

# BANK OF UGANDA



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## Monetary Policy Statement for July 2022

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At the extra-ordinary Monetary Policy Committee (MPC) meeting held in July 2022, the Bank of Uganda increased the Central Bank Rate (CBR) by 1 percentage point to 8.5 percent.

Inflation continues to rise, largely influenced by external cost pressures stemming from higher global food and energy prices, persisting global production and distribution challenges, as well as rising domestic food crop prices due to dry weather across the country. The annual headline and core inflation rose to 6.8 percent and 5.5 percent in June 2022 from 6.3 percent and 5.1 percent in May 2022, respectively. Annual food crop inflation has sharply risen from 0.7 percent in February 2022 to 14.5 percent in June 2022.

The rising food and energy prices, intensified by a weaker Uganda shilling, have worsened the inflation outlook for the remaining part of 2022 and into 2023. The headline and core inflation are now forecast to average 7.4 percent and 6.3 percent, respectively, in 2022, slightly higher than the 7.2 percent and 6.1 percent that were projected in the June 2022 forecast round. Inflation is forecast to peak in the second quarter of 2023 before gradually declining to stabilise around the medium-term target of 5 percent by mid-2024.

The inflation outlook is significantly uncertain, with the balance of risks tilted to the upside, including:

- Global inflationary pressures amidst persistently higher world food and energy prices.
- A faster shilling depreciation as advanced economies raise their policy rates to control escalating inflation.
- Higher prices in the global markets that could further increase the demand for foreign exchange (US\$ in particular) required to purchase about the same quantity of goods, which may further weaken the shilling.
- Potential worsening of disruptions of global production and distribution due to stringent controls of Covid-19 outbreaks, especially in Asia.
- Higher domestic food crop prices due to the effect of prolonged dry weather conditions on food harvests.

The downside risks include:

- Weaker domestic consumption and investment as higher inflation reduces consumers' real incomes and tighter financial conditions constraining private sector access to funding.

- Escalation of global inflationary pressures could ease much faster than currently assumed, resulting in a decline in imported inflation.

The June 2022 preliminary GDP estimates by the Uganda Bureau of Statistics (UBoS) indicate that the economy grew by 4.6 percent in Financial Year (FY) 2021/22 from a revised growth rate of 3.5 percent the previous year. The economic growth was driven largely by private investment despite imports far exceeding exports. On the production side, the industry and services sectors were the main drivers of growth, with some of the services sector activities, such as education and trade recovering. However, households' and businesses' expectations about economic developments have grown more tepid, and the global economic outlook is highly uncertain. Indeed, the Composite Index of Economic Activity (CIEA), a high-frequency indicator of economic activity, continues to signal a slowdown in the pace of economic recovery in the second half of the financial year. The CIEA growth in the three months to May 2022 decelerated to 0.9 percent from 2.1 percent in the three months to February 2022.

Overall, economic activity is projected to remain modest as the shocks to commodity prices, production and distribution disruptions, and global inflation continue to dim the prospects for domestic economic growth. Economic growth is still projected in the range of 4.5-5.0 percent in 2022 and rising slightly to 5.0-5.5 percent in 2023, in part supported by public investments. Weaker external demand, high domestic inflation and resultant tighter domestic financial conditions will constrain exports, consumption, and investment.

The risks to the growth outlook, which are tilted to the downside, include weaker global growth, escalation of geopolitical conflicts, heightened global economic uncertainty, and higher inflation. Other downside risks are a further decline in consumer confidence, heightened exchange rate volatility and weakening investor optimism. Nonetheless, in the medium-term, the economy is projected to grow in the range of 6.5-7.0 percent, supported by public and private investments in the oil sector.

While the inflationary pressures are likely to be temporary, the MPC assessed that a markedly higher policy rate is needed to stabilise inflation around the target. Accordingly, the MPC raised the CBR to 8.5 percent and maintained the band on the CBR at +/- 2 percentage points. The margins on the CBR for the rediscount and bank rates remain at 3 percentage points and 4 percentage points, respectively. Consequently, the rediscount and bank rates are now 11.5 percent and 12.5 percent, respectively.

The BoU also increased the Cash Reserve Requirement by 2 percentage points to 10 percent, effective 23 June 2022. The MPC considers that the monetary policy stance will have to be tightened even further so as to ensure that inflation eases back to target in the medium-term.



Michael Atingi-Ego

Deputy Governor

05 July 2022