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Post-election economic woes IMF, donors withhold support for Uganda



Posted by Musa

Rachel Kimono could not hide her excitement on the eve of the Feb. 18 general election. She was waiting for money promised by mobilizers for the ruling NRM party in her Nakaloke village in Mbale district to potential voters. She bagged Shs 20,000.

Kimono is one of millions of Ugandans who made a hit during the election. They included politicians, printers, transporters, advertising agencies, events managers, and bribed voters.

A Uganda Bureau of Statistics (UBOS) report for February 2011 showed that production of meat, beer, sodas, and water went up mainly because of election related consumption.

Even as the spending binge led by the ruling NRM party was going on, however, Finance minister Syda Bbumba made an ominous revelation on Jan.24 to *The Daily monitor* newspaper; the government was having “cash limitations” i.e. it was broke.

Other reports indicated that by December; just mid-way into the 2010/11 financial year, up to 85 percent of the Shs 7.3 trillion national budget had been spent. According to *The East African* newspaper, which quoted a Finance ministry official, Shs 3 trillion was spent in the month leading to the election alone. Most of this money allegedly went to President Museveni's campaign and the Shs 20,000 Kimono received was possibly part of it.

Bbumba's revelation that government was 'broke' followed parliament's passing of a Shs 605 billion supplementary budget for various government departments that sparked donor and civil society fury.

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Observers say the supplementary budget money went into campaigns because even after the parliament passed the additional money, most departments still did not have money; salaries remained unpaid, official travel was cancelled, office supplies not bought, and projects were stalling.

Then on Feb. 11, exactly one week to the Feb. 18 Uganda general elections, the Executive Board of the International Monetary Fund (IMF) issued a statement that has gone largely unreported but could have adverse impacts on the economy.

The IMF said it had not completed the first review under the three-year Policy Support Instrument (PSI) for Uganda. This means Uganda does not now have IMF support to borrow from multilateral development bodies like the World Bank Group, the African Development Bank, and other international development agencies.

A week later, on Feb. 17, the Dutch government revealed it was withholding EUR 3.2 million (about Shs10 billion) in budget support to Uganda over the government's failure to punish officials who swindled US\$44 million during the Commonwealth Heads of State and Government Meeting (CHOGM) in Kampala in 2007.

Ambassador Jeroen Verheul warned that as chair of the donors Working Group in the sector affected, it would monitor it closely.

"We look forward to the budget workshop preparing for the fiscal year 2011/2012," the ambassador concluded ominously.



The next opportunity to review the IMF Uganda PSIs is in June and the Dutch funding is in December but anxiety is mounting over the economy.

Troubling signs

Campaign euphoria may have muffled Bbumba's cry for help, the IMF's rebuff and the Dutch anger but, just weeks after the election, they are attracting fresh attention as the post-election economy wobbles.

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Kimono now has to cope with rising prices for almost everything. Food prices, which are already unusually high for the usually wet first quarter of the year, are set to rise as a prolonged drought persists and crops fail.

A kilogram of sugar has shot to Shs 2900 from Shs 2300 and rice to Shs 2500 from Shs 1700. Rising global fuel prices and supply chain glitches by leading local operator, Total Uganda, have pushed local pump prices to an all time high. Declining value of exports have ensured that the current account balance weakens further.

Amid this gloom and uncertainty, sometime in early May, President Yoweri Museveni who won the Feb. 18 election will be sworn-in. His new term will start with the reading on a new budget in June. Before that, post-election economy will be intensely scrutinized.

How will government officials interpret the IMF and donor positions, the much-discussed negative pre-election indicators, and confounding profligate government spending?

Donor influence in Uganda is waning as they increasingly opt to channel support to specific projects and the government moves to fund more of the national budget. In the 2010/11 FY, donors funded up to just 25 percent. However, donor opinion can still affect the Uganda government's ability to deliver public services, its international image, and its credit rating.

Significantly, therefore, while the government can either resolve or pretend to resolve the local issues surrounding its shocking campaign expenditures, it cannot fudge around restoring IMF/World Bank belief in its macro-economic management.

The World Bank has said it is studying the situation carefully. Kundhavi Kadiresan, the World Bank Country Manager, said persistent reversion to supplementary budgets could undermine the credibility of the budget process, minimize the link between the budget and the policy formulation framework and make the budget a less effective tool of fiscal policy and economic planning.

"Of particular concern are the off-budget expenditures which further undermine budget discipline, transparency and stated spending priorities, and can greatly impact the actual fiscal position of a country," she said.

But the government is determined to put positive sheen on the economic indicators.

The February reports from the research department of Uganda's Central Bank, Bank of Uganda (BoU) and the Uganda Investment Authority (UIA) are all positive.

"In the midst of an election period," the UIA report said, "there were fears that investors would be wary of investing ... (but) we did better in February than in January 2011."

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“The Ugandan economy has reverted to its pre-crisis growth trajectory, with strong growth in the first half of the 2010-11,” the BoU report said.



However, the BoU report – which carries more substance than the UIA’s speculative format and is based on January economic indicators with an eye on the outlook for a few months into 2011, was really a bag of subtle belt-tightening tricks. In that sense, it realistically mirrored the options open to the country and Museveni in the new term.

The BoU report focused on its efforts manage the unnecessary election induced consumption, mop up excess liquidity and, stabilize prices. Early moves include issuing two two-year Treasury bills worth Shs 170 billion and a Shs 100 billion 3-year bond offered in January, aggressive intervention in the forex market, and pulling the brakes on government expenditure.

Belt-tightening

As a sign of times ahead, in January the government collected Shs506 billion but spent only Shs 400 billion. It was the first time in three months that it was spending less than it collected. In November 2010, it collected Shs 347 in taxes but spent Shs 791 billion.

“Since the beginning of 2010/11, with the exception of August and November 2010, net government injections have underperformed relative to projected levels, which at times have resulted in tight liquidity conditions in the money market,” BoU said.

The combination of contractionary monetary policies, lower government expenditure, more costly and reduced commercial lending, intense tax collection, high food prices, and rising global crude oil prices mean that more Ugandans will this year be saying “money is scarce these days.”

John Mubazi, an economics expert at Makerere University says the local person is likely to feel the pinch further as the Uganda Revenue Authority (URA), in a bid to avoid a repeat of the Shs 29 billion half-year tax shortfall, tightens its noose on local industries.

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URA, which has a target of Shs 1.1 trillion for the third quarter (January to March), collected Shs2.46 trillion against a target of Shs2.49trillion.

Commissioner General Allen Kagina, says URA is stepping up its enforcement of tax compliance through “street by street mopping of Kampala roads to identify all non-registered rental taxpayers.” Areas in focus are the high-growth sectors like telecom, banking, and the informal sector.

February salaries for civil servants were late and Prof. Edward Kakonge, the Chairman of the Uganda Debt Network says the economy is already paying the price of undisciplined expenditure as the government fails to pay public servants on time. He warns that four months to close of the financial year 2010/11 economic growth will stall because there is no money, and unemployment will rise since the government cannot spend to spur the economy and create new jobs.

Bruno L. Yawe, an economics expert at the Department of Economic Theory and Analysis at Makerere University said the effects of government spending dearly in the 2011 elections “will manifest in limited or no infrastructural development, high cost of living, the vicious circle of poverty and damage that might take generations to solve.



The increasing fuel prices are pushing up food prices and costs of production. Food constitutes 27 percent of average household expenditure in Uganda and annual food crops inflation shot up for the first time this fiscal year from minus 4.6 percent in December to 1.5 percent in January.

Yawe warns that food related inflation would rise because “price increases on food do not wait for salary increment”. This therefore will increase the cost of living and reduce the standard of living.

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“The economy would at a particular point face a broke government, fail to pay salaries of civil servants, sell treasury bills which show that Bank of Uganda wants to mop up the excessive money in circulation and inflation due to the increase in fuel prices,” he said.

His colleague, Erias Hissali, says government service delivery could be crippled because there could be insufficient funds for running government departments.

He adds, however, the common person may not notice the effects of government spending expensively in the elections since complaints of poor service delivery, inefficiency, and work absenteeism have become common.

Hissali says some effects, like changes in the government’s spending, could only be estimated after a period; probably by May but Ugandans should pay attention to reports on inflation, any kind of government borrowing both internal and external, and changes in TB rates.

“Intermediate effects are raising interest rates on treasury bills to attract commercial banks and individuals,” he said.

Printing new money?

At the height of the government’s campaign splurge, donors and opposition politicians queried the source of the supplementary budget funding. Some alleged that the government was printing new currency, raiding the national foreign reserves, or depleting the Consolidated Fund account.

Hissali cited the consolidated funds, national reserves, new money and private funding such as membership as possible sources for the election money for the government.

“Foreign reserves are always protected and used as a last resort for emergencies. It is unlikely that elections and campaigns were an emergency,” he said.

In a recent interview, Finance Minister Syda Bbumba told *The Independent* that the supplementary budget was funded within the allocations in the 2010/2011 financial budget.

“It was just a change of priorities and the money had been pre-budgeted for incase something like this was to come up since the ministry always does budget allocations and reallocations,” she said.

Adam Mugume, BoU’s Director of Research also said no new money was printed or injected in the economy. He said, however, if the government used the foreign reserves, there are factors to consider.

“If the reserves were excessive, then it was good to reduce liquidity,” he said, “There are costs for keeping and borrowing foreign exchange. If the risk point of Uganda to borrow is high so as to meet the import requirement, it will be alarming.”

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BoU's Communications Director, Elliot Mwebya said, however, that the supplementary budget was funded by grants, non-tax revenue, and unspent balances on the Consolidated Fund. He said the government national reserves are intact. "The foreign exchange reserves currently stand at about USD2.4 billion and can support about five months of imports," he said.

According to the February monthly economic indicators by BoU, however, the foreign exchange reserves stood at US\$2.8 billion in December 2010. That means in January alone, they slid by US\$431 million (Approx. Shs 1 trillion). The BoU statement does not give the Forex reserves figure for January.

As the confusion over where the supplementary budgets money came from persists, Hissali says the source of money does not matter; only the effects of government campaign expenditure on the economy do. Assuming that new money was printed and injected in the economy during campaigns, there is a high possibility that the currency in circulation increased. Therefore, the surplus could trigger inflation.

"If there was any inflation, then it was in the rural where wads of notes were handed over to buy votes, but it is deflationary for civil servants whose salary payments were delayed," Mubazi said. The IMF projects a 5.5 percent rate of inflation for Uganda in 2011.

According to BOU update as at Mar. 4, annual headline inflation increased to 5.0 percent in January from 3.1 percent and 1.4 percent in December 2010 and November 2010 respectively. Annual core inflation also increased to 5.6 percent in Jan. from 4.8 percent and 2.9 percent respectively during the same period. Core inflation exceeded BOU target of 5.0 percent by 0.6 percent.

In addition, Uganda is one of the Heavily Indebted Poor Countries (HIPC) and donor, World Bank, and IMF support remains critical for budget and development projects. Withdrawal of support by the Dutch and IMF/World Bank could have far-reaching implications.