BANK OF JAMAICA

Quarterly Press Statement

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Bank of Jamaica

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Good Morning Ladies and Gentlemen:

Today the Bank is releasing the Quarterly Monetary Policy Report for the March 2012 quarter. Given the current anxieties regarding the likely path for the main economic variables, I will first speak to the Bank's perspective on how they are likely to unfold in the near-term and the risks attending these perspectives. After that, I will highlight the major economic developments which had an impact on the achievement of the Bank's inflation target.

Near-term Outlook

Inflation

The Bank is currently forecasting that headline inflation will be in the range of 1.5 per cent to 2.5 per cent for the June 2012 quarter. This follows the out-turn of 1.7 per cent for the March 2012 quarter, which was within our forecast range of 1.0 per cent to 2.0 per cent. The current forecast assumes that imported inflation, domestic inflation expectations and capacity conditions will be relatively stable during the quarter.

Additionally, at this point, the Bank is projecting that headline inflation will be within the range of 6.0 per cent to 8.0 per cent for FY2012/13, largely similar to the previous fiscal year's out-turn. The assumptions underpinning this forecast include generally favourable weather patterns, both in Jamaica and the major grain producing countries, and a moderate increase in the price of crude oil given the projection for continued growth in the global economy.

However, there are significant upside risks to the forecast for inflation for both the current quarter and the fiscal year. The primary risk relates to the measures that may be announced in the imminent budget presentation to set the fiscal accounts and debt dynamics on a sustainable path for the medium-term. These measures could result in inflation exceeding the upper bound of the forecast range for both the June quarter and the fiscal year. This could be exacerbated by higher-than-anticipated oil prices if there is a resurgence in geopolitical tensions and growth in the world economy is stronger than is currently being projected.

Real GDP Growth

Continued slow growth is projected for domestic output for the June 2012 quarter, largely similar to the estimated expansion for the March 2012 quarter. ***Agriculture, Forestry & Fishing*** continues to be the major driver of growth and is expected to be supported by expansion in ***Mining & Quarrying***, ***Hotels & Restaurants*** and ***Electricity & Water Supply***.

For FY2012/13, economic output is projected to grow marginally in the range of 0.0 per cent to 1.0 per cent. The current outlook reflects the expectation of continued weak domestic demand, albeit improving relative to the crisis period, and a slower pace of expansion in world growth in calendar year 2012 relative to 2011. In spite of the forecast for a slowdown in world growth in 2012 relative to 2011, it is anticipated that with the steady recovery in the US economy there will be an increase in external demand for Jamaica's goods and services as well as acceleration in remittance flows to Jamaica.

Upside risks to the growth forecast include the impact on growth and employment of major investment projects later in the fiscal year. However, the risks to the growth forecast at this time are largely to the downside. Primary among these is the uncertainty regarding the extent of the fiscal consolidation to be announced. Fiscal consolidation would result in reduced domestic demand in the near-term which could be exacerbated by weaker global growth and the impact of adverse weather.

However, the Bank is forecasting that, should the fiscal measures materialise, the adverse impact on growth will be temporary. Inflation, after the initial impact of potential fiscal measures, is expected to decelerate over the medium-term towards the rate of inflation of our major trading partners. Additionally, economic growth should pick up in FY2013/14 and strengthen in the subsequent years consistent with the forecast for expansion in the world economy, the successful implementation of a number of foreign direct investment projects and the re-opening of two alumina plants.

Developments in the March 2012 Quarter

The performance of the main macroeconomic indicators was largely favourable in the March 2012 quarter. Inflation was 1.7 per cent for the review quarter, within the Bank's forecast range, which contributed to inflation of 7.3 per cent for the fiscal year, also within the range expected for the year. The foreign exchange market was also relatively stable with the weighted average selling rate of the US Dollar vis-à-vis the Jamaica Dollar depreciating by 0.8 per cent for the quarter and 1.8 per cent for FY2011/12. In addition, the Bank's estimates suggest that the nascent recovery in economic activity continued in the review quarter and resulted in the expansion for the fiscal year being also within the forecast range of 1.0 per cent to 2.0 per cent.

Of note, the up-tick in credit to the private sector which was observed in the December 2011 quarter continued into the March 2012 quarter. The increased demand for private sector loans could be reflective of the continued decline in commercial bank loan rates as depicted in the fall of 35 basis points in the weighted average rate of interest on private sector credit. Also encouraging was a marginal improvement in the quality of private sector credit with the ratio of non-performing loans, three-months and over declining to 8.4 per cent at end-March 2012 from 8.8 per cent at end-December 2011.

During the March 2012 quarter, market-determined interest rates remained broadly stable in the regular auctions of 30-, 90- and 180-day GOJ Treasury Bills. For example, the average yield on the 180-day Treasury Bill was 6.47 per cent at the March auction compared to 6.46 per cent at the auction last December.

There were intermittent periods of excess demand for foreign currency during the quarter in spite of the adequacy of net private capital flows to finance the demand for current account transactions. To augment supplies in the market the Bank sold US$102.1 million net which contributed to a decline of US$189.0 million in the net international reserves (NIR) to US$1 777.1 million by end-March. Partly as a result of these sales, the Bank's gross reserves at end-March 2012 amounted to US$2 638.9 million, representing 17.0 weeks of projected goods and services imports. During the review quarter, there were also concerns about the volatility of international commodity prices, particularly that of crude oil. Against the background of these uncertainties, the Bank maintained its monetary policy rate at 6.25 per cent for the March quarter.

Conclusion

Successful fiscal consolidation efforts, notwithstanding the near-term effects that I have identified today, will establish a downward trajectory to the government's debt burden and secure the macroeconomic stability that is the cornerstone of sustained long-term investment in the productive and social sectors alike. I will say also that while fiscal and debt sustainability are critical prerequisites for Jamaica to emerge from an extended cycle of low growth and high inflation, there also must be significant improvements in the country's external competitiveness. In that context, we have included an article on **External Competitiveness in Jamaica** in this quarter's report. We contend that external competitiveness has to be achieved and maintained not only through flexibility in the exchange rate but also critically through determined action to address our long-standing structural impediments.

In this regard, the Bank will continue to make its contribution by striving for low and stable inflation in support of sustained growth and development in the medium-term.

Thank you.