Effects of Policy Response During the COVID-19 Crisis: A Monetarist Analysis of Uganda

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The COVID-19 Crisis and the dismal response of the GoU and the BoU.

In 2020, Uganda faced the COVID-19 pandemic, prompting the Government of Uganda to enforce multiple lockdowns between 2020 and 2021, with the first beginning on March 30, 2020. Sub-sectors such as manufacturing, transportation and storage, retail (non-food items), tourism, and Micro, Small, and Medium Enterprises (MSMEs) experienced significant damage from COVID-19 (Mukiza, 2020). As a result, Uganda experienced a decline in output, an increase in unemployment, and slower economic growth, estimated to be between 4.6 percent and 5.1 percent during the FY2019/20 period, down from pre-pandemic projections of 6.0 percent, according to the Statement on the Economic Impact of COVID-19 on Uganda presented to Parliament by Hon. Matia Kasaija in March 2020.

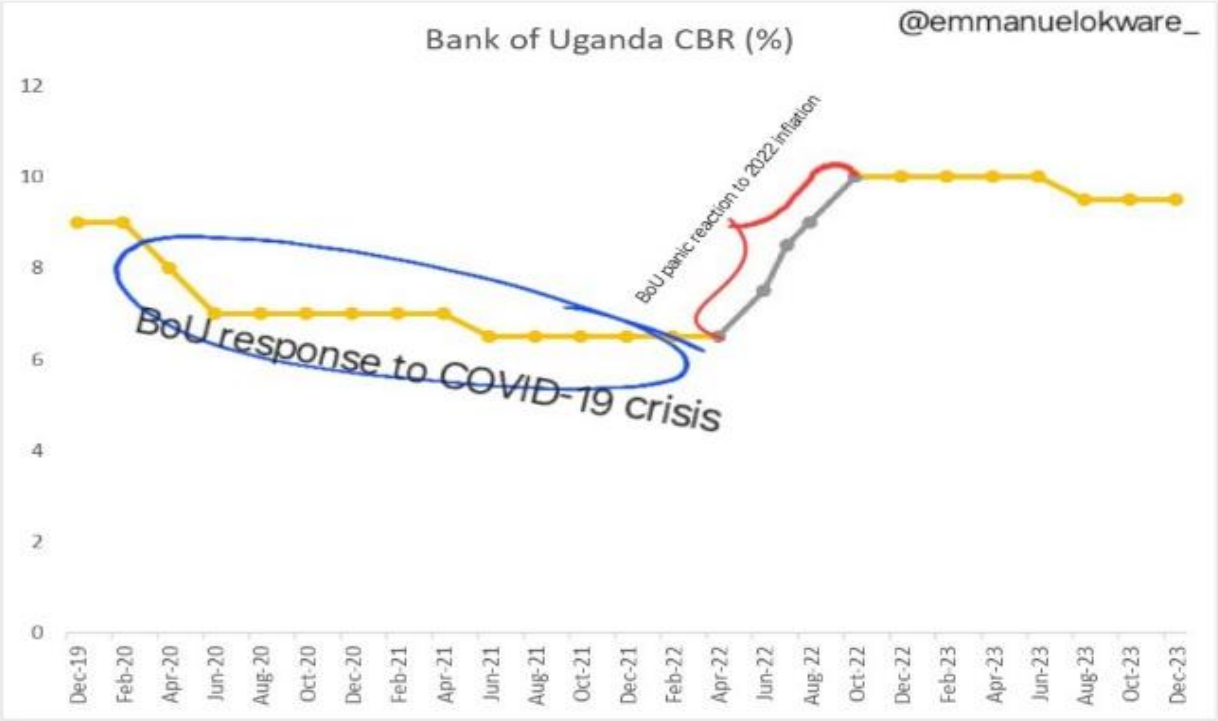
The response from the Government of Uganda and the Bank of Uganda was clear, similar to actions taken by many other governments and central banks around the world. They prioritized supporting household spending and helping businesses stay afloat, announcing several fiscal stimulus measures in a desperate effort to restore household incomes and restart business activity. For example, the COVID-19 Relief Fund, totaling approximately UGX 54 billion, as reported by NTV, targeted urban poor and informal sector workers who lost their livelihoods due to lockdowns and restrictions. As a result, the government deficit increased, causing a significant rise in the national debt from just under UGX 53 trillion in 2019 to well over UGX 97 trillion in 2023, according to IMF data. In fact, over the five years leading up to 2019, the national debt averaged UGX 38,998.67 billion, compared to the period between 2020 and 2023, where the average was UGX 81,846.37 billion.

The Bank of Uganda's Monetary Policy Committee, hereafter referred to as the MPC, responded to the COVID-19 crisis by significantly easing its CBR requirement, lowering the reserve requirement ratio for commercial banks, encouraging supervised financial institutions (SFIs) to restructure loans, and purchasing treasury bonds held by microfinance deposit-taking and credit institutions. The CBR decreased substantially from 10 percent in December 2018 to 7.0 percent between June 2020 and April 2021, reaching its lowest point of 6.5 percent between June 2021 and April 2022, when inflation was initiated. As inflation surfaced later in 2022, panic gripped the MPC. They raised the CBR quickly throughout late 2022: 7.5 percent in June, 8.5 percent in July, 9 percent in August, climbing sharply to 10 percent from October 2022 through June 2023.

Figure 1 demonstrates the reaction of the Bank of Uganda on the onset of the Coronavirus Pandemic, which, as you can observe, indicates they didn't quite view the events as

capable of being inflationary. At the onset, the Bank of Uganda panicked, rapidly increasing the Central Bank Rate month on month from 7.5% in June 2022 to 10% in October 2022.

Figure 1: Central Bank Rate movements since end 2019



The preceding texts highlight not only the startling neglect of money in response to the COVID-19 crisis but also the terrible outcomes manifesting as bloated government deficits and high inflation resulting from it. The post-COVID-19 pandemic period, contrary to the predictions of most prominent economists and central banks, overwhelmingly provided substantial evidence across both developing and developed economies. Throughout this essay, Uganda will serve as the primary backdrop for examining the effects of money growth, inflation, and spending from 2020 to the present and in the years to come.

M3 Broad Money growth rates in Uganda

As a result of extensive fiscal and monetary stimulus by the Government of Uganda and the Bank of Uganda, as explained in the introduction, Uganda experienced a significant surge in M3 broad money growth during FY 2019/2020. The growth rate of M3 broad money reached 23.1%, which is well above the already above-optimal average of 14.8%

recorded from FY 2009/10 to FY 2018/19. Notably, this sharp increase in M3 broad money occurred in less than a year.

Figure 2: %M3 growth rates in Uganda, 2005-2025

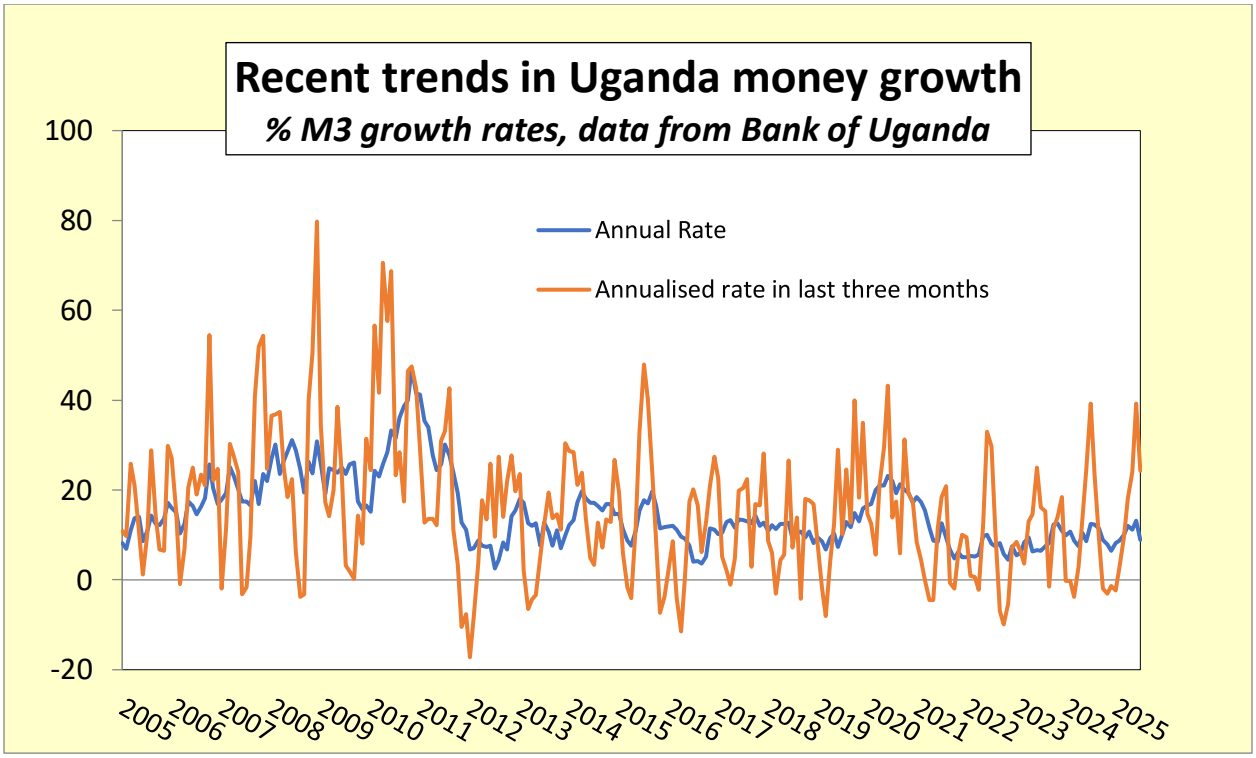


Figure 2 shows that Uganda had already started diverging from the path of monetary stability in 2019. During the five years leading up to the end of 2018, the annual growth rate of broad money averaged 12.3%, and it grew at 13.1% in the second half of 2019. The annual growth rate then surged to about 15.9% by the end of 2019. In fact, the monetary developments in Uganda by the end of 2019 were already inflationary, meaning they were incompatible with a rate of around 5%.

In 2020, the annual growth rate of broad money averaged 19.8% during the first half of the year, reaching a record eight-year high of 23.2% in June 2020. The three-month annualized rate was even more inflationary, soaring to 43.2% in the same month, the highest since August 2015. Suddenly, broad money growth sharply declined, with the annual rate falling to 4.5% in December 2022, and the annualized rate over the last three months dropping to -9.8% in October 2022. This was due to subsequent monetary policy tightening in an attempt to curb inflation.

The annual growth rate of broad money remained moderate between the end of 2022 and September 2023 at 7.2% on average, before rising in October 2023 to an annual rate of 12.3%, and then staying stable through 2024 to 2025 until now. Table 1 below clearly shows the significant increase in broad money growth in Uganda when comparing the

three-year periods from 2016 to the end of 2018 and from 2019 to the end of 2021. The difference in broad money growth using compound annual percentage increase is +2.2%, and the difference is even larger when measured as a simple increase, +9.1%.

Table 1: Broad money growth compared for three-year periods, end-2018 and end-2021

Increase in broad money, %, over three years		Compound annual % increase in broad money		Difference between rates of annual increase, %, in two periods
To end-2018	To end-2021	To end-2018	To end-2021	
35.5	44.6	10.7	13.1	+2.2

M3 broad money growth and Nominal spending

A widely accepted proposition among both modern and classical followers of the quantity theory of money is that there is a consistent though not precise relationship between the growth rate of the money supply and the growth rate of nominal income. Nominal income is particularly important because monetary changes can manifest either through price changes or through alterations in the quantity of goods traded. It is fairly accurate to say that changes in nominal variables, such as an increase in the money supply, produce effects that are also mainly nominal, like a rise in money incomes. In other words, changes in broad money growth are more closely linked to changes in nominal GDP, ultimately leading to actual changes in prices.

This is not immediately obvious to the naked eye because monetary growth impacts income with a delay, and the duration of this delay varies. In essence, the current rate of money growth is not directly linked to the current rate of income growth. Similarly, current income growth depends on past monetary activity, and present money trends influence future income. Usually, a shift in monetary growth results in a change in nominal income growth after about six to nine months. Nonetheless, this timeframe can differ; sometimes the effect takes longer, other times shorter.

Figure 3: Money and Nominal GDP medium-term relation in Uganda, 1971-2021

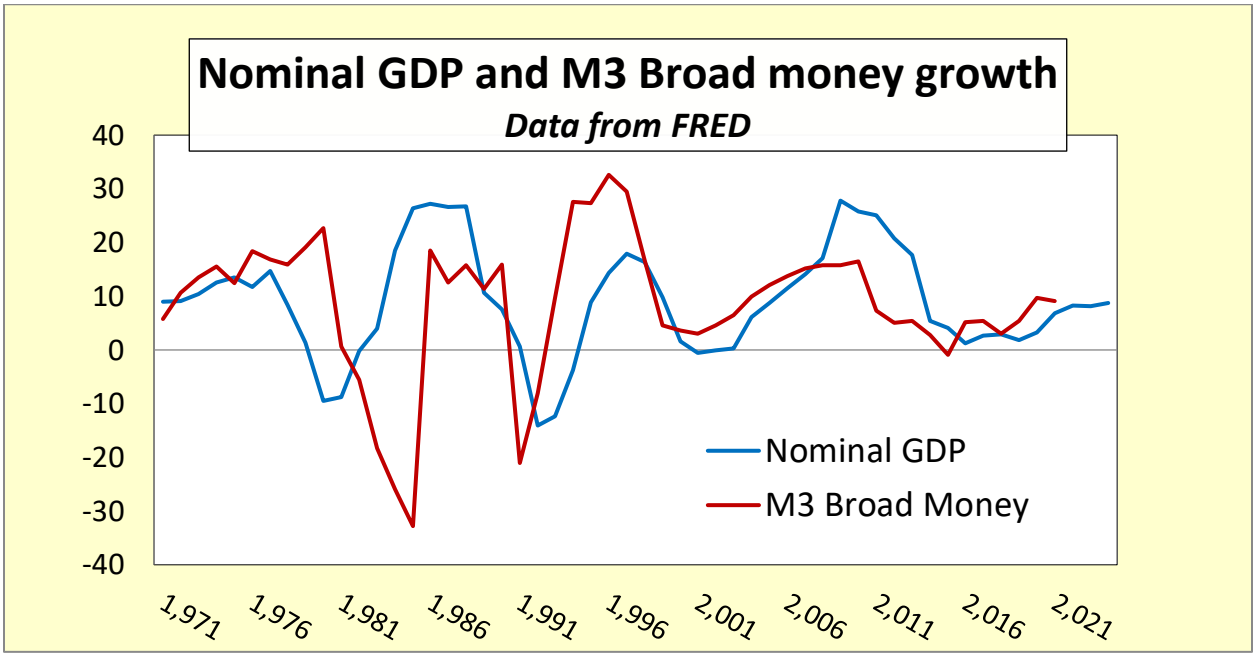


Figure 3 pretty much depicts a fairly good correlation between M3 Broad money growth and Nominal spending in Uganda between 1971 and 2021. Looking at Table 2 below, we can again observe a closeness in the figures of annual growth rates of M3 broad money and Nominal GDP growth across the periods compared. We can also observe extraordinary growth rates of M3 broad money for the year to February 2021 and the three months to February 2021, 20% and 17% respectively.

Table 2: Monetary growth in Uganda up to February 2021

Period	% annual growth rate (M3)	Nominal GDP
1967-2019	8.5	9.0
Nine years to 2019	3.2	3.4
Year to February 2021	20	n.a
Three months to February 2021	17	n.a

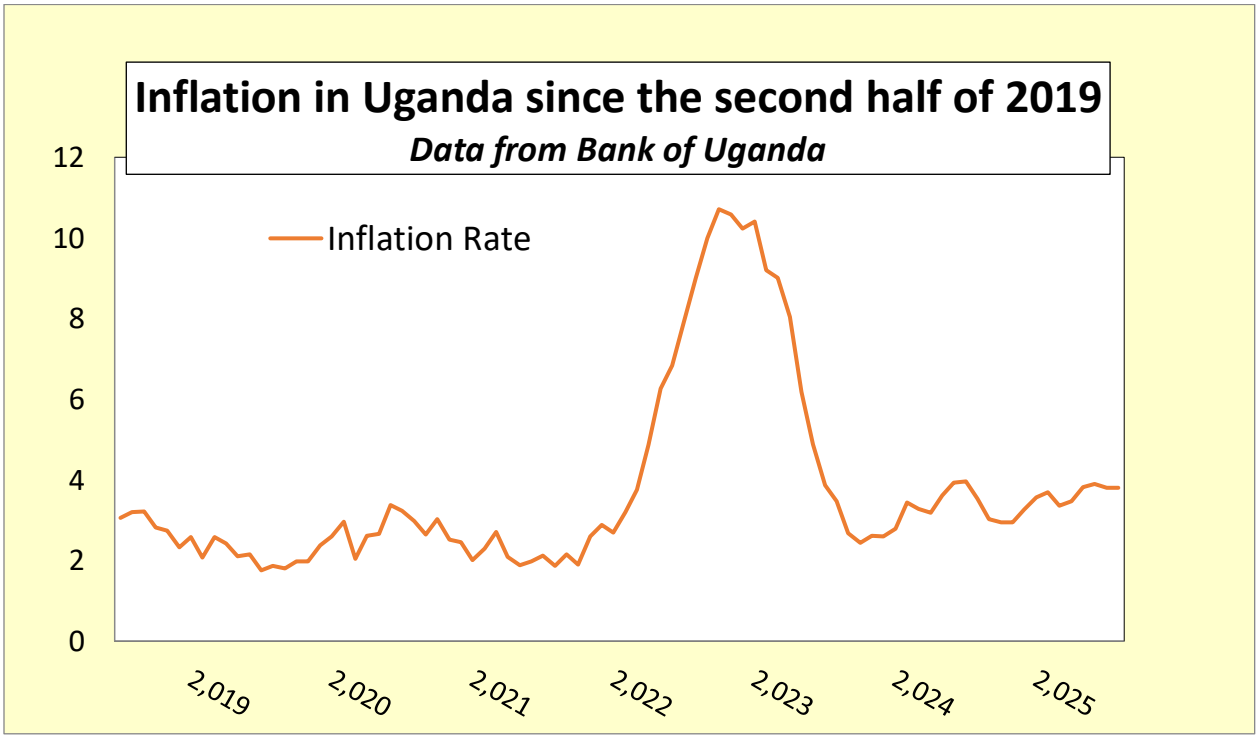
Post-COVID-19 Inflation in Uganda

Before the COVID-19 crisis, Uganda's M3 broad money growth was well above the optimal level, clearly indicating that any small increase in the money supply would, after the necessary delay, cause inflation. It's not surprising that a +2.2% difference in the compound annual growth rates of M3 broad money over the last three years ending in 2018, compared to the three years ending in 2021, though smaller than those of the US and the UK, led to inflation in 2022.

Considering an average annual growth rate of 5.3% over the past ten years leading up to FY 2018/2019 and a 5% inflation target set by the Bank of Uganda, M3 broad money growth between 10.3% and 10.7% would be an ideal level to maintain economic stability. However, the average M3 broad money growth during that period was about 14.8%. As you may have noticed, the level of M3 broad money growth, which exceeded the optimal level from FY 2009/10 to FY 2018/19, was not associated with inflation exceeding the 5% target set by the Bank of Uganda.

It is fair to argue that what happened was not due to any deliberate monetary policies by the Bank of Uganda. Two main explanations stand out: first, Uganda's inflation target is relatively high at 5%; second, this scenario is not unique to Uganda but also applies to many other developing countries experiencing rapid growth. Countries like India, with more room to expand in high-tech sectors, can sustain high growth rates of M3 broad money without experiencing high inflation. This, in itself, does not negate the importance of broad money growth in both developed and developing countries, as I will explain Uganda's post-COVID-19 inflation in the next section.

Figure 4: Inflation trends in Uganda since 2019-2025.



As I explained in the introduction, the dismal reactions of the GoU and the BoU paved the way for the post-COVID-19 inflation in Uganda. Unfortunately, several reasons were put forward to explain the causes of inflation during that period, with the greatest blame being on the Ukraine War, which only started on February 24, 2022, supply disruptions caused by numerous COVID-19 lockdowns, and many prominent figures and economists even

regarded it as imported inflation. But, “inflation is always and everywhere a monetary phenomenon in the sense that it is and can be produced only by a more rapid increase in the quantity of money than in output,” as Friedman put it.

With the Ugandan economy starting from approximate monetary equilibrium in late 2019 and early 2020, the surge in money supply would, on the correctness of Friedman’s proposed two-year lag, likely lead to an inflation peak in the second half of 2022. As the annual rate of money growth reached 23.2%, the risk of double-digit inflation became even more acceptable. The Consumer Price Index, which averaged just 3.2% over the seven fiscal years leading up to 2018/19, was at 7.2% in 2022. The monthly increase in the consumer price index, which had averaged just above 2.5% from July 2018 to December 2020, was 6.3% in May 2022 and peaked at 10.7% by October 2022.

However, inflation quickly eased, reaching its lowest monthly rate of 2.4% in October 2023. Since then, the month-to-month inflation rate has remained moderate and stable until August 2025. The average over that period is only 3.3%. Figure 4 highlights relatively stable inflation as it transitioned into the post-COVID-19 inflation period, from July 2019 to February 2022, when inflation averaged just 2.4% per month. Due to the money surge in 2020, inflation began to rise around March 2022, reaching a peak of about 10.7% in October 2022. In fact, the average monthly inflation rate between July 2022 and April 2023 was 9.5%, with rates exceeding 10.4% from September 2022 to January 2023.

From a monetary perspective, the medium and long-term inflation could remain moderate, below the 5% target set by the Bank of Uganda, at the current level of broad money growth rate. The M3 broad money growth continues at a moderate rate, decreasing in July 2025 to 8.9% from a 13.2% annual rate in June 2025, and the three-month annualized rate drops in July to 24.2% from 39.3% in June 2025. These explanations clearly suggest that monetary policy is important and that its key feature is its impact on the amount of money rather than on bank credit, total credit, or interest rates. They also indicate that large fluctuations in the change of the amount of money are destabilizing and should be avoided.

Conclusion

Uganda’s policy response to the COVID-19 crisis, characterized by significant fiscal stimulus and monetary easing, led to a surge in M3 broad money growth, peaking at 23.2% in June 2020, and a substantial increase in national debt from UGX 53 trillion in 2019 to over UGX 97 trillion by 2023. These measures, while aimed at supporting households and businesses, fueled post-COVID-19 inflation, which reached 10.7% in October 2022, driven by excessive money supply growth rather than external factors like the Ukraine War or supply disruptions. The Bank of Uganda’s reactive tightening of monetary policy, with the CBR rising to 10% by late 2022, along with issuing securities, eventually stabilized inflation to an average of 3.3% by August 2025.

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