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Country Development Strategy Statement

~~FY 1985~~

FY 1984 Supplement

Uganda

March 1983

Agency for International Development
Washington, D.C. 20523

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UGANDA

COUNTRY DEVELOPMENT

STRATEGY STATEMENT

SUPPLEMENT

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USAID/UGANDA

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I. INTRODUCTION

Since the FY 1984 Country Development Strategy Statement: Uganda was prepared in early 1982, several key documents on the Ugandan economy have been completed. The most significant papers are Recovery Program 1982-84, Republic of Uganda, April 1982; Uganda: Country Economic Memorandum, World Bank, March 1982; Uganda: Agricultural Sector Assessment, AID, March 1982; and Uganda - Request for Stand-By Arrangement, IMF, July 1982. These documents and the convening of the Consultative Group meetings in May 1982, have afforded an opportunity to prepare a supplement to the FY 84 CDSS to help refine AID development strategy over the next three years.

Because this document is a supplement to the CDSS it does not include sections on the full range of topics required for a CDSS. Furthermore, this paper is prepared with the understanding that the decisions which were made on various program elements during the course of the CDSS review still stand and therefore need not be treated in this supplement. This paper concentrates on presentation of a review of the present status of the Ugandan economy and, combining the results with AID programatic emphases and constraints, offers a course of action for the AID assistance program over the next three years.

The data in Table 1 show that up to 1971-72 the Ugandan economy was performing moderately well when the economy went

Table 1. UGANDA: COUNTRY DATA[a]

Population	12.63 million (1980)	Area	236,000 sq km
Rate of Growth	2.6% (between 1969-1980)	Population Density	53.5 persons per sq. km.
		Pop Density less lake and swamp areas	65.0 persons per sq. km.
		GNP per capita in 1980	U.S. $280.00

GROSS NATIONAL PRODUCT IN 1980	US$ Million	%	ANNUAL RATE OF GROWTH (%, Constant Prices) 1967-71	1971-79	1980
GNP at Market Prices	3,536	100.0	4.4	-1.7	-8.1
Gross Domestic Investment	129	3.4	4.0	-13.0	21.9
Gross National Savings	-128	-3.8	3.8	-	-
Current Account Balance	-248	-7.0	-	-	-
Export of Goods, NFS	332	9.4	0.4	-10.6	-22.4
Import of Goods, NFS	572	16.2	-0.1	-7.5	18.0

	1960-70	1970-80
Average Annual Rate of Inflation	3%	30%

VALUED ADDED IN 1980 (at 1966 prices)[b/]	US$ Million	%
Agriculture	424	51.7
Industry	46	5.6
Services	350	42.7
TOTAL	820	100.0

GOVERNMENT FINANCE	Central Government (USh Million) 1980/81	(% of GDP) 1971/72	1980/81
Current Receipts	3,096	13.5	1.0
Current Expenditure	9,996	13.5	3.1
Current Surplus	-6,900	-	-2.1
Capital Expenditure	3,440	8.6	1.1

Source: World Bank, Uganda: Country Economic Memorandum (CEM), March 1982 and World Bank, World Development Report 1982.

a The data vary slightly depending on the source. Eastern Africa Country Profiles: Uganda (by L. Berry and E. Hughes, Clark University, 1980) places 1978 population at 12.78 million, growing at 3.3% which would be 13.64 million in 1980. The World Bank World Development Report 1982 credits Uganda with $300 per capita GNP.

into a decade of negative growth. Relative to other low-income African economies, before 1970, Uganda ranked among the highest in terms of international economic integration (exports were 26% of GDP in 1960); in terms of the relative shares of industry and manufacturing (12% and 9% of 1960 GDP respectively); and GDP growth (5.6% per annum between 1960 and 1970, third highest after Togo--8.5%--and Tanzania--6%).[1/] The current account tended to be in surplus and in 1970, for example, net reserves were equivalent to four months of imports. Between 1972 and 1980-81 the index of real income per capita fell from 100 to 55; annual inflation climbed from 5% to 110%.

This CDSS supplement consists of three sections: Economic Overview, Elements of the AID Assistance Strategy; and Program Aspects of the Strategy. The Economic Overview section describes the Ugandan economy as one with large, long-range economic potential and concludes that the main, immediate problem confronting the Ugandan economy is idle production capacity caused by severe disruptions under the former military regime and by the War of Liberation and sustained by the limited ability of Uganda to import necessary materials and parts to restore existing production capacity. The Economic Overview further notes that Uganda continues to implement broad economic policy reforms and is demonstrating consistent movement toward a market-oriented, outward-looking, mixed-economy system.

Based on the material in the Economic Overview, the second section calls for an AID program which will provide rapid disbursing assistance to rehabilitate small holder and small holder-related agriculture and to restore productive capacity of enterprises that provide inputs needed by rural Ugandans or that process agricultural output. The program calls for a total of $46 million in DA during 1983, 84 and 85. The $46 million constitutes a $10 million increase over the present planning level. Efforts by AID to encourage policy reform will concentrate on the sector level with particular emphasis on enlarging the participation of private entrepreneurs and farmer-controlled cooperatives on pricing agricultural inputs. AID will continue to monitor ongoing policy discussions between the Government of Uganda and the Multilateral Financing Institutions and AID will provide input when such action is judged to be constructive and productive. The Elements section also draws attention to the fact that the structure of Ugandan agriculture was essentially formed in the 1950's and 1960's but, because a large number of changes have occurred, there is a need to initiate a process (e.g., data gathering, analysis and planning) that will permit Uganda to restructure its agricultural production pattern and marketing to the economic conditions of the 1980's.

The last section outlines a program in which a majority of total AID assistance will be allocated to two major rehabilitation activities--provision of intermediate and final inputs to agriculture and enterprises serving agriculture, and rehabilitation of agricultural institutions. About one-seventh of the three-year budget will go to facilitating longer-term adjustment of the agriculture sector and preparation for activities after the rehabilitation phase is completed. It will not be necessary to change the size of the American direct-hire staff from the planned level of six persons.

II. ECONOMIC OVERVIEW

A. Recent Economic Performance

1. Sectoral Structure and Change

The data in Table 2 show the contribution of major sectors to GDP and trends over a fifteen year period. In 1980 agriculture was the largest source of GDP with a 46.3% share of which 20.1% of total GDP was monetary and 26.2% was subsistence agriculture. Government was the second largest sector with a 15% share followed by services and rents. There are no systematic data available on the distribution of employment and exports by sector but by 1980, agriculture was the source of employment for about 90% of the population and monetary agriculture provided over 97% of foreign exchange earnings. Agriculture accounts for about 60% of government revenue.

As opposed to the 1963-72 period when GDP was growing at an average rate of 4.8% per annum and the economic base was expanding, the Ugandan economy in 1980 had become more concentrated and there had been a shift from the monetary to the subsistence sector. Manufacturing and agricultural processing which had accounte. for 8.8% of GDP in 1972, comprised 4.3% of GDP in 1980. The deterioration of the Ugandan economy appears to have occurred in two stages. After peaking in 1972, GDP slowly declined (averaging minus .17% annually) until 1978 when output in all of the important sectors of the economy went

Table 2. GROSS DOMESTIC PRODUCT BY INDUSTRY
(in millions of shillings at 1966 prices)

Item	1965 GDP	1965 Share	1972 GDP	1972 Share	1978 GDP	1978 Share	1980 GDP	1980 Share	1980/1972
Monetary Economy	3939	68.1	5200	69.0	4333	60.3	3762	64.2	.72
Agriculture	1324	22.9	1680	22.3	1462	20.4	1177	20.1	0.70
Agro Processing [a]	85	1.5	95	1.3	39	.5	43	0.7	0.45
Manufacturing [b]	375	6.4	545	7.5	333	4.6	213	3.6	0.39
Other [c]	299	5.0	373	5.0	272	3.8	177	3.0	0.47
Commerce	779	13.5	806	10.7	646	9.0	527	9.0	0.65
Trasp & Comm	203	3.5	332	4.4	167	2.3	183	3.1	0.55
Government	345	6.0	627	8.3	800	11.1	882	15.1	1.41
Services [d]	319	5.5	502	6.7	262	3.6	278	4.8	0.55
Rents	212	3.7	240	3.2	352	4.9	282	4.8	1.18
Subsistence Production	1848	31.9	2342	31.0	2848	39.7	2094	35.8	0.89
Agriculture	1494	25.9	1886	25.0	2291	31.9	1535	26.2	0.81
Forestry, Fishing & Hunting	127	2.2	162	2.2	198	2.8	209	3.6	1.29
Construction	26	.4	32	0.4	40	0.6	12	0.2	0.38
Owner Occupied Dwellings	201	3.5	262	3.5	319	4.4	338	5.8	1.29
GDP at Factor Cost	5787		7542		7181		5856		0.78

Source: World Bank, Uganda: Country Economic Memorandum, Report No. 3773 - UG, March 31, 1982, Washington, DC, adapted from Table 2.2

a cotton ginning, coffee curing and sugar manufacture
b includes manufactured food products
c includes forestry, fishing, hunting, mining and quarrying, electricity and construction
d includes education, health, social and personal services and water supplies

into a sharp decline. Between 1972 and 1978, the monetary economy was declining by 2% annually but growth in subsistence production, at 3.4% per annum, was continuing to match approximately the growth in population. Average annual growth rates over the 1972-80 period, however, showed appreciably higher rates of decline: minus 2.8% for GDP, minus 7.6% for combined agro-processing and manufacturing, minus 3.5% for the monetary economy and minus 2.3% for subsistence agriculture. Part of the decline in subsistence agriculture can be attributed to drought.

The last column in Table 2 expresses 1980 GDP as a proportion of 1972 GDP and shows the incidence of decline by industry. By 1980 GDP was 78% of 1972 GDP. In 1980 productive, monetized industries were slightly over one-half of 1972 GDP, subsistence production was about nine-tenths of 1972 output and government had increased relative to 1972 by a factor of 1.4.

Gross investment--expressed as a ratio of GDP in average, per annum figures--was 12.7% in 1963-70, 8.6% between 1970-78 and 3% during the 1978-80 period. The national savings rate was 13.0%, 7.7% and 2.6%, respectively. Although estimates are not available it is clear that Uganda began a prolonged period of net dissaving as it began to consume its capital stock during the late 1970's. The data, while informative, does not fully reveal the magnitude of the disaster which has fallen on the Ugandan economy and people. A process of gradual, long-term capital consumption was accelerated by large-scale, systematic looting of farms, factories, schools, stocks and urban dwellings. The result was not just an economy with a badly depreciated capital stock, but one which by 1978 was virtually stripped of tools, parts ,stocks, equipment and breeding stock. The physical infrastructure was in a deteriorated or damaged state and key institutions such as universities and agriculture research facilities had lost virtually everything that was portable or consumable.

In summary, while the data are not comprehensive, they permit the formation of a basic idea of the structure and recent performance of the Ugandan economy. The Ugandan economy is predominantly agrarian with subsistence agriculture producing the single largest share of GDP but monetized agriculture also constitutes a significant share of GDP and is the predominant foreign exchange earner. There has been an eight-year period of economic decline in two stages: gradual decline from 1972 to 1978 and rapid decline between 1978 and 1980. The end result is a more concentrated economic base with an expansion in the relative size of subsistence production and government accompanied by a decline in the monetary economy including small but critical sectors such as agricultural processing and manufacturing.

2. External Sector

During the late 1960's and early 1970's, Uganda's principal merchandise exports were coffee (50-60% of total export earnings), cotton (16-20%), tea (4-7%) and copper (6-8%). By 1980 exchange earnings from the latter three items as well as from tobacco and manufactures had fallen virtually to zero. The merchandise export volume in 1980 was 36% of the 1972 level. Tourism, which ranked third as a foreign exchange earner, ceased to exist. Coffee constituted 98% of total export earnings in 1981. 2/

In 1981 almost 80% of Uganda's merchandise export earnings went to purchase petroleum and government imports.3/ The volume of petroleum imports had remained relatively constant, but because the foreign exchange cost of petroleum had risen 168% over the last three years, 30% of the total import bill went to cover petroleum supplies. In 1980 direct government imports (defense, security and administration) were $100 million, down from $185 million in 1977 when these imports constituted 44% of the total import bill. Direct government imports were estimated to be $60 million in 1981.

In addition to the chronic decline and concentration of Ugandan exports in coffee, the terms of trade fell 51% between 1979 and 1981.4/ This decline is attributed to the increase in petroleum prices and associated transportation costs and the decline in coffee prices. Between 1979 and 1981 the decline in coffee exports leveled off at about 110 to 120,000 tons per year. Uganda exported 150,000 tons of coffee in the 1982 season, fully meeting its ICO quota.

Table 3 below provides a summary of Uganda's trade and payments positions over a 13 year period. The increase in projected export earnings is based on anticipated increases in coffee and noncoffee exports, particularly cotton. 5/

Table 3 BALANCE OF PAYMENTS

(in millions of dollars)

	1970	1980	1982/83
Merchandise exports f.o.b.	261.6	319.1	365
Merchandise imports c.i.f.	-204.9	-503.7	-592
Trade Balance	56.7	-184.6	-227
Services (net)	-43.4	- 62.9	-116
Unrequitted transfers			129
Current Account Balance	13.3	-247.5	-214
Official flows (net)	28.3	168.8	167
Private (net)	-36.8	-123.4	12
IMF credit		26.4	
Capital Account Balance (net)	- 8.5	71.8	179
Overall Balance of Payments	4.8	-175.7	- 35

Sources: World Bank, Uganda: Country Economic Memorandum, March 1982. Adapted from Table 2.2 IMF, Uganda- "Request for Standy-By Arrangement," July 1982.

a. IMF projections

b. For IMF data, "private" includes net errors and omissions.

Between 1970 and 1980 the overall balance of payments was negative seven out of ten years with increasingly severe deficits occurring in 1978, 1979 and 1980. The greater proportion of the deficits was covered by involuntary loans (accumulation of arrears) and, in 1978 and 1980, by drawing down reserves. By 1980 and 1981, debt cancellation or rescheduling, increased official inflows and IMF credits were used to finance the international payments deficit. 6/

The Ugandan debt service ratio for 1981, including IMF credit, is estimated by the World Bank to be 50% and about 42% according to the IMF. Between 1982 and 1990 the debt service ratio, including IMF credits, is projected to average about 41%.7/

By the end of the War of Liberation in 1979, the Ugandan economy was in an extremely difficult economic and financial trap. Given the country's debt arrearages it was virtually impossible to obtain the goods and services necessary to maintain monetary production and thereby earn foreign exchange to pay overdue international debts. Productive investment was not feasible because of the existence of pervasive price controls, large budget deficits, an extremely overvalued exchange rate and a high inflation rate. In June 1981, the first steps were taken by the Ugandan government in concert with the IMF to address the most serious policy problems and the IMF provided funds through a Stand-by Agreement to assist the economy during the transition period. The Ugandan shilling was devalued from 7.8 to 78 to the dollar; producer prices for main export crops were increased by four to six times their previous levels; most price controls were removed; reforms were made in taxes; ceilings were placed on the budget deficit and on the rate of growth in the money supply; and interest rates were raised. [8/] The objective of the program was to stabilize the economy and start to reestablish conditions which would revive productive economic activity and initiate investment in economic rehabilitation.

The stabilization and recovery of the Ugandan economy are critically dependent on the level of foreign exchange available to the economy. Since over four-fifths of Uganda's foreign exchange earnings are allocated to cover the costs of basic imports, for an interim period Uganda will be heavily dependent on external assistance to obtain the inputs necessary for rehabilitation of the economy. Because of standing demands on foreign exchange earnings, the structure of Uganda's external debt and the time required to restore production, Uganda's balance of payments will be in a state of crises for the next three years.[9/] The crisis period will be prolonged if Uganda cannot obtain the inputs to rehabilitate its production capability and thereby increase foreign exchange earnings or saving activities. According to World Bank estimates, a financing gap averaging $180 million annually will persist for the next few years. 10/ There are obviously other important elements involved in Uganda's economic recovery; however, foreign exchange availability will remain a critical constant over the next few years.

3. Government Finance

Because of a major movement of economic activities into "magendo" markets (unofficial and unrecorded transactions) and into smuggling and declining monetary production the data on public finance essentially reflects the shrinking of the government sector as an economic agent. 11/ In 1972 central government recurrent expenditure was equal to current revenue; the expenditure to revenue ratio was 1.4 by 1980, 4.0 in 1981 but dropped to 0.9 in 1982. 12/ The problem of high government expenditure in 1980 and 1981 was compounded by the fact that a large proportion of it was for non-productive purposes. Public administration--including large amounts for foreign travel--and defense accounted for more than 50% of expenditure in 1981.

Because the large central government deficits were financed by borrowing from the Bank of Uganda, the money supply doubled between 1979-1981. The IMF estimates that the inflation rate during this 1979-1981 period was about 100% per year.

With the series of reforms in 1981, government revenues increased eightfold while expenditure increased by about two and one-third times. 13/ There is now an effort to reduce both the budget deficit and the share of the deficit financed by government borrowing from the Bank of Uganda. The budget deficit was 76% of government expenditure in 1980-81. The deficit declined to 36% in the 1981-82 period and it is anticipated that the deficit will be about 21% in 1982-83. The share financed by the Bank of Uganda was equivalent to about 50% of the money supply at the end of FY 81 but the share is estimated to be about 5% in 1982-83. Total net domestic credit expanded by 95% in FY 81 but the rate of credit expansion is expected to decline to 33% for FY 82. 14/ The changes between FY 81 and FY 82 suggest that there is a deliberate and concerted policy to reestablish economic equilibrium.

Interest rates have been increased since 1981 but the particular circumstances which have existed in Uganda have tended to diminish their significance. In June, 1981 commercial banks were offering 5% on savings deposits; in July, 1982 the rate was increased to 9%. Time and savings deposits increased by 60% during the year ending June 30, 1982. Lending rates in June, 1981 for agriculture were 8.6% and 12% for export and manufacturing, commerce and unsecured loans. By June, 1982 lending rates were increased to 15% for agriculture and for export and manufacturing; 16% for commerce; and 17% for unsecured loans. In November, 1982 lending rates for commerce and for unsecured loans were increased to 20%.

For the present time the interest rate is not important as a device to ration funds because of prevailing excess liquidity in the economy. At one point last year banks had stopped accepting deposits because of their liquidity positions. The IMF reports that excess liquidity is gradually being absorbed and the opening of the second window is certain to accelerate the process. It is speculated that the predominant investment determinants now are the relative availability of investment opportunities and the level of investor confidence. As investment opportunities and investor confidence increases and liquidity declines, interest rates will resume their traditional function. The IMF has indicated that the adequacy of the interest rate structure will be appraised in 1983. For now interest rates are not an issue.

B. Economic Potential: Agriculture and Industry

Based on its natural resource endowment, its accumulation of social and physical infrastructure and economic performance up to the early 1970's, there is little doubt that Uganda has major economic potential. Ugandan economic potential may rank first among the other countries of sub-Saharan Africa. It has favorable climatic and soil conditions which combine to form a highly productive and varied agricultural base. By 1972, the industrial sector was able to supply significant amounts of basic inputs, consumer goods and some exports (textiles). Uganda's road network was one of the best in Africa and the country was linked by two rail routes to the sea. For its size Uganda has perhaps the largest hydroelectric potential in the world. Prior to the early 1970's Uganda's school system at all levels had a reputation for high quality.

Ugandan economic potential has been hampered by two factors: strong ethnic differences and the fact that the country is landlocked. Today, a third factor is the damaged condition of the social and physical infrastructure. 15/ The significance of the damage and the resilience of the system are the critical questions over the next few years. Given the government's willingness to institute a series of policy reforms, however, it is reasonable to expect that the damage factor will not become a long-term problem inhibiting Ugandan economic growth.

Agriculture has been the engine of growth in Uganda. Given the soil, abundant water resources and varied growing conditions, agricultural potential is robust. There are no significant natural constraints to achieving large gains in output or in productivity.

For any economy it can be difficult to sustain growth in agriculture over the long-term unless there is scope to diversify production. Ugandan agriculture, in spite of its present concentration on coffee exports, is already highly diversified and a wide variety of crops can be grown within virtually all of the major crop categories. 16/

The diversified nature of Ugandan agriculture does not emanate from several specialized subsectors but from typically highly diversified farming operations throughout the country. The Agricultural Sector Assessment observes that "most peasant farmers will grow at least a dozen crops with a considerable amount of interplanting and keep from one to five varieties of livestock." (p. 3). The economic significance of diversification at the farm level is that it provides substantial income stability and it is firm evidence that the farmer is both technically versatile and sensitive to alternative earning opportunities.

Eighteen percent of Uganda is covered by lakes. 17/ The Uganda Agricultural Sector Assessment notes that "the potential for increasing the (fish) catch is tremendous. 18/ Livestock are found throughout the country and Uganda has a substantial dairy industry.

To provide some insight into Uganda's overall economic potential, it is also useful to look briefly at the industrial sector, i.e., manufacturing and agro-processing. In 1972, when aggregate industrial output was at its peak, the sector produced 8.5% of GDP, the result of a respectable 6% average annual rate of growth during the late 1960's. Ugandan industry made a significant contribution to meeting domestic demand in a variety of areas including basic consumer goods, wood products, building materials, engineering goods (including iron and steel production, rolling mill and fabrication of iron, steel and non-ferrous parts), fertilizers and chemicals. There was a substantial amount of vertical integration of industry not only in agricultural processing but in activities such as metal processing. Ugandan industry also exported textiles to neighboring countries. Blister copper was an important mineral export. Uganda has appreciable industrial potential because of the country's diverse agriculture production, a moderate supply of mineral resources (iron, copper, phosphates), the remains of the pre-1970 industrial base and the availability of hydroelectric power. There have been major changes in the international and Ugandan economies since industrial output peaked in 1972 but the fundamental potential for industrial development remains.

C. Policy: Changes, Remaining Issues and Ugandan Economic Priorities

To help form an idea of the kind of AID program best suited to Uganda and to make a judgment on the degree of confidence in achieving country program goals, it is useful to review the Ugandan economic policy climate and to consider the direction and rate of policy change. The first notable change after the War of Liberation was an increase in producer prices for coffee and cotton in 1979; however, the adjustment was insignificant because no measures were taken to address basic macroeconomic problems such as the high inflation rate or the overvalued shilling. Indeed, the interim administrations injected UShs 4.4 billion into the economy over an eight month period during 1979 and 1980.[19/]

The first significant policy measures were instituted in June, 1981. The Ugandan shilling was devalued by 100%, producer prices for traditional export crops were increased by 400 to 600%, between April and October of 1982, petroleum retail prices were increased by about 1000% (over 1000% for gasoline and about 700% for diesel and kerosene); most price controls were removed and taxes, money creation and interest rate policies were revamped. [20/] In addition, the Government of Uganda announced its intentions to turn some parastatals back to the private sector, place parastatal operations on a more market-oriented basis and to develop a mixed economy working in "open and free market" conditions. [21/] The government announced its intention to revise the Foreign Investment Act to provide foreign investors with a series of tax incentives and measures to protect their investment (e.g., profit repatriation; and dividend, interest and debt payments in foreign currencies). A bill to compensate or restore ownership of property to Asians was passed and entered into force in February, 1983.

Several serious problems remained after the 1982 reforms. In early 1982 some of the problems were:

1. The Ugandan shilling was still overvalued by a rate of about 3.6:1;

2. Foreign exchange was allocated administratively, under extreme pressure and with ill-prepared administrative machinery;

3. The budgetary process was based on projected expenditures which were not closely related to the likely availability of funds;

4. Expenditure control was weak;

5. The investment plan was overly optimistic in its assumptions about future economic performance and availability of investment resources;

6. Adequate statistics were not available to serve as a basis for well-informed decision making;

7. Powerful and essentially unproductive parastatals continued to exist;

8. Official producer prices for coffee, tobacco and cotton provided lower returns than food production and the tea price did not cover production costs. 22/

In mid-1982 the IMF determined that the Government of Uganda had satisfied all of the 1981-82 program performance criteria. The GOU requested and received another stand-by arrangement for 1982-83. By mid-1982 most of the problems noted above were already starting to be addressed. In June the government increased producer prices for coffee, cotton, tobacco and tea between 33 and 100%. Consumer petroleum product prices were increased 41% in June and raised again by 25% in November. 23/ In June President Obote announced the government's intention to establish a dual exchange rate (a "second window") and to reform government expenditure practices. (Between mid-1981 and mid-1982 the official exchange rate had been allowed to depreciate about 12%). In April, 1982 the Ugandan Government approved and adopted a new plan, Recovery Programme 1982-84, as a "blueprint for the economy." 24/

The June and November price adjustments are beneficial, but the opening of the second window, more rigorous expenditure control and the contents of the Recovery Programme constitute significant responses to the problems listed above. The second window consists of a weekly auction of two million dollars which opened August 23, 1982. In addition to private importers some government entities are required to obtain their foreign exchange through the second window. There are no restrictions on items to be imported although precautions are taken to prevent capital flight. In the first auction 19 out of 28 bids were accepted and a rate of 300 Uganda shillings to the dollar was established, but the full allocation was not exhausted. In subsequent auctions the full $2 million has been sold. While a significant part of initial purchases were for travel, education and medical expenses, most funds are now used to import consumer goods, raw materials and spare parts. The rate has appreciated to UShs 230:$1. Foreign exchange is purchased at the second window "with no questions asked," and the amount of foreign currency surrendered far exceeded the GOU's expectation. 25/

The GOU has made a number of administrative changes to improve the operation of the second window. It has directed that import licenses be issued within five days and has abolished the 1% import license charge by the Board of Trade and the 5% predeposit requirement. An increasing number of items can only be procured through the second window; recently tires and vehicle spare parts were shifted to window two. Import duties have been lowered. Also, the practice of granting import licenses to importers with their own foreign exchange has been abolished.

The dual rate system is temporary. The GOU plans to unify the exchange rates before mid-1984 and Uganda will have established a market-based exchange rate system. The opening of the second window addresses two of the problems noted above. It effectively devalues the shilling and within a limit it lets importers, not the government, determine the allocation of foreign exchange for imports.

A range of measures have been initiated to control and to restrain growth in government expenditure and improve budgetary performance. However, given the country's weak administrative capacity this continues to be a major problem. One example of the GOU's determination to control expenditures is the reduction in monthly cash allowances for ministries that do not maintain a timely flow of expenditure data.

Another example was the government's decision to hold wage and salary increases to only 25%. It has taken measures to improve the structure of the tax system and tax administration. Collection of tax arrears and current collections are up significantly. Support for parastatals is subject to closer scrutiny and the conditions for support are being placed on a more formal basis through the development of standard agreements covering repayment of principal, interest rate, dividend policy, etc.

The Recovery Programme 1982-84 provides a balance of payments and budget analysis, a resource allocation plan based on the analysis and a reaffirmation of the GOU's commitment to improve the institutional environment for agriculture. The Recovery Programme document, prepared and approved by the GOU, concentrates on resuscitating existing productive capacity over the next two years. The rehabilitation program itself is directed toward foreign exchange earning activities. The pattern of economic priorities is evident in the document's list of project criteria. The criteria are: 26/

(a) projects which promise rapid earnings of foreign exchange through increased exports or savings of foreign exchange through judicious import substitution;

(b) projects which will quickly stimulate industrial and agricultural production, particularly those which promote self-sufficiency in food;

(c) projects which have a positive or at least minimal impact on the government's recurrent budget;

(d) new projects which must be started to sustain and enhance economic recovery and growth; and

(e) projects of an urgent humanitarian and social character.

Table 4 below shows the allocation of investment by sector over the planning period and the total size of the program.

Table 4. ALLOCATION OF INVESTMENT BY SECTOR (millions of dollars) a/

Sector	82/83	83/84	84/85	Total	Share (%)
Agriculture	78.9	81.1	60.0	220.0	30
Industry & Tourism	62.2	96.0	53.3	211.5	29
Minerals & Energy	15.8	17.0	8.6	41.4	5
Transport & Communication	40.7	68.3	46.0	155.0	21
Social Infrastructure	42.5	54.0	12.1	108.6	15
TOTAL	240.1	316.4	180.0	736.5	100

a. Cost estimates are in 1982 prices.

Source: Government of Uganda, Recovery Program 1982-84, April 1982, p. 14.

The balance of payments analysis in the plan is an improvement over earlier plans; however, the Recovery Programme analysis, relative to World Bank estimates, assumes higher export levels, a lower invisibles deficit, a higher level of IMF credit and it excludes direct government imports. Nevertheless, the balance of payments projections in the Recovery Programme are viewed as "a viable macro framework" because the level of additional external financing necessary to implement the proposed program is within the range of external requirements made in World Bank projections. Approximately 80% of the $736 million total requirement over the three year period is foreign exchange.[27/]

Within agriculture, investment priority will be placed on rehabilitating production of traditional export crops (coffee, cotton, tobacco and tea). Planned activities include increasing the supply of inputs and implements, restoration of processing capacity, improvement in transport and collection services and strengthening of extension services. In livestock, the primary emphasis is on disease control plus restocking of cattle and poultry.

With respect to improving the institutional environment for agriculture marketing agencies the Recovery Programme contains the following proposals. [28/]

1. Auditing accounts for recent years and introducing sound accounting procedures.

2. Instituting effective cost controls linked to the volume of produce handled and the marketing services performed.

3. Reducing the size and operating costs of the Lint Marketing Board. This will include the handing back of edible oil and soap factories to the private sector.

4. Carrying out a study of the export marketing of coffee. This will consider alternative selling arrangements such as auctions and investigate the economic viability of the central coffee processing and storage unit and the scope for improving the quality of coffee from the rural processing factories as an alternative to reprocessing.

5. Reorganizing and streamlining the parastatals serving the tea industry.

The Recovery Programme also states the intention to strengthen agricultural extension services' abilities to provide technical assistance to farmers. Extension staff will be equipped with demonstration materials, given refresher courses and will work together with foreign agricultural advisors.

Agricultural pricing policy will take into account the relative prices of farm products and the price of the collection of consumer goods and inputs purchased by farmers. The Programme further states that there will be systematic adjustments in export crop prices to reflect world market trends and currency fluctuations.

An Agriculture Secretariat recently has been established to coordinate agricultural policy and programs among the diverse ministries that influence production and marketing. The Secretariat will include experts provided by the World Bank. A principal task of the Secretariat is to make agriculture price recommendations based on analyses of farmer production costs, opportunity costs and other prime factors.

Production of consumer goods oriented toward farmers is emphasized in the industrial rehabilitation program and the Recovery Programme calls for conversion of industries from oil to electrical power in recognition of Uganda's high petroleum import bill. The Recovery Programme states that resources will be allocated to regenerate industry on a selective basis. Priority will be given to: 29/

1. The rehabilitation of agro-based industries for processing coffee, cotton, tea, sugar and others.

2. Import substitution industries in the production of:

   a) agricultural inputs such as hoes, fertilizers, insecticides, gunny bags and packaging materials.

   b) the production of essential consumer goods, e.g., sugar, salt, soap, scholastic materials, textiles, footwear, pharmaceuticals.

3. Construction materials industries; such as cement, steel, wood, clay, paint, nails and quarry products.

4. Industries with great impact on government revenue earnings, e.g., beer, tobacco, soft drinks and spirits.

There are no broad economic policy issues still remaining that impinge directly on AID country program concerns that are not being addressed by the GOU. It is crucial that Uganda continue to refine its sectoral policies in line with the broad macroeconomic reforms and that progress be made in improving administrative capabilities. These concerns, however, are not significant policy issues per se. Some specific policy problems do remain, however, concerning the existence of official prices for coffee, cotton, tea and tobacco, the future role of the crop marketing boards and possible impediments to growth of rural, private traders.

The setting of producer prices administratively for Ugandan traditional export crops remains a concern even though export crop prices are to be linked to international prices and systematically reviewed. With the notable exception of coffee, there does not appear to be any discussion of eliminating administered prices altogether. The idea of auctioning coffee is being considered. It is also significant that the Agriculture Secretariat is not restricted in the recommendations it can make. This means the entire set of agriculture prices and price policies are subject to change. Because price policy is such a critical area, the operation of the system will be monitored.

The questions concerning the Coffee and Lint Marketing Boards are closely related to the issue of administered producer prices.

There is broad agreement that these boards, which control the marketing of coffee and cotton, do not provide essential services whereas they add to total costs. Again, given the plans to overhaul the Lint Marketing Board, and the proposals for the Coffee Marketing Board (items 3 and 4 above), there appears to be movement toward a much more efficient arrangement. 30/

The AID country program may not concentrate specifically on assisting in production of traditional crops but these crops are important to most Ugandan farmers and the economics of these commodities interact with other efforts directly supported by AID. Obviously Uganda is in a time of major policy change. Both administrative pricing and marketing boards are being reviewed by the GOU and the World Bank. It is not necessary for AID to become actively engaged in policy discussions in these areas now; however, they both warrant close monitoring.

The issues of restraints on entry of private traders into rural commerce and pricing of agriculture inputs are more immediately relevant to AID concerns. The government no longer restricts or controls movement of goods by private traders among districts. But, to engage in commerce, traders are required to be licensed by district-level authorities. The district authorities frequently have close links to district unions and/or established and powerful private enterprises which conduct business with farmers. Thus there are circumstances in which district authorities may be reluctant to allow entry of new competitors. A competitive rural distribution system is important because it enhances efficiency and because a competitive industry tends to pass on cost savings and input price reductions while paying higher prices for farmers' products. Although there is no systematic evidence that there is widespread restraint on entry of new enterprises, the conditions are such that the issue will receive close attention as the AID program is implemented.

Input pricing policy has been a problem because the government has tended to set the prices of some agricultural inputs and tools below the market clearing price. Hoes, one of the basic agricultural tools, are a case in point. The existence of the difference between the official price (ex factory) and the higher price which can be obtained in the market, creates an incentive to divert supplies from their scheduled distribution, e.g., through the cooperative system to farmers, and sell them privately at the market price. This activity is not particularly adverse in terms of the economy as a whole so long as farmers obtain the inputs, but the subsidy is not passed on to the intended recipients. The major economic problem of underpricing the tools is that there is frequently an incentive to export the implements to neighboring countries thus thwarting the entire effort. This problem is compounded by the dumping of hoes by foreign manufacturers or the provision of hoes on a grant basis by foreign donors, with the government passing the hoes on as a grant to farmers. There have been some upward adjustments in input prices over the last year but there remains a need to establish a policy which links the price of inputs provided under grant assistance to their real c i.f. import prices. AID is following up on this problem with the government, other donors and domestic hoe manufacturers.

Security is and will remain an issue in Uganda for some time. "Security" is an euphemism for referring to a situation in Uganda involving threats, coercion or actual destruction of lives and property. Insecurity is a more descriptive term. The degree of insecurity has varied from a state bordering on anarchy in the spring of 1979, to a more stable condition in which violence or the imminent threat of violence are relatively infrequent and not commonplace. Insecurity is related to economic performance by impeding economic transactions and discouraging investments. Thus insecurity can exert a powerful negative effect on rehabilitation efforts and economic performance. Because of the nature of the problem, systematic information is not available; however, it was indicated in the FY 1984 CDSS, based in part on travel experiences through most of Uganda by the CDSS team, that the security situation has improved appreciably over the last year and that most of the countryside is peaceful. It is not feasible to forecast the future. The process of setting out a three-year assistance program requires an assumption about security over the next three years. The assumption in this strategy is that the trend of decreasing insecurity established over the last year will continue. In addition to the general evidence of declining insecurity in support of the assumption, it is noteworthy that: (a) the large-scale and rapid movement by the government toward economic liberalization of the economy is evidence of the government's interest in increasing stability in general; and (b) the U.S. is an important bilateral donor in Uganda both with respect to Uganda and to other donors, and therefore, because of its strong presence in Uganda, will encourage further improvement in the security situation.

D. Summary and Conclusions

Up to 1971 Uganda was one of the most economically advanced countries in sub-Saharan Africa. But after almost a decade of decline the Ugandan economy was mired in a classic state of economic crisis and stagnation. The economy was characterized by high inflation, large international debts, a highly overvalued exchange rate, a decimated modern sector and a heavy burden of economic regulation and state control.

Since 1981, however, major policy reforms have been introduced to stabilize the economy, to reduce the degree of government economic involvement and to initiate an economic recovery program. The structural makeup of the Ugandan economy is unusually diversified for a country with an annual per capita income of $280. About two-thirds of GDP is produced in the monetary sector (in 1980) and one-third is subsistence production. Uganda is predominately an agrarian economy and society where agriculture accounts for 46% of GDP with subsistence agriculture producing 26%; the agriculture sector produces over 95% of exports; and 85 to 90% of the population lives in rural areas. The external sector is characterized by a new, dual exchange rate system, a significant foreign exchange constraint, a heavy demand on foreign exchange earnings to pay for necessary commodity imports (e.g., petroleum) and debts, while merchandise exports consist almost exclusively of coffee. The economy is critically dependent on official inflows to provide the equipment, spare parts and commodities necessary to restore the productive capacity necessary to maintain and eventually increase export levels.

Because of a favorable natural resource endowment and industrious and market-conscious farmers, Uganda has a high potential in diversified agriculture. The country also has substantial industrial potential. Uganda is in the midst of a widespread economic policy overhaul in which pervasive government economic regulations, control mechanisms and ownership are being dismantled in a major policy shift to a market-oriented, mixed economy. The full range of macroeconomic policies are being adjusted to stabilize the economy and to complement the shift. The exchange rate is being put on a market basis; monetary and fiscal policies have been drastically altered. The central government budget is being brought under control as is demonstrated by the ratio of recurrent expenditure to recurrent revenue which has declined from 1.4 to .9 between 1980 and 1982. Central Bank financing of the budget deficit has declined from 50% of the money supply in 1981-82 to a projected 5% in 1982-83 thereby drastically reducing growth in the money supply. A rational economic recovery plan has been adopted which stresses rehabilitation of agricultural export production and processing capacity.

The preceding examination of the Ugandan economy yields the following conclusions:

1. The Ugandan economic resource endowment--natural, human and institutional--and Uganda's pre-1972 economic performance, taken together, indicate that Uganda possesses the economic potential to attain readily and to maintain a high rate of economic growth and development.

2. The Ugandan economy has moved from chaos to a stable condition while the entire economic policy framework--fundamental, macroeconomic and sectoral--is being dismantled and rebuilt.

3. Ugandan economic strategy is based on an outward-looking, market-oriented, mixed-economy model which seeks to utilize those domestic resources which are in most abundant supply.

4. Foreign exchange is the critical element needed to fuel economic recovery and thereby allow the economy to generate the additional foreign exchange to pay its large external debt obligations while continuing to recover. The Ugandan economy can productively utilize the amount of resources called for in the government's economic plan.

Based on the preceding points it is concluded that with respect to the AID country program, Uganda strongly warrants the maximum possible increase in development assistance in the shortest possible time. Recognizing the unique situation, i.e., rapid rehabilitation of production capacity over a short time period, it is necessary that development assistance be in a form which is tailored as closely as possible to respond to the situation. Finally, it is abundantly clear that AID assistance be directed to rehabilitating agricultural production--including agro-processing--in activities which will increase foreign exchange earnings or savings.

III. ELEMENTS OF THE AID ASSISTANCE STRATEGY

A. Introduction

Section II of this CDSS supplement described the Ugandan economy. In the process of examining the macro-economic aspects and the changing policy environment, Section II also indicated the general direction for the AID program to follow. One purpose of this section is to develop the recommendations from Section II by incorporating other general guidance and constraints which impinge on an AID program. A second purpose is to provide a sense of proportion and indicate what can be expected from the AID program in Uganda. A third purpose is to outline how the AID program in Uganda will address the Agency's priorities of policy reform, private sector development, technology transfer and research, and institutional development.

B. Assistance Level and Rationale

The annual level of AID assistance to Uganda is a prime element in the design of the country strategy. In the review of the *FY 1984 CDSS* AID concluded that the FY 83 funding level for Uganda should be increased from \$5.5 million to at least \$10 million as a base from which the program would grow if budget levels permitted (State 100928, April 15, 1982). The premise for this strategy supplement is that the annual assistance levels contained in Table 4 of the *FY 1984 ABS* will essentially be shifted back one year such that the

FY 83 level will be $12 million; the FY 84 level will be $15 million and the budget will be $19 million in FY 1985, for a total of $46 million over the three-year period. This constitutes a $10 million increase over the complete plan period from the projections contained in the FY 1984 ABS.

To provide some perspective on the planned AID assistance budget relative to aggregate levels and to other donor levels, the projected balance of payments financing gap (average) for each of the three coming years is $180 million. 31/ The World Bank began disbursement of $95 million for rehabilitation in 1981-82 and recently committed an additional $207 million for a combination of industrial, agricultural, education and general rehabilitation purposes. The European Community (EC) will be committing approximately $100 million over the Recovery Programme period. It is not possible to say with precision where the United States will rank among bilateral donors in 1983 but it is plausible that, with a DA level of $12 million in FY 1983, the United States will be one of the larger donors, perhaps along with the Saudi Fund, the African Development Bank and the European Development Fund if these institutions continue their 1982 commitment levels of approximately $15 million each. 32/ The UK, FRG, Italy, France, Australia, and Canada each are committing annually between $3-10 million.

With an average annual budget of $15 million AID will pursue three overall objectives in Uganda: (1) help relieve the pressing foreign exchange constraint; (2) contribute to rehabilitation of productive capacity; and (3) maintain an active role in the continuing process of policy change. In the pursuit of these three objectives AID is only one of several donor participants and the objectives cannot be achieved by AID alone. The relative level of assistance is not directly proportional to the degree of contribution to the three objectives: there tends to be a directly proportional relationship between the budget level and relief of the short-term foreign exchange constraint. However, for the second objective, the contribution can be more or less depending on the promptness and quality of the AID program. The role of AID in the policy process is disproportionately greater because the United States is a repository of large amounts of technical expertise and because of the international position of the United States.

There are several reasons why the cumulative $10 million increase is warranted. These include the following:

1. Uganda has the human and natural resources which, if complemented by the incremental financial resources, can yield steady, long-term growth;

2. Uganda has already implemented sweeping policy reforms and is continuing the process. The fundamental policy reforms which constitute the necessary conditions for economic growth have been instituted. Additional funds are important to reinforce the government's commitment to the reform effort.

3. Uganda, because of its current economic status which is characterized by under-utilized plant and farm capacity can rapidly and productively absorb additional foreign exchange resources;

4. It is important for the United States to demonstrate in material terms that it is responsive to African countries which make major moves toward a market-oriented economic model and which cooperate with multilateral institutions;

5. Uganda, in concert with the international donor community, can demonstrate to other African countries what sound, market-oriented economic policies can accomplish;

6. Uganda clearly has the potential to become a regional growth center and efficient supplier of agricultural products and basic manufactures to neighboring countries thereby providing an impetus to economic growth for the entire region.

C. Local Currency Programming

The three-year program will generate a substantial amount of Ugandan shillings. The guiding principle for local currency programming will be that the financial resources be used to support, as directly as possible, the AID effort to rehabilitate small holder agriculture and to assist activities closely related to agriculture. The emphasis on agriculture should be acceptable to the GOU since Ugandan officials have been consistently receptive to this emphasis in discussions on the subject.

Assuming that growth in money supply will be maintained within the bounds set out in IMF-GOU agreements, local currency generations will be directed to the following areas:[33/]

1. Rural Credit - There is a large potential demand by farmers and by primary cooperative societies for tools and other purchased inputs. Making credit available to farmers would facilitate the AID effort to provide agriculture inputs. AID initiated a successful small farmer credit scheme in the 1960's, and the GOU is eager to reactivate it. 34/

2. Reconstructions and Repair - There is a substantial need for local currency to pay for reconstruction and repair work on educational and research facilities in the agricultural sector. Uganda has seventeen district farm institutes, two agricultural colleges and one cooperative college, all in need of physical rehabilitation. This non-recurrent expenditure will directly complement the AID effort to rehabilitate agricultural institutions.

3. Rebuild Inventories - Agricultural institutions do not have the stocks of spare parts and consumables which are necessary to allow full-scale operation. Much of these materials can be obtained locally. Again, this type of shilling expenditure will directly support the AID effort to rehabilitate agricultural institutions.

4. Agriculture Reassessment - There will be substantial local costs associated with AID efforts to develop alternative crops and production methods and to collect and analyze data for decision-making.

D. Equitable Growth

The promotion of equitable growth is a basic tenant of AID assistance policy. That is, to the maximum extent feasible, AID assistance is designed to reach the maximum number of participants who cannot otherwise readily increase their incomes and in amounts large enough to accomplish the purpose of the assistance. The AID strategy in Uganda will incorporate equitable will be maximized by designing projects to yield as much domestic value added as possible (i.e., projects that tend to provide intermediate inputs, equipment and spare parts rather than final goods) and thereby restart local production processes and maximize the employment effect. Experimentation with new technologies during the rehabilitation program will be kept to a minimum.

E. Functional and Geographic Concentration

Neither functional (e.g., specific crops or activities) nor geographic concentration are seen as prime determinants influencing the AID program over the next three years. The rehabilitation emphasis of the strategy implies that the allocation of assistance will be responsive to opportunities to restore productive capacity for activities which are linked to small holders or to help increase the production or income of small holders. Some inputs may be distributed throughout the country. And, because Ugandan farmers are polyculturalists, farm inputs such as hoes may be used for a variety of crops.

There is no a priori reason to designate a specific geographic region in Uganda as the one in which AID will concentrate except that the distribution of some inputs and the location of some activities will be influenced by other donor efforts. For example, the International Fund for Agricultural Development is providing comprehensive assistance to farmers in growth concerns by directing assistance toward Ugandan small holder farmers. Whereas systematic data are not available on rural land holdings, it is known that Ugandan agriculture is predominately small holder in form. The final users of AID-provided commodities can be determined by the selection of the goods themselves and by designing projects which have small holder-oriented delivery systems. Thus the AID program will directly assist small holder farmers and activities which are critical to small holder farming, i.e., production or processing of farm outputs.

The fact that the AID strategy is to assist in the rapid regeneration of existing production capacity, imposes certain inherent constraints. To use an imaginary example, it may be possible to choose between rebuilding a single firm or establishing 10,000 artisans to produce the same quantity of output. Assume further that both alternatives have similar rates of return but the second alternative has a gestation period three times greater than the time required by the first alternative and the risk factor is also three times greater. The second alternative has more favorable income distribution and developmental characteristics than the first alternative. In the proposed strategy the first alternative would be chosen because the first alternative is more likely to yield results rapidly. Given the limits implied by the rehabilitation approach, the economic impact of the AID program six districts in eastern and northern Uganda while the British are assisting cotton production and processing in eastern Uganda (Teso and Bugisu). Thus, AID assistance which would otherwise tend to duplicate other donor efforts will be directed to districts in the central and western part of the country.

F. Private Sector and Policy Aspects

The AID country program will support the expansion and development of the Ugandan private sector as a basic element of AID strategy. This strategy element will be put into practice by designing projects in ways which emphasize private entrepreneur participation as well as the development of Uganda's private cooperative movement. [35/] AID already has provided major assistance to Ugma Engineering which has been returned to the original Asian owners but with government participation. Virtually all activities involving provision of intermediate inputs to manufactures and agricultural processing will involve private or private-government enterprises. As noted above, AID project design will place special emphasis on the use of private businesses and traders as intermediaries in the distribution process. In addition, there will be the maximum possible stress on utilization of farmer-controlled cooperatives and other farmer-level groups as project participants.

The policy framework now exists in Uganda that should enable the private sector to reassume its considerable influence on economic development. While AID will urge the government to revise some administrative barriers inhibiting more rapid rehabilitation of the private sector (e.g., licensing requirements), our greatest contribution to its development will be through the provision of foreign exchange on a term credit basis. AID also will help reestablish the capacity of the banking system to service private sector needs.

Private sector and market forces will also be promoted in policy discussions at all levels. The Ugandan Government is already moving rapidly to divest itself of control and ownership of a large number of activities in favor of the private sector. AID efforts on behalf of the private sector at this level will tend to concentrate on facilitating this process rather than unnecessarily "convincing" the government to do what it is already doing. At the macroeconomic policy level USAID will conduct informal discussions with GOU officials as a means to keep AID appraised of progress in Uganda's reform effort and to keep Ugandan officials informed about AID interests. At the same time USAID will maintain contact with IMF and World Bank representatives, again to exchange views and information on macroeconomic policy developments. USAID will not seek to engage directly in the highly technical and sensitive discussions which are occasionally conducted between

Ugandan and IMF or World Bank officials. If, in the judgment of USAID, a serious macroeconomic policy issue arises, USAID will discuss the problem with Ugandan officials, and, if appropriate, with IMF, World Bank or other donor officials. USAID will participate directly in policy decisions by supporting an effort to collect and analyze data on agriculture. USAID will make this data available to the Agriculture Secretariat which has been established in a collaborative effort between the GOU and the World Bank. One of the Agriculture Secretariat's key functions is to recommend pricing changes to the Ministry of Agriculture.

It will be AID strategy to play a direct role at the sector level, particularly with respect to policies which relate directly to AID assistance activities. Thus, in the course of implementing its development assistance activities AID will encourage the GOU to liberalize input and output distribution and marketing systems and to alter the agriculture input pricing system. Simultaneously AID will explore measures which will stimulate private enterprise activities such as the elimination of administrative barriers to the efficient functioning of private traders.

G. Technology Transfer and Research

The AID program in Uganda during the Recovery Programme period will help restore existing productive capacity and enable poorly functioning institutions to resume more productive operations. Therefore, AID will have only a limited impact on technology transfer and research during the period of this CDSS supplement. As the Economic Overview has outlined, Uganda's farmers are sophisticated, produce a variety of crops and livestock, and are quite responsive to new technological developments that will enable them to increase productivity. But, they are unable to produce now at capacity given the technology with which they are already aware because of the lack of agricultural inputs and transport and because of the inefficiency of the institutions (cooperatives, banks, marketing system, etc.) that should be serving their needs. Thus, during the 1983-1985 period AID will focus on recapitalizing small farmer enterprises and on rehabilitating agricultural service institutions.

While technology transfer and research will not be major components of the AID program in Uganda over the near term, a number of proposed activities nonetheless will develop more efficient production methods and increase production capacity through new technology. Our efforts to restore edible oil production will require the identification of new oil seed varieties and their adaptation to Ugandan conditions. The Manpower for Agricultural Production project should restore the capacity of a number of Ugandan agricultural training institutions to impart production skills already existing in the country. Rehabilitation of the cooperative movement will require the adaptation of modern accounting and financial systems as well as improved methods of stock control and transport management. Thus, in all three instances the transfer of appropriate technology adapted to Ugandan realities will be an important by-product of our larger effort.

During the period of the CDSS supplement AID will initiate a number of activities that will lead to a program with an emphasis on technology transfer and research during the out years. First, AID will undertake a study of agricultural production costs and returns. The results of this should help identify areas of production inefficiency and provide guidance on areas where new technology should be explored. AID will also initiate an appraisal of the status and priorities of Ugandan agricultural research. This should provide the basis for determining future agricultural research activities as well as the role of AID in supporting this work.

H. Institutional Development

The 1984 CDSS provided a comprehensive overview of the key institutions that influence Uganda's economic development. It details how they progressively deteriorated under the Amin regime and were supplanted by the army, which became the most important institution in the country. In terms of mobilizing Uganda's considerable economic development potential, the most important institutions are its private co-operative movement, the marketing system, existing productive enterprises, the transportation and communications system, financial services, the educational system, extension networks, health systems, the country's research capability, and institutions to maintain law and order.

By the time the current government initiated its economic recovery program most institutions were functioning at low capacity; morale and commitment to institutional growth were subordinated to personal gain. As Uganda became increasingly isolated from modern western developments, technology used in its institutions became stale. Physical infrastructure deteriorated as few investments were made in maintenance and repair, much less in increasing capacity. The looting that accompanied the Liberation War destroyed much of the physical assets that had not been consumed during the military regime.

The 1984 CDSS also identified the key institutions on which AID should focus its resources in order to rehabilitate and expand their capacity to contribute to the Recovery Programme's goals. The priorities include rejuvenating the once strong cooperative movement, improving the efficiency of the crop marketing function, and rehabilitating the industries and training institutions serving the country's small holder farmers.

The cooperative movement in Uganda provides a number of vital services to the country's rural poor. It functions as a source of vitally needed farm inputs such as seeds, agricultural implements, pesticides, fertilizer and cattle drugs. It is a democratic movement, operates in response to free market forces, and functions as a private enterprise. It encourages rural savings and has handled production credit schemes. It processes, transports and markets virtually the country's entire export cash crop output. Further, it operates a number of crop processing facilities as well as a number of enterprises such as poultry or pig production, butchering and marketing.

Through the Food Production Support project AID is deeply involved in the rehabilitation of the cooperative movement. This includes restoring not only the institutional functions of cooperatives such as accounting, crop financing, production credit and transport but also its role as a purveyor of agricultural inputs. This effort will continue through 1984 in the Food Production Support project, and thereafter will be expanded into new areas under the Cooperative Development project.

The efficient functioning of Uganda's marketing institutions is vitally important to the income and standard of living of the country's rural poor. These institutions include not only the cooperative societies, district unions and processing facilities, but also the marketing boards and banking system that service related needs. As outlined above

AID already is working to make the cooperative system more effective. AID was instrumental in drawing GOU attention to the critical importance of the marketing boards through a study AID financed on the Lint and Coffee Marketing Boards. Since then the GOU has decided that its export sales operations must be improved, and is considering a number of the recommendations made in the AID-financed report. While we do not anticipate having further financial input to this process, it is an important element in our policy agenda with Ugandan officials.

An efficient banking sector is important to the production and marketing of Uganda's foreign exchange earning crops. The banks not only provide crop financing, but also they have funded production credit programs and are integral participants in the restoration of productive capacity through their financing of cooperative enterprises such as gins, coffee processing factories, dairy operations, and tobacco curing facilities. AID is working on restoring the institutional capacity of the cooperative banking network through the Rehabilitation of Productive Enterprise project,an activity that will finance long term training and advisory services to the bank as well as providing needed foreign exchange on medium term credit terms.

The third element of AID's institution building strategy in Uganda is our direct participation in the rehabilitation of individual enterprises. This will expand as the

Rehabilitation of Productive Enterprise project gets underway. Already AID has gotten two farm implement manufacturers, one of which is under a private management arrangement, back into production. We anticipate getting another 10-12 enterprises underway, including a panga factory, cooperative pig and poultry production and marketing facilities, small farmer dairy operations, and other manufacturing enterprises. Through a combination of capital assistance, technical services and training each of these individual enterprises should be able to continue operating as viable private sector institutions without need for further assistance in the medium term as Uganda restores its capacity to finance needed imports with its own foreign exchange earnings.

AID efforts to support the development of self-sustaining institutions in Uganda also is manifested in our efforts to revitalize the training facilities that are providing new technology and production skills to the country's farmers. The Manpower for Agricultural Development project emphasizes the importance of reestablishing the close relationship that once existed between the District Farm Institutes and agricultural colleges and the country's rural producers. It will develop not only the physical infrastructure at these facilities but also the capacity of their trainers and staff to better serve locally identified production needs.

In summary, the proposed program for Uganda places heavy emphasis on getting a number of vital institutions functioning again as well as improving their capacity to serve rural needs. All of these institutions existed in the past and filled major needs of the agricultural and productive sectors. But, they decayed under the military regime and are not now operating at full capacity. The AID program will focus on restoring their functions, rebuilding needed staff, improving their adaptability and motivation, and establishing a self financing base for their continued operation in the future.

I. Adjusting to the 1980's

The basic structure of the Ugandan economy in 1982 is the economy which developed in the 1950's and 1960's; the composition of production for domestic and foreign markets, the input mix and the technology go back to the 1960's and earlier. During a decade of economic hiatus the Ugandan population has expanded by 30 to 40% (from 10.5 million to approximately 13.5 million persons), the international price structure has changed radically, the East African Community no longer exists, the structure of international markets and demand has changed and there have been major changes in technology. If Ugandan economic rehabilitation and ensuing growth and development are to be guided by market forces and principles of economic efficiency, it is unlikely and inadvisable that the future structure of the Ugandan economy replicate that of the late 1960's.

The first objective of rehabilitating existing productive capacity (guided by economic efficiency criteria) is a valid and rational goal, but it is also necessary that steps be taken during the rehabilitation phase which will form the basis for making adjustments during the 1980's.[36/] While Uganda retains its basic comparative advantage in agriculture and in its major export crop, coffee, the composition of agricultural production must be reexamined and adjustments made if Uganda is to sustain growth over the long-term. For example, the potential for expansion in earnings from coffee exports is limited because of a quota constraint and the long-term price prospects for coffee are mediocre. It will be possible to increase revenue from coffee by upgrading quality, but this alone is not adequate to support long-term growth. Cotton is another example. This commodity was the second largest exchange earner in the late 1960's but its export prospects are doubtful. With the 30 to 40% increase in population between 1972 and 1982, there has also been a proportionate increase in domestic demand for cotton textiles. At the same time the freight costs of exporting cotton have increased several fold, making the net return on cotton exports lower. Also, cotton is not as well suited to Ugandan growing conditions as some other crops which offer a higher return.

The Ugandan economy is heavily dependent on coffee for foreign exchange earnings with cotton a distant (and dubious) second. It is apparent that over the next few years steps should be taken to exploit Uganda's substantial agricultural potential by systematically diversifying agriculture. Two general directions are indicated in light of the relative changes in prices during the 1970's. With the increase in transportation charges, it is necessary to develop either high value crops or crops which can be processed to a higher unit value in Uganda. There is also greater scope for economically efficient import substitution because of the increase in the price of imports and Uganda's larger population. An ideal situation, of course, is to find a set of new crops which are import substitutes but which can also be exported profitably. Oilseeds are one example of a family of commodities which fall into this category.

On the production side, it is likely that the input mix and the technology for many activities are no longer economically efficient because of the different price structure and because of changes in technology that have occurred over the past decade. To the extent a new activity has a sound economic design these factors are taken into account. However, it may be useful to look selectively at some existing activities. For this reason it is urgent that AID initiate and complete a study of production costs and returns for differing production patterns.

Given the increase in population in neighboring countries during the 1970's and their increase in food imports, Uganda may be able to develop a substantial food export industry. Many of the foods that Uganda can produce in surplus--for example maize and millet--are staples within the region. However, unless some of Uganda's neighbors are able to establish convertability in their currencies, Uganda will be limited essentially to a series of bilateral barter arrangements for most trade within the region. The food export option, nevertheles, offers appreciable potential given Uganda's landlocked position and the need to pay overland transport charges to Kenya and Tanzania.

To be able to sustain growth and development in agriculture beyond the rehabilitation phase, it is necessary to initiate the establishment of a foundation for the diversification of agriculture as soon as possible. To facilitate this effort USAID will initiate a selective review of diversification possibilities and survey Ugandan institutional capabilities to support agricultural development. This process can be expected to involve studies of technical feasibility, processing and marketing studies, assessments of foreign markets and pilot projects. One study will concentrate on assessing Ugandan agricultural research capabilities. This assessment will be used to design an assistance program for agriculture research and to help develop a research strategy designed to support long-term diversification. In order to move as rapidly as possible into a directly-productive activity, AID already has investigated the economic and technical feasibility of expanding and diversifying oilseed production and is developing a project to accomplish this.

J. Summary of Strategy Elements

Section II provided sufficient information on the Ugandan macroeconomic situation to yield the conclusion that the AID program can be most effective if it concentrates heavily on rapidly disbursing assistance to help recapitalize small farmer agriculture and help restore productive capacity in the foreign exchange earning/saving areas of agriculture and agriculture-related industry. This general direction is elaborated in Section III. It is recommended that the assistance level be increased by $10 million to a total of $46 million over the next three years. The increase is warranted because of Uganda's ability to use the resources productively in the short term and because of the economy's long-term potential to become a regional economic growth center. To promote equitable growth, the strategy will direct assistance to small holders and to small holder-related activities. There will not be deliberate functional concentration other than that implied by the process of pursuing the objectives of rehabilitation and assistance to small holders. A number of institutions that service small farmer needs will be rehabilitated as part of this strategy. The strategy will tend to be neutral with respect to geographical concentration except to the extent that other donor activities cause duplication. Given other donor activities it is possible that geographical concentration will tend to be in the central and western districts.

AID strategy in the area of policy will be to play an active role at the agriculture sector level, particularly regarding issues related to specific AID assistance efforts. At the macroeconomic and broad policy level USAID will closely monitor the situation, maintain contacts with GOU and IMF officials and, if a distinct opportunity or problem arises, USAID will discuss the issue as appropriate. USAID will contribute substantively to pricing policy decisions by making primary data available from its agriculture census project. The thrust of AID policy efforts at every level will be to promote the expansion of private enterprise and to encourage market liberalization. AID will also support private sector expansion to the maximum extent possible directly through its assistance efforts.

Section III concludes by drawing attention to the fact that major changes have occurred during the decade the Ugandan economy degenerated. Major structural adjustments will be necessary if growth is to be sustained beyond the rehabilitation phase. The time to start laying the groundwork for adjustment is during the rehabilitation phase. Uganda is confronted with the problem of having a narrow export base and limited long-term prospects for increasing the level of traditional exports. To facilitate the development of agricultural commodities that are better suited to the economics and markets of the 1980's AID will initiate efforts to diversify Ugandan agriculture and pursue new market opportunities with high unit value commodities and foods for regional markets.

IV. PROGRAM ASPECTS OF THE STRATEGY

A. Assistance Planning Levels and Program Composition

Table 5 summarizes the three-year program. The program will use the development assistance account and assistance activities will be in project form. All projects will be grant funded. Almost 90% of total funding will go into projects which provide necessary production inputs either in the form of intermediate or final products or as improved skills and better technology. A small part of total assistance will go to project activities intended to facilitate changes in production methods to diversify agricultural production and help identify new markets. No PL 480 resources will be required.

In the past USAID has relied upon central and regional funds to finance limited family planning activities in Uganda. Recently an assessment of Ugandan family planning programs was prepared. It recommended that USAID continue developing a cadre of trainers, particularly at the nurse, midwife and auxiliary level, to carry out in-country family planning clinical training and refresher programs. These training sessions would be assisted through AID financed intermediaries. In addition, direct AID funding of some participants would be required. USAID will continue to rely on central AID/W and regional funds to support these activities.

Table 5. PROPOSED ASSISTANCE LEVEL
(in millions of dollars)

Category	Fiscal Year 83	84	85	Total
Agriculture Intermediate Inputs	7	8	8	23
Agricultural Institution Rehabilitation	5	5	7	17
(strengthening farmer organizations)	(1)	(1)	(2)	
Development and Diversification of Agriculture	-	2	4	6
(oil seed production)	-	(1)	(2)	
Family Planning	No USAID funding: Central/Regional funding only.			
Total	12	15	19	46

B. Program Management

The AID Office in Uganda has six approved direct hire positions: Mission Director, Executive Assistant, Assistant Director for Program, Project Officer, Agriculture Officer and a Management Officer. The Acting Mission Director believes that the staff size is sufficient to manage the proposed program so long as staff time is allocated to areas which are contained within the AID country strategy. The Uganda AID Office will continue to rely heavily on the services (legal, contract, commodity management, project and technical) provided by REDSO/ESA and on the accounting services of the Regional Financial Management Center in Nairobi.

To manage adequately the rapid expansion of the development assistance program we recommend that AID/W and Mission Management consider altering the composition of the six person staff from the currently approved pattern. It is suggested that the Mission Director also function as the Program Officer and that the Program Officer position be converted to either a Commodity Management Specialist (with project experience) or to a Project Officer (with commodity management experience). This modification, in combination with continued assistance in commodity management from REDSO will improve the Mission's ability to manage the resource-intensive program over the next three years.

Footnotes

1. World Bank, World Development Report, 1982

2. World Bank, Uganda: Country Economic Memorandum (CEM), March 1982, Table 3.2

3. ibid, pp. 17-18

4. World Bank, CEM, March 1982, pp 15-17. Using data from Table 3.7 of the CEM, this percentage change in the terms of trade between 1979 and 1981 is negative 46%.

5. IMF, "Uganda - Request for a Stand-By Arrangement," July, 1982, p. 18

5. For more detail see IMF, "Uganda: Use of Fund Resources--Compensatory Financing Facility" May 1981, IMF, "Review of Stand-By Agreement," March 1982; and IMF "Uganda - Request for Stand-By Arrangement, " July 1982. The 1981 balance of payments estimates by the World Bank (Table 2.2) and the IMF are not readily comparable because of different procedures. The World Bank estimates the current account deficit to be $250 million; the IMF estimate is $235 million. Their estimates of the overall balance, however, are $91.3 million and negative $108 million. The seeming $200 difference is partially explained by the fact that the World Bank includes items in its capital account category which the IMF excludes.

7. World Bank, CEM, March 1982, p. 38 and IMF, "Request...," p. 8b. Again there are differences between World Bank and IMF debt service estimates, e.g., the World Bank and IMF debt service ratios of 50%, 49%, 37%, and 51% from 1981 through 1985, whereas, the IMF projects ratios of 42%, 23%, 22%, 23.5% and 23% from 1981/82 through 1985/86. Both institutions have similar export projections.

8. Republic of Uganda. Recovery Programme: 1982-84, April 1982, p. 4.

9. World Bank, CEM, March 1982, p. 43.

10. ibid. p. 43

11. See World Bank, CEM, p. 18 for more detail.

12. ibid, Tables 5.2 and 5.3

13. The IMF, July 1982, "Request for Stand-By Arrangement," p. 6, states that tax revenues increased by 700% whereas the March 1982, World Bank, CEM, p. 144, indicates a 1000%

increase. The IMF, "Uganda - Staff Report for the Article IV Consultation and Review of Stand-By Arrangement," January 10, 1983, revises its estimate to 800%.

14. IMF, "Request...," 1982, p.6; IMF, "Uganda - Staff Report...," 1983, pp 12-14

15. This single sentence covers a broad range of problems. Perhaps one of the most critical and more difficult to assess issues is the long-term consequences of the removal of the Asian community from commerce. Asians were a vital element in the pre-1972 Ugandan economy. It is reasonable to expect, however, that a new commercial group composed of Ugandans, some expatriate Europeans and some Asians can become an effective and dynamic economic force so long as the government provides adequate security and a favorable economic climate.

16. Ugandan conditions permit cultivation of cereals, oil seeds, fibers, vegetables, tubers, tree crops and legumes. Deciduous fruits are the major exception.

17. USAID, Eastern Africa Country Profiles: Uganda, 1980, p. 83

18. USAID, Uganda: Agriculture Sector Assessment

19. Government of Uganda, Recovery Programme 1982-84, April 1982, p. 3

20. IMF, "Request for Stand-By Arrangement," 1982

21. ibid, pp 6,7

22. See World Bank, CEM, March, 1982, Chapter 3 for detailed discussion of the listed problems and additional examination of problems concerning tax collection, aid coordination and sector planning.

23. To provide a more accurate idea of the significance of the price changes it is necessary to compare the new domestic prices to estimates of the international parity prices for the various commodities. This has not been done; however, it is certain that the price changes move the domestic prices closer to their international parity levels and therefore constitute an improvement.

24. World Bank, "Review of Uganda's Recovery Program 1982-84" May 1982, p. 1, mimeo.

25. The first window will continue to operate a managed rate (now at about USHs 110:$1) and foreign exchange will be sold for imports deemed essential to economic rehabilitation and for principal and interest payments. Window one receives foreign exchange from traditional export crop sales and official grants and loans. Window two receives foreign exchange from window one. All foreign exchange earnings which are not required to be sold at window one can be sold at window two

    For a detailed description of the June 1982 adjustments see IMF, "Uganda - Request for Stand-by Arrangement," July 1982.

26. Government of Uganda, Recovery Programme 1982-84, April, 1982

27. World Bank, "Review of Uganda's Recovery Programme 1982-84," May 1982, mimeo, pp. 1,2

28. Government of Uganda, Recovery Programme 1982-84, April 1982, p. 38

29. ibid, p. 15

30. For more detail on problems posed by the marketing boards see: Institute for International Studies, "The Reorganization of the Marketing and Processing of Crops in Uganda: Report to the Ministry of Cooperatives and Marketing," by Robert Bates et al, November, 1981; and World Bank, Uganda: Country Economic Memorandum, March, 1982

31. World Bank, CEM, 1982-84

32. In 1980 the U.S. was the largest bilateral donor with $23 million whereas other donors (6) were averaging around $3 million. In 1982 it is anticipated other donors' contributions average around $4 to $5 million. See the FY 1984 CDSS for additional information.

33. If the money supply were expanding at some excessive rate it could be more beneficial economically to hold the counterpart funds out of circulation. This decision would depend on taking several variables into account in addition to money supply growth.

34. The Ministry of Cooperatives has requested AID to consider financing a two-year USHs 350 million pilot credit scheme. The credit would be made available to 200 primary societies and to the farmers in primary societies to pay for tools, other production inputs and for small-scale projects undertaken by the primary societies.

35. Prior to Amin's military regime private enterprise provided the greater part of agricultural inputs and processing and marketing services. It was noted earlier that it is government policy to reinstate private enterprise but with substantial government participation in some of the larger enterprises, e.g., 49 to 51% ownership in Ugma Engineering but with Ugma holding an independent management contract.

36. Concern was expressed in the FY 1984 CDSS and in the Agricultural Sector Assessment that the Ugandan economy of the 1960's not be recreated.