NATIONAL PLANNING AUTHORITY

MONTHLY ECONOMIC UPDATE

JANUARY 2021

Key Economic Highlights

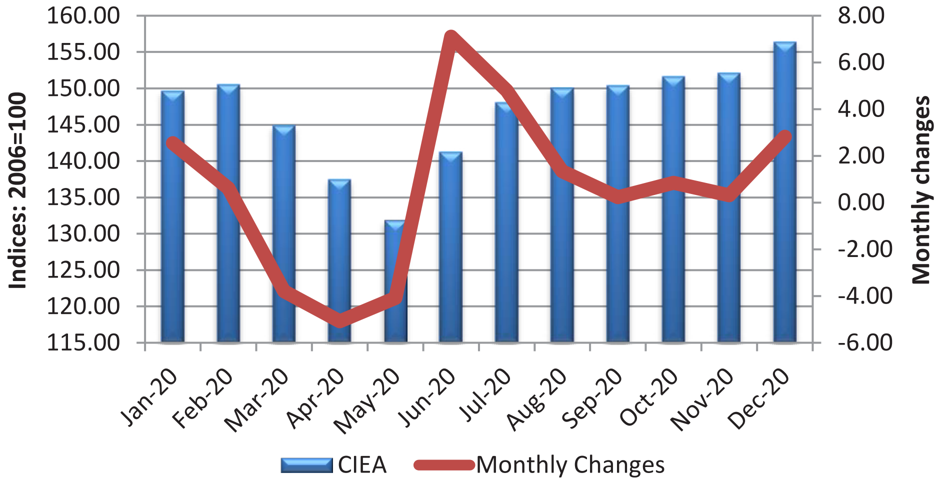
- Recovery in economic activity has gained momentum although not to the pre-pandemic levels. This is evidenced by the 2.82percent growth in the composite index of economic activity in December 2020 as compared to 0.31percent growth in November 2020.
- The risks to the economic outlook have somehow gradually eased since recovery in economic activity is evident. Growth is now projected to rise to 3.1 percent in FY 2020/21 and 4.3 percent in FY 2021/22 although all the projections are below the NDPIII's.
- Inflation remained subdued below the policy target of 5 percent in the year ending January 2021. However, upward inflationary pressures were recorded during this period, leading to a slight increase in inflation to 3.7 percent as compared to 3.6 percent during the year ending December 2020.
- The Uganda Shilling depreciated against the US Dollar in the month ending January 2021, trading at an average rate of UGX3,691 per USD as compared to UGX3,666 per USD in the month ending December 2020.
- The Government operations recorded a fiscal surplus of UGX382.7 billion in December 2020, attributed mainly to the lower than planned spending during this period. This is in addition to a surplus in Government receipts from grants and revenues as compared to the targets.
- The external position worsened in December 2020, with the trade deficit widening to USD 324.7 million from USD294.48 million in November 2020 as a result of a rising import bill that offset the gains from the increased export receipts during the same period.
- Nominal public sector debt remains sustainable, and is projected to increase from 41.0 percent of GDP in FY2019/20 to a peak of 54.1 percent of GDP in FY2022/23. On the other hand, the PV of public sector debt to GDP is projected to increase from 31.8 percent in FY2019/20 to a peak of 42.9 percent in FY2022/23.
- The high rate of accumulation of debt in the medium term has increased the risks and vulnerabilities associated with debt. Consequently, the country's risk rating was downgraded from low risk to moderate rate risk of debt distress.

1.0 State of the Economy

1.1 Real Sector

Recovery in economic activity has gained momentum although not to the pre-pandemic levels. For example, the composite index of economic activity (CIEA) grew by 2.82percent in December 2020 as compared to 0.31percent in November 2020 (see Fig 1) The continued increase in economic activity has been supported by Government's fiscal stimulus to support recovery as well as the accommodative monetary policy stance to shield private sector investment against the negative impacts of COVID-19. Nonetheless, the recovery in economic activity has been uneven, with some activities especially in the services sector like education, tourism and hospitality remaining constrained by the lock down measures in place as well as reduced demand for such services in fear of contraction of the corona Virus.

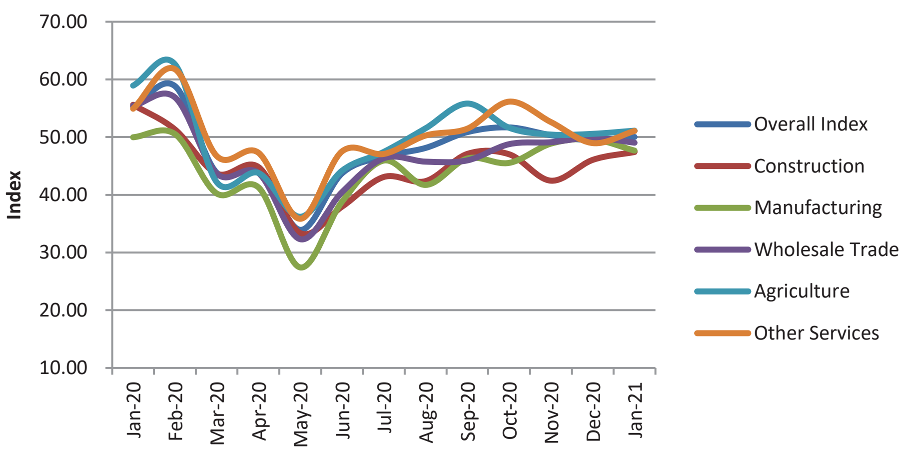
Figure 1: Composite Index of Economic Activity



Source: Bank of Uganda 2021

The Business Tendency Index1 (BTI) also points towards positive business expectations in the business environment, with the overall index rising above the 50-threshold mark in January 2021 from 49.43 in December 2020. However, positive business sentiments are only seen in the Agriculture and other services sectors with indices of 51.12 and 51.07 respectively. The Construction, Manufacturing and Wholesale Trade sectors still recorded negative expectations of economic activity (see Figure 2) owing to the fact that most of these sectors are still facing the lagged effects of the shutdown of the economy.

Figure 2: Business Tendency Indicators



Source: Bank of Uganda 2020

[1] BTI value of less than 50 implies negative expectations while value greater than 50 implies positive expectations

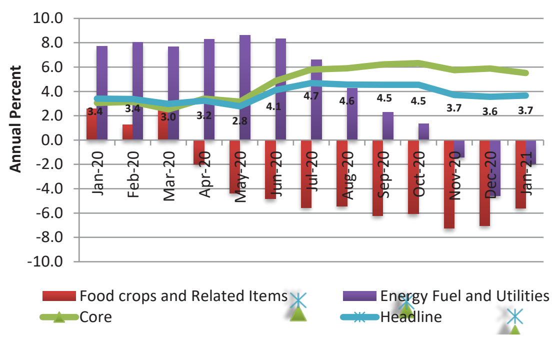
Generally, economic recovery is expected to be gradual, remaining below potential until FY 2023/24 (Bank of Uganda, 2021). In addition, risks to the economic outlook have somehow eased. This arose because of the expectations of recovery in economic activity sooner than anticipated both in the domestic and global economy owing to the discovery of the COVID-19 Vaccine. Consequently, growth is projected to rise to 3.1 percent in FY 2020/21 and 4.3 percent in FY 2021/22 (MoFPED, 2021). Nonetheless, risks to economic growth still exist, including the continued rise in COVID-19 infections, rising fiscal financing pressures, increasing non- performing loans and persistent high lending rates (Bank of Uganda, 2020).

1.2 Monetary Sector Developments

1.2.1. Inflation rate

Inflation remained subdued below the policy target of 5 percent in the year ending January 2021. However, upward inflationary pressures were recorded during this period, leading to an increase in inflation to 3.7 percent as compared to 3.6 percent during the year ending December 2020 (Figure 3). As a consequence, there have been slight increments in prices on items such as energy fuel and utility (EFU), food crops and related items. The prices of EFU items rose from minus 4.6 percent in the year ending December 2020 to minus 1.9 percent in the year ending January 2021 mainly due to the rise in prices of solid fuels, particularly charcoal. The food crop and related items inflation increased to minus 5.6 percent from minus 7 percent during the same period largely due to the higher prices of fruits like bananas. The rise in inflation has been driven by the general increase in aggregate demand resulting from the gradual economic recovery after the lifting of lockdown measures. However, core inflation declined to 5.5 percent in the year ending January 2021 as compared to 5.9 percent during the ending December 2020. The fall in prices was attributed to the fall in prices in the services sector, in particular, the road transport services most likely as a result of the drop in prices after the festive season. In the medium term, inflation is projected to converge to 5 percent (Bank of Uganda, 2020).However, there are risks to this forecast, including a rebound in world commodity prices as economies recover from the pandemic and increased food prices due to increased demand and shocks from bad weather conditions.

Figure 3: CPI and Inflation rates



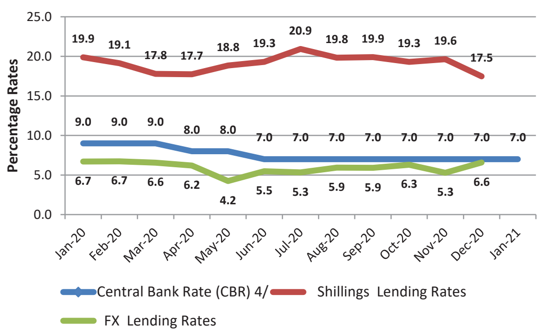
Source: Bank of Uganda

1.2.2. Interest Rates

To foster economic recovery as well as attain the 5 percent inflation medium term target, Bank of Uganda maintained the central bank rate at 7 percent in January 2021 (Figure 4). In December 2020, the shillings lending rate was reduced by 2.1 percentage points to 17.5 percent, which is the highest reduction in the lending rates that has been recorded since the outbreak of the pandemic in Uganda. Despite the efforts made by the central bank to reduce the central bank rate throughout the pandemic period, commercial banks have maintained relatively high lending rates. The Bank Lending survey conducted by the Bank of Uganda also indicates that most banks expect their lending rates to remain unchanged in the quarter ending

March 2021. The high lending rates have greatly stifled economic recovery, especially in terms of private investment and have contributed to the rising number of non-performing loans which are expected to even rise further in the next three months due to increased economic uncertainty (Bank of Uganda, 2020)

Figure 4: Interest Rates

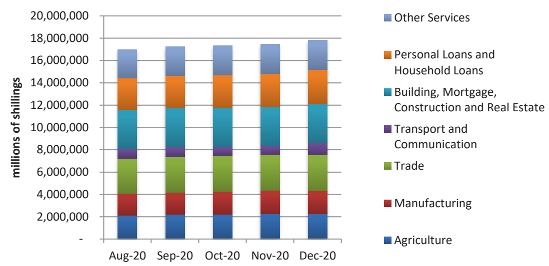


Source: BoU 2021

1.2.3. Private Sector Credit

The month of December 2020 was marked by a modest recovery in private sector credit, recording a higher monthly growth in private sector credit of 2.1 percent as compared to 0.8 in November 2020. The stock of outstanding credit at the end of December 2020 therefore increased to UGX 17,830,148.9 million. This was mainly attributed to the increased credit extended to the transport and communication sector during this period (Figure 5). During December 2020, the Building, Mortgage, Construction and Real Estate sector and trade sector received the largest proportion of credit, estimated at 19 percent and 18 percent respectively, whereas transport and communication (6%) and manufacturing sector (13%) which are part of the key sectors supposed to drive economic recovery received the least credit. Deliberate efforts should be made to increase access to credit in these key sectors. In the quarter ending March 2021, demand for credit is expected to increase but at a slow pace, mainly in the import sector owing to continued easing of trade restrictions all over the world.

Figure 5: Outstanding total lending in millions of Uganda shillings

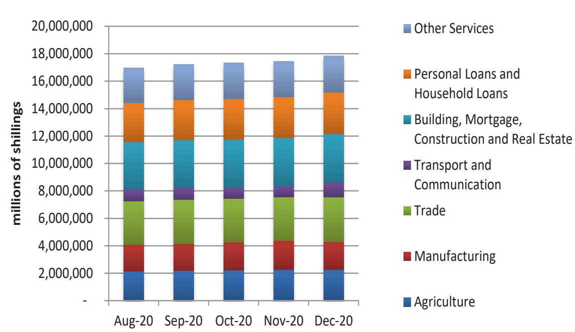


Source: Bank of Uganda

1.2.4. Exchange rate

The Uganda Shilling depreciated against the US Dollar in month ending January 2021, trading at an average rate of UGX3,691 per USD as compared to UGX3,666 per USD in the month ending December 2020 (see Figure 6). The pressure on the shilling was on account of increased demand of foreign currency as import activity rises following the easing of border restrictions by most countries. The exchange rate is likely to be stable in 2021 on account of the expected recovery in economic growth and trade following the discovery of the Corona virus vaccine. However, there is a likelihood of depreciation due to the market uncertainty caused by the continued effects of the COVID-19 pandemic (BoU, 2020).

Figure 6: Exchange rate for January 2021



Source: Bank of Uganda, 2021

1.3 Fiscal Sector Developments

The Government operations recorded a fiscal surplus of UGX382.7 billion in December 2020, differing significantly from the planned fiscal deficit of UGX21.2 billion for this period. The higher fiscal surplus was mainly attributed to the lower than planned spending during this period, coupled with a surplus in government receipts from grants and revenues as compared to the target.

The total revenue receipts amounted to UGX2,497.7 billion in December 2020, recording a small surplus of UGX20.73 billion as compared to the budgeted revenue of UGX2,476.96 billion. The surplus came from tax revenues that amounted to UGX2,409.49 billion as compared to the target of UGX2,342.95 billion owing to more tax returns that were filled for international trade and direct domestic taxes. To the contrary, non-tax revenues recorded a deficit of UGX45.8 billion in December 2020, resulting in revenues worth UGX88.2 billion. The grants received during December 2020 also exceeded the target by UGX7.22 billion, amounting to UGX111.86 billion as compared to the target of UGX104.6 billion.

The Government recorded expenditures amounting to UGX2,226.84 billion in December 2020, falling short of the target spending of UGX2,602.8. The shortfall resulted from lower spending on development expenditures due to low implementation of both domestic and external development projects. However, expenditures on recurrent spending and arrears exceeded the target, recording surpluses of UGX 186.4 billion and UGX66.93 billion respectively.

Table 1: Overall Fiscal Operations December 2020 (Billion Shillings)

	Program	Outturn	Performance	Deviation
Revenues and grants	2,581.60	2,609.55	101.08%	27.95
Revenues	2,476.96	2,497.69	100.84%	20.73
Tax	2,342.95	2,409.49	102.84%	66.54
Non-tax	134.01	88.2	65.82%	-45.81
Grants	104.64	111.86	106.90%	7.22
Project support	104.64	111.86	106.90%	7.22
Expenditures and lending	2,602.82	2,226.84	85.55%	-375.98
Current expenditures	1,171.07	1,357.48	115.92%	186.41
Wages and salaries	417.17	433.25	103.85%	16.08
Interest payments	325.97	325.97	100.00%	0.00
o/w domestic	224.78	224.78	100.00%	0.00
o/w external	101.19	101.19	100.00%	0.00
Other recurrent expenditure	427.93	598.26	139.80%	170.33
Development expenditures	1,205.10	779.68	64.70%	-425.42
Domestic	427.93	395.96	92.53%	-31.97
External	777.17	383.72	49.37%	-393.45
Net lending/repayments	203.99	0.1	0.05%	-203.89
HPP GoU	0	0.1	-	0.10
HPP Exim	203.99	0	-	-203.99
Domestic arrears repayment	22.66	89.59	395.37%	66.93
Overall fiscal balance (incl. grants)	-21.22	382.71		403.93
Domestic fiscal balance	956.49	755.76	79.01%	-200.73

Source: MoFPED 2020

1.4 External sector Developments

The external position worsened in December 2020, with the trade deficit widening to USD 324.7 million from US 294.48 million in November 2020 as a result of a rising import bill that offset the gains from the increased export receipts during this period (Table 2). The export receipts increased by 8.8 percent to USD 416.9 million in December 2020 from USD 383.1 million in November 2020 driven by the increase in receipts from non-coffee exports and Informal Cross Border Trade (ICBT) exports particularly gold and cocoa beans. However, receipts from coffee exports declined by 1.3 percent from USD 38.29 million in November 2020 to USD 37.8 million in December 2020, owing to the fall in the volume of coffee exported.

The import bill increased form USD677.5 million in November 2020 to USD741 million in December 2020 driven by the increase in government project imports from USD13.7 million to USD21.92 million during this period. The formal private sector import bill also contributed to the increase in the import bill, recording an 8.4 percent rise in the import bill to USD719.6 million in December 2020. The rise in the formal private sector import bill resulted from the increased import bill of both the oil and non-oil imports during this period.

Table 2: Composition of the Trade Balance, March 2020 – July, 2020

	Jul-20	Aug-20	Sep-20	Oct-20	Nov-20	Dec-20
Trade Balance	**-185.55**	**-277.19**	**-197.21**	**-251.12**	**-294.48**	**-324.74**
Total Exports	**419.47**	**416.27**	**417.93**	**363.86**	**383.05**	**416.86**
Coffee (Value)	49.98	46.06	44.64	38.61	38.29	37.78
Non-Coffee formal exports	368.38	369.15	372.16	324.15	343.61	377.85
ICBT Exports	1.11	1.05	1.14	1.10	1.15	1.23
Total Imports (fob)	**605.02**	**693.46**	**615.14**	**614.98**	**677.52**	**741.61**
Government Imports	40.96	55.78	4.09	8.35	13.72	21.92
Project	40.96	55.78	4.09	8.35	13.72	21.92
Non-Project	0.00	0.00	0.00	0.00	0.00	0.00
Formal Private Sector Imports	563.93	637.56	610.91	606.50	663.67	719.55
Oil imports	47.96	63.62	57.23	60.53	51.40	88.82
Non-oil imports	515.97	573.93	553.69	545.97	612.26	630.72
Estimated Private Sector Imports	0.13	0.12	0.13	0.13	0.14	0.14

Source: Bank of Uganda, 2020

2.0 Other Developments in the Economy

2.1. Public Debt Sustainability

The Ministry of Finance recently released the Debt Sustainability Analysis (DSA) report for FY 2019/20. The DSA is usually aimed at assessing the ability of the country to meet all its current and future debt payment obligations without exceptional financial assistance or going into default as well as identifying the key risks and vulnerabilities associated with the public debt portfolio. Given the current economic shock arising from the Corona virus pandemic and the onset of a new development plan, the 2020 DSA was mainly conducted to assess the impact of the COVID-19 pandemic and the new flagship projects of the National Development Plan III (NDPIII) on Uganda's debt sustainability.

Public sector debt increased from 35.3 percent in FY 2018/19 to 41.0 percent of GDP in FY 2019/20 largely due to increased expenditure pressures on Government to contain the effects of the COVID-19 pandemic, revenue shortfalls due to a decline in economic activities. The drastic rise in public debt has also resulted from the rising real average interest rate on debt as government takes on more non-concessional loans to meet the rising expenditure requirements. Of the total public debt, external debt contributed 28.1 percent, while domestic debt contributed 12.9 percent of GDP. To maintain ensure sustainability of public debt real GDP growth must consistently be higher than the interest rate on debt. The implementation of the economic growth recovery plan as outlined in the NDPIII is critical for maintaining debt sustainability.

In the medium term nominal public sector debt is projected to increase from 41.0 percent of GDP in FY2019/20 to a peak of 54.1 percent of GDP in FY2022/23. On the other hand, the present value of public sector debt to GDP is projected to increase from 31.8 percent in FY2019/20 to a peak of 42.9 percent in FY2022/23. This is still below the 55 percent benchmark for debt sustainability as well the East African Monetary union Convergence criteria of 50%.

These risks include: a large and increasing burden of debt service on the budget, with debt service recorded at 21.7 percent of domestic revenue at the end of June 2020; increased rate of non-concessional debt accumulation; low economic growth; low tax revenues; increased domestic borrowing; low export growth; and slow project implementation which leads to cost overruns. Consequently, the country's risk rating was downgraded from low risk to moderate rate risk of debt distress (MoFPED, 2020). In order to mitigate these risks, government has put in place measures including; implementation of the Domestic Revenue Mobilisation Strategy (DRMS); developed an integrated bank of ready projects; prioritised concessional financing; and development of industrial parks for export promotion and import substitution.

References

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The National Planning Authority was established by the NPA Act (15 of 2002) in accordance with Article 125 of the 1995 Constitution of the Republic of Uganda to produce comprehensive and integrated development plans for the country, elaborated in terms of the perspective Vision, long and medium–term plans.

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