Domestic Resource Mobilization in Uganda

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Uganda's Growth Performance

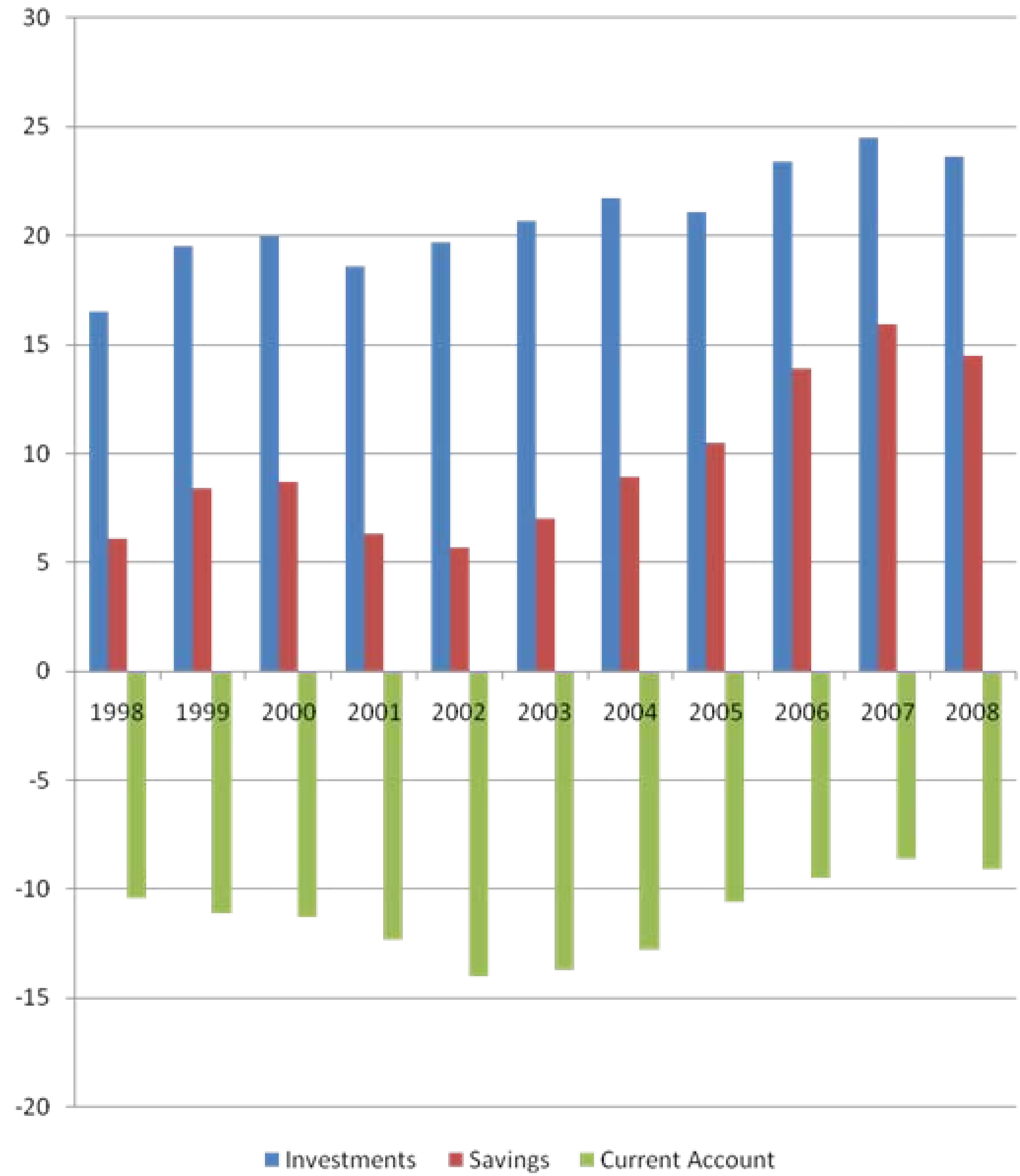
- The period 2000-2008 was very impressive. For example, estimates by the UBOS show that average GDP growth rate for the five years(2003/04-2007/2008) was as high as 7.9 per cent.
- Slow down due to the global economic crisis (7.2 percent)—but still very high.
- Growth mainly driven by services sector and agriculture has continued to shrink.

Despite Growth Savings Performance has been Poor

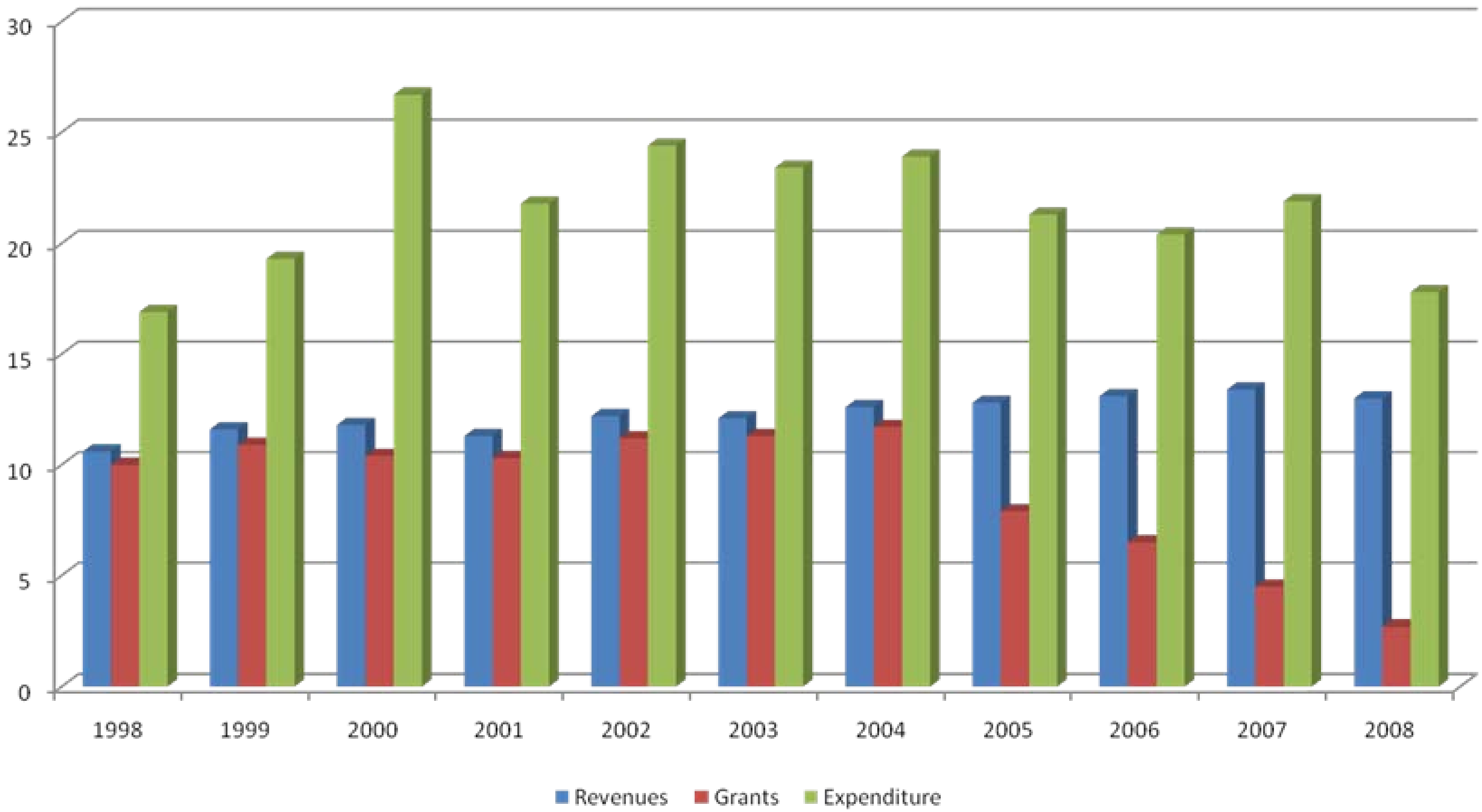
•Savings have been low over the years to finance the required investments

•This is partly reflected by the persistent Current Account Deficit

•While savings have been on the increase, they are way below the required investments.



Revenues Expenditures and Grants (percent of GDP)



Tax Performance and Problems

- Revenue performance has been very modest (increasing by about 0.2 percent of GDP)—a lot has already been done on tax administration.
- Tax handles remain few with a few commodities being overtaxed (especially excise duties).
- Largely the informal sector remains untaxed.

Constraints to Domestic Revenue Mobilization

- **Limited tax handles –**Abolition of trade taxes and over reliance on excise duties and domestic VAT.
- **Structure of Uganda's economy:** Uganda's low revenue performance has been attributed to the structure of the economy. Uganda has a significantly large agriculture sector, accounting for 21.4% of GDP in 2007/08.
- **Large informal sector** : Large informal sector is harder to tax.
- **Unregulated Small to Medium Enterprises (SMEs)** constitute 75% of all companies in Uganda.
- **Tax evasion and avoidance** remains a serious constraint to Uganda's ability to raise resources.
- **Tax incentives and holidays.** Incentives still remain and are largely arbitrarily given with no clear expiration and coverage (estimated at 2 percent of GDP).
- **Corruption** within the revenue authority is an impediment to collect revenue

Opportunities to Enhance Revenue Collection

- **Tapping on the informal sector**. The URA should make an effort of targeting businesses and commodities that are under-taxed. For instance, the VAT system has not been fully implemented at the retail stage. The bulk of this tax is collected on imports and large whole sellers and manufacturers. By registering all informal traders for VAT on the commodities they trade in, this would expand its coverage.
- **Streamlining of tax incentives:** Given the cost of tax incentives to the ability to collect taxes, the government should make an effort to streamline these incentives in its quest for attracting investors. This should be done by undertaking due diligence on the benefits and costs of the investments vis-à-vis the revenue foregone.
- **Implementation of the National Identity Card**: To identify the small informal businesses, it would require implementation of the National Identity where an individual or business (small or big) can easily be tracked.
- **Implementation of the presumptive taxes:** While this tax already exists, its implementation has been weak. Presumptive taxes would largely address the weaknesses associated with small enterprises not keeping financial records. The tax mainly relies on turnover.

Opportunities to Enhance Revenue Collection

- **Introduction of a Property Tax**: This tax should mainly be levied on residential and commercial properties. The tax is highly progressive and can be used to finance especially the local government development programs (Political economy of the tax being implemented)
- **Simplification of the Tax System**: Albeit education on tax system, there is need for further simplification. The number of tax disputes between URA and taxpayers are large. Harmonization of agencies on tax law.
- **Corruption**—exact amount revenue lost due to rent seeking, stealing, undervaluation is not known**.** (raising wages for revenue officers has no particularly worked).

Savings-Financial Markets Intermediation

	Private Credit/ GDP	Bank Deposits/ GDP	Loan/ Deposit Ratio	Overhead Costs/ total earnings
Uganda	7	19.6	42.1	7.9
Tanzania	6.8	22.2	40.9	7
Kenya	22.6	42.9	60.1	6.1
SSA	19.1	31.3	74.2	6.1
LICs	15.1	30.7	70	5.9

Constraints for the Financial Sector

- **Concentration of Banks:** Most banks still remain a preserve of the urban areas. In addition, they are largely dominated by a few banks, few large depositors and loans largely concentrated among the few borrowers. Without spreading banking to the rural areas, the ability to mobilize savings would still remain very limited.
- **Risk sharing of Banks across sectors:** Banks still mainly focus on lending to specific sectors due to their low risk tolerance. Agriculture which is a major sector in Uganda has had problems attracting bank financing given its risky nature.
- **The maturity structure.** Only 12 percent of total loans, 35 percent of loan volume, 17 percent of total deposits, and less than 0.4 percent of time deposits have a maturity of more than one year.
- **Range of products is a constraint.** Available financial products still very limited.
- **High Interest rate spreads explained by overhead costs, credit risk, and weak competition remains a major constraint.** Interest rate spread—is about 20 percentage points at present. Operating costs explain about 50 percent of the spread, and profits are the second largest component with 30 percent of the overall spread.
- **Risky borrowers** with no information to assess them (Credit reference bureau will partly address this problem.

Opportunities to enhance financial intermediation

- **Increase availability of development finance for investors in priority sectors of the economy.** The would entail recapitalization of Uganda Development Bank (UDB), as well as ensuring that systems and procedures are in place for proper functioning of these institutions.
- **Encourage opening of alternative sources of long term capital.** This would entail liberalizing of the pension sector and working on governance problems within the National Social Security Fund which currently is the largest pension fund for individuals working with private sector.
- **Strengthen the Credit Reference Bureau (CRB).** This will provide timely and accurate information on borrower’s debt profile and repayment history to enable lenders make informed decisions on the allocation of credit. This is expected to reduce the premium attached to risky borrowers.
- **Modernize the land and company registries as a means of hastening the process of extending credit.** The process of computerizing the land registry started in 2007.
- **Widening financial instruments for example mortgage financing to encourage collateralization of loans and mobilization of savings:** The current mortgage market is still very shallow and limited with the availability of long-term financing. Banks should venture into accessing long-term financing as a way of diversifying their products.

Other Emerging Issues

- National Development Plan projecting an increase of 0.5 percent of GDP of revenues during the period 2010-15.
- Potential impact of oil discoveries on DRM and the role of donors is not yet known (role will diminish).
- Status quo is that oil revenues will be cushioned for the huge infrastructure spending needs.