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Monetary Policy Statement for October 2024

On 7 October 2024, the Bank of Uganda's Monetary Policy Committee (MPC) reduced the Central Bank Rate (CBR) by 25 basis points to 9.75% due to an improved inflation outlook.

Inflation remains subdued, in part reflecting the unwinding of the global shocks, stable shilling exchange rate partly due to sturdy coffee export receipts, moderate import growth, and prudent monetary policy that balanced economic growth recovery while maintaining price stability. Over the twelve months to September 2024, annual headline and core inflation both averaged 3.2%. Specifically, annual headline and core inflation decreased to 3.0% and 3.7% in September 2024, down from 3.5% and 3.9% in August 2024, respectively. Notably, inflation declined in September 2024, driven by lower oil prices and reduced food prices. The decline in core inflation was primarily attributed to a reduction in services inflation, particularly in passenger transport services.

The Bank of Uganda projects average core inflation to remain below the medium-term target of 5% over the next 12 months, supported by a relatively stable shilling exchange rate and favourable food and oil prices. However, inflation is expected to return and stabilise around the target in the medium term.

The inflation outlook is susceptible to risks. On the downside, inflation may be lower if:

- the previous policy actions dampen demand more than expected;
- the economic environment in the rest of the world worsens unexpectedly;
- favourable harvest that results in lower food crop inflation than currently projected; and
- stronger appreciation of the shilling, partly due to stronger capital inflows coupled with softer global inflation.

On the upside:

- heightened geopolitical tensions could push energy prices and freight costs higher and disrupt global trade, resulting in higher domestic inflation;
- ongoing global developments could result in faster shilling exchange rate deprecation, causing inflation to rise sharply;
- extreme weather events could drive food prices higher than projected; and
- higher domestic economic growth due to increased investment in the extractive industries and effective implementation of the government's programs could result in stronger aggregate demand than currently envisaged, resulting in higher inflation.

Overall, the risks to the inflation outlook are balanced.

GDP estimates for the quarter ended June 2024 by the Uganda Bureau of Statistics (UBoS) indicate that growth has been strong, with an annual quarterly real GDP growth of 6.6%. High-frequency indicators of economic activity and business sentiments point to a continuing pick-up in economic activity. Economic growth is still projected at 6.0-6.5% in FY 2024/25 and 7.0% in the subsequent years. This growth trajectory is underpinned by strategic government interventions, an increase in foreign direct investment in the extractive industry, and the commencement of oil production in FY2025/26. However, the growth outlook is subject to several risks. On the downside:

- intensified geopolitical tensions could generate further economic shocks through disruption of trade and supply chains, leading to higher commodity prices, especially oil;
- elevated trade restrictions and debt levels in many countries could add significant inflationary pressure to the world economy, generating tighter financial conditions for Uganda; and
- domestic financial conditions could remain tight, resulting in higher borrowing costs and, subsequently, private sector credit growth remaining sluggish. Higher domestic borrowing to finance fiscal deficits could crowd out the private sector and exacerbate the already constrained private sector credit.

By contrast, growth could be higher if:

- inflation drops much lower, raising confidence and real incomes, resulting in stronger demand;

- the world economy grows more strongly than expected;
- investment in the minerals sector is higher than anticipated;
- more favourable weather conditions yield good food crop harvests; and
- monetary policy conditions are more accommodative.

Overall, risks to the growth outlook are balanced.

The MPC assesses that inflation is expected to remain below the target in the near term and that the risks to inflation are balanced but acknowledges the inherent uncertainty in the outlook, which warrants a cautious monetary policy stance. Against this backdrop, the MPC reduced the policy rate by 25 basis points to 9.75%. The bands on the CBR remained at +/-2 percentage points, and the margins on the CBR for the rediscount and bank rates at 3 and 4 percentage points, respectively. As a result, the rediscount and bank rates have been reduced to 12.75% and 13.75%, respectively.

The MPC notes that easing of monetary policy is necessary to keep inflation on track while supporting socio-economic transformation. Any additional changes to the policy rate will continue to rely upon the incoming data and the evolving assessment of risks to guide its decisions.

Michael Atingi-Ego
Deputy Governor

7 October 2024