

SUR/09/1

January 8, 2009

**The Acting Chair's Summing Up
Uganda—2008 Article IV Consultation and Fourth Review Under the
Policy Support Instrument
Executive Board Meeting 09/01
January 7, 2009**

Executive Directors agreed with the thrust of the staff appraisal. They commended the authorities for their sound macroeconomic management that has contributed to an impressive economic performance and steady poverty reduction. The current global economic downturn and reduced prospects for external financing pose immediate challenges to the Ugandan economy. Directors considered the economy to be well-positioned to face these challenges given its low public debt, comfortable level of international reserves, and relatively sound banking sector. Nevertheless, this difficult external environment calls for heightened vigilance.

While the medium-term outlook remains favorable, Directors agreed with the authorities that infrastructure bottlenecks and dependence on subsistence agriculture represent important impediments to growth. Thus, they welcomed the preparation of a new National Development Plan, which entails, among other things, a scaling-up of government investment in infrastructure. In this connection, they stressed the need for careful evaluation of investment projects, including their impact on debt sustainability and on international reserves.

Directors recognized the strong fiscal performance in 2007/08, and agreed that fiscal policy should maintain the modest stimulus underlying the 2008/09 budget. In the event of a revenue shortfall for 2008/09, they encouraged the authorities to avoid precipitous cuts in current expenditures, strengthen expenditure management, and prevent further accumulation of domestic arrears. For the medium term, Directors supported the authorities' target to increase tax revenues by ½ percent of GDP annually and welcomed their consideration of introducing a fiscal rule, which would underpin fiscal consolidation and prudent use of oil revenues.

Directors stressed that monetary policy should aim at sustaining confidence in the currency, while supporting the disinflation process. They encouraged the authorities to seize the opportunity provided by falling international food and fuel prices to bring inflation back toward its medium-term objective. Directors underscored the importance of ensuring that the necessary pre-conditions are in place before introducing a formal inflation-targeting framework.

Directors considered that Uganda's flexible exchange rate regime has served the country well, facilitating adjustment to external shocks. They took note of the staff's assessment that the real effective exchange rate is broadly in line with fundamentals, consistent with strong export performance over the past few years. Directors also saw scope for targeted intervention in the foreign exchange market to avoid excessive volatility.

Directors noted that Uganda's banking sector remains sound overall, with banks being well-capitalized and relatively insulated from the global financial crisis. They noted, however, the recent rapid expansion of bank lending and the significant share of foreign-exchange loans in banks' portfolios. To address these vulnerabilities, Directors saw the need to further strengthen prudential supervision as well as close collaboration with the home supervisors of banks operating in Uganda.

It is expected that the next Article IV consultation with Uganda will be held within 24 months, subject to the applicable provisions of the Executive Board decision on consultation cycles.