BANK OF UGANDA

Statement by Prof. Emmanuel Tumusiime-Mutebile, Governor, Bank of Uganda

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I would like to say something about the significance of fiscal discipline in the country's growth and stability. Prudent management of public financing is very critical to macroeconomic stability. The Government has a medium term fiscal program which sets out clearly the path of revenues, expenditures and government borrowing for the next five years. The fiscal program is absolutely consistent with ensuring that public debt remains sustainable and that domestic borrowing will remain within levels which will not threaten to crowd out private sector borrowing. We will ensure that all Government borrowing is fully funded from the market by issuance of Government Securities through primary auctions. Therefore I want to state clearly that the Bank of Uganda fully endorses the Government's fiscal stance and absolutely has no problem with fiscal management.

Central Bank Rate

As you all know the Central Bank raised its Central Bank Rate (CBR) in September 2013 to 12% to avert the second effects of food prices but also to counter any rise in inflation expectations. Consequent upon the threat of high inflation being reduced, BoU reduced CBR 11.5 in December 2013 and further to 11 percent in June 2014. The annual core inflation rate has fallen in 2014 but is forecast to edge over 5 percent over the next 12 months due to exchange rate depreciation which has occurred in 2014 and early 2015 due to domestic demand. As a result of this, we have retained the CBR at 11 percent and we will watch carefully the next few weeks to see where things move.

Developments in the foreign exchange market

The shilling has been depreciating against the US dollar over the last few weeks. Since February 2014, the shilling has depreciated by about 14 percent against the US dollar. This followed sustained appreciation during 2013 and the first months of 2014. The depreciation of the exchange rate since February 2014 reflects several factors. First, there has been a correction of the exchange rate which had become over valued in 2013. Secondly there has been strong demand for foreign exchange from the real sectors of the economy especially manufacturing and oil sectors. Thirdly, there has been weakening of global sentiment towards emerging markets with the currencies of these markets coming under persistent depreciation. Finally, recently, the dollar has strengthened against the major currencies as a result of expectations that America will be the first among the industrialized countries to raise interest rates.

Financial Sector

The latest quarterly data available is for September 2014 and this indicates that the banking system is financially very sound and well capitalized. Asset quality has improved. The Non-Performing loan ratio has declined from 6.2 percent of the loans in March 2014 to 5.3 percent of the loans in September 2014. Banks' profitability has reduced partly as a result of loan provisioning and a slight drop in the net interest margin. The banks' total regulatory capital position remains very strong at 22.5 percent of risk weighted assets as at end of September 2014 which is almost double the statutory minimum of 12 percent. The banking systems' average return on assets and equity declined to 2.2 percent and 13.1 percent respectively in the year to September 2014 from 3.1 percent and 18.8 percent in the previous 12 months.

Private Sector credit

With regard to private sector credit growth, since the start of 2014, Private Sector credit has recovered with annual growth increasing to 13 percent as of end of September 2014. The building and construction sector, trade and household loans continued to account for the bulk of the PS credit. The three sectors together (building and construction sector, trade and household) accounted for over 55% of banking systems' outstanding credit to the Private Sector since February 2014. Annual growth of PS credit during 2014/15 is projected at 15 percent.