The case for increased domestic financing in Uganda

A Uganda National Academy of Sciences Consensus Study Report calls for mindset shifts towards greater ownership of national development

Uganda is currently in a unique position. As several different national, continental, and global agendas and plans are ending and others beginning, an opportunity exists to re-examine its systems and processes of development. Uganda has recently started its third National Development Plan in 2020[1] as the continental African Union Agenda 2063[2] continues, and the endpoint of the Sustainable Development Goals in Agenda 2030[3] is fast approaching. Historically, most discussions regarding sustainable development in Uganda have focused on technical solutions to its various challenges, whether economic, political, or social. However, the effectiveness of these solutions has consistently been impeded by their implementation. One of the more under-appreciated aspects of implementation has been a collective mindset that owns and actively participates in development. The active participation and leadership in the development process by Ugandans creates the foundation for sustainable development because individuals, communities, and institutions build the necessary confidence to pursue increasingly complex and challenging solutions to their problems.

One of the most pressing concerns underpinning the challenge of implementation is the approach to financing sustainable development. Currently, public and private resources are being leveraged towards improving development indicators, with little focus given to how those resources can stimulate mindset shifts towards greater ownership of the development process. In part, the emphasis on development indicators has been due to the substantial influence of conventional methods of analysis to assess Uganda's economic trajectory. While those methods have been instrumental in creating Uganda's current economic success, a holistic approach to sustainable national development remains widely debated.

In this report, we summarise the outcome of a study undertaken by Uganda National Academy of Sciences (UNAS) in 2020. Its aim was to expand the scope of economic trajectory analysis to consider how ownership of the development process can strengthen the impact of domestic investments. To explore how to invest domestic resources in a way that supports ownership of the development process by Ugandans, UNAS convened a committee of experts to review scientific evidence and come to consensus on recommendations for action. The Committee responded to a series of questions from stakeholders and distilled these questions into four distinct challenges in the current financing approach to building ownership of the development process. These challenges are: (1) a focus on improving development indicators to the exclusion of mindset shifts, (2) a lack of clarity on which stakeholders should be involved in financial decision-making, (3) stricter oversight of public institutions as a means of building trust not having the desired effect, and (4) financial innovation being stifled due to the current socio-economic-political conditions.

One strategy to address these challenges is to focus on competitive advantages that create programmatic success. By capitalising on competitive advantages, leaders and participants in the development process can build the confidence necessary to pursue increasingly complex and innovative solutions to their development challenges. Competitive advantages are opportunities that capitalise on timing, scale, and responsiveness to change.

The study identified four angles from which to approach competitive advantages: finding and using existing competitive advantages; creating competitive advantages; using benefits of indirect contributors to competitive advantage; and using the successes of those advantages to create an ongoing cycle of new advantages.

The Committee focused on three areas of inquiry: institutions, taxation, domestic and external financing, and their relationships with ownership of the development process.

Institutions as trust builders

Institutions, broadly understood, are critical pieces in building a process of development that stakeholders own because they represent incremental and accumulated consensus on how decision-making processes should function. In examining the deficit of trust in government organisations, the Committee considered how public institutions lack the perception of legitimacy necessary to establish tax compliance effectively. Taxpayers are more likely to comply with tax demands if they experience tangible benefits from public spending. An absence of benefits has meant poor perceptions of government legitimacy and low tax morale. Aggressive decentralisation efforts without commensurate financial and human resources have resulted in a proliferation of districts, smaller shares of available funding, frustrating service delivery, and strict accountability measures. Other blocks to tax participation come from a lack of clarity on tax obligations and skepticism around the benefits of tax compliance by Uganda's large informal economy.

A civil society call for increased domestic financing

Based on the evidence presented in this study, the Committee recommended as follows:

1. The Government of Uganda should strengthen existing mechanisms that communicate government performance and provide citizens with opportunities to actively give feedback on service delivery. This approach would give the government a platform to win public confidence while simultaneously being responsive to citizen demands outside of elections. The Office of the Prime Minister's Baraza programme is an example.
2. The Government of Uganda should halt the creation of new administrative districts unless there is requisite financial and personnel resources to deliver on service obligations. If districts have sufficient resources in line with their obligations, failures in service delivery can more meaningfully be held to account, thereby strengthening trust in public institutions.
3. The Government of Uganda should consider centralising political and administrative oversight to regional hub districts, if resources are available to promote ownership of the development process in local communities. Centralisation in this way may reduce administrative costs while still providing local communities with forums to work with technical leadership and service delivery personnel to improve their local circumstances.
4. The Ministry of Local Government should undertake a review to examine the potential efficacy of a results-based financing policy on chief administrative officers. This review can help determine how to keep chief administrative officers accountable while understanding the flexibility necessary for chief administrative officers to execute on their responsibilities.

Taxation in national development

Taxation is one of the most fundamental ways governments build ownership of the national development process because it is an explicit financial stake intended to provide a theoretical degree of control over certain decisions. The Committee conducted a review of the history of taxation in Uganda, identifying current tax collection issues such as low tax morale and duplication and inaccuracy in the taxpayer registry. Due to the abolition of the graduated tax in 2005, local governments lost a substantial portion of their own-source of revenue. One technical solution that has gained significant traction in recent years has been the introduction of a tax on unimproved land value that could provide a vital influx of funds to local governments. Owners would benefit directly from the provision of public services through increases to their property value, raising tax morale, and raising revenues for local governments. While there are several challenges facing the possibility of expanding property taxation, including lack of mass appraisal techniques, exemptions for owner-occupiers, exemptions for vacant lands, and legal disputes over land ownership and titleship, the direct connection between property tax and a community's development interests could strengthen ownership of such a tax's implementation.

Based on the evidence presented in this study, the Committee recommended as follows:

5. Municipal governments should stimulate behaviors on vacant land in terms of disincentivising and incentivising action through taxation. This policy approach will increase tax compliance on vacant lands and provoke economic activity in line with local priorities.
6. The Uganda Revenue Authority and Local Authorities should continue to strengthen taxpayer associations to clarify the connection between the payment of tax and service delivery. Strengthened associations could encourage compliance, understanding, and appreciation for tax and its role in community development.
7. Legal disputes over land ownership and titles should be more fully and efficiently addressed. This shift will expedite tax compliance on disputed lands.
8. The Parliament of Uganda should consider ways to provide sufficient flexibility for local governments, through the amendment of the Local Government (Rating) Act, to collect property rates on vacant lands that are contextually informed. This approach could avoid stringent one-size-fits-all policies and promote tax compliance.

Leveraging domestic resources

While financial inclusion is recognised as a core driver of economic growth and country ownership, estimates suggest 45% of Ugandans still do not access financial services. Despite progress made in outreach and access to microfinance, further gains have stalled or been reversed through unregulated expansion and commercialisation of financial services resulting in cases of exploitation and fraud. Current development planning has focused on urban areas without equal attention to rural areas. This approach has left rural areas underserved in terms of financial services. There is little incentive for individuals to engage in new or more productive forms of economic activity outside subsistence farming with limited financial services available. Domestic financial markets remain also constrained by high-interest rates and the resulting high costs of borrowing. With uneven access to formal, semi-formal, and informal financial institutions, trust in financial institutions is easily compromised and may cause Ugandans to avoid engagement with financial systems as a result.

Based on the evidence presented in this study, the Committee recommended as follows:

9. The Bank of Uganda should consider the creation of an independent platform with private sector actors such as the Uganda Bankers Association (UBA), the Uganda Cooperative Savings and Credit Union (UCSCU), microfinance institutions, and mobile money providers to build consensus on how best to provide widespread access to finance, increase financial literacy, and provide sufficient protections to creditors. A platform of this nature could build broader trust and participation in the financial system, particularly in rural areas.

Leveraging external resources

Recent discovery of substantial oil and gas reserves in Uganda presents an opportunity to bolster economic growth. However, effective exploitation of these resources will depend on foreign direct investment. By leveraging external resources in combination with focused local content policies, it will be possible to maximise Ugandan participation in oil and gas development through employment opportunities and economic linkages. Capital flight, the extraction of profits from domestic ventures to foreign investors, is a pitfall of foreign investment that has been given little attention at a policy level. Unfortunately, there is limited literature on current foreign investment, its impact on domestic growth in Uganda, and how the participation of domestic actors could be strengthened in the development process.

Based on the evidence presented in this study, the Committee recommended as follows:

10. The Government of Uganda should take a synergistic approach to oil and gas development, considering how districts can benefit one another. For example, oil and gas development in one district may be supported by ensuring that other necessary resources are catered for by nearby or surrounding districts such as agricultural produce and light-manufacturing goods such as textiles.
11. The Office of the President should establish an independent commission to review and make recommendations on policy about corporate transparency and capital flight.
12. The Ministry of Finance, Planning, and Economic Development (MoFPED) and other interested stakeholders should support further research on capital flight to collect domestic data on the movement of profits.

Conclusion

The challenges facing Uganda are significant, and an approach to domestic financing that focuses on how Ugandan leaders and citizens alike can collectively own the development process can potentially change the future of Uganda's development for the better. While conventional approaches to domestic financing have helped improve economic indicators, combining those methods with approaches that provide opportunities for Ugandans to participate in the development process can unlock new possibilities for growth. Those new possibilities will rely on institutions and their leaders playing an active role in creating those opportunities for participation and building a history of success. In doing so, Ugandans can collectively address issues of limited trust in government institutions, poor tax compliance, and investment of domestic and external resources that inclusively promotes ownership of the development process.

References

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