development initiatives

the 2017/18 Uganda budget

what is in for the poorest and most vulnerable people?

briefing paper

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Background

Uganda's reduction of poverty rates over the last 25 years suffered a setback this year. According to the Uganda National Household Survey 2016/17 report, poverty increased from 19.7% in 2012/13 to 27% in 2016/17. In absolute terms, the number of poor people increased from 6.6 million to 10.1 million in these years. This increase is attributed to effects of climate change that has affected agricultural production for most households that had previously been able to move above the poverty line. The country faces development challenges ranging from a weak economy with a seemingly weak trade and investment sector, to social and environmental challenges like increasing impacts of climate change.

As the budget is the government's main instrument for financing activities that can address these challenges, it is critical that the fiscal policies within it are studied in-depth, to determine whether key decisions on resource mobilisation and investments are made towards the goal of addressing these challenges. Understanding how the government budget responds to the needs of the poorest people and how it is tackling wider issues relevant to reducing poverty and vulnerability in the country is therefore very important.

This paper summarises key messages from our analysis of the Uganda national budget for the 2017/18 financial year. It looks at funding priorities in the year and deduces the extent to which the country's financial investments are oriented towards poverty-reducing sectors.

Is Uganda's budget pro-poor?

The 2016 Commitment to Equity report and the 2017 International Monetary Fund (IMF) Policy Support Instrument report highlight that public spending in Uganda is not being sufficiently redistributive in nature nor leading to inclusive growth. This is because the country's revenue expenditure is not sufficiently targeting the poorest. For the past three years Uganda’s budget and resource allocation shows high priority towards infrastructure spending. To reduce poverty and sustain growth, the IMF recommends higher social spending and stronger social safety nets such as health insurance and pension schemes for inclusive growth, rather than putting emphasis on large infrastructure projects and the energy sector as drivers of growth and development.

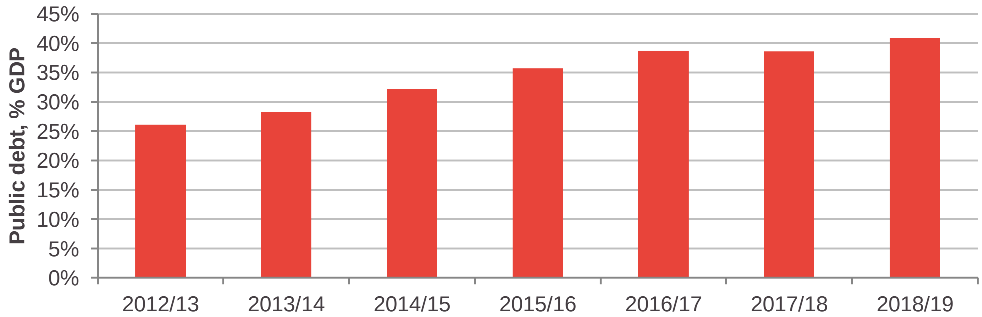
Uganda's development plans such as the National Development Plan II and Uganda Vision 2040, while emphasising transformation and industrialisation, stress the importance of 'inclusive growth' to create sustainable development. However, the 2017/18 budget allocations are skewed towards infrastructure development and the energy sector, compromising the efforts for inclusiveness. From our analysis of the 2017/18 budget we arrive at the following conclusions and recommendations:

- **Government's revenue mobilisation** effort is below regional neighbours constraining its fiscal space and limiting the resources it can allocate to fund commitments to sustainable development. In its quest to improve this, government has continued to provide progressive reforms in areas that reduce the burden of taxation on the poorest. This is commendable and would do well to be maintained.
- **Government is heavily borrowing** from non-concessional sources to drive its industrialisation policy because of reduced fiscal space to finance its increased expenditure. While debt level is still in sustainable, continued preference for this mode of financing will cause public debt to rise leading to further increase in interest payments and debt vulnerability. Therefore, the government could ensure financing is appropriately used (both in the type of finance and the investment decisions).
- **Focus on 'industrialisation'** with hope that its medium-term payoffs will result in trickle-down benefits for social sectors assumes inclusiveness, good utilization and economic-geography informs use of these investments. The outcomes of such assumptions are not clearly known and this risks leaving key sectors relevant to the poorest deprioritised, at least in the immediate term.
- **Government continues to reliance significantly on development partner support** in key sectors relevant to the poorest even though overall the it is reducing dependence on development partners. This is a vulnerable position given current policy environment around Official Development Assistance. Therefore, development partners could be cognisant of needs by supporting priority areas, disbursing in a timely fashion and providing predictability of funding to help government planning. Also, to tackle issues around climate change, the government could look at alternative sources of funding to support mitigation and adaptation efforts.

The Uganda 2017/18 budget: highlights

- **Increased budget:** Total budgeted government expenditure for the 2017/18 financial year is Uganda shillings (UGX) 22 trillion, an increase in nominal terms from the previous budget of UGX 20.5 trillion.
- **Increasing public debt** to gross domestic product (GDP) ratio (currently at 38%) (Figure 1), while lower than some countries in the region such as Kenya and Tanzania, is still concerning. Rising levels of interest payments risk reducing fiscal space for government, which may inhibit spending in areas responsive to the needs of the poorest. Interest payments now rival, or even indeed surpass, allocation to some entire sectors.
- **Overall resource envelope.** The government will borrow UGX 954 billion (3.2% of the total budget) domestically. The domestic borrowing grew by 175.7% from the previous financial year's UGX 346 billion.

Figure 1: Increasing public debt is driven by increased borrowing



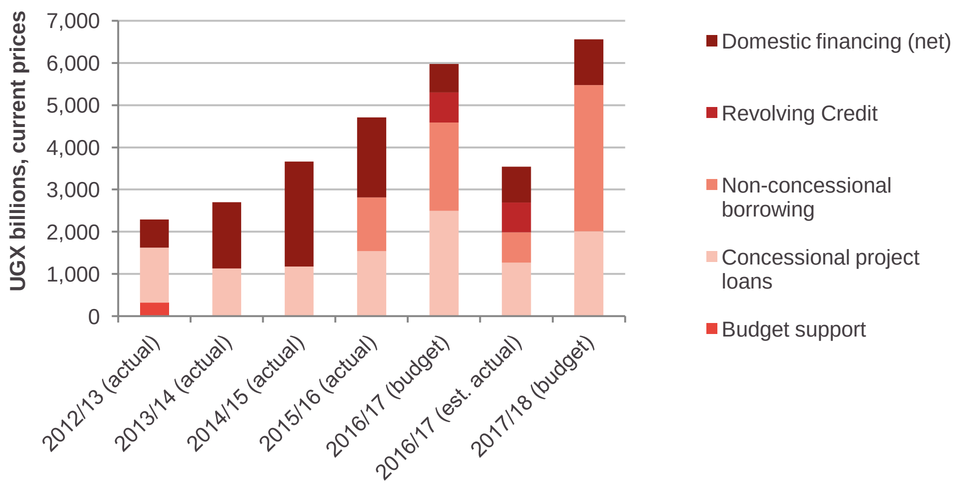
Source: IMF Country Report No 17/206 and Ministry of Finance 2017/18 approved estimates of revenue and expenditure.

- **Government revenue:** Since 2012/13 government revenue has increased in nominal terms as a proportion of GDP (12.7% in 2012/13 to 16.5% in 2017/18). The central factor behind this increase has been improvements in tax collection, both in direct (income tax) and indirect sources (VAT, excise and international trade taxes), highlighted in Figure 2. Grant funding continues to provide significant support to government revenue, at around 10% of the total, and is predominantly project based. While increases in tax collection have provided more fiscal space to facilitate increased spending, the government recognises there is potential to increase it further, given the relatively low proportion of non-grant revenue as a percentage of GDP. Meanwhile other countries in the region such as Rwanda and Kenya have higher proportions (17.6% and 20.5% respectively). Hence, government could:

1. increase revenue mobilisation to manage debt and public service provision
2. in the process, maintain its relatively progressive tax regime.

Financing: Even though more than half of the 2017/18 budget was raised domestically, Uganda continues to rely heavily on donors and other public financing mechanisms to meet its spending obligations. External project financing for 2017/18, for example, stands at UGX 7,077 billion, equivalent of 24.3% of the total budget. It grew by 8.6% from the 2016/17 figure of UGX 6,525 billion. The government of Uganda continues to use a range of different financing mechanism to balance the budget (see Figure 2). In 2012/13 the largest of these were external concessional budget support and project loans, which, combined, were larger than net domestic finances.

Figure 2: Improved direct and indirect tax collection has driven revenue increases



Source: IMF Country Report No 17/206 and Ministry of Finance 2017/18 approved estimates of revenue and expenditure

- **Prioritisation**: From this overall perspective, and as highlighted by the latest IMF staff report (No 17/206), the government is prioritising infrastructure and industrialisation development mostly using non-concessional borrowing, whereas investment in social development has not increased. Some key sectors with high relevance to the poorest saw funding cut. The government could instead ensure sufficient funding commitment to social sectors in order for development to be more inclusive and responsive to the poorest.

Our analysis looks in detail at selected sectors, to understand their projects and programmes and how the 2017/18 budget allocations respond to the needs of the poorest and relate to the government's commitments outlined in the second National Development Plan (NDPII).

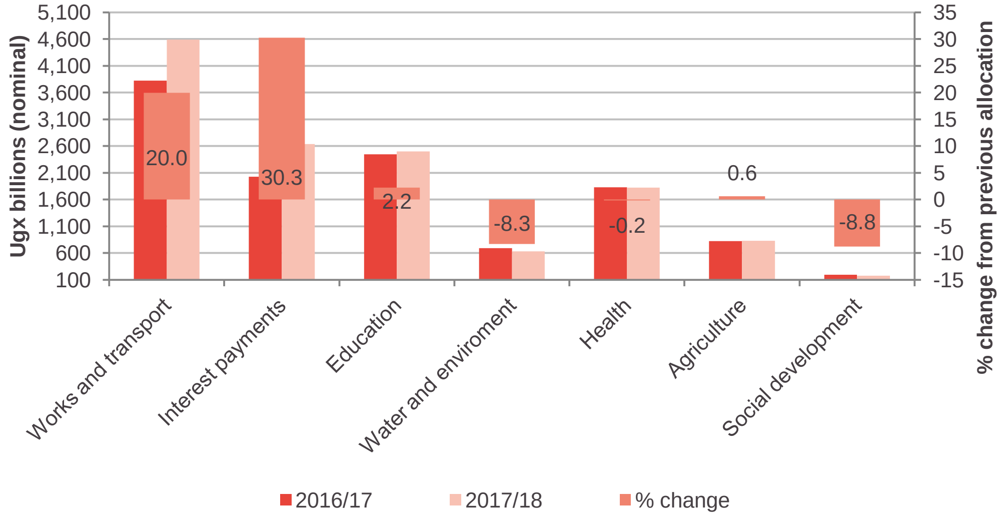
Spending on poverty-reducing sectors

While many areas of government spending could be classified as relevant to the poorest and most vulnerable people (e.g. security-peace-economy nexus), it is important to stress that some areas could benefit from direct investing of resources to address challenges of poverty and vulnerability. The trickle-down effects of interventions in other sectors may be insufficient in responding to events, such as disaster and other emergencies, that exacerbate people's poverty and vulnerability.

Since it is not possible to conduct an extensive analysis on all government allocations, we chose in this paper to focus on those which have most potential to disproportionately benefit or exclude the poorest (Figure 3). The government of Uganda – for example through its Policy Support Instrument programme with the IMF – has set targets of expenditures on poverty alleviating sectors, which it defines as domestic public spending on health, education, water, environment and agriculture. These sectors together take up 26.5% of the country's total budget, based on the 2017/18 approved budget allocations. As Figure 3 shows, the agriculture, health, education and water sectors were allocated 3.8%, 8.4%, 11.5% and 2.9% of the budget respectively.

Although the country has exceeded its Policy Support Instrument targets each year since 2011/12, spending on education, health, pensions and social assistance as a proportion of economic output is significantly lower than the average of other East African countries.[1] This therefore calls into question not only the ambition of this target, but also the definition, given that key areas for poverty alleviation like social protection and rural infrastructure are excluded.

Figure 3: The 2017/18 budget allocations to key sectors deemed more responsive to the poorest will see only marginal increases, and some will see cuts



Source: 2016/17 and 2017/18 approved estimates of revenue and expenditure, Volume I, Ugandan Ministry of Finance

Agriculture

Agriculture remains the backbone of Uganda's economy and is identified by the NDPII as one of the five priority sectors with greatest multiplier effect.[2] The sector employs over 72% of Uganda's labour force,[3] with between 75% and 80% of total agricultural output and marketed agricultural produce coming from poor subsistence farmers.[4]

Allocations to agriculture in the 2017/18 budget

The agriculture sector was allocated UGX 828.5 billion in the 2017/18 budget, up slightly in nominal terms from UGX 823.4 billion in 2016/17, representing a 0.6% increase. Much of the sector resource allocation will go into financing the National Agricultural Advisory Services (NAADS) programme and secretariat, which take UGX 279.7 billion or 34% of the total sector budget.

External financing contributes significantly to the sector, making up to 25% of the total, with the Ministry of Agriculture, Animal Industry and Fisheries and the National Agricultural Research Organisation budgets 48% and 54% respectively financed from external sources.

Government's current agriculture sector focus is on the Operation Wealth Creation initiative under NAADS, in which heavy investment has gone into agricultural input (seeds and planting materials) purchase and distribution. The sector received slight higher funds in 2017/18 compared with 2016/17.

Implications

A key challenge for the government is to strategically invest in modernising agriculture to transform it from the predominantly rain-fed low external input subsistence farming methods to modern climate smart and market-oriented production. This could be through increased resource allocations and investments in small-scale irrigation; training of farmers in new methods of production that are less prone to climate shocks; increased investment in pro-poor agricultural research; technology transfer and fixing gaps in delivery of quality extension; ensuring greater efficiency in implementing on-going programmes like NAADS; and increasing poor farmers' access to affordable credit.

Health

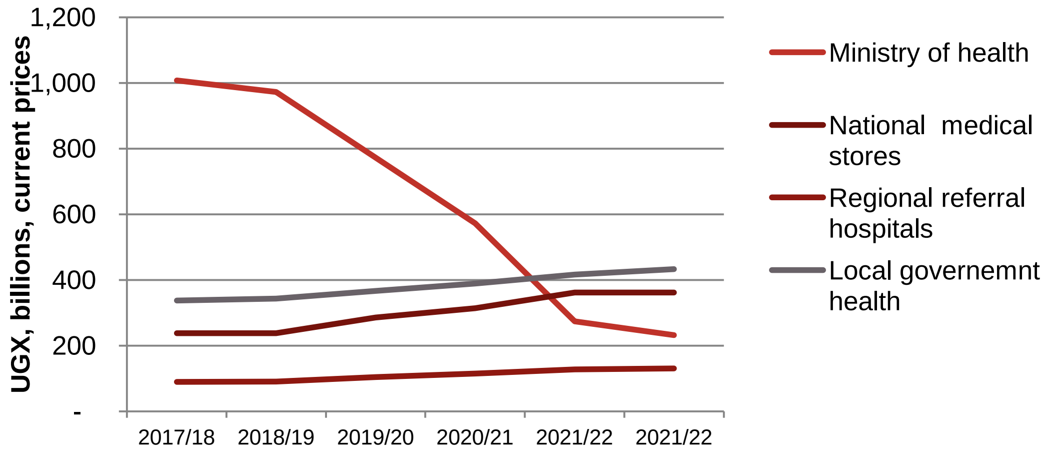
Social health protection is of utmost importance for sustainable poverty reduction because sickness is among the most frequent causes of poverty in developing countries and poverty is one of the greatest health risks facing low-income countries.[5] Targeted interventions in promoting good health among the population are, therefore, vital in breaking the vicious circle of poverty in which one-third of Uganda's population is trapped. The NDPII identifies health as a key sector in meeting Uganda's medium-term development targets through human capital development.

The government's target of attaining universal health coverage has been supported with increasing resource allocations to the health sector. The increments are majorly on account of the rising wage bill and the on-going development-partner supported projects in the sector.[6] Government resource allocation for health as a percentage of the total government budget has averaged at about 8% from 2010/11 to 2015/16, which is 1.8% short of the Health Sector Development Plan target of 9.8%.

However, Uganda's per capita health expenditure at an average of US$56 is low compared with neighbours like Kenya (US$77) and Sudan (US$129)[7] it is also far below the five-year Health Sector Development Plan-recommended minimum of US$73 per capita in 2015/16.[8]

The health sector was allocated UGX 1,824 billion for 2017/18, which is 0.2% less than the 2016/17 allocation. Analysis of long-term financing projections also shows that health sector budget allocation is on a downward trend from the current year into 2021/22 (see Figure 4).[9]

Figure 4: Declining projected allocations to the health sector



Source: Approved budget 2017/18 sub-programmes and medium-term expenditure framework

- Government's renewed focus on health infrastructure development and construction of new buildings and equipment, especially for hospitals, has skewed financing for health facilities away from recurrent costs for utilities and maintenance.
- Donor funding to the health sector is very high at 50% of total health sector budget though the level of external financing is projected to gradually drop to 6% by 2021/22. However, 50% of the current budget relies heavily on donor support, which brings uncertainty about future funding if government does not stick to its commitment of increasing domestic financing in the medium term.
- High reliance of the health sector budget on external donor financing poses a significant risk for sustainability. While donor support to the health sector budget remains critical in addressing government's resource gaps, this very high proportion of external financing comes with challenges.[10] That is because government cannot channel donor resources to finance key healthcare priorities like universal access to family planning, health infrastructure development and reduction of maternal, neonatal and child morbidity and mortality. This dynamic, if not changed, could affect poor people the most since they are worst affected by poor quality health service delivery.

Implications

Commensurate resource allocations and efforts to address challenges and constraints within public healthcare systems are needed to improve poor people's access to quality healthcare. Government's increased per capita healthcare spending is likely to cut back on high prevalence of out-of-pocket health expenditure and people's preference of private providers over government health services centres. To be relevant and responsive to the needs of the poorest, the 2018/19 budget could address resource-related gaps in the health sector by improving allocations to address key challenges and gaps in medical supplies to health centres, quality assurance and monitoring of service delivery. These would shape progress towards increasing access to quality healthcare for the poorest.

Education

According to the World Bank, education is among the most powerful instruments for reducing poverty and inequality because it lays the foundation for sustainable economic growth. The UN Educational, Scientific and Cultural Organization (UNESCO)[11] also argues that no country has succeeded in reducing poverty without first educating its population. This is because education outcomes complement gains in other social sectors to deliver positive outcomes in poverty reduction. Education is also relevant to the poorest because it is among the factors limiting their participation in Uganda‘s labour market, which according to the NDPII faces a shortage of requisite skills. Universal primary education is one of government’s main policy tools for poverty reduction and human development.[12]

Allocations to the education sector

The education sector was allocated UGX 2,501 billion representing a 2% increase in resource allocation from the previous year’s budget. The largest shares of the education sector budget were allocated to three programmes: pre-primary and primary education, secondary education and delivery of tertiary education programmes. While education sector resource allocation increased by 2% in nominal terms from 2016/17 to 2017/18, some sector programme’s resource envelope declined. For example, resource allocation to all sub-programmes and projects under the Ministry of Education and Sports declined. Most affected sub-programmes are pre-primary and primary education and higher education whose resource envelopes declined by 22% each from 2016/17 to 2017/18.

Implications

The government could proactively work towards addressing access and quality gaps for the poor in all levels of education to progress well in the direction of attaining its NDP goal of making education and skills development serve as the foundation for sustainable economic growth. To help serve the interests of the poorest Ugandans, budget resource could be allocated towards monitoring delivery of quality education services, improving education infrastructure for the poorest regions, streamlining pre-primary education into the formal public education curriculum, and including adult literacy and skills development programmes in the national education system.

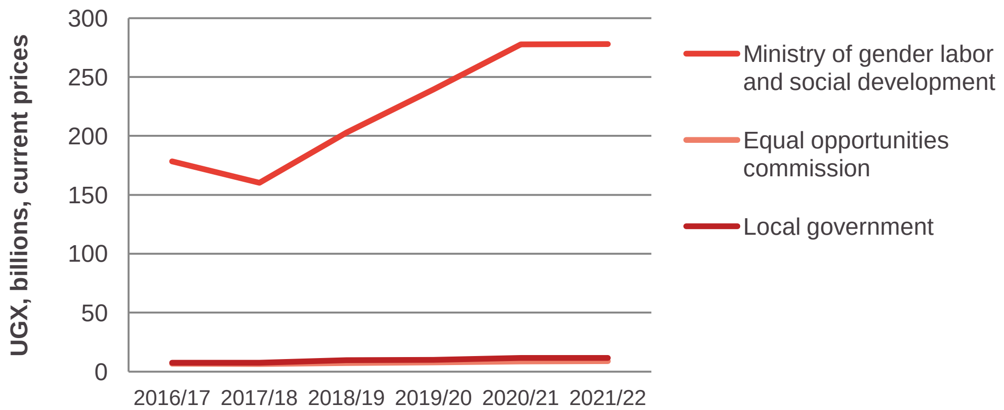
The social development sector

On average, a developing country spends between 1% and 2% of GDP on social safety nets per year. Simulations from the World Bank and Uganda’s Expanding Social Protection Programme show that at a cost of about 0.15% of GDP, Uganda could reduce poverty by 2.6% by targeting children of school age. At a cost of 0.9% of GDP, poverty prevalence could be reduced by 8.6% by directing grants to children aged between 0 and 2. Financing can initially come from a joint effort by government and donors (potentially through the World Bank, UK Department for International Development, World Food Programme, UN Children's Fund and other bilateral partners). The government could create fiscal space in its currently constrained budget in the context of its revenue enhancing strategy. The forthcoming oil wealth will facilitate this task in the medium term.

Allocations to the social development sector

The social sector was allocated UGX 175.8 billion for 2017/18 representing a 9% decline from the previous year. The Youth Livelihood Project whose budget was cut by UGX 8.4 billion was most affected by the decline in the social sector budget.

Figure 5: Allocations to the Ministry of gender labour and social development expected to increase, but allocations to local governments will remain stagnant in the medium term



Source: Approved budget 2017/18 sub-programmes and medium-term expenditure framework

Implications

While this year's resource allocations to the Ministry of Gender, Labour and Social Development declined by 10% from 2016/17, allocation over the medium term reflect significant increases (UGX 277.9 or 73% in 2021/22 from 2017/18, Figure 5). Government will move in line with its medium-term commitment if it adheres to and allocates resources as projected. However, budget re-allocations and cuts as observed from 2016/17 to 2017/18 if replicated into the next year's budget could derail government from achieving its medium-term social sector targets.

Infrastructure

Infrastructure and particularly transport play a critical role in a country's economic growth and development. Efficient and effective transport infrastructure and services facilitate domestic and international trade; contribute to national integration; and provide access to markets, jobs, healthcare, education and other essential social services[13] that directly benefit the poorest. The NDPII recognises that an efficient transport system is a pre-requisite for economic and social transformation; it also recognises that Uganda's infrastructure – especially the road network – is inadequate and cannot enable significant growth in many sectors, particularly agricultural production, which requires good rural road networks to connect production to markets.

The UGX 4,587 billion allocation to the works and transport sector is largely consistent with allocation in the previous three financial years and shows a clear prioritisation of national infrastructure development projects as the engine for economic growth.

Implications

While investments in key national roads projects are predicted to have positive impacts on Uganda's economic growth in the medium and long term and play a key role in Uganda's economic development, they can also be a key driver of unequal growth. Lower allocation of funding for district, urban and community access road sub-programmes mean that less priority is given to improving the quality of rural and community access roads. Yet poor maintenance of such roads was pointed out as one of the key challenges facing Uganda's transport sector.

Conclusion and recommendations

The focus of the 2017/18 budget is towards driving economic development through investment on major infrastructure in the works, transport and energy sector, rather than investing in social sectors and infrastructure that directly responds to the needs of the poorest people. While investment in infrastructure is vital for driving economic growth, the focus could instead be on promoting inclusive growth as outlined in the NDPII.

Overall the increase in Uganda’s national budget presents the government with greater opportunity for allocating resources towards addressing the needs of the poorest. However, at present, allocations are skewed towards infrastructure development and the energy sector. For allocations to address the needs of the poor, we make the following recommendations to the government and its partners:

- **Revenue mobilisation** – Government's efforts in revenue mobilisation are below regional neighbours and are constraining its fiscal space, limiting the resources it can allocate to fund commitments to sustainable development. In its quest to improve this, it has continued to provide progressive reforms in areas that reduce the burden of taxation on the poorest. This is commendable and would do well to be maintained.
- **Role of non-concessional finance** – Government is heavily borrowing from non-concessional sources to drive its industrialisation policy because of reduced fiscal space to finance the policy. While debt is still in sustainable levels, continued preference for this mode of financing its priorities will cause public debt to rise, which could lead to rising interest payments and debt vulnerability. Therefore, the government could ensure financing is appropriately used (both in the type of finance and the investment decisions).
- **Focus on 'industrialisation'** with the view that long- and medium-term payoffs of such focus will result in trickle-down benefits for social sectors assumes inclusiveness, good utilisation and economic-geography informed use of these investments – assumptions whose outcomes are not clearly known. This could risk leaving key sectors relevant to the poorest deprioritised, at least in the immediate term.
- **Development partner support** – Government continues to rely significantly on development-partner support in key sectors relevant to the poorest, even though overall it is reducing dependence on development partners. This is a vulnerable position given current policy environment around official Development Assistance. Therefore, development partners could be cognisant of needs by supporting priority areas, disbursing in a timely fashion and providing predictability of funding to help government planning. Also, to tackle issues around climate change, the government could look at alternative sources of funding to support mitigation and adaptation efforts.

Notes

[1] IMF, 2017. *IMF Country Report No. 17/206*: Uganda. Available at: https://www.imf.org/en/Publications/CR/Issues/2017/07/12/Uganda-2017-Article-IV-Consultation-and-Eighth-Review-Under-the-Policy-Support-Instrument-45069
[2] Government of Uganda. 'NDPII (2015/16–2019/20)', 2015. Available at: http://npa.ug/wp-content/uploads/NDPII-Final.pdf
[3] UNDP, 2014. *Poverty Status Report 2014.* Available at: http://www.ug.undp.org/content/dam/uganda/docs/UNDPUg2014 - POVERTY STATUS REPORT 2014.compressed.pdf
[4] Government of Uganda. 'NDPII (2015/16–2019/20)', 2015.
[5] OECD, 2009. Available at: http://www.oecd.org/dac/povertyreduction/43280818.pdf
[6] Annual Health Sector Performance Report 2015/16. Available at: http://health.go.ug/download/file/fid/1069
[7] Available at: http://data.worldbank.org/indicator/SH.XPD.PCAP?contextual=region&locations=TZ-UG&name_desc=true
[8] Annual Health Sector Performance Report 2015/16.
[9] The decline in the Ministry of Health allocations is because of a fall in donor funding. This uncertainty around commitments beyond the short term (two years) limits the government's ability to plan for the longer term in the health sector.
[10] Available at: https://www.ncbi.nlm.nih.gov/pmc/articles/PMC3178194/
[11] Available at: http://www.unesco.org/education/poverty/news.shtml
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[13] Ministry of Works & Transport. Annual Sector Performance Report 2015/16. Available at: http://www.works.go.ug/wp-content/uploads/2016/10/Final-MoWT-ASPR-Report-2015-16.pdf

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