BANK OF JAMAICA

Quarterly Press Briefing
Hon. Derick Latibeaudiere
Governor, Bank of Jamaica
9th May 2007

Good Morning Ladies and Gentlemen:

It is a pleasure to welcome you to the release of the Monetary Policy Report for the quarter ended March 2007.

My presentation this morning will focus on the macroeconomic developments of the review quarter and will point to some of the economic highlights of the fiscal year just ended. As usual, I will also give you some indication of the Bank's near term outlook.

The Bank operated in a generally favourable global and domestic environment during both the review quarter and the fiscal year. Growth in the world economy remained strong, driven largely by rapid expansion in some emerging market economies, but inflation continued to be of concern to some of our major trading partners.

In this context, the pace of growth in the domestic economy was slightly slower than was expected although well above the average rate of 1.1 per cent for the previous eight years. Inflation for the fiscal year declined sharper than we had originally projected and the exchange rate remained relatively stable. Consequently, the Bank was able to ease monetary policy somewhat, particularly in the first half of the year.

Let me now turn to some specifics.

Inflation

Headline inflation for the fiscal year was 6.6 per cent - the lowest rate since FY 2002/03. For the March quarter, it was 1.0 per cent. The out-turn for the year was below the Bank's original target range of 9.0 per cent to 10.0 per cent but for the quarter it was broadly in line with the Bank's expectations.

Estimated core inflation for the fiscal year followed the trend in headline inflation, declining sharply to 3.3 per cent - the lowest out-turn since F/Y 2001/02. The fiscal year out-turn was also below the Bank's target range of 4.0 per cent to 5.0 per cent. Core inflation for the March quarter was estimated at 0.8 per cent.

The favourable inflation for the fiscal year was largely attributable to the stability of the exchange rate in the first half of the year and to the reduction in the prices of some domestic agricultural commodities in the second half of the year.

Looking ahead to this fiscal year, the Bank is forecasting inflation in the range of 6.0 per cent to 7.0 per cent for the year – roughly the same as last year.

The forecast for the fiscal year is based on the Bank's assessment that inflationary impulses could emanate from higher factor costs in the context of the growing demand for labour. In addition we do not expect the prices of agricultural commodities to fall much lower as we believe that production in the sector has normalised following the effects of the adverse weather conditions in 2004 and 2005. The risks to this forecast are the uncertainty of oil prices and the possibility of adverse weather conditions.

We are projecting headline inflation in the range of 2.0 per cent to 3.0 per cent for the June quarter. This projection assumes the seasonal increase in the prices of some agricultural commodities, as well as an upward movement in the price of international crude oil due to increased demand associated with the driving season in the USA. Consumer prices in the quarter will also be affected by the impact of the recently announced tax measures. The impact of these increases should be tempered by relative stability in the exchange rate.

Foreign Exchange Market

Let me now turn briefly to developments in the foreign exchange market. The market was fairly stable in the March quarter with the exchange rate depreciating marginally by under 1 percent (0.96 per) relative to 1.63 per cent for the December quarter. The outturn for the quarter contributed to a depreciation of 3.4 per cent for the fiscal year, relative to 6.0 per cent for F/Y 2005/06.

Despite the overall moderate movement in the exchange rate, there was some instability in the foreign exchange market during the March quarter, particularly in January. The instability was partly influenced by the high levels of Jamaica Dollar liquidity that stemmed from the Government's net redemption of maturing instruments during the quarter. In addition, there was a fall off in net private capital inflows.

In the context of the prevailing conditions, the Bank increased its presence in the money and foreign exchange markets. This was done by the offer of two special variable rate certificates of deposit, the sale of securities from its holding of Government securities as well as the sale of foreign exchange to smooth supplies in the market.

Notwithstanding the sale of foreign currency to the market, the stock of net international reserves remained strong at approximately US$2.33 billion at the end of March, an increase of US$11.8 million relative to end-December. Gross reserves at end-March were US$2.6 billion, representing 19.7 weeks of estimated imports of goods and services.

For the June quarter, we are expecting relative stability in the exchange rate in spite of the recent bouts of instability which the Central Bank views as temporary. Indications are that the recent demand pressures stemmed from the coincidence of a number of private sector obligations becoming due at around the same time. The Bank therefore intervened to smooth supplies to the market and to ensure an orderly adjustment in the exchange rate. However, despite the intervention we expect to maintain a strong level of Reserves throughout the quarter.

Real Sector Developments

The Bank's estimate of Gross Domestic Product (GDP) for the March 2007 quarter indicates growth in line with that of the three previous quarters. Accordingly, the fiscal-year growth should be around 2.5 per cent, similar to the rate recorded for the last calendar year.

With respect to performance during the quarter, all sectors are estimated to have grown with the exception of Miscellaneous Services, which includes the tourism industry. The major contributors to growth were Construction & Installation, Agriculture Forestry & Fishing, Electricity & Water and the Distributive Trade. The contraction in Tourism stemmed from a decline in the number of visitor arrivals, associated with the revitalization of Cancun, the mild winter season in the USA, the new USA passport requirement and the temporary CARICOM visa requirement during the period of the World Cup Cricket.

Just to elaborate a little on the performance of tourism for 2007 so far. The tourism industry performed exceptionally in 2006. However, the performance was in the context of the diversion of many additional visitors to Jamaica as a result of the hurricane damage to competing destinations, particularly Cancun. If we discount 2006 as an unusual year, we will notice that stopover arrivals in 2007 so far, are 11 percent above what they were in 2005, a relatively normal year. When this is compared to the long-term growth trend of an average of 3.0 per cent per year, the Bank is of the view that the industry continues to do well.

Returning to the overall expansion in the economy, there has been continued economic growth in the context of solid world growth and favourable international commodity prices. Investment in the domestic economy has also continued to be strong and lending by domestic commercial banks to the productive sector has continued apace. In addition the economy recovered from the adverse shocks of 2005 and productivity has increased in some sectors. The normalisation in cement supplies, following the problems experienced in the industry in the first half of 2006, would also have facilitated a rebound in Construction.

Going forward, the Bank is forecasting relatively strong economic growth for the June 2007 quarter, led by Construction, Mining and Basic Services, which includes electricity generation, transportation and communication. However, the performance of the tourism industry is likely to temper growth in the quarter. For fiscal year 2007/2008, growth is expected to accelerate in the range of 2.5 per cent to 3.5 per cent. A special article on the financial programme, which is the framework that guides the Bank's actions, is included in Box 1. We hope that this will give you a better understanding of the variables that are considered in our forecasts.

Ladies and Gentlemen: monetary policy is always challenging. The challenges may arise from changes in the domestic or external economic environment or in both. Whatever the challenge, be assured that the Central Bank is committed to the goal of low and stable inflation as the fundamental basis for sustainable growth and development. I urge you to play your part in helping us to create the conditions that will facilitate these objectives.

Thank you.