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Monetary Policy Statement for January 2014

Inflation continued to abate in December 2013. Annual headline inflation declined to 6.7 percent in December 2013 from 6.8 percent, reflecting mainly the decrease in transport and communication and beverages and tobacco. Annual core inflation declined to 5.7 percent from 7.0 percent in November 2013. Annual non-food inflation also declined to 5.7 percent from 6.3 percent in November 2013. Annual food inflation however, rose to 9.2 percent from 8.1 percent. The increase in food inflation was largely driven by relatively low food prices in December 2012 as monthly food inflation stood at minus 1.0 percent.

The Bank of Uganda (BoU) forecasts suggest that inflation will edge down further in the near term driven by improved food crop harvests, but rise to 6.5 – 7.5 percent during the latter part of 2014. The potential rise in inflation and its timing will depend largely on movements in the exchange rate, changes in commodity prices, and the degree to which momentum in economic activity spills over into broader cost and price pressures.

Growth in the first quarter of 2013/14 was lower than expected as quarterly GDP declined by 0.6 percent compared to the previous quarter. This decline was precipitated by the drought, which led to a 3.4 percent decline in agricultural output. Nonetheless the economy is projected to pick-up in the remaining part of 2013/14, driven by the recovery in agricultural production and public investment in infrastructure, which could enhance competitiveness in the short to medium term. Private consumption and investment activity is expected to rise as consumer and household credit extension gradually gain momentum following the declines in Commercial Banks' lending rates. Growth in 2013/14 is still projected at 6 percent – 6.5 percent, well within the level of potential GDP growth.

Inspite of the better-than-expected October 2013-December 2013 inflation outcome, the BoU continues to assess the risks to the inflation outlook to be on the upside. Monetary policy therefore has to balance current modest inflation outturn against the likelihood that inflationary pressures will rise over the medium term. Therefore, the Bank of Uganda will maintain the Central Bank Rate (CBR) at 11.5 percent in January 2014. The band on the CBR will be maintained at +/-2 percentage points and the margin on the Rediscount rate at 3 percentage points on the CBR. Consequently, the Rediscount rate and the Bank rate for January 2014 will be 14.5 percent and 15.5 percent, respectively.

The BoU will continue to assess the global and domestic economic developments and their implications on the overall outlook for inflation and growth of the Ugandan economy. The Bank shall take appropriate action to ensure that annual core inflation remains around the policy target of 5 percent in the medium term.

Prof. Emanuel Tumusiime-Mutebile

<u>Governor</u>

January 03, 2014