International Monetary Fund

Uganda and the IMF

Press Release:
IMF Executive Board Completes Sixth Review Under Policy Support Instrument for Uganda and Approves a New Three-Year PSI
June 28, 2013

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Uganda: Letter of Intent, Memorandum of Economic and Financial Policies, and Technical Memorandum of Understanding

June 17, 2013

The following item is a Letter of Intent of the government of Uganda, which describes the policies that Uganda intends to implement in the context of its request for financial support from the IMF. The document, which is the property of Uganda, is being made available on the IMF website by agreement with the member as a service to users of the IMF website.

LETTER OF INTENT

Kampala, Uganda
June 13, 2013

Ms. Christine Lagarde
Managing Director
International Monetary Fund
Washington, DC 20431

Dear Ms. Lagarde:

On behalf of the Government of Uganda, I would like to provide you with an update on the progress we have achieved under our economic program supported by the IMF's Policy Support Instrument (PSI). Economic growth has been stronger than expected, inflation has been reduced close to our 5 percent medium-term target, credit growth is accelerating, and the external position has been strong enough to allow an accumulation of reserves significantly higher than programmed. In light of these favorable developments, and in consideration that all December 2012 quantitative assessment criteria under the program were met, we request completion of the sixth and final review under our PSI-supported program.

Going forward, we have developed a strong program of economic reform aimed at achieving broad-based growth, generating employment, and eradicating mass poverty. Specific measures will center on maintaining macroeconomic stability, improving public financial management, raising revenue, improving the business climate, preparing the economy for oil production and revenue, and completing the transformation towards full-fledged inflation targeting. To assist us in carrying out this ambitious reform agenda, the government of Uganda wishes that our existing PSI arrangement, which runs to August 10, 2013, be cancelled, and that a new three-year PSI-supported program be approved in support of our reform agenda.

The attached Memorandum of Economic and Financial Policies (MEFP) sets out Government's objectives for the three-year PSI-supported program, and provides details of the policies to be pursued in the first year. Government believes the policies set forth in the MEFP are fully sufficient to achieve the objectives of our PSI-supported program, but as always we stand ready to take any further measures that may become appropriate for this purpose.

We intend to work with the IMF and other development partners in the implementation of our program, and will consult with the Fund on the adoption of any such further measures, and in advance of revisions to the policies contained in the MEFP, in accordance with the Fund's policies on such consultation. We will provide the IMF with such information as the Fund requests in connection with our progress in implementing the policies and reaching the objectives of the program. We also consent to publication of the documents for the sixth review under the PSI.

Sincerely yours

/s/

Maria Kiwanuka
Minister of Finance Planning
and Economic Development

/s/

Prof. E. Tumusiime-Mutebile
Governor
Bank of Uganda

Attachments
Memorandum of Economic and Financial Policies
Technical Memorandum of Understanding

Attachment 1: Memorandum of Economic and Financial Policies

This Memorandum of Economic and Financial Policies lays out Government's objectives for the next three years, and provides details of the policies Government intends to implement over the next year to stimulate growth and job creation while maintaining overall macroeconomic stability.

I. Performance Under the Current PSI

1. The objective of macroeconomic policy under the current three-year PSI was to ensure that the economy could adjust to a much less benign external economic environment following the global crisis and could sustain broad-based growth. Key policy reforms to achieve these objectives included a re-orientation of budgetary resources towards growth-promoting public investment and the modernization of the central bank's monetary policy framework. Despite several shocks—including a severe food price shock in 2011 and the suspension of budget support by donors in 2012—progress has been made. Economic growth is recovering, inflation has been brought down to close to the policy target and the balance of payments has been restored to surplus.

2. All quantitative assessment criteria for the sixth PSI review have been met. Fiscal performance for the first half of 2012/13 was in line with program projections and the ceiling on net claims on government by the banking system was observed. The ceiling on net domestic assets was met and the floor on the stock of net international reserves of the Bank of Uganda (BoU) was exceeded by a substantial margin. The indicative target on the increase in base money was not met, but this did not pose any risks to inflation control. All indicative targets for end-March 2013 were achieved.

II. Recent Economic and Policy Developments

3. **Economic growth** was stronger than expected over the first half of FY2012/13 indicating that the economy has begun to recover from the recent supply side shocks. For FY 2012/13 as a whole, the economy is expected to expand by 5.3 percent—a full percentage point more than our previous projection and significantly higher than the 3.4 percent recorded in 2011/12. Growth has been broad based, with the largest contributions coming from telecommunications, construction, services and manufacturing. Aggregate demand has been boosted by, inter alia, an increase in net exports, while aggregate supply has benefitted from the expansion in electricity generating capacity arising from the commissioning of the Bujagali hydropower facility and from better agricultural harvests.

4. **Annual headline and core inflation** have both fallen sharply in the first 11 months of the fiscal year, as a result of the dissipation of supply side shocks and the much slower growth in domestic demand, which was brought about by a tightening of monetary policies. The BoU policy rate—the Central Bank Rate (CBR)—which is the operating target of monetary policy under the inflation targeting lite (ITL) monetary policy framework, was raised from 13 percent in July 2011

(when it was first introduced) to 23 percent in October 2011. As inflationary pressures subsided, the CBR was reduced gradually, beginning in February 2012. It stood at 12 percent between December 2012 and May 2013, and was reduced to 11 percent in June 2013 as inflation remained at low levels. In May 2013 annual headline and core inflation stood at 3.6 percent and 5.6 percent respectively, compared to 18 percent and 19.6 percent in June 2012.

5. **Private sector credit growth** is projected at about 15 percent for 2012/13, compared to 11 percent in 2011/12. Credit growth up to March was entirely attributable to foreign currency lending. In contrast, domestic currency lending stagnated because of a combination of high lending rates and structural factors, including the recent closure of the Land Registry, which administers the land titles needed for loan collateral. With the resolution of these issues, domestic currency lending is now showing signs of recovery.

6. **The banking sector** is in a healthy financial condition, recording strong profits in 2012, in part because of high net interest margins. Non-performing loans edged up to 4.2 percent of total loans at end-December 2012, but the banks' capital position remained very strong, with core capital for the banking system as a whole standing at 18.8 percent of risk weighted assets. At the beginning of March 2013, the statutory increase in the minimum paid up capital of banks from Shs 10 billion to Shs 25 billion took effect, with all 24 banks in operation now in compliance.

7. **The BOP** has been stronger than expected because of a decline in the current account deficit and larger than projected net capital inflows. The current account deficit is projected to fall to 9.3 percent of GDP (10.4 percent excluding project grants) in 2012/13 from 13 percent of GDP in 2011/12 (12 percent excluding project grants), mainly because of a reduction of imports and stronger export growth. As a result of the large overall BOP surplus, projected at $414 million, gross international reserves are projected to rise to just over US$3 billion at end June 2013, from US$2.6 billion at end June 2012.

8. **The overall fiscal deficit** in 2012/13 is projected to be 3.9 percent of GDP, 0.5 percent GDP larger than programmed. The larger deficit is attributable mainly to lower than programmed revenues and grants, slightly higher than expected current expenditures and the need to recapitalize the central bank (0.7 percent of GDP), which were only partially offset by underperformance of the development budget primarily due to delays to the start of the Karuma hydropower project. Lower tax revenues partly reflected the disruption caused by the imposition of a cash bond by Kenya earlier in the year and logistical problems with the fuel pipeline. A supplementary budget was appropriated in the last quarter of the year, of which over 50 percent was allocated to paying outstanding certificates in the road sector.

9. Uganda has already met the MDG target on **poverty** and is on track to meet the one on hunger as well. Between 1992 and 2010, the share of the population living below the poverty line has declined from 56 to 24.5 percent, and the prevalence of underweight children aged under 5 from 26 to 13.8 percent. However, the global economic crisis may have negatively impacted these gains.

III. Macroeconomic Objectives

10. To meet the strategic objectives of achieving broad-based growth, generating employment and eradicating mass poverty, Government will continue strengthening the business climate; implement targeted public investments, especially in roads and energy; enhance production and productivity of agriculture and promote agro-processing; enhance human capital formation, particularly through vocational skills development; and maintain price stability and a competitive real exchange rate through sound macroeconomic management.

IV. Macroeconomic Outlook and Risks

11. Real economic output is expected to pick up during 2013/14, as implementation of key infrastructure projects (notably the Karuma hydropower and the Kampala-Entebbe express highway) intensifies, while bottlenecks are alleviated. GDP growth is projected to rise to 6 percent during 2013/14 and further to an average of 7 percent per annum over the medium term. The BoU will aim to achieve its target for annual average core inflation of 5 percent over the medium term which, after incorporating base effects, implies an inflation rate of 6.3 percent in 2013/14. Moreover, foreign exchange reserves will be kept at a level of at least the equivalent of 4 months of import cover.

12. Government is focusing on improving the quality of essential services and the efficiency with which they are provided without compromising on equity in access. Government will put in place a framework to enable public private partnerships (PPPs) to be used to finance and deliver essential services in most sectors while also safeguarding against fiscal risks.

13. Regarding support for the poor and vulnerable households, Government's efforts are concentrated on enhancing their participation in economic activities. Interventions to this end are mostly geared at eliminating barriers to the uptake of essential services by these households (e.g. improving access roads, extending coverage of services, improving staff motivation and supervision especially for hard-to-reach and hard-to-stay areas).

14. Government policies are guided by the National Development Plan (NDP). Experience in the implementation of the NDP has shown that reconciling investment demands with fiscal sustainability and a stable macroeconomic framework remains challenging. In order to address these challenges, Government will update and improve project cycle management capacities, which will not only ensure the highest possible value for money of key projects, but will also allow mobilization of additional resources and optimally combine different financing options without undermining sound macroeconomic management. The new PSI will support government efforts to mobilize finance for infrastructure investments and to implement them efficiently.

15. Areas of concentration of the new PSI-supported economic reform program, that will run from June 2013 to June 2016, will be:

- Supporting revenue enhancement through measures to broaden and deepen the tax base and achieving more effective tax administration;
- Reforming PFM to enhance the effectiveness with which public funds are used;
- Preparing the economy for oil production and optimal management of petroleum revenues;
- Moving from inflation targeting 'lite' to full-fledged inflation targeting during the course of the program; and
- Improving the business environment, supporting the development of the financial sector, and continuing to maintain financial sector stability.

16. The main risks to the outlook include domestic and external shocks. On the domestic front, the economy remains vulnerable to the impact of weather-related agricultural shocks on domestic food prices. On the external front, Uganda's increasing integration into global markets generates vulnerabilities to a sudden reversal of short-term portfolio flows, and to terms of trade shocks, notably through increased oil prices or a decline in external demand. The likely rapid scaling up of investment in the oil sectors may also pose risks to domestic stability if spending on nontraded goods—e.g. in the construction sector—outstrips supply capacities. Government will ensure that it retains sufficient policy space (e.g. through prudent fiscal policy and the holding of adequate foreign reserve cover) to counter the impact of negative shocks without compromising macroeconomic stability.

V. Macroeconomic Policies Under the Program

17. The fiscal strategy for 2013/14 will seek to address the weaknesses in domestic and external revenue mobilization and improve the allocation of resources to key strategic priorities, as identified in the NDP. Revenues are projected to be higher than in the current fiscal year as Government expects to collect taxes on capital gains from oil transactions. Capital expenditure prioritizes infrastructure development, increasing agricultural production and productivity, enhancing human skills including technical capacity, and improving service delivery. Current expenditure will support maintenance of infrastructure and payments of services to sustain the efficiency of government offices. Government will make all efforts to avoid accumulation of arrears in FY 2013/14.

18. Government has developed a comprehensive five-year debt management strategy, which sets out guidelines and benchmarks for external and domestic debt to guide debt policy over that period. The main objectives of the strategy are to: i) ensure that the level of public debt remains sustainable; ii) meet Government's financing requirements; and iii) promote the development of the domestic financial market. Government will mobilize external resources in line with its debt strategy and the private sector will be invited to participate in infrastructure projects. To support these objectives, Government is requesting a ceiling on nonconcessional external debt with a maturity of

more than one year, during the programme period, of US$1.5 billion to be used to finance priority infrastructure projects, particularly in roads, railways, energy and water for production.

19. The BoU will continue to focus its Central Bank Rate (CBR) on the primary policy objective of maintaining price stability by holding core inflation to 5 percent over the medium term. A secondary objective—subordinated to the inflation objective—will be to help ensure that real output is in line with the economy's potential. The CBR will continue to be set every month on the basis of forecasts for inflation and output, and the interest rate decision will be explained to the public through a press briefing and monetary policy statement.

20. The BoU pursues a flexible exchange rate regime, and implements sterilized interventions in the foreign exchange market to dampen excessive exchange rate volatility.

VI. Reform Agenda

Tax Policy and Tax Administration

21. Government is committed to raising total revenue and especially the tax-to-GDP ratio to improve tax efficiency and fund critical projects. A Government's key objective within the PSI supported program is to raise the tax-to-GDP ratio by at least 0.5 percentage points annually from 2013 to 2016 (indicative target). Government will submit to cabinet a new tax procedure code by June 2013. Government will achieve the objective of raising revenue through a combination of tax policy and tax administration measures.

22. In the coming financial year Government will review the exemptions inherent in the tax system with the aim of eliminating those that are not cost efficient. The objective is to improve tax efficiency, facilitate tax administration, enhance compliance, and increase revenue collections. To this end, Government, with technical assistance from IMF, will undertake a VAT gap analysis, which will inform the course of action addressing exemptions, and will publish such analysis (structural benchmark). Government will then prepare an action plan to implement the recommendations on addressing exemptions from the VAT gap analysis (structural benchmark). As a usual undertaking, Government will continue publishing on the internet the names and beneficiaries (whether individual or corporation) of all tax expenditures. Further, Government will also move to VAT accounting on a net basis rather than budgeting for VAT refunds as a spending item.

23. Government will take tax measures to strengthen revenues for next fiscal year's budget. In FY 2013/14 Government will terminate VAT exemptions on: i) hotel accommodation; ii) water for domestic consumption; iii) the textile sector and iv) feeds for poultry and livestock.

24. In the FY 2013/14 budget, Government will also: i) increase the registration fee and stamp duty on third party insurance policies for motor vehicles; ii) introduce capital gains tax on the disposal of commercial buildings by individuals; iii) amend the thin capitalization rule to limit excessive use of related party debt; iv) increase excise duty of cigarettes; v) eliminate income tax exemptions on income derived from agro processing (structural benchmark); vi) expand the number

of withholding tax agents; vii) increase excise duty by 50 shillings on petrol and diesel; viii) restore excise duty of 200 shillings on kerosene; ix) introduce a transaction levy on mobile money transfers; and x) review the taxation of the petroleum and mineral sector. In this regard, Government will seek TA from IMF in the area of natural resource taxation. Implementation of these measures will be structural benchmarks under the PSI.

25. Tax administration has improved tremendously in service delivery in recent years. In the coming year, the Uganda Revenue Authority's (URA) efforts will be focused more explicitly on the major taxpayer segments: large, medium, small and micro. It will rank compliance risks by taxpayer segments and define response across functions. In particular, URA will ensure that the taxpayer service and enforcement functions that support the large taxpayers are improved. This will be accomplished by ensuring that staffing and training needs are met to promote compliance and improve auditing capacity. As part of implementing an effective system of binding public rulings, URA will publish in the gazette all public rulings it makes on interpretation of the law.

Public Financial Management

26. Government will continue implementing PFM reforms to strengthen controls on use of public funds and protect priority areas of the budget. The Public Financial Management Bill (PFMB), currently in Parliament, aims at consolidating the existing 2003 Public Finance and Accountability Act (PFAA) and the Budget Act 2001, and strengthening the fiscal and macroeconomic framework and the budget process. Key milestones include ensuring that the budget is passed before the start of the financial year; providing for a contingencies fund to help manage in-year expenditure pressures and reduce the stock of domestic arrears; setting out a legal framework for the management of oil revenues; and introducing a charter for fiscal responsibility.

27. Government will submit to Parliament a set of amendments to the PFMB 2012 to bring it up to international best practice Amendments will include, inter alia: i) a chapter to strengthen and enforce sanctions; ii) an explicit reference to the decision to establish a Treasury Single Account (TSA); iii) a requirement to specify the source of financing of any supplementary expenditure; iv) a requirement to specify an annual ceiling for the issuance of Treasury securities that is not subject to change without Parliamentary approval; v) a requirement that proceeds from Treasury securities issuance for monetary policy purposes be held in a special fund which is not available for spending by Government; and vi) amendments to the Bank of Uganda Act to significantly tighten access of Government to advances from the BoU. It is expected that the bill will be enacted into law during FY 2013/14.

28. Misappropriation of funds and payment arrears were made possible by the incomplete migration of payroll and pensions votes to the Integrated Personnel and Payroll System (IPPS). To address this issue, Government will complete the rollout of IPPS to cover personnel management and payroll of all entities within central government by December 2013 (structural benchmark).

Treasury Single Account

29. Government is committed to introducing a TSA to improve cash management, control, and transparency of government operations, and to avoid unnecessary interest costs. The Ministry of Finance will submit to cabinet in May 2013 a cabinet information paper reflecting the decision to introduce a TSA. The implementation of the TSA will be undertaken in a phased approach starting with a pilot scheme involving 6 votes followed by a roll out to the rest of Central Government. Government will start introducing a TSA for all Integrated Financial Management Systems (IFMS) related transactions, including for the Treasury General Accounts (TGAs), salaries, and IFMS projects by March 2014 (structural benchmark). Prior to this, by December 2013 Government will complete the expansion of IFMS to all central government votes (structural benchmark).

Management of Arrears

30. Government will reduce the stock of unpaid bills, as measured by the Accountant General, by at least 50 billion shillings between July 1, 2013 and June 30, 2014. The PFMB will require accounting officers to prepare work plans, procurement plans, and recruitment plans to be approved by the Secretary to the Treasury, which will thereafter form the basis for issuing cash limits and releases. This is expected to prevent over committing of government expenditures beyond available resources. In the interim period, as a structural benchmark, Government will continue to submit to Cabinet regular quarterly reports on unpaid bills of nine ministries based on data in the Commitment Control System for the previous quarter of the fiscal year. In addition, Government will publish, on a quarterly basis, releases by the MoFPED for utilities (water, power and telephone) obligations of spending ministries and actual payments for them. This will enhance transparency and facilitate control and elimination of domestic arrears.

Improvements in Implementation Capacity

31. In order to streamline and improve project identification, selection and execution, government will complete the review of the Public Investment Program (PIP) by end May 2014. The review is intended to ensure that the program only contains projects for which cost-benefit analysis and feasibility studies have been conducted and sources of financing have been secured. To this end, Government will ensure that capacity to carry out cost benefit analysis and prepare feasibility studies is developed. Moreover, quarterly project portfolio reviews will be conducted to ensure efficient implementation of projects.

Management of Oil Revenues

32. The PFMB provides for the establishment of fiscal rules that will be designed upon approval of the law with a view to determining a clear framework for savings and investment of oil resources. Under this structure, the non-oil primary balance will be the main measure of the fiscal stance. Government will establish a petroleum fund into which all oil revenues will be deposited and held. A proportion of oil income will be spent through the budget through transparent annual

appropriations. The petroleum fund will belong to the Government of Uganda and be held abroad and managed by the BoU, separately from the foreign exchange reserves.

33. Tax revenue from capital gains from oil company transactions has been accumulated in a special fund in the BoU. Government will use these resources exclusively for the construction of the Karuma hydroelectric project. Similarly, resources in the energy fund will be exclusively used for energy projects.

Other Reforms

34. While delays have impeded the issuing of national identity cards, Government remains committed to bringing this project to completion. This will facilitate tax administration and financial sector development. By May 2014, Government will issue at least 1 million cards under the new national identification system (structural benchmark). To accelerate implementation of the project, budgetary funds have been allocated to it and in addition voluntary payment for ID cards will be encouraged.

VII. Transition to Fully Fledged Inflation Targeting

35. The ITL framework has now been in operation for almost two years and has proved successful in bringing down inflation to its current level which is only slightly higher than the BoU's medium-term target. The BoU is determined to continue to improve the current ITL regime to ensure low inflation over the medium term and allow a transition to Fully Fledged Inflation Targeting, through a combination of institutional reforms and technical capacity building.

36. On the institutional front, Government is finalizing arrangements to carry out by July 2013 the first stage of recapitalization of the BoU with marketable securities to the amount stipulated by law (structural benchmark). To this end, a formal agreement will be signed by the Minister of Finance and the Governor of the BoU that will also enhance operational independence of the BoU by ensuring that the BoU has sufficient instruments at market interest rates and adequate maturities to implement monetary policy; will reflect the BoU's commitment to control inflation and to streamline its operating expenditures; and will recognize that a second phase of recapitalization will be needed in the future.

37. By February 2014, the Ministry of Finance will submit to cabinet amendments to the Bank of Uganda Act including provisions for capital adequacy of BoU as an adequate percent of monetary liabilities as well as other measures to support comprehensive reforms in support of inflation targeting (structural benchmark) and central bank modernization.

38. On the operational side both the MoFPED and BoU are strengthening their technical capacities for macroeconomic modeling. In improving its inflation forecasting skills, the BoU is receiving TA from the Research Department of the Fund. The BoU will improve the efficacy of its monetary policy instruments and enhance its communications strategy to facilitate understanding by the public of monetary policy decisions and forecasts of macroeconomic variables.

39. To support the transition to a fully fledged inflation targeting framework, the Government requests that the quantitative performance criteria on net domestic assets (NDA) be replaced with an inflation consultation clause, while retaining the net international reserves (NIR) floor for external stability.

VIII. Financial Sector Soundness and Development

40. The BoU is implementing Basel III reforms in a phased manner. It has carried out a pilot exercise on the use of a liquidity coverage ratio by large banks, and now intends to enforce the use of this ratio by all banks. A capital conservation buffer will be also imposed. Using the methodology recommended by the Bank for International Settlements, the BoU is identifying the systemically important financial institutions that will be subject to higher capital requirements. Legislations to introduce a capital charge to cover market risk, prevent money laundering, and amend the Financial Institutions Act are under Parliament and will be implemented as soon as they are approved.

41. Most of the commercial banks operating in Uganda are subsidiaries of regional or international banks. The BoU has signed Memorandum of Understanding with several home supervisors to facilitate consolidated supervision and sharing of information. The BoU is also participating in supervisory colleges of international banks.

42. Government is advancing reforms in the pension sector. It will ensure the financial viability of the Public Service Pension Scheme, and improve oversight of the pension sector including the National Social Security Fund. The Uganda Retirement Benefits Regulatory Authority Board has enacted licensing regulations and guidelines for the establishment of private retirement benefit schemes and has started issuing provisional licenses.

43. To promote financial deepening and inclusion, the BoU will improve financial literacy, ensure consumer protection, and promote financial innovation (including through mobile money and agency banking). The BoU will also reinforce efforts to regulate mobile money transactions by preparing legislation governing the national payment system. We expect this strategy will increase access of the population to financial services.

IX. Enhancing the Business Environment

44. Uganda's competitiveness agenda aims at attracting foreign investment to generate growth and employment. The agenda comprises infrastructure development, institutional and legal reforms to lower the costs of doing business, reduction of red-tape, and access of small and medium enterprises to credit. In addition, Government has developed a policy and legal framework to support the PPP model as an option for providing long-term value and reliability to critically important infrastructure sectors. To enhance transparency, by March 2014 Government will include in the Budget Framework Papers a status report of ongoing PPP programs, including individual estimates of each project's contingent liability (structural benchmark).

45. Government has introduced an approach called Contractor Facilitated Financing, a system that integrates supplier credits into the tendering process, which is aimed at reducing delays in the implementation of Government projects. Government considers that this approach has potential to improve the efficiency of project execution, but is fully mindful of its inherent risks. Consequently, Government will ensure full transparency in the use of CFF including by publishing details of all agreements and clearly assessing and differentiating the cost of both the projects and the financing terms. The applicable terms and conditions will be detailed in the Revised National Debt strategy to be published by end June 2013.

X. Program Monitoring

46. Progress in the implementation of the policies under this program will be monitored through quantitative assessment criteria (QACs), indicative targets (ITs), and structural benchmarks (SBs) detailed in the attached Tables 1 and 2 and through semi-annual reviews. Quantitative assessment criteria are proposed for end-June 2013 and end-December 2013, to be monitored respectively at the first and second reviews. The first review is expected to be completed by end-December 2013 and the second review by end-June 2014. The attached Technical Memorandum of Understanding—which is an integral part of this Memorandum—contains definitions and adjustors.

Table 1. Uganda: Quantitative Assessment Criteria and Indicative Targets for June 2013 - March 2014[1]
(Cumulative change from the beginning of the fiscal year, unless otherwise stated)

	June 30, 2013 [2]	September 30, 2013 [3]	December 31, 2013 [3]	March 31, 2014 [3]
		(Billions of Ugandan shillings)		
Assessment criteria				
Ceiling on the increase in net domestic financing of the central government	868	257	-421	-54
		(Millions of US dollars)		
Ceiling on the stock of external payments arrears incurred by the public sector [4]	0	0	0	0
Ceiling on the contracting or guaranteeing of new nonconcessional external debt with maturities greater than one year by the public sector [4, 5]	1,500	1,500	1,500	1,500
Ceiling on new external debt with maturity up to one year contracted or guaranteed by the public sector [4, 6]	0	0	0	0
Minimum increase in net international reserves of the Bank of Uganda (US$mn)	361	16	52	107
Share of oil revenue placed in the Petroleum Fund [7]	100	100	100	100
		(Billions of Ugandan shillings)		
Indicative targets				
Ceiling on the increase in base money liabilities of the Bank of Uganda	836	239	504	591
Floor on tax revenue	7,015	1,813	4,024	5,977
Expenditures on poverty alleviating sectors	2,498	607	1,246	1,745
Ceiling on the issuance of guarantees by the Government/Bank of Uganda	0	0	0	0
		(Annual percentage change)		
Inflation consultation clause				
Outer band (upper limit)	9.8	9.0	9.7	9.6
Inner band (upper limit)	8.8	8.0	8.7	8.6
Core inflation target [8]	6.8	6.0	6.7	6.6
Inner band (lower limit)	4.8	4.0	4.7	4.6
Outer band (lower limit)	3.8	3.0	3.7	3.6

[1] Defined in the Technical Memorandum of Understanding (TMU). Values for June 2013 and December 2013 are quantitative assessment criteria except as marked. Values for September 2013 and March 2014 are indicative targets except as marked.

[2] Proposed targets are measured as the change from June 2012, except as marked.

[3] Proposed targets are measured as the change from June 2013, except as marked.

[4] Continuous assessment criterion.

[5] Cumulative change from June 28, 2013. To be used exclusively for infrastructure investment projects.

[6] Excluding normal import-related credits.

[7] To ensure full and transparent transfer of oil revenues to the fiscal accounts.

[8] Annual percentage change, twelve-month period average core inflation. Calculated as stipulated in the TMU.

Table 2. Structural Benchmarks

Policy Measure	Macroeconomic Rationale	Date
1. Government to carry out the first stage of recapitalization of the Bank of Uganda with marketable securities to the amount stipulated by law.	To enhance monetary policy independence and central bank credibility.	July 2013
2. Ministry of Finance to submit to cabinet regular quarterly reports on unpaid bills of nine ministries based on data in the Commitment Control System (CCS) for the previous quarter of the fiscal year.	To facilitate control and elimination of expenditure arrears.	October 1, 2013, for quarter ending June 30, 2013; January 1, 2014, for quarter ending September 30, 2013; April 1, 2014, for quarter ending December 31, 2013.
3. Government to carry out a VAT gap analysis in consultation with IMF staff and to publish such analysis.	To make transparent the costs of VAT tax expenditures.	December 2013
4. Government to complete the rollout of the IPPS to cover personnel management and payroll of all entities within central government	To improve both governance and transparency of budget execution	December 2013
5. Government to complete the expansion of the treasury system (IFMS) to all of central government votes	To improve both governance and transparency of budget execution.	December 2013
6. Ministry of Finance to submit to cabinet amendments to the Bank of Uganda Act including a provision for capital adequacy of BoU as an adequate percent of monetary liabilities, as well as other provisions to support implementation of inflation targeting.	To enable full monetary policy independence and credibility of the central bank. This measure would complete the second stage of the recapitalization of BoU.	February 2014
7. Government to start introducing a Treasury Single Account for IFMS related transactions, including for the Treasury General Accounts, salaries, and IFMS projects.	To improve both governance and transparency of budget execution.	March 2014
8. Government to prepare an action plan to implement the recommendations on addressing tax exemptions that come out of the VAT gap analysis	Improve tax efficiency	March 2014
9. Government to include in the Budget Framework Paper a status report of all ongoing PPP programs, including individual estimates of each project's contingent liability.	To enhance fiscal transparency	March 2014
10. Government to have issued a minimum of 1 million ID cards under the new national identification system.	To support efforts to strengthen revenue collection, promote the unique identification of financial sector clients, and combat money laundering and the financing of terrorism.	May 2014
11. Government to eliminate the income tax exemption on income derived from agro-processing.	To increase revenue and tax administration efficiency.	May 2014

Attachment 2. Technical Memorandum of Understanding

I. Introduction

1. This memorandum defines the quarterly assessment criteria and indicative targets described in the Memorandum of Economic and Financial Policies (MEFP) for the financial program supported by the IMF Policy Support Instrument (PSI) over the period of June 30, 2013—March 31, 2014 (until June 2014 for inflation consultation clause), and sets forth the reporting requirements under the instrument. For the first year of the PSI-supported program, all foreign assets and liabilities will be converted into U.S. dollars at each test date using the average cross exchange rates referred to in the table below for the various currencies and then converted into Uganda shillings using the program average U.S. dollar-Uganda shilling exchange rate for March 2013.

Program Exchange Rates (end-March 2013)	
US Dollar (US$)	1
British pound/US$	0.66
Japanese Yen/US$	94.2
SDR/US$	0.67
Kenyan Shilings/US$	85.6
Tanzania Shilings/US$	1598.7
Euro/US$	0.78
Ugandan Shilings/US$	2594.8

II. Consultation Mechanism on Inflation

2. **The quarterly consultation bands for the twelve-month average rate of consumer price inflation** (as measured by the core consumer price index (CCPI) published by the Uganda Bureau of Statistics (UBOS)) are specified in the text table: Inflation Targets. Projected CCPI inflation for end-June 2013 and end-December 2013 will be subject to the consultation mechanism, while those for end-September 2013, end-March 2014 and end-June 2014 are indicative targets.

Text Table. Inflation Targets					
	Jun. 2013	Sep. 2013	Dec. 2013	Mar. 2014	Jun. 2014
Outer band (upper limit)	9.8	9.0	9.7	9.6	9.3
Inner band (upper limit)	8.8	8.0	8.7	8.6	8.3
Core inflation target	6.8	6.0	6.7	6.6	6.3
Inner band (lower limit)	4.8	4.0	4.7	4.6	4.3
Outer band (lower limit)	3.8	3.0	3.7	3.6	3.3

3. Should the observed average CCPI inflation for the test date linked to a PSI program review (i.e., end-June 2013 for the first review and end-December 2013 for the second review) fall outside the outer band as specified in the above table, the authorities will complete a

consultation with the Executive Board of the Fund on their proposed policy response before requesting completion of the review under the program. The authorities will not be able to request completing a review under the PSI-supported program if the average CCPI inflation has moved outside of the outer band as of the test date linked to such review, until the consultation with the Executive Board has taken place. In line with the accountability principles, the BoU will report to the public the reasons for any breach of the outer bands, and its policy response. In addition, the BoU will conduct discussions with the Fund staff when the observed average CCPI inflation falls outside the inner band as specified for the end of each quarter in the above table.

III. Base Money

4. Base money is defined as the sum of currency issued by the BoU and the commercial banks' deposits in the BoU. The commercial bank deposits include the statutory required reserves and excess reserves held at the BoU and are net of the deposits of closed banks at the BoU and Development Finance Funds (DFF) contributed by commercial banks held at the BoU. The base money limit for June 2013 will be a ceiling on the cumulative change from the monthly average based on daily data for June 2012 to the same monthly average for June 2013. The base money limits for September 2013 and December 2013 will be ceilings on the cumulative change from the monthly average based on daily data for June 2013 to the same monthly averages for September 2013 and December 2013, respectively. Base money limits for June 2013, September 2013, and December 2013 will be indicative targets under the PSI-supported program.

IV. Ceiling on the Cumulative Increase in Net Domestic Financing of the Central Government[1]

5. **Definition.** The cumulative increase in net domestic financing of the central government (NDF) is defined from below the line on a cash basis as the sum of:

a. the change in net claims on the central government by the banking system: Net claims on the central government by the banking system is defined as the difference between the outstanding amount of bank credits to the central government and the central government's deposits with the banking system, excluding oil revenues in the petroleum fund and deposits in administered accounts and project accounts with the banking system, including the central bank. Credits comprise bank loans and advances to the government and holdings of government securities and promissory notes. Central government's deposits with the banking system include the full amount of resources freed by the IMF Multilateral Debt Relief Initiative (MDRI). NDF by the banking system will be calculated based on data from balance sheets of the monetary authority and commercial banks as per the monetary survey.

[1] The central government comprises the treasury and line ministries.

b. *the change in net claims on the central government of domestic nonbank institutions and households*: net claims on the general government of domestic nonbank institutions and households are defined as treasury bills, bonds or other government securities held by nonbank institutions and households (including nonresidents and nonresident financial institutions), plus any other liabilities of the central government to domestic nonbank institutions or households;

6. All changes will be calculated as the difference between end-of-period stocks, net of any valuation changes resulting from currency movements.

V. Floor on Net International Reserves of the Bank of Uganda

7. Net international reserves (NIR) of the BoU are defined for program monitoring purpose as reserve assets of the BoU net of short-term external liabilities of the BoU. Reserve assets are defined as external assets readily available to, and controlled by, the BoU and exclude pledged or otherwise encumbered external assets, including, but not limited to, assets used as collateral or guarantees for third-party liabilities. Short-term external liabilities are defined as liabilities to nonresidents, of original maturities less than one year, contracted by the BoU and include outstanding IMF purchases and loans.

8. For program-monitoring purposes, reserve assets and short-term liabilities at the end of each test period will be calculated in U.S. dollars by converting the stock from their original currency denomination at program exchange rates (as specified in paragraph 1). The NIR limit for June 2013 will be a floor on the change of the NIR stock from June 2012 to June 2013. The NIR limits for December 2013 and March 2014 will be floors on the change of the NIR stock from June 2013 to December 2013, and March 2014, respectively. The NIR limit for December 2013 will be quantitative assessment criteria under the PSI-supported program; the floor for March 2014 will be an indicative target.

VI. Expenditures on Poverty Alleviating Sectors

9. The indicative target on poverty alleviating expenditures includes domestic expenditures inclusive of wages and salaries in the Health, Education, Water and Environment and Agriculture sectors as defined by the Government of Uganda's functional budget classification. Compliance with the indicative floor for poverty alleviating expenditures will be verified on the basis of releases.

VII. Ceiling on Issuance of Guarantees by the Government or Bank of Uganda

10. The indicative target on issuance of guarantees by the Government or Bank of Uganda aims to prevent accumulation of contingent liabilities by the Government (including Government entities such as ministries, agencies and authorities). Included against the ceiling are any direct,

contingent liabilities of Government (including entities that are part of Government such as ministries, agencies and authorities) issued after June 30, 2012, and including any guarantees issued prior to July 1, 2012 but which are extended after June 30, 2012. This excludes guarantee programs which have explicit budget appropriations.

VIII. Share of Oil Revenue Placed in Petroleum Fund

11. The purpose of this assessment criterion is to avoid a situation whereby petroleum revenues bypass the Ugandan budget framework. A petroleum fund will be created upon passage of the revised PFMB; in the meantime, government has established a petroleum revenue account in the Bank of Uganda. This QAC will be deemed satisfied if 100 percent of petroleum revenues are transferred to this account upon collection by URA. These resources may then be spent or saved as governed by the organic budget law in force at the time (PFAA 2003 until the new PFMB is enacted).

IX. Tax Revenue

12. A floor applies on tax revenue of central government measured cumulatively from the beginning of the fiscal year. For program monitoring purposes, tax revenue is defined as the sum of direct domestic taxes (PAYE, corporate tax, presumptive tax, other direct taxes, withholding tax, rental income tax, tax on bank interest, casino tax and unallocated receipts), excise duty and value-added taxes net of refunds and taxes on international trade minus temporary road licenses as defined by the Government of Uganda's revenue classification.

X. Adjusters

13. The NIR target is based on program assumptions regarding budget support, assistance provided under the Heavily Indebted Poor Countries (HIPC) Initiative and the MDRI, external debt-service payments. The NIR target is based on program assumptions regarding automatic access by commercial banks to the BoU's rediscount and discount window facilities.

14. The Uganda shilling equivalent of projected budget support (grants and loans) plus HIPC Initiative assistance in the form of grants on a cumulative basis from July 1 of the relevant fiscal year is presented under Schedule A. The ceilings on the cumulative increase in NDF will be adjusted downward (upward), and the floor on the cumulative increase in NIR of the BoU will be adjusted upward (downward) by the amount by which budget support, grants and loans, plus HIPC Initiative and MDRI assistance, exceeds (falls short of) the projected amounts.

Schedule A: Budget Support[1]
(Ush billions)

	Jun-13	Sep-13	Dec-13	Mar-14
Cumulative change from July 1, 2012	469	…	…	…
Cumulative change from July 1, 2013	…	50	79	130

[1]Including HIPC and MDRI.

15. The ceiling on the increases in NDF will be adjusted downward (upward) and the floor on the increase in NIR will be adjusted upward (downward) by the amount by which debt service due[2] plus payments of external debt arrears less deferred payments (exceptional financing) falls short of (exceeds) the projections presented in Schedule B. Deferred payments are defined to be (i) all debt service rescheduled under the HIPC Initiative; and (ii) payments falling due to all non-HIPC Initiative creditors that are not currently being serviced by the authorities (that is, gross new arrears being incurred).

Schedule B: External Debt Service[1]
(Ush billions)

	Jun-13	Sep-13	Dec-13	Mar-14
Cumulative change from July 1, 2012	300	…	…	…
Cumulative change from July 1, 2013	…	92	185	284

[1]Debt service is defined as pre-HIPC Initiative debt service.

16. The ceiling on NDF will be adjusted upward (downward) by the amount by which the domestic currency equivalent of Karuma spending (using the market exchange rate) exceeds (falls short of) the projected amounts as set out in Schedule C.

Schedule C: Expenditures for Karuma Hydropower Project[1]
(US$ millions)

	Jun-13	Sep-13	Dec-13	Mar-14
Cumulative change from July 1, 2012	0	…	…	…
Cumulative change from July 1, 2013	…	0	0	0

[1]Adjustor is the domestic currency equivalent of Karuma spending.

[2] Debt service due is defined as pre-HIPC Initiative debt service due, excluding debt service subject to HIPC Initiative debt rescheduling.

17. The ceiling on NDF will be adjusted upward (downward) by the amount by which inflows into the petroleum fund falls short of (exceeds) the projected amounts as set out in Schedule D.

Schedule D: Inflows into Petroleum Fund
(US$ millions)

	Jun-13	Sep-13	Dec-13	Mar-14
Cumulative change from July 1, 2012	0	…	…	…
Cumulative change from July 1, 2013	…	0	279	279

XI. Ceiling on the Contracting or Guaranteeing of New Nonconcessional External Debt by the Public Sector, and Ceiling on the Stock of External Payments Arrears Incurred by the Public Sector[3]

18. The assessment criterion on short-term debt refers to contracting or guaranteeing external debt with original maturity of one year or less by the public sector. Excluded from this assessment criterion are normal import-related credits and non-resident holdings of government securities and government promissory notes. The definition of "debt" is set out in paragraph 20.

19. The program includes a ceiling on new nonconcessional borrowing with maturities greater than one year contracted or guaranteed by the public sector.[4] Nonconcessional borrowing is defined as loans with a grant element of less than 35 percent, calculated using average commercial interest rates references (CIRRs) published by the Organization for Economic Cooperation and Development (OECD). In assessing the level of concessionality, the 10-year average CIRRs should be used to discount loans with maturities of at least 15 years, while the 6-month average CIRRs should be used for loans with shorter maturities. To both the 10-year and 6-month averages, the following margins for differing payment periods should be added: 0.75 percent for repayment periods of less than 15 years; 1 percent for 15–19 years; 1.15 percent for 20–25 years; and 1.25 percent for 30 years or more. The ceiling on nonconcessional external borrowing or guarantees is to be observed on a continuous basis. The coverage of borrowing includes financial leases and other instruments giving rise to external liabilities, not only current as defined below, but also contingent, on nonconcessional terms. External debt for the purpose of this assessment criterion means borrowing giving rise to liabilities to non-residents. Excluded

[3] Public sector comprises the general government (which includes the central government, local governments, and monetary authorities), and entities that are public corporations which are subject to 'control by the government', defined as the ability to determine general corporate policy or by at least 50 percent government ownership.

[4] Contracting and guaranteeing is defined as approval by a resolution of Parliament as required in Section 20(3) and 25(3) of the Public Finance and Accountability Act, 2003.

from the limits are changes in indebtedness resulting from non-resident holdings of government securities and government promissory notes, refinancing credits and rescheduling operations, and credits extended by the IMF. For the purposes of the program, arrangements to pay over time obligations arising from judicial awards to external creditors that have not participated in the HIPC Initiative do not constitute nonconcessional external borrowing. Excluded from these limits are also nonconcessional borrowing within the limits specified in Table 1 of the MEFP. The ceiling also excludes nonconcessional borrowing by one state-owned bank, Housing Finance Bank, which poses limited fiscal risk and is in a position to borrow without a government guarantee.

20. The definition of debt, for the purposes of the limit, is set out in point 9 of the Guidelines on Performance Criteria with Respect to External Debt (Executive Board's Decision No. 6230-(79/140), as amended by Decision No 14416-(09/91), effective December 1, 2009). It not only applies to the debt as defined in Point 9 of the Executive Board decision, but also to commitments contracted or guaranteed for which value has not been received. The definition of debt set forth in No. 9 of the Guidelines on Performance Criteria with Respect to External Debt in Fund Arrangements reads as follows:

> (a) For the purpose of this guideline, the term "debt" will be understood to mean a current, i.e., not contingent, liability, created under a contractual arrangement through the provision of value in the form of assets (including currency) or services, and which requires the obligor to make one or more payments in the form of assets (including currency) or services, at some future point(s) in time; these payments will discharge the principal and/or interest liabilities incurred under the contract. Debts can take a number of forms, the primary ones being as follows: (i) loans, i.e., advances of money to the obligor by the lender made on the basis of an undertaking that the obligor will repay the funds in the future (including deposits, bonds, debentures, commercial loans and buyers' credits) and temporary exchanges of assets that are equivalent to fully collateralized loans under which the obligor is required to repay the funds, and usually pay interest, by repurchasing the collateral from the buyer in the future (such as repurchase agreements and official swap arrangements);
> (ii) suppliers' credits, i.e., contracts where the supplier permits the obligor to defer payments until sometime after the date on which the goods are delivered or services are provided; and (iii) leases, i.e., arrangements under which property is provided which the lessee has the right to use for one or more specified period(s) of time that are usually shorter than the total expected service life of the property, while the lesser retains the title to the property. For the purpose of the guideline, the debt is the present value (at the inception of the lease) of all lease payments expected to be made during the period of the agreement excluding those payments that cover the operation, repair, or maintenance of the property. (b) Under the definition of debt set out in point 9(a) above, arrears,

penalties, and judicially awarded damages arising from the failure to make payment under a contractual obligation that constitutes debt. Failure to make payment on an obligation that is not considered debt under this definition (e.g., payment on delivery) will not give rise to debt.

21. The ceiling on the accumulation of new external payments arrears is zero. This limit, which is to be observed on a continuous basis, applies to the change in the stock of overdue payments on debt contracted or guaranteed by the public sector from their level at end-June 2013. External debt payment arrears consist of external debt service obligations (reported by the Statistics Department of the BoU, the Macro Department of the Ministry of Finance) that have not been paid at the time they are due as specified in the contractual agreements but shall exclude arrears on obligations subject to rescheduling.

XII. Monitoring and Reporting Requirements

22. The Government of Uganda will submit information to IMF staff with the frequency and submission time lag as indicated in Table 1. The quality and timeliness of the data submission will be tracked and reported by IMF staff. The information should be mailed electronically to AFRUGA@IMF.ORG.

Attachment II. Table 1. Summary of Reporting Requirements

Reporting institution	Report/Table	Submission Frequency	Submission lag
I. Bank of Uganda	Issuance of government securities, repurchase operations and reverse repurchase operations	Weekly	5 working days
	Operations in the foreign exchange	Weekly	5 working days
	Interest rates (7 day interbank, commercial bank prime lending rate, government securities)	Weekly	5 working days
	Private sector credit growth by shilling and forex, and excess reserves of commercial banks	Weekly	5 working days
	Disaggregated consumer price index.	Monthly	2 weeks
	Balance sheet of the BoU, consolidated accounts of the commercial banks, and monetary survey.	Monthly	4 weeks
	Daily balances of net foreign assets, net domestic assets, and base money of the BoU.	Monthly	4 weeks
	Monthly foreign exchange cash flow table of BoU.	Quarterly	4 weeks

Attachment II. Table 1. Summary of Reporting Requirements			
Reporting institution	**Report/Table**	**Submission Frequency**	**Submission lag**
	Statement of (i) cash balances held in project accounts at commercial banks; (ii) total value (measured at issue price) of outstanding government securities from the Central Depository System (CDS); and (iii) the stock of government securities (measured at issue price) held by commercial banks from the CDS.	Quarterly	6 weeks
	Summary of (i) monthly commodity and direction of trade statistics; (ii) disbursements, principal and interest, flows of debt rescheduling and debt cancellation, arrears, and committed undisbursed balances—by creditor category; and (iii) composition of nominal HIPC Initiative assistance.	Quarterly	6 weeks
	Summary of stock of external debt, external arrears, and committed undisbursed loan balances by creditor.	Quarterly	6 weeks
	Standard off-site bank supervision indicators for deposit money banks.	Quarterly	4 weeks
	Summary table of preliminary program performance comparing actual outcome with adjusted program targets for (i) base money; (ii) net claims on central government by the banking system; (iv) new nonconcessional external borrowing; and (v) net international reserves	Quarterly	6 weeks
II. Ministry of Finance	Summary of central government accounts. Revenues shall be recorded on a cash basis. Expenditures shall be recorded when checks are issued, except for domestic and external debt-service payments[5], cash transfers to districts, and externally funded development expenditures. Expenditures on domestic interest will be recorded on an accrual basis and external debt service will be recorded on a commitment basis (i.e., when payment is due).	Monthly	4 weeks

[5] The budget records domestic interest payments on cash-basis while for program purposes this entry will be reported on an accrual basis.

Attachment II. Table 1. Summary of Reporting Requirements			
Reporting institution	**Report/Table**	**Submission Frequency**	**Submission lag**
	Summary of outstanding stock of unpaid payment claims	Quarterly	6 weeks
	Summary of contingent liabilities of the central government and the Bank of Uganda. For the purpose of the program, contingent liabilities include all borrowings by statutory bodies, government guarantees, claims against the government in court cases that are pending, or court awards that the government has appealed.	Quarterly	6 weeks
	Detailed monthly central government account of disbursed budget support and project grants and loans (less change in the stock of project accounts held at the BoU and commercial banks), HIPC support, and external debt service due and paid.	Quarterly	4 weeks
	Detailed central government account of disbursed donor project support grants and loans.	Monthly	6 weeks
	Statement on new external loans contracted or guaranteed by the central government and the Bank of Uganda during the period according to loan agreements.	Quarterly	6 weeks
	Updated national accounts statistics (real and nominal) according to UBOS and medium-term projections.	Quarterly	12 weeks