BANK OF JAMAICA

Jamaica Exporters' Association
Quarterly Members' Luncheon

Address

Brian Wynter
Governor, Bank of Jamaica

Wednesday, 10 February 2010

Implications of an IMF Relationship for Expanding Jamaica's Exports

Ladies and Gentlemen:

It is a pleasure for me to be here this afternoon and I want to thank the Jamaica Exporters Association for inviting me to address your first quarterly luncheon for 2010. I am particularly grateful for the opportunity to speak to you about the implications of a renewed borrowing relationship with the International Monetary Fund, especially for the export sector. Indeed, at this juncture, it is important that all stakeholders in Jamaica have a clear view of where we are in terms of the economy and where the policies being implemented by the Government will take us.

As you all know, the renewed borrowing relationship with the IMF is coming on the heels of the global economic crisis which exacerbated Jamaica's significant and persistent fiscal and current account deficits. The ability to meet the country's external obligations and to generate sustained growth has been severely impaired and this precipitated the need for support from the IMF.

The renewed borrowing arrangement was preceded by the development of a comprehensive plan to redress the unsustainable economic imbalances that restrained economic growth, particularly in the export sector. The plan was crafted over the last seven months in close collaboration with the IMF and other international development partners. The resulting medium-term economic programme received the endorsement of the Board of the IMF. Last week, the Executive Board of the IMF approved a 27-month Stand-By Arrangement for Jamaica of approximately US$1.3 billion. Half of this amount was received two days ago. Also, Government of Jamaica domestic bondholders recently registered broad support for the new policy direction through their voluntary participation in the debt exchange at exceptionally high levels.

So, how does all this relate to the export sector?

The main objective of the medium-term economic programme is to fundamentally transform the Jamaican economy to facilitate growth. In the process, the programme will also allow us to build a more resilient economy so that we will have more maneuvering room to cope with external shocks, such as the effects of the global crises from which we suffered so badly.

Jamaica needs to generate sustained growth in excess of 3 per cent over the medium-term to allow for an improved standard of living for all its citizens. Over the last fifteen years we have recorded average yearly growth of just 0.7 per cent. Given the size of the domestic economy, it is clear that the transition to strong and sustained growth has to be led by our exporters. Over the last fifteen years, export growth, including both goods and services, expanded at an average annual rate of 4.7 per cent. Compare this with two of our non-oil competitors, Costa Rica and the Dominican Republic, that achieved 10.0 per cent and 7.0 per cent respectively over the same period.

Well, in addition to the recession in global economic activity which reduced the demand for exports and profoundly affected domestic economic activity, Jamaica's export growth has been hampered by periods of macroeconomic instability for many years. This is in addition to the problems of weak labour productivity and other non-economic factors such as the high level of violent crime. These, of course, are outside the ambit of the central bank.

The instability that has retarded the country is reflected in the movements in the inflation rate which have been higher and more volatile than those of our main trading partners. It is also reflected in the recurrent bouts of instability in the exchange rate. These factors together contributed to relatively high nominal and real interest rates.

We all know that an exporter-friendly macroeconomic environment assumes a low rate of inflation, relatively low interest rates and high levels of productivity underpinned by a stable social environment.

The main objective of the medium-term economic programme is to fundamentally transform the Jamaican economy to facilitate growth. It does this in part through a reduction in inflation, greater stability in the exchange rate and lower interest rates. In the process, the programme aims at building a more resilient economy so that we will have more maneuvering room to cope with external shocks, such as the effects of the recent global crises which had such a devastating impact on Jamaica.

The immediate targets of the programme are the reduction of the debt overhang and stabilization of the fiscal accounts. The strategy to achieve this rests on two main pillars:

The first is a voluntary par-for-par exchange of domestic bonds for longer dated, lower coupon instruments. A key feature of these instruments is the liquidity they provide, which will facilitate greater trading of securities and hence the development of the domestic financial markets. The exceptionally high participation rate in the exchange (97 per cent) makes the Jamaica Debt Exchange (JDX) one of the most successful debt exchanges in the world. Significant savings to the Government and Jamaican tax payers will ensue from this exchange. Central Government interest payments in particular, will fall sharply from 16.2 percent of GDP in this fiscal year (ending 31 March 2010) to 9.7 percent of GDP by fiscal year 2013/14. Additionally, the magnitude of maturing debt is expected to decline by 65 percent over the next three years. This significant reduction in Government's refinancing needs will ease the crowding-out effect of Government debt and the upward pressure that this would have placed on domestic interest rates. We are already beginning to see strong signals from the market of a trend decline in interest rates following the JDX.

The second main pillar is represented by a package of measures and supporting reforms aimed at fiscal consolidation and entrenching fiscal and debt sustainability. Two key initiatives in this regard are the establishment of a fiscal responsibility framework and the implementation of a centralized treasury management system. The fiscal responsibility framework will codify the principles and make legally binding the application of prudent fiscal management, while the centralized treasury management system will facilitate more efficient management of financial resources across the public sector. Other initiatives include public sector reform and the divestment of non-core assets.

The fiscal programme aims to virtually eliminate the deficit over the next four years, thereby placing the debt trajectory on a sustained downward path. The progressive reduction in public sector demand will eliminate a sizeable portion of the current premium in Jamaica's interest rates that is related to macroeconomic uncertainty and sovereign risk. In short, the productive sectors of the economy will be able to finance working capital and longer-term investment at more competitive interest rates.

Underpinning the decline in interest rates is a low inflation regime that will target single digit inflation. In this regard, the annual rate of consumer price increases is expected to fall to the six to seven per cent range over the next four years. The Central Bank will therefore remain focused on its mandate of price stability, specifically single digit inflation. Low and stable inflation will facilitate longer-term planning by the productive sector. It will also temper the rate at which labour and other input costs will rise thereby enhancing the competitiveness of the export sector. The reduction in fiscal dominance implied by the fiscal and debt consolidation will enable the Central Bank to pursue the low inflation objective more effectively.

Critical to a stable macroeconomic environment is a sound financial system. A stable financial sector is important for the efficient intermediation of domestic and foreign investment financing on which the export sector depends. In this regard, the Bank of Jamaica Act will be amended to vest in the Central Bank the responsibility for overall financial system stability. Supporting this, will be the passage of an omnibus banking law that allows for more effective supervision of financial conglomerates. The financial sector reform process will also stimulate the expansion of the types of investment vehicles available to individual savers, thereby expanding the pool of loanable funds for the productive sector.

The comprehensive public and financial sector reforms are core structural benchmarks under the IMF Stand-by Arrangement. This agreement may prove to be a pivotal moment in Jamaica's economic history.

Let me conclude by acknowledging the significant effort that has been made in retooling and diversifying the export sector in Jamaica. I would also like to commend the initiatives that are being taken to enhance the development of the sector. I can assure you that the Bank will do its best to support your efforts from the standpoint of a central bank.

However, although a stable macroeconomic environment is a necessary condition for expanding Jamaica's exports, it is not a sufficient condition for improving competition in the world market, which requires us to produce sufficient quantities at the right quality and price. Indeed, some of the real challenges facing export sectors worldwide are the need for improvements in productivity and for adjustments in product quality to meet market requirements. Better marketing strategies are also needed. These factors are at least as important as a sound macroeconomic environment.

The message is therefore for the sector to focus on building on its achievements and on reshaping itself to take advantage of the new opportunities that are bound to arise as the global crisis subsides and growth resumes. Indeed, now is the time for all of us to act and to do so with conviction.

Thank you.

- ooo -