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Monetary Policy Statement for December 2011

Although annual inflation rates remain too high, with headline and core inflation standing at 29 percent and 30.6 percent respectively in November, there are now signs that inflation has peaked and that inflationary pressures have begun to abate. Monthly inflation rates fell sharply in November, especially in comparison with those recorded in the third quarter of 2011. The monthly headline inflation rate stood at only 0.1 percent in November; hence the average increase in prices of the items in the consumer basket was negligible. Food prices actually fell in November, by 0.3 percent, while non food prices rose by only 0.4 percent during the month. The marked deceleration in monthly inflation rates provides a clear sign that inflation is being brought under control and that the prospects for lower annual inflation rates have strengthened.

In last month's monetary policy statement I identified the persistent and very rapid growth in bank credit to the private sector as a major contributor to the demand side pressure on inflation in Uganda. The latest data available to the BOU indicates that the growth of bank lending began to decelerate in October and that this deceleration continued through the first half of November, as a result of the increases in bank lending rates. The slowing down of bank credit growth will help to ameliorate inflationary pressures over the coming months. Furthermore, the strengthening of the monthly average exchange rate in November, by 8 percent against the US dollar, will also serve to dampen inflationary pressures provided that it is sustained over the next few months. Both the deceleration in credit growth and the strengthening of the exchange rate bear testament to the effectiveness of the monetary policy strategy implemented by the BOU over the last few months.

Looking ahead, my confidence that inflation will fall during the course of 2012 has been reinforced by the positive developments observed in November. The BOU forecasts that core inflation will fall to approximately 10 percent by the end of 2012 and will continue declining in 2013. At the global level, inflation for both commodities and manufactured goods are forecast to moderate in 2012, which will also facilitate our efforts to bring down inflation in Uganda.

Nevertheless there are still major risks to the inflation outlook for Uganda for 2012 which cannot prudently be discounted. In particular further turbulence on global financial markets could have deleterious consequences for capital flows to our economy and thus for the stability of the exchange rate, which in turn would have an adverse impact on the prices of imported goods. Furthermore, food prices remain very vulnerable to supply side shocks.

In the light of the developments that I have noted, the BOU will keep its monetary policy stance unchanged in December 2011. Although the outturn for inflation and developments in financial markets in November were generally positive for the future outlook for inflation, it is important to maintain downward pressure on aggregate demand to ensure that the fall in inflation is sustained. It would be premature to loosen monetary policy until significant falls in annual inflation rates have been achieved.

Consequently the BOU will maintain the Central Bank Rate (CBR) at 23 percent, with a band of plus/minus 400 basis points. The margin on the rediscount rate will remain at 500 basis points on the CBR. Hence the rediscount rate and the Bank Rate will remain at 28 percent and 29 percent, respectively.

Emmanuel Tumusiime-Mutebile
GOVERNOR
December 02, 2011