STATE OF THE ECONOMY REPORT

SEPTEMBER 2024

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ACRONYMS AND ABBREVIATIONS

ADB	Africa Development Bank
ADF	Africa Development Fund
AEs	Advanced Economies
EIA	Energy Information Administration
EIB	European Investment Bank
BOU	Bank of Uganda
CBR	Central Bank Rate
CRM	Credit Relief Measure
CIEA	Composite Index of Economic Activity
Covid-19	Corona Virus Disease 2019
CPI	Consumer Price Index
EAC	East African Community
EU	European Union
EFU	Energy, Fuel and Utilities
EMs	Emerging Market Economies
EMDEs	Emerging Market and Developing Economies
FDI	Foreign Direct Investment
Fed	Federal Reserve
GDP	Gross Domestic Product
IDA	International Development Association
IFAD	International Fund for Agricultural Development
IMF	International Monetary Fund
LICs	Low Income Countries
NEER	Nominal Effective Exchange Rate
NPLs	Non- Performing Loans
OPEC	Organization of Petroleum Exporting Countries
OPEC+	OPEC and partners
PSC	Private Sector Credit
REER	Real Effective Exchange Rate
SDR	Special Drawing Rights
SSA	Sub-Saharan Africa
TDB	Trade and Development Bank
UK	United Kingdom
US	United States
USA	United States of America
US$	United States Dollar
URA	Uganda Revenue Authority
y/y	Year-on-Year

EXECUTIVE SUMMARY

1. The State of the Economy report presents economic developments up to the three months to August 2024 where data is available, policies, outlook and associated risks to the macroeconomy. The report is structured into two parts. Part 1 presents the external environment and its implications for Uganda's economy, and Part 2 presents domestic developments, outlook, and policies.

2. The global economy is projected to expand by over 3.2 percent in 2024 and 2025, driven by growth in emerging market economies and Sub-Saharan African countries. The major downside risks to this growth include geopolitical conflicts, adverse climatic conditions, and trade tensions. On the positive side, these could be moderated by monetary policy easing as the inflationary pressures abate.

3. The global disinflation process which begun in 2023 has continued into 2024 but, has waned even though inflation remains above central bank targets in many countries. However, global commodity prices continued to rise in July 2024, building on the increases observed since April 2024, driven by oil prices, precious metals, and beverages. This is likely to boost Uganda's export earnings, particularly from coffee, tea, and cocoa.

4. The domestic money market has responded positively to the monetary policy easing with appropriate adjustments in rates as liquidity conditions improved. In line with these developments, the uptake of the standing lending facility (SLF) significantly dropped, reflecting the easing of liquidity pressures. The yields on treasury securities showed mixed movements across various tenors. The yields on the 2-year and 3-year bonds increased while the yields on longer tenors, the 10-year and 15-year bonds declined. The weighted average shilling lending rate rose in the three months to July 2024 to 18.0 percent from 17.7 percent in the three months to April 2024. Similarly, the lending rate on foreign currency-denominated loans also rose slightly. The rise in the lending rates was partly attributed to a series of previous tightening cycles.

5. Private sector credit (PSC) growth remains sluggish, reflecting banks' preference for high-yield government papers, the lingering effects of the pandemic, and structural impediments to private loans. As Covid-19-related asset quality problems in banks dissipate and financial market reforms and fiscal consolidation advance, credit growth should pick up. Nonetheless, in the recent past, PSC has shown signs of recovery, reflecting the positive economic outlook and a stable foreign exchange rate.

Additionally, the net credit extensions experienced a significant upturn in the three months to July 2024. This growth can be attributed to the Bank of Uganda's recent monetary policy action that has enhanced macroeconomic stability and improved liquidity conditions, which provides for loanable funds. Furthermore, there has been a marked improvement in the demand for and supply of credit.

6. The domestic economy remained resilient and was estimated to have expanded by 6 percent in FY2023/24, driven by robust domestic demand, favourable weather conditions, subdued inflation, and the positive impact of the roll-out of the Parish Development Model (PDM). The growth outlook is more optimistic, with economic growth expected in the range of 6.0 to 6.5 percent in FY2024/25, and over 7.0 percent in the medium term, boosted by oil production. There are risks to the forecast that are broadly balanced and these include weak private sector credit growth, delayed investments in oil production, the effects of geopolitical conflicts on trade flows and freight costs, and adverse climatic conditions. These downside risks are likely to be moderated by investment in oil production activities, conducive weather conditions that support production, and favourable international prices.

7. The FY2023/24 fiscal deficit is estimated at 4.8 percent of GDP, compared to 5.5 percent in FY2022/23 but higher than what was initially projected at 3.8 percent. The higher-than-projected deficit is due to (i) revenue underperformance and (ii) higher current spending. In FY2024/25, the overall fiscal deficit is projected to widen to 5.8 percent of GDP. The widening largely reflects a sizable increase in interest payments on domestic debt. The government is committed to pay the maturing securities in FY2024/25 and they are expected to securitize the stock of unreimbursed government securities as at June 2024 redeemed by BoU. Nevertheless, Uganda's public debt is assessed to be sustainable with a moderate risk of debt distress. Public debt, as a share of GDP, is expected to remain at about 50 percent of GDP over the medium term. The Debt Sustainability Analysis indicates that the external debt burden and public debt indicators remain below their respective thresholds and benchmarks under the baseline scenario. The stress tests suggest breaches of the thresholds, indicating a moderate risk of overall and external debt distress.

8. The current account balance improved and registered a lower deficit in the three months to July 2024, largely due to improvements in all sub-accounts except the services and primary income accounts. Similarly, the capital account improved. However, the financial account surplus narrowed, and the balance of payments (BOP) position recorded a deficit mainly attributed to low inflows into the financial account despite improvements in the current and capital accounts.

9. Despite strong FDI inflows, other financial flows weakened substantially and weighed on foreign exchange reserves. While net FDI inflows have been strong since 2021, mainly reflecting oil-related investments, net portfolio and other investment inflows have been weak and volatile, as experienced elsewhere in the region, reflecting less favourable global financial conditions. Net other investment inflows have seen a significant decline in recent years from a peak of US$500 million in FY2019/20 to around US$200 million in FY2023/24 as external project and budget support fell. Overall, despite strong FDI inflows, other financial flows weakened substantially and weighed on forex reserves.

10. In the short term, the current account deficit (CAD) is projected to be supported by increased export revenues from in-season agricultural commodities such as coffee and cocoa due to both increased volumes and prices. Over the medium term, developments in the domestic oil sector will probably drive the direction of the current and financial accounts, with a worsening of the current account as the import bill widens this year to accommodate the oil project-related infrastructural developments. However, as oil exports pick up, the current account will improve in the medium term. The financial account surplus is expected to widen as foreign investment in the oil sector increases towards the target date for oil production.

11. The bilateral shilling/US$ exchange rate has largely been stable, appreciating by an average of 0.9 percent between April and August 2024 after coming under pressure in the first quarter of 2024. The stability has in part, been due to tight monetary policy, which has moderated the outflow of portfolio capital and increased inflows from export revenues, particularly coffee, despite the strong demand from corporates to finance imports and other obligations. Gross foreign exchange reserves fell to US$ 3.3 billion in July 2024 from US$ 3.7 billion in December 2023, with coverage of imports at 3.0 months (excluding oil projects), reflecting higher external debt service payments, inability to secure external loans at affordable terms, and limited foreign exchange purchases by the BoU due to unfavourable domestic foreign exchange market conditions. The BoU has taken measures to build foreign exchange reserves in the short term. Indeed, the BoU utilised foreign exchange swaps/cross currency repos in 2024 with no impact on the exchange rate. Additionally, the Bank plans to purchase gold to build and diversify its composition of reserve assets, an approach which does not directly affect the foreign exchange market.

12. Inflation remains below the target, with the average headline inflation and core inflation decreasing from 4 percent in July 2024 to 3.5 percent and 3.9 percent, respectively, in August 2024. Given the relative stability of the exchange rate coupled with waning global inflation, core inflation is projected to remain below 5 percent in FY2024/25 but is expected to continue

rising moderately in the next four months due to seasonal factors but stabilise around the 5 percent target by the first quarter of 2025. Going forward, risks to the inflation outlook remain broadly balanced. On the upside, inflation could be higher than projected if there is an increase in domestic growth due to increased investment in the extractive industries, unfavourable weather patterns that could affect food production, and a stronger-than-expected path for domestic demand.

In addition, the signs of lingering inflation in other parts of the world and heightened volatility in capital flows and the exchange rate could result in stronger depreciation of the shilling exchange rate and, therefore, higher inflation than currently assumed. On the downside, inflation could be lower than the forecast due to an appreciation of the exchange rate following oil exports in FY 2025/26, lower domestic and global growth, and softer global inflation.

13. The short to medium term outlook is optimistic. The domestic economy remains resilient, and it is projected to grow above 7 percent in the medium term. Notably, Uganda's inflation remains muted given the stable exchange rate, but it is expected to gradually rise to the 5 percent target in 2025. The positive outlook for growth and the exchange rate is likely to improve business prospects and enhance the recovery in PSC growth. Similarly, the CAD is projected to improve in the medium term as oil exports pick up. On the fiscal front, government remains committed to fiscal consolidation however the deficit is expected to initially rise due to interest payments and clearing of outstanding obligations before gradually declining in the medium term.

14. In view of the recent macroeconomic developments and forecasts, the MPC assessed that although risks of higher inflation remain, the adverse impact from past external shocks has abated, and there has been some progress in moderating risks of inflation persistence. Therefore, the MPC noted that it was appropriate to reduce slightly the degree of monetary policy restrictiveness by reducing the CBR by 25 basis points to 10.0 percent and will adjust the policy stance informed by incoming economic data.

1. EXTERNAL ECONOMIC ENVIRONMENT

1.1 Global economic activity and outlook

The global economy is projected to grow at 3.2 percent in 2024 according to the July 2024 update of IMF's World Economic Outlook (WEO), the same as the forecast released in April 2024. Moreover, disparities in growth are projected to have reduced across economies, except for India and China. Similarly, the level of economic activity is projected to expand by 3.3 percent in 2025, a one percentage point upward revision from the previous forecast round. The uptick in 2025 is driven by an anticipated strong recovery of consumption, higher investment from easing of financing conditions, recovery in trade, and stronger growth in Asia, particularly China and India.

Advanced economies (AEs) are forecasted to expand by 1.7 percent, the same growth pace observed in 2023 driven by continued strong growth in the US in 2025. The level of economic activity in the AEs is expected to expand by 1.8 percent in 2025 despite the lower growth outlook for the US economy. In the euro area growth is projected to recover from the region's significant exposure to the Russia-Ukraine war. The euro area's growth has been revised upward by 0.1 percentage points to 0.9 percent in 2024, largely due to expected strong recovery of the services sector and merchandise exports. Similarly, the United Kingdom's (UK) growth forecast for 2024 has been adjusted upward by 0.2 percentage points, bringing it to 1.5 percent. The outlook for the euro area and UK for 2025 were maintained at 1.5 percent as detailed in **Table 1**.

Table 1: Global economic growth projections (y-o-y, % change)

			Projections		Difference from April 2024 WEO Projections 1/	
	2022	**2023**	**2024**	**2025**	**2024**	**2025**
World Output	**3.5**	**3.3**	**3.2**	**3.3**	**0.0**	**0.1**
Advanced Economies	**2.6**	**1.7**	**1.7**	**1.8**	**0.0**	**0.0**
United States	1.9	2.5	2.6	1.9	-0.1	0.0
Euro Area	3.4	0.5	0.9	1.5	0.1	0.0
Japan	1.0	1.9	0.7	1.0	-0.2	0.0
United Kingdom	4.3	0.1	0.7	1.5	0.2	0.0
Emerging Market and Developing Economies	**4.1**	**4.4**	**4.3**	**4.3**	**0.1**	**0.1**
China	3.0	5.2	5.0	4.5	0.4	0.4
India 4/	7.0	8.2	7.0	6.5	0.2	0.0
Russia	-1.2	3.6	3.2	1.5	0.0	-0.3
Brazil	3.0	2.9	2.1	2.4	-0.1	0.3
Saudi Arabia	7.5	-0.8	1.7	4.7	-0.9	-1.3
Sub-Saharan Africa	**4.0**	**3.4**	**3.7**	**4.1**	**-0.1**	**0.1**
Nigeria	3.3	2.9	3.1	3.0	-0.2	0.0
South Africa	1.9	0.7	0.9	1.2	0.0	0.0

Source: IMF World Economic Outlook, July 2024

The emerging markets and developing economies (EMDEs) are expected to be the main drivers of growth despite remaining below the pre-Covid-19 levels. Economic activities in EMDEs are expected to decelerate from the 4.4 percent recorded in 2023 to 4.3 percent in 2024 and 2025, a 0.1 percentage point upward revision from the April 2024 WEO projection, due to improved outlook for China and India. The forecast for China has been revised up by 0.4 percentage points to 5.0 percent in 2024 on account of expectation for strong domestic consumption and exports. Similarly, India's growth projection has been adjusted upward by 0.2 percentage points to 7.0 percent on account of improved prospects for private consumption, particularly in rural areas.

In contrast with the other regions, the growth forecast for Sub-Saharan Africa (SSA) has been revised downward by 0.1 percentage points to 3.7 percent, mainly due to a weaker-than-expected performance of the Nigerian economy in the first quarter of 2024. This SSA outlook is, however, higher than the 3.4 percent growth achieved in 2023 and almost two thirds of these countries are expected to experience higher growth. The recovery is expected to continue in the outer years with economic activity levels projected to reach 4.1 percent in 2025.

1.2 Global inflation and outlook

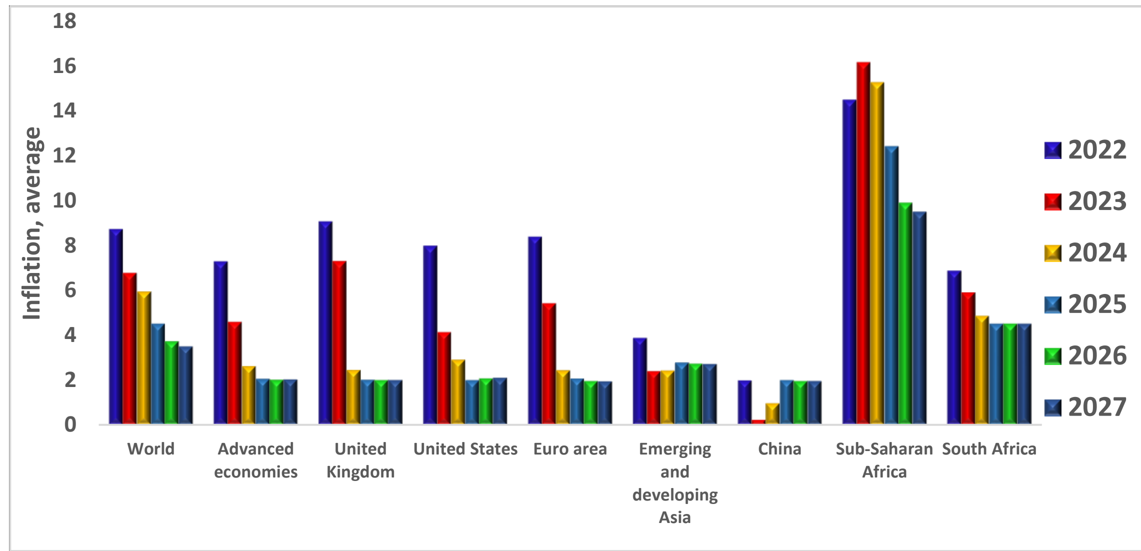
The disinflation process that begun in 2023 is expected to continue until 2024 but, the pace has started to wane with inflation remaining above central bank targets in many countries. Constrained by the services inflation, which remains sticky downwards hampering the disinflation process. Global headline inflation is expected to fall from an annual average of 6.7 percent in 2023 to 5.9 percent in 2024 and 4.4 percent in 2025 (**Figure 1**).

In the AEs, headline inflation is expected to average 2.7 percent, Association of Southeast Asian Nations (ASEAN) at 2.5 percent, EMDEs at 8.2 percent and SSA at 15.3 percent. The persistence of inflation in SSA is partly attributed to food prices due to prolonged droughts and floods as well as protracted conflict in the Sahel region. In the UK, inflation hit the 2 percent target, prompting the Bank of England's Monetary Policy Committee to reduce the policy rate by 25-basis points to 5 percent in July 2024.

Despite the progress with the disinflation process there are upside risks to the outlook. These include the possible effects of extreme weather conditions on agricultural production, escalation of the geopolitical tensions, especially in the Middle East leading to a rise in shipping costs, trade

tensions that could cause supply-chain disruptions, and commodities prices which are expected to rise over the forecast horizon.

Figure 1: Global inflation (y-o-y, % change)



Source: World Economic Report, July 2024

1.3 International commodity prices

Global commodity prices continued to rise in July 2024, building on the increase observed since April 2024, as illustrated in **Figure 2**. Energy prices, which had been on a declining trend between October 2023 and February 2024, are now forecasted to rise by 0.8 percent over the course of 2024. This increase in prices is driven by planned production cuts from the Organization of the Petroleum Exporting Countries (OPEC) and Russia as well as other non-OPEC oil exporters. The price pressures are anticipated to persist due to the effects of the conflicts in the Middle East.

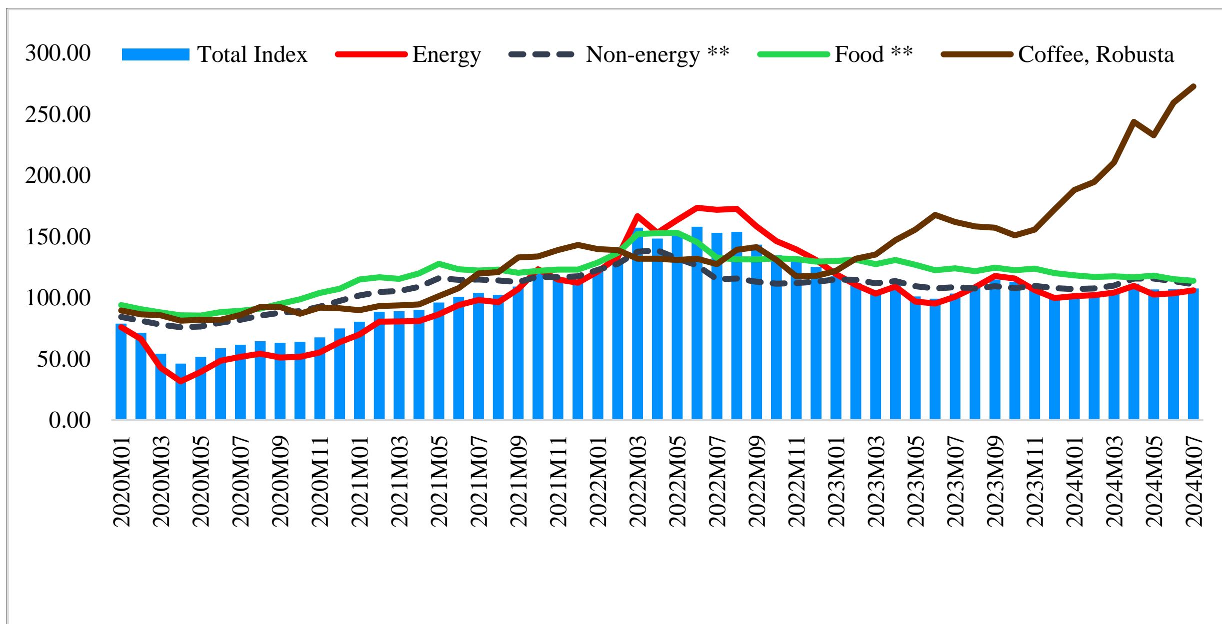
In the three months to July 2024, the global commodity price index, an estimate by the World Bank, registered a 5.9 percent rise driven by increases in prices of precious metals and minerals, energy, and beverages. Boosted by the fluctuations of the oil prices, the energy price index rose to 6.6 percent in the three months to July 2024. Moreover, non-energy prices are anticipated to rise by 5 percent in the 12 months to June 2024 and continue to increase further by 1.6 percent in 2025.

While food prices are on a downward trend due to lower prices for grains, oils, meals, and cereals like wheat and maize, beverage prices surged in June 2024, particularly driven by coffee, tea, and cocoa prices. This could boost export earnings of producers of these commodities. However,

currency devaluations in Ethiopia could negatively impact the market for Uganda's coffee by making Ethiopian coffee prices more competitive.

Metal prices are anticipated to remain high in 2024 and 2025 building on the rise recorded in June 2024 and are expected to continue with this upward trajectory. These price increases reflected positive sentiment about demand amidst concerns of supply disruptions and continued confidence in metals as global uncertainty persists. Gold prices are projected to steadily rise in 2025.

Figure 2: International prices for selected commodities (Indices, 2009=100)

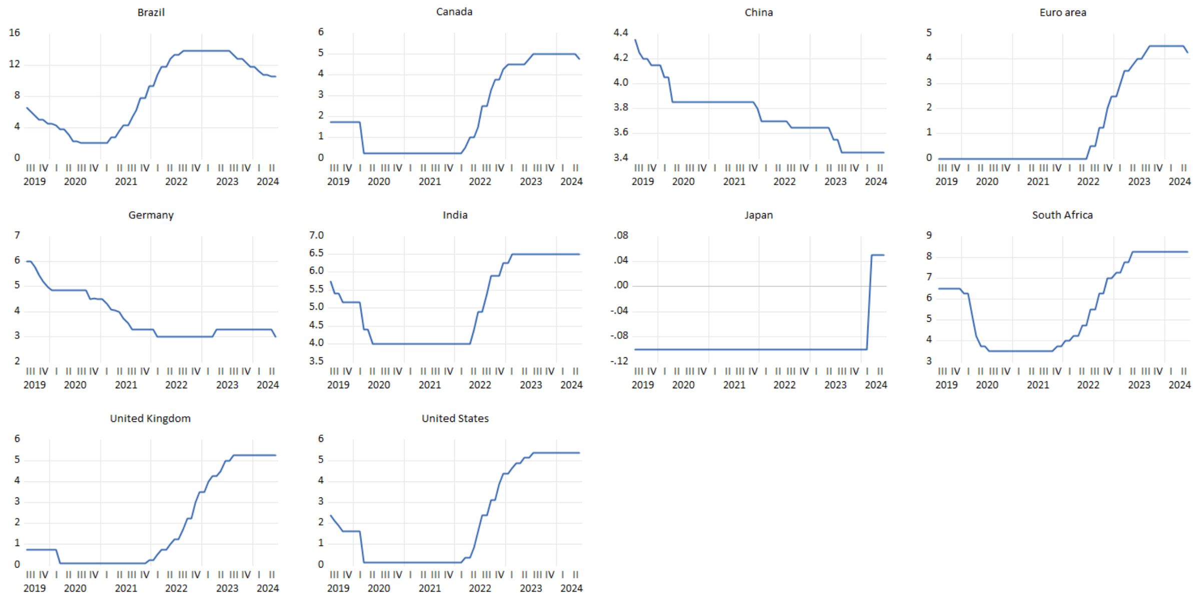


Source: World Bank pink Sheet, May 2024

1.4 Global financial markets

Global financial markets conditions have remained relatively stable. Several AEs central banks have now lowered their key policy rates as inflation pressures reduce, which has galvanized investors to put pressure on the US Federal Reserve to lower its rates too. For example, the Bank of England lowered its key policy rate to 5 percent from 5.25 percent after its inflation fell to the target of 2 percent in June 2024. The European Central Bank reduced its policy rate by 0.25 percent to 4.25 percent in the June meeting and maintained the same position in July 2024. The Bank of Canada followed a similar trend in adjusting its policy rate. However, the Bank of Japan raised its policy rate to 0.25 percent, initiating a gradual retreat from the bond market and reducing its balance sheet (**Figure 3**).

Figure 3: Expectations of policy rates in selected economies (%)



Source: BIS data portal

2. DOMESTIC DEVELOPMENTS OUTLOOK

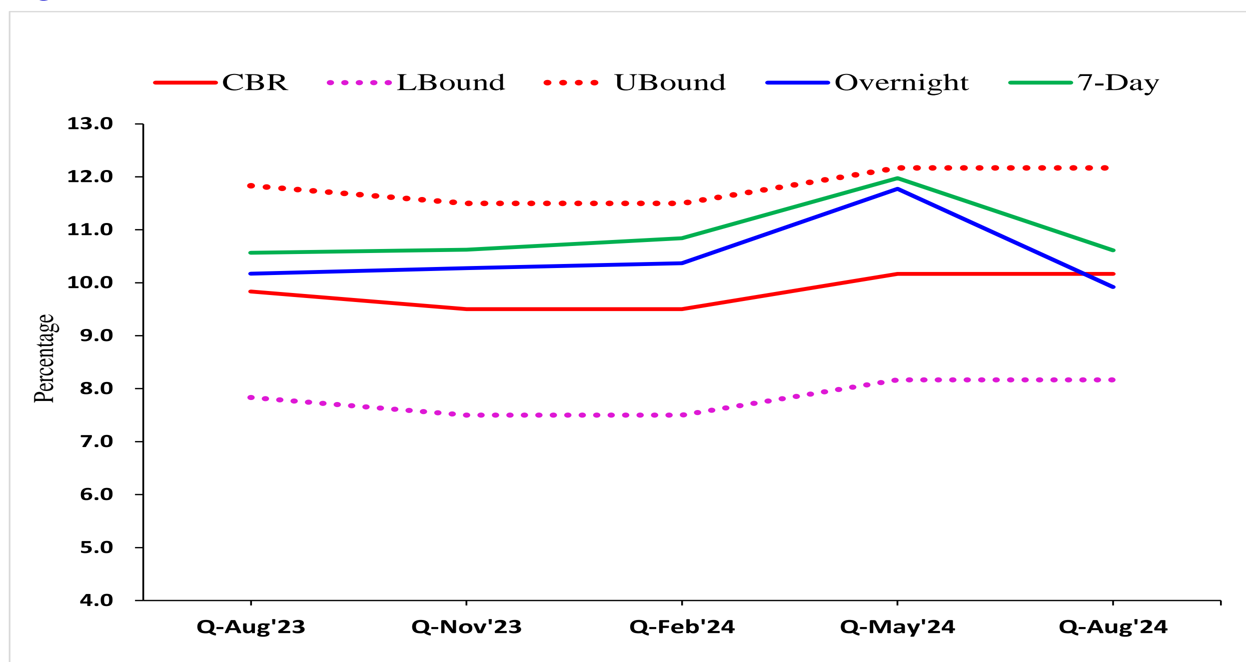
2.1 Domestic financial markets

2.1.1 Monetary policy and the interbank money market

In August 2024, the BoU Monetary Policy Committee (MPC) lowered the central bank rate (CBR) by 25 basis points to 10.00 percent. The lower and upper bands on the CBR were maintained at +/-2 percentage points, while the rediscount and bank rates were set at 13.00 percent and 14.00 percent, respectively. The reduction in the policy rate was mainly to anchor inflation around BoU's target in the medium term as domestic inflation moderated. In the 12 months to July 2024, annual headline and core inflation averaged 3.2 percent and 3.0 percent, respectively. Despite a rise in headline and core inflation to 4.0 percent in July 2024 from 3.9 percent and 3.8 percent in June 2024, it remained below the medium-term target of 5 percent. These developments in inflation coupled with the monetary policy tightening created stability in the exchange rate market with a bias towards appreciation, since March 2024. On the other hand, economic growth for FY 2024/25 was projected to be in the range of 6.0 to 6.5 percent and further to 7.0 percent in the medium term driven by private sector investments, government interventions, and expectation for global growth. Although there are some vulnerabilities, it was assessed that the risk to inflation is moderate and there was room to reduce the policy rate to support economic activity.

The money market has responded positively to the monetary policy actions with appropriate adjustments in rates as liquidity conditions improved. The overnight rate decreased to 9.9 percent in the three months to August 2024, down from 11.8 percent in the three months to May 2024. Similarly, the 7-day interbank weighted average rate declined to 10.6 percent from 12.0 percent over the same period (**Figure 4**). In line with these developments, the uptake of the standing lending facility (SLF) significantly dropped, to Shs.3.7 trillion in the three months to August 2024 from Shs.26.8 trillion recorded in the three months to May 2024. This decline reflects the easing of liquidity pressures.

Figure 4: Central Bank Rate and interbank interest rates



Source: Bank of Uganda

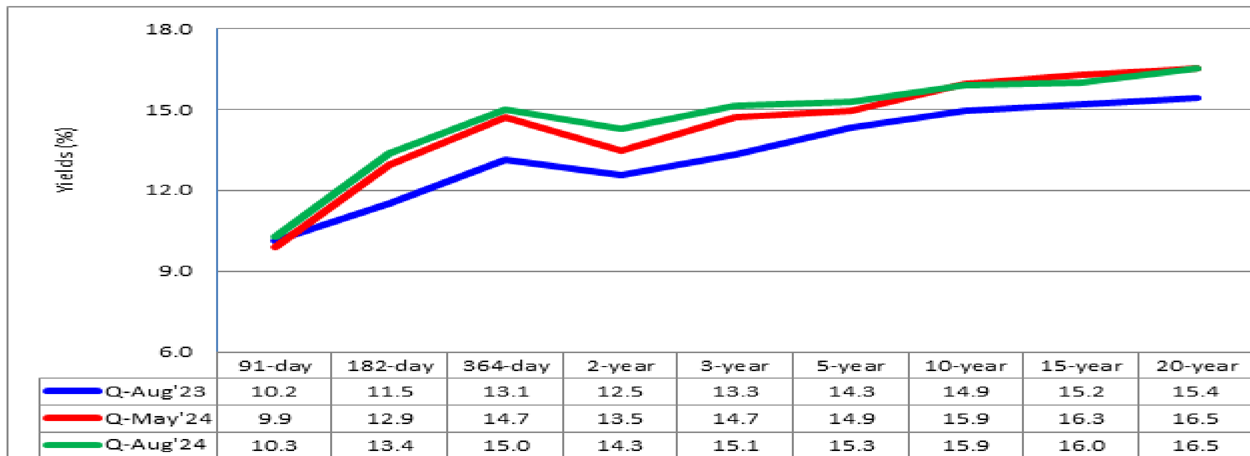
2.1.2 Primary market for treasury securities

In the three months to July 2024, yields on treasury securities showed mixed movements across various tenors compared to the three months to May 2024. The yield on the 2-year bond increased from 13.75 percent to 15.25 percent, and the 3-year bond yield rose from 15.00 percent to 15.38 percent. The 5-year bond yield remained unchanged at 15.50 percent. However, yields on longer tenors slightly declined; the 10-year bond yield decreased from 16.00 percent to 15.75 percent, the 15-year bond yield dropped from 16.50 percent to 15.80 percent, while the 20-year bond yield remained stable at 16.75 percent.

2.1.3 Secondary market for treasury securities

Yields on the treasury securities in the secondary market also rose for securities with short to medium term maturities in August 2024. The yields on the long-dated securities (i.e., 10 years and above) remained more or less the same with those recorded in May 2024 despite policy rate cuts as global financial conditions remained tight (**Figure 5**).

Figure 5: Secondary market annualized yields on t-bills and t-bonds (Average for the quarters)



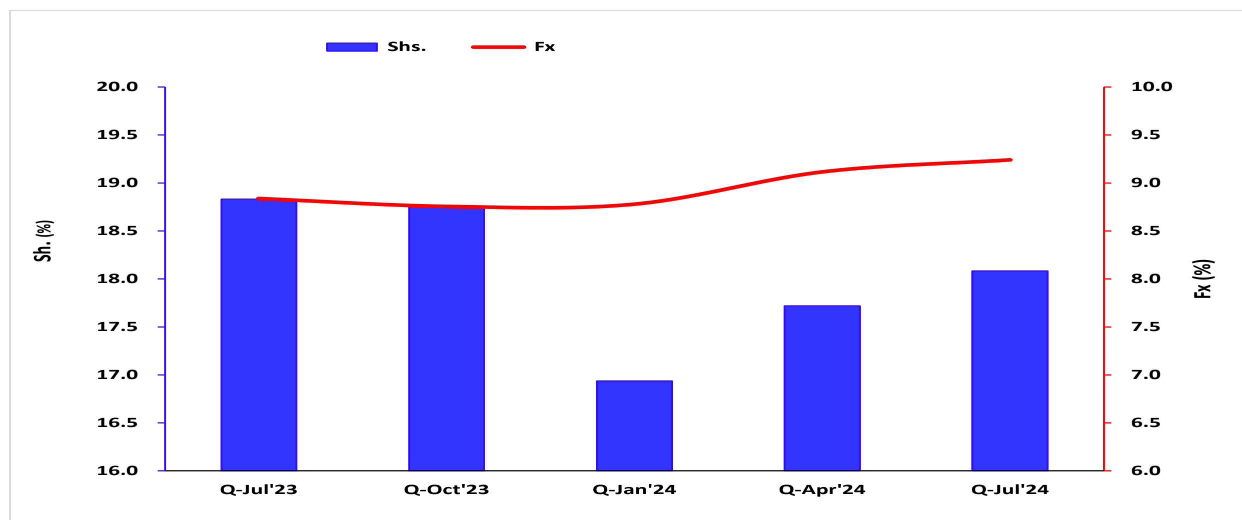
	91-day	182-day	364-day	2-year	3-year	5-year	10-year	15-year	20-year
Q-Aug'23	10.2	11.5	13.1	12.5	13.3	14.3	14.9	15.2	15.4
Q-May'24	9.9	12.9	14.7	13.5	14.7	14.9	15.9	16.3	16.5
Q-Aug'24	10.3	13.4	15.0	14.3	15.1	15.3	15.9	16.0	16.5

Source: Bank of Uganda

2.1.4 Lending interest rates

The weighted average shilling lending rate rose in the three months to July 2024 to 18.0 percent from 17.7 percent in the three months to April 2024. Over the same period, the lending rate on foreign currency-denominated loans also rose slightly to average 9.2 percent from 9.1 percent (**Figure 6**). The rise in the lending rates was partly attributed to a series of previous tightening cycles conducted by the MPC as well as increased private sector credit demand.

Figure 6: Quarterly Shilling and Foreign Currency weighted average lending rates



Source: Bank of Uganda

2.1.5 Private sector credit

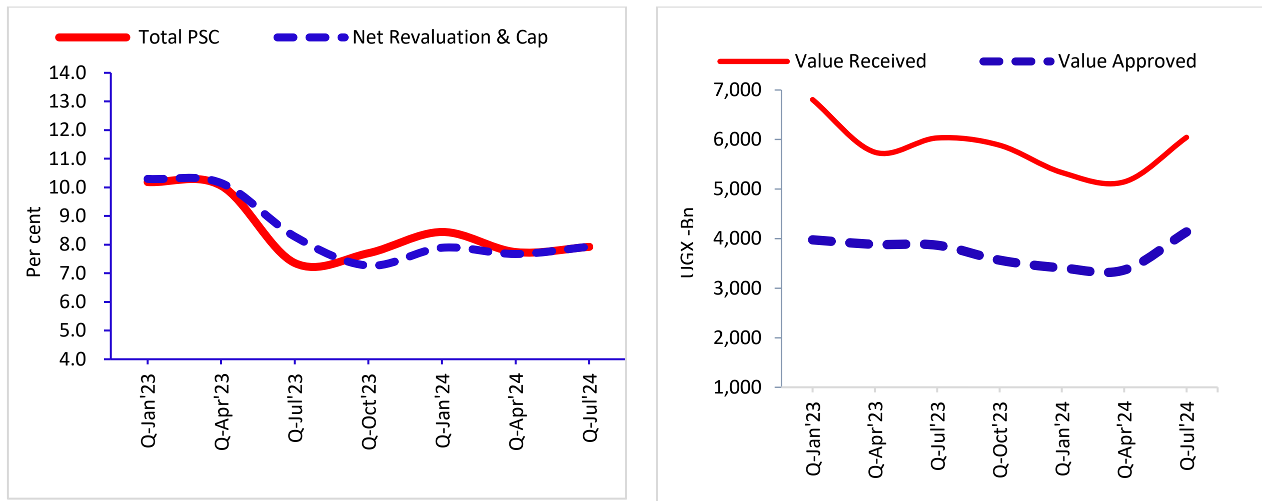
Private sector credit (PSC) growth remains sluggish, reflecting banks' preference for high-yield government securities, the lingering effects of the pandemic, and structural impediments to private loans. As Covid-19-related asset quality problems in banks dissipate and financial market reforms and fiscal consolidation advance, credit growth should pick up. Nonetheless, in the recent past, other depository corporations' private sector credit has shown signs of recovery, reflecting the positive economic outlook and a stable foreign exchange rate. Indeed, in the three months to July 2024, annual average PSC growth improved to 7.92 percent, up from 7.74 percent in the three months to April 2024. The growth in PSC is attributed to improvement in economic activity driven by the building, construction, and real estate, as well as the trade, manufacturing, and agriculture sectors.

Net of valuation and capitalised interest, PSC growth accelerated to 7.9 percent, up from 7.7 percent, reflecting pick-up in demand and increased confidence in the lending environment. Shilling-denominated loans grew at 9.42 percent, an improvement from 9.35 percent, while foreign currency-denominated loans saw a notable increase to 4.08 percent from 3.76 percent over the same period. This resurgence in credit growth, particularly in the local currency, signals a strengthening of the private sector that is poised to support economic growth.

The net credit extensions experienced a significant upturn in the three months to July 2024, reaching Shs.1.24 trillion, a substantial increase from Shs.277.41 billion in the three months to April 2024. This robust growth can be attributed to the BoU's recent monetary policy actions that have enhanced macroeconomic stability and improved liquidity conditions, providing loanable funds.

The demand and supply of credit have shown a marked improvement. Credit demand picked up in the three months to July 2024, reaching Shs.6.0 trillion, up from Shs.5.1 trillion in the three months to April 2024. This resurgence in demand is indicative of growing confidence in the economy. On the supply side, credit availability also increased, with supply rising to Shs.4.1 trillion in the three months to July 2024, compared to Shs.3.4 trillion in the three months to April 2024 (**Figure 7**). This upward trend partly reflects improved macroeconomic conditions.

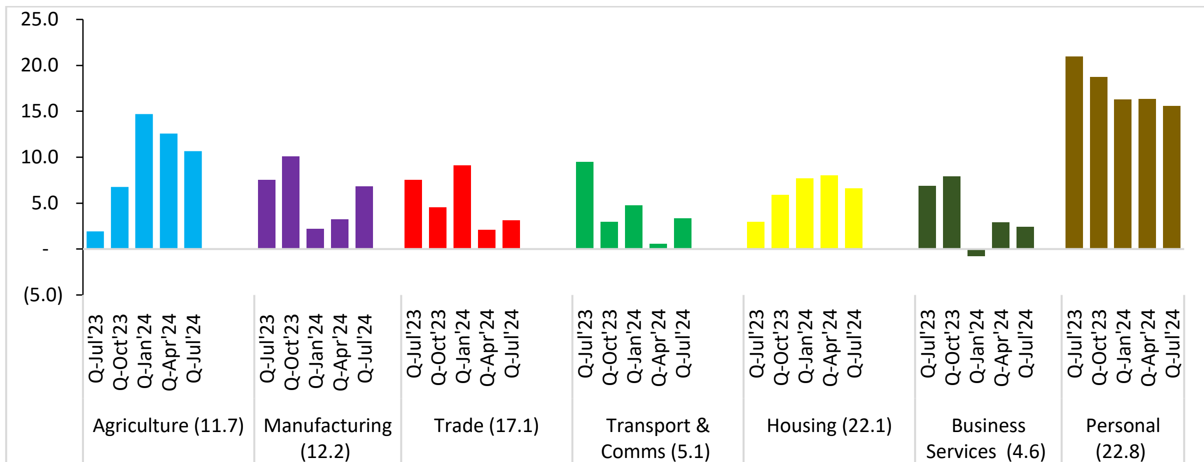
Figure 7: Private Sector Credit Growth (y-o-y, %, Left) and Loans applications (Shs., billion, Right)



Source: Bank of Uganda

Credit growth showed improvement across some major economic sectors, notably manufacturing, trade, transport, and communications (**Figure 8**). The main contributors to the growth in manufacturing were a pick-up in advances to firms producing building and construction materials, while for trade, it was wholesale and retail services. For the transport and communication sector, it was advances to water and air transport.

Figure 8: Sectoral PSC Growth (y-o-y, %, sectoral shares in brackets)



Source: Bank of Uganda

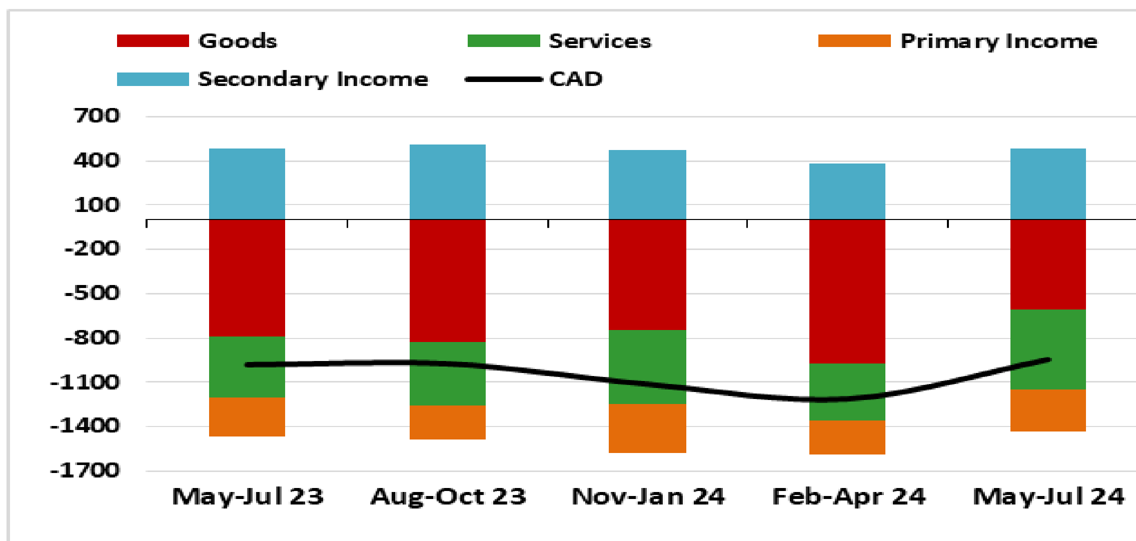
2.2 Balance of payments and exchange rates

2.2.1 Balance of payments

The balance of payments (BOP) recorded a deficit of US$ 711.0 million in the three months to July 2024, in contrast to the surplus of US$ 63.6 million in the three months to April 2024. It recorded a surplus of US$ 410.9 million in a similar period in 2023. The decline in the BOP position was mainly due to low inflows into the financial account despite improvements in the current and capital accounts. This shift highlights the need for strategies to boost financial inflows to stabilise the BOP.

The current account balance improved, registering a lower deficit of US$ 944.9 million in the three months to July 2024, which was 22.0 percent lower than the US$ 1,210.7 million deficit in the three months to April 2024, largely due to improvements in all sub-accounts except the services and primary income accounts. The goods deficit narrowed by US$363 million to US$ 609.8 million in the three months to July 2024, partly due to the expansion in the export receipts from coffee and gold. Similarly, the secondary income surplus improved mainly on account of an increase in personal transfers. However, the primary income deficit deteriorated on account of an increase in debt service interest payments and the services account deficit widened on account of an increase in freight, construction and government service payments. The developments in the current account are depicted in **Figure 9**. These developments underscore the importance of boosting exports and personal transfers while managing debt service costs and service-related expenses to further improve the current account balance.

Figure 9: Current account its components



Source: Bank of Uganda

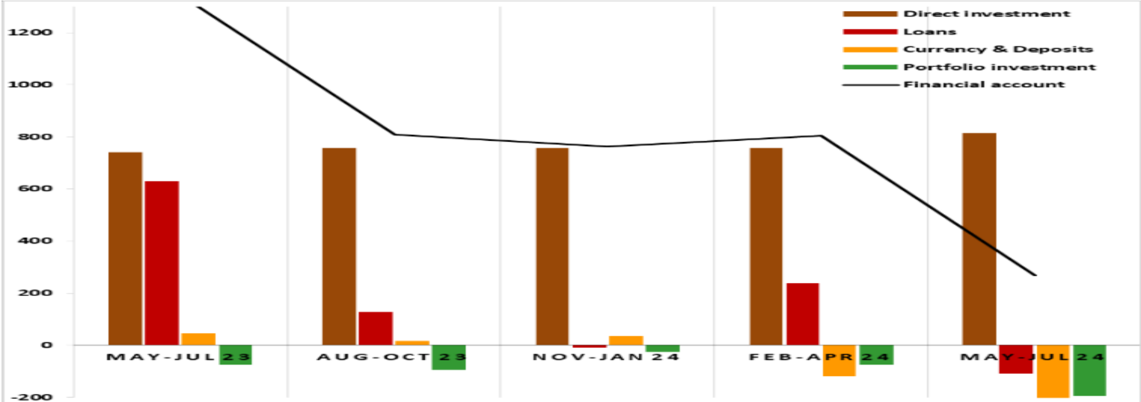
Over the same period, the capital account surplus increased to US$ 51.8 million from US$ 30.7 million in the quarter to April 2024. However, the financial account balance declined from a surplus of US$ 805.1 million in the quarter to April 2024 to US$ 268.4 million in the quarter to July 2024. FDI inflows remained robust and increased by US$ 55.3 million to US$ 813.7 million in the three months to July 2024, mainly on account of investment in the oil sector. Despite strong FDI inflows, other financial flows weakened substantially and weighed on forex reserves. While net foreign direct investment (FDI) inflows have been strong since 2021, mainly reflecting oil-related investments, net portfolio and other investment inflows have been weak and volatile, as experienced elsewhere in the region, reflecting less favourable global financial conditions. Net other investment inflows have seen a significant decline in recent years from a peak of US$ 500 million in FY2019/20 to around US$ 200 million in FY2023/24 as external project and budget support inflows fell. Despite strong oil-related FDI, Uganda faces challenges with volatile financial inflows and reduced external support, impacting overall financial stability.

Similarly, in the three months to July 2024, the portfolio investment account deteriorated with net outflows of US$194.0 million, an increase from a net outflow of US$75.6 million in the quarter to April 2024. This was largely attributed to offshore investment outflows on domestic debt securities. The other investment account also recorded net outflows of US$352.7 million in the quarter to July 2024, a turnaround from net inflows of US$120.9 million registered in the quarter to April 2024, as banks increased their placements of deposits abroad and a decrease in both budget

and project support loans. These trends highlight Uganda's challenges with capital outflows and reduced external financial support, which could impact economic stability.

These developments in the financial account are primarily reflected in a combination of factors, including offshore exits, high debt service payments and constrained donor support inflows. On the upside, however, FDI inflows remained robust to support the surpluses registered during the reporting quarters. Overall, while robust FDI inflows provide some stability, addressing the issues of capital flight, debt service, and donor support is crucial for maintaining financial health. The developments in the financial account are depicted in **Figure 10**.

Figure 10: Financial Account flows (US$ million)



Source: Bank of Uganda

The developments in the BOP resulted in a drawdown in reserve assets. The estimated stock of reserves as of the end of July 2024 was US$ 3,323.4 million (equivalent to 3.0 months of future import cover, excluding oil project-related imports). This was lower than the US$ 3,467.5 million (3.2 months of imports excluding oil project imports) registered at the end of April 2024 and US$3.7 billion in December 2023, with coverage of imports at 3.0 months (excluding oil projects), reflecting higher external debt service payments, inability to secure external loans at affordable terms, and limited forex purchase. This reduction in reserve assets underscores the need for improved public debt management and strategies to enhance foreign exchange inflows. The BoU has taken measures to build foreign exchange reserves in the short term. Indeed, the BoU utilised foreign exchange swaps/cross currency repos in 2024 with no impact on the exchange rate. Additionally, the Bank plans to purchase gold to diversify its composition of reserve assets, an approach which does not directly affect the foreign exchange market.

2.2.2 Balance of payments outlook

In the short term, the current account deficit (CAD) is projected to be supported by increased export revenues from in-season agricultural commodities such as coffee and cocoa due to increased volumes and prices. These agricultural commodities are experiencing increased production due to favourable weather conditions. The downside risk to the CAD is likely to arise from the increase in global oil prices on account of lower OPEC+ production and the Middle East tensions. The rise in oil prices might feed into the cost of other imported commodities, which could adversely raise the import bills. The primary income account is likely to deteriorate further due to payments of interest on public debt. The outflows in the income accounts could put depreciation pressures on the Uganda shillings' exchange rate. Managing the current account deficit will require continued efforts to increase agricultural export revenues given the risks posed by rising global oil prices and higher interest payments on public debt.

In the medium term, developments in the domestic oil sector will probably drive the direction of the current and financial accounts, with a worsening of the current account as the import bill widens this year to accommodate the oil project-related infrastructural developments. However, as oil exports pick up, the current account will improve in the medium term. The financial account surplus is expected to widen as foreign investment in the oil sector increases towards the target date for oil production. In other words, in 2 – 3 years, while the current account may worsen initially due to higher imports for oil infrastructure, it is expected to improve as oil exports increase, and the financial account surplus will likely grow with rising foreign investment in the oil sector. The BOP projections are depicted in **Table 2**.

Table 2: BOP Medium Term Projections

BOP Accounts	FY2024/25		FY2025/26		FY2026/27		FY2027/28	
	US$bn	%GDP	US$bn	%GDP	US$bn	%GDP	US$bn	%GDP
Current Account	**-4.1**	**-7.1%**	**-3.2**	**-5.1%**	**-2.5**	**-3.5%**	**-0.3**	**-0.4%**
Trade balance	-3.4	-6.0%	-2.7	-4.2%	-2.1	-3.0%	-0.5	-0.7%
Services	-1.6	-2.8%	-1.5	-2.3%	-1.3	-1.9%	-0.8	-1.1%
Primaary income	-1.1	-1.9%	-1.1	-1.8%	-1.2	-1.7%	-1.2	-1.5%
Seconadry income	2.0	3.5%	2.1	3.2%	2.1	3.0%	2.2	2.9%
Capital account	**0.2**	**0.4%**	**0.3**	**0.5%**	**0.3**	**0.4%**	**0.3**	**0.4%**
Current and Capital Account*	**-3.9**	**-6.7%**	**-2.9**	**-4.6%**	**-2.2**	**-3.1%**	**0.0**	**-0.1%**
Financial Account*	**3.8**	**6.6%**	**3.3**	**5.1%**	**3.6**	**5.1%**	**2.8**	**3.7%**
FDI*	3.7	6.4%	3.1	4.9%	2.8	3.9%	2.6	3.3%
Portfolio investment*	-0.1	-0.1%	-0.1	-0.2%	-0.1	-0.2%	-0.2	-0.2%
Other investment*	0.2	0.4%	0.3	0.4%	1.0	1.4%	0.4	0.5%
Overall Balance	**0.1**	**0.2%**	**0.5**	**0.8%**	**1.2**	**1.6%**	**1.9**	**2.5%**

**Sign inverted to reflect direction of flows*

Source: Bank of Uganda

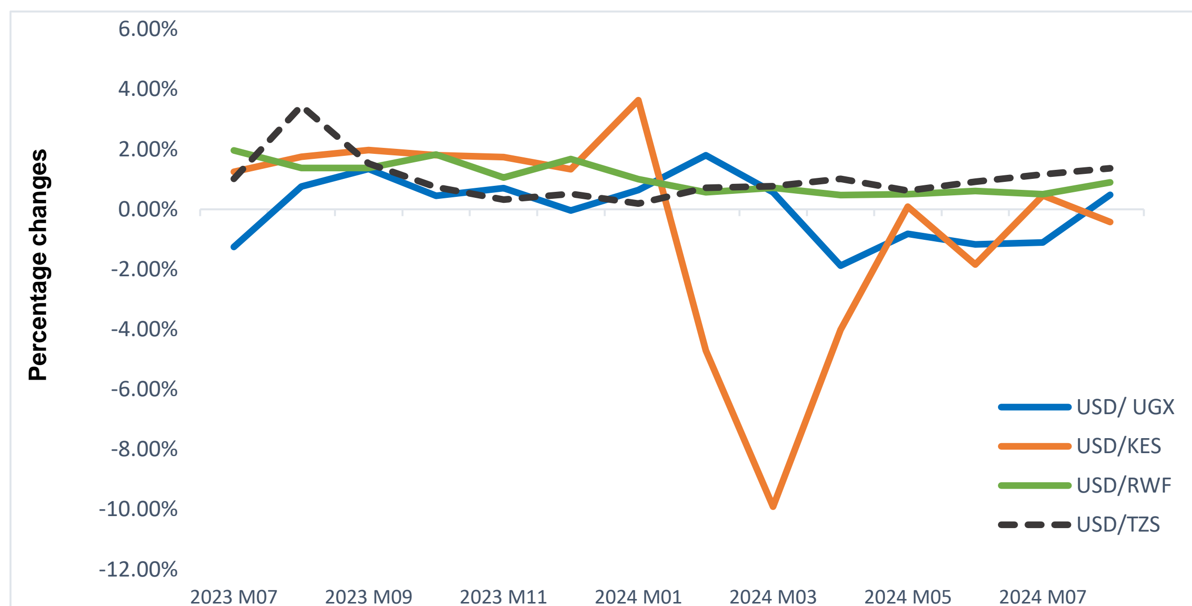
2.2.3 Exchange rates

The Ugandan shilling has generally maintained relative stability against the US dollar, with gradual appreciation since March 2024. The stability has partly been due to increased inflows from export revenues, particularly coffee, despite the strong demand from corporates to finance imports and other obligations, and partly the tight monetary policy, which has moderated the outflow of portfolio capital. However, in August 2024, the shilling depreciated by 0.48 percent month on month and by 0.94 percent year on year to an average mid-rate of Shs. 3,723.65/ US$. The shilling, which had been relatively strong since the early months of 2024, began to experience some depreciation pressures towards the end of July 2024 as banks sought to cover their short dollar positions. In addition, demand from the manufacturing, oil and telecom sectors caused some shilling depreciation. However, by the end of August 2024, the shilling had stabilised due to inflows from NGOs, coffee export receipts, and offshore inflows.

The nominal effective exchange rate (NEER), a trade-weighted index of a basket of currencies, depreciated by 1.2 percent month-on-month in August 2024, a reversal from the 1.1 percentage appreciation in July 2024. On an annual basis, the NEER depreciated by 1.5 percent in August 2024, further from the slight 0.1 percent deprecation recorded in July 2024.

In the EAC region, the Uganda shilling remains quite stable, similar to the Tanzania shilling and Rwanda franc. However, Kenya faced high depreciation pressures as the country sought funds to repay the maturing Eurobond at the beginning of 2024, and the Kenya shilling has since stabilised. The Kenyan shilling reversed its trends and appreciated by 9.9 percent month on month in March 2024 following the issuance of a new Eurobond to repay its inaugural bond but remained slightly depreciated. The Rwandan franc and Tanzanian shilling exhibited relative stability in the last four quarters. **Figure 11** depicts monthly exchange rate developments for selected currencies in the EAC region.

Figure 11: Monthly percentage change of selected EAC currencies against the US dollar



Source: Bank of Uganda

2.3Fiscal policy

2.3.1 Government expenditure and revenue

The FY2023/24 fiscal deficit is estimated at 4.8 percent of GDP, compared to 5.5 percent in FY2022/23 but higher than what was initially projected at 3.8 percent. The higher-than-projected deficit is due to (i) revenue underperformance and (ii) higher current spending. In FY2024/25, the overall fiscal deficit is projected to widen to 5.8 percent of GDP. The widening largely reflects a sizable increase in interest payments on domestic debt. Nevertheless, the government is commitment to pay the maturing securities in FY2024/25 and they are expected to securitize the stock of unreimbursed government securities as at June 2024 redeemed by BoU.

The data for the first month of FY2024/25 indicates that fiscal operations were contractionary relative to the first month of FY 2023/24; revenue collections surpassed the target while expenditures were contained below budget **(Table 3).**

The total revenue, including grants, amounted to Shs. 2,233.73 billion, Shs. 52.2 billion above the target, and 18.2 percent higher than a similar period in FY2023/24 due largely to the strong performance of tax revenue collections. The project support grants disbursement was Shs. 62.0

billion below budget estimates, which was also 36.5 percent lower than the receipt when compared with the inflows July 2023. Total expenditure in July 2024 amounted to Shs. 2,198.5 billion, Shs. 648.1 billion lower than planned, mainly due to Shs.213.4 billion and Shs.209.8 billion underperformance in compensation of employees and purchase of goods and services, respectively. These developments in fiscal operations resulted in a fiscal deficit of Shs. 30.0 billion, which was lower than planned, by Shs. 945.6 billion. This was largely due to the shortfalls in government expenditure and was mainly financed from domestic sources.

Table 3: Fiscal operations (Shs., billions)

	Jul-23	Jul-24	Prog.Jul-24	Variation	Annual (%)
Revenue	**1,890.09**	**2,233.73**	**2,181.5**	**52.2**	**18.2**
Taxes	1,734.66	2,102.71	1,978.4	124.3	21.2
Grants -Project Support	19.04	12.10	74.1	-62	-36.5
Other revenue	136.39	118.92	129	-10.1	-12.8
Expenses	**1,864.47**	**2,198.50**	**2,846.6**	**-648.1**	**17.9**
Compensation of employees	279.66	337.69	551.1	-213.4	20.8
Purchase of goods and services	216.42	222.58	432.3	-209.8	2.8
Interest Payments	644.29	816.05	841.2	-25.1	26.7
Domestic	449.20	597.00	597	0	32.9
External	195.00	219.10	244.2	-25.1	12.3
Grants	680.06	759.75	768	-8.2	11.7
Social benefits	15.68	22.69	21.5	1.2	44.7
Other expense	28.03	39.74	232.5	-192.8	41.8
Gross operating balance	**25.96**	**35.23**	**-665.1**	**700.3**	**35.7**
Net Acquisition of Nonfinancial Assets	62.21	65.18	310.4	-245.3	4.8
Net lending / borrowing	(36.59)	(29.95)	-975.5	945.6	-17.4
Transactions in financial Assets and Liabilities (Net)	(36.59)	(29.95)			-17.4
Net acquisition of financial assets	(1,660.57)	(542.11)			-67.4
Domestic	(1,660.57)	(542.11)			-67.4
Foreign	-	-			0
Net incurrence of liabilities	(2,520.96)	1,065.87			-142.3
Domestic	(2,209.06)	1,471.02			-166.6
Foreign	(311.90)	(405.16)			29.9
Errors and Omissions	(896.97)	1,578.03			-276

Source: Ministry of Finance Planning and Economic Development

In the first month of the financial year, relative to the Uganda Revenue Authority (URA) targets, the outturns for net tax and non-tax revenue (NTR) collections for July 2024 amounted to Shs. 2,221.6 billion, of which net URA tax revenue amounted to Shs. 2,102.7 billion, and NTR amounted to Shs. 118.9 billion, corresponding to an overperformance of Shs.124.3 billion and a shortfall of Shs.10.1 billion, respectively **(Table 4).**

The overperformance in net URA tax collection was largely attributed to higher international trade and direct domestic tax collections. Indirect tax collections, on the other hand, underperformed by Shs. 13.3 billion, largely because of lower collections in VAT on manufactured goods.

Direct taxes overperformed by Shs. 36.7 billion due to an overperformance of Shs. 31.6 billion in withholding tax collections. International trade taxes overperformed by Shs. 33.9 billion on account of the higher-than-target collections of import duty. On an annual basis, total net tax revenue registered a growth of 17.5 percent in July 2024 compared to 8.4 percent growth in the previous year while NTR declined by 23.7 percent in the period compared to an increment of 31.4 percent in the previous year.

Table 4:Revenue performance (billion shillings)

	Jul-22	Jul-23	Jul-24	URA Target Jul-24	Jul-24 Variation from Target	Annual change 2022/23-2023/4 (%)	Annual change 2023/24-2024/25 (%)
Total Net Tax & Non-Tax Revenue	**1,743.90**	**1,890.50**	**2,221.60**	**2,107.40**	**114.20**	**8.4**	**17.5**
Net URA tax revenue (excl. Refunds)	**1,625.30**	**1,734.70**	**2,102.70**	**1,978.40**	**124.30**	**6.7**	**21.2**
Direct Domestic Taxes	472.90	537.40	686.70	650.00	36.7	13.6	27.8
o/w PAYE	231.70	288.90	327.30	329.90	-2.6	24.7	13.3
o/w Corporate tax	47.7	30.30	48.60	48.30	0.4	-36.5	60.7
o/w Withholding tax	98.7	106.30	172.30	140.60	31.6	7.7	62.1
Indirect Domestic Taxes	390.70	506.70	544.10	557.40	-13.3	29.7	7.4
o/w Excise duty	142.10	163.80	184.40	180.50	4	15.3	12.6
o/w VAT	248.60	342.90	359.60	376.90	-17.3	37.9	4.9
Taxes on international Trade	756.00	733.60	862.10	828.20	33.90	-3	17.5
Stamp duty & Embossing Fees	8.7	10.1	9.9	9.9	0	16.5	-1.7
Non-Tax Revenue	118.60	155.80	118.90	129.00	-10.1	31.4	-23.7
Tax refunds	-3	-53.1	-0.1	-67.1	67	1696.2	-99.9

Source: Ministry of Finance Planning and Economic Development

Domestic revenue exhibited strong performance in July 2024, supported by the modest increase in tax measures, coupled with enhanced tax administration, rationalisation of tax exemptions, and a positive economic outlook for FY 2024/25. The downside risks to the revenue outlook include challenges related to compliance with the Electronic Fiscal Receipting and Invoicing Solution

(EFRIS) in tax administration, weak demand, and disruptions of trade flows arising from the effects of global geopolitical tensions.

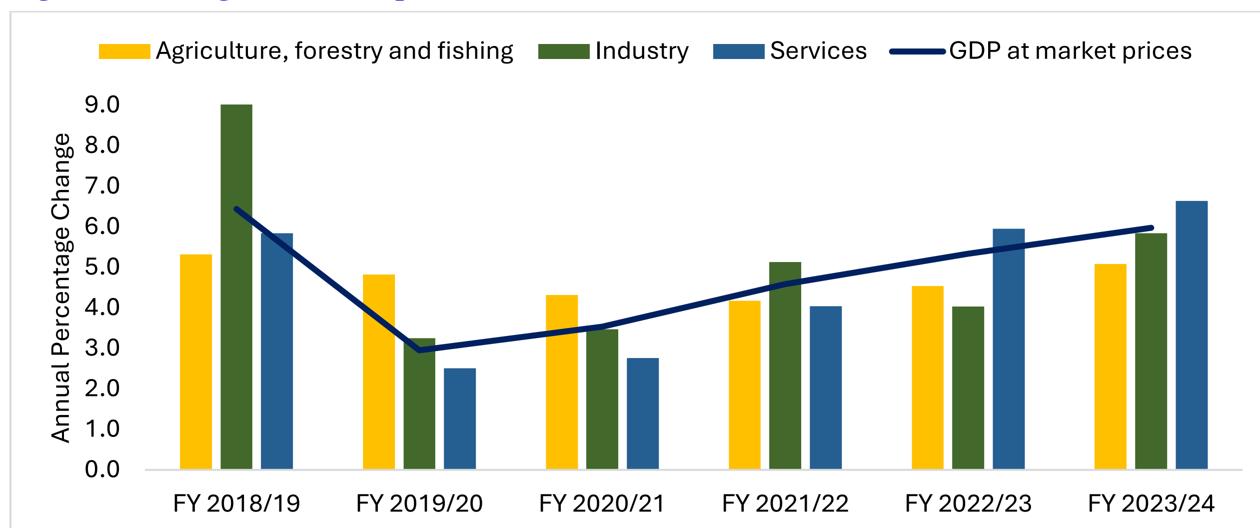
Uganda's public debt is considered sustainable, with a moderate risk of debt distress. Public debt, as a share of GDP, is expected to remain at about 50 percent of GDP over the medium term. The Debt Sustainability Analysis indicates that the external debt burden and public debt indicators remain below their respective thresholds and benchmarks under the baseline scenario. The stress tests suggest breaches of the thresholds, indicating a moderate risk of overall and external debt distress. Therefore, while Uganda's current debt levels are sustainable under normal conditions, the moderate risk of debt distress under stress scenarios underscores the need for prudent fiscal management and contingency planning to mitigate potential vulnerabilities.

2.4. Domestic economic activity

The domestic economy remains resilient. Preliminary estimates from the Uganda Bureau of Statistics (UBOS) indicate that real gross domestic product (GDP) growth increased to 6.0 percent, in FY2023/24, up from 5.3 percent registered in the previous year (**Figure 12**). Growth was driven by robust domestic demand, favourable weather conditions, subdued inflation, and the positive impact of the roll-out of the Parish Development Model (PDM).

In the reporting period, the services sector expanded by 6.6 percent, an improvement from the 5.9 percent increase in the preceding period. A resurgence in trade and real estate operations largely fuelled the growth in the services sector. The industrial sector also saw a notable rise, growing by 5.8 percent compared to the 4.0 percent growth previously, with manufacturing and construction activities contributing significantly to this uptick. The agricultural sector's growth accelerated to 5.1 percent, up from 4.5 percent, with the expansion being robust in the cash crops and livestock subsectors, which saw increases of 7.6 percent and 7.9 percent, respectively.

Figure 12: GDP growth decomposition



Source: Uganda Bureau of Statistics (UBOS)

Growth in economic activity also improved, as signaled by the composite index of economic activity (CIEA), a high-frequency indicator of economic activity produced by BoU. Indeed, in the 12 months to July 2024, growth in the CIEA stood at 5.6 percent, higher than growth of 5.2 percent registered a year ago. The improvement in the CIEA was attributed to the growth in the sectors.

Similarly, the IHS Markit purchasing managers index (PMI) improved to 56.3 in August 2024 from 53.7 in the previous month, indicating improved business conditions for the private sector and further increases in output and new orders. This is in line with the business tendency index (BTI), which increased to 59.7 points from 59.2 points in July 2024 on account of a stronger assessment of the current situation, which more than offset a decline in optimism for the near term. The near-term outlook for businesses indicates optimism.

In general, economic growth performance and outlook are optimistic. Uganda's economy is projected to grow from 6.0 to 6.5 percent in FY2024/25 and over 7.0 percent in the medium term, supported by stronger private sector investment, government intervention, especially in agriculture and the continued recovery of the global economy. Risks to the growth outlook are balanced with downside risk emanating from possible further weakening of private sector credit growth due to tighter domestic and external financing conditions, resulting in lower demand, a weakening of the global economy on account of sustained geopolitical conflicts, supply chain disruptions, higher freight costs, and adverse climatic condition. Growth could be boosted, on the upside, by increased investment in the extractive industry, expected oil exports in FY 2025/26, good weather for crop production, and strong demand and prices for exports.

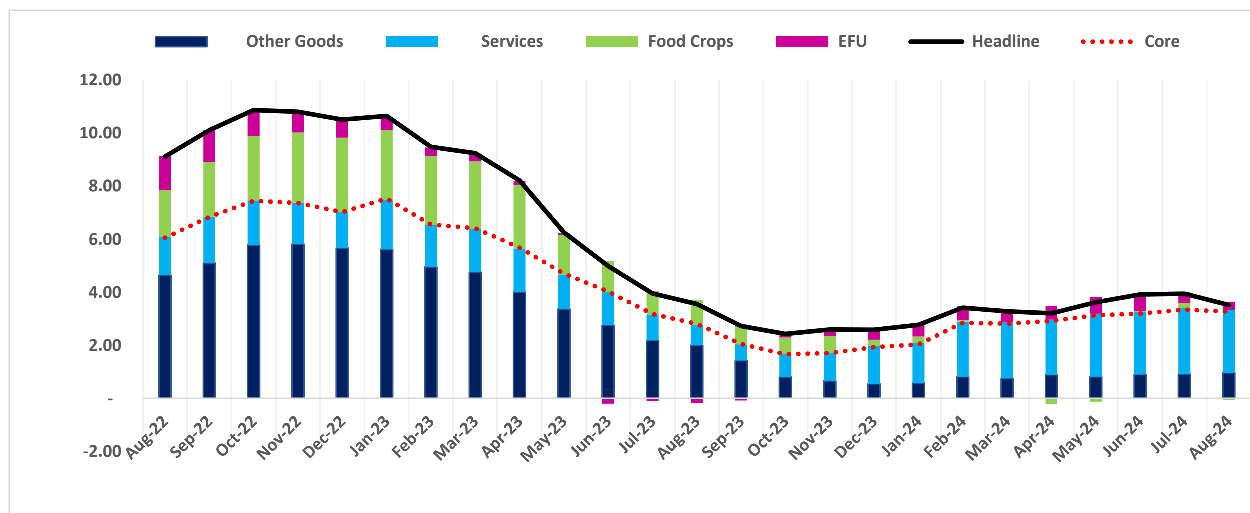
2.5 Domestic Inflation and Outlook

2.5.1Domestic Inflation

Inflation remains below the target, with the average headline and core inflation decreasing from 4 percent in July 2024 to 3.5 percent and 3.9 percent, respectively, in August 2024 **(Figure 13).** This reduction in core inflation was primarily driven by a decrease in services inflation, which dropped to 6.2 percent in August 2024 from 6.5 percent in July 2024 primarily driven by reductions in the costs of transport, food and beverages, and financial services. Passenger transport and food & beverages inflation declined to 6.9 percent and 2.7 percent in August 2024 from respective rates of 8.2 percent and 3.8 percent in July 2024. Financial services also saw a reduction in inflation, falling from 5.0 percent in July to 4.3 percent in the previous month. On the other hand, other goods inflation rose marginally to 2.1 percent from 2.0 percent in the previous month, from 2.0 percent to 2.1 percent.

Non-core inflation saw a more pronounced decline, decreasing from 3.8 percent in July 2024 to 1.7 percent in August 2024. This was largely due to a significant reduction in the energy fuel and utilities (EFU) index, which fell to 4.7 percent from 6.2 percent over the same period, driven mainly by a decrease in prices of liquid fuels. The food crops and related items Index also experienced a substantial drop, falling to minus 0.6 percent in August 2024 from 2.0 percent in July 2024.

Figure 13: Domestic Inflation decomposition (y-o-y, %)



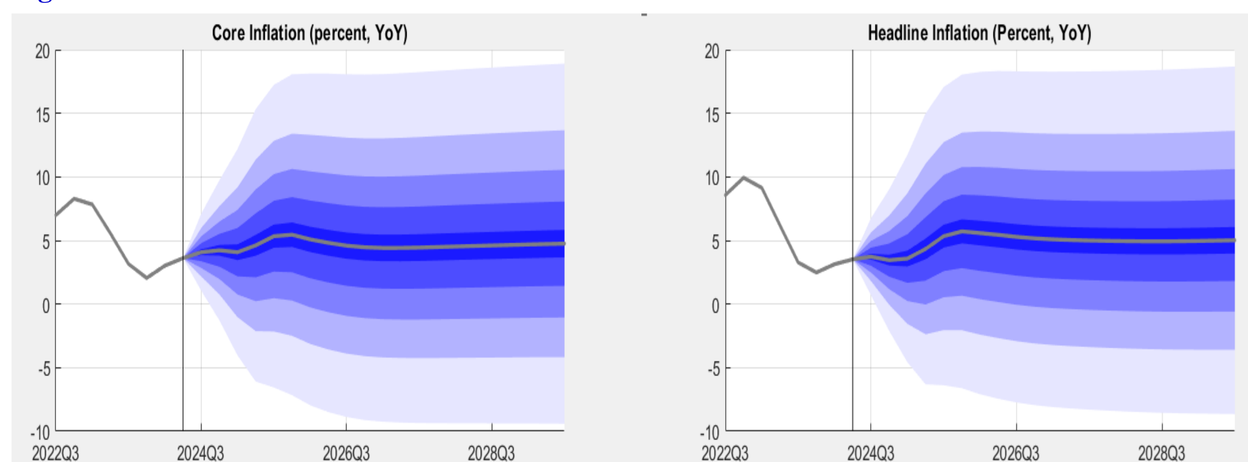
Source: UBOS

2.5.2 Inflation Outlook

The inflation projection has been revised slightly downwards relative to the June 2024 forecast round, largely due to a lesser depreciated shilling exchange rate. Headline and core inflation are projected to be 1.3 percentage points and 1.1 percentage points lower than the previous forecast round in FY 2024/25, respectively (**Figure 14**). Inflation is projected to be below the 5 percent target in FY 2024/25, broadly reflecting stable demand conditions, lower imported inflation, and exchange rate stability. However, inflation is expected to continue rising moderately in the next four months due to seasonal factors but is expected to stabilise around the target by the first quarter of 2025.

There are risks to the outlook. On the upside, inflation could be higher than projected if there is an increase in domestic growth due to increased investment in the extractive industries, unfavourable weather patterns that could affect food production, and a stronger-than-expected path for domestic demand. In addition, the signs of lingering inflation in other parts of the world and heightened volatility in capital flows and the exchange rate could result in stronger depreciation of the shilling exchange rate and, therefore, higher inflation than currently assumed. On the downside, inflation could be lower than the forecast due to an appreciation of the exchange rate following oil exports in FY 2025/26, lower domestic and global growth, and softer global inflation. The risks around the projection for inflation are judged to be balanced.

Figure 14: Baseline inflation forecast.



Source: Bank of Uganda

3. CONCLUSION

The global economy is projected to strengthen in 2024 and 2025. However, the major downside risk to this growth outlook emanates from geopolitical conflicts, adverse climatic conditions and trade tensions. This could be moderated by monetary policy easing by most central banks as the inflationary pressures abate. Indeed, the disinflation process continues into 2024, although the pace has waned, with inflation still above target in many countries. International commodity prices are expected to rise, driven by oil prices, precious metals and beverages, while food prices are likely to exhibit downward trends.

The domestic economy remains resilient with an optimistic near-term outlook driven by the recovery in domestic demand, private investment, government interventions, and strong external demand. Uganda's economy is projected to grow from 6.0 to 6.5 percent in FY2024/25, and over 7.0 percent in the medium term. The major risks to this growth outlook are likely to emanate from weak private sector credit growth, delayed investments in oil production, the effects of geopolitical conflicts on trade flows and freight costs, and adverse climatic conditions. These downside risks are likely to be moderated by investment in oil production activities, conducive weather conditions that support production, and favourable international prices.

Inflation remains below the target, with the average headline and core inflation decreasing from 4 percent in July 2024 to 3.5 percent and 3.9 percent, respectively, in August 2024. Given the relative stability of the exchange rate coupled with waning global inflation, core inflation is projected to remain below 5 percent in FY2025/25 but is expected to continue rising moderately in the next four months due to seasonal factors but stabilise around the target by the first quarter of 2025. There are, however, risks to these forecasts that are relatively balanced. On the upside, inflation could be higher than projected if there is an increase in domestic growth due to increased investment in the extractive industries, unfavourable weather patterns that could affect food production and a stronger-than-expected path for domestic demand. On the downside, inflation could be lower than the forecast due to an appreciation of the exchange rate following oil exports in FY 2025/26, lower domestic and global growth, and softer global inflation.

The short to medium term outlook is optimistic. The domestic economy remains resilient, and it is projected to grow above 7 percent in the medium term. Notably, Uganda's inflation remains muted given the stable exchange rate, but it is expected to gradually rise to the 5 percent target in 2025. The positive outlook for growth and the exchange rate is likely to improve business prospects and enhance the recovery in PSC growth. Similarly, the CAD is projected to improve in the medium

term as oil exports pick up. On the fiscal front, government remains committed to fiscal consolidation however the deficit is expected to initially rise due to interest payments and clearing of outstanding obligations before gradually declining in the medium term.

In view of the recent macroeconomic development and forecasts, the MPC assessed that although risks of higher inflation remain, the adverse impact from past external shocks has abated, and there has been some progress in moderating risks of inflation persistence. Therefore, the MPC noted that it was appropriate to reduce slightly the degree of monetary policy restrictiveness by reducing the CBR by 25 basis points to 10.0 percent.