DETERMINANTS OF REAL EXCHANGE RATE VOLATILITY IN UGANDA

2000 - 2014

BY

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ABSTRACT

This study aimed at investigating macroeconomic determinants of Exchange Rate volatility in Uganda. The study was based on time series quarterly data from 2000 to 2014 obtained from Bank of Uganda and Uganda Bureau of statistics. The Augmented Dickey Fuller test was used in testing for stationary of the variables. The study was based on the Generalized Autoregressive Conditional Heteroskedasticity (GARCH 1, 1) to estimate volatility, and the vector error correction model and the OLS methodology for investigating the relationship between the study variables.

It was revealed that Exchange Rate volatility is very strong in Uganda's economy and it is as a result of movements in a number of macroeconomic variables. There exists both short run and long run relationships between the study variables. Money supply has positive significant effect on Exchange Rate volatility while inflation and GDP have negative effects. Findings further show that Exchange Rate responds to the changes in the selected macroeconomic variables but with a lag.

The study recommends that government should exercise direct control of viable macroeconomic variables which have direct influence on Exchange Rate. For example it should direct its expenditure to the key productive sectors of the economy such as agriculture and manufacturing as this will go a long way in increasing the production of goods and services thereby reducing on dependence on imports Further, bank of Uganda should institute a policy that will ensure the limit within which Exchange Rate can fluctuate within a given time period.