



PARLIAMENT OF UGANDA

**REPORT OF THE COMMITTEE ON NATIONAL ECONOMY ON THE PROPOSAL
BY GOVERNMENT TO BORROW UP TO SDR 145.9 MILLION (US\$200 MILLION)
FROM THE INTERNATIONAL DEVELOPMENT ASSOCIATION (IDA) OF THE
WORLD BANK GROUP TO SUPPORT THE UGANDA INTERGOVERNMENTAL
FISCAL TRANSFERS PROGRAM (UGIFT) FOR RESULTS IN THE EDUCATION
AND HEALTH SECTORS**

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Office of the Clerk to Parliament
Parliament Building
Kampala

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MARCH 2019

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1.0 INTRODUCTION

The Committee on National Economy considered the request by Government to borrow up to SDR 145.9 million (US\$200 million) from the International Development Association (IDA) of the World Bank Group to support the Uganda Intergovernmental Fiscal Transfers Program (UgIFT) for results in the Education and Health Sector, in accordance with **Rule 175(2)(b)** of the Parliamentary Rules of Procedure.

The request was presented to the House by the Hon. Minister of Finance, Planning and Economic Development on 13th September 2018, and was accordingly referred to the Committee on National Economy for consideration.

The Committee considered and scrutinized the request and now begs to report.

2.0 METHODOLOGY

2.1 Meetings

The Committee held meetings with the following:

- i. The Minister of Finance, Planning and Economic Development;
- ii. The Minister of Health; and
- iii. The Minister of Education.

2.2 Documentary Review

The Committee studied and made reference to the following documents:

- i. The Minister of Finance, Planning and Economic Development's Brief on the loan request;
- ii. The Draft Loan Agreement between the International Development Association (IDA) of the World Bank Group and the Republic of Uganda for financing the Project;
- iii. The Program Appraisal Document (June 2017);
- iv. The letter from H.E the President to the Minister of Finance, Planning and Economic Development on Pipeline Projects under Design: Request for Approval, dated 13th November 2017 (Ref: PO/10);
- v. The action extract from Minute No.204 of the Meeting of the Cabinet on 16th April 2018 for action by Permanent Secretary/Secretary to the Treasury (PS/ST), Ministry of Finance, Planning and Economic

Development on the proposal to borrow up to SDR 145.9 million (US\$200 million) from the International Development Association (IDA) of the World Bank Group to support the Uganda Intergovernmental Fiscal Transfers Program (UgIFT) for results;

- vi. The Uganda Intergovernmental Fiscal Transfers Program (UgIFT) Operations Manual cleared by the Program Oversight Committee on 4th September 2018;
- vii. The National Planning Authority Report on the Review of the Loan for the Intergovernmental Fiscal Transfers Program, dated 3rd October 2018;
- viii. The letter from the Commission Secretary, Local Government Finance Commissions to the PS/ST, Ministry of Finance, Planning and Economic Development on the nomination of Mr. Gumisiriza Johnson as the contact person for implementation of the Intergovernmental Fiscal Transfers Program, dated 5th October 2018;
- ix. The letter from the Permanent Secretary, Ministry of Local Government to the PS/ST, Ministry of Finance, Planning and Economic Development on the nomination of Mr. Gad Twesigye as the contact person for implementation of the Intergovernmental Fiscal Transfers Program, dated 5th October 2018;
- x. The letter from the Permanent Secretary, Ministry of Education and Sports to the PS/ST, Ministry of Finance, Planning and Economic Development on discussion of the Intergovernmental Fiscal Transfers Program by Parliament, dated 8th October 2018;
- xi. The letter from the Permanent Secretary, Ministry of Works and Transport to the PS/ST, Ministry of Finance, Planning and Economic Development on the nomination of Engineer Nabbosa as the contact person for implementation of the Intergovernmental Fiscal Transfers Program, dated 8th October 2018;
- xii. The letter from the Permanent Secretary, Office of the Prime Minister to the PS/ST, Ministry of Finance, Planning and Economic Development on the on discussion of the Intergovernmental Fiscal Transfers Program by Parliament dated 10th October 2018;
- xiii. The letter from the Auditor General, Office of the Auditor General to the PS/ST, Ministry of Finance, Planning and Economic Development on the nomination of Mr. Kateregga Stephen as the contact person for implementation of the Intergovernmental Fiscal Transfers Program dated 15th October 2018;
- xiv. The letter from the Permanent Secretary, Ministry of Health to the PS/ST, Ministry of Finance, Planning and Economic Development on the discussion of the Intergovernmental Fiscal Transfers Program by Parliament dated 15th October 2018; and

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- xv. The Procurement Plan of the Uganda Intergovernmental Fiscal Transfers Program (UgIFT) for results in the Education and Health Sector Project.

3.0 BACKGROUND

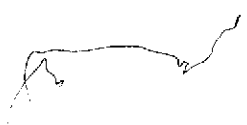
From the last three decades, Government of Uganda has been implementing the Decentralization Policy where, based on the 1995 Constitution and the Local Government Act Cap 243, functions, powers and responsibilities are devolved and transferred from the Central Government to Local Government units in a coordinated manner to ensure peoples' participation and democratic control in decision making.

In 2001, Government conducted a fiscal decentralization study that informed the Fiscal Decentralization Strategy (FDS), 2002. To deliver on the mandate of fiscal decentralization, Government is providing Local Governments (LGs) with Unconditional, Conditional and Equalization Grants as sources of financing that enable them to fulfill their service delivery mandates. Key objectives of the FDS were to strengthen the process of decentralization by increasing LGs' autonomy, widening the local participation in decision making, and streamlining the fiscal transfer modalities to the LGs. These measures were aimed at increasing the efficiency of LGs to achieve national development goals within a transparent and accountable framework. The implementation of the FDS succeeded in streamlining of budgeting and reporting processes, but it also demonstrated some shortcomings.

The shortcomings of the FDS triggered two studies that were undertaken by Local Government Finance Commission (Review of Local Government Financing, 2012) and the World Bank in partnership with the Ministry of Finance, Planning and Economic Development (Service Delivery with more Districts in Uganda-Fiscal Challenges and Opportunities for Reform - 2012).

The main findings of the studies were as follows:

- i. The FDS was successful in streamlining of budgeting, accounting and reporting processes;



- ii. LGs had limited discretion to decide on allocation of resources;
- iii. Sizable inequalities in the allocation of resources;
- iv. Lack of incentives for LGs to account adequately for resources; and
- v. Reduced per capita value of transfers.

To implement the recommendations of the two aforementioned studies, a reform of Intergovernmental Fiscal Transfers was initiated in FY 2015/16 and led to the development of the Intergovernmental Fiscal Transfer Reform Program (IFTRP) by the Ministry of Finance, Planning and Economic Development. The IFTRP sought to address adequacy in the financing of service delivery by LGs, ensure equity in the allocation of resources to LGs and achieve efficiency in local government service delivery efforts.

The reform of the Intergovernmental Fiscal Transfers identified and agreed upon the following four phases:

- i. Phase 1 - Consolidation of conditional transfers;
- ii. Phase 2 - Revision of allocation formulae and budget requirements and consolidation of discretionary development transfers;
- iii. Phase 3 - Reforming frameworks for accountability and strengthening incentives for performance; and
- iv. Phase 4 - Fiscal Decentralization Architecture and Share Transfers.

In 2017, Government started to implement the Intergovernmental Fiscal Transfers Reform Program focusing on three main objectives, which particularly relate to Phase 2, 3 and 4, that is, restore adequacy in financing of decentralized service delivery, ensure equity in allocation of funds to LGs for service delivery and improve the efficiency of LGs in the delivery of services.

In order to restore adequacy and implement the allocation formulae to ensure equity without reducing any existing allocations to LGs, Government sourced for credit financial support (US\$200 million) from the World Bank, through an Intergovernmental Fiscal Transfers Program for results in the education and health sectors.

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4.0 PROJECT LINKAGE TO COUNTRY STRATEGIES

Uganda's medium term objectives are guided by the National Development Plan (NDP) II 2015/16 - 2019/20. The Intergovernmental Fiscal Transfer Reform Program (IFTRP) for results in the education and health sectors is in line with the National Development Plan (NDP) II 2015/16-2019/20, in particular strategic objective 4, which focuses on strengthening mechanisms for quality and effective service delivery. As a result, this program is fully linked to the National Development Plan (NDP).

The IFTRP furthers the implementation of GoU's Fiscal Decentralization Strategy (FDS). The FDS agenda was given renewed impetus by Uganda's Second National Development Plan (NDP) II 2015/16 - 2019/20. The FDS seeks to strengthen the process of decentralization in Uganda through increasing LGs' autonomy, widening local participation in decision making and streamlining fiscal transfer modalities to LGs in order to increase the efficiency and effectiveness of LGs in service delivery.

5.0 PERFORMANCE OF DEBT FINANCED PROJECTS IMPLEMENTED BY THE MINISTRY OF HEALTH AND THE MINISTRY OF EDUCATION AND SPORTS

There are 11 approved ongoing projects in the education sector being implemented by Ministry of Education and Sports amounting to US\$386,900,000 of which US\$126,138,630 million has been disbursed representing a disbursement rate of 32.7% as at 31st December 2018. The majority of loans in the Education Sector have disbursement rates that are still below 50% (**Table 1**).

There are also five approved ongoing projects in the health sector being implemented by Ministry of Health amounting to US\$375,700,000 of which US\$207,000,000 million has been disbursed, representing a disbursement rate of 55.1% as at 31st December 2017 (**Table 2**).

TABLE 1: FINANCIAL PERFORMANCE OF PROJECTS UNDER THE MINISTRY OF EDUCATION AND SPORTS AS AT 31ST DECEMBER 2017

LOAN TITLE/PURPOSE	CREDITOR	APPROVAL DATE	AMOUNT IN US\$	DISBURSED AMOUNT IN US\$	% DISBURSED
National Education Project (NTCs Devt & Expansion)	IDB	18/05/2010	14,100,000	8,360,000	59.3%
Construction and Equipping of 14 Technical Institutes in the TVET	Saudi Fund for Devt	18/05/2010	12,400,000	4,500,000	36.3%
Construction and Equipping of 14 technical Institutes in the TVET	OPEC	18/05/2010	23,000,000	22,000,000	95.7%
ADB Education IV PPET Expansion & Improvement Project (Supplementary)	Exim Bank-South Korea	02/12/2010	26,800,000	26,600,000	99.3%
Construction and Equipping of four (4) technical institutes in the technical, vocational education and training programme	KUWAIT FUND	31/10/2012	11,900,000	6,503,000	54.6%
Higher Educational Science and Technology Project	ADB	21/05/2013	103,900,000	44,677,000	43.0%
Albertine Region Sustainable Development Project	IDA	22/07/2015	25,000,000	3,423,530	13.7%
East African Centres of Excellence for Skills and Tertiary Education in Biomedical Sciences - Phase 1	ADB	20/08/2015	31,500,000	2,500,000	7.9%
Skills Development Project	IDA	20/4/2016	100,000,000	3,065,100	3.1%
Eastern and Southern Africa Higher Education Centres of Excellence Project	IDA	21/02/2017	24,000,000	4,400,000	18.3%
Vocational Education Project Phase II	OPEC	21/02/2017	14,300,000	110,000	0.8%
Total			386,900,000	126,138,630	32.6%

Source: MoES & MoFPED, December 2018

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- ii. The FDS agenda was given renewed impetus by Uganda's Second National Development Plan (NDP II) 2015/16-2019/20. In response to the declining trends in LG financing, the NDP II includes objectives to "increase financing and revenue mobilization of LGs to match the functions of LGs" which commits the Government to "redesign the fiscal decentralization architecture to provide for adequate and sustainable local government financing" and "review grants allocation formulae to promote adequacy in financing of decentralized services." (NDP II, p.235)
- iii. The IFTRP covers all fiscal transfers to LGs, which together fund the bulk of local administrative costs and service delivery in six sectors, and account for 3.4 percent of GDP (as at June 2017). These sectors include; agricultural production and marketing, works and transport, education, health, water and environment, and social development. Within this, UgIFT will focus on health and education sector expenditures on conditional non-wage recurrent and development transfers.

7.0 PROGRAM OBJECTIVES

The overall goal of the Uganda Intergovernmental Fiscal Transfer Reform Program (UgIFTRP) is to improve the adequacy and equity of fiscal transfers and improve fiscal management of resources by LGs for health and education services.

7.1 Specific Program Objectives:

The Intergovernmental Fiscal Transfer Reform Program (IFTRP) has been developed to address the challenges in the functioning of the national government's financing of local government service delivery. The IFTRP has five specific objectives:

- i. Increasing discretion over allocation decisions to enable LGs deliver services in line with local needs while ensuring that national policies are implemented.
- ii. Restoring adequacy and equity in allocation of funds for service delivery.
- iii. Shifting the focus away from fragmented input-based conditions toward accountability for budgetary allocation decisions, expenditure, and results.
- iv. Using the transfer system to lever institutional and service delivery performance.
- v. Allowing new national policies to be funded via the transfer system, whilst avoiding future fragmentation of transfers and reduction in discretion.

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Services	Number of Performance Improvement Plans prepared for Local Governments and thematic areas	Number of LGs and thematic areas	0 LGs & 0 Areas (2016/17)	20 LGs & 2 Areas (2021/22)
	Value for Money Audit Completed		No (2016/17)	Yes (2021/22)

Source: Program Operation Manual (September, 2018)

9.0 PROGRAM BENEFICIARIES

Beyond the development objectives of UgIFT, it is envisaged that more equitable, adequate and efficient financing of health and education services will ultimately lay the foundation for improved service delivery outcomes. In doing so, it will complement other sectoral programs, including World Bank operations in health and education, and planned governance operations. The impact of UgIFT on service delivery outcomes will depend on these operations, as well as other interventions. The final beneficiaries of UgIFT will be consumers of health and education services at the local level. Those who will benefit the most will be those living in the most underfunded districts and municipalities.

10.0 PROGRAM SCOPE

The Program will support the next stage of the reform (launched in 2016), that is, the new consolidated framework for the grants, development of formulae, grant conditions, budgeting and reporting guidelines for the new framework in three areas. UgIFT will:

- i. support the implementation of new, simple and transparent formulae for education and health non-wage conditional grants;
- ii. help restore the adequacy of funding to LGs, by providing additional resources to support the associated plan for uplifting transfers, which will also enable the phase in the new formulae; and

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TABLE 5: PROGRAM SUMMARY EXPENDITURE FRAMEWORK (USHS. BILLION)

Grant Allocations	2017/18	2018/19	2019/20	2020/21	2021/22	Total
Total Education	263.88	349.75	431.63	481.25	526.64	2,053.15
Education Sector Non-Wage Recurrent Grant	231.38	290.89	337.50	381.11	422.51	1,663.39
Education Sector Development Grant	32.51	58.86	94.14	100.14	104.14	389.79
Total Health	47.07	118.69	147.87	176.04	203.14	692.81
Health Non-Wage Recurrent Grant	47.07	68.43	86.61	107.78	129.88	439.77
Health Sector Development Grant	0.00	50.26	61.26	68.26	73.26	253.04
Total Management, Assessment & Support	8.00	10.50	10.50	10.50	10.50	50.00
GRAND TOTAL (UGX billions)	318.95	478.94	590.00	667.79	740.28	2,795.96
IDA Resources (UGX billions)	143.18	141.80	141.85	141.84	141.83	709.99
GoU Resources (UGX Billions)	175.77	337.14	448.15	525.95	598.45	2085.97
GRAND TOTAL (US\$m)	89.85	134.91	166.20	188.11	208.53	787.59
IDA Resources (US\$m)	40	40	40	40	40	200
GoU Resources (US\$m)	49.1	95.1	126.39	148.3	168.72	587.59

Source: Program Appraisal Document (June, 2017)

Table 5 shows how IDA resources will be disbursed. The IDA resources, in effect, pay for the annual increase in sector grants each year from 2018/19 onwards. Cumulative increase in conditional transfers to LGs for health and education services in the course of the program implementation, compared to a scenario where their amounts would remain at their 2016/17 levels, is projected at US\$475 million (US\$315 million for education and US\$160 million for health). This increase exceeds the amount of IDA credit by US\$275 million.

TABLE 6: PROGRAM SOURCES OF FINANCING

Sources of Financing	Amount (US\$, millions)	% Total
IDA	200.00	25.3%
Government of Uganda	587.59	74.7%
Total Program Cost	787.59	

Source: Program Appraisal Document (June 2017)

12.0 SECTOR UTILISATION OF THE IDA LOAN

In line with the Cabinet approval, the following guidance was provided:

12.1 Education Sector:

The education sector development component of the loan financing will be allocated **US\$130 million** equivalent to Ushs.460 billion, and will be spent on construction of 242 Seed Secondary Schools in sub-counties where they are not (Refer to Annex 1 attached, for the list of sub-counties/Seed Secondary Schools to benefit from the UgIFT program; this list was reduced from 322 to 242 to fit within the resources of the anticipated loan facility).

12.2 Health Sector:

The health development component of the loan financing will be allocated **US\$55 million** equivalent to Ushs.200 billion and will be spent on upgrading 124 HCIIIs to HCIIIs in sub-counties that do not have a government HCIII and provision of funds for health infrastructure maintainance.

12.3 Program Management:

The program implementation component of the loan financing will be allocated **US\$15 million** equivalent to Ushs.50 billion, and will be used to support the smooth implementation of the program. This will include;

- i. Management and implementation of annual Local Government Performance Assessment (**Ushs.21.2 billion**) to be conducted by the Office of the Prime Minister;
- ii. Targeted Technical Support (**Ushs.10 billion**) to poor performing LGs under the coordination of the Ministry of Local Government;
- iii. Value for Money Audit (**Ushs.5.2 billion**) to be undertaken by the Office of the Auditor General; and
- iv. Grant Management (**Ushs.13.6 billion**), including verification protocols that will be undertaken by Local Government Finance Commission.

13.0 CONDITIONS FOR GOVERNMENT ACCESS TO THE IDA LOAN FUNDS

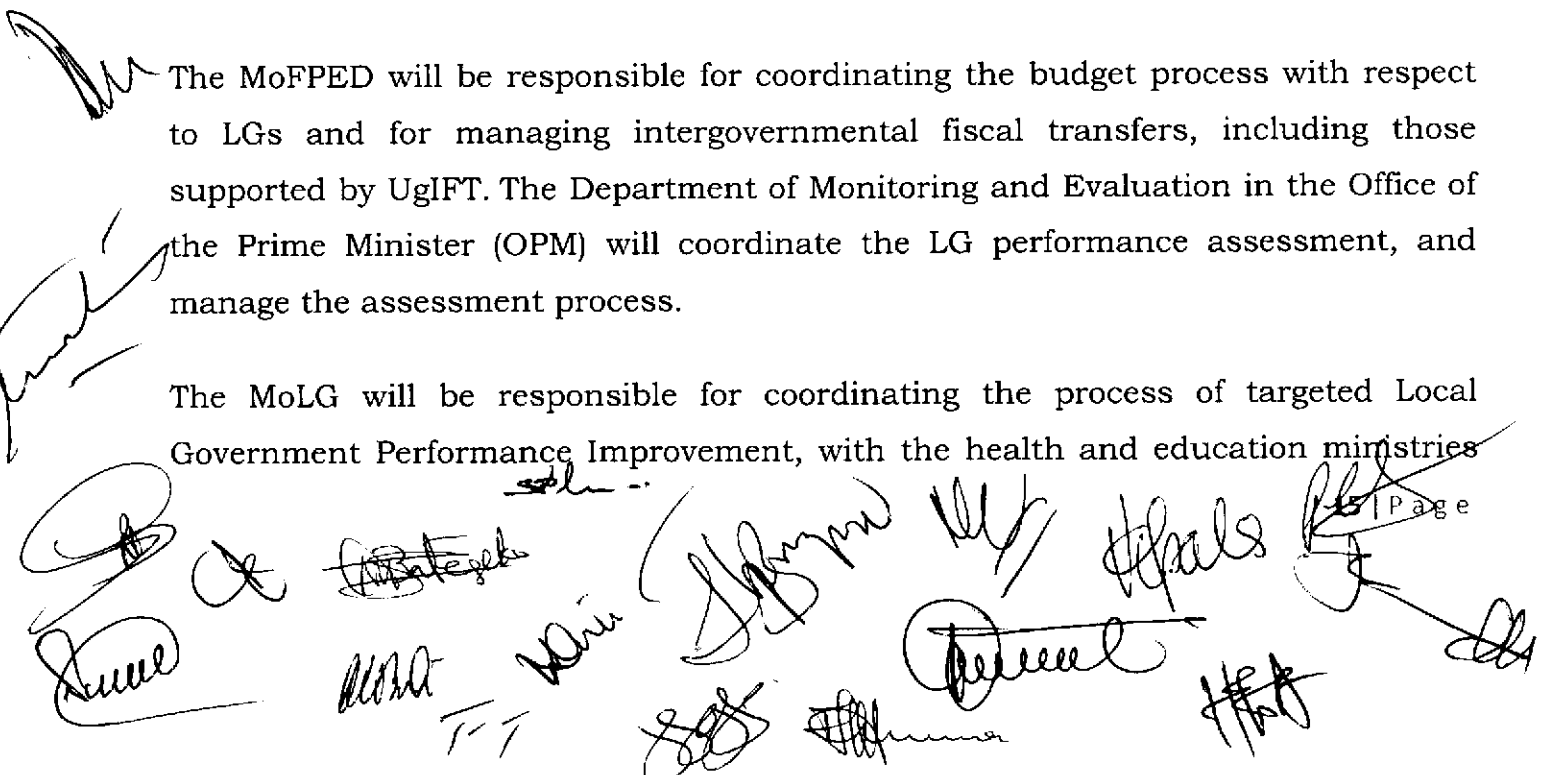
- a) To access the loan funds, Government will have to achieve a number of results measured through the Disbursement Linked Indicators (DLIs), which are focused on adequacy, equity and efficiency improvement. These include the following for both the education and health sectors:
 - i. Enhancing adequacy and equity of fiscal transfers and fiscal management of resources;
 - ii. Increasing the annual budget allocation to sector conditional grants (wage, non-wage, recurrent and development);
 - iii. Enhancing equitable formula for allocating both operational and development grants; and
 - iv. Conducting performance assessments, value for money audits and fiscal management improvement planning.
- b) After the World Bank disbursement, the funds become part of Government of Uganda budget and are indistinguishable from government resources.
- c) The funds will be budgeted and directly disbursed to LGs as part of the health and education non-wage recurrent and development grants.

14.0 PROGRAM IMPLEMENTATION

The implementation of Uganda Intergovernmental Fiscal Transfer Program (UgIFT) will use existing GoU structures and no parallel implementation and oversight structures will be created.

The MoFPED will be responsible for coordinating the budget process with respect to LGs and for managing intergovernmental fiscal transfers, including those supported by UgIFT. The Department of Monitoring and Evaluation in the Office of the Prime Minister (OPM) will coordinate the LG performance assessment, and manage the assessment process.

The MoLG will be responsible for coordinating the process of targeted Local Government Performance Improvement, with the health and education ministries



and other relevant parties, and for ensuring clear communication to stakeholders, including LGs, of their roles in the context of the program.

The Ministries of Health and Education are responsible for sector policies and strategies, which govern local service delivery, for development of the grant formulae and guidelines, and medium term grant allocations within sector ceilings. They will also be responsible for overseeing the sectoral elements of the assessment process, and providing targeted performance improvement support to LGs in their sectors.

Two committees, chaired by MoFPED, to oversee the management of Fiscal Transfers will be established under the IFTRP. They will be made up of the representatives of the Ministries of Health, Education, OPM, MoLG, Local Government Finance Commission (LGFC), local authorities associations and other relevant parties. LGFC will advise these two committees on issues relating to local government financing, and also verify all Disbursement Linked Indicators (DLIs) except those relating to the LG performance assessment.

While all program activities will be implemented by the central government, the LGs will be responsible for:- preparation of LG budgets and work plans, which adhere to requirements set out in grant guidelines; generating accounting warrants to access releases; delivery of services and infrastructure; preparing quarterly budget performance reports; and capacity building. Poorly performing LGs will be required to also agree to and implement the performance improvement plans.

15.0 PROGRAM ECONOMIC IMPACT

The provision of basic health and education services benefits not only recipients of these services, but also others and the nation as a whole. The Program will increase value-for-money in education and health expenditures in the districts that are lagging behind, which will help to achieve better outcomes for any given level of spending. Bringing every district up to the outcome-to-spending ratio of the districts that perform very highly in both health and education sectors is estimated to save about 0.8 percent of GDP.

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The financial resources from and the more equitable allocation formulae supported by the Program will support LGs' plans to improve delivery of health and education services, which will lead to improved outcomes.

The Program supports the principle that every child should have the same opportunities no matter where they live. Equality of opportunity embodies not only an equity benefit, but also can produce economic benefits for the reasons stated above. Shifting resources to those areas that currently offer less opportunity and less funding, will have a larger effect on education and health outcomes.

16.0 LOAN TERMS AND BUDGETARY IMPLICATIONS

The International Development Association (IDA) of the World Bank Group will make available SDR 145.9 million (**US\$200 million**) to support the Uganda Intergovernmental Fiscal Transfers Program (UgIFT) under the terms indicated below.

The loan terms are as follows:

TABLE 7: IDA LOAN TERMS

Item	Terms
Loan Amount	SDR 145.9 million (US\$ 200 million)
Maturity Period	38 years
Repayment period	32 years
Grace period	6 years
Service charge	0.75% p.a. on disbursed and outstanding loan
Commitment fee	0.5% p.a. on undisbursed

Source: Draft Loan Agreement (May 2017)

Table 7 shows that a service charge of 0.75% will be applied on the principal amount of the loan disbursed and outstanding throughout the availability period. Furthermore, the undisbursed amount of the loan will be subjected to a commitment charge of 0.5% per annum during the grace period. With the above terms, the cost of the loan is indicated in the **Table 8**.

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A commitment fee of 0.5% will be applied per annum on the undisbursed amount of the loan. This implies the conditions of disbursements should be met as per Article V of the Draft Agreement.

TABLE 8: LEVEL OF CONCESSIONALITY OF THE LOAN

Item	Value/ Rate
Maturity	38years
Grace period	6 years
Present value of the loan(PV)	US\$95.21 Million
Total Debt Service of the loan	US\$235.75 Million
Grant Element (%)	52%
Discount Rate	5%

Source: Draft Loan Agreement, DRS

From **Table 7**, the present discounted value of the loan (US\$95.21 million) is smaller than the nominal value of the loan contracted (US\$200 million). This implies that the total future payment of the loan is cheaper than the proposed amount to be borrowed in present terms. The total future payment of the loan will amount to US\$235.75 million after the loan period of 38 years.

The loan is highly concessional since its grant element (52%) is higher than the PDMF, 2013 threshold of 35% for concessional loans.

16.1 Conditions for Disbursements:

The following conditions are attached to the Loan:

- i. Issuance of a legal opinion of the Attorney General of Uganda on the legal validity of the loan; and
- ii. Preparation and adoption of the Program Operational Manual.

16.2 Budgetary Implications:

- For FY 2018/19 budget, Ushs.96 billion was provided to start construction of 127 seed secondary schools.
- For FY 2018/19 budget, Ushs.69.36 billion was provided to upgrade 124 HCIIIs to HCIIIs.

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