Uganda's Public Debt is Growing too high: should Ugandan's be Concerned

Presenter: Mr. Corti Paul Lakuma

Presented to **Rotary Club of Kampala North, 14th** , June, 2021

1 Background

2 General issues to consider

3 Issues to consider in the context of COVID 19

4 Conclusion

5 Policy recommendations

Background

INTRODUCTION

- Matters of debt acquisition, structure, usage and sustainability have increasingly come to the fore following COVID 19 that has triggered an economic crisis and global recession that has persisted longer than predicted.
- Besides, implications on developing countries such as Uganda raise fresh concerns about economic resilience in light of global shocks and turbulence.
- Memories of previous economic crises such as the financial crises of 2008, Mexican crisis of 1994 and the Asian crises of 1997 demand a review of current conditions in order to draw parallels and differences for relevant policy implications.

Background

INTRODUCTION

- In Uganda, the stock, structure and sustainability of the national debt have become contested issues for a number of reasons. For example, one of the main issues is related to sustainability that government is not a problem largely on the basis of the debt/GDP ratio of less than 40 or 50%.
- Yet debt sustainability encompasses a broader definition “the ability of a country to meet its debt obligations without requiring debt relief or accumulating arrears” . Accordingly, the the sustainability indicators used by government, notably the Debt/GDP ratio need to be augmented by other indicators such as debt/export ratio and debt/tax revenue ratio.

Background

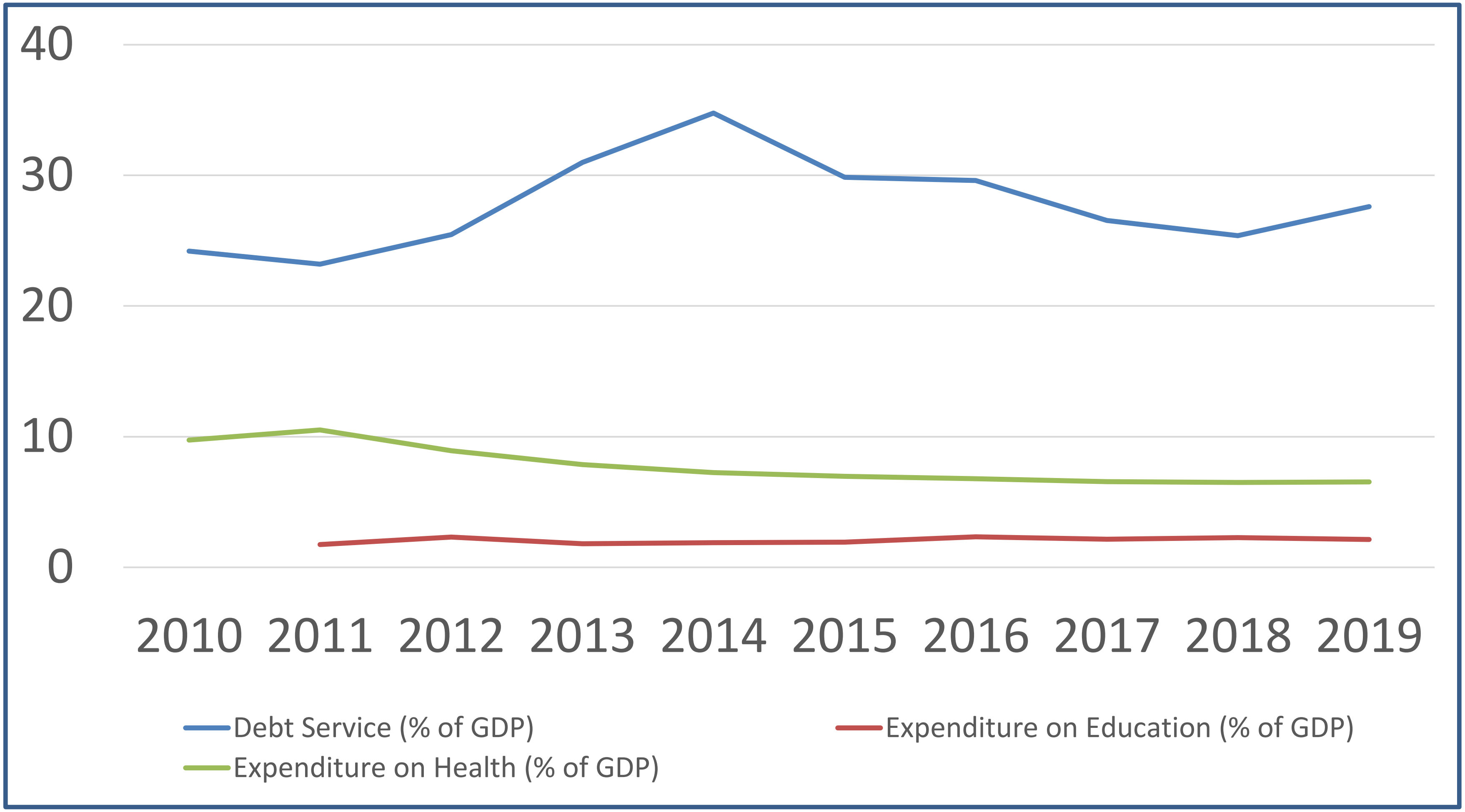
INTRODUCTION

- The relevant debt sustainability assessment methodologies for Uganda would be the Heavily Indebted Poor Country (HIPC) Debt Relief Analysis (for comparison with past trends when Uganda was a HIPC) and the Low Income Country Debt Sustainability Framework (LIC-DSF). These analyses involve making projections of intended borrowings and economic variables over a maximum 20-year period, and then using ratios comparing debt stock, present value or service with GDP, exports or budget revenue to assess payment capacity .
- But we must also be reasonable and evaluate debt in the context of the disruptions caused by COVID 19. Beyond health risks, the COVID-19 shock to African economies is coming in three waves: (i) lower trade and investment from China in the immediate term; (ii) a demand slump associated with the lockdowns in the European Union and OECD countries; and (iii) a continental supply shock affecting domestic and intra-African trade.

Key General Issues to Consider

Key General Issue to Consider

Figure: Debt Service Crowds out Service Delivery to the Poor



Key General Issue to Consider

Key Debt Indicators

- Country Policy and Institutional Assessment (CPIA) framework of the World Bank. On the basis of the CPIA rating, Uganda’s debt burden thresholds are:
- (i) Present value (PV) of debt-to-GDP ratio of 50%;
- (ii) PV of debt-to-exports ratio of 200% (the debt reference ratio of set at 150%).
- (iii) PV of debt-to-revenue levels of 300%; debt service-to-exports ratio of 25%; and debt-service and
- (iv) debt service-to revenue-ratio of 35%.

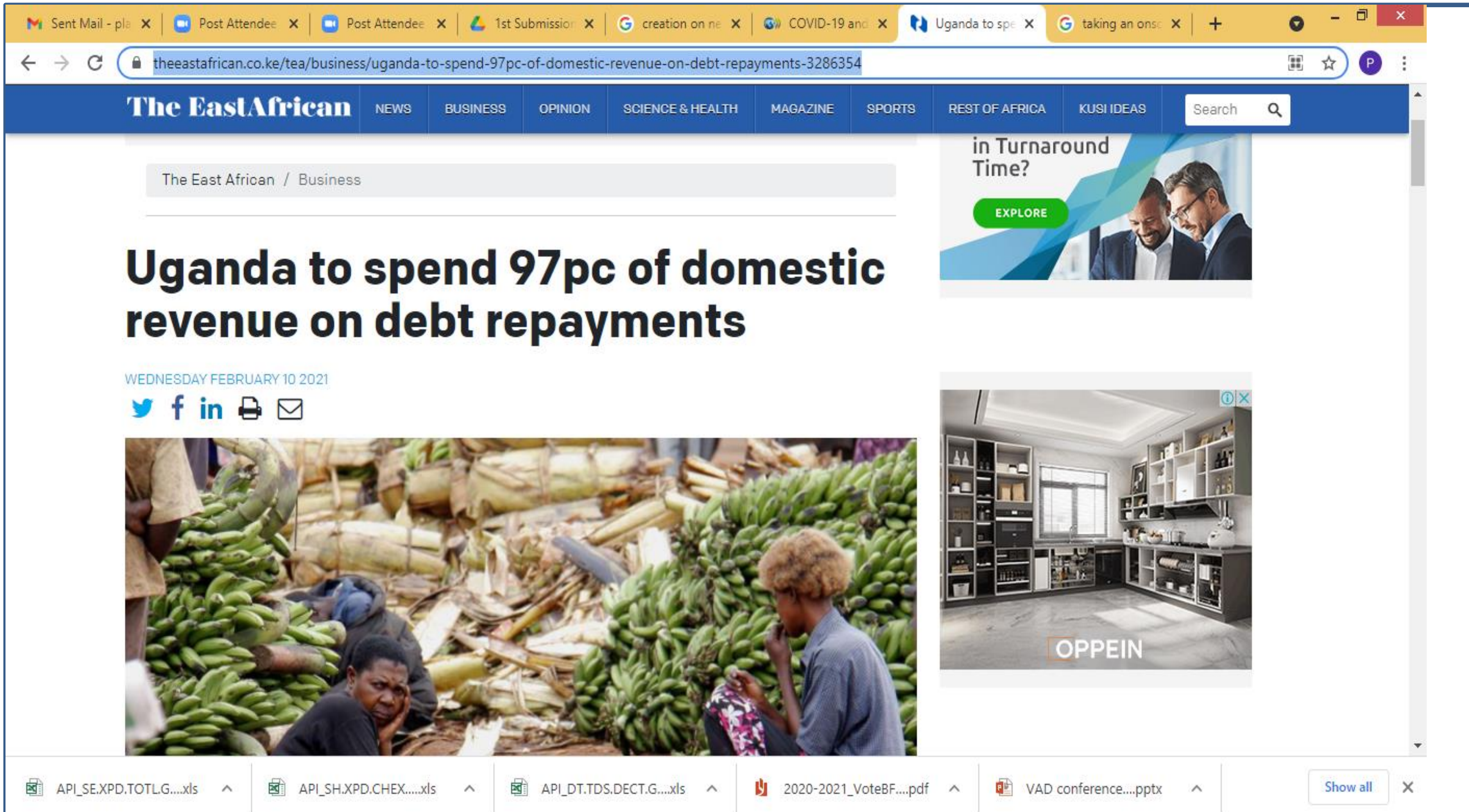
Key General Issue to Consider

Consequences of Uganda's Debt

- Deterioration of other economic variables like the stock of foreign exchange reserves
- Inability to deliver critical services due to debt service obligations.
- Unsustainable debt levels can also lead to instability in key macroeconomic variables such as inflation and exchange rates by imposing pressure on foreign reserves and budget resources.

Key General Issue to Consider

Uganda spends almost all of her domestic revenue on debt repayment


theeastafrican.co.ke/tea/business/uganda-to-spend-97pc-of-domestic-revenue-on-debt-repayments-3286354

The EastAfrican NEWS BUSINESS OPINION SCIENCE & HEALTH MAGAZINE SPORTS REST OF AFRICA KUSI IDEAS

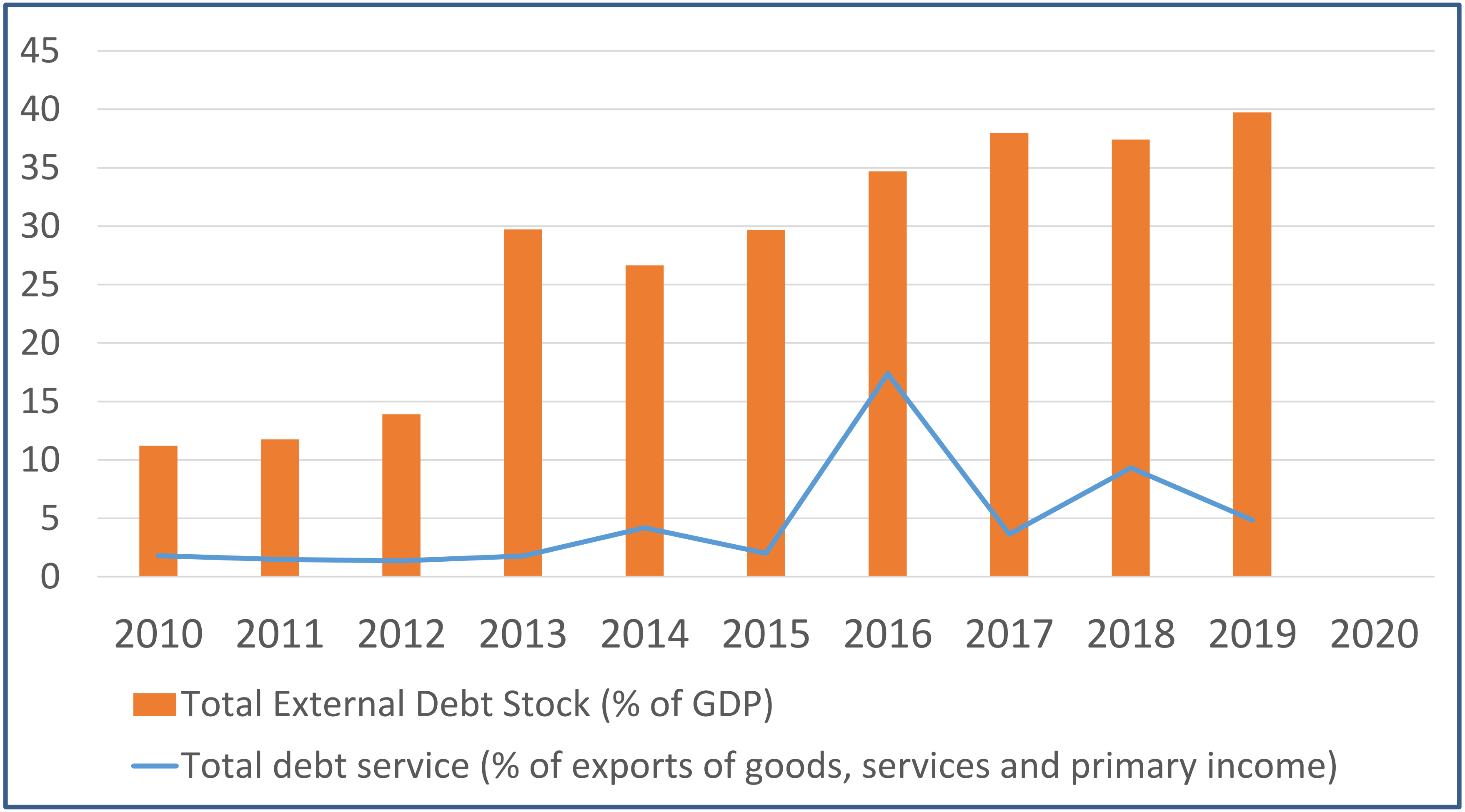
The East African / Business

Uganda to spend 97pc of domestic revenue on debt repayments

WEDNESDAY FEBRUARY 10 2021

Key General Issue to Consider

Stock of total external debt (% of GDP) and Debt service (% of exports of goods and services



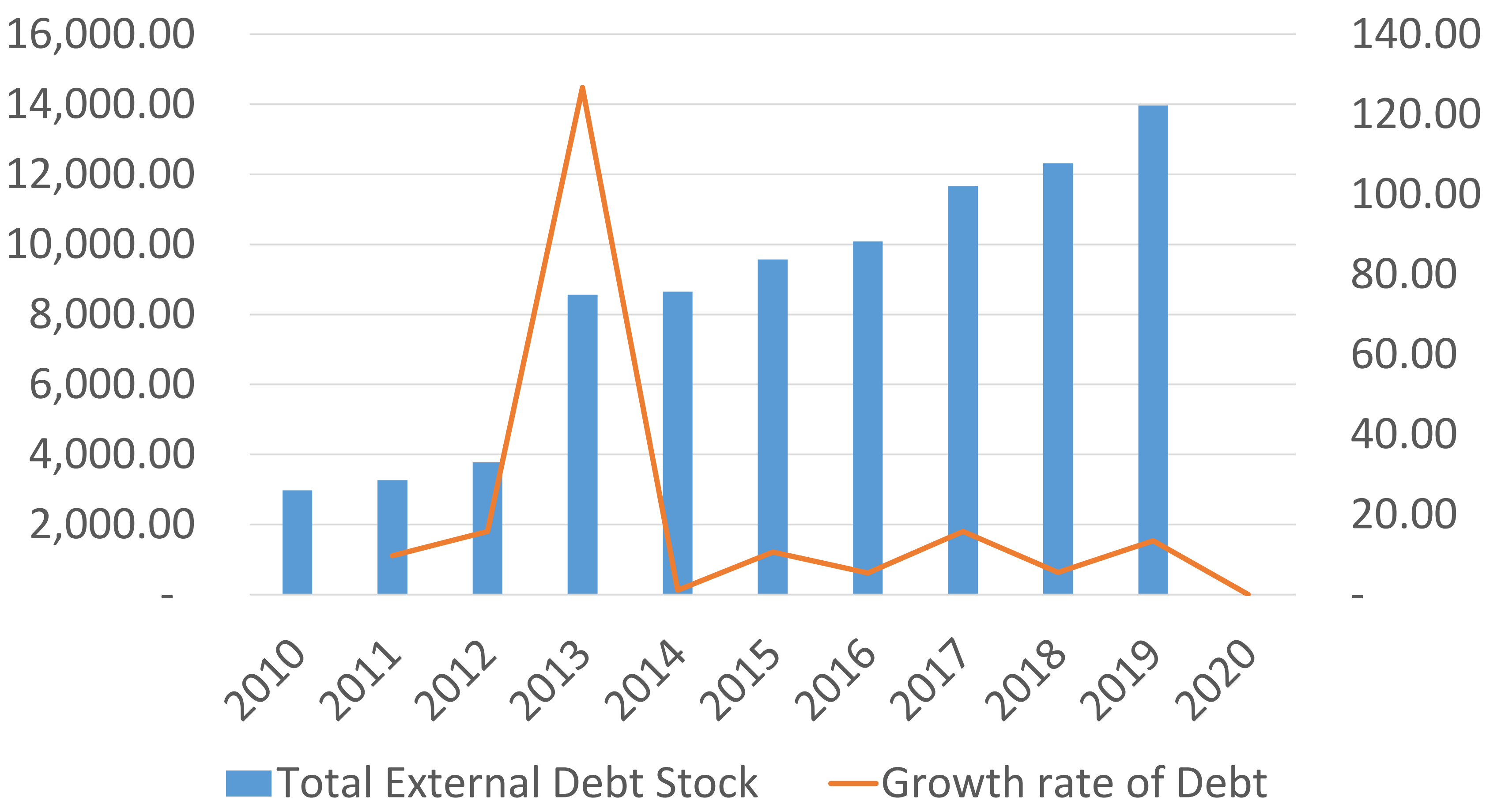
Key General Issue to Consider

Stock of total external debt (% of GDP) and Debt service (% of exports of goods and services

- The external debt stock as a percentage of GDP remained above 40%.
- Debt service, as a percentage of exports of goods and services increased to nearly 200% in 2016, largely on account of poor export performance.
- The heavy debt burden also affects government ability to stimulate economic growth including exports that led to deterioration of the current account.

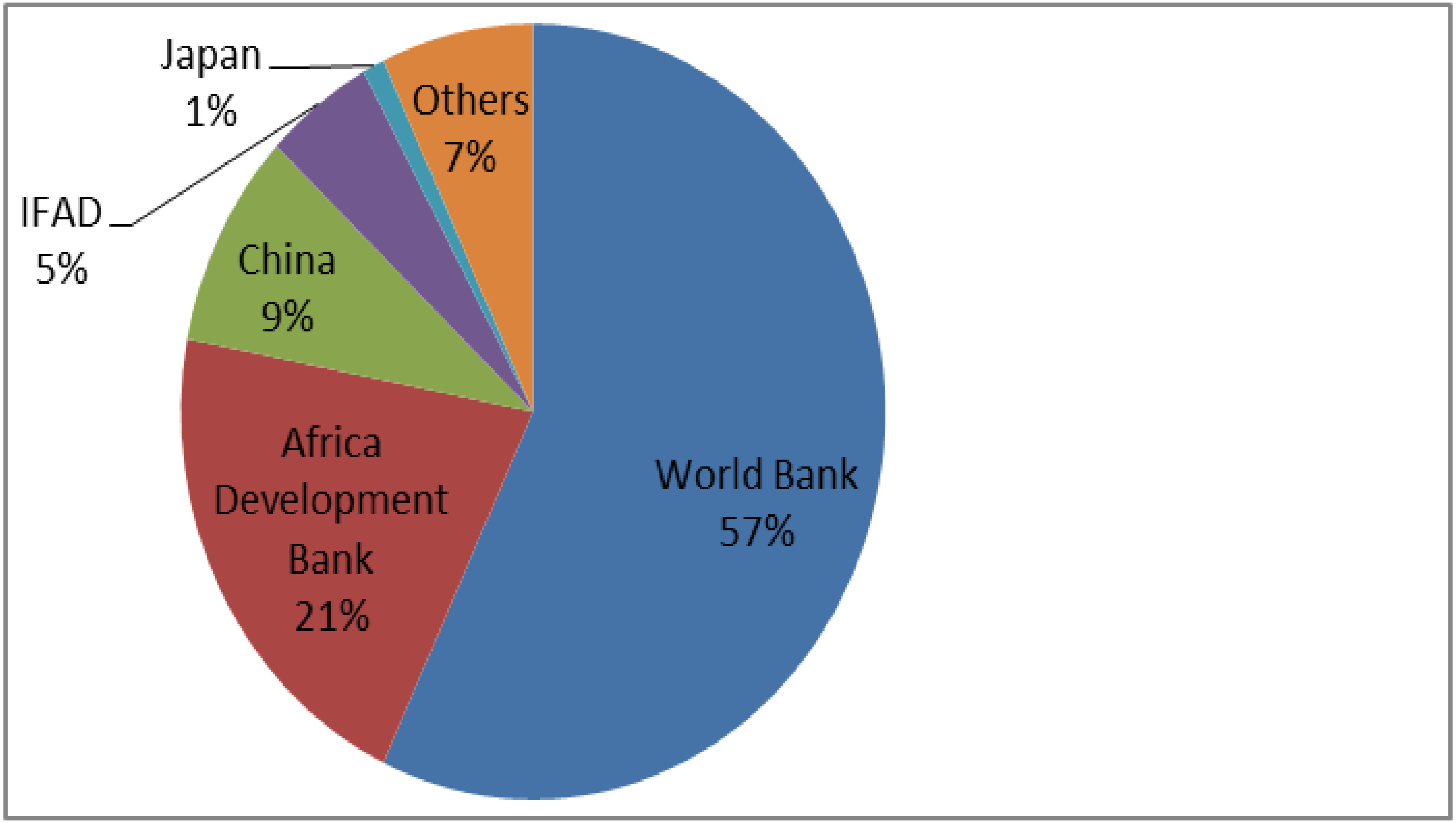
Key General Issue to Consider

Trend in Stock of total external debt US$ million)



Key General Issue to Consider

Source of Uganda's Debt



Key General Issue to Consider

Key Issues from External debt

- There is a need concerns about the contribution of this debt to the economy and future sustainability.
- The argument, presented in the NDP III, that new debt being contracted, which is largely being committed to infrastructure, will increase productivity and economic growth by bridging the infrastructure gap, appear to be simplistic as it assumes that infrastructure is the only driver of productivity.
- More so, government seems to assume that productivity will increase uniformly across the traded and non-traded sectors. In the event that productivity in the non-tradable sector increases faster or is the only one increasing, which is often the case in countries with sustained budget deficit, both tax revenues and exports are likely to grow less than expected.

Key General Issue to Consider

Key Issues from External Debt

- Reviews of Uganda’s capital accumulation process have indicated that it was biased towards construction rather than equipment and had a positive but weak impact on productivity . Borrowing, especially short- to medium term that is intended for increasing productivity, should target presence of excess capacity and not investments of a long-term nature, which should be built using long-term debt.
- Otherwise, a stronger impact of capital accumulation on productivity depends on government use of domestic tax revenues and long-term debt to finance public investment, as well as reform of the financial sector to mobilize domestic savings and channeling them into private sector investments. Domestic savings would include remittances from citizens working abroad.

Key General Issue to Consider

Composition of Domestic Debt

	Maturity	Stock (Shs)	Stock (US$)	% of total stock
Treasury Bills	91 days	69,071,327,632	23,824,435.7	0.80
	182 days	250,577,353,539	86,430,422.93	2.80
	364 days	2,612,382,445,105	90,076,319.89	29.00
	Sub-total	**2,932,031,126,276**	**1,011,331,178.57**	**32.60**
Treasury Bonds	2 years	1,602,668,259,355	553,145,461.60	17.80
	3 years	1,147,373,799,305	395,758,041.69	12.70
	5 years	1,869,578,077,050	644,864,436,.51	20.80
	10 years	1,091,031,667,429	367,324,255.27	12.10
	15 years	356,726,001,613	123,043,577.76	4.00
	Sub total	**6,068,377,804,752**	**2,093,135,922.83**	**67.40**
Grand Total		**9,000,408,931,028**	**3,104,467,101.40**	**100.00**

Key issues on Domestic Debt

- The structure of domestic debt indicate a reality of heavy concentration of debt under 5 years, as well as a significant portion under treasury bonds, which are largely contracted for monetary purposes.
- In terms of debt repayment, the information described in the table shows that, nearly US$ 3 billion or 12% of GDP, of debt will be due in the next 10 years. This excludes interest repayment on this and any new short-term debts to be contracted within the same period.

Composition of Domestic Debt

- There should be a concern knowing that part of the previous domestic debt was not being retired but rescheduled – rolled over. The near exponential increase in domestic debt raises concern of debt sustainability, more so when the conditions responsible for the increase, mainly financing the government budget deficit, are still ongoing.

Key Issues to Consider in the Context of COVID 19

Key Issue to Consider in the context of COVID 19

Figure: Government Fiscal Position, %

	2018/19	2019/20	2020/21
Domestic Revenue	12.70	12.50	12.80
Grants	0.90	0.80	1.20
Expenditure	18.50	20.50	23.80
Fiscal Deficit (including grants)	-4.90	-7.20	-9.80
Nominal Debt	35.40	40.20	47.50

Figure: % of Uganda's firms experiencing new constraints with COVID-19

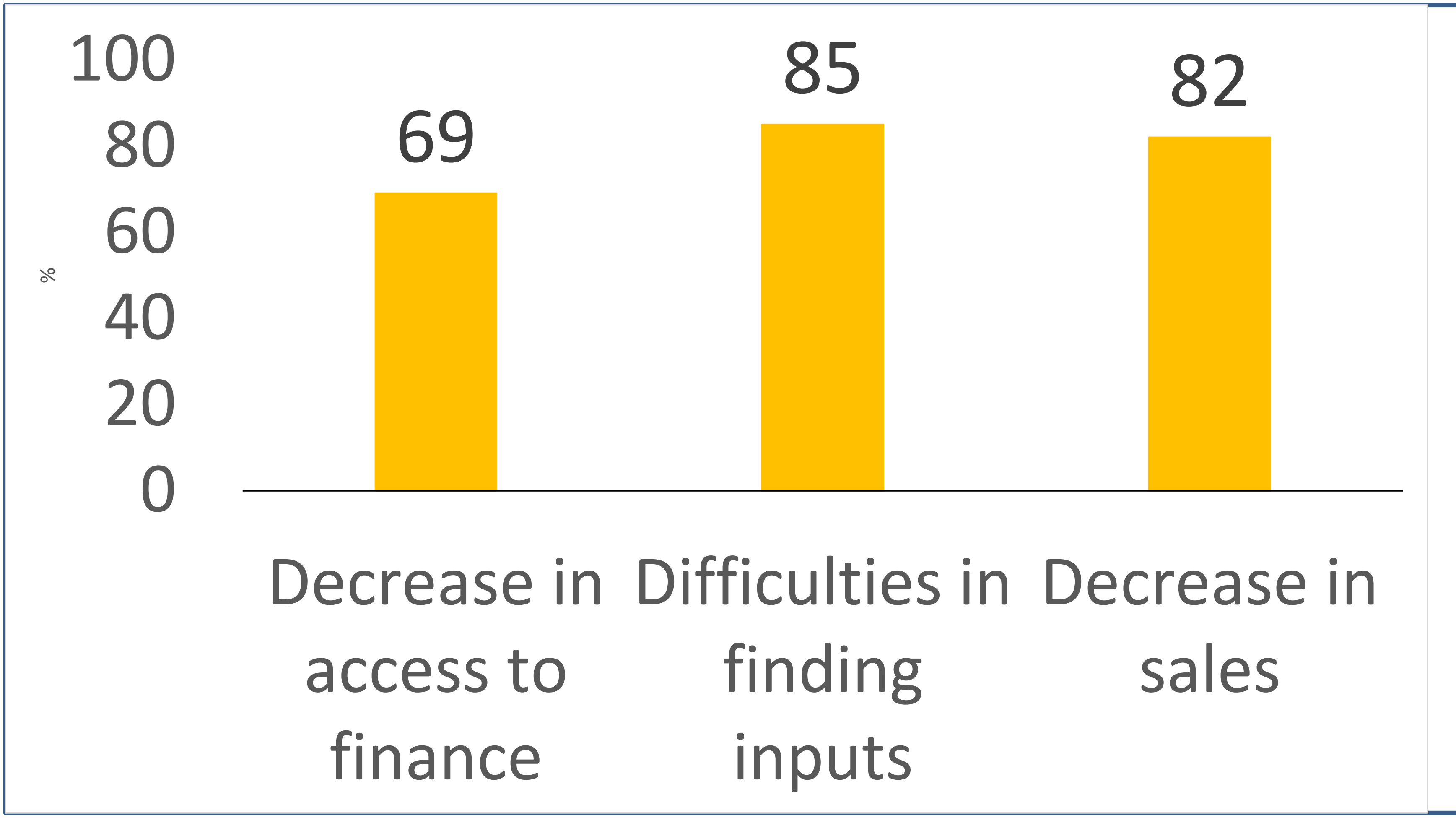
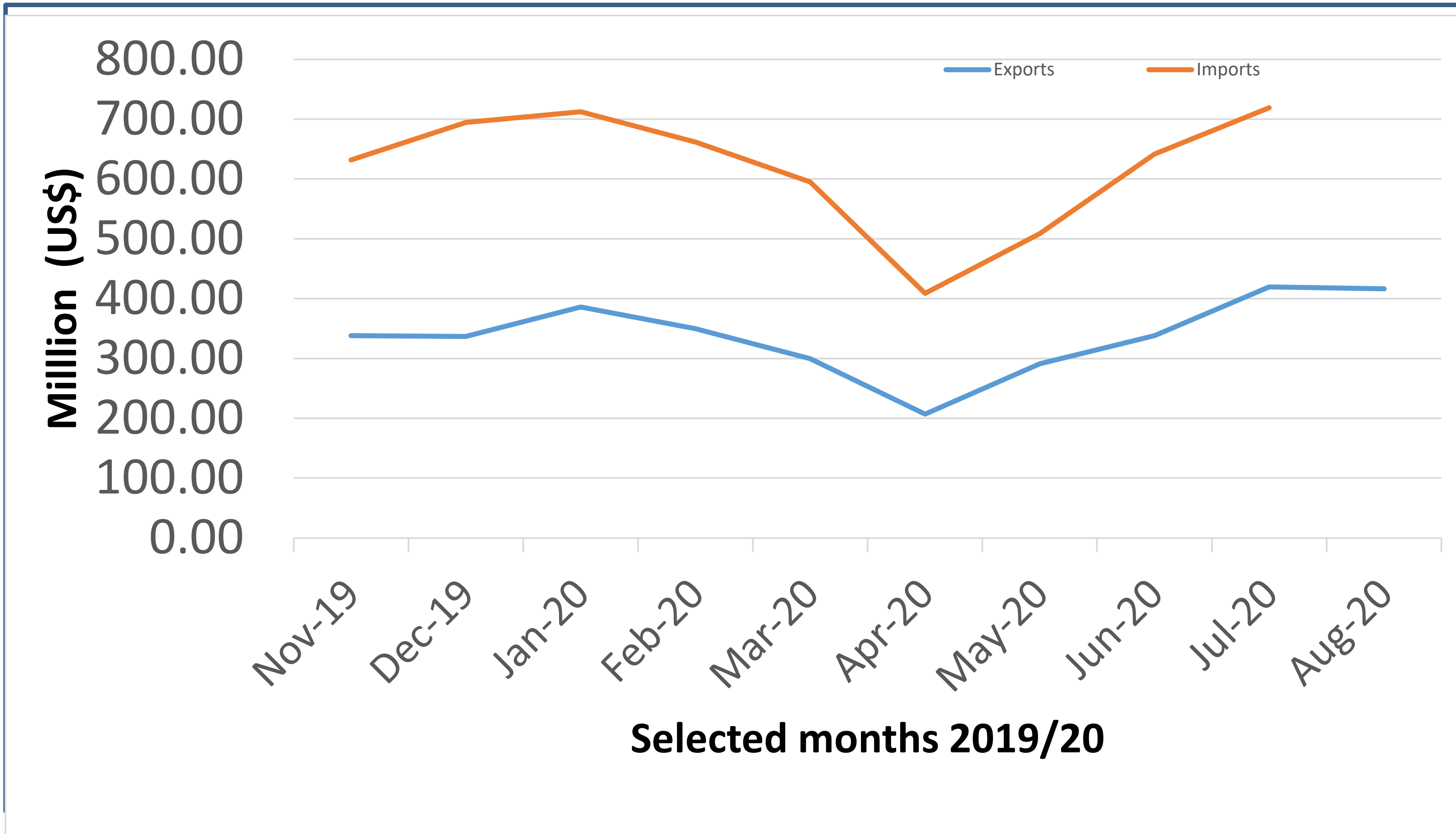
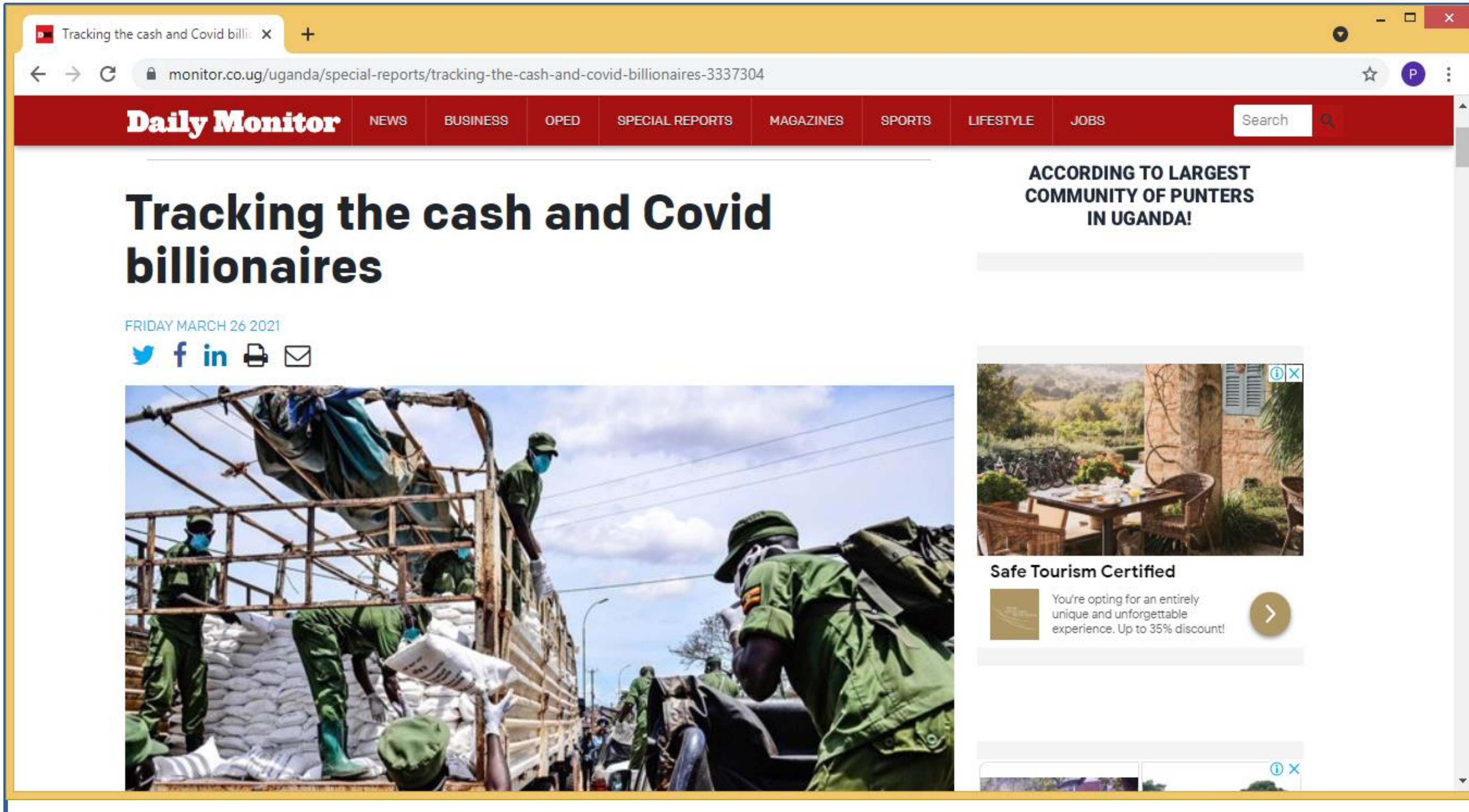


Figure: Uganda's Imports and Exports, Nov. 2019 to August 2020



Key Issue to Consider in the context of COVID 19

Issues of Governance


Tracking the cash and Covid billi
monitor.co.ug/uganda/special-reports/tracking-the-cash-and-covid-billionaires-3337304

Daily Monitor | NEWS | BUSINESS | OPED | SPECIAL REPORTS | MAGAZINES | SPORTS | LIFESTYLE | JOBS | Search

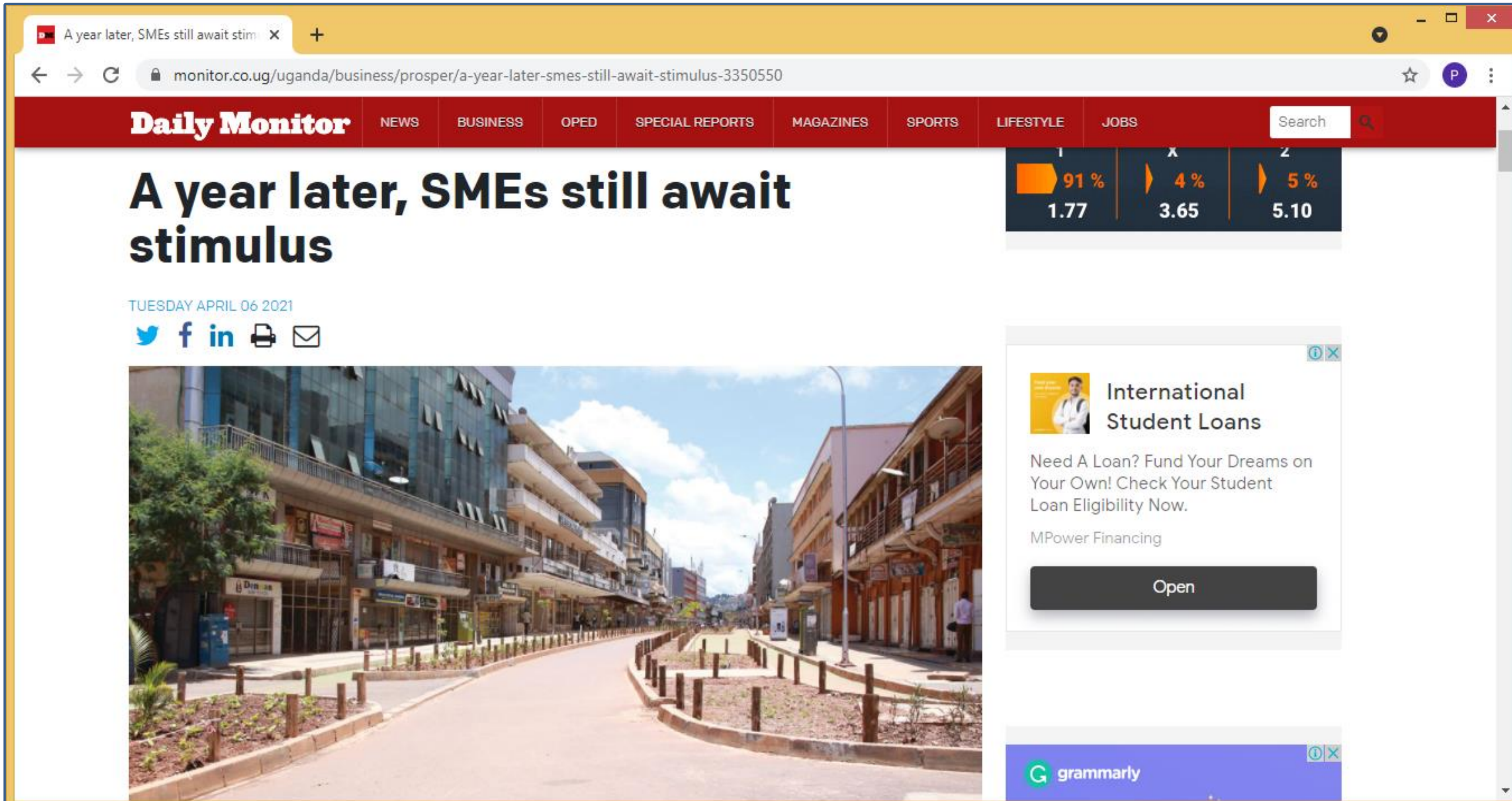
Tracking the cash and Covid billionaires

FRIDAY MARCH 26 2021

ECONOMIC POLICY RESEARCH CENTRE

Key Issue to Consider in the context of COVID 19

Issues of Equity



A year later, SMEs still await stim

monitor.co.ug/uganda/business/prosper/a-year-later-smes-still-await-stimulus-3350550

Daily Monitor NEWS BUSINESS OPED SPECIAL REPORTS MAGAZINES SPORTS LIFESTYLE JOBS Search

A year later, SMEs still await stimulus

TUESDAY APRIL 06 2021

Conclusion

- Debt service will worsen service delivery
- Heavy debt burden also affects government ability to stimulate economic growth including exports that led to deterioration of the current account.
- There is a need concerns about the contribution of this debt to the economy and future sustainability.
- Infrastructure is not the only driver of productivity.
- Debt may impact the growth of tax revenues and exports
- Borrow long term for long term Project
- The economy is growing at slower rate than the weighted interest rate
- A lot of debt has not been disbursed on time while disbursed debt has not been utilized.
- The low absorption capacity of resources has increased the cost of government debt due to commitment charges on committed but undisbursed loans
- The structure of domestic debt indicate a reality of heavy concentration of debt under 5 years,
- Nearly US$ 3 billion or 12% of GDP, of debt will be due in the next 10 years.
- Lack of governance and equity in managing COVID related financing

Recommendation

- Delivery of international and local development finance does not automatically translate into development outcomes. Strong State and institutional capacities are needed.
- Increase tax revenues, reduce leakages through corruption, and amplify the effectiveness of its budget through better priority setting, better targeting and better sequencing.
- The balance between pursuit of growth and social developments is critical
- There is need for institutional realignment, from excessive costs of administration and facilitation at the center, to actual elements of service delivery at the lower local governments. Improving service delivery both for social and development related interventions funded through debt, will enable the country to raise its growth rate to levels that are in line with future debt repayment obligations.
- The framework used to compute debt sustainability is undermined by the limited scope it adopts and assumptions that do not seem to be realistic in terms of capturing liquidity flows required to service the debt. For example, the framework does not take into consideration the limited capacity to absorb and utilize the public debt effectively as well as potentially deleterious effects of corruption.

Thank you for listening