Investment Financing and Interest Rates in Uganda

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Executive Summary

The real interest rates charged by commercial banks are very high, largely because of the high costs of transacting banking business in Uganda. Nevertheless, the high lending rates have not prevented very rapid real growth in bank lending to the private sector since the start of the millennium. Instead it is the volume of funds which can be mobilised by the domestic financial system which determines how much finance can be made available for investment by the private sector in Uganda, together with the quality of private investment projects (e.g. their financial viability), rather than the cost of credit per se. Therefore, policy reforms to stimulate the supply of domestic finance for investment in Uganda should focus on measures to deepen and broaden (i.e. diversify) the domestic financial system. Institutional reforms offer the best prospects for achieving these objectives. In particular, the liberalisation of the pension sector will make a vital contribution to boosting resources available for investment finance because it will stimulate the growth of an industry (the pension industry) which mobilises long term savings and thus requires long term assets (such as equities and bonds) in which to invest its resources.