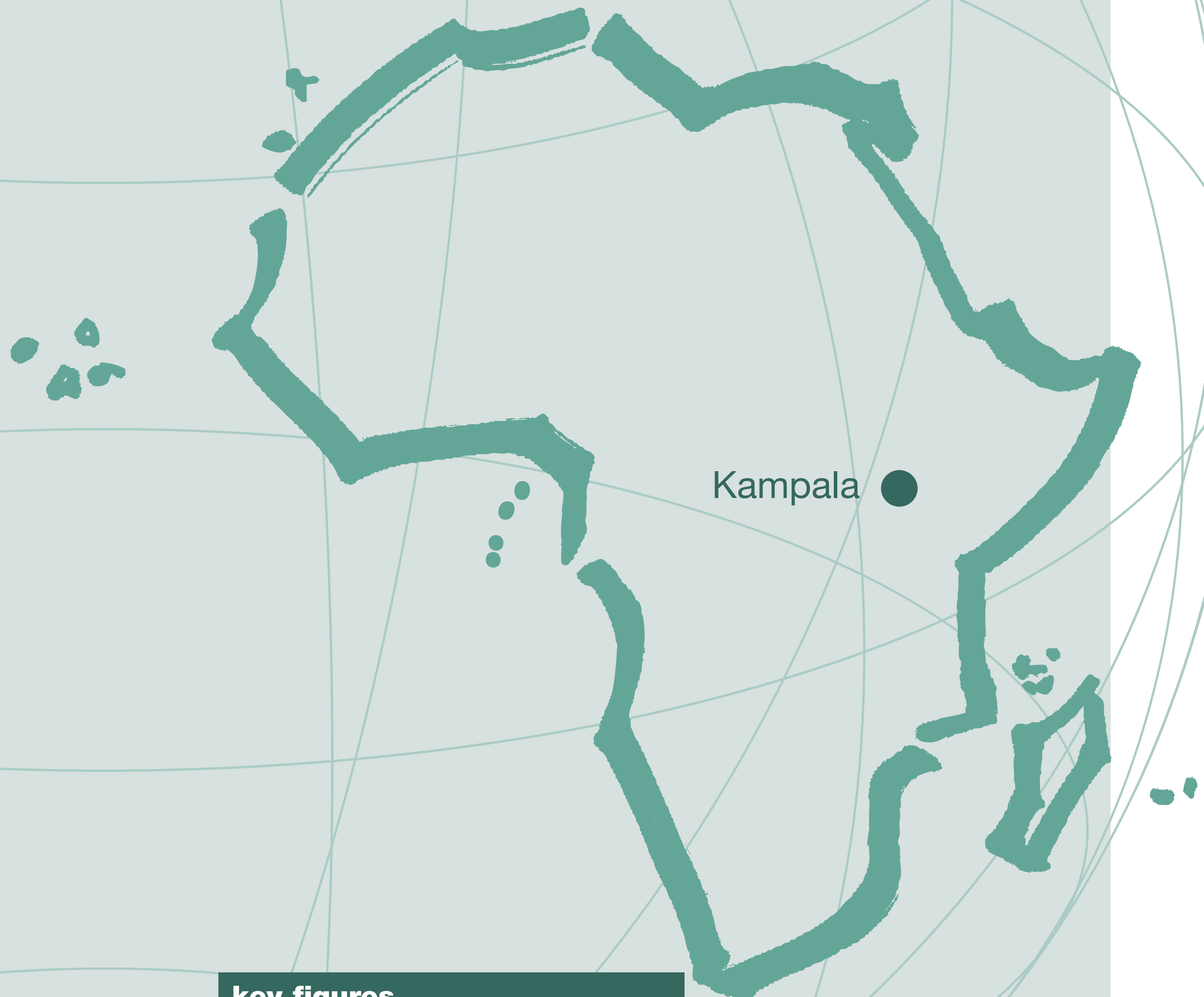
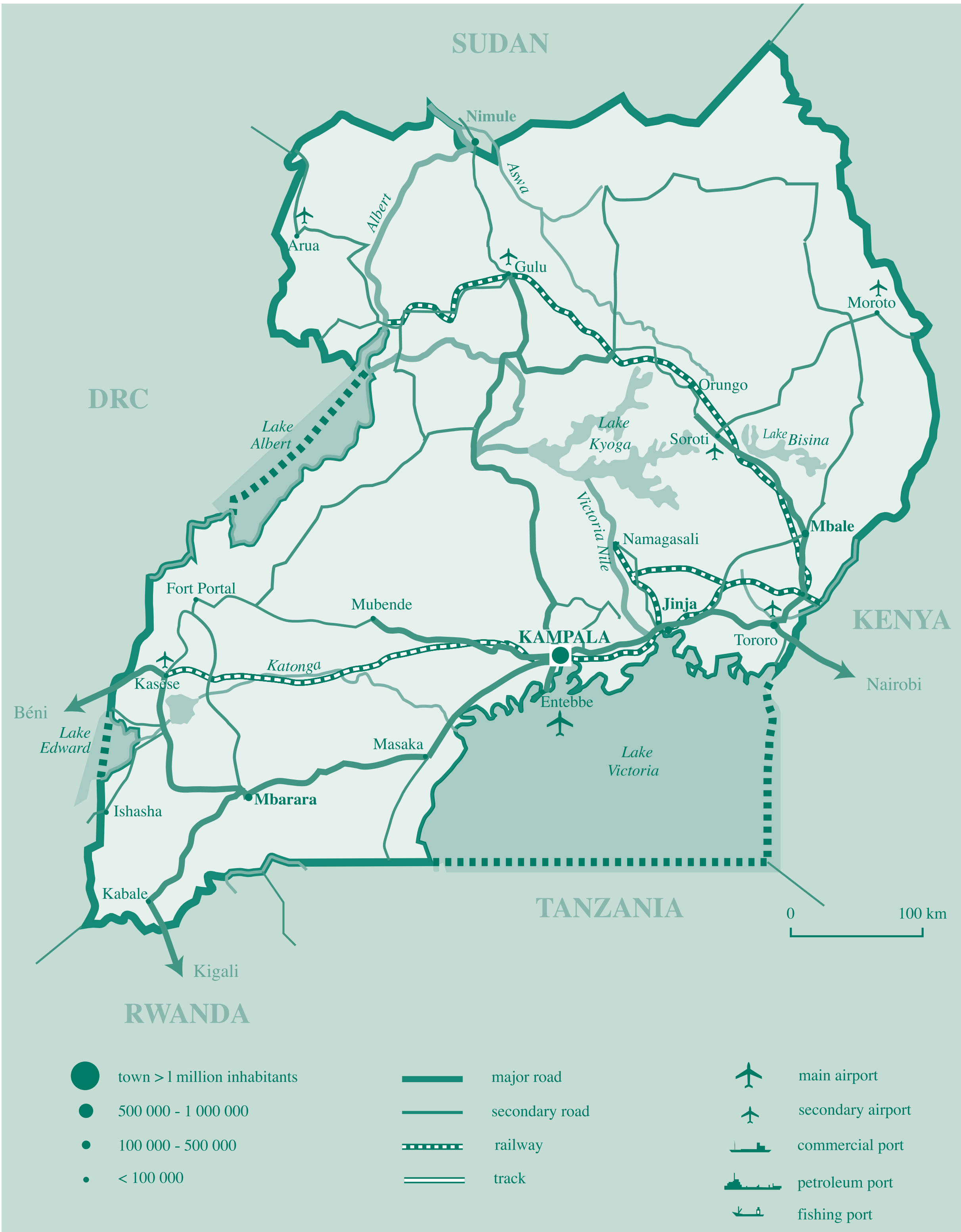
Uganda



key figures

• Land area, thousands of km²	241
• Population, thousands (2007)	30 884
• GDP per capita, USD at constant 2000 prices (2005/06)	273
• Life expectancy (2007)	51.5
• Illiteracy rate (2007)	26.8

Uganda


SUDAN
DRC
KENYA
TANZANIA
RWANDA
Nimule
Aswa
Albert
Arua
Gulu
Moroto
Orungo
Lake Kyoga
Soroti
Lake Bisina
Lake Albert
Victoria Nile
Namagasali
Mbale
Fort Portal
Mubende
Jinja
KAMPALA
Tororo
Nairobi
Katonga
Kasese
Béni
Entebbe
Lake Edward
Masaka
Lake Victoria
Ishasha
Mbarara
Kabale
Kigali
0
100 km
town > 1 million inhabitants
500 000 - 1 000 000
100 000 - 500 000
< 100 000
major road
secondary road
railway
track
main airport
secondary airport
commercial port
petroleum port
fishing port

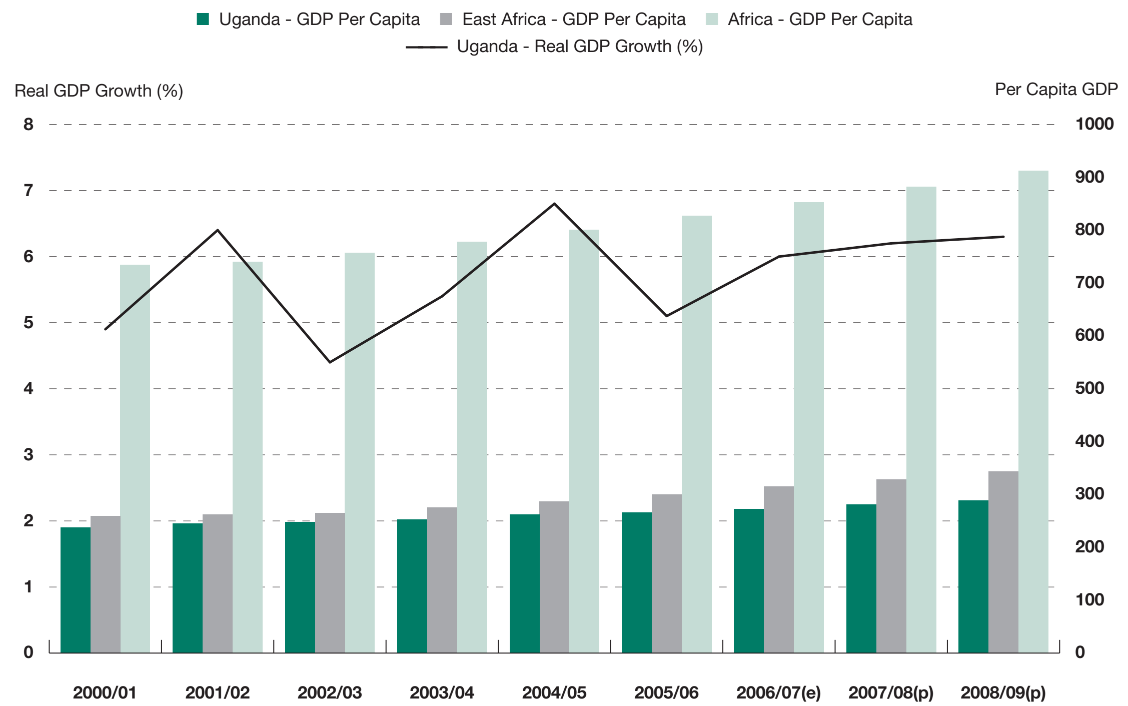
Uganda

UGANDA CONTINUES TO SUSTAIN THE SUCCESS of the last two decades with the economy characterised by high growth and low inflation. The real GDP growth rate was 6.0 per cent in the 2006/07 fiscal year and is projected to rise to 6.2 per cent in 2007/08. Economic performance in 2006/07 benefited from increased export diversification and investment in construction and services. The base of Uganda's growth seems to be broadening as reflected in the introduction of new products, exports, technology and movement of labour into new occupations. But growth remains below potential because of infrastructure constraints, especially the energy deficit, and shocks as a result of flooding that destroyed crops and transport infrastructure in some areas.

As in previous years, sound macroeconomic management and pro-market reforms supported by large inflows of concessional credit and grants from donors helped Uganda to maintain overall macroeconomic stability in the face of strong external and internal shocks, including increasing oil prices and declining terms of trade. Banking-sector reforms and the licensing of four new commercial banks led to higher lending to the private sector, but high interest rates and spreads are major constraints. Growth in employment in manufacturing and large-scale commercial agriculture remains limited and much

Fiscal decentralisation and financial autonomy are essential for improved service delivery.

Figure 1 - **Real GDP Growth and Per Capita GDP**
(USD at constant 2000 prices)



Source: IMF and local authorities' data; estimates (e) and projections (p) based on authors' calculations.

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of the growth in output and employment has been in informal and micro enterprises.

Uganda continues to enjoy political stability and has successfully hosted the Commonwealth Heads of Government Meeting (CHOGM) in November 2007. Deepening decentralisation is strengthening political and economic management and helping to improve the delivery of public services. The political environment has improved following the agreement with the Lord Resistance's Army (LRA) on cessation of hostilities signed in August 2006 and the new security accord with the Democratic Republic of Congo (DRC) signed in September 2007. However, large regional inequalities – with the eastern and northern regions trailing behind – and the security situation along the DRC border remain major concerns.

Despite economic and political challenges, Uganda has made notable improvements in social well being. This has been manifested in terms of increased per capita income, improved education (including universal primary and secondary education programmes), better health outcomes and continued reduction in HIV/AIDS infection rates. But, due to limited economic diversification and heavy dependence on subsistence agriculture, further significant progress in poverty reduction will be difficult. Uganda needs to strengthen and sustain measures introduced in recent years to improve governance and combat corruption in particular.

Recent Economic Developments

The Ugandan economy experienced robust 6.0 per cent growth in 2006/07, rebounding from the slowdown in 2005/06. Economic growth in 2006/07 was driven mainly by good performance in the services sector, which registered a 9.5 per cent growth rate compared to 5.8 per cent growth for industry and 1.8 per cent for agriculture. The transport and communication sub-sector which expanded by 22.3 per cent continued to spur growth in services, followed by construction (11.3 per cent) and wholesale and retail services (9.7 per cent). Telecommunications was the fastest growing sub-sector (33.3 per cent) due to rapid expansion in mobile telephone services, while rehabilitation and maintenance of roads, as part of the 10-year road-sector development plan, boosted growth in transport.

Despite the impact of flooding, growth in the agricultural sector improved in 2006/07 compared to 2005/06 thanks to normal and evenly distributed rainfall in the previously drought-stricken eastern and western parts of the country. This led to increased production of food and cash crops and should help poverty reduction efforts as income and asset inequality declines. Currently agriculture employs about 67 per cent of the labour force. However, the high population growth rate, coupled with declining average farm size, is an obstacle to agricultural production. A recent World Bank report shows that Uganda has the highest dependency ratio, i.e., the number of young people (under 16) and older people (over 64) who depend on people of working age (16 to 64) in the world[1]. This highlights the need for Uganda to modernise its agriculture at the same time as reducing dependency on it by diversifying the economy and creating more jobs in industry in particular.

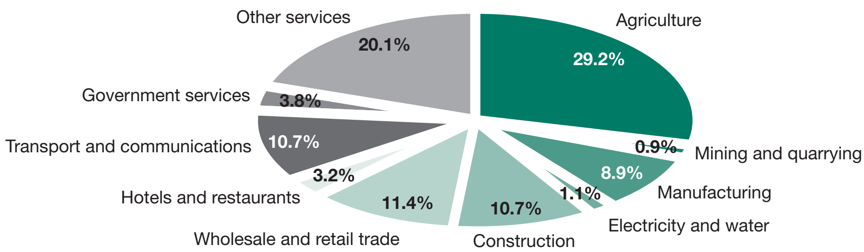
Industrial output grew at 5.8 per cent in 2006/07, up from 5.6 per cent in 2005/06, despite the adverse impact of electricity shortages and increasing costs of inputs[2]. This strong performance was due mainly to high growth in the mining and quarrying sub-sector (14.2 per cent) in 2006/07, stimulated chiefly by increased construction activities. Growth in the manufacturing sub-sector although higher, remained modest at around 2.9 per cent (up from 0.1 per cent in 2005/06). Recent oil discoveries have raised hopes of Uganda becoming an oil producer by 2009.[3]

1. World Bank (2007), "Beyond Recovery: Investment and behavior change for growth," Uganda *Country Economic Memorandum* (vol. 2).

2. The energy shortage was caused by high demand and a drop in hydroelectric generation of nearly 200 MW due to falling water levels in Lake Victoria, along with a deficient transmission network and dilapidated distribution meters.

3. Ministry of Finance, *Background to the Budget 2006/07.*

Figure 2 - **GDP by Sector in 2006/07** (percentage)



Source: Authors' estimates based on local authorities' data.

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The services sector's share in GDP continued to rise, reaching 47.1 per cent in 2006/07 compared to 45.8 per cent in 2005/06. In contrast, the share of agriculture declined from 33.3 per cent to 31.9 per cent over the same period. The share of industry remained virtually unchanged at about 21 per cent in 2005/06 and 2006/07. A major cause of the declining share of agriculture in aggregate output is the decline in food crop prices. Increases in the productivity of other crops were not sufficient to offset this fall. Meanwhile, despite progress in some sub-sectors, agriculture remains constrained by inadequate infrastructure, lack of market information, concentration on low-value crops and limited access to support services such as agricultural extension and food-processing technology.

Public and private investment remains the key source of recent GDP growth. Private investment in the services sector, especially in construction and telecommunications, attracted sizeable foreign direct investment (FDI). Oil exploration is another area that continued to attract increased foreign investment. Electricity shortages are a major constraint on investment in manufacturing.

Agriculture is expected to continue to recover despite the ongoing effects of HIV/AIDS and problems with plant and livestock disease. Increased agricultural investment and productivity is vital for Uganda to reduce poverty in view of the fact that over 83 per cent of all households and the majority of poor households

Table 1 - **Demand Composition**

	Percentage of GDP (current prices)		Percentage changes, volume			Contribution to real GDP growth		
	1998/99	2005/06	2006/07(e)	2007/08(p)	2008/09(p)	2006/07(e)	2007/08(p)	2008/09(p)
Gross capital formation	**19.4**	**23.3**	**16.1**	**10.6**	**6.6**	**3.2**	**2.3**	**1.5**
Public	6.2	4.9	21.2	7.8	5.0	0.9	0.4	0.2
Private	13.2	18.5	14.8	11.4	7.0	2.3	1.9	1.2
Consumption	**92.3**	**91.9**	**5.7**	**6.3**	**7.2**	**5.2**	**5.7**	**6.5**
Public	13.3	14.7	8.7	0.9	4.5	1.1	0.1	0.5
Private	79.0	77.3	5.2	7.2	7.6	4.1	5.6	6.0
External demand	**-11.7**	**-15.3**				**-2.4**	**-1.9**	**-1.7**
Exports	12.4	14.8	2.2	4.9	4.9	0.3	0.6	0.6
Imports	-24.2	-30.0	11.5	10.1	8.8	-2.7	-2.5	-2.3
Real GDP growth						**6.0**	**6.2**	**6.3**

Source: Domestic authorities' data; estimates (e) and projections (p) based on authors' calculations.

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live in rural areas. Although Uganda's poverty rate declined from 56.4 per cent in 1992/93 to 31.1 per cent in 2005/06, over the past two decades, farmers and the rural population have consistently trailed behind other sectors in terms of welfare benefits from strong growth and economic transformation. In this context, Uganda's 2007 Human Development Report argues for modernisation of agriculture as a means to reduce poverty in the country.

Macroeconomic Policies

As in previous years, macroeconomic policy in Uganda in 2006/07 remains focused on: *i)* maintaining annual consumer price inflation at a maximum of 5 per cent; *ii)* reducing the fiscal deficit and encouraging greater private sector credit and investment; and, *iii)* maintaining adequate foreign exchange reserves (the equivalent of a minimum of five months of imports) and a competitive real exchange rate to encourage exports.

Economic policy is broadly based on the Poverty Eradication Action Plan (PEAP), which runs from 2004/05 to 2007/08. PEAP's key aims are to improve tax collection and management of the fiscal deficit, upgrade infrastructure, and widen access to education and health services. Besides the electricity shortages, key challenges include low levels of financial intermediation, an inadequate transport network and corruption. Economic policy continues since January 2006 to be monitored by a new IMF facility, the Policy Support Instrument (PSI) programme. The PSI provides surveillance and technical assistance to help Uganda maintain macroeconomic stability, while sending a positive signal to other donors. The PSI monitors government progress towards achieving the goals of the PEAP as well as broader issues of public-sector management and governance, including tackling corruption.

Fiscal Policy

In addition to emphasising fiscal prudence, the 2007/08 budget focused squarely on reorienting government expenditure towards prosperity for all in the context of the PEAP. The overall fiscal deficit, excluding grants, remained low at 2.8 per cent of GDP in 2006/07 compared to 2.4 per cent in 2005/06.

The fiscal deficit is driven by high government spending on development programmes, especially road infrastructure and universal secondary education, as well as expenditure associated with the Commonwealth Heads of Government Meeting, and for flood relief and peace efforts in the north. However, despite the fall in tariff revenue following the implementation of the East African Customs Union in 2005, the budget deficit is projected to stay low in 2007/08 and 2008/09 with

Table 2 - **Public Finances** (percentage of GDP)

	1998/99	2003/04	2004/05	2005/06	2006/07(e)	2007/08(p)	2008/09(p)
Total revenue and grants[a]	**16.6**	**22.3**	**20.7**	**18.6**	**19.3**	**17.8**	**17.2**
Tax revenue	10.8	12.0	11.9	12.6	12.6	12.8	12.9
Grants	5.0	9.6	8.2	5.2	6.0	4.3	3.6
Total expenditure and net lending[a]	**17.8**	**23.8**	**21.4**	**20.9**	**22.0**	**22.2**	**21.7**
Current expenditure	10.6	14.7	13.4	13.4	13.1	13.3	12.9
Excluding interest	*9.7*	*12.7*	*11.9*	*11.9*	*11.8*	*12.0*	*11.7*
Wages and salaries	4.2	5.2	5.1	5.0	4.8	4.6	4.5
Interest	0.9	2.0	1.6	1.4	1.3	1.3	1.2
Capital expenditure	7.2	9.0	8.0	7.7	8.9	9.1	8.9
Primary balance	**-0.4**	**0.5**	**0.9**	**-0.9**	**-1.4**	**-3.1**	**-3.2**
Overall balance	**-1.3**	**-1.5**	**-0.7**	**-2.4**	**-2.8**	**-4.4**	**-4.4**

a. Only major items are reported.
Source: Domestic authorities' data; estimates (e) and projections (p) based on authors' calculations.

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strong GDP growth, increases in some excise tax rates, and government efforts to improve tax collection. While the fiscal deficit, including grants, also remains low, it is expected to rise over the medium term due to an expected decline in official development assistance.

Monetary Policy

The main aims of Uganda's monetary policy are to contain inflation below 5 per cent and maintain stability in the money and foreign exchange markets. To achieve these objectives, the Bank of Uganda (BoU) often engages in sterilisation of excess liquidity through purchases and sales of treasury bonds and foreign exchange. The BoU also uses repos (repurchase agreements) to manage liquidity (intra-auction liquidity). In addition to liquidity management tools, BoU uses the rediscount rate and the bank rate to achieve its monetary policy objectives.

In 2006/07 broad money supply, M2, grew by 15.4 per cent, up from 10.3 per cent in 2005/06. Bank lending to the private sector grew by 20.7 percent, although commercial banks' credit policies remain cautious and banks continue to prefer buying treasury bills and lending to foreign banks rather than to domestic businesses. A major challenge for monetary policy in Uganda is how to address the structural causes of high real interest rates and limited lending to the private sector. Also, liquidity sterilisation of balance of payments surpluses tends to appreciate the shilling and adversely affect export competitiveness.

The average consumer price inflation rate for 2006/07 was 6.4 per cent compared with 7.3 per cent in 2005/06. Although the actual inflation rate is higher than the target rate of 5.0 per cent, BoU's tight monetary policy has been successful in containing inflationary pressure and there appears to be no need for further tightening. The price increase was the result of strong growth in private consumption demand and increased oil and electricity prices, which led to higher transportation costs. Although food prices increased at the beginning of 2006/07 due to natural shocks (drought and later flooding), the annual food price index declined by the end of the year owing to a larger than expected increase in food production[4]. On top of this, relatively high demand and increased prices for imported non-food consumption items pushed underlying inflation (excluding food items) slightly above headline inflation in 2006/07[5] on an annual basis.

Interest rates in 2006/07 were largely unchanged from the year before. The yield to maturity on two-year treasury bonds was 12.4 per cent in September 2007. The yield on 364-day treasury bills rose slightly from 10 per cent in April 2006 to 10.3 per cent in September 2007, while the effective yield on 91-day bills declined from 7.9 per cent to 7.6 per cent over the same period. The inter-bank money market rate and the repo rate followed the same trend as the 91-day yield rate. These parallel interest-rate movements suggest that the financial markets are becoming more efficient.

The commercial banks' average lending rate remained very high at 19 per cent in 2007 compared to the time deposit rate of 11 per cent. The high spread indicates lack of competition in the banking sector and high operational inefficiency. Indeed government reports attribute high lending rates and spreads to high operating costs and perceived high risk of lending to the private sector. In addition, the government's fiscal deficit provides an ample supply of low-risk government securities, crowding out commercial bank lending to the private sector. There is a need for credit information agencies to assist banks to assess risk and thus increase lending to the private sector.

Uganda maintained its flexible exchange rate policy, with the Ugandan shilling's exchange rate freely determined by economic fundamentals. As is normally the case under flexible exchange rate regimes, BoU often intervenes to smooth short-term volatility. The

4. BoU's *Quarterly Bulletin*, December 2007.

5. According to the rebased consumer price index (rebased to 2005/06 instead of 1997/98), the headline inflation rate rose to 4.9 per cent in the year ending September 2007, while the annual underlying/core inflation rate dropped moderately to 5.7 per cent.

Ugandan shilling appreciated against the US dollar by about 5.9 per cent in 2007 due to an increase in foreign currency inflows from the export sector, NGOs, and foreign purchases of Ugandan government bills and bonds. From June 2006 to March 2007, foreign exchange supply exceeded demand by USD 19.6 million and BoU bought USD 16.2 million of foreign currencies during this period that it endeavoured to sterilise.

External Position

Uganda's external position remains healthy. The overall balance of payments registered a surplus of USD 172 million in 2006/07 compared to USD 254 million in the previous year. As in previous years, the surplus was mainly the result of a large capital and financial account surplus, which amounted to USD 452 million in 2006/07 compared to USD 635 million in 2005/06. The capital and financial account surplus resulted largely from inflows of FDI, which increased from USD 257 million in 2005/06 to USD 322 million in 2006/07.

The current account deficit including grants edged up to USD 373 million (2.9 per cent of GDP) in 2006/07 compared to USD 265 million (2.2 per cent) in 2005/06. Excluding grants, the deficit remains relatively low (4.0 per cent of GDP), below the 5 per cent sustainability threshold, indicating the declining role of foreign aid in Uganda's balance of payments position.

The trend of the current account balance is largely a reflection of developments in the trade balance. In absolute terms, the trade deficit increased from USD 1.10 billion in 2005/06 to USD 1.24 billion in 2006/07. However, the growth rate of the trade deficit declined considerably, from 34.2 per cent in 2005/06 to 12.7 per cent in 2006/07. This decline was the result of the higher growth rate of merchandise exports (35.4 per cent) than imports (22.9 per cent). Much of the increase in Uganda's export receipts is attributable to higher unit prices for coffee (USD 1.7 per kilogramme in 2006/07 compared to USD 1.4 a year earlier) and to a lesser extent higher coffee export volumes (from 2.6 million 60-kilogramme bags to 2.7 million in 2006/07).

Uganda's exports are still dominated by a few agricultural exports such as coffee, tea, fish and cotton, which are highly vulnerable to weather and terms of trade shocks. Exports of coffee, the main export commodity, increased from USD 173 million in 2005/06 to USD 227 million in 2006/07 owing to favourable world prices, improved husbandry practices and good weather conditions at the critical time of bean maturation. Moreover, new coffee plantations, fostered under the government's strategic intervention since 2001, have continued to start production. Non-coffee exports rose from USD 717 million to USD 953 million, an increase of 33 per cent over the same period. Improvements were recorded for most non-coffee exports. Growth in import demand was due largely to capital goods imports, in particular the thermal generators required to counter the electricity shortage and for the construction of the Bujagali hydroelectric project. Relatively large increases in domestic investment that are awaited are expected to

Table 3 - **Current Account** (percentage of GDP)

	1998/99	2003/04	2004/05	2005/06	2006/07(e)	2007/08(p)	2008/09(p)
Trade balance	-7.2	-9.5	-9.6	-11.5	-11.8	-13.1	-13.4
Exports of goods (f.o.b.)	9.0	9.3	9.2	9.3	9.1	8.8	8.4
Imports of goods (f.o.b.)	16.2	18.8	18.9	20.7	20.9	21.9	21.8
Services	-3.8	-3.4	-3.9	-3.7	-5.3	-4.5	-4.3
Factor income	-1.8	-2.2	-2.0	-1.4	-1.2	-2.9	-3.1
Current transfers	4.2	13.9	13.9	13.8	14.3	13.7	12.7
Current account balance	**-8.6**	**-1.2**	**-1.6**	**-2.8**	**-4.0**	**-6.8**	**-8.1**

Source: Domestic authorities' data; estimates (e) and projections (p) based on authors' calculations.

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result in widening trade and current account deficits in 2007/08 and 2008/09. Capital imports are projected to rise further if the government and private investors move ahead with the development of the recent oil discoveries.

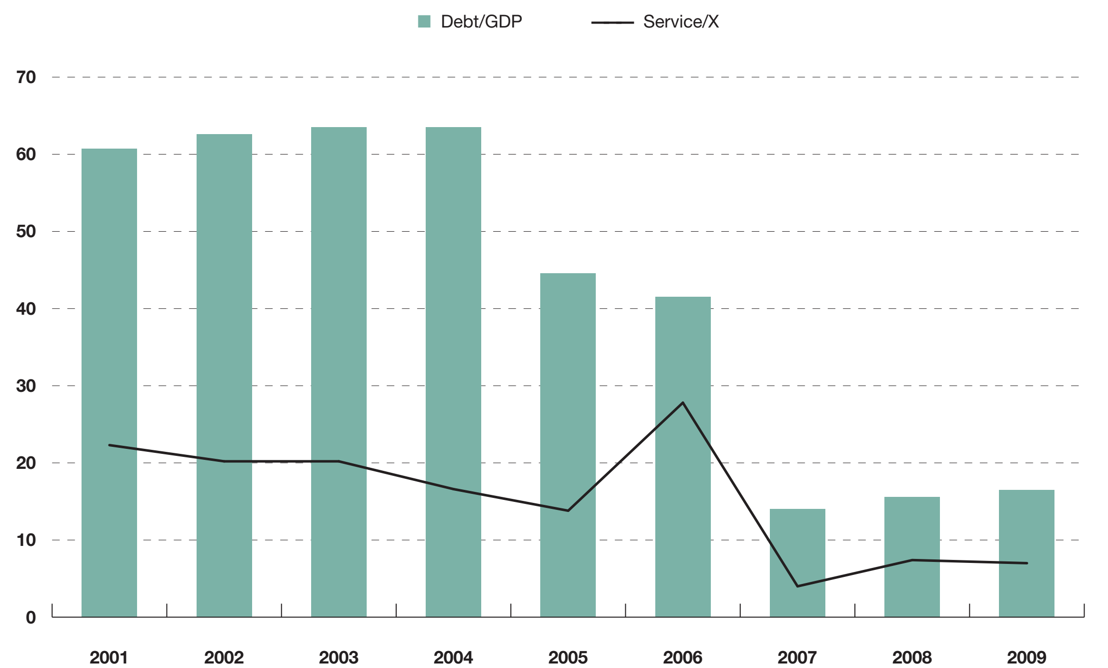
Uganda's foreign exchange reserves increased by over USD 85 million during the year ending September 2007, reflecting the balance of payments surpluses. The country's foreign exchange reserves are equivalent to about four months of imports in 2006/07 compared to five months of imports in the previous year.

As a result of the debt relief under the Heavily Indebted Poor Countries (HIPC) Initiative and the Multilateral Debt Relief Initiative, Uganda's external debt declined to USD 1.4 billion in 2007 and debt service decreased from 13.1 per cent of exports in 2005/06 to 3.5 per cent in 2006/07. Uganda was granted debt cancellation of USD 2.96 billion from the International Development Association and USD 486.26 million from the African Development Bank under MDRI. While debt relief is now declining, aid in the form of budget support and project support increased substantially, to USD 573 million and USD 494 million respectively in 2006/07.

Regional integration in the framework of the East African Community (EAC) continues to influence trade and development policy in Uganda. Consolidation of the EAC Customs Union (covering Kenya, Tanzania, Uganda, Rwanda and Burundi) led to lower or zero excise tax rates on some commodities, but expanded the regional market for Uganda's exports. To promote regional trade, the EAC is currently establishing a cross-border payments system to facilitate the efficient and safe transfer of funds within the region. The regional payment system is expected to be implemented in 2008.

Another key development is the signing by the ministers of the EAC of an economic partnership agreement with the European Union (EU) on 27 November 2007. This framework agreement will,

Figure 3 - **Stock of Total External Debt** (percentage of GDP) **and Debt Service** (percentage of exports of goods and services)



Source: IMF.

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over a transition period of 25 years, abolish tariffs on 81 per cent of current EU exports in industrial and agricultural products entering the EAC markets. In return Uganda has benefited from duty and quota-free access to the EU for most export of goods (excluding sugar and rice) since 1 January 2008. A deal on services and investments, not covered in the current agreement, will be negotiated in 2008.

The Ugandan Capital Market Authority has continued harmonising its laws with those of Kenya and Tanzania to enable a regional capital market by 2009 as envisaged in the EAC development strategy (2006-10). Rwanda and Burundi have joined the EAC. Further steps in the EAC integration project are to consolidate the customs union, complete negotiations for a common market protocol, and create the necessary conditions for monetary union.

Structural Issues

Recent Developments

Uganda has introduced several reform measures to increase economic growth and accelerate progress towards achieving the MDGs. The challenge Uganda faces now is how to deepen reforms already underway in the context of the current PEAP. The reforms focus on the promotion of private-sector led growth that is broadly shared across sectors and regions. They include institutional as well as fiscal and monetary measures aimed at improving the business environment and investment climate. Nevertheless, in 2007 Uganda's global ranking in the World Bank *Doing Business* indicators fell from 107th to 116th (out of 175 countries). Uganda performed relatively well regarding the ease of employing workers, protection for investors and ease of making tax payments, but performed poorly on the cost of starting a business, dealing with licenses, registration of property, securing credit and trading across borders.

These weaknesses can have an adverse impact on the government's efforts to enhance productivity and promote competitiveness and employment creation. Indeed a World Bank study published in 2007 pointed out that lengthy and costly business registration procedures (an average of 11 procedures taking on average 63 days) are to blame for observed high informality among Ugandan firms. Corruption has also been cited as a factor that encourages informality. While large domestic firms do not consider corruption as a binding constraint, small and medium enterprises (SMEs), foreign firms and exporters seem to be severely affected. Corruption adversely affects the quantity as well as quality of public service delivery especially in the area of infrastructure.

In addition to land-policy reforms that give investors easy access to, and flexible use of land, the government is developing a number of industrial parks to provide critical infrastructure to potential investors in central locations. Three business parks are under development: the Kampala Industrial and Business Park, Luzira Industrial Business Park, and, the Bweyogerere Industrial Estate. In 2007, the Uganda Investment Authority licensed a total of 330 projects with planned investment of USD 1.75 billion and estimated employment of 42 950. This represents a 100 per cent increase over the previous year in terms of investment value and a 26 per cent increase in terms of employment. Foreign capital accounted for 57 per cent of new investments in 2007.

Credit market participation by Ugandan firms remains very low, especially for SMEs. Also, access to bank credit is extremely limited for rural households. The economy is characterised by low credit demand and even lower credit supply, with high lending rates and interest rate spreads. Bank lending is concentrated on the building and construction sector (69.4 per cent) followed by trade (20.4 per cent) and other services (6.6 per cent). In efforts to increase competition and enhance financial intermediation, BoU relaxed the freeze on licensing of new commercial banks. Accordingly, four new commercial banks were licensed by September 2007.

Financial-sector development strategies for the short and medium term also include implementation of the Microfinance Outreach Plan (MOP) and its associated

Rural Financial Services Programme (RFSP) to promote access to credit for SMEs and rural households. Implementation of the RFSP aims to develop a financial infrastructure of Savings and Credit Cooperative Organisations (SACCOs) that are capable of reaching the population in all sub-counties. The government is considering formulating a policy to guide and regulate all interventions in the microfinance industry in the area of supervision, regulation, coordination, lending, and savings mobilisation.

While the number of deposit-taking microfinance institutions remained the same in 2007, their total assets registered a 24 per cent growth. They also registered strong growth in deposits (50 per cent), loans (21.7 per cent) and return on equity (14 per cent). In order to reduce informality, the government registered a total of 250 SACCOs, which can eventually develop into deposit-taking microfinance institutions after fulfilling certain requirements.

The total labour force increased from 9.8 million to 10.9 million over 2003-2006. The official national unemployment rate was 2 per cent, while the urban unemployment rate was 7 per cent and the underemployment rate was estimated at 12 per cent in 2006/07. Self-employment in agriculture accounts for about 70 per cent of total employment and only 5 per cent of the workforce are in permanent formal employment. The labour market survey indicates that the average nominal wage increased by 5.3 per cent per year over 2001-2005 while employment grew by 6.8 per cent per annum over the same period. However, total factor productivity growth accounts for the bulk (about 80 per cent) of GDP growth in Uganda (World Bank, 2007).

Technical and Vocational Skills Development

Until recently technical skills development in Uganda was fragmented and lacked substantive policy direction. In 2003, a Business, Technical and Vocational Education and Training (BTVET) policy was formulated and adopted by the Ministry of Education and Sports (MoES). The aim of the policy is to provide a framework for technical skills development at the post-primary school level that prepares students for direct entry into the labour market as well as entry into higher-level technical and tertiary education. This requires changes in curricula, adequately trained staff as well as specialised institutions that can effectively respond to labour-market demand. MoES is preparing the BTVET Act for consideration and approval by parliament in 2008.

The Act aims to establish an institutional framework for the promotion and co-ordination of BTVET that clearly defines the scope and levels of its programmes and the roles of the different stakeholders in delivering them. It also: separates training and delivery of BTVET from quality assurance functions; specifies the criteria and the process of admission of students and trainees to BTVET institutions; provides for the effective education, training, governance and management of BTVET institutions; and, establishes mechanisms and organs for the regulation of qualifications (standards, assessment and certification) and training delivery in formal and non-formal institutions.

PEAP explicitly recognises BTVET as a priority area, to match training and education needs with the economy's need for skills. Beside the establishment and operationalisation of the Uganda vocational qualifications framework, PEAP calls for appropriate balance within post-primary education between academic and vocational education. In this regard, the secondary school curriculum is being reviewed to make it more responsive to national labour demands, and 56 secondary schools are being transformed into vocational schools. The Education Sector Plan envisages that BTVET will become an alternative to academic education in the last two years of secondary level, rather than an alternative to the early years of secondary education. The introduction of short modularised courses should also make it possible for adults to acquire skills over their lifetime.

Uganda's BTVET system is currently comprised of 145 public institutions, about 600 private training service providers, and an unknown number of apprenticeship and enterprise-based training programmes. The public BTVET system includes technical institutes, vocational training institutes and centres, technical schools, farm schools and community polytechnics. In terms of subject areas, public BTVET institutions cover: agriculture and forestry, business, co-operative programmes, hotels and tourism, health, wildlife, survey and planning, meteorology and technical studies. Formal BTVET programmes (colleges, schools and institutes) generally target students who have passed primary education grade 7. Typical programme duration is one to three years leading to the award of diplomas and/or certificates. Other training programmes vary in terms of intake requirements, duration, subjects and certification. They include institutional and enterprise-based training as well as on-the-job training programmes[6].

Although enrolment has been rising – from 23 206 students in 1999/2000 to 40 435 in 2006/07 – the public BTVET institutions reach only a fraction of potential demand. Females accounted for 50 per cent of total intake in 2007. While most BTVET institutions registered with the MoES are government-owned (87.1 per cent), 4.3 per cent are owned by the private sector and 2.6 per cent by the local community.

Private BTVET institutions include vocational training centres and schools, vocational secondary schools, and technical schools. About 450 of these institutions are members of the Ugandan Association of Private Vocational Institutions[7]. However, the full number and kind of private BTVET programmes is unknown and there are numerous informal vocational training institutions. Also, several government departments, such as the Ministry of Trade and Tourism, offer vocational and technical training outside the BTVET umbrella. In fact some government units offer similar training and support programmes, such as business incubation, without any co-ordination. This underscores the need for central registration and co-ordination of public and private BTVET activities in order to increase efficiency.

Firm-level data shows significant skill gaps in Uganda as well as low labour productivity. Studies indicate that the contribution of human capital to total productivity in Uganda is less than 10 per cent[8]. Forty-seven per cent of Ugandan firms report the lack of skills as either a moderate, major or very severe constraint to business and 60 per cent of top managers in Uganda have no university training compared with 6.8 per cent in Zambia and 30 per cent in Kenya and Tanzania. Meanwhile, the number of training programmes offered by Ugandan firms per worker is below the average for sub-Saharan Africa. Because Ugandan firms cannot find the workers with the right skills set, the current employment level in Uganda is 50 per cent lower than the optimal level or expected level of employment under current production technology (World Bank 2007).

Women accounted for 47.4 per cent of Uganda's total labour force of 9.8 million in 2002/03 while 85 per cent of the labour force lived and worked in rural areas[9]. Just over 17 per cent of the labour force was illiterate in 2003 and another 59.6 per cent had only primary school education, whilst 17.2 per cent had secondary education, and above-secondary education 5.6 per cent. Reports indicate a high demand for BTVET in the modern private sector and traditional subsistence agriculture[10].

Formal-sector incomes increase substantially with the level of education. While an employee with no formal education earns on average USH 25 000 per

6. BTVET Directorate, Ministry of Education and Sports (2007) "Data on BTVET public and private institutions".

7. See www.ugaprivi.org

8. Berthelemy, J. and L. Soderling, (2002), "Will There Be New Emerging-Market Economies in Africa by the Year 2020?" *IMF Working Paper* WP/02/131.

9. *Uganda National Household Survey 2002/03*. Uganda Bureau of Statistics. Kampala.

10. Wirak, A., Heen, B., Moen, E. and S. Vusia (2003), "BTVET for employment and private sector development in Uganda." A report commissioned by the Royal Norwegian Embassy in Kampala and Norwegian Agency for Development Cooperation (NORAD).

month, average salaries rise to USH 40 000 for primary education, USH 99 000 for secondary education and USH 237 000 for specialised training or tertiary level[11]. However, the business-climate survey shows that return to education has been stagnant or declining in recent years because capital is the more binding constraint and schools are not providing the skills employers seek.

The public BTVET system is financed mainly through the government budget, contributions by employers and donors, and fees. BTVET programmes financed by the government received only 3.6 per cent (USH 670 billion) of the budget of the MoES in 2006/07 compared to 4 per cent (USH 540 billion) in 2002/03[12]. The budget for BTVET has not been protected within the Education Strategic Investment Plan and has therefore suffered from repeated cuts in absolute terms. The incorporation of BTVET subjects in secondary schools' curricula provides additional support to the BTVET system. Government also provides indirect support especially for private informal BTVET institutions through contributions to instructor training and wages. However, private BTVET institutions rely mainly on own sources of finance, especially fees, and donor support.

The government has encouraged local government and district-level ownership and participation in BTVET programmes through planning and construction of BTVET institutions, monitoring and supervision, and mobilisation of local support. Donors and NGOs such as German Technical Cooperation have contributed to the establishment and running of several BTVET institutions, although they consider slow progress towards finalisation of the BTVET Act as a constraint on their involvement. They want to make sure that the institutions they support offer standardised curricula and award certificates that are formally recognised by government and employers. Finally, some BTVET institutions obtain additional funding through levies on training activities and services.

A key challenge to the BTVET system is the lack of a legal framework and central co-ordination and guidance to upgrade and maintain standards. This calls for the urgent adoption of the BTVET Act to provide a national qualification framework for the classification and recognition of formal and informal training programmes, as well as the establishment of a central BTVET registry, or empowerment of the BTVET Directorate of the MoES to perform registration, co-ordination and supervisory functions. Other challenges include: inadequate human and physical BTVET infrastructure especially in terms of access to technology and teaching material; negative attitudes and stigma among key stakeholders; relatively low staff salaries; and, lack of reliable and up-to-date manpower surveys to inform curricula development.

Political Context

President Museveni and his National Resistance Movement party continued to consolidate their hold on power after winning the first multi-party elections in Uganda in 2006. Despite isolated incidences of unrest led by opposition parties, Uganda's overall political situation remained stable in 2007. The government successfully hosted the Commonwealth Head of Government Meeting (CHOGM) on 22-25 November 2007. President Museveni will serve as the Chairman of the Commonwealth for the next two years. In preparation for the meeting, there were many infrastructure developments including new roads and several hotels. However, the full contribution of CHOGM to the Ugandan economy, in terms of attracting tourism, is yet to be fully evaluated.

There is a tenuous prospect of peace in the north following the cessation of hostilities between the government and the Lord's Resistance Army (LRA) in August 2006. Despite serious challenges, the agreement is a major breakthrough and the talks provide the best

11. *Uganda National Household Survey 2002/2003.*

12. MoES, *Education Sector Medium Term Budget Framework Paper 2004* and *MoES Annual Performance Report 2007.*

opportunity in 20 years for peace in northern Uganda. The government remains committed to the Peace, Recovery and Development Plan for northern Uganda and neighbouring districts that was launched in 2007. Many former rebels have returned to their villages and northern Uganda regained some sense of normality in 2007. The year also witnessed intensified disarmament of the Karimojong warriors and reduction in incidents of cattle rustling in Western Uganda's districts of Bundibugyo.

The country's self-assessment exercise under the African Peer Review Mechanisms of the New Partnership for Africa's Development was officially launched by the president in 2007. Under this exercise, Uganda is being assessed on the following thematic areas: democracy and political governance; economic governance and management; social governance; and corporate governance. The results of this assessment will help to improve governance mechanisms in Uganda.

Transparency International's corruption perception index shows that corruption in Uganda has improved slightly. Whilst Uganda's ranking in the corruption league table dropped from 105th position to 111th position, its average CPI score edged up from 2.7 in 2006 to 2.8 in 2007. In its 8th Annual Report, the Uganda Human Rights Commission highlighted a number of activities undertaken to fulfil its mandate, including training of different state agencies and public officials in human rights, coordinating civic education, and monitoring state agencies (e.g. military detention centres, police and prisons cells) in the observance of human rights. The report highlights key challenges that include poor quality of civic education programmes, non-enforcement of tribunal decisions, and delayed enactment of the law against torture.

Human development indicators also show modest progress. Uganda's ranking in the UNDP Human Development Indicators declined very slightly from 144th position in 2005 to 145th position in 2006. Despite this decline, Uganda remains in the medium human-development category. Improvements occurred in adult literacy and net enrolment in primary school.

The decentralisation process in Uganda has been deepened as a means to improve service delivery and reduce poverty in the context of the PEAP. Although the average poverty rate has declined from 56.4 per cent in 1992/93 to 31.1 per cent in 2005/06, some observers see the expansion in the number of districts from 56 to 72 in 2004 as a drag on efficient service delivery, especially education. To improve service delivery, local governments need sufficient resources and authority, along with effective local mechanisms of accountability. A recent report found that local authorities in Mbarara District have very limited financial capacity and autonomy to effectively improve service delivery, and parents lack effective mechanisms to hold local authorities accountable[13]. Also, local governments face a major challenge of revenue mobilisation that is negatively impacting good governance and service provision. The country's constitution empowered local governments in 1995 to collect graduated income tax, which accounted for 75 per cent of local government revenue in rural areas and 35 per cent in urban areas in 1997. However, the tax was abolished in 2006 and local governments have yet to find adequate alternative local revenue sources while compensations by the central government are insufficient.

The government of Uganda needs to design effective contingency measures to address economic and social problems arising from violence in neighbouring countries. For example, the recent post-election violence in Kenya resulted in fuel and goods shortages that affected huge sectors of the economy and exposed the inadequacy of existing government contingency measures[14].

13. Yan, T. (2007), "Education and poverty reduction in Uganda," A Consultancy Report. Education Decentralisation Group, University College London.

14. *Economist Intelligence Unit* (January 2008), Uganda country report.

Social Context and Human Resources Development

Primary school enrolment is at 90 per cent and Uganda is on track to achieve the primary education's MDG target, according to national authorities. Total enrolment has increased slightly from 7.5 million in 2002/03 to 7.6 million in 2005/06. Investments in expansion of basic education infrastructure and facilities (particularly increases in the number of schools, class rooms and teachers' houses), improvement in availability of training materials, and the increased number of skilled and trained teachers have contributed to maintaining and slightly increasing the enrolment level. The government also made progress regarding access to education for children with special needs and promotion of gender parity.

Although gross enrolment in primary schools has continued to increase as a result of the Universal Primary Education (UPE) programme, the net enrolment ratio remained about 86 per cent over the last 5 years. The net enrolment ratio tends to be lower because a sizeable number of children attending school are outside the official age bracket; others have never attended school while some pupils continue to drop out of school. Being considered "too young", financial cost, disinterest by parents, and socio-cultural barriers largely explain why some children do not go to school. Most children who drop out of school do so because of costs – uniforms, stationery, transport, and boarding fees – that are unaffordable for poor households.

Investment in human capital through high-quality and affordable education is essential for Uganda to attract foreign investors. Despite notable improvements, the net secondary school enrolment ratio remains low (34.2 per cent in 2006) and higher for males than females. There is a high secondary school dropout rate due largely to high costs and unavailability of secondary schools. In January 2007 the implementation of the Universal Post Primary Education and Training (UPPET) initiative commenced. UPPET will serve to absorb the increasing numbers of pupils completing primary education as a result of the UPE initiative.

Preliminary findings from the Demographic Health Survey 2005/06 show marginal improvements in a number of core health indicators under the health sector strategic plan. Infant mortality declined from 88 to 76.9 deaths per 1 000 children between 2000/01 and 2005/06 while maternal mortality decreased from 505 to 435 deaths per 100 000 births over the same period. The percentage of deliveries in health facilities increased from 22.6 per cent in 2000/01 to 41 per cent in 2005/06 and the percentage of approved posts filled by trained personnel based on the 2005/06 local government staffing norms improved from 46.8 per cent in 200/01 to 75 per cent in 2005/06. The health sector achieved an out-patient department attendance at public and private not-for-profit health facilities of 100 per cent surpassing its 2006/07 target of 96 per cent. However, the sector suffers from shortages of drugs and difficulties in attracting and retaining trained staff.