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Monetary Policy Statement for October 2015

Inflation rose in September 2015, with annual headline inflation edging up to 7.2 percent from 4.8 percent in August 2015. Annual core inflation also rose to 6.7 percent in September 2015 from 5.5 percent in August 2015. The heightened inflationary pressures were driven by the rise in food crop prices, in combination with the effects of exchange rate depreciation and strong base effects on account of low inflation in September 2014.

Although real GDP growth in FY 2015/16 is projected at 5 percent, down from an earlier projection of 5.8 percent, this is still strong growth given the weakening of global economic growth. The downward revision was necessitated by four factors: the subdued global growth, which will reduce demand for our exports; reduced capital flows and low international commodity prices which will exacerbate the effects of declining exports; exchange rate depreciation which will increase the cost of imported capital; and the impact of tight monetary and fiscal policies, which may weaken domestic demand.

After sustained depreciation pressures, since the beginning of 2014, we have witnessed less volatility in the exchange rate in the months of September and October 2015. More recently, the exchange rate has strengthened by close to fifty Shillings. The Bank of Uganda expects that the exchange rate will remain relatively stable going forward, though sporadic exchange rate volatility cannot be ruled out due to the global economic conditions.

The Bank of Uganda's inflation forecasts based on the prevailing domestic and external economic conditions and outlook indicate that inflation will continue to rise over the course of FY 2015/16. External sources of inflation are likely to stay generally benign, given weak global demand conditions. On the domestic front, the exchange rate depreciation experienced over the last 12 months is yet to feed through completely to prices and will therefore continue to put upward pressure on inflation. In addition, the projected El Nino weather conditions could result in higher food crop prices in Q4-2015 and Q1-2016, thus leading to heightened inflationary pressures.

The Monetary Policy actions taken by the BoU since April 2015, which have entailed a rise in the CBR by 5 percentage points, have already dampened inflationary pressures and reduced the risks to high inflation. Nevertheless, to ensure that medium term inflation converges towards the BOU's policy target of 5 percent, a further monetary policy tightening is warranted. Therefore, the BOU will raise the CBR by 1 percentage point to 17 per cent. 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. The rediscount rate and the bank rate will therefore be increased to 21 per cent and 22 per cent, respectively.

Prof. Emmanuel Tumusiime-Mutebile

Governor

October 20, 2015