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Good Morning Ladies and Gentlemen:

As we release another of our Quarterly Monetary Policy Reports, I will be sharing with you the Bank's assessment of economic developments in the June quarter and the effect of these developments on monetary policy and price stability. I will also provide you with the Bank's near-term outlook.

Review of June Quarter

You would have noticed that the foreign exchange and money markets remained fairly stable in the June quarter, underpinned by a strong net international reserves position.

The positive influences on the markets during the quarter were:

- higher-than-expected foreign exchange availability;
- incremental borrowing by the Government, and
- the growing level of investor confidence in the sustainability of the current direction of monetary policy.

The stability of the foreign exchange market was reflected in a marginal depreciation of 0.6 per cent in the weighted average selling rate of the domestic currency. This followed a cumulative appreciation of 0.6 per cent over the two previous quarters.

Government's debt - raising initiatives on the international market also received positive responses as confidence in the macroeconomic policy increased. During the quarter the Government borrowed **US$300 million** from the international capital market. The bond carried a coupon rate of 9.0 per cent, which is the lowest rate at which a Jamaican bond has ever been issued on the international capital market.

As a result of the buoyant inflows to the foreign currency market, the net international reserves (NIR) was **US$2.156 billion** at the end of June, an increase of **US$255.2 million** relative to end-March. Gross reserves at end-June were **US$2.179 billion**, representing **19.6 weeks of estimated goods and service imports.**

In the context of the strong NIR position, buoyant foreign currency inflows and stable financial markets, the Bank reduced the Special Deposit Requirement from 3.0 per cent to 1.0 per cent on May 16th. This was followed by a reduction in interest rates on the spectrum of open market instruments on 26 May 2005. Consequently, at the end of June, the highest rate offered by the Bank was 13.6 per cent on the 365-day instrument relative to 14.25 per cent at end - March.

The Bank estimates that there was moderate growth in the June quarter. This growth emanated primarily from services, as expansion in the goods - producing sectors was constrained by an estimated decline in *agriculture*. Recovery in this sector has continued to be retarded by adverse weather conditions.

I now turn to **INFLATION,** which was the major area of concern during the quarter.

For the June quarter, headline inflation was 5.7 per cent - higher than we had anticipated when I last addressed you in May.

The higher-than-expected out-turn for inflation stemmed largely from increases in the prices of domestic agricultural products and higher increases in international oil prices than we anticipated. In addition, the tax measures that were implemented in April/May added significant impulses to inflation during the quarter. On a monthly basis, inflation was 1.9 per cent in April, increased to 2.2 per cent in May and moderated to 1.5 per cent in June.

The effects of the hurricane and drought conditions, which we experienced between September 2004 and March 2005, continued to have a negative impact on the supply of agricultural products. In fact, the production of some of the major agricultural commodities suffered declines ranging from 11.8 per cent to 46.5 per cent in the June quarter. This led to significant increases in the prices of these commodities, particularly those in the *Starchy Foods* and *Fruits & Vegetables* category.

In spite of the sharp increase in headline inflation, the Bank continued to restrain monetary expansion. Consequently, the movement in core inflation was kept to 1.7 per cent for the June quarter, slightly higher than the 1.1 per cent estimated for the March quarter.

<u>Near – Term Outlook</u>

Ladies and Gentlemen, as you are aware, Jamaica suffered some damage from the recent passage of Hurricanes Dennis and Emily. While we were spared a direct hit, some parishes were badly affected by severe flooding. Preliminary estimates indicate that once again ***Agriculture*** sustained some damage, albeit, much less than with the passage of Ivan. There are also reports of some agricultural areas being cut off due to the collapse of roadways.

With the damage to the agricultural sector, the Bank has revised its growth forecast downwards for the September quarter and also for the fiscal year. We expect that expansion in the real sector will be led by mining, construction, manufacturing and distribution.

Against this background, the Bank expects some moderation in inflation in the September quarter, relative to the June quarter. However, we expect that the deceleration will be at a slower pace than originally anticipated. However, going forward, the Bank is forecasting a faster rate of deceleration in inflation during the second half of the year.

For the September quarter, we are anticipating some inflationary impulses from the increased prices of agricultural commodities due to temporary short supplies arising from the recent adverse weather conditions. In addition, the upward trend in international oil prices will continue to affect the prices of goods in the consumer basket. The Bank is also expecting some lagged impulses from the recent increases in GCT and SCT.

However, we expect that during the September quarter the inflationary impulses will be moderated by continued stability in the foreign exchange market, especially as this will be supported by a strong NIR position.

With the concerns regarding inflationary pressures, the Central Bank, in the near term, intends to maintain a conservative policy stance consistent with the targets in the financial programme.

However, as the inflationary tendencies are reversed and the growth momentum resumes, the Bank will adjust policy accordingly so as to continue on our path to attaining inflation in line with that of our major trading partners. In this context we remain committed to the goal of achieving a stable economic environment that will sustain strong long-term economic growth.

In closing, I would like to draw your attention to two special features in the Quarterly Monetary Policy Report, which deal with issues related to the work of the Central Bank. These are: “Credit Bureaux and Financial Market Efficiency;” (Box 1) and “Trends in Labour Productivity,” discussed in Box 2. We trust that these articles will provide additional information to assist your understanding of the issues.

I now welcome your questions.

Thank you.