Quarterly Press Briefing

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07 March 2016

Accommodative Monetary Policy in Support of Growth

Good morning.

Today, Bank of Jamaica releases the Quarterly Monetary Policy Report for the October to December 2015 quarter. It describes the developments in the economy during the quarter and explains the Bank's policy actions and operations in this context.

Today, I would like to continue our discussion on 'crowding in'. Fiscal consolidation, a stable macroeconomic environment and Bank of Jamaica's accommodative monetary policy stance have created conditions in Jamaica for crowding in private sector investment. This is in contrast to most of our history when the government's appetite for domestic borrowing crowded out private sector investment.

I am pleased to report that we are seeing continued evidence of the crowding-in effect. Private sector credit increased by 9.6 per cent over the 12 months to the end of December 2015, compared to 7.8 per cent over the 12 months to the end of September 2015. In addition, the quarterly Credit Conditions Survey at September 2015 indicates that the supply of credit increased both to households and to businesses. Lenders also reported an increase in the demand for credit from small and medium-sized enterprises. A box on the credit conditions survey in today's report outlines how credit conditions have improved since the start of the economic reform programme.

When we last met, I noted that a prominent manifestation of the crowding-in effect would occur this year with the pay-out of the first maturing NDX bonds. The $62 billion pay-out took place as scheduled on 11 February 2016 with payments made smoothly, without incident and virtually instantaneously to bondholders through the JamClear - RTGS system.

Simultaneously, the government successfully restarted the domestic bond market with a $15 billion bond issue in three maturities: a two-year, a six-year and a 30-year. The issue was heavily oversubscribed and had to be closed early, within two hours of the opening. By that time, $17 billion, over and above the $15 billion accepted by the Ministry of Finance, had committed to these medium and long-term fixed-rate issues. This demonstrated overwhelming investor acceptance of government risk just ten business days before the general election, a period traditionally associated with risk-aversion and avoidance of long-term commitment. Clearly, domestic investors are again willing to buy long-term government debt and accept fixed interest rates in local currency.

However, unable to find a home, investment funds that were not taken up by the government sought short-term protection from uncertainty by seeking US dollars in the days that followed. Bank of Jamaica promptly met the resulting excess foreign exchange demand with sales of US Dollars and by issuing US Dollar-indexed one-year certificates of deposit ("CDs"). These operations together drained $23 billion from the system and restored balance to supply and demand in the foreign exchange market. The exchange rate has remained stable and net international reserves are still well in excess of the target.

As stakeholders turn their attention away from the recent electoral events, we expect that the weight of surplus liquidity in the banking system will intensify the crowding-in effect and we will see increasing downward pressure on interest rates and easing of credit terms for households and firms.

Turning to inflation, we are encouraged by the continued favourable flow of data as well as the near-term outlook. Inflation ended the December quarter, and therefore the calendar year, at 3.7 per cent, down from 6.4 per cent the year before. The consumer price index fell in January 2016 by 0.4 per cent to give a 12-month inflation rate of 3.7 per cent, which was below the 5.3 per cent recorded for the same period in 2015. Inflation for fiscal year 2015/16 is now expected to come in well below the target range of 5.5 to 7.5 per cent.

Our current projection for 12-month inflation over the next four quarters is between 4.5 per cent and 6.5 per cent. The public's expectations for inflation, as measured by Bank of Jamaica's latest survey of inflation expectations, are lower. In the December 2015 survey, the expected annual inflation 12 months ahead fell to an encouraging 4.4 per cent from 4.6 per cent in the September survey.

Exchange rate movements in free markets normally tend to compensate for the difference between inflation in a country and its trading partners. With the Jamaican dollar no longer overvalued, the improving inflation outlook and the resulting narrowing of the inflation differential between Jamaica and the United States means that the exchange rate will likely continue to exhibit relative stability going forward, although some correction may become necessary if the US dollar continues to strengthen against third currencies.

Macroeconomic stability has been supported by the ten successfully completed reviews of the economic reform programme under the Extended Fund Facility ("EFF") agreement with the International Monetary Fund ("IMF"). The eleventh review, covering the December quarter, would have commenced in February but was postponed by agreement between the government and the IMF because of the impending general election. We can note, though, that in our assessment the quantitative performance criteria and structural benchmarks for the review quarter have all been met. The eleventh review will now be combined with the twelfth review in May. Between now and then, we will be engaged in a period of intense policy dialogue with the IMF as the plans and programmes of the new government are developed in the context of the objectives of the EFF agreement. This dialogue began with a successful meeting on the first day of the new government between the Prime Minister and a Fund mission.

Ladies and gentlemen, BOJ has maintained an accommodative monetary policy stance in a context of the benign inflation environment and a supportive fiscal policy. This stance has encouraged an upward trend in credit to the productive sector. A further boost to credit expansion has come from the recent bond pay-out. These conditions bode well for faster growth from investments in infrastructure, capital equipment and training driving increased exports and import substitution.

Thank you.