BANK OF JAMAICA

News Release
7th May 2008

Quarterly Press Briefing
Hon. Derick Latibeaudiere, Governor,
Bank of Jamaica

Good Morning Ladies and Gentlemen:

Today we are releasing the Quarterly Monetary Policy Report for the period ended March 2008. My briefing will therefore highlight the economic developments in that quarter and the Bank's response to them. I will then speak briefly on the economic events that are unfolding and their likely impact on the economy in the near term. My closing remarks will indicate the Bank's likely policy stance for the current quarter in the context of the near-term outlook for the economy.

Inflation

When we last spoke in February I indicated that our forecast for headline inflation ***for the March quarter*** was 3.5 per cent ± 0.5 percentage point. This outcome was contingent on a rebound in the supplies of short-term agricultural commodities, lower demand and the impact of the Government's intervention to ease the pass-through of imported inflation to domestic prices. We indicated, however, that continued increases were expected in the prices of international commodities while the prices of some domestic staples could remain elevated.

Against the risks we had outlined, headline inflation for the March quarter was 5.2 per cent, which was above the Bank's forecast. The outturn for the quarter also exceeded the average increase of 1.2 per cent for the March quarters of the last 5 years. Given the outturn for the March quarter, headline inflation for the fiscal year was 19.9 per cent.

Increases in the prices of domestic agricultural commodities were the dominant influences on inflation during the review quarter. While there was evidence of an increase in supplies, the decline in the prices for these commodities was not as sharp as the Bank had anticipated.

Other significant influences on inflation in the review quarter were higher international grain prices and the pass-through of increases in energy costs. For example, the prices of rice and corn rose by 35.9 per cent and 28.0 per cent, respectively, in the quarter. This is in comparison to our forecast of respective increases of 12.9 per cent and 8.8 per cent. The price for crude oil was also above our expectation.

Further, the Bank had expected a moderation in the cost of some commodities from the Government's intervention to ease the pass-through of imported prices. However, the reports are that there was a noticeable level of non-compliance in some areas. Some of the pass-through of the increases in imported prices to domestic prices would, however, have been moderated by the relative stability in the exchange rate in the March 2008 quarter.

The Bank is forecasting headline inflation in the range of 5.0 per cent to 6.0 per cent for the June quarter. The forecast is based on expected administrative price increases, in particular bus and taxi fares and water rates, as well as continued upward movement in international commodity prices. In addition, there should be some price movements following the Government's removal of the subsidies that were used to cushion the effect of the increase in the prices of some international commodities. We are expecting, however, that as in the March 2008 quarter, continued stability in the exchange rate should have a moderating impact on the pass-through of imported prices to domestic prices.

In the context of the developments that we have outlined, the Bank is forecasting inflation in the range of 11.5 per cent to 14.5 per cent for FY2008/09. We expect that the sharpest increase will be in the first half of the year, and that the projected rebound in domestic agricultural commodities should temper the rate of increase for these items in the second half of the year. We also expect some moderation in international commodity prices, in light of the slowdown in the global economy. In addition, we anticipate some tempering in demand pressures in the context of the policy actions taken by the Bank in the earlier part of the year.

Foreign Exchange Market

There was relative stability in the foreign exchange market during the review quarter. This was reflected in the depreciation of approximately 0.7 per cent in the value of the Jamaica Dollar vis-à-vis the US dollar. For fiscal year 2007/08, the exchange rate depreciated by 4.6 per cent, relative to 3.4 per cent in FY 2006/07.

With the exchange rate appreciating in February and March, the overall depreciation for the quarter was due to developments in January. The depreciation in January occurred in the context of high levels of Jamaica Dollar liquidity, no new offers of GOJ instruments and heightened inflationary expectations. These factors fuelled the preference of investors for US dollar denominated assets.

In an effort to stabilize the market, the Bank reintroduced its 365-day instrument and offered a special 18-month variable rate instrument to the market. In addition, we increased interest rates on all tenors of open market instruments in early January and February. The positive response of the market to these monetary policy actions contributed to the appreciation in the exchange rate in February and March.

During the quarter a softening in external interest rates together with increased uncertainty regarding conditions in the international financial market, encouraged investments in domestic instruments. In addition, there were inflows to satisfy tax obligations due in March. Conditions in the market were also buoyed by inflows related to the sale of a Jamaican rum manufacturing company (Lascelles de Mercado) to a Trinidadian company, (Angostura).

Against the background of these factors, there was a marked increase in net private capital inflows during the quarter. With the improved market conditions the Bank was a net purchaser of foreign exchange in the March quarter. This contrasted with the December and March 2007 quarters when the Bank was a net seller of foreign exchange. As a consequence at the close of the quarter, the NIR was US$2 083.4 million or US$205.7 million above the outturn at the end of December 2007. At the close of business on Tuesday, the NIR was US$2,160 million.

For the June quarter the Bank is expecting continued stability in the foreign exchange market. This stability should be supported by the lagged impact of the Bank's monetary policy actions, lower interest rates in the US and the general uncertainty in the international financial markets. Nonetheless we are expecting some increased foreign exchange demand to meet payment obligations for the imports of fuel and durables.

I now turn to the Performance of the Real Sector

The Bank's estimates of real sector activities indicate that the economy grew within the range of 1.0 per cent to 1.5 per cent in the March quarter. This was a marked improvement relative to the average expansion of 0.2 per cent over the two previous quarters. Given the estimated growth for the March quarter, growth for the fiscal year 2007/08 is estimated in the range of 0.8 per cent to 1.2 per cent. This estimate is down from the expansion of 2.4 per cent recorded for FY 2006/07 and the average growth rate of 1.8 per cent over the last five fiscal years.

We estimated that growth in the tradable sector recovered somewhat in the review quarter, while there was continued expansion in the non-tradable sector. The main drivers of growth were estimated to have been ***Construction & Installation***, ***Transport, Storage & Communication***, ***Distributive Trade*** and ***Financing & Insurance and Miscellaneous Services*** which includes ***Tourism***. ***Agriculture, Forestry & Fishing, Electricity & Water*** and ***Mining & Quarrying*** were estimated to have declined in the quarter.

For the June quarter and the FY 2008/09, the Bank is anticipating stronger growth in real output. We project that growth for the period will be driven by expansion in the ***Mining & Quarrying, Miscellaneous Services, Construction & Installation*** and ***Transport, Storage & Communication sectors***.

In concluding

Let me say that the external challenges that we have been experiencing since last year are persisting. We are particularly concerned about the slow-down in world growth, especially in the USA, our main trading partner. Historically, a recession in the USA has had marginal impact on the Jamaican economy, as the fall in the prices for our exports of goods and services was almost fully offset by reduced prices for imports. In this regard we have included a special feature on '*The Impact of the US Recession'* in **Box 1** of this Report. However, with this US recession and global slowdown, international oil prices remain volatile. In addition, there is still a lot of uncertainty with regard to the future path of grain prices as strong demand coupled with supply constraints could continue to exert an upward pull on prices. Some of these issues are set out in **Box 2.**

Going forward, the main challenge for the central bank will be to temper the rate of price increases and moderate inflationary expectations. In this regard, the Bank will continue to maintain a conservative monetary policy stance and will take the appropriate policy actions in an effort to maintain macroeconomic stability.