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Monetary Policy Statement for April 2016

Annual headline and core inflation declined to 6.2 percent and 6.9 percent, respectively, in March 2016 after peaking at 8.5 per cent and 7.6 percent in December 2015. However, monthly core inflation edged up slightly in March 2016 by 0.1 percentage point compared to February 2016, in part because of the revision of school fees in the Consumer Price Index basket. The decline in annual headline inflation is largely because of the fall in food crops inflation, which declined to 0.8 percent in March 2016 from 7.1 percent and 16.2 percent in February 2016 and December 2015, respectively.

The economy has continued to grow at a moderate pace. The high frequency indicators of economic activity suggest that economic activity was lower in the first quarter of 2016 compared to the last quarter of 2015. However, the indicators for the first eight months of the FY 2015/16 are consistent with the real economic growth forecast of 5 percent for FY 2015/16.

There are, nonetheless, downside risks to the projected output growth, partly emanating from the difficult external economic environment. This remains challenging for the macroeconomy and may even deteriorate further over the next 12 months, if commodity prices fall further and growth slows in major Emerging Market Economies. Consequently, Uganda's balance of payments in the short to medium-term will remain vulnerable to the turbulences in the global economic environment.

The inflation outlook has improved since the February 2016 Monetary Policy Statement, mainly because of the easing of the exchange rate depreciation pressures, faster decline of food prices, and the subdued global economic outlook. External weakness is expected to weigh on inflation both directly (through persistently lower import prices) and indirectly (by dampening domestic economic activity).

The Bank of Uganda (BoU) is cognisant of the fact that demand pressures on inflation are more subdued than at the time of the last Monetary Policy Committee meeting, and indications are that domestic demand is likely to remain constrained.

The BoU now forecasts that both headline and core inflation will remain in the range of 6.5±1percent in H1-2016 before gradually declining to the BoU's medium-term target of 5 percent in Q1-2017. Nonetheless, there are upside risks to this outlook, including the future path of the exchange rate, which in part is contingent on external economic environment.

Given that the inflation outlook has improved and to ensure that real economic growth remains close to potential, the BoU believes that it is warranted to cautiously ease monetary policy. The BoU will therefore reduce the CBR by 1 percentage point to 16 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 20 percent and 21 percent, respectively.

Prof. Emmanuel Tumusiime-Mutebile

Governor

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