BANK OF JAMAICA

Quarterly Press Briefing

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Bank of Jamaica

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Good Morning Ladies and Gentlemen:

This morning the Bank is releasing the Quarterly Monetary Policy Report for the September 2011 quarter. In addition to the customary review of economic developments in the quarter and our outlook for economic developments in the near term, the report includes a special article on recent trends in electronic small-value retail payments and their relationship to economic growth.

Developments in the September 2011 Quarter

Global Developments

For the review quarter, global economic growth is estimated to have accelerated relative to the June 2011 quarter. This estimate largely reflects a faster pace of growth in the United States as well as normalization of economic activity in Japan. However, growth in the United Kingdom and the Eurozone as well as in emerging market economies is estimated to have slowed in the September quarter. In spite of the stronger growth in the September quarter, we are of the view that global expansion for the fiscal year will be at a slower pace than earlier projected.

There was a general decline in international commodity prices in the review quarter in spite of the estimate for a faster pace of expansion in world output. The decline in commodity prices largely reflected a sharp fall in the price of crude oil following the downgrade of US long-term debt by Standard & Poor's rating agency in August and the intensification of the European debt crisis. In addition, grain prices fell in the context of increased production in major producing countries and weak global demand.

Developments in the Domestic Economy

The Bank resumed the gradual easing of its monetary policy stance in the September 2011 quarter. The Bank's policy rate, the interest rate payable on 30-day certificates of deposit, was reduced on two occasions by a cumulative 50 basis points. Accordingly, at the end of September the policy rate was 6.25 per cent. The Bank's action was informed by an improved outlook for inflation for the rest of the fiscal year, a protracted period of stability in the exchange rate, adequate net international reserves and weak but improving domestic demand conditions.

You may recall that when we last met, I had indicated that volatility in the prices of international commodities in the June 2011 quarter had contributed to the decision to pause in the reduction of the Bank's policy rate. Well, the prices of international commodities generally declined during the September quarter and the outlook is for slower rates of increase for the rest of the fiscal year. In particular, the average price of crude oil declined by 12.5 per cent for the September quarter, more sharply than we had anticipated, and is expected to increase at a slower pace than previously projected for the fiscal year.

Against this background, headline inflation was 2.1 per cent for the September 2011 quarter, within the Bank's forecast range of 1.5 per cent to 2.5 per cent. The outturn also compared favourably with the 5-year average of 3.8 per cent for September quarters. In addition, at the end of September, the 12-month point-to-point inflation rate was 8.1 per cent relative to 11.3 per cent a year earlier. Similarly, at the end of September, all the Bank's annual measures of core inflation were markedly below the rates at the corresponding period a year ago.

Inflation in the review quarter largely reflected seasonal increases in the prices of domestic agriculture commodities as well as higher costs for educational items and tuition. However, the impact of these factors was moderated by continued weak but improving domestic demand conditions, a reversal in the prices of international commodities and the extended period of relative stability in the exchange rate. In fact, the exchange rate depreciated by a negligible 0.06 per cent between the end of September 2010 and the end of September 2011.

Outlook for the December 2011 Quarter & Fiscal Year 2011/12

For the December 2011 quarter, inflation is projected to be in the range of 1.0 per cent to 2.0 per cent, lower than the outturn for the previous quarter. The forecast is predicated on low imported inflation, a continued decline in inflation expectations and stable domestic capacity conditions. Given this forecast, the Bank expects that for the fiscal year ending on 31 March 2012, inflation will be within the target range of 6.0 per cent to 8.0 per cent.

The outlook for inflation for both the December quarter and the fiscal year has incorporated a projection for the seasonal increase in demand pressure in the foreign exchange market. This should mainly reflect the usual lower net private capital inflows. The demand for foreign exchange to facilitate current account transactions should abate given the expected moderation in commodity price increases and the seasonal increase in tourism flows. In this context, the Bank will intervene as necessary to smooth supplies in the market and ensure orderly movement in the exchange rate. However, gross reserves will remain comfortably above the international benchmark of 12 weeks coverage of projected imports of goods and services.

In this regard, I will digress a bit to speak briefly on the issue of the adequacy of the Bank's reserves. A central bank's international reserves are considered to be adequate when it satisfies a minimum desired precautionary balance and the central bank, as in Jamaica's case, is able to intervene in the foreign exchange market as the need arises.

The literature has identified three common indicators of reserves adequacy. These indicators compare the level of gross international reserves to, respectively, imports, short-term external debt or a broad measure of money supply. More recent thinking suggests that the reserves should be adequate to cover potential outflows in times of stress from all three sources combined. An assessment of the trajectory of the Bank's reserves against all of these indicators suggests that the Bank's reserves will be adequate into the medium term.

Returning to the report, the Bank's estimates indicate that there was continued real economic growth in the review quarter, albeit at a slower pace than the two previous quarters. The economy is estimated to have grown in the range 0.0 per cent to 1.0 per cent relative to average quarterly growth of 1.8 per cent for the first half of the calendar year. Expansion in the September quarter reflected growth in both the tradable and non-tradable industries, in particular, ***Mining & Quarrying*** and ***Construction***.

Growth is expected to accelerate in the December quarter relative to the previous quarter. In this regard, the economy is expected to grow in the range 1.0 per cent to 2.0 per cent in the quarter. The projected expansion will be driven by growth in ***Mining & Quarrying, Hotels & Restaurants, Construction*** and ***Agriculture, Forestry & Fishing***. These sectors are also expected to be the main growth poles for the fiscal year, which is still expected to reflect output growth in the range of 1.0 per cent to 2.0 per cent.

There are risks to the Bank's projections for both inflation and economic growth. Adverse weather conditions could derail both forecasts, while an unfavourable international environment could depress economic growth but lead to a better-than-expected inflation outturn. In addition, the persistence of weak domestic demand could also lead to lower output but a more satisfactory inflation rate. Conversely, improvements in the global economy could lead to sharper increases in commodity prices, hence higher-than-expected inflation, but would spur increased demand for Jamaican goods and services. Further, speculation about the date of the next general elections could add to uncertainties caused by the delay in the reviews of the medium-term economic programme by the International Monetary Fund (IMF).

Discussions are continuing with the IMF. The Government is engaged in talks with the public sector unions to agree on a way forward. Public consultations on the proposals for tax reform continue in accordance with the parliamentary schedule and in public forums across the country.

One of the structural benchmarks under the Stand-By Arrangement with the IMF is to amend the Bank of Jamaica Act to give the Bank overall responsibility for financial stability. Already approved by Cabinet, the proposals have also received comments from a number of stakeholders. The responsibility for financial stability being initiated in Jamaica is similar to what is being done by countries around the world. This is against the background of the recent global financial crisis which clearly indicated the need for a single authority to be in charge of macro-prudential regulation with the capacity to recognize and address systemic risks. Jamaica's initiative to formalize the financial stability role is based on a survey of international experience as well as our own experience. A discussion paper on the issue is on the Bank's website and I encourage you to read it and share your comments with us.

In summary, the macroeconomic indicators continue to point in the right direction. The Government is continuing to pursue the policies that underwrite long-term fiscal and debt sustainability, which in turn support macroeconomic stability. Against this background, the Central Bank will continue to monitor domestic and international economic developments and pursue policies consistent with ensuring price and financial system stability.

Thank you.