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Monetary Policy Statement for August 2016

Inflation continued on a downward trend that began at the end of December 2015. Annual headline and core inflation declined to 5.1 percent and 5.6 percent, respectively in July 2016 from 5.9 percent and 6.8 percent in June 2016. The stability of the exchange rate, lower fuel and subdued domestic demand have contributed to the gradual dampening of inflation pressures over the last seven months.

Although real output declined in the third quarter of Financial Year (FY) 2015/2016, the Bank of Uganda's high frequency measure of economic activity for July 2016, indicates a recovery in the fourth quarter of the Financial Year. As domestic demand picks up, the economy is projected to grow more strongly in FY 2016/2017, at about 5.5 percent compared to the preliminary estimate of 4.6 percent for FY 2015/16. The recovery in private sector credit growth and higher public infrastructure spending are expected to support economic growth. However, uncertainty over international economic activity has increased substantially and this could constrain international demand for Uganda's exports.

The near-term outlook for inflation has improved as a result of the recent stability of the exchange rate. Annual core inflation is now expected to converge to the medium term target of 5 percent slightly faster than was anticipated during the last Monetary Policy Committee meeting held in June 2016. Both annual headline and core inflation are now forecast to decline to around 5 percent by end 2016.

The outlook for inflation is subject to several risks emanating from both the external environment and the domestic economy. Uncertainty over international developments has increased which could affect the exchange rate. In addition, weather related risks could affect food prices heightening the upside risks to domestic inflation.

Given that inflation is forecast to stabilize around the policy target of 5 percent over the next 6 months, the Bank of Uganda believes that a continued easing of monetary policy is warranted. This will also help to support a recovery of private sector credit and hence support real economic growth. Accordingly, the BoU will reduce the CBR by 1 percentage point to 14 percent. The band on the CBR will be maintained at +/-3 percentage points and the margin on the rediscount rate at 4 percentage points on the CBR. Consequently, the Rediscount rate and the Bank rate have been reduced to 18 percent and 19 percent, respectively.

Prof. Emmanuel Tumusiime-Mutebile

Governor

August 8, 2016