Economic Commentary

2013/14 Economic Performance
The overall performance of the Uganda economy as measured by the real GDP at market prices is estimated to have grown by 5.7% for the financial year 2013/14 which is a 0.1% decrease compared to the revised growth of 5.8% that was recorded in the prior year 2012/13. The projected growth is however slightly lower than the earlier projections on account of the unfavourable weather conditions with drought affecting both food and livestock production. The regional instability especially in South Sudan affected trade as the war hampered smooth flow of goods and services.

The IMF projects that Uganda’s GDP will grow by 5.7% and 6.1% in 2014 and 2015 respectively mainly supported by the public investment despite a slowdown in agriculture and unrest in South Sudan. International reserves are expected to remain ample at a level equivalent to 4.0 to 4.2 months of imports, providing a good buffer against shocks to the Ugandan economy. The external current account deficit is anticipated to widen next year, but would be fully financed by foreign loans, foreign direct investments, and some use of international reserves. Medium-term growth prospects are strong, helped by integration of the East African Community, infrastructure development, and oil production.

Inflation
Inflationary pressures remained relatively stable in 2013/14 with an annual headline rate of 5.4% in May 2014 (3.6 in May 2013) and a general price rate (annual inflation) of 3.3% (5.6% in May 2013) having peaked at 8.4% and 7.3%, respectively, in September 2013.

Oil production expected to spur Ugandan economic growth.

Having edged upwards during the first quarter of the financial year, the trend in annual inflation reversed and declined during the second quarter. The inflationary pressures experienced in the first quarter were largely attributed to prolonged dry conditions which prevailed in many parts of the country and affected food crop production. The Improved weather conditions observed in the second quarter, coupled with a relatively stable exchange rate and international oil prices have since helped ease inflation.

Over the medium term, the objective is to keep annual inflation low and stable.

Interest rates
The Bank of Uganda Central Bank Rate (CBR) has remained relatively stable moving from 12% in May 2013 to 11.5% in May 2014. This is in line with the relatively stable inflation rates throughout the year. As inflationary pressures eased, BOU cautiously maintained the CBR between 12% -11% during the year.

Nominal weighted average lending interest rates slightly reduced to 21.65% per annum in April 2014 from a high of 24.62% in April 2013.

By May 2014, the annualized yields (interest rates) on the 91-day, 182-day and 364-day treasury Bills were 9.52%, 10.79% and 10.89% respectively, slightly up from 9.39%, 10.27% & 10.37% as at May 2013. The stability in the yield on Treasury Bills reflected the relatively stable inflation rates.

Exchange rate
The shilling opened trading at UShs. 2,591.79 against the US dollar at the beginning of July 2013 and closed at UShs. 2,557.72 at the end of May 2014, representing appreciation of 1.3 % in the first eleven months of the fiscal year. The appreciation of the exchange rate during the year is largely attributed to the weakening of the US dollar against other international reserve currencies. In addition, there were stronger inflows from exports, private remittances and short term capital flows.
Budget Commentary

The theme for this year’s budget is “Maintaining the Momentum for Investment, Growth and Socio-Economic Transformation.” The budget sector priorities will focus on:

» Improving the Business Climate by undertaking key economic infrastructure investments, while maintaining peace, security, and macro-economic stability;

» Leveraging Government assistance Agriculture, Agribusiness, Agro-processing, Tourism and Industry and the Services such as ICT;

» Improving the Productivity of Uganda’s Human Resource by enhancing the provision of quality education, health and water services; and

» Strengthening Institutional Governance, Accountability and Transparency.

Key Highlights

» To improve Uganda’s business climate, focus will be on inter-linked actions that reduce the cost of doing business in Uganda. This will include initiatives like:

- Enhancement and expedited enactment of laws that facilitate the business climate and encourage investment;

- Implementation of key interventions that enhance regional integration under the East African Community;

- Enhancing support to industrial research institutions in order to develop and commercialise technology innovations and;

- Deepening the financial sector to facilitate the availability of affordable credit for the private sector

» To strengthen institutional governance, accountability and transparency, Government has vigorously instituted accountability measures to effectively and efficiently utilize public resources. Some of the key initiatives include:

- Implementing a single treasury account to strengthen day to day cash and debt management, and eliminate the need for cash rationing which affects service delivery.

- Decentralizing payroll management in the public sector from the Ministry of Public Service and the Ministry of Finance, Planning and Economic Development, to Accounting Officers. This will also address the perennial problem of delayed salary payments and existence of “Ghost” workers on the Government payroll and;

- Publishing quarterly releases to all Government Departments and Agencies in the print media.

» The 2014/15 budget seeks to:

- Scale up investment in key growth sectors like agriculture, tourism, industries and trade to create the much needed employment opportunities;

- Reform the curriculum to enhance market orientation and private sector entrepreneurship;

- Implement the skilling Uganda initiative in the business, technical and vocational education training with an emphasis on provision of hands-on technical skills training, business skills development, and re-orienting the mind-set of potential entrepreneurs

- Enhance financial literacy and inclusion, and facilitate the financing of productive assets;

- Facilitating investment in small, medium and large businesses.
Resource envelope
The resource envelope for 2014/15 is projected to be Ushs 15,044 billion of which Ushs 12,311 bn (81.8%) will be from domestic resources and Ushs 2,733 bn (18.2%) from external assistance. Domestic resources are projected to include, collections from the Uganda Revenue Authority - Ushs 9,577 bn, non-tax revenue - Ushs 206 bn, issuance of government securities - Ushs 1,427 bn and net Government drawdown from savings - Ushs 1,102 bn. External financing will be sourced from budget support – Ushs 69 bn and project aid – Ushs 2,664 billion.

Key Growth Sector priority areas and budget allocations

Agriculture production and productivity
Agriculture and agribusiness is a priority to government to create jobs, improve productivity and expand exports in the medium term. During the year 2014/15, government will support interventions in the agriculture sector as follows:

» Focus on provision of inputs;

» Minimize expenditure on administrative costs, seminars and workshops;

» Place resources available for inputs under a single umbrella and leverage them by focusing on graduates;

» Encourage small holders to produce surplus;

» Focus on enterprises that provide high returns to farmers; and

» For medium and commercial scale farmers, encourage commercial ranching, large scale crop production and value addition.

Tourism sector
The tourism industry has a potential of significantly contributing to national output if fully utilised. Government will formulate a comprehensive Tourism Sector Strategy that addresses promotion, training, regulation, and infrastructure development and has allocated Ushs 5 billion to the Uganda Tourism Board (UTB) for Tourism Promotion and the formulation of the strategy.

Security Sector
The key priorities in this sector will be in professional development of the disciplined forces, consolidation of peace, promotion of defence and diplomacy, resolution of conflicts, internally, regionally and internationally and support the country’s foreign policy of peaceful co-existence and good neighbourliness. In order to facilitate the Government programme of professionalization and equipping the security agencies, Ushs 1,005.5 billion has been allocated to the security sector in the FY 2014/15 representing 7.1% of the total budget.

Transport Sector
The resources allocated to the roads in the year 2013/14 were used to rehabilitate, maintain and construct new roads. In the year 2014/15, Ushs 2,510 bn has been allocated to works and transport sector and government has targeted to upgrade roads from gravel to bitumen, reconstruct roads, construct and rehabilitate bridges and

Stimulus packages to propel growth in the agricultural sector.
re-grade unpaved roads.

Government, in collaboration with other Partner States within the East African region, is scaling up efforts to revitalize the railway transport system. Construction of an Inland Container Depot at Mukono, and the re-development and upgrading of facilities at Port Bell and Jinja piers is planned to commence in FY 2014/15.

**Energy Sector**

**Electricity**

During financial year 2013/14, the total national power generation capacity increased to 852 MW. Feasibility studies were completed for several small hydropower sites totalling to 130 MW. Construction of these projects will begin in Financial Year 2014/15, with the support from development partners including the World Bank, Norway, the United Kingdom, the European Union and Germany, together with the Private Sector. Special attention will also be placed on accelerating and implementing the construction of the major Hydropower plants at Karuma and Isimba.

**Oil, Gas and Petroleum Development**

Government has made significant progress in oil, gas and petroleum development. The oil refinery will be developed as a Public-Private Partnership (PPP) with the selected lead investor holding a 60% shareholding; and government and participating East African Community partners states holding up to 40% of the oil refinery equity. In 2014/15, the engineering design of the oil refinery will be completed to pave way for construction to begin.

**ICT platform to reduce the cost of doing business.**

**Information and Communication Technology (ICT) Sector**

Government has completed construction of two phases of the National Transmission Backbone Infrastructure (NBI). This has improved Internet connectivity at a more affordable cost.

In the Financial Year 2014/15, government will accelerate the commercialization of the second phase of the NBI project and commence construction of the National ICT Park and Innovation Center. This is expected to encourage innovation and further drive down the cost of doing business.

**Health, Education and Water Sector**

Government spending on the three sectors of health, education and water in the FY 2014/15 will amount to more than Ushs 3,550 billion, which is approximately 25% of the total budget.

Ushs 1,699.4 billion has been allocated to the education sector in the 2014/15 to enhance the quality of education. Priorities to be implemented include the enhancement of Teachers’ salaries, with emphasis on primary school teachers and supporting teachers’ SACCOS.

Ushs 1,197 billion has been allocated to the health sector in the 2014/15 to enhance health workers remuneration and improve their skills through capacity building and expand health facility infrastructure at both local government and referral levels.

Government has made considerable progress in access to clean safe water and sanitation. 65% of Ugandans now have access to safe water within a distance of 0.5 km. Ushs 30 billion has been allocated for the purpose of enhancing safe water provision and sanitation.
Tax Highlights

In the financial year 2014/15, government’s focus is on revenue generation, enhancing tax compliance and transparency in collection and enforcement and encouraging investment.

The government plans to increase revenue through scrapping of tax exemptions, introduction of new taxes or charges, gathering information to identify non-compliant taxpayers through collaboration within government Agencies and use of technology tools, and amending laws to enable Uganda Revenue Authority to access more information to aid tax audits and investigations.

The following measures were proposed by the Minister of Finance:

Value Added Tax

VAT exemptions: Rationalizing the VAT law
Government proposes to remove the following supplies from the list of exempt supplies.

» Supply of new computers, desktops printers, computer parts & accessories and computer software licenses;

» Supply of hotel accommodation in tourist lodges and hotels outside Kampala district;

» Supply of liquefied petroleum gas;

» Supply of feeds for poultry and livestock;

» Supply of agriculture and diary machinery;

» Supply of packaging materials to the diary and milling industries;

» Supply of salt;

» Supply of insurance services except medical insurance and life assurance;

» Supply of specialized vehicles, plant and machinery services and civil works related to roads and bridges construction, agriculture, water, education and health.

All the above supplies will be taxable at a standard rate of 18%.

Life just got more expensive with the removal of zero-rating!
Government also proposes to remove the following supplies from the list of zero-rated supplies:

» Supply of printing services for educational materials;

» Supply of cereals grown, milled or produced in Uganda;

» Supply of processed milk and milk products;

» Supply of machinery and tools for agriculture;

» Supply of seeds, fertilizers, pesticides and hoes.

All the above supplies will be taxable at a standard rate of 18%.

Income Tax

Scraping initial allowance to broaden tax base
The government has proposed to scrap initial allowance on items of eligible property. This implies that accelerated depreciation as an investment incentive will no longer be enjoyed by businesses. Normal wear and tear will however apply.

Small businesses to pay more
The top slice percentage of tax on revenue from presumptive taxpayers (businesses with annual revenue of less than Ushs 50 million) is to be increased from 1% to 3%. This will see small businesses pay higher taxes and may discourage voluntary compliance among small business owners.

Agricultural loans set to spike?
Interest income earned by financial institutions from agricultural loans will be taxable. This may reduce loans by financial institutions to the agricultural sector given the sector’s inherit risks. Financial institutions are also likely to pass on the tax costs resulting in an increase in interest rates on agricultural loans.

Capital gains tax on commercial property
Capital gains tax will be imposed on sale of commercial properties. Currently, incomes from sale of commercial properties is taxed as business income. This emphasis may however impact the modalities of computing the taxes on sale of commercial properties.
**Thin capitalisation: Tightening the noose**
Deductions of interest paid to non-resident associated persons will not exceed 50% of the earnings before interest and depreciations. The Income Tax Amendment Bill will clarify whether this is to replace or add to the existing debt to equity ratio of 2:1.

**Business income from educational institutions**
Business income from running or managing educational institutions will no longer be exempt from tax. Private education institutions are likely to increase school fees and tuition fees to retain their margins while complying with this amendment.

**Defining start-up costs...**
Start-up costs have been defined to mean non-recurring preliminary costs associated with starting up a business. Previously, there was no definition for start-up costs which qualify for deduction at 25% p.a. This proposed amendment means that some expenses will be capitalised as opposed to being expensed when computing income tax.

**Other technical amendments**
More technical amendments will be included in the Income Tax Amendment Bill, 2014.

**That bet is now subject to tax!**
Government has proposed to introduce 15% withholding tax on wins by players of gaming and pool betting. Gambling houses will be designated as withholding tax agents to collect this tax. This proposal is similar to the 2013 amendments in Kenya that brought to tax gains from games of chance.

15% - proposed withholding tax rate on wins by players of gaming and pool betting

**Excise Duty**
Government proposes the following amendments to the Excise Duty Act.

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**Aligning to international best practice**
The Financial Institutions Act, 2004 and the Bank of Uganda Act, 2001 are to be amended to provide for Agent Banking, Islamic Banking, bancassurance, and Mobile Money.

The Investment Code (Amendment) Bill, Counterfeit Bill and the Public Private Partnerships Bill will be enacted to further facilitate the business climate and encourage investment.

In the next financial year, amendments to laws affecting 307 licenses requirements will be completed to ease business licensing and encourage investment.

Government will also amend the Capital Markets Authority (CMA) Act in order to provide for a greater diversity of financing opportunities.

All these proposals point to government’s determination to attract investment, modernise regulatory oversight and align to international best practice.
The budget proposals included in this BudgetBrief may be amended significantly before enactment of the Finance Act. Please note that our interpretation of tax legislation may differ from that of the various Revenue Authorities. Similarly, the content of this BudgetBrief is intended to provide a general guide and should not be regarded as a basis for ascertaining tax liability or as a substitute for professional advice. If you would like specific advice on the contents of this publication, please get in touch with your regular contact at KPMG.

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