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EBS/84/7

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January 16, 1984

To: Members of the Executive Board

From: The Secretary

Subject: Uganda - Staff Report for the 1983 Article IV Consultation and Review of Stand-By Arrangement

Attached for consideration by the Executive Directors is the staff report for the 1983 Article IV consultation with Uganda and a review under the stand-by arrangement. Draft decisions appear on pages 26 and 27.

This subject will be brought to the agenda of the Executive Board for discussion on a date to be announced.

If Executive Directors have technical or factual questions relating to this paper prior to the Board discussion, they should contact Mr. Basu, ext. 76542, Mr. Callender, ext. 73397, or Mr. Ebrahim-zadeh, ext. 73739.

Att: (1)

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INTERNATIONAL MONETARY FUND

UGANDA

Staff Report for the 1983 Article IV Consultation and Review of Stand-By Arrangement

Prepared by the African Department and the Exchange and Trade Relations Department

(In consultation with the Fiscal Affairs, Legal, and Treasurer's Departments)

Approved by L.M. Goreux and W.A. Beveridge

January 16, 1984

I. Introduction

A Fund mission visited Kampala during the period October 31-November 13, 1983 to conduct the 1983 Article IV consultation discussions and review Uganda's performance under the financial program supported by the current one-year stand-by arrangement ending September 15, 1984. The Ugandan representatives included Ambassador E. Kamuntu of the Ministry of Finance; Mr. S. Odaka, Minister of Planning and Economic Development; Mr. L. Kibirango, Governor of the Bank of Uganda (BOU); and other senior officials of ministries and agencies concerned with economic and financial matters. The mission also met with His Excellency Milton Obote, President and Minister of Finance. The staff team consisted of Messrs. A. Basu (head-AFR), C.V. Callender (AFR), C. Sisson (FAD), Z. Ebrahimzadeh (AFR), J. Hicklin (ETR), and Mrs. C.A.S. Gardiner (secretary-STAT). The mission was assisted by Mr. E. Martey, the Fund's Resident Representative in Uganda.

The current stand-by arrangement, which was approved by the Executive Board on September 16, 1983, provides for a total amount of SDR 95 million (126.7 percent of present quota or 95.4 percent of proposed new quota) (Table 1). So far, Uganda has made two purchases totaling SDR 44 million under the current arrangement. The remaining amount of SDR 51 million would be available in three further purchases after satisfactory completion of the mid-term review with the Fund in February 1984 and subject to observance of performance criteria for end-December 1983 and end-March 1984 and the understandings regarding the dual exchange rate system.

The Fund holdings of Uganda's currency subject to repurchase, excluding the special facilities, amounted to SDR 275.50 million (367.4 percent of quota) at end-November, 1983. If the purchases under

Table 1. Uganda: Actual and Proposed Purchases and Repurchases During the Period January 1, 1984-September 30, 1984

	1984			Total
	Jan. 1- March 31	April 1- June 30	July 1- Sept. 30	Jan. 1, 1984- Sept. 30, 1984
	(In millions of SDRs)			
Purchases	21.00	15.00	15.00	51.00
Ordinary	--	--	--	--
Borrowed	21.00	15.00	15.00	51.00
CFF	--	--	--	--
Repurchases	4.05	5.31	13.37	22.73
Oil facility	--	--	--	--
CFF	3.75	3.75	9.38	16.88
Stand-by	0.30	1.56	3.99	5.85
Of which:				
regular	(0.30)	(1.56)	(3.99)	(5.85)
enlarged access	(--)	(--)	(--)	(--)
Repurchases of Fund's holdings of national currency in excess of 75 percent of quota	--	--	--	--
Net purchases	16.95	9.69	1.63	28.27
Outstanding Fund credit	354.95	364.64	366.27	366.27
	(As percent of new quota)			
Outstanding Fund credit	356.38	366.10	367.76	367.74
Of which: CFF	59.04	55.32	45.88	45.88

Source: Data provided by the Treasurer's Department.

the current stand-by arrangement were fully utilized, these holdings would increase to SDR 320.57 million, or 427.4 percent of present quota and 321.9 percent of the proposed quota by end-September 1984.

Uganda has benefited from extensive technical assistance from the Fund in several areas. Currently, a member of the FAD panel of fiscal experts (Mr. Thompson) is assigned as Budget Advisor to the Ministry of Finance and five CBD experts are attached to the Bank of Uganda: Director of Foreign Exchange Operations Department (Mr. Abdul Rahman), Director of Research (Mr. Vollan), Chief Accountant (Mr. Lindsay), Head of External Debt Management Office (Mr. Bourke), and Advisor for Bank Supervision and Development Finance (Mr. Bhagavat). Furthermore, in September 1983 a BUR technical assistance mission visited Uganda to study the accounts of the banking system, and between August and October 1983 two FAD technical assistance missions visited Uganda to review the tax system.

A World Bank mission visited Uganda in October 1983 to review the implementation of the second IDA reconstruction credit (US$75 million) and to initiate discussions on a third IDA reconstruction credit (US$50 million). The World Bank will chair a Consultative Group meeting of donor countries scheduled for January 25 and 26, 1984.

Uganda continues to avail itself of the transitional arrangements of Article XIV. A summary of Uganda's relations with the Fund is presented in Appendix I, and tables on World Bank lending operations and on selected economic and financial data are contained in Appendix II.

II. Background

For a decade up to May 1981 the Ugandan economy had suffered the consequences of economic and financial mismanagement, a war, and a virtual breakdown of law and order. The volume of exports and per capita real GDP had fallen dramatically. The annual increase in the cost of living had reached more than 100 percent. As a result of widespread price controls, the domestic prices of essential goods and services had become divorced from economic realities. In the nation's enterprises the productive apparatus was largely destroyed. In the public sector, financial discipline had broken down, and government expenditures were financed by heavy recourse to bank credit. A cumbersome network of restrictions had sharply reduced the inflow of essential imports. A substantial amount of external payments arrears was accumulated. In reality, the economy functioned through a widespread network of parallel markets for both goods and foreign exchange, with foreign exchange being sold at 30 times the official exchange rate. To steer the economy out of this chaotic situation, since May 1981 dramatic changes have been made in economic and financial policies with the implementation of three successive financial programs supported by stand-by arrangements with stand-by arrangements with the Fund. 1/ The Government also made serious efforts to improve the internal security situation.

The adjustment process was started with a 90 percent devaluation of the exchange rate in June 1981. As a result of this and further depreciation during fiscal year 1981/82, 2/ the exchange rate was moved from U Sh 7.8 per U.S. dollar in May 1981 to U Sh 96 per U.S. dollar by end-June 1982. The ratio of the parallel to the official exchange rates declined from about 30 at the beginning of June 1981 to 3.6 at the end of June 1982. Although foreign exchange receipts responded vigorously and the scope of parallel market operations narrowed as a result of the large depreciation of the exchange rate, in August 1982 a temporary and flexible dual exchange system was introduced to improve the mechanism for foreign exchange allocation (especially to the private sector), to eliminate the parallel market, and to determine (within an agreed timetable) an equilibrium exchange rate in a unified regime. To this end, in November 1982 several technical measures were taken to improve the functioning of the second window auctions. Between August 1982 and June 1983 there was a rising trend in the weekly sales of foreign exchange at the second window, a further decrease in the ratio between the two official exchange rates from three to two, and a continued decrease in the differential between the parallel market and second window rates.

Over the past two fiscal years 1981/82-1982/83 with the sizable and continued exchange rate depreciations, more flexible price policies were adopted (including large increases in agricultural producers' prices and retail prices of petroleum products), and exchange control regulations were substantially liberalized. Moreover, fiscal and domestic credit policies were characterized by much greater restraint and discipline, and government expenditure policies were oriented toward investments that supported the recovery of agricultural output and exports and the rehabilitation of the nation's productive enterprises. As a result the progress made toward economic and financial recovery was impressive. After recording a declining trend over several years, during 1981/82-1982/83 exports grew at an annual average rate of 23 percent, and the annual growth rate of real GDP averaged 7 percent. The budgetary deficit, which was equivalent to 2.3 percent of GDP in 1982/83 compared with the program's target of 1.6 percent, was lower than in the previous two years. The bank financing component of the fiscal deficit was also reduced. As a ratio of GDP, the current account deficit was lower

1/ The financial programs covered the periods from May 1, 1981 to June 30, 1982; from July 1, 1982 to June 30, 1983; and from July 1, 1983 to June 30, 1984.

2/ Fiscal year ends on June 30.

than programmed, and the overall BOP deficit narrowed substantially to a level well below the program target. The domestic rate of inflation was also cut by three-fourths to less than 30 percent (Table 2 and Chart 1). 1/ Moreover, following the introduction of the new policies, Uganda obtained significant amounts of debt relief through the Paris Club (in November 1981 and December 1982) and was able to mobilize additional foreign assistance.

III. Report on the discussions

The current program for 1983/84 is designed within a medium-term scenario that foresees a continued improvement in the balance of payments along with a minimum recovery of domestic production and investment. With present projections of annual growth in exports (at least 8 percent) and in grants (14 percent), imports would increase by about 7 percent annually and the external current account deficit would decline progressively. As net capital inflows are forecast to increase by 9 percent annually, the overall BOP deficit would be cut by more than one half in 1983/84 and turned into a surplus in the following years (Table 3). However, even with the large foreign aid inflows, there would be financing gaps (averaging about US$55 million) during the next three years, especially on account of a sharp rise in repurchase obligations to the Fund.

The 1983/84 financial program's initial objectives were an increase of about 5-7 percent in real GDP (as against 10 percent in 1982/83), a reduction in the domestic inflation rate from 25-30 percent to 20-25 per cent, a narrowing of the overall BOP deficit from US$71 million to US$ 34 million, a decrease in external arrears through cash payments by a net amount of at least US$20 million, and an increase in gross official reserves of US$15 million. In formulating the external objectives, it was assumed that Uganda would approach the Paris Club to request an estimated debt relief of US$15 million in fiscal year 1983/84. However, at the time of the mid-term review, it became clear that pending the legal settlement of certain claims on Uganda, the Paris Club would not consider Uganda's request for debt relief.

In view of the pressing need for substantial external adjustment in the medium term and the uncertainties regarding debt relief, the Ugandan authorities decided to aim at a better performance than the program's external objectives for 1983/84. Hence, the program now includes an additional package of measures to reduce the external current account deficit by an amount somewhat larger than the program's estimate of debt

1/ Performance under the 1981/82 and 1982/83 financial programs was discussed in detail in EBS/83/85, dated January 10, 1983 and EBS/83/80, dated August 31, 1983.

Table 2. Uganda: Selected Economic and Financial Indicators, 1980/81-1983/84

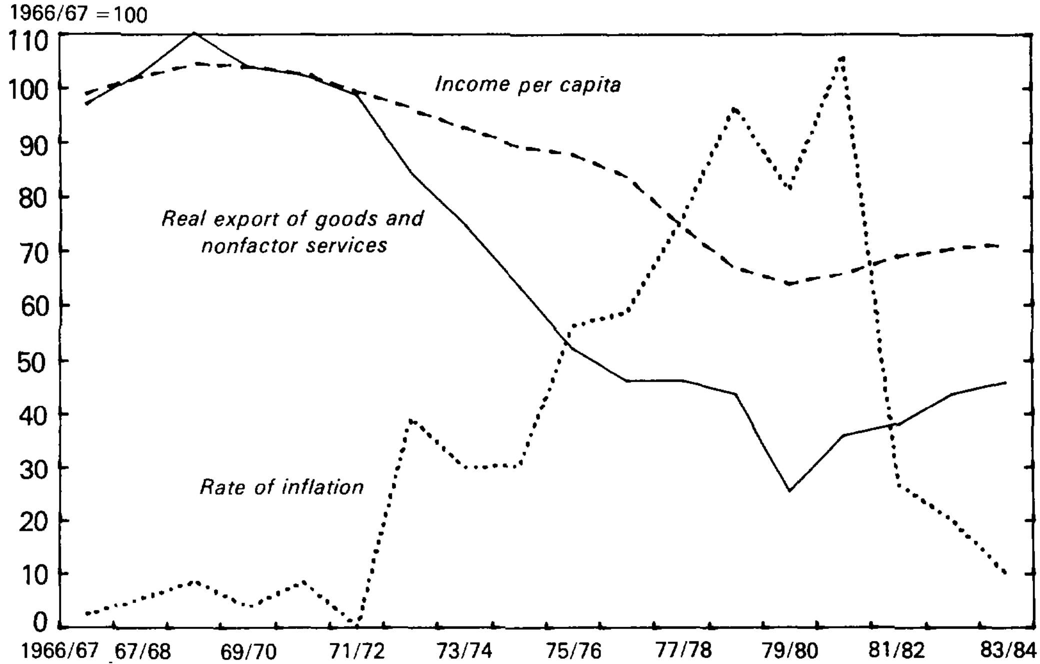
	1980/81	1981/82 1/		1982/83		1983/84	
	Actual	Program	Actual	Program	Prel. actuals	Program	Estimate
			(Annual percent changes, unless otherwise specified)				
National income and prices							
GDP at constant prices	-8.4	9-10	6	10	8	5-7	5
Consumer prices (annual average)	81	22	106	25	27	20-25	20
External sector (on the basis of U.S. dollars)							
Exports, f.o.b.	-30	62	38	24	7	15	20
Imports, c.i.f.	-16	33	2	38	0	20	18
Non-oil imports, c.i.f.	...	...	14	48	-7	32	26
Export volume	-42	60	45	26	5	10	15
Import volume	-7	25	5	20	3	16	15
Terms of trade (deterioration -)	-7	-5	-3	-8	5	...	2
Nominal effective exchange rate (depreciation -)	-28	...	-86	...	-26 2/	...	...
Real effective exchange rate (depreciation -)	9	...	-76	...	-11 2/	...	...
Government budget							
Revenue (excluding grants)	-28	802 2/	804	80	114	46	...
Revenue (including grants)	-15	732 2/	746	64	89	60	...
Total expenditure	64	155	250	29	58	38	...
Money and credit							
Domestic credit	62	...	82	33	44	28	...
Government	81	...	63	6	34	11	...
Private sector	20	...	144	79	67	54	...
Money and quasi-money (M2)	50	...	62	23	39	24	...
Velocity (GDP relative to M2)	27	...	20	24	21	24	...
Interest rate (annual rate, one year savings deposit)	6	...	12	13	13	15	...
			(In percent of GDP) 3/				
Central government budget deficit	6.3	0.9	2.8	1.6	2.3	1.5	...
Domestic bank financing	5.4	1.1	1.9	0.2	1.2	0.2	...
Foreign financing (net)	0.3	-0.2	0.1	1.3	0.4	1.2	...
Current account deficit 4/	1.6	2.6	1.6	2.5	1.6	2.6	...
External debt							
Exclusive of use of Fund credit	2.6	...	16.1	12.0	12.0	17.0	...
Debt service ratio 5/	40.0	47.0	45.5	26.0	31.7	34.0	42.6
Interest payments 5/	4.0	...	5.8	7.0	8.5	9.2	...
			(In millions of U.S. dollars)				
Overall balance of payments 6/	-132	-142	-187	-82	-77	-34	-19
External payments arrears (at end of period)	204 7/	160	157	73	78	30	58
Gross reserves (end of period)	108	...	43	...	52	75	...

1/ Converted to 12-month basis.
2/ Window I rate.
3/ The following ratios should be treated with caution owing to the highly tentative nature of the GDP estimates.
4/ Includes grants. Current account deficit reflects severe constraint on foreign exchange availability.
5/ In percent of exports of goods and services and including debt services to IMF.
6/ Overall balance reflects severe constraint on foreign exchange availability.
7/ End-May 1981.

CHART 1

UGANDA

INDICES OF REAL INCOME PER CAPITA AND VOLUME OF EXPORTS, ANNUAL RATE OF INFLATION AND BALANCE OF PAYMENTS STRUCTURE



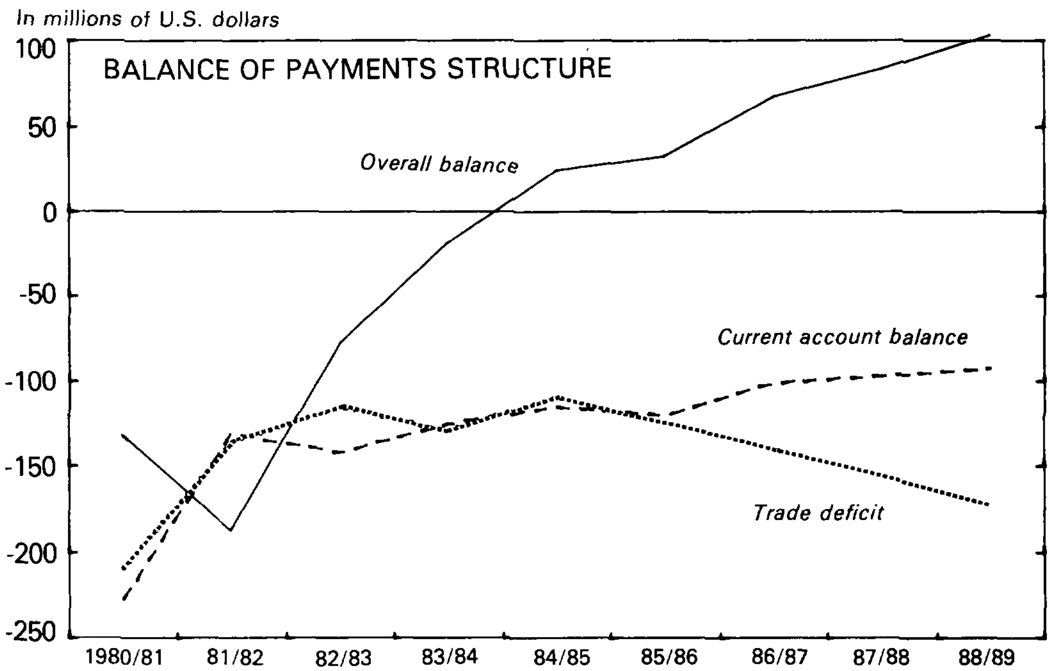


Table 3. Uganda: Balance of Payments, 1980/81-1988/89

(In millions of U.S. dollars)

	1980/81	1981/82	1982/83	1983/84 1/ Program	1983/84 1/ Revised	1984/85 1/	1985/86	1986/87	1987/88	1988/89
Trade balance	-209	-136	-115	-151	-129	-114	-125	-140	-145	-158
Exports, f.o.b.	(213)	(294)	(316)	(371)	(380)	(419)	(448)	(479)	(520)	(575)
Imports, c.i.f.	(-422)	(-430)	(-431)	(-522)	(-509)	(-533)	(-573)	(-619)	(-665)	(-733)
Services (net)	-83	-75	-84	-78	-69	-77	-78	-70	-66	-62
Unrequited transfers	65	80	57	73	73	85	105	130	137	140
Current account	-227	-131	-142	-156	-125	-106	-98	-80	-74	-80
Debt cancellation	7	69	--	--	--	--	--	--	--	--
Capital account	81	-125	64	122	106	126	138	137	144	162
Official inflows	118	168	251	213	198	190	195	195	195	195
Of which:										
rescheduling of amortization	(--)	(32)	(40)	(15)	(--)	(--)	(--)	(--)	(--)	(--)
rescheduling of arrears	(--)	(63)	(48)	(--)	(--)	(--)	(--)	(--)	(--)	(--)
Official outflows	-94	-264	-142	-89	-89	-69	-65	-68	-66	-53
Principal payments	(-87)	(-100)	(-54)	(-74)	(-89)	(-69)	(-65)	(-68)	(-66)	(-53)
Principal rescheduled	(--)	(-32)	(-40)	(-15)	(--)	(--)	(--)	(--)	(--)	(--)
Arrears rescheduled	(--)	(-63)	(-48)	(--)	(--)	(--)	(--)	(--)	(--)	(--)
Principal and arrears canceled	(-7)	(-69)	(--)	(--)	(--)	(--)	(--)	(--)	(--)	(--)
Private (net)	57	-29	-44	-2	-2	5	8	10	15	20
SDR allocation	7	--	--	--	--	--	--	--	--	--
Overall balance	-132	-187	-77	-34	-19	20	40	57	70	82
Financing	132	187	77	34	19	-20	-40	-57	-70	-82
External arrears 2/	91	47	-17	-20	-20	-30	-28	--	--	--
Monetary authorities	41	140	93	54	39	-64	-82	-78	-70	-82
Change in gross reserves	(-54)	(63)	(-9)	(-15)	(-23)	(-6)	(-4)	(-10)	(-4)	(-24)
IMF (net)	(67)	(73)	(118)	(86)	(79)	(-58)	(-78)	(-68)	(-66)	(-58)
Other (net)	(28)	(4)	(-16)	(-17)	(-17)	(--)	(--)	(--)	(--)	(--)
Financing gap	--	--	--	--	--	74 3/	70 3/	21 3/	--	--

Sources: Bank of Uganda; and staff estimates.

1/ The last purchase of SDR 15 million under the 1983/84 arrangement is shown in 1983/84, although it is expected to be made in early July 1984.

2/ Minus sign denotes arrears reduction through cash payments.

3/ With no further use of Fund resources, a continuation of the auctioning of foreign exchange would imply a closing of the financing 'gaps.' Adjustment would most likely fall on imports bought through the auction market.

relief. The policies designed to steer the economy in this direction are contained in the President's letter and accompanying policy memorandum (Attachments I and II) and are discussed below by reviewing successively external policies and exchange arrangements; production and price policies, and the operations of parastatals; government finance; and domestic credit and interest rate policies.

1. External policies and exchange arrangements

At the outset of the 1983/84 financial program, special efforts were made to progress towards a unified exchange rate system. To this end, in June 1983 the transactions at the first window, to which a lower exchange rate is applied, were narrowed by shifting all non-oil cash imports, service payments on newly contracted debt, and all exports other than coffee and cotton to the second window. The lower first window rate remained applicable for servicing the outstanding external debt, imports of petroleum products, and imports tied to aid financing (such as those under the second IDA reconstruction credit). All remaining transactions were conducted through the second window at a more depreciated (auction determined) rate. Furthermore, new measures were taken to improve the functioning of the auction system. Despite these measures, in early 1983/84 the foreign exchange cash flow situation was expected to be tight during the first quarter, due to a temporary delay in coffee export proceeds. To tide over this situation, early in that quarter the Ugandan authorities mobilized an external (cash) loan of US$20 million through the Bank of Uganda, 1/ and in addition, arranged to obtain an advance payment for the forward sale of 19,000 metric tons of coffee (for a total value of US$38.7 million). Consequently, a substantial amount of official reserves (US$77.4 million) was accumulated. This was achieved in full compliance with the program's performance criterion of maintaining an average of at least US$3 million of foreign exchange sales per week at the second window (as compared with US$2 million in 1982/83).

Between the first auction (on July 8) of the program period and December 16, 1983, the auction determined second window rate, which had fluctuated between U Sh 270 and U Sh 340 per U.S. dollar, recorded an overall depreciation of about 10 percent, and the officially controlled first window rate was depreciated by 47 percent. As a result, the ratio of the second window rate to that at the first window continued to decline (from 1.85 to 1.28). Moreover, the gap between the second window rate (presently U Sh 300 per U.S. dollar) and the parallel market rate is

1/ In November 1983, the cash loan of US$20 million was fully repaid and there was no other nonconcessional foreign borrowing in the maturity of 0-12 years.

believed to have further narrowed. 1/ The scope of parallel transactions is also reported to have been reduced primarily to some capital outflows.

In real effective terms, although the domestic inflation rate was much higher than Uganda's trading partners, the first window rate depreciated by 15 percent between end-August 1982 and end-June 1983; over the following five months, it depreciated further by 30 percent. However, at the second window, where the auction-determined nominal rate fluctuated without a persistent trend, the real effective rate appreciated by 17 perpercent between August 1982 and November 1983 (Chart 2). On a weighted basis, the real cost of foreign exchange has been rising, mainly because of the progressive shift of transactions from the first to the second window and the continued depreciation of the first window rate.

Along with continued progress toward a unified exchange rate, the Ugandan authorities are now commited to reducing the 1983/84 BOP deficit from the program target of US$34 million to US$19 million (as compared with a recorded overall deficit of US$77 million in 1982/83). To achieve this additional adjustment, the external current account deficit is to be limited to US$125 million (2.4 percent of GDP), which is US$31 million lower than the original program target and about 12 per percent less than the 1982/83 deficit. The newly targeted decline in the 1983/84 current account deficit represents a reversal from the small increase that had been earlier programmed.

In 1983/84 the required adjustment in the external current account is to be achieved mainly through a reduction of US$11.5 million in imports channelled through the second window, but also partly through a projected increase of US$9 million in cash export earnings above the originally programmed levels (Table 4). With these estimates of trade flows, the Bank of Uganda would still be able to sell an average of at least US$ 3 million per week during the program period, in accordance with the original performance criterion for such sales. Notwithstanding the reduction in second window sales of foreign exchange, the overall level of imports would still be about 18 percent higher than the preceding year because of a targeted increase in foreign aid financed imports under the ongoing recovery program. The higher than programmed growth of exports is forecast as a result of a third round of substantial increases in agricultural producers' prices and significant improvements in the marketing system (see section 2 below). With this evolution of foreign trade, in 1983/84 the trade deficit would increase much less sharply than had been earlier programmed.

1/ The exchange rate in the parallel market is reported to be about U Sh 350 per U.S. dollar.

Table 4. Uganda: Foreign Exchange Cash Flow, 1982/83-1983/84

(In millions of U.S. dollars)

	1982/83 1/	1983		1984		1983/84 2/
	Total	Q3	Q4	Q1	Q2	Total
A. Inflows	444.5	182.8	82.7	105.5	114.6	485.6
1. Window 1	427.1	176.5	72.7	92.5	101.6	443.3
Coffee exports	(302.8)	(118.2)	(57.6)	(67.5)	(82.8)	(326.1)
Cotton exports	(1.7)	(2.4)	(2.0)	(3.0)	(3.0)	(10.4)
BOU loans	(122.6)	(53.2)	(13.1)	(22.0)	(15.8)	(104.1)
Unutilized cover returned	(--)	(2.7)	(--)	(--)	(--)	(2.7)
2. Window 2	17.4	6.3	10.0	13.0	13.0	42.3
Exports	(1.9)	(1.4)	(4.0)	(6.0)	(6.0)	(17.4)
Services	(15.5)	(4.8)	(6.0)	(7.0)	(7.0)	(24.8)
Unutilized cover returned	(--)	(0.1)	(--)	(--)	(--)	(0.1)
B. Outflows	433.0	107.5	147.5	114.0	105.7	474.7
1. Window 1	332.8	65.6	107.8	71.6	62.7	307.7
Oil imports	(115.6)	(18.5)	(34.0)	(26.8)	(26.8)	(106.1)
Costs related to exports	(16.3)	(5.0)	(3.4)	(--)	(--)	(8.4)
BOU debt service	(41.4)	(12.6)	(35.8)	(20.9)	(12.0)	(81.3)
Official debt service	(56.6)	(19.1)	(27.2)	(17.8)	(17.8)	(81.9)
Cash arrears reduction)	(61.1)	(8.8)	(1.2)	(5.0)	(5.0)	(20.0)
L/Cs payments)		(1.6)	(6.2)	(1.1)	(1.1)	(10.0)
Non-oil imports	(29.6)	(--)	(--)	(--)	(--)	(--)
Services	(12.2)	(--)	(--)	(--)	(--)	(--)
2. Window 2	100.2	41.9	39.7	42.4	43.0	167.0
Imports	(56.7)	(31.1)	(29.9)	(31.5)	(32.0)	(124.5)
Services	(43.5)	(10.8)	(9.8)	(10.9)	(11.0)	(42.5)
C. Net inflows (A-B)	11.5	75.3	-64.8	-8.5	8.9	10.9
Memorandum items:						
Gross reserves (end-period)	38.1	115.5	48.6	40.1	49.0	49.0
Change in reserves	8.8	77.4	-66.9	-8.5	8.9	10.9
Other	2.7	-2.1	2.1	--	--	

Sources: Bank of Uganda; and staff estimates.

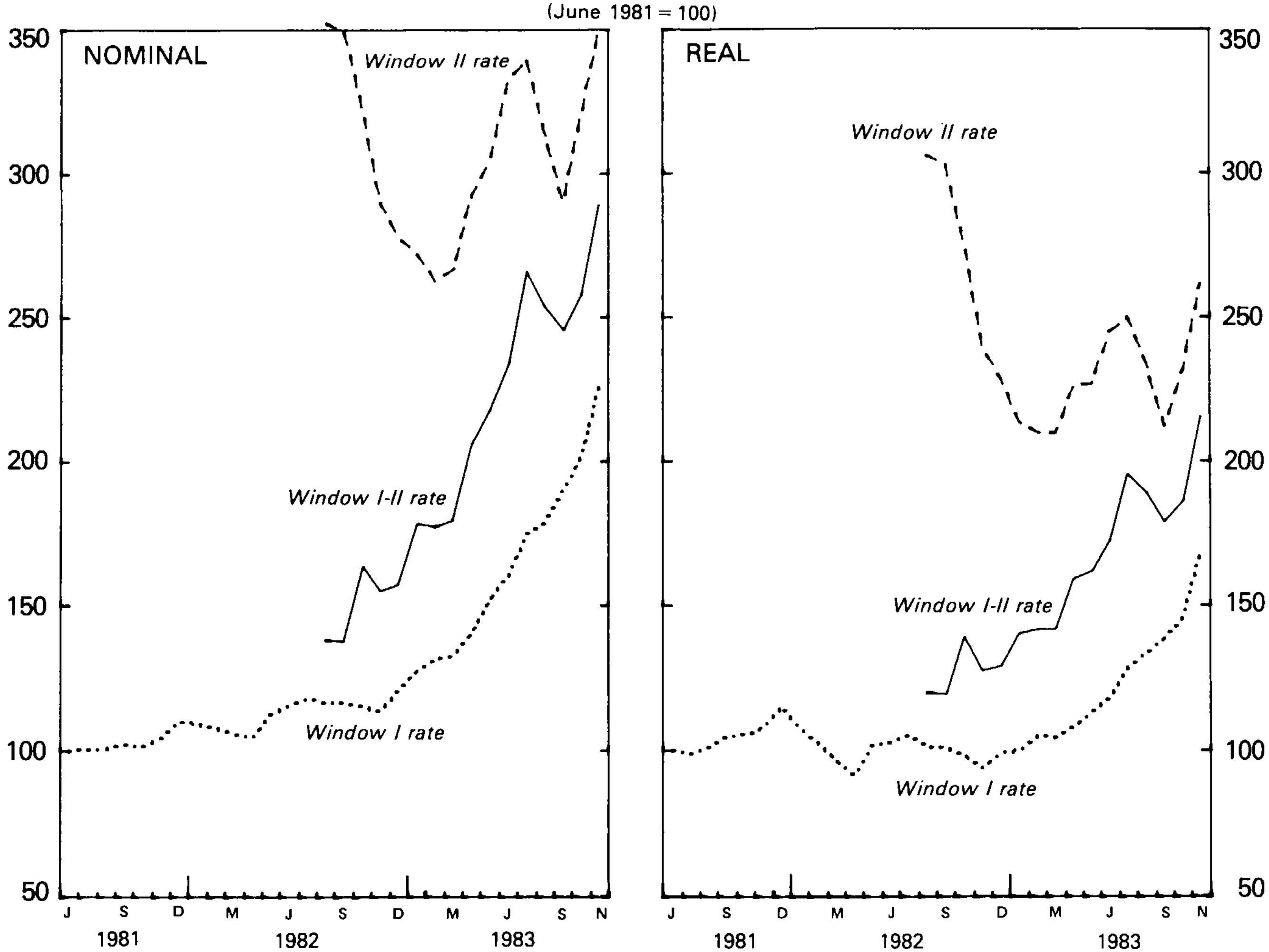
1/ Provisional estimates.
2/ Assumes SDR 1 = US$1.05.

CHART 2

UGANDA

IMPORT WEIGHTED REAL AND NOMINAL EFFECTIVE EXCHANGE RATES, JUN. 1981 - NOV. 1983

(June 1981 = 100)



With the anticipated reduction in foreign exchange sales at the second window, the Ugandan authorities recognize that the second window rate would tend to further depreciate beyond what had been initially expected. At the same time, the Ugandan authorities believe it important to increase the second window's coverage of private sector demand for cash imports as far as possible. Thus, the Government will be reducing its share in the second window sales from an average of 30 percent per quarter to 25 per cent per quarter (with no more than 30 percent per week in any two-week period). Nongovernment sales at the second window outside the auction will be kept to a minimum. Also, effective January 1, 1984, the cash imports of goods and services that are made by the Coffee Marketing Board and the Lint Marketing Board for their own operations, and those made by the oil companies except for gasoline (super and regular), diesel fuel, and kerosene, will all be transferred from the first to the second window. Furthermore, in view of the more depreciated rates expected at the second window, the Ugandan authorities have agreed to depreciate the rate at the first window more rapidly than hitherto, in order to move in a determined manner toward a unified exchange system. This is expected to minimize the possible misallocation of resources that could result from a dual exchange system.

The existing dual exchange market involves the continuation of a multiple currency practice, for which temporary approval was granted by the Executive Board in September 1983. Although existing restrictions were relaxed in August 1982 at the time of the introduction of the dual exchange market, foreign exchange restrictions still exist on travel and all remittances except profit, dividend, and interest payments. In addition, arrears remain outstanding on current transactions; their elimination is subject to performance criteria (discussed in Section IV below). However, since the last consultation in 1982, Uganda has not introduced or intensified its exchange and import restrictions and multiple currency practices. Uganda maintains no bilateral payments agreements.

The staff stressed the importance of continued avoidance of new exchange control restrictions. The Ugandan authorities indicated that they will continue to rely on the existing system, under which bona fide requests for import licenses are granted expeditiously and bids for foreign exchange that are properly supported by domestic bank credit or own cash resources are allowed to be presented freely at the second window auctions. However, they remained concerned about the need to curb nonessential imports and eliminate leakages of export proceeds. In order to discourage nonessential imports, the authorities have already made some efforts to tighten customs administration, but indicated that they are looking forward to the report of the last FAD technical assistance mission for recommended improvements in both the administration and structure of customs taxes. To prevent leakages in export proceeds, the authorities will be ensuring a stricter surveillance of export operations, especially those of the Coffee Marketing Board.

Over the 1982/83 fiscal year the level of outstanding arrears had declined by US$78.9 million to US$78.3 million, primarily through rescheduling. In the first quarter of 1983/84 (June to September) the cash reduction of arrears amounted to US$8.8 million, as compared with a programmed amount of US$10 million for the six months (June to December). During 1983/84 the Ugandan authorities remain committed to reducing the outstanding external arrears through cash payments by a net amount of at least US$20 million. They plan to eliminate the remaining arrears (about US$60 million) 1/ by 1985/86.

At the end of June 1983, Uganda's external medium- and long-term public debt (disbursed) totaled US$650 million, the bulk of which has been contracted on highly concessional terms. Largely on account of the interest and charges, and repurchase obligations to the Fund, Uganda's debt service burden (estimated on the basis of existing and anticipated commitments 2/) is projected to remain close to an average of about 43 percent of exports during 1983/84-1986/87 before declining to around 27 percent in 1988/89. 3/ In view of this situation, the authorities will be following prudent borrowing policies by strictly limiting non-concessional borrowing to ceilings that are lower than those for the first half of the program period. An External Debt Management Office has been established in the Bank of Uganda, and a Borrowing Committee will be set up by January 1, 1984 to review all proposed loans. Data on the outstanding debt and on related service payments will be surveyed comprehensively and will, henceforth, be maintained on a current basis. All foreign borrowing will be subjected to prior authorization by the Ministry of Finance and the Bank of Uganda, and all potential lenders and borrowers will be advised that unauthorized debts will not be honored.

The mission inquired about the progress made in resolving the legal problems associated with Uganda's debts to Israel. The Ugandan representatives indicated that they had authorized a foreign consultant firm (Messrs. Morgan Grenfell & Co.) to set up a technical working party to make an independent examination of the legal validity of Israel's claims. A part of Israel's claims (about US$10 million) is sub judice, and the technical working party's major preliminary conclusion is that the legal validity of all of the remaining claims is in doubt. Moreover, the authorities have identified counterclaims against Israel (totalling U Sh 78 million) arising from Israel's outstanding indebtedness to the Ugandan private sector.

1/ This includes some old arrears that were newly discovered (US$18 million).
2/ From sources other than the Fund.
3/ External debt service statistics are contained in Appendix Table VI.

2. Production and price policies

The recovery of the economy over the past two years was led by a strong performance in the export sector. Both coffee and, more recently, noncoffee exports have shown encouraging signs of recovery. To a large extent this was the result of timely and significant increases in the minimum producer prices of the major agricultural exports (Appendix Table II). As on earlier occasions, the program for 1983/84 included substantial increases in the producer prices for coffee (60 percent), cotton (50 percent), tea (150 percent), tobacco (50 percent), and cocoa (300 percent). With the intention of providing an additional stimulus to the process of export growth and diversification, effective mid-February 1984 the Government has decided to implement another round of sizable increases in the producers' prices of the major export crops: coffee (25 percent), cotton (50 percent), tea (60 percent), tobacco (33 percent), and cocoa (63 percent).

Under the current program the Government will also be taking steps to increase the efficiency of the marketing process in the export sector. In the coffee sector the Government will encourage competition among private and union processors, and the cooperative unions will be urged to negotiate their credit needs directly with the commercial banks without the backing of a guarantee from the Coffee Marketing Board. In the cotton sector the Lint Marketing Board will be required to concentrate mainly on export operations, and the ginneries will be encouraged to negotiate their credit requirements directly with the commercial banks. In the tea sector steps will be taken to permit the estates with factories to export their production directly instead of through the (state-owned) Uganda Tea Authority.

The Ugandan authorities also remain fully committed to flexible price policies in other sectors. To cover the import costs of petroleum products, which will be rising in domestic currency terms with the progressive depreciation of the first window exchange rate, and to raise some revenues through taxes on the consumption of petroleum products, effective January 14, 1984 a second round of large increases will be made in the prices of gasoline (12-13 percent), kerosene (50 percent), and diesel fuel (36 percent). The Government has also kept the tariff policies of the major public utilities under constant review. In November 1983 the tariffs for the external services of the Post and Telecommunications were raised by an average of 1,000 percent. The external passenger fares for Uganda Airlines were increased in two steps in August and November 1983, by a total of 50 percent above their July 1983 level. In addition to these increases, the tariffs of the Uganda Electricity Board will be raised by 25 percent effective January 1, 1984. Tariff adjustments for the Uganda Railways and for the National Water and Sewage Corporation, which are presently being considered by the Government, will be implemented by end-January 1984.

A major element of the Government's efforts to revive the economy is the ongoing rehabilitation program for various industries and enterprises, which are now benefiting from supplies of essential raw materials and spare parts under the second IDA reconstruction credit (US$75 million). The enterprises are required to pay for these imports at the first window rate, either with their own resources and/or with the support of domestic bank credit. A part of the IDA credit has also been directly on-lent by the Government to selected parastatals. With this program of assistance, capacity utilization in industry is estimated to have increased from an average of 20-25 percent in 1981/82 to about 30-35 percent more recently; in some industries such as cement, beer, and cigarettes, it has reached 60 percent. In view of the results already achieved, and to ensure a more efficient use of resources, the Government intends to accelerate the utilization of the IDA credit by channeling the remaining amounts to the more viable parastatals. To continue this rehabilitation program, the World Bank is presently preparing to put in place a third IDA reconstruction credit (US$50 million). Furthermore, the Government has set up a verification committee to examine ownership issues under the Expropriated Properties Act. In some cases, the initial steps have already been taken to return certain expropriated properties to their former owners. The Government recognizes that the speedy resolution of ownership claims will substantially reduce the size of the parastatal sector, increase efficiency, and improve the prospects for investment.

Another important element of the Government's policies to promote economic growth is the public investment effort, which is being implemented under the Revised Recovery Program for 1983/84-1985/86. This program aims at mobilizing a total of US$928 million in external aid to finance key development projects, with the major allocations being provided to agriculture (25 percent), industry and tourism (32 percent), and transport and communications (23 percent). The remainder represents the share of the mining sector and social infrastructure projects. Since 1982/83 Uganda has succeeded in mobilizing about US$ 498 million in external aid commitments for financing various projects. Thus, the Government is actively engaged in improving the coordination of foreign aid inflows and in removing physical and managerial bottlenecks to accelerate the rate of project execution. Furthermore, early in 1984 the Government will be seeking the support of a Consultative Aid Group to mobilize the additional resources that are needed for the recovery program. With the assistance of an already selected foreign consultant firm and the support of IDA funds, the authorities will be beginning studies of the operations of the parastatal sector.

3. Fiscal policies

During the fiscal years 1981/82 and 1982/83 the Ugandan authorities implemented restrictive fiscal policies to contain excess demand pressures on the balance of payments and the domestic price level. On a commitment basis, the overall fiscal deficit was reduced sharply from 75.6 percent of total expenditure in 1980/81 to 41 percent in 1981/82 and 29 percent in 1982/83. Over these years the share of the fiscal deficit financed by domestic bank credit was decreased markedly from 86 percent to 52 percent. The Government's recourse to net foreign borrowing and nonbank domestic financing accounted for only about 10.5 percent and 5.5 percent, respectively, of the total fiscal deficits incurred during 1980/81-1982/83 (Chart 3). As the budgetary support provided by these normal financing sources was insufficient to meet expenditure commitments fully, the Government also accumulated domestic arrears of about U Sh 9.7 billion, equal to roughly 19 percent of the fiscal deficits. 1/

In accordance with earlier programmed objectives, in 1983/84 the overall fiscal deficit is to be held to U Sh 18.1 billion (on a commitment basis), to reduce it as a proportion of total expenditure to 17 percent (Table 5). As a preliminary estimate of outstanding domestic arrears had become available, the Government decided to make a net reduction of domestic arrears (U Sh 4 billion), of which about U Sh 0.65 billion is to be made through cash payments and the remainder through the sale of Treasury bonds. Moreover, to facilitate the economic recovery process, the Government decided to channel some of the external resources it had mobilized for its operations back to the private sector by making a net repayment of U Sh 2.5 billion to the domestic banking system over the fiscal year. This decision to repay the domestic banking system also reflected a need to offset a higher-than-programmed recourse to domestic bank financing in the final quarter of 1982/83 and the increase in domestic liquidity that resulted from it. The authorities moved to implement this policy in the first quarter of 1983/84, when the Government relied on receipts derived from forward sales of coffee and on increased sales of Treasury bills to nonfinancial domestic enterprises to reduce its net indebtedness to the banking system (by about U Sh 4 billion) and hold it within the end-September ceiling. For the year as a whole, the overall budgetary financing need (U Sh 22.1 billion) would be more than covered by a larger than earlier programmed sale of Treasury bills to domestic nonfinancial enterprises (about 42 per cent of the deficit) and a slightly higher level of net foreign borrowing (69 per cent of the deficit). The level of net foreign borrowing, after fully accounting for all scheduled debt repayments, is expected to be slightly above the earlier program estimate mainly because of more depreciated exchange rates.

1/ Domestic arrears were incurred primarily during the 1970s when fiscal discipline was inadequate. The Government is in the process of identifying the amount and the validity of such outstanding claims in consultation with various domestic claimants.

Table 5. Uganda: Budgetary Operations, 1980/81-1983/84

(In billions of Uganda shillings)

	1980/81	1981/82	1982/83		1983/84	
			Program	Prel. actuals	Program	Revised program
Revenue and grants	3.3	27.9	45.8	52.8	84.5	88.1
Revenue	2.7	24.4	44.0	52.2	76.3	80.5
Tax	(2.6)	(23.7)	(42.5)	(50.3)	(68.2)	(73.4)
Nontax	(0.1)	(0.7)	(1.5)	(1.9)	(8.1)	(7.1)
Grants	0.6	3.5	1.8	0.6	8.2	7.6
Expenditure 1/	13.5	47.3	60.9	74.6	102.6	106.2
Recurrent outlays	11.9	31.7	39.7	48.0	66.3	69.6
Wages and salaries	(5.1)	(6.4)	(6.4)	(7.0)	(10.5)	(10.5)
Other	(6.8)	(25.3)	(33.3)	(41.0)	(55.8)	(59.1)
Development	2.0	7.3	16.6	9.4	36.3	36.6
Other (net)	-0.4	8.3	4.6	17.2	--	--
Main Treasury clearance account	(...)	(10.0)	(--)	(27.1)	(--)	(--)
Other government account at the Bank of Uganda (credit -)	(...)	(-1.1)	(--)	(-6.9)	(--)	(--)
Other outlays 2/	(-0.4)	(-0.6)	(4.6)	(-3.0)	(--)	(--)
Overall deficit on a commitment basis	-10.2	-19.4	-15.1	-21.8	-18.1	-18.1
Identified change in domestic arrears (decrease in arrears -)	0.4	4.0	--	5.3	--	-4.0
Overall deficit (cash basis)	-9.8	-15.4	-15.1	-16.5	-18.1	-22.1
Financing	9.8	15.4	15.1	16.5	18.1	22.1
External (net)	0.8	1.0	12.6	3.6	14.1	15.3
Borrowings	(1.0)	(4.5)	(16.0)	(5.8)	(24.9)	(25.3)
Repayments	(0.2)	(3.5)	(3.4)	(2.2)	(10.8)	(10.0)
Domestic	9.0	14.4	2.5	12.9	4.0	6.8
Bank	(8.8)	(13.3)	(2.0)	(11.4)	(2.5)	(-2.5)
Nonbank	(0.2)	(1.1)	(0.5)	(1.5)	(1.5)	(9.3)

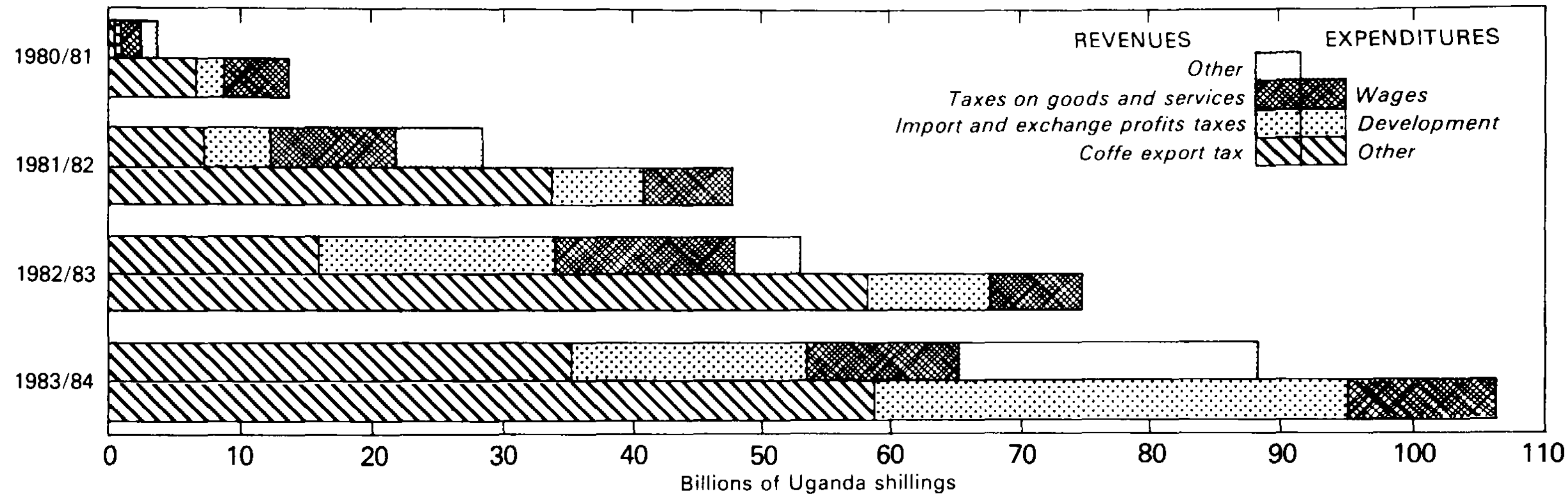
Sources: Data provided by the Ugandan authorities; and staff estimates.

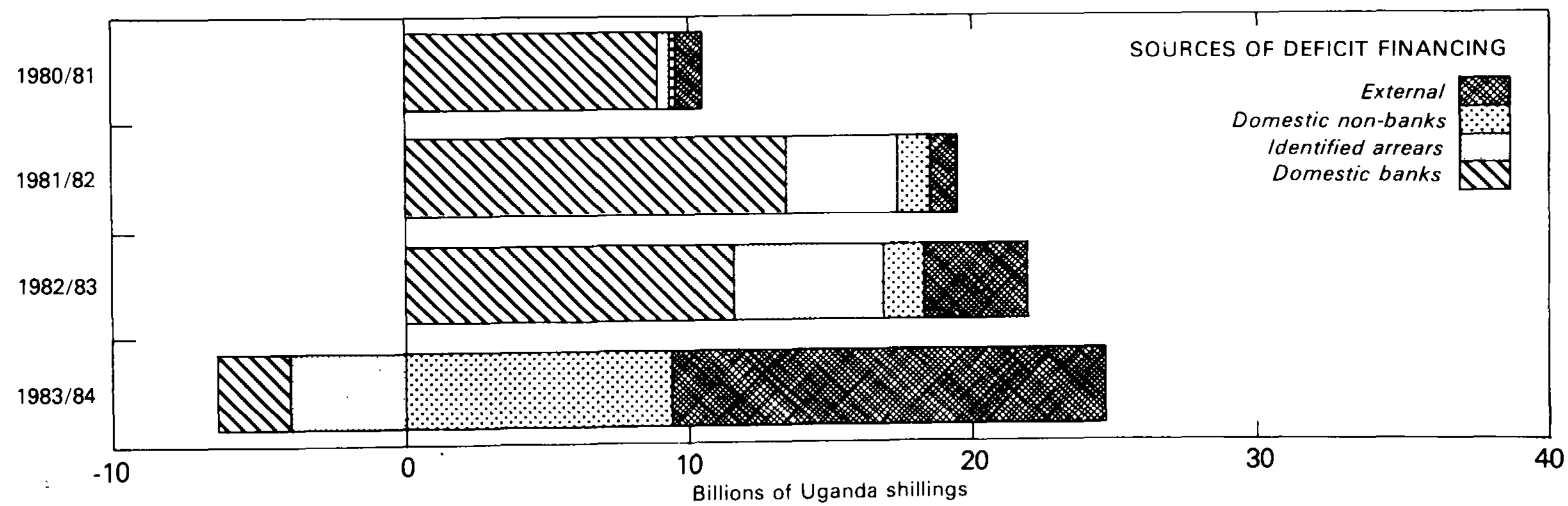
1/ Cash expenditures plus identified unpaid commitments.
2/ Includes the net change in extrabudgetary fund balances, differences between Treasury disbursements and a cash basis, and contingencies.

CHART 3

UGANDA

GOVERNMENT BUDGETARY OPERATIONS, 1980/81 - 1983/84





The Ugandan representatives indicated that the Government would be making a determined effort to achieve the current program's fiscal objectives described above. This would be done by raising a somewhat higher level of revenues than earlier programmed and by limiting the growth in nominal expenditures to no more than the additional revenue growth. On the receipts side, the more rapid depreciation of the exchange rate is expected to lead to sizable gains in revenues from coffee export taxes and, to a lesser extent, also from non-oil import taxes. However, these gains in revenues from trade-related taxes will be partly offset by lower taxes on petroleum products.

As the net gain in revenues will be modest (about U Sh 3.5 billion), the Government will be maintaining a tight restraint on expenditure growth. Nevertheless, there are some unavoidable increases in certain expenditure categories. With the greater depreciation of the first window exchange rate, the foreign exchange component of development expenditures and of nonwage recurrent outlays (including all scheduled interest payments on the public debt) is expected to be higher. Furthermore, the budgetary provision for the payment of Fund charges had to be increased. As the net increase in budgetary expenditures due to these factors is estimated to amount to about U Sh 6.5 billion, the expected gain in revenues will have to be accompanied by a reduction in discretionary outlays (of U Sh 3.0 billion). Hence, the Government will be making a determined effort to economize on the discretionary part of foreign exchange outlays by reducing its share of second window foreign exchange sales from 30 percent per quarter to 25 percent per quarter. Additional expenditures in local currency under both the recurrent and development budgets will be strictly curtailed, and, in particular, extra-budgetary outlays will be avoided. To this end the system of expenditure control will be tightened significantly and improved. 1/

The Ugandan representatives noted that the revenue effort had been substantial under the financial programs implemented since May 1981. Domestically generated government revenues, which increased eightfold in 1981/82 and doubled in 1982/83, are expected to rise further by 54 per cent in 1983/84. However, by far the major part of this revenue growth stemmed from the increased taxation of foreign trade. The Ugandan representatives felt that by the end of 1983/84 the domestic taxes on exports and imports would be exceptionally high and that, in the case of imports, the retail prices inclusive of taxes would become prohibitively high with the forseeable depreciation of the exchange rate. They felt that both the tax structure and its administration needed to be rationalized and improved, to avoid creating incentives for tax evasion and to increase the efficiency of the tax collection system.

1/ The specific measures are summarized in paragraph 20 of the memorandum of economic and financial policies (Attachment II).

The mission assured the authorities that the recent FAD technical assistance mission would make appropriate recommendations in its report for timely implementation with the 1984/85 budget.

The Ugandan representatives also expressed concern over the exceptionally depressed level of civil service wages 1/ and the problems of holding government expenditures down in the face of rapidly depreciating exchange rates. The staff stressed that, as financial constraints were likely to remain tight for some time, stronger efforts were needed to improve resource allocation and make the most effective use of available financial resources. To progress in this direction, it would be important to reduce the size of the civil service in the less essential services and strengthen administrative capacities in areas that are essential to the ongoing recovery process. This approach would also provide a rational basis for implementing a policy of selective wage increases, whereby the necessary wage incentives could be provided to the more productive sections of civil service employment. The staff also emphasized that the control and monitoring of the budgetary process should be improved to ensure that expenditures are made in accordance with agreed priorities and the implementation of the development effort is well coordinated with the available foreign aid and adequately budgeted amounts of foreign exchange and local currency contributions. The authorities agreed to make renewed and serious efforts to move in these directions.

4. Domestic credit and interest rate policies

The tight fiscal policies of the past two years were accompanied by appropriately restrained rates of domestic credit expansion. 2/ The growth rate of broad money declined from 55 percent in 1981/82 to 39 percent in 1982/83 (Table 2). The annual increases in domestic bank credit were held to increasingly lower proportions of the stock of broad money at the beginning of the period, largely due to the Government's declining net recourse to domestic bank financing. By 1982/83 these policies contributed to a sizable reduction in the overall BOP deficit and a sharp decrease in the domestic inflation rate.

The domestic credit program for 1983/84 was initially formulated with the broad objectives of reducing the overall BOP deficit by about one half, preventing the emergence of new inflationary pressures, and ensuring an adequate credit expansion for productive economic activities. Within this framework, the growth rate of broad money was to be reduced from 39 percent in 1982/83 to 10 percent in 1983/84.

1/ Civil service wages were increased by 20 percent in 1982/83 and by 50 per cent in 1983/84. The monthly wage for civil servants is about US$40-60.

2/ The monetary survey is contained in Appendix Table IV.

On account of a higher-than-programmed increase in net credit to Government in the quarter ending June 1983, the Government made a substantial net repayment (of U Sh 4 billion) to the banking system to keep within the corresponding credit ceiling for the subsequent quarter (ending September 1983). As bank credit to the private sector increased in line with the programmed path, total domestic credit was held to the program's target for September 1983. The annual rates of expansion in total domestic credit for the years ending June 1983 and September 1983 were substantially lower than those recorded in the corresponding periods of the previous year.

At the time of the mid-term review the Ugandan authorities considered it especially important to aim at a somewhat larger than initially programmed reduction in the overall BOP deficit (in terms of U.S. dollars) and to continue containing domestic inflationary pressures associated with any further depreciation of the exchange rate at the second window auctions. In view of this, although the credit financing needs of the export sector and of imports under the second IDA reconstruction credit were expected to be higher due to more depreciated exchange rates at the first window, the quarterly ceilings for total domestic credit were maintained for the remainder of the program period. The authorities felt that, with the Government's newly programmed net repayment to the banking system, there would be an adequate margin within the overall increase in credit for financing exports and essential imports. However, there would be need for greater restraint on bank credit to other and lower priority areas of private sector activity.

Within this framework of external objectives and domestic credit policies, although the BOP deficit would be reduced in U.S. dollar terms, its magnitude in Uganda shillings is projected to be higher due to a higher than initially programmed depreciation of the exchange rate. As broad money at the end of June and September 1983 exceeded the original estimates of money demand, and the program's BOP deficit in local currency terms is expected to be larger than initially targeted, the growth in broad money over the last three quarters of the program period is projected to be much less than the original program estimate.

Within the tight credit programs for 1981/82 and 1982/83, the Ugandan authorities have not only made direct efforts to channel bank credit to productive activities but have also relied on progressively higher interest rates to achieve greater efficiency in resource allocation. To continue this policy, in July 1983 interest rates were raised again by 2 percentage points for all domestic bank deposits and lending operations. Effective December 1, 1983, the interest rates for bank deposits, for Treasury bills, and for loans to the agricultural, export, and manufacturing sectors were increased by a further 2 percentage points. The rates that the Bank of Uganda applies to its advances and rediscounts were also raised by 2 percentage points (Appendix Table V). 1/ These increases in interest rates and the steps that have been taken to encourage various agricultural marketing entities to negotiate their domestic credit needs directly with the commercial banks are expected to contribute importantly to increasing the efficiency of the domestic financial intermediation process.

IV. Performance Criteria and Review Clause

The performance criteria for the 1983/84 financial program and the actual performance in relation to them are shown in Table 6. Based on the available data, all performance criteria were observed for the quarter ending September 1983. As envisaged earlier, in implementing the second half of the current financial program, the Ugandan authorities will be adhering strictly to performance criteria that relate to total domestic credit, net credit to Government, net foreign borrowing, the cumulative sales of foreign exchange at the second window, and the net reduction of external arrears through cash payments. In addition, performance criteria have been set for the net cash reduction of domestic arrears by the Government. Over the second half of 1983/84 these arrears are to be reduced through cash payments by at least a net amount of U Sh 0.65 billion, of which a payment of U Sh 0.5 billion will be made by end-March 1984.

For total domestic credit and net credit to the Government, the originally programmed amounts for end-March 1984 will be treated as performance criteria, while those for end-June 1984 will remain indicative ceilings. For net credit to Government, the ceiling for March 31, 1984 and the indicative ceiling for June 30, 1984 will be reduced (raised) by the excess (shortfall) of the cumulative profits from the operation of the second window from July 1, 1983 above (below) the projected amounts of U Sh 9.7 billion and U Sh 10.4 billion, respectively.

Although in the second half of the program period the total foreign exchange sales at the second window are expected to be lower than earlier envisaged, the minimum amounts to be sold will remain at the levels earlier programmed.

As regards foreign borrowing, in the second half of the program period the contracting of new public and publicly guaranteed external debt will not exceed US$30 million for maturities of 0-12 years and

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1/ With the decline in the inflation rate and the increases in nominal interest rates, real interest rates have become increasingly less negative. The real rates for one-year time deposits and nonpriority lending operations are about minus 6 percent and minus 2 percent, respectively.

Table 6. Uganda: Indicators of Performance Under the Program, September 1981-June 1984

	1981/82		1982/83		1983/84	
	Program 1/	Actual	Program 1/	Actual	Program	Actual
	(In millions of U.S. dollars)					
Balance of payments						
Current account deficit	232.0	131.0	201.0	142.0	125.1	...
Overall deficit	142.0	187.0	82.0	77.0	18.7	...
Debt service ratio (in per-cent of exports of goods and services)	47.0	45.5	26.0	31.7	38.2	...
	(In billions of U Sh)					
Ceiling on net domestic credit						
September	34.8	34.4	57.9	49.3	70.0 2/	67.3
December	...	40.7	62.6	55.7	76.8 2/	...
March	46.9	43.6	64.2	61.5	81.1 2/	...
June	51.6	48.5	65.6 3/	70.6	84.1 3/	...
Ceiling on net credit to Government						
September	27.2	25.9	36.0	32.0	41.1 2/	39.2
December	...	29.2	36.0	34.2	41.6 2/	...
March	31.0	30.2	38.0	37.2	42.1 2/	...
June	33.7	33.6	38.5 3/	45.3	42.6 3/	...
Cash reduction in domestic arrears						
March	--	--	--	--	0.5	...
June	--	--	--	--	0.15 3/	...
	(In millions of U.S. dollars)					
Net external borrowing						
Of which:						
0-12 years maturities						
September	70.0	--	120.0	--	30.0	20.0
December	70.0	--	120.0	--	40.0	0.0
March	70.0	--	120.0	30.0	30.0	...
June	80.0	--	150.0	50.0	30.0 3/	...
0-6 years maturities 4/						
September	34.4	--	54.0	--	30.0 5/	20.0
December	34.9	--	54.7	--	20.0 5/	0.0
March	33.7	--	54.3	20.0	10.0	...
June	33.1	--	65.0	40.0	10.0 3/	...
Net cumulative reduction in arrears						
September	12.6 6/	24.2	5.5 7/	11.2 8/	...	...
December	... 6/	24.7	11.0 7/	16.9 8/	10.0 8/	...
March	1.1 6/	4.8	12.0 8/	27.3 8/	...	...
June	3.3 6/	22.2	15.0 8/	16.5 8/	20.0 8/	...
Cumulative sales at second window						
September	...	...	10.0	6.1	39.0	41.9
December	...	...	24.0	27.3	78.0	...
March	...	...	53.0	60.5	117.0	...
June	...	...	99.0	100.5	156.0 3/	...

1/ Revised program targets.
2/ The ceilings for September 30 and December 31 of 1983 will be reduced (raised) by the excess (shortfall) of the cumulative profits from the operations of the second window from July 1, 1983 above (below) the projected U Sh 3.6 billion and U Sh 5.3 billion, respectively. For March 31 and June 30 of 1984, the corresponding figures are U Sh 9.7 billion and U Sh 10.4 billion, respectively.
3/ Indicative ceilings.
4/ Of which no more than SDR 20 million of maturities within the range of 0-6 years contracted in 1981/82 and 1982/83 will carry an interest rate equal to or in excess of LIBOR.
5/ Only through cash borrowing by the Bank of Uganda.
6/ Quarterly reductions through cash payments and rescheduling.
7/ Of which half through cash payments and rescheduling
8/ Reduction through cash payments.

US$10 million for maturities of 0-6 years. These amounts represent a moderate reduction from the total amounts that had been programmed for the first half of the program period.

The Ugandan authorities remain fully committed to a comprehensive review of exchange rate policies before the end of June 1984, when understandings are to be reached on exchange rate policy.

V. Staff Appraisal

Over the two fiscal years 1981/82 and 1982/83 Uganda's economic and financial situation improved considerably as a result of bold policy measures implemented under two successive stand-by arrangements with the Fund. Production and exports increased substantially. Despite the large depreciation of the exchange rate, the domestic inflation rate was reduced significantly. By 1982/83 there was also a sizable decline in the overall balance of payments deficit. An orderly process of servicing the external debt and of reducing external payments arrears was established, and Uganda was able to obtain substantial amounts of debt relief and additional external aid in support of its adjustment effort. The Government also succeeded in bringing about an improvement in the domestic security situation.

The economic recovery recorded over the past two years was stimulated primarily by significant adjustments in the exchange rate and flexible price policies. Increasingly depreciated exchange rates provided the basis for large and frequent increases in the producer prices of export crops. In August 1982 a flexible and temporary dual exchange rate system was introduced to improve the mechanism of foreign exchange allocation (especially to the private sector) and to determine ultimately an equilibrium exchange rate within a unified exchange regime. At the same time, exchange control regulations were substantially liberalized. The operation of the dual exchange system has helped to practically eliminate smuggling activities and increase the flow of foreign trade transactions through the banking system. At the same time, the risks of serious distortions in resource allocation have been minimized by both progressively narrowing the gap between the two official exchange rates and increasing the volume and coverage of transactions at the second window.

During 1981/82-1982/83 financial policies were implemented with restraint and discipline. As a proportion of total expenditure, the overall fiscal deficits declined. The bank financing component of the fiscal deficits was substantially reduced. With rising levels of foreign aid, steps were taken to channel resources to development projects and rehabilitate the country's productive enterprises. Concurrently, domestic credit expansion was slowed, and efforts were made to allocate an increasing share of it to productive activities. Finally, domestic interest rates were adjusted upward periodically to help the financial intermediation process.

When the 1983/84 financial program was adopted, the main issue facing the authorities was how to accelerate the external adjustment process while at the same time ensuring a reasonable pace of economic recovery and price stability. It was clear that in the medium term the balance of payments would have to move rapidly into a significant surplus position, so that in the near future Uganda would be able to eliminate the remaining amounts of external payments arrears and begin reducing the presently sizable outstanding amount of net use of Fund credit. To achieve these goals, the external current account deficit would have to be narrowed substantially. The current program seeks to achieve such a reduction in the deficit during 1983/84.

In the first half of the 1983/84 financial program a wide range of measures was again implemented to improve the price incentives for agricultural production, establish rational cost-price relationships in other sectors, and rehabilitate the nation's productive enterprises. The program puts special emphasis on progressing toward the establishment of a unified exchange regime in accordance with a firm timetable, which is to be achieved through a continued depreciation of the first window rate and through tight financial policies that would contain the depreciation of the second window rate. Based on data up to end-September 1983, the program has remained on track, all performance criteria have been observed, and significant progress has been made toward closing the gap between the two official exchange rates.

Over the second half of the program period the Ugandan authorities will be strengthening the adjustment effort through a comprehensive package of new measures. The exchange rate at the first window will be depreciated at a pace sufficient to accelerate substantially the move toward a unified exchange regime. A third round of increases in agricultural producer prices will be implemented to encourage the growth and diversification of exports. The prices of petroleum products and the tariffs of selected public uitilities will again be increased substantially. The rehabilitation of productive and potentially viable enterprises under the second IDA reconstruction credit will be speeded up, and the authorities have taken steps to accelerate the implementation of public investments under the ongoing Revised Recovery Program. Furthermore, domestic financial policies will be tightened.

In government operations, despite the increased costs of imports through the second window and a higher than initially programmed level of external debt service payments, the authorities will be holding the overall fiscal deficit to the originally programmed level. To this end the Government will be raising more revenues, reducing discretionary expenditures (especially nonessential foreign exchange outlays), and strengthening the expenditure control system. In the period ahead the Ugandan authorities will need to undertake an appropriate reform of the tax structure and its administration. In this context the staff would urge the authorities to act quickly after the FAD technical assistance report on tax policy becomes available in early 1984. Moreover, it will also be necessary for the Government to make more vigorous efforts to economize on the size of the civil service, strengthen administrative capacities in areas that are essential to the recovery effort, and formulate a more rational wage policy. The monitoring and control of the budgetary process will also have to be considerably improved.

The stance of domestic credit policies will also be tightened during the second half of the program period. The financing needs will be higher for exports due to the increases in producer prices; essential imports through the first window will also require more credit due to further exchange rate depreciation. However, as the authorities have agreed to adhere to the program's original ceilings for net credit to Government and total domestic credit, the margin for credit expansion to other lower priority areas of activity will be far more limited than was foreseen at the start of the program. Recognizing the need to improve resource allocation, the authorities have recently implemented a further round of interest rate increases. However, as real interest rates are still negative, the staff would urge the authorities to move expeditiously toward positive real rates of interest.

In the area of external debt management, the authorities will be following prudent policies by strictly limiting nonconcessional borrowing to ceilings that are lower than those for the first half of the program period. In this regard, the staff would urge the authorities to avoid future recourse to various forms of short-term borrowing for budgetary purposes (as was the case with the forward sales of coffee in the third quarter of 1983). With the External Debt Management Office that has been set up, the system for monitoring and authorizing foreign borrowing operations should be improved considerably. As in the two earlier years, the Government should continue to reduce its outstanding external payments arrears in accordance with the programmed objectives.

Although existing exchange restrictions were relaxed in August 1982 and no new restrictions have been introduced since then, restrictions still remain, including external arrears, on certain payments and transfers for current international transactions. All existing restrictions require Fund approval. The staff welcomes the authorities' commitment to move rapidly to a unified exchange regime. It recommends approval of the multiple currency practice until end-June 1984, by which time understandings are to be reached with the Fund on exchange rate policy. For the other exchange restrictions, including payments arrears, the staff recommends approval until end-October 1984, by which time it is the intention of the Ugandan authorities that a new financial program for 1984/85 would have been considered by the Executive Board.

The staff feels that the additional measures taken to strengthen the adjustment effort are adequate to achieve the program's objectives.

However, the Government will need to continue its strong adjustment effort in the coming years, with considerably greater emphasis on improving key areas of economic management and administration. With such adjustment policies and with a continued improvement in the internal security situation, Uganda should be able to attain a viable balance of payments situation in the medium term along with reasonable rates of growth and financial stability.

It is recommended that the next Article IV consultation with Uganda be held before the end of 1984.

VI. Proposed Decisions

The following decisions are proposed for adoption by the Executive Board:

Article IV Consultation

1. The Fund takes this decision relating to Uganda's exchange measures subject to Article VIII, Sections 2(a) and 3, and in concluding the 1983 Article XIV consultation with Uganda, in the light of the 1983 Article IV consultation with Uganda conducted under Decision No. 5392-(77/63), adopted April 29, 1977 ("Surveillance over Exchange Rate Policies").

2. As described in EBS/84/7, Uganda maintains exchange restrictions on payments and transfers for current international transactions, including restrictions evidenced by external payments arrears, and a multiple currency practice, all of which are subject to approval under Article VIII, Section 2(a) and 3, respectively. The Fund welcomes the intention of the authorities to progressively reduce payments arrears and to eliminate the multiple currency practice. In the meantime, the Fund grants approval of the multiple currency practice until June 30, 1984, and of the existing exchange restrictions on payments and transfers for current international transactions, until October 31, 1984.

Review Under Stand-By Arrangement

1. Uganda has consulted with the Fund in accordance with paragraph 4(b) of the stand-by arrangement for Uganda (EBS/83/180, Supplement 1, September 19, 1983) and paragraph 26 (g) of the memorandum for economic and financial policies annexed to the letter of June 24, 1983 attached to the stand-by arrangement.

2. The letter of November 13, 1983, from the President and Minister of Finance, together with annexed memorandum setting forth the economic and financial policies which Uganda will pursue during the second half of 1983/84, shall be attached to the stand-by arrangement for Uganda and the letter dated June 24, 1983, shall be read as supplemented by the letter of November 13, 1983.

3. Uganda will not make purchases under the stand-by arrangement for Uganda that would increase the Fund's holdings of Uganda's currency in the credit tranches beyond 25 percent of quota, or increase the holdings of that currency resulting from purchases of borrowed resources beyond 12.5 percent of quota, during any period in which any of the performance criteria set out in paragraph 25(a), (b), (c), (e), (f), and (g) of the memorandum annexed to the letter of November 13, 1983, is not observed, or if at any time the performance criterion set out in paragraph 25 (d) of that memorandum is not observed.

Relations with the Fund
(As of October 31, 1983)

IMF data

Date of membership:	September 27, 1963
Quota:	SDR 75 million
Intervention currency and the rate:	U.S. dollar: US$1 = U Sh 185.3
Local currency/SDR equivalent:	U Sh 194.6
Fund holdings of currency	SDR 397.65 million (530.20 percent of quota)
Of which: CFF	SDR 63.13 million (84.17 percent of quota)
Enlarged access under stand-by	SDR 188.04 million (250.72 percent of quota)
Credit tranches (including SBA)	SDR 75.00 million (100.00 percent of quota)
Net cumulative allocation:	SDR 29.40 million
Holdings:	SDR 3.88 million
Trust Fund loan disbursement: (second period)	SDR 22.51 million
Direct distribution of profits from gold sales:	US$6.36 million
Gold distribution: (Four distributions)	34,232.819 fine ounces

Table I. Uganda: IBRD Loans and IDA Credits by Sector

(As of September 30, 1983; in millions of U.S. dollars)

	Total 1/			Disbursed			Undisbursed		
	Total	IBRD	IDA	Total	IBRD	IDA	Total	IBRD	IDA
Agriculture	80.4	--	80.4	12.7	--	12.7	67.7	--	67.7
Education	49.3	--	49.3	18.6	--	18.6	32.0	--	32.0
Water supply	9.0	--	9.0	2.7	--	2.7	6.3	--	6.3
Transport and communication	38.6	--	38.6	18.4	--	18.4	22.0	--	22.0
Power	8.4	8.4	--	8.4	8.4	--	--	--	--
Industry	39.0	--	39.0	1.6	1.6	--	37.4	--	37.4
Reconstruction 2/	142.5	--	142.5	81.7	--	81.7	60.8	--	60.8
Technical assistance	8.0	--	8.0	1.0	--	1.0	7.0	--	7.0
Total	375.2	8.4	366.8	145.1	10.0	135.1	233.2	--	233.2

Source: Data provided by the World Bank.

1/ Total amounts may differ from the sum of disbursed and undisbursed due to exchange rate adjustments.
2/ Includes one bilateral credit administered by IDA.

Table II. Uganda: Commodity Prices, April 1981-February 1984

	1981				1982			1983		1984		Feb. 1984/ April 1981 ratio
	April	May	June	Oct.	Jan.	June	Nov.	May	July	Jan.	Feb.	
					(Uganda shillings per kg)							
Minimum producer prices for export crops												
Coffee	7.00	20.00	20.00	35.00	35.00	50.00	50.00	60.00	80.00	80.00	100.00	14.29
Tea	1.35	1.35	4.00	6.00	6.00	10.00	10.00	15.00	25.00	25.00	40.00	29.63
Cotton	6.00	15.00	15.00	30.00	30.00	40.00	40.00	50.00	60.00	60.00	90.00	15.00
Tobacco	8.60	8.60	20.00	50.00	50.00	100.00	100.00	115.00	150.00	150.00	200.00	23.26
Cocoa	3.20	3.20	3.20	3.20	20.00	30.00	30.00	40.00	80.00	80.00	130.00	40.63
					(Uganda shillings per liter)							
Consumer prices for petroleum products												
Premium gas	7.44	27.00	81.00	85.00	85.00	120.00	150.00	150.00	170.00	190.00	190.00	25.54
Regular gas	7.13	25.00	78.40	80.00	80.00	110.00	140.00	140.00	160.00	180.00	180.00	25.25
Diesel fuel	6.00	15.00	47.20	50.00	50.00	60.00	90.00	90.00	110.00	150.00	150.00	25.00
Kerosene	4.00	7.00	30.00	30.00	35.00	40.00	80.00	80.00	100.00	150.00	150.00	37.50

Source: Data provided by the Ugandan authorities.

Table III. Uganda: Average Monthly Consumer Price Index for Middle Income Groups, June 1981-November 1983

(April 1981 = 100)

Items	Weights	1981 June	1981 Sept.	1981 Dec.	1982 March	1982 June	1982 Sept.	1982 Dec.	1983 March	1983 June	1983 Sept.	1983 Oct.	1983 Nov.
Food	4.10	136.8	125.1	124.2	146.9	169.0	186.1	199.3	209.5	246.5	262.2	275.6	261.9
Drinks and tobacco	17.0	131.8	109.8	104.9	113.9	112.1	119.6	123.3	125.8	137.0	126.6	123.3	124.9
Fuel and lighting	6.0	125.4	124.7	120.1	145.3	162.2	194.6	267.7	269.1	285.9	307.8	307.8	307.0
Transport	10.0	103.2	244.5	245.2	341.2	354.6	306.6	320.1	433.3	436.6	449.0	449.0	481.7
Clothing	14.0	343.6	324.7	330.5	348.6	343.7	347.2	354.7	325.9	334.4	332.7	331.4	294.8
Other consumer goods	10.0	139.7	115.5	124.8	136.6	143.9	147.0	150.2	146.1	149.0	143.5	138.3	136.1
Other manufactured goods	2.0	235.8	210.2	200.3	245.1	205.3	230.3	232.9	266.8	244.0	241.7	236.6	240.3
Consumer price index	100.0	163.1	163.1	163.2	189.8	200.2	206.9	220.1	232.4	251.8	258.2	262.2	254.9

Sources: Bank of Uganda; Ministry of Planning and Economic Development (MPED); and staff estimates.

Table IV. Uganda: Monetary Survey, December 1981-June 1984

(*In billions of Uganda shillings*)

	1981	1982				1983				1984	
	Dec.	March	June	Sept.	Dec.	March	June	Sept. Prov.	Dec. Proj.	March Proj.	June Proj.
Foreign assets (net)	14.59	-13.75	-18.05	-19.02	-20.38	-26.23	-39.93	-40.95	-72.61	-84.90	-93.25
Monetary authorities	-15.50	-14.38	-18.93	-20.69	-22.37	-30.65	-44.16	-45.56	-79.18	-91.93	-100.94
Commercial banks	0.91	0.63	0.88	1.67	1.99	4.42	4.23	4.61	6.57	7.03	7.69
Domestic credit	40.79	43.33	48.73	49.66	55.58	59.79	70.15	67.29	76.80 1/	81.10 1/	84.10 2/
Claims on Government (net)	29.33	29.93	33.69	31.95	34.11	37.64	45.06	39.22	41.60 1/	42.10 1/	42.60 2/
Claims on private sector	11.46	13.40	15.03	17.71	21.47	22.15	25.09	28.07	35.20	39.00	41.50
Broad money	34.55	31.21	34.03	33.97	38.51	42.75	47.43	48.55	48.00	48.50	49.00
Money	28.31	23.50	26.07	25.96	29.78	33.43	36.63	37.59	...	...	...
Quasi-money	6.24	7.71	7.96	8.01	8.73	9.32	10.80	10.96	...	...	...
Other items (net)	-8.35	-1.63	-3.35	-3.33	-3.31	-9.19	-17.21	-22.21	-43.81	-52.30	-58.15

Sources: Data provided by the Ugandan authorities; and staff estimates.

1/ Ceiling.
2/ Indicative ceiling.

Table V. Uganda: Structure of Interest Rates, 1981-83

(Percent per year)

	1981		1982		1983	
	June	Oct.	July	Dec.	July	Dec.
Bank of Uganda						
Ways and means	2.5	5.0	2.0	2.0	2.0	2.0
Rediscount rate	7.0	9.0	10.0	10.0	12.5	14.5
Bank rate to commercial banks	8.0	10.0	11.0	11.0	13.5	15.5
Treasury bills						
35 days	4.71	8.0	9.0	10.0	10.0	12.0
63 days	4.90	8.5	9.5	11.0	11.0	13.0
91 days	5.08	9.0	10.0	12.0	12.0	14.0
Government stocks						
5 years	8.5	11.0	12.0	12.0	12.0	12.0
10 years	9.5	11.5	12.5	12.5	12.5	12.5
15 years	10.5	12.0	13.0	13.0	13.0	13.0
Commercial banks						
Deposit rates 1/						
Demand deposits			Optional			
Savings deposits	5.0	8.0	9.0	9.0	11.0	13.0
Time deposits						
Minimum 1 year	5.0	12.0	13.0	13.0	15.0	17.0
More than 1 year			Negotiable			
Lending rates 2/						
Agriculture	8.0	13.0	14.0	14.0	16.0	18.0
Export and manufacturing	12.0	14.0	15.0	15.0	17.0	19.0
Commerce	12.0	15.0	16.0)	up to)	22.0)	22.0
Unsecured	12.0	17.0	17.0)	20.0)	)	

Source: Data provided by the Ugandan authorities.

1/ Minimum rates.
2/ Maximum rates.

Table VI. Uganda: Debt Service Projections, 1/ 1981/82-1990/91

(In millions of U.S. dollars)

	Actual									
	1981/82	1982/83	1983/84	1984/85	1985/86	1986/87	1987/88	1988/89	1989/90	1990/91
Total debt service payments	134	100	162	185	194	180	172	148	116	81
Official debt	105	58	101	86	85	86	86	76	63	59
Bank of Uganda debt	29	42	61	99	109	94	86	72	53	22
Of which: IMF	(15)	(26)	(44)	(95)	(109)	(94)	(86)	(72)	(53)	(22)
Memorandum items:										
Total debt service ratio 2/	45.6	31.7	42.6	44.2	43.3	37.6	33.9	27.3	20.0	13.0
Official debt service 3/	35.7	18.4	26.6	20.5	19.0	18.0	16.9	14.0	10.9	9.5
Merchandise exports	294.0	316.0	380.0	419.0	448.0	479.0	520.0	575.0	580.0	621.0
End-year stock of arrears	157.2	78.3	58.3	28.3	--	--	--	--	--	--

Sources: Bank of Uganda; and staff estimates.

1/ On basis of existing debts as of September 30, 1983 and anticipated commitments. Assumes program with IMF during 1983/84 but not beyond.
2/ As percentage of merchandise exports. Includes IMF and other Bank of Uganda obligations.
3/ As percentage of merchandise exports. Excludes IMF and other Bank of Uganda obligations.

Table VII. Uganda: Exchange Rates at WI, WII, WI-II, June 1981-November 1983

	Weights		U Sh per US$			Import-weighted nominal effective exchange rate 1/ June 1981=100			Import-weighted real effective exchange rate 1/ June 1981=100		
	WI	WII	WI	WII	WI-II	WI	WII	WI-II	WI	WII	WI-II 1
June 1981	100	0	77.0		77.0	100.0		100.0	100.0		100.0
July 1981	100	0	79.8		79.8	100.9		100.9	98.8		98.8
August 1981	100	0	81.4		81.4	100.9		100.9	101.2		101.2
September 1981	100	0	80.6		80.6	102.3		102.3	104.9		104.9
October 1981	100	0	79.3		79.3	101.7		101.7	105.5		105.5
November 1981	100	0	80.2		80.2	104.3		104.3	108.0		108.0
December 1981	100	0	85.1		85.1	110.3		110.3	115.2		115.2
January 1982	100	0	85.5		85.5	109.4		109.4	107.7		107.7
February 1982	100	0	86.2		86.2	107.9		107.9	102.7		102.7
March 1982	100	0	85.7		85.7	105.7		105.7	96.6		96.6
April 1982	100	0	85.9		85.9	104.5		104.5	91.5		91.5
May 1982	100	0	90.4		90.4	112.7		112.7	102.3		102.3
June 1982	100	0	96.7		96.7	115.8		115.8	102.8		102.8
July 1982	100	0	100.0		100.0	118.0		118.0	105.3		105.3
August 1982	91	9	99.3	300.0 2/	117.5	116.5	352.2 2/	138.0	101.3	306.3 2/	120.0
September 1982	91	9	100.0	300.0	118.2	116.4	349.3	137.6	101.0	303.1	119.4
October 1982	77	23	100.0	280.0	141.9	115.2	322.6	163.5	98.1	274.8	139.3
November 1982	77	23	100.2	255.0	136.3	113.8	289.7	154.8	94.0	239.2	127.8
December 1982	77	23	104.3	240.0	135.9	120.8	277.9	157.4	99.3	228.5	129.4
January 1983	65	35	110.0	235.0	153.9	127.5	272.5	178.4	100.0	213.7	139.9
February 1983	65	35	115.0	230.0	155.4	131.4	262.7	177.5	104.9	209.8	141.7
March 1983	65	35	117.8	236.0	159.3	133.0	266.5	179.9	104.7	209.8	141.6
April 1983	57	43	124.5	260.0	182.8	140.2	292.8	205.9	108.5	226.5	159.2
May 1983	57	43	135.0	270.0	193.0	152.2	304.4	217.6	113.5	227.0	162.3
June 1983	57	43	145.0	300.0	211.7	160.5	332.1	234.3	118.4	245.0	172.9
July 1983	45	55	160.0	310.0	243.0	175.3	339.6	266.2	129.0	249.9	195.8
August 1983	45	55	166.5	292.0	235.9	179.1	314.2	253.8	133.5	234.2	189.2
September 1983	45	55	176.7	270.0	228.3	190.0	290.4	245.5	138.7	211.9	179.2
October 1983	53	47	185.6	295.5	236.9	201.7	321.1	257.8	145.6	231.8	186.1
November 1983	53	47	212.1	327.5	266.3	227.2	350.6	288.9	169.6	261.7	215.6

Sources: Bank of Uganda; and staff estimates.

1/ The import weights used are: U.S. 22.93; U.K. 26.09; Japan 9.02; France 14.00; Federal Republic of Germany 8.55; Italy 5.24; the Netherlands 6.04; and Spain 8.13 percent.
2/ The rate applies to the last week of August.

Table VIII. Uganda: Main Elements of the Financial Programs, 1981/82-1983/84

	1981/82 Actual	1982/83 Actual	1983/84 Measures and targets
1. Exchange system	Depreciation of the currency from U Sh 8.0 per US$ to U Sh 78 per US$ in June 1981 and to U Sh 96 per US$ in June 1982.	Dual exchange system became operational August 1982. Rate at Window I depreciated from U Sh 99.25 per US$ at end-August 1982 to U Sh 150 per US$ at end-June 1983. Rate at Window II depreciated from U Sh 300 per US$ at end-August 1982 to U Sh 300 per US$ at end-June 1983.	Exchange rate ar Window I to depreciate faster. Minimum weekly sales at Window II to increase from US$2 million to US$3 million. All non-oil cash imports shifted from Window I to Window II. All major exports except for coffee and cotton shifted to Window II.
2. Supply side policies	Fivefold increase in producer prices of main export crops; elevenfold increase in prices of petroleum products; decontrol of most other prices.	Producer price increases for the main export crops ranged from 33 percent to 100 percent; increases in prices of petroleum products ranged between 75 percent and 128 percent.	Increase in producer prices of major export crops that occurred in May and July 1983 ranged between 50 percent and 166 percent; further increases in prices ranging from 25 percent to 62.5 percent will be implemented by February 14, 1984; prices of all petroleum products other than lubricants raised by U Sh 20 per liter in June 1983, and subsequently by between U Sh 20 and U Sh 50 per liter in November 1983.
3. Public finance	Specific tax rates converted to an ad valorem basis; rates of sales tax on imports and domestic production equalized; wage and salary increases for civil servants restricted to an average of 25 percent.	Zero rating of PAYE on civil servants' salaries introduced in July 1982; restraints on automatic cash increases for recurrent expenditure introduced; other measures to limit recourse to extrabudgetary accounts implemented; revenue collection administration improved; increase in tariffs on some public utilities implemented in November 1982.	Wages of civil servants increased by 50 percent in July 1983; tariff structures of major public utilities were raised between 25 percent and 1,000 percent between August 1983 and January 1984. Study of selected parastatals will begin January 1984.
4. Money and credit	Increase in cash reserve ratio from 10 percent to 15 percent; increase in deposit rates and most categories of lending rates by one percentage point in June 1982.	Lending rates for trade and commerce and unsecured loans allowed to float up to a maximum of 20 percent from November 1982; rates on Treasury bills increased by an average of 2.5 percentage points in November 1982.	Interest rates raised by 2 percentage points in July 1983 and will be raised by an additional 2 percentage points in December 1984.
5. External borrowing	Although new borrowing limits of SDR 30 million and SDR 80 million were allowed for maturities of 1 to 5 years and 1 to 12 years, no new borrowing was undertaken.	New borrowing limits of SDR 50 million and SDR 120 million from July 1, 1982 to March 31, 1983 were only partly utilized.	New external borrowing for the quarter ended December 1983 is limited to short-term loans of no more than US$30 million to be contracted by the Bank of Uganda; new external borrowing for the quarter ended December 1983 will be limited to US$20 million in the maturity range of 6-12 years and no additional borrowing in the maturity range of 0-6 years; new external borrowing for

THE REPUBLIC OF UGANDA
State House
Entebbe
Uganda

PO/10.6

13th November 1983

Dear Mr. de Larosière,

1. Uganda has benefitted considerably from the three financial programs that have been supported by successive stand-by arrangements with the Fund. The adjustment measures taken in the context of these programs have contributed significantly to the marked improvement in Uganda's economic and financial situation. Production has increased, the temporary dual exchange arrangement has resulted in a more efficient allocation of foreign exchange and in the narrowing of the deficits in government operations and in the overall balance of payments.

2. The current financial program is on track, and all performance criteria for end-September of 1983 have been observed. Despite this the Government has decided to take additional measures to strengthen the program, primarily to ensure the achievement of the program's fiscal and external objectives and to make a determined effort to unifying the dual exchange system. These measures, together with the performance criteria proposed for end-March 1983 and indicative criteria for end-June 1984, are described in the attached Memorandum.

3. The Government of Uganda believes that the policies set out in the attached Memorandum are adequate to achieve the objectives of the program. During the period of the stand-by arrangement, the Government of Uganda will consult with the Fund, in accordance with the policies of the Fund on such consultations and on the adoption of additional measures that may be appropriate to ensure the success of the program.

4. In conclusion, we would like to emphasize that the Government is fully committed to the objectives of the program and would continue to seek the support of the International Monetary Fund in implementing our Revised Recovery Program in the coming years.

Yours sincerely,

L. Kibirango
Governor
Bank of Uganda

A. Milton Obote
President and Minister
of Finance

Mr. Jacques de Larosière,
Managing Director
International Monetary Fund,
WASHINGTON, D.C. 20431,
U.S.A.

Memorandum of Economic and Financial Policies for the Second Half of 1983/84

1. When the 1983/84 financial program was launched, a wide range of measures was taken to improve the incentives for agricultural production, establish rational cost-price relationships, and rehabilitate the nation's productive enterprises. In addition, the Government continued its strong commitment to restrain fiscal and domestic credit policies, so that the recovery of the economy could be accompanied by both reduced inflationary pressures and an improvement in the overall balance of payments (BOP). As earlier envisaged, the Government has undertaken a mid-term review of the current program and has decided to implement an appropriate package of additional measures to strengthen the program, with the objectives of achieving a somewhat larger reduction in the balance of payments deficit than was initially programmed, containing the inflation rate to about 20-25 percent, and attaining a rate of real economic growth of around 5 percent.

2. The new measures are designed to achieve a realistic exchange rate system; to provide a more rational framework of cost-price relationships for selected export crops, petroleum products, and the public utilities; to speed up the rehabilitation of parastatals under the IDA-financed second reconstruction credit; and to tighten fiscal and credit policies in the second half of the program period. The latter takes into account our desire to achieve a relatively smaller overall BOP deficit than was initially programmed, so that even without the earlier planned debt relief, the originally programmed increase in official reserves can be achieved. The new measures that have been adopted and their background are set out below in five sections that deal with (I) external policies and exchange arrangements; (II) price policies; (III) production policies and operations of parastatals; (IV) fiscal policies; and (V) domestic credit policies. Section (VI) summarizes the performance criteria for the second half of the fiscal year.

I. External Policies and Exchange Arrangements

3. The Government's external objectives for 1983/84 are to reduce the overall BOP deficit by one-half to a maximum of US$34 million, decrease the level of its external arrears through cash payments by a net amount of US$20 million, and increase gross official reserves by at least US$15 million by the end of the program period.

4. To achieve the targeted reduction in the BOP deficit, the financial program had initially aimed at limiting the external current account deficit to US$156 million and at mobilizing net capital inflows of US$122 million (including an originally estimated debt relief of US$15 million). The Government intends to seek debt relief from its official creditors through the Paris Club by end of December 1983.

However, even if the envisaged debt relief is not forthcoming, the target of reserve accumulation will be maintained. The capital account surplus will be lower than originally programmed by the amount of debt relief expected from the rescheduling. The adjustment will take the form of reducing sales of foreign exchange at the second window, and hence lowering non-oil imports and service debits, while maintaining payments for debt service, arrears reduction and oil imports. With cash export earnings expected to yield US$9 million more than initially programmed (from cotton and nontraditional exports), the current account deficit is now projected to be reduced by US$31 million to US$125 million in 1983/84, and the overall deficit by US$15 million to US$19 million. These estimates allow for the Bank of Uganda to continue to sell an average of at least US$3.0 million per week during the program period, in accordance with the performance criterion for such sales.

5. Between the first auction of the program period July 8 and November 11, 1983, the ratio of the second window rate to that at the first window narrowed from 1.85 to 1.60. The rate at the first window was depreciated by 24 percent, while that at the second window depreciated by 12.5 percent. It is the intention of Government to adopt appropriate measures to restrain demand at window two with a view to achieving unification in accordance with the program's initially agreed timetable and targets for the ratio between the two rates.

6. The implication of lower than initially assumed sales of foreign exchange at the second window is that for a given demand for foreign exchange the second window rate will tend to be more depreciated. Ceteris paribus, therefore, it is expected that the dual exchange system will be unified at a more depreciated level than initially envisaged. To facilitate the unification of the two windows and to minimize the inflationary impact of a more depreciated rate, the stance of fiscal and domestic credit policies will be tightened, (See sections IV and V below). To increase the supply of foreign exchange auctioned, the Government's share in the second window sales will be reduced to an average of 25 percent per quarter, with a maximum of 30 percent per week in any two-week period. Nongovernment sales at the second window outside the auction will be reduced to a minimum. Before the end of 1983, sales of foreign exchange related to the operations of the Coffee Marketing Board and the Lint Marketing Board will be transferred to the second window; as will the sales of foreign exchange for service payments and all goods imported by the oil companies, except super, regular, diesel, and kerosene. Moreover, with the larger than programmed depreciation of the exchange rates, adjustments will be made to the structure of producer prices and oil prices, (section II below) to ensure efficient resource allocation and encourage exports.

7. It is the Government's objective to prevent misallocation of scarce foreign exchange and improve the monitoring of export earnings. The Government will take steps to improve customs administration and is considering an appropriate restructuring of customs taxes to discourage imports of nonessential goods. In this regard, the Government is awaiting the report of the recent Fund technical assistance mission. As was agreed earlier, with a view to eliminating leakages in export proceeds, the Government will shortly take steps to rely on export surveillance operations.

8. The Government is committed to reducing the level of external arrears through cash payments by a net amount of at least US$20 million in 1983/84. It is expected that all remaining guaranteed letters of credit will be paid by the end of the fiscal year. In order to limit the increase in the debt burden, foreign borrowing on nonconcessional terms will continue to be limited. Attempts will be made to reschedule the immediate debt service burden of some bilateral loans outside the auspices of the Paris Club. The External Debt Management Office has been established within the Bank of Uganda and it is the Government's intention to make rapid progress in improving the quality and consistency of the external debt data. Revised estimates of outstanding debt and arrears by creditor and type of loan, and of the debt service and disbursements schedule to 1990/91, will be provided to the Fund staff by end-December 1983. In order to ensure that all foreign borrowing is subjected to prior authorization by the Ministry of Finance and the Bank of Uganda, a Borrowing Committee will be established before January 1, 1984 to review proposed loans. All potential lenders and borrowers will then be advised that unauthorized debts will not be honored.

II. Price Policies

9. The producer prices for the traditional export crops were adjusted in two stages in May and July 1983. Compared to their April levels the producer prices were increased by 60 percent for coffee (kiboko), 50 percent for cotton, 150 percent for tea, 50 percent for tobacco, 300 percent for cocoa. Since coffee production accounts for nearly 96 percent of export proceeds and is substantially higher than the ICO quota, one of our major objectives is to accelerate the export diversification process. To achieve this, the Agricultural Secretariat is currently undertaking a study of producer prices to formulate proposals for price adjustments for next year. Meanwhile, the Government has decided to increase by February 14, 1984, the minimum producer prices of the following major export crops:

Coffee	from U Sh 80/kg to U Sh 100/kg
Cotton	from U Sh 60/kg to U Sh 90/kg
Cocoa	from U Sh 80/kg to U Sh 130/kg
Tea	from U Sh 25/kg to U Sh 40/kg
Tobacco	from U Sh 150/kg to U Sh 200/kg

Moreover, steps will be taken to ensure that farmers are paid cash on delivery.

10. The Government intends to continue its policy of ensuring that the retail prices of petroleum products are set at levels that fully cover all costs and also the need for a reasonable level of tax revenues. As the cost of petroleum imports is expected to rise with the progressive depreciation of the rate at the first window, the Government has decided to increase the retail prices of petroleum products by no later than January 14, 1984 as follows:

Super	from U Sh 170/litre to U Sh 190/litre
Regular	from U Sh 160/litre to U Sh 180/litre
Kerosene	from U Sh 100/litre to U Sh 150/litre
Diesel	from U Sh 110/litre to U Sh 150/litre

Moreover, prices will be reviewed regularly and, if necessary, they will be adjusted periodically to cover all costs. In addition to lubricants, all other petroleum products (including jet fuel) will be shifted from the first to the second window.

11. The Government is determined to pursue a policy of encouraging competition and increasing productivity. To this end, the following steps will be taken:

(i) Measures will be introduced to encourage greater competition among private and cooperative coffee processors.

(ii) Steps will be taken to abolish the system of requiring the Coffee Marketing Board (CMB) to provide guarantees to the commercial banks for crop financing extended to the processing unions; instead the Government will encourage the unions to negotiate their credit requirements directly with banks.

(iii) The activities of the Lint Marketing Board will be streamlined and it will be required to concentrate mainly on exporting cotton.

(iv) Ginneries will be encouraged to negotiate their credit requirements directly with the commercial banks.

(v) Uganda Tea Authorities (UTA) will discontinue the marketing of tea produced by tea estates with factories, as soon as the existing law is amended.

(vi) Steps will be taken to increase the number of appointed agents for distributing cigarettes produced by the National Tobacco Corporation.

III. Production Policies and Operations of Parastatals

12. The Government has continued its efforts to implement key projects in the agricultural, industrial, and transportation sectors under the Recovery Program (1982/83-1984/85). Since 1982/83, a total of US$498 million in external aid commitments have been mobilized for financing various projects. However, as various physical and financial constraints became evident during the first year of the implementation of the Recovery Program, the Government has decided to extend the Program for a further year. The Revised Recovery Program (1983/84-1985/86), which was recently finalized, aims at mobilizing a total amount of US$928 million in the form of external resources, of which nearly 25 percent are to be allocated to the agricultural sector, 32 percent to industry and tourism, 23 percent to transportation and communications, and the rest to the mining sector and social infrastructure. To accelerate the rate of project execution, emphasis will be put on removing physical and managerial bottlenecks, and improving government coordination of aid inflows.

13. The rehabilitation of various industries has benefitted from the second IDA reconstruction credit (US$75 million). Thus far nearly US$22 million have already been disbursed, and the remainder of the credit is expected to be fully utilized by about March 1984. Reflecting larger supplies of imported raw materials and spare parts, capacity utilization in industry has increased from an average of 20-25 percent to 30-35 percent, and in some industries such as cement, beer, and cigarettes, reached the level of 60 percent.

14. The Government has completed a review of its tariff policies for some of the major parastatals. On the basis of this review, the following tariff increases have been implemented:

- In November 1983, the tariffs for the external services of the Post and Telecommunications were increased by an average of 1,000 percent.

- The external passenger fares for Uganda Airlines were raised in two steps in August and November 1983, by a total of 50 percent above their July 1983 level.

In addition to these increases, the tariffs of the Uganda Electricity Board will be raised by 25 percent effective January 1, 1984. Tariff adjustments for the Railways and for the National Water and Sewage Corporation, which are presently being considered by the Government, will be implemented by end-January 1984.

15. A foreign consultant firm has already been selected to begin the study of the financial operations of selected parastatals by end-January 1984. Moreover, a verification committee has been established to examine ownership issues under the Expropriated Properties Act, and it has already submitted a preliminary report to the Government. In some cases, the

properties have been returned to their former owners, and ownership certificates are expected to be issued to them shortly. The Government recognizes that the speedy resolution of ownership claims will substantially reduce the size of the parastatal sector, increase efficiency and improve prospects for investment. In the meantime, the Government has onlent a part of the IDA II reconstruction credit to selected parastatals with a view to rehabilitating their operations.

IV. Fiscal Policies

16. The Government will be making a determined effort to hold the 1983/84 budget deficit to the programmed target of U Sh 28.9 billion (17.8 percent of total expenditure). Revised forecasts of revenues suggest an increase of more than 50 percent, as compared with an earlier estimate of 45 percent. In this circumstance, the growth rate of total expenditures (including all debt service) will be contained to about 52 percent in order to limit the overall deficit to the originally programmed level.

17. The overall fiscal deficit will be financed by a slightly higher than initially programmed real level of gross foreign borrowing (U Sh 25.3 billion) and by somewhat lower than initially targeted recourse to net domestic financing (U Sh 3.6 billion). More importantly, during the fiscal year the Government will be making a net repayment of U Sh 2.5 billion to the banking system, and other domestic resources will be mobilized through sales of U Sh 6.1 billion of Treasury bills. This will enable the Government to keep within the program's originally agreed ceilings for net credit to Government.

18. The larger than originally targeted increase in revenues is expected to be realized mainly because the depreciation of the window one exchange rate will yield higher trade-related receipts. The more favorable prices of exported commodities in domestic currency terms will increase coffee duty receipts and allow the imposition of a new cotton duty while providing for higher producer prices. On the import side, the continued depreciation of the window one rate will contribute to higher customs duties and sales taxes deriving from imports. Exchange profit receipts are also expected to be higher than programmed. The revenue gains from these sources will be only partially offset by lower petroleum taxes. Although retail petroleum prices will be raised to avoid any net subsidy, the Government has decided to accept a reduced level of petroleum taxes, as the first window rate is depreciated progressively towards the second window rate.

19. The increase in overall expenditure will be largely the result of a higher than programmed increase in debt service payments. The levels of nonwage recurrent outlays other than debt service payments and of development outlays will be reduced by about 6 percent and 2 percent respectively. In the event that additional external project aid is

mobilized, both development outlays and the fiscal deficit will be correspondingly higher. In accordance with the program, government wages were increased by 50 percent early in the year, but the average level of civil service wages still remains exceptionally low; the wage bill accounts for only 10 percent of all outlays, supporting the objective of freeing resources for the development budget.

20. Expenditure restraint will be facilitated by new administrative measures to control budgetary outlays. In the past, efforts to control expenditure have had limited success, as evidenced by the experiences of last year. Despite higher than progrmmed revenue collections, recourse to the banking system in 1982/83 exceeded budgetary targets by some U Sh 10 billion, and about U Sh 4 billion in unpaid arrears were created. To tighten expenditure controls and to ensure that the fiscal objectives are achieved, the Government will undertake a two-pronged program. To improve the monitoring of aggregate expenditure levels, the Government will take measures to expedite the closing of the large number of accounts at the Bank of Uganda (BOU). In the unlikely event that any new check appears more than six months after the end of the fiscal year, it will not be honored. A committee exists for monitoring the accounts for expenditure trends on a weekly basis. Further, we will continue our recent practice of utilizing the Treasury main Clearance Account only in exceptional circumstances and only after consultation with the Ministry of Finance. In regard to known domestic arrears, the Government will regularize those debts by providing U Sh 0.65 billion in cash for the immediate resolution of outstanding minor debts and guarantee the payment of all other accepted claims through the issuance of short-term bonds. To prevent the re-emergence of domestic arrears, the Government will reintroduce the practice of maintaining vote books and commitment registers for all government accounts, and establish the practice or reducing Treasury disbursements to government units which do not maintain budgetary accounts on a current basis. The Government has issued a presidential directive to notify all government units that further domestic arrears will not be honored by the Treasury, and will be the responsibility of the responsible officer at the Ministry which has incurred arrears.

V. Domestic Credit Policies

21. In order to contain the depreciation of the exchange rate at the second window and reduce pressures on the domestic price level and the balance of payments, the Government will continue its policy of reducing the rate of credit expansion during the program period.

22. The net foreign liabilities of the banking system are now projected to increase from U Sh 40 billion at the end of June 1983 to U Sh 93 billion at the end of June 1984, compared with the program's original target of U Sh 80 billion at the end of June 1984. Given this larger than expected increase in net foreign liabilities and our intention to maintain

the initial domestic credit targets of the program, broad money is expected to rise by only 3.3 per cent during 1983/84. The programmed increases in credit and broad money of 19.5 percent and 3.3 percent, respectively, compare with increases of 34 percent and 46 percent in 1982/83. The increase in credit will be used primarily to finance crop marketing, imports associated with the second IDA Reconstruction Credit, and other priority areas of domestic economic activity, while lending to commerce will be restrained. These policies are expected to contain the depreciation of the rate at the second window and the domestic inflation rate.

23. The Government recognizes the need to provide adequate credit on a timely basis for financing agricultural crops. In order to provide greater incentive to the commercial banks for lending to agriculture, and export and manufacturing, the lending rates to those sectors will be raised by 2 percentage points. Simultaneously, the rates on savings and time deposits will also be raised by 2 percentage points.

24. There is a growing need to provide medium-term financing for projects to be undertaken in the Recovery Program. To establish appropriate debt instruments and related Bank of Uganda rediscounting facilities, the Government has requested technical assistance in this area from the Fund's Central Banking Department.

VI. Performance Criteria and Review Clause

25. The implementation of the package of measures described in this Memorandum will be subject to the following performance criteria:

(a) Total net domestic credit, which was programmed not to exceed U Sh 76.8 billion by December 31, 1983, will not exceed U Sh 81.1 billion by March 31, 1984. The indicative ceiling for June 30, 1984 is U Sh 84.1 billion.

(b) Net credit to Government, which was programmed not to exceed U Sh 41.6 billion by December 31, 1983, will not exceed U Sh 42.1 billion by March 31, 1984. The indicative ceiling for June 30, 1984 is U Sh 42.6 billion. The ceiling for March 31, 1984 and the indicative ceiling for June 30, 1984 will be reduced (raised) by the excess (shortfall) of the co-cumulative profits from the operation of the second window from July 1, 1983 above (below) the projected amounts of U Sh 9.7 billion and U Sh 10.4 billion, respectively.

(c) At the second window, in addition to selling a minimum of US$78 million between July 1, 1983 and December 31, 1983, the Bank of Uganda will sell a minimum of US$117 million between July 1, 1983 and March 31, 1984, and of US$156 million between July 1, 1983 and June 30, 1984.

(d) From January 1, 1984 through March 31, 1984, and as an indicative ceiling for the period from January 1, 1984 to June 30, 1984, the contracting of new public and publicly-guaranteed external debt will not exceed US$30 million for maturities of 0-12 years and US$10 million for maturities of 0-6 years. These limits will not apply to concessional loans, loans contracted to refinance existing debts, capital contributions to international financial institutions and to normal trade credits of less than one year. Concessional loans are defined as those by the DAC of the OECD, while normal trade credits are defined as credit gained from the supplier to be repaid following shipment.

(e) The level of external arrears will be reduced through cash payments by a net amount of no less than US$5 million between January 1, 1984 and March 31, 1984 and, as an indicative target by at least US$ 10 million between January 1, 1984 and June 30, 1984.

(f) During the fiscal year 1983/84, the level of known domestic arrears will be reduced through cash payments by a net amount of no less than U Sh 0.65 billion, of which U Sh 0.5 billion will be paid by March 31, 1984.

(g) Before June 30, 1984, the Government of Uganda will review with the Fund the progress made toward the unification of the dual exchange rate system and understandings will be reached on exchange rate policy.