figure 2.9. Sectoral Composition of Poverty



Source: Uganda Poverty Assessment using 2005/6 and 2012/13 UNHS.

C. DETERMINANTS OF THE PERFORMANCE ON THE TWIN GOALS

Uganda's performance on the twin goals is largely explained by the expansion of agriculture, fluctuations in agricultural prices and weather, and, increasingly, nonfarm activities, which has been the main source of job creation in recent years. Improvements in infrastructure, health, and education also contributed to poverty alleviation.

2.12. **The sustained period of high growth in Uganda during 1987–2010, averaging 6.9 percent a year, reached the poor largely through increases in agricultural incomes and also through increases in nonfarm incomes.** Real agricultural incomes per capita grew by 4.7 percent between 2006 and 2012, behind the growth of 6.3 percent in nonagricultural incomes. Agricultural income increases were more strongly associated with increased consumption and reduced poverty, but those who increased their nonagricultural income also increased their consumption and moved out of poverty.

Impact of Agriculture on the Twin Goals

2.13. **Although limited agricultural growth has been recorded in the Ugandan national accounts, household survey data shows substantial growth in real per capita agricultural incomes.** Agricultural growth in Uganda has consistently been low, averaging only 2 percent over the past five years and below the performance achieved by other regional economies (table 2.5).

Table 2.5. Agricultural GDP Growth Rates for Selected Eastern African Countries, 2000–2012

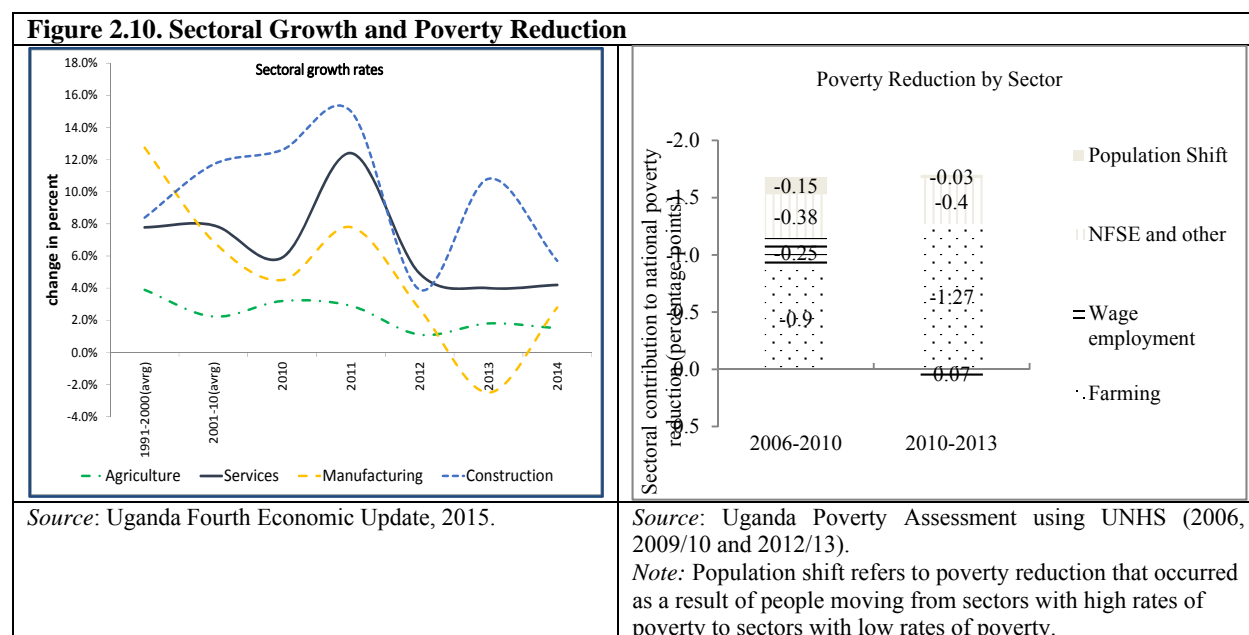
Country	2000–09	2010–12
Ethiopia	6.6	6.3
Tanzania	4.6	3.9
Kenya	2.3	4.6
Uganda	2.6	1.5

Source: World Bank, World Development Indicators (WDI).

2.14. **Growth in agricultural incomes has resulted in increased welfare, particularly among the poorest who derive more income from agriculture than other households.** Kaminski and Christiaensen (2014) calculate that agricultural income growth contributed to 18 percent of the consumption growth from 2006 to 2010. Subsistence farming is the main source of income for 52.6 percent of the bottom 40 percent and for 51 percent of households living below the national poverty line. The impact of agricultural growth on consumption is stronger for the poorest. Analysis undertaken as part of the Uganda Poverty Assessment finds that the impact of crop income growth is 1.5 times higher for households in the bottom 40 percent than for the average household and the impact of livestock income growth is 1.2 times higher for households in the bottom 40 percent.

2.15. **As a result, over half of the poverty reduction that Uganda experienced since 2006 occurred among households that were primarily active in agriculture.** Poverty reduction among households primarily engaged in agriculture accounted for 0.9 of the 1.7 annual percentage point reduction in poverty from 2006 to 2010 and 1.3 of the 1.7 annual percentage point reduction

in poverty from 2010 to 2013 (figure 2.10).¹¹ The relatively high elasticity of poverty to changes in agricultural GDP is also consistent with findings from macro simulations using Uganda's Social Accounting Matrix (Dorosh and Thurlow, 2012; Government of Uganda, 2014).



2.16. **Agricultural income growth was driven by an increase in the area under cultivation, good weather, and high prices. Improved access to markets in neighboring countries also played a role.** The increase in aggregate crop production came largely from the expansion of the area under cultivation and marginally because of an increase in the use of modern production technologies. In addition, the overall policy environment was also beneficial and was characterized by macroeconomic stability, post-conflict rebound, and pro-market reforms. However, analysis undertaken as part of the Uganda Poverty Assessment shows that key drivers of crop income changes were favorable weather and high prices for agricultural commodities in domestic (matooke) and regional (maize) markets (table 2.6) which in turn had an impact on consumption, particularly for the bottom 40 percent. Improvements in access to markets and extension services also seem to have helped.

Table 2.6. Impact of Weather and Prices on Crop Incomes, 2006–2012

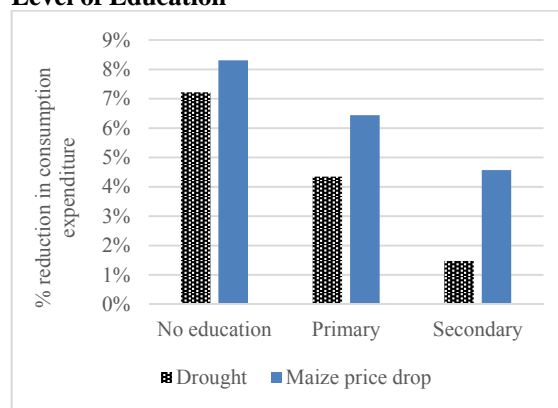
	Percent Increase in Income		Percent Increase in Consumption	
	All	Bottom 40 Percent	All	Bottom 40 Percent
1% increase in:				
Rainfall (WRSI)	2.18	2.90	0.43	0.47
Maize prices	0.42	0.41	0.23	0.22
Matooke prices	0.82	0.77	0.18	0.19
Cassava prices	0.19	0.27	-0.13	-0.12

Source: Uganda Poverty Assessment using UNPS 2006–2012.

¹¹ Agricultural growth contributed to 70 percent of the poverty reduction observed among panel households from 2006 to 2010 (Kaminski and Christiaensen, 2014).

2.17. **The inadequate availability and use of productivity-enhancing factors such as technology, training, water and land management, and farm-to-market infrastructure, renders the agriculture sector highly vulnerable to exogenous shocks such as variable climate and price falls that reduce the welfare of households.** Figure 2.11 indicates the likely increase in poverty resulting from a moderate drought and price fall in maize. Higher agricultural productivity, better access to markets and diversification are therefore important to help manage income shocks. The educated are better able to insure their welfare through diversification and the impact of shocks on welfare is therefore more muted for those with higher levels of education. When shocks do occur, the most common coping mechanisms used by those in the bottom 40 percent are to use savings (30 percent), to ask for help from family members (25 percent), reduce consumption (11 percent) or take nonfarm work (9 percent). Only 5 percent report receiving support from the government (Nikoloski, Christiaensen, and Hill 2015). Floods have however had a limited impact on poverty as they do not affect too many households.

Figure 2.11. Impact of Shocks on Welfare by Level of Education



Source: Uganda Poverty Assessment using UNPS 2006–12.

Other Determinants of the Twin Goals

2.18. **Growth in nonfarm self-employment and, to a lesser extent, wage employment, also raised incomes of the bottom 40 percent.** The bottom of the consumption distribution has largely transitioned into self-employment to supplement their incomes while those who have transitioned to wage employment have generally had higher levels of education. The distinguishing feature of households in the bottom 40 percent that were able to transition into wage employment was their level of education. In addition, own-savings has enabled self-employment income growth among the bottom 40 percent. However, women, are generally in lower-earning self-employment activities and are 8 percent less likely to experience self-employment income growth. During 2006–10, poverty reduction among those in wage employment and nonfarm self-employment accounted for 30 percent of the poverty reduction in Uganda and contributed to 66 percent of consumption growth experienced during this time (Christiaensen and Kaminski 2014). These contributions are relatively high compared to other developing countries. In Rwanda, from 2003–11, increases in nonfarm income sources contributed to 15 percent of the poverty reduction and in Cambodia from 2004 to 2011 increases in nonfarm income sources contributed to 23 percent of the poverty reduction.

2.19. **Migration, within rural areas also brought about substantial growth in consumption.** Poverty reduction was twice as fast for those who moved out of their village between 2005 and 2009 than for those who stayed (4 percentage points rather than 2 percentage points) even though migrants were just as likely to be poor as non-migrants before they moved. On average, those who migrated saw a 7 percent increase in consumption (controlling for selection bias as much as possible), but those who migrated from rural to urban areas saw a 37.5 percent increase in consumption. However, despite the larger impact on consumption, the impact of rural to urban

migration on poverty was smaller as those who migrated from rural to urban areas were less poor to begin with.

2.20. Education, smaller household size and improved infrastructure access has aided poverty reduction. Low levels of education and limited access to infrastructure are both determinants and consequences of poverty. So, quantifying the impact of this improvement on poverty reduction is difficult. However, a panel data analysis shows that improvements in access to markets as a result of infrastructure investments, reductions in household size, and increased education contributed to improving household income and consumption in Uganda, thereby reducing poverty. A reduction in the distance to the nearest input market by 1 km increased crop income by 1 percent while household heads with a completed primary education earned 10 percent more than those with incomplete primary education.

2.21. However, fiscal redistribution through social protection did not reduce poverty as there is no comprehensive safety net program in Uganda. This is in stark contrast to some other countries in the continent such as Botswana, South Africa, and Ethiopia. About 0.4 percent of GDP (excluding contributory social security) is given in direct transfers in Uganda, one of the lowest in the region. Only 5 percent of the working population are covered by a pension scheme and only 4.5 percent of the total population receive any kind of direct income support, while the coverage of social care and support services is still lower. Informal transfers are present, but do not comprise a large share of income. As many as 47 percent of households reported taking a loan from family and friends in 2013, one of the highest rates in the world. Informal transfers (including remittances) and formal transfers together comprise a small share of the income of the poor. Those living below the national poverty line receive only 6 percent of their income in transfers of any kind. As a result, growth in incomes and changes in the shape of the income distribution are almost entirely driven by the nature of growth and shocks experienced by Ugandan households.

D. LOOKING AHEAD

Addressing regional inequality, generating productivity gains in agriculture to raise incomes of farmers, facilitating the transition to nonfarm employment, and developing social protection programs will be key to achieving the twin goals.

2.22. Like most countries in the world, poverty reduction in Uganda will largely be driven by the country's capacity to grow at a faster rate in the medium term and to share that growth with the population. If the GDP growth rate averages around 7 percent over the next decade and assuming the same historical elasticity between GDP growth and poverty reduction, by 2025, the level of poverty will reduce to approximately 6.6 percent based on the national poverty line and 7.1 percent based on the international poverty line.¹² However, this will require the government to reach those sections of the population which have so far not benefited from the growth process and might require targeted interventions. In other words, business as usual might not result in the same poverty-growth elasticity and will therefore, require the authorities to find new ways to address this challenge. There are two options: either the country could grow faster than its historical rates, following the example of China or other East Asian countries; or it can

¹² Based on World Bank staff's calculations.

attempt to increase the elasticity of poverty reduction to GDP growth. Of course, a combination of these two options will be optimal.

2.23. Given the preponderance of poor households in the north and the east, a regional focus will be necessary to reduce poverty and improve the living conditions of the bottom 40 percent. There are stark regional differences in poverty rates, asset levels, and access to infrastructure services and markets, as well as in livelihoods (figure 2.6). Efforts at raising incomes and consumption levels will need to be particularly focused on the northern and eastern parts of the country. The current growth pattern, led by the urban services sector, is likely to widen regional disparities making it hard for Uganda to boost shared prosperity and end extreme poverty. Growth in the services sector is projected to be high and this will benefit few in the north where only 31 percent of household income is derived from nonagricultural activities (compared to 65 percent in the central region).

2.24. Addressing vulnerability will require more sustained income growth which will need concerted efforts to raise agricultural productivity and generate high quality nonfarm jobs together with investment in human and physical capital. Poverty in Uganda is rural and transformation of the employment structure will take time because urbanization is still in its incipient stage with only 15 percent of the population living in cities. Hence, increasing agricultural incomes will continue to be crucial. At the same time, creation of jobs in cities will be important to absorb the large incoming labor force and to enable rural-urban migration. Past data shows that education was a determining factor among those in the bottom 40 percent who managed to successfully migrate out of farm income. Hence, accumulation and more effective use of assets at the micro level will be important, which will require improvements in public services. Savings have also helped households migrate and transition into new forms of self-employment.

2.25. Managing fertility will also be crucial to reduce poverty. The high fertility rate has resulted in high dependency ratios and has increased the resource requirements for households and the government. There is a clear relationship between a large family size and high incidence of poverty because lesser financial resources are available for each member of the family and there is a lower possibility for them to save and invest in human capital. The fast growing and young labor force has also put pressure on the job market and has reduced wages and made it more difficult to secure a good and stable employment.

2.26. Increasing social protection and improving financial inclusion will help build and protect the assets of the poor and shield them from income shocks. Some of the poorest households in Uganda are unable to participate in the growth process as a result of their limited asset base which inhibits their income-generating capacity. Investment in the asset base of the poor can potentially be achieved through a robust social protection system. Many of the poor households face a variety of shocks but only 5 percent of households report receiving government assistance in a time of need and many households in the bottom 40 percent also do not have access to credit or family networks for support. This is a gap that a well-designed social protection system can fill. Improving financial inclusion by improving access to savings and credit instruments can also help the poorest to smooth consumption.

3. ASSESSING THE DRIVERS OF GROWTH IN UGANDA

A. UGANDA'S GROWTH PERFORMANCE AND DRIVERS

Uganda's growth performance during 1987–2010 was associated with rapid expansion of the public sector; private consumption and private investment in services sectors as a result of macroeconomic stability; post-conflict rebound; and pro-market reforms. Since 2010, the growth rate has slowed down because of suboptimal fiscal management, slower pace of reforms, and a series of exogenous shocks.

3.1. Uganda's growth story since 1987 can be divided into two periods. The period from 1987 to 2010 during which Uganda experienced its strongest economic growth and the period post 2010 (2011–14) which was characterized by a slowdown in growth. The period before 1987 (1970–86) was characterized by political instability and civil war.

3.2. During 1987 to 2010, Uganda experienced a sustained period of high growth as a result of macroeconomic stability, post-conflict rebound, and pro-market reforms. GDP expanded at an annual average rate of 6.9 percent, far higher than the average for African countries and other LICs (figure 3.1), especially non-oil producing countries. As a result, Uganda transformed from a failed state (with a real GDP per capita averaging minus 2.5 percent over 1970–86) to one of the fastest growing economies in the world. Following the end of the armed conflict in 1986, the government introduced a sequenced package of structural reform policies and investments designed to free up markets and create price incentives, stimulate private investment, and encourage competition. Marketing boards were abolished and the financial sector was liberalized, together with an ambitious privatization program for banks and public enterprises, including those in telecommunications and electricity. As a result, there were substantial aid inflows which helped finance public expenditures, thereby, improving social and infrastructure service delivery. Consumption increased, fueled by economic opportunities and the rebound in the economy. Private investment increased from 8.1 percent of GDP in FY1993 to 18.3 percent in FY2011. During the same period, exports grew from 5.7 percent of GDP to 15.4 percent. Per capita GDP grew at a more modest pace of 3.6 percent per year during 1987–2010, essentially because of the fast growing population escalated by the high fertility rate in Uganda.

Figure 3.1. Uganda's GDP Per Capita Growth



Source: World Bank Staff analysis using WDI data.

3.3. With the growth dividend from the first spurt of reforms waning and in the face of domestic and external shocks, economic expansion in Uganda decelerated from an average of 6.9 percent a year during FY1987–2010 to 5.5 percent from FY2011–14. Uganda's recent growth performance has been lower than the average of LICs, in sharp contrast to its relative

performance in the earlier periods (table 3.1).¹³ This recent decline is partly related to the more volatile external environment and partly to domestic policy slippages. While the economy was insulated from the direct effects of the 2008/09 global financial crisis, there were significant secondary effects in subsequent years on Uganda's exports and private capital inflows. The recurrent political crisis in South Sudan and the Democratic Republic of Congo has also negatively affected many Ugandan households, particularly, those living in districts such as Kitgum, Masindi, Lira, Buliisa, Arua, and Gulu, which are close to the border of these countries. Also, the performance of the agricultural sector suffered from inconsistent weather, in particular, the severe drought in FY2011. In addition, the first (and arguably easier) round of policies has already been implemented, but the momentum has been somewhat lost as reflected by the deterioration in the Doing Business and governance indicators in recent years. As a result, the overall private investment rate declined from 18.3 percent of GDP in 2010/11 to 16.5 percent in 2013/14.

3.4. In addition, inconsistent fiscal and monetary policies also negatively impacted growth in recent years.

In particular, structural weakness in revenue generation compounded by fiscal slippages in 2011¹⁵ and corruption scandals in 2012 (leading to lower aid inflows) forced the authorities to adopt restrictive fiscal and monetary policies.¹⁶ These adjustments, while necessary to restore fiscal sustainability and control inflation, contributed to the slower economic expansion during the period 2012–14.¹⁷ Growth slowed to 3.3 percent in FY2013—the lowest rate achieved in the last three decades—largely because of the required fiscal adjustment to restore macroeconomic stability and as a result of the aid suspension. The economy rebounded in FY2014 to 4.5 percent because of improved terms of trade and good climatic conditions.

Table 3.1. Uganda's Growth Performance in Relation to Comparators¹⁴

	1990–99	2000–10	2011–13
Uganda	6.7	7.1	5.8
Bangladesh	4.8	5.8	6.3
Cambodia	7.2	8.1	7.3
Ethiopia	2.7	8.5	10.1
Kenya	2.2	4.0	5.4
Lao PDR	6.3	7.0	8.2
Vietnam	7.4	6.6	5.6
Zambia	1.3	7.1	6.6
LICs	2.3	5.2	6.2
SSA (LDC)	1.8	5.0	4.0

Source: UBOS; WDI.

Note: LDC = Least developed countries.

3.5. Monetary policy has become more complex in Uganda, with structural changes in the domestic financial sector and the rapid expansion of mobile money. The Central Bank has historically relied on targeting monetary aggregates to control inflation. While this served the purpose well, the underlying relationship between base money, broader monetary aggregates, and inflation had weakened and the money multiplier had become very unstable following the structural transformation of the economy and developments in the financial sector over the past two decades. For example, with the introduction of mobile banking in 2009/10, the demand for

¹³ Uganda's growth performance over 2011–13 remained, however, higher than the average of the least developed countries in SSA.

¹⁴ Several factors were used in the selection of peer comparators. These include the level of income, regional peers, fertility management, agriculture development, resource endowment, and fragility.

¹⁵ Public expenditure as a share of GDP increased from 16.7 percent in 2008/9 to an average of 19.7 percent over the next two financial years (2009/10 and 2010/11).

¹⁶ For instance, the government reduced public expenditures from 19.1 percent of GDP in 2010/11 to 15.6 percent in 2011/12. Meanwhile, the average lending rate increased to 24.8 percent in 2011/12 from 19.8 percent a year earlier as a result of a tighter monetary policy.

¹⁷ While the fiscal deficit increased from 3 percent of GDP to 4.1 percent between 2011/12 and 2013/14, the average inflation rate declined from 24.6 percent in 2011/12 to 5.2 percent in 2013/14.

money had increased by 74 percent by 2013/14 while the velocity of money doubled from 0.2 in 2008/09 to 0.4 in 2013/14. In response to these changes, Uganda adopted an inflation-targeting-lite-monetary-policy framework in July 2011, moving to using short-term interest rates to signal the monetary policy stance. Since the huge inflationary pressures observed in 2011, the Central Bank has followed a somewhat restrictive policy stance, which together with declining food and energy prices, reduced inflation from 30.5 per cent in October 2011 to less than 5 percent in the first quarter of 2015. The Central Bank has influenced the bank lending rates only marginally, given that they are stickier than deposit rates. The persistent high margin between deposits and lending rates is partly due to limited competition among banks in the domestic market and high fixed costs associated with lending activities.

Table 3.2. Sectoral Composition and Growth of GDP (1990–2014)

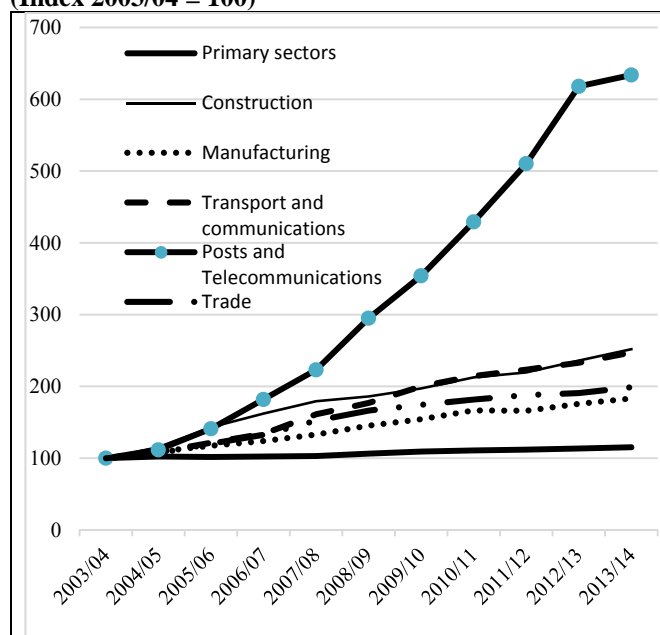
	Growth Rate (%)			Sectoral Contribution to GDP Growth (%)			Sectoral Share of Nominal GDP (%)		
	1990–99	2000–10	2011–14	1990–99	2000–10	2011–14	1990–99	2000–10	2011–14
<i>Supply of GDP (factor costs)</i>	6.4	6.8	5.1	6.4	6.8	5.1	100.0	100.0	100.0
Agriculture	2.9	2.6	1.8	0.9	0.8	0.5	31.0	29.6	25.7
Industry	10.3	8.7	5.8	2.0	1.8	1.1	19.6	20.6	19.9
Services	7.1	8.7	6.4	3.5	4.3	3.5	49.4	49.8	54.4
<i>Demand of GDP (market price)</i>	6.7	7.1	5.5	6.7	7.1	5.5	100.0	100.0	100.0
Consumption	6.3	5.4	4.4	6.3	4.8	4.0	99.7	90.9	83.8
Public	6.4	5.4	6.4	1.1	0.7	0.6	16.7	12.4	9.5
Private	6.3	5.3	4.6	5.2	4.2	3.4	83.0	78.6	74.3
Gross Fixed Capital	7.8	10.9	6.8	2.2	2.9	1.9	27.6	25.6	27.4
Public	7.8	6.2	7.5	0.7	0.4	0.5	9.3	6.3	6.6
Private	7.8	12.8	6.8	1.4	2.5	1.4	18.4	19.3	20.8
Exports	12.5	23.0	4.2	1.1	2.5	0.7	8.4	11.1	17.8
Imports	8.4	10.9	4.4	1.9	2.7	1.3	22.6	24.6	29.2
Statistical discrepancy	6.8	14.5	41.7	-0.9	-0.4	0.1	-13.1	-3.0	0.2

Source: UBOS.

Note: The difference between market price GDP and factor cost GDP is the impact of net indirect taxes.

3.6. In the last decade, growth from the production side was largely driven by the expansion of services followed by the industrial sector. The services sector currently accounts for more than half of the GDP followed by agriculture and industry (table 3.2). Among services, communication, transport, and financial services have grown by over 7 percent every year, reflecting higher local demand and technological changes (dominated by the mobile phone revolution). This pattern of growth has not directly benefitted the bottom 40 percent since most of them depend on the agricultural sector and these subsectors are not labor intensive. The expansion of industrial activities, to a large extent, captures the sustained boom in construction, initially fueled by increased private investment and lately by public investment, and the gradual urbanization process. Some growth in manufacturing, particularly agro-processing, has also contributed to industrial growth. Finally, the contribution of the agricultural sector to GDP has declined over time as this sector has grown at a slower rate than the overall economy (figure 3.2).

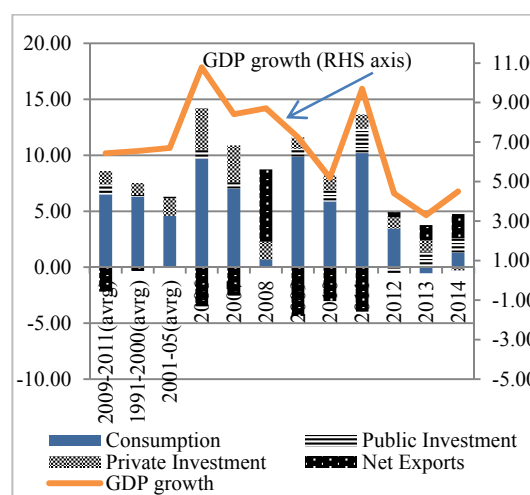
Figure 3.2. Real GDP Growth Across Selected Sectors (Index 2003/04 = 100)



Source: World Bank staff analysis using UBOS data.

3.7. Since 1990, consumption has been the largest contributor to growth, followed by private investments. Private investment and consumption responded favorably to the first round of pro-market reforms and the increase in incomes of the population. Given the level of poverty in Uganda, the high share of consumption in income, and the relatively closed economy, there are large multiplier effects to increased incomes. As a result, the share of private consumption in aggregate demand has averaged around 80 percent since 1990 (figure 3.3). Public consumption also contributed, although the ratio of public expenditures to GDP decreased from 23 percent in 2002 to 20 percent in 2010. However, the macroeconomic slippages and the government's response thereafter slowed down the economy and private investment and consumption declined during FY2012–14. During FY2013–14, the government stepped up its public investment program as part of its efforts to improve connectivity within Uganda and to neighboring markets and to increase electricity generation. This impetus in

Figure 3.3. Private Consumption and Other Contributors to Growth



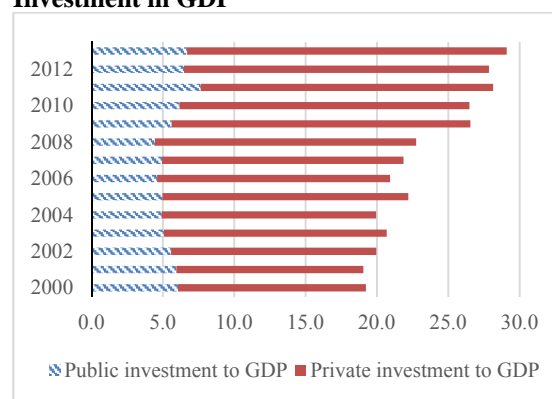
Source: Staff analysis using UBOS data.

public investment, together with the favorable terms of trade, boosted export performance and overall economic growth.

3.8. **The contribution of the external sector to GDP growth has been rather limited.** Net exports has been a drag on growth, primarily because of a narrow export base (partly because of the country being landlocked) and the need to import a large proportion of inputs that are not available in the country. In addition, a low domestic savings rate (12–13 percent of GDP) results in high dependence on foreign savings which are typically associated with increased imports. However, export diversification has increased over time with a decline in the share of the top 5 exported products from about 97 percent in the early 1980s to 55 percent in 2010–12. After nearly three decades, coffee and cotton still account for 39 percent of Uganda’s export earnings.

3.9. **While economic expansion was driven by TFP growth in the 1990s, it was replaced by factor accumulation in the 2000s.** TFP growth (productivity gains) explained about 34 percent of Uganda’s growth during 1990–2000, 28 percent during 2001–10, but was negative at minus 15 percent over 2011–2012. The reforms in the late 1980s resulted in significant TFP growth during the 1990s reflecting rebound on account of post-conflict reconstruction, policy reforms, as well as transformational growth. Since, then, TFP growth has slowed down indicating lower returns on investment. This was largely because of suboptimal allocation of resources necessitated by the relentless constraints in the investment environment and the limited progress on competitiveness. The decline in public investment also partly explains the lower overall returns on investment since it complements private investment. A comparison of Uganda with its comparators including Cambodia, Ethiopia, and Zambia suggests that Uganda needs to leverage its productivity gain which explains most of the growth differential with its comparators (table 3.3 and figure 3.4).

Figure 3.4. The Share of Public and Private Investment in GDP



Source: WDI.

Table 3.3. Productivity Performance of Uganda and its Comparators (%)

		Output	Labor	Capital	TFP
Uganda	1990–2000	6.5	1.49	2.8	2.2
	2001–10	7.1	1.29	3.8	2.0
	2011–12	5.1	1.71	4.2	-0.8
Bangladesh	1990–2000	4.8	0.9	3.7	0.3
	2001–10	5.7	2.4	4.2	-0.9
	2011–12	6.3	1.6	4.2	0.4
Ethiopia	1990–2000	2.4	1.3	1.8	-0.7
	2001–10	8.3	1.5	2.9	3.8
	2011–12	9.4	1.8	3.6	4.0
Vietnam	1990–2000	7.4	1.3	6.1	0.0
	2001–10	6.6	1.4	6.3	-1.1
	2011–12	5.6	1.4	6.2	-2.1
Zambia	1990–2000	1.2	1.0	-0.9	1.2
	2001–10	5.5	1.4	1.6	2.4
	2011–12	6.8	1.4	1.9	3.6
Kenya	1990–2000	2.0	2.1	1.1	-1.2
	2001–10	4.1	1.4	2.2	0.5
	2011–12	4.4	1.6	3.7	-0.9
Cambodia	1990–2000	6.2	1.3	1.0	3.9
	2001–10	7.7	1.4	4.2	2.1
	2011–12	6.9	0.8	4.3	1.8
SSA	1990–2000	3.6	1.3	1.6	0.7
	2001–10	6.4	1.5	3.6	1.3
	2011–12	6.0	1.4	5.2	-0.7

Source: The Conference Board Total Economy Database™, January 2014, <http://www.conference-board.org/data/economydatabase/>

Note: The choice of comparators is motivated by the level of income, regional peers, fertility management, agriculture development, resource endowment, and fragility.

B. JOBS AND PRODUCTIVITY

About 70 percent of the population is still engaged in agriculture while most of the new jobs have been created by nonfarm businesses in the informal sector with low productivity.

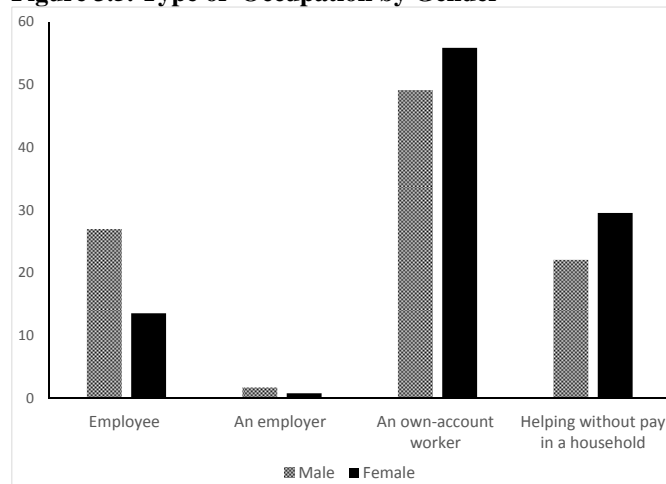
3.10. While the unemployment rate in Uganda is low, the problem is more of underemployment and employment in low-productivity jobs. With one of the youngest and fastest growing populations, a million young people enter the Ugandan labor market every two years. Due to limited job creation in the formal sector, most of them end up in informal employment or become underemployed. The overall unemployment rate, at 4.2 percent, is low, primarily because most Ugandans cannot afford not to work in the absence of an unemployment policy and the prevalent poverty rates. Unemployment rates are relatively higher in urban areas and among the youth and women (table 3.4) since, in rural areas, labor is absorbed into the agricultural sector as a residual employer. The higher youth unemployment can largely be explained by a lack of high productivity jobs, dearth of employable skills, limited access to land and capital, and a negative attitude toward certain types of work.

Table 3.4. Unemployment Rates by Gender, Location, and Age Group

Background Characteristics	2005/06		2009/10	
	Number	Unemployment Rate (%)	Number	Unemployment Rate (%)
Sex				
Male	89,600	1.7	162,500	3.0
Female	120,100	2.1	317,800	5.2
Residence				
Urban	104,900	6.4	198,100	9.5
Rural	104,800	1.1	282,200	3.0
Regions				
Kampala	17,400	8.3	87,100	11.4
Central	3,600	1.7	154,000	5.7
Eastern	1,500	0.7	91,000	3.0
Northern	6,900	3.3	89,200	4.1
Western	1,500	0.7	59,000	2.1
Youth				
15–24	110,400	4.4	174,700	5.4
18–30	143,800	3.4	256,700	4.7
Uganda	209,700	1.9	480,300	4.2

Source: UBOS.

3.11. Gender disparities in the labor force are persistent. Females as heads of households earn 28 percent lower than men. Nearly 55 percent of the women work in agriculture and they also dominate the informal economy. The existing land tenure system limits access to land for women. When employed in commercial farms and estates, women are less likely to reach managerial positions. While lesser number of years of schooling could be a part of the reason, the large families and households that women have to care for and cultural norms and perceptions about women are also responsible for the gender differences in the labor force (figure 3.5).

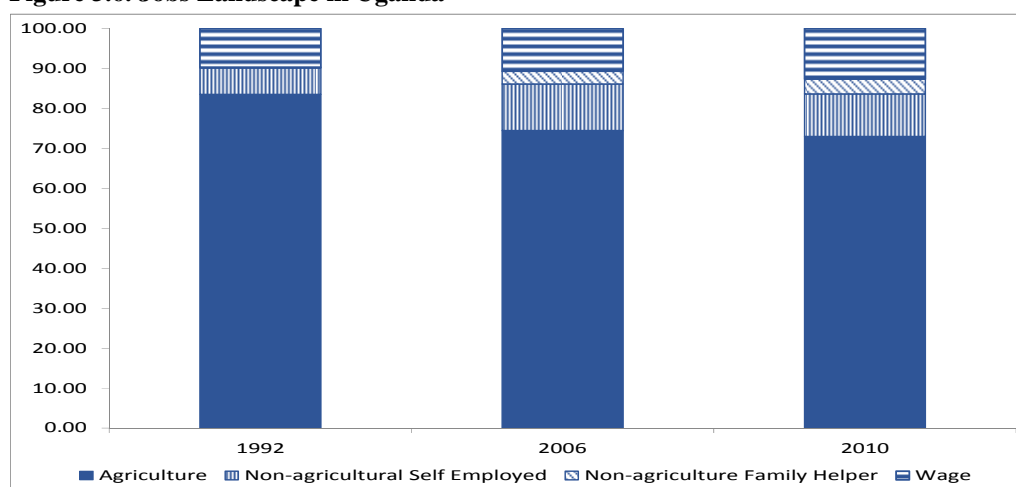
Figure 3.5. Type of Occupation by Gender

Source: Uganda Poverty Assessment using 2012/13 UNHS.

3.12. Child labor is more common in poor households as nearly half of the children in the age group of 5–17 years in Uganda were employed in some form of economic activity in 2010. This is much higher than the SSA average of 28 percent. According to the Understanding Children Work Report of Uganda, 43 percent of families which keep children out of school do so because it is too expensive for the household to have the child in school. Children are also more likely to be working, if the household has been affected by shocks such as natural disasters, epidemics, social shocks, civil strife, or loss of family members. Labor inspections are not carried out in rural areas. As a result, agricultural work accounts for almost all of children's economic activity in rural areas. In addition, child labor in the agriculture sector is one of the critical issues hindering investors' commitment of more capital to the sector.

3.13. **While Uganda has seen a structural transformation in its output structure, the jobs transformation is yet to happen.** Uganda's job landscape can be divided into three main categories: the agricultural sector, the nonagricultural informal sector, and the formal enterprise sector, a large component of which includes the wage sector. The majority of the workforce is still employed in the agricultural sector which includes crop farming, animal husbandry, and fishing (figure 3.6). The nonagricultural informal sector employed 15 percent of the labor force in low-end services and manufacturing. The formal nonagricultural sector employed 19 percent of the labor force with about 300,000 public sector jobs. The service sector (retail and restaurant) has been the major contributor to job creation in formal enterprises. The rapid strides that have been made in the telecommunications sector have given a boost to the business and financial sector.

Figure 3.6. Jobs Landscape in Uganda

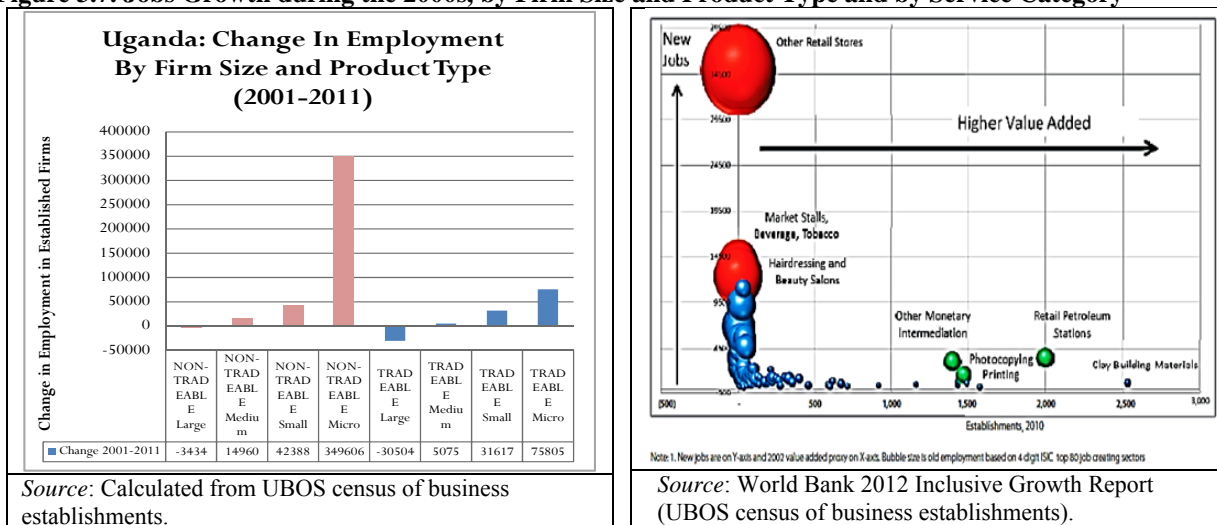


Source: UBOS.

3.14. **The main driver of job creation has been the nonfarm informal sector.** UBOS estimates that 79 percent of the firms in Uganda are informal. In 2013, only 63 percent of Ugandan firms which started their business in the year were in the formal sector which is low compared with 85 percent in LICs.¹⁸ In addition, nearly 95 percent of the 762 firms which were surveyed in the World Bank's 2013 Enterprise Survey, said that they faced competition against informal or unregistered businesses and this was the second biggest constraint that they faced in doing business in Uganda. Job creation by micro non-tradable enterprises (figure 3.7) dominated all other types of job creation between 2001 and 2011 with 350,000 new jobs, mostly in the urban areas. Large formal enterprises, mostly in the tradable sector, however saw a decline in jobs during this period. Most of the poor and those in the bottom 40 percent are typically engaged in the informal sector where they are underpaid, subject to hazardous working conditions, and unable to improve their skill base. The majority of the informal enterprises are engaged in retail sales but a large number of them are also in light manufacturing (brick making, charcoal manufacture, and beverages). Nearly 31 percent of informal sector workers receive pay only in the form of food and lodging rather than cash. Much of the reason for this informality lies with weaknesses in taxation, regulation, and property rights. Formalizing the business will involve very high costs for these small businesses.

¹⁸ 2013 Business Enterprise Survey.

Figure 3.7. Jobs Growth during the 2000s, by Firm Size and Product Type and by Service Category



3.15. **Most of the jobs that have been created have been in sectors where productivity is constrained by limited access to finance.** Agriculture, commerce, household-based services, and informal manufacturing are among the most common activities in Uganda, all of them being in the low end of the productivity spectrum. While the jobs are in general more productive than in subsistence agriculture, they require limited skills and so are not very productive. The average monthly wage is estimated at UGX 85,000 in agriculture and UGX 188,000 for other services and commerce, most of which are informal activities (figure 3.8). The main constraint to raising productivity in the informal sector is low access to finance which constrains available capital. Since these firms operate in the informal sector, they have very limited access to formal credit facilities and most of the start-up capital comes from own savings or informal credit sources. In addition, these firms also face a lack of technical and business skills and a lack of fixed locations to conduct their business. Many of them operate in the streets without authorization.

Figure 3.8. Average Wage (UGX), by Sector

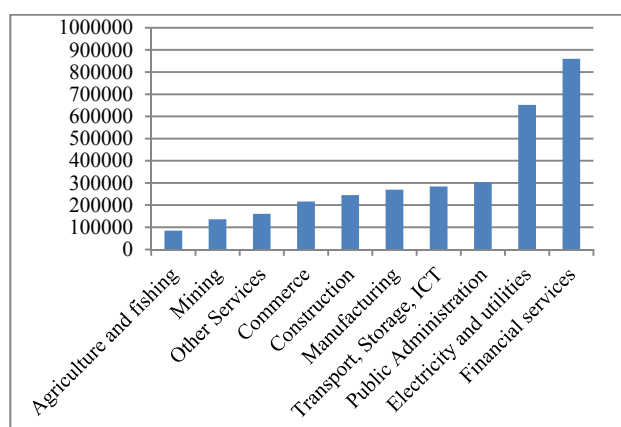
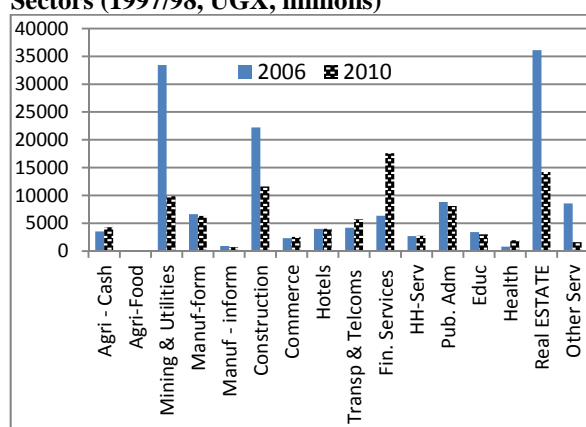


Figure 3.9. Uganda Labor Productivity Across Sectors (1997/98, UGX, millions)



Box 3.1. The Behavioral Challenge

There is a behavioral dimension to the productivity problem in Uganda which seems to pose an added challenge to the policy makers. Typically, employers use monetary incentives or a threat of dismissal to motivate employees. Similarly, governments make use of subsidies and extension services to increase the use of fertilizers and seeds in agriculture. However, these efforts may not always bring about the desired outcome.

Examples from other countries suggest that the type of contract matters. In India, for example, data entry clerks in a firm, who were paid weekly for every accurate field they entered were not motivated to enter more number of fields. They typically increased their effort close to pay days and before festivals. Discussions with the employees indicated that they would prefer rules against being absent. So the company introduced another kind of contract in which they could set their own target for the week and if they met the target, they would be paid the usual amount, if not, they would be paid at a reduced rate. This kind of a commitment contract increased the workers' productivity.

In China, a company offered an ad hoc one-time bonus of 20 percent of the pay of employees which was not tied to performance. This bonus increased hourly productivity by 3–5 percent, long after the bonus was discontinued. Hence, productivity can be increased by exceeding expectations of workers.

Public recognition can also be an inexpensive alternative to improve productivity. Female hairdressers in Zambia who sold condoms to their clients received either a monetary commission or a star for every packet of condoms sold which would be displayed in their salons. Those who received the stars sold twice as many condoms.

Small entrepreneurs in Ghana who received support in the form of in-kind grants such as equipment, increased their profits by 24 percent while those who received it in cash, did not increase their profits. Bicycle taxi drivers in Kenya worked just enough to meet their daily cash needs. These failures to capitalize on potential opportunities can be tackled through training programs, but they need to be customized. In the Dominican Republic, an accounting training based on thumb rules such as maintaining two separate drawers for business and personal income and having a system of notes for any exchanges between the drawers was more successful than a formal accounting training.

In 2011, farmers in SSA, on average used 13.2 kg of fertilizers compared with 118.3 kg in Organisation for Economic Co-operation and Development countries. An important factor among farmers in LICs is to translate their intentions into actions. Obstacles can be monetary or related to the lack of supply chains. Providing free delivery of fertilizers to farmers in rural Kenya right after the harvest (when they had cash), resulted in a significant increase in fertilizer use. Learning from peers and social networks is also crucial in the adoption of increased inputs. This was a key factor in the Green Revolution in India.

Overall, there are several non-remunerative interventions which can increase productivity such as commitment contracts, public recognition, and social networks. However, people are heterogeneous and respond to incentives in different ways. Therefore, an experimental approach to these issues is needed. The low cost of these interventions and the inherently large payoffs to some of these intractable problems, however, justifies these experiments.

Source: World Development Report 2015.

3.16. Productivity of labor in Uganda is low and declined during 2006–10, as labor shifted into lower-value-added sectors. The number of jobs in high-productivity sectors has declined while the number of jobs in low-productivity sectors has increased and this has been a drag on transformational growth (figure 3.9). Even the 300,000–400,000 graduates from universities and technical colleges every year find it difficult to get jobs which use their skills and they end up as taxi drivers and in other similar occupations despite having technical degrees. Moreover, output per worker for many sectors including mining and utilities, construction, real estate activities, and

other informal services has declined between 2006 and 2010.¹⁹ The low level of productivity is also explained by the attitude toward work, as incentives and motivation can pose major obstacles in contexts such as Uganda. Behavioral economics offers a glimpse on how to tackle some of these difficult problems and given that many of these interventions are low-cost options, they can be added to the list of policy interventions in specific areas (box 3.1).

C. IDENTIFYING THE KEY CONSTRAINTS TO GROWTH

Infrastructure bottlenecks, particularly in the power and road sector, access to finance, low level of skills, and the administrative burden of taxes are the key constraints to growth.

3.17. Several factors constrain growth in Uganda, but a series of analytical studies and surveys have repeatedly emphasized electricity, roads, access to finance, skills, and specific business regulations. Growth literature has emphasized that economic expansion is the result of a combination of factors at the micro-enterprises level or at the macroeconomic- environment level. They can range from the limited accumulation of labor and capital to the absence of innovation, an inefficient business environment, taxes, underdeveloped infrastructure, low skills, and inappropriate macroeconomic and fiscal policies. All these factors have been playing a role in Uganda's growth process, but a series of recent analytical studies have identified a few priorities that are summarized in table 3.5.

Table 3.5. Key Constraints to Growth

Study	Top Constraints
Country Economic Memorandum (CEM) 2007, World Bank (using the Growth Diagnostic framework)	<ul style="list-style-type: none"> • Underinvestment in infrastructure (electricity and roads) • Financial intermediation • Skills training
CEM 2015, World Bank	<ul style="list-style-type: none"> • Limited economic diversification • Weak institutions of governance and accountability • Weak PIM systems • Inadequate infrastructure (electricity and roads)
Business Enterprise Survey 2013	<ul style="list-style-type: none"> • Electricity • Competition from informal firms • Tax rates • Access to finance
Doing Business Report 2015	<ul style="list-style-type: none"> • Getting electricity (ranking: 184 out of 189 countries) • Starting a business (ranking: 166 out of 189 countries) • Dealing with construction permits (ranking: 163 out of 189 countries) • Trading across borders (ranking: 161 out of 189 countries)
Global Competitiveness Report 2015	<ul style="list-style-type: none"> • Corruption • Access to finance • Tax rates • Inadequate infrastructure

3.18. Sales losses due to power outages and the high cost of electricity were key constraints cited by firms but the commissioning of the Bujagali hydropower plant has helped significantly. Power cuts were pronounced during 2012 and this reflected in the 2013 Enterprise Survey (January 2013–July 2014) in which nearly 23.2 percent of the firms identified unreliable

¹⁹ The average real value added per worker in formal firms in Uganda fell by 19 percent between 2000/01 and 2009/10.

electricity services as the main obstacle for conducting business in the country. This was significantly higher than 10 percent of the firms perceiving this as a key constraint worldwide and 13.4 percent in SSA. The cost of electricity is relatively high and many enterprises complain about the inflated cost of electricity during peak hours (between 6 p.m. and midnight). In addition, power outages and load shedding is frequent in Uganda. With the commissioning of Bujagali in 2013, the power supply situation in Uganda has significantly improved, pushing supply to almost match demand. However, demand is growing fast and hence will quickly outstrip supply, if adequate investments in power generation and grid network are not undertaken. The Power Sector Investment Plan (2011), estimates that the investment requirement for power generation, transmission, and distribution between 2010 and 2030 is US\$8 billion, of which US\$5.5 billion is for power generation, US\$2 billion for transmission, and US\$0.6 billion for distribution.²⁰ Strengthening the transmission network and cross-border connectivity with neighbors will help build the resilience of the system and allow Uganda to benefit from regional energy exchanges.²¹

3.19. Despite significant investments in the road sector, Uganda is still plagued by poor transit and transport infrastructure which has raised the cost of doing business. Uganda is a landlocked country but a transit for the other countries in the EAC and Great Lakes regions. Currently, the national road network carries 90 percent of all land transport in the country. The prevalence of overloading and inadequate road maintenance has resulted in the deterioration of roads exacerbated by climatic shocks such as floods. In addition, the rail and inland water transport infrastructure is underdeveloped. As a result, the cost of moving goods within and outside Uganda is particularly high, making it less attractive to potential foreign investors. In addition to maintenance, there is also a need to remove pinch points and increase investments in road infrastructure along the key corridors, particularly the northern corridor. Border crossings need to be improved by consolidating the number of agencies at the border and by removing multiple and redundant non-tariff barriers.

3.20. Given the large infrastructure gaps, it will be important to leverage private resources and prioritize infrastructure investments—one possible way to prioritize is to target resources, for example, to connect producers to markets for emerging product champions identified through the product space analysis. Public resources are limited and the infrastructure requirements are astronomical. In such a scenario, it will be important to leverage private resources, particularly through public-private partnerships. In addition, specific investments in roads and electricity can be targeted to remove market failures for sectors identified to be on their way to developing capabilities to move up along the value ladder. The product space analysis,²² for example, identifies some emerging product champions with potential—light manufacturing (garments, leather, and wood products), agro-processing (cereals, dairy products, more types of cooking oils, and new sugar products), and a few chemicals and metal products industries. Many of these sectors were also identified by the agriculture market linkage analysis for Uganda. Infrastructure investments can be targeted in areas which will be particularly beneficial for these specific industries, although adequate attention needs to be given to inclusion as well (discussed

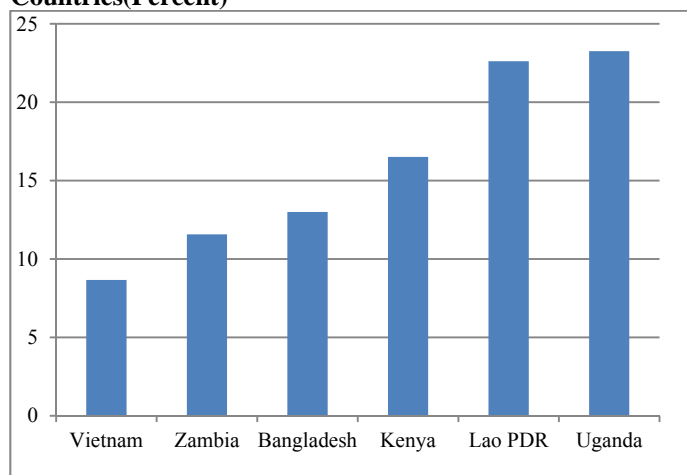
²⁰ The Second Rural Electrification Strategy and Plan estimates that an additional US\$1 billion will be needed between 2013 and 2022 for rural electrification.

²¹ These efforts should be complemented by other interventions such as building in-country capacity, in-country generation, use of renewable energy (wind, solar), and designing and implementing plans to incorporate climate variability and change, which is particularly important for hydropower that depends on reliable water resources.

²² See chapter 1, Uganda CEM 2015

in chapter 4). As an example, roads can be built to connect garment producers to input and output markets and the like.

Figure 3.10. Lending Interest Rates In Selected Countries(Percent)*



Source: WDI.

Note: (*) Latest data available in 2010–14.

financing is also very high in Uganda compared to other countries in the region and the world. Countries in Africa generally have quite high interest rates and the high cost of financing creates a significant obstacle to enterprise growth and operation, particularly for small and medium enterprises.²³ Commercial bank lending rate at about 22 percent in Uganda is high, compared with 9 percent in Vietnam and 12 percent in Zambia (figure 3.10). The high rates are largely because of a lack of competition and high overheads explained by high salaries because of the scarcity of qualified professionals, high costs of expansion, especially in rural areas, and high costs of due diligence in an environment where information is very scarce and not sufficiently reliable. The high rates also reflect the high risk premium.

3.22. The availability of long-term funding in Uganda is extremely limited because the main source of funding for banks are short-term consumer deposits. Increasing the availability of long-term funding will require capital market development and pension reforms while credit lines from development institutions can also be useful. According to the World Economic Forum Global Competitiveness Report 2014–15, Uganda ranks 121 (out of 144 countries) by affordability of financial services, which shows deterioration in ranking compared to a year earlier (116). In comparison, Kenya and Rwanda rank 64 and 56, respectively, on this indicator, and both countries improved their ranking by several points compared to last year.

3.23. The limited availability of high quality collateral, in the form of properly registered land, provides an explanation for the limited access to bank loans and their high cost. Only 20 percent of Uganda's land is registered, most of which is *mailo* land that is unacceptable as collateral because the banks cannot liquidate it, as the rights of the landowners overlap with those of the tenants (legally recognized as lawful or bona fide occupants) who enjoy inheritable and

3.21. Very few Ugandan firms have a bank loan/line of credit and the ones who have a loan get it at a high cost with relatively high collateral requirements. Only 9.8 percent of the firms in Uganda have a bank loan/line of credit from a bank compared to 23.8 percent in SSA and 36.5 percent worldwide. The value of collateral required for a loan is slightly lower than the world average, but the proportion of loans requiring collateral is higher. Few firms in Uganda use bank loans to finance investments (3.3 percent in Uganda compared to 10 percent in SSA and 16 percent worldwide, table 3.6). The cost of

²³ High interest rates are the third most cited reason by firms in Africa for not applying for loans, according to the research by Beck, Thorsten, and Cull (2014)

transferrable rights as landlords. The low rate of Uganda's land registration compares unfavorably with Rwanda's (60 percent) and even more unfavorably with that of Western European countries (95 percent). However, it compares favorably with the average SSA country. Measures to accelerate land registration and develop the capacity of institutions responsible for resolving land disputes need to be prioritized since land tenure insecurity imposes a bearing on economic growth. It is estimated that land disputes in Uganda reduce annual agricultural production by 5–11 percent.

Table 3.6. Uganda Access to Finance Indicators vs. SSA and the World²⁴

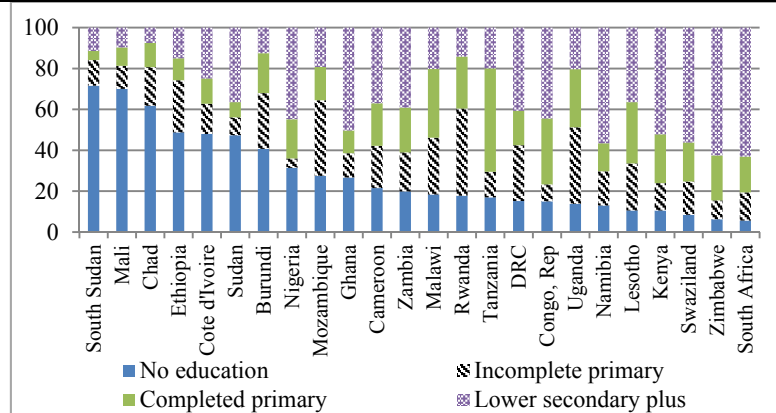
Indicator	Uganda	SSA	All Countries
Percent of firms with a checking or savings account	86.7	88.1	88.2
Percent of firms with a bank loan/line of credit	9.8	23.8	36.5
Proportion of loans requiring collateral (%)	86.4	79.7	77.3
Value of collateral needed for a loan (% of the loan amount)	159.4	175.2	182.2
Percent of firms not needing a loan	41.9	34.1	40.9
Percent of firms whose recent loan application was rejected	7.7	15.3	14.5
Proportion of investments financed internally (%)	79.5	78.3	69.2
Proportion of investments financed by banks (%)	3.3	9.9	16.3
Proportion of investments financed by supplier credit (%)	3.2	3.9	5.1
Proportion of investments financed by equity or stock sales (%)	13.0	3.7	5.0
Percent of firms using banks to finance working capital	21.7	23.5	31.0
Proportion of working capital financed by banks (%)	7.0	9.9	12.6
Proportion of working capital financed by supplier credit (%)	3.5	7.2	10.8
Percent of firms identifying access to finance as a major constraint	20.2	43.0	30.8

Source: Enterprise Survey (2013).

3.24. Skills gaps are emerging in Uganda as evidenced by the large skills premium in some sectors. This is particularly true for the high-end jobs in financial services, transport, and communication. The inward migration of skilled workers, especially in telecommunications, engineering, and banking also points to specific skills shortage. However, low education does not seem to be particularly binding at this stage, as evidenced by the

ranking of constraints faced by firms. In addition, the fact that even the university graduates remain underemployed and do not find suitable jobs, partly reflects the lack of jobs that require their skills and partly the irrelevance of the education curriculum. Also, while primary enrollment rates have gone up, primary completion rates are still very low which show low 'perceived' gains from education and also high poverty levels which act as a deterrent for households to send children to schools. In Uganda, only 20 percent of the labor force has completed at least secondary education,

Figure 3.11. Education Attainment of Labor Force



Source: UBOS

²⁴ Enterprise Surveys in Uganda (2013)

compared with 50 percent in Ghana (figure 3.11). Education and skills are discussed in detail in chapter 4.

3.25. Firms cite taxation as a key obstacle, due to the huge administrative burden and unfairness of the system. The administrative tax burden in Uganda is high. A complicated tax administration system acts as a disincentive for entrepreneurs to operate in the formal sector. Nearly 75 percent of the firms surveyed in the 2013 World Bank Enterprise Survey were inspected by tax officials during the year with several of them hosting four visits by tax inspectors. With this burden, formal firms spend comparatively much more time with tax officials than in other LICs. With the high informality, efforts to raise overall tax revenue have also raised the burden for the formal firms, who feel overtaxed. There are also complaints by firms about taxes and licensing at the local level with businesses being viewed as ‘cash cows’ and being taxed onerously. Firms in the agriculture sector complained about the increase in the taxes on inputs which dramatically increased the cost of operations. Companies also disclosed rampant evasion of taxes through the falsification of invoices.

3.26. While these constraints have been singled out, there are several other constraints that businesses face while operating in Uganda. A lot of them are related to business regulations such as starting a business, dealing with construction permits, and the prevalence of informal payments to operate in the country. These governance and other challenges also increase the cost of doing business in Uganda.

D. OPPORTUNITIES FOR GROWTH

Looking forward, the oil sector, regional integration, ICT development, and efficient urbanization offer significant opportunities to raise growth in Uganda.

3.27. Uganda has been transforming rapidly in recent years and sectors which offer significant potential include oil, regional integration, ICT, and urbanization. The discovery of oil has the potential to be a game changer for the country. The prospect of further regional integration, technological ICT innovation, and the rapid urbanization process also represent opportunities for accelerating the development process in the coming years. Optimizing those drivers will, to a large extent, determine Uganda’s capacity to make progress on the twin goals over the next decade. These opportunities were identified by a diagnostic using past and ongoing analytical work within the Bank (Uganda CEM, 2015 and various issues of the Uganda Economic Update); and outside.

Driver 1: Harnessing Extractives for Growth and Resilience

3.28. As of 2015, Uganda’s oil reserves are estimated by the government at 6.5 billion barrels with only 1.1–1.4 billion barrels considered recoverable. The current official estimates of oil reserves may underestimate the country’s potential in minerals by a wide margin since only 40 percent of the oil-rich Albertine Graben region has been explored so far. In addition, recent surveys have identified numerous viable deposits of minerals, ranging from iron ores to uranium.

3.29. There is significant uncertainty on the start of oil production and the expectation is that it could begin earliest by 2018 with the smallest oil reservoir, exploration area 3A (EA3A) (box 3.3). At this stage, the investment plans are influenced by two important factors that

are not entirely under the control of Uganda's government. The first is the construction of the pipeline that will enable Uganda to export its oil through Kenya, as there is still disagreement on the location of the pipeline. The second is the medium- to long-term price of oil on international markets.

3.30. The economic viability of the three main oil areas will largely depend on the future price of oil. At the current level of oil prices at around US\$50 per barrel, the consortium of private oil companies will find it difficult to recoup their investment costs. This is because of the terms of the existing production sharing agreement between the government and the oil companies. As a result, there is significant uncertainty on the start date of oil production. Whenever it starts, oil will have a large impact on the Ugandan economy. If managed properly, it has the potential to substantially raise government revenues, increase exports, and result in impressive growth rates. A decline in energy prices and forward and backward linkages will also boost growth. However, the oil sector will provide limited employment opportunities given the capital-intensive nature of the hydrocarbon industry.

Box 3.2. Basic Assumptions for the Projection of Future Oil Production

- Oil reserves of 6.5 billion barrels, of which 1.3 billion are recoverable (923 million in EA1, 231 million in EA2, and 134 million in EA3A).
- Oil production is expected to begin in 2018 as EA3A goes on stream, followed by EA1 and EA2 in 2020. Production will peak in 2025, decline gradually, thereafter, and end in 2044.
- Total downstream capacity will reach 230,000 barrels per day, including 30,000 barrels per day processed by the refinery (which will begin production in 2019) and 200,000 exported through the pipeline.
- Initial production of crude oil will be used primarily for power generation until the downstream capacity is in place.
- 30,000 barrels per day will be reserved for the refinery. Surplus production will be exported through the pipeline.
- Total capital expenditures for the development of oil fields will reach US\$7.6 billion. The construction of the refinery and the pipeline will cost US\$4.5 and US\$3 billion, respectively, including a government equity contribution of US\$2 billion to the overall project (field development, refinery, and pipeline).
- The long-term price of oil will average US\$90 per barrel, as projected by the World Bank Global Economic Prospects, with a 15 percent discount for Uganda's oil due to high viscosity.
- The pipeline will charge US\$10.18 for each barrel of oil piped to the Kenyan coastline. This includes a US\$0.18 transit fee.

Source: Uganda CEM (World Bank 2015c)

3.31. Sound oil revenue management is a precondition for harnessing the significant potential benefits of oil. Uganda's performance in budgetary management is generally solid on transparency and the new PFM Act has instilled expectations of a sustained improvement in budget operations. However, as seen with other public management reforms the key will be implementation. Andrews and Bategeka (2013) argue that Uganda has a poor history with 'off-the-shelf' governance initiatives. The new PFM Act, which includes among others, clauses on budget credibility and oil management, benefitted from extensive consultations to contextualize the reform and therefore to improve the likelihood of its implementation as they recommended. Some of the outstanding PFM challenges include weak budget credibility, controls, and compliance. Overall, governance is a main point of concern, and an area of weakness in the

3.32. As will be discussed in chapter 5, natural-resource-rich countries have often faced syndromes, collectively termed the resource curse, which pose the main obstacle to capitalizing on oil. This manifests itself through (a) real appreciation of the local currency that hampers the country's export competitiveness and production; (b) economic volatility following oscillating world market oil prices that affect investment and economic growth over time; (c) rent-seeking behavior that leads to corruption and socially-inefficient spending; and (d) a false sense of security that reduces human and social capital investments. The country therefore needs to sustain the gains in PFM reform, while critically addressing the broad areas of governance including property rights, fiscal management, quality of public administration and transparency, accountability, and corruption to effectively leverage the benefits from oil.

Box 3.3. An Uncertain Date for the Start of Oil Production

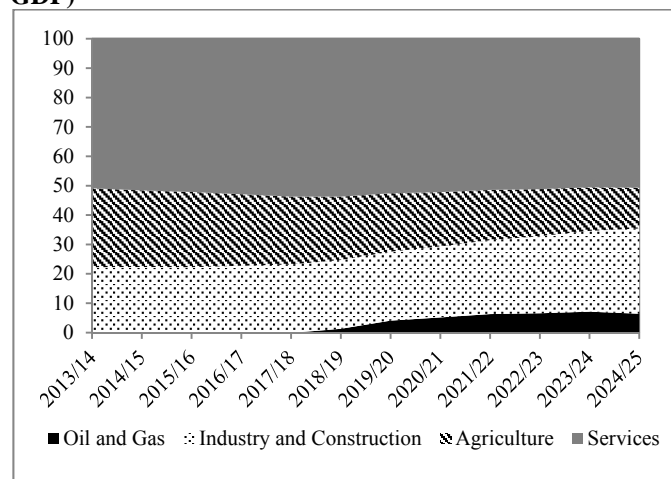
In spite of sizable proven reserves and favorable prospects, there is still considerable uncertainty about the magnitude and the timing of the expected investments. Negotiations between the government and the international investors began about four years ago, but are not yet finalized. The three major international oil companies operating in Uganda (Total, Tullow, and the China National Offshore Oil Corporation (CNOOC)) plan to start production in 2018 (CNOOC) and 2019 (Total and Tullow). Total production will peak at 230,000 barrels per day by 2025, but will decline thereafter and end around 2044. The plan is to process 30,000–60,000 barrels per day in a local refinery for the domestic and the regional markets (Burundi, the Democratic Republic of Congo, South Sudan, and Rwanda), while the remainder will be exported through a pipeline from Uganda's oil fields to Kenya's coast line. Delays in the granting of production licenses to oil companies by the government has frustrated these companies, resulting in the downsizing of a large part of their expatriate staff in the country.

Oil companies and the government of Uganda (GoU) are aiming to begin basin-wide development in early 2016 which will imply first commercial-scale production, most likely by 2020. A production license has already been issued on the CNOOC-operated Kingfisher field and this can lead to some very limited early oil production sold into the domestic market before 2019. If this occurs, it will probably be widely trumpeted as 'First Oil' but will have little impact on government revenues. The export pipeline continues to be a source of uncertainty and delay.

There now is apparently an agreement in principle on a combined Uganda/Kenya pipeline, consolidating Ugandan oil with oil from the Lukeino Basin in Kenya for export at a terminal near Lamu. However, the specific routing is still undecided and debate carries on within both the Ugandan and Kenyan governments about whether such a pipeline should be a public sector or private sector project. As a result, the technical, financing, and commercial arrangements governing the pipeline are not progressing as quickly as the upstream work. The GoU is in the final stages of selecting a strategic investor for the planned 60,000 barrels per day Hoima refinery. Even once the partner is selected, the process of finalizing technical and financial arrangements for the refinery will be lengthy. Peak government oil revenue is likely to be reached only by the mid-2020s. The government can use this interim period to improve transparency, tackle corruption, and raise capacity within the government. Moreover, a frank discussion with oil companies on pending issues such as production licenses and cost recovery will be needed.

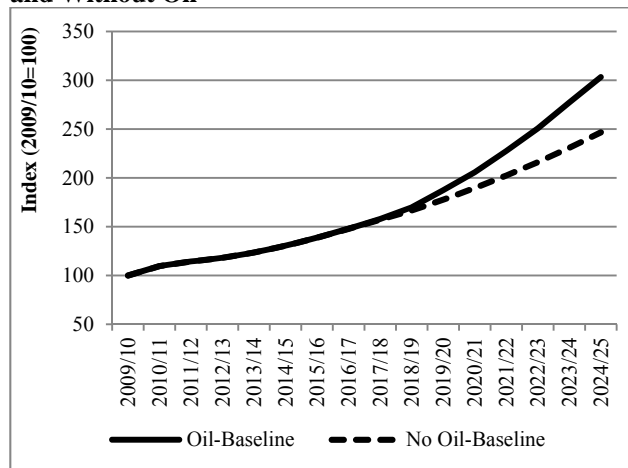
3.33. Although there is uncertainty over the start of oil production, simulations show that oil will have a large impact on the Ugandan economy. Oil production is expected to generate around US\$85 billion over the 25-year life of the resource. Net of all expenses, this will translate to US\$14.1 billion in net present value.²⁵ The total value added by the oil sector is expected to reach 7 percent of GDP by the mid-2020s (figure 3.12 and box 3.2). In terms of jobs, about 13,000 direct jobs are expected to be created during the initial phase of construction of the pipeline and refinery. Most of the impact will be indirect. Moreover, the oil sector will become a source of growth for other businesses linked directly or indirectly to oil activities. Although permanent jobs are expected to settle at around 3,000 when production begins, the development of local capacity through training and linkages, notably in sectors like transportation and logistics, will boost the economy. This can stimulate the creation of new and higher paying jobs and benefit the overall Ugandan community. The growth projection can go even higher if second-round effects, through linkages originated for the efficient use of oil revenue, are taken into account.

Figure 3.12. Sector Contribution to GDP (as % of Overall GDP)



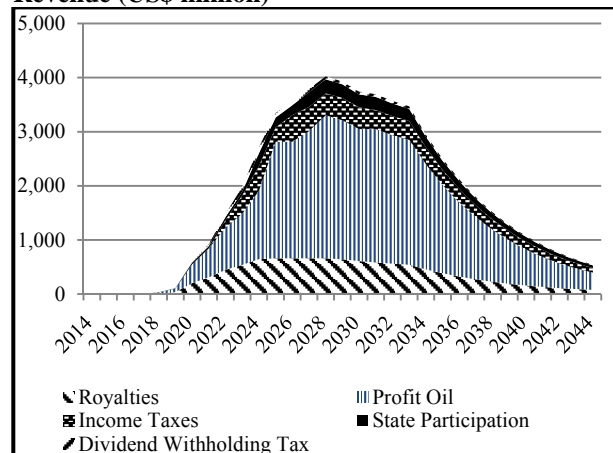
Source: Uganda CEM (2015) estimations using Macroeconomic Model for Uganda (MacMod-UG).

Figure 3.13. Uganda's Real GDP Growth Path with and Without Oil



Source: Uganda CEM (2015) estimations using MacMod-UG.

Figure 3.14. Projected Government Petroleum Revenue (US\$ million)



Source: Uganda CEM (2015) estimations using MacMod-UG.

3.34. The emergence and the development of Uganda's oil industry and the capacity of the government to increase public investment will have a major impact on GDP growth during the next decade. Figure 3.13 illustrates Uganda's growth path with and without oil. Assuming

²⁵ The net present value assumes a 10 percent discount factor. A lower discount factor will result in a higher net present value.

that oil production comes on stream in 2017/18 (box 3.3) and that public investment continues to accelerate during the next decade, real GDP growth is expected to average 8.8 percent annually between 2015/16 and 2024/25, that is, 2.2 percentage points higher than in a scenario without oil and a more limited investment surge. In per capita terms, the emergence of the oil sector and a continued emphasis on public investment will allow Uganda to reach the US\$1000 GDP per capita mark by 2019/20 and lead to a 32 percent larger GDP per capita than in a situation without oil and less public investment.

3.35. The largest share of total oil revenue will accrue to the government. On the basis of production sharing agreements concluded by the government and the oil companies and assuming a long-term price of oil of US\$90 per barrel, 70 percent of the net present value of oil production will go to the government. This is in line with agreements in other new oil producing countries. In Ghana, the government's share of the net cash flow of offshore oil fields is about 69 percent.²⁶ Oil production in Uganda is expected to generate US\$57 billion in government revenue between 2017/18 and 2044/45, through the government share of oil profits, royalties, income taxes, dividends, and interest on the 15 percent government equity in oil fields (figure 3.14). Additional government revenue will average US\$2.1 billion per year (two-third of the domestic revenue in FY2013/14) and will reach US\$4 billion in peak production years.

3.36. A big contribution of Uganda's petroleum sector will be in the form of additional public investment in key sectors such as infrastructure, health, and education but this contribution will not be automatic. Oil revenues will offer a great opportunity to meet some of the most important public spending needs and to ease some of the country's key economic constraints. However, this will require efficient management of resources and mismanagement is a strong possibility in a weak governance context. Pitfalls associated with the extractives are discussed under chapter 5.

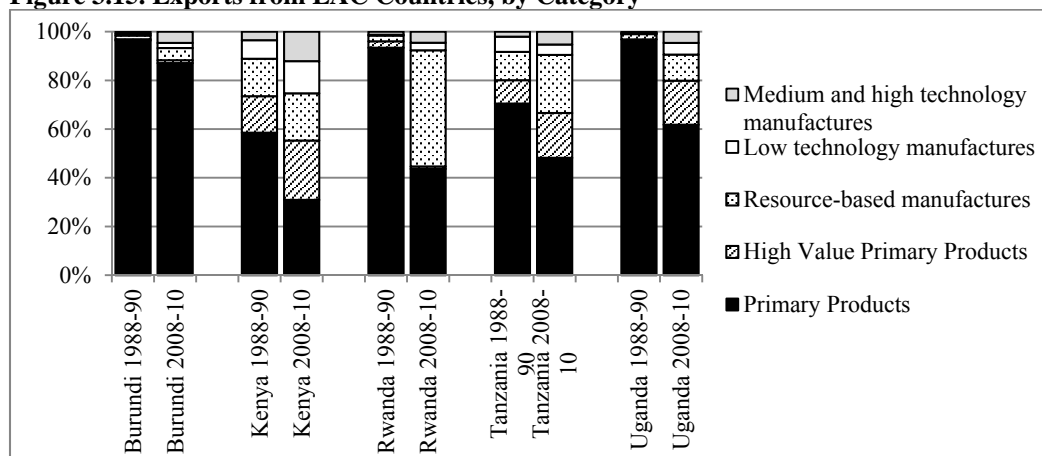
Driver 2: Expanding Trade and Investment and Deepening Regional Integration

3.37. Uganda is a member of several regional agreements, including the EAC and COMESA. These regional agreements have led to a surge in trade.²⁷ Uganda's exports to the four EAC partners nearly doubled from 15 percent of total exports in FY2007 to nearly 25 percent in FY2011. This opening has allowed the diversification of the export base to manufacturing products such as iron sheets, cement, and plastics, which have also gradually substituted imports in the domestic market (figure 3.15). Regional integration can bring further benefits if the remaining trade barriers are removed, including high transport costs and non-tariff barriers. There is also a need to promote financial integration and to facilitate the regional movement of people and capital. At the same time, the development of new regional markets remains affected by ongoing regional insecurity.

²⁶ See World Bank (2009): Economy-wide impact of oil discovery in Ghana.

²⁷ During 2001–2010, the EAC was the second-fastest growing economic bloc in the world.

Figure 3.15. Exports from EAC Countries, by Category



Source: Bank staff calculations based on Lall (2000); using mirror export data from Comtrade/World Integrated Trade Solution databases.

3.38. To fully capture the benefits from regional integration, Uganda will need to improve its competitiveness. This will require reducing transport costs through more efficient modes of transport and improved logistical services. The focus on improving roads in the trade corridors must be complemented with regional coordination with neighbors to maintain these roads, development of more efficient and cheaper modes of transport such as railways, and improvement of ports. Transport costs will come down by improving both infrastructure and transport logistics, including improvements to the trucking, freight, and storage industries. For agricultural exports, the challenge is to ensure enough quantities (to realize economies of scale along the value chain), of sufficiently high quality and at competitive prices. Overall, while Uganda needs to sustain its efforts to deepen regional integration as a means of facilitating greater trade and investment opportunities, this will have to go together with an increase in the competitiveness of the sectors that have the highest potential for regional expansion, particularly in agriculture (maize, beans), light manufacturing (cements, plastics), and some services like tourism.

Driver 3: Accessing New Information and Communication Technologies (ICT)

3.39. Ugandan firms lag in the use of ICT compared with peers. According to the World Bank 2013 Enterprise Survey, only 40 percent of the firms were using email to communicate with clients and suppliers, compared to 73 percent in Kenya and 53 percent in Zambia. Website use is even less prevalent with 19 percent of firms having their own website compared to 47 percent in Kenya. While the use of cell phones in operations is relatively widespread at 84 percent, it is lower than in Bangladesh (almost 100 percent) and Kenya (92 percent). However, Ugandan firms appear to be ahead of other SSA countries in the use of mobile money. The most important reason for the use of mobile money by Ugandan firms is that it reduces the time and cost of financial transactions. More generally, Uganda is ranked 104 out of 144 countries worldwide on innovation and business sophistication and 119 on technology readiness in the Global Competitiveness Index (2014–15).

3.40. The government has made efforts to strengthen the policy and institutional environment in the ICT sector. It completed the implementation of Phases I and II of the National Backbone Infrastructure (NBI) funded by a bilateral credit from China including over 1,500 km of fiber optic cables. The NBI was commercialized following open access principles and it is

managed and marketed by a competitively selected private company (Soliton, Kenya) under a management contract. The third phase of the NBI is under implementation. During this phase, the government intends to improve the reliability of the NBI by constructing additional fiber optic links through additional major towns in the northern and southwestern regions of Uganda and connecting to existing and future regional infrastructure.

3.41. Despite these efforts, access to broadband networks remains low, with poor quality and high prices primarily because of inadequate infrastructure and high energy costs. Entry level mobile broadband service (500 MB per month) costs about 19 percent of the average Ugandan's monthly income,²⁸ compared to the United Nations (UN) Broadband Commission's target of 5 percent. Broadband internet connections, available in Kampala, provide faster connections but the service is prohibitive for many small businesses, costing up to US\$500 a month. The high costs are reflected in low broadband penetration rates of just 1.4 percent (1 percent mobile and 0.4 percent fixed), compared with a regional average of 4.3 percent. The high costs and low penetration result from a number of factors, including Uganda's position as a landlocked country requiring overland access to submarine cables landing in neighboring countries, previous technical problems of the national backbone network, and perceived limited market opportunity by private operators given the high rates of poverty and illiteracy in most rural areas. A more stable and lower-cost energy supply will be important for developing the potential of the ICT sector (energy represents up to 25 percent of the operating expense of the telecommunications industry).

3.42. The efficient development of the ICT sector has the potential to increase the availability of jobs, improve public service delivery, and thereby, spur growth. The prospects of using more and better ICT can improve firms' competitiveness by reducing their information costs as well as by facilitating access to formal credit over time. These gains will promote private sector expansion and help create jobs for the fast growing Ugandan labor force. In addition, ICT has the potential to be a source of employment for Uganda's English speaking population and the increasingly unemployed university graduates. There is significant potential to improve public service delivery using ICT but it is also the hardest to achieve in a developing country context. E-government services remain highly underdeveloped in Uganda. The 2014 UN e-Government Development Index ranked Uganda at 156 out of 193 countries for e-government development, in the middle of the range for African countries. The impact of ICT in development can be far reaching as summarized in the examples in table 3.7.

²⁸ International Telecommunication Union

Table 3.7. ICT for Development - Some Examples

ICT Enablers	What it means for development and specific examples
Mobile-enabled services	<ul style="list-style-type: none"> • Agriculture mobile-based services are providing localized information about price, weather and climate, pest control, cultivation practices, and agricultural extension services to aid farmers in increasing productivity. • Governments are embracing mobile solutions to put public services literally into the pocket of each citizen, create interactive services, and promote accountable and transparent governance.
Digital identity/e-ID	<ul style="list-style-type: none"> • In Nigeria, digital IDs, introduced in 2011, eliminated about 43,000 ghost workers from the public payroll saving more than US\$75 million. • Administrative costs for Brazil's <i>Bolsa Familia</i> dropped from 12.5 percent to 2.5 percent with the use of digital ID cards.
Digital/mobile money	<ul style="list-style-type: none"> • In Kenya, over 17 million (two-thirds of the population) now use M-Pesa for cash transfers through mobile devices. 25 percent of the country's gross national product flows through it.
Predictive analytics/ Sentiment analysis/ Crowdsourcing	<ul style="list-style-type: none"> • Mapping disease outbreak data through crowdsourcing and predictive analytical tools enables health care providers to predict and prepare for the arrival of diseases.
Open Data	<ul style="list-style-type: none"> • Studies have found that every dollar invested in Open Data can generate five dollars of new economic value. • Kenya's government estimates that Open Data can save it US\$1 billion in annual procurement costs, while increasing beneficiary feedback and participation.
Cloud computing infrastructure	<ul style="list-style-type: none"> • By promoting economies of scale and sharing of a common infrastructure, cloud computing infrastructure can produce cost savings of up to 80 percent.
Citizen engagement tools	<ul style="list-style-type: none"> • Ureport is used to map banana bacterial wilt infection and disseminate disease treatment options (food security). • Ureport is also used to get insights into use of textbooks and science kits from direct beneficiaries (students, teachers, and parents).
Cybersecurity infrastructure	<ul style="list-style-type: none"> • According to a recent study, the average global cost of data breaches was US\$136 per record in 2012, up from US\$6 in 2011. A robust cybersecurity infrastructure is paramount in safeguarding a country's economic and social well-being.
Institutional, legal and regulatory frameworks	<ul style="list-style-type: none"> • The establishment of trustworthy ICT legal and regulatory frameworks have enabled countries like South Korea and Singapore to accelerate their national ICT programs and attract foreign investments.
ICT skills	<ul style="list-style-type: none"> • Large numbers of ICT-skilled citizens enable India to export more than US\$70 billion annually in ICT services. • Impact sourcing provides jobs in data entry and digitization for disadvantaged youth in Cambodia, Laos, and Kenya.

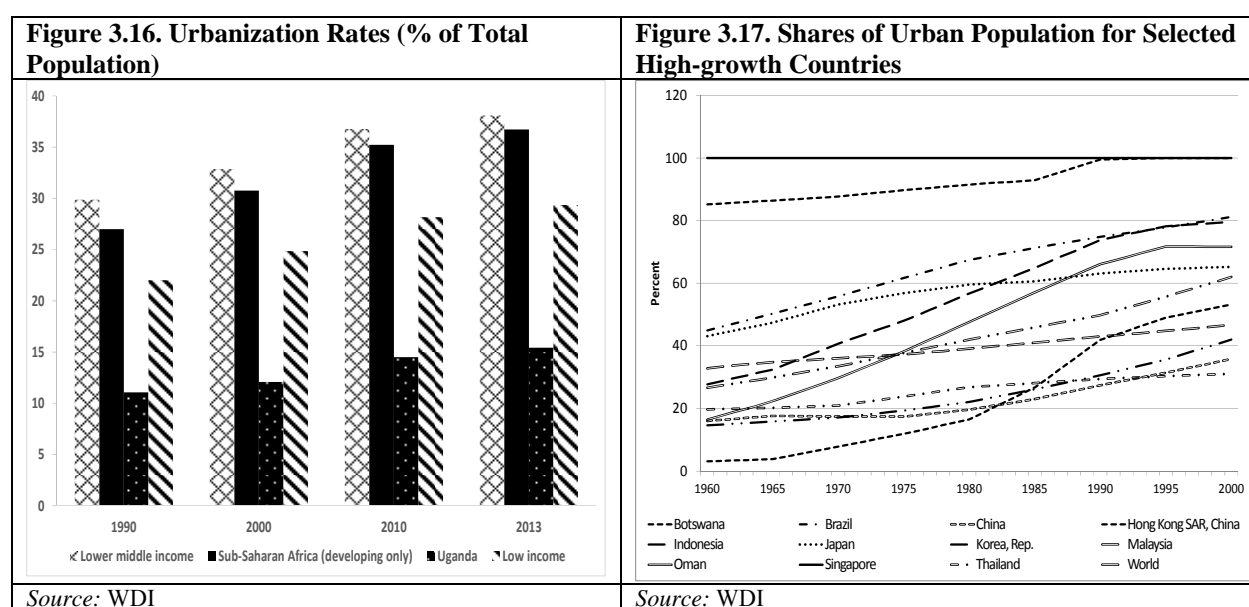
Driver 4: Accelerating Urbanization

3.43. **Uganda's urbanization rate remains relatively low at about 15 percent in 2013.** This was significantly lower than that of its EAC counterparts (Kenya stands at 25 percent and Tanzania at 31 percent) and below that of the average LICs and SSA countries and other high growth countries (figure 3.16 and 3.17).²⁹ However, the pace of urbanization is increasing in Uganda and

²⁹ While the UN definition of urbanization focuses on the national definition of urban and rural areas, another measure of urbanization is the agglomeration index which uses three indicators (population density, population size of large urban centers, and proximity [travel time] to the nearest such urban center) to estimate the level of urban concentration in a country or region. According to this measure Uganda's urbanization rate is estimated at 25 percent compared to Kenya (28 percent) and Tanzania (24 percent) in 2010. Uganda's level of agglomeration is estimated to have increased further over the past four years, to reach 34 percent in 2014.

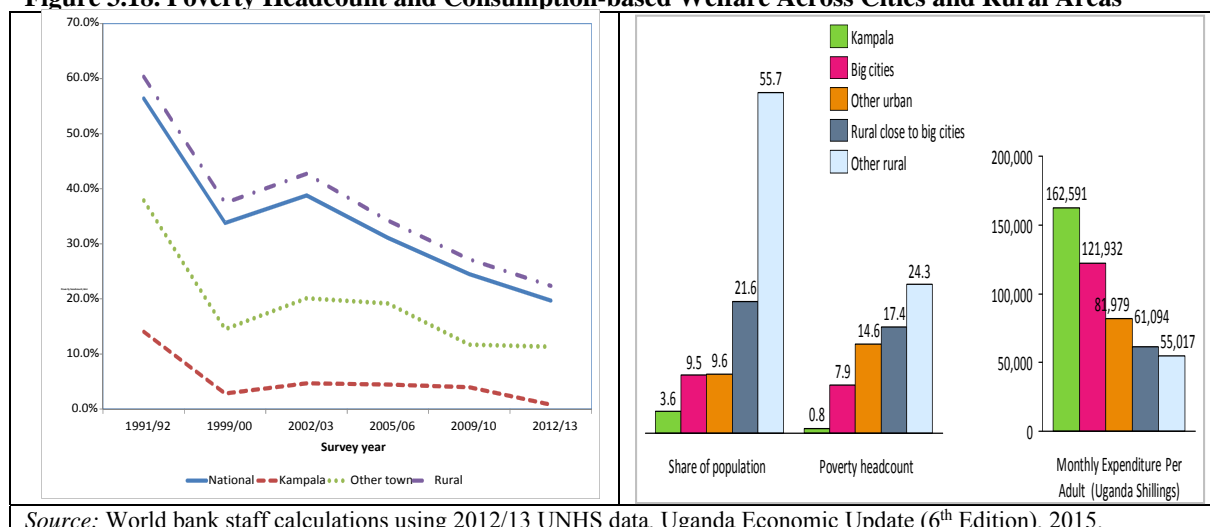
it is estimated that the population in Kampala and other urban areas will be close to 10 million by 2030.

3.44. International experience shows that urbanization, through agglomeration effects, can boost growth. No country has ever reached high-income levels with low urbanization. There is a strong correlation between urbanization and levels of income for the following reasons. First, as more people interact, there is more scope for innovation. Second, larger groups of population living in close proximity allow for economies of scale. Firms can produce goods in larger quantities at lower marginal costs and deliver them more cheaply, serving a larger number of customers. Urban centers play a dual role as a producer and consumer. As a producer, the urban sector, if well-enabled, produces more jobs, revenue, houses, skills, value addition, and knowledge. As consumers, the urban sector provides ready markets for goods and services to meet the needs of the urban dwellers, who have higher disposable incomes. Third, the transformation of the rural economy, particularly agriculture, will benefit strongly from the development of the urban economy.



3.45. The initial gains from urbanization are already evident in Uganda. More than 70 percent of manufacturing activities are conducted in urban areas while 65 percent of the new jobs over the past decade were created in cities and urban centers. In addition, employment opportunities in the formal sector are concentrated in urban areas. Urban areas also have lower poverty levels and higher consumption levels (figure 3.18).

Figure 3.18. Poverty Headcount and Consumption-based Welfare Across Cities and Rural Areas



Source: World bank staff calculations using 2012/13 UNHS data, Uganda Economic Update (6th Edition), 2015.

3.46. **However, the economic gains associated with urbanization are not automatic.** The rapid urbanization process in Uganda is putting pressure on the delivery of social and infrastructure services in urban areas. Housing has become a challenge and it is estimated that slums and informal settlements provide accommodation to more than 60 percent of the Ugandan urban dwellers. Such settlements are characterized by a lack of basic services, over crowdedness, homelessness, makeshift dwelling units, crime, and poor sanitation. It is estimated that the urban areas have a total housing stock of 700,000 housing units with a backlog of 153,000 housing units. Most of the urban development in Uganda is currently happening without planning and lacks infrastructure, particularly transport infrastructure.

3.47. **The key constraints to urbanization in Uganda include the policy and legislative framework, the land tenure system, markets, and housing, among others.** The policy³⁰ and legal³¹ framework for Uganda's urban sector is too diffused and sometimes conflicting and therefore does not take care of the current challenges and realities of the urban sector. Under the umbrella of the National Urban Policy which is in an advanced stage of preparation, existing policies such as the National Land Use Policy and the Decentralization Policy need to be reviewed and harmonized. About 70 percent of the land in Kampala is under *mailo* tenure in which the rights of landowners overlap with those of tenants (legally recognized as lawful or bona fide occupants) who enjoy inheritable and transferrable rights similar to landlords, thereby making it very difficult to sell such land or use it for long-term investments. In addition, due to the absence of a land tax, a considerable amount of urban land has been accumulated and left idle by speculative buyers. Both the land tenure system and lack of a land tax and enabling site and construction standards have led to inefficient horizontal expansion, rather than more efficient vertical expansion achieved through the construction of high-rise multipurpose buildings. There is therefore a need for urban

³⁰ Policies relating to urban development include the National Land Use Policy, Decentralization Policy, Health Policy, National Environment Management Policy, National Land Policy, and Water Policy, among others.

³¹ The legal framework regulating the urban sector includes the Local Government Act, Cap 243; the Public Health Act, Cap 281; the National Environment Act, Cap 153; Access to Road Act, Cap 350; the Land Act, Cap 227; the Condominium Property Act, 2001; the Physical Planning Act, 2010; the Water Act, Cap 152; and the Market Act, Cap 94, among other laws.

land policy measures that support efficient investments and service delivery in urban areas, including promotion of satellite towns. A public-private partnership framework to promote low-cost housing schemes for the low- and middle-income people will help address the urban housing concerns. In addition, the urbanization process also suffers from inadequate financing and the lack of institutional development.

4. BUILDING ASSETS FOR INCLUSIVE GROWTH

4.1. **The objective of every country is to improve the standard of living of its citizens and enhance human welfare which not only requires higher economic growth but also progress on various other dimensions.** These dimensions include the ability “to lead long and healthy lives, to be knowledgeable, to have access to the resources needed for a decent standard of living, and to be able to participate in the life of a community”.³² Hence, notions of welfare and standards of living go beyond the narrow dimension of material welfare and include social, political, and environmental factors. These factors also determine the accumulation and use of assets by individuals and households to earn returns. The income-generating capacity of individuals depends on crucial assets like human, physical, natural, financial, and social capital and the ability to effectively use this capital.

4.2. **So far, Uganda has underinvested in the asset base of its citizens and this has had a significant impact on their income-generation capacity.** For Ugandan citizens in general and more so for the poor and those in the bottom 40 percent, access to social and infrastructure services is severely limited. Not only is the access limited, there are also concerns on quality. And this is coupled with the near absence of a formal social assistance program. These factors have constrained development outcomes in Uganda and the country remains one of the poorest in the world despite two decades of sustained high growth.

4.3. **This chapter discusses the factors which affect the capacity of individuals and households to accumulate assets and use these assets effectively to earn incomes.** These factors include health, education, and skills, access to land and infrastructure services, access to finance, voice and participation, and social protection.

A. HEALTH

With a high disease burden and low public spending on health, out-of-pocket (OOP) expenses on health care are large and potentially impoverishing.

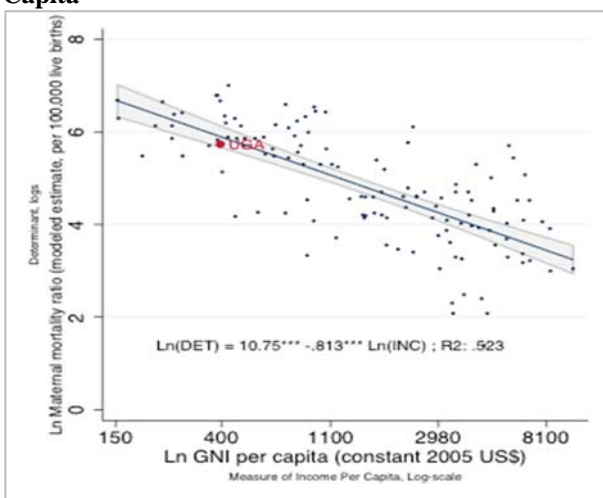
4.4. **Health outcomes have improved in Uganda but still remain far from international standards.** With regard to the health-related Millennium Development Goals (MDGs), Uganda will achieve MDG1 (child nutrition) and MDG4 (child mortality), partly achieve MDG6 (communicable disease control), and will not meet MDG5 (maternal mortality). Uganda is making progress to reduce infant and under-five mortality, but the rates remain high (but comparable with countries with a similar GNI per capita) at 90 and 54 deaths per 1,000 live births, respectively (figure 4.1). Despite several initiatives to promote safe delivery services including antenatal and postnatal care, the maternal mortality rate has stagnated at 438 deaths per 100,000 live births and is comparable with countries with a similar GNI per capita (figure 4.2).

4.5. **Ugandan youth are particularly afflicted by adverse health and demographic developments.** Teenagers bear a disproportionate burden of maternal morbidity and mortality

³² The UN.

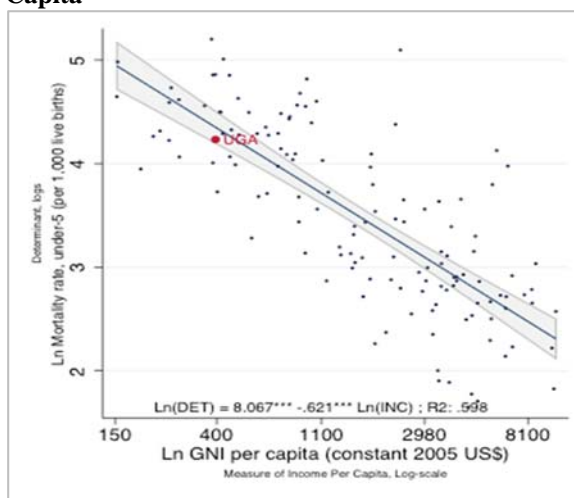
owing to the high rate of teenage pregnancies, with 24 percent giving birth to their first child before turning 19 years of age. In addition, despite the provision of antiretroviral drugs for HIV patients, there has been an increase in HIV prevalence rates in the 15–24 age group. This is partly because the improved treatment has resulted in greater longevity for those with HIV and there is growing complacency among the general population.

Figure 4.1. Maternal Mortality Rate vs. GNI Per Capita



Source: Gable et al. 2014.

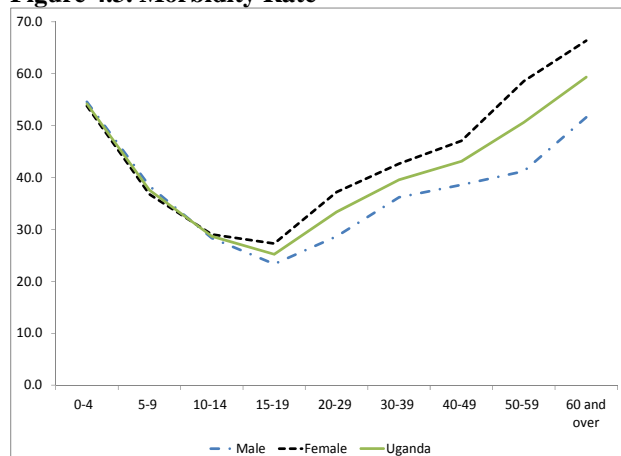
Figure 4.2. Under-five Mortality Rate vs. GNI Per Capita



Source: Gable et al. 2014.

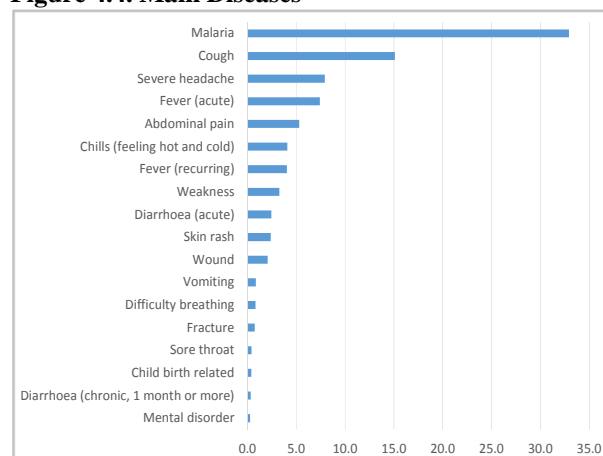
4.6. The high disease burden is being compounded by noncommunicable diseases (NCDs) and emerging challenges to public health. Malaria, maternal and neonatal disorders, HIV/AIDS, respiratory tract infections, and diarrheal diseases are the main health concerns. Morbidity is high (figure 4.3). About 40 percent of the population report to have suffered from an illness or accident over the previous 30 days. Morbidity rates are apparently lower for the bottom 40 percent. However, it is well known that the poor tend to underreport episodes of sickness. The main symptom cited in episodes of illness is fever which is usually diagnosed as malaria. As a result, malaria accounts for 32.9 percent of the episodes of illness (figure 4.4). The bottom 40 percent are more likely to report symptoms of malaria. Next are symptoms of respiratory tract infections, headache, fever, and abdominal pain, which account for 44 percent of the episodes. The country still has one of the highest fertility rates in the world and lower life expectancy at birth compared to LICs (figures 4.5 and 4.6). The burden of NCDs is so large and growing that it accounted for over 27 percent of all deaths by 2010. Uganda has one of the highest alcohol consumption per capita (16.8 pure liters of alcohol per capita) in the world, contributing to an increased incidence of NCDs. Women (particularly those from poorer households) are likely to bear a larger share of the NCD burden, as they are at increased risk of obesity, chronic obstructive pulmonary disease (due to increased exposure to indoor pollution) and intimate partner violence. Nearly half of the Ugandan women have experienced intimate partner violence and those whose partners drink frequently have a sixfold higher risk than those whose partners abstain from alcohol. Alcohol use, household air pollution from solid fuels, and being underweight during childhood contribute to the heavy disease burden in Uganda.

Figure 4.3. Morbidity Rate



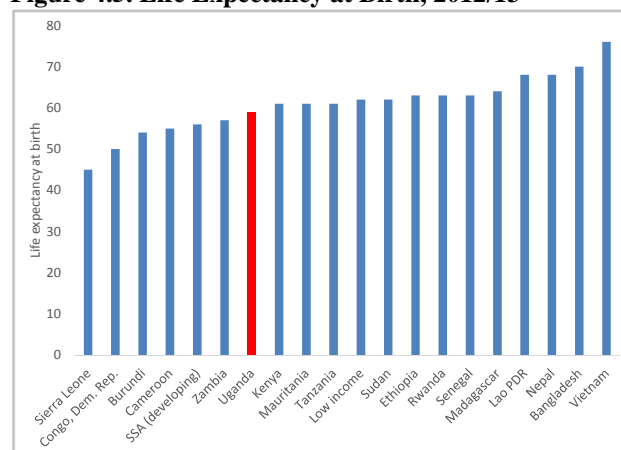
Source: Uganda Poverty Assessment using 2012/13 UNHS.

Figure 4.4. Main Diseases



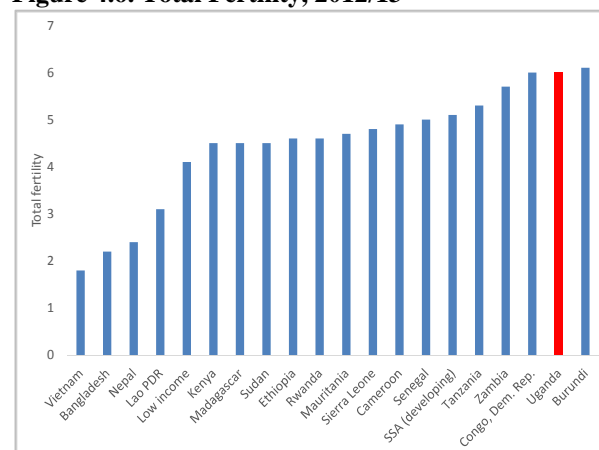
Source: Uganda Poverty Assessment using 2012/13 UNHS.

Figure 4.5. Life Expectancy at Birth, 2012/13



Source: WDI and World Health Organization (WHO).

Figure 4.6. Total Fertility, 2012/13



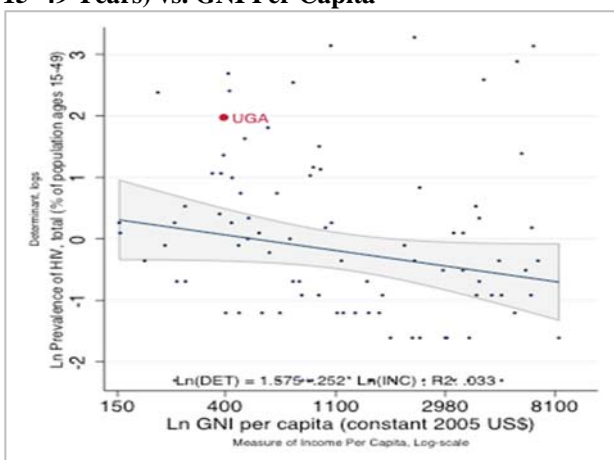
Source: WDI and WHO.

4.7. HIV/AIDS and malaria remain the leading causes of mortality, even though Uganda has made some progress on disease management. Although deaths from HIV/AIDS have declined by 53.5 percent since the peak of the epidemic in 2005, mortality remains high. In 2010, deaths from HIV/AIDS represented 17.2 percent of all deaths in Uganda and 3.5 percent of all global deaths from the disease. In Africa, Uganda ranks third in the number of deaths attributable to malaria and has some of the highest recorded malaria transmission rates. In other diseases, Uganda has been able to achieve progress similar to its peers and for tuberculosis Uganda's performance has been better than other countries with a similar GNI per capita (figure 4.7 and 4.8). The improvement has been driven mainly by improved case detection and treatment.

4.8. There are also large disparities in health outcomes based on a household's income level and geographical location. Typically, the health outcomes of those living in the western and central part of the country, those living in urban areas, and those belonging to wealthier households are much better than the others. The infant and under-five mortality rates in rural areas in 2011 were 66 and 111 deaths per 1,000 live births compared to 54 and 77 deaths per 1,000 live births, respectively, in urban areas. Similarly, in 2011, infant mortality rates ranged from a low of 47 deaths per 1,000 live births in Kampala to 87 and 88 deaths per 1,000 live births in Karamoja

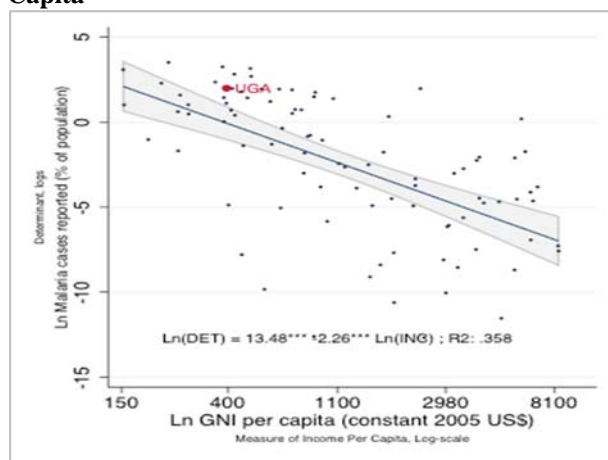
and West Nile, respectively. Childhood mortality rates were also highest among children in the lowest or second lowest wealth quintile and lowest among those in the wealthiest quintile. For example, in 2011 under-five mortality ranged from 72 deaths per 1,000 live births among the richest children to 125 deaths per 1,000 live births among children in the second lowest quintile (UBOS 2011).

Figure 4.7. HIV Prevalence (% of Populations Aged 15–49 Years) vs. GNI Per Capita



Source: Gable et al. 2014.

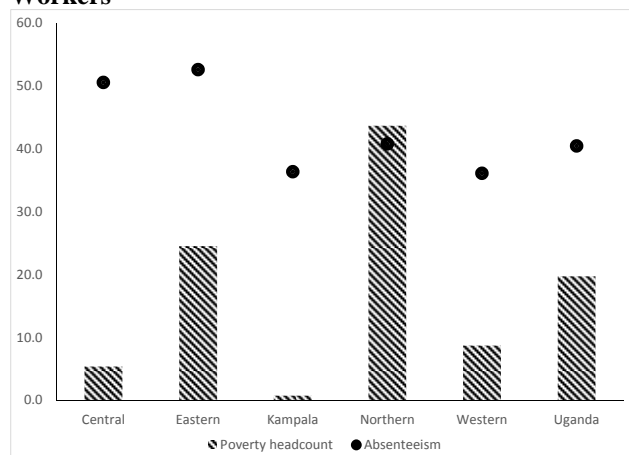
Figure 4.8. Malaria Cases Reported vs. GNI Per Capita



Source: Gable et al. 2014.

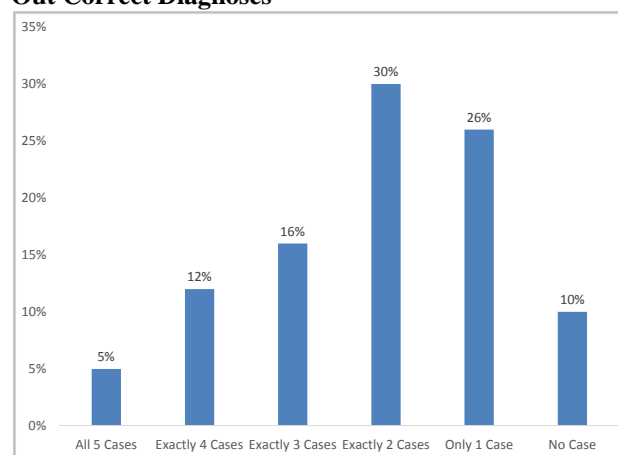
4.9. Although access to health services has improved for the country as a whole, there is inequity in access and concerns on quality of care provided, particularly to the poor. The bottom 40 percent still have limited access beyond basic health care. For them, the main reasons for not seeking care are costs, physical access to a health center, and availability of drugs. Among the poorest 20 percent of the population, almost 32 percent did not seek health care because of financial reasons while 14 percent did not seek care because the health facility was too far (Wodon and Tsimpo 2015). Although there are several private health service providers, most of the poor depend on public facilities. The LGs are responsible for these public health centers but they are severely underfunded and often understaffed. These limitations, along with other governance challenges, particularly those stemming from decentralization have resulted in the poor quality of service provided, disproportionately affecting the poor who depend more on public care. The lack of incentives, mismanagement, a difficult working environment (particularly in the north and the east), and inadequate inputs (drugs and infrastructure) have resulted in low-skilled health care professionals and high rates of absenteeism (figures 4.9 and 4.10). Results from the World Bank's Service Delivery Indicators (SDI) survey show that close to half the health workers (49 percent) in public facilities could not accurately diagnose and follow clinical guidelines in five tracer conditions and less than half (47.9 percent) the public health facilities had adequate infrastructure.

Figure 4.9. Poverty Rate and Absenteeism of Health Workers



Source: Uganda Poverty Assessment using 2013 SDI

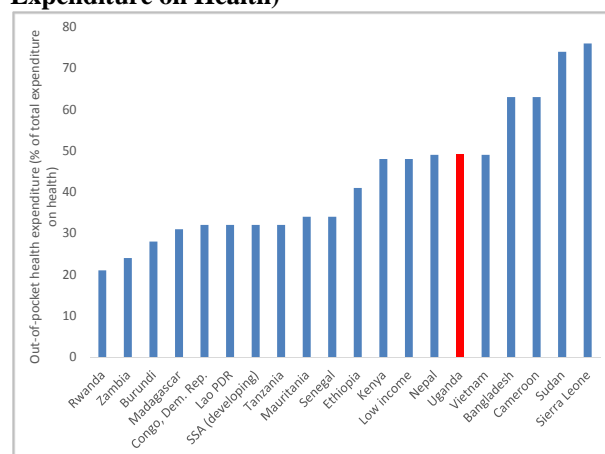
Figure 4.10. Share of Health Providers Who Carry Out Correct Diagnoses



Source: Uganda Poverty Assessment using 2013 SDI.

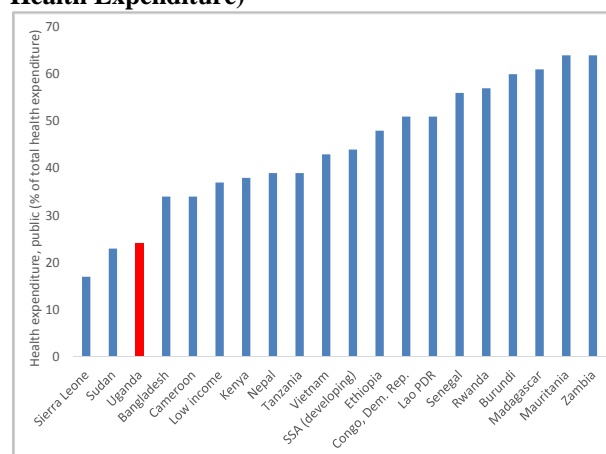
4.10. Uganda's population is not financially protected against illness. Although publicly provided health services are meant to be free, OOP spending on health by Ugandans is high and potentially impoverishing because overall public expenditure on health is low. Total health expenditure per capita in Uganda is comparable with other countries in the region as well as with those with similar levels of GDP per capita. However, public sector spending on health is low—in 2013, health accounted for only 24 percent of total public spending, compared to the average spent in the LICs of 37 percent and the SSA countries of 44 percent. As a result, OOP payments are generally higher in Uganda than those in other countries (figures 4.11 and 4.12). According to the WHO, a country is considered to offer financial protection against the cost of illness if OOP expenditure does not exceed 15–20 percent of the total health expenditure. However, in Uganda, it stands at almost 50 percent and can be impoverishing. The share of private health insurance is negligible in Uganda and although Uganda has over 15 community-based health insurance schemes, households pay premiums which are too low to make them sustainable and viable (Fenenger and de Jager, 2007).

Figure 4.11. OOP Health Expenditure (% of Total Expenditure on Health)



Source: WDI and WHO.

Figure 4.12. Public Health Expenditure (% of Total Health Expenditure)



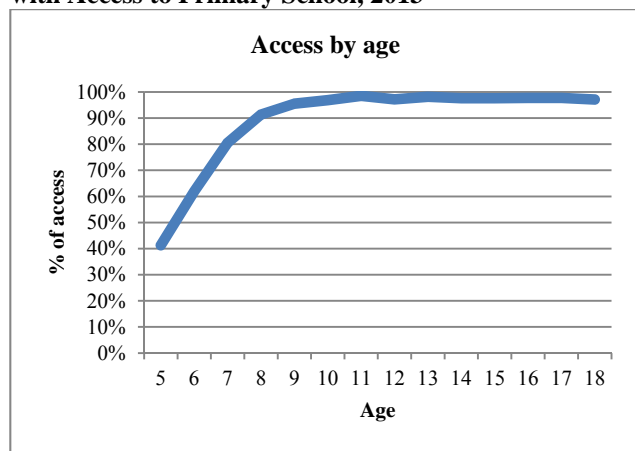
Source: WDI and WHO.

B. EDUCATION AND SKILLS

The Ugandan population, 25 years and above, has an average of 4.7 years of schooling while women have only 3.8 years of schooling.³³ In addition, there are big concerns on the relevance and efficiency of the education system which has resulted in a low-skilled workforce.

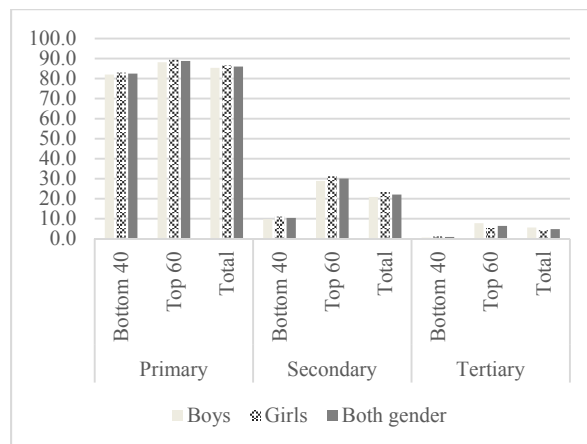
4.11. Primary school enrollment increased for both boys and girls, but secondary and tertiary enrollments are still low, more so for the bottom 40 percent. With the introduction of universal primary education in 1997 and universal lower secondary education in 2007, the number of students enrolled in primary and secondary education increased significantly. The primary school net enrollment ratio was 82 percent in 2013, up from 67 percent in 1995. In 2013, access to primary school was quite good (figure 4.13). However, enrollment in secondary and tertiary education remains very low, particularly for those in the bottom 40 percent (figure 4.14). The main constraints facing the poor include costs (including opportunity cost) and low perceived returns from education. Disability and shocks are also important factors preventing some children from attending school. Uganda's secondary education gross enrollment rate was 26 percent in 2010, which compares unfavorably with 40 percent in SSA and 80 percent in the East Asia and Pacific region. Promoting transition from primary to secondary, and subsequently to tertiary education will be important for poverty reduction, as returns to education more than double for secondary, compared with primary education (figures 4.15 and 4.16). Currently, there are almost no students belonging to the bottom 40 percent who are enrolled in tertiary education. In addition, while there is gender parity at the primary level, the percent of girls in total enrollment declines to 47 percent in secondary education, and 44 percent in tertiary education. Only 40 percent of those enrolled in vocational training in 2013 were women. Moreover, the still low access to early childhood education (gross enrollment rate of 12 percent according to the Systems Approach for Better Education Results (SABER, 2012)), provided mostly by the private sector, constrains access among poor and rural households.

Figure 4.13. Share of the population (5–29 years old) with Access to Primary School, 2013



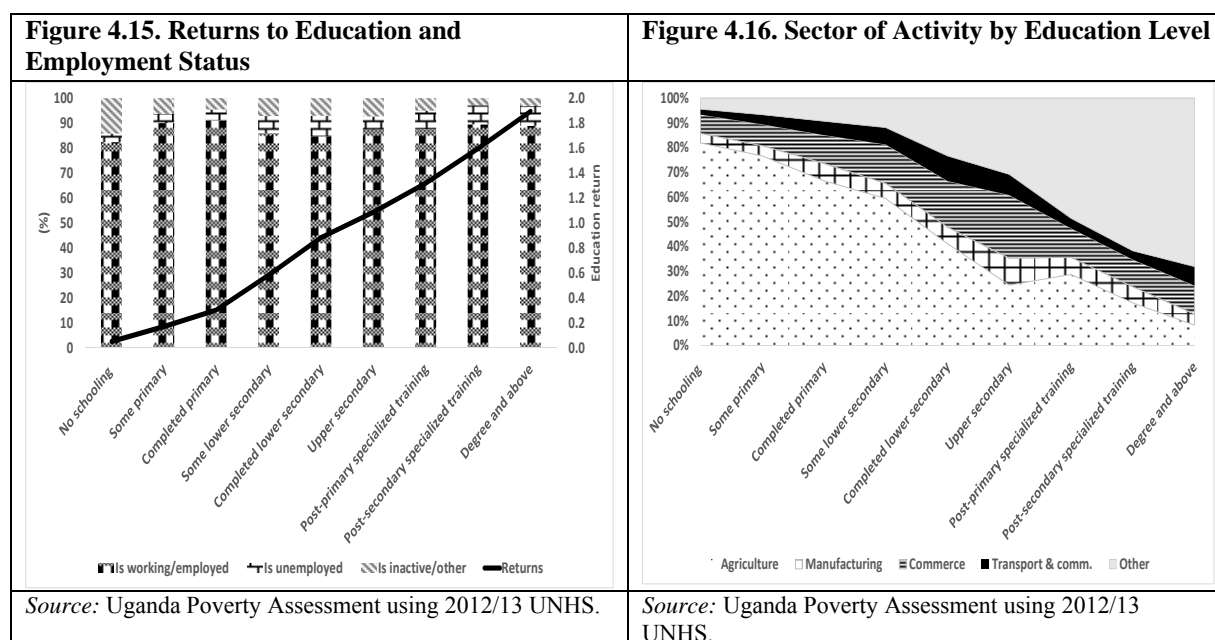
Source: Bank staff's calculations using the 2012/13 UNHS.

Figure 4.14. Net Enrollment by Level (Percent)



Source: Uganda Poverty Assessment using 2012/13 UNHS.

³³ Uganda Labor Market Profile 2014, Council for International Development Corporation (CIDC).



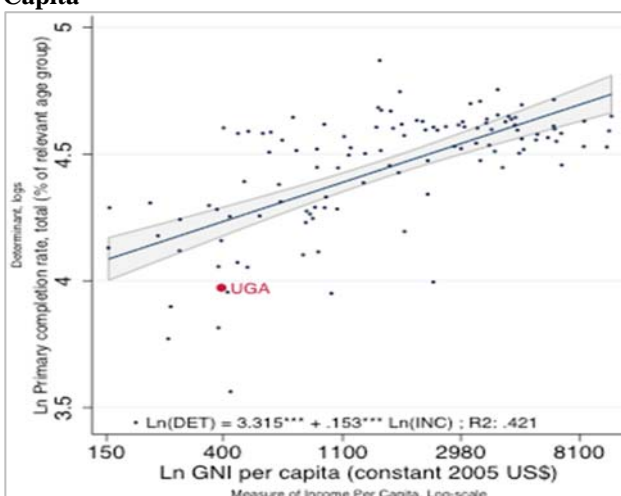
4.12. **A high primary dropout rate and still low secondary enrollment have resulted in large-scale functional illiteracy.** When compared with other countries with a similar GNI per capita, the primary completion rate and progression to secondary education rate are much lower in Uganda (figure 4.17 and 4.18). According to the Ministry of Education and Sports (MoES), the primary completion rate in 2012/13 was 59 percent (figure 4.19).³⁴ In addition, the repetition rate for primary education remains high at over 10 percent. The high dropout rate coupled with a still relatively low enrollment in secondary schools, result in a large number of individuals who leave school too early without having developed generic skills essential for life and work. In 2012, less than half of the grade 6 students tested by the National Assessment of Progress in Education were proficient in literacy (40.8 percent) and numeracy (45.2 percent).³⁵

4.13. **Education outcomes have been worsening.** There was a significant decline in the proportion of Secondary 2 (second year of secondary school) students displaying proficiency in biology, mathematics, and English language in 2012. In 2012, only 17.7 percent of sampled Secondary 2 students were proficient in biology compared with 36.7 percent in 2008. For mathematics, the 2012 figure was 43.3 percent compared with 69.4 percent in 2008 while in English language it was 48.3 percent compared with 81.9 percent five years earlier. In Business, Technical, and Vocational Education and Training (BTJET) as well as tertiary education, the employability of graduates is low, largely as a result of the mismatch between the skills imparted through educational institutes and the skills demanded by the economy.

³⁴ The MoES defines the primary completion rate as the total number of pupils who register for the Primary Leaving Examinations each year, regardless of age, expressed as a percentage of the projected population at the official primary graduation age of 12 years.

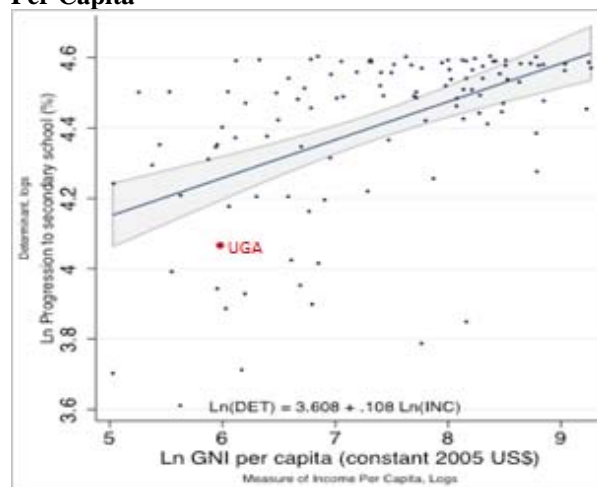
³⁵ Education Sector Strategic Plan Implementation Progress Review 2013.

Figure 4.17. Primary Completion Rate vs. GNI Per Capita



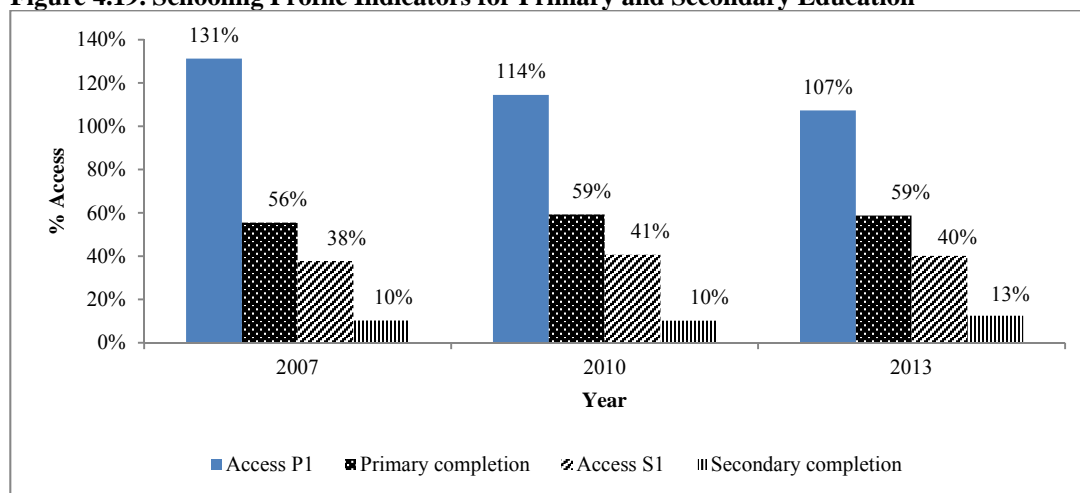
Source: Gable et al. 2014.

Figure 4.18. Progression to Secondary School vs. GNI Per Capita



Source: Gable et al. 2014.

Figure 4.19. Schooling Profile Indicators for Primary and Secondary Education

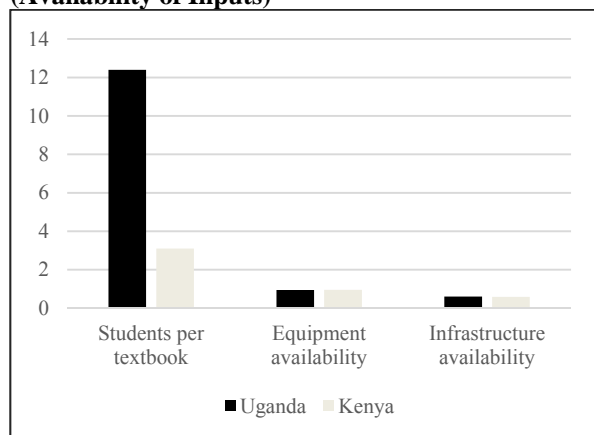


Source: Bank staff calculations using data on enrollment from MoES 2013/14 statistical yearbook and population data from the 2014 census.

4.14. Poor educational outcomes are related to poverty, inadequate availability of teaching material, poor teacher quality, and lack of accountability. There is a lack of inputs such as scholastic materials which is coupled with a high teacher-to-pupil ratio and crowding of classrooms (figure 4.20). The SDI study of 2013 found that less than 1 in 5 (19 percent) public school teachers showed mastery of the curriculum they taught. In addition, there was both student and teacher absenteeism. About 27 percent of teachers in public schools were not at work. Of those who were in school, about 30 percent were not teaching. The result is 40 percent of public school classrooms with no teacher teaching and the incidence of teacher absenteeism was much higher in the poorer regions of the north and the east (figure 4.21). Absenteeism, together with time use within classrooms, suggests that out of the official teaching day of 7 hours 20 minutes, the average Primary 4 (fourth year of primary school) student experiences only 3 hours 17 minutes of teaching and learning time with the teacher. The lack of inputs and teacher absenteeism is more pronounced in public schools and free private schools, where most of the poor go. There are no performance-

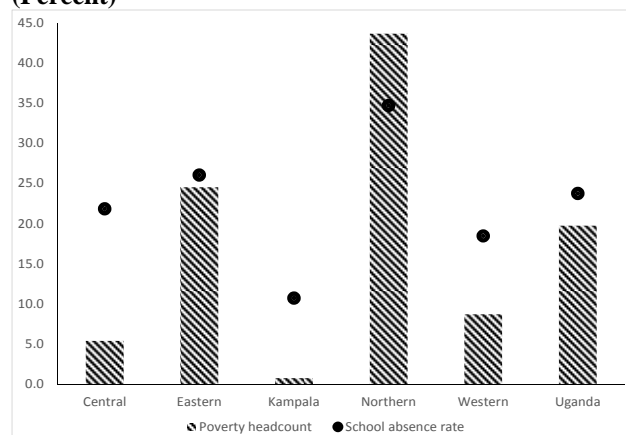
based financing systems at any level of the education system and little incentive for the system to perform better. Taking the BTVET subsector as an example, neither institutional managers nor instructors are held accountable for training results. Poor pass rates do not result in sanctions; good pass rates do not result in recognition and rewards. In fact, pass rates are not even published by programs and institutions. Private educational institutions enroll nearly 30 percent of all students (figure 4.23). At the primary level, private schools perform significantly better than the public ones but there is no significant difference in proficiency rates between government and privately-owned secondary and tertiary schools.

Figure 4.20. Inputs Providers Have to Work With (Availability of Inputs)



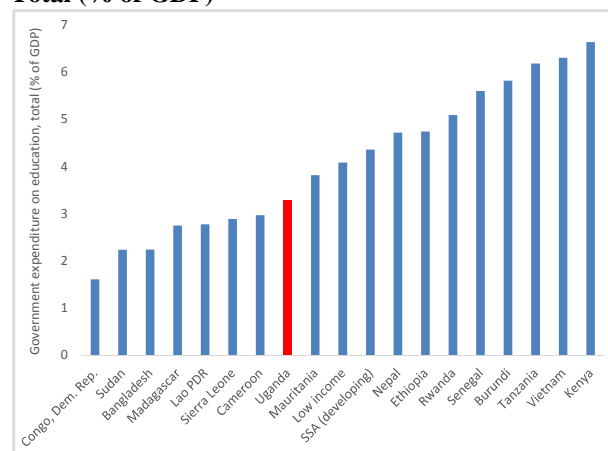
Source: World Bank (2013j) SDI 2013.

Figure 4.21. Poverty Rate and Teachers' Absenteeism (Percent)



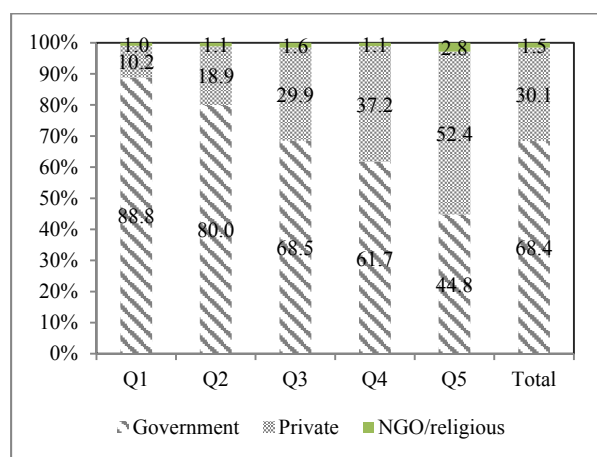
Source: Uganda Poverty Assessment using 2013 SDI.

Figure 4.22. Government Expenditure on Education, Total (% of GDP)



Source: WDI.

Figure 4.23. Market Share for Education (Percent)



Source: Uganda Poverty Assessment using 2012/13 UNHS.

4.15. The government is also focusing its efforts on vocational education to enhance skills. Given the inadequacies of the education system in Uganda, graduate students are finding it difficult to leverage their assets into productive, income-earning employment. Therefore, the government recently approved a BTVET Strategic Plan which envisages a substantial growth in student enrollment in BTVET over the next decade. This will help provide opportunities to people outside of the formal education system. However, only 1.5 percent of the 15–24 year olds in Uganda were

enrolled in vocational training in 2009 which is lower than the SSA average of 2.1 percent. Nearly 35 percent of firms offered formal training programs for their full-time employees but very few employees have full-time status.

4.16. The amount of financing allocated to education as a share of GDP (figure 4.22) and as a share of the government's overall budget has been declining. The share of education in total government expenditures declined from 17 percent in FY2007 to 15 percent in FY2013. Over the same period, the share of education as a percent of GDP fell from 3.4 percent to 2.9 percent. This compares unfavorably with peers like Tanzania, Burundi, Kenya, and Vietnam. Combined with the lack of education resources, demographic pressure is a major challenge to the achievement of education objectives. The school-aged population (6 to 18 years) is growing at a very high rate. In 2010, it stood at 10.9 million and by 2025, it is expected to reach 20.6 million. This means the education system will have to double its current intake capacity to achieve universal primary education enrollment and universal secondary education and post-primary education and training objectives by 2025.

C. INFRASTRUCTURE SERVICES

Water and sanitation: Nearly 72 percent of the Ugandan population has access to improved drinking water but only 35 percent have access to safe sanitation facilities and there is inequity in access.

4.17. About 35 percent of the Ugandan population does not have access to safe water which includes over 10 million people in rural areas and 1.7 million people in urban areas. The principal inequality lies in service delivery to rural versus urban households primarily because of infrastructure related costs of providing water in remote and rural areas.

4.18. Although the primary challenge in Uganda is the lack of access to available water, there is already localized scarcity of water resources that is predicted to increase in the future. The country withdraws only 1 percent of its annual renewable

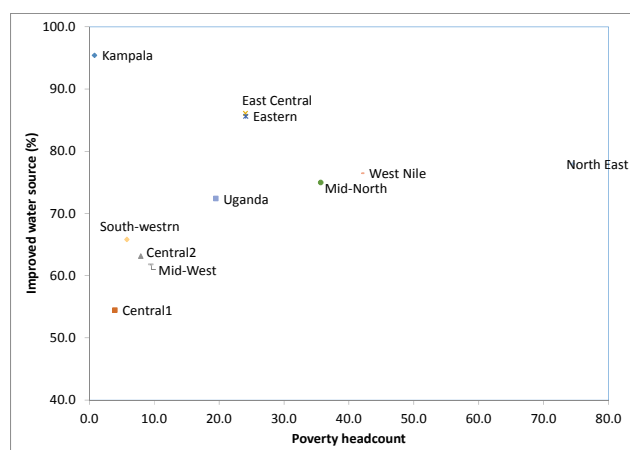
Table 4.1. Drinking Water Source in Different Regions in Uganda (Percent)

Drinking Water Source	Central	Eastern	Northern	Western	National
Piped Scheme	28	14	5	26	19
95% Confidence Interval	24–33	9–20	3–7	21–33	17–22
Borehole	19	54	57	16	35
95% Confidence Interval	15–24	46–62	51–62	12–21	32–38
Other Improved Sources	18	18	14	22	18
95% Confidence Interval	14–22	14–23	11–18	18–27	16–20
Unimproved Sources	33	14	24	35	27
95% Confidence Interval	29–33	9–19	20–29	30–41	24–29

Source: Review of Uganda's 2006 pro-poor strategy for water and sanitation, 2015.

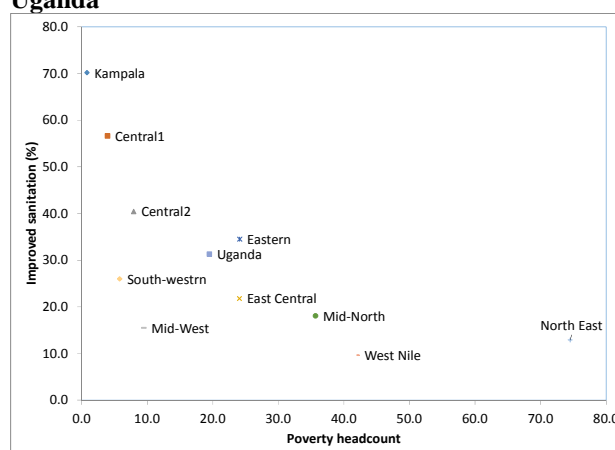
water resource. Uganda has an abundance of fresh water resources and can be considered water rich at the national level. However, the distribution of water resources is uneven with over half of all the districts being water stressed. Estimates show that within the next 20 years, water stress will spread to the majority of districts due to population growth, economic development, and increasing demands. Interestingly, the poorer northern and eastern regions have better access to improved drinking water sources compared to the better off central and western region (table 4.1 and figure 4.24).

Figure 4.24. Coverage of Safe Water in Uganda



Source: Uganda Poverty Assessment using 2012/13 UNHS.

Figure 4.25. Coverage of Improved Sanitation in Uganda



Source: Uganda Poverty Assessment using 2012/13 UNHS.

4.19. Only 1 in 3 Ugandans has access to improved sanitation which offers health benefits and there is inequity in access. Although 75 percent of the rural population and 84 percent of the urban population has access to improved sanitation facilities, this number includes shared toilets and does not reflect the quality of the sanitation facilities. Adjusting for these limitations results in sanitation coverage of 35 percent for the population. In large urban areas, sewerage coverage is only 3–6 percent while in small urban areas, it is virtually nonexistent (figure 4.25). Most urban areas rely on on-site sanitation and have limited fecal sludge management systems, with obvious implications for water quality and health problems. The poor, in general, have lower access to sanitation facilities compared with the rich and there are regional variations as well. For those living in Karamoja, the poorest region, the coverage of improved sanitation is only 12.9 percent. Moreover, according to government estimates, Uganda loses about US\$177 million per year (that is, US\$5.5 per capita per year or 1.1 percent of GDP) due to poor sanitation. The social costs extend beyond these factors and are felt not only at the individual level but also at the community level. Women and children are disproportionately affected.

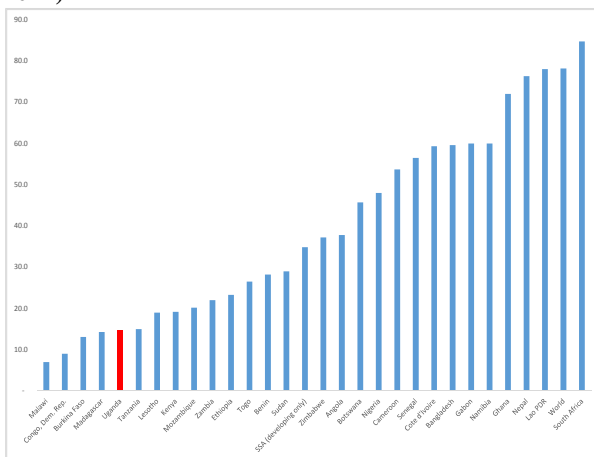
4.20. Uganda has met its MDG target for improved water access but not for sanitation. The MDG national targets for improved water and sanitation access in Uganda are 72 percent and 70 percent, respectively. The latest Joint Monitoring Program estimates for Uganda for 2012 indicate that Uganda has already met the MDG for improved water access but is far behind the sanitation access target. Moreover, although Uganda has met its MDG target for improved access to water, the level of service is still very low with only 19 percent of the population having access to piped water.

Electricity: Access to electricity in Uganda is one of the lowest in the world.

4.21. Access to electricity in Uganda, estimated at 14 percent nationally and 7 percent in rural areas, is very low. Within this low overall access, there is a large regional variation in electricity access and usage (figure 4.26). About 72 percent of the total grid-based electricity is consumed by only 12 percent of the domestic population within the major load centers of Kampala, Jinja, and Entebbe. As a consequence, Uganda has a very low per capita electricity consumption, which, at 80 kWh per year, is far below its peers—Kenya at 155 kWh per year and Ghana at 300

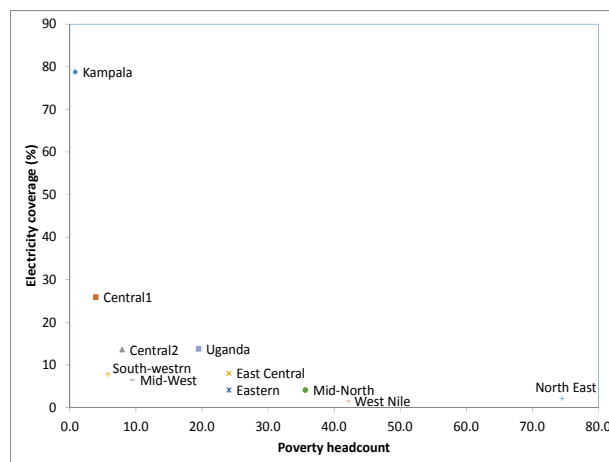
kWh per year; and not comparable to industrialized economies such as South Africa at 4,694 kWh per year or South Korea at 8,502 kWh per year. A majority of households mention affordability as a key constraint for access to electricity (box 4.1). Coverage rates are much higher among households in the top 60 percent of the distribution than among those in the bottom 40 percent. In fact, connections are virtually nonexistent for the bottom 40 percent of the population (figure 4.27).

Figure 4.26. Access to Electricity (% of Population, 2011)



Source: WDI.

Figure 4.27. Poverty and Access to Electricity



Source: Uganda Poverty Assessment using 2012/13 UNHS.

Box 4.1. Reasons for Low Connection Rates: Case of Zombo

“To get connected, one needs to acquire one or more electric poles depending on the distance from the grid line. One pole costs about UGX 800,000 and this is a deterrent for households who are otherwise interested in getting electricity connections. In addition, the installation and maintenance costs of electricity are very high. Having a grass thatched house also hinders one from having electricity.” (A focus group participant)

Source: MoFPED “Energy for Rural Transformation (ERT): Impact Assessment”, 2011.

Transport: Uganda’s district and rural roads are in poor condition leading to poor connectivity to markets and other services, especially for the poor. In addition, air and rail transport is underdeveloped.

4.22. Uganda’s national road network is in fairly good condition with high density and heavy traffic. The national road network has a density of 32.2 km per km² which is four times the density of an average low-income African country (Ranganathan and Foster 2012). The paved roads carry as much traffic as Africa’s middle-income countries (Ranganathan and Foster 2012). Around 87 percent of Ugandan national roads are in good or fair condition compared to only 72 percent in a typical African LIC. However, in addition to maintenance and overloading challenges, a rising issue with national roads has been that of capacity, since many of them are single carriageway roads which accommodate the current traffic with difficulty.

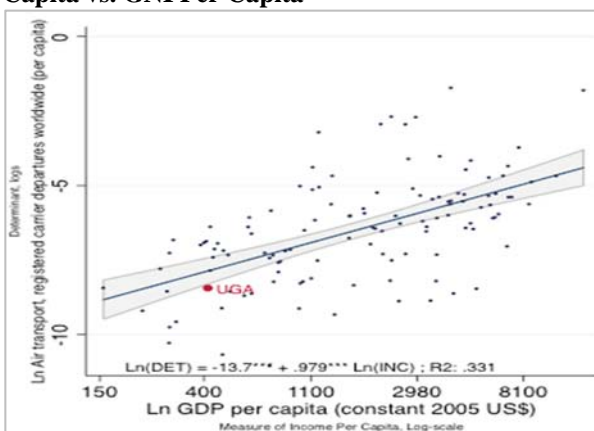
4.23. However, nearly 54 percent of the district roads and 60 percent of rural roads are in poor condition. This particularly affects the poor and those in the bottom 40 percent as most of the poor live in rural areas and they lack good connectivity to markets, health clinics, schools, and other public amenities. This restrains improvements in agricultural productivity and poverty

reduction. In addition, the share of population living within 2 km of an all-season road is not higher than in other low-income African countries (Ranganathan and Foster 2012) while the road fatality rate at 81 per 100,000, is double the African average (World Bank 2009).

4.24. Urban congestion is also concerning. The lack of an efficient and affordable public transportation system may increasingly become a barrier to inclusion, as the poor and vulnerable may be excluded from employment opportunities and social services given that their only means of transport is by foot. Given its size, Kampala presents particular challenges. With a rapidly increasing population (an estimated 4.5 percent per annum) and an even faster increase of motorization, the Kampala Metropolitan Area is rapidly moving towards total gridlock.

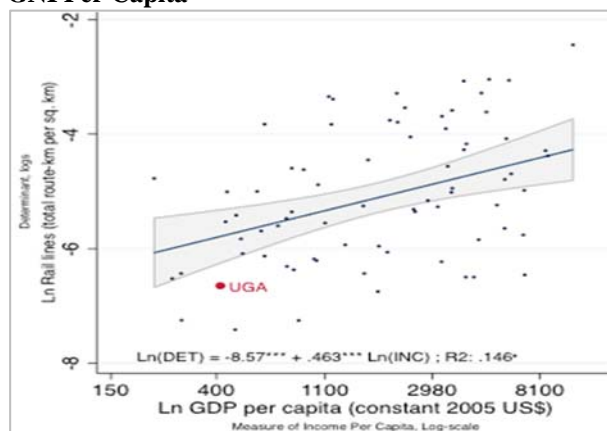
4.25. Uganda still has very low usage of air and rail transport infrastructure compared to its peers. Airline departures per capita and rail lines (length per square kilometer) are much lower than other countries with comparable GNI per capita (figures 4.28 and 4.29). Moreover, inland waterways transport remains underdeveloped.

Figure 4.28. Air Transport Carrier Departures Per Capita vs. GNI Per Capita



Source: Gable et al. 2014.

Figure 4.29. Length of Rail Lines Per Square Km vs. GNI Per Capita

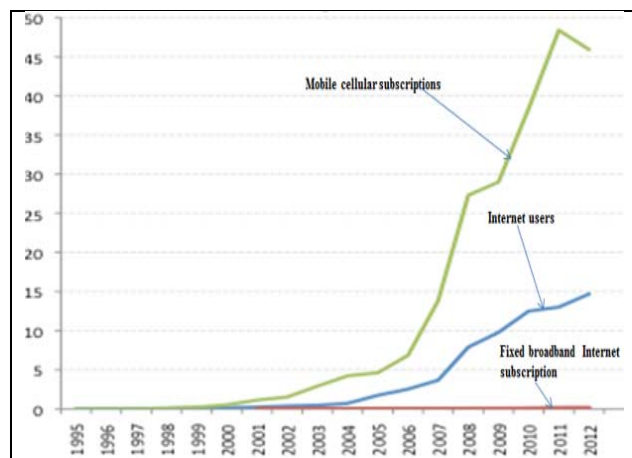


Source: Gable et al. 2014.

ICT: Access to mobile telephony has increased substantially but use of the Internet is still limited.

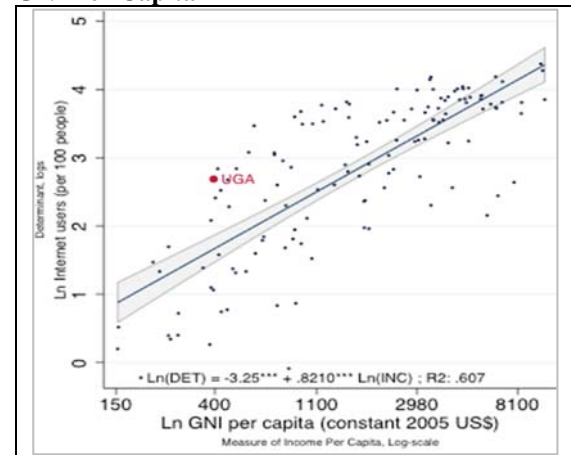
4.26. Mobile telephony increased from less than 1 percent in 2000 to 53 percent in June 2014 in response to major policy reforms in the ICT sector. The government established an independent regulatory body, the Uganda Communications Commission, fully liberalized the telecommunications market, and implemented a technology-neutral converged licensing framework. The government has also completed the implementation of Phases I and II of the NBI. As a result, nearly 14 million Ugandans used mobile money platforms in 2013 with the value of transactions up 40 percent year-on-year (figure 4.30). Government agencies, development partners, and the private sector in Uganda are already experimenting with a wide variety of mobile-based technologies to improve public service delivery. For example, the United Nations Children's Fund's ICT4D (ICT for development) tools include mTrac (a nationwide mobile disease surveillance and malaria tracking tool), EduTrack (a platform for tracking school performance data) and a few others. The Grameen Foundation is leveraging mobile technology to provide targeted agricultural extension services to farmers.

Figure 4.30. ICT Users per 100 People



Source: Gable et al. 2014.

Figure 4.31. Internet Use (per 100 People) vs. GNI Per Capita



Source: Gable et al. 2014.

4.27. However, there is low broadband adoption and limited access to mobile broadband services in rural areas. The number of Internet users has increased but broadband is currently available only in some (mostly urban) areas of Uganda and the current level of broadband prices is not low enough to be truly inclusive (figure 4.31). Hence, there is a risk that the bottom 40 percent of population in Uganda will remain excluded from the information revolution that is shaping the modern world. Increasing access and lowering costs will require increased investment in the backbone infrastructure.

Land: Land disputes, lack of planning for land use, and lack of appropriate property valuation are the key constraints affecting the functioning of land markets in Uganda.

4.28. Rights to land remain mainly insecure and land markets are underdeveloped. While land registration in Uganda is advanced relative to SSA, it remains significantly below Western Europe standards. Rehabilitation and modernization of land administration is at an advanced level for cadastral surveying and registration but is still in the early stages for topographic surveying and mapping, land use planning, and property valuation. While as much as 20 percent of Uganda's land is registered, compared to only about 10 percent in Africa as a whole but much lower than the 95 percent in Western Europe, Uganda has relatively high land tenure insecurity characterized by unclear property rights and land disputes. The reengineering, computerization, and decentralization of cadastral and registration services has reduced the time needed to register property from 227 days in 2007 to 43 days in 2014. However, persistent land disputes and prevalence of micro farms have constrained the incomes of the poor and those in the bottom 40 percent and limited the prospects for commercialization of agriculture. Land dispute resolution services are understaffed and underfunded. Underdeveloped property valuation and high land-compensation costs have resulted in difficulties in acquiring land for public use. In addition, customary practices in Uganda prevent women from owning or inheriting land. Rectifying this situation will require changes to the legislative framework, sensitization and public awareness campaigns, and implementation.

4.29. Inefficient functioning of land markets have, in part, resulted in disorderly urbanization and proliferation of informal settlements and slums. More efficient operation of

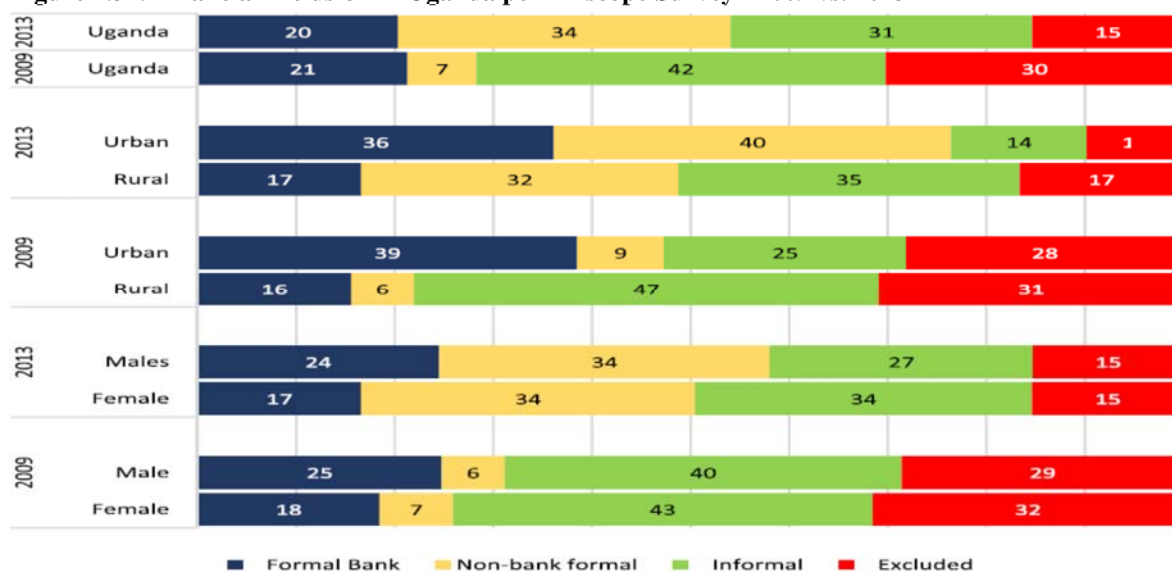
land markets will help efficient urbanization and will permit households to rent their land so as to become mobile between rural and urban areas. In addition, government handling of urban land has lacked transparency and undermined land markets.

D. ACCESS TO FINANCE

Although financial inclusion of Ugandan households stood at 85 percent in 2013, formal bank inclusion was only 20 percent. In addition, 65 percent of the population lacked access to credit, limiting their ability to smooth consumption in the face of shocks.

4.30. **In 2013, 85 percent of the adult population aged 16 years and above were financially included, an improvement from 70 percent in 2009.** Formal inclusion was 54 percent in 2013, compared to 28 percent in 2009.³⁶ This improvement in financial inclusion was largely driven by mobile money financial services. The increase occurred from half a million subscribers in 2009 to 14.2 million in December 2013, representing over 80 percent of the adult population with access to money financial services. Overall, 76 percent of Ugandans in urban areas use financial services at bank and non-bank formal institutions, while this number is only 49 percent for residents of rural areas (figure 4.32). There are however no differences in financial inclusion based on gender.

Figure 4.32. Financial Inclusion in Uganda per Finscope Survey - 2009 vs. 2013



Source: Financial Sector Review (World Bank 2015e).

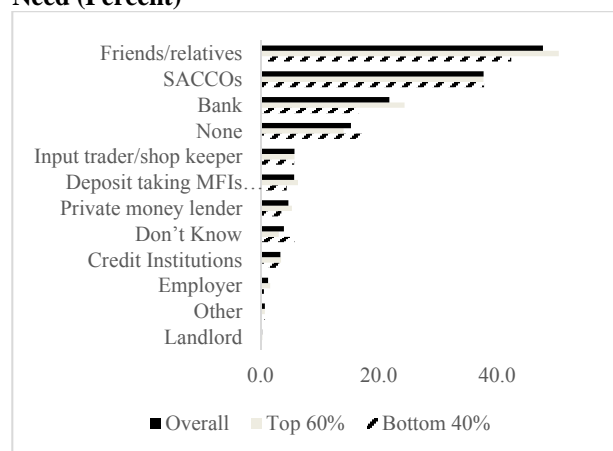
4.31. **However, formal bank inclusion did not increase over the years and there are large disparities in this area among the rich and the poor.** Formal bank inclusion was 20 percent in 2013 compared to 21 percent in 2009. Given the high costs of expansion to rural areas for formal bank institutions in Uganda, formal bank inclusion was 36 percent for urban areas compared to

³⁶ There are four major categories of financial service usage: (a) formal financial institutions regulated by the Bank of Uganda (BoU) - Tier I-III; (b) non-bank formal financial institutions (for example, savings and credit cooperatives [SACCOs], non-regulated microfinance institutions, insurance, mobile money services); (c) informal institutions (for example, money lenders, savings clubs); and (d) the financially excluded, that is, persons who do not use either the formal banks or non-bank formal or informal institutions.

only 17 percent for rural areas. Less than 14 percent of the adult population in the bottom 40 percent has access to a formal financial institution (compared to an average of 37 percent in the top 60). The gap by education level is even wider, with about 40 percent of those with secondary or higher education banked versus just 20 percent for those with primary education or lower. Gender differences exist and are quite important as well, with a 10 percentage point difference (figure 4.33).

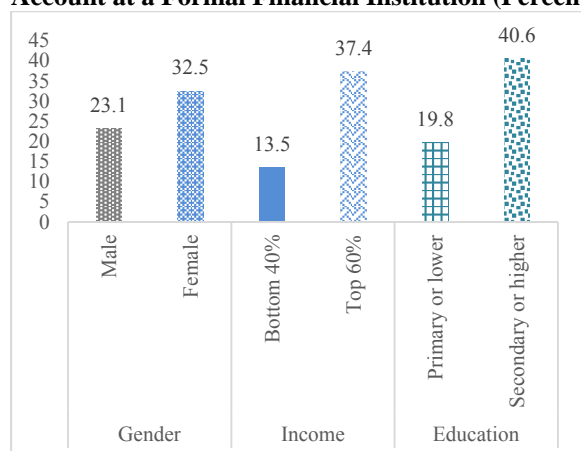
4.32. In terms of borrowing, the majority of adults in Uganda are unserved and the percentage of adults who used credit declined from 2009. A slightly higher percentage of adults used formal sources of borrowing (5 percent in 2009 compared to 12 percent in 2013), while the share of adults who used informal methods declined and the majority of them became unserved. Lack of access to the formal financial market makes it difficult for households to cope with short-term shocks such as illness, loss of employment, drought/irregular rains, and landslides (figure 4.34). It may also be a significant barrier to their ability to invest in building human and other physical assets or to start and operate a small business. Estimations from the UNHS 2012/13 suggest that the majority of the population rely on friends/relatives and SACCOs when they need financial assistance. The predominance of SACCOs is more pronounced in the northern and western regions whereas in the central region, it is more common for people to seek a loan from friends/relatives. As mentioned before, the lack of access to formal sources of borrowing is also explained by the land tenure system which is dominated by *mailo* land tenure that is unsuitable as collateral by banks.

Figure 4.33. Available Source of Credit in Case of Need (Percent)



Source: Uganda Poverty Assessment using 2012/13 UNHS.

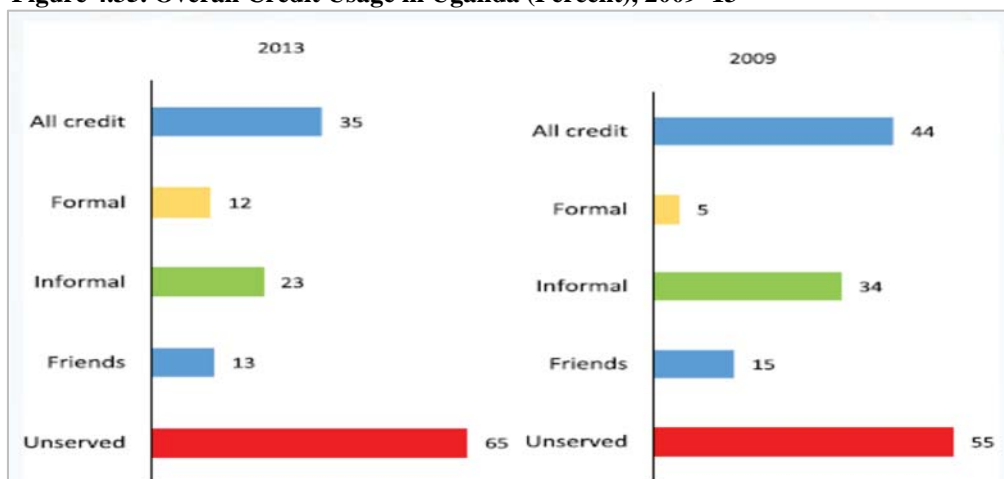
Figure 4.34. Share of Adult Population with an Account at a Formal Financial Institution (Percent)



Source: World Bank, Global Findex Database of Financial Inclusion.

4.33. The fear of debt is the single largest reason why people do not borrow. The Finscope survey shows that the high cost of loans is the second biggest factor for not taking loans. On the other hand, a lot of the people do not qualify for loans because of the high collateral requirements (87 percent), mostly immovable, such as titled land, and most of the land in Uganda is not titled (80 percent). Financial illiteracy also plays a role—when in dire need, people end up borrowing from loan sharks and do not have the capacity to shop around (figure 4.35).

Figure 4.35. Overall Credit Usage in Uganda (Percent), 2009–13



Source: Financial Sector Review (World Bank 2015e).

E. SOCIAL PROTECTION SYSTEM

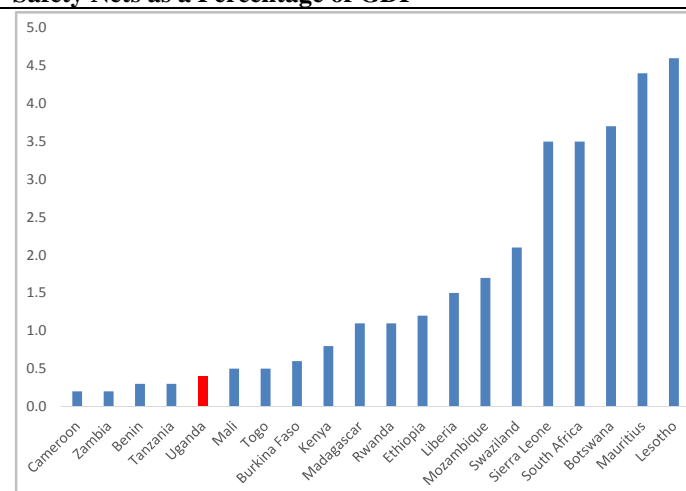
Social spending in Uganda is low, has very limited coverage, and is largely financed by donors. This has limited investments in human capital, has impacted income and consumption, and led to intergenerational transmission of poverty.

4.34. Total social spending in Uganda was 1.2 percent of GDP in 2013 which is relatively low.

Nearly two-thirds of the Ugandan population is either poor or vulnerable but social spending has remained low and has not only inhibited the accumulation of assets but also impacted income and consumption in the event of adverse shocks. Spending on social security amounted to 92 percent of all social protection spending (pensions 57 percent and direct income support 35 percent) in 2013 while the remaining 8 percent was on social care and support services. Estimates suggest that countries in Africa spend around 2.8

percent of GDP on social security.³⁷ Uganda's total spending on direct income support amounted to US\$88 million in 2013 or 0.40 percent of GDP (figure 4.36) compared with the 1.1 percent spent in other LICs in Africa and 1–2 percent of GDP, globally. Only 4.5 percent of the total population received any kind of direct income support.

Figure 4.36. Government and Donor Spending on Social Safety Nets as a Percentage of GDP



Source: Monchuk 2014.

³⁷ World Bank. Social Protection Strategy for Africa.

4.35. **Donors constituted the largest source of financing for social protection in 2013.** Nearly 42 percent of funding for social protection in Uganda comes from donor agencies, 35 percent from the government, and 23 percent from individuals. Notably, donor funding is allocated to direct income support and social care services, while government funding is almost entirely allocated to the private service providers (with a small allocation to social care and support services). Individual contributions are made to the National Social Security Fund.

4.36. **Uganda's heavy reliance on donors to finance direct income support and social care and support services is resulting in a stop-start approach to programming and contributing to the high cost of implementation.** Most programs are less than five years old, have recently incurred or are in the process of incurring start-up costs, and, because they are new, have limited institutional knowledge. Furthermore, most programs are either implemented directly by external agencies or with substantial contract assistance. Not only do these agencies cost more than using preexisting government systems to implement a program but also they often invest in creating temporary institutions just for the lifetime of the programs rather than in building long-term core systems.

4.37. **Only 5 percent of the working population are part of a pension scheme.** Contributory social security coverage is currently largely limited to a small proportion of those in the formal sector. The pension sector is confined to those in government employment or those employed by organizations with more than five employees. As a result, only 29 percent of wage earners contribute to or are part of a pension scheme. In comparison, the proportion of the labor force covered by a contributory pension in other countries ranges from a high of 51.6 percent in Mauritius to a low of 1.5 percent in the Central African Republic. Insurance coverage in the health sector is even smaller with less than 1 percent of the population covered by health insurance or prepayment schemes. These schemes are largely private except for the community-based health insurance schemes that exist in 17 districts in the central and southwestern regions.

F. OPPORTUNITIES FOR INCLUSION

The single largest opportunity to improve inclusion is by enhancing the performance of the agricultural sector which supports most of the poor.

4.38. **A significant increase in public social spending is needed to enhance education and health outcomes and provision of infrastructure services and social protection.** Such an increase is unlikely in the short to medium term because of fiscal constraints and competing demands for the limited fiscal revenues. Uganda's tax collections are relatively low and large increases in revenues are unlikely. Oil revenues certainly hold promise, but they are not expected over the next 10 years or so. Hence, fiscal constraints will be binding in terms of provision of public services.

4.39. **Even if the government had the resources to spend, building human capital takes time.** Typically, improved outcomes on health and education are visible after a long lag but quick improvements can be achieved in the provision of infrastructure services, if resources are available and spent wisely. Nevertheless, long-term and sustainable development requires significant investment in human capital.

4.40. While the GoU balances priorities in the social and infrastructure sectors, focused interventions are needed in agriculture. These interventions will help boost the incomes of the poor and those in the bottom 40 percent. The poor, and particularly those in the north and east of the country, derive most of their income from agriculture and an increase in farm incomes can have a far-reaching impact on their well-being. Agriculture as an opportunity was identified based on team discussions and past and ongoing analytical work, particularly, ‘Promoting Inclusive Growth in Uganda’, 2012.

Agriculture

To boost farm incomes of the poor and those in the bottom 40 percent, investments need to be concentrated in rural roads, sustainable land and water management (including irrigation), and extension services as well as land tenure security and rental markets, particularly in the north and the east.

4.41. The majority of the poor report farm income as their main source of income. Despite the modest performance of the sector (box 4.2), household survey data shows substantial growth in real per capita agricultural incomes and their contribution toward poverty reduction.³⁸ The key drivers of crop income changes were favorable weather conditions and high prices for agricultural commodities, in addition to an increase in the land area under cultivation. Improvements in access to markets and extension services also seem to have helped.

4.42. With the exception of the communally owned lands in the north, there are limitations to further increases in land under cultivation and an increase in productivity is needed to increase agricultural production and support commercialization. Uganda faces low land and labor productivity in agriculture. TFP in agriculture has steadily fallen in Uganda and is now minus 0.4 percent whereas other countries in East Africa and overall for SSA showed increases. In particular, labor productivity in Uganda declined and land productivity improved marginally (table 4.2). The yield potentials in Uganda are much higher than actuals and the poor performance is attributable to very low use of modern inputs, poor agricultural infrastructure, limited value addition, weak market linkages with very high associated costs, and low levels of human capital in the sector. Ugandan farms can double production of some important commodities and quadruple production of others merely through the adoption of yield-enhancing technologies that are already available. The share of agriculture in GDP has halved from 50 percent in 1990 to 25 percent today. However, the share of population dependent on agriculture has remained constant at 70 percent. As a result, agricultural output per worker has declined.

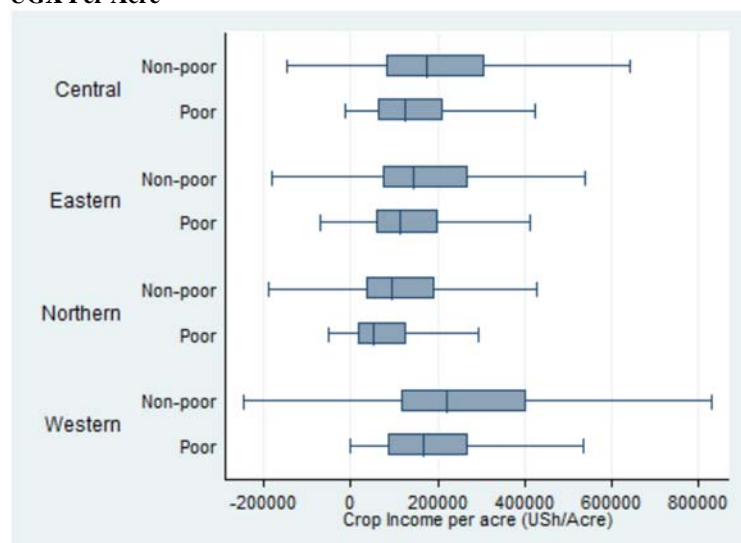
³⁸ The data from the national accounts often contradict the data from the household surveys. For example, according to the UNHS, maize and bean yields increased between 1999/00 and 2004/05, but according to the national accounts, they decreased. These conflicting data highlight the weaknesses of the official statistics in Uganda and indicate the need to improve the collection of agricultural statistics.

Box 4.2. The Agricultural Sector in Uganda

On average, the performance of the agricultural sector in Uganda has been rather modest and the sector has been characterized by low yields and weak value chains and market linkages. There are about 500,000 smallholder farmers. Nearly 90 percent of the farms average between 0.5 and 2.5 ha. Owners of these micro farms lack access to the capital necessary to buy tools, fertilizer, or machinery. Most of the farming is at the subsistence level. Recent trends and experiences in other developing countries suggest that farmers can increase their earnings through commercialization and crop and market diversification. Commercialization in Uganda will require farmers to move away from subsistence farming through improvements in productivity with the use of modern equipment, sustainable land and water management, and improved quality inputs (fertilizers and seeds) as well as better skills and access to finance. However, progress within the farm will not be sufficient as linkages with markets also need to be strengthened through better transport and storage (post-harvest loss is estimated at 40 percent) infrastructure, transparent and competitive value chains, and consistent government policies (including taxation). Public expenditure on agriculture remains low at 4–5 percent of total government expenditure. Crop and market diversification is also important as it will help farmers to hedge their risks. A shift toward high-value vegetables or fruits can also bring additional jobs and foreign exchange. Improvement in agricultural productivity will need to be combined with sustainable use of water and land to address environmental issues.

There are differences in regional agricultural production (figure 4.37). The best performing region is the west, which is

Figure 4.37. Value Added in Crops by Region and Poverty Category, UGX Per Acre



Source: Agriculture for Inclusive Growth in Uganda, World Bank, 2012.

well-equipped not only with good natural conditions but also with high population density and developed infrastructure. Farmers select the most profitable crops and achieve higher yields, having good access to infrastructure and markets for inputs and outputs. The country's central and east regions perform worse, having worse agricultural conditions, fewer people, and weaker infrastructure. The differences in performance between the poor and non-poor farm households are also not significant, with both households generating agricultural income far below those in the nonagricultural sectors. Undoubtedly, the north lags behind and requires targeted attention during the next decade to catch up with the rest of the country.

Table 4.2. Average Annual Growth of Agricultural Output and TFP and Land and Labor Productivity

Country	Land Productivity kg per ha				Labor Productivity UGX per worker				Output Growth (%)			TFP Growth (%)		
	1990	2000	2005	2012	1990	2000	2005	2012	1991- 2000	2001- 2006	2007- 2012	1991- 2000	2001- 2006	2007- 2012
SSA	82	109	135	179	600	646	735	853	3.1	4.8	4.3	1.7	2.6	2.4
Ethiopia	82	144	194	250	255	219	269	313	1.8	6.7	5.1	1.4	2.8	2.5
Tanzania	116	129	175	235	374	324	412	498	1.1	7.3	4.8	0.0	2.2	2.8
Kenya	150	168	233	321	513	418	523	643	1.1	6.4	5.2	0.2	4.7	2.1
Rwanda	590	742	830	1289	392	382	401	541	1.1	4.3	7.8	2.0	-1.2	2.6
Uganda	322	395	425	438	578	586	587	534	2.5	2.1	1.8	-0.3	0.1	-0.4

Source: International Food Policy Research Institute (IFPRI) Global Food Policy Report, 2014–15.

4.43. Input use has been limited because of poor quality and availability, cost considerations, and output price unpredictability. Maintenance of many rural roads has been inadequate, keeping the costs of inputs (such as fertilizers, seed, and chemicals) high and farm prices low. There is also a problem of poor quality of many agricultural inputs, including

counterfeits. The low availability of quality inputs and their high input prices, which require significant cash advances, is therefore too risky for many smallholders and even large farms because of volatile weather and output price unpredictability. As a result, the use of modern technologies remains modest. In addition, extension services can play a significant role in removing information asymmetries and ignorance on input use. Also, improved access to finance in agriculture can help but a majority of the farmers will not be creditworthy given the predominance of subsistence agriculture. These investment and policy measures need to be underpinned by strengthening of land tenure security, rental markets, and institutions for land administration. In the north and, to a lesser extent, in the east, local group owners of communal land need to be formalized and their land registered. This will protect the land rights of local communities while also encouraging access to communal land by non-community members through rental arrangements, including long-term leases for investors.

4.44. Further investments in access to markets and extension services are also needed. The transaction costs of moving commodities internally and across the border must be lowered and reliable linkages between Ugandan producers and prospective purchasers in the domestic, EAC, and COMESA markets established. There is also a need to provide effective extension services to supply farmers with the necessary knowledge and information on effective use of the inputs. The existing extension program, which was supported by the World Bank, gradually lost effectiveness and credibility (because of corruption and mismanagement) over the past five years. It was formally dismantled last year (from its institutional home at the semiautonomous institution of the agriculture ministry called the National Agricultural Advisory Service) with the plan to rebuild extension services from scratch within the Ministry of Agriculture, Animal Industries, and Fisheries and the district government. This process is ongoing—for now extension is still essentially absent—but a new program will be put into place (over the course of the next 1–2 years). So lack of extension is at present an important constraint.

4.45. Weather and agricultural prices are given risks and these risks can be hedged by crop diversification or formal, but costlier, insurance. Crop and market diversification are useful tools for the poor to hedge risks arising from weather- and price-related risks. The availability of weather-related insurance products are, however, limited and deter investments in agriculture. Exposure to natural hazards such as droughts and floods is a key risk for the agricultural sector in Uganda and the irrigation infrastructure is underdeveloped. Index insurance is a relatively new but innovative financial product for insurance provision that pays out benefits on the basis of a predetermined index (for example, rainfall level, seismic activity, livestock mortality rates). The benefits paid out depend on the loss of assets and investments, primarily working capital, resulting from weather and catastrophic events, without requiring the traditional services of insurance claims assessors. However, the cost of buying such insurance will largely be beyond the means of the subsistence farmers.

4.46. Investment in irrigation facilities can also help reduce weather-related risks, to an extent, and will support agricultural commercialization. Uganda, generally enjoys two rainy seasons, March–May and October–December, leaving much of January–March and June–October dry. Statistics indicate that only 1 percent of the ordinary farmers and 5 percent of the commercial farmers use irrigation facilities. Uganda is a water-rich country and investment in irrigation facilities can improve agricultural incomes significantly and will also contribute to strengthening food security.

4.47. The agro-processing industry also holds potential for the poor and vulnerable population. Uganda processes only 1 percent of its agricultural produce and meat processing is also limited. The constraints faced by the agro-processing sector are similar to those faced by the agricultural produce sector in terms of lack of access to markets, poor transport and storage infrastructure, inadequate access to finance, and pests and diseases.

4.48. Lending to the agricultural sector has exhibited an upward trend since 2009 but its share in the total credit to the private sector remains low. Total agricultural lending by regulated institutions almost tripled from UGX 291 billion in 2009 to UGX 837 billion in 2013. The majority of the lending was for short-term marketing activities through invoice and warehouse receipt financing products. However, lending to the agricultural sector accounted for only 8 percent of the total lending to the private sector in 2013. The low level of lending is primarily a reflection of the agricultural sector in Uganda which is dominated by smallholder farmers with low and irregular average incomes and few agro-processing/value addition firms. The establishment of the agricultural credit facility with the aim of promoting agricultural commercialization was instrumental in providing medium- and long-term financing on favorable terms (through banks) for farming and agro-processing. The bulk of the loans financed through this facility went toward investments in agro-processing machinery. However, lending to smallholder farmers remains limited because of the high interest cost (30 percent) and associated fees and collateral and guarantor requirements. Accelerating systematic land registration will increase the country's registration rate and expand the supply of collateral and access to collateral-based credit for many smallholder farmers.

5. PROGRESSING SUSTAINABLY ON THE TWIN GOALS IN UGANDA

5.1. **It is important to make the growth and inclusion process sustainable to avoid reversals in the gains made in poverty reduction and shared prosperity, and also to make further progress on them.** Making growth sustainable will require accumulation of wealth and effective management of resources. Addressing the large infrastructure gaps and poor social service delivery will require improvements in public sector management, particularly fiscal management, and governance. Similarly, an increase in per capita income will be aided by a reduction in the fertility rate. These challenges, which need to be addressed to progress on making the twin goals sustainable, are discussed in this chapter.

5.2. **Wealth accumulation is crucial for making growth sustainable.** This is particularly so in a natural-resource-abundant and dependent country like Uganda. This abundance and dependence is likely to increase further with the advent of oil. Sustainable management of these natural resources is required to effectively transform them into productive infrastructure and human capital. This highlights the importance of natural resource management, fiscal management, and public sector management for sustainable growth and progress on the twin goals.

5.3. **In the Ugandan context, social cohesion and effective management of fertility are also crucial elements of sustainability.** The significant differences in the standard of living of residents in different parts of the country, the influx of refugees from nearby countries, and a growing labor force with inadequate jobs, could result in social instability. Also, the high fertility rate has stretched the limited resource base of households and the government and has lowered asset accumulation of the citizens. A sustainable improvement in the standard of living of Ugandan citizens is unlikely with the existing fertility rate.

A. WEALTH ACCUMULATION IN UGANDA

Uganda has increased its wealth per capita by 30 percent during 2000–10.

5.4. **Wealth accounting measures the stock of assets a country uses to generate income.** The total wealth of a nation includes produced capital, natural capital, and intangible capital. Produced capital essentially covers the infrastructure base of a country and includes machinery, structures, equipment, and urban land. Natural capital includes agricultural land, protected areas, forests, minerals, and energy. Intangible capital measures human, social, and institutional capital. While produced capital and natural capital can be observed, intangible capital is derived as the residual of the net present value of consumption (box 5.1). Compared to the GDP which measures the flow of income accruing to a country within a year, wealth accounting measures the stock of assets a country uses to generate its income.

Box 5.1. Wealth Estimates - Methodological Note

The idea of wealth can be conceptualized in the same way as GDP. However, some components are not observable and must be deducted. Total wealth is the present value of future consumption, and the sum of all the wealth components must equal this value. A basic decomposition of wealth may look like this:

$$\text{Total Wealth} = K + V + \text{NFA} + \text{IC},$$

where K is produced capital, including machinery, equipment, structures, and urban land; V measures natural capital (energy resources, minerals, timber, forest, crop land, pasture land, and protected areas); NFA stands for net foreign assets, and IC for intangible capital. The latter can be estimated as a combination of human capital and rule of law. In practice it is calculated as the residual of the above equation when total wealth is estimated as the present value of future consumption,

$$\int_t^{\infty} C(s) * e^{-\rho(s-t)} ds$$

It is important to note that future consumption is not easy to measure. Therefore, in practice the estimate for present value of future consumption is calculated in a way to mimic a situation where the economy is on a sustainable path (that is, where savings offset capital depletion). In order to do this, researchers use 5-year averages centered on the year of interest (in order to smooth out any irregularities in consumption) and afterwards adjust the savings/consumption breakdown to reflect a sustainable consumption path. For a more detailed discussion on the methodology used to estimate wealth, please see Annex A in the World Bank publication: “The Changing Wealth of Nations.” 2011.

5.5. Uganda’s total wealth per capita grew by over 30 percent between 2000 and 2010, largely driven by an increase in produced capital and an expansion of pasture lands. Produced capital grew by an average annual rate of 6.4 percent per capita. In addition, Uganda’s natural capital grew due to a rising size and value of its crop and pasture lands which grew by an average annual rate of 4.9 percent per capita since 2000. However, this was offset by significant deforestation. Between 2000 and 2010 the overall value of Uganda's forests fell by 26 percent. Intangible capital, which includes human capital among others, remained constant. Uganda’s total wealth is low compared to other countries in SSA. In 2010, Uganda’s total wealth per capita (excluding oil) amounted to US\$7,190. In the absence of oil, Uganda’s total wealth per capita (measured as the discounted per capita consumption expenditure over the next 25 years) would have risen by only 12 percent in real terms from 2009/10 to 2014/15 compared to 26 percent in real terms over the same period if the discovery of oil is taken into account. This is below most of its peers in East Africa, and well below the largest economies in SSA. In addition, the share of intangible and produced capital in total capital is relatively low. While this reflects the reliance on agriculture, it also highlights the need to invest in physical and human capital that can deliver higher and more sustainable income levels.³⁹

5.6. The discovery of oil will provide an opportunity to raise produced and intangible capital in future years. Uganda’s GDP grew at an annual average of 7 percent since 2000, but unlike most of the other SSA countries with similar growth patterns, Uganda’s economic growth was not driven by the depletion of nonrenewable natural resources but by high rates of investments in produced capital. Rents from nonrenewable natural resources over the last decade remained almost negligible, amounting to less than 0.001 percent of GNI in 2012. The beginning of oil production at the end of this decade will change the situation. Oil prospects boosted Uganda’s total

³⁹ According to the ‘Changing Wealth of Nations’, 2010, the wealth per capita of Uganda increased by 39 percent from 1995 to 2005. Uganda’s adjusted net savings was however, negative during this period but it is not fully representative as it does not include agricultural land and some forms of intangible capital (which includes human, social and institutional capital).

wealth by 17 percent. To maintain this new level of wealth in the long run (that is, beyond the 25-year horizon used to calculate total wealth), Uganda needs to build up other forms of capital as oil reserves are gradually depleted. If the depletion of oil reserves is not matched with increased investments in other forms of capital and leads to an increase in consumption, Uganda will experience a decline in its overall wealth in the long run.

B. MANAGING NATURAL RESOURCES AND ENVIRONMENTAL SUSTAINABILITY

Land degradation, deforestation, and threatened biodiversity are the key concerns on environmental sustainability.

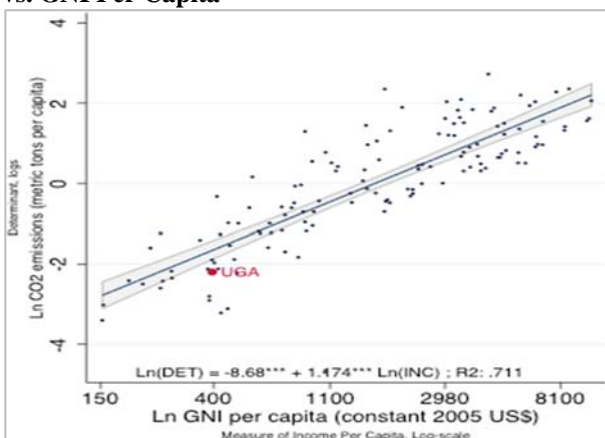
5.7. With the majority of the poor and those in the bottom 40 percent dependent on agriculture, sustainability of the natural environment is crucial in Uganda. With a lack of access to electricity, the poor are also dependent on the forests for their energy needs. Natural resources are important in the Ugandan context. The country has an abundance of water resources which is crucial for hydropower generation and other uses, the discovery of oil is a potential game changer, the rich biodiversity offers tourism opportunities, fisheries provide livelihoods, and there are also other minerals which are being mined. However, the country is also vulnerable to droughts and floods.

5.8. On carbon-dioxide emissions which are critical on the climate change agenda, Uganda is much lower than countries with a similar level of GNI per capita. According to the fourth inter-governmental Panel on Climate Change Assessment Report, Uganda's temperature is likely to increase on average by up to 1.5°C in the next 20 years and up to 4.3°C by the 2080s. Based on the climate change models, predictions indicate an increase in rainfall of 10–20 percent over most of the country with a decrease expected over the semiarid cattle corridor. This could aggravate existing vulnerabilities. However, Uganda's level of CO₂ emissions are low, much lower than that for SSA, and could be attributable to the low level of industrialization, very limited access to electricity and dependence on hydroelectric sources for electricity generation (figure 5.1).

5.9. For electricity generation, Uganda's use of fossil fuels is comparable to other countries with a similar level of GNI per capita and is comparatively higher in the use of hydro resources, which enables a less carbon-intensive energy mix. At the current rapid growth, demand for electricity is expected to surpass the current available generation capacity by 2016 (figure 5.2). The generation capacity shortfall over the medium term is expected to remain until the planned large hydropower plants of Karuma (600 MW) and Isimba (183 MW) are commissioned around 2018. As an additional effort to avoid power shortages and reliance on expensive rental power plants, the GoU is also promoting the development of small private power producers that can be commissioned faster and could be developed simultaneously without imposing financial and managerial burden on the GoU (figure 5.3).

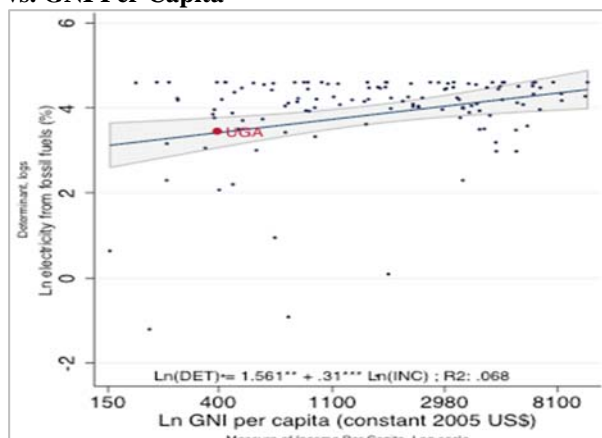
5.10. Nearly 46 percent of the land in Uganda is severely degraded. Land is increasingly being transformed because of agricultural expansion (conversion to croplands and pastures, and so on), unsustainable agricultural practices, expansion of urban areas, and other pressures. Average soil erosion is estimated to exceed 5 tons per ha per year, and the associated soil nutrient loss is particularly pronounced because most of the nutrients in tropical agriculture are in the top 5 to 10 centimeters of the soil. This has significant implications for the agricultural sector.

Figure 5.1. CO₂ Emissions (Metric Tons per Capita) vs. GNI Per Capita



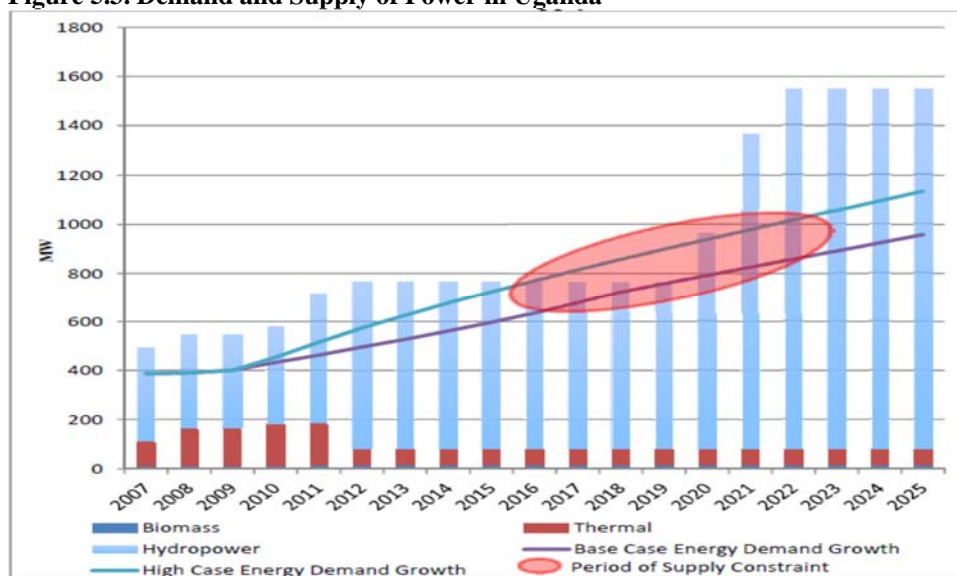
Source: Gable et al. 2015.

Figure 5.2. Electricity From Fossil Fuels (% of Total) vs. GNI Per Capita



Source: Gable et al. 2015.

Figure 5.3. Demand and Supply of Power in Uganda



Source: Uganda electricity Transmission Company Ltd (UETCL).

5.11. Between 2005 and 2010, Uganda lost an estimated 88,000 ha of forest each year or 2.6 percent of forest cover per annum. It lost over 40 percent of its forest cover over the past two decades largely due to fuel wood/charcoal consumption, clearing for agriculture and timber for construction. Parts of Uganda are beginning to suffer a deficit of fuel wood. Fuel wood or charcoal now needs to be transported from more distant areas. The women in many poor households now have to walk over 1.5 km each day to gather fuel wood and often of lower quality. In addition, when forest cover is removed, the loss of ground cover results in soil erosion and nutrient leaching during rains, making reforestation and farming difficult.

5.12. Significant overharvesting has resulted in a 50 percent decline in the catch of the Nile perch on Lake Victoria since the mid-2000 peak. Increasing fishing effort is exerting pressure on capture fisheries, leading to a decline in fish stocks and catches prompting the use of destructive fishing gears and technologies and employing extra-fishing power to chase few fish. This has

resulted in increased investment costs in fishing operations. This situation is fueled by the open access fish management regime, climate change, water pollution, and invasive species. However, there are opportunities for some of these pressures to be addressed through the development of aquaculture.

5.13. At the national level, Uganda has an abundance of water resources but increasingly suffers from localized water stress and pollution. Water resources are abundant in Uganda but are not accessible because of poor infrastructure. Uganda's total renewable water resources are about 43 billion m³ out of which about 13 percent is sustainable groundwater and the balance is surface water. With withdrawals at only 1 percent of renewable annual water resources, there is scope to increase the use of water for agricultural and industrial purposes as well as to cater to increased demand of water from urbanization. However, given that water resources are highly variable in time and space, addressing these competing water uses will need to be managed carefully. Water management is even more critical given the recent occurrence of floods and droughts and reduced water availability due to climate change. The quality of surface and groundwater in Uganda is generally good but it has been declining, particularly for Lake Victoria, due to pollution from domestic and industrial waste, agricultural run-off and poorly constructed sanitation facilities. In addition, wetlands in the country are being degraded at an alarming rate reducing their ability to provide critical goods and services.

5.14. Wetlands around the Lake Victoria and Kyoga drainage basins are threatened. The main causes are uncontrolled land reclamation for agricultural and industrial activities, and the expansion of human settlements. This is exacerbated by weak enforcement of existing laws and regulations. Degraded wetlands lose their ability to store/absorb water and prevent flooding, clean water and support the provision of crops, fish, and plants. Loss of wetlands and near-shore pollution in Lake Victoria threatens the productivity of its fisheries as well as its tourism potential. Periodic infestations of water hyacinth, can have particularly severe impacts, blocking virtually all economic uses of the Lake in severe cases, and contributing to further deterioration of water quality. Wetland losses are not currently well-documented.

5.15. The country's rich biodiversity is under threat because of poaching, land use changes, mining and more recently from oil discovery. As the natural resources in non-protected areas dwindle, protected areas are the remaining repositories of fuel wood and forage and are becoming a focus for poaching, illegal grazing and other activities. Land use changes that degrade or destroy habitats and cut off migratory routes through deforestation, overgrazing, pollution, expansion of agricultural and urban areas, and unsustainable harvesting (for example, medicinal plants and non-timber forest products), amongst others have affected the country's biodiversity. Uganda's oil discoveries are in a prime area rich in biodiversity and ecotourism assets (Albertine Graben) and pose an environmental concern.⁴⁰

⁴⁰ The petroleum resources discovered in Uganda so far are mainly located within national parks and wildlife game reserves such as the Murchison Falls National Park which is the second most visited tourist destination in Uganda and the Queen Elisabeth National Park which is the largest National Park in Uganda.

C. FISCAL SUSTAINABILITY

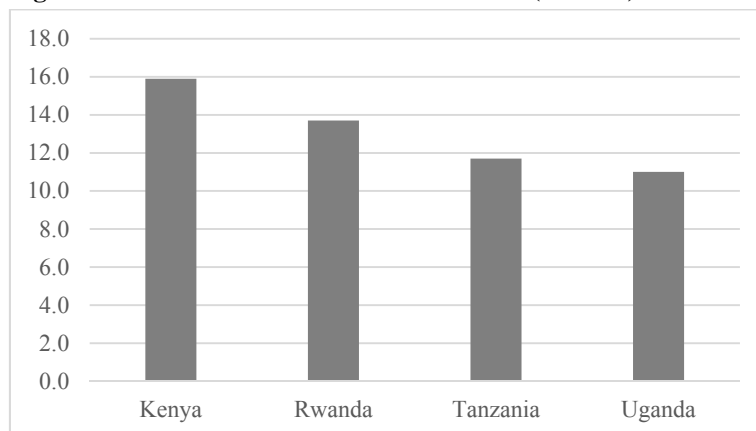
Fiscal sustainability will hinge on: (a) increased domestic revenue generation to reduce dependence on external aid in financing the budget; (b) improved allocative and financial efficiency of the budget by implementing clear and transparent PFM rules and systems; and (c) prudent management of oil revenue.

5.16. **The fiscal deficit has averaged 3.3 percent of GDP during FY2011–14 while public debt at 28.9 percent of GDP in FY2014 indicated low risk of debt distress.** Grants, which accounted for about 5.4 percent of GDP in FY2006 reduced to only 1 percent in FY2014. This decline in aid is partly explained by the suspension of budget support by development partners in response to the governance issues that emerged in 2013. This suspension has now been lifted. Given low domestic revenue generation and a decline in grants, the fiscal deficit was contained by reducing recurrent expenditures which declined from 12.7 percent of GDP in FY2011 to 9.8 percent in FY2014. The successful implementation of reforms undertaken in the context of the highly indebted poor countries initiative and Multilateral Debt Relief Initiative contributed to a drastic decline in external debt, from an average of 63.5 percent of GDP in FY1999/2000–2005/06 to 12.6 percent in FY2006/07–2009/10. The most recent debt sustainability analysis for Uganda indicates that the country faces low risk of debt distress.

5.17. **At 11.9 percent of GDP in FY2014, total domestic revenue collection in Uganda is one of the lowest in the region.** The poor tax mobilization performance is attributable to an inefficient tax policy and administration (figure 5.4) and the presence of a large informal sector. Uganda faces a large shortfall in value added tax revenues because of statutory exemptions and poor administration and enforcement of tax laws (IMF 2013). Some progress has been made on removing tax exemptions and increasing excise on some products but there is a need to bolster tax administration through improvements in audit coverage, audit risk criteria and better compliance management by focusing on sectors with the highest revenue potential. Improved tax administration becomes even more crucial to better manage the oil windfall.

5.18. **Higher revenues are needed not only to bolster social services but also to finance the government's ambitious investment program.** The authorities have stated their intent to finance mega infrastructure projects in energy and transport to address the large infrastructure gap in the country. Such an approach is justified but has been delayed because of limited budgetary resources. The execution of the investment program has been less than 70 percent in recent years. The increase in public investment calls for strengthening of PIM (box 5.2) and PFM. In addition, there is a need to increase spending on social services as well.

Figure 5.4. EAC: Tax Revenue-to-GDP Ratio (Percent)



Source: Uganda CEM (World Bank 2015c). WDI data.

Box 5.2. PIM in Uganda

Uganda ranks 46th out of 71 countries in the IMF's PIMI. Its overall score is lower than the average of EAC and SSA. This is particularly explained by its low score with respect to project appraisal, implementation, and evaluation (table 5.1). The Uganda CEM 2015 argues that improved efficiency in public sector spending would lead to higher GDP growth

rates. That is, higher growth would be achieved using fewer resources. PIM systems need to improve, with regard to strategic guidance for public projects (alignment to the NDP priorities and adoption of minimum technical and financial standards), project selection, budgeting and implementation (integration into the budget cycle and medium-term expenditure frameworks), project audit, and evaluation. Improving the efficiency of PIM, with regard to project appraisal, selection, implementation and evaluation, would increase the fiscal space available to developing countries, like Uganda, to invest in vital infrastructure projects much needed for growth and development.

The GoU has already taken steps to address the shortcomings in the area of PIM. The restructuring of the Ministry of Finance to create a department in charge of projects analysis and PPP is already a positive step forward. The World Bank is providing technical assistance for strengthening PIM to the GoU through a Department for International Development trust fund. The aim of this technical assistance is threefold: (a) develop public investment guidelines and manuals; (b) Capacity building; and (c) establish an institutional organization, framework and arrangements to improve PIM system. The following activities are being prioritized in the context of the technical assistance: (i) Simplified Manual for Public Investment Appraisal; (ii) PIM Framework with recommendations on how the government can improve the public management process to select better projects; (iii) Training activities in Log Frame Approach, Cost Benefit Analysis and Cost Effectiveness for public officials; (iv) Action Plan with recommendations to establish an institutional organization, framework and arrangements to improve PIM System.

Source: Uganda CEM (World Bank 2015c).

Table 5.1. PIMI

	PIMI	Appraisal	Selection	Implementation	Evaluation
Uganda	0.36	0.20	0.70	0.38	0.18
EAC	0.38	0.30	0.45	0.53	0.23
SSA	0.38	0.33	0.45	0.48	0.28

Source: IMF and World Bank PIMI database.

Note: Parameterized indicators initially between 0 and 4, with 4 being the best.

5.19. Given the low level of revenues, the government has alternated between prioritizing social spending and infrastructure expenditures. The period 1987–96 was characterized by adjustment programs (fiscal restraint, tight monetary policy, and institutional reforms) aimed at maintaining macroeconomic stability. It was followed by the prioritization of social expenditures during 1997–2010 and then a move to infrastructure spending from 2011 to date. Since 2012, fiscal policy has also been used to stimulate aggregate demand with an increase in development expenditures from 6.1 percent of GDP in 2011 to 7.2 percent of GDP in 2014. However, with the decline in grants over the years without a corresponding increase in domestic revenue, total government spending (expenditure + net lending) declined from 18.6 percent of GDP in FY2007 to 16.7 percent in FY2014. However, Uganda needs to develop both physical and human capital stocks to accelerate its socioeconomic transformation. Oil is therefore an opportunity to provide additional government revenue to address some of the binding constraints to growth including infrastructure, social capital, and skills.

5.20. While Uganda is eager to maximize the direct benefits derived from extractives, it also needs to avoid the mistakes that other resource-rich countries have made. In fact, whilst the opportunities are large, the pitfalls often associated with natural-resource-driven economies can be equally challenging (see box 5.3). These pitfalls generally can manifest themselves in different ways and have been termed as the natural resource curse: (a) real appreciation of the local currency that undermines the competitiveness of other export industries and of import-competing industries by encouraging imports; (b) increase in volatility due to oscillating oil prices in world markets that harm investment and economic growth over time; (c) relative price increase in non-tradable sectors compared to tradable sectors that causes a shift of resources from the tradable sector to the non-tradable sector, starving the tradable sector of labor and capital; (d) increase in rent seeking that results in socially inefficient spending and allocation of resources preventing widespread sharing of resource rents; and (e) false sense of security driven by oil revenue inflows that leads to a reduction in necessary human and social capital investments.

5.21. Given the risks associated with oil, diversified development - in the sense of a more balanced contribution from institutions, assets, and natural resources, is the best way to sustainably achieve the twin goals for Uganda. Achieving this contribution requires a strategy articulated around 4 building blocks: (a) ensuring that oil revenues are able to ease the financing constraints on critical social and infrastructure investments which currently face a difficult choice between them; (b) strengthening of results orientation in the public sector to realize the benefits of existing institutional reforms; (c) a reconfigured relationship with the private sector more focused on the enabling environment with regard to regulatory institutions, market functioning, and infrastructure; and (d) spatial policies which can calibrate a policy mix matched to the distinctive needs of rural and urban areas and the foundational market institutions for each, especially regarding land.

5.22. Sound oil revenue management stands on the two pillars of good governance and strong PFM. Governance is particularly important because resource rents create perverse incentives for the elites to appropriate them. Strong PFM is important for every country but it assumes a more crucial role in resource-rich countries because resource revenues accrue to the government in the first instance and get transmitted to the economy through the level, timing, and composition of public expenditure.

5.23. After an initial period of ramp up in infrastructure spending, the government plans to follow the permanent income rule to manage oil revenues. The permanent income approach, which, if followed literally, comes down to restricting spending out of oil wealth to a level that can be maintained over a long period of time. It essentially entails saving in good years and dissaving in bad years by calculating a stream of income that is equal in net present value to the projected revenues from oil. Since permanent income is relatively unresponsive to current oil prices and oil production, the rule would automatically insulate the fiscal balance from current developments in the oil sector. As a result, the rule would have the effect of smoothing out government expenditure over time. However, implementing this approach will require a strengthening of institutional capacity, which is particularly weak in Uganda.

Box 5.3. Risks Associated with the Extractives Sector

The gains from natural resources rents are normally dependent on the country's state of governance as well as the macroeconomic management capacity. If not well managed, like other natural resource booms, the discovery, and extraction of oil may be synonymous with the 'resource curse' or 'mixed blessing'. The Dutch disease is a manifestation of the resource curse, which turns poorly managed natural resource wealth into a mixed blessing through reduced long-term growth.

The resource curse works through different mechanisms, including (a) an overvaluation of the currency and (b) the volatility of key economic aggregates, including exchange rates, export earnings, and output. If poorly managed, the Dutch disease could impact the agriculture and the tourism sectors through exchange rate movements. The increased supply of foreign exchange through oil may increase the price of a shilling to a dollar hence the capacity to buy imported foods rather than producing food locally. Agriculture will contract over time, with regard to manpower and share of GDP, as farmers adopt modern methods that necessitate fewer working hands to feed the population. Tourism may face declining profitability as a result of (a) a real term appreciation of the shilling, discouraging tourists into Uganda and (b) price hikes for services triggered by expatriate workers in the oil sector that may affect the economy alike. The overall earnings from the sector may therefore decline following the benefits from the oil sector.

Volatility of commodity prices produces fluctuations in exchange rates, export earnings, output, and employment, and discourages investment and growth. Like other natural resource-rich countries, depending on oil for export makes the country like Uganda dependent on international price movements. Export price volatility is another reason why natural-resource-rich countries may be prone to sluggish investment and slow growth. Similarly, high and volatile exchange rates slow down investment and growth.

The other channels through which natural resource wealth (including oil) may prove to be a mixed blessing have been identified to include (a) reduced sense of priority for the need to build up human capital through education and training; (b) reduction in productivity gains due to poor quality of investment; (c) deterioration of social capital (for example, good governance, independence of the judiciary, freedom of press, public trust, equality, low corruption, and political freedom); (d) rent-seeking behavior that diverts resources away from socially beneficial economic activity; (e) crowding out non-resource revenue; and (f) increasing spending pressures and subsidies that promotes inefficiencies and inequalities.

Source: Uganda CEM (World Bank 2015c).

D. GOVERNANCE AND PUBLIC SECTOR MANAGEMENT

Governance and effective public sector management are not only a sustainability concern but they also impact growth and inclusiveness. The key issue in the public sector is the policy implementation gap which is the result of a lack of enforcement of sanctions which in turn is driven by political incentives. In the existing circumstances, efforts need to be focused on relieving technical constraints and putting legislative frameworks, structures, and institutions in place to improve the accountability framework.

5.24. Uganda's performance in PFM is good on transparency but weak on budget credibility, controls, and compliance, essentially highlighting implementation gaps. The new PFM Act 2014 will, if implemented, support faster progress to address these issues. The key aspects of a good PFM system include macro-fiscal control and stability (macroeconomic management), budget planning and execution (including monitoring and evaluation), procurement, cash and debt management, financial systems and accounting, internal controls, and external oversight. As indicated in the Public Expenditure and Financial Accountability (PEFA) assessment of 2012, Uganda's performance is strong in the following areas: budget documents are comprehensive; the general public has access to key fiscal information, tax payers' obligations and liabilities are transparent, good accounts are kept, reporting systems are adequate and external audits are extensive and of high quality. Uganda is doing well with regard to budget transparency

(ranking 18th out of 100 countries) but its PFM systems are weak with regard to budget credibility, budget execution controls (particularly payroll), procurement compliance and legislative scrutiny of external audit reports. In most of these areas, Uganda's performance is below its East African neighbors. The Auditor General's annual reports regularly identify weak compliance with PFM regulations, resulting in avoidable or wasteful expenditure, build-up of arrears, inadequate accountability and, in some cases, the risk of fraud or misappropriation. To address the various shortcomings in PFM, the government passed the PFM Act in November 2014 and implementation of the provisions of this bill will help strengthen Uganda's PFM framework.

5.25. Various interventions will be needed to address the weaknesses in the PFM system.

The unpredictability in the budget is often due to a lack of internal controls and poor planning for expenditures which is being addressed through the creation of a contingency fund. The introduction of the Treasury Single Account (TSA) should promote greater transparency and accounts

Table 5.2. Recent Performance on PFM Compliance Indicators

PFM Compliance Measures	2011/12	2012/13	Trend
Unqualified audit opinion - all sectors (%).	37	42	↑
Number of dormant bank accounts.	586	14	↑
Advances to officials' private bank accounts or in cash for activities (UGX, billion) - 9 sectors.	108	21	↑
Total domestic arrears (UGX, billion) - all sectors.	763	1,127	↓
Mischarging against budget - 9 selected sectors (%).	6.4	2.2	↑
Procurement risk rating (PPDA Institutional audits) - average 9 sectors (%).	29	28	↑
<i>Source: Various including the Financial Management and Accountability Program (FINMAP)</i>			

reconciliation and facilitate a shift from cash rationing to more active cash and debt management. Under a TSA arrangement, comparing expenditures with budget allocations is done through the Integrated Financial Management System (IFMS). With only 77 percent of expenditures going through IFMS, there remains a substantial gap that can be exploited. Some of the most significant risks of wastage, errors, delays, and fraudulent losses are found in payroll and pensions management. The government is committed to rolling out the IPPS, introducing biometric payroll records for civil servants and decentralization of the payroll to improve accountability. Around 70 percent of public expenditures go through procurement systems that are affected by poor practices. There is evidence of payments for goods or services that were not delivered and only 21 percent of contracts have complete procurement records. There has been a significant improvement in the quality of audits produced by the OAG. However, there is a large backlog of audit reports that are not debated in the Parliament and these reports are not published, creating a missing step in the accountability cycle. Some of the PFM measures adopted by the government over the past few years has resulted in some improvements (table 5.2 and annex 4).

5.26. In the last two decades, the government has actively pursued decentralization, anticorruption, and civil service and PFM reforms. These issues are not only important from the lens of sustainable improvements on the twin goals but they also have a far-reaching impact on growth and inclusion as discussed in chapters 3 and 4. Uganda was an early adopter of independent revenue agencies, medium-term expenditure frameworks, public expenditure tracking surveys, and results-oriented management mechanisms. During the mid- to late-1990s, Uganda implemented a host of initiatives aimed at streamlining civil service and formalizing PFM systems,

which laid the foundation for a series of interventions introducing decentralization and emphasizing service delivery.^{41,42} The 2000s saw the enactment of a plethora of laws with a view to further improving PFM and anticorruption. More recently, in 2013, the government amended the public procurement and disposal of assets legislation to enhance enforcement, improve local content, and strengthen mechanisms for redressal by aggrieved bidders. In November 2014, the government passed the PFM Act, which will be a key pillar for strengthening the overall budget process and improving governance. In addition, FINMAP and other instruments are financing the adoption of the IFMS and the IPPS. Furthermore, the GoU has continued to bolster its formally robust anticorruption legislation, in addition to introducing a performance management approach anchored on results-oriented management and output-oriented budgeting mechanisms.^{43,44}

5.27. Governance, according to the World Bank’s CPIA, includes the four broad areas of property rights, fiscal management, quality of public administration and transparency, accountability and corruption.⁴⁵ Property rights include both the laws and regulations for secure property rights and the quality of the judicial system as an enforcement agency. Fiscal management includes the quality of budgetary and financial management as well as the efficiency of revenue mobilization. Both these aspects were discussed in the previous section (5C). Public administration includes policy implementation and coordination with the larger public sector. The fourth area includes the accountability of the public officials, access of civil society to information, and state capture by vested interests (annex 3).

5.28. Laws and regulations related to property rights in Uganda are available online and not changed arbitrarily but there is room for improving the judicial system. The index of economic freedom, which measures an individual’s right to control his or her labor and property, ranked Uganda 9th out of 46 SSA countries in 2014. Uganda is making progress in registering

⁴¹ Decentralization is anchored in the 1995 Constitution, the Decentralization Statute No. 15 of 1995, and the Local Government Act of 1997.

⁴² After the launch of a Civil Service Reform Programme in the early 1990s, the government focused on civil service reform again in the late 1990s by implementing the Public Service Reform Programme, a new commitment to pay reform, and efforts to introduce performance management mechanisms.

⁴³ Criminal responsibility for bribing public officials, diversion of public funds, influence peddling, or nepotism is provided for in both the Penal Code Act and the Anti-corruption Act of 2009; The Leadership Code Act (2002), the Anti-Corruption Act (2009) and the Code of conduct and ethics of the Ugandan Public service regulate conflict of interest; also, the President, Ministers, members of the Parliament, judges, and civil servants, and their spouses, must comply with asset disclosure requirements, in accordance with the Leadership Code Act. Furthermore, the Whistle-blowers Protection Act of 2010 provides for mechanisms encouraging individuals to blow the whistle on corruption cases; the Access to Information Act of 2005 provides every citizen the right to access information; and the Anti-Money Laundering Act of 2013 penalizes money-laundering activities. In December 2014, the government passed the Leadership Code Amendment Bill, which will allow for the enforcement of the asset declaration clause.

⁴⁴ As part of the implementation of the results-oriented management/output-oriented budgeting framework, the majority of ministries, departments, and agencies (MDAs) and more than half of LGs have been able to develop Client Charters, which are a valuable means for communicating expected service standards as well as improving service delivery.

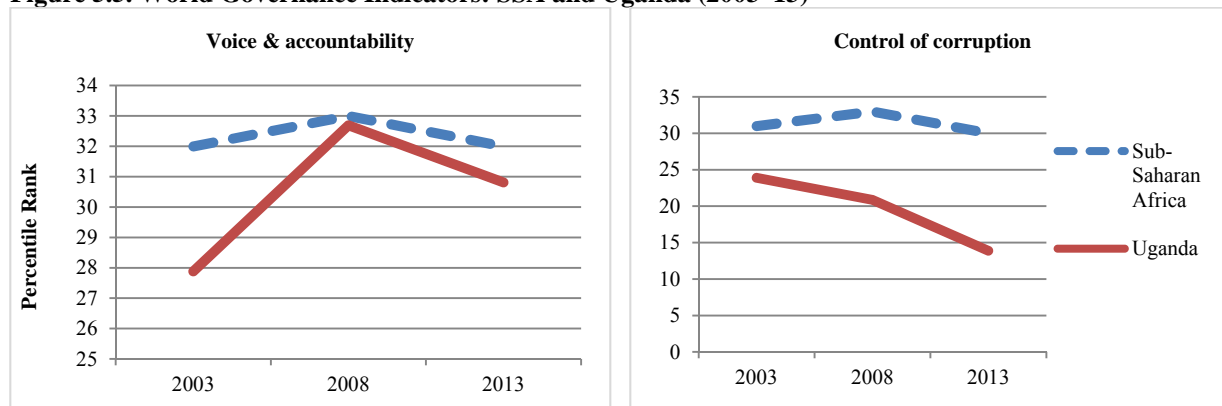
⁴⁵ The CPIA of the World Bank provides an assessment of the conduciveness of a country’s policy and institutional framework to poverty reduction, sustainable growth, and the effectiveness in the use of development assistance. Its focus is on the key elements that are within the country’s control. Countries are rated on a set of 16 criteria grouped in four clusters: (a) economic management; (b) structural policies; (c) policies for social inclusion and equity; and (d) public sector management and institutions. For each of the 16 criteria, countries are rated on a scale of 1 (low) to 6 (high).

land and has increased the percent of land that is titled to 20 percent, well ahead of other SSA countries. However, land tenure insecurity remains mainly due to overlapping rights in the Central region and lack of effective institutions to manage communal landownership predominantly in the Northern and Eastern regions of the country. Since the land market has large ramifications for urbanization, access to finance, and agriculture, among others, the government is taking steps to accelerate systematic registration of land and rehabilitate and modernize land administration including computerization of land registration, property valuation and physical development planning. In addition, the Industrial Property Act was passed in 2014 to promote inventive and innovative activities and facilitate the acquisition of technology. Uganda ranked 80th out of 189 countries in enforcing contracts, above the SSA average, as per the 2015 Doing Business Report. However, it still takes 490 days to enforce a contract and costs 31.3 percent of the claim value. In addition, judges are appointed by the President following recommendations from the Judicial Service Commission. However, the appointment process lacks transparency and some key positions remain vacant for long durations, weakening the system.

5.29. On the quality of public administration, key dimensions of the governance environment have been declining since 2003, especially Uganda's capacity to control corruption. According to the World Governance Indicators, Uganda's government effectiveness and regulatory quality are on a declining trend. Similarly, the voice and accountability environment, which improved between 2003 and 2008, is steadily deteriorating (figure 5.5). Uganda's capacity to control corruption appears to have reached an all-time low and is only above that of Kenya's, East Africa's worst performer. The high prevalence of bureaucratic corruption negatively affects the poor and was deemed the most significant obstacle to doing business in Uganda in the latest Africa Competitiveness Report. Transparency International's Global Corruption Barometer Survey (2013) found that 61 percent of Ugandans had paid a bribe to one of the eight institutions ((judiciary, education, tax services and customs, permits/registries, medical services, police, land services or utilities) in the last 12 months (figure 5.6). The average value of small bribes paid was approximately 20 percent of citizen's annual income (IG 2014). In addition, the fact that public sector wages are low compared to their private sector equivalents and even by African standards, creates obstacles for the acquisition of talent, encourages public servants to seek supplementary sources of income to the detriment of performance, and incentivizes corruption.⁴⁶

⁴⁶ As a whole, the wage bill represents about 4 percent of GDP, compared to an average across Africa of about 6.5 percent for central government and 9.8 percent for all government.

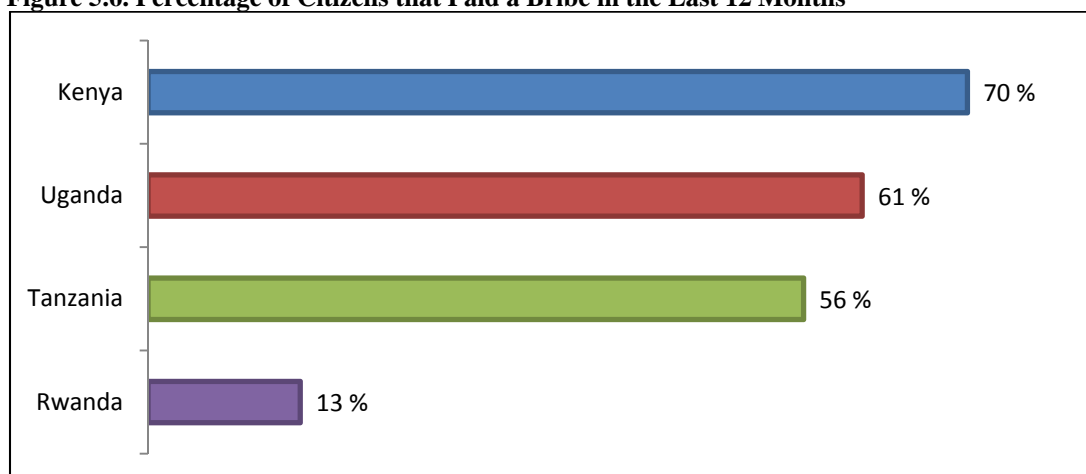
Figure 5.5. World Governance Indicators: SSA and Uganda (2003–13)



Source: World Governance Indicators.

Source: World Governance Indicators.

Figure 5.6. Percentage of Citizens that Paid a Bribe in the Last 12 Months



Source: Transparency International (2013).

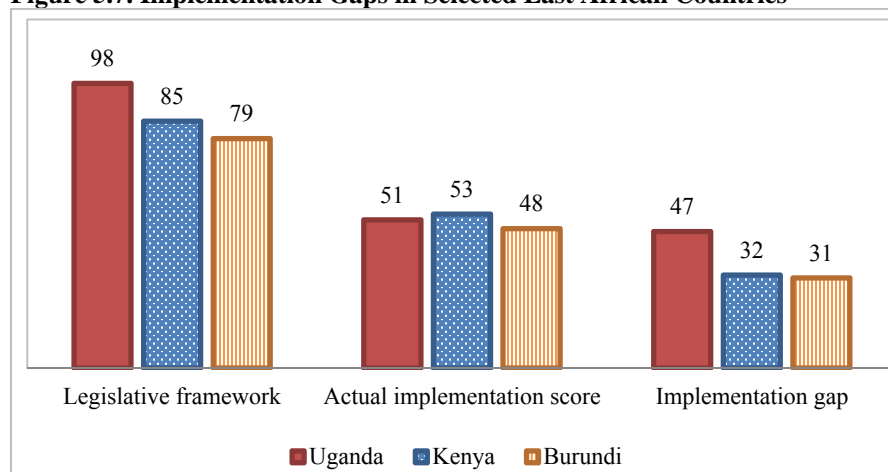
5.30. The quality of the decentralization framework has worsened since 2005, negatively impacting service delivery. Given that a significant portion of public services is delivered through LGs, the country's decentralization framework is a key determinant of service quality. Since 2005, policy reversals have weakened LG's discretionary powers and reduced financial and human resources at the district level. These policy reversals have included the near-elimination of local revenue base, reduction of transfers to LGs, increase in conditional grants, and the creation of new districts, mostly for political patronage (World Bank, 2013e).⁴⁷ Uganda is also marked by inequality across districts in terms of public spending per capita. For example, in 2010, public spending on health differed by a factor of 11.5 across districts, and public spending on education differed by a factor of 6.3. The increase in conditional grants has made the process of allocation of money to districts ad hoc. Own revenues account for 10 percent of the total revenues of local self-governments, another 10 percent are unconditional grants while the remaining 80 percent are conditional grants. The low tax base has eroded bottom-up accountability to the citizens while the

⁴⁷ The real per capita budgets of the districts fell about 10 percent over 2003/04–2011/12. Transfers to LGs declined as a share of central government spending from 25 percent to 20 percent over 2003/04–2011/12. District own-source revenues declined over 2003/04–2011/12 with the abolition of graduated tax and the suspension of taxation of owner-occupied dwellings (World Bank 2014b).

large share of conditional grants has made the system opaque and vulnerable to corruption. In addition, LGs are characterized by weak management systems, blurred lines of accountability, political interference, and a lack of compliance with PFM and procurement rules. This is worrying as good governance at the local level in Uganda, including receiving unqualified audits at the Auditor General's Annual Report, is associated with more efficient education and health provision (World Bank 2013e).

5.31. Uganda's main public sector management challenge is to bridge the implementation gap which is primarily the result of failure to impose sanctions. In practice, public institutions in Uganda tend to perform poorly, the acquired capacity is underutilized, and laws are not fully implemented. For instance, Uganda has one of the biggest implementation gaps when it comes to anticorruption legislation in East Africa (Global Integrity 2011, figure 5.7). Further, the general breakdown in accountability relationships and impunity for low-performing or corrupt civil servants is one of the main factors contributing to poor service delivery in Uganda. Some supervisory mechanisms do exist, such as the inspectorates in the public service, LG, judiciary, and education sector, but these are often poorly resourced and overwhelmed by the magnitude of the problems. There is often no follow-up to reports and Inspectors have little or no power to enforce or act where they find poor performance. The persistence of very high absenteeism among health and education workers, as well as the failure to sanction officers responsible for the lack of compliance with PFM rules is a great illustration of this malaise.

Figure 5.7. Implementation Gaps in Selected East African Countries



Source: Global Integrity (2011).

5.32. The key obstacle to effective sanctioning is a lack of political incentives. The lack of political incentives goes a long way towards explaining why the public service, decentralization, anticorruption, and PFM reforms have not yielded the expected results.

5.33. Detection is the strongest link in the accountability chain in Uganda while sanctions are the weakest link. The accountability chain has three fundamental stages: first, detection - Office of the Auditor General, Public Accounts Committee, and Public Procurement and Disposal of Public Assets Authority; second, investigations - Central Intelligence and Investigation Department and Inspectorate of Government; and third, criminal and administrative sanctions - Anti-Corruption Division of the High Court, IG, Department of Public Prosecutions, and Ministry of Public Service. Detection is the strongest link in the chain in Uganda and investigations is

adequate, but the power and functioning of the sanctioning authorities needs to be ramped up significantly and they need to be free from political interference.

5.34. Citizen engagement, CSOs, and the media have not had much impact in improving accountability. Inspectorate of Government's citizen reporting mechanisms, including the free, mobile phone-based anticorruption hotline and the social accountability committees, showcase the government's efforts to support a critical mass of informed citizens to demand good governance. This has increased the number of corruption complaints but not much has been done about it. Similarly, the impact of 'Demand for Good Governance' interventions have depended on the degree of information that the government has been willing to share and their alignment with the political incentives faced by the Government. Stimulating citizens' demand for good governance without a commitment to closing the feedback loop can contribute to citizen apathy. Since 2006, the freedom of media organizations to monitor corruption appears to be on a declining trend as reflected by the Freedom of the Press which showed a decline in Uganda's ranking from 104 to 110 from 2012 to 2013 (Freedom House 2014). The government also has a productive relationship with CSOs working on budget transparency, procurement, and anticorruption issues.

5.35. The government is cognizant of the weaknesses in the accountability chain and is taking measures to address some of them. In 2013, the government improved conditions for imposing criminal and administrative sanctions by appointing a Director of Public Prosecution and fully constituting the Inspector General of Government (IGG). In addition, the fact that the government has shown its support for the Department for International Development's Strengthening Uganda's Anti-Corruption and Accountability Regime program – which will, among others, provide technical assistance to the institutions within the accountability chain – further demonstrates its commitment to deter corruption. The key technical constraints in the accountability framework, which the government is willing to work on, include (a) legal constraints (amendment of the Anti-Corruption Act to facilitate the recovery of stolen funds and assets); (b) inadequate case management systems to effectively deal with the caseload; (c) weak technical skills (especially regarding investigations and prosecutions); (d) insufficient staffing levels and resourcing; and (e) the need to strengthen mechanisms within OAG and the Public Accounts Committee to clear the backlog of audit findings.

5.36. The country has not performed well on the four broad World Bank CPIA governance indicators: property rights, fiscal management, quality of public administration and transparency, accountability and corruption. Various interventions are needed to sustain the gains made on PFM and to strengthen the governance systems. The country's judicial system needs to be improved and the capacity to control corruption should be strengthened. Public sector management should also better address the growing implementation gap—partly resulting from failure to impose sanctions—and civil society and media should be better equipped to enforce accountability. These challenges need to be addressed together with progress in implementing governance reforms. This will be particularly important in preparation for oil production to avoid any risk of the Dutch disease and other negative consequences as experienced elsewhere.

5.37. Addressing the technical constraints will help but a perceptible change in governance will result only if the incentive framework changes. The government is on the right track by focusing its efforts on improving legislation and putting adequate structures and institutions in place. These institutions will become more effective whenever conditions for change are more

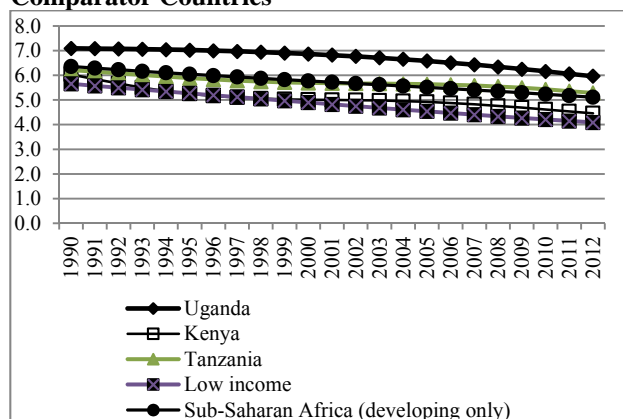
conducive. Meanwhile, efforts to improve the PIM, PFM, and accountability framework, introduction of performance-oriented approaches, and greater citizen demand for accountability will certainly help.

E. MANAGING HIGH FERTILITY RATES

The key to reducing fertility is to promote programs which combine education and vocational training for women together with training on family planning and health. However, fertility preferences are rooted in social and cultural values and will take time to reduce perceptibly.

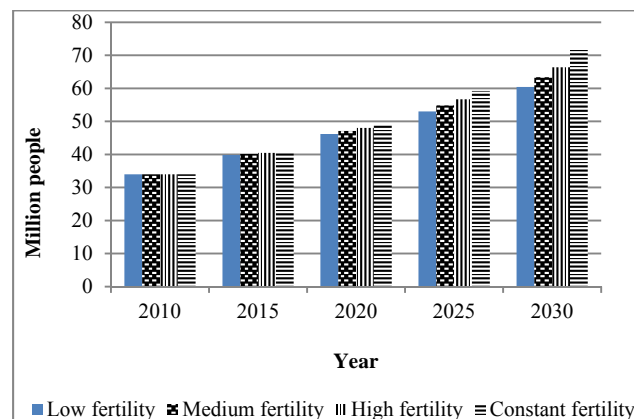
5.38. Uganda has one of the youngest and most rapidly growing populations in the world, resulting in a high youth dependency ratio. The total fertility rate is estimated at 6.2 children per woman (figure 5.8). About half (48.5 percent) of Uganda's population is younger than 15, well above SSA's average of 43 percent and the world average of 26 percent (box 5.3). Both the high level of fertility and the youthfulness of the population results in a very high youth dependency ratio which is 45 percent higher among the bottom 40 percent of the households compared to the top 60. The country's population growth rate, currently at 3.3 percent, has also been steadily above Africa's average, except during the period of peak prevalence in HIV/AIDS in the early 2000s. Uganda's population is expected to increase from about 38 million in 2014 to 60–70 million in 2030, depending on the fertility rate dynamics (figure 5.9) and its population density will increase accordingly.⁴⁸ While population density in the rural areas is not critically high right now, it might become a problem in future.

Figure 5.8. Total Fertility Rates in Uganda and Comparator Countries



Source: WDI.

Figure 5.9. Population Projections for Uganda, 2010–30



Source: UN Population Division.

5.39. The increasing population has taken a toll on household and government finances. Households have found it difficult to save and have not been able to invest much on human capital which has in turn limited their income-generating capacity. Given the scarcity of Uganda's fiscal resources, the government has found it difficult to invest in both infrastructure and social services in adequate amounts. An increase in one of these categories of investment leads to gaps in the

⁴⁸ Life expectancy in all scenarios is assumed to increase from 57.9 to 66.9 years between 2010 and 2030; total fertility rate is expected to decline from 6.2 in 2010 to 3.4 (low variant), 4.4 (medium variant), or 5.4 (high variant) in 2030.

other. In the 1990s and early 2000s, the government focused its efforts on social services until it became apparent that the country's infrastructure required urgent attention.

Box 5.4. Stylized Facts on Fertility in Uganda

- Uganda's fertility rate at 6.2 children per woman is one of the highest in the world
- Fertility in urban areas—and especially in Kampala—is lower
- Education is a significant predictor of fertility and so is the increase in the age when the first sexual intercourse occurs
- Increasing contraceptive use made a significant impact on fertility
- Fertility is negatively correlated with access to electricity
- Women who earn some cash from their work have fewer children than those who do not and female labor participation increases the age at marriage and decision making by women in the home.

5.40. **So far, Uganda has not been able to capitalize on its large and young labor force.** The 25 years and above population in Uganda has an average of only 4.7 years of schooling. In addition, there is a lack of productive jobs to employ the youth given the constraints to doing business and the large informal sector. An increase in the working-age population has the potential to increase GDP growth, boost savings, and enhance human capital.

5.41. **Combined interventions which target improvements in labor market outcomes of women along with increased use of contraceptives and family planning services have the largest impact on fertility.** A program (Empowerment and Livelihoods for Adolescents, for women between the age of 13 and 21 years) designed to provide vocational training along with awareness on life skills to build confidence, effectively manage time and finances, and improve health found a 72 percent increase in employment, 26 percent lesser likelihood to have a child, and a 43 percent drop in having sex against their will among program participants, in 2 years. In addition, fertility decline also tends to be associated with a decline in infant and child mortality rates because as the number of births per woman falls, maternal and child health outcomes improve. Investment in girls' education, laws promoting gender equality, large-scale use of contraceptives, effective communication campaigns, and improvements in health services are crucial to reduce fertility.

5.42. **However, fertility choices are rooted in social and cultural norms and will take time to change.** Nevertheless, efforts at reducing fertility need to be accelerated because it is a big drain on the limited resources of Uganda. Bangladesh managed to achieve a spectacular decline in fertility rate from 6.3 births per woman in 1975 to 2.3 in 2011 (box 5.4).

Box 5.5. Bangladesh's Success in Reducing Fertility

Bangladesh managed to achieve a spectacular decline in fertility rate from 6.3 births per woman in 1975 to 2.3 in 2011. Fertility decline in Bangladesh was accompanied by sharp reductions in infant and child mortality and an increase in life expectancy.

The key driver of fertility decline was an aggressive and supply-driven family planning program which provided doorstep delivery of contraceptives along with improved family planning service delivery. As a result, contraceptive prevalence in Bangladesh increased from 8 percent in 1975 to 61 percent in 2011.

Source: Bangladesh Poverty Assessment (World Bank 2013a).

F. REGIONAL PEACE AND SOCIAL SUSTAINABILITY

The main risks to social sustainability arise from the lower level of assets among households in Northern Uganda, fewer opportunities for income generation, influx of refugees, and the large youth population coupled with a limited number of jobs.

5.43. Systematic exclusion of certain groups from the growth process can exacerbate the divide within the population. Although Northern Uganda has been enjoying relative peace and stability after decades of conflict, there are elements of fragility that are rooted in the societal dynamics and other drivers of conflict. Several communities are still in a state of latent conflict, often driven by new and long-standing grievances, poverty, perception of marginalization, competition over national resources, and societal fracture as a result of the legacies of the decades of violent conflict. This violence created vulnerable groups (like orphaned children, widows, ex-child soldiers, unemployed youth, internally displaced persons, returnees, and those born in captivity in Lord's Resistance Army (LRA) hideouts who have limited access to public services and limited assets.

5.44. The high levels of poverty and youth unemployment pose particular political, economic, and social challenges to peacebuilding in Northern Uganda. A large percent of the population in Northern Uganda is currently under 18 years of age, with limited or no education and skills (International Alert 2008). Over 80 percent of youth in Northern Uganda have limited employment opportunities in the formal sector due to low qualification levels. Traditional subsistence farming is unfamiliar to many young people who have grown up in the camps. Others have mainly military experience, having been either abducted by the LRA or recruited into local militias by the government. Youth have very limited access to and control over key assets, including land and physical and human capital (Advisory Consortium on Conflict Sensitivity (ACCS) 2013). In addition, land disputes are pervasive in Northern Uganda, making up roughly 94 percent of the cases before local courts. This aggravates the risk of future armed conflicts as young people are unable to secure an income and become an easy target for recruitment into armed rebellion. The inability of the youth to fully benefit from the economic opportunities in Northern Uganda reinforces economic marginalization (International Alert 2008). In addition, the presence of disenfranchised youth, many former combatants, with high illiteracy rates, and no hope for a future, turning to crime and antisocial behavior drives conflict by increasing insecurity in communities (Advisory Consortium on Conflict Sensitivity (ACCS) 2013).

5.45. Compared to the rest of the country, Karamoja still suffers disproportionately from insecurity. For decades, it has suffered high levels of conflict and insecurity, alongside low levels of development and serious challenges to individual well-being. Apart from being affected at certain points by the conflict between the LRA and the GoU, groups living in Karamoja have also been involved in cycles of cattle raiding and counter raiding. At various times, pastoralist or semi-pastoralist groups living across the border in Kenya and South Sudan have also actively participated in these attacks (Saferworld 2010).

5.46. A large influx of refugees, over the years, has led to conflicts between the host communities and the refugees. As a result of ongoing conflicts and instability in the Democratic Republic of Congo, Somalia, and South Sudan, Uganda is currently hosting over 420,000 refugees and asylum seekers making it the third largest refugee-hosting country in Africa. Of the total,

188,000 are Congolese mainly hosted in Southwest and Midwest Uganda, and 154,000 South Sudanese mainly hosted in Adjumani, Arua, and Kiryandongo districts. Uganda has a generous and progressive refugee policy framework. The 2006 Refugee Act and 2010 Refugee Regulations entitle refugees to work, to move freely, and to access social services, including access to documents such as government IDs, and birth, death, marriage, and education certificates. Refugees in the southwestern part of Uganda reside in gazetted settlements and are provided with a subsistence agriculture plot, albeit of diminishing size due to overcrowding. On the other hand, most of the South Sudanese refugees in northern and northwestern Uganda are accommodated in settlements on communally-owned land and are provided with a little more than a small kitchen garden. Refugees can own property and enter into contracts including land leases. However, refugee communities typically suffer from lower agricultural productivity and greater environmental degradation due to poor climatic and soil conditions and/or overuse. Their access to basic social and infrastructure services is also limited because of remoteness. The presence of a large number of refugees has its own economic, social, and environmental impacts on the host communities and has contributed to conflict between the refugees and host communities.

5.47. Uganda's youth, who are on average better educated than their parents, can pose a challenge to social stability if they are not productively employed, especially in urban areas where inequalities are bigger and more visible. As described earlier, Uganda will see a rapid increase in its workforce from 20 million to over 60 million between 2015 and 2060. With universal primary education access and improvements in secondary and tertiary enrollments, this young workforce is likely to be better educated than the previous generations and will therefore demand better economic opportunities. If such expectations are not managed efficiently, they can be a potential source of social instability.

6. PRIORITY AREAS FOR ACTION

A. SUMMARY OF KEY CHALLENGES

6.1. **Since returning to peace and stability in the mid-1980s, Uganda has made important progress by adopting more market-oriented policies and implementing a range of courageous reforms that have contributed to achieving and sustaining macroeconomic stability.** Uganda has dramatically reduced poverty and improved its human development indicators over the last two decades.

6.2. **However, a large number of Ugandans are still living in extreme poverty—and what is of even greater concern is the proportion of the population which is vulnerable.** Still many Ugandans are living on subsistence farming or dependent on small enterprises with very low productivity that provide incomes that are dangerously close to the poverty line. Many vulnerable groups are exposed to extreme shocks whose impact is exacerbated by a very weak social protection system in the country.

6.3. **The growth and transformation challenge for Uganda is embodied in the fact that the proportion of the population employed with formal small and medium enterprises and in large enterprises is growing far too slowly to provide enough productive opportunities for the fast-growing labor force.** Moreover, the productivity performance of formal firms continues to decline (it went down by 19 percent between 2001 and 2010). The vast majority of Ugandans remain employed in low-productivity subsistence agriculture or in unskilled services that do not provide sufficient income to climb the ladder of economic empowerment. Every year more than 300,000 Ugandans graduate from universities and technical colleges, only to end up in low-productivity and low-paying jobs.

6.4. **Uganda's economy needs to become more productive and more diversified.** At the same time, growth needs to be more inclusive if Uganda is to make progress on the twin goals. The SCD's diagnosis shows that Uganda will not move to the next level of the development ladder without addressing constraints to (a) capitalizing on emerging and prospective drivers of growth, notably oil, regional integration, ICT, and urbanization; (b) inclusion of all its citizens in the development process—including in the lagging regions; and (c) ensuring sustainable management of its human, financial, institutional, and natural resources. The growth model for most of the last twenty years reliant on consumption underpinned by government spending, has reached its limits. The economy needs to create more productive jobs and improve the business environment for a more vibrant private sector to invest and create new businesses.

6.5. **The strategies prepared by the government and the plans to further reduce poverty and accelerate inclusive growth have been generally sound.** However, there is a widening implementation gap that is leading to a deterioration of public services to the general population. For example, the government has rightly placed infrastructure and education at the center of its strategy but overall spending per primary school student remains below the average in LICs. This may explain low completion rates and poor quality of services with a large proportion of children unable to read or write correctly when they graduate from primary schools. Shortcomings in PIM impede delivery of infrastructure, which is central to the government's strategy.

6.6. **The main challenges faced by Uganda in the areas of growth, inclusion and sustainability are summarized in table 6.1.** These challenges have been identified in the preceding chapters and come from the existing evidence base and analytical work on Uganda. The challenges listed represent a streamlining of the pervasive constraints discussed in the preceding chapters.

Table 6.1. Summary of Constraints on Growth, Inclusion, and Sustainability Facing Uganda

Area	Challenge
Growth	<ul style="list-style-type: none"> • Expanding power generation capacity and investment in the electricity grid network • Increasing maintenance expenditures for the national road network, investing in the northern trade corridor, and developing multimodal connectivity around Lake Victoria • Addressing climate risks including for infrastructure • Increasing low-cost access to finance for firms, including long-term finance • Improving tax administration • Reducing nontariff barriers in trade • Improving the urban policy and legal framework, land tenure system and markets, housing availability, and institutional capacity • Addressing risks associated with the extractives sector • Increasing the ICT backbone infrastructure • Increasing women's participation in the labor market
Services for Inclusion	<ul style="list-style-type: none"> • Scaling up and sustaining health interventions in HIV/AIDS, malaria, and maternal and child health • Improving public health services, particularly in the north and east of the country, by increasing input availability, reducing absenteeism, and improving infrastructure • Improving primary and secondary education by targeting underserved areas, reducing the cost of education to households, reforming teacher education and incentive structures, and improving the curriculum, as well as introducing early childhood education/preschool to improve learner readiness • Improving the relevance of and enrollment to vocational education programs to address the skills shortage • Increasing household access to electricity by addressing the affordability of connection drops from the electricity distribution grid • Improving access to and quality of water supply and sanitation • Improving district and rural roads and urban public transport • Improving land dispute resolution, national rate of land registration, land administration services, and landownership by women • Increasing access to credit and financial services, particularly, savings instruments for individuals • Increasing the coverage and targeting of social safety nets • Improving agricultural water management (for crops, fishery, and livestock), storage, and agricultural extension services, particularly in the north and the east
Social and Institutional Sustainability	<ul style="list-style-type: none"> • Preventing further land degradation, deforestation, and over fishing • Improving and preventing further urban pollution • Increasing domestic revenue generation • Strengthening the allocative and financial efficiency of the budget, implementing clear and transparent PFM rules, and strengthening PIM

Area	Challenge
	<ul style="list-style-type: none"> Improving accountability at the central level by strengthening the functioning of the sanctioning authorities Improving accountability and horizontal equity at the local level through changes in the intergovernmental fiscal transfers and enhancement of own-source revenues of LGs Enhancing the provision of family planning services and the use of contraceptives

B. PRIORITIZING AMONG CONSTRAINTS

6.7. There are several binding constraints facing a poor, infrastructure-deficit, and landlocked country with low educational attainment, a high disease burden, and weak institutions. These constraints coupled with a limited resource base make it imperative for the government to prioritize its interventions. The prioritization of constraints in this SCD is primarily based on the impact of the constraints on the twin goals of reducing poverty and boosting shared prosperity. This is, however, not a recommendation to the government to abandon ongoing or new efforts in the non-priority areas.

6.8. The prioritization process included a review of the evidence, consultations with stakeholders in Uganda, and team discussions. The starting point for the prioritization process was the evidence and analysis presented in the report. This was used to identify the key challenges in the growth, inclusion, and sustainability domains. A first round of consultations was held with the government, academia, CSOs, and the private sector on the main constraints and opportunities facing Uganda (annex 2). The team then used informed judgment to prioritize the constraints. A second round of consultations was also held with the stakeholders during which most of the identified constraints were reinforced. The priorities reflected in the SCD represent the collective judgment of the team which has significant institutional memory on Uganda and the process is more an art than a science. These priorities are also reinforced by the existing evidence base and analytical studies (annex 6).

6.9. The prioritization process resulted in the identification of eight priority areas which are summarized in table 6.2. The proposed priorities are mainly based on their linkages with the poverty story and the need to ensure continued progress on the twin goals in the future. These priorities are in the area of (a) macro-fiscal stability, (b) agricultural productivity and commercialization, (c) consumption smoothing, (d) public service delivery, (e) urbanization, (f) fertility reduction, (g) private sector competitiveness and diversification, and (h) public sector effectiveness. Under each of these priority areas a set of actions was also proposed.

Table 6.2. Priorities Areas and Proposed Actions (Not Ranked in Any Order of Importance)

Priority Areas	Proposed Actions
Macro-fiscal stability	<ul style="list-style-type: none"> Improving domestic revenue mobilization and tax administration Strengthening the allocative and financial efficiency of the budget by implementing clear and transparent PFM rules, strengthening PIM and procurement, and encouraging PPPs to enable delivery of critical services Strengthening debt management to ring fence rising commercial borrowing and the burden of debt-service

	<ul style="list-style-type: none"> • Build awareness of the need for highly resilient fiscal institutions ahead of the onset of oil revenues
Agricultural productivity and commercialization	<ul style="list-style-type: none"> • Improving land and water management (for crops, fishing, and livestock) in a sustainable manner • Improving agricultural storage facilities. • Strengthening extension services, particularly in the north and the east • Increasing the use of quality agricultural inputs • Improving rural feeder roads, particularly in the north, to reduce input costs and increase market access • Increasing agricultural access to finance • Strengthening land tenure security, rental markets, and institutions for land administration • Reversing and preventing further land degradation, deforestation, and over fishing • Addressing challenges of climate variability and change
Consumption smoothing	<ul style="list-style-type: none"> • Strengthening the social protection system • Increasing access to credit and financial services, particularly, savings instruments for individuals and through secure landownership to increase access to collateral-based credit
Public service delivery	<ul style="list-style-type: none"> • Increasing public health and education expenditures with efficiency improvements • Increasing access to social and infrastructure services for the bottom 40 percent and for the people in the north and the east of the country • Improving the quality of public services (education, health, water supply and sanitation, electricity, roads, and the Internet) by addressing sector-specific challenges • Improving the demand side of good governance by promoting the voice and accountability of citizens
Urbanization	<ul style="list-style-type: none"> • Improving the urban policy and legal framework, land tenure system and markets, housing availability, and institutional capacity • Strengthening urban public transport • Preventing urban pollution
Fertility reduction	<ul style="list-style-type: none"> • Enhancing the provision of family planning services and the use of contraceptives
Private sector competitiveness and diversification	<ul style="list-style-type: none"> • Increasing low-cost access to finance for firms, including long-term finance • Reducing administrative costs associated with taxes, land, buildings, construction permits, border crossings, and basic infrastructure • Improving land markets by reducing the cost of transferring land • Increasing maintenance expenditures for the national road network, investing in the northern trade corridor, and developing multimodal connectivity around Lake Victoria

	<ul style="list-style-type: none"> • Expanding electricity generation, access, and usage and improving reliability and access to ICT through expanding the NBI • Improving district and rural roads • Promoting technical and vocational training through partnerships and targeted programs for youth and women • Increasing women's participation in the labor market • Enhancing skills for and around the oil sector and in other productive sectors such as tourism
Public sector effectiveness	<ul style="list-style-type: none"> • Instilling a delivery focus through an open and participative monitoring, evaluation, and de-bottlenecking process which draws on external inputs • Strengthening sanction mechanisms by consolidating fiduciary management systems and reinforcing central-level institution' accountability • Improving LG accountability and horizontal equity at the local level through strengthening of the intergovernmental fiscal transfer and enhancement of own-source revenues of LGs • Continuing to build specialized capacity for the oil sector

C. CONCLUDING REMARKS AND KNOWLEDGE GAPS

6.7. **The proposed eight areas of priority pathways are derived from the analysis presented in this report and the significant amount of knowledge on Uganda accumulated over the years.** It is also important that these priorities are flexible enough so they can be adapted as new knowledge emerges during implementation.⁴⁹

6.8. **Mentioned below are some of the knowledge gaps that emerged during the SCD process.** These gaps can be filled through future advisory services and analytics work.

- (a) **Informality in Uganda.** Most of the poor and those in the bottom 40 percent work in the informal sector. However, very little is known about the informal sector in Uganda beyond anecdotal evidence.
- (b) **Malnutrition and income levels.** While Uganda has made some progress, malnutrition is higher in the richer regions of central and western Uganda. The issue needs to be analyzed further and appropriate programs may need to be developed.
- (c) **Attitudes.** It will be useful to understand better the disincentives to work that poor people face and what can be done about it.
- (d) **Agricultural statistics.** The agricultural sector is crucial to achieve progress on the twin goals and there is considerable room to improve agricultural statistics.

⁴⁹ Flexibility and adaptability can be built on the approach sketched out by Matt Andrews, Lant Pritchett, and Michael Woolcock, "Problem-Driven Iterative Adaptation", Kennedy School, Harvard.

- (e) **Value chain analysis for specific sectors.** This can include growth sectors (identified, for example, by a product space analysis or similar studies) to help address market and coordination failures and to prioritize investments.
- (f) **Climate variability and change.** The current and future climate represent risks (and opportunities) for planning, designing, and implementation. There is a need to identify and incorporate appropriate methodologies for addressing these risks.

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ANNEXES

Annex 1: Data on the Spatial Dimensions of Poverty

Table A1: Access to Markets and Services, and Use of Assets

	Central	Eastern	Northern	Western
<i>Access to markets and services</i>				
Proportion of communities in which the following are available:				
Primary school (public or private)	80.8	56.6	31.4	54.8
Health clinic or center (public or private)	27.8	17.3	12.7	17.8
Agricultural extension	12.1	26.4	13.2	34.2
Veterinary services	12.9	15.7	3.6	10.3
Market for selling agricultural produce	7.4	15.8	4.8	11.0
Bank or financial institution	3.4	5.5	0.1	5.8
<i>Use and return to assets</i>				
Median monthly nominal wages (UGX)	170,000	77,000	66,000	110,000
Underemployed (%)	11.7	7.3	11.8	5.5
Underpaid* (%)	7.4	18.5	23.1	14.6

Source: Uganda Bureau of Statistics (UBOS, 2013). Report on the UNHS 2012/13 * Earning less than two-third of the average monthly wage.

Figure A1: Income of the Bottom 40 Percent, By Region



Source: Uganda Poverty Assessment using UNPS.

Annex 2: Summary of Consultations with Stakeholders

Introduction

Uganda's economic and socioeconomic progress over the last three decades represent a mixed bag of positives and negatives. While growth has averaged 6 percent over the last two decades and poverty has more than halved from 56.4 percent in 1992 to 19.7 percent in 2013, the level of vulnerability at 43.3 percent in 2013 was still high. Besides, between 2005 and 2006, more than 60 percent of the people who had moved out of poverty fell back. Furthermore, poverty by international standards of US\$1.25 a day is relatively high at 30 percent. On the social and human capital development aspects, while enrollment rates increased from 65 percent in 1995 to 86 percent in 2013 and the percentage of underweight children below the age of five reduced from 25.5 percent to 13.8 percent, overall service delivery remains a daunting challenge. Absenteeism of staff in public facilities (education and health) remains high as the facilities themselves lack basic ingredients like drugs, water, and electricity.

Realities like those described above, point to non-inclusive growth and hence is difficult to sustain as it is bound to not only lack local momentum but also lead to social and political tensions related to lack of shared prosperity. The benefiting class will want to capture more of the national assets and opportunities such as land, education, and employment/business to keep the momentum. The changing ownership of the basics of economic production pose a threat of accelerating inequality, which, in Uganda, has increased over the last two decades as shown by the deterioration of the Gini coefficient from 0.36 in 1993 to 0.40 in 2013.

Objectives of the Consultation

Resolution of the current state and realization of the twin goals of ending extreme poverty by 2030 and increasing shared prosperity called for fulfilment of the following two objectives.

- (a) Obtain a detailed diagnosis and hence explain the dilemma of a mixed bag of good and bad results.
- (b) Adopt a new thinking that will help prescribe reforms for a better future.

Approach of the Consultation

To meet the two objectives, a two-pronged strategy was adopted. First, there was a need to analyze available data as well as compile evidence from existing reports to get a clear description of the current state of development outcomes. This process provided an initial SCD report that set a basis for the stakeholder consultation. The consultation formed the second part of the strategy.

The Bank engaged in consultations with a large and diverse group of stakeholders during March and April 2015.⁵⁰ The consultation too, had two main related objectives: (a) to obtain an explanation of what people thought was responsible for the observed outcomes, and (b) what will be the drivers of shared and inclusive growth going forward.

⁵⁰ The stakeholders included government officials (both political and technical) at the central government and LG levels, private sector, civil society, communities at the grassroots, and donors.

To get candid objective opinions, the stakeholders were engaged in separate meetings, whenever possible, in a manner that allowed for progressive appreciation of the development aspects. For example, engagement began with the political and technical teams involved in the planning and design of programs for certain specific objectives. This was followed by donors and CSOs who monitor results from an independent view and finally the communities which are the direct beneficiaries of the outcomes.

The selection of LGs was informed by the need to address the social, cultural, and development diversities in the country. For example, Buliisa and Kotido are in hard-to-reach areas with poor infrastructure, limited development, and yet with great opportunities and potential for the future. The two districts also reflect the effect of cultural orientations on development as most of the people are inclined to a non-diversified source of livelihood.

In northern Uganda, Gulu District and Municipality and Kotido District in the northwest were selected to represent a post-conflict situation. In this region, the recovery and reconstruction efforts may have contributed to the mixed results. Significant financial injections have been made through Northern Uganda Social Action Fund (NUSAF) I&II, Northern Uganda Reconstruction Programme (NURP), and now Peace Recovery and Development Plan (PRDP). Based on the interviews and physical observations, it is inferred that though poverty has declined, both welfare and vulnerability have not improved..

Two other areas of Bushenyi (in the west) and Mbale (in the east), represented areas, which have had peace over the last three decades, are highly accessible in terms of infrastructure, and have relatively high levels of education and social amenities. However, these districts also portray a need for new approaches to the development process given the numerous socioeconomic problems identified during the consultations.

Findings

To ease the reading, the findings have been analyzed in selected thematic areas under the following two broad categories: explanation for the observed development outcome and possible drivers of future growth. The themes range from strong government and governance through cultural attitudes and individual mindset.

Explanations of Past Performance

Participants were asked to share their views on what they considered to be the most outstanding three/four things that have been responsible for past progress in the country. This subsection presents a synthesized summary of the responses.

The Positives

- (a) **Improved transport infrastructure especially trunk and feeders roads.** Most areas of the country have become accessible albeit with considerable difficulty in a few places. The road network has improved greatly over the last three decades rendering rural agricultural places fairly accessible to traders of both outputs and inputs.

- (b) **Commercialization of agricultural products that were traditionally meant for local food consumption.** In addition to commercialization of crops such as maize and beans and revival of the livestock sector, there has been an introduction of new high-value crops like oil seeds and upland rice; poultry; and piggery among others. The increase in urbanization and the opening up of regional food and livestock markets in South Sudan, Rwanda, and Eastern Democratic Republic of Congo have facilitated the growth trend.
- (c) **The peace dividend across the country and more recently in northern Uganda has a lot to explain about the growth.** The relatively high level of peace and security compared to the period before 1986, and 2006 in the case of northern Uganda, has enabled households and communities to focus on long-term asset-building and development activities. These include: education, adoption of new farming technologies, improvements in housing, and other productive investments in transport and communication sectors. The massive private sector investments in education, health, trade, and housing have increased the scope of opportunities for the general public to tap into the development process.
- (d) **The large financial resources including donor support contributed to general service infrastructure that increased access to basic social services.** Access to education, health, and water facilities has increased despite the lingering challenges of quality and consistency. Decentralization contributed toward distribution of resources to rural and previously remote areas but was largely unable to deliver the required levels and quality of public services. The weak governance and associated corruption were reported as great contributors to unequal distribution of quality services and impact.

The Negatives

- (a) **There was a general lack of adequate focus on development challenges in rural areas.** It would appear that most of the development rhetoric and planning was based on high-level ideas such as macroeconomic stability; big infrastructure projects such as roads, irrigation, and rural electrification; and privatization and liberalization of markets. Yet, local-level development is hampered by big knowledge gaps, limited access to critical finance, intense poverty levels, limited relevant skills, and ineffective markets. Participants argued that the policy framework neglects specific regional and cultural characteristics of land tenure and related conflicts, inadequate local personnel required for service delivery, chronic poverty, and limited diversification of economic opportunities. For example, in Buliisa and Kotido, communities had spent decades depending on fishing and nomadic pastoralism, respectively. Furthermore, high-level quality education and health services are constrained differently and hence require various efforts across the country.
- (b) **Weak government and governance systems at both the national and local levels have undermined the development objectives.** Effective decentralization is an essential aspect of a rural development strategy that is capable of facilitating poverty reduction. A strong government, especially at the local level is necessary to fine-tune policies and invoke necessary bylaws to anchor the development process.

- (c) **Vulnerability among some groups or in certain areas needed special strategic interventions.** A number of households/communities needed strategic support to leverage the broad-level investments in infrastructure. Despite special programs for northern Uganda such as Northern Uganda Social Action Fund (NUSAF), Northern Uganda Reconstruction Programme (NURP), and Peace, Recovery and Development Plan for Northern Uganda (PRDP), many households failed and continue to fail to link up to the big government programs, in sectors like roads, markets, education, and health facilities.
- (d) **The poor still have limited resources and are voiceless in the light of weak and ineffective local institutional structures.** The years of civil strife and now continued politicization of the local development processes have undermined community leadership, sharing of opinions, and provision of guidance and insight, among others. Therefore, many local areas lack the civil and intellectual capacity required to implement development programs.
- (e) **Difficulties in establishing a homogenous and cohesive national and local sense of nationalism and unity.** Participants underscored that conflicts surrounding questions of cultural and tribal identity, nationality, and internal immigration existed. These had created divisions in society, partly based on a feeling of exclusion and marginalization, and had adversely affected social stability. Better governance, in particular, more equitable access to justice was essential to instilling a sense of homogeneity and cohesion in society.
- (f) **A difficult business environment related to inadequate infrastructure, poor access to financial services, and weak business management skills.** The difficult business environment across the country continues to undermine the birth and sustainable growth of both big industries and micro small and medium enterprises. While constraints exist across a number of areas, the most problematic areas concern the insecurity of land tenure and relations between the government and the private sector that have raised a lot of mistrust, access to finance, logistics, and lack of technically skilled labor. The development of micro small and medium enterprises—many with limited managerial and technical capacity—and the shortcomings in agricultural input chains have prevented progress in many rural areas.
- (g) **General apathy and resignation by communities has undermined innovation and instead fueled alcoholism and gambling/betting practices.** Many youth and older persons have resorted to non-development practices like selling of productive assets hoping for quick wins in urban areas—land for petty trade or motorcycle transport. While some have succeeded, many have fallen by the wayside indicating an increase in risky behavior and practices.

Recommendations of Drivers of Future Growth

- (a) **Reconstruction of the social, cultural, and psychological structures will be critical for leveraging the physical infrastructure.** The population needs to appreciate the logic of development as not only being the hardware in terms of physical infrastructure but also the individual personal drive toward success.

- (b) **Service delivery in the social sectors of education and health needs to improve by resolving ‘small’ but critical binding constraints.** These include remuneration and motivation of health workers, supervision of staff to eliminate absenteeism, and increasing the supply of basic services. Revival of health and school inspectors can go a long way to impart the necessary skills and focus on grassroots delivery of basic services by both the government and communities.
- (c) **Reviving effective governance across all levels of government will be critical for future development to deliver sustainable inclusive growth.** Local-level public institutions require realignment that is more focused toward actual and not hypothesized service delivery. The focus should be on better facilitation of service facilities such as schools and hospitals rather than on high-level meso-institutions such as district offices, which are supposed to supervise the delivery of social services.
- (d) **Provision of infrastructure remains critical but should be tailored and harmonized toward local conditions and solutions.** Provision of solar energy for lighting, feeder roads, and rain-water-harvesting facilities was seen as being more reliable, sustainable, and appropriate for most areas, the immediate needs of which included lighting, charging phones, news, and entertainment. The districts with power did not seem to have any significant difference in terms of development, despite power being available for many years. Over the medium term, the government should focus on the provision of basic infrastructure required to trigger sustainable and inclusive growth for the bottom 40 percent.
- (e) **Resolution of land tenure and management of proceeds from natural resources, mainly extractives, is key for inclusive growth.** Most of the population still lack skills and assets required to tap into the service sector and hence have to rely on primary growth from natural resources. The ownership of and access to land and sharing of associated wealth from natural resources, requires redress to strengthen both transparency and involvement of local communities in the receipt of benefits.
- (f) **Access to finance by the local communities is key and requires building of sustainable local financial institutions that are well-integrated into the national-level financial infrastructure.** The government and other stakeholders need to enhance systematic capacity building to enable growth and where possible, graduation of local financial institutions such as Village Savings and Loans Associations (VSLAs) and SACCOs to more effective and well-managed institutions. While the VSLAs and SACCOs are low cost in operation, they have limited ability to trigger greater traction needed to propel poor households into inclusive sustainable development.

Annex 3: CPIA Assessment

The CPIA of the Bank provides an assessment of the conduciveness of a country's policy and institutional framework, to poverty reduction, sustainable growth, and effectiveness in the use of development assistance. Its focus is on the key elements that are within the country's control. Countries are rated on a set of 16 criteria grouped into four clusters: (a) economic management; (b) structural policies; (c) policies for social inclusion and equity; and (d) public sector management and institutions. For each of the 16 criteria, countries are rated on a scale of 1 (low) to 6 (high).

Following a decline from its 2012 score of 3.8, Uganda's CPIA rating in 2014 remained steady at 3.7, the same as its 2013 score. The main difference between 2014 and 2013 was the improvements on the public sector management and institutions cluster, which increased from 3.0 to 3.1, mainly explained by improvements in the quality of budgetary and financial management (that is, from 3.0 to 3.5). However, this is not reflected in the overall score. Its highest score among the clusters is with regard to economic management and structural policies where it scores 4.2 and 4.0, respectively. Its relative policy weaknesses are in the areas of public sector management and institutions and policies for social inclusion/equity where it scores 3.1 and 3.7, respectively. Among the 16 specific criteria, Uganda scores the lowest on transparency, accountability, and corruption in the public sector (2.0) and the quality of public administration (3.0).

Table A2. Comparison of Uganda's CPIA Ratings, 2012–2014

No.	Question	CPIA 2012	CPIA 2013	CPIA 2014
1	Monetary and exchange rate policies	4.0	4.0	4.0
2	Fiscal policy	4.0	4.0	4.0
3	Debt policy and management.	4.5	4.5	4.5
Average	A. Economic management	4.2	4.2	4.2
4	Trade	4.5	4.5	4.5
5	Financial sector	3.5	3.5	3.5
6	Business regulatory environment	4.0	4.0	4.0
Average	B. Structural policies	4.0	4.0	4.0
7	Gender equality	3.5	3.5	3.5
8	Equity of public resource use	4.0	4.0	4.0
9	Building human resources	4.0	4.0	4.0
10	Social protection and labor	3.5	3.5	3.5
11	Policy and institutions for environmental sustainability	3.5	3.5	3.5
Average	C. Policy for social inclusion/equity	3.7	3.7	3.7
12	Property rights and rule-based governance	3.5	3.5	3.5
13	Quality of budgetary and financial management	3.5	3.0	3.5
14	Efficiency of revenue mobilization.	3.5	3.5	3.5
15	Quality of public administration	3.0	3.0	3.0
16	Transparency, accountability, and corruption in public sector	2.5	2.0	2.0
Average	D. Public sector management. and institution	3.2	3.0	3.1
	Overall CPIA	3.8	3.7	3.7

Annex 4: Public Financial Management

Uganda's PFM system is anchored in the recently enacted PFM Act, which includes among others, provisions on commitment controls, management of natural resource rents, and improvement in the budget preparation calendar. Effective PFM is also essential for the efficiency of service delivery and implementation of public projects, which will facilitate the proper planning, execution, and monitoring of the activities needed to bring about diversification and achieve the economic objectives of government. It also creates further fiscal space by reducing wasted resources and enabling better targeting of funds to where it is needed most and improving the value for money. Key aspects of a good PFM system include macrofiscal control and stability (macroeconomic management), budget planning and execution (including monitoring and evaluation), procurement, cash and debt management, financial systems and accounting, internal controls, and external oversight. Underpinning all PFM functions is required for an effective legal and regulatory framework and its implementation through individuals and their application of rules required for the systems to work effectively.

Uganda's performance in PFM is strong on transparency and weakest on budget credibility, controls, and compliance. As indicated by the PEFA assessment in 2012, performance is strongest in a comprehensive and open budget, public access to key fiscal information, transparency of tax payers' obligations and liabilities, maintaining a good accounting, recording, and reporting system, and the high quality and scope of external audits. Moreover, the Bank's CPIA assessment revealed that Uganda scores the lowest on transparency, accountability, and corruption in the public sector (2.0), quality of budget and financial management (3.0), and quality of public administration (3.0). Internationally, Uganda performs well in budget transparency, ranking 18 out of the 100 countries assessed across the world. PFM systems are the weakest however, in budget credibility, budget execution controls (particularly payroll), procurement compliance, and legislative scrutiny of external audit reports. On most of these aspects, Uganda performs below its East African neighbors. Indeed, the auditor general's annual reports of the government regularly identify weak compliance with PFM regulations, resulting in avoidable or wasteful expenditure, buildup of arrears, inadequate accountability, and, in some cases, the risk (or actual identification) of fraud or misappropriation. These challenges and the opportunities to address them are further outlined below.

Budget Planning, Execution, and Monitoring

Improving the quality and credibility of budget planning will help deliver national economic objectives and support effective service delivery and development projects. At the highest level of planning, the budget should be able to deliver national economic development objectives. Nonetheless, there is still significant divergence between the NDP and the sector allocations in the budgets, where in practice, security, public administration, justice, law and order, and interest payments tend to exceed those planned, at the expense of priority growth and social sectors. Furthermore, the Medium Term Expenditure Framework (MTEF) is, in principle, prepared on the basis of 5-year NDP priorities, including medium-term forecasts of revenue, grants, expenditure by sector, and financing. In practice, however, the MTEF is still revised at least annually, adjusting to changing economic conditions, uncertain forecasts, and under or over-execution of budgets.

The recently enacted PFM Act introduces a Contingencies Fund providing only for unforeseen, unavoidable, and urgent requirements without destabilizing other budgets. Nonetheless, part of the unpredictability of the annual budget is currently due to lack of internal controls (discussed below) and dependence on the approval of supplementary budget requests, resulting from weak controls and poor planning for expenditures such as utilities, taxes, and other recurrent costs. While the government's output-based planning system yields a lot of information on outputs linked to expenditure items, further monitoring and feedback is required to review the realism of cost estimates, take action to tackle arrears, establish unit costs, and develop a methodology for planning of recurrent cost implications of investment expenditures. Strengthening the linkage between immediate outputs and the required results (outcomes) at the sector level is needed to be able to assess the effectiveness as well as the efficiency of the budget. This should help make a stronger logical link between inputs, outputs, and actual results for growth and diversification, such as how to design activities and outputs that will contribute to improving agriculture productivity, education, and health performance and so on.

Cash and Debt Management

The introduction of the TSA arrangement should help promote greater transparency and regular accounts reconciliation and reduce the risk of misuse (for example, of dormant accounts), which have been a challenge in recent years. The TSA should also help facilitate a shift away from a cash rationing system to more active cash and debt management. Cash rationing has been a further cause (and result) of unpredictability in the budget, partly due to weak internal controls, but also from inaccuracy of expenditure and revenue forecasts, requiring budget cuts (through issuing cash limits) to pay for arising spending pressures through the fiscal year.

Attempts to break the cycle of excess recurrent spending and inadequate budget planning are improving timely releases and resisting supplementary requests. Releases in FY2013/14 and FY2014/15 have improved in timeliness and levels compared to planned and further improvements to cash management have been achieved through quarterly cash flow forecasts and issuance of quarterly ceilings to MDAs. Approved supplementary requests reduced to below 4 percent of the originally approved budget in FY2013/14. The capacity of the new Cash and Debt Management Directorate of MoFPED will need to be strengthened to develop better cash flow forecasts to realize the full benefits of the TSA framework.

Strengthening Control and Compliance in Fiduciary Systems

Oil revenues, drawn from the Oil Fund into the Consolidated Fund will, among other sources, finance the budget through the TSA arrangement. Under a TSA arrangement, the control of expenditures against budget allocations is primarily through the IFMS. While unspent balances are swept back into the main account for managing cash flows through the year, spending agencies can only spend up to their budget ceilings and on the items appropriated by the parliament and entered into the IFMS. To track expenditure and monitor budget execution, the IFMS needs to be able to generate customized reports to demonstrate that funds were spent for the purposes intended, even from funding sources that have specific conditions attached, for example, donor projects.

Furthermore, not all entities are yet operating through the IFMS and therefore not under the TSA. Excess expenditure can still be incurred through transactions undertaken outside the system and/or spending nontax revenues without authority. With only about 77 percent of expenditure going through the IFMS, there remains a gap in controls that can be exploited. Even within the IFMS, the recent Office of the Prime Minister (OPM) case highlighted a number of security issues that can lead to further fiduciary risks. Furthermore, there is evidence that some MDAs regularly mischarge expenditures to the wrong codes to spend outside the budgeted allocations without formal transfers. As noted in the auditor general's special investigation report on the OPM, more still needs to be done to address the existing lack of integration between the accounting and budgeting systems, which leads to weaknesses in control over the release of funds due to numerous manual interventions and lack of proper reconciliation. Payroll and pensions management pose some of the most significant risks of wastage, errors, delays, and even fraudulent financial losses, which are slowly being addressed, but with major delays. The government is committed to rolling out the IPPS, interfacing the IPPS with the IFMS, introducing biometric payroll records for civil servants as well as decentralization of the payroll to improve accountability.

The government, through the PFM reform program (FINMAP) and the Bank, is also committed to completing the rollout of the IFMS to all entities over the next 3–4 years. The information technology audit is also being stepped up to tackle system weaknesses, such as use of passwords, assignment of responsibilities, defense against cyberattacks, and so on. These issues are expected to be further addressed through the strengthened role of internal audit, which has been granted a directorate status in the new PFM Act and greater independence through direct reporting to the secretary to the Treasury. Along with this, there is a need to ensure that the rollouts of these fiduciary systems are being properly understood and implemented, through increased audit, monitoring, and review. This also requires stepping up change management training, sensitization, and communications to ensure responsibilities are understood, as well as more regular monitoring of their use and effective incentives and sanctions to improve compliance.

Public Procurement

Procurement in Uganda accounts for around 70 percent of all public expenditure and is critical to effective service delivery, but continues to suffer from poor practices. Unpredictable and late release of funds can lead to underspending or rushed spending at year-end, making procurement less competitive and more costly. This has been identified as one of the key constraints to the efficient absorption of available funds and the credibility of the budget. Furthermore, there is evidence of wastage within these contracts, including payment for goods or services not delivered. The quality of contract management is weak, there are regular breaches of procedure and unauthorized variations and only 21 percent of contracts have complete procurement records.

There is some evidence of improvement in the performance of contracts audited by PPDA, which rated 46 percent of contracts as satisfactory in FY2013 compared to 27 percent in 2011. Reforms to improve budget predictability and planning, as outlined above, should facilitate improved procurement practices, appear to be making progress. Nonetheless, these efforts need to be considerably strengthened and enforced more widely across the government to improve the overall effectiveness of procurement. There is a need to balance efficiency and simplicity of

processes with effective controls and transparency. The government is committed to enforcing bulk purchases and standardized unit costs to realize economies of scale, as well as enhancing institutional capacity for project-cycle management and is assessing the potential feasibility and benefits of introducing e-Procurement to enhance reporting and transparency. As with the effective integration of other fiduciary systems, to ensure proper implementation and compliance, an e-Procurement system should be interfaced or integrated with other systems, such as the IFMS and accompanied by appropriate change management to reap efficiency and compliance benefits.

Quality and Independence of Oversight

Reforms to enhance the independence of external audits appear to have been successful in improving the quality of audits produced by the OAG. The OAG was awarded the Swedish National Audit Office Prize for the Best Performance Audit Report 2011 and in 2013. Audit findings appear to be discussed more regularly in the press and other forums, including the parliament. However, the parliament still has a significant backlog of audit reports that do not receive adequate debate in the parliament and reports are not issued, creating a missing step in the accountability cycle that prevents the appropriate follow up with the executive taking place. Parliamentary processes need to be reviewed and streamlined for more efficient handling of audit reports through the parliament and the inter-institutional linkages between the OAG and its partners, such as investigation bodies and other regulators/auditors, for example, PPDA, need to be strengthened to improve coordination and the focus of reporting toward risk and impact.

Complementary Public Sector Management

In addition to developing the systems for PFM, it is also critical to ensure that individuals who operate systems and follow the rules and procedures understand their responsibilities and are able to carry out their functions effectively. There is therefore a need to invest in the capacity of public servants working in PFM functions for the effective administration of public finances, generally. Basic accounting, audit, cash management, procurement, monitoring, reporting, management, and supervision, among other skills, are needed to perform essential ongoing PFM functions and to be able to implement new reforms.

Furthermore, incentives and performance management frameworks, such as pay reform and performance appraisal need further consideration. While a number of public service reforms were implemented in the 1990s and the technical system investments in the IPPS will improve efficiency of financial management, public sector wages appear to have stagnated and are now low, compared to private sector equivalents and even by African standards. As a whole, the wage bill represents about 4 percent of GDP, compared to an average across Africa of about 6.5 percent for the central government and 9.8 percent for all governments. Furthermore, the PFM Act, provides for accounting officers to enter into an annual budget performance contract with the secretary to the Treasury, which should be binding on delivery of activities in the work plan of the vote for any financial year. If this is introduced, the government needs to ensure that this arrangement is effectively enforced.

Annex 5: Data Sources

Area	Data source
Growth	<ol style="list-style-type: none"> 1. National accounts (UBOS) 2. Fiscal and monetary information from Central Bank (Bank of Uganda) and Ministry of Finance databases 3. World Bank WDI 4. World Bank Commodities Prospect database 5. Census of business establishment (UBOS) 6. The Conference Board Total Economy Database (productivity) 7. Enterprise Survey 8. COMTRADE/WITS 9. Uganda Electricity Transmission Lines
Inclusion	<ol style="list-style-type: none"> 10. UNHS (1992/93–2012/13) 11. Uganda National Panel Survey (2006–12) 12. WDI 13. Human Development Index 14. PovCalNet database (2014) 15. WHO 16. SDIs 17. Global Findex database of financial inclusion
Sustainability	<ol style="list-style-type: none"> 18. IFPRI policy Reports 19. Transparency International (2013) 20. Global Integrity (2011) 21. UN Population Indicators 22. WDI 23. World Bank Natural Wealth Database (2005, 2010) 24. Uganda CPIA (2013) 25. Uganda PEFA (2012)

Annex 6: Selected Macroeconomic and Fiscal Indicators

	2012/13	2013/14	2014/15	2010/11– 2014/15	2015/16– 2019/20	2020/21– 2024/25
			Est.	Average Annual Est. NDP1	Average Annual Proj. NDP2	Average Annual Proj. NDP3
National Income and Prices						
Real GDP growth (%)	3.3	4.5	5.0	5.4	7.8	10.3
Real Non-petrol GDP growth (%)	3.3	4.5	5.0	5.4	7.3	9.7
GDP per capita (US\$)	731	781	798	721	937	1,540
GDP deflator (%)	4.1	2.4	3.9	7.2	5.7	7.5
National Accounts (% of nominal GDP)						
Gross domestic saving	21.5	20.6	19.1	20.0	31.9	26.2
Gross public investment	6.7	6.6	4.9	7.8	10.7	15.4
Gross private investment	22.4	21.9	23.1	21.5	28.4	21.2
Public Sector (% of nominal GDP)						
Domestic non-petrol revenue	11.5	11.9	12.5	11.5	14.1	14.3
Petrol revenue	0.0	0.0	0.0	0.6	0.3	2.8
Grants	1.5	1.0	1.4	1.5	0.8	0.4
Total expenditure and net lending	16.5	16.7	18.4	17.4	19.1	20.6
Fiscal balance including grants and petrol revenue	-3.5	-3.8	-4.5	-3.6	-3.8	-3.0
Balance of Payments (% of nominal GDP)						
Trade balance	-10.3	-9.7	-10.2	-11.6	-9.2	-7.1
Current account balance including grants	-7.6	-7.9	-8.9	-7.5	-7.2	-10.4
Monetary Sector (% of nominal GDP)						
Money and quasi-money	14.0	14.9	16.3	15.1	17.9	19.6
Foreign Reserves and Debt (% of nominal GDP)						
Gross foreign reserves (months of imports)	4.4	4.9	4.3	4.3	3.7	3.6
Public debt	26.2	28.9	31.9	27.3	44.6	–

Source: World Bank; MacMod-UG, Ministry of Finance.

Annex 7: Evidence Supporting the Priority Areas and Proposed Actions

Roads:

- **Estache et al. (2012).** Computable General Equilibrium (CGE) simulations indicate that a 1 percent increase in road investment funded by reduction of other public spending, leads to a GDP increase of 0.21 percent and household welfare increase of 0.16 percent.
- **Uganda Poverty Assessment 2015.** Reductions in the distance to the nearest input market by 1 km increased crop income for the bottom 40 percent by 1 percent.
- **Gollin and Rogerson (Static General Equilibrium Model).** The effect of a 10 percent reduction in transportation costs has half the impact on welfare as a 10 percent increase in agricultural TFP. At any given moment in time, the price that spreads across markets for a given commodity are substantial and high transport costs drive this. The gap between the second highest price and the second lowest price averaged 10 percent of the minimum price in the United States, compared with 27 percent of the minimum price for Uganda, despite the distances being much larger in the United States. Unit transport costs in Uganda are estimated to be 4–7 times the unit transport costs in the United States.
- **CEM 2007.** Identified the poor road network as one of the key constraints to growth.
- **Global Competitiveness Report of 2015.** Ranks inadequate infrastructure as the fourth leading constraint.
- **Uganda 5th Economic Update.** The special section on urbanization also notes the importance of urban public transportation to provide connectivity to the poor.
- **Tsimpo and Wodon (2014)** argue that the bottom 40 percent households rank district and rural roads among social and infrastructure services of poor quality.

Urbanization:

- Uganda's urbanization at 15 percent is below that of the average LICs and SSA countries.
- **Uganda 5th Economic Update.** Provides evidence of the importance of accelerated urbanization for Uganda's socioeconomic transformation.
- **Dorosh and Thurlow.** Investing in southern urban centers to harness agglomeration effects accelerate national growth, but has little effect on other regions' welfare because of weak growth linkages and small migration effects.
- **Uganda Poverty Assessment 2015.** Until now, migration has had a limited impact on poverty reduction, despite the substantial consumption growth that accompanies migration when it occurs. Stronger migration linkages are needed. Those that migrate from rural areas to urban areas see a 37.5 percent increase in consumption. This is very similar to the increase in consumption found for rural to urban migration in Tanzania by Beegle et al.

(2011) using a similar method. However, the impact on poverty of rural to urban migration is smaller as those that migrate from rural to urban areas are less poor to begin with (O’Sullivan and Mensah for the Uganda Poverty Assessment).

Fiscal:

- **Matovu et al. (2014) and Agenor et al. (2014)** find that improved efficiency in public sector spending leads to higher GDP growth. Improving public expenditure efficiency by a yearly average of 10.5 percent will result in an average 0.25 percentage point improvement in GDP growth rates.
- **Dabla et al. (2012)** reported that Uganda ranks 46th out of 71 countries in the IMF’s PIMI, with relatively poor scores in project implementation and evaluation.
- **The 2013 Business Enterprise Survey and the 2015 Global Competitiveness Report** identified tax rates among the top 3 constraints.
- The fiscal slippages in the recent past which resulted in a significant decline in aid from donors was the result of weak PFM.

Health:

- The incidence of Malaria and HIV/AIDS in Uganda is higher than other countries with a similar GNI per capita.
- **Alderman et al. (2008)**. Improvement of child health and nutrition of poor children has been regarded as an efficient way of improving school attendance.
- **Dillon et al. (2014)**. According to them, malaria testing and treatment increases earnings of poor households by 10 percent following a mobile clinic visit in Nigeria.
- Among the countries in East Africa, Uganda has the second-lowest life expectancy at birth, second-highest total fertility, and highest prevalence of HIV/AIDS.

Education:

- **Hanushek and Woessmann (2008)**. An increase of one standard deviation in student scores on international assessments of literacy and mathematics is associated with a 2 percent increase in annual GDP per capita growth.
- **Uganda Poverty Assessment 2015**. Completing primary education increases agricultural earnings by 10 percent. Younger, more educated households are more likely to increase their income from nonagricultural sources. Education is more strongly correlated with increases in wage income than with increases in self-employment income. Individuals with higher levels of education are more likely to be employed and receive higher returns when they are employed. This is particularly true among the poorest. The distinguishing feature

of households in the bottom 40 percent that are able to transition into wage employment is their higher levels of education.

- **Barr et al. (2012).** Participatory community monitoring interventions increased schooling quality in Uganda. It reduced pupil and teacher absenteeism by 8.9 and 13.2 percent, respectively. As a result, pupils' test scores increased by 0.19 standard deviations.
- **Gakidou et al. (2010).** It is estimated that of the 8.2 million fewer deaths of children younger than 5 years between 1970 and 2009, one-half can be attributed to more education among women of reproductive age.
- The Ugandan population, 25 years and above, has an average of 4.7 years of schooling while women have only 3.8 years of schooling.

Fertility:

- At 6.2 children per woman, Uganda has one of the highest fertility rates in the world.
- **Bangladesh Poverty Assessment 2012.** Bangladesh managed to achieve a spectacular decline in fertility rate from 6.3 births per woman in 1975 to 2.3 in 2011. The key driver of fertility decline was an aggressive and supply-driven family planning program which provided doorstep delivery of contraceptives along with improved family planning service delivery.
- Contraceptive use is slowly picking up, but unmet need for family planning still stands at 34.4 percent.

Agriculture:

- **Dorosh and Thurlow (2012), and Government of Uganda (2014).** Simulations using Uganda's Social Accounting Matrix show that agricultural growth has a larger impact on poverty reduction than an equal amount of growth in other sectors.
- **Uganda Poverty Assessment.** Agricultural income growth contributed more to poverty reduction than growth in other sources of income. The elasticity of poverty reduction with respect to agricultural growth is stronger than the elasticity with respect to other sources of growth. Of the 1.7 annual percentage point reduction in poverty from 2010 to 2013, 1.3 took place among agricultural households.
- **Gollin and Rogerson.** A 10 percent increase in agricultural productivity led to a welfare increase of more than 30 percent. When combined with a 10 percent reduction in the cost of transporting goods (as a result of investments in roads) welfare increased by 77 percent.
- Agricultural growth rate in Uganda was less than 2 percent per year over the past five years which is well below the 4 percent agricultural growth rate achieved by the continent as a whole.

- The output per agricultural worker is only 13 percent of that of workers in the rest of the economy.

Accountability:

- **World Governance Indicators 2014.** On the control of corruption, Uganda is in the 14th percentile; on political stability and absence of violence, it is in the 20th percentile; and in voice and accountability, it is in the 31st percentile.
- **Transparency International's Global Corruption Barometer Survey (2013).** This survey found that 61 percent of Ugandans had paid a bribe to one of the eight institutions (judiciary, education, tax services and customs, permits/registries, medical services, police, land services, or utilities) in the last 12 months.
- **Global Integrity 2011.** Uganda has one of the biggest implementation gaps when it comes to anticorruption legislation in East Africa.
- **Freedom House 2014.** Uganda's ranking in freedom of the press showed a decline from 104 to 110 from 2012 to 2013.
- **Public Expenditure Review 2013.** According to the review, improving service delivery at the local level will require changes in intergovernmental fiscal transfers as well as own-source revenues of LGs.