

## big story

# Tough economic year offers reality

**Uganda's Economy.** If 2011 was a tough year, 2012 could be worse. As economists peer into this year, there are questions as to whether the economy will go burst or remain afloat now that it is struggling to stabilize from the major blows of double digit inflation, a weakening shilling, global shocks, increased oil prices and the Eurozone's debt woes.

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**KAMPALA.** After the economy registered a slowdown in 2011 from about 6 per cent in June to 5 per cent by December, the government is now projecting that Uganda's economic growth rate will rebound to 7 per cent by the end of 2012, as a result of anticipated gradual stability in the macroeconomic environment.

Over the past 10 years, Uganda's economy has been one of the fastest growing regionally and internationally - growing by an average of 7 to 8 per cent, thanks especially to the services sector. But the global economic slowdown and its related problems have not spared Uganda.

#### Growth in 2011

In an interview with *Prosper* on December 22, Deputy Secretary to Treasury, Keith Muhakanizi said Uganda's economic growth slowed down in 2011 due to exogenous shocks arising from the global economic crisis especially in the Euro zone which is struggling with a debt crisis. He added that this was compounded by spiraling inflation rates which went beyond government policy of controlling it (inflation rate) at 5 per cent and the depreciating shilling. The shilling lost about 25 per cent of its value against the dollar between January and October 2011, trading between Shs2,800 and Shs2,900 per dollar in mid-September due to high dollar demand, volatile global oil prices and increased imports.

"It is being estimated that Uganda's economy growth rate slowed down to 5 per cent in 2011, lower than 7 per cent we had earlier projected at the beginning of the year. However, we expect the economy to rebound to a higher growth rate of 7 per cent in 2012 because of stability beginning to take place internally and internationally," he said.

#### Escalating inflation rates in two decades

"During 2011, Uganda's economy experienced the highest inflationary rates after more than two decades of low inflation below 6 per cent per annum. The increase in inflation rate to 30 per cent was caused by both external and internal factors. In 2011, the Ugandan shilling also experienced a drastic depreciation against the US dollar attributed to the difficult global economic environment," he explained.

Mr Muhakanizi added: "This development led to instabilities in Uganda's macroeconomic environment which resulted into a fall in investment confidence in the country. The rising inflation necessitated Bank of Uganda to tighten monetary policy."

By November 30 2011, Uganda's annual headline inflation rate which includes food crop items in the Consumer price Index closed at 29 per cent from the previous month high of 30.4 per cent, while the annual core inflation which excludes food crop items from the Consumer Price Index closed 30.6 per cent in November.

Some analysts have however blamed Uganda's economic woes on government's reckless spending and weak macro-economic governance. They have highlighted

among others, last year's controversial procurement of jet fighters at \$740million and the passing of a supplementary budget of over Shs600billion in the run-up to last year's presidential elections. Analysts say that these and other issues like massive corruption heavily contributed to the current instability in the economy.

Bank of Uganda Governor Emmanuel Tumusiime Mutebile last year complained to the UK's *Financial Times* about President Museveni's demands to have the Central Bank withdraw money from the country's reserves for the purchase of jet fighters. Some analysts perceived this to be an interference with the Central Bank's independence.

Following intense pressure from the public, BoU chose to institute a tight monetary policy which has started offering some signs of economic recovery. With things beginning to change from a negative outlook to a more positive one as inflation rate begins to fall and the shilling appreciating against the US dollar, Mr Muhakanizi said the economy is regaining its strength as far as GDP rate growth rate is concerned.

"Inflation is falling; the shilling has significantly appreciated against US dollar in the recent weeks. The investor confidence which had fallen has now picked up. This positive development is the reason we are projecting a rebound in growth rate to 7 per cent in 2012," Mr Muhakanizi forecasted.

Executive Director Research Functions at Bank of Uganda Dr Adam Mugume told *Prosper* that the Ugandan economy remained resilient despite bouts of both domestic and external shocks.

"After declining to 5.9 per cent in 2009/10, largely on the backdrop of the global economic crisis, the economy recovered in 2010/11, with real GDP growing by 6.7 per cent. This growth was registered despite the dismal performance of the agricultural sector, which was adversely affected by drought. Growth is however expected to be about 5 per cent in 2011/12," he said.

Dr Mugume explained that in the first and second quarter of 2011, GDP growth decelerated from 10.4 per cent in quarter four of 2010 to 7.4 per cent and 5.0 in quarter one and two of 2011, respectively.

#### Economy's measure of performance

On how Uganda's total GDP has been over the two years, Dr Mugume said in 2008/09 GDP at prices stood at 7.3 per cent, in 2009/10 at 5.9 per cent, in 2010/11 at 6.7 per cent and it is being anticipated to grow at 5 per cent in 2011/12.

Giving a break down on how the various sectors of the economy had performed over the same period as per the Bank of Uganda projections, Dr Mugume explained that agriculture, forestry and fishing grew by 2.9 per cent, 2.4 per cent, 0.7 per cent and 2.1 per cent. Industry grew by 5.8 per cent 6.5 per cent, 7.9 per cent and 5.5 per cent, whereas services grew by 8.8 per cent, 8.2 per cent, 8.4 per cent and 6.0 per cent respectively.

"Overall, the economy is likely to continue to grow in the next two years, but there are many pitfalls still to negotiate along what is likely to be a long and bumpy road to optimal economic growth," Dr. Mugume observed.

#### Eurozone woes' impact on economy

Senior Research Fellow (Public sector policy) at Economic Policy Research center, Dr Lawrence Bategeka told the *Prosper* that Uganda's economy registered achievements and challenges in 2011.

On the challenges Dr Bategeka said Uganda's economy was affected by the negative developments in global economy most especially in the Euro zone crisis (debt crisis) which caused external shocks on Uganda's economy during the year.

"Expectation on high economic growth started slackening in Uganda, when the Euro zone debt crisis intensified leading to decline in commodity exports from

Uganda to Europe. Locally the weather conditions in form of droughts affected food crop production hence resulting into supply constraints and subsequent high food prices domestically and the results of these negative developments was high inflation rates," he said.

"All these challenges caused volatilities in the real economy in form of price instability during 2011 and subsequently a slowdown in the GDP growth rate," he said.

On the positive achievements Dr Bategeka said the determination by the Bank of Uganda to execute tight monetary policy to bring down inflation has yielded some positive results because inflation is beginning to fall much as productivity is likely to suffer in the short and medium term.

The weakening of the local currency against the world's major currencies could have been a blessing in disguise as Ugandan exports would have been cheaper to buy, improving the country's balance of payments.

#### Private sector contributes to growth

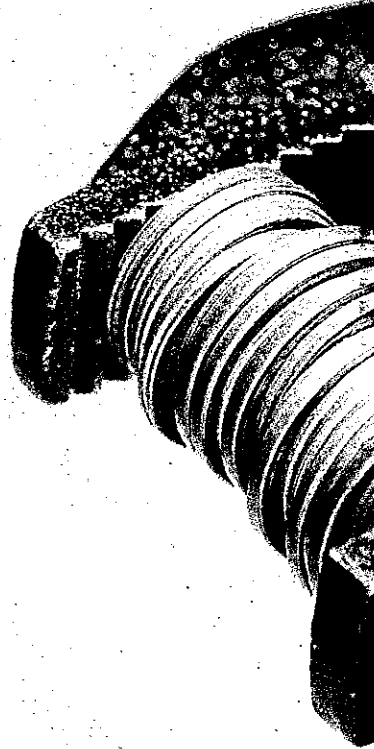
Uganda's economic growth has been supported over the years by the private sector led growth strategies policy.

The Executive Director of Private Sector Foundation Uganda, Mr Gideon Badagawa told the *Prosper* that the economic environment during the year was made harsh with the sharp depreciation of the shilling against US dollar in a situation where 60 per cent of manufacturing inputs used in production of goods in Uganda are imported from outside countries.

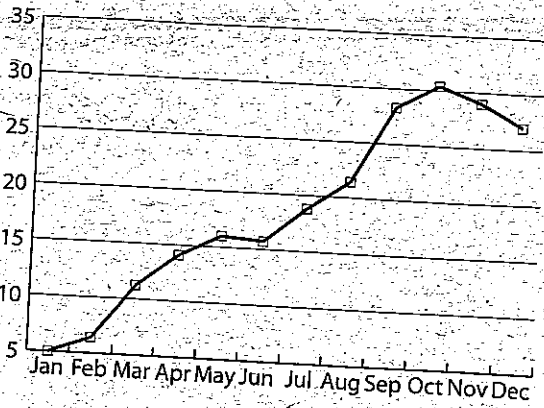
Mr Badagawa added that 2011 was made more challenging for the private sector in Uganda because of the high commercial lending rates instituted by commercial

#### REGIONAL INFLATION RATES

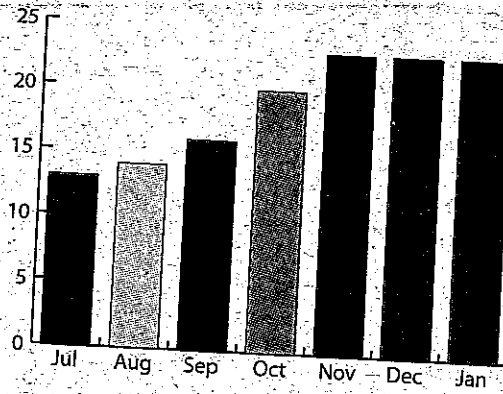
MONTHS	UGANDA	KENYA	TANZANIA
January	5	5.42	6.4
February	6.4	6.54	7.5
March	11.2	9.19	8
April	14.1	12.05	8.6
May	16	13	9.7
June	15.7	14.49	10.9
July	18.8	15.5	13
August	21.4	16.67	14.1
September	28.3	17.3	15.8
October	30.4	18.9	17.9
November	29	19.7	



## UGANDA'S ANNUAL INFLATION TRENDS



## CENTRAL BANK RATE TRENDS



banks following the tight monetary policy by the Bank of Uganda.

"The policy actions by the Bank of Uganda was necessary because it wanted to control inflation which was hurting the economy but they also affected the private sector in terms high credit cost that led slowdown in economic activities in the country during the year," he said.

However, by the end of last week, traders in and around Kampala were threatening to close their shops and withdraw money from banks unless government comes up to rescue them from crippling interest rates which they say are making doing business impossible.

Economists like Makerere University's Professor Augustus Nuwagaba have previously advised BoU to reconsider its tight monetary policy saying it is hurting inno-

cent borrowers, with some of them already losing their assets to commercial banks.

"They [Central Bank] need to find an appropriate policy but not this one - current tight monetary policy. High interest rates are likely to lead us into stagflation and recession," he said.

Given the intertwined nature of the global economic system and the heavy reliance on imports like oil, the factors that influenced Uganda's economy in 2011 are unlikely to change significantly in the short and medium term. However if government executes effective short term policy interventions to restore stability, there will be need to establish and strengthen policies that are meant shore up the country's balance of payments in order to cushion the country.