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SENIOR SIX TERM 2

TOPIC 2/2: Public Finance and Fiscal Policy

Competency: The learner advises the community on the sources of Public Finance and its uses, the need to have an effective Fiscal Policy for a country, the need to improve a country's tax revenue collection and the need for good public debt management practices in an economy for national development.

Public finance versus private finance

Public Finance

Public finance is a science which studies the principles of allocation of government revenue and distribution of Public expenditure.

OR.

It is a science which deals with the principles concerning the collection of government revenue and how it is allocated for development purposes through public expenditure.

Private finance

Private finance deals with income and expenditure of private individuals, companies and Non-government organizations.

Public finance include the following divisions

- (i) Public expenditure
- (ii) Public revenue
- (iii) Publicdebt
- (iv) Financial administration
- (v) Fiscal policy

Public expenditure

This is the total amount of money the government spends on the provision of social services and other development activities.

Forms (Types) of Public expenditure

(a) Recurrent (Operating) Expenditure

This refers to government expenditure for the day to day running of the state for example expenditure of salaries of civil servants, defense, education, medical services etc.

(b) Capital (Development) Expenditure.

This is the form of government expenditure on medium and long-term development projects for example expenditure on construction of roads, dams, industries, buildings etc.

Problems (Challenges) Faced in effecting Public expenditure

- (i) **Revenue limitations:** Low tax base and weak tax collection systems reduce available funds for expenditure.
- (ii) **Budget deficits and debt dependence:** Heavy reliance on borrowing (domestic and foreign) leads to debt servicing pressures, leaving fewer resources for development.
- (iii) **Corruption and mismanagement:** Misuse of public funds, embezzlement, and lack of transparency reduce efficiency and effectiveness of spending.
- (iv) **Political interference:** Expenditure decisions are often influenced by political priorities rather than economic needs, leading to misallocation of resources.
- (v) **Inefficient financial administration:** Weak planning, poor monitoring, and delays in disbursement hinder timely and effective use of funds.
- (vi) **Structural bottlenecks:** Poor infrastructure, low productivity, and weak institutions limit the impact of public spending.
- (vii) **Overdependence on foreign aid:** Reliance on donor funding can cause instability when aid flows are delayed or withdrawn.
- (viii) **Inflationary pressures:** Excessive government spending without matching production can fuel inflation, reducing the real value of expenditure.
- (ix) **Limited human capacity:** Shortage of skilled personnel in financial management and project implementation leads to inefficiency.

Example (Uganda Context)

- (i) Uganda faces **budget deficits** due to limited tax revenue, forcing reliance on external loans.
- (ii) **Corruption scandals** in public procurement reduce trust and effectiveness of expenditure.
- (iii) **Delays in disbursement** of funds for infrastructure projects slow down development.
- (iv) Heavy dependence on **donor funding** sometimes disrupts projects when aid conditions are not met.

Public revenue

This refers to the total income received by the government from different sources in a given time.

Sources of public revenue

- (i) **Tax Revenue: Direct taxes** such as Income tax, corporate tax, property tax and **Indirect taxes such as** Value Added Tax (VAT), excise duty, customs duties.

- (ii) **Non-Tax Revenue:** Fees and charges such as Court fees, license fees, registration fees; Fines and penalties such as Traffic fines, regulatory penalties and Profits from state-owned enterprises.
- (iii) **Grants and Aid:** Financial assistance from foreign governments, international organizations (World Bank, IMF), and NGOs. Often used to support development projects and budget deficits.
- (iv) **Borrowing (Public Debt):** Domestic borrowing such as Treasury bills, bonds from local banks and citizens and External borrowing such as Loans from international institutions and foreign governments.
- (v) **Natural Resource Revenue:** Income from exploitation of natural resources such as oil, minerals, and forests and Royalties, licenses, and export earnings.
- (vi) Privatization proceeds (sale of government assets).
- (vii) Dividends from government investments.

Example (Uganda Context)

- (i) **Taxes:** Uganda Revenue Authority (URA) collects VAT, excise duty, and income tax as major sources.
- (ii) **Non-tax revenue:** Fees from passports, driving permits, and court services.
- (iii) **Aid and grants:** Support from the World Bank and IMF for infrastructure and health projects.
- (iv) **Borrowing:** Treasury bills and Eurobonds to finance budget deficits.
- (v) **Natural resources:** Oil exploration and mineral royalties expected to boost future revenue.

Public debt

Public debt refers to the total amount of money that a government borrows to finance its expenditure when revenues (like taxes) are not sufficient. It is also called **national debt** or **government debt**.

Financial administration

This involves ways of controlling public finances through budgeting public auditing

Fiscal policy

This refers to deliberate government policy of using taxation, government expenditure and borrowing to regulate the level of economic activity.

Tools (Instruments) of the fiscal policy

1. Government expenditure
2. Taxation
3. Public borrowing

Taxation

Taxation refers to the legal compulsory transfer of money from individuals and companies to the government as a source of revenue.

A **tax** refers to the non-quid proquo compulsory payment to the government by public. It is non- quid proquo in a sense that services or benefits received by the payer from the government may not necessarily correspond to the amount of tax paid.

Objectives (Aims) of taxation (Fiscal policy) in an Economy

- (i) **Revenue Generation:** The primary aim is to raise funds for government expenditure on public goods and services such as education, healthcare, infrastructure, and defense.
- (ii) **Economic Stabilization:** Taxes help control inflation and deflation by regulating demand. Higher taxes can reduce excessive demand (anti-inflationary), while lower taxes can stimulate demand during recessions.
- (iii) **Redistribution of Income and Wealth:** Progressive taxation ensures that the rich contribute more, reducing inequality. Funds collected can be used for welfare programs to support low-income groups.
- (iv) **Resource Allocation:** Taxes can direct resources toward productive sectors. For example, tax incentives encourage investment in agriculture, industry, and renewable energy, while higher taxes discourage harmful activities (like tobacco or carbon emissions).
- (v) **Encouraging or Discouraging Behavior:** Taxes on harmful goods (alcohol, cigarettes, polluting industries) discourage consumption. Tax breaks encourage savings, investment, and innovation.
- (vi) **Debt Management:** Tax revenue reduces reliance on borrowing, helping governments manage public debt sustainably.
- (vii) **Promoting Economic Growth:** By funding infrastructure, education, and health, taxation supports long-term productivity and development.

Example (Uganda Context)

- (i) Uganda uses **income tax and VAT** to raise revenue for public services.
- (ii) **Excise duties on alcohol and fuel** discourage excessive consumption and raise funds.
- (iii) **Tax incentives** are offered to investors in agriculture and manufacturing to promote industrialization.
- (iv) Progressive taxation helps redistribute income, while fiscal policy stabilizes inflation through adjustments in tax rates.

Principles (canons) of taxation

The **principles (or canons) of taxation** are guidelines that ensure a tax system is fair, efficient, and effective. These were first popularized by economist **Adam Smith** in his book *The Wealth of Nations* (1776), and later expanded by other economists.

- (i) **Canon of Equity (Fairness):** Taxes should be based on the ability to pay. Hence, richer individuals should contribute more than poorer ones (progressive taxation).
- (ii) **Canon of Certainty:** Taxpayers should know clearly how much, when, and where to pay. Avoids arbitrary or unpredictable taxation.
- (iii) **Canon of Convenience:** Taxes should be collected in a manner and time convenient to taxpayers. Example: income tax deducted directly from salaries.
- (iv) **Canon of Economy (Efficiency):** The cost of collecting taxes should be low compared to the revenue raised. Avoid wasteful administrative expenses.

Additional Modern Principles

- (v) **Canon of Productivity:** Taxes should generate sufficient revenue to meet government needs.

- (vi) **Canon of Elasticity (Flexibility):** Tax system should adjust easily to changing economic conditions (e.g., crises, recessions).
- (vii) **Canon of Simplicity:** Tax laws should be simple and easy to understand to avoid evasion.
- (viii) **Canon of Neutrality:** Taxes should not distort economic decisions unnecessarily (e.g., discourage investment or trade).
- (ix) **Elasticity (Flexibility).** The tax revenue should vary directly with the exchange in tax base e.g. is the tax base increases the tax changed on the tax base should also increase & vice versa.
- (x) **Diversity (comprehensiveness).** A good tax system should have a wider coverage so that all sectors and groups of society contribute to government tax revenue.
- (xi) **None discriminative:** A good tax system should not discriminate tax payers basing on tribe, race religion etc.

Example (Uganda Context)

- (i) **Equity:** Progressive income tax ensures higher earners contribute more.
- (ii) **Certainty:** Uganda Revenue Authority (URA) sets clear tax rates and deadlines.
- (iii) **Convenience:** Mobile money tax collection makes payment easier for rural populations.
- (iv) **Economy:** URA uses digital systems to reduce collection costs.

Features (Characteristics) of a good tax system

A **good tax system** ensures that taxation is fair, efficient, and supportive of economic growth while providing adequate revenue for government expenditure. Economists highlight several essential characteristics:

- (i) **Equity (Fairness):** Taxes should be based on the ability to pay. Progressive taxation ensures wealthier individuals contribute more than poorer ones.
- (ii) **Certainty:** Taxpayers should clearly know how much, when, and how to pay. Avoids arbitrary or unpredictable taxation.
- (iii) **Convenience:** The method and timing of tax collection should be convenient for taxpayers.
 - Example: income tax deducted directly from salaries.
- (iv) **Economy (Efficiency):** The cost of collecting taxes should be low compared to the revenue raised. Prevents wasteful administrative expenses.
- (v) **Elasticity (Flexibility):** The tax system should adjust easily to changing economic conditions, such as inflation or recession.
- (vi) **Productivity (Adequacy):** Taxes should generate sufficient revenue to meet government needs without excessive **borrowing**.
- (vii) **Simplicity:** Tax laws should be easy to understand, reducing evasion and compliance costs.
- (viii) **Neutrality:** Taxes should not distort economic decisions unnecessarily (e.g., discourage investment or trade).
- (ix) **Stability:** A good tax system should provide a steady and predictable flow of revenue.

Example (Uganda Context)

- (i) **Equity:** Progressive income tax ensures higher earners contribute more.
- (ii) **Convenience:** Uganda Revenue Authority (URA) uses mobile money and online platforms for easy tax payment.

- (iii) **Economy:** Digital tax systems reduce collection costs.
- (iv) **Elasticity:** VAT and excise duties adjust automatically with consumption levels, ensuring revenue stability.

Concepts used in taxation

- (a) **Tax Avoidance.** This refers to the legal tax payer's exploitation of the loopholes (weaknesses) in the tax law as a way of dodging paying the tax.
- (b) **Tax Evasion.** This refers to the deliberate refusal by the tax payer to pay the tax assessed on him or her and it is illegal.

Why people Evade paying taxes

- (i) **Unfair tax assessment** where by the tax administrators fix the tax without considering the income levels of taxpayers.
 - (ii) **Low income levels** due to high levels of poverty.
 - (iii) **Inadequate** information about the importance of paying taxes by the tax payers.
 - (iv) **Discontent** about the provision of services by the government as a result of the tax paid.
 - (v) **Political** instabilities and sabotage especially by people who oppose the government
 - (vi) **Laxity** (weakness) in the tax law.
- (c) **Taxable Income.** This is the amount of income subjected to taxation after deducting personal allowances.
 - (d) **Tax Threshold.** This is the minimum amount of income which is not subjected to taxation.
 - (e) **Tax Liability.** This is the amount of money the tax payer is expected to pay as tax in a given time.
 - (f) **Tax Havens.** These are countries which offer very low tax rates as a way of attracting foreign investors.
 - (g) **Tax Yield.** This refers to the tax revenue after all the collection costs have been subtracted from the total tax collections.
 - (h) **Tax Exemption.** This is where the tax payer is relieved from paying taxes by the tax authorities.
 - (i) **Tax Capitalization.** This is where the firm converts profits into capital as a way of paying less profit tax.
 - (j) **Dead Weight Tax.** This is the tax which when imposed causes the tax payer to abandon the activity he or she is undertaking which forms the tax base.
 - (k) **Tax Structure.** This is the composition of the tax according to either the mode of payment or percentage of income paid as tax.
 - (l) **Taxable Capacity.** This is the ability of the tax payer to pay the tax assessed on him or her and remain with enough disposable income to maintain the standard of living he/she is accustomed to.
 - (m) **Tax Base.** This is any economic activity, property, person or institution which forms the source of income from which the tax is imposed for example land, business etc.

Causes of a narrow Tax base in Uganda (Developing Countries)

- (i) **High levels of poverty:** Many Ugandans earn very low incomes, making them exempt from income tax. While a large share of the population survives on subsistence farming, which is difficult to tax.
- (ii) **Large informal sector:** Most businesses operate informally without proper registration. This makes it hard for the Uganda Revenue Authority (URA) to track and collect taxes.
- (iii) **High unemployment and underemployment:** With limited formal jobs, fewer people pay Pay-As-You-Earn (PAYE) taxes. Underemployment reduces taxable income.

- (iv) **Tax evasion and avoidance:** Weak enforcement and loopholes in tax laws allow individuals and businesses to evade taxes. Corruption among tax officials worsens compliance.
- (v) **Small industrial sector:** Uganda has a limited manufacturing base, reducing corporate tax contributions. Heavy reliance on agriculture and imports narrows taxable activities.
- (vi) **Generous tax exemptions:** To attract investors, the government offers tax holidays and incentives. While encouraging investment, this reduces the overall tax base.
- (vii) **Weak tax administration:** Inadequate skilled personnel and poor monitoring systems hinder effective collection. This leads to revenue leakages and under-collection.
- (viii) **Political interference:** tax policies are sometimes influenced by political motives, exempting certain groups to gain support. This undermines fairness and reduces the taxable population.

Example (Uganda Context)

- (i) Farmers in rural Uganda often operate outside the formal economy, making taxation difficult.
- (ii) Traders in Kampala have protested against **high taxes and harsh enforcement**, showing the tension between broadening the tax base and maintaining compliance.
- (iii) Uganda's reliance on **donor funding and borrowing** reflects the weakness of its domestic tax base.

Tax Impact versus Tax Incidence

Impact of the tax (formal incidence)

Formal incidence of tax refers to the **initial burden of taxation** — that is, the person or entity on whom the tax is legally imposed. For example, if income tax is levied, the formal incidence falls on the individual earning the income; if corporate tax is levied, it falls on the company.

Tax incidence. It refers to the final person who bears that tax burden. OR. It refers to the final resting position of the tax. For example when person A pays the tax to the government on a certain commodity, he can shift the tax burden to the consumer B. therefore the tax incidence finally rests on B.

Note. The tax incidence can be shifted forward or backward.

Forward shifting of the tax. This is where the tax payer shifts the tax burden to the next party in the distribution chain for example a retailer shifting the tax burden to the final consumer in form of increased prices on commodities.

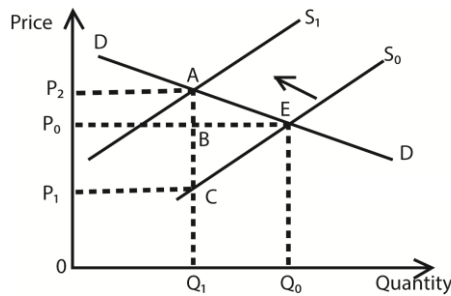
Backward shifting of the tax. This is where the tax payer shifts the tax burden to the previous party in the production process for example the producer shifting the tax burden to the supplier of raw materials by paying low price.

Money burden of the tax. This refers to the tax burden felt when the tax is paid in monetary terms.

Real tax burden. This is the amount of the commodity foregone when the consumer buys less of the commodity due to high prices charged as a result of the tax imposed.

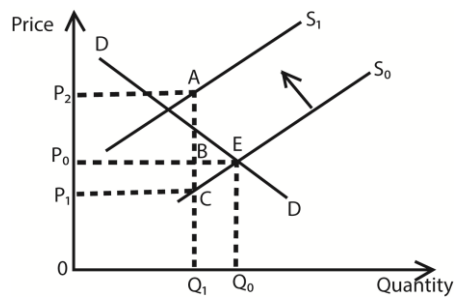
Tax incidence and elasticity of demand

(a) Elastic demand



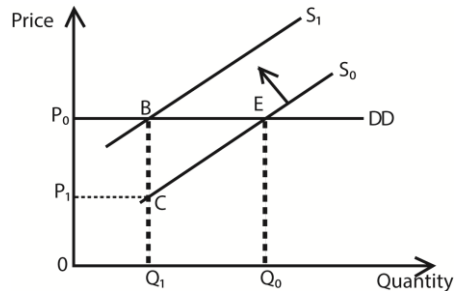
From the graph, when the tax is imposed on the producer, the supply curve shifts to the left from S_0 to S_1 (decrease in supply). The total tax is represented by AC. The proportion of the tax paid by the consumer is **AB** and that of the producer is BC. Since **BC** is greater than **AB**, it means that the producer bears a bigger tax burden than the consumer.

(b) Inelastic demand



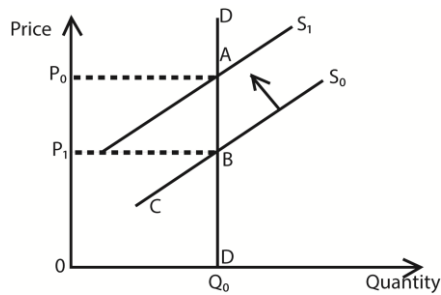
From the graph, when the tax is imposed on the producer, the supply curve shifts to the left from S_0 to S_1 (decrease in supply). The total tax is AC. The proportion of the tax paid by the consumer is AB *and* that of the producer is BC. Since AB is greater than BC, it means that the consumer bears a bigger tax burden than the producer.

(c) Perfectly elastic demand



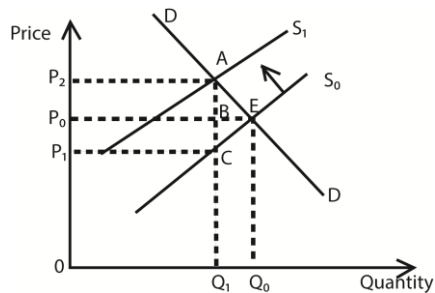
From the graph, when the tax is imposed on the producer, the supply curve shifts to the left from S_0 to S_1 (decrease in supply). The total tax is BC. The proportion of the tax paid by the producer is BC; it means that the producer bears the entire tax burden.

(d) Perfectly inelastic demand



From the graph, when the tax is imposed on the producer, the supply curve shifts to the left from S_0 to S_1 (decrease in supply). The total tax is AB . The proportion of the tax paid by the consumer is AB ; it means that the consumer bears the entire tax burden.

(e) Unitary elastic demand



From the graph, when the tax is imposed on the producer, the supply curve shifts to the left from S_0 to S_1 (decrease in supply). The total tax is AC . The proportion of the tax paid by the consumer is AB and that of the producer is BC . Since AB is equal to BC , it means that the consumer and producer bear equal tax burden.

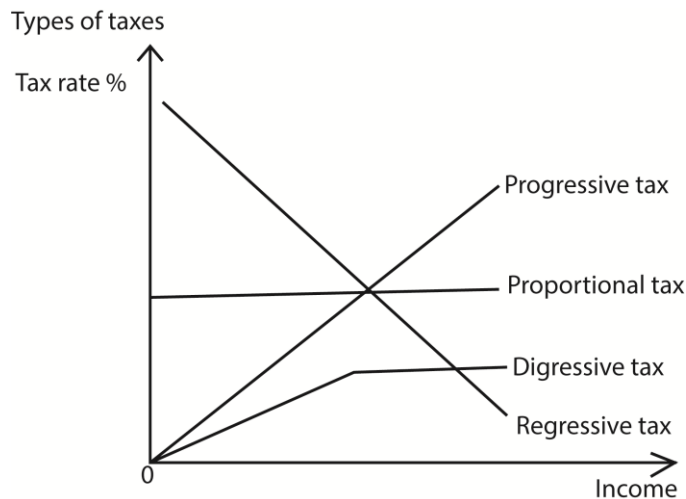
Types of taxes

Taxes can be classified according to;

- (a) Tax to income ratio (tax rates)
- (b) Tax incidence.

Classification according to tax income ratio (Tax rates)

Illustration of different taxes



(i) Proportional tax.

This is where the tax rate is constant for all tax payers irrespective of the level of income. For example 10 percent as tax on the tax payer's income

(ii) Progressive tax.

This is where the tax rate increases as the tax payer's income increases. That is, the more income one earns, the more percentage of it is paid as tax.

Effect of a progressive tax

- (i) **Redistribution of income:** Shifts resources from the wealthy to the poor through government spending on welfare, healthcare, and education. Helps reduce income inequality.
- (ii) **Fairness (Equity):** Ensures that those with greater ability to pay contribute more. Protects low-income earners from excessive tax burdens.
- (iii) **Encourages social welfare:** Revenue collected from the rich can be used to fund social programs that benefit the poor.
- (iv) **Reduction in consumption inequality:** By taxing higher incomes more, it reduces the gap in consumption levels between rich and poor households.
- (v) **Economic stabilization:** Progressive taxes act as automatic stabilizers; that is, during booms, higher incomes are taxed more, reducing overheating and during recessions, lower incomes face lighter taxes, supporting demand.
- (vi) **Possible disincentives:** Very high progressive rates may discourage work, savings, and investment among high earners and could lead to tax avoidance or evasion if rates are perceived as unfair.
- (vii) **High tax revenue is realized by the government.** This is because it minimizes the chances of tax evasion.

Example (Uganda Context)

- (i) Uganda applies **progressive income tax rates:** low-income earners pay little or no tax, while higher earners face higher rates.
- (ii) This helps redistribute income, but challenges like **tax evasion, informality, and corruption** reduce effectiveness.

- (iii) Progressive taxation supports funding for **education, healthcare, and infrastructure**, benefiting lower-income groups.

(iii) Regressive tax.

A **regressive tax** is a system where the **tax burden falls more heavily on low-income earners** than on high-income earners. In this case, the tax rate decreases as income increases, meaning poorer individuals pay a larger proportion of their income compared to the rich.

Effects of a regressive tax

- (i) **Increased inequality:** Poorer households spend a larger share of their income on taxed goods, widening the gap between rich and poor.
- (ii) **Reduced purchasing power of the poor:** Low-income earners have less disposable income for essentials like food, healthcare, and education.
- (iii) **Stable government revenue:** Since everyone consumes basic goods, regressive taxes provide a steady and predictable income stream for the government.
- (iv) **Encourages consumption reduction:** Higher taxes on goods like alcohol, cigarettes, or fuel may reduce consumption, but this disproportionately affects the poor.
- (v) **Inflationary pressures:** Indirect taxes raise the prices of goods and services, contributing to higher living costs.
- (vi) **Possible social unrest:** When regressive taxes affect essentials (like fuel or mobile money), they can trigger protests and dissatisfaction among citizens.
- (vii) **It encourages hard work** for the low income earners. This is because they have to work hard in order to pay taxes

Example (Uganda Context)

- (i) **VAT (18%):** Applied equally to all consumers, but poorer households spend more of their income on taxed essentials.
- (ii) **Excise duty on fuel:** Raises transport costs, which in turn increases food prices, hitting low-income earners hardest.
- (iii) **Mobile money tax:** Disproportionately affects rural and low-income Ugandans who rely on mobile money for transactions.

(iv) Digressive tax.

A **digressive tax** is a type of taxation system where the **rate of tax increases up to a certain level of income**, but beyond that level, the rate remains constant. In other words, it is partly progressive and partly proportional.

Classification of taxes according to Tax incidence

In this case, we have direct taxes and indirect taxes.

(i) Direct Taxes

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These are taxes imposed on income and properties of individuals and companies where by the impact and incidence of the tax cannot be shifted to a mother party.

Examples of direct taxes

- (i) **Income tax:** Levied on the earnings of individuals. **It is progressive** in nature: higher earners pay a larger percentage of their income.
- (ii) **Pay-As-You-Earn (PAYE):** A form of income tax deducted directly from employees' salaries. Ensures convenience and certainty in collection.
- (iii) **Corporate (Company) tax:** Charged on the net or gross profits of companies. Usually a fixed percentage of profits.
- (iv) **Local Service Tax** is an annual tax imposed on individuals in gainful employment, self-employed professionals, and business owners within local government jurisdictions in Uganda.
- (v) **Property tax Rental income::** Levied on the value of land, buildings, or other immovable assets. Helps local governments fund infrastructure and services.
- (vi) **Wealth tax:** Imposed on accumulated wealth or assets of individuals. Aimed at reducing inequality.
- (vii) **Capital gains tax:** Charged on profits from the sale of assets like land, shares, or property.
- (viii) **Poll tax:** A fixed tax levied on individuals regardless of income or property. Rare today but historically significant.
- (ix) **Sur tax.** This is the tax imposed on very high incomes exceeding certain limits asset by the tax authorities in a given country. It is aimed at reducing income inequalities among the tax payers.
- (x) **Death (Estate) duty.** This is the tax levied on the property of deceased person. It is based on the principle that a person cannot command property rights beyond the term of his/her life. Therefore, society should take part of his or her property in form of taxes.
- (xi) **Inheritance tax (duty).** This is the tax imposed on property or wealth inherited by a certain person.
- (xii) **Land tax.** This is the tax imposed basing on the ownership of land. It is aimed at breaking land monopoly and improving on land tenure system.
- (xiii) **Gift tax.** This is the tax imposed on gifts. The principle on which the tax is levied is that the receiver of the gift has not earned it through hard work.
- (xiv) **Super profit tax.** This is the tax imposed on profits of the company exceeding certain limits as determined by the tax authorities.

(xv)

(xvi) Advantages (Merits) of Direct taxes

- (i) **Equity (Fairness):** Direct taxes are based on the ability to pay. Progressive rates ensure that wealthier individuals contribute more, reducing inequality.
- (ii) **Certainty:** Taxpayers know exactly how much, when, and how to pay. This avoids arbitrary or unpredictable taxation.
- (iii) **Economy (Low cost of collection):** Direct taxes like PAYE are deducted at source, making collection cheap and efficient.
- (iv) **Convenience:** Taxes such as PAYE are collected when salaries are paid, making it easy for taxpayers.
- (v) **Elasticity (Flexibility):** Direct taxes can be adjusted with changes in income levels, ensuring revenue grows with the economy.

- (vi) **Discourages harmful consumption:** High direct taxes on luxury goods or wealth discourage excessive spending and promote savings.
- (vii) **Promotes civic responsibility:** Since taxpayers feel the burden directly, they demand accountability from government, strengthening democracy.
- (viii) **They are easy and simple to understand and administer.** Therefore they fulfill the principle of simplicity.
- (ix) **They are elastic.** A small increase in the tax rate yields much tax revenue. They also change with the changes in tax base.
- (x) **Their tax revenue is easy to estimate** because they are fixed for a given period. This facilitates proper budgeting and planning.
- (xi) **They can be used to control inflation.** This is done by taxing heavily the disposable incomes of the tax payers so as to reduce aggregate demand.

Disadvantages (Demerits) of Direct taxes

- (i) **Discourages work and investment:** High income tax rates may reduce motivation to work harder or invest more, as extra earnings are heavily taxed.
- (ii) **Encourages tax evasion and avoidance:** Because the burden is felt directly, individuals and businesses often seek loopholes or underreport income.
- (iii) **Inconvenience to taxpayers:** Filing returns and complying with tax laws can be complex and time-consuming. Requires proper record-keeping, which is difficult for small businesses and individuals.
- (iv) **Possibility of inequity:** If poorly designed, direct taxes may unfairly burden middle-income earners while the wealthy exploit exemptions.
- (v) **Reduced savings and capital formation:** Heavy taxation on income and profits reduces disposable income, lowering savings and investment in the economy.
- (vi) **Political interference:** Tax rates may be manipulated for political reasons, leading to unfair treatment of certain groups.
- (vii) **Administrative challenges:** Requires strong institutions and skilled personnel to assess and collect taxes effectively. In developing countries, weak tax administration leads to inefficiency and corruption.
- (viii) It is **difficult to determine the tax payer's taxable capacity** under direct taxes. This is because individuals have different sources of income which may not be known by the tax administrators.
- (ix) **They are associated with a high degree of corruption, embezzlement and sectarianism during tax assessment and collection.**

Example (Uganda Context)

- (i) Many Ugandans in the informal sector avoid direct taxes, leaving the burden on salaried workers.
- (ii) Complex tax procedures discourage compliance, especially among small businesses.
- (iii) High corporate taxes sometimes discourage foreign investors, pushing them toward countries with lower tax rates.

(ii) Indirect taxes (Outlays/ Expenditure taxes)

Indirect taxes are taxes imposed on commodities where the tax incidence and tax burden can be shifted by the tax payer to other parties for example by increasing commodity prices.

Examples of indirect taxes

- (i) **Value Added Tax (VAT):** A tax on goods and services at each stage of production and distribution. In Uganda, VAT is charged at 18% on most goods and services.
- (ii) **Excise duty:** Levied on specific goods like alcohol, cigarettes, fuel, and soft drinks. Used both to raise revenue and discourage harmful consumption.
- (iii) **Customs duty:** Taxes on imports and exports. Import duty protects local industries, while export duty raises revenue and ensures local supply.
- (iv) **Sales tax:** Charged at the point of sale of goods and services. Similar to VAT but applied only once at the final sale.
- (v) **Expenditure tax:** Levied on spending for certain goods or services, e.g., luxury items.
- (vi) **Service tax:** Applied to services such as telecommunications, banking, or insurance.
- (vii) **Turn over tax.** This is the tax levied on the total sales of the business at each stage of transaction of the commodity.
- (viii) **Sumptuary tax.** This is a special tax levied on consumption of certain commodities which may be dangerous to human health. For example a tax on cigarettes, alcoholic drinks etc.
- (ix) **Octori tax.** This is tax levied on commodities in transit from one country to another through the territory of another country. For example commodities from Japan through Kenya to Uganda are charged octori tax by the Kenyan government.

Example (Uganda Context)

- (i) **VAT (18%):** Applied to most goods and services.
- (ii) **Excise duty:** Charged on beer, soft drinks, cigarettes, and fuel.
- (iii) **Customs duty:** Imposed on imported goods to protect Ugandan industries.
- (iv) **Mobile money levy:** A form of indirect tax on financial transactions, affecting everyday users.

Advantages (Merits) of VAT

- (i) **Broad-based revenue generation:** VAT is charged at multiple stages of production and distribution, covering a wide range of goods and services. This ensures governments collect significant and reliable revenue.
- (ii) **Difficult to evade:** Since VAT is collected at each stage of the supply chain, it is harder for taxpayers to avoid compared to direct taxes.
- (iii) **Reduces corruption:** Payments are often made through banks or electronic systems, limiting opportunities for bribery and under-collection.
- (iv) **Economical in administration:** VAT is relatively simple to administer and cost-effective for tax authorities, lowering compliance and collection costs.
- (v) **Promotes efficiency in business management:** Firms must maintain proper records and bookkeeping to comply with VAT, which improves accountability and management practices.
- (vi) **Distributes tax burden fairly:** Since VAT is paid at different stages of production, the burden is shared among producers, distributors, and consumers.

- (vii) **Avoids double taxation:** VAT receipts at each stage ensure that tax is only charged on the value added, not on the entire product repeatedly.
- (viii) **Encourages savings and investment:** Unlike income tax, VAT does not penalize savings; it only taxes consumption, which can promote investment.
- (ix) **It increases employment opportunities since business units employ accountants for book keeping** while the URA (Uganda Revenue authority) employs personnel in tax administration.
- (x) **It minimizes discrimination in taxation** basing on income levels of the tax payers.

Example (Uganda Context)

- (i) Uganda applies **VAT at 18%** on most goods and services.
- (ii) It is a major source of government revenue, contributing significantly to the national budget.
- (iii) The Uganda Revenue Authority (URA) uses electronic systems to collect VAT, reducing corruption and improving compliance.

Disadvantages (Demerits) of VAT

- (i) **Regressive nature:** VAT affects all consumers equally, but poorer households spend a larger share of their income on taxed essentials, making it regressive.
- (ii) **Inflationary impact:** VAT increases the prices of goods and services, raising the cost of living. This can trigger inflationary pressures, especially when applied to basic commodities.
- (iii) **Complexity in administration:** Requires strict record-keeping and compliance at every stage of production. Small businesses often struggle with VAT paperwork and reporting.
- (iv) **Encourages evasion and fraud:** Businesses may underreport sales or falsify invoices to avoid paying VAT. This reduces government revenue and undermines fairness.
- (v) **Burden on consumers:** The final burden of VAT falls on consumers, who pay higher prices for goods and services.
- (vi) **Discourages consumption:** Higher VAT rates can reduce demand for goods and services, slowing economic growth.
- (vii) **Unequal impact across sectors:** Essential goods (like food and medicine) may be taxed the same as luxury goods, disproportionately affecting the poor.
- (viii) **It discourages production.** This is because it increases the costs of production.
- (ix) **High rates of VAT may cause unemployment** as it discourages production and investment.

Example (Uganda Context)

- (i) Uganda's **VAT rate of 18%** applies to most goods and services.
- (ii) Poor households spend a large share of their income on food and transport, so VAT raises their living costs more than for wealthy households.
- (iii) Small traders often complain about the **complexity of VAT compliance**, leading to evasion and disputes with the Uganda Revenue Authority (URA).

Advantages (Merits) of Indirect taxes

- (iv) **Convenience in payment:** Paid automatically when purchasing goods or services. Taxpayers often don't feel the burden directly compared to direct taxes.

- (v) **Wide coverage:** Levied on a broad range of goods and services, ensuring a large tax base.
- (vi) **Difficult to evade:** Embedded in the price of goods, making it harder for individuals to avoid payment.
- (vii) **Stable and regular revenue:** Since everyone consumes goods and services, governments collect steady income.
- (viii) **Encourages savings and investment:** Indirect taxes target consumption, not income, leaving savings and investments untaxed.
- (ix) **Flexibility (Elasticity):** Rates can be adjusted easily to meet government revenue needs. Example: raising excise duty on fuel during budget shortfalls.
- (x) **Discourages harmful consumption:** Higher taxes on alcohol, cigarettes, and fuel reduce excessive or harmful use.
- (xi) **Equitable burden sharing:** The tax burden is spread across all consumers, not concentrated on a few individuals.
- (xii) **Promotes efficiency in administration:** Easier to collect compared to direct taxes, especially in countries with large informal sectors.
- (xiii) **They are used to protect domestic infant industries:** by charging high import duties. This promotes the creation of employment opportunities in the country.
- (xiv) **They are more economical:** This is because they involve low costs in assessment, administration and collection as compared to direct taxes.
- (xv)

Example (Uganda Context)

- (i) **VAT (18%):** Provides a major share of Uganda's revenue, collected on most goods and services.
- (ii) **Excise duty:** Applied on alcohol, cigarettes, and fuel, discouraging harmful consumption while raising revenue.
- (iii) **Customs duty:** Protects local industries and generates income from imports.
- (iv) **Mobile money levy:** Ensures taxation of financial transactions in Uganda's large informal sector.

Disadvantages (Demerits) of Indirect taxes

- (i) **Regressive nature:** Indirect taxes affect all consumers equally, but poorer households spend a larger share of their income on taxed goods, making them regressive.
- (ii) **Inflationary impact:** They raise the prices of goods and services, increasing the cost of living and sometimes fueling inflation.
- (iii) **Unequal burden:** Essentials like food, fuel, and medicine may be taxed at the same rate as luxury goods, disproportionately hurting low-income earners.
- (iv) **Discourages consumption:** Higher taxes reduce demand for goods and services, which can slow economic growth.
- (v) **Encourages smuggling and black markets:** High customs duties or excise taxes may lead to illegal trade as people seek cheaper alternatives.
- (vi) **Administrative challenges:** Requires strict monitoring to prevent evasion, fraud, and underreporting, which can be difficult in countries with weak institutions.
- (vii) **Hidden burden:** Consumers often don't realize how much tax they are paying since it is embedded in prices, reducing transparency.

Example (Uganda Context)

- (i) **Uganda's VAT (18%)** raises the cost of basic goods, disproportionately affecting poor households.
- (ii) **Excise duty on fuel** increases transport costs, which in turn raises food prices.
- (iii) **Mobile money levy** has been criticized for hurting rural and low-income Ugandans who rely on mobile money for transactions.
- (iv) High **import duties** sometimes encourage smuggling across borders with Kenya, Tanzania, and South Sudan.

Why Uganda (LDC's) rely (depend) more on Indirect taxes than on Direct taxes

Uganda, like many **Less Developed Countries (LDCs)**, depends heavily on **indirect taxes** (VAT, excise duty, customs duty) rather than **direct taxes** (income tax, corporate tax). This reliance is shaped by structural, economic, and administrative realities.

Reasons for Reliance on Indirect Taxes

- (i) **Large informal sector:** Most Ugandans work in subsistence farming or informal businesses that are hard to track. Direct taxes (like income tax) are difficult to collect from these groups.
- (ii) **Low income levels:** A significant portion of the population earns below taxable thresholds. Direct taxes yield little revenue because many citizens cannot afford them.
- (iii) **Ease of collection:** Indirect taxes are embedded in goods and services, making them easier to administer. Governments collect them at points of sale, imports, or production.
- (iv) **Stable and predictable revenue:** Since everyone consumes goods and services, indirect taxes provide a steady income stream. Even the poorest contribute through consumption of essentials.
- (v) **Weak tax administration:** Limited institutional capacity makes it hard to enforce direct taxes. Indirect taxes require less monitoring and fewer resources to collect.
- (vi) **Political acceptability:** Indirect taxes are less visible to taxpayers compared to direct taxes. Governments avoid resistance by embedding taxes in prices rather than demanding direct payments.
- (vii) **Encourages compliance:** Businesses and consumers pay automatically when buying goods, reducing deliberate evasion.
- (viii) **Indirect taxes are used to protect the domestic industries** and to correct the balance of payment problems which is not possible with direct taxes.
- (ix) **Uganda greatly depends on international trade.** Therefore it is likely to raise more revenue from indirect taxes than direct taxes in form of import and export duties which form a big percentage of the tax revenue.

Uganda Context

- (i) Uganda Revenue Authority (URA) collects most of its revenue from **VAT (18%), excise duty on fuel, alcohol, and cigarettes**, and **customs duty on imports**.
- (ii) Direct taxes like income tax and corporate tax contribute less because:

- Many Ugandans are in the informal sector.
- Salaried workers are a small fraction of the population.
- Poverty levels keep most citizens below taxable thresholds.

Problems faced by the Tax authority in Uganda (LDC's)

- (i) **Narrow tax base:** High poverty levels mean many citizens earn below taxable thresholds. A large share of the population works in subsistence farming and informal trade, which are difficult to tax.
- (ii) **High tax evasion and avoidance:** Loopholes in the tax system allow individuals and businesses to dodge taxes. Weak enforcement and corruption among officials worsen compliance.
- (iii) **Weak administrative capacity:** Inadequate skilled manpower and lack of modern technology hinder effective tax collection. Taxpayer compliance burden is high due to complex procedures.
- (iv) **Corruption and misuse of revenue:** Perceived misuse of tax revenue and unfairness erode public trust. Citizens resist broadening the tax base when they feel funds are mismanaged.
- (v) **Inflationary pressures:** High inflation reduces disposable incomes, making taxpayers less willing or able to pay taxes.
- (vi) **Low literacy and awareness:** Many taxpayers lack knowledge of tax laws and procedures, leading to non-compliance.
- (vii) **Political interference:** Tax exemptions and holidays are often granted for political reasons, narrowing the tax base further.
- (viii) **Dependence on indirect taxes:** Heavy reliance on VAT and excise duty burdens consumers, especially the poor, and sparks resistance.
- (ix) **It is difficult to determine the taxable capacity for the tax payers.** It is difficult to determine how much tax is to be paid by each tax payer and yet remain with enough disposable income which is enough to enable him/her to enjoy the desired standards of living.
- (x) **Inadequate facilities** such as computers and other materials required for tax collection and administration. This makes the tax assessment process very difficult.

Uganda Context

- Only about **1 million Ugandans actively pay taxes**, despite a population of over 45 million.
- Uganda's tax-to-GDP ratio is around **11%**, far below the African average of 16% and regional peers like Kenya (15.3%) and Rwanda (16.9%).
- The Uganda Revenue Authority (URA) struggles with **limited resources, corruption, and weak enforcement**, making it difficult to expand the tax base.

Ways of improving Tax revenue and Tax collection in Uganda (LDC'S)

- (i) **Broadening the tax base:** Bring more people and businesses into the tax net, especially the informal sector. Reduce excessive exemptions and tax holidays that shrink revenue.
- (ii) **Strengthening tax administration:** Invest in modern technology (digital tax systems, e-filing, mobile payments). Train and expand skilled personnel in the Uganda Revenue Authority (URA).
- (iii) **Reducing corruption:** Enforce strict accountability measures for tax officials. Use automated systems to minimize human contact and bribery opportunities.

- (iv) **Enhancing taxpayer education:** Increase awareness about tax laws, obligations, and benefits. Simplify procedures to encourage compliance among small businesses.
- (v) **Promoting formalization of businesses:** Provide incentives for informal enterprises to register and pay taxes. Link tax compliance to access to credit, government contracts, and licenses.
- (vi) **Improving enforcement:** Strengthen penalties for evasion and avoidance. Use audits and monitoring systems to detect fraud.
- (vii) **Diversifying tax sources:** Expand property taxes, capital gains taxes, and environmental levies. Reduce over-reliance on VAT and excise duty.
- (viii) **Regional cooperation:** Work with East African Community (EAC) partners to harmonize tax policies. Reduce smuggling and cross-border tax evasion.
- (ix) **Ensuring political stability and security in the country.** This is done by promoting democratic governance in the country. In addition, peace talks with the rebels can be emphasized as a way creating peace in the country so as to promote investment hence widening the tax base.
- (x) **There is need to expand the industrial sector.** This is because industries have the potential to increase tax revenue as compared to other sectors like agriculture.

Uganda Context

- (i) Uganda's tax-to-GDP ratio is about **11%**, below the African average of 16%.
- (ii) Heavy reliance on **indirect taxes (VAT, excise duty, customs duty)** burdens consumers.
- (iii) Improving **direct tax collection** from salaried workers, corporations, and property owners would balance the system.
- (iv) Digital initiatives like **URA's e-tax system** and mobile money integration are steps toward modernization.

Taxation financing versus debt financing

Taxation financing: This is where government expenditure is fulfilled by using government tax revenue.

Debt financing: This is where government expenditure is fulfilled by using borrowed funds got from internal or external sources.

Deficit financing: This refers to the excess of government expenditure over public government revenue.

Methods (ways) of Deficit financing (Methods of financing a Deficit budget)

- (i) **Borrowing from the public:** Government issues bonds, treasury bills, or securities to raise funds from citizens and institutions. Example: Uganda issues Treasury Bills through the Bank of Uganda.
- (ii) **Borrowing from banks:** Government borrows directly from commercial banks or the central bank. This increases money supply but may cause inflation.
- (iii) **External borrowing:** Loans from foreign governments, international organizations (IMF, World Bank), or external markets. Provides foreign exchange but increases external debt burden.
- (iv) **Printing of currency:** Central bank prints new money to cover the deficit. Quick solution but highly inflationary if overused.

- (v) **Use of reserves:** Government may use foreign exchange reserves or accumulated savings to finance deficits. Limited option in LDCs with small reserves.
- (vi) **Taxation measures:** Increasing existing taxes or introducing new ones to raise revenue. May be unpopular and burdensome for citizens.
- (vii) **Public-private partnerships (PPPs):** Government collaborates with private investors to finance infrastructure and services, reducing direct budget pressure.

Uganda Context

- (i) Uganda often relies on **external borrowing** from the IMF and World Bank to cover deficits.
- (ii) **Treasury Bills and Bonds** are issued domestically to raise funds.
- (iii) In times of crisis, the **Bank of Uganda** has resorted to deficit financing through monetary expansion (printing money), though this risks inflation.
- (iv) Heavy reliance on **foreign aid and loans** makes Uganda vulnerable to debt sustainability issues.

Advantages (Merits) of Debt financing over Taxation financing

- (i) **Avoids immediate burden on citizens:** Borrowing allows governments to raise funds without increasing taxes, which could reduce disposable income and spark public resistance.
- (ii) **Encourages investment and consumption:** By not raising taxes, households and businesses retain more income to spend and invest, stimulating economic growth.
- (iii) **Flexibility in timing:** Debt can be repaid gradually over time, while taxation imposes an immediate burden. This helps governments manage short-term deficits without hurting current economic activity.
- (iv) **Supports development projects:** Borrowed funds can be directed toward infrastructure, education, and health projects that generate long-term growth. Taxation alone may not provide sufficient capital for large-scale projects.
- (v) **Political acceptability:** Raising taxes is often unpopular and resisted by citizens. Debt financing avoids direct confrontation with taxpayers.
- (vi) **Access to foreign capital:** External borrowing provides foreign exchange needed for imports and development projects. Taxation cannot generate foreign currency directly.
- (vii) **Spreads burden across generations:** Debt repayment can be shared by future taxpayers who also benefit from today's investments. Taxation places the entire burden on the current generation.
- (viii) **Debt financing has a wider source of rising government revenue** as compared to taxation. Unlike taxation which is limited to one country in mobilizing and rising financial resources, borrowing enables the country to raise revenue from internal and external sources
- (ix) Unlike taxation, borrowing is **associated with a lower degree of corruption and embezzlement** of government revenue. There is a high degree of corruption during tax assessments, administration collection which lowers the revenue under taxation financing.

Uganda Context

- (i) Uganda frequently relies on **external borrowing** from the IMF, World Bank, and international markets to finance deficits.
- (ii) This avoids heavy taxation on a population where many earn below taxable thresholds.
- (iii) Borrowed funds have been used for **infrastructure projects** like roads, dams, and energy, which taxation alone could not finance.

Demerits of Debt financing (Borrowing)

- (i) **Debt burden:** Borrowing increases national debt, which must be repaid with interest. This can strain future budgets and reduce funds for development.
- (ii) **Risk of debt trap:** Excessive borrowing, especially external loans, can lead to dependency on creditors. Countries may fall into a cycle of borrowing to repay old debts.
- (iii) **High interest payments:** Servicing debt consumes a large share of government revenue. This reduces funds available for social services like health and education.
- (iv) **Inflationary pressures:** Borrowing from the central bank (printing money) increases money supply, which can fuel inflation.
- (v) **Crowding out effect:** Heavy government borrowing from local banks reduces funds available for private businesses, discouraging investment.
- (vi) **Loss of sovereignty:** External borrowing often comes with conditions from lenders (IMF, World Bank). This limits a country's freedom to set independent economic policies.
- (vii) **Future tax burden:** Debt repayment eventually requires higher taxes, shifting the burden to future generations.
- (viii) **Exchange rate risks:** External debt in foreign currency exposes countries to depreciation risks, making repayment more expensive.
- (ix) **It leads to inflation in case of external borrowing.** This is because it increases money supply and aggregate demand in the economy hence demand pull inflation.
- (x) **Borrowing increases income inequalities among people** .This is true especially when the borrowed funds are used to develop one region or misused through corruption to benefit a few individuals
- (xi) **It limits capital accumulation and investment.** This can occur when the borrowed funds are used to service the debts contracted in the past or to finance the recurrent expenditure of the government.
- (xii) **It does not promote a sense of civic responsibility among the citizens towards nation building.** This is because the citizens do not contribute to the government revenue and therefore they are not concerned how the government allocates the borrowed funds.

Uganda Context

- (i) Uganda's public debt has risen significantly, with external borrowing from IMF and World Bank financing infrastructure projects.

- (ii) Rising **debt servicing costs** consume a large share of the national budget, limiting funds for health, education, and poverty reduction.
- (iii) Heavy reliance on external loans risks pushing Uganda into a **debt trap**, especially if *economic growth slows*.

Revision exercise 1

Section A questions

- 1 (a) Distinguish between public finance and private finance
(b) Give any two problems faced in effecting public expenditure
- 2 (a) Distinguish between recurrent expenditure and capital expenditure
(b) Give two factors which influence public expenditure
(c) Give four ways of reducing government expenditure
- 3 (a) What is meant by public revenue
(b) Give any four non tax sources of government revenue.
- 4 Give four objectives of the fiscal policy
- 5 (a) Distinguish between tax incidence and tax impact
(b) With the help of the graph illustrate the tax incidence when demand is inelastic
- 6 (a) What is fiscal policy?
(b) State any three instruments of fiscal policy
- 7 (a) Differentiate between tax evasion and tax avoidance
(b) Mention any two causes of tax evasion in your country
- 8 (a) Distinguish between a proportional tax and a regressive tax
(b) Mention two effects of a regressive tax
- 9 (a) Distinguish between a progressive tax and digressive tax
(b) State any two merits of a progressive tax
- 10 (a) Distinguish between octroi tax and sumptuary tax
(b) Mention two ways of widening the tax base in your country
- 11 (a) Distinguish between tax base and taxable capacity
(b) Give two causes of low taxable capacity in your country
- 12 (a) What is meant by 'tax structure' of a country?
(b) Mention three salient features of Uganda's tax structure.
- 13(a) What is meant by VAT
(b) Given that Value Added Tax (V.A.T) is levied at a rate of 18% in Uganda, a registered supplier buys raw materials at Ug. shs. 200,000 and sell the final output at Ug. shs 300,000, Calculate the amount of V.A.T. payable to Uganda Revenue Authority (U.R.A.) by the registered supplier
(c) What are the advantages and disadvantages of VAT.?
- 14 (a) Distinguish between recurrent expenditure and development expenditure
(b) Give two examples of recurrent expenditure incurred by the government of your country
- 15 (a) Define the term fiscal policy

- (b) Outline three instruments of the fiscal policy in your country.
- 16 (a) What is meant by deficit financing?
(b) Outline three methods of financing a deficit
- 17 Distinguish between the following terms;
(a) Forward shifting of the tax and back ward shifting of the tax.
(b) Money tax burden and real tax burden.

Section B questions

- 1 (a) Distinguish between tax base and tax structure
(b) What are the implications of levying indirect taxes in an economy?
- 2 (a) Account for the low tax revenue in low developing countries
(b) Suggest the ways of improving tax collection in your country
- 3 (a) Explain the principles (cannons) of taxation
(b) Explain why your country prefers indirect taxes to direct taxes
- 4 (a) Distinguish between Direct taxes and expenditure taxes
(b) Why does the government impose taxes in the economy?
- 5 (a) Why is it necessary to levy different forms of taxes in an economy?
(b) Examine the role of taxation in the economic development process of your country
- 6 (a) Distinguish between debt financing and taxation financing
(b) Explain why the government of your country prefers to finance its expenditure by borrowing instead of using tax revenue

The government budget/ national budget

The budget is a financial statement showing the estimated (planned/anticipated) government revenue and the estimated government expenditure in a given financial year.

Types of budgets

(a) Balanced budget

This is a budget where the planned government revenue is equal to the planned government expenditure in a given financial year.

(b) Unbalanced budget

This is a budget where the planned government revenue is not equal to the planned government expenditure in a given financial year.

Note. The unbalanced budget may either be surplus budget or deficit budget.

(c) Surplus budget

This is a budget where the planned government revenue exceeds the planned government expenditure in a given financial year.

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Reasons as to why the government may deliberately plan for a surplus budget

- (i) **Control inflation:** By reducing expenditure and collecting more revenue, the government withdraws excess money from circulation. This helps stabilize prices and prevent overheating of the economy.
- (ii) **Debt repayment:** Surplus revenue can be used to pay off existing public debt. This reduces interest burdens and strengthens financial stability.
- (iii) **Build reserves:** Governments may save surplus funds to create financial buffers for future emergencies (e.g., pandemics, natural disasters).
- (iv) **Strengthen currency:** A surplus budget improves investor confidence and can stabilize or strengthen the national currency.
- (v) **Promote economic stability:** Surpluses reassure investors and international lenders that the country is fiscally responsible. This attracts foreign investment and aid.
- (vi) **Finance future development:** Surplus funds can be allocated to capital projects in subsequent years without relying on borrowing.
- (vii) **Reduce dependence on external aid:** By generating surplus revenue, governments reduce reliance on foreign loans and donor funding.
- (viii) **Encourage savings culture:** A surplus budget signals fiscal discipline, encouraging citizens and businesses to adopt similar saving habits.

Uganda (LDC) Context

- (i) Uganda may plan for a surplus budget to **control inflation**, especially when donor funds or external loans increase money supply.
- (ii) Surplus revenue can be used to **repay external debt** owed to IMF and World Bank.
- (iii) Building **foreign exchange reserves** helps Uganda stabilize its currency against shocks in global markets.

Negative effects of a Surplus budget

- (i) **Slows economic growth:** Reduced government spending means less investment in infrastructure, education, and health. This can weaken long-term development.
- (ii) **Unemployment rise:** Cutting expenditure reduces demand for goods and services, leading to job losses in both public and private sectors.
- (iii) **Underutilization of resources:** Surplus budgets may leave productive resources idle, especially labor and capital, instead of being used for development.
- (iv) **Public dissatisfaction:** Citizens may feel overtaxed if revenue collection is high but government spending is low. This can reduce trust in government.
- (v) **Reduced social welfare:** Essential services like healthcare, education, and subsidies may suffer from underfunding.
- (vi) **Discourages investment:** Businesses may face reduced demand due to lower government spending, discouraging private investment.
- (vii) **Political backlash:** Surplus budgets can be unpopular if citizens perceive the government as hoarding money instead of addressing pressing needs.

Uganda (LDC) Context

- (i) If Uganda runs a surplus budget, it may **limit spending on poverty reduction programs**, worsening inequality.
- (ii) Reduced investment in infrastructure could slow economic growth and discourage foreign investors.
- (iii) Citizens may resent high taxes when they see little improvement in public services.

(d) Deficit budget

This is the budget where the planned government expenditure exceeds the planned government revenue in a given financial year.

Reasons as to why the government may deliberately plan for a deficit budget

OR. Why may the government under take Deficit financing?

A **deficit budget** occurs when government expenditure exceeds revenue. While it may seem undesirable, governments sometimes deliberately plan for a deficit budget to stimulate growth, support development, or address economic challenges.

- (i) **Stimulate economic growth:** Increased government spending boosts demand for goods and services. This encourages production, investment, and job creation.
- (ii) **Finance development projects:** Deficit budgets allow governments to invest in infrastructure, education, and health. These projects may not be possible with limited tax revenue.
- (iii) **Reduce unemployment:** Higher spending creates jobs directly (public works) and indirectly (private sector demand).
- (iv) **Support social welfare:** Governments may run deficits to fund subsidies, healthcare, and poverty reduction programs.
- (v) **Counter economic recession:** Deficit spending injects money into the economy, helping to revive demand during downturns.
- (vi) **Encourage industrialization:** Borrowed funds can be directed toward industries and agriculture to accelerate modernization.
- (vii) **Military and security needs:** In times of conflict or insecurity, governments may deliberately spend beyond revenue to strengthen defense.
- (viii) **Political reasons:** Leaders may plan deficit budgets to gain popularity by funding visible projects and subsidies.
- (ix) To **reduce the tax burden** on the tax payers especially in situations where taxable capacity is too low due to high levels of poverty

Uganda (LDC) Context

- (x) Uganda often runs deficit budgets to **finance infrastructure projects** like roads, dams, and energy plants.

- (xi) Deficit spending supports **poverty reduction programs** and social services in health and education.
- (xii) During economic shocks (e.g., COVID-19), Uganda used deficit financing to **stimulate demand and protect vulnerable groups**.

Why may the planned budget differ from the Actual budget OR. Why is it difficult to achieve a balanced budget?

A **planned budget** is the government's estimate of revenue and expenditure for a given period, while the **actual budget** reflects what is truly collected and spent. In practice, these two often differ due to economic, political, and administrative factors.

Reasons for Differences

- (i) **Revenue shortfalls:** Tax collections may fall below projections due to evasion, weak administration, or slower economic growth.
- (ii) **Unexpected expenditures:** Emergencies such as natural disasters, pandemics, or conflicts force governments to spend more than planned.
- (iii) **Inflation and price changes:** Rising costs of goods and services increase government spending beyond initial estimates.
- (iv) **Foreign exchange fluctuations:** Changes in currency value affect the cost of imports, debt servicing, and foreign-funded projects.
- (v) **Political decisions:** Governments may introduce new subsidies, tax cuts, or programs for political reasons, altering the budget.
- (vi) **Donor funding variations:** In LDCs like Uganda, reliance on foreign aid means delays or reductions in donor support can affect actual revenue.
- (vii) **Implementation challenges:** Weak institutions, corruption, and poor planning lead to inefficiencies in executing the budget.
- (viii) **Economic shocks:** Global recessions, commodity price drops, or regional instability reduce revenue and increase expenditure unexpectedly.
- (ix) **Improvement in the economic performance** which may help the government to raise more revenue than what is expected hence a surplus budget.
- (x) **Existence political instabilities and insecurity** in the country which may force the government to increase expenditure so as to facilitate and maintain the security of the economy.

Uganda (LDC) Context

- (i) Uganda's planned budgets often assume **high tax revenue**, but actual collections fall short due to a large informal sector and evasion.
- (ii) **Unexpected expenditures** like COVID-19 relief and security operations have widened gaps between planned and actual budgets.
- (iii) **Donor funding delays** and **exchange rate depreciation** also distort budget outcomes.

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Objectives of the Budget as an instrument of Social and Economic development

A **budget** is not just a financial plan; it is a powerful tool governments use to guide **social and economic development**. In countries like Uganda and other **Less Developed Countries (LDCs)**, the budget plays a central role in shaping growth, reducing poverty, and stabilizing the economy.

Key Objectives

- (i) **Resource allocation:** Directs funds to priority sectors such as health, education, agriculture, and infrastructure. Ensures scarce resources are used efficiently for maximum social benefit.
- (ii) **Economic growth stimulation:** Provides capital for development projects (roads, energy, industry) to expand production and employment.
- (iii) **Reduction of inequalities:** Uses subsidies, welfare programs, and progressive taxation to bridge the gap between rich and poor.
- (iv) **Price stability:** Controls inflation by balancing expenditure and revenue, ensuring stable purchasing power.
- (v) **Employment creation:** Funds public works and industrial projects to absorb labor and reduce unemployment.
- (vi) **Social welfare improvement:** Allocates resources to healthcare, education, housing, and social security for better living standards.
- (vii) **Debt management:** Plans borrowing and repayment to avoid unsustainable debt burdens.
- (viii) **Mobilization of resources:** Expands the tax base and encourages savings and investment to finance development.
- (ix) **Regional balance:** Ensures equitable distribution of resources across regions to reduce disparities.
- (x) **Economic stability:** Acts as a tool for counter-cyclical policies, using surplus or deficit budgets to stabilize the economy.
- (xi) **To discourage the production and consumption of harmful commodities like cigarettes.** This is done by imposing high sumptuary taxes on such commodities
- (xii) **To control monopoly power.** This is done by imposing heavy taxes on the super normal profits earned by the monopolist hence making it possible for other firms also to
- (xiii) **To discourage dumping.** This is done by taxing the dumped commodities heavily so as to raise their prices and discourage their consumption by the local
- (xiv) **To control population growth.** This is done by imposing heavy taxes on people with large families as a way of discouraging child birth.
- (xv) **To reduce income inequalities.** This is done by taxing the rich heavily and subsidizing the poor. The tax revenue received can also be used to provide the people especially the poor with social services. For example free education, medical services

Uganda (LDC) Context

- (i) Uganda's budget prioritizes **infrastructure (roads, energy, ICT)** to stimulate growth.
- (ii) **Social sectors** like education (Universal Primary Education) and health (free maternal care) are funded to improve welfare.
- (iii) The government uses the budget to **reduce poverty**, manage inflation, and attract foreign investment.
- (iv) Regional balance is sought by allocating funds to rural development and agricultural modernization.

The public debt

Public debt refers to the debt contracted by the central government, local authorities and co-operate organizations as a result of borrowing from within and outside the country.

National debt refers to debt contracted only by the central government on behalf of its citizens by borrowing from within or outside the country.

Sources of Public debts

- (i) **Domestic borrowing:** Loans raised within the country through treasury bills, bonds, and securities. Borrowing from commercial banks, insurance companies, pension funds, and individuals.
- (ii) **External borrowing:** Loans from foreign governments, international organizations (IMF, World Bank, African Development Bank), and external markets. Often comes with conditions on economic reforms or repayment schedules.
- (iii) **Central bank financing:** Borrowing directly from the central bank (e.g., Bank of Uganda). May involve printing new money, which risks inflation.
- (iv) **Supplier's credit:** Foreign suppliers provide goods and services on credit, creating external debt obligations.
- (v) **Foreign aid and grants:** Though grants are not repayable, concessional loans (low-interest aid loans) add to public debt.
- (vi) **Public-private partnerships (PPPs):** Government enters into agreements with private investors to finance projects, sometimes involving debt guarantees.
- (vii) **State-owned enterprises borrowing:** Loans taken by government-owned corporations,

Reasons for public debts (Why countries borrow?)

Governments often resort to **public debt** when their expenditures exceed revenues. Borrowing is a common practice worldwide, but it is especially significant in **Less Developed Countries (LDCs)** like Uganda, where tax bases are narrow and development needs are high.

Key Reasons Why Countries Borrow

- (i) **Finance budget deficits:** When government spending exceeds revenue, borrowing bridges the gap.
- (ii) **Fund development projects:** Loans finance infrastructure such as roads, dams, schools, and hospitals that tax revenue alone cannot cover.
- (iii) **Support social services:** Borrowing helps fund healthcare, education, and welfare programs, especially in times of crisis.
- (iv) **Stabilize the economy:** In recessions, governments borrow to inject money into the economy and stimulate demand.
- (v) **Meet emergency needs:** Natural disasters, pandemics, or wars force governments to borrow for relief and recovery.
- (vi) **Service existing debt:** Sometimes countries borrow to refinance or repay old debts, especially when facing liquidity challenges.
- (vii) **Acquire foreign exchange:** External borrowing provides foreign currency needed for imports and international trade.
- (viii) **Military and security expenditure:** Governments borrow to strengthen defense and maintain national security.
- (ix) **Political reasons:** Leaders may borrow to fund popular projects or subsidies to gain political support.

Uganda (LDC) Context

- (i) Uganda borrows heavily from the **IMF, World Bank, and China** to finance infrastructure projects like roads, energy, and dams.
- (ii) During **COVID-19**, Uganda borrowed externally to fund healthcare and economic recovery programs.
- (iii) Rising debt levels show Uganda often borrows to **service existing loans** and cover recurrent expenditure.

Types of Public debts

- (i) **Internal debt:** Borrowed from within the country (citizens, banks, insurance companies, pension funds). Examples: Treasury bills, government bonds.
- (ii) **External debt:** Borrowed from foreign governments, international organizations (IMF, World Bank, AfDB), or external markets. Provides foreign exchange but increases dependency on external creditors.
- (iii) **Short-term debt:** Payable within one year. Usually raised through treasury bills and short-term loans to meet immediate needs.
- (iv) **Medium-term debt:** Payable within 1–10 years. Often used for development projects requiring moderate financing.
- (v) **Long-term debt:** Payable after 10 years or more. Used for large infrastructure projects like dams, highways, and energy plants.

- (vi) **Productive debt (Self-liquidating debt):** Borrowed funds invested in projects that generate income or economic growth (e.g., roads, industries).
- (vii) **Unproductive debt (dead weight):** Borrowed funds used for non-income-generating purposes (e.g., wars, administrative expenses).
- (viii) **Redeemable debt:** Debt that has a fixed repayment schedule and maturity date.
- (ix) **Irredeemable debt:** Debt with no fixed repayment date; government pays interest indefinitely.
- (x) **Voluntary debt:** Citizens willingly buy government securities.
- (xi) **Compulsory debt:** Government forces borrowing through legal measures (rare in modern economies).
- (xii) **Floating (Marketable) debt.** This is a form of unfunded debt contracted by government through the sale of government securities to the public. For example treasury bills and bonds.
- (xiii) **Concessional Loan (Soft loan).** This is a loan extended to the borrower at a very low interest rate with a long redemption period.
- (xiv) **Hard loan.** This is a loan extended to the borrower at a very high interest rate with a short redemption period.

Uganda (LDC) Context

- (i) Uganda's **internal debt** is raised through treasury bills and bonds issued by the Bank of Uganda.
- (ii) **External debt** is borrowed from IMF, World Bank, and China to finance infrastructure projects.
- (iii) Much of Uganda's borrowing is **long-term and productive**, aimed at roads, energy, and dams.
- (iv) However, some borrowing becomes **unproductive** when used for recurrent expenditure or debt servicing.

Public debt Management

Public debt management refers to the strategies and policies governments use to handle borrowing, repayment, and sustainability of debt. Effective management ensures that debt supports development without leading to financial crises.

Objectives of Public debt management

- (i) **Ensure sustainability:** Keep debt levels within manageable limits to avoid a debt crisis.
- (ii) **Minimize borrowing costs:** Secure loans at the lowest possible interest rates and favorable terms.
- (iii) **Maintain macroeconomic stability:** Prevent excessive borrowing that fuels inflation or destabilizes currency.
- (iv) **Support development goals:** Direct borrowed funds to productive investments (infrastructure, education, health) that generate growth.

- (v) **Strengthen investor confidence:** Transparent debt management reassures lenders and attracts foreign investment.

Tools (methods) of Public Debt management

- (i) **Debt restructuring:** Renegotiating repayment terms with creditors to extend maturity, reduce interest rates, or reschedule payments. Helps countries avoid default and manage liquidity crises.
- (ii) **Diversification of borrowing sources:** Balancing between domestic and external borrowing to reduce risks. Prevents overdependence on foreign creditors.
- (iii) **Use of concessional loans:** Prioritizing low-interest, long-term loans from institutions like the IMF, World Bank, and AfDB. Reduces debt servicing costs compared to commercial loans.
- (iv) **Development of domestic debt markets:** Issuing treasury bills and bonds locally to mobilize savings. Strengthens financial markets and reduces reliance on external borrowing.
- (v) **Transparency and accountability:** Publishing debt statistics, audits, and reports to build trust with citizens and investors. Reduces corruption and misuse of borrowed funds.
- (vi) **Debt sustainability analysis (DSA):** Regularly assessing debt levels relative to GDP, exports, and revenue. Ensures borrowing remains within safe limits.
- (vii) **Linking debt to productive projects:** Ensuring borrowed funds finance infrastructure, education, and industry rather than recurrent expenditure. Productive debt generates growth to repay loans.
- (viii) **Refinancing and rollover strategies:** Replacing expensive short-term loans with cheaper long-term debt. Helps smooth repayment schedules and reduce interest burdens.
- (ix) **Debt Redemption.** This refers to the act of repaying back the debt that is both the principle and the interest.
- (x) **Debt Retirement.** This is where the government borrows money to pay the old debt. This works only if the borrowing conditions of the new debt are better than the conditions of the old debt.
- (xi) **Sinking fund.** This is money set aside by the government in the budget with the aim of paying the debt.
- (xii) **Debt Repudiation.** This is where the borrower refuses to honour the debt obligations.

Uganda (LDC) Context

- (i) Uganda's **Ministry of Finance and Bank of Uganda** use **Debt Sustainability Analyses** to monitor risks.
- (ii) The country prioritizes **concessional loans** from IMF and World Bank but also issues **domestic treasury bills and bonds**.
- (iii) Rising debt servicing costs have pushed Uganda to explore **debt restructuring** and **regional cooperation** to manage obligations.

Ways of Clearing (Paying back) the Public debt Internal debt

- (i) **Redemption at maturity:** Repaying debt when treasury bills, bonds, or securities reach their maturity date. Ensures creditors receive their principal plus interest.
- (ii) **Sinking fund method:** Government sets aside funds annually into a special account to gradually repay debt. Reduces repayment burden at maturity.
- (iii) **Conversion of loans:** Replacing high-interest debt with new loans at lower interest rates. Helps reduce debt servicing costs.
- (iv) **Refinancing or rollover:** Issuing new debt to pay off old debt. Extends repayment period and smooths cash flow.
- (v) **Budgetary surplus:** Using surplus revenue (when government collects more than it spends) to repay debt. Requires strong fiscal discipline.
- (vi) **Taxation revenue:** Raising taxes or improving tax collection efficiency to generate funds for repayment.
- (vii) **Monetization of assets:** Selling government-owned enterprises, land, or other assets to raise money for debt clearance.
- (viii) **Voluntary debt cancellation:** Citizens or institutions may voluntarily waive repayment, though rare in practice.
- (ix) **Inflationary repayment:** Repaying debt with money that has lost value due to inflation. Reduces real burden of repayment but can harm creditors.

Uganda (LDC) Context

- (i) Uganda clears internal debt mainly through **redemption at maturity** of treasury bills and bonds issued by the Bank of Uganda.
- (ii) The government uses **budgetary surpluses** and **tax revenue** when available, though deficits often limit this option.
- (iii) **Refinancing** is common, where new securities are issued to pay off maturing debt.
- (iv) Occasionally, Uganda has relied on **asset monetization** (privatization of state enterprises) to reduce debt burdens.

Ways of Clearing (Paying back) the external debt

External debt refers to money borrowed by a government from foreign creditors such as international organizations (IMF, World Bank), foreign governments, or private international lenders. Clearing or repaying this debt is critical for maintaining financial stability and sovereignty.

Methods of Clearing External Debt

- (i) **Export promotion:** Increase exports to earn foreign exchange needed for debt repayment. Diversifying exports reduces reliance on a few commodities.

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- (ii) **Debt servicing from foreign reserves:** Use accumulated foreign exchange reserves to repay loans. Requires strong reserve management.
- (iii) **Debt rescheduling:** Negotiating with creditors to extend repayment periods or reduce interest rates. Provides relief during financial crises.
- (iv) **Debt refinancing:** Taking new loans (often at lower interest rates) to repay old ones. Helps manage liquidity but risks a debt trap if overused.
- (v) **Debt cancellation/forgiveness:** Creditors may cancel part of the debt, especially for LDCs under international debt relief initiatives (e.g., HIPC – Heavily Indebted Poor Countries).
- (vi) **Debt conversion (swap):** Converting debt into investment projects, equity, or development programs. Example: Debt-for-nature swaps, where debt is forgiven in exchange for environmental conservation.
- (vii) **Foreign aid and grants:** Using concessional loans or grants from donors to ease repayment burdens.
- (viii) **Import substitution:** Reducing imports to save foreign exchange for debt repayment. Encourages domestic production.
- (ix) **Fiscal discipline:** Cutting unnecessary expenditure and improving tax collection to generate funds for repayment.

Uganda (LDC) Context

- (i) Uganda relies on **export earnings** (coffee, gold, fish) to service external debt.
- (ii) The country has benefited from **debt relief initiatives** like HIPC and MDRI (Multilateral Debt Relief Initiative).
- (iii) **Debt rescheduling and refinancing** are common strategies when facing repayment difficulties.
- (iv) Rising external debt servicing costs remain a challenge, consuming a large share of Uganda's budget.

Causes of a huge Public debt (budgetary deficits) in Uganda (LDC's)

- (i) **Low tax base:** Uganda has a narrow range of taxable sources, with most citizens in subsistence farming and informal trade. Limited revenue forces the government to borrow to finance expenditure.
- (ii) **High levels of inflation:** Inflation erodes the real value of government revenue, making it harder to meet planned expenditure. This widens deficits and increases borrowing needs.
- (iii) **Persistent debt servicing:** Large portions of revenue are used to repay old debts. In FY 2023/24, debt servicing consumed **UGX 8.76 trillion**, projected to rise to **UGX 12.72 trillion** in FY 2024/25. This forces the government to borrow more to cover recurrent costs.
- (iv) **High demand for investment vs. low savings:** Uganda faces a savings-investment gap, with domestic savings too low to fund development. Borrowing bridges this gap.
- (v) **Political instability and insecurity:** Conflicts, insecurity, and political pressures increase government spending on defense and subsidies. This worsens deficits and raises borrowing.

- (vi) **Dependence on external borrowing:** Uganda relies heavily on loans from IMF, World Bank, and China to finance infrastructure. External debt increases vulnerability to global shocks and foreign exchange risks.
- (vii) **Donor funding fluctuations:** Delays or reductions in foreign aid force Uganda to borrow more to meet budgetary needs.
- (viii) **Corruption and mismanagement:** Misuse of funds reduces efficiency of borrowed money, leading to repeated borrowing.
- (ix) **Under taking over ambitious projects** like Universal Primary Education (U.P.E), Universal Secondary Education (U.S.E), and Poverty alleviation programs etc. without enough resources. This forces the government to borrow hence a huge public debt.
- (x) **High population growth rates leading to high dependence burden.** This forces the government to borrow in order to cater for the social needs of the rapidly growing population e.g. education, medical care etc.
- (xi) **Excessive capital out flow inform of profit repatriation.** This leads to loss of public revenue hence balance of payment deficits for the country.

Uganda Context

- (i) Uganda's **public debt stock** has grown rapidly, with external borrowing financing major infrastructure projects.
- (ii) Debt servicing now consumes a **significant share of the national budget**, crowding out spending on health, education, and poverty reduction.
- (iii) The Ministry of Finance acknowledges that **low domestic revenue mobilization** and **high borrowing costs** are key drivers of deficits.

Measures to reduce the budgetary deficits (Curb the huge public debt) in Uganda

Uganda, like many **Less Developed Countries (LDCs)**, faces persistent budget deficits and rising public debt due to limited revenue, high expenditure needs, and reliance on external borrowing. To address this, governments adopt both **short-term fiscal measures** and **long-term structural reforms**.

Key Measures

- (i) **Enhance domestic revenue mobilization:** Broaden the tax base by formalizing the informal sector; Improve tax administration to reduce evasion and corruption; and introduce progressive taxation to ensure fairness.
- (ii) **Control government expenditure:** Cut unnecessary spending on non-essential projects; Reduce recurrent expenditure (e.g., administrative costs, allowances); while prioritizing productive investments that generate growth.
- (iii) **Promote export growth:** Diversify exports beyond coffee and gold to earn more foreign exchange; Strengthen agro-processing and industrialization to increase competitiveness.

- (iv) **Encourage domestic savings:** Develop financial markets to mobilize savings through bonds and treasury bills. Encourage pension schemes and insurance to provide long-term funds.
- (v) **Debt restructuring and relief:** Negotiate with creditors to extend repayment periods or reduce interest rates. Seek concessional loans instead of expensive commercial borrowing.
- (vi) **Strengthen governance and reduce corruption:** Ensure borrowed funds are used productively. Increase transparency in debt management and budget execution.
- (vii) **Promote import substitution:** Reduce reliance on imports by supporting local industries. Saves foreign exchange for debt servicing.
- (viii) **Public-private partnerships (PPPs):** Engage private investors in infrastructure projects to reduce government borrowing.
- (ix) **Fiscal discipline:** Stick to realistic budgets and avoid politically motivated overspending. Ensure expenditure aligns with available resources.
- (x) **Use of the Privatization policy.** This can help reduce on government expenditure on non performing Parastatals hence reducing the budgetary deficits.
- (xi) **Cost sharing** especially in providing public services to the people. The cost of providing social services can be shared between the government and the people as a way of reducing government expenditure.
- (xii) **Maintaining political stability and security in the country.** Democratic governance should be promoted and practiced. In addition peace talks and amnesty laws should be respected as a way of promoting peace in the country. This can also help to reduce defense spending.
- (xiii) **Checking on the high population growth rate.** This can be done by encouraging people to use family planning methods as a way of controlling population growth.
- (xiv)

Uganda Context

- (i) Uganda's **Ministry of Finance** has emphasized **domestic revenue mobilization** through the Uganda Revenue Authority (URA).
- (ii) Efforts to **diversify exports** (fish, flowers, manufactured goods) aim to reduce reliance on coffee and gold.
- (iii) Uganda has benefited from **debt relief initiatives** (HIPC, MDRI) but still struggles with high debt servicing costs.
- (iv) **Corruption and mismanagement** remain major obstacles to effective debt reduction.

Revision exercise 2

Section A questions

- 1 (a) Distinguish between a surplus budget and a deficit budget ,
(b) Outline two effects of a surplus budget on an economy
- 2 Mention four ways of financing a deficit budget
- 3 (a) What is meant by a national budget?

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- (b) State four objectives of a national budget
- 4 (a) Distinguish between external public debts and internal public debts.
(b) Give two demerits of external borrowing to the economy.
- 5 Distinguish between the following terms
 - (a) Reproductive debt and deadweight debt .
 - (b) Funded debt and unfunded debt.
 - (c) Debt redemption and debt rescheduling
 - (d) Debt Conversion and debt retirement
- 6 (a) Distinguish between Balanced budget and a deficit budget.
(b) Give two ways of financing a deficit budget in an economy.
- 7 (a) Distinguish between a public debt and a national debt.
(b) Mention two ways of redeeming a public debt in your country.
- 8 (a) Distinguish between public debt and national debt
(b) Suggest two ways in which an external public debt may be cleared.
- 9 (a) What is meant by public debt management?
(b) Mention three tools of public debt management in your country.
- 10 Mention four objectives of public debt management.
- 11 (a) Distinguish between the internal debt and external debt
(b) Mention two reasons why countries incur public debts
- 12 Give any four sources of public debts in an economy

Section B questions

- 1 (a) Distinguish between a balanced budget and unbalanced budget.
(b) How can the national budget be used as an instrument of fiscal policy?
- 2 (a) Account for the persistent budgetary deficits of your country
(b) Suggest the measures that should be taken to reduce the huge public debt in your country
- 3 (a) Distinguish between a balanced budget and a surplus budget
(b) Outline the effects of a surplus budget on an economy
(c) Explain the role of the national budget in the development process of your country
- 4 (a) Distinguish between a balanced budget and unbalanced budget.
(b) Why is it difficult to achieve a balanced budget?
- 5 Explain why the government may plan for;
 - (a) a surplus budget.
 - (b) a deficit budget
- 6 (a) Why do countries borrow?
(b) Explain the ways of clearing;
 - (i) Internal public debt
 - (ii) External public debt

Thank you
Dr. Bbosa Science