THE REPUBLIC OF UGANDA

STATE OF UGANDA POPULATION REPORT 2017

Theme:

Transforming Uganda's Economy: Opportunities to Harness the Demographic Dividend for Sustainable Development

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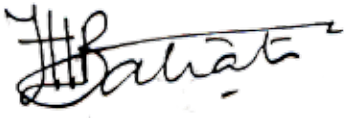
Foreword

Over the last 30 years or so, Uganda has witnessed considerable growth of it's population. This increase in population is a result of a number of positive factors. Although fertility in Uganda has remained high, infant and child mortality have declined. Infant mortality declined from 122 per 1,000 live births in 1990 to 43 per 1,000 live births in 2016. This fairly rapid decline in infant mortality is a result of better health care (e.g. increased immunization, better nutrition, improved water and sanitation, etc.). In addition, Ugandans are living longer. Life expectancy in Uganda increased from a mere 43 years in 1990 to 63.3 years in 2014. A combination of reduced mortality, increased life expectancy and high fertility have been responsible of Uganda's population increase. It is noteworthy that Uganda's population increased from 16.7 million people in 1990 to 34.6 million in 2014 and it is projected to reach about 40 million by mid 2018. Most of this population is young and about half of it is under the age of 15 years. Such a young population poses both opportunities and challenges for development.

The Government of Uganda is fully aware of the above challenges and is prioritizing skilling of young population so that they could fulfill the demand for skilled workers in the country. In order to harness the demographic dividend Uganda has identified three (3) areas of focus:- i) creating opportunities and skills development by focusing on training the youth, ii) review education system and making vocational education a national priority and iii) imparting market-relevant skills and creating an innovative and entrepreneurial workforce.

The State of Uganda Population Report, 2017 synthesizes the contents of 2014 report by focusing on the **Economy** as one of the drivers/wheels for harnessing the Demographic Dividend in Uganda. The report gathered information from a wide range of sources, it synthesized and communicated the policy-relevant results of the demographic process, and it is aimed at raising awareness and it highlighted the important population policy actions.

It is therefore for this reason, that policy makers should benefit from a clearer understanding of the relationship between economic development and changes in age structure that result from the unfolding demographic transition. I wish to recommend this report to all policy and decision makers, community leaders, researchers and academia and to all those who in one way or another contribute to the improvement of the quality of life of the people of Uganda.



David Bahati, M.P.
Minister of State for Finance, Planning and Economic Development (Planning)

Message of Support

Today there are over 20 million young people in Uganda. Young people aged 18 years and below constitute (54 percent) of the total population. This youthful population is Uganda's greatest resource. If properly nurtured and supported, the youth will positively contribute to Uganda's socio-economic development.

Uganda is signatory to the 2013 Addis Ababa Declaration on Population and Development in Africa Beyond 2014, under the theme "Harnessing the Demographic Dividend: The Future We Want for Africa". The declaration recognizes the role of population dynamics in socio-economic transformation and seeks to unleash the full potential of the youth to boost socio-economic development. In this regard, this year's State of Uganda Population Report (SUPRE), underscores the importance of transforming Uganda's Economy, as a pathway to attaining a demographic dividend as well as realizing Vision 2040.

Attainment of economic growth and the demographic dividend is possible for Uganda. If decision and policy makers work to deliberately eliminate inequalities in access to quality education, health including sexual reproductive health services, and economic opportunities associated with age, gender, tribe and location which disempower young people.

Access to sexual and reproductive health information and services are of specific importance to economic benefit – as it allows girls to prevent unplanned pregnancy, stay in school and participate in gainful employment. Information from this publication indicates that, over 70 percent of the unskilled youths and in "vulnerable employment" live in rural areas – these should be at the heart of all our socio-economic transformation interventions – in sectors such as agriculture which have the multiplier job effects.

I sincerely thank the National Population Council (NPC) and all contributors of chapters for their thoughts and input into this important publication. I encourage decision and policy makers to support implementation of the key recommendations of this report on how Uganda can harness the potential of her youthful population to achieve socio-economic development as envisioned in Vision 2040.

Alain Sibenaler
Representative, United Nations Population Fund, Uganda

Acknowledgement

The State of Uganda Population Report development process is a result of multi sectoral consultative meetings under the leadership of National Population Council (NPC). We therefore recognize the important inputs of all stakeholders who participated in the production of this report.

The National Population Council is particularly grateful to the Government of Uganda and United Nations Population Fund (UNFPA) for the financial support that enabled the development and production of the State of Uganda Population Report 2017 with the theme *"Transforming Uganda's Economy: Opportunities to Harness the Demographic Dividend for Sustainable Development".*

The 17th edition of the State of Uganda Population Report 2017 was prepared by a dedicated team of authors and National Population Council recognizes and appreciates the role of these authors in the development of the chapters of this report. The authors are: Mr. John Okalai Ariko (MUBS), Dr. Francis Mwesigye (EPRC), Mr. Paul Corti Lakuma (EPRC), Mr. John Atwebembeire Mushomi (MUK), Mr. Calyst B. Ndyomugabi (MoFPED) and Mr. Kezekia Golooba Lwanga (MoFPED).

Special thanks also go the members of the Editorial Committee namely Mr. Gilbert Siima (NCDC), Mr. Bright Richard Kimuli (UBOS), Mr. Paul Ssenyonga (MoGLSD), Ms. Edith Akiror (UNFPA), Mr. Madani Kakeeto (NPC), Mr. John Ampeire Kaijuko (NPC), Mr. James Peter Olemo (NPC) and Mr. Tiondi Andrew (NPC).

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Finally, gratitude is also extended to the staff of National Population Council for spearheading the process that led to the production of this report, and in particular Monitoring and Evaluation Department (MED) for coordinating the development and production of the report. Appreciation also goes to Mr. Joshua Kwebiha and Ms. Susan Swaga for stakeholder coordination, and secretarial and administrative support.

Prof. Fred Wabwire – Mangen
Chairperson, National Population Council (NPC)

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ACF	-	Agricultural Credit Facility
ACMVC	-	Agricultural Commodity Market Value Chain
AfDB	-	Africa Development Bank
AGOA	-	African Growth and Opportunity Act
AIDS	-	Acquired Immune Deficiency Syndrome
AMFIU	-	Association of Microfinance Institutions of Uganda
AUC	-	Africa Union Commission
BOU	-	Bank of Uganda
BTVET	-	Business, Technical and Vocational Education and Training
BUBU	-	Buy Uganda Build Uganda
CBO	-	Community Based Organization
CMA	-	Capital Markets Authority
COMESA	-	Common Market for Eastern and Southern Africa
CFTA	-	Continental Free Trade Area
CTL	-	Commercial Tax Levy
CSF	-	Civil Society Fund
CSOs	-	Civil Society Organizations
DANIDA	-	Danish International Development Agency
DFCU	-	Development Finance Company of Uganda
DFID	-	Department for International Development
DGF	-	Democratic Governance Facility
EAC	-	East African Community
ECA	-	Economic Commission for Africa
EIA	-	Environmental Impact Assessment
EmOC	-	Emergency Obstetric Care
EPA	-	Economic Partnership Agreement
EPP	-	Export Promotion Policies
EPRC	-	Economic Policy Research Centre
ERP	-	Economic Recovery Programme
EU	-	European Union
FDI	-	Foreign Direct Investment
FAL	-	Functional Adult Literacy
FAO	-	Food and Agricultural Organization
FAWE	-	Federation of African Women Educationist
FBOs	-	Faith Based Organizations
FDI	-	Foreign Direct Investment
FGM	-	Female Genital Mutilation
FIA	-	Financial Intelligence Authority
FIDA	-	Federation of Women Lawyers
FM	-	Frequency Modulation

FOWODE	-	Forum for Women in Democracy
FP	-	Family Planning
FUE	-	Federation of Uganda Employees
GBV	-	Gender based violence
GDP	-	Gross Domestic Product
HIV	-	Human Immuno-Deficiency Virus
HMO	-	Health Membership Organisations
HPAC	-	Health Policy Advisory Committee
IBRD	-	International Bank for Reconstruction and Development
ICPD	-	International Conference on Population and Development
ICT	-	Internet Communication Technology
IDA	-	International Development Assistance
IDPs	-	Internally Displaced Persons
IGG	-	Inspector General of Government
IMF	-	International Monetary Fund
IOM	-	International Organization for Migration
IRAU	-	Insurance Regulatory Authority of Uganda
KALIP	-	Karamoja Livelihoods Program
MAAIF	-	Ministry of Agriculture, Animal Industries and Fisheries
MDAs	-	Ministries, Departments and Agencies
MDG	-	Millennium Development Goal
MFN	-	Most Favoured Nation
MoFPED	-	Ministry of Finance, Planning and Economic Development
MoGLSD	-	Ministry of Gender, Labour and Social Development
MISP	-	Minimum Initial Service Package
MMR	-	Maternal Mortality Rates
MOES	-	Ministry of Education and Sports
MOH	-	Ministry of Health
MOIA	-	Ministry of Internal Affairs
MPM	-	Marginal Propensity to Import
MPs	-	Members of Parliament
MSTI	-	Ministry of Science, Technology and Innovations
MTN	-	Mobile Telecommunications Network
MW	-	Mega Watts
NAADS	-	National Agricultural Advisory Services
NAR	-	Net Attendance Ratio
NAWMP	-	Network of African Women Ministers and Parliamentarians
NCDC	-	National Curriculum Development Centre
NDP	-	National Development Plan
NPHC	-	National Population and Housing Census
NEMA	-	National Environment Management Authority
NFA	-	National Forest Authority
NGOs	-	Non Governmental Organizations
NPA	-	National Planning Authority
NRM	-	National Resistance Movement

NSE	-	Nairobi Stock Exchange
NUDIPU	-	National Union of Disabled Persons of Uganda
NUSAF	-	Northern Uganda Social Action Fund
OIES	-	Oxford Institute of Energy Studies
OPM	-	Office of the Prime Minister
PAC	-	Public Accounts Committee
PEAP	-	Poverty Eradication Action Plan
PHP	-	Private Health providers
PIASCY	-	Presidential Initiative for HIV/AIDS Communication for Youth
PMTCT	-	Prevention of Mother to Child Transmission
PNC	-	Post Natal Care
PNFP	-	Private, not for Profit
PoA	-	Program of Action
PPP	-	Private Public Partnership
PSIS	-	Private Sector Investment Strategy
PSFU	-	Private Sector Foundation Uganda
PWD	-	Persons with Disabilities
RH	-	Reproductive Health
ROSCAs	-	Rotating Credit and Savings Associations
RR	-	Reproductive Rights
SACCOs	-	Savings and Credit Organizations
SAGE	-	Special Assistance Grant for Empowerment
SDF	-	Special Development Facility
SGBV	-	Sexual and Gender Based Violence
SNE	-	Special Needs Education
SRHR	-	Sexual and Reproductive Health and Rights
STD	-	Sexually Transmitted Diseases
STI	-	Sexually Transmitted Infections
TCMP	-	Traditional and Complementary Medicines Providers
TV	-	Television
UBOS	-	Uganda Bureau of Statistics
UCA	-	Uganda Cooperative Alliance
UCSCU	-	Uganda Cooperative Savings and Credit Union
UDHS	-	Uganda Demographic and Health Survey
UGX	-	Uganda Shillings
UJCC	-	Uganda Joint Christian Council
UK	-	United Kingdom
ULGA	-	Uganda Local Government Authorities
UN	-	United Nations
UNADA	-	Uganda National Agricultural Development Association
UNCTAD	-	United Nations Conference on Trade and Development
UMLA	-	Uganda Money Lenders Association
UMRA	-	Uganda Microfinance Regulatory Authority
UNEB	-	Uganda National Examination Board
UNESCO	-	United Nations Educational, Scientific and Cultural Organization

UNICEF	-	United Nations Children's Fund
UNIDO	-	United Nations Industrial Development Organisation
UNFPA	-	United Nations Population Fund
UNHS	-	Uganda National Household Survey
UNISE	-	Uganda National Institute for Special Education
UPE	-	Universal Primary Education
URBRA	-	Uganda Retirement Benefits Regulatory Authority
USAID	-	United States Agency for International Development
USE	-	Universal Secondary Education
USE	-	Uganda Stock Exchange
USDP	-	Uganda Skills Development Project
UShs	-	Uganda Shillings
UWEAL	-	Uganda Women Entrepreneurs Association Limited
UWONET	-	Uganda Women's Network
UWOPA	-	Uganda Women Parliamentary Association
UYDEL	-	Uganda Youth Development Link
VAT	-	Value Added Tax
VHT	-	Village Health Team
VSLA	-	Village Savings and Loans Associations
WFP	-	World Food Program
WTO	-	World Trade Organisation
YES	-	Youth Entrepreneurial Scheme
YLP	-	Youth Livelihood Programme
YVCF	-	Youth Venture Capital Fund

Chapter 1: **Overview**

1.1 Background

According to the 2014 Population and Housing Census, Uganda had a population of 34.6 million people and high Total Fertility Rates (TFR) of 5.4 children per woman (UBOS & ICF, 2016) implying a high population growth rate of 3.0%. The country is a youthful population with 47.9% between 0-14 years, 49.2% between 15 – 64 years and 2.9% above 65 years. In addition to that, the dependency ratio is 103 which implies that for every 100 economically active persons there are 103 dependents. Furthermore, majority of the population 75% reside in rural areas while only 25% of the population resides in urban areas (UBOS, 2014). The high population growth rate made demographers at the National Population Council to forecast that Uganda's total population will grow to 47 million by 2025 and up to 63 million people by 2030 (Ggoobi, 2016).

Uganda's journey to the middle income status as envisaged under the Uganda Vision 2040 takes into account all the 17 Sustainable Development Goals and other regional and global development agendas. The Government proposed to drive Uganda from a *"Predominantly Peasant Society to a Modern Prosperous Country within 30 years"*, targeting the upper middle class with an annual average national income of over Ushs. 34,000,000 per Ugandan (at current conversion rate). Uganda Vision 2040 revolves around harnessing the opportunities through strengthening fundamentals to foster faster socio-economic transformation.

Uganda is poised to take advantage of its demographic situation and as it begins to realize the demographic dividend potential, it should be able to continue to invest in the development process. In principle, openness to trade combined with flexible labour markets will create work opportunities for the enlarged working-age cohort of the young population.

Looking at the demographic transition theory, Uganda is currently accomplishing stage two of the transition (World Bank, 2009) that is why the country is characterized by high population growth rate majorly because mortality especially under-five (64/1000 deaths) has declined whereas fertility levels are still high at 5.4 children per woman.

High population growth rates in the country lead to limited or no land for large – scale mechanized agricultural production. This certainly means low agricultural productivity, that is the output per acre/output per household. Recent research has found that Ugandans use nearly six acres of land to produce one processed ton of coffee (Ggoobi, 2016). The industrial sector will also incur low productions because most of the industries in the country are agro – based. Low productions lead to low incomes and low savings hence slow or no development at all.

High population growth rates often compete with the growth rate of the household incomes. In Uganda the former is currently winning the race. Increase in the population cancels out the increase in aggregate output which keeps average incomes low and stagnant thus keeping people in the vicious cycle of poverty (Ggoobi, 2016).

Uganda's youthful population is majorly unskilled or semi - skilled and as well not financially empowered. In the short run, this leads to low participation of Ugandan

nationals in the market economy. In addition, the few Ugandans who are engaged in the market economy are concentrated mainly in small, informal businesses majorly vending products that foreigners produce.

Uganda's population is characterized by low levels of saving and capital accumulation Ugandans. This economy is structured to promote a consumer culture or what economists refer to as the culture of consumerism. It encourages people to overspend. People living in the culture of consumerism love to live luxurious and ostentatious styles; hang out in eateries and consume sumptuous meals and alcohol, holding parties, weddings and fanfare, carry expensive gadgets such as Smart phone, iPads, and other electronics. Some borrow to finance these ostentatious lifestyles (Ggoobi, 2016).

The need to spur industrialization cannot be over emphasized. The argument in favor of manufacturing is that it would provide numerous low skilled jobs for Uganda's young population. UNCTAD (2015) argues that with rising labour costs in Asia, African countries such as Uganda could attract a significant part of world manufacturing. Dennis et. al., (2016) findings indicated that between 2002 and 2009, 20 percent of the aggregate growth in labour productivity in Uganda reflected the shifting of labour towards industries and sectors where it was more productive on average and at the margin. In addition, given that there is low productivity in agriculture, relocation of workers from the sector to other sectors (industry and services) impacts per capita growth and employment positively (Bbaale, 2013).

Going by the official GDP series, Uganda's economy has grown, quite impressively. However, people tend to look at their situation and wonder whether indeed the economy has grown as fast as is indicated in the official figures from Government. Recently, the economy narrowly evaded a full-blown recession, but GDP has experienced four quarters of negative growth in the last five years (World Bank, 2017).

1.2 Economic Policies and Reforms

Uganda's policy shifts have been recorded to be as many as, there have been, regime changes. The nationalist sentiment of the post-independence period led to in-ward looking policies based on import-substitution, central planning and licensing. This culminated in the concentration of power in the Central Government and in nationalization. When Idi Amin took power in the early 1970s, a combination of erratic domestic policies and external shocks led to economic decline. Milton Obote's return to power at the beginning of the 1980s marked a reversal of the earlier emphasis on controls and nationalization. To encourage foreign investment, market-based policies were re-adopted. However, the regime failed to establish a viable political coalition to ensure longevity.

President Yoweri Museveni assumed power in 1986 and his National Resistance Movement (NRM) Government has had the longest spate in power of any regime since independence. The period has seen some of the most far-reaching political and economic changes in the country, beginning in 1987 with the launch of an economic reform programme supported by the World Bank and the IMF.

However, Ugandan economic growth has been mainly urban based, while the rural subsistence farmers have been left behind. Integration of those into the market economy will be essential for increasing their income. It will take time to integrate these groups, so in the short term the most effective way of increasing their standard may be via improved provision of social services.

1.3 Harnessing Uganda's Demographic Dividend

The Demographic dividend is the economic growth that may result from changes to a country's age structure, due to the shift from people living short lives and having large

families to living long lives and having small families (John Ross 2014). This change in age distribution means, fewer investments are needed to meet the needs of the youngest age groups and resources are freed up for what is called the ***"Economic gift."*** This means that the labor force is growing more rapidly than the population that is dependent, leading to rise in per capita productivity that results, in a window for faster economic growth and better family welfare.

Uganda can draw inspiration from the Asian Tiger economies like South Korea, Indonesia, Singapore, Taiwan and Malaysia which have made significant gains in increasing local production and promoting export. Gaining a demographic advantage for development goes beyond making positive demographic gains, it requires implementing policies and programmes focused on skilling, creating job and trade opportunities and building institutions for good governance. The implications here are clear, the benefits of the demographic dividend are not automatic, and it depends on the proactive initiatives a country takes to productively engage its workforce, the nature of political, economic and social reforms undertaken and the commitment to effective resource allocation and good governance.

1.4 Agriculture as an enhancement for job Creation

Agriculture is the core sector of Uganda's economy. It presents a great opportunity for poverty eradication because it employs over 80% of Uganda's labour force. However, subsistence agriculture is still predominantly practiced at 69% in Uganda, leading to low productivity and earnings from this sector. Agriculture remains the backbone of Ugandan economy because it contributes 40 percent to the total goods export earnings and 22 percent to GDP (UBOS, 2016). The sector is also a major source of raw materials to the local industries and, being the largest employer, the majority of women (about 73 percent) are employed in agriculture as primary producers (UBOS, 2016). Agriculture, hence, has the potential to be a driver of economic growth and poverty reduction in Uganda (MAAIF, 2013). Applying modernized agricultural practices will generate a number of productive jobs in agriculture and allied industries and provide an opportunity out of poverty for many.

Most recently, the desire to develop local businesses and industry has been articulated in several ***adhoc*** Uganda Government initiatives among them the ***Buy Uganda Build Uganda*** (***BUBU***) slogan that seeks to promote public procurement of locally manufactured inputs to enhance growth and create employment for the bulging youth population. This initiative can be accelerated if well-structured investments are directed towards agricultural production not only for commercial purposes but also to stimulate industrial production.

1.5 Financial Sector Deepening

It is important that efforts for financial sector deepening in Uganda are aligned to support the changing demography, technology, and attitudes in the country. While having a youthful population currently manifests itself more as a strain on the resources of the country, it may bode well for future growth of the economy if skills are developed, literacy levels continue to rise and productivity of the working population increases. The financial sector, through digital financial services, can contribute to harnessing this opportunity by improving proximity and bringing harder-to-reach clients into the formal economy at potentially lower costs through innovations such as agent banking, mobile money and electronic payments.

1.6 Youth Empowerment through Skills Development

As Uganda pursues the vision of getting into the middle income category, youth unemployment has remained a major challenge for the country. Providing employment opportunities to the youth is paramount for the country's economic

transformation. A critical mass of youth require employment to increase their incomes and better their standards of living. Youth unemployment or vulnerable employment is always likely to reduce the future productive potential and earnings of the people. Unemployment leaves them with limited incomes, and unable to access good health and education services (ADB, 2017). For the youth to be sustainably employed, they need to be empowered through skills development.

Empowerment through skills development plays a critical role in providing them with better job opportunities in industries and related entities. It also enhances their business acumen. A number of countries have taken off and developed through creating a critical mass of personnel through developing vocational skills. For instance, China has over the years had several deliberate policies on skills development. The deliberate efforts have ensured that about one third (33%) of upper secondary school students are enrolled in vocational schools. This has largely contributed to the country's economic growth and transformation. Similar policies targeting vocational training for skills development were implemented in some European countries such as Germany. In contrast, the percentage of secondary school students enrolled in vocational training across many of the Sub-Saharan Africa remained low for many years.

1.7 Conclusion

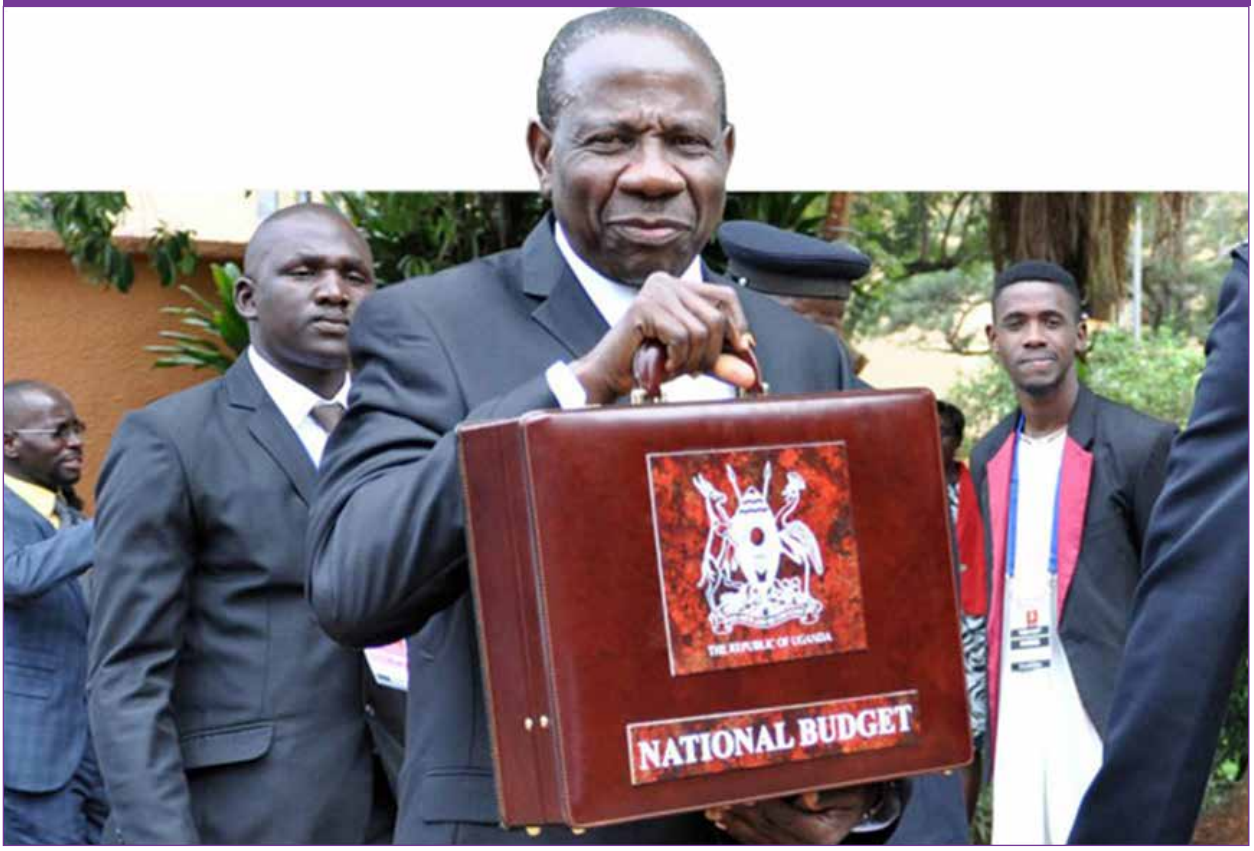
Uganda has since the adoption of liberalization as a development strategy in the early 1990s provided a conducive environment for the private sector to take leadership in the economy. This is due to the fact that across the globe, Micro, Small and Medium sized Enterprises (MSMEs) are highly associated with considerable employment opportunities for the youth. It is estimated that by 2020 1 million people will enter the working age population (>15) each year. The key issues the country must address to benefit from the demographic dividend include:

- Modest decline in the poverty level, despite sustained economic growth over the past decade
- Majority of people are underemployed
- Fastest growing sectors have low job-multiplier effects and most jobs have been created in the low-value informal sector
- High skill mismatch between what the market requires and what the educational system produces.

1.8 Policy Recommendations

1. Modernize agriculture to enhance its productivity and develop value-addition industries.
2. Promote better quality expenditure and investment in agriculture; via improved budget processes aligned to well-articulated strategies.
3. Prioritize enhancement of economic infrastructure and export oriented economic reforms, and enforce accountability in the use of public resources in order to attract investments and create mass quality jobs for the "surplus" labour force.
4. Reform education curricula and teaching methods to focus on innovation, skills development, science and technology, and entrepreneurship development
5. Attract more private investment in export-oriented industries with high job-multiplier effects.

Chapter 2: **Economic Policy Environment and Reforms**



Minister of Finance, Planning and Economic Development, Hon. Matia Kasaija at Serena Conference Centre Kampala.

2.1 Introduction

Following fifteen years of political instability and economic mismanagement, the Ugandan economy was in ruins but since 1986 the country has consistently been among the fastest growing economies, leading to a substantial reduction in poverty. Most of the reforms, that transformed the economy of Uganda, originated inside the Ugandan Government during the 1990s. However, there were mixed results in terms of promoting export diversification, creating an adequate regulation of the trade system and integrating with neighbouring countries, among other factors, warranted a more active intervention of the public sector in trade policy and a change in reforms. In this chapter, an attempt is being made to discuss how the economic policies and reforms instituted brought about Uganda's success. The chapter therefore attempts to explore and discuss how the economic policies and reforms brought about Uganda's success, how they were implemented, their impact and challenges.

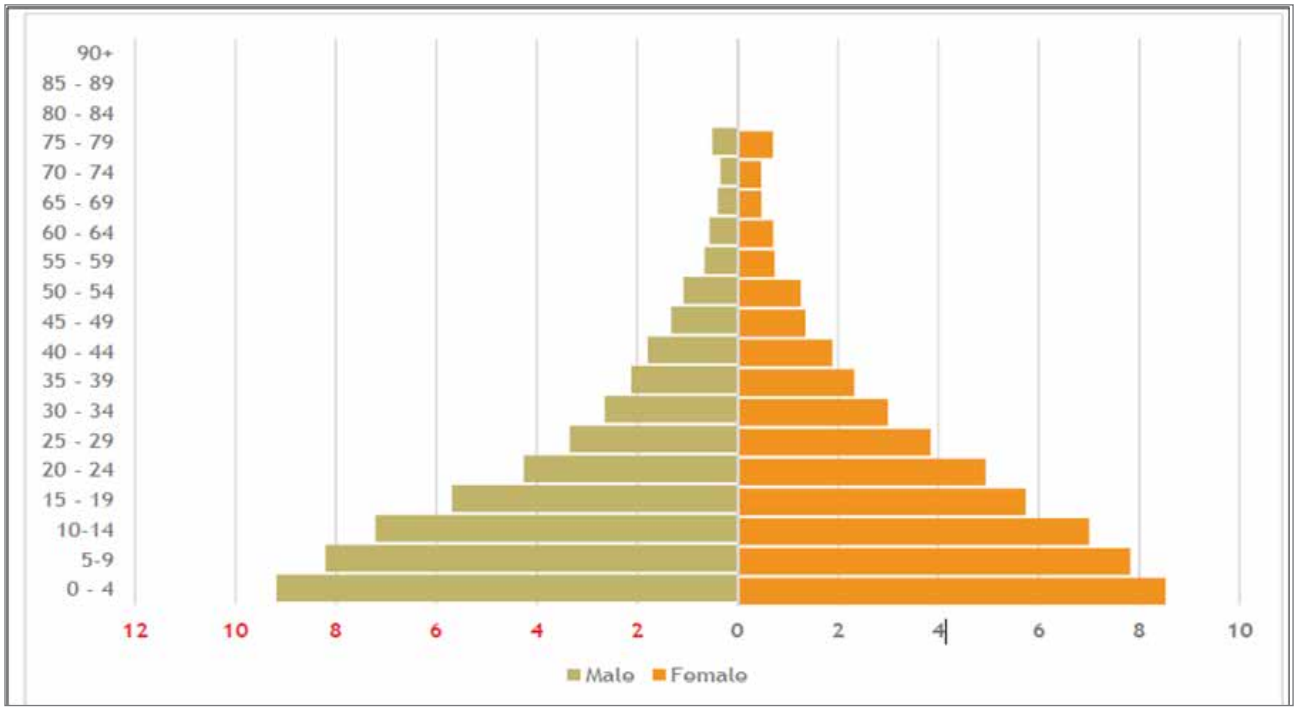
2.2 Population

In 2014, Uganda had a population of 34.6 million people and high Total Fertility Rates (TFR) of 5.4 children per woman (UBOS & ICF, 2016) implying a high population growth rate of 3.0%. The country is a youthful population with 47.9% between 0-14 years, 49.2% between 15 – 64 years and 2.9% above 65 years. In addition to that, the dependency ratio is 103 which imply that for every 100 economically active persons there are 103 dependents. Furthermore, majority of the population 79% reside in rural areas while

only 21% of the population resides in urban areas (UBOS, 2014). Furthermore, the high population growth rate made demographers at the National Population Council Secretariat to forecast that Uganda's total population will grow to 46 million by 2025 and up to 63 million people by 2030 (Ggoobi, 2016).

Data from the Uganda Bureau of Statistics show that in 2005/06 working students accounted for 12.3 percent of the working population, a share which had risen to 14.5 percent in 2009/10; an increase which is consistent with the expansion in the share of the population in fulltime education. A growing share of working students in the working population implies that a larger share of the working population works part time, and hence the total amount of hours worked will not increase as fast as the size of the working population. An example is shown in the age sex population pyramid in figure 2.1 below. The working age population is classified as all people in the age group of 15 to 64 years. The labour force is a subset of the working age population, and comprises persons engaged in any economic activity or who are unemployed but looking for work. However, as a share of the total population, the working age population has largely remained the same over the years. The age dependency ratio was therefore 107 dependents (people of non-working age) per 100 persons of working age; one of the highest in the world. This is because the Total Fertility Rate (TFR) in Uganda is still very high at 5.4 births per woman (UBOS, 2014B). As such, Uganda has barely begun its demographic transition. It will not derive a demographic dividend until the TFR has fallen substantially, thereby reducing the age dependency ratio.

Figure 2.1: Uganda's Age – Sex Structure



Source: 2014 NPHC

Uganda's journey to the middle income status as envisaged under the Uganda Vision 2040 takes into account all the 17 Sustainable Development Goals and other regional and global development agendas. The Government proposed to drive Uganda from a *"Predominantly Peasant Society to a Modern Prosperous Country within 30 years"*, targeting the upper middle class with an annual average national income of over Ushs 34,000,000 per Ugandan (at current conversion rate). Uganda's Vision 2040 revolves around harnessing

the opportunities through strengthening fundamentals to foster faster socio-economic transformation.

Uganda is poised to take advantage of its demographic situation and as it begins to realize their demographic dividend potential, it should be able to continue to invest in the development process. In principle, openness to trade combined with flexible labour markets will create work opportunities for the enlarged working-age cohort of the young population.

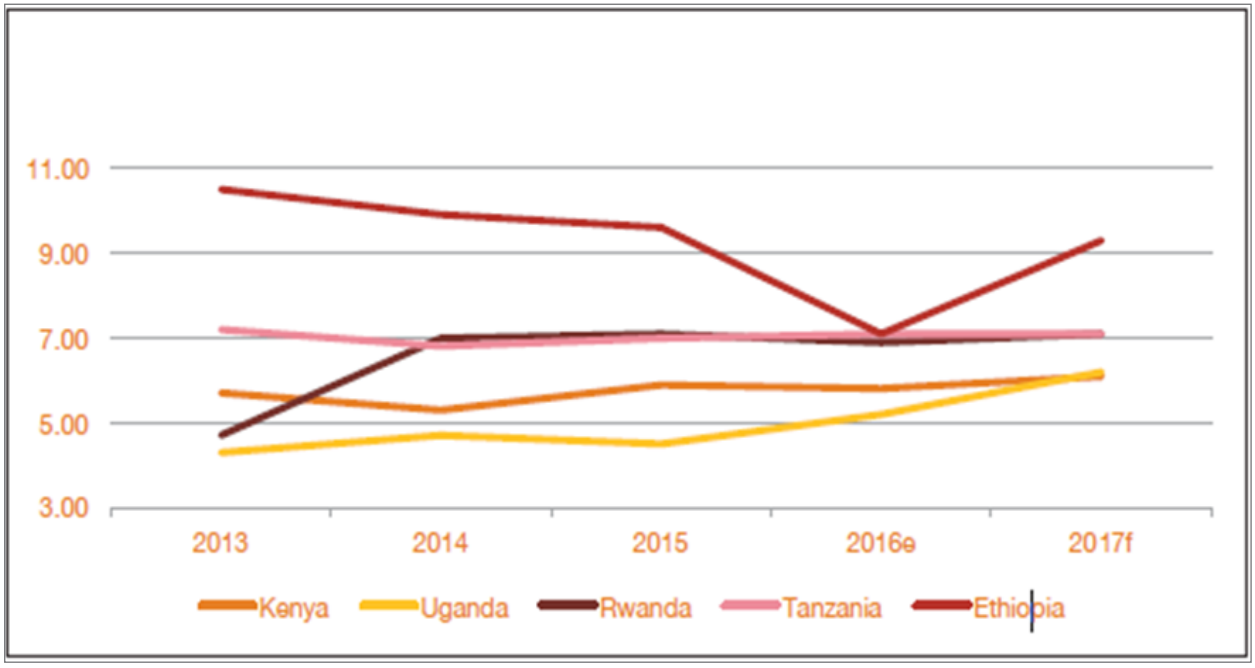
2.3 Uganda's Socio- Economic Development Context

Table 1: Uganda's Salient Economic Indicators

Economic indicators	Years			
	2014/15(a)	2015/16(a)	2016/17(f)	2017/18(f)
Real GDP growth (%change)	5.1%	4.8%	5.0%	5.5%
Annual headline inflation (average)	3.0%	6.6%	5.4%	4.8%
Fiscal balance (% of GDP)	-3.0%	-5.0%	-3.0%	-4.0%
Public debt (% of GDP)	34.4%	36.5%	38.5%	40.5%
Current account (% of GDP)	-9.4%	-8.7%	-8.7%	-8.9%
External debt (% of GDP)	41.3%	45.0%	48.0%	50.0%

Source: Economic Intelligence Unit- World Bank

Figure 2.2: GDP Growth among selected countries in East Africa



Source: Economic Intelligence Unit - World Bank

Looking at the demographic transition theory, Uganda is currently accomplishing stage two of the transition (World Bank, 2009) that is why the country is characterized by high population growth rate majorly because mortality especially under-five (64/1000 deaths) has declined whereas fertility levels are still high at 5.4 children per woman. The latter situation has affected economic development in either positive or negative ways as indicated in figure 2.2 and table 1 above.

High population growth rates in the country lead to limited or no land for large – scale mechanized agricultural production. This certainly means low agricultural productivity. This is the output per acre or output per household. Recent research has found that Ugandans use nearly six acres of land to produce one processed ton of coffee (Ggoobi, 2016). The industrial sector will also incur low productions because most of the industries in the country are agro – based. Low productions lead to low incomes/revenue, low savings hence slow or no development at all.

In addition to that, high population growth rates create limited land for settle and as well give birth to crimes and vice like land grabbing and theft. The latter leads to loss of lives, deformation and destruction of property in the short run. Furthermore, in the long run, such insecurities will scare away investors who would want to invest in the economy hence underdevelopment.

High population growth rates often compete with the growth rate of the household incomes. In Uganda the former is currently winning the race. Increase in the population cancels out the increase in aggregate output which keeps average incomes low and stagnant thus keeping people in the vicious cycle of poverty (Ggoobi, 2016).

Uganda's youthful population is majorly unskilled or semi - skilled and as well not financially empowered. In the short run, this leads to low participation of Ugandan nationals in the market economy. The few Ugandans who are engaged in the market economy are concentrated mainly in small, informal businesses majorly vending products that foreigners produce. Examples of such business include; ***boda-boda***, hair salons, bars, etc. The few big-time investors are investing in non tradable items mainly construction of shopping malls and apartments, land, etc. Since these cannot be exported, their multiplier effect is low. However, in the long run, the low participation of Ugandans in the market economy leads to profit repatriation because most of the large and thriving businesses in Uganda and particularly those in the fastest growing sectors such as telecommunications, banking, large scale manufacturing, wholesale and retail trade etc are foreign owned (Ggoobi, 2016).

Furthermore, Uganda's high population growth rate which is characterized by very low productions increases the marginal propensity to import (MPM): The MPM measures the response of imports to domestic income (GDP). In 2016, the MPM for Uganda stood at 33 percent. This rate of MPM was high compared to other countries in the region such as Tanzania (29 percent), Zambia (23 percent) and South Africa (27 percent) (UNDP, 2015). In simple terms it implies that about 33 percent of each extra shilling earned by Ugandans was shipped out of Uganda to the countries that produce Uganda's imports – China, India, Kenya, South Africa, South Korea, Malaysia etc. That is why the incomes of the Koreans and Malaysians have grown geometrically in the last three decades while those of Ugandans have remained stagnant (Ggoobi, 2016).

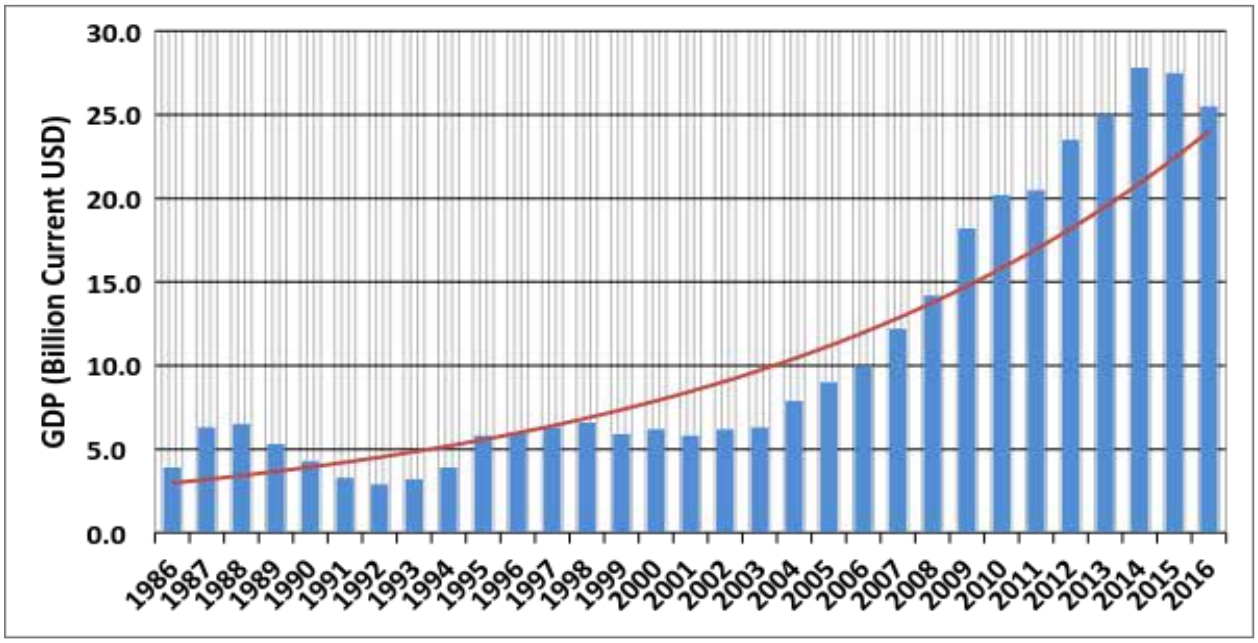
Uganda's population is characterized by low levels of saving and capital accumulation among Ugandans. Uganda's economy is structured to promote a consumer culture or what economists refer to as the culture of consumerism. It encourages people to overspend. People living in the culture of consumerism love to live luxurious and ostentatious styles of living; hang out in eateries and consume sumptuous meals and alcohol, holding parties, weddings and fanfare, carry expensive gadgets such as Smartphone, iPads, and other electronics. Some borrow to finance these ostentatious lifestyles (Ggoobi, 2016).

The need to spur industrialization cannot be over emphasized. The argument in favor of manufacturing is that it would provide numerous low skilled jobs for Uganda's young population. UNCTAD (2015) argues that with

rising labor costs in Asia, African countries such as Uganda could attract a significant part of world manufacturing. Dennis, et. al. (2016) findings indicated that between 2002 and 2009, 20 percent of the aggregate growth in labour productivity in Uganda reflected the shifting of labour towards industries and sectors where it was more productive on average and at the margin. In addition, given that there is low productivity in agriculture, relocation of workers from the sector to other sectors (industry and services) impacts on per capita growth and employment positively (Bbaale, 2013).

Going by the official GDP series, Uganda's economy has grown, quite impressively. However, people tend to look at their situation and wonder whether indeed the economy has grown as fast as the bars and trend-line in the figure 2.3. Recently, the economy narrowly evaded a full-blown recession, but GDP has experienced four quarters of negative growth in the last five years (World Bank, 2017).

Figure 2.3: Uganda's GDP (in Billion Current USD) 1986 - 2016

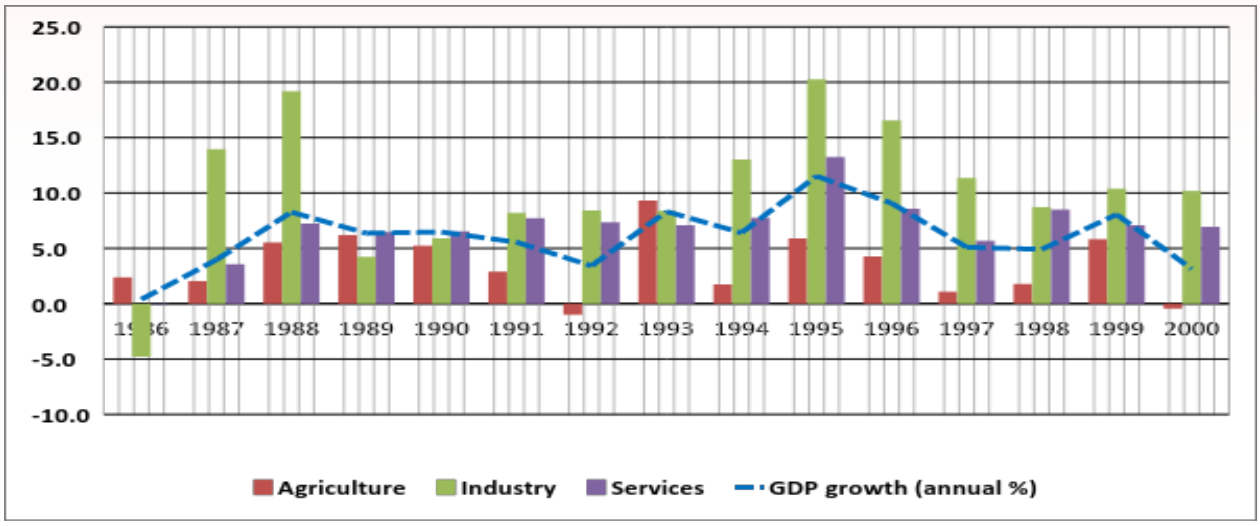


Source: Calculations from WDI Database

2.4 Disaggregation of Sectoral Growth in Uganda's Economy

On average, the industrial sector has been Uganda's fastest growing sector in the economy, while agriculture was the slowest. Industry—a sector whose main activities are mining and quarrying; manufacturing; electricity; water; and construction—registered an average growth rate of 10.3 percent per year (Figure 2.4). This growth rate was much higher than what was achieved by services sector (6.9 percent) and agriculture sector (3.5 percent). After the turn of the new millennium, industry slowed down but still continued to lead, growing at an annual average rate of 7.5 percent (Figure 2.5). Services converged towards industry, registering an annual average growth rate of 6.5 percent between 2001 and 2016. On its part, agriculture continued trailing other sectors managing an average growth rate of only 2.7 percent per year.

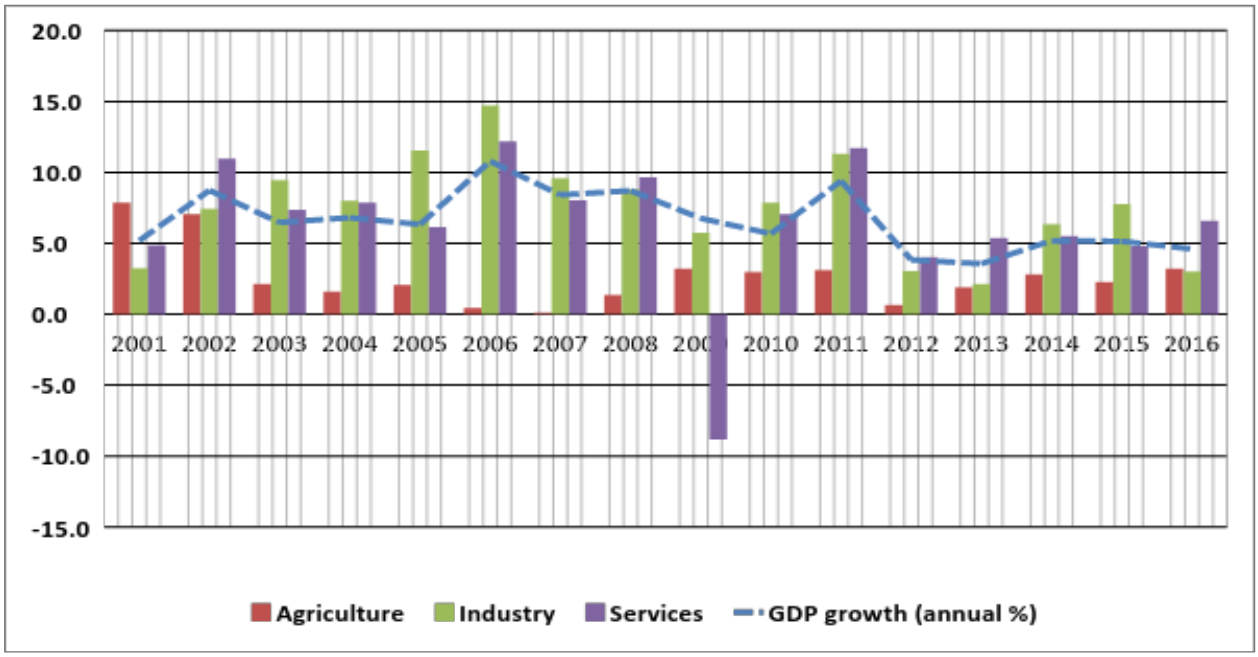
Figure 2.4: Uganda Economy Growth between 1986 and 2000 (percentage change)



Source: Calculations from WDI Database

The data constraint notwithstanding, it is important to disaggregate the so-called fastest growing sectors. The sector that employs most Ugandans (agriculture) stopped growing at averages commensurate with Uganda's population growth rate (3.2 percent) in 2002. Since then, the population has been winning the race in every single year. This would imply that the per capita income growth for a section of Ugandans employed by agriculture (80 percent) has been negative for about 15 years. Yet these are the people involved in harvesting and extraction of resources used as raw materials in industries. It would therefore be interesting to look at the growth drivers in the 'fast growing' industrial sector.

Figure 2.5: Growth in 2001 – 2016 (percentage change)



Source: Calculations from WDI Database

2.5 Economic Policies and Reforms

By the end of 1990s Uganda was not considered to be in economic crisis even though still a poor country. On the other hand political uncertainties, partly owing to wide social and regional gaps, remain, while the country's earlier reputation as a high-risk business environment is not yet eliminated. Still, the recent period of sustained peace has enabled a large portion of the population to be re-incorporated into the market economy and policymakers to embark on wide-ranging social and political reforms.

Uganda's policy shifts have been recorded to be as many as, there have been, regime changes. The nationalist sentiment of the post independence period led to in-ward looking policies based on import-substitution, central planning and licensing. This culminated in the concentration of power in the Central Government and in nationalization. When Idi Amin took power in the early 1970s, a combination of erratic domestic policies and external shocks led to economic decline. Milton Obote's return to power at the beginning of the 1980s marked a reversal of the earlier emphasis on controls and nationalization. To encourage foreign investment, market-based policies were re-adopted. However, the regime failed to establish a viable political coalition to ensure longevity.

President Yoweri Museveni assumed power in 1986 and his National Resistance Movement (NRM) Government has had the longest spate in power of any regime since independence. The period has seen some of the most far-reaching political and economic changes in the country, beginning in 1987 with the launch of an economic reform programme supported by the World Bank and the IMF.

Government of Uganda's first national development plan had the goal of raising the standard of living for all Ugandans, with a view to 'eliminating poverty' altogether (Uganda, 1965). In a peasant economy, this initially led to policy initiatives towards the agricultural sector, including subsidies on essential agricultural equipment and fertilizer, and the expansion of extension services and research. This led in turn to wage legislation, or incomes policy, and the policy of import substitution. The latter was seen as the best means of economic diversification and employment creation (see Elliot, 1973, p.9).

From the point of view of the economy, a major negative event was the expulsion of the Ugandan-Asian business families in 1972. Though anti-Asian sentiment was rife in the 1960s, the expulsion was unprecedented. Jamal (1976) has argued that though a long history of economic inequalities between the African majority and the Asians has caused resentment, the expulsion did little to improve income distribution or the welfare of the 'common man' in Uganda. In retrospect, the expulsion put an end to Uganda's post-independence prosperity. Investments dried up, exports declined, and per capita incomes fell continuously from 1973.

2.6 Uganda's Political and Economic History

Mugisha and Kitamirike (2017) explain that when the NRM Government came to power in 1986, it had already developed strong views on the way forward from both a political and economic perspective, as presented in the Ten-Point Programme. Among others, the NRM/A wanted to "build an independent, integrated and self-sustaining national economy" (Point No.5). This was to be a mixed economy, with small business in the hands of the private sector but heavy industry and key sectors in the hands of the state. The Ministry for Planning and Economic Development developed a statement of macroeconomic strategy called 'The Way Forward 1', which called for liberalization and other market reforms.

In May 1987 the NRM Government, started the process of adopting neo-liberal policies

as dictated by the IMF and the World Bank, under what they termed Economic Recovery Programme (ERP). A couple of years later, several policy reforms, such as financial and trade liberalization, privatization, and deregulation, were implemented to build a "private sector-led economy" under the Washington Consensus.

The architects of the liberalization policy promised to free the economy of "Government failures", such that the economy may become efficient, expand, create jobs, eradicate poverty and inequalities, and get integrated in the global economy. This was under the conventional economic doctrine associated with "neo-liberalism" as laid out in the Structural Adjustment Programmes (SAPs). However, as already seen Uganda has not realized the benefits that the policy architects promised. Among many other shortcomings, the 'growth' has not created the jobs as anticipated. In Uganda, Government left the economy to operate without rules. Stieglitz (2014) argues that today, many of the socio-economic problems faced by poor countries stem from having too much market and too little Government. The deeper issue that Uganda is facing concerns the appropriate roles of the State and the market, particularly in the areas of investment and economic regulation. Although the architects of the market reforms were aware of "Government failure," it appears their understanding of the intertwining of politics and economics was more limited, and so too was their analysis of how to address Government failures.

Uganda's economic policy environment and reforms over the last 10-15 years have been very modest. In particular, the modern, private sector of the economy, comprising formal sector firms, still commands a very small share of output and especially of the labour force. The majority of the labour force still works in agriculture and over two thirds of the agricultural workforce comprises subsistence farmers.

2.7 Uganda's Policy Environment Reformation

According to Drew (2010), economic reformation in Uganda has been impeded by absence of "Green Revolution" in agriculture. The growth in agricultural output that has occurred has been the result mainly of increases in the area of cultivated land and the labour force employed in agriculture, hence yields per acre and labour productivity have been stagnant. The vast majority of agricultural output in Uganda is produced by smallholder farmers, who use rudimentary farm technologies and produce mainly for subsistence rather than the market. The failure to modernize smallholder agriculture reflects a raft of self-re-enforcing constraints. The low rates of adoption of productivity enhancing technologies are caused by smallholders' lack of resources and knowledge and inability to bear risks. In turn this means yields are low, soils are often depleted and marketable surpluses are small. Small marketable surpluses raise transactions costs and depress farm gate prices. Consequently returns to farming are low, which leaves smallholders in poverty, with little or no savings and no capacity to bear the risks of trying to modernize their farming.

Another impediment to economic reformation in Uganda is the lack of private investment in labour intensive industries. There have been quite substantial levels of private gross fixed investment in recent years, probably in the region of 19 percent of GDP. However most of this investment has been in residential and commercial buildings and in oil exploration, which provides very little employment. Investment in residential buildings alone accounted for almost 40 percent of private sector investment during 2008/09-2014/15. The large firms covered by the Private Sector Investment Strategy (PSIS), which have probably accounted for most of the investment undertaken by formal sector firms outside of the oil sector, undertook investment equivalent to just over 3 percent of GDP during 2011-2014. It is these firms which provide the bulk

of high productivity jobs in the economy. They are not investing enough and, therefore, not expanding quickly enough, to absorb more than a miniscule share of the labour force.

The problem of the death of private investment in formal sector, labour intensive industries such as manufacturing, is not unique to Uganda; rather it affects most economies on the African continent. There are three theories of why there is so little private investment in manufacturing industry in Africa. One theory emphasizes deficiencies in physical infrastructure which raise the cost of doing business; e.g. by increasing the cost of power. The second emphasizes the costs of labour in Africa relative to those of potential competitors in manufacturing exports elsewhere in the world, arguing that labour costs are higher in the former and that this differential is not matched by a differential in relative labour productivity (Gelb, Meyer and Ramachandran, 2013). This might reflect overvalued real exchange rates in Africa, because of natural resource flows or large inflows of aid and/or remittances. The third explanation emphasizes weaknesses in the institutional environment for business which increase the risks for private investors (Lim, 2013). It must be acknowledged that empirical research has not yet been able to conclusively identify the binding constraint to private sector investment in manufacturing and other, labour intensive, modern sectors of the economy, in Africa.

The above explanation resonates with the fact that Uganda has barely begun its demographic transition is also associated with the lack of structural transformation. Uganda's very high age dependency ratio, which results from its high total fertility rate, unavoidably depresses savings rates which, in turn, constrains the resources available for investment in human and physical capital. Countries which have experienced rapid economic growth and structural transformation, such as those in East Asia, have far lower TFRs and dependency ratios. Although the relationship between demographic and structural change is not uni-directional, it is difficult to believe that Uganda's retarded demographic transition has not contributed to its economy's failure to achieve more rapid structural transformation.

The economy has not achieved strong growth in labuor productivity. At the level of the whole economy, labuor productivity increased from Ushs 2.6 million per worker in 2002/03 to Ushs 3.2 million in 2012/13, in constant 2009/10 prices; an average annual real increase of only 2 percent, which is mediocre for a developing economy. This reflects the fact that most of the shifts which have occurred in the composition of the workforce have involved workers moving from one low productivity sector to another, such as from self-employment in agriculture to self-employment in services or artisanal manufacturing or paid employment in informal micro enterprises in the services or artisanal manufacturing sectors. Rapid labour productivity growth would require labor being absorbed in large numbers into high productivity formal sector firms, but that has not taken place.

Government of Uganda in 1987 embarked on an Economic Recovery Programme (ERP) supported by the World Bank and the IMF. While coverage and emphasis might have evolved with time, the goals of the reform programme remained more or less intact in the following decade: to stabilize the economy, bring about a resumption of growth and enable maintenance of a sustainable balance of payments position. This was to be pegged on public-sector reforms, market and price reforms and exchange rate reforms and trade liberalization.

Since the fiscal disruptions of 1992, Uganda has managed to combine high levels of economic growth with low levels of inflation. However, while the first bout of growth was partly ascribed to the recovery of production capacities as peace returned to the country and policies became more predictable (the peace premium), subsequent growth demands investment from both domestic and foreign investors.

2.8 Investment and Productivity Growth

In any country, per capita income growth may be caused by either capital accumulation or productivity growth. The reason for the rapid productivity growth in Uganda is probably more due to improved utilization of existing capacities, made possible by the return of peace and by the gradual reduction in market distortions in, for example, the foreign exchange and labour markets and not new investment. However, there should be a concern about the implications for long-term growth, since the effects mentioned are of a one-off character. Without capital deepening Uganda will not be able to diversify its production nor expand its industrial structure. This is necessary if the country is to achieve sustained growth. It is therefore essential to also look at the issues of savings mobilization and investment behavior.

Uganda has grown rapidly during the 1990s, but one of the questions being asked is who the beneficiaries have been and the extent to which the country has been able to reduce poverty. In response to the poverty challenge, the Government launched a Poverty Eradication Action Plan (PEAP) in late 1996, although it did not take final shape until 1997. The goal of PEAP was to guide all future public investment and to empower the poor by enhancing their incomes. Among its main strategies is the consolidation of macroeconomic policy in order to maintain the growth momentum.

Foreign aid has been important for development in Uganda, as indeed for other developing countries. Over time, concerns have arisen with regard to the lack of aid effectiveness and the problem of aid dependence, as countries fail to embark on sustainable development (Elbadawi 1998).

Uganda embarked on economic reform in the second half of the 1980s from a position of serious economic weakness. The country had just gone through close to a decade of civil disturbances and war, the infrastructure was badly damaged, while the social services, education and health especially, had been badly disrupted, and close to non-existent in the countryside.

Beginning with the late 1980s, aid inflows have increased rapidly. In 1991, for example, aid inflows were the equivalent of 20 per cent of GNP, over 100 per cent the value of exports of goods and services. Aid per capita in current dollars had risen to 41.7. By then the dangers of aid dependence, including the implications of a rising debt burden were frequently voiced. For a poor country, still ravaged by civil war, some of the conditionalities imposed, on public sector expenditures, seemed excessive. Similar demands were rejected by other African countries. In retrospect, the conditionalities helped impose a level of discipline on the public sector and the bureaucracy at a time of a general shortage of managerial and technical resources. For Uganda to eventually escape dependence on aid, it is necessary to put in place measures to attract other forms of long-term capital. Development of the private sector will be crucial in this regard.

2.9 Geopolitical Cooperation and Policy Environment

The Ugandan economy is much stronger today than during the civil war of the early 1980s. However, concerns are still abound that the increased regional insecurity might disrupt the Government's focus on political and economic reform and that in the military theatres human rights abuses of the past might return.

East African economic co-operation is finally taking concrete shape. Policymakers have taken a slower and more careful path to renewed co-operation. In Uganda; therefore, meetings have taken place to sensitize the various groups and to bring on board their suggestions and concerns. In introducing the first East African passport, policymakers

have likewise had their eye on public opinion, which allows holders to travel unhindered within the region.

Experience shows that few African countries have been able to maintain high average growth rates for any appreciable period. The issue here is whether Uganda will be able to sustain the high growth rates that it has seen since 1987. There is little doubt, however, that much of it has been made possible by the adoption of sensible policies, not least the stabilization of the economy and removal of controls on economic activities. Still, a number of issues remain. Uganda's social indicators are poorer than of other countries at the same level of average income. Its education status lags behind that of its neighbors, morbidity and mortality levels are high, while some of the infrastructure is still poorly developed. Governance and the rule of law have been emphasized in the past decade, but there remains a lot to be done in strengthening the police and the judiciary. For a reforming Government that does not want to regress into controls and declining growth, they cannot be avoided. To maintain credibility in its policies, mobilize domestic support as well as that of the donors, the main ingredients of the Government's reform programme will have to remain in place.

2.10 Macro-economic Policy Environment

Public finances have been at the centre of Uganda's reform effort in the past decade. The goal has been fourfold: to maintain macroeconomic stability, increase the efficiency of public expenditure, devise less distortionary and equitable methods of taxation, and develop managerial and institutional capacities in both taxation and expenditure. A fifth goal, voiced frequently in the budget speeches, has been to reduce Uganda's aid dependence. Although the Government has been able to increase its revenue collection in the past few years, public resources remain low and vulnerable. The public sector's capacity to address poverty via own resources are all but impossible. Donor aid thus continues to be a key resource input in the economy. This implies in turn that a number of crucial initiatives, such as the anti-poverty measures, will remain donor driven (Goetz and Jenkins, 1998), with threats to local ownership and sustainability.

Regarding revenue, in comparison to many countries in Africa, even those that have experienced a prolonged period of political destabilization and civil war, the Government's capacity to generate revenue has been below average. Trade taxes have traditionally been a major source of Government revenue in Uganda, a situation not very different from that of its neighbors.

Improvements in revenues over the past decade have been the result of a more organized tax collection effort, spearheaded by the Uganda Revenue Authority. The Government introduced a 17 per cent VAT in July 1996 to replace sales tax and the commercial transactions levy (CTL) first introduced in 1972. The objective was to broaden the tax base and to increase revenue collected. It is hoped that the uniform tax rate will reduce the need for detailed information and thus the cost of administration. It could also help reduce tax evasion.

The Government also needs to find ways of widening its tax base to include more groups than is currently the case. Many of Uganda's self-employed and agricultural producers are not paying income taxes. Furthermore, fishermen in the islands of Lake Victoria as well as Uganda's other lakes are largely outside the tax net. In the past, it was difficult to justify a rapid extension of the tax net when social services to most of the country remained so poor. However, the Universal Primary Education programme noted above, provides the Government with some arguments for a broader tax effort. Key policy concerns are now the long-term viability of the Government's revenues as well as soundness of its expenditure. Both are

crucial for the success of the Government's poverty reduction strategy and, generally, for sustaining growth.

On expenditure, besides policy commitment, Uganda's much lauded reform has been a result of rapidly rising expenditure. In the past decade, the size of domestic revenues has not been a serious constraint on Government expenditure thanks to foreign aid. Whereas tax revenues have increased, the budgetary process remains weak. The goal of the cash budget ought to eliminate payment arrears, which had distorted macroeconomic policy.

2.11 Exchange Rate Regimes

The history of exchange rate reforms in Uganda is closely related to the economic management abilities of the various regimes. The over valuation is blamed on excessively inward oriented policies, and its reduction on increased openness.

2.12 The International Debt Burden

In Uganda, foreign assistance led to a high level of indebtedness. With regard to debt sustainability, the main concern relates to the appropriate use of the available resources. Uganda has gone beyond the stage of emergency repairs even that of rehabilitation and needs to plan its aid resources better in order to ensure high growth. Poor planning has in the past led to problems of aid absorption. Generally, inadequate institutional capacities, especially in the line ministries and at the Bank of Uganda, were blamed for the slow pace of project implementation and the speedy utilization of disbursed funds. In responding to these micro deficiencies, some donors, such as Sweden, used their aid budgets to pay off Uganda's debt arrears, especially to the World Bank, under a scheme referred to as the Fifth Dimension. By resolving the arrears problem with the IBRD loans (that is the harder loans of the World Bank proper) Uganda has then had access to the much softer loans from the IDA.

Although Uganda has not accumulated a large domestic debt and the role of the treasury bills is still fairly limited, it has in recent years accumulated substantial domestic arrears, which have had a disruptive impact on macroeconomic aggregates because they are poorly structured and almost informal in character.

2.13 Strengthened Financial System

In Uganda, a number of policies exist to address challenges of a weak financial sector: Under a Financial Sector Adjustment Credit, the Government has embarked on a number of policies aimed at rehabilitating and expanding the services provided by the sector. A 1993 Financial Sector Act was passed by Parliament and it stipulates importantly that the Bank of Uganda would supervise the financial sector and would have to be satisfied with the 'competence and integrity' of the proposed management of a bank or financial company. Among other policy issues were the following: 1) To be allowed to operate banks had to meet all capital adequacy requirements; 2) Financial sector legislation had to be revised regularly in order to meet the demands of a rapidly changing economic environment; 3) The regulatory framework for the various parts of the financial sector: banks, insurance companies and capital markets needed to be strengthened; and 4) Bank of Uganda was mandated as the overseer of the financial sector.

2.14 Bank Portfolio and Bank Interest Rates

Macroeconomic policy outcomes have had important impacts on the financial sector in Uganda. The sector's response has in turn impacted on the overall economic environment. Traditionally, the banking sector provided a more favorable rate for agriculture in the general belief that this would spur

development. However, in recent years banks have been less willing to extend cheap credit to farmers or agricultural projects.

Several small banks have entered the market. These are controlled by a small group or a family and at times have close connections with powerful political factions. The owners of these banks often have vast business interests in other branches and seem to use the banks to finance these, and sometimes provide loans on dubious grounds. This has meant that some of the banks have very large stocks of nonperforming assets. Most of the local banks have for a long time failed to make adequate provision for non-performing loans and also failed to satisfy capital adequacy requirements. The mushrooming of weak banks has increased the fragility of the financial sector and its susceptibility to shocks, both internal and external. Recent experience in Uganda has shown that the impact of a bank's collapse can be larger than its market share.

In Uganda, the modern sector elite i.e. those demanding 'profitable' banking services, though expanding, is still very small. Smaller still is the financial elite. There is thus considerable scope for inbreeding and recycling of ideas, that is borrowers and lenders might be one and the same. A notable outcome has been the failure, even after the recent economic reforms, to isolate politics from finance – that is to keep politicians from being policymakers and patrons at the same time. This type of system creates inefficiencies, which tend to constrain economic growth.

Uganda's experience indicates that if not remedied, the currently poor performance of its financial sector threatens the progress made in other sectors of the economy. There is need for the development of a new bank culture to match the increasingly market-oriented nature of the economy. Under the increasingly globalised nature of the economy, banks need to devise systems that enable them to lend profitably once again and their clients to borrow responsibly. A system based on the presumption of a high rate of default cannot be good for the development of the financial sector or the economy.

2.15 Infrastructure and Social Capital Investment

Public sector's involvement in the provision of social services in Uganda was fairly extensive backed up by a performing economy. Education and Primary Health Care were given considerable emphasis, seen as instruments that would help reduce ignorance and disease in the countryside, and boost overall economic development. However, the rapid population growth and the onset of crisis in the 1970s began to depress the supply and quality of social services (Heinemann, 1979).

Four problems have been associated with the poor delivery of infrastructure and social services in Uganda. First, the overriding problem has been the inability of the central and local governments to provide adequate resources. Second, the institutions set up by the Government for training, regulation and research gradually fell into disrepair. Third, the financial constraints reduced the levels of remuneration in the service sector, notably the pay for civil servants and teachers, to intolerable levels, and Government workers became lethargic. Fourth, the provision of social and infrastructure services in Uganda has been plagued by an urban bias. Modern services, roads and telecommunications are concentrated in the confines of the major urban centres. There is a shortage of resources and personnel to modernize and adapt the institutions to the needs of the rapidly expanding population.

Kampala – Entebbe Express High Way Intersection

The demand for education has increased in the past few years with rising enrolments in both primary and secondary schools. The construction of structures has also expanded although at a lower pace. This implies increased overcrowding in many schools. However, there is concern that the number of teachers in the various institutions has not risen by much. Thus the capacity for Ugandan schools to impart learning skills might still be weak. One of the of the workable solutions is to extend primary school by one year from 7 to 8 years. Since students leaving primary school will be somewhat older, this would enable an increased vocationalisation of education to the benefit of those who might not be able to continue.

Uganda's health status is poorer than that of countries at its level of per capita income, reflecting in large measure the persistence of the effects of civil war and the institutional disruptions of the past decades. Since, the thrust of the current system has been curative rather than preventive, the availability of drugs has been crucial to its functioning. However, Uganda has poor drugs culture characterized by massive phone demand. Lack of a drug administration and licensing policy has led to shortages of crucial drugs but to an apparent excess supply of others, given the proliferation of drug stores.

The reforms in service provision and UPE seems to have had a positive impact on school attendance, even for poor households. Still, the rising share of the social sectors in the budget should have had a larger impact on the ground. It is thus important to devise measures to ensure better service delivery at the local level. This demands improvements in the resource delivery functions in line ministries as well as strengthened accountability. However, although there was a general decline in social service provision in Uganda, it was more marked in the countryside. The improvement of rural services and infrastructure will thus be important in attempts to bring the benefits of reform to the rest of the country.

The decentralization process is a real challenge for the Government. It is essentially a good strategy for the long term development of the regions outside the capital, but there

is a glaring gap between the plans and the actual capacity and competence on the ground. Since the decentralized councils are to handle important services such as health and education it is essential that these be strengthened.

2.16 Conclusion

Uganda is one of the countries in Africa, which by now has a fairly satisfactory policy environment, and it has been growing rapidly over the last decade. However, its investment rate remains fairly low, so the high growth is to a large extent the dividend to policy reform. Unless the investment rate can be raised the growth will not be sustainable in the longer term. Since domestic income levels still are low this will require external inflows of private and/or public investment resources. However, at present investors perceive risks to be high and many take a wait and see attitude. Recent studies have shown that aid can function as a catalyst for private investment (Burnside and Dollar, 1997) in a reformed policy environment, but there is also need for measures that either reduces risks or insures inventors against risks if private investors are to come in on a large scale. Visible support from donors to countries that are on the right track would constitute a powerful signal to investors. The emphasis is now on the development of the private sector within a market economy. Much needs to be done before private investors can feel that there is an enabling environment where investments are secure.

Ugandan growth has been mainly urban based, while the rural subsistence farmers at least have been left behind. Reintegration of those into the market economy will be essential for increasing their income. It will take time to reintegrate those groups, so in the short term the most effective way of increasing their standard may be via improved provision of social services

There is a general concern that the poorest have not benefited much from the general improvements. Therefore efforts directed at reaching them need to continue. They have seen improved access to education, but direct private costs are still substantial enough to keep children of the poor out of school. Increased funding for education should be one of the top priorities of the Government. Primary Health Care is another area which is grossly under funded. In both these areas clients are forced to bribe their way through the system, and again there is a need to have a two-pronged strategy with administrative reforms and better salaries for employees.

2.17 Policy Recommendations

a) **Macroeconomic stability**. Sound fiscal and monetary policies are prerequisites for successful development, and the stabilization efforts in Uganda. The Ministry of Finance is keeping tight controls on spending and is committed to the preservation of stability.

b) **International competitiveness.** One important indicator of whether Uganda has taken off is whether it has become internationally competitive in areas outside traditional commodity exports. Uganda's external competitiveness is thus improving only slowly. To be able to achieve rapid growth it is necessary to also make a breakthrough in the export of manufactured goods.

c) **Competitive domestic markets**. There is less Government interference in domestic markets. In many other areas competition is still weak. In the utilities, for example, the regulatory framework is yet to become operative.

d) **A stable financial system**. There has been some progress in efforts to create a more diversified and reliable financial system, but the sector is still fragile and prone to abuse. The weakness of the financial system, with few products, mostly confined to the capital, is a good illustration of the type of institutional

constraints that the country still faces.

e) **Human capital for competitive production**. Human capital development is crucial if growth is to be sustained. In the area of education, there has been some progress with the introduction of UPE and USE. However, technical skills are scarce, with white-collar employment still the driving goal of education. Still, countries that were able to industrialize also had a good supply of skilled labour. Uganda's healthcare services reach only a small portion of the population and the country still has poorer health indicators than most African countries.

f) **An effective physical infrastructure**. Uganda has focused on the development of the transportation network. Some trunk roads are relatively good, while other roads in some areas are still in poor condition. Energy and telecommunications are still major bottlenecks for large- scale producers.

g) **Unbiased institutions**. Growth requires effective public institutions, such as courts, while the rule of law is essential for the development of a market economy. There have been some improvement and innovations in this area in Uganda, but the process is slow and inefficient.

h) **Good Governance.** Growth requires good governance. The Ugandan public sector has been streamlined and there have been significant improvements in its effectiveness in the 1990s. Still, there is much rent seeking and corruption, with negative consequences for the economy. The decentralization efforts undertaken in Uganda are interesting and will in the longer term probably make it easier to achieve development outside the core areas in the south of the country. However, local capacities are still low and funds are inefficiently used at the district level.

i) **A broad-based development pattern.** This is a problem that cannot be solved by economic policy measures in a narrow sense. There is certainly a need for economic improvements in these regions. However, the problem is that while there is need for improvements, the instability there makes it hard to achieve.

j) **Political maturity.** The main constraints on Uganda's future growth are probably to be found in the political sphere. This will lead to economic pressure and probably lead to policy reversal.

k) **Reduced aid dependence**. The achievement of self-sustaining growth also requires that the country increasingly can grow from its own resources, that is a reduction of aid dependence. In the case of Uganda the aid inflows have remained unchanged in nominal terms in the last few years, but as the economy has grown quite rapidly there has also been a reduction in the extent of aid dependency, as measured by the Aid/GDP ratio.

l) **Domestic saving and foreign private investment as the major source of investment finance**. A large share of investment is still financed by official foreign resources, but the domestic share has been increasing, while foreign private capital is flowing in as well. Aid dependency remains high, and it is not certain that positive per capita income growth can continue without aid. The political and institutional structures are weak and are an encumbrance to the effective functioning of the economy.

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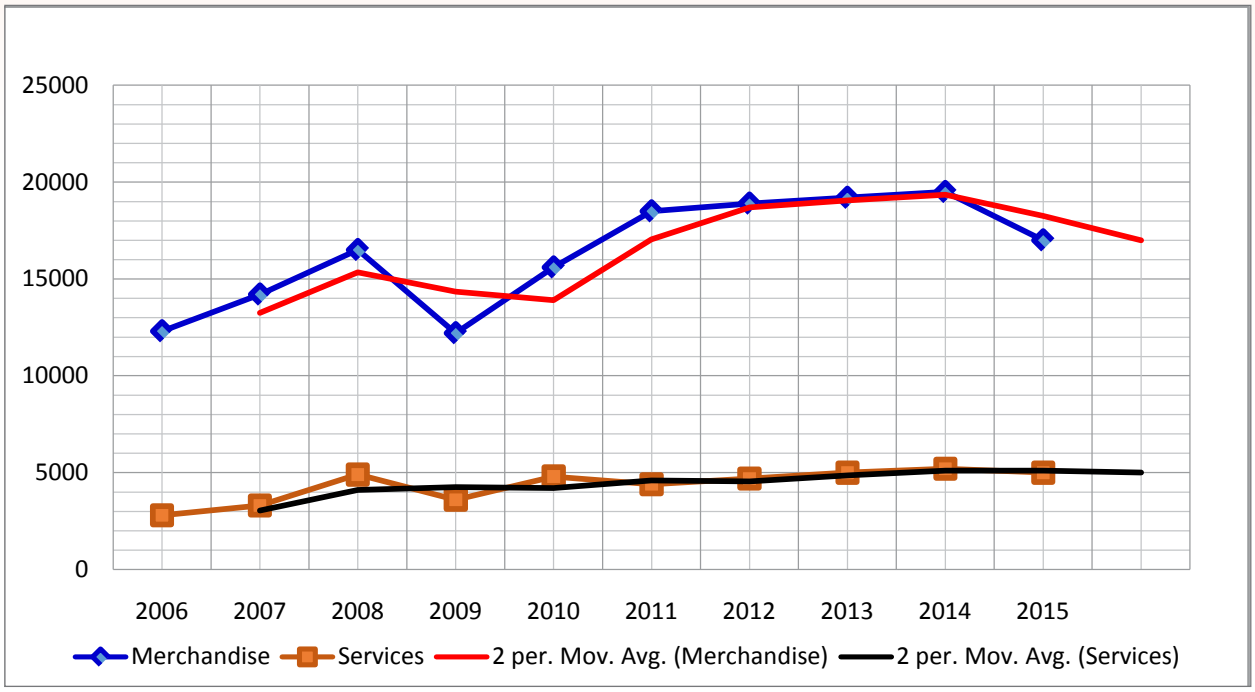
Chapter 3: **Local Production and Export Promotion In Uganda**

Workers Picking Tea leaves in Tea Plantation in South Western Uganda

3.1 Introduction

In modern times the wealth in nations to a great extent is being derived from trade through specialization in economic activities in which a nation commands a comparative advantage over the others. In specializing in production activities where their resources can yield most output, nations have been able to lower their local production costs, increase productivity and generate surpluses, goods and services. The surplus from local production is transferred through trade to other nations through an export process. The country in turn imports those goods which it cannot produce more efficiently at home. This is the essence of international trade, it encompasses export and import trade which means the exchange of goods and services across national borders. The goal of export trade is to facilitate the distribution of a wide range of products produced in different parts of the world to global markets across the world. Consumers in one nation can buy more goods produced in other nations using the wages they earn, and standards of living should, in theory improve as a result of trade. The recent trends in global trade both in terms of value and tonnage, is on the rise (WTO 2016) as shown in figure 3.1.

Figure 3.1: World merchandise trade and trade in commercial services (US$ billions), 2005-2015



Source; Extracts from WTO (2016)

The structure of todays' global trade is anchored on corporations, meaning it's not nations trading but mostly corporations within nations and the end products of trade being consumed largely by individuals. The nation simply plays a regulatory role and customs oversight capturing data on trade flows.

3.2 Global Trade: The Historical Perspective and Trends

The evolution of global trade can be articulated in three major phases of development; in the first phase spanning until about the 1970s; factors of production were much less mobile, global trade was fairly unregulated and there was limited mobility of raw materials, parts, finished products and a limited trade in services. This began to change after the World War II, impediments such as tariffs, quotas and limitations to foreign ownership ushered in an error of increased regulation. Trade was further limited and delayed by inefficient freight distribution and trade was used as a coping mechanism to address scarcity rather than promote national economic growth.

The second phase from around the 1980s was characterized by mobility of capital and other factors of production. Nations focused on their comparative advantages, regional trade agreements took center stage and a global trade framework (GATT/WTO) was established. Further containerization and growing air traffic provided the capabilities to support more complex and long distance trade flows. Foreign direct investments surged, particularly towards new manufacturing regions as multinational corporations became increasingly flexible in the global positioning of their assets.

In the third phase, growth in international trade has included a wide variety of services, this has seen a shift from regional to geographical and functional integration of production, distribution and consumption systems as a result of emerging global networks and the need for a high level of export and imports logistics management. This integration has been driven by advances in information technology and have created changes in global trading systems with a high level of integrated services, finance, retail, manufacturing and distribution systems,

allowing nations to more efficiently exploit their regional **comparative advantages.**

The volume of exchanged goods and services between nations is increasingly responsible for wealth creation. By 2007, international trade surpassed for the first time 50% of global GDP, representing a twofold increase since 1950 (WTO 2015). The contribution of Least Developed Countries (LDCs) to global trade is mainly in the area of raw materials, compared to developed and developing countries which have industrialized and engage in trading services and manufactured goods. Uganda is an agrarian country and the bulk of the exports come from agricultural products which contribute 70% of the country's export earnings and 23.6% of GDP in 2015/16. Overall agricultural exports contributed to 10% of global exports in 2015 (WTO 2016). Agriculture continues to be the major employer in Uganda employing 80 % of the working population. Smallholder farmers account for 98% of agricultural production in Uganda, while 2% are commercial farmers. Besides agriculture other productive sectors in the economic include the services, manufacturing, extractive industry and the construction sectors. Most of these sectors are regarded to be at a nascent stage and represent opportunities for future growth and trade for Uganda.

3.3 Trends in Uganda's Global trade; (Export and Imports)

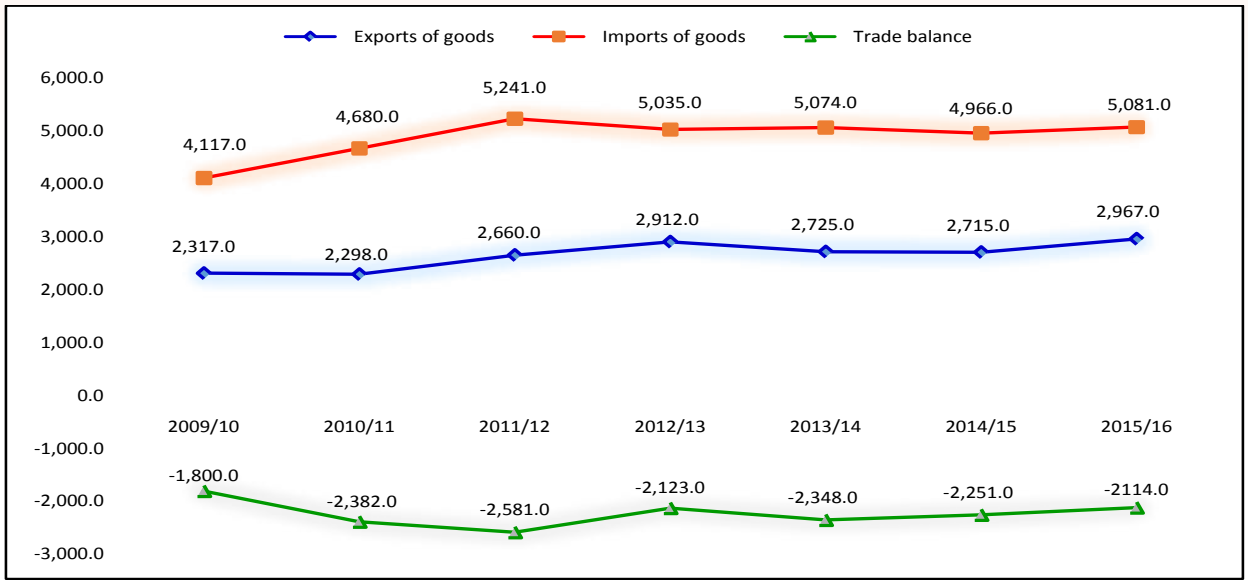
According to WTO (2016) developing nations and LDCs participation in the export trade declined in 2016, the global share of exports from LDCs fell by 6% leading to a decline in their overall share of global exports down to 0.94% in June 2017. Uganda's exports in the period 2015 to 2016 increased by US$ 215.30 million from US$ 2,666.13 million as shown in table 2 and figure 3.2 below. The growth in exports between 2015 and 2016 was largely driven by exports of agricultural and petroleum products. On the other hand Imports decreased to US$ 506.60 million in June from US$ 520.60 million in May of 2017. The main trading partners for Uganda have been Kenya, Rwanda, Southern Sudan, China, UAE and India. The trade deficit in June 2017 stood at US$ 224.40 million, The monthly Balance of Trade between 1993 and 2017 averaged US$ -142.09 million, reaching an all-time high of US$ 14.60 million in April of 1996 and a record low of US$ -431.20 million in December of 2015. Agricultural and petroleum products will in the near future become the major export product; Uganda currently has one of the largest oil reserves in the region estimated at 6.5 billion barrels (OIES, 2015).

Table 2: Summary of Uganda's Exports and Imports Statistics $'000 (2011-2016)

Trade Flow	2010	2011	2012	2013	2014	2015	2016
Informal Exports	528.34	355.84	453.74	421.29	414.59	399.13	419.24
Formal/Official Exports	1,618.60	2,159.08	2,357.49	2,407.74	2,261.96	2,267.01	2,482.31
Total Exports	**2,146.94**	**2,514.91**	**2,811.24**	**2,829.02**	**2,676.56**	**2,666.13**	**2,901.55**
Informal Imports	66.49	53.91	52.99	53.65	65.81	64.27	64.87
Formal/Official Imports	4,664.34	5,630.87	6,042.84	5,817.51	6,073.53	5,528.12	4,829.46
Total Imports	**4,730.83**	**5,684.78**	**6,095.83**	**5,871.16**	**6,139.34**	**5,592.39**	**4,894.33**
Trade Balance	**-2,583.9**	**-3,169.9**	**-3,284.6**	**-3,042.1**	**-3,462.8**	**-2,926.3**	**-1,992.8**
% change (Total exports)		**17.1**	**11.8**	**0.6**	**-5.4**	**-0.4**	**8.8**
% change (Total imports)		**20.2**	**7.2**	**-3.7**	**4.6**	**-8.9**	**-12.5**

Source; UBOS (2017)

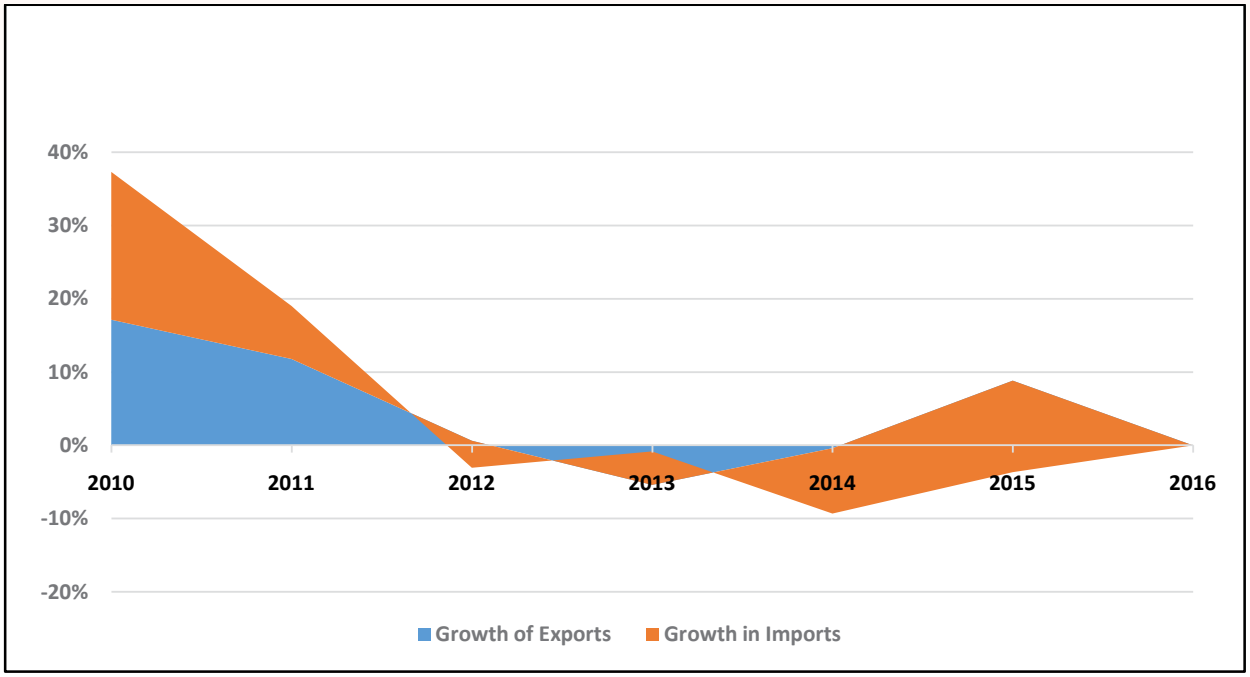
Figure 3.2: Uganda's International Trade story (2010-2016)



Source: National Planning Authority

There is a growing relationship between local production, export trade and GDP growth. According to econometric studies (Khaled, et. al., 2010), there is a positive influence of export growth on the GDP growth and economic development in both the short and long-run. It implies that promoting exports through a robust export promotion policies will contribute to overall economic growth which is reflected in the key indicators of economic growth. The gross domestic product (GDP) in 2015/2016 was US$ 23.1 billion, with a per capita GDP of US$ 754. The economy grew by 0.8 percent in the second quarter of 2016/2017, following a 4.8 percent growth in FY 2015/2016. Furthermore the economic growth is predicted to drop to 4 percent in FY 2017/18 due to global macroeconomic factors and a sluggish recovery from the national elections in 2016. In the medium term, Government projects are expected to average growth of 6 percent over the next five years, this prediction assumes a timely implementation of several complex multi-billion dollar infrastructure projects (Mutebile, 2017). The contraction in the economic growth and decline in exports is a partial indicator of contraction in local production in relative terms. The decimal performance of Uganda's external trade is consistent with the overall lower share of LDCs in international trade, however the country has the opportunity to benefit from the existing regional agreements to boost its export sector and improve the balance of payments. The overall decline in the percentage growth of exports in the last five years means Uganda must do more to actively promote and increase the value of its exports as shown figure 3.3. This can be achieved by focusing on high value exports like manufacturing products, services and processed agricultural products in place of raw materials. Similarly the decline in imports is attributed to the challenges the economy has faced since 2012, and not a result of imports substitution arising from increased local production or self-sufficiency.

Figure 3.3: Growth trends for Uganda's Exports and Imports in the last five years



Source: Extract from UBOS Data (2017)

3.4 Uganda's population growth and Implications to Export and Import Trade

Uganda has one of the highest rates of population growth, which has averaged over 3.0% in the last decade. The dependency ratio stands at 103%, these have combined to put strong pressure on the economy. The economy was projected to grow at 5.5%, but recent trends in the global economy and the national population dynamics have contributed to a decline in the growth down to 3.9% in 2016/17 (Budget Speech June 2017). This growth is higher than the average Sub-Saharan Africa growth rate of 1.4% in 2016/17, nevertheless it represents a decline in the overall performance of the economy.

According to the 2014, National Housing and Population Census, the youth form a large proportion of the population, 23% are in the age bracket of 18-30, while 55% are below the age of 18 years. The 65% of youth in the age bracket of 20-24 are unemployed, while 90% of those above 25 years are either unemployed or underemployed. This means their contribution to national production is marginal. In spite of the current population structure the (UDHS, 2017) report indicates a glimmer of hope towards creating and harnessing the demographic dividend. Recent statistics show that the fertility levels per woman have dropped to 5.4 children in 2016, the population growth rate down to 3.0%, while the infant mortality rates dropped to 45 per 1,000 live births and family size stands at 4.7 persons. According to NPHC, 2015 Ugandans are living longer with a life expectancy of 63.3 years and family planning access has also improved with unmet need in 2016 dropping to 28% from 34% in 2011. If this trend can be accelerated Uganda will be able to harness the demographic divided with appropriate policies will strengthen Uganda's position in international trade through increased local production as a precursor to growth in the country's export volumes.

The key question for Uganda today is whether the country can create a real demographic dividend and turn it into an economic advantage for sustainable growth. Uganda's population is projected to reach 41.2 million

by 2020, the working age group of 15 - 64 is expected to reach 22.5 million, representing 53.3% of the population. The major population characteristics from the 2014 Population and Housing Census shows a trend in declining family sizes, falling fertility rates, improved literacy levels and increasing life expectancy and but also a growing level of unemployment. This calls for concerted effort by Government and Development partners to tap into and turn these trends into a demographic dividend for Uganda. In theory, the demographic dividend can become an engine for national development and economic transformation at the micro level, this transformation can result in better living standards for families and higher incomes per person while at the macro level, it can lead to significant gains in the economic development of a country. This transformation should be anchored around the sectors with a greater multiplier effect on job creation and employment. In Uganda agriculture has been a key sector in job creation, employing directly and indirectly 80% of the working population, 68% of these employed in subsistence agriculture. Other emerging sectors are the services sector, petroleum (extraction sector) and the construction sector.

3.5 How Uganda can Harness the Demographic Dividend to promote exports

The demographic dividend is the economic growth that may result from changes to a country's age structure, due to the shift from people living short lives and having large families to living long lives and having small families (John Ross 2014). This change in age distribution means, fewer investments are needed to meet the needs of the youngest age groups and resources are freed up for what is called the *"Economic gift."* This means that the labor force is growing more rapidly than the population that is dependent, leading to rise in per capita productivity that results, in a window for faster economic growth and better family welfare.

Uganda can draw inspiration from the Asian Tiger economies like South Korea, Indonesia Singapore, Taiwan and Malaysia which have made significant gains in increasing local production and promoting export. Gaining a demographic advantage for development goes beyond making positive demographic gains, it requires implementing policies and programmes focused on skilling, creating job and trade opportunities and building institutions for good governance. The implications here are clear, the benefits of the demographic dividend are not automatic, and it depends on the proactive initiatives a country takes to productively engage its workforce, the nature of political, economic and social reforms undertaken and the commitment to effective resource allocation and good governance.

An example of a large family size with improper child spacing

Idle youth engaged in non productive activities

3.6 The Policy Framework and Environment to Boost Local production and promote exports

Uganda's trade policy gives the Government the primary role of eliminating barriers to trade, and providing an enabling environment for the private sector to thrive (Ministry of Trade policy statement 2007). The policy identifies the salient relationship and linkage between the trade, the productive sectors as key pillars for export promotion and domestic investment. The growing regionalization and globalization of trade means that countries are increasingly focusing on producing what they can produce with greater efficiency and importing those products they cannot produce with the same level of efficiency. The essence is to concentrate resources in the short-term to produce those goods where the country enjoys a comparative advantage over its trading partners. This happens even if a nation has the absolute advantages over a wide array of economic sectors. Employing a comparative advantage means focusing resources on those sectors where the total productivity gains are most significant, it is important to note that comparative advantages tend to be a temporary characteristic that can change with the evolution of labour costs and a nation's human resource. Uganda should also look at its factor endowment as a way of expanding the comparative advantage to promote its export sub-sector. Uganda's most basic factor endowments are; land and cheap labour (though mostly unskilled or semi-skilled). There is however need to gradually improve the labour factor endowment through capital and human resource investments.

The budget speech for the 2017/18 financial year highlighted the state of Uganda's economy in 2016/17. The growth in agricultural output slowed to 1.3% compared to 2.8% in in 2015/16. This was significant considering the proportion of agricultural export earnings. The slowdown was attributed to climate change effects, but critics have attributed it to

declining Government funding relative to other sectors which has constrained investments in climate smart and resilient technologies. The industrial sector growth dropped from 4.7% in 2015/16 to 3.4% in 2016/17, another key sector driving regional exports for Uganda. Besides the agricultural and the industrial sector, growth in the services sector which was one of the fastest growing sectors in the same period slowed down to 5.1% compared to 5.9% in 2015/16. Uganda seeks to attain the lower middle income status by 2020, the economy must generate US$ 17 billion more on top of the projected US$ 25.7 billion in the 2017/18 to realize this by 2020 with a capita income of US$ 1.039. The Government of Uganda identified key interventions needed to achieve this middle income status by 2020, top among these are; increasing production and productivity in the key primary growth sectors of Agriculture, Tourism, Minerals, Oil and Gas and Industrialization.

3.7 The Trade Policy Framework and Trade Agreements

Uganda as a member is bound by WTO and has signed up to regional trade agreements, these agreements prohibit protectionist trade policies through the creation of tariff and non-tariff barriers to protect the local industry. Uganda is also signatory to other regional trade protocols and global trade arrangements like Economic Partnership Agreements (EPA) with the European Union. Other trade agreements from which Ugandan exports can benefit include; the African Growth and Opportunity Act (AGOA) and enjoys the Most Favored Nation (MFN) trade status with the USA, which allows duty free access to the USA market, the China Free Trade Agreement, the India Free Trade Agreement and the WTO services waiver.

The Ministry of Trade, Industry and Cooperatives is mandated to promote external and internal trade and ensuring harmony with international and regional trade protocols. The Ministry is presently implementing the Buy Uganda Build Uganda (BUBU) campaign, the policy aims at increasing consumption of local products to boost local production and increase the competitiveness of local firms. BUBU is therefore a behavioral change campaign encouraging Ugandan consumer to choose Ugandan made products over competing imports. The policy objectives are spelt out in the strategic objectives which form the basis for the BUBU campaign which was launched in June 2015. The campaign is intended to stimulate and support local production by promoting the consumption of local products. Large infrastructure projects in Uganda and retail level businesses have focused on the use of imported products at the expense of local production. This has rendered Uganda's industrial and other production sectors less competitive both at home and abroad. The success of the BUBU campaign as a launch pad for exports will depend on the commitment from Government to improve the business environment, by building human resource capabilities, creating the infrastructure and cost effective energy resources needed to produce cost efficiently and the private sector positively working to improve the quality of Ugandan products to meet international standards. The goal is to ensure Ugandan firms become competitive both domestically and internationally.

Namanve Industrial Park, Kampala

In spite of the range of export opportunities established by the various trade agreements and the harmonized world trade system, Uganda's global trade is skewed towards imports and continues to suffer from a negative Balance of Payments. The Government has developed programmes and policy actions aimed at increasing local production and promoting exports to reduce the trade imbalance. The youth entrepreneurship is one of the key government initiatives towards economic transformation. This transformation can only be achieved if the Government can put in place policies and programmes that will help the country exploit its factor endowments. Uganda's basic factor of endowments include; Natural resources, Climate, central geographic location within the Great lakes region and the demographics. Government should further build capacity to create advanced factor endowments in form of better communication systems, skilled labor, research, and technology and education systems. These advanced factor endowments come as a result of investments by people, companies and Government enterprises. These should be accompanied by concerted efforts to develop suitable demand conditions, build related industries and a supporting macroeconomic structure.

3.8 Potential drivers of Uganda's Exports and Local Production

The need to align the national production strategies with the trade policy framework for export promotion is urgent in Uganda. Promoting exports and boosting the local production in key sectors is central to Uganda's Vision 2040 and industrialization drive. The goal of attaining lower middle income status by 2020 requires that Uganda's GDP must grow to US$ 42.7 billion by 2020 and a per capita income of US$ 1,039. Export trade is expected to be one of the key drivers of the lower middle income by 2020 agenda. It is projected that exports earnings must grow from the current US$ 2.3 billion to US$ 8 billion by 2020. Government has done well in negotiating many favorable bilateral and multilateral trading agreement, but evidence from our performance under the trade protocols such as AGOA and EPA shows that the country lacks the production capacity to

benefit from the trade opportunities created from these initiatives.

The primary constraint to exporting for Uganda is limited capacity to produce, and the resulting inability to sustain an export market. Lack of an operational and coordinated Government driven export oriented production strategy is at the center of this failure. Agriculture which accounts for 80% of our export earnings continues to receive marginal support in real terms, despite all the rhetoric from Government, agricultural production has remain largely at subsistence level with nearly 96% of production coming from subsistence farming.

A Typical Subsistence Farmer in Uganda

In the FY 2016/17 budget the sector received only 3.8% share of the budget, a trend that has persisted from previous years. Government has emphasized the push for industrialization and value addition as a strategy to boosting and raise the value of Uganda's export earnings, but the practical efforts towards industrialization are not anchored on the countries strategic advantage and factor endowment. Agriculture which is Uganda's main source of exports has averaged annual growth of 2.2% (The Agriculture Sector Strategic Plan 2015/16–2019/20), this is below GDP growth of 3.9% and the average annual population growth rate of 3.0%. Considering that the majority of Uganda's industry and industrialization potential is linked to agriculture, the poor growth in the sector means a slow pace of industrialization. The fact is demonstrated by the poor performance of Uganda's manufacturing sector, which consistently suffers from low capacity utilization due to persistent lack of raw materials, and high operational costs due to energy and utility costs. The vegetable oil sub-sector is a good example, despite the

enormous demand in the EAC, great Lakes region and the COMESA market, Uganda still relies on import of vegetables oils and crude palm oil to run its industries. The installed vegetable oil milling capacity in Uganda is estimated at 1,200 metric tonnes per day of sunflower and Soyabean (Uganda Oilseeds Sub-sector Platform 2013), the sub-sector is currently operating at 35% installed capacity due to shortage in the supply of sunflower and soybean. The leading factories and Mukwano Industries, Mt. Meru millers and others have resorted to importing and refining crude palm oil to boost capacity utilization.

The structure of Uganda's basic factor endowment and evidence from export earnings at 70% imply strategic investment in agriculture is needed to transform from subsistence to market or export oriented production is a pre-requisite to a successful export promotion programme. The Government policy on industrialization should take a systematic and logical approach build on sectors where the country enjoys a comparative advantage and have a shorter payback period. The investments cost for an initial industrialization programme anchored on the agricultural sector is bound to be lower. This is because of a shorter learning curve effects, due to a wealth of local/indigenous knowledge in agriculture and a potentially shorter learning curve to transit from subsistence to market oriented agriculture. Uganda spends over US$ 400 million on imports of rice and vegetable oil alone per year, yet boosting local production in these enterprises can have a strong import substitution effect and saved the country significant amount of forex. A typical experience of Uganda's industrialization challenge was captured at the Kingdom Rice factory, *quote"…..When we set up the factory, Uganda Investment Authority had told us that there was more than enough supply of rice in the local market. So we mobilized investors, got money and set up a rice mill in three months, but when we went out to buy rice, we bought on 50,000 metric tonnes of rice in two weeks and there was nothing more to buy…" an official from Kingdom Rice.* Typically small rice meals in Uganda operate for only 3 months in a year, the large commercial mills in Eastern Uganda; rely on imported rice and contract milling for traders from Kenya.

Another similar case is Uganda's performance under the African Growth and Opportunities Act (AGOA). These cases show the urgent need to address the production issues to harness export opportunities. According to the Ministry of Trade, Industry and Cooperatives data, Uganda's export performance under AGOA dropped from US$ 3.31 million (about Shs11 billion) in 2010 to US$ 1.15 million (about Ushs 3.9 billion) in 2014. Kenya by far the most successful EAC nation under AGOA accounted for 96% of the total exports in the region. Trade experts faulted the Government's strategy on AGOA which was not anchored on Uganda's comparative advantage. They have argued that Uganda should have integrated the Apparel production with the cotton production since the country was ranked as one of the best producers of cotton in world. The failure of Uganda to anchor its strategy on local production of cotton, and instead allowed Tri-Star Apparel firm to import cotton from Sri Lanka was a strategic mistake.

The key to promoting exports lies in Uganda identifying and prioritizing key production areas, adopting an integrated and coordinated production and export strategy and building the human resource capacity through skilling and job creation to provide the needed labor force to drive the production and industrialization programs. Transforming agriculture from subsistence to a market based farming system should be a primary entry point to increasing Uganda's productivity, industrialization and export promotion. Agriculture is a major anchor for the manufacturing, tourism and services sub-sectors, as well as the largest employer with a greater multiplier effect for every job created at any level of production and trade.

3.9 Challenges and Strategies for increasing Local Production

Local production in this context is defined in two ways; first it refers to the domestic production of goods and services by a country utilizing those products to meet local demand in place of imports. In this context local production works towards import substitution. Secondly, local production can be defined on the basis of the rules of origin as defined in different regional trade agreements. It can refer to the proportion of inputs (raw materials) originating from the domestic country that go into the production of a given product or the ownership, by either an international or national firm where the majority of its ownership should be national. Uganda can boost its local production capacity by adopting strategies that can boost production in key sectors for import substitution and creating surplus for export promotion. Despite past efforts by Government to increase production and promote exports through the modernization of agriculture, strengthening the services sector through infrastructure and skills development, promotion of industrialization and regional trade, Uganda has not realized the expected export levels. The critical challenges that must be addressed to increase local production and boost exports can be listed as;

a) **Systemic challenges**; the first challenge is in the areas of financing and payment systems, the flow of funding between payers and providers of goods and services, both public and private has been poor and a major constraint to business cash flows. Strategies to address the financing challenges in the our production systems should aim to reduce domestic arrears owed by Government to public and private firms which stood at Ushs. 2.25 trillion as at 30th June 2016 (Auditor General's report for the year ended 30th June 2016), improve financial transaction systems and financial dispute settlement mechanisms for national and international trade. Government should also put pressure on the financial system especially the banking sector to provide competitive and affordable credit for investment. The introduction of alternative financing instrument accessible by the public can force commercial finance providers to become more efficient, adjust interest rates and reduce the cost of borrowing. Financing models built on equity financing, patient capital (development) financing and capital markets development can provide competitive pressure on the commercial credit institutions to adopt a more competitive pricing of credit facilities.

Secondly the human resource challenge, characterized a limited skill pool in the available labour force, lack of a systematic human resource skilling strategy and deployment of the available human resources. Notwithstanding the shortage of skilled labour, much of the existing skilled labour is concentrated in major centers like Kampala or are deployed inappropriately in jobs where these skills are underemployed. Take the example of Uganda's agricultural graduates at certificate, diploma, degree and higher degree levels, the number of them engaged in farming is insignificant, instead agriculture has been left to the uneducated and the old folks in villages. Uganda must come up with a clear educational and skilling policy that provides a proper balance between theoretical and conceptual skills and applied technical or vocational skills. Uganda's formal educational system remains one of the most competitive in the region. Despite this it has faced internal criticism, for its inability to deliver employable graduates. The major gap exists in skilling, there is no mechanism to help the human resource transform conceptual and theory knowledge into practical solutions to address national and community problems. Successful educational systems have

a strong apprenticeship and internship programmes which are mandatory for all graduates at various academic levels supported by a robust vocational training system. They also have a national agenda for research and mechanisms for the transfer of knowledge and technologies generated from research to the users for adoption.

Thirdly systemic constraint relating to infrastructure, poor infrastructure such as feeder roads, reliable access to electricity, and communication networks have limited productive capacity especially in peri-urban and rural Uganda. Infrastructure is vital for the management of core logistics needed for production, buying and selling products and services to viable markets (local, national and international). Government should priorities investment in the creation of relevant infrastructure along the major production corridors, while this can be a highly capital intensive investment, the cost of lost production more than justifies any capital investments required.

b) **Policy challenges;** there is lack of clarity in Government policy towards local production due to uncoordinated actions from different Government ministries and departments charged with the responsibility of implementing Government policy. Uganda Investment Authority has not been able to put together marshal plan for coordinating action from the various Government agencies towards promoting local production. Government investment and production policies have been severally criticized for favoring foreigners over locals. At the same time foreign investors are allowed handsome tax holidays, 100% repatriation of profits and Government subsidies. The policy on 100% repatriation of profits denies the country of the increased production that would arise from re-investment of profits. Other unfavorable regulatory and tax mechanisms undermine the motivation to invest and produce with small entrepreneurial enterprise suffocated at their nascent stages. The recent drive by KCCA to clean up the city by evicting micro business without providing alternative business centers was criticized and rightly so because it led to loss of many business that could grow into tomorrow small and medium scale or even multi-national corporations. Government policy should look into promoting local enterprise by providing business safe havens and incubation centers for emerging micro-enterprises to compliment and provide services to the large corporations. Only then can Government strive to promote local content be a reality.

c) **Organizational challenges;** high business start-up costs, inadequate financing for early-stage entrepreneurs are some of the factors that constrain innovation and production in Uganda. Production and innovation processes are associated with their own range of technological and market-related uncertainties. Start-up companies or business ventures are seen as high risk; credit finance providers are reluctant to finance them. When they do the interest rates, the cost of capitalization are very high and the loan periods too short to realistically allow the business to generate the return needed to repay the loan. Rural enterprises in particular tend to be considered risky investments because of investee profiles of relative poverty and limited access to resources. Indeed, access to financing and early-stage capital often figures prominently on the wish list of entrepreneurs, and among the obstacles to becoming an entrepreneur. However, while early-stage financing is important, it is equally important to ensure that entrepreneurs have access to credit throughout the business life-cycle. Government should seek to build a robust business ecosystem; a robust ecosystem requires financial organizations that understand the various

stages of a business growth cycle. It is no coincidence that the nations that offer financial assistance to all stages of business life cycle also have the largest concentrations of large-scale businesses within their borders. These businesses tend to have a relatively greater impact in increasing a nation's GDP than the sum total of micro-, small-, and medium size businesses combined.

The lack of a robust business ecosystem in Uganda is responsible for a combination of weak production capacity and uncertain markets, which together results in limited economies of scale. For example, manufacturers in Uganda generally produce at a cost disadvantage compared to the large Asian generic manufacturers (i.e. in India and China). A shirt from Taiwan or Indonesia costs 50% less than a shirt made in Uganda. Political, legal and regulatory barriers have often made it difficult for local producers to exploit regional economies of scale. Local production facilities operate in unfavorable environments which increase basic operational costs and impede the quality of products. Government should consider setting up cluster technology parks and special economic zones where entrepreneurial ventures can be natured and local production facilities established.

d) **Partnerships and other challenges;** frequently, ambiguous policies and lack of policy coordination between various relevant ministries, departments and agencies (MDAs) have meant Government has failed to build collaborative linkages with Government programmes and between the different industries and supporting industries within the economy. This is a major barrier to meaningful and sustainable local production. Competing agendas of Government organizations, lack of a collaborative culture between the productive sectors, the policy organs and the academia, is responsible for lack of access to knowledge and resources for innovation. Technology transfer may be very difficult to induce, particularly for products where technology holders and users are likely to be market competitors. In such cases, public or public interest collaborative structures featuring Government institutions, foundations and NGOs may play a stronger role in providing incentives for sharing, or alternative paths to access needed technologies. Government should provide an enabling environment to support the growth of viable Public Private Partnerships which can provide the collaborative structures to support diffusion of knowledge, innovation and national capabilities to produce.

In taking a strategic view the Government of Uganda and the public should focus on deploying the proposed strategies to address the barriers to increasing local production as outlined above. Dealing with these barriers will enable proper focus on sector specific strategic actions in each of the identified potential export sectors; Agriculture, Manufacturing and Service and Tourism.

3.10 The Agriculture Sector

a) **Adoption of location specific interventions and specialized enterprise approach to increasing agricultural production.** Location specific interventions are more likely to have a greater impact increasing agricultural production than national wide intervention. These together with enterprise specialization based on the agro-ecological zoning of the countries production areas would enable more focused activities to promote and increase production of selected industrial and export commodities to deliver on the countries import substitution strategy and the export promotion strategy.

b) **Invest in improving the quality of farm labour force and support structures;** Government must begin to priorities the

agricultural sector both in word and deed. The most skilled labour force in agriculture is not engaged in farming and the labour force doing farming lacks the requisite skills or tailor made facilities and programmes to acquire these skills. Government policy and action to increase agricultural productivity should be directed towards building and strengthening linkages between knowledge systems (research and technology development), skills and technology transfer and functional community agricultural extension and learning systems. The African Institute for Strategic Animal Resource Service and Development (AFRISA) in Makarere University has pioneered an academic programme build on development and transfer of usable skills through practical training and incubation as an alternative to the traditional class based training programmes and it has born results in places like Bushenyi in Western Uganda.

c) **Mainstream agricultural education in Uganda's vocational training programmes to motivate youth to take up farming as a business;** Youth have the energy to make a difference in country like Uganda where labor intensive agriculture is practiced. Youth also have the ambition and motivation to adopt new technologies, explore knowledge and build a carrier. A specialized fund in the line of the youth livelihood fund should be put in place as stimulus to support youth who choose to engage in specific priority export based production. Such support should focus facilitating youth to invest in agriculture through tailored skills and apprenticeship or incubation programmes similar to AFRISA programme, input credit financing and acquisition of farm management technology.

d) **Support and strengthen cooperatives as vehicles for delivery of agricultural productivity enhancement support;** for Uganda to make a successful shift to manufacturing as a key export earner, we must transform our agriculture by tripling or quadrupling yields of trade able farm commodities to feed the industries. Government and key stakeholders should go beyond talk and focus on the following interventions to transform Uganda's agriculture by creating structures for aggregation in order to build production and market economies of scale in smallholder farm settings.

Bugisu Cooperative Union Limited Coffeee Processing Factory in Mbale Municipal Council.

e) **Strengthen research in high-yielding and marketable varieties;** increased research into plant breeding to produce varieties suitable for the unique soil types of Uganda and its agro-ecological zones is needed. Rice for example is widely consumed in Uganda and 60% of local consumption is imported. While Uganda is capable of producing rice to meeting its local demand and produce surplus for regional export, average yields of local rice varieties under good agronomic management is 2.5-3.0 metric tonnes per acre. This compared to countries which export rice to Uganda such as India, Pakistan, Indonesia, Cambodia, Vietnam and Egypt which register yields of 6-10 metric tonnes per acre of milled rice. The difference in yield under the same level of management practices is attributed to the quality of genetic material used.

f) **Build agricultural production and climate resilience infrastructure; Uganda's agriculture is rain fed and suffers severely from any short-term variation in climatic conditions.** The growing effects of climate change on weather patterns, is changing farming patterns across the country. To allow the predictability and consistency in production demanded by markets, irrigation is an inevitable condition for reliable production. Uganda's agriculture will never realize its potential unless irrigation systems and post-harvest handling infrastructure is developed to increase productivity, stabilize production patterns and reduce post-harvest losses.

g) **Promote use of productivity enhancement technologies and use of fertilizers; soil exhaustion due to over use and poor management resulting in erosion is a major factor in some parts of Uganda today. Government must put in place incentives and improve access to fertilizers by smallholder farmers. Major constraint to fertilizer use is the availability, price and knowledge gaps. Strengthening information systems through ICT use c**an support better crop, fertilizer and pesticide use and selection. It can improves land and water management, provides access to weather information, and connect farmers to sources of credit.

h) **Reform land ownership with productivity and inclusiveness in mind; Uganda** has one of the highest percentage area of arable uncultivated land in Africa yet most farms occupy less than 2 hectares. This results from poor land governance and ownership systems; what Government needs to do is create genuine land reforms that clearly define property rights, ensure the security of land tenure, and enable land to be used as collateral. This will enable increased flow of investment finance towards increasing agricultural production and growth of related industry.

i) **Step up integration into Agricultural Commodity Market Value Chains (ACMVCs); d**riven partly by the growth of local and international supermarket chains, and export opportunities. Ugandan farmers have progressively diversified from traditional cash crops into non-traditional crops for income like; sesame, soybean, sunflower, fruits, vegetables, fish, and flowers. However the failure to master production efficiencies and access investment finance alongside other constraints has slowed progress and growth in acreage for most of these commodities. Government support is crucial to coordinate the integration of smallholder farmers into larger cooperatives and producer organizations to create production and market economies of scale and integrate with global and national markets.

3.11 Industrialization and manufacturing sector to advance value addition

Government policies in Uganda encourage and support investment operations, particularly in value-added manufacturing and agro-processing. Growth of the manufacturing sector has been undermined by dependency on imported inputs/raw materials, low capacity utilization. The factors that contribute to low capacity utilization have been well articulated in the National Development Plan I & II. These include credit rationing, limited skills and inadequate infrastructure and high energy costs and availability of inputs/raw materials. Start-up manufacturing operations are extremely susceptible in Uganda, there are many graduates and artisans with potential to start-up enterprises or better improve on their product production processes and prototypes if technically supported. Innovation and the transformation of new product concepts into marketable products is the weakest link in Uganda's industrialization plan. It's important to note that, to be competitive in the domestic and international markets (export markets), Ugandan industries need to build capabilities, advance value addition, quality and standardization. Abundance of raw natural resources and or cheap unskilled workforce are no longer sufficient to sustain industrial competitiveness and growth. The manufacturing sector growth trend and rate of industrialization can be improved if Government considered some of these proposed action.

a) **Strengthen mechanisms for technology transfer and absorption from the developed countries, either by attracting FDIs or improvement of the business environment to promote local investments**; to produce at a competitive level our industrial sector must upgrade production systems, realize technological improvements and adopt cleaner production technologies, invest in skills development and employ skilled and experienced human resource personnel. The FDIs will benefit Uganda in this direction if Government puts a deliberate policy to improve the local human resource by requiring the transfer of foreign expertise into the hands of local citizens through a skills development and apprenticeship plan. It should be a requirement for investors to show how they will implement this requirement as a condition for granting an investment license.

b) **Promote R&D and cluster based industrial development strategies**: A new approach to doing business and economic development planning to compete globally is the Industry Cluster concept. The cluster model emphasizes internal linkages, where cluster gains are furthered by local firm cooperation, local institutions, and local social capital. External linkages also matter, global buyers can help local clusters access distant markets, acquire new forms of knowledge and upgrade. Porter (1998) argues that it is the competition between rival firms in the cluster that drives growth because it forces firms to be innovative and to improve and create new technology. This, in turn, leads to new business spin-offs, stimulates R&D, and forces the introduction of new skills and services. In short, cluster development is attributable to several benefits, including technology transfer, knowledge transfer, development of a skilled labour force in related industries, the benefits of agglomeration economies, and social infrastructure. The Government should further the creation of serviced regional industrial parks similar to Namanve to encourage cluster formations and the creation of high level value chains.

c) **Formation of a national business and industrial incubation networks**; A national incubator networks accelerate and nurture innovations (social as well as technological). This increases the

resilience of the national economies and firms or societies to respond to uncertainties. Incubators should act as entrepreneurship and technological information hubs and consider themselves as service providers. The incubators should further be important partners with the youth and SME entrepreneurship programmes that should act as the pre-incubator phase in the incubation and industrialization process.

Collaboration increases interaction between entrepreneurs and universities/ research institutions to advance innovation and entrepreneurship development. Institutions like Africa Institute of Strategic Animal Resource Service and development (AFRISA) in Makerere and existing big companies are a source vital knowledge and experience that can be tapped to develop a functional national incubation program. Government should also address the problem of protection of intellectual property in order to foster confidence in the incubation programmes. The weak laws on the protection intellectual properties and rights of owners of intellectual assets have a major concern in Uganda.

d) **Structural Transformation and improvement of the business environment**; A successful manufacturing sector requires a business-enabling environment. This includes the organizational, support institutional and physical infrastructure, human capital, financial systems, technology and innovations. Structural transformation should work to increased forward and backward industry linkages to eliminate systemic inefficiencies in the manufacturing sector. Government initiatives towards securing favorable financing for infrastructure development should be backed by a strong commitment to public–private-people partnerships (PPPP) to leverage the growth of the proposed forward and backward linkages.

3.12 Challenges and Strategies for Promoting Exports

Export trade refers to the sale of goods and services across national borders, Export promotion means an active process by a nation to engage with its local production systems to produce for the export market and foreign institutions or Governments to advance the export of a countries output. In Uganda, the Uganda Export Promotions Board is the Government organ charged with championing Uganda's export agenda. Government has initiated a number of bilateral and multi-lateral trade agreements which have paved markets for Uganda's products. However, the actions taken to build capacity to produce and exploit trade opportunities provided by these agreements has lagged behind. Critical actions needed to promote exports should include interventions at both production and the market end.

a) **Trade financing through availing affordable credit.** The availability of short and long-term credit for trade finance is a necessary condition to build a national export platform. Countries like Japan rapidly grew their exports in the aftermath of world-war II by creating a credit mechanism to finance export ventures. The need for trade and export financing is a decisive intervention that Uganda should make targeted at the small and medium enterprises (SMEs). The SMEs make up the large majority of firms in developing countries and grow into future large corporations. Improvements in the SME domain are necessary to achieve realistic growth of exports. Trade financing is useful to manage the effect of the export payment cycles which leads to delay in the realization of cash and does not favor small and medium business enterprise.

b) **Improving cooperation among economic actors.** A part from applying traditional policy instruments, export growth could be favored by improving cooperation among exporters and

between the Government and business actors. There is a global trend towards using export consortia (such as export associations and cooperatives) to support SMEs access the international markets. This may be seen as a complement to other forms of Government intervention, but also improve the image of Ugandan exporters abroad by providing a confidence bridge to the importers intending to buy Uganda products.

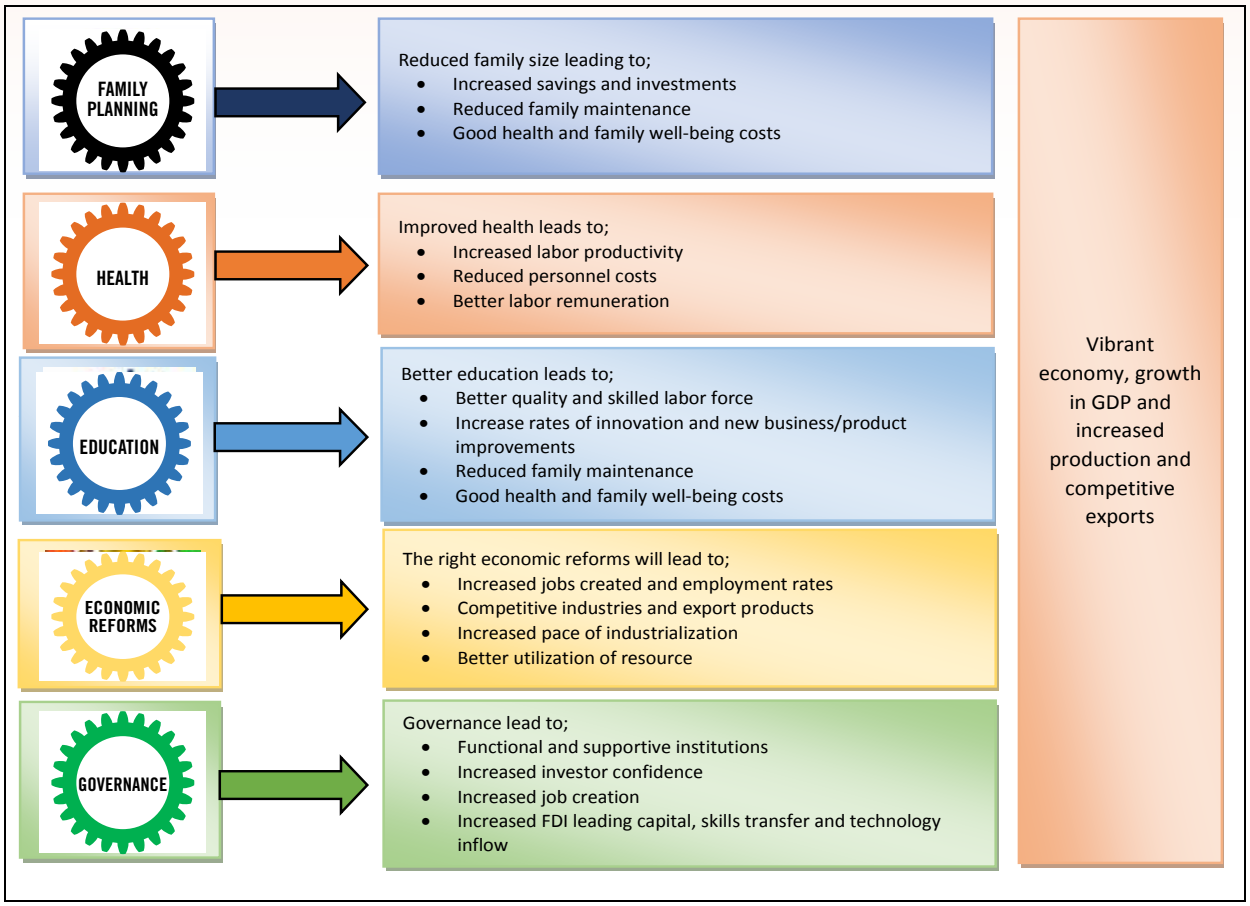
c) **Combining short-term and long-term export growth policies.** The stimulation of export growth requires the combination of short- and long-term policies. In this context, it is important to also exploit the complementarity between export promotion policies (EPPs) and other domestic policies which aimed to increasing productivity, adoption of technology and industrialization.

3.13 Linking Investments to Local Production and Export Promotion

The economic benefits that accrue from export trade are not disputed, but there have been arguments against building an economy entirely dependent on exports. The risks can be both geopolitical and economic. Many successful and developing economies have a good balance between domestic market absorption and export trade. Sustainable investment requires linking investment to local production and export promotion targeting investments in sectors which have a domestic market to absorb a significant volume of local products. The surplus produced can be traded in the export market; domestic markets provides local firms with a local market safety net and a strong platform to venture into the foreign markets.

There is a strong link between a nation's investments, local production capability and the countries demographic structure. Where a country has a demographic dividend and puts in place favorable policies to harness this dividend, local production is boosted and surplus is created for export. This in-turn attracts more investments into the productive sectors and creates a multiplier effect which leads to growth in production outputs and export volumes. In the linkage of production to the demographic dividend, there are four pillars the Government must pay attention to the highlighted issues in figure 3.4 below

Figure 3.4: Link between the demographic dividend pillars with local production and export promotion and competitiveness



Increased production can be achieved by creating job openings for skilled, semi-skilled and unskilled to absorb the majority of Uganda's youth population. The economies of South East Asia relied on employment opportunities from export-led industries in the manufacturing and service sectors. Uganda needs to explore economies of comparative advantage that take advantage of the increasing economic integration and the emerging global opportunities in ICT, the extractive and agro-processing industries to accelerate and grow its export base. Some policy actions to bring this about are summarized in the section below.

3.14 Conclusion

The Government of Uganda has negotiated and signed up to several regional and international trade protocols that have created markets for Ugandan goods. The failure to exploit these export opportunities lies in the countries low capacity to produce for export. This situation is reflected in Uganda's negative balance of payments account. The negative balance of payment could have been avoided if the country reduced on its imports through import substitution in those areas and commodities where we have abundant resource endowment like agriculture. Similarly the country could increase its volume of exports if we exploit our comparative advantage. By increasing the flow of investments towards the sectors which have a strong import substitution effects; we can build capacity to increase production through industrialization, improve human capital development and export of value added products to meet domestic market demand, and generate surplus output for the export market. Government should pursue a policy of import substitution and export promotion through a targeted investment

programme to promote internal and external trade in sectors that can create "static economic gains" like agriculture, tourism and manufacturing. The current emphasis from Government has focused on investments in sectors like the extractive and construction (infrastructure) sectors, these sectors create transient but not static economic gains and if not anchored on a sound economic model built on sectors that create "static gains" it will result in growth in the short-term, but the growth realized will dissipate in the long-term.

3.15 Policy Recommendations

Strengthening the capacity to produce for export is key to any export promotion campaign. Uganda's inability to take advantage of international trade opportunities like AGOA is attributed to failure to produce enough products of the correct quality standards demanded by the destination export markets. To realize Uganda's socioeconomic transformation into a lower middle income status, government should seek to transform the predominantly subsistence approach to production to a market led production systems. Government must adopt policy options that can drive production, internal trade and export trade. Suggested policy option below should be considered in line with government's efforts to increase local production and promote exports.

1. **Government should adopt import substitution as a major element of trade policy and a spring board for industrialization to achieve increase in local production.** Government should adopt the policy of import substitution for selected commodities and sectors where Uganda can enjoy a comparative advantage. The import substitution should be focused on industries which can consume raw materials readily produced in Uganda. The challenge today is dependence on imports of commodities even in sectors where Uganda has a naturally or absolute advantage because of the low capital investment in required production infrastructure. Targeted import substitution policy would channel more capital resources towards expanding local capacity to produce these commodities like rice, vegetable oil, textiles for which we have abundant resources to produce but lack the capital resource. The policy could also encourage inflow of external capital for investment towards sectors earmarked for import substitution. This policy can be implemented without employing protectionist measures that could compromise Uganda's participation in export markets, but by making investments that increase local production efficiencies to render Ugandan goods more competitive than similar imported substitutes.

2. **Establish an export oriented policy on improving the quality of the human factor;** for Uganda to improve the quality its laboru force there must a good balance between vocational and professional training. This requires building education and institutional structures and system equipped with capacity to deliver skills and knowledge development programmes relevant for the country production and exports needs. High-quality skills that will make more productive workers and position the country to be competitive in the global market are a pre-requisite for export promotion. This demand that Government diversifies the educational programmes to include others form of skills

development besides professional and vocational training. These may include development and accrediting apprenticeship training programmes, mentorship and incubation and learning centers. This is critical to developing higher level skills in innovation and creativity. The Government policy of promoting science education at the expense of business and social science education is counter productive in a long-run as it deprives the country of the vital soft skills to manage business growth and entrepreneurial transitions.

3. **Establish an innovation, entrepreneurial and industrial development policy;** replicating the Namamve model to establish serviced industrial parks and business incubation centers in other regions of Uganda. The greater part of Uganda's industries are concentrated within a 50 km radius from Kampala, often far away from the source of raw materials. Together with an inefficient transport system, this has increased the cost of production and reduced the competitiveness of Uganda's manufactured goods in the regional and international markets. Poor infrastructure further away from Kampala together with poor services and supply of utilities has discouraged investors from setting up industries outside the greater Kampala zone. The industrial park in Lira dominated by vegetable oil milling factors is testimony how industries can stimulate local production for supply of raw materials. Lira and the vicinity of Acholi sub-region have been major production hubs of sunflower and soybean spurred by the demand from the industries. This should be stimulated in other regions targeting specific commodity based agro-industries and support the local production systems to produce and supply sufficient raw materials for the industrial demand.

4. **Develop an investment policy to prioritize investment in sectors that can drive exports and support industrialization**. These should be identified and aligned with Uganda's comparative advantage in region. These sectors should be strengthened to form the springboard for Uganda's economic transformation. Agriculture, tourism and services are sectors Government has already identified as key to Uganda's exports and foreign exchange earners. What is required is to deliver real support through budgetary allocation, programme implementation and technical assistance to ensure that productivity in these sectors is increased to commercially competitive levels. Developing water for production sites for agricultural production to transform Uganda's agricultural from rain fed can unlock investments in the sector that will result in the increased utilization of fertilizers, better quality planting material and recommended pest and disease control technologies. The uncertainty that comes with rainfall patterns is the one major factor that constrains investments in farm production, adoption of technologies and transformation from subsistence to commercial or market led agriculture.

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Chapter 4: Enhancing Agricultural Productivity and Commercialization to Harness the Demographic Dividend

Agricultural Mechanization in Kigumba – Kiryandongo District.

4.1 Introduction

Africa, and specifically sub-Saharan African region, has experienced rapid population growth in the recent past. Uganda's population growth rate (3 percent per annum) is the second in the world. In addition, Uganda has the world's youngest population with over 78% of its population below the age of 30 (UBOS, 2016). In 2014, the total population of Uganda was estimated to be 34.6 million people with the majority (56.7%) being children aged less than 18 years. The youth also form a significant proportion of the country's total population; 18.4 percent of the populations are youth aged 18 – 30 years, while 16.6 percent are aged between 15 – 24 years. Additionally, in Uganda, the youth constitute a significant proportion (57%) of the total labour force and most of them (79%) live in rural areas where poverty levels are relatively high and agriculture is the major economic activity (NPA, 2015).

4.2 Background

Agriculture is the core sector of Uganda's economy. It presents a great opportunity for poverty eradication because it employs over 80% of Uganda's labour force. However, subsistence agriculture is still predominantly practiced at 69% in Uganda, leading to low productivity and earnings from this sector. Agriculture remains the backbone of Ugandan economy because contributes 40 percent to the total goods export earnings and 22 percent to GDP (UBOS, 2016). The sector is also a major source of raw materials to the local industries and, being the largest employer, the majority of women (about 73

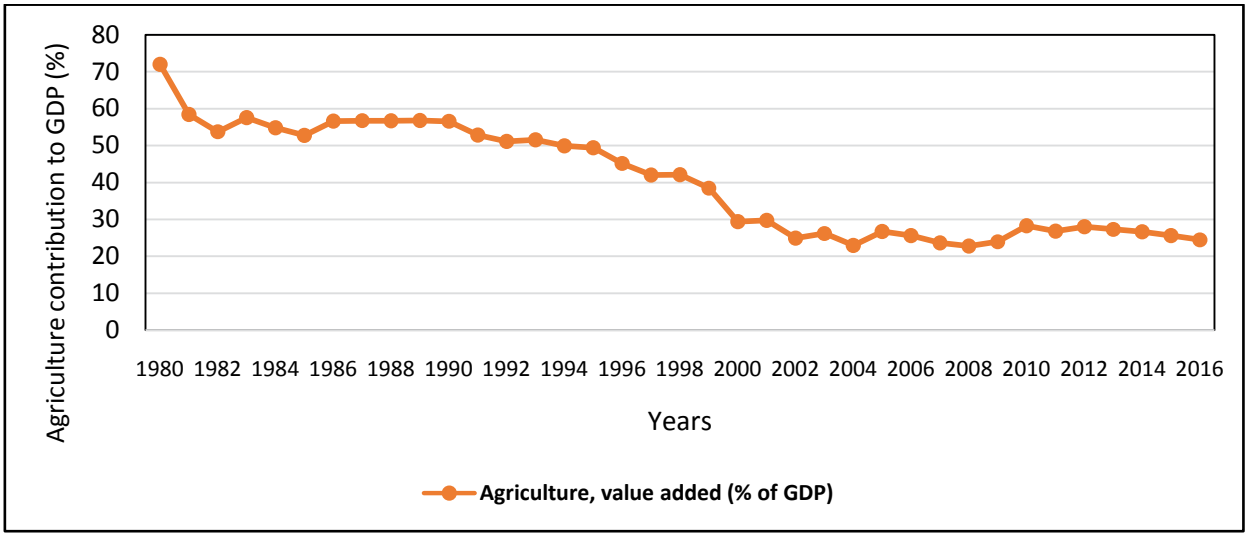
percent) are employed in agriculture as primary producers (UBOS, 2016). Agriculture, hence, has the potential to be a driver of economic growth and poverty reduction in Uganda (MAAIF, 2013). Applying modernized agricultural practices will generate a number of productive jobs in agriculture and allied industries and provide an opportunity out of poverty for many.

Youth unemployment remains high at 11.1% in Uganda and it is higher than the national average unemployment rate of 9.4%. It is higher among females than males; the proportion of female youth of working age who are unemployed (13.7%) is higher than that of male unemployed youth (8.9%) (UNDP, 2015). According to EPRC (2015), 13 percent of youth aged 15 – 29 years are unemployed while 63 percent are underemployed. Since the majority of the youth live in rural areas and are employed in agriculture, efforts should be geared towards enhancing agricultural production and productivity so as to transform the sector from the subsistence to commercialized agriculture.

4.3 Growth and Trends of Agricultural Sector in Uganda's Economy

While Agricultural sector is critical for employment, food security and export earnings, the share of the agriculture in the structure of Ugandan economy has significantly declined over time as show in figure 4.1 below. For instance, the share of agriculture to GDP was 72 percent in 1980 and 57 percent in 1990, and not it stands at about 24 percent. The sharp decline in the share of agriculture represents a significant structural transformation with the economy shifting towards service and industry sectors.

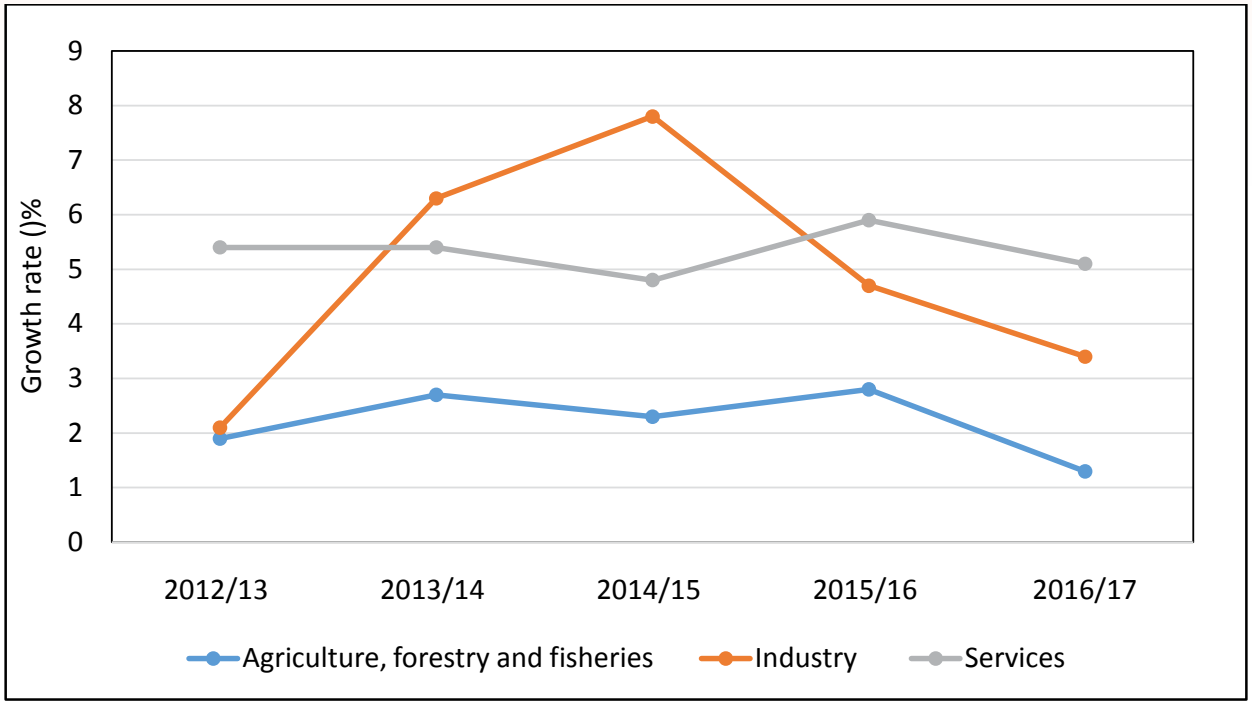
Figure 4.1: Trends in the Agriculture, value added as percentage of GDP (1980-2016)



Source: By authors using World Bank's development indicators data

The country is also grappling with measures to enhance agricultural productivity, competitiveness and export growth. To achieve that, farmers have be supported to practice commercial farming and not small scale production for only home consumption. This, thus, requires that agriculture is conducted as a business and not as a tradition. Because agriculture is still practiced in a traditional context with limited use of technology, the agricultural sector has experienced a dismal performance with growth that has stagnated at about 2 percent for almost two decades. In addition, the agriculture sectoral growth is lower than other sectors (industry and services) as shown in figure 4.2 below.

Figure 4.2: Growth rate of different sectors in Uganda (2012-2017)



Source: Background to the budged, 2017/18

Disentangling the growth rate for agriculture sub-sectors from cash crops, food crops, livestock, fisheries and forestry reveals that the growth of cash crops has been highly volatile signaling the limited performance of commercial production as shown in table 3 below. The forestry sub-sector has had a high but volatile growth. The dairy sector has also enjoyed a positive and steady growth for the last 5 years, but registered a decline in 2017.

Table 3: Growth rate of Agriculture Sub-Sectors

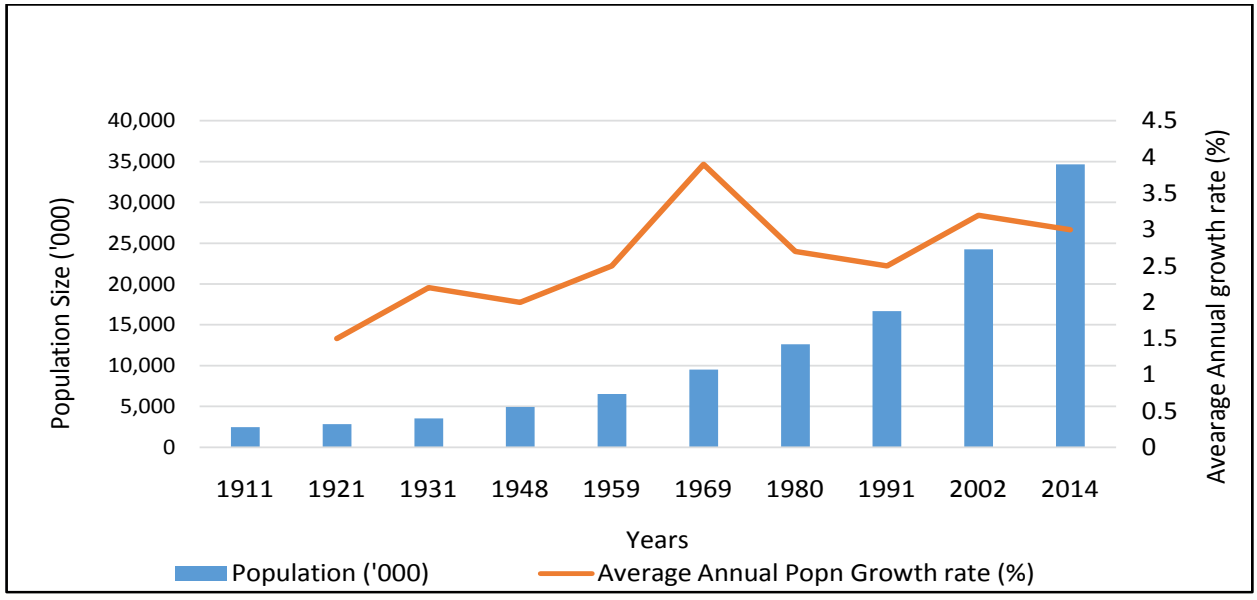
Year	2012/13	2013/14	2014/15	2015/16	2016/17
Agriculture, forestry and fisheries	1.9	2.7	2.3	2.8	1.3
Cash crops	-0.1	-0.3	4	7.9	-0.4
Food crops	-0.3	2.9	2.2	1.3	1.4
Livestock	2.5	2.7	2.9	2.8	1.6
Forestry	11.2	3.5	1.7	4.7	1.2
Fishing	-3.5	2.1	1.5	4.8	2.2

Source: Background to the budget 2017/18

Dairy Farming in Western Uganda.

The overall agricultural growth rate is lower than the population growth rate of about 3 percent per annum, signaling the likelihood of food insecurity and increase in poverty incidence (UBOS, 2016). The increase in Uganda's population overtime calls for increased investment in agriculture and food production through enhancing technology which would increase the productivity as shown in figure 4.3 below.

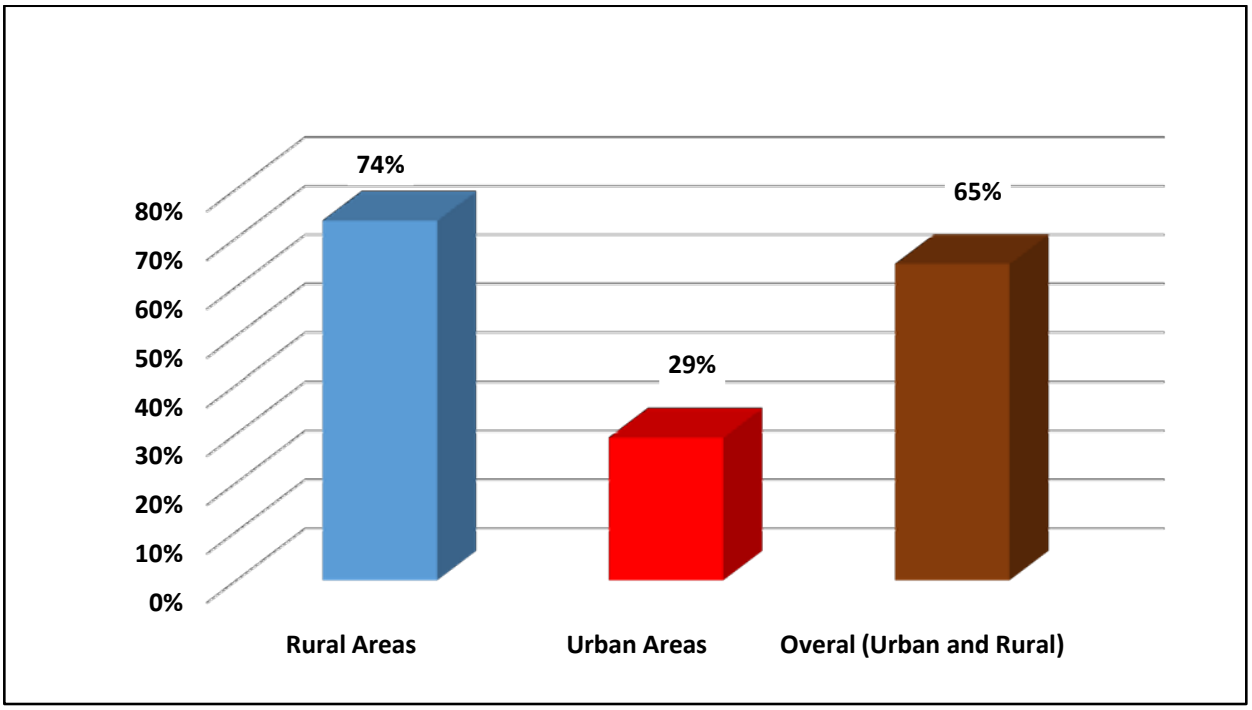
Figure 4.3: Population Size and annual population growth rate for Uganda



Source: Own computation using data from 2014 National Population and Housing Census Report

Because of low productivity resulting from the low technology investments in agriculture, a large population participates in subsistence production which constitutes about 69% of the total population. Figure 4.4 below shows that 74% and 29% of the working age population in rural and urban areas, respectively, practice subsistence farming.

Figure 4.4: Percentage of Ugandans aged 14-64 that are working in Subsistence Agriculture



Source: Own computation using data from 2014 National Population and Housing Census Report

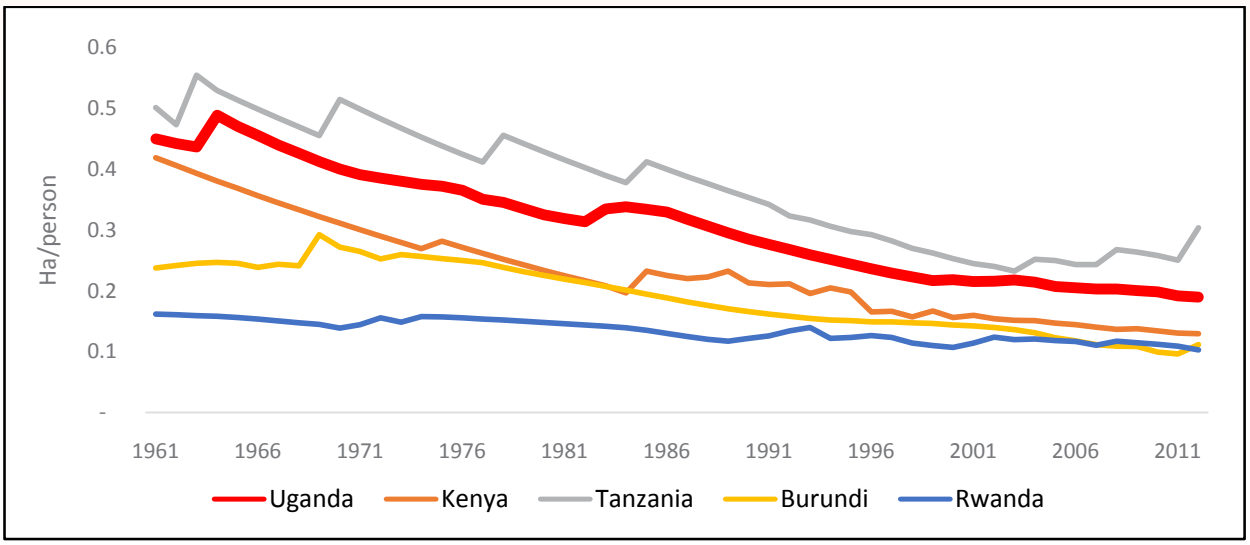
The poor performance of agriculture sector thus calls for workable interventions, and innovations to transform the sector. These interventions should range from strengthening agricultural related institutions, enhancing agro-input use, curbing land fragmentation and land conflicts, enhancing agricultural research and development, and strengthening extension provision systems. These, among others, remain the major hindrances to a better agricultural performance as discussed below.

4.4 Factors affecting Agriculture Performance

4.4.1 Low Technology Adoption

Despite the fact that land is increasingly getting scarce as indicated by the average land holding of 1.1 hectare per household, Ugandan farmers still practice extensive farming and apply less of modern agricultural technology such as fertilizers, use of improved seed, irrigation and mechanization. The decline in land holding size is not a problem for Uganda only, figure 4.5 below shows a comparative situation in other East African countries where the land holding size especially in Tanzania and Kenya decreased from 5 and 4 hectares per person in 1961 to 3 and 1 hectare per person in 2011 respectively.

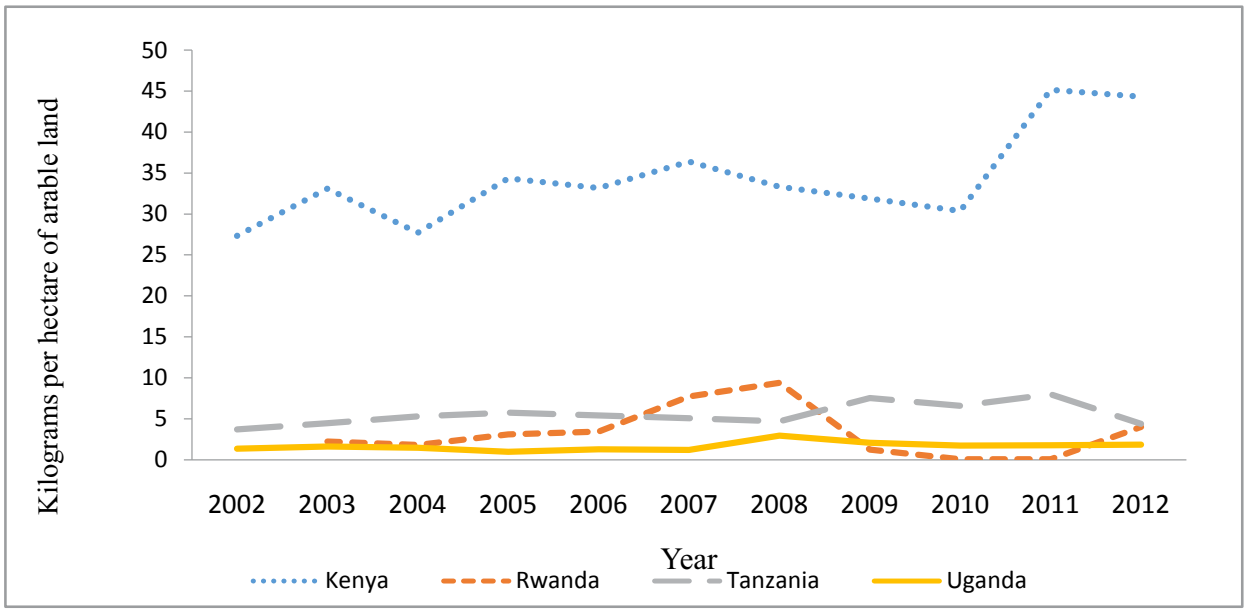
Figure 4.5: Trends in Arable Land holding per Person in East African member countries



Source: Mwesigye, Sserunjogi, and Mbowa, 2017

In order to enhance production despite the decline in average land holding per household, farmers have to adopt modern agricultural practices such as use of fertilizer and improved seed, and irrigation to guard against the effects of climate change. However, this seems not to be materializing in rural Uganda. For instance, in 2014, 85% of farmers reported that they used no fertilizers and planted local seed, while about 6.5% of farmers combined used fertilizers and improved seed on their plots, suggesting very low levels of intensification. Indeed, Uganda trails her neighboring countries in terms of fertilizer application as shown in figure 4.6 below.

Figure 4.6: Fertilizer Use in East Africa (2002-2012)



Source: By authors using World Bank's development indicators data

Mechanized Rice production in Eastern Uganda.

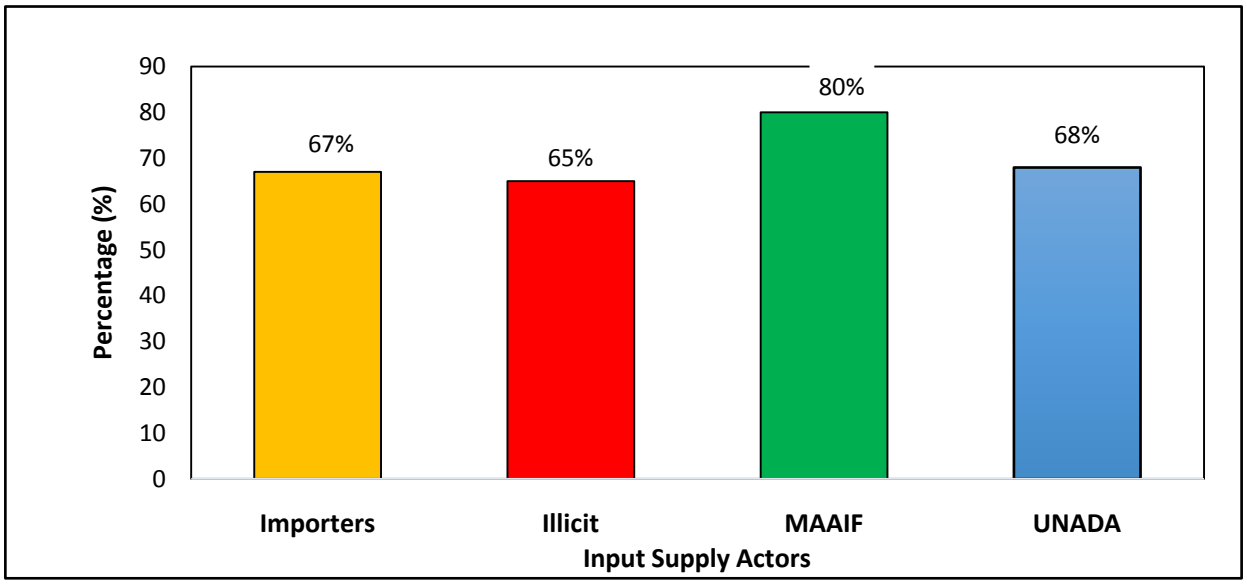
Low technology adoption has implications on production and productivity. For example, in a study on Robusta and Arabica coffee growing in Uganda by Wang et. al. (2015) found that yield gaps ranged between 45% and 57% of the attainable yield. Coupled with low levels of fertilizer application, farmers use local or recycled seed that are of poor quality. Farmers tend not to use pesticides and thus are affected by pests and diseases and irrigation is poorly practiced with less than 1 percent of farmers practicing irrigation in Uganda which leaves agriculture vulnerable to drought shocks.

Irrigation Systems in Central Uganda.

4.4.2 Institutional Challenges and Weak Regulation

Actors in agriculture sector are weakly regulated; among the implications of weak regulation is the presence of counterfeits and sub-standard agro inputs on the market. Indeed, a study by Bold et.al, (2015) that tested modern products purchased in local markets in Uganda, found that 30%of nutrient is missing in fertilizer, and hybrid maize seed contains less than 50% authentic seeds. These results are similar to that of Mbowa et.al, (2015) which found low use of fertilizers and most of which were below the acceptable moisture content limits of 0.5 -1.5 percent. For instance, in figure 4.7 below, the study by Mbowa et, al. (2015) obtained samples of fertilizers procured from supply chain actors (i.e. importers; MAAIF registered and unregistered; and UNADA members) and re-classified them on the basis of compliance to the weight (the 50 Kg), and the acceptable moisture content limits of 0.5-1.5 percent. A sample was considered non-compliant if found lacking in either dimension (moisture content or weight). Non-compliance ranged from 65 percent (illicit actors) to 80 percent (MAAIF registered actors). The findings indicated that MAAIF inspectors pay less attention, if any, in enforcing fertilizer quality control measures among its registered input stockists.

Figure 4.7: Percent Share of Non-Compliant 50kg bag Fertilizer Samples

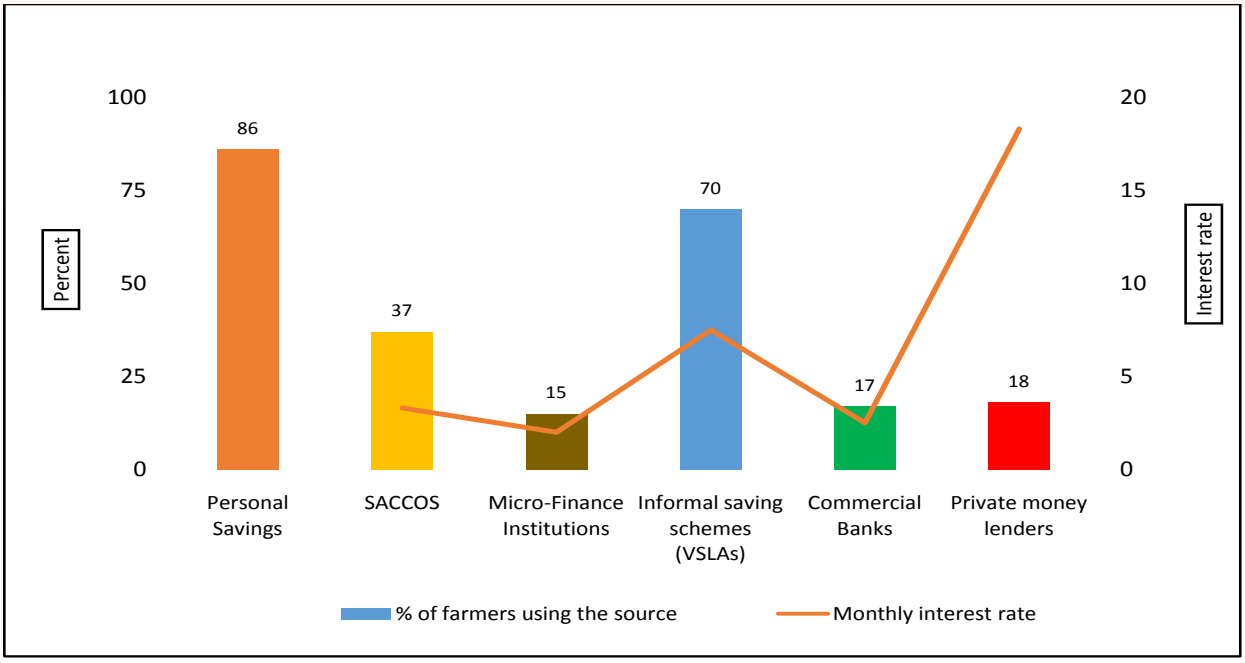


Source: Mbowa, Luswata, and Bulegeya, 2015

4.4.3 Limited Agricultural Financing

Limited finance access remains one of the major challenges facing rural farmers in Uganda (Mwesigye, Serunjogi, and Mbowa, 2017). The Government has made significant effort to provide agricultural finance through the agricultural credit facility (ACF) with little access. For example, a study of potato farmers in south western Uganda revealed that 86 percent of farmers relied on personal finance while 70 percent sourced their agricultural credit from informal savings schemes as shown in figure 4.8 below. Only 17 percent accessed finance from commercial banks and 15% from micro-finance institutions, while 18 percent obtained financing from private money lenders whose monthly interests are as high as 19 percent. The limited access of agricultural credit from formal sources such as commercial banks, SACCOs and micro-finance institutions which charge a small interest, emanates from the perception that subsistence farming is highly risky and non-profitable (Mwesigye, Serunjogi, and Mbowa, 2017).

Figure 4.8: Sources of finance for potato production and interest rates in Kigezi sub-region



Source: Barungi and Mwesigye (2015).

4.4.4 Land Scarcity, Fragmentation and Tenure Insecurity

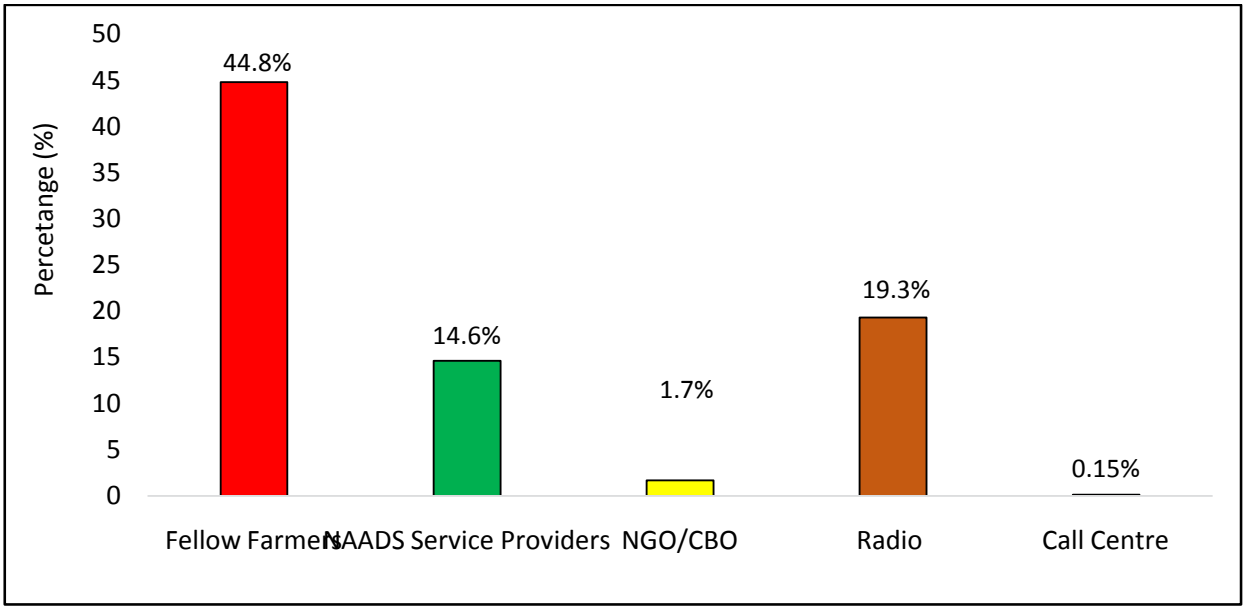
Land is increasingly getting scarce due to rapid population increase which has resulted into land fragmentation which makes it hard to mechanize and increases farm operation costs. There has also been an increase in the incidence of land conflicts which are affecting agricultural sector. For instance, Mwesigye and Matsumoto (2016) found eviction related land conflicts reduces yield by 45% yet the land policy is weak and not well coordinated with other guiding policies to tackle land conflicts. The relationship between the land lords and bonafide occupants as stipulated in the land policy raises tensions and can result into land conflicts. Indeed, the cases of land disputes have increased of recent and these are mainly influenced by lack of secure rights over land as most of the land in Uganda is not surveyed and not titled. The Government came up with a land fund which sets up a compensation for land lords but the fund is not enough to clear all the land lords.

Land Scarcity and Land Fragmentation in South Western Uganda.

4.4.5 Knowledge gap on proper farming practices

Farmers do not have access to quality extension services and have resorted to other knowledge sources like radio and other farmers for production knowledge. The study by Guloba, Barungi, and Adong (2015) showed that of the farmers who reported to have sought for extension services, 45% received trainings from the fellow farmers and peers, and about 15% got training from NAADS. The second source of information to farmers are radio as about 20% of surveyed farmers reported to have gotten knowledge from this source as shown in figure 4.9 below. These findings indicate that there is limited knowledge to farmers from the trained extension officers on better farming practices.

Figure 4.9: Farmer's main sources for agricultural information/advisory services (%)



Source: Guloba, Barungi, and Adong, 2015

Greenhouses for Irish Potato Seed Multiplication in South Western Uganda.

4.4.6 Gaps in the Major Agricultural related Policies

The challenges facing agriculture are dynamic and they change over time. Climate change, land tenure insecurity, and the counterfeit in the agro-input market are some of major challenges facing the sector. The existing policies do not clearly provide for how these challenges can be addressed. The country has no seed policy and the fertilizer policy was only passed in 2016 and is yet to be implemented. These are the two policies that can guide the input industry and can help reduce the problem of counterfeits in the agro-input market.

The agriculture policy does not provide for crop insurance and other measures to reduce risks and uncertainties facing smallholder farmers. Agriculture in Uganda is rain-fed which makes farmers susceptible to weather shocks such as prolonged droughts and erratic rains, and environmental hazards such as floods. Without insurance, smallholder farmers remain hesitant to invest in land in form of fertilizer application and use improved seeds because of high uncertainty and risks involved. The agriculture policy should therefore come up with strategies such as crop insurance so as to reduce risks. Innovations such as Kilimo Salama in Kenya which insures maize and wheat farmers against losses from drought and excess rains have proved helpful in reducing small holder's risks and hence promoting the use of improved inputs, applications of fertilizers and better soil management practices.

The land policy has also fallen short of curbing land conflicts. In an attempt to remove the overlaps in land ownership on Mailo tenure system and to improve the tenure security on the same tenure regime, the policy reinforces the provisions of the Land (Amendment) Act, 2010 which grants statutory protection to the bonafide and lawful occupants and their successors against any arbitrary eviction as long as the prescribed nominal ground rent is paid. However, this provision alone does not remove land tenure insecurity and overlaps in land rights because of the ambiguities that surround it. It instead raises tensions because it threatens the powers of land owners. In most cases, due to powers given to tenants and bonafide occupants by protecting their rights and to be compensated before they vacate the land they occupy, land tenants normally demand for high and unrealistic compensation. The policy does not elaborate on whether there could be an independent body to value land and determine the compensation the land lord will have to pay to the tenant in order to take full control of the land. In addition, it is not clear who sets the ground rent to be paid by the tenants; it is known that most tenants do not pay rent and the 10 shillings set by the Land decree of 1975 is too little. Therefore, strengthening the powers of the tenants at the expense of land lords had led to increased cases of forced evictions, and land disputes which all negatively affect land investment and productivity.

The land policy states that to curb the conflicts between the land lords and tenants, the Government will buy the interests of land lords using land fund and give the land to tenants. However, the land fund is not capitalized and hence unable to facilitate land acquisition from land lords to tenants. The policy is also not clear on who will finance the land fund, which leaves the implementation of the policy questionable.

Fish farming

Lastly, the weak coordination between different implementing agencies also affects agricultural commercialization. For example, irrigation requires concerted efforts from ministry of Agriculture, Animal Industry and Fisheries, Ministry of Lands, Housing and Urban Development, Ministry of Water and Environment under water for production policy. This requires clear coordination between the different implementing organizations. However, there are reported cases in eastern and northern Uganda where the Ministry of Water and Environment evict low land rice farmers from swamps yet lowland rice only grows in swampy areas. The potato farmers in Kabale are also being barred from using swamps to grow Irish potatoes yet swamps are the only areas where farmers can grow it during the dry season of June to September. There is even a potato variety called Victoria that farmers grow in swampy areas during the dry season. There is thus a need to streamline land use planning across different Government implementing ministries, departments and agencies (MDAs).

4.5 Conclusion

It's clear that the full potential of agriculture has not been achieved in Uganda despite the importance of the agricultural sector in terms of employment, export earnings, and food security. This problem has been exaggerated by limited technology adoption such as fertilizers, improved seed, and irrigation; counterfeits in the agricultural input supplies; land scarcity, fragmentation and land disputes; limited extension provision; and limited access to finance. Therefore, interventions that address these challenges will transform the sector and therefore improve the economic situation of the farming households and hence reduce poverty.

4.6 Policy Recommendations

1. Enhance the access and timely use to quality inputs. Several interventions have been subsidizing the costs of inputs through supply and direct distribution of inputs to farmers. However, the concerns have been that the inputs arrive late and

farmers either reject them or the seed does not germinate when planted late which causes losses and further discourages farmers from adopting new technologies. Indeed, the cases of farmers rejecting inputs are common in rural Uganda. Secondly, the problem of counterfeits on the market is high and this too has discouraged farmers from using modern inputs. This therefore calls for a timely input delivery and strong regulation and enforcement to ensure good input quality so as to enhance the adoption and sustainable use of modern inputs.

2. Promote agriculture financing efforts through:

    - Amplifying the existing agriculture finance initiatives e.g. extending the Agriculture Credit Facility, capitalizing the Uganda Development Bank, supporting the Microfinance Support Centre etc.

    - Supporting the agriculture finance desk to coordinate and harmonize all agriculture finance activities to both public and private.

3. Address land tenure insecurity challenge that is escalating in Uganda. Land disputes and evictions have increased of recent. This is mainly caused by poorly defined land rights and the high level of corruption which catalyzed title forgeries. The Government should thus up their efforts of strengthening land tenure security and resolving the settlement problems to free off land for large scale agricultural projects.

4. Support to other segments of the value chains need to be enhanced so as to pull the young people from farms to marketing and value addition. Since the young people have practical knowledge and ability of technology, they need to be supported to use technology in produce marketing and processing. Marketing and value addition are more attractive, highly paying, and essential for agriculture commercialization yet they are still under developed in Uganda.

5. Support mechanization of agriculture (use of ploughs, tractors, combined harvesters, modern storage facilities e.g. silos, etc.), this will speed up work with which farming operations can be performed hence a raise in output and efficiency of agriculture labour in the country.

6. Promote low cost irrigation systems.

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Chapter 5: Viability of Local Content Requirements in Uganda: An Industry and Enterprises Perspective

Metal Fabrication Workshop in Kampala Industrial area.

5.1 Introduction

Uganda's draft Local Content Bill of 2017 aims to ensure exclusive procurement of supplies and inputs from Uganda if the undertakings is of a public nature or is carried out by a private entity under a public private partnership agreement. The drive for use of local content has been catalyzed by the need to transform the structure of Uganda's economy and the need to shift jobs from agriculture to industry creating jobs for the bulging youth population. This debate has also been sparked by the need to comply with Sustainable Development Goals (SDG) which requires supporting livelihoods through investments on infrastructure, industry and innovations.

In addition, the quest to attain middle income status by 2040 as articulated in the Vision 2040 and the National Development Plan, and the discovery of large oil and natural gas reserves in the Albertine Grabben has led to development of large infrastructure projects that lent credence to the need for local content in public and private investments in Uganda. Most recently, the desire to develop local businesses and industry has been articulated in several ***ad-hoc*** Uganda Government initiatives among them the ***Buy Uganda Build Uganda*** (***BUBU***) slogan that seeks to promote public procurement of locally manufactured inputs to enhance growth and create employment for the bulging youth population. In Uganda, about 400,000 youth join the job market annually (World Bank 2012).

However, the draft Uganda Local Content Policy of 2017 of 2017 and the ***BUBU*** initiative does not specify the threshold of local content to be used in Uganda and provides only for an100 percent procurement of supplies and inputs from Uganda, which may have negative consequences. Exclusive (100 percent) procurement increases market power, reduces output, and raises the cost of procurement and production that significantly diminishes the ability of firms to export, innovate, employ and skill its workers (Perez 2013).

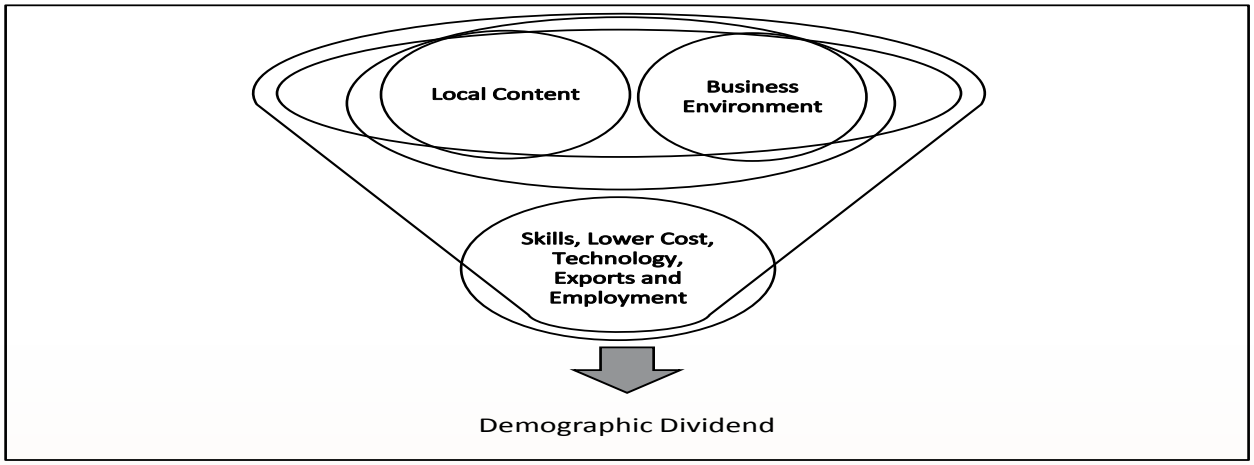
Therefore, understanding the capabilities of local firms is the first step toward developing a sound local content policies (Neuman et. al. 2017). As such, having a good understanding of the capabilities of companies in the country based on economic concepts and managerial principles can help policymakers develop the right local content policy (Ibid). In this respect, some inputs and supply are cheaper if imported, while others are cheaper when domestically sourced and others are cheaper with a mix of imports and local content. The degree of local content procurement could also vary from sector to sector. In this case, it is prudent for the local content policy to identify the threshold of local content procurement per sector in the context of increasing the productive capacity without increasing industrial cost that could constrain the ability of industries in Uganda to export, employ the bulging youth population, innovate and skill the youth.

In this regard, the chapter examines the effects of hypothetical local content thresholds (25, 50, 75 and 100 percent) on the performance of manufacturing, retail and service sectors in the context of exports, employment for the bulging youth population, innovation, skilling and cost of inputs. The thresholds are useful for policy makers in determining the local content proportion that would not increase the cost of input constraining the industry's ability to exports, employ the bulging youth population, and innovate and skill. It will also examine other constraints of an infrastructural (for example electricity) and institutional (for example corruption) nature that may constrain industrial competitiveness in light of the aforementioned local content thresholds.

5.2 Conceptual Framework for Local Content and Business Environment

Figure 5.1 below shows the conceptual framework of this chapter and it proposes that a combination of local content with a favourable business environment create incentives for firms to innovate, export, skill their employee and harness modern technology to remain low cost, increase internal productivity and upward mobility of employees and ensure retention of jobs for harnessing the demographic dividend in Uganda.

Figure 5.1: Local Content, Business Environment and Demographic Dividend Mix



This chapter utilizes the World Bank Enterprise Survey (WBES) 2013. The sample consisted of 762 business establishments in Uganda surveyed from January 2013 through July 2014 by the Uganda Bureau of Statistics (UBoS). The interviews were conducted on a nationally representative sample of the private sector in the most active economic regions of Kampala, Mbarara, Jinja, Mbale, Wakiso and Lira in the manufacturing, retail and service sector. The Enterprise Survey covers aspects of performance measures such as skilling, cost, export and employment; as well as of the business environment such as electricity and corruption. Unfortunately, no follow up survey has been done to update the WBES 2013. As such, the data set is quite old. However, we assume that not much has changed in Uganda since the last survey. It should also be noted that the analysis done in this study is largely descriptive, which calls for rigor in future studies to validate the conclusions made in this analysis.

5.3 Local Content Thresholds on the Performance of Key Sectors of the Economy

The section discusses the effects of local content thresholds on the performance of manufacturing, retail and service sectors in the context of exports, employment for the bulging youth population, innovation, skilling, cost of inputs and constraints to doing business in Uganda.

Mechanical Engineering Workshop in Kampala

5.3.1 Input and Supplier Development for Exports

Local content driven exports create better employment thus advancing the process of demographic dividend. However, this may affect the competitiveness of industries through competition from firms using cheaper foreign inputs and supplies. As such, there is a need to balance between the use of domestic and foreign inputs and supplies to account not only for the size and dynamism of demand, but also to achieve other national objectives such as employment, while remaining competitive.

Table 4 below shows that more than one half (66 firms) of the exporting firms under the food manufacturing sector tend to perform well

under an exclusive local content requirement of at least 76 percent domestic input and supplies. This is the same case with exports of leather and furniture manufacturers. This calls for increased foreign and domestic investment in the food, leather and furniture industry to allow capital to capture the relatively superior technology from other country's without having to import the technology.

In contrast, there is also a significant number (27) of furniture exporters who are only competitive when importing at least 76 percent of input and supplies. This segment of the market is driven by acceleration of demand for more sophisticated furniture in the global market, particularly in China that reduced tariffs on furniture to zero (0) percent in 2004/05 (ITTO and ITC 2004).

Also more than one half of industries participating in the chemical and fabrication exports sector are better of importing up to 75 percent of their inputs and supplies. This suggests that the chemicals and fabrication sectors tend to benefit from the lower cost and the relative higher degree of productivity in imports and global value chains (GVCs). In particular, the chemical sector in Uganda is not well developed due to low investments into the sector. What stands out is that an attempt to increase local content use in the chemicals and fabrication sectors would require a long-term approach to avoid an increase in sale prices driven by an increase in production costs. An increased sales price and production costs reduces the productiveness and competitiveness of other industries that compete for similar inputs, as well as for households that buy the final product.

Meanwhile, close to 80 percent of the firms in the textile export industry are competitive when inputs and supplies of domestic origin are not greater than 75 percent. While Uganda has enormous potential to develop the textile value chain using local content, the industry is affected by a drastically changing economic environment as global free trade initiatives provide for unrestricted competition from synthetics and low cost producers in Asia. As such, export of textile manufacturing in Uganda requires at least 25 percent of supplies and inputs to be imported to reduce production cost that constrain the industry's competitiveness.

In the service sector, the services to motor vehicle segment can export competitively when at most 75 percent of input and supplies are local content. Overall, at least 76 percent of inputs and supplies of 162 (35 percent) exporting firms are domestically supplied. More than 40 percent (66) of these firms are from the food manufacturing segment. This suggests that food manufacture has the highest impact on generating income through export and employment through use of local content in Uganda.

Table 4: Number of Exporting Companies, by Local Content Threshold, 2010 -2013

Industry	Sector/Threshold	0 - 25%	26-50%	51-75%	76-100 %	Total
Manufacturing	Food	28	23	2	66	119
	Textile	-	2	8	-	10
	Garments	3	4	11	16	34
	Leather	-	-	-	18	18
	Wood	-	-	-	-	-
	Paper	-	-	7	7	14
	Publishing	3	-	4	4	11
	Chemical	17	10	-	-	27
	Plastic	-	-	-	-	-
	Non-metal	-	-	7	-	7
	Basic Metal	-	-	-	17	17
	Fabrication	22	-	4	18	44
	Machinery	-	-	-	-	-
	Electronics	-	-	-	-	-
	Furniture	27	-	3	31	61
Retail	Retail	34	-	-	-	34
Other Services	Transport	-	-	-	-	-
	Construction	-	-	-	-	-
	Services to motor vehicles	-	-	85	-	85
	Wholesale	-	-	-	-	-
	Hotel and restaurants	-	-	-	-	-
	Info. Tech.	-	-	-	-	-
	Total	**134**	**39**	**120**	**162**	**455**

Source: Authors' Calculation based on the World Bank Enterprise Survey (Uganda) 2013.

5.2.3 Employment

Increased employment driven by local content use is one of the path-ways to achieve demographic dividend. However, producing strong local content results in the short run can be difficult due to industrial technical requirements and the ability of country to supply such capabilities in the short -run (Rueda-Cantuche and Sousa 2016). Table 5 below shows the weighted total number of full time permanent employees from 2010 to 2013 per economic sector by local content threshold. In the food manufacturing sector, firms whose inputs and supplies where at least 76 percent local content provided 32,415 full time jobs from 2010 to 2013. This accounts for 76.7 percent of jobs in the food manufacturing sector and 41.2 percent of total permanent jobs of 78,612 created in Uganda from 2010 to 2013.

Other sector that were relatively competitive in provision of permanent employment, while using input and supplies whose local content composition was at least76 percent are: garment with 973 jobs, wood (1,308), publishing (373), plastics (2,002), non-metal (1,722), basic-metal (2,400), fabrication (2,365), furniture (7,363) and hotel and restaurants (2,287).

However, the creation of jobs in some sectors depended on use of imports to some degree. For instance, the textile and chemical manufacturing sector created 105 and 2,694 jobs, respectively, using inputs and supplies whose import composition was not less than 75 percent. In the leather and the electronics manufacturers segment, up to 2,100 and 330 permanent jobs were created respectively,

using inputs and supplies whose local content composition was not lesser than 25 percent, but not greater than 50 percent. Meanwhile, the paper manufactures and the motor vehicles service sector created 700 and 850 jobs respectively using inputs and supplies whose local content composition was greater than 50 percent, but less than 75 percent.

What stands out from this analysis is that using inputs and supplies whose local content was greater than 75 percent created 54,403 permanent jobs from 2010 to 2013, which explains close to 70 percent of permanent jobs created during that period. As earlier mentioned, the food and furniture manufacturing sector explain a bulk of these jobs. This suggests that these two sectors have a ready demand in the face of foreign competition and would therefore not be constrained by a high local content threshold.

However, it should also be noted that the two sectors (food and furniture manufacturing) are already sourcing a significant part of their inputs and supply locally with little or no supply shocks. This suggests that the effects of a local content requirement on the sector and the economy will be marginal. The marginal improvement in sectors that are performing well is common in many measurable cases of implementing a local content requirement (OECD 2016).

As for the textile and the chemical manufacturing sector, the ability to create permanent jobs with relatively low shares of imported inputs and supplies is constrained. Therefore, it would be prudent for such sectors to exploit the benefits of global value chain (GVC) for importation of their input and supplies in order to reap from the economies of scale for a greater impact on other sectors and spillover effects on employment (Lakuma et. al. 2016).

Table 5: Number of Permanent Employees in the last 3 years by Local Content Threshold

Industry	Sector/Threshold	0 - 25%	26-50%	51-75%	76-100 %	Total
Manufacturing	Food	5,833	3,205	802	32,415	42,255
	Textile	105	60	-	30	195
	Garments	251	197	379	973	1,800
	Leather	-	2,100	143	213	2,456
	Wood	-	-	-	1,308	1,308
	Paper	-	-	700	85	785
	Publishing	122	-	73	373	568
	Chemical	2,694	635	-	-	3,329
	Plastic	69	60	-	2,002	21,31
	Non-metal	-	-	689	1,722	2,411
	Basic Metal	-	-	-	2,400	2,400
	Fabrication	1,132	143	175	2,365	3,815
	Machinery	-	-	-	40	40
	Electronics	165	330	-	-	495
	Furniture	2,027	-	629	7,363	10,019
Retail	Retail	608	26	7	511	1,152
Other Services	Transport	-	-	-	16	16
	Construction	-	-	-	-	-
	Services to motor vehicles	-	-	850	300	1150
	Wholesale	-	-	-	-	-
	Hotel and restaurants	-	-	-	2,287	2,287
	Info. Tech.	-	-	-	-	-
	Total	**13,006**	**6,756**	**4,447**	**54,403**	**78,612**

Source: Authors' Calculation based on the World Bank Enterprise Survey (Uganda) 2013.

5.3.3 Innovations and Technological Spillovers

An efficient local content policy does not set high thresholds of local inputs and supplies use that may constrain the ability of an industry to innovate and remain competitive. In this case, the shift from imports to local content will need to be implemented incrementally in some industries in order to develop the capacity for industries to innovate, absorb technology and develop business process (OECD 2016). Table 6 below shows the number of innovations made by various economic sectors in the last 3 years by local content threshold. The table reveals that out of 1,768 innovations realized from 2010 to 2013, close to 76 percent of them were from firms using inputs and supplies whose local content was greater than 75 percent.

Once again, the furniture and the food manufacturing sector explained the bulk of these innovations at 568 and 243 innovations respectively. It is possible that the locally sourced inputs and supplies are cheap in the food and furniture manufacturing that releases a significant share of resource to support expenditure on innovation. However, there is a need to interrogate the level and the type innovations supported by such a high threshold of local content. It is likely that the innovations are not cutting edge, which calls for Government and the private sector to support the intensification, sophistication and the scaling up of such initiative.

Nevertheless, this is not to say that the Government should only support innovative industries using a high threshold of local content. While those industries should be given priority, innovative industries using imported inputs and supplies should also be supported for sustainability of existing innovations. The unsustainability of such innovations whether generated from imports or not, can lead to efficiency losses in the market place proportional to innovation made using local content (Ibid). In this case, there is a need to balance between local content and imports when it comes to driving innovations.

Table 6: Number of Innovations in the Last 3 years, by Local Content Threshold, 2010 - 2013

Industry	Sector/Threshold	0 - 25%	26-50%	51-75%	76-100 %	Total
Manufacturing	Food	39	29	12	243	323
	Textile	3	3	-	3	9
	Garments	19	19	23	43	104
	Leather	-	7	11	7	25
	Wood	-	-	-	20	20
	Paper	-	-	7	5	12
	Publishing	12	-	9	39	60
	Chemical	22	16	-	-	38
	Plastic	4	3	-	33	40
	Non-metal	-	-	18	52	70
	Basic Metal	-	-	-	160	160
	Fabrication	24	16	7	228	275
	Machinery	-	-	-	-	-
	Electronics	11	11	-	-	22
	Furniture	32	-	15	568	615
Retail	Retail	-	2	17	33	52

Industry	Sector/Threshold	0 - 25%	26-50%	51-75%	76-100 %	Total
Other Services	Transport	-	-	-	-	-
	Construction	-	-	-	-	-
	Services to motor vehicles	-	-	85	101	186
	Wholesale	-	-	-	-	-
	Hotel and restaurants	-	-	-	163	163
	Info. Tech.	-	-	-	-	-
	Total	**166**	**106**	**158**	**1338**	**1768**

Source: Authors' Calculation based on the World Bank Enterprise Survey (Uganda) 2013.

5.3.4 Skilling Programmes

As earlier mentioned, approximately 400,000 job seekers enter the labour market annually. However, few possess the technical skill required to succeed in the job market (Lakuma et.al. 2016). As such, much of skills development is acquired on job. In this regard, one need to question the threshold of local content required for firms to remain competitive in imparting skills and creating employment.

Table 7 below reveals that that there were more skilling programmes in industries that tended to use inputs and supplies that are not more 25 percent local content. More than one half (91) of the training programmes were implemented in the threshold of local content not exceeding 25 percent (imported input and supplies exceeding 75). Out of the 91 programmes, the food (39), fabrication (20) and the furniture (16) sector explained 82 percent of the skilling programmes. For the greater than 25 but not exceeding 50 percent threshold, the food industry skilled its employees 24 times, the garment industry provided 8 skilling programmes, while the chemical industry provided 10 skilling programmes.

The many training programmes in the two thresholds may emanate from the fact that many imported inputs and supplies are technology based and may require a substantial amount of employee training and development. As such, imported inputs facilitate the transfer of technology to employees enhancing employability.

Table 7: Number of Skilling Programmes for Employees, by Local Content Threshold

Industry	Sector/Threshold	0 - 25%	26-50%	51-75%	76-100 %	Total
Manufacturing	Food	35	24	9	-	68
	Textile	-	-	-	-	-
	Garments	6	8	15	-	29
	Leather	-	7	11	-	18
	Wood	-	-	-	-	-
	Paper	-	-	-	-	-
	Publishing	5	-	-	-	5
	Chemical	3	10	-	-	13
	Plastic	1	3	-	-	4
	Non-metal	-	-	-	-	-
	Basic Metal	-	-	-	-	-
	Fabrication	20	-	-	-	20
	Machinery	-	-	-	-	-
	Electronics	-	-	-	-	0
	Furniture	16	-	3	-	19
Retail	Retail	5	-	-	-	5
Other Services	Transport	-	-	-	-	-
	Construction	-	-	-	-	-
	Services to motor vehicles	-	-	-	-	-
	Wholesale	-	-	-	-	-
	Hotel and restaurants	-	-	-	-	-
	Info. Tech.	-	-	-	-	-
	Total	**91**	**52**	**35**	**-**	**178**

Source: Authors' Calculation based on the World Bank Enterprise Survey (Uganda) 2013.

5.3.5 Cost of Input and Supply

On average, foreign inputs allows firms to lower their costs of production by using better, cheaper, or novel inputs from abroad (Blaum et. al. 2015). A low cost industry is able to provide more jobs for the bulging youth population and provide consumer goods at a lower price enhancing welfare. However, such gains differ from sector to sector. Some Sectors are better off using a combination of foreign and local inputs. More so, when a country produces that input at a lower domestic cost than imports.

Table 8 below demonstrates that using a high local content threshold of at least 76 percent costed the food manufacturers industry in Uganda Ushs. 394.72 billion. Meanwhile, firms in the food industry who used a local content threshold of between 51 and 75 percent saved significantly by lowering the cost to Ushs. 0.84 billion. This suggests that using a mix of foreign inputs (not greater than 50 percent) and local content (between 51 and 75 percent) was cost saving. It should be noted that the high proportion of local content in the food manufacturing sector is largely explained by Uganda's comparative advantage in food production relative to foreign suppliers.

As for the textile industry, the results are mixed, using less than 25 percent inputs that are local content and using at least 76 percent local content kept the industry cost below Ushs. 0.10 billion. This pattern was the same for garments industry. The textile and the garment industry results suggest that an industry demand system determines the

threshold a firm chooses. Some consumer will only consume a specific type of textile regardless of price. As such an industry will use certain types of inputs depending on its consumers taste and preference.

In the fabrication manufacturers, cost rose in cases where the industry did not equally combine local content and foreign inputs. Table 8 below, reveals that a low local content threshold of not more than 25 percent pushed industry cost to Ushs. 5.88 billion, while a very high local content threshold of at least 76 percent pushed industry cost to Ushs. 5.88 billion. Costs were considerably lowered to Ushs. 0.09 billion in the fabrication manufacture when local content was kept between 26 and 50 percent to accommodate the use of foreign inputs. Overall, the threshold of between 26 and 50 percent is the relatively the better least cost of option across all industries of Ushs. 11.95 billion. This threshold allows firms across industry to leverage a combination of local content with cheaper, better or novel inputs from abroad, reducing their costs of production freeing resources for job creation.

Table 8: Cost of Input and Supply by Local Content Threshold in Ushs. Billions, 2010 - 2013

Industry	Sector/Threshold	0 - 25%	26-50%	51-75%	76-100 %	Total
Manufacturing	Food	1.24	3.90	0.84	394.72	400.7
	Textile	0.06	0.87	-	0.04	0.97
	Garments	0.17	0.20	1.40	0.38	2.15
	Leather	-	-	-	1.10	1.10
	Wood	-	-	-	0.30	0.30
	Paper	-	-	-	0.00	0
	Publishing	0.15	-	0.24	0.98	1.37
	Chemical	131.25	0.38	-	-	131.63
	Plastic	1.13	-	-	-	1.13
	Non-metal	-	-	1.10	3.17	4.27
	Basic Metal	-	-	-	0.48	0.48
	Fabrication	5.88	0.09	1.02	5.99	12.98
	Machinery	-	-	-	-	-
	Electronics	-	-	-	-	-
	Furniture	162.94	-	0.08	18.90	181.92
Retail	Retail	0.16	-	7	1.65	8.81
Other Services	Transport	-	-	-	-	-
	Construction	-	-	-	-	-
	Services to motor vehicles	-	-	0.27	3.02	3.29
	Wholesale	-	-	-	-	-
	Hotel and restaurants	-	-	-	2.17	2.17
	Info. Tech.	-	-	-	-	-
	Total	**302.98**	**5.44**	**11.95**	**432.9**	**753.27**

Source: Authors' Calculation based on the World Bank Enterprise Survey (Uganda) 2013.

5.3.6 The Business Climate

Factors that affect the business climate such as electricity, access to finance and tax rates need to be improved to enable industries lower their cost as they integrate local content in their value chain creating jobs for the bulging youth population. A conducive business environment enables a firm to perform cost-effective sourcing and staffing, improve its operational proficiency and productivity, and increase capacity utilization. Benefits of an improved business climate can also trickle down to the population in terms of sustainable economic development, long-term employment creation, higher living standards, improved education and training, and better infrastructure (Dupont, 2012).

Firms using less than 25 percent local content as indicated in table 9 below suggest that electricity was the key constraint to the food, garment, plastic, electronics and furniture manufacturing sectors between 2010 and 2013. Nevertheless, the delivery of electricity has improved in recent time and as such, the reliability of electricity in Uganda is now similar with that of other low income countries. What remains to be done is to lower the cost of power. The high cost of power could be a cause and a consequence of low consumption/distribution. Uganda Bureau of Statistics (UBoS) in 2016 estimated that only 20 percent of households in Uganda use electricity.

As for the 26 to 50 percent threshold, table 6 shows that there was a mix of constraints. The practices of the informal sector affected the food and the plastic industry the most. The cost of finance affected the garment industry and land was a major constraint to textile.

Tax rate impeded the chemicals and the fabrication industry as shown in table 6 below. World Bank in 2017 estimated Uganda's total tax rate at 31% to be the lowest in East Africa and one of the lowest in Africa, the problem is the practices of the informal sector who don't pay taxes transferring the burden to the formal sector rendering the formal sector uncompetitive. This practice also affects the principle of taxation such as equity and fairness. In other cases, firms would rather not pay taxes due to negative perception on the Government's ability to provide public service. This speaks to the concept of fiscal legitimacy and how it influences tax non-compliance amongst firms and individuals in Uganda. This argument suggest that the people of Uganda would be happy to pay taxes if they enjoyed the benefits emanating from that tax in amenities such schools and hospitals (Mawejje and Okumu 2016).

At high thresholds of local content use of at least 76 percent, electricity affected the food, paper, publishing, chemical, basic metal and fabrication. The practices of the informal sector affected the garment and the retail sector. Finance constrained the textile, non-metal, machinery and transport sector. The high cost of finance speaks to the many firms, in the aforementioned sectors, experiencing external financial constraints such as access to loans from commercial banks and also running up against the risks of raising fresh equity in capital markets. Given that most businesses depend on personal/internal finance to facilitate business venture, analysis of household income is prudent. In this regard, in Uganda only 22 percent of households have functional bank accounts (UBoS 2016). Majority of these account are held in commercial bank in urban areas. The nature of enterprise credit is short term and expensive and this curtails the financing enterprise. More importantly, finance does not appear to be a constraint amongst firms who use less than 25 percent of local content, which suggest that firms who participate in importation of imports are likely to be having access to both internal and external finance.

Table 9: Key Business Constraints by Local Content Threshold, 2010 - 2013

Industry	Sector/Threshold	0 - 25%	26-50%	51-75%	76-100 %
Manufacturing	Food	Electricity	Informality	Transport	Electricity
	Textile	Tax rates	Land	-	Finance
	Garments	Electricity	Finance	Finance	Informality
	Leather	-	License	Customs	Corruption
	Wood	-	-	-	Tax rates
	Paper	-	-	Electricity	Electricity
	Publishing	Land	-	Electricity	Electricity
	Chemical	Corruption	Tax rates	-	Land
	Plastic	Electricity	Informality	-	-
	Non-metal	-	-	Crime	Finance
	Basic Metal	-	-	-	Electricity
	Fabrication	Electricity	Tax rates	Customs	Electricity
	Machinery	-	-	-	Finance
	Electronics	Electricity	Electricity	-	-
	Furniture	Electricity	-	Informality	Finance
Retail	Retail	Tax rates	Customs	License	Informality
Other Services	Transport	-	-	-	Finance
	Construction	-	-	-	-
	Services to motor vehicles	-	-	Land	Transport
	Wholesale	-	-	-	-
	Hotel and restaurants	-	-	-	Politics
	Info. Tech.	-	-	-	-

Source: Authors' Calculation based on the World Bank Enterprise Survey (Uganda) 2013.

Table 10: Local Content Threshold by Industry, 2010 - 2013

Industry	Sector/Factor	Input and supplier Development	Employment	Innovation and Tech. spillovers	Skilling programs	Cost of inputs and supplies	Average
Manufacturing	Food	76-100 %	76-100 %	76-100 %	0 - 25%	0 - 25%	76-100 %
	Textile	51-75%	0 - 25%	0 - 25%	-	0 - 25%	0 - 25%
	Garments	76-100 %	76-100 %	76-100 %	51-75%	0 - 25%	76-100 %
	Leather	76-100 %	26-50%	51-75%	51-75%	0 - 25%	51-75%
	Wood	-	76-100 %	76-100 %	-	0 - 25%	76-100 %
	Paper	76-100 %	51-75%	51-75%	-	-	51-75%
	Publishing	76-100 %	0 - 25%	76-100 %	0 - 25%	0 - 25%	0 - 25%
	Chemical	-	0 - 25%	0 - 25%	26-50%	26-50%	0 - 25%
	Plastic	-	76-100 %	76-100 %	26-50%	26-50%	26-50%
	Non-metal	51-75%	76-100 %	76-100 %	-	0 - 25%	76-100 %
	Basic Metal	76-100 %	76-100 %	76-100 %	-	0 - 25%	76-100 %
	Fabrication	0 - 25%	76-100 %	76-100 %	0 - 25%	26-50%	0 - 25%
	Machinery	-	76-100 %	-	-	-	76-100 %
	Electronics	-	26-50%	0 - 25%	-	-	0 - 25%
	Furniture	76-100 %	76-100 %	0 - 25%	0 - 25%	51-75%	51-75%
Retail	Retail	0 - 25%	0 - 25%	76-100 %	0 - 25%	0 - 25%	0 - 25%

Industry	Sector/Factor	Input and supplier Development	Employment	Innovation and Tech. spillovers	Skilling programs	Cost of inputs and supplies	Average
Other Services	Transport	-	76-100 %	-	-	-	76-100 %
	Construction	-	-	-	-	-	
	Services to motor vehicles	51-75%	51-75%	76-100 %	-	0 - 25%	51-75%
	Wholesale	-	-	-	-	-	-
	Hotel and restaurants	-	76-100 %	76-100 %	-	0 - 25%	76-100 %
	Info. Tech.	-	-	-	-	-	
	Average	**76-100 %**	**76-100 %**	**76-100 %**	**0 - 25%**	**26-50%**	**76-100 %**

Source: Authors' Calculation based on the World Bank Enterprise Survey (Uganda) 2013.

5.4 Conclusions and Policy Recommendations

The examination of the effects of hypothetical local content thresholds (25, 50, 75 and 100 percent) on the performance of manufacturing, retail and service sectors in the context of exports, employment for the bulging youth population, innovation, skilling and cost of inputs. The thresholds are useful for policy makers in determining the local content proportion that would not increase the cost of input constraining the industry's ability to exports, employ the bulging youth population, innovate and skill. The examination of constraints of an infrastructural (e.g. electricity) and institutional (e.g. corruption) nature indicated that it may constrain industrial competitiveness in light of the aforementioned local content thresholds.

From table 10 above, it can be concluded that input and supplier development for exports, employment of the bulging youth population, and innovations and technology spillover thrive under a high local content threshold of at least 76 percent. However, skilling programmes are constrained by high local content threshold and the costs of inputs and supplier rise with local content proportion. The positive effects of exports, employment, and innovation and technology spillovers on the economy dominates the negative effects of cost overruns and reduction of skilling programmes that arise when the local content threshold is at least 76 percent.

At the sectoral level, the food manufacturing sector is competitive to export, employ and innovate when the local content contribution to inputs and supply is at least 76 percent. However, a high local content threshold of at least 76 percent discourages the food manufacturing sector from investing in skilling programmes due to cost overruns. On the other hand, the textile manufacturing sector is competitive to employ, innovate and operate at low cost when importing more than 75 percent of input and supplies. Reducing imports may lower innovations and reduce connectivity. However, the proportion of imports in inputs and supplies should be less than 50 percent for the sector to be competitive in the export market.

1. What stands out from the above analysis is that the local content policy cannot be generalized and should be industry specific and implemented incrementally to give time to domestic firms to develop capacity to respond to demand to avoid supply shortages. Supply shortages may affect the employment the local content policy intends to create and other longer term objectives such as development of the capacity to export.

2. The analysis also reveals that it is imperative to understand the business climate that face firms and the capacity building requirement to support industries to create job, innovate and export. Such an understanding should also be sector specific, because different sectors face different constraints.

3. Provision of cheaper electricity and reduction of tax rates will require public intervention that increases consumption of power and expand the tax base.

4. Availability of cheap credit will require a public private partnership (PPP) intervention that reduces risk perception, increases competition in the financial sector and improve the land registry to facilitate collateral.

5. There is need for more analysis, use of more rigorous methodology and a more recent data set to discern the thresholds appropriate for local content use in Uganda's industrial sector. It should also be noted that there are many other factors other than exports, employment, innovation, cost and the business climate that affect industrial competitiveness and they deserve to be analyzed.

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Chapter 6: **Financial Sector Deepening in Uganda**

Bank of Uganda Building

6.1 Introduction

While Uganda's economic growth is still impressive i.e. averaging 4.4 percent between 2011-2017 driven by the services industry and thus above the Sub-Saharan average (1.3 percent) for the same period, the economy grew at only 3.9 percent in FY 2016/17, even slower than the 4.7 percent recorded in FY 2015/16 (GoU, 2017). This performance is below the National Development Plan (NDP) (2015/16 – 2019/20) projected growth rates at 5.8 percent and 5.9 percent for the same periods respectively. It is therefore apparent that Uganda's current economic growth trajectory is not aligned to the country's medium and long term national aspirations, namely: to achieve lower middle income status by 2020 and upper middle income status by 2040 (NPA, 2013). This slowdown in economic growth has been attributed to challenges in productivity growth, physical and human capital accumulation, business environment and cyclical factors such as the conflict in neighboring South Sudan and a recent drought (IMF, 2017). It is increasingly clear is that there is need for new development tools and approaches to refocus policy interventions for the revival of Uganda's economic growth to average 7.65 percent over the last 3 FYs of the NDP (2015/16 – 2019/20), given the population growth rate at 3.0 percent (UBOS, 2016), to mitigate the deficits registered in 2015/16 and 2016/17 if national aspirations are to be achieved. This Chapter examines the role that the financial sector has played in Uganda's economic growth and interrogates the contribution financial sector development can make towards renewed efforts for accelerated and sustained economic growth in the context of a youthful population.

For an economy to reap economic gains associated with the demographic dividend there must be improvements in human capital development of the younger population. Productivity of this population depends on access to employment and affordable finance (UNFPA, 2016). Financial Sector deepening refers to increasing the provision of financial services. A developed and robust financial sector has the ability to stimulate economic activity by mobilizing savings into the formal economy for investment; protecting the population from inappropriate and expensive sources of capital and credit particularly during hard economic times; and reducing informal transactions thereby strengthening domestic revenue mobilization which creates new fiscal space for service delivery and infrastructure development. Furthermore, the depth of the financial sector has generally been found to promote economic growth by increasing economic efficiency and investment. Financial sector deepening enables the financial intermediaries perform their functions of mobilizing, pooling and channeling domestic savings into productive capital more effectively thereby contributing to economic growth of a country (Sindani M, 2013). The financial sector therefore has the ability to act as a facilitator and multiplier for renewed economic growth and prosperity in Uganda.

6.2 Financial Sector Structure, Legal Framework, Policies, Plans and Programmes

6.2.1 Financial Sector Structure, Legal Frameworks and Policies

The Financial Sector in Uganda consists of three broad groupings which include Banking Financial Services categorized into Tier 1, 2 and 3 Financial Institutions; Non-Bank Financial Services including Tier 4 Microfinance Institutions, Insurance services, Capital markets, Pension funds, Money Lenders and more recently Digital Financial service providers and the third grouping is Development Banks. At the apex of the Financial Sector is the Ministry of Finance, Planning and Economic Development (MoFPED) whose mandate, with respect to the sector, is to develop and maintain an enabling and consistent legal, regulatory and policy framework for the sector's soundness, stability and development.

6.2.2 Financial Sector Regulators

These include the Bank of Uganda (BOU) established by the 1995 Constitution of the Republic of Uganda; Uganda Microfinance Regulatory Authority (UMRA); Uganda Retirement Benefits Regulatory Authority (URBRA); Insurance Regulatory Authority of Uganda (IRAU); Capital Markets Authority (CMA); and the Financial Intelligence Authority (FIA).

6.2.3 Banking Financial Services

This industry is supervised by BOU which is also mandated to issue legal tender, maintain Uganda's external reserves and to promote stability and soundness of the financial sector. BOU supervises 25 Tier 1 Financial Institutions (Commercial Banks); 4 Tier 2 Financial Institutions (Credit Institutions); and 4 Tier 3 Financial Institutions (Microfinance Deposit-Taking Institutions) under the Financial Institutions Act, 2004 (as amended) and the Microfinance Deposit-Taking Institutions Act, 2003. BOU also supervises 265 Forex bureaus; 38 money remitters; and 2 Credit Reference Bureaus. Given the poor savings culture, the Banking industry still faces high costs in mobilizing medium to long term resources and a reduction in the Central Bank Rate has therefore not triggered a commensurate reduction in the Commercial lending rates charged by banks which are still high ranging between 18 to 23 percent. New gains are expected to be realized from the implementation of Agent and Islamic Banking arising out of the enactment of the Financial Institutions (Amendment) Act, 2016.

6.2.4 Microfinance Services

Uganda's microfinance industry is composed of at least 1,997 operational Savings

and Credit Cooperative Organizations (SACCOs); numerous Financial Non-Governmental Organizations (NGOs); Credit-Only Microfinance Companies; and thousands of informal Village Savings and Loan Associations (VSLAs). The industry is supervised by UMRA established under the Tier 4 Microfinance Institutions and Money Lenders Act, 2016 and it is organized under numerous industry associations including the Association of Microfinance Institutions in Uganda (AMFIU); Uganda Cooperative Savings and Credit Union (UCSCU); Uganda Money Lenders Association (UMOLA) and the Uganda Cooperative Alliance (UCA). Unlike other industries in the financial sector, there are significant data gaps in the microfinance industry and on informal saving mechanisms to inform policy formulation and business processes.

6.2.5 Pension Funds and Retirement Benefits Schemes

The Retirement Benefits sector in Uganda consists of a National Provident Fund - the National Social Security Fund for the private sector, a Pension Fund for the public sector and 63 licensed private Retirement Benefits Schemes. The industry is supervised by URBRA established under the Uganda Retirement Benefits Regulatory Authority Act, 2011.

6.2.6 Insurance Services

The Insurance industry consists of 29 licensed Insurance Companies (21 Non-Life and 8 Life Insurance Companies); 1 Re-insurance Company; 11 Health Membership Organizations (HMOs); 30 Brokers; and 1,350 Agents under the supervision on IRAU established under the Insurance Act, 2017. Unfortunately, insurance penetration levels are currently below 1% of GDP and more needs to be done for the industry to achieve its full potential. New gains are expected to be realized from the implementation of Banc assurance and Takaful (Islamic Insurance) arising out of the enactment of the Financial Institutions (Amendment) Act, 2016.

6.2.7 Capital Markets

The industry consists of 2 Securities Exchanges with 16 listed Equities and is supervised by CMA established under the Capital Markets Authority Act, 1996 (as amended). Overall, Uganda's capital markets are characterized by under capitalization and limited investment opportunities. There are only 16 companies listed on the Uganda Securities Exchange (USE) with 8 of these cross-listed on the Nairobi Stock Exchange (NSE) in Kenya. There is limited knowledge and reach of Capital Markets; public perceptions of lack of safety in capital markets and change aversion

6.2.8 Development Banks

Uganda's financial sector also consists of 2 Development Banks established under the Uganda Development Bank Act, 1972 and the East Africa Development Bank Act, 1985. While Development Banks are the best suited to provide long term financing, they still have relatively small lending operations in comparison to the total credit extended by the Commercial Banks. At a macro level, a particular concern of Government should be how best to configure efficient partnerships and coordination of collective action by all stakeholders to support financial sector development for accelerated economic growth and job creation.

6.2.9 Financial Sector Policies and Programmes

Uganda's Vision 2040 recognizes the enabling role of the financial sector and identifies 7 policy goals including deepening and broadening of the financial sector through research on financial development (NPA, 2013). In addition the NDP (2015/16–2019/20) has recommended the implementation of strategies to raise insurance penetration and national savings to GDP ratio; increase the level of capitalization and widen investment opportunities in the capital markets; and improve statistical data production and policy research for financial sector development.

Despite the overarching policy direction enumerated in the high level National Development Planning Framework strategic documents, the sector lacks a comprehensive Financial Sector Development Strategy to coalesce the efforts of the numerous stakeholders to collectively achieve the identified strategic policy goals and rally around a shared vision, objectives and programmes that guide public and private investments into the sector. Never the less, the sector has seen the development and implementation of a National Microfinance Policy and Financial Literacy Strategy to guide public investments in the sector. Policies that are still at development stage include the National Payment Systems Policy; National Agriculture Finance Policy; and National Financial Inclusion Strategy. Uganda also signed up to the East African Community (EAC) Common Market Protocol in 2010 and while not yet fully functional, there are efforts to broaden and deepen the financial sector through the establishment of a single market for financial services among the EAC Partner States. Some of the efforts to achieve this goal include the development of an EAC Microfinance Policy; EAC Insurance Policy; and an EAC Retirement Benefits Policy. Regional cooperation in East Africa will be taken to yet another level when the EAC Monetary Union Protocol becomes operational by 2020/21. The objective of the Protocol is to promote and maintain monetary and financial stability aimed at facilitating economic integration to attain sustainable growth and development of the EAC community.

The major existing public programmes in Uganda's financial sector include: the Agriculture Credit Facility (ACF) administered by Bank of Uganda in partnership with Commercial Banks, Development Banks and Microfinance Deposit-Taking Institutions. The Facility is designed to provide medium to long term credit to agricultural and agro-processing projects on terms more favorable relative to the open market; the Uganda Agricultural Insurance Scheme (UAIS) pilot which is a subsidy programme for premiums taken out on agriculture-related insurance policies also commenced operation in FY 2016/17 to attract more private sector investment in agricultural credit. The Scheme is administered by MoFPED in partnership with the Uganda Insurers Association (UIA); the Microfinance Support Centre Ltd was established in 2001 as a State Owned Enterprise to provide affordable wholesale credit facilities to Cooperatives and Small and Medium Enterprises (SMEs); the Project for Financial Inclusion in Rural Areas (PROFIRA) is being implemented in partnership with contracted service providers to sustainably increase access to and the use of financial services by the rural population targeting not less than 750,000 rural poor men, women, youth and vulnerable groups; the Youth Livelihood Programme is a micro-credit programme being implemented by the Ministry of Gender, Labour and Social Development (MoGLSD) through the Community Development Office at the Local Government level to empower the target youth population with a view to harness their socio-economic potential and increase self-employment opportunities and income levels.

6.3 Reforms for Financial Sector Development

The Governor, Bank of Uganda, Prof. Emmanuel Tumusiime – Mutebile at the Launch of Interswitch ATM System in Kampala.

As with most developing countries that have pursued economic and structural reforms, Uganda has undergone a process of financial sector reform and the financial system that has emerged is relatively diversified in the range of services and products offered. The intention of Uganda's financial reforms was to strengthen and broaden the financial system as well as to enhance competition in the financial system. Most notable among these reforms included privatization of the Uganda Commercial Bank (UCB) which was the largest public bank; lifting of the moratorium on new Bank licensing to encourage competition; decontrolling of interest rates determination; establishment of independent regulators for various non-bank financial services and more recently the consolidation of the legal and regulatory framework for all non-deposit taking microfinance institutions and money lenders.

As a result of the reforms, extension of credit to the private sector improved over the last decade, with an average credit growth of about 24 percent per annum. However, the degree of diversification of the financial systems and the level of gross domestic savings stands at 9.57 percent of GDP, which is very low compared to 28.6 percent for lower Middle Income Countries (NPA, 2015). The pension assets are still low at 2.18 percent of GDP compared to 58 percent of GDP in South Africa. It is therefore evident that further financial sector reforms and new approaches are required to develop Uganda's financial sector.

6.4 Ensuring Universal Access and Usage of Financial Services

Empirical evidence shows that financial inclusion can aid self-employment, improve household incomes, support greater local economic activity, and reduce inequality (World Bank, 2014). There is also macroeconomic evidence that economies with deeper financial intermediation tend to grow faster and reduce income disparities. It is against this background that Uganda signed up to the Maya Declaration for improving financial inclusion under the Alliance for Financial Inclusion (AFI) framework in 2011. Although financial inclusion is improving in Uganda as demonstrated by the FINSCOPE study findings that 54 percent of the adult population was observed as financially included in formal finance in 2013 up from 28 percent in 2009 (see table 11), the adult population operating a Bank Account declined from 21 out of every 100 adults to 20 during the same period despite significant increases in Bank branches and Automated Teller Machines (ATMs) (EPRC, 2013). The improvement in formal financial inclusion was driven by the phenomenal uptake of the mobile money service after it was introduced in April 2009. The FINSCOPE Study also found that rural adults are twice as likely as their urban counterparts to utilize informal mechanisms such VSLAs for financial services and are 1.7 times more likely to be completely excluded from informal and formal financial services. This data clearly reflects that addressing the existing gaps for financial inclusion will require a significant focus on the rural areas where 79 percent of the population resides (UBOS, 2016).

Table 11: Aspirations under the Financial Inclusion Strategy (2017 - 2022)

Key Performance Indicator	2009	Current State	Desired State (by 2022)
Financial Inclusion	70%	85%	95%
Formal Financial Inclusion	28%	54%	80%
Bank services Usage	21%	20%	40%
Insurance Usage	3%	2%	7%
Savings with formal FIs	21%	25%	50%
Credit Bureaus coverage	N/A	6%	40%
Access points per 100,000 adults	N/A	548	615
Active Mobile Money Users	N/A	31%	60%

There is more work that needs to be done to broaden the scope of financial services that can be provided through digital platforms such as the mobile phone beyond payments and transfers as well as improving the competitive framework for digital financial services via interoperable clearing and settlement mechanisms. These reforms are all the more relevant now considering that Uganda has the second most youthful population in the world with at least 50 percent of Uganda's population aged 15 years and below (UBOS, 2016) and a high literacy rate at 73 percent embodying a new type of consumer willing to adopt new approaches and technologies in the consumption of financial services. An increase in the use of formal finance will mobilize more savings into the formal economy for investment in productive activities by the workforce and strengthen domestic revenue mobilization for better health and education service delivery facilitating the reaping of even higher demographic dividends from Uganda's youthful population. Multiple stakeholders have also emphasized the need for changes to broaden the scope of Credit Reference Bureaus to include Tier 4 Microfinance Institutions and other Non-Bank

services such as utilities and digital financial service providers. To this end, the Financial Institutions (Amendment) Act, 2016 has provided for special access to the Bureaus by other credit service providers.

6.5 Digital Financial Services

MTN Uganda - Mobile Money Kiosk.

The significant increase in formal financial inclusion in Uganda between 2009 and 2013 was driven largely by the growth of mobile money. Mobile Network Operators (MNOs) report 18.7 million active registered Subscriber Identity Module (SIM) cards and approximately Ushs. 7 million unique and active users of mobile money service in Uganda as of August 2016 up from Ushs. 500,000 in 2009. The high usage of mobile money is the result of a combination of domestic and regional factors and some of these factors include a relatively low usage of the formal Banking system, general consumer willingness to adopt new technologies, and the demand for efficient financial services among the new generation of consumers. New developments in the digital financial services space include the launching in August 2016 of "Mo-Kash", a product delivered through a partnership between MTN and Commercial Bank of Africa that allows clients to save with and borrow money from the Bank via a mobile money platform. This business model is similar to the "M-Shwari" and "M-Kesho" products launched in Kenya. Major payment service providers have also deployed various self-service kiosks to enable bill payments, point of sale transactions, money transfers and other e-money services to Banks, Non-Bank corporations and Governments. A private switch company also provides interoperability across ATMs that are owned and operated by the various Banks.

BOU issued Mobile Money Guidelines in

2013 to provide consumers with a basic set of protections and a process for remedy in the event of complications. Other than these Guidelines, the Government has hereto adopted a "watch and learn" approach to allow operators to innovate and experiment.

Despite these stellar achievements, the Financial Inclusion Insight surveys by Inter Media for 2013-15 found that one of the biggest barriers to mobile money usage in Uganda is that 55 percent of adult population do not own a handset. Another key challenge for digital financial services providers has been customer identification as service providers were not always able to authenticate the national ID but this is gradually improving with the renewed efforts by the National Identification and Registration Authority (NIRA). Several infrastructure barriers such as low levels of electrification (approximately 15% of coverage nationally and 7% in rural areas) also exist which may hamper the growth of digital financial services, especially in rural areas.

6.6 Conclusions

It is important that efforts for financial sector deepening in Uganda are aligned to support the changing demography, technology, and attitudes in the country. While having a youthful population currently manifests itself more as a strain on the resources of the country, it may bode well for future growth of the economy if skills are developed, literacy levels continue to rise and productivity of the working population increases. It is increasingly becoming apparent that the financial sector, through digital financial services, can contribute to harnessing the demographic dividend by improving proximity and bringing harder-to-reach clients into the formal economy at potentially lower costs through innovations such as agent banking, mobile money and electronic payments. However the new technology and new participants present new risks that the current legal and regulatory framework has not considered.

There is also need to address the inadequate interoperability across Uganda's evolving financial sector landscape. Financial Service Providers other than those supervised by BOU such as SACCOs do not have direct access to the national payments system which constrains such providers from offering modern and competitively priced payment solutions to more Ugandans. The absence of a mechanism to clear and settle payments between the traditional financial sector's electronic clearing system and the MNOs systems also limits cross-sector functionality.

6.7 Policy Recommendations

To contribute to accelerated economic growth and job creation for Uganda's youthful population, through financial sector deepening, the following policy interventions are recommended:

1. **Legal Reforms:** Digital Financial Services continue to demonstrate solutions to the two fundamental challenges that have for centuries constrained traditional delivery channels, namely: information asymmetry and transaction costs to the client and service providers but the new dynamic business models, technology and participants are presenting new risks that have proved challenging for policy makers and regulators to appreciate. There is therefore urgent need for authorities in Uganda to design and enact enabling legal and regulatory frameworks such as a Payments Systems Law to protect consumers without stifling innovation.

2. **Financial Infrastructure Investments:** As a policy, Government should support access and use of formal financial services through initiatives such as mandating interoperability among

financial service providers and across the entire digital financial services landscape. Government should also consider providing subsidized digital devices to marginalized segments of the population in partnership with companies/initiatives providing low cost digital services.

3. **National Level Coordination:** Government should develop a comprehensive Policy for Financial Sector Development in Uganda consistent with the national aspirations enumerated in Uganda's overarching National Development Planning Framework and sensitive to the changing demography, technology, and attitudes in the country and the EAC region. A national blue-print for the sector would serve to coalesce the efforts of the numerous stakeholders to collectively achieve the identified strategic policy goals and guide public and private investments into the sector to support the realization of outcomes such as the demographic dividend.

4. **Research and Analysis:** Regular sector-wide data collection and analysis particularly in the microfinance industry is still weak. There is therefore need for Government to deliberately invest in research and build the capacity of the recently established UMRA to set performance benchmarks for the microfinance industry and regularly monitor them for cross sector comparability and analysis.

5. **Competitiveness:** There is need for Government to design and implement support programmes particularly for member-owned financial service providers to enhance their capacity to compete globally particularly as full implementation of the EAC Common Market Protocol draws closer.

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Chapter 7: **Enhancing Entrepreneurship and Industrialisation in Uganda**

Century Bottling Company Limited Located at Namanve Industrial Park.

7.1 Introduction

Uganda's vision is to transform the Ugandan society from a peasant to a modern and prosperous country within 30 years. The aim is to become a lower middle income country by 2020, with a GDP per capita of $1,039, and an upper middle income country by 2040 with a GDP per capita of $9,500. This national aspiration is expected to be achieved through a number of strategies that are laid out in six National Development Plans in the run up to 2040. Promotion and enhancement of entrepreneurship and industrialisation are highly linked to the economic transformation of economies. Government of recognises the fact that entrepreneurship and industrialisation have a high multiplier effect in regard to harnessing the population dividend. It is for this reasons the two variables rank highly on Uganda's Economic Development Agenda.

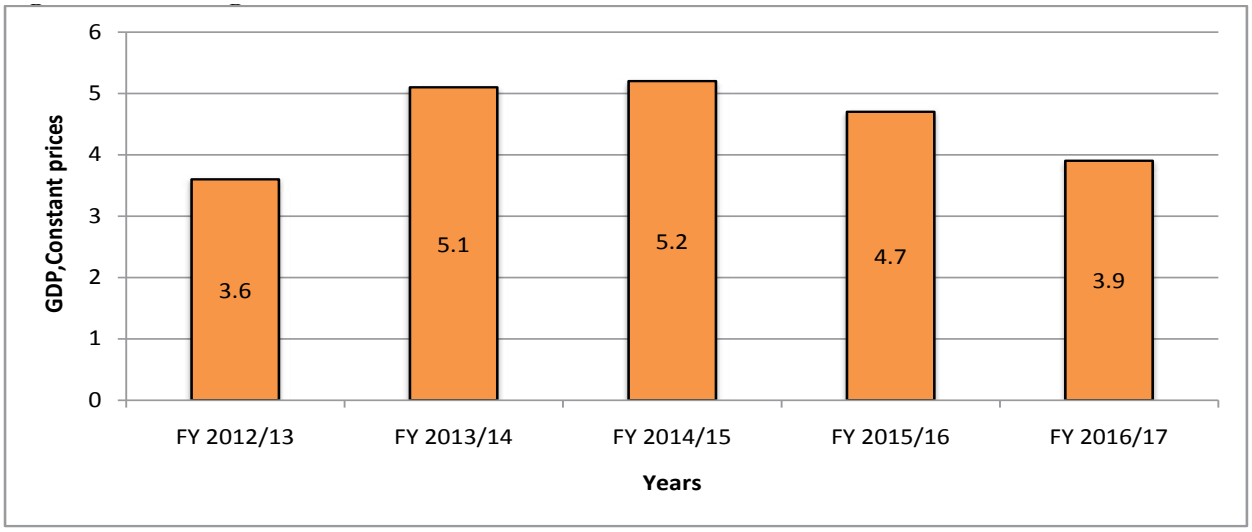
7.2 Situational Analysis

Uganda's population is currently estimated at 37.7 million people and is projected at 41.2 million people in 2020 (UBOS, 2017). Young people constitute the largest share of Uganda's population. The share of the population aged below 18 years is estimated at about 55 percent, while that of the primary school age population of 6 to 12 years is at 22 percent. The youth aged between 18 and 30 years constitute 21 percent of the population. The share of the population aged below 18 years is estimated at about 55 percent, while that of the primary school age population of 6 to 12 years is at 22 percent. The youth aged between 18 and 30 years constitute 21 percent of the entire population (UNHS, 2017).

The economy has over the last 5 years expanded at an average rate of about 4.5 percent. In the last two years, the country has experienced slow growth as indicated in figure 7.1 below. The economy constitutes

three broad economic sectors, namely Agriculture, Forestry and Fishing; industry and the services sector. In FY 2016/17, the agriculture, forestry and fishing sector accounted for 25.0 percent of the total Gross Domestic Product (GDP), while the industrial sector contributed 19.6 percent. The services sector is currently the biggest of the economy, having contributed 51.7 percent of total real GDP (MoFPED, 2017). The growth experienced in the industrial sector was mainly attributed to improved value addition in the manufacturing sector among others. In FY 2016/17, manufacturing grew by 2.5 percent, mainly on account of improvements in food processing, chemical and pharmaceutical production and cement and lime production.

Figure 7.1: GDP growth rates over the last 5 Financial Years (2012/13 – 2016/17)



Source: UBOS, FY 2016/17

7.3 Increasing youth employability through skills development

As Uganda pursues the vision of getting into the middle income category, youth unemployment has remained a major challenge for the country. Providing employment opportunities to the youth is paramount for the country's economic transformation. A critical mass of youth require employment to increase their incomes and better their standards of living. Youth unemployment or vulnerable employment is always likely to reduce the future productive potential and earnings of the people. Unemployment leaves them with limited incomes, and unable to access good health and education services (AfDB, 2017). For the youth to be sustainably employed, they need to be empowered through skills development.

Empowerment through skills development plays a critical role in providing them with better job opportunities in industries and related entities. It also enhances their business acumen. A number of countries have taken off and developed through creating a critical mass of personnel through developing vocational skills. For instance, China has over the years had several deliberate policies on skills development. The deliberate efforts have ensured that about one third (33%) of upper secondary school students are enrolled in vocational schools. This has largely contributed to the country's economic growth and transformation. Similar policies targeting vocational training for skills development were implemented in some European countries such as Germany. In contrast, the percentage of secondary school students enrolled in vocational training across many of the Sub-Saharan Africa remained low for many years.

Uganda has made great strides in ensuring that the majority of the young people attend school through the Universal Primary and Secondary Education. Many youth are also graduating from universities and entering into the job market. The youth often get jobs in the formal service sectors such as banking, insurance, finance, catering, communications, and information technology among others. However, jobs in such sectors are often characterised by relatively low employment elasticity. The sectors also often employ people that have excelled and with at least upper secondary school level.

On the other hand, the unskilled workers, including the youth often find jobs only in the informal services, including retail trade and distribution, passenger transport, catering and construction among others. It is often the case that wages and productivity in these sectors are very low. Employment in the manufacturing sector, particularly in traditional labour-intensive industries such as clothing and footwear often require on-the-job training and specific hands-on skills.

In 2015, the share of persons without work, and those actively looking for work among the economically active population was 6.5 percent. While Uganda has not been able to produce adequate jobs, the skills set among the job-seeking population has in most cases not matched the technical requirements of the labour market. This has been highly attributed to the education system that tends to focus people on enrolment at all levels of education, and less on imparting technical skills that are demanded in the job market. This could be the reason why Uganda's labour factor productivity is considered very low across the region (second lowest in EAC).

Evidence across all African countries shows that youth unemployment has been consistently rising with the level of education (AfDB, 2017). In fact, youth who have completed tertiary education on the entire continent are 2 to 3 times more likely to be unemployed than their counterparts with primary education or less (ILO, 2015). This clearly suggests that the existing education systems have and are not preparing young people with the requisite skills for the labour market. In Uganda, evidence shows that tertiary level unemployment rate was at 11.8 percent, while that of the young people with no education was 3.6 percent (UBOS, 2015).

7.4 Efforts to promote skills development in Uganda

In order to address the above anomalies, Government has put emphasis on promoting skills development, including through promotion of Business, Technical and Vocational Education Training (BTVET) among others. The legal and institutional frameworks in that regard have been upgraded to support skills training and development. The BTVET Act of 2008 and the skilling Uganda–BTVET Strategic Plan for FY 2012/13 – 2021/22 are among major instruments in place focusing on skills development to address the high unemployment rates among the youth.

It is highly recognised that investing substantial resources towards skills acquisition especially through vocational training is vital in accelerating human development and entrepreneurship development (AfDB et. al., 2017). In 2016, the World Bank (WB) approved a US$100 million credit to the Government of Uganda for the implementation of the Uganda Skills Development Project (USDP). The main objective of the project is to enhance the capacity of institutions to deliver high quality and demand driven training programs in key sectors such as agriculture, construction and manufacturing sectors.

The project also aims to create robust linkages between vocational training and industry which are critical aspects of harnessing the country's demographic dividend. Specifically, component 3 of the USDP focuses on the implementation of the Uganda Competitive Fund for employer-led short term training.

About US$ 18 million is dedicated towards providing grants for training activities through a Skills Development Facility (SDF), which is managed by the Private Sector Foundation of Uganda (PSFU). This presents a great opportunity for the youth to improve their skills and position themselves for better jobs and incomes.

Government has also invested public resources in training the youth to generate jobs and income growth. As of end 2016, a total of 114,471 youth (including 62,637 male representing, 55 percent and 51,834 female, representing 45 percent) were trained and directly received skills and financial support. The support facilitated them to generate 8,963 projects worth UShs 64,478,558,063 (MoFPED, 2017). More youth are being trained and all young people need to take advantage of the opportunities in place to enhance their skills for better jobs and incomes.

The above efforts notwithstanding, there is still much to be done especially with regard to creating awareness about the importance of BTVET education and skills development. There are still many people who perceive BTVET education for those that have failed at both primary and secondary school level. The BTVET institutions have continued to offer theoretical knowledge due to inadequate infrastructure for training students and imparting them with skills through practical sessions. This is highly attributed to insufficient Government funding to BTVET institutions. As a result, many graduates from such institutions get low-cost skills which do not match the current labour market demands.

Similarly, many institutions of higher learning especially universities are churning out many graduates every year. However, the majority lack or have inadequate hands on skills needed in the job market. Government has been not able to come up with a deliberate policy on skilling the educated youth, especially those that have graduated from tertiary institutions to give them the requisite skills through effective apprentice programmes. The universities have also continued to teach degree programmes that are not highly demanded and scrapping of such degree programmes has often met stiff resistance from key stakeholders.

Also, there are many youth who are uneducated, but are highly skilled. However, they have not been helped and supported to benefit from the existing formal opportunities. As such they have continued to operate informally, especially in Kampala city and the surrounding districts such as Wakiso and Mukono. Government through the second National Development Plan (NDPII) was to fast track certification of these youth to ensure that they benefit from the increasing opportunities, including those around the oil and gas sector among others. However, this has not yet been done and currently there are no concrete efforts in place to certify them before the end of NDPII period. This means that uneducated youth may not actually benefit from the employment opportunities around the major oil and gas core projects, such as the oil refinery and pipeline among others.

The other big challenge faced by the country is that whereas there are many initiatives to support and promote skilling of the youth in the country, majority of the initiatives are highly disjointed. The disjointed initiatives cannot effectively facilitate harnessing of the demographic dividend in the country, more especially employment creation and enterprise growth and development.

7.5 Youth employment through entrepreneurship development

Uganda has since the adoption of liberalisation as a development strategy in the early 1990s provided a conducive environment for the private sector to take leadership in the economy. This is due to the fact that across the globe, Micro, Small and Medium sized Enterprises (MSMEs) are highly associated

with considerable employment opportunities for the youth.

It is widely acknowledged that Ugandans have high aspirations and positive attitudes towards entrepreneurship (GEM, 2016). As a result, a large share of the active labour force, representing about 35.5% is engaged in entrepreneurship. The entrepreneurship levels in Uganda are highly concentrated in small and micro businesses, with about 2% of businesses expecting to employ 20 or more people in about five years. About 60% of the MSMEs operating business aged between 1 and 5 years are either sole proprietorships or partnership, which implies that at least one in every three people in the country is engaged in some kind of entrepreneurial activity (MTIC, 2015).

Uganda is among the top 3 countries (including Burkina Faso and Ghana) on the African continent that have seen a strong transition of early entrepreneurs to established businesses (AfDB et. al., 2017). An analysis of the experience from the three countries shows that support services and social norms play a major role in ensuring successful business start-ups in Africa. Key among the among the success factors include; presence of Government programmes that support the development of Small and Medium-sized Enterprises (SMEs); incorporation of training in creating or managing SMEs in vocational schools, colleges and business schools; presence of property rights and of commercial, accounting and other legal and assessment services and institutions that support or promote SMEs, and the social and cultural norms that encourage new business methods or activities. This presents an opportunity for harnessing demographic dividend in the country.

7.6 Steps to promote entrepreneurship in Uganda

Over the years, Uganda has undertaken a number of steps to promote entrepreneurship. The major steps include;

Strong promotion and access to microfinance as a critical factor in facilitating people (especially the youth and women for enterprise and job creation. This has been through strengthening laws and regulations to ease and streamline access to credit for investment. Government has strongly invested in capacity building for Microfinance institutions, through the Project for Financial Inclusion in Rural Areas (PROFIRA) and has extended credit through institutions such as the Microfinance Support Centre. This is intended to support and ensure growth and sustainability of SACCOs, support Village Savings and Loan Association (VSLAs) and Uganda cooperative Savings and Credit Union (UCSCU) and others to foster increased access to financial services for all including the youth. This presents a great opportunity for the youth to access credit and set up sustainable businesses and creates more jobs.

Government has also over the years developed a number of the initiatives such as the ***Youth Entrepreneurial Scheme*** (YES) in the 1990s. Also, the current Youth Venture Capital Fund and the Youth Livelihood Programme among others all targeting the youth to venture into business for self-employment.

Also, Government introduced entrepreneurship as a subject at both secondary and university levels of education. This is meant to impart practical knowledge and skills to enable young people become job creators after completion of their education. The country ranks highly in regard to entrepreneurship education at post school stage and internal market dynamics (GEM, 2017). Government is also through Enterprise Uganda offering training

and business advisory services to young entrepreneurs in regard to financial literacy and access to credit. All this presents an opportunity for harnessing the demographic dividend in the country.

Despite the above undertakings, there are gaps that have not been fully addressed. For instance, the youth venture fund was supposed provided hand in hand with entrepreneurship training and business development services. This includes incubation and development of workspace/infrastructure among others. However, these have not been well implemented and this means that many of the youth including those that access funds may not have acquired the requisite skills, attitude, knowledge and support services to use the funds effectively. It is these skills that greatly increase the business and employment opportunities for the youth.

Similarly, venture capital funds have often been associated with stringent criteria which prevents most of the youth, especially those leaving in rural areas from accessing the funds. Therefore, the overall objective of creating enterprises to close the unemployment gaps cannot be achieved with such stringent mechanisms of accessing credit.

Also, there are challenges relating to access to entrepreneur finance; R&D transfer; internal market burdens or entry regulation and Government policies in regard to taxes and bureaucracy (GEM, 2017). This could explain why there is a high business discontinuation rate at about 21%. Government needs to address the challenges so as to enable the youth develop sustainable businesses for increased job and income opportunities.

Government initiatives aimed at providing the youth with credit for business start-up have in most cases been misused. ***Youth Entrepreneurial Scheme*** (YES) of the 1990s suffered several challenges, including being seen as Government hand-out to the youth for free. Currently, the same situation is facing Youth Venture Capital Fund and the Youth Livelihood Programme. The two initiatives have been associated with governance issues as youth have sometimes received less than the anticipated financial support from the responsible people. In addition, the youth are in most cases not effectively trained to run businesses and so they put the credit received from Government into unproductive ventures and consequently are unable to pay back the loans.

7.7 Employment creation through labour intensive industries

During the early stages of economic development, low income countries such as Uganda usually tend to specialise in labour-intensive industries. Such industries have often been linked with increased output, job creation, poverty reduction and sustained and inclusive growth due to increased exports to global developed markets (UNIDO, 2016). With the increasing young population, the country is increasingly directing effort towards promoting labour intensive industries. Such industries are expected to play a major role in providing sustainable job opportunities for the youth which is critical for achieving the middle income aspiration.

Uganda needs to focus on promoting labour intensive industries especially those that use domestically produced raw materials. This is aimed at creating job opportunities so as to benefit from the increasingly unemployed youth in the country. Pro-poor economic and industrial policies are those that often put emphasis on increasing the economic returns to the productive factors that the poor (including the youth) possess. These could include, raising returns to unskilled labour among others (UN,2016). Policies that promote higher returns to capital and land have been associated with increased inequality. As a result, the use of capital-intensive instead of labour-intensive methods often leads to an increase in income disparities and this hinders opportunities for harnessing

the demographic dividend and economic transformation.

There is also need to strengthen the labour intensive industry policies, such as the 2014 Buy Uganda, Build Uganda (BUBU) and the local content policies. The policies provide for the need to support locally manufactured products, knowledge transfer, and human capital development. Effective implementation of such policies will greatly benefit the youth as it will encourage them to undertake strong business ventures including starting up industries. It will promote job creation and entrepreneurship to drive the country into the middle income category by 2040.

Despite having such an advantage, there is evidence to show that only a few developing countries, especially in East Asia and South East Asian (such as Korea, Singapore, and Taiwan, and more recently, China and Vietnam) have succeeded in the production and exportation of labour–intensive manufacturing products (UN, 2007). Currently, the youth are not aware of what the BUBU and local content policies are about and how they are meant to support them to grow business. Also, labour intensive industries require adequate skills for the youth to benefit from the industries and related policies. However, the youth are not adequately organised and trained to take up such opportunities. This may not have a sustainable impact in regard to the aim of harnessing demographic dividend in the long run.

7.8 Stimulating local production through Technological Transfer and Foreign Direct Investment

Technological change and innovations are key for the economic growth and broad structural transformation, if Uganda is to harness demographic dividend. As economies technologically advance, the more productive and profitable sectors and firms tend to displace the less productive and profitable ones. This has been termed as ''creative destruction''. This often leads to an increase in the aggregate productivity in such economies (UN, 2007). Uganda like many countries on the African continent are far below other developing countries in regard to deployment of technology in aspects of production and productivity (Agola, 2016).

Whereas Uganda aims at becoming a middle income country by 2040, her export basket is still dominated by exporting primary commodities. This is clear evidence to show that the manufacturing sector is under developed. As a result of exporting unprocessed commodities, Uganda is always at a disadvantage in trading at the international level. This is due to the fact that unprocessed commodities offer lower prices as compared to processed, value added and packaged products in the international markets (UNIDO, 2016). The prices from exporting primary products cannot motivate the youth to engage in sectors such as agriculture.

Technological Transfer and Foreign Direct Investment also encourage businesses and universities to carry out research (AfDB, 2017). This could play a critical role in building entrepreneurship and strengthening industrialisation through building the capacity of Uganda's youth graduating from universities and other institutions in science and technology related fields. FDI flows to Uganda has been increasing over the last decade, with the annual inward and outward flows and stock, increasing from US$ 644.3 million in 2006 to US$ 1205.4 million in 2012, and decreasing to US$ 541.2 million in 2016.

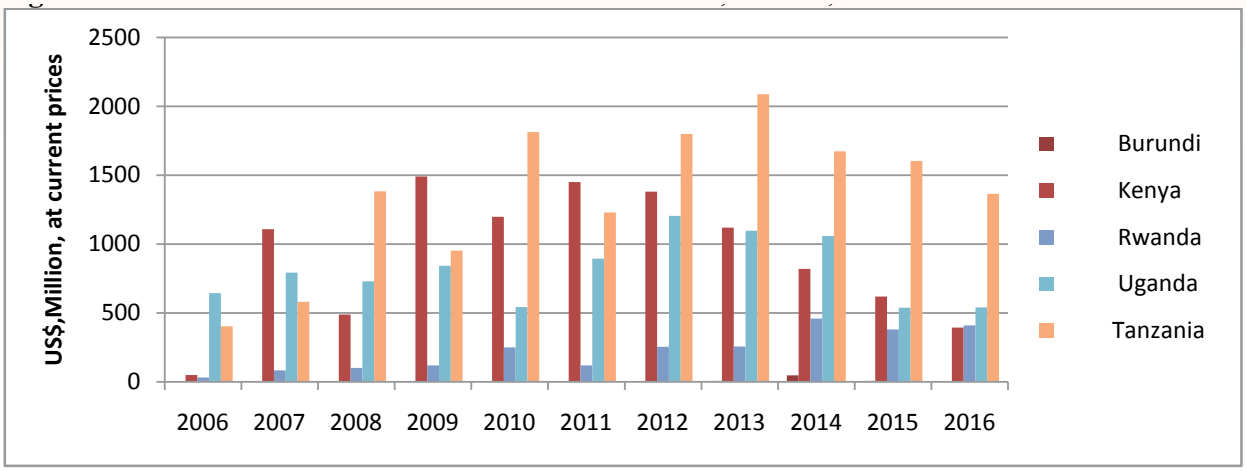
Oil Drilling along Lake Albert Shores, Bulisa District, Uganda

Uganda is only second to Tanzania among the East African Community (EAC) regional peers with regard to the inward and outward flows and stock of FDI as shown in Fig 7.2 below. The country is fast tracking improvements in technology and innovation and has established key institutions that are responsible for public investments in technology and innovation related such as the Ministry of Science, Technology and Innovation.

In addition, the country has directed efforts and put much emphasis on science teaching and training. This has for instance been through paying higher wages to science teachers, building science labs and allocation of more Government sponsored slots to science students at all public universities. These efforts are expected not only to attract investors, but will also offer jobs to the educated and skilled youth in the country. However, this will yield the anticipated results only if the youth acquire practical and relevant skills to uptake the increasing technological developments.

Also, the country's FDI flows have over the last decade been towards the oil and gas sector and a few in the telecommunication and banking sector. These sectors require advanced skills which are scarce in the country. Many youth have not yet benefited much from the investments in such sectors as they require certain skills that many of the youth do not have. Also the number of FDI related firms is still inadequate compared to the large number of entrants in the labour every year. The benefits will be much higher when the country develops the requisite skills in oil and gas for the youth to acquire direct and indirect jobs and when the conducive environment is created to attract many investments into the country.

Figure 7.2: FDI- Inward and outward flows and stock, annual, 2006-2016



Source: UNCTAD data set, 2017

7.9 Increasing local production capacity of domestically manufactured goods through industrialisation

As the country moves to attain the middle income status, increased local production capacity of domestically manufactured goods will play a major role in achieving the aspiration. This will be achieved through faster progression on the industrialisation agenda. Industrialisation facilitates reallocation of resources from low-productivity to higher-productivity sectors of the economy (AfDB et. al., 2017). Through industrialisation, the country will be able to improve productivity and add value to locally produced products. Uganda will also be able to compete with other developing countries, and hence achieve the target of becoming an upper middle income by 2040.

Kakira Sugar Works Factory in Jinja Districts

Industrial development has played a major role in accelerating economic growth and poverty reduction in many of the developing countries such as China and Indonesia among others. Industrialisation is highly associated with job creation, higher productivity and innovation (UN,2007), and it is at the higher end of Uganda's Development Agenda as enshrined in second National Development Plan (NDPII) and the Vision 2040. Uganda's aim is to accelerate industrialization and to increase the share of industry in GDP from 26.4 percent in 2010 to 31.4 percent in 2040. This is in line with Sustainable Development Goal 9, target two which requires that countries promote inclusive and sustainable industrialization by 2030, and to significantly raise the industry's share of employment and gross domestic product, and double its share in least developed countries taking into account the national circumstances (UN, 2015). Increased industrialisation will offer better direct and indirect jobs to the youth.

Uganda is increasingly becoming integrated at the regional, continental and intercontinental level. The country is a member of the East African Community (EAC), Common Market for Eastern and Southern Africa (COMESA), the Continent Free Trade Area among others. The country is also increasingly trading with the emerging markets such as China and India. With this huge market potential, the level of industrialisation will have to greatly improve so as to meet the expanding market opportunities, especially for the tradable manufactured goods, modern services and processed agricultural products, in which the country has a comparative advantage.

Uganda has not been able to strongly increase production of domestically manufactured products due a number of constraints including infrastructure (roads, energy, etc.) among others. In that regard, Government has over the last two decades directed efforts towards addressing the major impeding constraints focusing mainly on addressing the existing infrastructure gaps.

7.10 Major undertakings for increased local capacity of domestically manufactured goods and value addition

A number of undertakings are currently on going and more especially infrastructural development such as construction of more power dams (such Karuma and Isimba projects among others) and is expected to add 800 MW to the national grid. The initiatives also include construction of better roads linking market and production centres, development of industrial parks among others.

Government is also fast tracking the construction of the standard Gauge railway to ease the transportation of goods and services to and from the sea port of Mombasa in Kenya. The aim is to reduce the cost of production (power and transport) which has been a huge constraint to private sector growth and development. It discourages entrepreneurship and industrialisation and consequently impacts negatively on the middle income country aspirations. Government targets to complete all on-going projects on power and major roads by FY 2019/20 to increase power supply and reduce power tariffs. This is envisaged to lower the operational costs and increase production and productivity.

Government has put in place the Free Zones Act, 2014 which makes provision for the establishment, development, management, marketing, maintenance, supervision and control of free zones. It established the Free Zones Authority as a body corporate to establish, develop, manage, market, maintain, supervise and control Free Zones. The purpose of establishing Free Zones is to promote investment in export-led industrialization, create employment and promote technology transfer. It also aims to enhance the linkages between the domestic market and the regional and international markets, and to enhance value addition

through processing of raw materials without endangering the environment.

The above notwithstanding, there are some challenges that require attention on the part of Government. For instance, currently the country has no regulatory environment for Special Economic Zones. The current law on Free Zones requires a review to encompass all forms of economic zones, including Free Zones for broader benefits in relation to harnessing demographic dividend. This will be able to increase production and promote regional balance and the associated job opportunities for youth.

The New Roofings Uganda Limited Steel Rolling Mills at Namanve Industrial Park, Kampala

Also, many of the core projects are undertaken by foreign firms and these firms often employ few Ugandans. The local firms are not involved in development of such projects and therefore their capacity is not developed to undertake similar projects in the future. Local firms have the potential to construct such projects at a relatively lower cost than foreign firms and to employ the youth. The projects have also been marred with shoddy works and this has caused delays in the completion of projects. This increases the cost on Government, as the resources spent due to delays could have been devoted to other sectors of the economy such as agriculture and social sectors.

7.11 Conclusion

For a country that aspires to transform society from a peasant to a modern and prosperous one, Uganda will need to fast track all interventions that are aimed at facilitating entrepreneurship and industrialisation to be able to harness demographic dividend. The two will play a critical role in increasing value addition of exports including through agro-processing and manufacturing to meet demand requirements in both regional and international markets, creation of better jobs more especially for the youth, majority of who are currently unemployed. However, this will need to be accompanied by educated

and skilled youth who constitute the largest proportion of the population.

7.12 Policy Recommendations

1. **Address the cost of production.** There is need to fast track completion of the on-going infrastructure projects, especially those relating to access to electricity. The cost of power is still very high and this discourages potential investors in the industrial sector. It also hinders entrepreneurship and job creation, especially by the youth as the cost of power and transportation in Uganda is still very high.

2. **Strengthen the skills development at both secondary and tertiary institutions.** Whereas the country is churning out many graduates from university, they have been found in shortage of the labour market demanded skills. It is for that reason that many have remained unemployed. There is need for a policy on apprenticeship training and on-the-job training for the young people especially graduates and school drop outs to acquire practical skills that are relevant in the labour market.

3. **Strengthen and Implement labour intensive policies.** There is need to strengthen the labour intensive industry policies and fast track implementation of the 2014 Buy Uganda, Build Uganda (BUBU) and the local content policies. This should be done taking into account the regional integration objectives and aspirations. If well implemented, the policies will promote entrepreneurship and industrialisation, production and productivity and job creation, more especially for the youth, the majority of whom are unemployed.

4. **Encourage and support investors that set up labour intensive industries with productive incentives**. They will use local raw materials and labour rather than capital intensive industries. This should be done through providing productivity enhancing incentives such as cheap electricity. Continued support of capital intensive industries will not create the requisite jobs to absorb the increasing number of youth.

5. **Fast track efforts around enhancing value addition such Special Economic Zones.** The country has continued to export unprocessed commodities to both regional and international markets. This has led to low gains in terms of export revenues, but with more revenue spent on imports. This in turn has led to unfavourable terms of trade for the country. Special Economic zones will be able to promote value addition and job creation.

6. **There is need to consolidate all on-going skills training initiatives in the country**. Government should consider consolidating all skills training and development under a single and coherent skills development framework, more especially the Skilling Uganda programme. This will promote accountability of all the public investments being directed towards youth development.

7. **Strengthening the linkage between local MSMEs and large enterprises**: In order to ensure maximum benefits of entrepreneurship and industrialisation, it is important that the local companies and MSMEs in general take advantage of the potential opportunities, especially

the supply chains in which the large enterprises are operating in the country. This will promote increased productivity and employment opportunities for the youth.

8. **Need to retool the BTVET institutions**. This will enable them offer theoretical and practical knowledge to students and impart them with market demanded skills through practical sessions. Government needs to set aside funds for upgrading BTVET institutions.

9. **Fast tract certification of the uneducated skilled youth**. This is supposed to be done in order to enable them acquire formal employment, more especially as the country moves close to oil and gas production with the oil refinery and pipeline due for construction.

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Appendix

Appendix 1: Demographic, Health and Social, Economic and Development Indicators 2010/11 – 2016/2017

KEY INDICATORS	2010/11	2016/17
Demographic Indicators		
Total Population (millions)	31.8	37.7
Annual Population Growth Rate (%)	3.2	3.0
Total Fertility Rate	6.2	5.4
Health Indicators		
Infant Mortality Rate (IMR) per 1,000 live births	54	43
Under Five Mortality Rate per 1,000 live births	90	64
Maternal mortality Ratio per 100,000 live birth	438	336
Contraceptive Prevalence Rate (%)	30	39
Unmet need for Family Planning (%)	23.8	28
HIV Prevalence Rate (%)	7.3	6.8
Economic Indicators		
GINI Coefficient (Inequality measure in household consumption)	0.426	0.426
Percent of Population below the Poverty Line (%)	24.3	27
Environmental Indicators		
Proportion of Households using Biomass for cooking	99	94
Proportion of population with access to Electricity for Lighting	14	21
Proportion of Households with access to Toilet facilities (%)	69	92
Proportion of Households with access to safe drinking water (%)	70.2	72
Burden of Disease	**2010/11**	**2015/16**
Malaria (%)	36.0	35
Cough or Cold (%)	19.0	25
Intestinal Worms (%)	5.0	6
Acute Diarrhoea (%)	3.0	4
Skin Diseases (%)	3.0	3
All Others (%)	34.0	27

Source: Statistical Abstract 2010, 2011, 2012, 2013, 2014 and 2015; UDHS 1995, 2000/01, 2005/06, 2010/11 and 2015/16; Population and Housing Census Main Report 1991 and 2002, 2014 National Population and Housing Census, Provisional Results; Background to the Budget FY 201/11, 2011/12, 2012/13, 2013/14 and Human Development Report 2010, 2012, 2014, Uganda AIDS Indicator Survey Report 2011, Annual Budget Performance Reports (FY 2010/11 – 2013/14).

Appendix 2: Population and Development Indicators in Uganda, 1994/95 – 2016/17

Population and Development Indicators		1994/1995 Base-line	2000/2001	2005//2006	2010/2011	2016/2017
Mortality						
Infant Mortality Rate per 1,000 live births		97	88	76	54	43
Under -5 Mortality Rate per 1,000 live births		-	152	137	90	64
Maternal Mortality Ratio per 1,000 live births		505	505	435	438	336
Life Expectancy (years)	Male	48.8	48.8	-	-	62.2
	Female	52.0	52.0	-	-	64.4
Education						**2015/2016**
Gross Primary enrolment (%)	Male	48	130	118	128	117
	Female	36	124	117	120	118
Gross Secondary Enrolment (%)	Male	-	38.2	31.6	30.8	32.0
	Female	-	30.4	18.1	26.5	28.0
Percent Illiterate (age above 15 years)	Male	36	22.2	16	21	21
	Female	55	42.3	39	36	36
Reproductive Health						
Contraceptive Prevalence	Any method	15	19	24	30	39
	Modern Method	8	14	18	26	30
Unmet Need for Family Planning		25	35	41	34	28
HIV Prevalence Rate (%) 15-49 years	Male	5	5.1	-	-	-
	Female	7.5	8.3	-	-	-
Women Age 15-19 that have began child childbearing (%)		43	31	25	24.3	24

Source: UBOS Statistical Abstract 2012, UDHS 2011, 2016, UNHS 2009/10, 2002, 2017 Population and Housing Census Main Report (2005 and 2016), 1991 Population and Housing Census, Analytical Reports (1995), Volumes I, II and III, and Uganda AIDS Indicator Survey Report 2011

Appendix 3: Selected Key Demographic Indicators Reflecting Performance of the National Population Policy and Programme in Uganda

Key Indicator	Census Indicator Level		
	1991	2002	2014
Total Population (million)	16.7	24.4	34.6
Population Growth rate (%)	2.5	3.2	3.0
Percent Population under 15 years (%)	48.5	49.3	47.9
Average Household Size	4.8	-	4.7

Key Indicator	Uganda Demographic Health Surveys					
	1988/89	1995	2000/01	2005/06	2010/11	2015/16
Total Fertility rate	7.4	6.9	6.9	6.7	6.2	5.4
Infant Mortality rate	122	95	88	76	54	43
Under 5 Mortality rate	205	147	152	137	93	64
Contraceptive Prevalence rate (%)	4.8	14.8	22.8	23.7	30	39
Unmet need for Family Planning (%)		25	35	41	34	28

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