THE REPUBLIC OF UGANDA

Prioritization in the Energy and Mineral Sector: What important sector aspects are omitted?

OVERVIEW

The Energy and Minerals Sector supports the aspirations of the Vision 2040 and the objectives of the first and second National Development Plans (NDP) by ensuring that there is reliable, adequate and sustainable exploitation, management and utilization of energy and mineral resources. The key sector outcomes are:

i) Increased access to affordable modern sources of energy through enhanced generation capacity and distribution.

ii) Well managed and safeguarded mineral resources for production and exports; and

iii) Well managed and safeguarded petroleum, oil and gas resource chain for sustainable development.

Whereas the Energy and Mineral Sector between FY2010/11-2014/15 exhibited good allocative efficiency, (a state of the economy in which production represents consumer preferences. In this case expenditures were on items that yield the mostdesired outputs in the economy), constraints like insufficient stockof petroleum products on the market at all times persisted, and the country also lacks an alternative petroleum supply route from the existing Uganda-Kenya route. This was due to low allocations made to the Petroleum Supply, Infrastructure and Regulation Vote Function.

This briefing paper highlights the allocative efficiency of the sector using outputs whose expenditure share is more than 0.89% of the total expenditure and marginalized vote functions. Policy options and recommendations for achievement of sustainable petroleum supply are made.

KEY ISSUES

- The Energy and Mineral Sector exhibits good allocative efficiency, as there was an optimal expenditure on majority of the items that were prioritized by the sector.
- Lack of functional petroleum reserves and alternative supply route leads to revenue loss, suppressed demand and inflationary effects on the economy. In case of any external shocks, Uganda may suffer fuel shortages.
- Innovative alternative funding can help bridge the funding gap to aid achievement of sector objectives.

INTRODUCTION

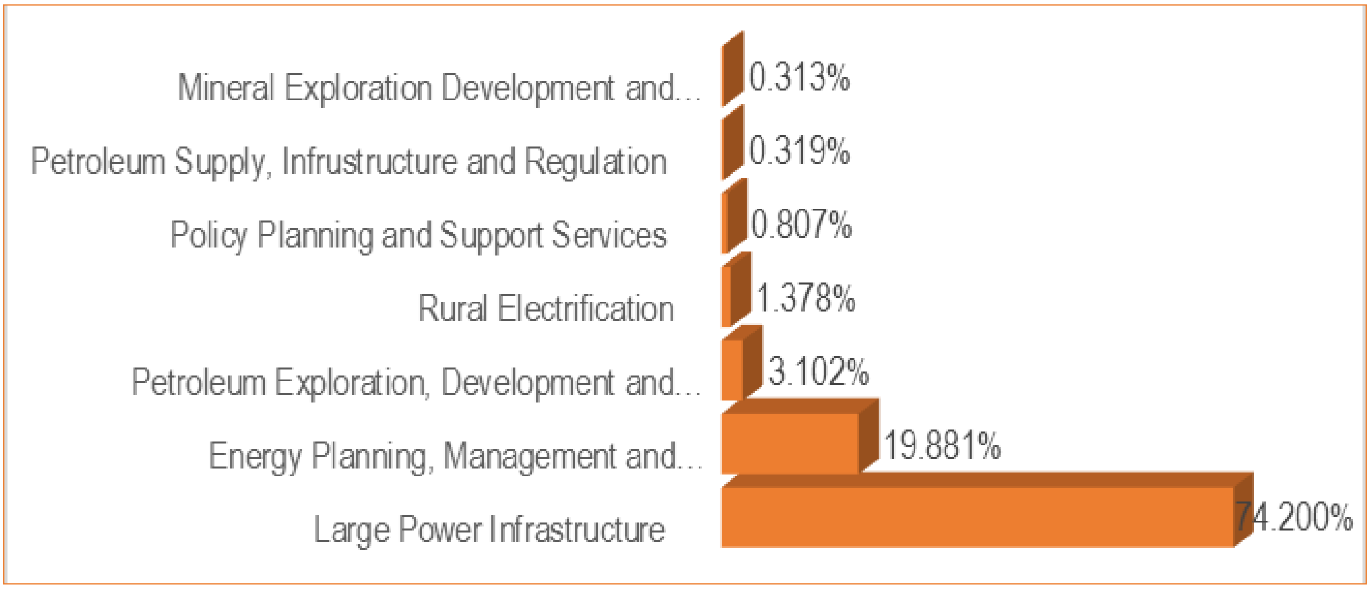
Between FY2010/11 and FY2014/15, the Government of Uganda (GoU) allocated a development budget of Ug shs 5.4870 trillion to the sector. By 30th June 2015, the cumulative disbursement was Ug shs 2.2444 trillion (41%) and expenditure performance was 99.65% (Ug shs 2.2365 trillion) of the release. Majority of expenditures were towards the sector priorities, which include:

- Increased electricity generation capacity and expansion of the transmission and distribution networks;
- Increased access to modern energy services through rural electrification and renewable energy development;

Allocations of the Sector by Vote functions

Figure 1 shows the allocations of the Energy and Mineral development sector by Vote Function (VF) for the period FY2010/11 to FY 2014/15.

Figure 1: Cumulative percentage share of the sector allocations for FY2010/11-2014/15

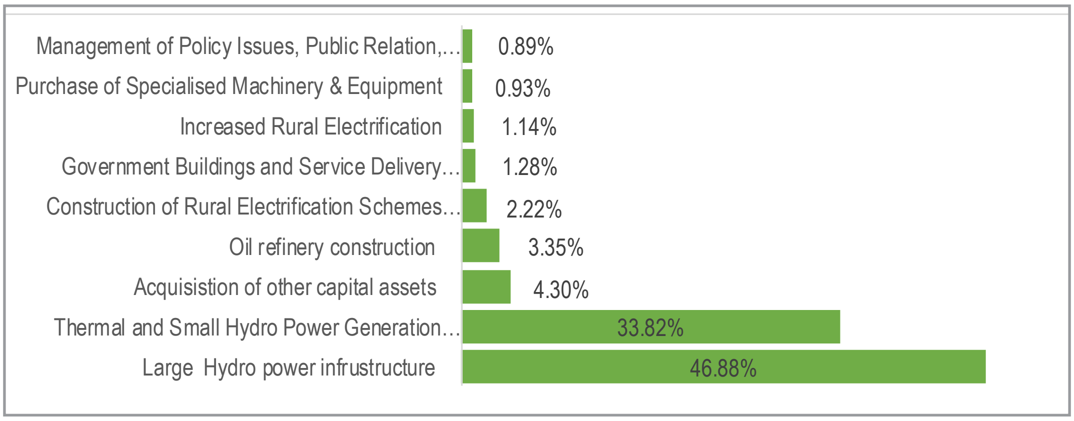


Mineral Exploration Development and Production and Petroleum Supply, Infrastructure and Regulation vote functions, were the least funded (Figure 1). The low prioritization is exemplified by the Policy Planning and Support Services vote function being allocated more funds, than Petroleum Supply Infrastructure and Regulation. This low funding affected implementation of some core vote function components such as restocking of oil reserves.

Allocative efficiency

Allocative efficiency was good. Large hydropower infrastructure had the highest expenditure (46.88%) among the top nine expenditure outputs. The funds were spent on activities of increased power generation. The least ranked output was Management of Policy Issues and Public Relations, ICT and Electricity Disputes Resolved (0.89%). Expenditure trends indicated an attempt by the sector to spend on outputs that are critical to achievement of the sector outcomes (Figure 2).

Figure 2: Cumulative proportion of expenditure by outputs for FY2010/11-2014/15



Source: IFMS Data

Marginalized Vote Functions

Despite allocative efficiency being good, Petroleum Supply, Infrastructure and Regulation VF and its related outputs remained poorly funded. The VF received 0.319% of total sector allocation between FY2010/11-2014/15. This VF addresses some the constraints and priority intervention areas mentioned in the first and second National Development Plans of sufficient stock of petroleum products on the market at all times.

Petroleum Supply, Infrastructure and Regulation Vote Function

Activities under this VF include; inspection and monitoring of the operations of private oil companies with respect to volumes, prices, product quality, safety of operation, technical and environmental standards. It manages, contributes and ensures that the country has sufficient national strategic reserves to act as a reserve buffer, when there is a supply outage and stabilize the supply of petroleum products in the country. It also implements the Petroleum Supply (General) Regulations, 2009.

Funding to the Vote Function

By 30th June 2015, the vote function had been allocated Ug shs17.50 billion which was not sufficient to restock Jinja reserve, complete the construction of and stocking of Nakasongola storage tanks among other activities between FY2010/11-2014/15. Todate the reserves have not been attended to due to inadequacy of funds. The funding requirement for restocking Jinja storage tanks is about Ug shs 20 billion. The VF however executed its other mandate including; monitoring the operations of private oil companies among other activities. Apart from the Jinja storage tanks, which are partially functional, no other potential storage tanks (Nakasongola) are functional.

Absence of functioning storage tanks and an operational alternative petroleum supply route (southern route through Tanzania) had adverse effects on the economy when there was political unrest in Kenya between July 2007 and February 2008. The effects are presented thus;

Implications of absence of national fuel reserves and functioning alternative supply route

Suppressed demand: This is a situation where Minimum Services Levels (MSL) necessary for human development are unavailable to people or only available to an inadequate level. Between August 2007 to February 2008, Uganda experienced supply disruptions. The lowest recorded supply between July 2007 and June 2008 was in December 2007.

Diesel supply reduced from 47.3220 million litres in July to 34.8045 million litres, while Petrol supply reduced from 24.316 million litres to 21.780 million litres, Kerosene reduced from 6.629 million litres to 4.103 million litres in December, 2007. This led to price increases.

The rising oil prices had significant impact on inflation, primarily by raising transport and manufacturing costs. In 2008, the household and personal goods inflation category was 16% higher and the rent, fuel and utilities category showed a 10% increase compared to 2007. Inflation peaked at 15.8% in August 2008, the highest it had been since the then inflation trend started in July 2005.

Loss of revenue; Between September 2007 and March 2008, 325.9672 million litres of Diesel were imported compared to the expected 512.9345 million litres over the same period with no without disruptions. The 186.9673 million litres difference translated into Ug shs 99,092,669,000 revenue loss at the Ug shs 530/litre tax.

Government intervention to the crisis

In response to the effects of lack of reliable supply of petroleum products to the country, the government and a private petroleum company (Hared) in 2012 entered into a concessional agreement to refurbish, restock, maintain and manage the petroleum strategic reserve facility at Jinja.

The restocking in Jinja reserve has however been completely left to Hared with limited capacity to even maintain the required 40% (12 million litres) of the storage capacity at all times as per the concession agreement.

In September 2015, there were only 274,000 litres of Petrol and 331,000 litres of Diesel in stock compared to the required stock levels of 20,000,000 and 10,000,000 litres respectively.

The national petroleum reserves are not serving the purpose for which they were established of ensuring available supply of fuel products at all times and Uganda is at a risk of experiencing the same challenges should political instability reoccur during the August 2017 elections in Kenya.

Policy options to ensure a sustainable supply

a) Restocking the 30 million storage tanks in Jinja whose cost is approximately Ug shs 20 billion and refurbishment /construction and operationalization of the Nakasongola 40 million storage tanks whose engineering design studies were completed in May 2015.

b) Operationalization of an alternative supply route. Since the southern route through Tanzania is distant compared to the Kenyan route, it requires a tax rebate to make it operational on a permanent basis. The proposed rebate of Ug shs 150 leaves the tax on Diesel at Ug shs 380 down from Ug shs 530 and as a result, the revenue loss would be Ug shs 28billion. The loss would be lower than the revenue loss that would be incurred as it were during the Kenya post-election violence in 2007.

Conclusion

Most of the expenditure from the development budgets is on grid power interventions, which is good allocative efficiency. However, the petroleum supply that is poorly funded has strategic objectives that should be considered. Absence of functioning fuel reserves and alternative supply route greatly affects the economy, as it is leads to suppressed demand, inflation, and revenue loss.

Recommendations

- The Ministry of Energy and Mineral Development; and Ministry of Finance, Planning and Economic Development (MFPED) should allocate more funds to the Petroleum Supply Vote Functions to enable the restocking of the strategic reserves.
- The MFPED should provide a tax rebate for the southern route.

References

1. Budget Monitoring Reports FY 2009/10 - FY 2014/15
2. MEMD, Ministerial Policy Statement FY 2009/10 - FY 2014/15
3. MFPED, Approved Estimates of Revenue and Expenditure FY 2009/10 - FY 2014/15
4. National Planning Authority, (2010, 2015) National Development Plan(I &II)
5. IFMS Data (FY2009/10- FY2014/15)
6. MEMD, Tax Rebate on the southern route of petroleum products transportation to Uganda: Financial implications.

For more information contact:

Budget Monitoring and Accountability Unit (BMAU)

Ministry of Finance, Planning and Economic Development

P.O Box 8147, Kampala

www.finance.go.ug