Konrad-Adenauer-Stiftung e.V.

UGANDA

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A KEYNOTE ADDRESS DELIVERED AT THE PRIVATE SECTOR FORUM ON EXPORTS PROMOTION IN UGANDA

REVERSING UGANDA'S TRADE DEFICIT: THE ROLE OF INDUSTRIALIZATION

Introduction

The purpose of this paper is premised on the need to increase exports as a means of creating jobs, stabilizing the exchange rate for better business planning, and boosting overall development through sufficient provision of foreign exchange.

The paper presents an analysis of the current state of exports at both the global and national level. The global trade in merchandise presents a context within which Uganda operates and which determines the opportunities for increasing exports. A review of the major destination of exports by region and country highlights opportunities for possible starting point by way of quick wins. A detailed breakdown of the composition of both exports and imports shows actual products that the country can target either for increased exports or import substitution. The share of manufactured products is quite small and mainly dominated by re-exports.

Key lessons and recommendations

The paper points to a number of policy gaps both in the area of detailed planning and financing along the entire value chain.

1) Policy should be specific for each strategic export and span the entire scope from skills training, development of standards, and business management.
2) There is need to go beyond the current generalized policy proposals and actions such as provision of physical infrastructure (electricity and energy) to 'software' aspects such as legal and contract enforcement, and resolving production levels for both quality and quantity.
3) A holistic approach that cuts across all respective and responsible sectors should be developed since the different components require mandatory inputs from the various sectors. For example, the development of specific skills for the textile or fish industry has to be prioritized by the Ministry of Education and Sports.

4) The challenge of an incomplete financial sector should be resolve to ease the burden of using short-term commercial finance for development activities. Government should work with global partners to establish strong development finance that should also provide agricultural and trade finance.
5) Finally, governance and related corruption should be addressed as it distorts market signals and incentives.

The rest of the paper presents selected trends as a way of analyzing the various developments so as to inform the above recommendations.

Analysis of trends and implications for policy actions

The steady increase in exports from 2004/05 was matched by a similar increase in exports that has worsened the trade balance. All the three variables: exports, imports and the trade balance have reduced over the last three years – something that is both local and global. It is worth noting that, if Uganda had maintained the upward trend of exports, the trade deficit would have declined even further. For this reason, it is recommended that the country targets specific exports and regions or countries to secure consistency in a turbulent global environment.

Exports of Goods and services (US$ Millions)

Global trends have strong similarities with Uganda's trends meaning Uganda is well linked into the global economy. Country has to find a niche to avoid being dragged down by current deceleration in global growth and trade. Food exports could be one such niche since food demand tends to be inelastic and has abundant demand in the region. Boosting exports has got to take ijnto consideration the

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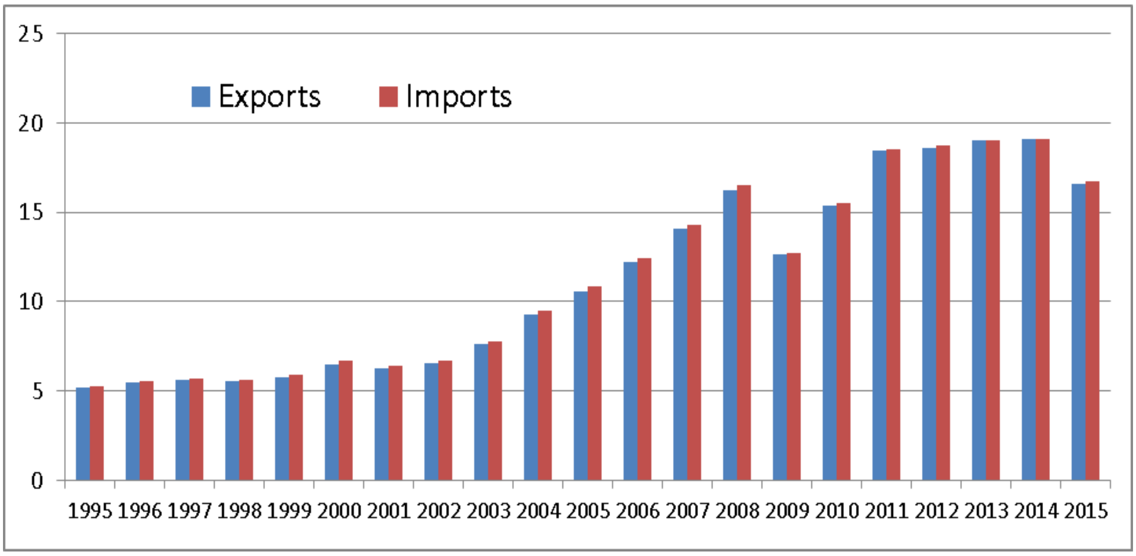
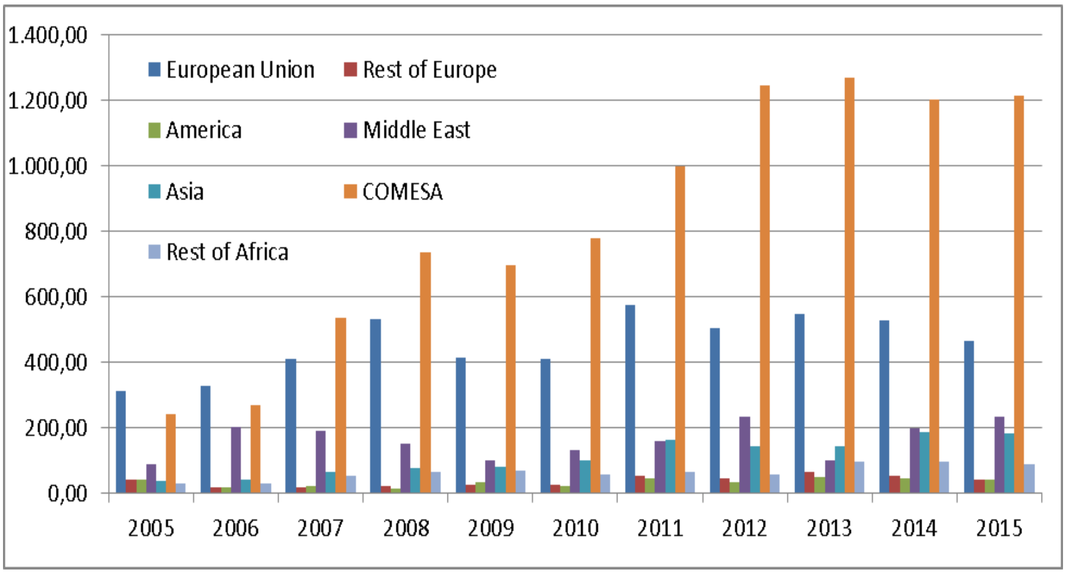
complementary factors (standards, physical infrastructure, business networks and financial sector)

Global Exports and Imports of Merchandise (US% Trillions)



A detailed breakdown of exports by destination reveleas three critical regions that Uganda should keep a strong focus even as the country seeks to diversify into new markets. Specifically, COMESA, the European Union and the Middle East have been the leading destination regions for Uganda's exports over the last fifteen years. The Middle East is dominated by UAE (export of human skills).

Main drivers of exports by destination



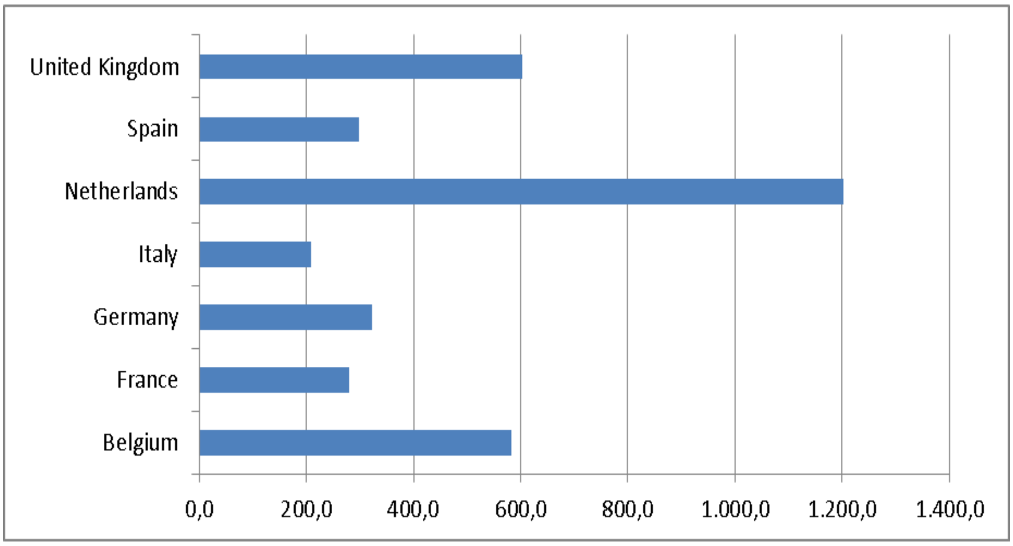
The main message is to focus on the existing exports and export regions since consolidation of markets where traction is easy is always a good initial strategy. This is partly due to the following reasons:

a) Individual companies already have business networks and knowledge of the markets in current destinations countries.
b) The existing export trade to such a magnitude impllies that the required standards have already been fulfilled to an acceptable level.
c) The necessary basic physical and other related trade infrastructure is in place.

As part of taking advanatge of such existing trade links, a quick understanding of the specific export items is needed. Discussions with the main actors or their associations should be conducted to reveal the critical path and what needs to be fixed to trigger the underlying trade potential.

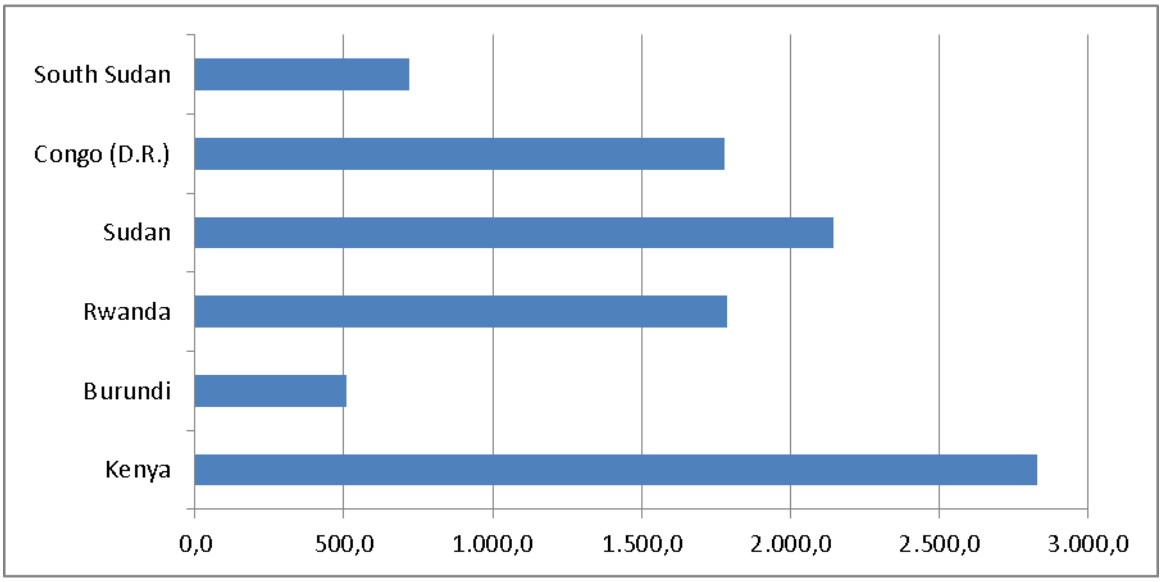
In line with the proposal to increase focus on existing export trends, the paper presents the main drivers of exports trends in the key regions of the European Union, COMESA and the Middle East. Three counries: the Netherlands, the UK and Belgium dominate the EU market and should be a major areaa of focus for Uganda.

Main export drivers in the Eurpean Union (US$ million, Totals for 1997 – 2015)



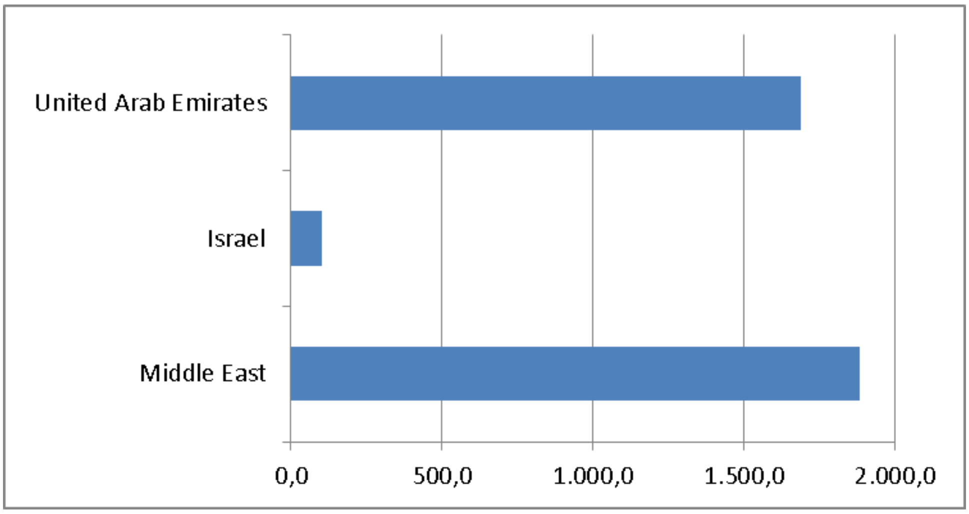
The COMESA region is dominated by Kenya, Sudan (and after 2011, South Sudan), the DRC and Rwanda. The region comprises Uganda's biggest source of exports and should, therefore, be treated with utmost priority and focus. There is ample benefit in terms of increasing production of agricultural products and basic services such as education, which dominate the trade in this region.

Main export drivers in COMESA (US$ million, Totals for 1997 – 2015)



The exports to the middle east, the third biggest export destination, is dominated by United Arab Emirates, which is largley dominated by export of human skills.

Main export drivers in Middle East (US$ million, Totals for 1997 – 2015)



A review of the exports data for more than a decade (2002 – 2015) shows a dominance of items such as fish and fish products, tbacco, tea, flowers, cotton, and maize. The manufactures merchandise are still limited, possibly protraying the effect of interntional competition and Uganda's existing niche in exports originating from the agricultural sector.

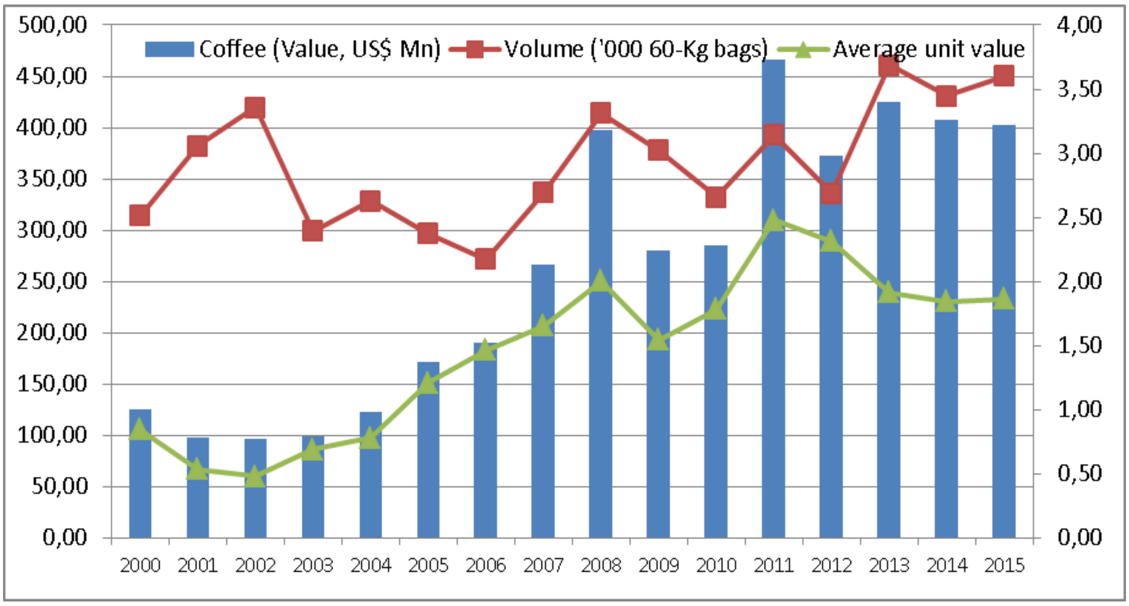
The country should not loose focus on the agricultyural sector much as high value exports are often preferred.

Total Exports (US$ Millions 2002 – 2015)

Export Commodity	Value	Export Commodi-ty	Value
Cotton	449.28	Simsim	223.59
Tea	769.76	Maize	454.23
Tobacco	812.21	Beans	189.40
Fish & its prod. (excl. regional)	1,681.35	Flowers	578.88
Hides & skins	362.99	Oil re-exports	1,092.96
Cobalt	162.38	Others	9,465.77

The value of coffee exports was largey driven by the unit price (average unit value) than the quantity produced. It follows therefore that the country can indeed increase the value of coffee exports through increased production. Research to cub diseases and promoted effective increase in acreage will be key to realization of quick benefist.

Coffee exports for 2002 – 2015 (Values, Volumes and Avearge Unit value)



The boosting of agricultural exports requires significant reform in the sector to focus on detailed community-based solutions including re-establishing of local leve cooperation among farmers for better organization. Lessons from Ethiopia show greater detail to provision of extension services and training of farmers that has provided better results than Uganda. For example, between 2004/5 and 2009/10, a total of 61,785 extension workers were trained and 9,265 farmer training centers established in every village.

On the contrary, Uganda relied on a market based extension service structure and financed a model whereby lead and model farmers supported by public funds were supposed to support local level learning. Such support should have gone into establishing local level public sector entities such as cooperatives and village farm institutes.

Regarding the role of export trade to growth and employment creation, Ethiopia focused more on poverty reduction and used growth as the secondary core route of achieving that goal. On the contrary, Uganda targeted growth and mainly relied on the trickle down process to result in poverty reduction. Thus, interest rates were more geared to stabilizing price as a means to improved planning for growth rather than a direct means of boosting investments. The current Monetary Policy Statement (October, 2016) by Bank of Uganda appears to reflect a positive change in policy where interest rates will be aligned towards enhancing consumer demand.

Import substitution

The table below presents a summary of major imports as part of understanding how to design any imprt substitution strategy. Areas of interest include: vegetable products, beverages, fats and oils, foodstuff, wood and wood products, and textiles.

The start of oil will not only increse exports but also reduce imports of cetrain petroleum related products. A cautious approach, however, is recommended to avoid mistakes that simply seek to reduce imports that require complex production skills, technology and finance.

Total Imports for 2004 – 2015 (US$ Million)

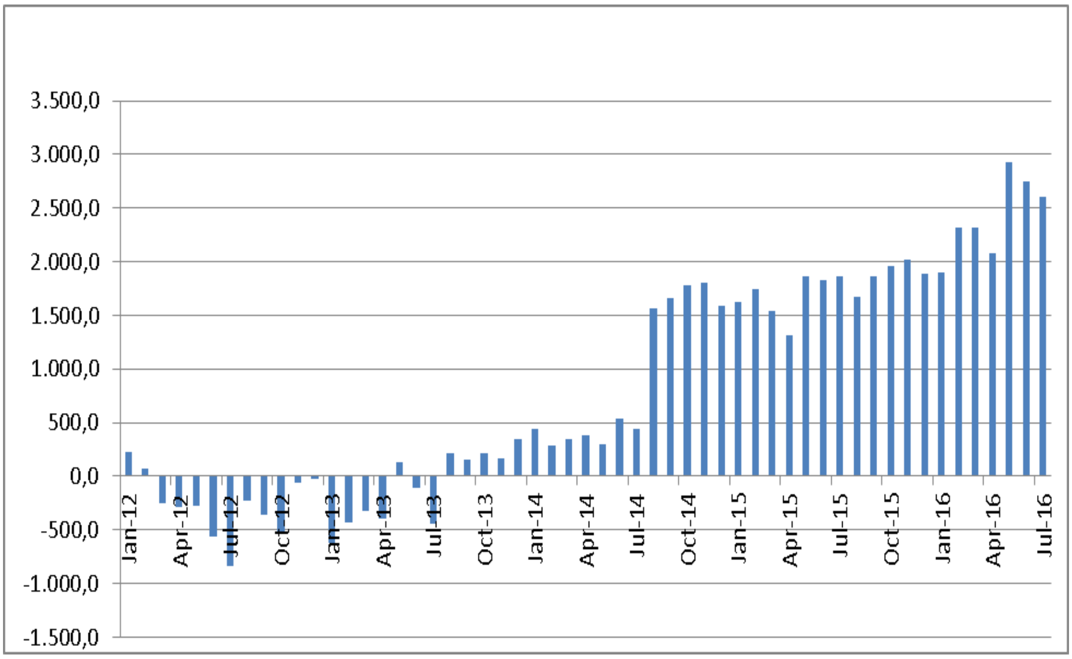
Vegetable Products, Animal, Beverages, Fats & Oil	3,928
Prepared Foodstuff, Beverages & Tobacco	1,849
Mineral Products (excluding Petroleum products)	2,242
Petroleum Products	7,535
Chemical & Related Products	4,112
Plastics, Rubber, & Related Products	2,208
Wood & Wood Products	1,294
Textile & Textile Products	1,419
Miscellaneous Manufactured Articles	1,884
Base Metals & their Products	3,240
Machinery Equipment, Vehicles & Accessories	11,326

The bulk of manufactired imports may continue until the medium term when sufficient capacity (skills, knowledge, money and markets) will have evolved.

Finacing of an export startegy

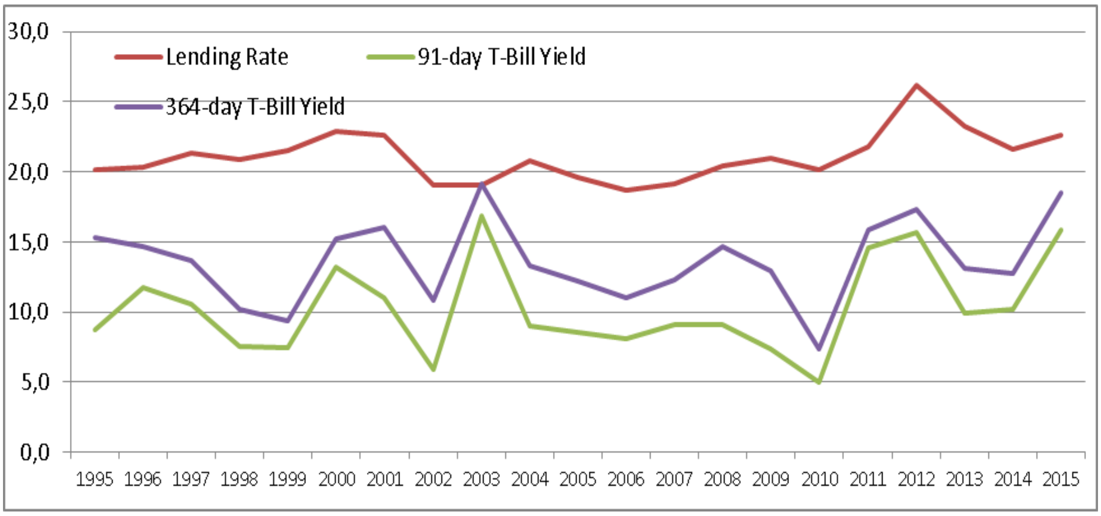
The curret structure of the financial markest in terms of products and costs cannot provdide the necessary support for the exprts sector. Despite stable lendong rates in the range of 20 – 23 percent over the last 20 years, the level is still high and tenures too short to support the necessary capital investments. Besides, the amounts are too little to suppot both fiscal and monetary policy requiremenst as well as the private sector. It is clear from the figure below that, over the last three years, governmet has moved from a net saving position to a net borrower from the financial sector. Governmnet borrowing has skyrocketed in the recent past, which has negative implications on the private sector.

Net credit to Governmnet (Shs Bn)



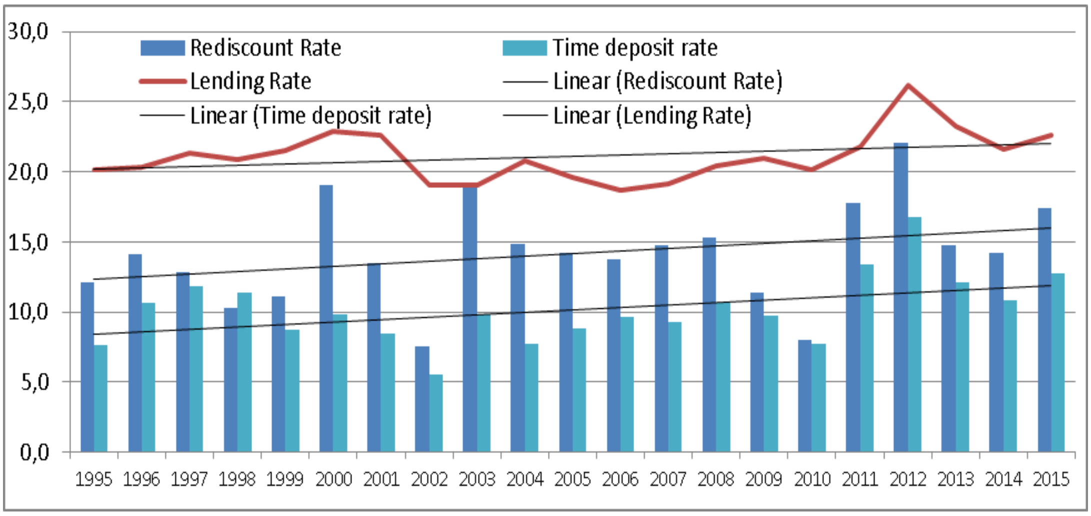
Lending rates to the private sector and governmnet demands for fiscal and moneaty policy objetives are so closely intertwined that they re bound to counteract any efforts to boost exports. financial institutions will always prefer short-term lending to governmnet, which is both less risky and offers a relativley higher return. TB rates in the range of 12 – 15 percent over a period of one year are ceratinly more attractive that provate credit at 22 percent.

Interest rates have been relatively stable over the last 20 years



Besides, the problem does not seem to be one of inefficiency in the financial market since the financial sector has not significantly increased lending rates despite significant increase in the cost of resource mobliization (time deposits, rediscount rate, and overnight as well as weekly borrowing rates for liquidity managemet. As can be seen below, the gap between the lending and resource mobilization costs has been stable or reduced slightly over the last 20 years. This could be due to competition and increased use of technology.

Efficiency indicators show stability or improvments in the financial sector



From the above analysis, it is plausible to conclude that the commercail bank rates and products are note the core problem underminig the expot sector. Commercial finace of this nature is only fit for short –term needs such as working capital or bridge finance. The core problem, therefore, is the incompleteness of the financial market that lack development and trade finance.

The solution, therefore, includes introduction of development finance to specifically support the export sector in particular and the overll economy in general. Financing should be at lower rates, for a longer duration and sufficient amounts across the whole range of borrowers who are active aong the value chain. Trade finance is critical since a lot of export trade involves payment after delivery, which can take months and involves a lot of finance.

Finally, the general slowdown in the local economy has to be addressed to enable the export sector, which is intertwined with all the other sectors, to thrive in a better economic environmnet.

Growth rates for Uganda have trended downwards since 2008