ANNUAL REPORT

2003

Report and Statement of Accounts for the
Year Ended 31 December 2003

Mission Statement

The mission of the Bank of Jamaica
is to formulate and implement
monetary and regulatory policies
to safeguard the value of the domestic
currency and to ensure the soundness
and development of the financial system
by being a strong and efficient
organisation with highly motivated
and professional employees
working for the benefit of
the people of Jamaica.

BANK OF JAMAICA
NETHERSOLE PLACE
KINGSTON

31 March 2004

Dr. The Hon. Omar Davies
Minister of Finance & Planning
National Heroes Circle
Kingston 4

Dear Minister:

In accordance with Section 44 (1) of the Bank of Jamaica Act, 1960, I have the honour of transmitting herewith the Bank's Report for the year 2002 and a copy of the Statement of the Bank's Accounts as at 31 December 2003 duly certified by the Auditors.

Yours sincerely,

Derick Latibeaudiere
Governor

PRINCIPAL OFFICERS

GOVERNOR & SUPERVISOR OF BANKS
Mr. Derick Latibeaudiere

DEPUTY GOVERNORS

Mrs. Audrey Anderson	Financial Institutions Supervisory Division
Mr. Colin Bullock	Research & Economic Programming Division Banking & Market Operations Division

GENERAL COUNSEL

Mr. Rudolph Muir	Corporate Secretary's Division

DIVISION CHIEFS

Mrs. Myrtle Halsall	Research & Economic Programming Division
Mrs. Gayon Hosin	Financial Institutions Supervisory Division
Mr. Herbert Hylton	Finance & Technology
Mr. Kenloy Peart	Administration & Technical Services Office
Mrs. Faith Stewart	Banking & Market Operations Division

SENIOR DIRECTORS

Mr. Randolph Dandy	Senior Legal Counsel Legal Department
Mrs. Natalie Haynes	Senior Director Financial Markets Sub-Division Banking & Market Operations Division
Mrs. Evadnie Sterling	Chief Internal Auditor Internal Audit Department
Mr. Oswald Tie	Senior Director Protective Services Department

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1. OVERVIEW

In 2003, the Bank of Jamaica (BOJ) operated within a context of severe macro-economic challenges, particularly in the first half of the year. Uncertainty in the domestic market coupled with unfavourable conditions in the international capital market contributed to significant volatility in the foreign exchange market and acceleration in the rate of depreciation. As a result of these developments, the Bank's monetary policy initiatives had to be focused on stabilizing the foreign exchange market and restoring investor confidence in holding Jamaica Dollar financial assets. By year-end this was achieved, albeit at higher domestic interest rates. The impact of the developments underscored the importance of the efforts of the Bank to fulfill its mandate to preserve the value of the Jamaica Dollar and foster the stability of the financial system.

In an effort to ensure the soundness and stability of Jamaica's financial system, the operations of the Bank were geared to further improving the integrity and efficiency of the payments system and continuing its close surveillance of the operations of the deposit-taking entities. During the year, remittance companies were added to the Bank's oversight and the banking legislation was amended and supporting regulations developed to provide the Central Bank with the legal authority to monitor these entities. The staff complement of the Bank was also increased by 47 to 472 in 2003 to accommodate new responsibilities assigned to various departments.

Uncertainty in the domestic market developed from as early as December 2002 with the official announcement of a fiscal disjuncture and a downgrade in the rating of Jamaica's sovereign debt by Standard and Poor's. This was exacerbated by the news of an impending war in Iraq. The prospects for the Government raising funds externally to cover a maturing euro-bond in February were unfavourable, and consequently, the debt was financed by the Government's purchase of foreign exchange from the BOJ. The resultant loss in the country's net international reserves contributed to an increase in speculative activity evidenced by a switching from domestic currency financial assets to foreign currency investments in the domestic market and abroad. The rate of depreciation in the exchange rate accelerated and monetary policy had to be progressively tightened in the first half of 2003.

In addition to selling greater amounts of foreign exchange to the market, the Bank instituted a 'Special Deposit' reserve requirement for deposit-taking financial institutions on 10 January 2003. In February, a 150-day open market instrument with an interest rate of 30.0 per cent was introduced for four days. Throughout this period the BOJ remained committed to ensuring that the interest rate structure was at a level that was consistent with restoring and sustaining a stable financial environment. In this context, the Bank raised interest rates on 19 March and again on 26 March, with the rate on the 365-day instrument peaking at 35.95 per cent at the end of the first quarter. As conditions in the money markets settled, rates were reduced twice in the second quarter, with the 365-day rate falling to 30.0 per cent. By end December, this rate had been gradually reduced to 23.0 per cent.

In the second half of the year, policy challenges arose mainly from the Government's demand for domestic financing. In this context, the Bank increased its holdings of Government of Jamaica (GOJ) securities in cases where public offers were under-subscribed due in part to insufficient market liquidity. The resulting un-programmed monetary injections led to base money increasing faster than programmed in the last four months of the year.

The monetary base increased by 13.3 per cent in 2003, reflecting a 12.4 per cent increase in the stock of currency issue. The broad measure of money supply, M2* increased by 11.2 per cent, slower than 13.0 per cent in 2002. Developments in the consolidated assets and liabilities of the commercial banks reflected the Government's high demand for domestic financing, depreciation in the exchange rate and the pattern of real economic activity. Total assets of the six commercial banks grew by 19.7 per cent in 2003, relative to 10.3 per cent in 2002. The 2003 out-turn largely reflected a 9.3 per cent increase in Jamaica Dollar GOJ securities and 29.4 per cent in GOJ foreign currency securities. The banks' liabilities at December 2003 showed an increase in the ratio of foreign currency deposits to total deposits to 31.1 per cent from 26.7 per cent in December 2002. This increase in the ratio partly reflected the proliferation of repurchase agreements by banks as a source of funding. Continued strong growth in private sector loans was primarily channeled into *personal loans, tourism, transport, storage & communication and distribution,* accounting for 76.7 per cent of the total private sector loan stock at end 2003.

The pattern in commercial bank lending was consistent with the distribution of growth in real economic activity. The Jamaican economy is estimated to have grown within the range of 2-3 per cent in 2003. Growth was stronger in the services industries, which together accounted for 72 per cent of real GDP in 2003. An expansion in mobile telephone networks and increased tourist arrivals contributed to the strong performance in the *transport, storage & communication and miscellaneous services* sub-sectors. In the goods producing sectors, strong economic performance is estimated in *domestic agriculture* and *mining*. Agricultural production benefited from favourable weather conditions in 2003 compared to the adverse impact of flood rains experienced in mid-2002. In the mining sector, with capacity utilization of approximately 97.0 per cent, alumina production grew by 5.7 per cent in 2003 and export volumes increased by 7.0 per cent. Unfavourable weather conditions led to a decline in bauxite mining.

Headline inflation of 14.1 per cent in 2003 disrupted the trend of six consecutive years of single digit inflation. The outturn was influenced by a number of factors, including foreign exchange rate depreciation, increased inflation expectations, revenue enhancement measures of the Government, as well as international commodity prices. A depreciation of 15.90 per cent in the exchange rate had a strong influence on price setting by producers and traders, and accounted for approximately 60.0 per cent of annual inflation. In the first quarter, inflation was due in part to the widening of the General Consumption Tax (GCT) net to include a wide range of items, which were previously exempt or zero-rated. During the year, taxes were increased on alcoholic drinks, and the introduction of a 2.0 per cent customs user-fee contributed to price movements in the *miscellaneous expenses* sub-category.

An increase in world commodity prices influenced local prices and reflected the unrest in the Middle East and heightened world demand. Crude-oil prices increased by 15.8 per cent in 2003, relative to 2.5 per cent in 2002. The prices of non-fuel commodities increased as world demand for rice and corn rose. The escalation in demand was in the context of a 3.2 per cent increase in global economic activity in 2003 compared to 3.0 per cent in 2002. The increase in crude oil prices had an unfavourable effect on prices in the f*uels and other expenses* sub-group accounting for 7.8 per cent of the inflation out-turn. Price movements in vegetable oils and grains had an impact on the sub-groups of *baked products, cereals & breakfast drinks, dairy products oils & fats*. These groups contributed 13.2 per cent to inflation.

Core inflation for the year was 8.1 per cent compared to 3.4 per cent in 2002. On a monthly basis, core inflation trended upwards in the first half of the year in the context of the sharp depreciation in the Jamaica Dollar. Underlying inflation, however, moderated in the second half of the year reflecting the effects of tightened monetary policy.

An improvement in Jamaica's balance of payments in 2003, after three years of deterioration, was associated with the increased spending and investment in the developed countries. In the United States of America, an expansion in investment and consumer spending contributed significantly to growth in that economy accelerating by 0.7 percentage points to 3.0 per cent in 2003. In that context, Jamaica's current account deficit is estimated to have improved by US$114.9 million to US$1 003.3 million or 12.4 per cent of GDP in 2003. This compares to a deficit of 13.3 per cent in 2002. Significantly contributing to this improvement was an increase in net receipts from travel and continued growth in current transfers, in particular, remittances. The impact of the improvement in the current account on the balance of payments was countered by a decline in *net other official inflows* category of the capital account. This resulted from the fact that the Government did not borrow on the international markets to facilitate a euro-bond loan repayment. *Net other private investments* increased, but provided insufficient financing to cover net outflows from official investment and the capital and current accounts. As a consequence, there was a reduction of US$432.1 million in Jamaica's foreign reserves, resulting in a stock of US$1 168.6 million at 31 December 2003, covering an estimated 12.9 weeks of imported goods and services.

In the financial sector, the Bank increased its scope of supervisory responsibility and commenced on-site examination of credit unions in August 2003. This group of institutions numbered 52 at end 2003. By year-end, 13 of the larger entities, representing 65 per cent of the sector's assets were examined by the Bank. In strengthening the general supervisory framework for deposit-taking institutions, policy initiatives continued to be geared towards achieving full compliance with the 25 Basel Core Principles. The primary areas of attention included consolidated supervision of banking groups, the preservation of the Anti-Money Laundering/Anti-Terrorism Financing Regime within international standards, the New Capital Accord (Basel II) and the financial system's adoption of International Financial Reporting Standards (IFRS).

Central to the continuation of real growth in 2004, is the sustained increase in global economic activity. Also, maintaining financial system stability will be contingent on the smooth functioning of domestic financial markets. The IMF's World Economic Outlook suggests that world output will increase by 4.1 per cent, and the US Federal Reserve Bank estimates that the USA, Jamaica's main export market, should grow by 4.0-5.0 per cent in 2004. However, security and geopolitical concerns continue to endanger the growth forecasts.

The Jamaican economy is well poised to realize growth of 2.0-3.0 per cent in 2004. This is predicated on continued increase in visitor arrivals, accelerated growth in finance and insurance services, as well as continued growth in agriculture and mining. The main economic challenges for the year include the restoration of single digit inflation in the context of the attainment of the fiscal targets and uncertain international oil prices. Stability in the financial system will depend on conditions in the international market, and continued efficiency in domestic financial intermediation. The realization of these objectives will provide the opportunity for further lowering of interest rates.

2. THE FINANCIAL SYSTEM

2.1 Base Money Management

2.1.1 Introduction

Price stability remained the primary objective of monetary policy during 2003. In the pursuit of this objective, the Bank of Jamaica was challenged by a variety of circumstances including episodes of volatility in the foreign exchange market as well as public sector financing requirements. Thus, several of the actions taken by the Bank during the year were motivated by the need to mitigate the inflationary impulses associated with excess demand in the foreign exchange market, especially in the first half of the year.

2.1.2 Developments and Challenges

The greatest challenge to macroeconomic policy management during the year was the restoration and preservation of domestic and foreign investor confidence in the Jamaican economy. Consequently, monetary policy was geared at stabilizing conditions in the Jamaican financial markets. For the January to March period, there was an exacerbation of deteriorating foreign exchange market conditions, which had begun in December 2002. The initial loss of confidence accompanied the revelation that Government had deviated from its fiscal targets. That announcement was immediately followed by Standard & Poor's downgrade of Jamaica's foreign currency sovereign debt. There were also uncertainties about programmed foreign currency inflows in light of the prospect of war in Iraq. Conditions were therefore unfavourable for the Government to source funds internationally to repay a Eurobond that matured in February. The settlement of this obligation via the purchase of foreign exchange from the BOJ led to a significant loss in the net international reserves.

Several approaches were taken to restore stability to the money and foreign exchange markets in the first quarter of the year. These included a Special Deposit requirement, the introduction of a 150-day open market instrument and upward adjustments of interest rates. Despite the tightening of the monetary policy stance in the March quarter, volatile conditions again emerged in the foreign exchange market towards the end of April. The resurgent instability was generated by excess demand for foreign currency by domestic investors in light of uncertainty about the impact of the fiscal measures announced in the 2003/04 budget.

The Bank was able to moderate the rate of depreciation and thereby lessen inflationary impulses via the sale of foreign exchange while it maintained the high premia on its open market instruments. This was supported by the Prime Minister's May 2003 statement of resolve to restore stability to the foreign exchange market. By mid-May, the instability in the foreign exchange market had been moderated. The policy stance also contributed to a shift of a significant amount of Jamaica Dollar liquidity into the 270-day and 365-day open market tenors that would mature in 2004. With the reduction of the pressure of heavy short-term maturities, the Bank was able to consistently reduce the rates applied to its open market instruments over the rest of 2003 and into 2004 (see **Table 2**).

A further challenge to monetary policy emanated from the Bank's temporary financing of Government needs, where primary offers by the government were under-subscribed. These unprogrammed monetary injections contributed significantly to the expansion in base money especially in the October to December period. The intention was to resell these securities as market liquidity permitted.

There was an increase of 13.3 per cent in the monetary base in 2003 relative to 4.2 per cent in 2002 (see **Table 1b**). The faster rate of expansion embraced a higher rate of growth in the stock of currency issue in the calendar year under review. The average annual growth rate of currency issue in 2003 was 12.4 per cent relative to 9.1 per cent in 2002. The higher growth was associated with the impact of higher headline inflation during the year.

At the end of the year, the stock of base money was $40 526.3 million, representing an outturn of $4 162.8 million or 11.4 per cent above the indicative target outlined in the financial programme (see **Table 1a**). The Net International Reserves (NIR) stock of US$1 165 million at end December surpassed the programme target of $709.8 million. This was due to foreign exchange market stability especially in the second half of the year as well as a significant block of official inflows. The Net Domestic Assets (NDA) was lower than the programmed ceiling despite the significant increase in net claims on the public sector and the unwinding of open market instruments. The lower NDA reflects the tighter monetary policy stance in the form of the special deposit.

2.1.3 January to June

For the first half of the year, the monetary base declined by $3 352.9 million or 9.4 per cent largely as a result of the $3 257.9 million or 9.1 per cent decline in the March quarter. The decline in the first quarter reflected the impact of the net seasonal currency redemption that amounted to $3 624.8 million.

The major source of the decline in base money for the first six months of the year was a reduction of $25 028.5 million in the NIR. At the end of June, the NIR stood at US$1 127.4 million, resulting from consecutive declines of US$257.3 million and US$212.3 million in the first and second quarters. The decrease in the March quarter was largely attributed to the sale of 200 million to the Government in February for the repayment of a maturing Eurobond. For the June quarter, the decline was mainly a result of significant sales of foreign currency by the Bank to arrest a prolonged episode of instability in the foreign exchange market. The high demand for foreign currency was for the most part funded by the unwinding of $12 854.9 million in open market instruments during the first half of the year and by the currency redemption.

The implementation of a special deposit scheme for commercial banks and institutions licensed under the Financial Institutions Act was the first in a series of actions taken by the Bank to restore order to the foreign exchange market. Effective 10 January, these institutions were required to hold 5.0 per cent of their average prescribed domestic liabilities on deposit at the Bank, a move designed to withdraw excess liquidity from the system. The impact of this action was only temporary as conditions in the foreign exchange market again deteriorated within a few weeks. In response to the acceleration in the rate of deprecation, on 10 February, the Bank introduced a 150-day open market instrument at an interest rate of 30.0 percent, 15.5 percentage points above the rate on the 365-day instrument (see **Table 2**). This engendered an immediate and sharp appreciation in the exchange rate and significantly tightened Jamaica Dollar liquidity. The instrument was withdrawn four days later on 14 February.

The appreciation of the exchange rate was short-lived, however, as a sufficiently influential block of investors continued to convert their Jamaica dollar deposits into foreign currency. The Bank responded by increasing interest rates on the entire spectrum of open market instruments on two occasions (19 March and 26 March). Consequently, during March interest rates increased by 21.45 percentage points on the 365-day instrument (see **Table 2**). This last initiative fostered orderly conditions in the foreign exchange market for the remainder of the March quarter and for the greater part of April.

Given the restoration of order in the foreign exchange market during this period, on 25 April the Bank reduced rates on some of its open market instruments. The rate on the 365-day

instrument declined by 2.95 percentage points (see **Table 2**). However, evidence of uncertainty re-emerged, as following the announcement of the fiscal measures for the 2003/04 fiscal year, there was intensification in the demand for foreign currency. To stem the pressure, the Bank augmented the supply of foreign currency. On 18 May, the Prime Minister made an announcement that communicated, *inter alia*, the Bank's continued commitment to a stable foreign exchange environment. This action, in tandem with the high premiums on the open market instruments and the continued sales of foreign currency, proved sufficient to stabilize the foreign exchange market. The improved outlook for increased foreign exchange inflows from tourism and the short duration of the war in Iraq further reinforced orderly conditions. Against this background, the Bank was able to further reduce rates on open market instruments, notwithstanding the downgrade of Jamaica's foreign currency sovereign debt from Ba3 to B1 by Moody's Investor Service. With this action, the highest rate was reduced to 30.0 per cent on 24 June (see **Table 2)**.

2.1.4 July to December

The monetary base expanded by $8 121.4 million or by 25.1 per cent during the second half of the year. This expansion was mainly reflected in the 27.2 per cent increase in currency for the month of December. This expansion of currency was higher than the average 23.5 per cent for December observed over the last three years and was funded by the liquidity emanating from the Bank's increase in its holdings of Government securities and the Government's draw down of its deposits held at the Bank. Additionally, the net redemption of open market securities by banks and other institutions also financed the demand for cash in the period. Despite the fact that the base money outturn was higher than target, the July to December period was characterized by relative stability in the financial markets. Liquidity levels were low as a direct result of the policy stance adopted by the Bank in the first half of the year. Domestic investors exhibited increased confidence in the economy as evident from the demand for Jamaica Dollar financial assets.

The major source of the growth in the monetary base was the expansion of $11 047.2 million in claims on Central Government by the Bank. Some of the liquidity from this source was offset by open market operations, as there were net issues of $4 843 million during the July to December period. In contrast to the first half of the year, the NIR contributed to the base money expansion as it was built up by US$37.6 million, which represented an injection of $2 217.9 million. As at end December, the NIR stood at US$1 165 million.

The improvement in financial market conditions in the second half of the year was due chiefly to the policy measures implemented between January and June. Given the resulting improvement in inflation expectations, the Bank aggressively implemented three reductions in interest rates on open market instruments during the September quarter (see **Table 2**). These adjustments resulted in reducing the premium on the longer dated open market tenors giving rise to a more normal yield curve (see **Chart 1**). While conditions in the financial system remained relatively calm in the December quarter, instability resurfaced in the foreign exchange market in October due to the seasonal demand for foreign currency to pay for imports. However, this brief episode was tempered by intervention sales by the Bank to the market. Market conditions permitted only one further interest rate reduction during the remainder of 2003 (see **Table 2**).

Chart 1

BOJ OMO Yield Curve

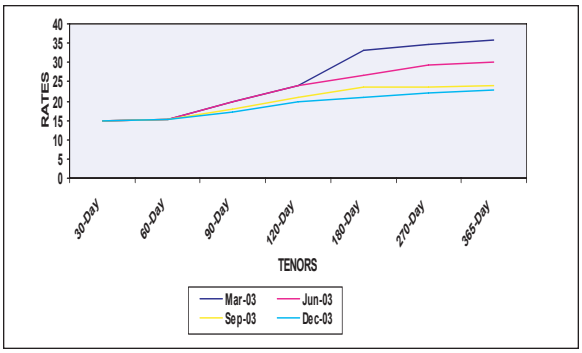


Table 1a

Bank of Jamaica - Economic Programme Targets Stocks J$M December 2003			
	Target	**Out-turn**	**Deviation from Target**
Net International Reserves (US$)	709.8	1 165.0	455.2
NET INT'L RESERVES (J$)	44 161.9	68 733.8	24 751.9
NET DOMESTIC ASSETS	-7 798.4	-28 207.5	-20 409.1
MONETARY BASE	36 363.5	40 526.3	4 162.8

Table 1b

Bank of Jamaica - Summary Flows J$M						
	2002 Total	**Jan- Mar**	**2003 Apr- Jun**	**2003 Jul- Sept**	**Oct-Dec**	**2003 Total**
Net International Reserves (US$)	**-243.8**	**-257.3**	**-212.3**	**55.2**	**-17.6**	**-432.0**
NET INT'L RESERVES (J$)	**-12 026.7**	**-13 140.8**	**-11 887.7**	**3 259.2**	**-1 041.3**	**-22 810.7**
-Assets	-12 825.4	-13 324.7	-12 149.2	3 036.1	-1 199.5	**-23 637.2**
-Liabilities	798.7	183.9	261.5	223	158.1	**826.5**
NET DOMESTIC ASSETS	**13 474.8**	**9 882.9**	**11 792.6**	**-3 041.5**	**8 945.1**	**27 579.2**
Net Claims on Public Sector	**17 899.5**	**13 115.0**	**3 622.5**	**3 160.5**	**7 885.5**	**27 783.5**
- Central Govt. Deposits	5 910.5	4 475.7	-1 692.1	967.4	3 048.9	6 799.8
- Govt. Securities	28 593.0	4 237.6	3 216.8	1 548.2	9 499.0	18 501.6
- FINSAC Securities	-26 996.8	0	0	0	0.0	0.0
- Other	10 392.8	11 313.5	-8 726.7	2 890.0	877.6	6 354.4
Net Credit to Banks	**953.6**	**-7 281.2**	**-643.6**	**310.5**	**-531.3**	**-8 145.5**
Open Market Operations	**-4 353.1**	**3 777.5**	**9 077.4**	**-6 573.9**	**1 730.9**	**8 012.0**
Other	**-1 025.2**	**271.6**	**-263.7**	**61.4**	**-140.1**	**-70.8**
MONETARY BASE	**1 448.1**	**-3 257.9**	**-95.0**	**217.7**	**7 903.7**	**4 768.5**
- Currency Issue	2 014.0	-3 624.8	529.4	286.6	7 880.7	5 072.0
- Cash Reserve	-635.1	411.5	-290.7	-148.8	116.9	89.0
- Current Account	69.3	-44.6	-333.8	79.9	-94.0	-392.4
Memo:						
NIR Stock (US$M) e.o.p.	1 597.0	1 339.7	1127.4	1 182.6	1 165.0	
Growth in Monetary Base	4.2	-9.1	-0.3	0.7	24.2	13.3
Inflation	7.3	-0.4	6.0	4.6	3.4	14.1

Table 2

BOJ Reverse Repurchase Rates (%)
January - December 2003

	Jan 01	Feb. 10	Feb. 14	Mar. 19	Mar. 26	Apr. 25	Jun. 24	Jul. 08	Aug. 04	Sept. 09	Dec. 10
30 Days	12.95	12.95	12.95	12.95	15.00	15.00	15.00	15.00	15.00	15.00	15.00
60 Days	13.05	13.05	13.05	13.05	15.30	15.30	15.30	15.30	15.30	15.30	15.30
90 Days	18.25	18.25	18.25	18.25	20.00	20.00	20.00	20.00	18.00	18.00	17.00
120 Days	18.40	18.40	18.40	18.40	24.00	24.00	24.00	24.00	22.00	21.00	20.00
150 Days	N/A	30.00	N/A	N/A	N/A	N/A	N/A	N/A	N/A	N/A	N/A
180 Days	13.45	13.45	13.45	19.65	33.15	28.00	26.50	26.50	25.00	23.50	21.00
270 Days	13.85	13.85	13.85	21.50	34.50	32.50	29.50	27.50	25.75	23.75	22.00
365 Days	14.50	14.50	14.50	24.00	35.95	33.00	30.00	28.00	26.00	24.00	23.00

2.2 Monetary Survey

The growth in broad money supply, M2*[1] slowed to an an increase of 11.2 per cent in 2003 relative to 13.0 per cent in 2002 (see **Table 3**). The outturn reflected not only an increase in the currency to deposit ratio but a shift in the currency composition of deposits, influenced by developments in the foreign exchange and money markets. During the first two quarters of 2003, there was significant accumulation of foreign currency deposits as investors sought to preserve the value of their financial assets in a context of the instability that prevailed in the foreign exchange market and a waning of investor confidence in the economy. In response to the increased demand for foreign currency, monetary policy was tightened through several initiatives (see **Base Money Management**), which led to the re-emergence of relative stability in the foreign exchange market and a restoration of investor confidence during the second half of the year. The eventual normalization of expectations was evidenced in an increased demand for Jamaica Dollar deposits and other domestic financial assets.

The M1*[2] component of broad money supply, M2* increased by 7.3 per cent, a slower rate of growth than the 13.6 per cent recorded in 2002, while quasi money grew by 12.9 per cent during 2003 relative to growth of 12.7 per cent in 2002.

[1]Money supply M2* represents banking system domestic and foreign currency liabilities to the private sector in the form of currency, demand, time and saving deposits.
[2]M1* excludes the time and saving deposits component of M2*.

Growth in M1* during 2003, was driven by a 13.6 per cent increase in currency with the public, a faster rate of expansion relative to 8.6 per cent in 2002. In real terms, currency with the public grew by 3.0 per cent during 2003 relative to 1.4 per cent in 2002. Demand deposits recorded growth of 3.2 per cent, a significantly slower rate than the 17.1 per cent increase in 2002. Simultaneously, there was slower growth in the components of quasi money, which would have been influenced by the relatively higher rates of return offered on alternate domestic instruments. Savings and time deposits increased by 18.0 per cent and 0.3 per cent, respectively, during 2003. This compared with growth of 12.8 per cent and 12.5 per cent, in savings and time deposits, respectively during 2002 (see **Table 3**).

The major source of expansion in M2* during 2003 was an increase in credit extended by the banking system to the public and the non-financial private sectors. Net claims on the public sector expanded by $44 989.8 million or 32.1 per cent in 2003, compared to an increase of $21 319.8 million or 16.4 per cent in 2002. This largely reflected Central Government's increased reliance on domestic financing as there was little borrowing from international markets during the year. Private sector credit increased by $22 876.3 million or 44.8 per cent in 2003, significantly faster rate than the 27.5 per cent recorded in 2002 and reflected the aggressive marketing strategies undertaken by the banks. A reduction of $8 011.9 million in the stock of BOJ's open market operations instruments outstanding also contributed to the growth in money supply.

Table 3

Money Supply, M2*
(Domestic and Foreign Currency)

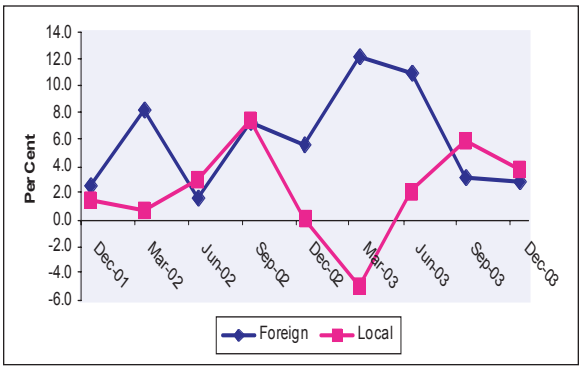
	2002 (J$M)	2003 (J$M)	2002 %	2001 (J$M)
		Components of Money Supply		
Money Supply (M2)*	18 964.5	18 466.5	13.0	11.2
Money Supply (M1)*	6 176.7	3 767.9	13.6	7.3
Currency with the public	1 621.4	2 779.4	8.6	13.6
Demand Deposits	4 555.4	988.6	17.1	3.2
Quasi Money	12 787.8	14 698.6	12.7	12.9
Savings Deposits	9 197.3	14 608.6	12.8	18.0
Time Deposits	3 590.5	90.0	12.5	0.3
		Sources of Money Supply		
Net Foreign Assets	**-9 474.8**	**-25 796.6**	**-7.6**	**-18.0**
Bank of Jamaica	-12 026.8	-22 810.8	-10.9	-15.7
Commerical Banks	2 552.0	-2 985.8	69.9	-48.1
Loans and Advances to Private Sector	**11 046.7**	**22 876.3**	**27.5**	**44.8**
Local Currency	4 973.3	14 495.1	17.3	43.1
Foreign Currency	6 073.4	8 381.2	53.5	48.1
Net Claims on Public Sector	**21 319.8**	**44 989.8**	**16.4**	**32.1**
Net Claims on Financial Institutions	**3 345.1**	**-4 484.1**	**23.0**	**40.0**
BOJ Open Market Operations	**-4 353.0**	**8 011.9**	**5.1**	**-8.9**
Other Items (Net)	**-2 919.3**	**-27 130.9**	**94.5**	**287.3**
TOTAL	**18 964.5**	**18 466.5**	**13.0**	**11.2**

The liquidity impact from these sources was partially countered by reductions of $25 796.6 million and $27 130.9 million in the net foreign assets (NFA) of the banking system and other items (net), respectively. The reduction in the NFA of the banking system largely reflected a $22 810.8 million decline in the NFA of the BOJ (see **Base Money Management**). A decline of $2 985.8 million in the NFA of the commercial banks was influenced by the widening of the interest rate spread on domestic currency vis-à-vis foreign currency investments and relative stability in the foreign exchange market during the second half of the year. The growth in other items (net) was largely reflected in a notable increase in securities sold under Repurchase Agreement by commercial banks. This non-traditional source of funding increased partly due to higher interest rates offered on the instruments during periods of tight liquidity conditions.

A more detailed analysis of money supply showed a shift in the currency composition of deposits. **Chart 2** reflects the evolution of the currency composition of deposits on a quarterly basis since 2001. During the first quarter of 2003, while local currency deposits declined, there was a sharp increase in foreign currency deposits in the context of the instability that prevailed in the foreign exchange market. Although the Central Bank responded to this instability by tightening monetary policy, there was further growth in foreign currency deposits during the second quarter albeit at a slower rate, and local currency deposits increased. This growth in local currency deposits continued into the September quarter when there was a notable slowdown in the rate of accumulation of foreign currency deposits that continued into the December quarter. During the December quarter, both local and foreign currency deposits increased at a slower rate relative to that which obtained during the September quarter. However, growth in local currency deposits continued to exceed that of foreign currency deposits.

Chart 2

Commerical Banks' Deposits
Quarterly Growth Rates



During the first quarter of 2003, M2* declined by $6 306.7 million or 3.8 per cent. This outturn compared to an increase of 1.1 per cent in the corresponding quarter of 2002. The reduction largely reflected declines in local currency deposits and currency in circulation as foreign currency deposits increased by 12.2 per cent. The decline in local currency deposits was a manifestation of a waning of investor confidence in the Jamaica Dollar and higher rates of return offered on alternate domestic assets. Reductions in the NFA of the BOJ and other items (net) were the main sources of the decline in M2* during the March quarter. However, the impact from these sources was partially offset by an increase in banking system credit and a reduction in BOJ's open market operations.

Growth in money supply M2* during the June quarter continued to reflect a strong preference for foreign currency deposits, as investors sought to preserve the value of their financial assets, motivated by an accelerated depreciation in the value of the Jamaica Dollar during the quarter. Money supply M2* increased by 5.1 per cent in the review quarter, a faster rate than the 1.9 per cent recorded in the corresponding quarter of 2002. The growth in June 2003 quarter largely reflected an increase of 11.3 per cent in foreign currency deposits as local currency deposits increased by 3.1 per cent. An expansion in banking system credit and a reduction in open market operations facilitated much of the growth in M2* for the period.

Money supply M2* increased by $6 009.5 million or 3.6 per cent during the September quarter, notably slower than the $10 059.4 million or 6.7 per cent growth that obtained during the corresponding period of 2002. The slower growth observed in the review quarter, was largely reflected in increases of 5.7 per cent and 3.1 per cent in local currency deposits and foreign currency deposits, respectively. The slow down in foreign currency deposits reflected a movement out of time deposits into domestic securities that offered higher rates of return and would have been motivated by a restoration of confidence in the Jamaican economy.

There was the usual seasonal increase in money supply during the December quarter of 2003 with M2* increasing by 6.2 per cent relative to growth of 2.8 per cent during the corresponding period of the previous year. The increase was primarily reflected in M1*, which expanded by 12.7 per cent in the December 2003 quarter associated with the seasonally high demand for currency in December. In nominal terms currency grew by 22.4 per cent during the December 2003 quarter, which implies growth of 17.6 per cent in real terms. During the corresponding quarter of 2002, currency grew by 10.3 per cent in real terms.

With respect to the currency composition of money supply, the outturn in M2* for the quarter reflected expansions of 3.7 per cent and 2.9 per cent in local currency deposits and foreign currency deposits, respectively. This outturn was consistent with improved confidence in the Jamaica Dollar in a context of the relative stability that had prevailed in the foreign exchange market since the end of the June 2003 quarter.

Credit expansion of $21 072.3 million and net maturities of $1 730.9 million in BOJ's open market instruments were the major sources of growth in broad money supply during the December 2003 quarter. The notable increase in lending largely reflected the Central Bank's accommodation of Central Government's financing needs during the period. There was a partially offsetting decline of $5 432.2 million in the NFA of the banking system.

Table 4

Money Supply
(Domestic and Foreign Currency)
Quarterly Flows
(J$M)

	Mar 03	Jun 03	Sep 03	Dec 03	2003
			Components of Money Supply		
Money Supply (M2)*	**-6 306.7**	**8 031.5**	**6 009.5**	**10 732.2**	**18 466.5**
Money Supply (M1)*	**-10 695.4**	**5 963.5**	**2 274.2**	**6 225.7**	**3 767.9**
Currency with the public	-3 075.1	1 467.4	149.1	4 237.9	2 779.4
Demand Deposits	-7 620.4	4 496.1	2 125.1	1 987.8	988.6
Quasi Money	**4 388.8**	**2 068.1**	**3 735.3**	**4 506.5**	**14 698.6**
Savings Deposits	6 340.9	1 316.7	3 743.0	3 208.1	14 608.6
Time Deposits	-1 952.1	751.4	-7.8	1 298.4	90.0
			Sources of Money Supply		
Net Foreign Assets	**-6 489.11**	**-11 766.3**	**-2 109.0**	**-5 432.2**	**-25 796.6**
Bank of Jamaica	-13 140.9	-11 887.7	3 259.1	-1 041.3	-22 810.8
Commerical Banks	6 651.8	121.4	-5 368.1	-4 390.9	-2 985.8
Loans and Advances to Private Sector	**3 623.4**	**7 010.1**	**6 129.8**	**6 113.1**	**22 876.3**
Local Currency	1 530.3	4 087.7	3 783.5	5 093.6	14 495.1
Foreign Currency	2 093.0	2 922.5	2 346.2	1 019.5	8 381.2
Net Claims on Public Sector	**10 713.7**	**14 760.9**	**4 556.1**	**14 959.2**	**44 989.8**
Net Claims on FInancial Institutions	**-2 724.0**	**-772.5**	**-362.4**	**-625.1**	**-4 484.1**
BOJ Open Market Operations	**3 777.5**	**9 077.4**	**-6 573.9**	**1 730.9**	**8 011.9**
Other Items (Net	**-15 208.1**	**-10 278.1**	**4 368.9**	**-6 013.6**	**-27 130.9**
TOTAL	**-6 306.7**	**8 031.5**	**6 009.5**	**10 732.2**	**18 466.5**

Money supply is expected to increase in line with nominal GDP during 2004. It is envisaged that an expansion in banking system credit will be the major source of this increase in money supply. The growth in private sector credit observed over the past three years is expected to continue in 2004, within an environment of increased competition among commercial banks and declining interest rates. However, the rate of expansion in banking system credit to the public sector will be contingent upon the strategy adopted by the Government to meet its financing requirements.

2.3 Commercial Banks

The commercial banking sector exhibited significant growth during 2003. This was characterized by a considerable increase in loans and advances which bolstered the growth in the sector's asset base. Correspondingly, there was a notable expansion and further diversification of the institutions' liability portfolio, reflected by an increase in deposits and the use of securities sold under repurchase agreements as a major source of financing. Concurrently, an improvement in the banks' asset quality was reflected in a notable decline in past due loans. During 2003, the number of commercial banks in operation remained at six with Bank of Nova Scotia (BNS), National Commercial Bank (NCB) and RBTT Jamaica, accounting for 87.4 per cent of total assets as at 31 December 2003.

2.3.1. Assets and Liabilities

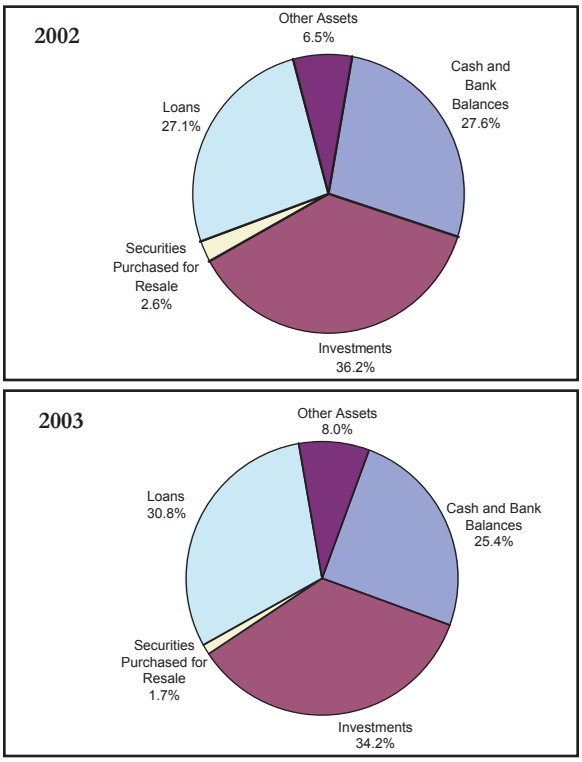
The consolidated balance sheet of the commercial banking sector reflected government's reliance on domestic financing. There was a notable growth in lending to the private sector, consistent with the buoyant performance of the real economy. Beyond this, a shift in the currency composition of deposits reflected developments in the foreign exchange and money markets.

Total assets of the commercial banking sector as at 31 December 2003 grew by 19.7 per cent during 2003, relative to the 10.3 per cent growth in 2002 (see **Table 5**). The expansion in the sector's asset base during 2003 was reflected in notable increases in *Loans* and *Advances, Investments* and *Cash* and Bank balances, which altogether accounted for 87.6 per cent of the total growth during 2003. The expansion in *Loans and Advances* in 2003 continued to reflect the aggressive marketing strategies undertaken by institutions in the sector, although concentrated in the two major commercial banks. This increase was consistent with real sector output during 2003 (see **Production and Prices**).

In spite of the notable expansion in commercial bank loans, the institutions' holdings of *Investments*[3] continued to dominate its asset portfolio, accounting for 34.2 per cent of total assets as at 31 December 2003 (see **Chart 3**). More specifically, investments increased by $12 199.2 million or 13.0 per cent in 2003, in contrast to the $5 523.5 million or 5.6 per cent decline in 2002. The expansion in 2003 largely reflected investments in domestic currency denominated instruments, which grew by $6 386.2 million or 9.0 per cent, compared to the $10 170.9 million reduction in 2002. The outturn for 2003 was mainly due to a $6 199.0 million or 9.3 per cent increase in holdings of Government of Jamaica (GOJ) securities. In addition, there was an increase of $6 229.6 million or 29.4 per cent in holdings of GOJ foreign currency securities, compared to the $4 250.0 million or 25.1 per cent in 2002.

Cash and Bank Balances increased by $7 168.3 million or 10.0 per cent during 2003, relative to the $7 538.0 million or 11.8 per cent growth in 2002. The expansion in 2003 resulted mainly from an increase of $6 990.4 million in placements of foreign currency with overseas banks during the first half of the year. This reflected a change in the banks' liability structure as foreign deposits grew. However, consequent on a tightening of liquidity conditions by the Central Bank during the July to December period, funds held in foreign banks

Chart 3
The Distribution of Commerical Banks' Assets as at 31 December 2002 and 31 December 2003



declined by $3 640.4 million. As a result, growth in placements with overseas banks amounted to $3 350.1 million or 17.6 per cent during 2003, relative to an increase of $3 973.7 million or 26.4 per cent in 2002. The increase in domestic assets reflected increased real sector activities as well as the heightened demand for financing by Central Government during 2003.

The expansion in commercial bank liabilities during 2003 was mainly attributable to increases of $19 795.3 million (or 11.1 per cent) and $16 149.4 million (or 75.1 per cent) in the deposit base and securities sold under repurchase agreements, respectively. A breakdown of total deposits presented in Table 6, shows an expansion in all categories with the exception of Government, which declined by 4.2 per cent. Further, the increase in total deposits largely reflected a $21 695.1 million or 40.1 per cent growth in foreign currency deposits during 2003 (see **Table 5**). Of the expansion in total deposits, private sector deposits grew by 10.8 per cent, somewhat slower than the 13.6 per cent growth observed in 2002.

[3]Investments represents securities (domestic and foreign) held by the commercial banks and exclude securities bought for resale.

Table 5

Commercial Banks
Summary of Assets and Liabilities
(J$M)

	Stock 2003	Flows 2001	Flows 2002	Flows 2003	% 2001	% 2002	% 2003
ASSETS	**309 640.3**	**18 171.4**	**24 078.9**	**50 933.2**	**8.4**	**10.3**	**19.7**
Cash and Bank Balances	78 518.6	10 028.3	7 538.0	7 168.3	18.6	11.8	10.0
Placements with Overseas Banks	*22 354.5*	*2 441.2*	*3 973.7*	*3 350.1*	*19.4*	*26.4*	*17.6*
Investments	105 928.8	331.4	-5 523.5	12 199.2	0.3	-5.6	13.0
-Domestic Currency	77 661.3	-8 065.7	-10 170.9	6 386.2	-9.0	-12.5	9.0
Jamaica Government Securities	72 500.4	57 240.4	-12 039.0	6 199.0	271.3	-15.4	9.3
Other Public Sector	2 351.7	-65 755.9	1 264.6	-176.2	-98.1	100.1	-7.0
Other Local	2 809.2	449.9	603.5	363.4	32.3	32.8	14.9
-Foreign Currency	28 267.5	8 397.1	4 647.4	5 813.0	89.2	26.1	25.9
Securities Purchased for resale	5 163.0	-316.4	-4 401.5	-1 476.9	-2.8	-39.9	-22.2
Loans (Net of provisioning)	95 273.7	9 256.8	25 496.9	25 201.3	26.2	57.2	36.0
Accounts Receivable	6 429.4	-1 959.5	-2 094.8	2 179.3	-23.6	-33.0	51.3
Fixed Assets	7 078.2	38.7	2 075.7	223.6	0.8	43.4	3.3
Other Assets	11 248.5	792.1	988.1	5 438.4	19.7	20.5	93.6
LIABILITIES	**309 640.3**	**18 171.4**	**24 078.9**	**50 933.2**	**8.4**	**10.3**	**19.7**
Deposits	198 774.8	9 251.3	20 061.4	19 795.3	6.2	12.6	11.1
Domestic	122 976.1	4 504.9	10 631.1	-1 899.8	4.1	9.3	-1.5
Foreign	75 798.6	4 746.4	9 430.3	21 695.1	11.9	21.1	40.1
Due to Bank of Jamaica	167.7	-2 960.9	51.8	32.9	-97.3	62.4	24.4
Due to Commercial banks	11 643.4	6 505.9	-42.4	2 322.6	227.7	-0.5	24.9
Due to Specialised Institutions	8 869.2	-522.1	-1 855.4	1 593.7	-5.4	-20.3	21.9
Securities sold under Repurchase Agreements	37 656.1	3 972.8	628.6	16 149.4	23.5	3.0	75.1
Other Liabilities	18 046.1	-759.4	347.5	5 154.9	-5.7	2.8	40.0
Capital Account	34 482.9	2 683.8	4 887.4	5 884.4	12.8	20.6	20.6

Data account for provisioning

Time deposits remained basically flat while savings deposits and demand deposits increased by $14 608.6 million (18.0 per cent) and $988.6 million (3.2 per cent), respectively. Local currency deposits of the private sector grew marginally by $1 049.2 million (or 1.1 per cent), relative to an expansion of $8 284.2 million (9.1 per cent) in 2002.

Private sector foreign currency deposits increased by $10 818.2 million during the first five months of 2003, compared to a $3 787.7 million increase for the same period in 2002. The stronger growth in foreign currency deposits during 2003 was particularly noteworthy in May. With the restoration of confidence and the tight monetary policy environment, there was a slower growth of $3 825.3 million in the June to December period. At end December 2003, the ratio of private sector foreign currency deposits to total deposits in commercial banks was 31.2 per cent, having peaked at 31.9 per cent at end June 2003. The ratio as at 31 December 2003 was relative to the 26.7 per cent observed at end December 2002. It should be noted however that these ratios exclude deposit-like liabilities which are mostly denominated in Jamaican Dollars.

With regard to these commercial bank holdings of securities sold under repurchase agreements, this source of funding increased by $16 149.4 million or 75.1 per cent during 2003, relative to the $628.6 million or 3.0 per cent growth in 2002. The increase during 2003 was concentrated in one commercial bank and was in a context of relatively tight Jamaica Dollar liquidity conditions, which characterized the second half of 2003.

2.3.2. Liquidity

The statutory cash reserve and liquid asset requirements for commercial banks remained at 9.0 per cent and 23.0 per cent, respectively, during 2003. The sector's holdings of liquid assets at end December 2003 stood at 33.2 per cent compared to 37.9 per cent at end December 2002.

Table 6

Commercial Banks Total Deposits (J$M)	Stocks 2003	Flows 2001	Flows 2002	Flows 2003	% 2001	% 2002	% 2003
Deposits	198 999.2	9 160.1	19 562.0	20 825.8	6.1	12.3	11.6
Private Sector	160 347.1	11 902.6	17 343.2	15 687.2	10.3	13.6	10.8
Demand[/1]	32 109.2	6 037.4	4 555.4	988.6	29.4	17.1	3.2
Savings	95 899.2	6 552.0	9 197.3	14 608.6	10.0	12.8	18.0
Time	32 338.8	-686.8	3 590.5	90.0	-2.3	12.5	0.3
Government	18 447.1	-4 307.6	1 577.5	-807.0	-19.6	8.9	-4.2
Other	20 205.1	1 565.1	641.3	5 945.6	13.0	4.7	41.7

[/1] *Deposits adjusted for Net Items in the Process of Collection*

Table 7

Commercial Banks Total Deposits[/1] Private Sector (J$M)	Stocks 2003	Flows 2001	Flows 2002	Flows 2003	% 2001	% 2002	% 2003
Private Sector Deposits	160 347.1	11 902.5	17 343.2	15 687.2	10.3	13.6	10.8
Local Currency	100 008.2	7 511.6	8 290.1	1 043.7	9.0	9.1	1.1
Foreign Currency	60 338.9	4 390.9	9 053.1	14 643.5	13.6	24.7	32.0

[/1] *Deposits adjusted for Net Items in the Process of Collection*

Consequent on this, the banks' excess reserves as at 31 December 2003, totalled $14 500.0 million, reflecting a $5 400.0 million reduction relative to the level at end December 2002 (see **Table 8**). This decline would have contributed to the notable expansion in lending which occurred during 2003.

2.3.3 Interest Rates and Spreads

Following successive declines in the interest rate spread for the last three years (see **Table 9**)[4], the spread increased by 124 basis points to 12.62 percentage points by the end of December 2003. This was consistent with the tightening of monetary policy during 2003. The overall average weighted loan rate increased to 19.32 per cent at end December 2003, relative to the 18.26 per cent observed as at 31 December 2002. However, the overall average weighted rate on domestic currency deposits decreased to 6.70 per cent, relative to the 6.88 per cent as at 31 December 2002. The developments in deposit rates offered by commercial banks during 2003 is explained by the concentration of new deposits in foreign currency savings accounts, rather than reductions in the rates offered on time and savings deposits in total.

[4]The interest rate spread as at 31 December 1999 and as at 31 December 2000 was 14.70 percentage points and 13.20 percentage points, respectively.

2.3.4. Loans and Advances

The stock of loans and advances outstanding to commercial banks stood at $99 150.0 million at 31 December 2003. This reflected an increase of $25 206.7 million (or 34.1 per cent), relative to the $24 908.2 million or 50.8 per cent expansion in 2002 (see **Table 10**). Expressed in real terms, total loans and advances increased by 21.6 per cent during 2003, compared to the 40.8 per cent growth obtained in 2002. The expansion in total loans and advances was concentrated in the two largest commercial banks which accounted for 79.5 per cent of the increase during 2003. In addition, the continued growth in bank lending was accompanied by an improvement in the quality of the banks' loan portfolio, as the ratio of non-performing loans (past due loans three months and over) to total loans outstanding, declined to 3.13 per cent at 31 December 2003, from 3.77 per cent at end December 2002 and 6.08 per cent at

Table 8

Commercial Banks Liquid Assets	2001 Dec	2002 Dec	2003 Mar	2003 Jun	2003 Sep	2003 Dec
Statutory Liquidity (%)						
Cash Reserve Ratio	10.0	9.0	9.0	9.0	9.0	9.0
Liquid Assets Ratio	28.0	23.0	23.0	23.0	23.0	23.0
Average Liquid Assets Holdings (%)	43.1	37.9	33.7	32.9	32.2	33.2
Excess Reserves (J$B)	22.5	19.9	13.5	11.1	16.1	14.5

Table 9

Interest Rates in the Domestic Market	2001 Dec	2002 Dec	2003 Mar	2003 Jun	2003 Sep	2003 Dec
COMMERCIAL BANKS	**11.91**	**11.38**	**10.40**	**12.41**	**13.07**	**12.62**
INTEREST RATE SPREAD	**19.50**	**18.26**	**17.23**	**19.23**	**19.87**	**19.32**
OVERALL AVERAGE WEIGHTED LOAN RATE	**7.59**	**6.88**	**6.83**	**6.82**	**6.80**	**6.70**
OVERALL AVERAGE WEIGHTED DEPOSIT RATE	**3.36**	**3.45**	**3.57**	**3.49**	**3.51**	**3.52**
Demand	6.99	6.38	6.42	6.41	6.31	6.33
Savings	10.13	8.92	8.87	8.98	9.02	8.68
Time						
Certificates of Deposit	11.98	9.98	9.95	9.95	10.06	10.06
1-month	12.22	10.77	10.50	10.53	10.64	10.85
3-month	12.04	10.08	10.76	10.76	10.86	10.65
12-month						
FOREIGN CURRENCY AVERAGE	**3.66**	**3.31**	**3.32**	**3.40**	**3.35**	**3.31**
WEIGHTED DEPOSIT RATE	**2.53**	**2.93**	**2.92**	**3.11**	**3.15**	**3.05**
Demand	3.12	2.40	2.54	2.45	2.29	2.28
Savings	5.45	5.28	5.29	5.34	5.52	5.45
Time						
6-MONTH TREASURY BILL RATE	**17.03**	**17.01**	**33.47**	**28.46**	**23.42**	**22.50**
BOJ 180-DAY REPURCHASE AGREEMENT RATE	**15.00**	**13.45**	**33.15**	**26.50**	**23.50**	**21.00**

end December 2001. This improvement continued to be sustained by the two commercial banks which influenced the positive outturn in the ratio at end December 2003. The ratio compares favourably with the international benchmark of 10.0 per cent.

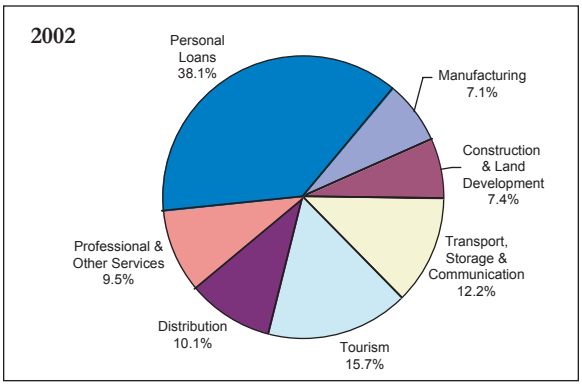
Loans and advances extended by commercial banks to the public sector grew by $4 450.3 million (or 17.7 per cent) during 2003, significantly less than the $12 484.9 million increase in 2002. An increase in loans and advances to the private sector of $22 484.0 million or 46.1 per cent, accounted for 89.2 per cent of the total expansion in credit and facilitated growth in the real sector during 2003. The expansion in private sector loans and advances was relative to a $10 442.8 million or 27.3 per cent increase during 2002, which represented 41.9 per cent of the total increase in loans during that year.

The growth in the commercial banks' loan portfolio during 2003 reflected notable increases by all categories of borrowers with the exception of *Electricity, Agriculture & Fishing, Entertainment and Overseas Residents* (see **Table 10**). In particular, *Personal Loans, Tourism, Transport Storage & Communication* and *Distribution* continued to

dominate the share of loans, accounting for 76.7 per cent of the total stock of private sector loans and advances outstanding as at 31 December 2003. This compared to the 69.9 per cent at 31 December 2002 (see **Chart 4**). *Personal Loans* recorded the strongest growth and was reflective of the aggressive marketing strategies undertaken by the institutions during 2003. The increase in loans to the Tourism sector was mainly to finance refurbishing activities in several hotels islandwide and was funded in part through resources from the Development Bank of Jamaica. The majority of the loans extended to the *Transport Storage & Communication* sector went to the communications industry and reflected increased investments in the provision of mobile telephone services. Growth in loans to the Distribution sector was consistent with the expansion in agricultural output and merchandise imports throughout 2003.

The foreign currency component of loans and advances increased by US$132.8 million (or 27.5 per cent) to total US$616.4 million at end December 2003. This increase was slightly below the US$144.9 million or 42.8 per cent growth at 31 December 2002. While there was an expansion in

Chart 4
Distribution of Private Sector Loans and Advances



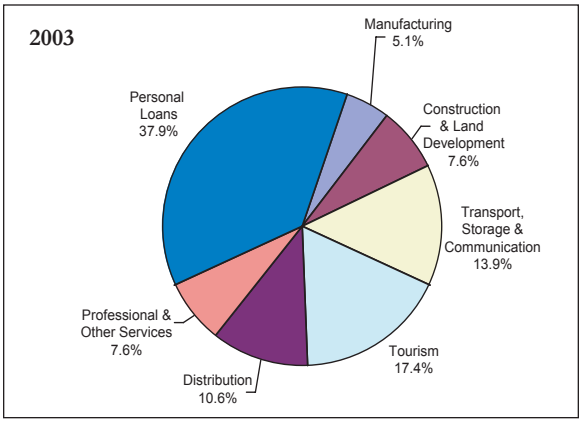


Table 10

Commercial Banks
Total Loans and Advances
(J$M)

	Stocks 2002	Stocks 2003	Flows 2001	Flows 2002	Flows 2003	% 2001	% 2002	% 2003
Public Sector	**23 061.3**	**27 511.6**	**3 879.6**	**12 484.9**	**4 450.3**	**57.9**	**118.0**	**19.3**
Other Financial Instituions	**2 158.7**	**431.0**	**-569.1**	**1 980.5**	**-1 727.6**	**-76.2**	**1 111.4**	**-80.0**
Private Sector	**48 723.4**	**71 207.4**	**5 150.8**	**10 442.8**	**22 484.0**	**15.5**	**27.3**	**46.1**
Agriculture and Fishing	1 737.8	1 421.6	-77.6	258.2	-316.3	-5.0	17.5	-18.2
Mining and Quarrying	102.4	408.4	11.0	4.2	306.0	12.6	4.3	298.8
Manufacturing	3 178.1	3 462.8	72.5	58.9	284.7	2.4	1.9	9.0
Construction & Land Development	3 326.4	5 180.7	313.2	987.0	1 854.3	15.5	42.2	55.7
Transport, Storage & Communication	5 443.1	9 536.9	2 596.1	1 321.3	4 093.8	170.2	32.1	75.2
Tourism	7 041.0	11 908.5	418.6	1 874.7	4 867.6	8.8	36.3	69.1
Distribution	4 512.4	7 250.4	-339.1	1 287.6	2 738.1	-9.5	39.9	60.7
Professional & Other Services	4 236.2	5 182.0	-1 177.3	683.5	945.8	-24.9	19.2	22.3
Personal Loans	17 047.2	25 915.1	2 868.4	3 296.0	8 867.9	26.4	24.0	52.0
Electricity, Gas & Water	1 826.3	785.5	483.0	569.4	-1 040.8	62.4	45.3	-57.0
Entertainment	191.7	103.7	-48.1	102.4	-88.0	-35.0	114.5	-45.9
Overseas Residents	80.7	51.8	30.3	-0.4	-28.9	59.6	-0.5	-35.8
TOTAL	**73 943.3**	**99 150.0**	**8 461.3**	**24 908.2**	**25 206.7**	**20.9**	**50.8**	**34.1**

foreign currency loans to the public sector and private sector, a reduction of US$23.9 in loans to other financial institutions was observed during 2003 (see **Table 11**). Foreign currency loans extended to the public sector by commercial banks grew by US$63.4 million in 2003, accounting for 47.7 per cent of the total increase in that year. This was relative to expansions of US$17.4 million and US$5.1 million for 2002 and 2001, respectively. The majority of loans and advances denominated in United States dollars was extended to the private sector, which accounted for US$93.3 million or 70.2 per cent of the total increase during 2003. This was relative to expansions of US$98.9 million and US$67.8 million in 2002 and 2001, respectively.

Against the background of an expansion in lending which surpassed growth in the sector's deposit base, there was an increase in commercial banks' advances to deposits ratio during 2003, which was a continuation of the trend observed since March 2002 (see **Chart 5**). At 31 December 2003, the advance to deposits ratio was 38.2 percent, increasing from 29.9 per cent at end December 2002. It is envisaged that the ratio will further increase during 2004 in the context of declining interest rates. This augurs well for continued growth and development of the real sector.

Chart 5
Commercial Banks Advance to Deposits Ratio
January 2001 to December 2003

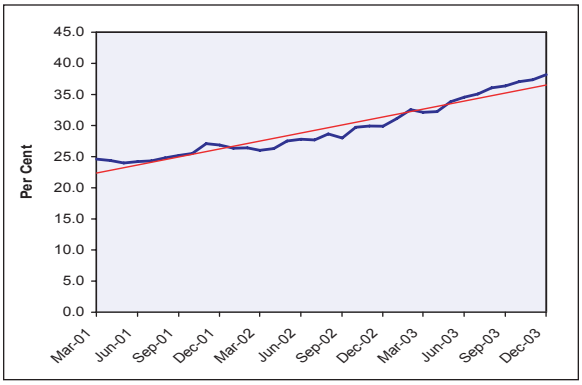


Table 11

Commercial Banks
Foreign Currency Loans and Advances
(US$000)

	Stocks 2002	Stocks 2003	Flows 2001	Flows 2002	Flows 2003	% 2001	% 2002	% 2003
Public Sector	**87 554**	**150 928**	**5 083**	**17 389**	**63 374**	**7.8**	**24.8**	**72.4**
Other Financial Instituions	**28 615**	**4 778**	**-11 741**	**28 556**	**-23 837**	**-99.5**	**48 400.0**	**-83.3**
Private Sector	**367 451**	**460 730**	**67 768**	**98 929**	**93 279**	**33.8**	**36.8**	**25.4**
Agriculture	1 742	1 459	-1 550	-1 993	-283	-29.3	-53.4	-16.2
Mining & Quarrying	72	4 689	-115	-13	4 617	-57.5	-15.3	6412.5
Manufacturing	19 683	18 342	2 058	4 236	-1 341	15.4	27.4	-6.8
Const., & Land Development	40 946	39 992	1 294	35 012	-954	27.9	590.0	-2.3
Transport, Storage & Comm.	92 800	113 248	64 183	20 592	20 448	799.8	28.5	22.0
Electricity, Gas & Water	25 450	10 345	10 616	4 828	-15 105	106.1	23.4	-59.4
Distribution	13 537	19 542	1 095	1 087	6 005	9.6	8.7	44.4
Tourism	125 068	197 327	-329	24 640	72 259	-0.3	24.5	57.8
Entertainment	979	199	-598	815	-780	-78.5	497.0	-79.7
Professional & Other Services	15 047	16 196	-10 847	5 390	1 149	-52.9	55.8	7.6
Personal Loans	32 123	39 391	1 983	4 348	7 268	7.7	15.7	22.6
Loans to Overseas Residents	4	0	-22	-13	-4	-56.4	-76.5	-100.0
TOTAL	**483 620**	**616 436**	**61 110**	**144 874**	**132 816**	**22.0**	**42.8**	**27.5**

2.4. Other Financial Intermediaries

2.4.1. Financial Institutions Act Licensees (FIAs)

During 2003, the process of consolidation among FIAs continued with the merger of two institutions and closure of two licensees. At the end of the year, there were seven entities in operation. Despite the contraction in the number of institutions, there was notable growth in the asset base of the institutions reflected largely in their holdings of securities denominated in local currency. The corresponding expansion in the liabilities of the entities was mainly reflected in securities sold under repurchase agreements. Growth was also observed in the capital base of the sub-sector although the capital paid up & assigned of the seven remaining institutions actually contracted, due to a separation of their managed funds operations from their core business functions in accordance with BOJ requirements. The separation of managed funds from core business functions in 2003 also influenced the size of FIAs' licensees asset portfolios.

The asset base of the sub-sector grew by $16 212.7 million or 58.5 per cent over the twelve-month period ending December 2003. The increase in total assets largely reflected growth of $6 147.5 million, $5 215.8 million and $2 976.9 million in the institutions' holdings of securities purchased under repurchase agreements, foreign assets and Government of Jamaica (GOJ) securities denominated in local currency, respectively. In addition, an expansion of $2 367.5 million in loans and advances also underpinned the growth in the licensees' asset base. The expansion in GOJ securities was significantly higher than the growth of $583.0 million in 2002 and was consistent with the increase in demand for domestic financing by the government.

The expansion in foreign assets mainly reflected investments of $4.9 billion in foreign currency securities, primarily US dollar bonds, relative to $10.5 billion in 2002 and was concentrated in three licensees. The lower level of investment was undertaken in the context of a widening of the interest rate spread in favour of domestic currency instruments, relative to foreign currency securities.

Table 12

Assets and Liabilities of FIA's
2002 and 2003
(J$M)

	December 2003***	Flow 2002	% Change	Flow 2003	% Change
Assets					
Cash and Bank Balances with Commercial Banks****	**98.1**	**117.5**	**43.4**	**-290.1**	**-74.7**
Balances with other Financial Institutions	4.8	-3.1	-41.9	0.5	11.0
Balances with Bank of Jamaica	92.3	-24.5	-5.8	-302.8	-76.6
Foreign Assets	**23 249.1**	**11 322.1**	**168.7**	**5 215.8**	**28.9**
Government Securities	4 480.8	583.0	63.3	2 976.9	197.9
Other Local Investments**	725.3	360.7	113.4	46.4	6.8
Loans and Advances*	5 931.1	537.4	17.8	2 367.5	66.4
Securities purchased under Repurchase Agreements	7 414.6	1 992.6	-45.2	6 147.5	485.2
Other Assets	1 915.5	-2 028.3	-39.3	-1 216.2	-38.8
Total	**43 912.6**	**10 864.9**	**64.5**	**16 212.7**	**58.5**
Deposits^	8 279.0	1 082.0	14.8	-92.7	-1.1
Balances due to Commerical Banks	39.4	32.8	20.5	-153.1	-79.5
Balances Due to Other Financial Institutions	397.1	144.0	44.5	-70.4	-15.1
Foreign Liabilities	**16 395.2**	**8 427.8**	**333.0**	**5 436.3**	**49.6**
Securities sold under Repurchase Agreements	11 706.6	1 335.6	133.0	9 366.7	400.3
Capital & Reserve*	3 384.6	328.6	12.3	393.3	13.1
Other Liabilities	3 710.7	849.7	22.0	-1 007.4	-21.4
Total	**43 912.6**	**10 864.9**	**64.5**	**16 212.7**	**58.5**
Number of Licensees	**7**				

** Refered to as Capital base*
^Includes Foreign Currency Deposits
*** Inclused Provision for Loan Losses*
**** Provisional*
*****Domestic Currency only*

This increase in foreign securities reflects portfolio diversification, given an expansion in foreign currency liabilities.

During 2003, foreign currency liabilities expanded by $5 436.3 million, lower than the growth of $8 427.8 million observed in 2002. The slower growth was due to a contraction in foreign currency borrowings from other financial institutions (OFIs). Simultaneously, there was a $9 366.7 million expansion in securities sold under repurchase agreements as the institutions sought an alternate source of financing, given a contraction in their deposit base. During 2003, total deposits contracted by $92.7 million, relative to growth of $1062.0 million in 2002.

At end December 2003, the FIAs' capital base totalled $3 384.6 million. This represented an expansion of $393.3 million over the capital base at end December 2002. Despite an expansion in the capital base during the review year, capital paid up & assigned of the seven remaining institutions actually contracted, due to a separation of their managed funds operations from their core business functions during 2003 in accordance with BOJ requirements (see Supervision of Deposit-Taking Financial Institutions).

2.4.1.1 Sectoral Distribution of Loans

Loans and advances extended by FIA's increased by $2.4 billion during 2003 with disbursements to the private sector increasing by $1 651.0 million or 66.4 per cent to $5 015.8 million at the end of December 2003. With the exception of three categories namely, *Manufacturing, Construction & Land Development* and *Transport, Storage & Communication*, all other categories recorded an expansion in loans during the review year.

The largest expansion in credit was observed in the categories Professional & Other Services and Mining & Quarrying, which expanded by $1 022.0 million and $712.6 million or 94.4 per cent and 1, 312.3 per cent respectively. During 2002, *Professional & Other Services and Mining & Quarrying* grew by $66.1 million and $30.7 million, respectively. The significant expansion observed in the Professional & Other Services category in 2003 largely resulted from the aggressive marketing strategies undertaken by the licensees. In terms of exposure, the *Professional & Other Services sub-sector* remained the largest category with the stock of loans valued at $2 104.9 million, accounting for 35.5 per cent of total loans. The largest reduction in loans occurred in the

Table 13

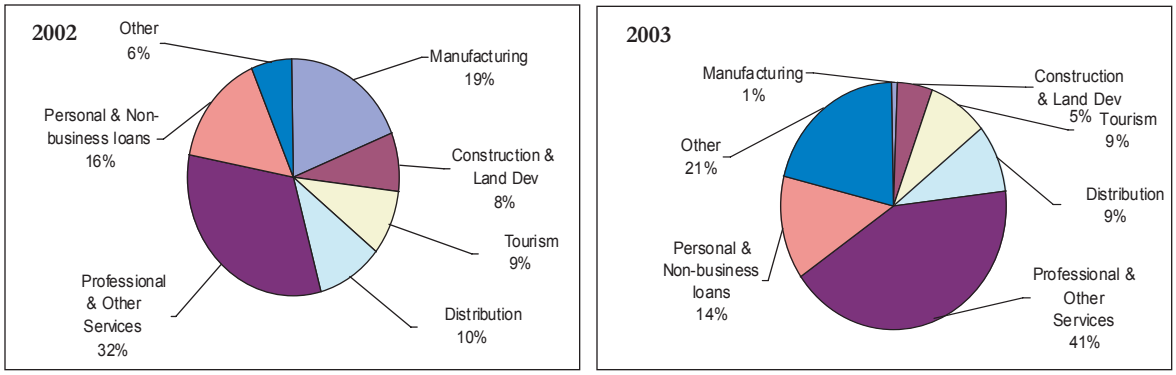
Sectoral Distribution of Loans and Advances of Institutions Licensed under the Financial Institutions Act at December 2002 and 2003 (J$M)

	2002 Stock	Share of Total (%)	2003** Stock	Share of Total (%)	Annual Change in Stock
Public Sector	**167.8**	**4.7**	**914.3**	**15.4**	**746.5**
Financial Institutions	**30.9**	**0.9**	**1.0**	**0.0**	**-29.9**
Private Sector	**3 364.8**	**94.4**	**5 015.8**	**84.6**	**1 651.0**
Agriculture	71.3	2.0	93.9	1.6	22.6
Manufacturing	644.6	18.1	26.9	0.5	-617.7
Construction & Land Development	280.1	7.9	254.7	4.3	-25.4
Mining & Quarrying	54.3	1.5	766.9	24.7	712.6
Transport, Storage & Communication	22.3	0.6	17.2	0.3	-5.1
Tourism	293.1	8.2	434.4	7.3	141.3
Distribution	327.4	9.2	444.6	7.5	117.2
Professional & Other Services	1 082.9	30.4	2 104.9	35.5	1 022.0
Professional Non-Business Loans to Individuals	533.5	15.0	687.0	11.6	153.5
Electricity	37.7	1.1	163.1	2.8	125.4
Entertainment	13.4	0.4	7.8	0.1	-5.6
Overseas Residents	4.2	0.2	14.4	0.2	10.2
Total	**3 563.5**	**100.0**	**5 931.1**	**100.0**	**2 367.6**

**Includes provisions for loan losses*
*** Provisional*

Chart 6

Distribution of Private Sector Loans and Advances



category *Manufacturing*. This reduction largely reflected the repayment of a foreign currency loan by a major client in March 2003. The share of loans with respect to the Tourism sub-sector was 7.3 per cent of total credit, 9.0 percentage points below the share at the end of 2002.

The strengthening of the regulatory and supervisory framework through the separation of managed funds portfolio are all positive signs for future efficiency and transparency of the sub-sector.

2.4.2. Building Societies

At end December 2003, the total assets of the four building societies amounted to $65.7 billion, reflecting growth of 21.4 per cent during the review period. This was significantly higher than the $4.4 billion or 9.1 per cent recorded in 2002. The asset build-up during 2003 was reflected in investments, Government of Jamaica securities and mortgage loans.

Table 14

Assets and Liabilities of the Institutions Licensed under the Building Societies Act at the end of 2003 with annual change during 2003

	STOCK December 2001	STOCK December 2002	STOCK December 2003**	Annual Change 2003
Assets	**537.0**	**334.3**	**1 874.3**	**459.1**
Cash and Bank Balances with Commercial Banks`	0.0	20.5	0.0	-20.5
Balances with other Financial Institutions	757.5	845.0	1 080.9	235.9
Balances with Bank of Jamaica	7 916.3	8 052.4	8 301.4	249.0
Foreign Assets	8 132.1	7 873.7	12 259.9	4 386.2
Government Securities	1 071.4	981.3	13 713.9	12 732.6
Other Local Investments*	17 525.8	20 211.6	24 086.6	3 875.0
Lonas and Advances*	16 433.7	18 999.7	22 950.5	3 950.8
- of which Mortgages	13 333.0	15 428.2	4 392.9	-9 954.4
Other Assets	**49 273.1**	**53 747.0**	**65 709.9**	**11 962.9**
Total				
Liabilities	38 701.0	43 233.6	49 437.3	6 203.7
Savings Fund	0.0	0.0	0.0	0.0
Balances due to Bank of Jamaica	318.6	2.8	80.0	77.2
Balances due to Commerical Banks	1 456.9	1 377.2	0.0	0.0
Balances due to Other Financial Institutions	507.1	545.9	878.3	332.4
Foreign Liabilities	4 877.8	4 855.0	3 899.0	-956.0
Capital & Reserve	4 868.6	5 109.7	11 415.4	6 305.7
Other Liabilities	**49 273.1**	**53 747.0**	**65 709.9**	**11 962.9**
Total				
Indicative ratios (per cent)	21.3	18.7	42.4	
Liquid Assets*** : Total Assets	45.3	46.7	48.7	
Advance Savings Fund	42.5	43.9	46.4	
Mortgage Loan : Savings Fund	27.1	23.3	58.5	
Liquid Assets : Savings Fund	5	4	4	
Number of Licensees	5	4	4	
Number of Licensees qualifying for preferential reserve requirements				

* *Includes Provision for Loan Losses*
` *Domestic currency only*
** *Provisional*
*** *All liquid assets excluding Mortgages*

The primary component of the growth in building societies' liabilities was an expansion in the savings fund of $6 203.7 million or 14.3 per cent, relative to $4 532.6 million or 11.7 per cent in the corresponding period of 2002. This expansion facilitated an increase in mortgage loans during the review period of $4 120.4 million or 21.9 per cent compared to $2 396.4 million or 8.4 per cent in 2002. Also of note were the increases observed in the institutions' holdings of GOJ securities and other local investments of $4 386.2 million and $12 732.6 million, respectively, during the review period ending December 2003.

The expansion in other local investments resulted from capital gains made on their equity portfolios. During 2003, pre tax profits grew by 123.6 per cent relative to 17.8 per cent during 2002. The increase in profitability was the result of one institution's increase in investment income of 71.0 per cent.

The increase in the ratio of liquid assets to savings fund reflects liquid assets increasing faster than savings fund during the year. During 2003, the liquid assets to savings fund ratio significantly increased by 32.8 percentage points in to 56.3 per cent.

There were marginal improvements in the mortgage loans to savings fund and in the advance to savings fund ratios during the review period ending December 2003. The advance to savings fund ratio increased by 2.3 percentage points to 48.7 per cent.

2.4.2.1. New Mortgage Loans

For the review period ending December 2003, 3 121 new mortgage loans were granted by building societies, relative to 2 000 during 2002. The 56.1 per cent growth in mortgage loans was due primarily to an increase in mortgages in the Residential category. New residential mortgages continued to account for the largest proportion of new mortgages loans (96.6 per cent). This increase in new mortgages was in contrast to 2002, when there was a contraction of 491 or 19.9 per cent.

Table 15

Building Societies' New Mortgage Loans 2002 and 2003

	2002	2003	Flow	% Change
Value of New Accounts ($JM)				
Residential	13 462.6	5 890.4	2 427.8	70.1
Commercial	28.2	22.7	-5.5	-19.5
Agricultural & Other	102.4	130.3	27.9	27.2
Totals	**3 593.2**	**6 043.4**	**2 450.2**	**68.2**
Number of New Accounts				
Residential	1 833.0	2 917.0	1 084.0	59.1
Commercial	9.0	20.0	11.0	122.2
Agricultural & Other	158.0	184.0	26.0	16.5
Totals	**2 000.0**	**3 121.0**	**1 121.0**	**56.1**
Overall average weighted mortgage loan rate %	16.6	16.1	-0.5	

There was also a 68.2 per cent increase in the value of new mortgages during 2003, relative to 2002. This increase in the volume and value of new mortgages was consistent with the 0.5 percentage point decline in mortgage rates, during the review period. The average size of mortgages was $1.9 million at end 2003 relative to $1.8 million in 2002.

The operations of building societies remain very competitive with regular promotional features targeting different market segments and attractive interest rates. Different interest rates are offered to various categories of borrowers with the most attractive interest rates being offered to first time homeowners.

2.5 Development Banks

2.5.1. Development Bank of Jamaica

The Development Bank of Jamaica (DBJ) continued to provide medium and long-term financing at concessional interest rates in order to facilitate economic growth and development. Traditionally, loans from the DBJ are channeled through a network of Approved Financial Institutions (AFIs) that includes commercial and merchant banks, people's co-operative (PC) banks and credit unions. The DBJ, in recent years, has also organized financing for several GOJ programmes. During 2003, the institution played a significant role in the financing of Highway 2000, a major GOJ infrastructural project, which resulted in a considerable shift in the structure

of its asset base. At end December, monies on-lent for GOJ infrastructural programmes comprised 42.2 per cent of total assets, while those to AFIs accounted for 31.2 per cent. The DBJ recorded profits of $1.1 billion for the calendar year, which was 21.7 per cent above the performance for 2002.

During 2003, the assets and liabilities of the DBJ increased by 16.5 per cent to $25.4 billion (see **Table 16**). The increase in assets was mainly attributable to a $10.7 billion loan for the Highway 2000 project. In this regard, there was a shift in the concentration of assets from 'Receivables and Prepayments' to 'GOJ Infrastructural Loan Programmes' of which the National Road Operating and Constructing Company, Ltd. (NROCC), accounted for the major share.[5] Consequently, the share of 'Receivables and Prepayments' declined from 56.1 per cent to 21.7 per cent of total assets and amounted to $5.5 billion at end December. The fall-off in this category was mainly attributable to a decline of $7.0 billion in receivables from the Government.

There was net repayment of loans by financial institutions totalling $478.7 million.[6] Of the grouping, 'Loans to Financial Institutions', 'Loans to AFIs' was the only category to display an increase, rising by 7.7 per cent. 'Loans to PC Banks' and 'Other Loans' decreased by 9.2 per cent and 25.2 per cent, respectively.

The expansion in financing for DBJ's operations in 2003 was mainly reflected in the $1.6 billion or 11.0 per cent increase in 'Long-term Liabilities'. The growth in long-term liabilities was largely influenced by 'Other Loans', which increased by 18.9 per cent over 2002. The main source of this change was a loan of $1.1 billion from the National Housing Trust, secured for use in the Government's road rehabilitation programme. Funding from overseas institutions including the Caribbean Development Bank and the World Bank increased by $447.6 million or 11.1 per cent relative to 2002. Net repayments to the Government totalled $243.8 million. Other significant changes to total liabilities included increases in 'Shareholders Equity' and 'Short-term

Table 16

Development Bank of Jamaica
Assets and Liabilities (J$M)

	2002	2003	Change	% Change
Assets				
Cash and Bank Balances	516.6	296.0	-220.6	-42.7
Receivables and Prepayments	12 205.3	5 506.8	-6 698.5	-54.9
Investments	78.9	56.2	-22.7	-28.8
Securities - Resale Agreements	-	127.0	127.0	
Loans to Financial Institutions	8 393.8	7 915.1	-478.7	-5.7
- Loans to People's Co-operative Banks	*860.9*	*781.3*	*-79.6*	*-9.2*
- Loans to AFIs	*4 549.6*	*4 901.7*	*352.1*	*7.7*
- Other Loans	*2 983.3*	*2 232.1*	*-751.2*	*-25.2*
GOJ Infrastructural Loan Programmes	-	10 699.8	10 699.8	-
Fixed Assets	136.7	147.9	11.2	8.2
Other Assets	433.2	616.8	183.6	42.4
Total Assets	**21 764.5**	**25 365.6**	**3 601.1**	**16.5**
LIABILITIES AND SHAREHOLDER'S EQUITY				
Shareholder's Equity	3 803.4	4 884.9	1 081.5	28.4
Current Liabilities	2 112.1	2 313.2	201.1	9.5
Long-term Liabilities	14 432.0	16 017.3	1 585.3	11.0
- From Overseas Institutions	*4 047.8*	*4 495.4*	*447.6*	*11.1*
- From Government of Jamaica	*3 093.4*	*2 849.6*	*-243.8*	*-7.9*
- Other Loans	*7 290.8*	*8 672.3*	*1 381.5*	*18.9*
Short-term Liabilities	1 417.0	2 150.2	733.2	51.7
TOTAL LIABILITIES	**21 764.5**	**25 365.6**	**3 601.1**	**16.5**

[5]NROCC is the company through which funds for the Highway 2000 project are channelled on behalf of the Government.

[6]In 2002 there had been exceptional demand for loans for tourism rehabilitation following the fallout from the events of September 11, 2001.

Liabilities' of $1 081.5 million and $733.2 million, or 28.4 per cent and 51.7 per cent, respectively, during the year. At end 2003, 'Long-term Liabilities' accounted for $16.0 billion (63.1 per cent), 'Shareholder's Equity' $4.9 billion (19.3 per cent) and 'Short-term Liabilities' $2.2 billion (8.5 per cent) of total liabilities.

DBJ loan approvals and disbursements for the calendar year 2003 are presented in **Table 17** and **Table 18**. Loan approvals were concentrated in the manufacturing, agriculture and tourism industries, which together received 80.8 per cent of local currency approvals. Loan disbursements for the year reflected a similar pattern, with services - including tourism - commanding the greatest share. In October 2003, the DBJ, in response to a request from the Ministry of Industry and Tourism, committed to support the implementation of the Tourism Master Plan by advancing $250 million to a specially dedicated fund. The institution also agreed to manage the fund on behalf of the Ministry.

Loans channeled through the AFIs were priced at a concessional rate of 10 per cent and on-lent to sub-borrowers at a rate of 13 per cent. Loans specially financed through the proceeds raised from Development Bond 2000 and 2002[7] were priced at a lower rate of 6 per cent, for on-lending at 9 per cent.

Table 17

Loan Approvals to AFIs and PC Banks by Sector January - December 2003

Sector	Local Currency J$M	%	Foreign Currency US$M	%
Agriculture	272.9	25.6	-	0.0
Agro-Industry	90.5	8.5	-	0.0
Manufacturing	378.3	35.4	0.80	2.9
Mining & Quarrying	98.0	9.2	-	0.0
Other Services	16.9	1.6	-	0.0
Tourism	211.0	19.8	26.87	97.1
Total	**1 067.7**	**100.0**	**27.67**	**100.0**

[7]The DBJ raised $2.5 billion through the issue of two Development Bonds. The bonds were issued to financial institutions and funded by the liquidity generated from the reduction in their cash reserve requirement.

Table 18

Loan Disbursements to AFIs and PC Banks by Sector January - December 2003

Sector	Local Currency J$M	%	Foreign Currency US$M	%
Agriculture	261.8	22.2	-	0.0
Agro-Industry	49.0	4.2	-	0.0
Manufacturing	343.9	29.2	-	0.0
Mining & Quarrying	116.5	9.9	-	0.0
Other Services	279.2	23.7	-	0.0
Tourism	128.6	10.9	5.01	100.0
Total	**1 178.9**	**100.0**	**5.01**	**100.0**

2.5.2. National Export-Import Bank of Jamaica

2.5.2.1. Introduction

The National Export-Import Bank of Jamaica (Ex-Im Bank) continued to provide financial support to the export sector with particular focus on non-traditional exports. At the beginning of 2003, there was increased utilization of loan programmes and various lines of credit, particularly the Cuban Line of Credit (CLC), as the bank expanded its medium-term loan facilities in response to customer demand. However, the increase in utilization of these loan programmes, coupled with higher than anticipated use of the CLC, necessitated the temporary suspension of medium-term loans to ensure that the bank's ability to adequately fund its short-term lending window was not compromised. Consequently, total loan disbursements for 2003 remained at approximately $2.8 billion, the same level achieved for the previous year. The Ex-Im Bank nevertheless recorded un-audited net profit of $148.3 million for the calendar year, representing an increase of 32.8 per cent over net profit recorded in 2002.

With the increased demand for medium-term loans during 2003, the Ex-Im Bank intensified its efforts at securing additional resources. Accordingly, with the assistance of the Ministry of Finance, the Ex-Im Bank successfully negotiated additional funding of CAD $5.0 million for the CLC from a local private sector source. The funds served to supplement the bank's existing CAD $5.00 million Buyer Credit Line, which facilitates the export of Jamaican manufactured goods to Cuba. Additionally, the bank successfully negotiated J$100.0 million bridge-financing from the local financial market to supplement its short-term local currency lending activities. Both these initiatives allowed the Ex-Im Bank to achieve better cash flow management thereby meeting the financial requirements of its customers on a structured basis.

During the year, the Ex-Im Bank also completed the establishment of a J$80.00 million Loan Fund earmarked for the Information, Communication and Technology (ICT) sector. The programme is aimed at providing financial assistance to young entrepreneurs engaged in start up enterprises, as well as established companies in the ICT business. The fund is scheduled to be launched in the first quarter of 2004. Additionally, the bank remained the only provider of Export Credit Insurance, a vital marketing and financial tool for exporters. In 2003, the portfolio recorded growth of 21.43 per cent.

2.5.2.2. Loan Disbursements

In spite of cash flow constraints and an overall reduction in the country's non-traditional exports, the Ex-Im Bank was able to maintain its disbursement level at $2.8 billion for 2003. This resulted mainly from the temporary suspension of medium term lending activities occasioned by initial cash flow constraints. Increased demand for foreign currency loans compensated for the reduction in local currency disbursements and resulted in the Bank attaining the overall level of utilization achieved in 2002.

2.5.2.3. Local Currency Disbursements

As outlined in **Table 19**, total local currency lending for 2003 was $2.0 billion, representing a decline of 5.8 per cent over the previous year. The decline was observed in most of the facilities and was due largely to reductions in the use of the Bankers' Export Credit, Pre-shipment/CoPack and Small Business facilities. The decline was partially offset by increased usage of the Export Credit Facility.

Table 19

Loan Currency Disbursements (J$M)

Facilities	2002	2003	Change	% Change
Bankers Export Credit Facility	806.1	714.4	-91.7	-11.4
Export Credit Facility	619.7	758.2	138.5	22.3
Insurance Policy Discounting Facility	72.9	58.1	-14.8	-20.3
Pre-Shipment/CoPack Facilities	259.1	193.8	-65.3	-25.2
Apparel Sector Financing	21.2	21.0	-0.2	-0.9
Modernization Fund for Exporters	148.2	135.5	-12.7	-8.6
Small Business Facility	133.1	79.1	-54.0	-40.6
Ornamental Fish	10.1	3.4	-6.7	-66.3
Export Growth and Incentive Fund	-	3.5	3.5	-
JMA/ExBed	-	2.0	2.0	-
JEA/ExBed	72.0	49.1	-22.9	-31.8
Total	**2 142.4**	**2 018.1**	**-124.3**	**-5.8**

2.5.2.4. Approved Local Currency Loans by Industry

The food and beverage sector remained the primary beneficiary of the Ex-Im Bank's funding in 2003, accessing J$1.3 billion or 63.0 per cent of approved loans, see **Table 20**. However, while the sector continued to dominate the share of funding, the absolute amounts over the past two years have declined by J$21.5 million in 2002, and a further J$22.9 million in 2003. The decline in this sector for 2003, was attributable to challenges faced on both the local and export markets. The agro-processing industry, which is one of the growth areas targetted by the Ex-Im Bank, utilized an additional $151.0 million. The services industry also accessed additional funding in response to the bank's efforts to assist linkage and import substitution industries.

Table 20

Approved Loans by Industry	2002		2003	
Industries	**J$M**	**Share (%)**	**J$M**	**Share (%)**
Agro-processing	268.5	12.5	419.8	20.8
Food & Beverage	1494.1	69.7	1271.2	63.0
Textile & Apparel	25.3	1.2	25.0	1.2
Other manufacturing	196.3	9.2	135.6	6.7
Mining	10.0	0.5	4.8	0.2
Distribution/Services	148.1	6.9	161.6	8.0
Total	**2 142.3**	**100.0**	**2 018.0**	**100.0**

2.5.2.5. Foreign currency disbursements

In 2003 foreign currency loan disbursements increased by US$0.8 million or 6.5 per cent, due mainly to increased demand for line of credit financing. During the year, the private sector recorded high usage in comparison to 2002 when utilization was almost equally distributed between the public and private sectors.

Table 21

Foreign Currency Disbursements	2002 US$M	2003 US$M	Change	% Change
Facilities				
Lines of Credit	11.9	12.5	0.6	5.0
Bankers Export Credit Facility	0.3	0.5	0.2	66.7
Total	**12.2**	**13.0**	**0.8**	**6.6**

Table 22

Utilization of Foreign Currency	2002		2003	
Sectors	**US$M**	**%**	**US$M**	**%**
Private	5.8	47.2	8.8	67.7
Public	6.5	52.8	4.2	32.3
Total	**12.3**	**100.0**	**13.0**	**100.0**

3. FINANCIAL MARKET OPERATIONS

3.1. Money Market Operations

3.1.1. Bank of Jamaica Operations

During the first half of 2003, the Bank encountered significant monetary policy challenges in the context of high demand for financing by GOJ and unstable conditions in the foreign exchange market. In order to foster stability in the foreign exchange and money markets, the Bank implemented a number of policy initiatives (see **Base Money**).

The Bank primarily depended on its open market operations in managing liquidity in the financial system during the year. Primary Dealers (PDs) and commercial banks remained the main institutions through which open market operations were conducted, with PDs accounting for approximately 75.0 per cent of the new agreements. The number of primary dealers remained unchanged at 14 during 2003.

For 2003, there was a net injection of $18 292.7 million, emanating from the BOJ's open market window (**see Table 23**). The most significant injection occurred during the first half of the year in a context where Banks and FIAs needed to finance the special deposit requirement. In addition, Primary Dealers were forced to unwind portfolios of OMO instruments in light of the overwhelming demand for the GOJ Investment Debenture issued in April at 36.25 per cent. In this regard, by end June, there was a decline of $12 854.9 million in the stock of OMOs relative to December 2002.

In the September quarter, the Government continued to rely on the domestic market for financing. However, the liquidity available in the market was insufficient to fund the Government's needs, and the Bank accommodated the Central Government by increasing its holdings of GOJ securities. With this un-programmed monetary injection, the Central Bank was required to re-absorb liquidity through OMO instruments.

The Bank's acquisition of Central Government securities continued in the December quarter. The liquidity injection was partially offset by payments to BOJ by financial institutions to satisfy the seasonal demand for currency in December. For the quarter, the BOJ net injected $3 121.3 million.

3.1.2. Government Activities 2003

During the review year, a total of forty (40) GOJ bonds were issued to the domestic market through the Bank of Jamaica. These issues consisted of seven (7) US Dollar Indexed Bonds, sixteen (16) Treasury Bills, three (3) Variable Rate Investment Bonds, one (1) US Dollar denominated bond, seven (7) Local Registered Stock issues and six (6) fixed rate Investment Debentures (**see Table 24**). The domestic debt stock increased by $66 727.5 million to $417 834.2 million.

Table 23

Bank of Jamaica Open Market Operations 2003 (JSM)

	Q1	Q2	Q3	Q4	Total
A. Net Outright Sales (+)/ Purchases (-)	-	(1,261.91)	1,511.78	153.64	403.51
B. Net Reverse Repurchase	(7,889.24)	(12,262.16)	4,730.10	(3,274.95)	(18,696.24)
C. Net Absorption (+)/Injection (-)	(7,889.24)	(13,524.07	6,241.88	(3,121.31)	(18,292.73)

** The data include principal and interest payments*

Table 24

Comparative Profile of GOJ Public Offers - 2002/2003

		No. of Offers 2003		No. of Offers 2002
March	Investment Debenture	1	Investment Debenture	1
			Local Registered Stock	5
	US$ Indexed Bond	3	US$ Indexed Bond	1
	Treasury Bills	2	Treasury Bills	5
June	Investment Debenture	2	Eurobond (US$)	1
	Local Registered Stock	3	Local Registered Stock	10
	US$ Indexed Bond	2		
	Treasury Bills	3	Treasury Bills	5
September	VR Investment Bond	2	Investment Debenture	1
	FR US$Bond	1	Local Registered Stock	13
	Investment Debenture	1	US$ Indexed Bond	2
	Local Registered Stock	2	Treasury Bills	5
	US$ Indexed Bond	1		
	Treasury Bills	4		
December	VR Investment Bond	1	Investtment Debenture	1
	Investment Debenture	2	Local Registered Stock	5
	Local Registered Stock	2		
	US$ Indexed Bond	1	Treasury Bills	5
	Treasury Bills	7		
Total		**40**	**Total**	**60**

The Government's financing requirements were largely funded from sources in the domestic capital market. Generally, Jamaica Dollar and US dollar instruments were of short-term to medium-term tenors, with an average tenor of 28 months. This average tenor excludes two US dollar indexed bonds issued in January, with tenors of 7 and 6 years.

For the first half of the year the Government continued to issue fixed rate instruments. However, in the context of declining interest rates, the Government introduced short to medium term variable rate investment bonds that carried similar features as the variable rate Local Registered Stocks. The first issue of variable rate bonds was on 22 July and was the first public offer of a variable rate instrument since December 1999.

Public issues of GOJ Investment Debentures for the year doubled, relative to 2002, increasing from three to six. This was in a context where investors' preference for short-term instruments remained high throughout the year. Accordingly, the average tenor on these instruments was 26 months. Four debenture offers were timed to replace similar maturing instruments and by the end of the year, the stock of these instruments increased to $80 631.2 million from $41 498.6 million at end-2002.

Similarly, the issue of US Dollar Indexed Bonds increased in 2003, totalling seven (7) offers relative to three (3) in 2002. The attractiveness of these instruments heightened in the context of an unstable foreign exchange market in the first five months of the year when most of the offers occurred. By the end of the year, the stock of US Dollar Indexed Bonds was $51 174.8 million, an increase of $21 600.4 million, relative to the end-2002 stock.

The stock of Treasury Bills outstanding increased marginally to $4.4 billion as at end-2003 from $4.2 billion as at end-2002. Generally, the Treasury Bills issued consisted of 6-month offers at the end of each month to replace maturing instruments. There was, however, one issue each of a 90-day, a 364-day as well as a 58-day cash management bill that were all offered in the December quarter. Additionally, two 270-day Treasury Bills were auctioned during the second half of the year.

Financing was also garnered through the private issues of four US Dollar denominated Bonds that raised US$150.0 million in the domestic market. The tenors of the bonds ranged from two to three

years, while the coupons ranged from 10.875 per cent to 11.875 per cent. Additionally, in early September, there was a public offer of a 3-year fixed rate US dollar bond with a coupon of 11.75 per cent. This offer raised US$176.94 million and replaced a US$99.6 million promissory note that matured on 3 September. Additional US dollar financing was obtained from the only Eurobond issued during the year through RBTT Merchant Bank, Trinidad and Tobago that raised US$50.0 million on 14 October.

3.1.3. Interest Rates

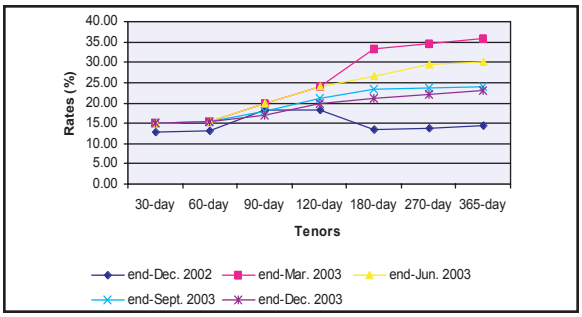
The Bank remained committed to maintaining interest rates at levels that were consistent with a stable macro-economic environment. In the March quarter, the declining trend in interest rates evidenced for most of 2002 was interrupted. In addition to the introduction of a 150-day instrument with a significant premium, interest rates were increased twice in the quarter in response to a protracted period of instability in the foreign exchange market.

A 150-day open market instrument at a rate of 30.00 per cent was issued on 10 February. This resulted in a significant tightening in Jamaica dollar liquidity and generated an appreciation in the exchange rate. The instrument was withdrawn on 14 February. With the reemergence of demand pressures in the foreign exchange market, the Bank responded by increasing rates on the 180-day, 270-day and 365-day tenors on 19 March. Interest rates on these instruments were increased by 6.20, 7.65 and 9.50 percentage points, respectively, to 19.65 per cent, 21.50 per cent and 24.00 per cent. Notwithstanding these adjustments, the rate of depreciation in the exchange rate accelerated and the Bank increased interest rates on 26 March on the entire spectrum of OMO instruments, with the rate on the 365-day instrument peaking at 35.95 per cent (**see Chart 7**).

Following improved conditions in the foreign exchange market, the Bank resumed the series of interest rate reductions. During the June quarter, interest rates were reduced twice to end the

Chart 7

BOJ Reverse Repurchase Rates



quarter with a 365-day rate of 30.00 per cent. Further adjustments in Banks interest rate structure brought rates down to 24.00 per cent and 23.00 per cent at end September and end December, respectively.

Average yields on Treasury Bill auctions increased in the March quarter but subsequently declined for the remaining quarters of the year. The six-month Treasury Bill yield peaked at 33.47 per cent in March, relative to 17.01 per cent at end December 2002. By December 2003, rates had declined to 22.05 per cent (**see Table 25**).

Table 25

Six-Month Treasury Bill Average Yield (%) 2003 (End of Period)			
Jan.	18.45	Jul	26.31
Feb	18.45*	Aug	25.74
Mar	33.47	Sep	23.42
Apr	30.34	Oct	23.07
May	30.34*	Nov	23.46
Jun	28.46	Dec	22.05

**There was no auction during the month, hence the previous month's 180-day rate prevailed*

Medium-term GOJ instruments issued during the year (LRS, Debentures, and Variable Rate Investment Bonds) reflected the variability in market rates. At the onset of the March quarter, a three (3) year fixed rate Debenture was issued, offering a coupon of 18.625 per cent, relative to the coupon of 13.875 per cent on a similar tenor issued during the latter part of 2002. During the June quarter, a 19-month fixed rate Debenture was offered at 36.25 per cent and by the December quarter the coupon declined to 25.00 per cent on a comparable tenor. The average yields on GOJ medium-term instruments declined from a high of 34.21 per cent in the June quarter to end the year at 25.94 per cent.

4. SUPERVISION OF DEPOSIT-TAKING FINANCIAL INSTITUTIONS

4.1. Supervisory Responsibility

The Bank of Jamaica undertakes supervision of deposit-taking financial institutions in Jamaica, as required by Section 34A of the Bank of Jamaica Act. The supervised population comprises:

1. Commercial banks licensed under The Banking Act,
2. Merchant banks licensed under The Financial Institutions Act, and
3. Building societies licensed under The Building Societies Act.

These statutes and related Regulations provide a standardized legal framework for the operations of the licensed deposit-taking intermediaries and the statutory principles on which supervision is conducted. The legal framework is further complemented by guidelines and Standards of Best Practice issued by the Bank to ensure that licensees are not only aware of the risks inherent in banking activities, but that these risks are managed prudently and in accordance with their fiduciary responsibilities to depositors.

Additionally, credit unions operating under the Co-operative Societies Act have been designated as 'specified financial institutions' under the Bank of Jamaica Act by the Minister of Finance, which brings them within the supervisory ambit of the Central Bank and currently allows the Bank to access information on the sector. The comprehensive legal framework to govern supervision of these entities is in process (see **Financial Legislation**).

4.2. Profile of the Supervised Deposit - Taking System

During the year under review, the number of supervised deposit-taking institutions (excluding credit unions) contracted to 17 from 20 as a result of the exit of two merchant banks (hereafter FIA licensees) and one merger involving another two institutions (see **Table 26**).

Table 26

Number of Deposit-Taking Entities

Supervised Entities	1999	2000	2001	2002	2003
Commercial Banks	6	6	6	6	6
FIA Licensees	14	11	11	10	7
Building Societies	5	5	4	4	4
Total	**25**	**22**	**21**	**20**	**17**

The imminent assumption by the BOJ of supervisory responsibility for credit unions, which numbered 52 at year end 2003, will result in significant expansion of the supervised deposit-taking population in the future.

4.3 Changes in Market Profile

The exit of two institutions and the sale of another, were influenced by legislative amendments passed in March 2002, which provided that all investment management operations conducted by deposit taking licensees be transferred to separate legal entities that fall under the regulatory purview of the Financial Services Commission (FSC) (see **Section 4.4.7. below**). The institutions which undertook corporate restructuring during 2003 in the face of the new requirements were:

(i) **International Trust and Merchant Bank**. This institution transferred its securities portfolio to an affiliate, ITMB Finance and Investment Company Limited and

all remaining deposit liabilities to National Commercial Bank Jamaica Limited. Its deposit-taking licence under the Financial Institutions Act was surrendered during January 2003.

(ii) **FirstCaribbean International Trust & Merchant Bank (Jamaica) Limited**. This institution transferred all its deposit liabilities to FirstCaribbean International Bank (Jamaica) Limited during July 2003. The entity was renamed FirstCaribbean International Securities Limited and now operates as a licencee of the Financial Securities Commission. Its licence under the Financial Institutions Act was surrendered.

There was one merger during the year with another two in progress at year end.

(i) **Dehring, Bunting and Golding Limited (DB&G)** acquired **Issa Trust and Merchant Bank** (Issa) and the assets and liabilities were amalgamated with **DB&G Merchant Bank Limited** during August 2003. The merged entity continues to operate under the name of DB&G Merchant Bank Limited.

(ii) **Pan Caribbean Merchant Bank Limited** and **Manufacturers Sigma Merchant Bank Limited** announced their intention to merge operations by March 2004 as part of a wider merger involving their respective parent companies and subsidiaries.

(iii) Grace Kennedy Limited, parent company of **George and Branday Limited** and **First Global Bank**, applied for the necessary approval to consolidate the operations of both licensed deposit-taking subsidiaries by end March 2004 into First Global Bank.

The licensed deposit-taking entities in operation at 31 December 2003 are shown in **Table 27**.

4.4. System Performance Review

4.4.1. Overview

Several factors had an impact on the operations and performance of the licensed deposit taking entities during the year, predominant of which were the implementation of the International Accounting Standards/International Financial Reporting (IAS/IFRS), the separation of off-balance sheet 'funds management' activities and movements in exchange rates and interest rates. The supervised system reflected significant expansion in assets during 2003, which was generated primarily from deposit inflows and borrowings which financed growth in loans, new

Table 27

Supervised Deposit-Taking Entities as at 31 December 2003

Sub-sector	Institution Name	Related Deposit-taking Institution
Commercial Banks	Bank of Nova Scotia Jamaica Limited	Scotia Jamaica Building Society
	Citibank N. A.	Citimerchant Bank Limited
	FirstCaribbean International Bank (Jamaica) Limited	FirstCaribbean International Building Society
	First Global Bank Limited	George & Branday Limited
	National Commercial Bank Jamaica Limited	
	RBTT Jamaica Limited	
FIA Licensees	Capital & Credit Merchant Bank Limited	Citibank N. A.
	Citimerchant Bank Limited	First Global Bank Limited
	DB&G Merchant Bank Limited	
	George & Branday Limited	
	Manufacturers Sigma Merchant Bank Limited	
	MF&G Trust and Finance	
	Pan Caribbean Merchant Bank	
Building Societies	FirstCaribbean International Building Society	FirstCaribbean International Bank (Jamaica) Limited
	Jamaica National Building Society	Bank of Nova Scotia Jamaica Limited
	Scotia Jamaica Building Society	
	Victoria Mutual Building Society	

investments and increased placements with banks, both locally and overseas. With regard to profitability, institutions in general benefitted from the upward movement in interest rates during the year, resulting in higher returns and some capital accretion, which however, did not keep pace with the rate of asset growth. Although prudential capital indicators exhibited decline, these were still above the minimum levels considered to be satisfactory.

4.4.2. Assets

System[7] assets grew by 23.3 per cent (J$79.1 billion) during 2003, to total J$419.3 billion, surpassing growth rates of 13.1 per cent for 2002 and 12.3 per cent for 2001. This growth was influenced by increased foreign currency assets, which totalled US$2.6 billion (J$145.0 billion) at end December 2003, compared to US$2.2 billion at end December 2002, as well as, the impact of revaluations of foreign currency portfolios arising from exchange rate movements. Additionally, in complying with new accounting standards, institutions were obliged to recognize/transfer on balance sheet, certain obligations relating to off-balance commitments, which contributed to the larger asset base reported.

The commercial banking sub-sector continued to dominate the system, accounting for 74 per cent of total assets, down from 76 per cent at the end of 2002. At end December 2003, assets of the sub-sector stood at J$309.6 billion, up from J$258.7 billion the previous year.

During the year, FIA licensees continued the process of separation of 'managed funds' portfolios from their banking portfolios in order to comply with the 2002 legislative amendments regarding non-deposit taking activities. Although, two licencees exited the system, assets for the sub-sector grew by J$16.2 billion to total J$43.9 billion which served to enlarge this group's share of the market to 10 per cent at the end of December 2003 up from 8 per cent at the end of 2002 to 10 per cent at the end December 2003.

The building societies group retained its 16 per cent share of the system with assets growth of J$11.9 billion (22.3 per cent) as against growth of J$4.5 billion during 2002 (see **Table 28**).

The growth in system assets was financed from incremental deposits and borrowings of J$25.9 billion and J$36.8 billion, respectively, and reflected primarily in new lending (J$31.4 billion), investments (J$26.3 billion), and cash and bank placements (J$7.5 billion).

There was further repositioning of asset portfolios with investments being reduced in favour of a growing loan stock. Investments, including assets acquired under repurchase agreements and margin contracts, represented 40.9 per cent of system assets, down from 42.7 and 47.8 per cent as at end 2002 and 2001, respectively. On the other hand, loans portfolio increased to 29.6 per cent, relative to 27.2 per cent and 21.2 per cent as at end 2002 and 2001 respectively. Cash and bank placements (including BOJ Certificates

Table 28

Market Share of Deposit-Taking Financial Sub-sectors (Assets*)

	December 2001		December 2002		December 2003	
	J$B	Per cent	J$B	Per cent	J$B	Per cent
Commercial Banks	234.3	78	258.7	76	309.6	74
Building Societies	49.3	16	53.8	16	65.7	16
FIA Licensees	16.8	6	27.7	8	43.9	10
Total	300.7	100	340.2	100	419.3	100

**Assets net of contingent liabilities and provisions for losses*

[7]Aggregated system balances represented in this section of the report reflects balances in respect of commercial banks, building societies and licensees under the financial institutions Act (FIA).

of Deposit) accounted for 18.9 per cent of total assets (21.1 per cent and 21.6 per cent at year ends 2002 and 2001, respectively).

Deposit liabilities continued to be the predominant source of funding, representing 69.8 percent of total liabilities. This was supplemented by borrowings, including securities sold under repurchase agreements and borrowings under margin contracts, which accounted for 24.9 per cent of total liabilities.

4.4.3. Liquidity

The Cash Reserve and Liquid Assets requirements for the system remained unchanged during the year (see **Table 31**). In general, licensees held declining but satisfactory levels of liquidity, in favour of expanding loan portfolios.

Average domestic currency liquid assets as a percentage of average prescribed liabilities fell to 33.0 per cent in December 2003 from 37.0 per cent in December 2002. All institutions satisfied the statutory requirements for domestic currency requirements during the year but there were a few instances of breach of the foreign currency requirements. At year end, all institutions were however, in compliance with both sets of liquid assets requirements. There were also occasions of infractions of the narrower Cash Reserve ratio, which resulted from untimely adjustments on the part of licensees, to their monthly Cash Reserve balances. Penalty charges pursuant to the relevant legislation were imposed at a rate of 45 per cent per annum on domestic currency shortfalls and 20 per cent per annum on foreign currency shortfalls in both the Cash Reserve and Liquid Assets ratios.

4.4.4. Asset quality

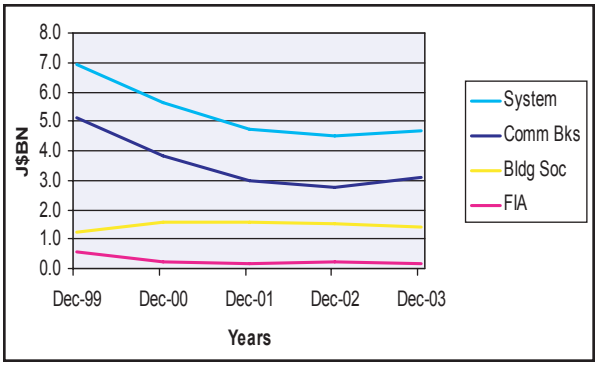
There was further improvement in the relative quality of assets reflected in a reduced ratio of non-performing loans to the total portfolio. As at 31 December 2003, non-performing loans represented 3.6 per cent of total loans down from 4.6 per cent at year end 2002 and 6.8 per cent at year end 2001. This occurred despite an overall increase of $183 million (4.1 per cent) in non-performing loans. This increase was however slower than the 32.2 per cent growth in the system's loan book (see **Table 31**).

While building societies and FIA Licensees were able to reduce their delinquent loan portfolios by 5.7 per cent and 22.7 per cent respectively, non-performing loans for the commercial banks grew by 11.3 per cent (J$0.3 billion) to total J$3.1 billion at the end of 2003. Notwithstanding this increase, all institutions were able to maintain ratio of non-performing loans to total loans well below the prudential benchmark of 10 per cent as compared to end 2002 when three institutions operated above this ceiling.

Total provision for loan losses in the three financial sub-sectors continued to offer coverage for over 100 per cent of the delinquencies being 106.7 per cent at the end of 2003 (114.1 per cent at end 2002).

Chart 8

Trends in Past Due Loans
Growth in Past Due Loans (3 mths & over)
Dec 1999 - Dec 2003



4.4.5. Profitability

The system reported unaudited pre-tax profits of $16.3 billion for 2003, as against $9.8 billion in 2002. This was reflected in an improved pre-tax profit margin and a return on average assets of 25.3 per cent and 4.3 per cent respectively, as compared to results of 21.5 per cent and 3.1 per cent for calendar year 2002.

Gross revenues for the system totalled $64.6 billion, generated mainly from interest income, on investments ($27.0 billion) and loans ($20.7 billion), and to a lesser extent, gains from foreign currency trading and revaluations ($5.3 billion). On the other hand, interest expense (primarily borrowings) accounted for over 50 per cent of the $48.5 billion in total operating expense.

Of the $16.3 billion in profits, the commercial banking group accounted for $12.3 billion or 75.3 per cent, followed by the building societies group with $3.1 billion (19.4 per cent) and FIA licencees with $0.9 billion (5.3 per cent). The FIA sub-grouping was the only one showing reduced profits, influenced by the decline in fee-based business, consequent on the transfer of 'managed fund' portfolios to other financial vehicles.

4.4.6. Capital Adequacy

Increased profitability allowed for some capital accretion and was largely responsible for growth in the statutory capital base of J$4.6 billion or 15.3 per cent during 2003 compared to $2.7 billion or 9.8 per cent, during 2002. Transfers totalling J$2.7 billion were made from internally generated profits to the Statutory Reserve Fund and Retained Earnings Reserve Fund. Capital impairment of J$2.2 billion at the end of December 2002, which was being carried forward by two licensees from the period prior to governmental intervention, was reduced to J$1.2 billion during 2003.

Additionally, new capital came from external sources with First Global Bank receiving an equity injection of J$170 million while Capital and Credit Merchant Bank (CCMB) raised just over $400 million through an initial public offer. CCMB is the only merchant bank currently listed on the Jamaica Stock Exchange.

The rate of incremental capital did not, however, keep pace with growth in asset portfolios, serving to dilute capital support for overall operations. Nevertheless, the ratio of primary capital to total assets ratio of 8.3 per cent at end December 2003 (8.9 per cent at December 2002) continued to be above the prudential benchmark of 6.0 per cent. Additionally, the deposit and borrowings to capital base ratios of 10.1:1 was also well within the statutory upper limits of 25:1 and 20:1 in place for commercial banks and FIA licencees respectively. Although there were individual instances of breach of both statutory and prudential capital adequacy ratios during the year, by year-end all licencees were in compliance with relevant requirements.

4.4.7. Investment Management Activities

The process of separation of investment management activities, consequent on the legislative amendments passed in March 2002, continued during 2003. At 31 December 2003, only one licensee had yet to complete the separation process. Accordingly, at year end 2003, balances related to these activities were reported at $2.2 billion, down from $66.2 billion at end December 2002, and included $0.2 billion in funds under management (representing Trust Assets as allowed under the Central Bank's guidelines) and $2.0 billion of repos for on-trading to clients. These balances are held off-balance sheet and therefore are not included in the system's asset base.

4.5 Credit Unions

4.5.1. Supervisory Framework

The Minister of Finance has designated credit unions as 'specified financial institutions' under Section 2 of the Bank of Jamaica Act, as a preparatory step to bringing them under the Bank of Jamaica's supervisory jurisdiction. The specifics of the credit unions supervisory framework, which are to be contained in the Bank of Jamaica (Credit Unions) Regulations, have been drafted, and have been the subject of extensive dialogue with the industry, prior to being finalized. These Regulations will address licensing and other prudential criteria and establish minimum solvency standards, including licensing, capital adequacy, detail prohibitions on certain areas of business, credit limits, provisioning, submission of prudential returns, financial statements as well as

remedial action that may be taken by the supervisory authority with respect to problem credit unions. During 2003, further amendments were effected to the draft Regulations, to incorporate input provided by the Attorney General's Department and the Office of the Chief Parliamentary Counsel. Amendments to the Cooperative Societies Act were also drafted to ensure that there was no conflict between this Act and the Regulations. It is anticipated that the Regulations, as well as the proposed amendments to the Act, will be passed during 2004, after which the formal licensing process for credit union cooperatives will commence.

4.5.2. Supervisory Developments

In anticipation of the new licensing regime, the Bank commenced on-site examination of credit unions in August 2003. This was subsequent to a meeting hosted by the Minister and the Bank of Jamaica with representatives of the credit union sector during July 2003, at which issues of concerns were discussed and the sector briefed on the imminent examination and licensing process. By the end of the year, 13 of the larger credit unions, representing approximately 65 per cent of the sector's assets, were examined by the Bank of Jamaica.

Additionally, pursuant to powers contained in the Bank of Jamaica Act, the Bank introduced a preliminary prudential reporting regime by credit unions (monthly balance sheet and quarterly income statement) directly to the Central Bank, effective November and December 2003. To facilitate a smooth transition to the new regime, the Bank conducted three workshops over a two-day period, in which representatives of the Jamaica Co-operative Credit Union League (JCCUL) participated, to train credit union staff in the completion and electronic submission of the required returns to the Bank.

4.5.3. Credit Unions' Performance Highlights

The number of credit unions in operation contracted to 52 from 56 as a result of mergers during the year. Notwithstanding the contraction in the number of entities, overall assets increased by $3.8 billion or 19.1per cent to $23.8 billion, compared to the asset base of $20.0 billion recorded at the end of 2002. Growth in the credit union sector was further reflected in an increase in membership to 728,447 from 680,338 during 2003.

As credit unions embarked on a campaign to grow loan portfolios during 2003, total loans increased by $2.2 billion or 19.8 per cent to $13.3 billion. Loans continued to represent the major component of overall assets with its relative share increasing marginally to 55.8 per cent from 55.6 per cent as at end 2002. Growth in loan demand was funded by an augmentation in overall savings by $2.6 billion or 16.4 per cent to $19.0 billion. Loans accounted for 71.0 per cent of total savings compared to 68.0 per cent in 2002. **Table 29** provides select credit union indicators over the past 8 years.

4.6. Legislative Developments

The major pieces of legislation and supporting regulations governing the operations of the licensed deposit-taking institutions are shown in **Table 30**.

Table 29

Selected Credit Union Data
(based on data provided by JCCUL)

EndYear	No. of Credit Unions	Membership	Total Savings($B)	Total Loans($B)	Loans/Savings Ratio	Total Assets ($B)
1996	**77**	502 090	4.7	3.6	75.7	5.8
1997	**73**	514 103	6.2	4.5	72.3	7.6
1998	**57**	532 818	7.9	5.5	70.3	9.4
1999	**65**	572 122	10.0	6.7	66.9	12.2
2000	**60**	597 041	12.0	7.9	65.6	14.6
2001	**58**	637 257	14.2	9.1	64.4	17.3
2002	**56**	680 338	16.4	11.1	68.0	20.0
2003	**52**	728 447	19.0	13.3	69.7	23.8

Table 30

Overview of Legislative Framework	
Name of Legislation	**Statute**
Principal Legislation	The Bank of Jamaica Act The Banking Act The Financial Institutions Act The Building Societies Act The Bank of Jamaica (Building Societies) Regulations
Subsidiary Legislation	The Building Societies (Licences) Regulations The Banking (Establishment of Branches) Regulations The Financial Institutions (Establishment of Branches) Regulations The Banking (Amalgamation and Transfers) Regulations The Financial Institutions (Amalgamation and Transfers) Regulations The Banking (Capital Base) Regulations The Financial Institutions (Capital Base) Regulations The Financial Institutions (Licence Fees) Regulations The Banking (Licence Fees) Regulations

For Amendments **see Section 9**, Financial Legislation.

4.7. Policy Developments

4.7.1 Overview

The focus of supervisory policy initiatives continued to be geared toward achieving full compliance with the Basel Core Principles for effective banking supervision. The policy agenda for 2003 was equally driven by local and international market developments given the global context in which financial markets now operate. The primary areas were: -

1. Consolidated Supervision,
2. Anti-Money Laundering/Anti-Terrorist Financing Regime,
3. The New Capital Accord (Basel II), and
4. International Financial Reporting Standards (IFRS).

4.7.2 Consolidated Supervision

Financial institutions continue to expand their operations through acquisition of shareholdings in other financial entities domiciled within the local jurisdiction, as well as in other regional/overseas territories. This has heightened the need for complementing the supervision of licensed financial entities on a "solo" basis with a consolidated supervisory framework that will ensure that all risks by a banking group are assessed wherever they occur, whether locally or cross-border.

In recognition of this, the Bank of Jamaica pursued certain initiatives to fully and effectively implement consolidated supervision during 2003. Firstly, further advancements were made in the drafting of Standards of Best Practices and Guidelines for Consolidated Supervision, which are slated for issuance to the industry during 2004. These Standards/guidelines seek to, *inter alia*:

(i) Facilitate practical implementation of the legal provisions for consolidated supervision in the relevant statutes which were passed in 2002;
(ii) Implement requirements for the submission of consolidated prudential returns to the Bank of Jamaica;
(iii) Establish prudential benchmarks for banking groups, including minimum consolidated capital requirements, banking group exposures to related companies, as well as commercial and industrial undertakings; and
(iv) Provide guidance to banking groups on the minimum principles that must be followed for effective risk management of conglomerate structures.

Secondly, the issue of consolidated supervision was placed on the agenda of the Caribbean Group of Banking Supervisors (CGBS)[8] at its 2003 Annual Conference. During those deliberations, the Caribbean regulators discussed the supervisory challenges being posed by existing regional conglomerates. It was determined that there was need for the adoption of a harmonized approach to consolidated supervision across the region. In that regard, a Technical Working Group commenced work on examining the issues of concern and developed a strategic plan, outlining the practical approach to be pursued by the region.

[8]The CGBS was formed in 1983 with the specific mandate to coordinate the strengthening and enhancement of bank supervisory practices in CARICOM member jurisdictions, consistent with internationally accepted standards. The membership later expanded to include regional non-CARICOM member countries and now stands at 14 jurisdictions.

In that regard, a Technical Working Group commenced work on examining the issues of concern and developed a strategic plan, outlining the practical approach to be pursued by the region to:

(i) Achieve harmonization of bank holding company legislation across member jurisdictions and in particular grant to regulators the statutory power to bring bank holding companies under a licensing arrangement and allow for some level of impact on their operations where it is seen to influence that of the deposit-taking entity;
(ii) Establish legal and other arrangements to facilitate information sharing between supervisory authorities;
(iii) Effect regional agreements to appoint a lead regulator where relevant;
(iv) Standardise accounting treatment for financial reporting and achieve convergence in prudential benchmarks to allow for meaningful comparisons and the avoidance of regulatory arbitrage.

Thirdly, the Financial Regulatory Council, which was established in 2001, continues to be the forum through which the Bank of Jamaica and the Financial Services Commission share information and determine policies for the effective supervision of financial conglomerates operating within the local jurisdiction (see **Section 4.9**).

4.7.3. Anti-Money Laundering /Combating the Financing of Terrorism (AML/CFT)

During 2003, the Bank continued to be an active participant in the national effort, to comprehensively revise legal and institutional arrangements existing in Jamaica to ensure that the country's AML/CFT framework is in keeping with international obligations under UN Security Council Resolutions and other international standards. The Financial Crimes Legislative Task Force, established by the Hon. Minister of Finance, under the chairmanship of the Deputy Supervisor of Banks, has made several recommendations for legislative enhancements, among other things, and the reform process has been far advanced.

Further to enhance the required anti-money laundering framework for deposit-taking entities, the Bank of Jamaica, during the year drafted comprehensive revisions to its existing Anti-Money Laundering Guidance Notes to include guidelines for detecting and preventing terrorist financing activities. This document incorporates the 'Eight Special Recommendations' on Terrorist Financing, which were issued by the Financial Action Task Force (FATF) during 2003. The enhanced Guidance Notes also take account of the provisions of the revised Forty Recommendations on Money Laundering by the FATF, as well as the Best Practice Standards for Customer Due Diligence Procedures issued by the Basel Committee on Banking Supervision. The draft Notes were issued to the industry for comment during January 2004 and are expected to become operational by end March 2004.

The Bank's examination methodologies are similarly being upgraded to allow for increased scope for the onsite review of the AML/CFT framework existing within the licensed financial institutions.

4.7.4. The New Capital Accord - Basel II

The Basel Committee on Banking Supervision issued its Third Consultative Paper on the New Capital Accord (Basel II) in April 2003. This document prescribes a new capital adequacy standard to be adopted initially by G-10 countries by 2007 and eventually worldwide. It proposes that minimum capital levels be determined based on three pillars of assessment:

(i) Pillar I requires a quantitative assessment of the adequacy of capital, which must be held at levels commensurate with a bank's risk exposures, specifically, credit, market and operational risks.
(ii) Pillar II addresses the supervisory review process, which should ensure that banks maintain capital adequacy ratios above the prudential minimum and that the policies and internal processes in each bank for assessing capital adequacy are effective.

(iii) Pillar III addresses disclosure and transparency issues and is intended to provide banks with a strong incentive to conducting their affairs in a safe, sound and efficient manner.

The Bank of Jamaica assessed the implications for implementation of the proposed New Capital Accord on the domestic banking system and provided detailed comments to the Basel Committee. The Bank (in its role as Secretariat to the CGBS) also coordinated a regional response to the Basel Committee on the proposed New Accord (see **Section 4.10**).

It is also planned to conduct a quantitative impact study during 2004, to more precisely quantify the additional capital requirements that the proposed New Accord will demand of the banking system as a whole.

4.7.5. International Financial Reporting Standards (IFRS)

The adoption of IFRS by the Institute of Chartered Accountants of Jamaica (ICAJ) in July 2002 required additional disclosure of information by licensed financial institutions. The Bank has, however, identified certain issues of conflict between the IFRS and banking laws, regulations and prudential requirements as well as with the Companies Act, and throughout 2003 continued to engage in discussions with the ICAJ with a view to arriving at an acceptable resolution. In this regard, the Bank of Jamaica and the ICAJ have agreed on an approach to address differential requirements relating to loan loss provisioning. In some instances, the new accounting provisions would require lower loan loss provisions than those stipulated under prudential standards issued by the regulatory authorities. It has been agreed that any shortfall in regulatory provisioning should be taken as an appropriation of retained earnings and carried in a non-distributable capital reserve created specifically for this purpose. The Bank has also stipulated that gains/losses on 'available-for-sale' assets be carried in a special revaluation reserve account and not be recognized in the profit and loss account until realised. Amendments to existing prudential returns were introduced shortly after year end to specifically incorporate the reporting of the new reserve accounts. Discussions continue regarding other areas of conflict or concern including the recognition of income on non-performing loans (i.e. loans on which payments of principal and or interest are ninety days or more past the due date).

One area of conflict, which has not yet been resolved, relates to the recognition of income on non-performing loans. Under IAS, interest income on loans that are non-performing for ninety days or more is carried to profits where there exists the possibility of recovery. This is in direct conflict with financial legislation and BOJ's prudential standards, which require licensees to cease accrual of interest on facilities for which payments of principal or interest are in arrears for three months or more. One proposal put forward for BOJ's consideration provides that any income recognized on non-performing facilities would be separately disclosed in the accounts of the licensee and an equivalent appropriation made out of profits to a non-distributable reserve. This proposal is not only in conflict with the legal non-accrual provisions but also with prudent banking practice that require income on non-performing loans to be recognized only on a cash basis. Further, the effect of this proposal would be an inflation of both the balance sheet and income statements with income for which the timing and realisability is known to be uncertain.

Another challenging issue to both the Bank of Jamaica as well as to the industry, relates to the valuation of certain classes of investments for which market valuations are not readily available (i.e. unquoted securities). IAS 39 (Financial Instruments - Recognition and Measurement) requires that instruments held 'as available for sale' (or in the trading book) be 'marked to market'. The absence of an appropriate market valuation mechanism for unquoted equities means that other techniques must be found to re-measure such instruments at fair value for the accounting process. Dialogue with relevant interest groups on this issue continues.

4.8. Developments In Supervisory Management

The Bank continued its efforts to strengthen the supervisory framework and methodologies via the development of Standards of Best Practices for the industry, training of supervisory staff and the enhancement of supervisory methodologies for the conduct of offsite and onsite reviews.

Central to these developments is the revamping of the existing information system solution to replace it with one or more such solutions that would, inter alia:

(i) Allow for faster processing and assessing of information submitted by licensees;
(ii) Incorporate the use of enhanced analytic and forecasting methods to allow for more proactive supervision;
(iii) Facilitate the adoption of enhanced market risk and consolidated supervision;
(iv) Facilitate the adoption of new/emerging supervisory methodologies (e.g. AML/CFT methodologies and Basel's New Capital Accord and AML/CFT methodologies).

Having evaluated several technology solutions from various vendors during 2003, the Bank of Jamaica is expecting to conclude contract negotiations and commence implementation during 2004. The entire project is expected to be completed by end 2005.

4.9. Financial Regulatory Council

The Financial Regulatory Council continues to fulfil its mandate to develop policies and strategies to facilitate greater co-ordination, reduce regulatory arbitrage and increase information sharing among BOJ, FSC and JDIC. The Council, which is chaired by the Supervisor of Banks and Financial Institutions, the Bank's Governor, met on six occasions during 2003 and addressed policy issues especially related to dually licensed institutions operating under statutes administered by the BOJ and the FSC.

4.10. Regional Co-operation

The Bank of Jamaica continues to have active representations on the following regional bodies:

(i) The Caribbean Group of Bank Supervisors - The Bank of Jamaica assumed the chair (Deputy Supervisor of Banks) and Secretariat responsibility of this regional body in January 2003 for an initial two-year term.

The primary areas of focus of the group during the year included an assessment of the Third Consultative Paper on Basel II and the provision of a regional response to the Basel Committee on Banking Supervision. Another significant area was the consideration given to practical implementation of consolidated supervision with regard to regional cross border institutions. A Memorandum of Understanding was drafted to which it is expected that all regional members will eventually be signatories. The Secretariat is also well advanced in the development of an electronic database in the form of an 'extranet' that will serve as a centralized repository of information (e.g. supervisory framework, relevant legislations and standards of member jurisdictions) for CGBS member jurisdictions and offer other critical functionalities such as a discussion forum and a facility for registration in regional supervisory training programmes.

(ii) The Association of Bank Supervisors of the Americas where the Bank of Jamaica is an associate member. The Deputy Supervisor of Banks commenced a two year term as Deputy Chairman of the Association in June 2003.

Additionally, the Bank of Jamaica continues to serve as a principal contact of the Caribbean Financial Action Task Force (CFATF) for Jamaica and maintains interaction with the Basel Committee on Banking Supervision both in its own capacity and that of Chair and Secretariat for the CGBS.

4.11. Outlook

During 2004, issues of particular supervisory focus, some of which are on-going from 2003 will include the following:-

(i) **Consolidated Supervision** - The Bank of Jamaica will be seeking to fully implement statutory provisions for consolidated supervision as well as issue Best Practice Guidelines to the industry on conglomerate risk management;

(ii) **Basel II Quantitative Impact Study (QIS)** - The BOJ plans to conduct a QIS among its supervisees to obtain a refined measure of the likely impact of the implementation of Basel II capital requirements on the operations of licensees. (Similar QIS are to be implemented by CGBS members within their respective jurisdictions.)

(iii) **Market Risk Supervision** - The QIS to be implemented with regard to Basel II will also incorporate calculations for capital charges in respect of market risk. Policy guidelines on market risk are also expected to be introduced to the industry during 2004.

(iv) **Revision of Prudential Returns** - this process, which is ongoing, will continue in 2004, with new returns being introduced to ensure that licensees and financial holding companies submit consolidated returns as well as returns relating to an upgraded capital framework that is consistent with the Basel standards and the Capital Adequacy Regulations, which are expected to become law in 2004;

(v) **Supervision of Credit Unions** - The Bank of Jamaica will be completing the programme of on-site examinations initiated during 2003, and commence the licence review process subject to finalization and passage of the Bank of Jamaica (Credit Unions) Regulations.

(vi) **Standards of Best Practices** - the BOJ is expected to issue finalised Standards of Best Practice on Corporate Governance, Operational Risk Management, Market Risk Management and Conglomerate Risk Management.

(vii) **E-banking Guidelines** - In response to market developments in the area of e-banking, the Bank of Jamaica is drafting detailed Guidelines to promote prudent governance and risk management in this area of activity. Services so far introduced by banks are essentially limited to service facilities such as account enquiries, bill payments etc.

(viii) **Fit and Proper Guidelines** - As a follow-up to its earlier issued "Ladder of Enforcement" which clarified for the industry the triggers for the various supervisory intervention stages and regulatory actions, the Bank of Jamaica proposes to issue to the industry, a policy statement on 'Fit and Proper' criteria. This will clarify the approach of the Central Bank in fulfilling its statutory obligation of assessing the fitness and propriety of principals/connected parties of the supervised deposit-taking entities.

(ix) **Regional Harmonization of the Supervisory Framework** - The Bank of Jamaica intends to maintain its full involvement in the CGBS project which seeks to achieve greater levels of harmonization of the laws and supervisory framework governing the activities of banking entities in the region.

Table 31

Prudential Indicators of Commercial Banks, Licensees under The Financial Institutions Act (FIA) and Building Societies
31 December 2003

	COMMERICAL BANKS			FIA LICENSEES			BUILDING SOCIETIES			SYSTEM TOTAL (CONSOLIDATION OF ALL 3 SECTORS		
	Dec-01	Dec-02	Dec-03	Dec-01	Dec-02	Dec-03[a]	Dec-01	Dec-02	Dec-03	Dec-01	Dec-02	Dec-03
Number of institutions in operation	6	6	6	11	10	7	4	4	4	21	20	17
J$M												
[1] Total Assets (incl. contingent accounts)	239,819	269,021	320,090	18,502	29,634	44,489	49,319	53,797	65,769	307,640	352,452	430,348
[2] Total Assets (excl. contingent accounts)	234,628	258,707	309,640	16,835	27,700	43,913	49,273	53,747	65,710	300,736	340,154	419,263
Total Deposits	158,918	178,979	198,775	7,290	8,372	8,279	38,700	43,233	49,437	04,908	30,584	256,491
Borrowings (incl. repos)	39,546	38,282	59,218	4,703	13,825	29,316	2,162	1,999	2,388	46,411	54,106	90,922
Total Loans (gross)	49,035	73,943	99,150	3,026	3,564	5,931	17,526	20,212	24,087	69,587	97,719	29,168
Total Loans (net of prov.)	44,576	70,072	95,274	2,863	3,413	5,747	16,373	19,093	23,144	63,812	92,578	124,165
Cash & Bank	61,040	67,085	74,923	2,424	3,287	2,995	5,248	6,150	10,539	68,712	76,522	88,457
Investments [incl. Securities Purch.] (net of prov.)	110,295	100,370	111,092	9,490	19,706	33,115	23,989	25,093	27,276	143,774	145,169	71,483
Past Due Loans [PDL] (3 mths & >)	2,982	2,786	3,100	160	198	153	1,590	1,521	1,435	4,732	4,505	4,688
Provision for Loan Losses	4,460	3,871	3,876	164	151	184	1,153	1,119	943	5,777	5,141	5,003
[3] Capital Base	19,945	22,266	26,152	2,663	2,991	3,385	4,808	4,855	5,188	27,416	30,112	34,725
Contingent Accounts [Accept.LC's & Guarantees]	5,191	10,314	10,450	1,667	1,934	576	46	50	59	6,904	12,298	11,085
Funds Under Management	667	1,682	0	35,814	21,825	163	0	0	0	36,481	23,507	163
Repos on behalf of or for on-trading to clients	1,360	1,007	2,003	56,137	41,699	0	0	0	0	57,497	42,706	2,003
%												
[2] Rate of Asset Growth	8.4%	10.3%	19.7%	102.2%	64.5%	58.5%	14.3%	9.1%	22.3%	12.3%	13.1%	23.3%
Rate of Deposit Growth	6.2%	12.6%	11.1%	83.8%	14.8%	-1.1%	10.0%	11.7%	14.4%	8.5%	12.5%	11.2%
Rate of Loans Growth (gross)	20.9%	50.8%	34.1%	14.2%	17.8%	66.4%	12.6%	15.3%	19.2%	18.4%	40.4%	32.2%
Rate of Capital Base Growth	9.7%	11.6%	17.5%	32.2%	12.3%	13.2%	16.2%	1.0%	6.9%	12.7%	9.8%	15.3%
Rate of PDL (3 Mths &>) Growth	-22.5%	-6.6%	11.3%	-19.2%	23.8%	-22.7%	1.1%	-4.3%	-5.7%	-15.8%	-4.8%	4.1%
Investments :Total Assets [2]	47.0%	38.8%	35.9%	56.4%	71.1%	75.4%	48.7%	46.7%	41.5%	47.8%	42.7%	40.9%
Fixed Assets:Total Assets [2]	2.0%	2.6%	2.3%	1.1%	0.7%	0.4%	2.5%	2.6%	2.4%	2.1%	2.5%	2.1%
Loans (net of prov.):Total Assets [2]	19.0%	27.1%	30.8%	17.0%	12.3%	13.1%	33.2%	35.5%	35.2%	21.2%	27.2%	29.6%
Loans (gross) : Deposits	30.9%	41.3%	49.9%	41.5%	42.6%	71.6%	45.3%	46.8%	48.7%	34.0%	42.4%	50.4%
Average Domestic Currency Cash Reserve: Average Prescribed Liabilities [4]	10.0%	9.0%	9.0%	10.0%	9.0%	9.0%	1.0%	1.0%	1.0%	8.1%	7.2%	7.2%
Average Domestic Currency Liquid Assets : Average Prescribed Liabilities [4]	43.7%	37.9%	33.2%	128.1%	89.0%	67.3%	26.3%	30.2%	31.5%	41.7%	37.0%	33.0%
Asset Quality												
Prov. for loan losses:Total Loans (gross)	9.1%	5.2%	3.9%	5.4%	4.2%	3.1%	6.6%	5.5%	3.9%	8.3%	5.3%	3.9%
Prov. For Loan Losses:PDL(3 Mths &>)	149.6%	138.9%	125.0%	102.5%	76.3%	120.3%	72.5%	73.6%	65.7%	122.1%	114.1%	106.7%
PDL (3 Mths &>):Total Loans (gross)	6.1%	3.8%	3.1%	5.3%	5.6%	2.6%	9.1%	7.5%	6.0%	6.8%	4.6%	3.6%
PDL (3 Mths &>): (Total Assets [2] + Provision for loan losses)	1.2%	1.1%	1.0%	0.9%	0.7%	0.4%	3.2%	2.8%	2.2%	1.5%	1.3%	1.1%
Capital Adequacy												
[5] Deposits + Borrowings: Capital (:1)	10.0	9.8	10.0	4.6	7.5	11.4	8.7	9.5	10.2	9.3	9.5	10.1
Capital Base:Total Assets 2	8.5%	8.6%	8.4%	15.8%	10.8%	7.7%	9.8%	9.0%	7.9%	9.1%	8.9%	8.3%
[6] Risk Asset Ratio [RAR] (estimated)	19.7%	15.4%	14.0%	29.8%	15.5%	11.5%	15.6%	14.6%	12.6%	19.6%	15.3%	13.5%
PDL(3 mths &>) :Capital Base+Prov for loan losses	12.2%	10.7%	10.3%	5.7%	6.3%	4.3%	26.7%	25.5%	23.4%	14.3%	12.8%	11.8%
Profitability												
[7]Pre - tax Profit Margin (for the Calendar Year)	14.9%	20.5%	25.2%	38.5%	35.8%	15.5%	16.2%	17.6%	30.6%	16.9%	21.5%	25.3%
Return on Average Assets (for the Calendar Year)	2.1%	2.8%	4.3%	9.7%	7.3%	2.5%	2.6%	2.7%	5.4%	2.6%	3.1%	4.3%
[8] Income Assets/Expense Liabilities (as at 31 Dec.)	100.0%	100.2%	100.4%	117.5%	114.4%	109.2%	106.3%	106.5%	109.4%.	101.9%	102.3%	102.7%

Table 31 cont'd

Prudential Indicators of Commercial Banks, Licensees under The Financial Institutions Act (FIA) and Building Societies
31 December 2003

Notes:
n.a. data not available
n/a not applicable

- Based on unaudited data submitted to BOJ by supervised institutions up to 30 January 2004. Prior years indicators may have minor revisions arising from amendments.

a - During the period December 01 to December 03, four (4) merchant banks surrendered their deposit taking licences thereby reducing the total number of FIA Licensees to seven (7). See details below:
Effective 1 August 03, ISSA Trust & Merchant Bank merged with DB & G Merchant Bank. The merged entity continues to operate under the name of D B & G Merchant Bank Ltd.
Effective 1 July 03, FirstCaribbean International Trust & Merchant Bank Ltd. transferred its assets and liabilities to FirstCaribbean International Bank (Jamaica) Ltd.
Effective 31 January 03, International Trust & Merchant Bank transferred its remaining deposit liabilities to National Commercial Bank Jamaica Ltd.
Effective 1 November 02, Scotia Trust & Merchant Bank transferred its deposit liabilities to Scotia Building Society.

1 Total Assets reflected net of Provision for Losses and include Contingent Accounts (Customer Liabilities for Acceptances, Guarantees and Letters of Credit).
2 Total Assets net of Provision for Losses and Contingent Accounts (Customer Liabilities for Acceptances, Guarantees and Letters of Credit).
3 Capital Base - Banks & FIA Licensees: (Paid - up Capital + Reserve Fund + Retained Earnings Reserve Fund + Share Premium) less impairment by net losses of individual institutions.
- Building Societies: (Permanent Capital Fund + Deferred Shares + Capital Shares + Reserve Fund + Retained Earnings Reserved Fund) less impairment by net losses of individual societies.
4 Prescribed Liabilities include:
(i) deposit liabilities, (ii) reservable borrowings and interest accrued and payable on (i) & (ii).
5 Data includes interest accrued and payable on deposits and borrowings.
6 Risk based capital ratio: Qualifying Capital in relation to risk weighted assets.
Capital Base used in the estimated Risk Asset Ratio (RAR) computation excludes investments in subsidiaries.
7 Data includes extraordinary income/expenditure and adjustments for prior period.
8 Income Assets comprise FC Cash Reserves, Placements, Investments, Repo Assets and Loans less Past Due Loans (3 months & over).
Expense Liabilities comprise Deposits and Borrowings including Repo Liabilities (from BOJ, Banks, OFI etc).

	COMMERCIAL BANKS			FIA LICENSEES			BUILDING SOCIETIES**		
	Dec-01	Dec-02	Dec-03	Dec-01	Dec-02	Dec-03	Dec-01	Dec-02	Dec-03
Required Special Deposit Ratio*	n/a	n/a	5.0%	n/a	n/a	5.0%	n/a	n/a	n/a
Required Cash Reserve ratio	11.0%	9.0%	9.0%	11.0%	9.0%	9.0%	1% / 11.0%	1% / 9%	1% / 9%
Required Liquid Assets ratio (incl Cash Reserve)	28.0%	23.0%	23.0%	28.0%	23.0%	23.0%	5% / 28.0%	5% / 23%	5% / 23%

* 5% Special Deposit requirement imposed on Commercial Banks and FIA Licensees Jan 2003 in accordance with Section 28 A (1) of the Bank of Jamaica Act.
** The requirements are differentially applied to societies not meeting the prescribed threshold of residential mortgage lending in relation to savings funds.
Societies that meet the prescribed 'qualifying assets' threshold attract the lower reserve requirements indicated above. Societies which do not, are requested to meet the requirements which apply to banks and FIA licensees.

Financial Institutions Supervisory Division
Bank of Jamaica

5. THE STOCK MARKET

The stock market expanded significantly during 2003. This expansion was driven by strong individual share price performances and an accommodative macroeconomic environment in the second half of the year. The growth in the market was reflected in the 48.9 per cent increase in the main Jamaica Stock Exchange (JSE) Index, which closed the year at 67 586.72 points[9]. The positive stock market performance was also reflected in increases of 20.6 per cent and 17.1 per cent in the All Jamaican Composite and the Jamaica Select indices, respectively. Concurrently, there was a 75.5 per cent growth in market capitalization over the year to $512.9 billion at end 2003.

The robust growth in the indices and gains in market capitalization over the period was reflective of buoyant market activity. During 2003, 2.8 billion units were traded at a value of $14.3 billion, relative to 1.4 billion units traded at a value of $6.9 billion during 2002 (see **Charts 9 and 10**)[10]. The increased trading during 2003 reflected a continuation of the positive developments within the JSE that have resulted in improvements in stock market liquidity and efficiency in recent years[11].

The significant year-over-year growth in the stock market occurred within a context of contrasting results for the first six months and the last six months of 2003. Approximately 11.0 percentage points of the annual per cent gain in the main JSE Index was recorded in the first half of the year (see **Chart 11**). During this period, efforts by the BOJ to curb foreign exchange market instability resulted in interest rate increases. The prevailing conditions provided investors with average monthly returns of approximately 2.2 per cent from fixed income investments and 2.5 per cent from the foreign exchange market, relative to 1.8 per cent from the stock market (see **Chart 12**)[12].

Chart 9

Total volume traded 1999 - 2003

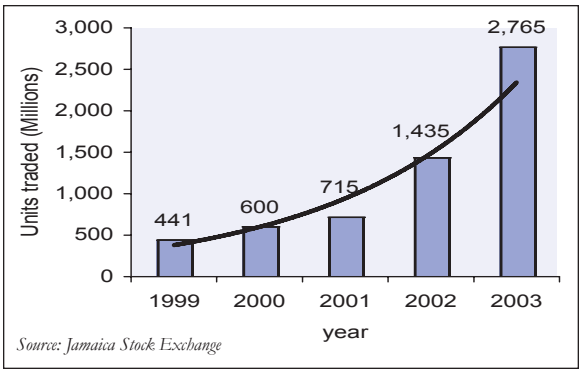
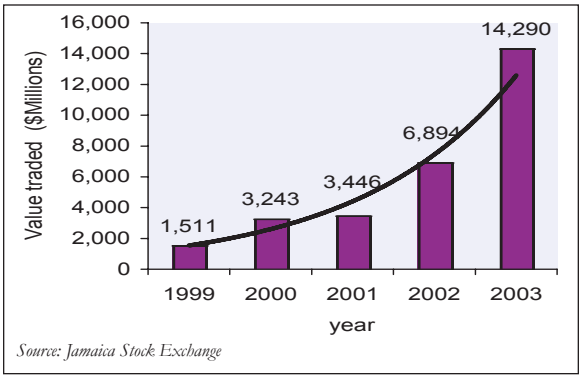


Chart 10

Total value traded 1999 - 2003



[9]The main stock market indices of the Barbados Stock Exchange and the Trinidad & Tobago Stock Exchange grew by 29.0 per cent and 27.2 per cent, respectively.

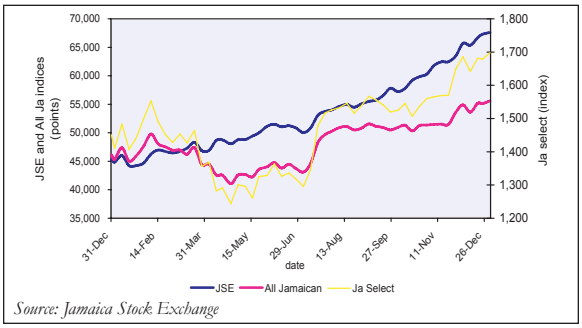
[10]The listing of Jamaica Money Market Brokers and Capital and Credit Merchant Bank contributed to the increased trading activity for the year. Island Life Insurance Company Limited was de-listed during the year, following the merger with Life of Jamaica Company Limited.

[11]In recent years there has been an increase in the number of brokers and improvements in trading efficiency on the Exchange.

[12]In this case the fixed income return is represented by the return on the six-month GOJ Treasury bills. During this period, comparative monthly returns on equities in Trinidad & Tobago and Barbados averaged 0.5 per cent and -0.9 per cent, respectively.

Chart 11

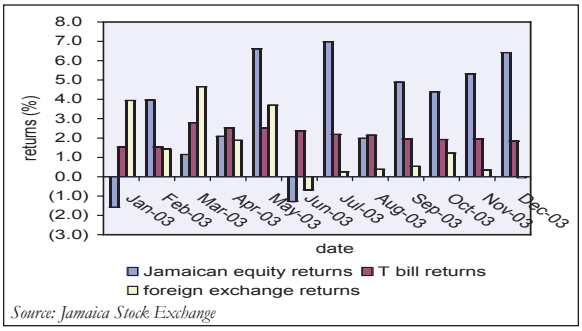
Stock market indices
December 2002 to December 2003



Source: Jamaica Stock Exchange

Chart 12

Monthly return on Jamaican equity, T-bill and foreign exchange - 2003



Source: Jamaica Stock Exchange

The relatively small gain in the main JSE Index, in the first half of the year, was mostly attributable to the existence of arbitrage opportunities that enhanced the attractiveness of cross-listed stocks. The rapid rate of depreciation of the Jamaica Dollar vis-à-vis the US dollar during the period provided an opportunity for investors to purchase cross-listed stocks on the JSE and then to sell these stocks on other regional exchanges to earn arbitrage profits. These opportunities were concentrated in the stocks of six entities.

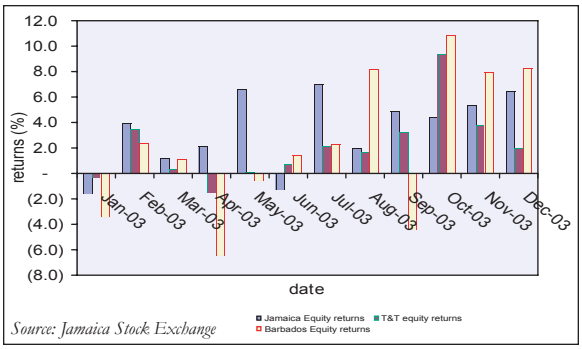
With the restoration of relative stability in the foreign exchange market, arbitrage opportunities were reduced in the second half of the year. The foreign exchange market conditions and the lowering of interest rates in this period facilitated reductions in the average monthly returns of fixed income securities and foreign exchange investments to 2.0 per cent and 0.45 per cent, respectively (see **Chart 11**)[13]. These reductions, as well as indications of relatively high inflation and improved microeconomic fundamentals, facilitated 37.7 percentage points of the annual per cent gain in the main JSE Index. This positive performance of the stock market during the second half of the year signalled an improvement in investor confidence, in the context of reduced uncertainty in key macroeconomic variables.

For the year, stock price gains were reflected in more than 60.0 per cent of the 39 stocks listed on the Exchange. As indicated in **Table 32,** financial sector stocks accounted for half of the top ten share price performers. The significant price increases for stocks in the financial sector, along with an increase in units issued by financial entities, resulted in a 16.2 percentage point growth in the financial sector share of stock market capitalization; this share was 78.4 per cent at end 2003, relative to 62.2 per cent at end 2002 (see **Chart 14**).

During 2003, the stock market provided investors with average monthly returns of 3.4 per cent. This return exceeded the average returns of 2.1 per cent and 1.5 per cent, respectively, from fixed income and foreign exchange investments; and 2.1 per cent and 2.3 per cent, respectively, from equities in Trinidad & Tobago and Barbados (see **Charts 12** and **13**). As shown in **Tables 32** and **33**, attractive earnings per share (eps) and dividends for a number of entities accompanied the positive returns observed in Jamaica's stock market. The anticipated growth in the economy in 2004 is expected to manifest in positive firm performances, and thus

Chart 13

Monthly return on major regional equity markets - 2003

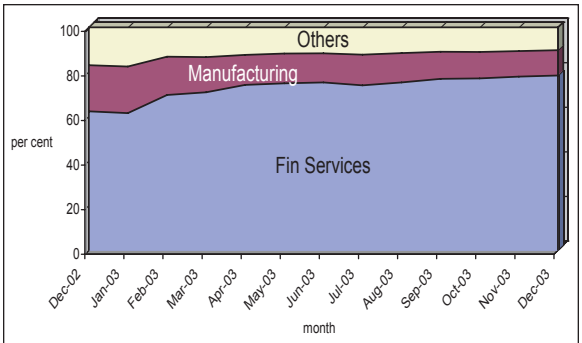


Source: Jamaica Stock Exchange

[13]During the second half of the year, the stock market yielded an average monthly return of 5.0 per cent. This compared to an average return of 3.7 per cent and 5.5 per cent on equities in Trinidad & Tobago and Barbados, respectively.

boost stock prices of a variety of entities. Continued stability in the foreign exchange and money markets, along with other institutional[14] improvements in the JSE, should also add stimulus to the market.

Chart 14
Share of market capitalisation by sector/category December 2002 to December 2003



Source: Jamaica Stock Exchange

Table 32

Top Ten Share Price Performances (December 2002 to December 2003)

Financial Services Sector	Price at end 2003 ($)	Annual Price Change (%)	Annual Movement in EPS
BNS	22.84	44.7	↑
JMMB	8.75	110.8	↑
NCB	14.60	64.2	↑
RBTT	345.00	130.0	↑
Guardian	323.00	90.0	↑
Manufacturing Sector			
CMP	2.99	49.5	↓
Distributive Sector			
Goodyear	6.75	58.8	↑
Hard & Lumber	9.50	54.5	↑
Other services			
Mont Freeport	2.43	273.9	↑
Pegasus Hotel	3.40	79.0	↓

Source: Jamaica Stock Exchange

Table 33

	Average Earning per Share (EPS) by Business Category		Average Dividend Yield by Business Category	
	2002	2003	2002	2003
Conglomerates	4.20	5.77	1.5	2.1
Distributive	0.60	0.89	11.0	5.1
Financial Services	3.20	3.41	1.9	1.7
Manufacturing	1.10	1.11	3.2	3.8
Other services	-0.10	-2.18	1.0	0.4
Telecom	0.30	0.25	5.1	7.1

Source: Jamaica Stock Exchange

[14]The most anticipated institutional adjustment is the announced demutualization of the JSE over the course of the next two years. The Exchange currently operates as a privately owned not-for-profit limited liability company. The adjustment will allow the company to pursue the profit motive and to offer shares to the public. This step will allow the company to generate useful funding and should result in a change in its decision-making structure. These modifications could assist in making the market more dynamically efficient and could enhance public interest.

6. EXTERNAL SECTOR DEVELOPMENTS

6. 1 International Economic Developments

6.1.1 Overview

Global economic activity expanded by 3.9 per cent during 2003, compared with growth of 3.0 per cent in 2002. For the United States of America (USA), Jamaica's main trading partner, economic growth accelerated by 0.9 percentage points to 3.1 per cent in 2003. The main driving force behind this expansion in economic activity in the USA was growth in consumer and investment spending. An improvement was also recorded in the economic performance of the developing countries. This was primarily associated with the acceleration of growth in the USA and Japan, which facilitated an increase in exports and tourism inflows. However, geopolitical tensions, including the war in Iraq, resulted in weakness in demand in both the developed and developing countries during the first half of the year. Stronger growth in world demand was evidenced towards the latter half of 2003.

Commodity prices recorded a significant increase of 13.1 per cent in 2003, after registering a marginal decline of 0.1 per cent in 2002. The most pronounced increases were noted for metals and energy related products, in the context of an increase in demand.

In relation to international trade negotiations, there was a lack of consensus among members of the World Trade Organisation (WTO) and the proposed Free Trade Area of the Americas (FTAA). The major issues of importance for developing countries included agricultural reform and the Singapore issues. For the Caribbean region, progress was made in negotiations toward the establishment of the CARICOM Single Market and Economy (CSME).

6.1.2 Industrial Countries

The major industrialised economies recorded growth in real output of 2.1 per cent in 2003 compared with growth of 1.7 per cent in 2002. The expansion in real output among the industrialised economies was primarily attributed to growth in consumer and investment spending during the year. However, against the background of geopolitical tensions in the Middle East, acceleration in economic activity among these economies was delayed until the second half of 2003. With global demand negatively affected by the war in Iraq, unemployment rates increased, while higher oil prices contributed to a rise in inflation among these economies.

Table 34

Industrial Economies
Real GDP, Consumer Prices and Unemployment Rates and Current Account Balances
(Annual percentage change and per cent of labour force and per cent of GDP)

	GDP		Unemployment Rate		Inflation Rate		Current Account % of GDP	
Country	**2002**	**2003**	**2002**	**2003**	**2002**	**2003**	**2002**	**2003**
USA	2.2	3.1	5.8	6.0	1.6	2.3	-4.6	-4.9
UK	1.7	2.3	5.2	5.0	1.3	1.4	-1.7	-2.4
Euro area	0.9	0.4	8.4	8.8	2.3	2.1	1.2	0.6
Canada	3.3	1.7	7.7	7.6	2.3	2.7	2.0	2.1
Japan	-0.3	2.7	5.4	5.3	-0.9	-0.2	2.8	3.2

Source: The World Economic Outlook, April 2004, Statistics Offices of individual countries

For the USA, growth in economic activity accelerated to 3.1 per cent in 2003, compared with growth of 2.2 per cent in 2002. Real GDP in the USA advanced at a faster rate of 6.2 per cent during the second half of the year, compared with growth of 2.5 per cent during the first half. Much of the growth in economic activity in 2003 was attributed to an expansion of 3.1 per cent in consumer spending, relative to 2002. Consumer spending was supported by the implementation of highly accommodative fiscal and monetary policies during the year, including substantial tax reductions and negative real interest rates. The acceleration in real GDP also reflected a significant expansion in private investment of 4.2 per cent in 2003, compared with a decline of 1.2 per cent in 2002.

With the fiscal deficit in the USA growing to approximately 3.4 per cent of GDP, the current account deficit is estimated to have reached 4.9 per cent of GDP in 2003, compared with 4.6 per cent in 2002. In the context of an expansion in aggregate demand, the average inflation rate for 2003 was 2.3 per cent, compared with 1.6 per cent in 2002. This higher inflation rate reflected significant increases in the cost of medical care, housing and food and beverages.

Real output growth in the Euro area decelerated to 0.4 per cent in 2003, compared with 0.9 per cent in 2002. The expansion in economic activity was partly attributed to increases of 1.0 per cent and 1.9 per cent in consumer and government spending, respectively. However, the deceleration in growth among the economies of the Euro area was partly attributed to continued weakness in investment spending, particularly within the three largest economies of France, Germany and Italy. Exports from the Euro area also remained weak during the year, the result of a 20.6 per cent appreciation in the Euro against the US Dollar, which caused a fall-off in external demand, particularly during the first half of 2003. In this context, the trade surplus of the Euro area deteriorated by 0.6 percentage points, to 0.6 per cent of GDP in 2003, relative to 2002.

Unemployment in the Euro area increased during the year to 8.8 per cent, from 8.4 per cent in 2002. However, inflation, given the appreciation of the Euro, fell to 2.1 per cent from 2.3 per cent the previous year.

For Japan and the United Kingdom (UK), growth in real output accelerated to 2.7 per cent and 2.3 per cent, respectively, compared with a decline of 0.3 per cent and growth of 2.3 per cent in 2002. Much of the recovery in the Japanese economy was due to respective expansions of 10.0 per cent and 9.7 per cent in exports and business investment. For the UK, the modest acceleration in economic activity emanated from growth of 2.9 per cent and 2.6 per cent in consumer and business investment spending, respectively.

Canada recorded a deceleration in economic growth of 1.6 percentage points to 1.7 per cent in 2003, largely attributed to a decline of 2.1 per cent in exports during the year. Exports were adversely affected by the power outage in Ontario in August 2003, large forest fires in British Colombia which led to restrictions on lumber exports to the USA, and the emergence of the Severe Acute Respiratory Syndrome (SARS) epidemic that negatively affected the travel industry. Cattle and beef exports were also affected by the emergence of a disease, Bovine Spongiform Encephalopathy (BSE or "Mad Cow Disease"), during the June 2003 quarter. Overall, exports were negatively affected by the 19.2 per cent appreciation in the Canadian Dollar, against the US Dollar, in 2003.

6.1.3 Developing Economies

Economic activity among the developing countries accelerated significantly by 1.5 percentage points to 6.1 per cent in 2003. Growth in real GDP among the developing economies was partly attributed to an increase in demand from the USA and Japan, which facilitated a significant growth in exports and tourism.

A significant acceleration in growth was evidenced among the developing economies of Latin America and the Caribbean. Real output grew by 1.7 per cent in 2003, which contrasts

favourably with the 0.1 per cent contraction in real GDP registered in 2002.

Within Latin America, Argentina, which was adversely affected by the financial crisis of 2001, recorded a noteworthy increase of 8.7 per cent in real output in 2003. The increase in economic activity in that country represented a partial recovery from the significant decline of 10.9 per cent the previous year. The economy benefited mainly from investments in the construction sector and growth in agricultural exports, due to a 65.0 per cent depreciation in the peso against the US Dollar.

The increase in real output from the Latin American sub-region was moderated by declines in real GDP in Venezuela and the Dominican Republic during the year. In Venezuela, real GDP is estimated to have contracted by 9.2 per cent, relative to a decline of 8.9 per cent the previous year. Much of the decline in real output in Venezuela in 2003 was related to the cessation of oil production and export during the general strike from December 2002 to February 2003[15]. The non-oil producing sectors in Venezuela were also negatively affected by the subsequent implementation of a 10-month currency control system[16] by the government. Political instability in the country also had a negative effect on investor confidence.

Economic activity in the Dominican Republic was adversely affected by a decline in investor confidence due to a financial crisis in the banking sector. With a significant depreciation in the peso during the year, the rate of inflation is estimated to have increased to 27.4 per cent, from 5.2 per cent in 2002.

Changes in economic activity in the Caribbean were mixed during 2003. Trinidad and Tobago recorded the most significant increase in economic activity. Real output for that country grew by an estimated 3.8 per cent in 2003, relative to an increase of 2.7 per cent in 2002. This growth was related primarily to developments in the energy sector, as crude oil production increased by approximately 12.6 per cent during the year. Economic activity in Barbados was positively affected by a moderate pickup in external demand and a consequent recovery in tourism. Guyana, however, registered a decline in real output of 0.2 per cent, compared with an increase of 1.1 per cent in 2002. This decline in real GDP during the year was partly attributed to reductions in business investment and tourism inflows. Several economies in the Caribbean region, experienced relatively low and stable inflation rates during 2003, compared with 2002.

6.1.4 Commodity Markets

The International Monetary Fund's index of primary commodity prices indicated an increase of 13.1 per cent in 2003, after recording a marginal decline of 0.1 per cent in 2002. All the sub-groups within the overall index increased during the year, particularly the metals and energy sub-groups.

Metal prices increased by 11.8 per cent in 2003, compared with a decline of 2.7 per cent in 2002. In particular, aluminium prices increased by 6.1 per cent during the year, relative to a decline of 6.7 per cent the previous year. The recovery in aluminium prices was attributed to increased demand for the commodity by China, as well as a recovery in global industrial activity during the second half of the year.

Crude oil prices increased by 15.8 per cent in 2003, relative to an increase of 2.5 per cent in 2002. However, the price of the commodity exhibited significant volatility during the year. In March 2003, as military action against Iraq became more certain, oil prices (as measured by the West Texas Intermediate), fell from over US$34.00 per barrel to US$25.50 per barrel, within a two week period. War-related disruptions to oil supply were limited

[15]The decline in oil production was partly responsible for upward pressures in oil prices in Jamaica during the year.

[16]The Venezuelan government suspended transactions on the foreign exchange market on 21 January 2003 after the Bolivar lost more than 30.0 per cent of its value during the strike, which began on 2 December 2002. In lifting the suspension two days later, the government imposed an exchange rate system, which fixed the Bolivar's value at 1,596 per US dollar for sales and 1,600 per US dollar for purchases but the government could adjust those rates as it saw fit.

Table 35

Selected Developing Countries
Real GDP and Consumer Prices
(Annual percentage change)

Country	GDP		Inflation Rate	
	2002	2003	2002	2003
Developing Countries	**4.6**	**6.1**	**6.0**	**6.1**
Western Hemisphere	**-0.1**	**1.7**	**8.9**	**10.6**
Latin America				
Argentina	-10.9	8.7	25.9	13.4
Brazil	1.9	-0.2	8.4	14.8
Chile	2.2	2.3	2.5	2.8
Colombia	1.8	3.6	6.3	7.1
Costa Rica	2.9	5.6	9.2	9.4
Dominican Republic	4.7	-1.3	5.2	27.4
Ecuador	3.3	2.6	12.6	7.9
Mexico	0.7	1.3	5.0	4.5
Paraguay	-2.3	2.3	10.5	14.2
Uruguay	-11.0	2.5	14.0	19.4
Venezuela	-8.9	-9.2	22.4	31.1
Caribbean				
Antigua & Barbuda	2.1	2.5	2.2	2.5
Barbados	-1.8	1.6	1.5	1.5
Dominica	-4.7	-1.0	0.1	1.6
Guyana	1.1	-0.2	5.3	5.8
Jamaica	1.1	2.3	7.2	14.1
St. Kitts/Nevis	2.1	2.1	2.1	1.4
St. Lucia	-0.5	2.3	-0.2	1.0
Trinidad & Tobago	2.7	3.8	4.2	3.5
Developing Asia	**6.4**	**7.8**	**2.0**	**2.7**
China	8.0	9.1	-0.8	1.2
Indonesia	3.7	4.1	11.9	6.6
Malaysia	4.1	5.2	1.8	1.1
Philippines	4.4	4.5	3.1	3.1
Thailand	5.4	6.7	0.6	1.8

Source: The World Economic Outlook, April 2004, Statistics Offices of individual countries

to Iraq, with increases in output by other OPEC members broadly offsetting the loss of Iraqi crude oil exports and a temporary loss in Nigerian output due to civil unrest. There was also a surge in demand with the colder than expected winter (2002/03) in North America, which exerted an upward pressure on oil prices. In this context, industry oil inventories fell and remained low for the remainder of the year. An increase in demand by USA and an announcement of a cut in production targets by OPEC in June and November 2003, as well as setbacks in the recovery of Iraq's oil production, resulted in significant increases in oil prices over the latter half of the year.

The prices of non-fuel commodities, in particular food and beverages, also increased during 2003. The food sub-index increased by 5.9 per cent in 2003, relative to an increase of 0.7 per cent in 2002. This was largely the result of higher rice and corn prices during the year, as world demand for the commodities increased, while supplies were negatively affected by unfavourable weather conditions. The beverages sub-index grew by 4.9 per cent during the year, reflecting an increase of 6.2 per cent in the average price of coffee (arabica), relative to the same measure in 2002. The increase in coffee prices reflected adverse weather conditions in Brazil.

6.1.5 Trade Negotiations

During the review year, Jamaica/CARICOM was involved in trade negotiations, which were geared towards the realisation of the WTO's Doha Development Agenda and the establishment of the FTAA and the CSME. The Fifth WTO Ministerial Conference held in Cancún, Mexico from 10 to 14 September 2003 was aimed at

assessing the progress of the negotiations under the Doha Development Agenda and providing negotiators with the necessary guidance to conclude such negotiations by 1 January 2005. The Conference also sought to develop framework agreements for negotiations on agricultural trade, non-agricultural market access, and to decide on the possible launch of negotiations on the 'Singapore issues'[17].

The Ministerial Conference failed to achieve the objectives it had set out, as member states were unable to arrive at a consensus on substantive issues and on the adoption of the draft Ministerial Declaration. Acute differences between the developed and developing countries on the 'Singapore issues' and agriculture were the main reasons behind the failure of the meeting.

Since the 1996 Singapore Ministerial Conference, there has been disagreement between developed and developing countries as to whether negotiations should be launched on the 'Singapore issues'. The European Union, the main advocate for launch of the negotiations, noted that the Doha Ministerial Declaration had called for negotiations to be launched on these issues at the Fifth Ministerial Conference. Developing countries, however, including Jamaica, objected to the launch of negotiations on the 'Singapore issues', noting that further clarification on how negotiations would proceed should be undertaken.

Agriculture also emerged as one of the main areas of contention between developed and developing countries. The discussions and negotiations were focused on developing a framework for the removal of subsidies and tariffs, while addressing the special needs of developing countries. Member states, however, were divided on the modalities in furthering the negotiations.

[17]The Singapore issues first emerged in 1996 at the WTO Ministerial Conference in Singapore. Member states agreed to explore the relationship between trade and investment, trade and competition policy and examine transparency in government procurement and trade facilitation. The broad objectives behind this initiative were to ensure greater access of foreign nationals to investment opportunities in host countries, foster the interplay of market forces through the standardisation of competition rules, allow greater transparency in the channelling of government investments, and ensuring the establishment of institutions that facilitates enhanced free trade.

The negotiations towards the establishment of the FTAA in 2005 also encountered difficulties during the year, due to a lack of consensus among the negotiating parties. On 20 November 2003, thirty-four Western Hemisphere Trade Ministers convened the eighth FTAA Ministerial Meeting in Miami, USA. The aim of the one-day Ministerial summit was the endorsement of a Ministerial Declaration, termed the vision of the FTAA. The vision, which represents a compromise between US and Brazilian objectives, introduced a two-tiered structure into the negotiations. On one level, countries would negotiate a common and balanced set of rights and obligations, which would be applicable to all countries. The second tier of the agreement allowed countries that so choose to agree to additional obligations and benefits, on a 'plurilateral[18] basis'.

At the level of CARICOM, the negotiations for the establishment of the CSME advanced during 2003, with reports of significant progress among the potential member states. The Ninth Special Meeting of the Conference of Heads of Government of the Caribbean Community was held in Castries, St. Lucia, on 13-14 November 2003. The Conference considered matters related to trade agreements, key requirements for the implementation of the CSME, among others.

It was noted that all Member States (with the exception of St. Vincent & the Grenadines), have the necessary arrangements in place to allow CARICOM nationals who are university graduates, media workers, artistes, musicians and sports persons to seek work, or to work without the need for work permits. Member states sought to remove the legal and administrative restrictions on the Right of Establishment, the Provision of Services and the Movement of Capital during the year. Progress was also made towards the realization of hassle-free travel for CARICOM nationals for intra-regional travel.

[18]Plurilateral agreements contrast with multilateral agreements in that plurilateral agreements are signed only by member countries that choose to do so, while all members are party to multilateral agreements.

It was also decided by the Heads of Government that CARICOM would launch negotiations in February 2004 with the European Union (EU), for an Economic Partnership Agreement (EPA). The Dominican Republic will join CARICOM in these negotiations with the EU.

6.1.6 Prospects for 2004

The IMF's World Economic Outlook suggests that world output will accelerate by 0.7 percentage points to 4.6 per cent in 2004. The advanced and developing economies are expected to grow by 3.5 per cent and 6.0 per cent, respectively, during the year. Among the advanced economies, it is anticipated that the USA will continue to lead the growth in real output, with economic activity in that country accelerating by as much as 1.5 percentage points. Growth in the USA is projected to fall within a range of 4.5 per cent and 5.0 per cent in 2004[19]. The expected growth in the USA is underpinned by increases in consumer and investment spending. In addition, continued depreciation of the US Dollar is expected to facilitate further gains in exports during the year. Growth in real GDP in the Euro Area, the UK, Japan and Canada is projected at approximately 2.8 per cent in 2004. Economic activity in these countries will be largely the result of increased demand from the USA, along with continued strengthening in domestic demand.

Real output among the developing economies will be reflective of continued expansion in Asia, particularly in China and India and an increase in demand from the USA. The economies of Latin America and the Caribbean are expected to register a significant growth in real output of 3.9 per cent in 2004. This projection is contingent on continued increases in tourism inflows and commodity prices.

The downside risks to the outlook for the global economy primarily relate to continued security and geopolitical concerns, as well as increases in oil prices. Barring these, it is expected that the acceleration in world output growth in 2004, and an increase in world demand, will engender increases in inflation within a number of economies. In this regard, it is expected that several policymakers will pursue contractionary fiscal and monetary policies during the year. Finally, in the area of international trade negotiations, both developing and developed countries have much to gain from the reduction in trade barriers. A renewed commitment to ensure a successful Doha Round should facilitate success in other trade negotiating fora, such as the FTAA. Although progress to date in the Doha Round has been slower than some countries expected, it is anticipated that the recent steps taken by the European Union and the USA toward agricultural reforms should form the basis for reopening these negotiations.

[19]The projection for growth in real output in the USA was provided by the US Federal Reserve.

6.2 Balance of Payments

Jamaica's balance of payments (BOP) showed signs of a recovery in 2003, following three years of deterioration. Between 1999 and 2002, the external accounts were adversely affected by a fall-out in the local mining sector due to the closure of the Kaiser Gramercy refinery in 1999, the impact of the events of 11 September 2001 on earnings from tourism and lower alumina prices in 2002 due to lower demand. The current account deficit is estimated to have narrowed by an estimated US$114.9 million to US$1003.3 million (12.4 per cent of GDP)[20] in 2003. This improvement was influenced mainly by respective expansions of US$173.7 million and US$48.1 million in the level of net receipts from services and current transfers, which was partly countered by an increase of US$79.0 million in the deficit on the goods account (see **Table 35**). The performance of the current account in 2003 was associated with accelerated growth in the major developed economies (see **International Economic Developments**), which, inter alia, resulted in record levels of visitor arrivals, buoyant private remittance inflows, as well as increased demand for alumina.

[20]This report uses detailed information on merchandise trade for the period January to September 2003. For the period October to December 2003, the value of total imports and exports were provided by the Statistical Institute of Jamaica while the details of merchandise trade were estimated by the Bank of Jamaica.

Table 36

Summary of Balance of Payments (US$M)

	1/ 2001	1/ 2002	2/ 2003	Change
CURRENT ACCOUNT	**-757.2**	**-1 118.2**	**-1 003.3**	**114.9**
A. GOODS BALANCE	**-1 618.1**	**-1 870.3**	**-1 949.3**	**-79.0**
Exports (f.o.b.)	1 454.4	1 309.2	1 356.5	47.4
Imports (f.o.b.)	3 072.5	3 179.5	3 305.9	126.4
B. SERVICES BALANCE	**383.1**	**270.7**	**444.4**	**173.7**
Transportation	-256.2	-245.6	-204.5	41.1
Travel	1 026.2	950.6	1 075.3	124.7
Other Services	-386.9	-434.3	-426.4	7.9
GOODS & SERVICES BALANCE	**-1 235.0**	**-1 599.6**	**-1 505.0**	**94.6**
C. INCOME	**-437.8**	**-605.5**	**-633.3**	**-27.8**
Compensation of Employees	74.6	82.1	75.5	-6.6
Investment Income	-512.4	-687.6	-708.8	-21.2
D. CURRENT TRANSFERS	**915.6**	**1 086.9**	**1 135.0**	**48.1**
General Government	119.7	107.6	84.7	-22.9
Other Sectors	795.9	979.3	1050.3	71.0
CAPITAL & FINANCIAL A/C	**757.3**	**1 118.2**	**1 003.3**	**-114.9**
A. CAPITAL ACCOUNT	**-23.6**	**-16.9**	**-17.1**	**-0.2**
General Government	2.2	0.2	0.1	-0.1
Other Sectors	-25.8	-17.1	-17.2	-0.1
B. FINANCIAL ACCOUNT	**780.9**	**1 135.1**	**1 020.4**	**-114.7**
Other Official Investment	653.4	77.1	-367.8	-444.9
Other Private Investments 3/	998.7	814.3	956.0	141.7
Reserves 4/	-871.2	243.7	432.1	

1/ Revised
2/ Estimates
3/ Includes Errors & Omissions
4/ Minus denotes increase

While there was an improvement on the current account, there was a deterioration of the *capital* and *financial accounts*, which resulted in a contraction of the net international reserves (NIR). This occurred in a context of relatively unfavourable international capital markets following the crisis in Argentina, as well as, concerns about the domestic macro-economy. While a fairly constant *capital account* deficit of US$17.1 million was recorded in 2003, there was a decline of US$114.7 million in the surplus on the *financial account* to US$1 020.4 million. Within the *financial account*, there was net official investment outflow of US$367.8 million. Net private investment inflows, on the other hand, increased by US$141.7 million to US$956.0 million but were insufficient to finance the deficits on the *current* and *capital accounts*, as well as, the deficit on the *official investment* sub-account. As a consequence, the NIR declined by US$432.1 million in 2003.

6.2.1 Merchandise Trade

Exports

Jamaica's earnings from merchandise exports grew in 2003, the first time since 2000. Earnings from goods exports were estimated at US$1 356.5 million (16.8 per cent of GDP) for the review year. *General merchandise exports* continued to account for the largest proportion of total exports and were valued at US$1 184.8 million while, *freezone exports* and *goods procured* in ports by foreign carriers totalled US$141.7 million and US$30.0 million, respectively (see **Table 37**).

Total export earnings in 2003 increased by an estimated US$47.4 million, or 3.6 per cent, over that of 2002, largely reflecting an expansion of US$67.5 million in the value of *general merchandise exports*. Partly offsetting this increase was a fall of US$21.0 million in *freezone exports*. For *general merchandise exports*, respective expansions of US$55.2 million and US$9.8 million in *major*

Table 37

Traditional & Non-Traditional Exports
(US$M)

	1/ 2002	2/ 2003	Change	% Change
GENERAL MERCHANDISE EXPORTS	**1 117.4**	**1 184.8**	**67.5**	**6.0**
TOTAL DOMESTIC EXPORTS	1 097.6	1 156.2	58.6	5.3
Major Traditional Exports	793.9	849.1	55.2	7.0
Bauxite	106.3	86.7	-19.7	-18.5
Alumina	603.8	676.0	72.2	12.0
Sugar	66.2	66.3	0.2	0.2
Bananas	17.6	20.0	2.5	14.1
Other Traditional Exports	74.6	68.3	-6.4	-8.5
Citrus	2.1	3.1	0.9	42.4
Cocoa	2.2	2.9	0.7	30.0
Coffee	32.7	29.4	-3.3	-10.1
Pimento	2.6	2.1	-0.5	-18.7
Rum	34.1	29.9	-4.2	-12.3
Gypsum	0.9	1.0	0.1	6.3
Non Traditional Exports	229.1	238.9	9.8	4.3
RE-EXPORTS	19.8	28.6	8.9	44.8
FREEZONE EXPORTS	162.7	141.7	-21.0	-12.9
GOODS PROC. IN PORTS	29.1	30.0	0.9	3.1
GRAND TOTAL	**1 309.2**	**1 356.5**	**47.4**	**3.6**

1/ Revised
2/ Estimates

traditional and *non-traditional exports* were recorded, the effect of which was partially countered by a decline of US$6.4 million in *other traditional exports*.

The performance of *major traditional exports* largely reflected an expansion of US$72.2 million (12.0 per cent) in alumina receipts, which was partly offset by a fall of US$19.7 million (18.5 per cent) in the value of bauxite exports. Earnings from sugar and banana, the other two major traditional export commodities, went up marginally by US$0.2 million and US$2.5 million, respectively. The growth in the value of alumina exports was due to respective increases of 5.7 per cent and 5.9 per cent in the average price of the product and export volumes. Alumina prices were positively affected by a rise in the demand for aluminium, associated with relatively strong growth in the main industrialised countries and China. Prices were also affected by the resurgence in demand for air travel after the war in Iraq. The growth in export volumes in 2003 reflected increased capacity utilisation.

Earnings from bauxite exports fell to US$86.7 million in 2003 from US$106.3 million in the previous year, largely reflecting a decline of 6.6 per cent in export volumes. Bauxite export volumes amounted to 3.8 million tonnes for the year, 0.3 million tonnes below the level recorded for 2002. The decline in exports reflected the temporary slow down in production at the Kaiser Jamaica Bauxite Company during the first quarter of the year, due to the parent company's (Kaiser Aluminium Chemical Corporation) decision to purchase crude bauxite from the United States government's stockpile during that quarter.

The value of sugar exports in 2003 was estimated at US$66.3 million, approximately the same as the previous year. The average realised price per tonne of sugar increased by 16.7 per cent in 2003, while export volumes contracted by 20.7 per cent to 109.7 thousand tonnes. The increase in the realized price was associated with a 20.6 per cent appreciation in the Euro vis-à-vis the US dollar during 2003, while the decline in volumes reflected a reduction of 21.5 thousand tonnes, or 12.3 per cent, in sugar production. This decline was associated with a reduction in the quantity of sugar cane milled, which was partly due to a lower level of replanting at the start of the crop year. There was also a decline in the quality of cane milled, reflected in an increase in the tonnes cane to tonnes sugar (TC/TS) ratio to 11.6 in 2003 from 11.0 in 2002.

Earnings from banana exports in 2003 amounted to US$20.0 million, which was 14.1 per cent above the earnings in 2002. This growth reflected increases of 13.5 per cent and 0.4 per cent in the average price of the fruit and export volumes, respectively. The increase, in US dollar earnings was also attributable to the appreciation of the Euro vis-à-vis the US dollar over the review period, while export volumes were influenced by improved weather conditions in 2003.

The value of other traditional exports fell by US$6.4 million in 2003 to US$68.3 million, relative to 2002, mainly reflecting contractions in the value of rum and coffee exports (see **Table 37**). Lower earnings from coffee were associated with a 9.3 per cent reduction in export volumes, while earnings from rum reflected contractions in both price and export volumes during the review period.

Non-traditional exports in 2003 amounted to US$238.9 million, representing an increase of US$9.8 million, or 4.3 per cent, relative to the previous year. This performance was largely associated with an expansion in food exports, partially offset by a contraction in the export of mineral fuels. Miscellaneous manufactured goods exports were also lower in the review period, relative to 2002, due primarily to the continued downturn in the garment industry.

Imports

The value of imports in 2003 exceeded that of 2002 by US$109.8 million, or 3.0 per cent, mainly reflecting increased spending on *general merchandise imports*, which expanded by US$107.9 million, or 3.0 percent in 2003 (see **Table 38**). The growth in 2003 was marginally below the 3.5 per cent expansion recorded for the previous year. Total imports (c.i.f.) were estimated at US$3 827.8 million in 2003, of which *general merchandise imports* accounted for US$3 694.1 million, while *freezone imports* and *goods procured* in ports by the domestic carrier were valued at US$94.3 million and US$39.4 million, respectively.

Increased expenditure of US$242.8 million on *raw material imports* accounted for the growth in *general merchandise imports*. This was partly offset by declines of US$42.7 million and US$92.3 million on *consumer goods* and *capital goods imports*, respectively. As a result of these developments, the share of *general merchandise imports* attributable to *raw material imports* increased to 56.0 per cent in 2003 from 50.9 per cent in 2002. The respective shares of *consumer goods* and *capital goods imports*

Table 38

Value of Imports by End-use (C.I.F.)
(US$M)

	1/ 2002	2/ 2003	Change	% Change
GENERAL MERCHANDISE IMPORTS	**3 586.3**	**3 694.1**	**107.9**	**3.0**
Consumer Goods Imports	**1 093.6**	**1 050.9**	**-42.7**	**-3.9**
Food	291.0	296.1	5.1	1.8
Other Non-Durables	304.5	313.3	8.8	2.9
Durables	498.2	441.6	-56.6	-11.4
(of which motor car)	151.1	149.5	-1.6	-1.1
Raw Material Imports	**1 826.3**	**2 069.1**	**242.8**	**13.3**
Fuels	635.7	821.2	185.4	29.2
Other Raw Materials	1 190.6	1 248.0	57.4	4.8
Capital Goods Imports	**666.4**	**574.1**	**-92.3**	**-13.9**
Transport & Equipment	119.9	82.1	-37.8	-31.5
(of which motor car)	3.5	2.4	-1.1	-31.4
Construction Materials	138.0	169.4	31.4	22.8
Other Machinery & Eqp.	398.4	315.7	-82.7	-20.7
Other Capital	10.1	6.9	-3.3	-32.1
FREEZONE	**93.6**	**94.3**	**0.7**	**0.7**
GOODS PROC. IN PORTS	**38.2**	**39.4**	**1.2**	**3.1**
GRAND TOTAL	**3 718.1**	**3 827.8**	**109.8**	**3.0**

1/ Revised
2/ Estimates

declined to 28.4 per cent and 15.5 per cent in 2003, from 30.5 per cent and 18.6 per cent in 2002.

The growth in expenditure on r*aw material imports* in 2003 was influenced by an estimated expansion of US$185.4 million in the value of fuel imports, associated with respective increases of 20.1 per cent and 7.6 per cent in oil prices and the volume of imports (see **International Economic Developments**). The growth in fuel imports was primarily due to higher demand arising from non-bauxite related activities.

Capital goods imports in 2003 continued to be dominated by the other machinery & equipment category. However, there was a decline of US$82.7 million in the value of these imports, due to a reduction in the level of new investment in the telecommunication sector against the background of significant expansions in previous years. The fall in *consumer goods imports* emanated principally from a contraction of US$56.6 million in durable imports, partially offset by expansions in food and other non-durables. The reduced demand for imported consumer goods may have been associated with the 15.9 per cent depreciation in the exchange rate during the review period, the removal of several items from the list of non-taxable commodities and the introduction of the 2.0 per cent cess on import.

CARICOM

Jamaica's merchandise trade with the rest of CARICOM increased in 2003 by US$118.6 million to US$566.0 million (see **Table 39**). The trade deficit with the region increased to US$472.1 million from US$349.9 million in 2002, due to a fall in exports and a rise in imports. Trinidad and Tobago, Barbados and Guyana continued to dominate Jamaica's trade with the region in 2003, accounting for a combined share of 62.0 per cent of total exports, while supplying 94.2 per cent of its imports. While Trinidad & Tobago remained Jamaica's main CARICOM trading partner, Barbados replaced Guyana as Jamaica's second largest regional trading partner in 2003.

6.2.2 Services

Estimated net earnings from *services* amounted to US$444.4 million in 2003, representing an increase of US$173.7 million above the outturn in 2002. This expansion in net inflows largely resulted from an increase of US$124.7 million in net receipts from *travel*, supported by lower deficits on the *transportation* and *other services* sub-accounts.

Transportation

Net payments for *transportation services* were estimated at US$204.5 million in 2003, relative to US$245.6 million in 2002. The lower deficit was largely influenced by higher inflows associated

Table 39

CARICOM Trade by Country (US$M)

	2002 1/			2003 2/		
	Exports	Imports	Trade Balance	Exports	Imports	Trade Balance
Trinidad & Tobago	17.3	330.2	-313.0	18.0	453.9	-435.9
Guyana	2.8	28.1	-25.2	2.9	19.2	-16.2
Barbados	9.5	14.1	-4.6	8.2	15.7	-7.4
Dominica	1.3	9.7	-8.4	1.9	9.6	-7.7
Belize	3.8	5.8	-2.0	3.2	12.8	-9.5
Suriname	0.7	7.9	-7.2	0.8	6.2	-5.4
Antigua	5.2	0.0	5.2	3.2	0.1	3.1
St. Vincent	1.3	1.7	-0.4	1.5	0.9	0.6
St. Lucia	3.6	0.3	3.4	4.0	0.2	3.8
Grenada	1.4	0.7	0.7	1.5	0.6	1.0
St. Kitts	1.5	0.1	1.5	1.6	0.0	1.6
Montserrat	0.1	0.0	0.1	0.1	0.0	0.1
TOTAL	**48.7**	**398.6**	**-349.9**	**46.9**	**519.0**	**-472.1**

1/ Revised
2/ Estimates

with a significant increase in the number of visitors to the country transported by local carriers over the review period. This was, however, partly offset by higher freight charges on imports.

Travel

The *travel* sub-account showed significant improvement in 2003, relative to the previous year. Gross earnings of US$1 327.7 million from visitor expenditure were US$118.7 million higher than the level recorded in 2002. In contrast, gross payments by Jamaicans travelling overseas, including expenditure by seasonal workers abroad (e.g., farm workers) decreased by US$6.0 million to US$252.4 million in 2003.

The estimated expansion in gross earnings from tourism resulted from a 16.4 per cent increase in total visitor arrivals, reflecting expansions of 30.9 per cent and 6.6 per cent in cruise passenger and stopover arrivals, respectively (see **Table 40**). There was also a 2.1 per cent increase in the average daily expenditure of stopover visitors, the effect of which was partly offset by a marginal decline in their average length of stay in 2003. The growth in tourist arrivals occurred within the context of the aggressive marketing efforts by the Jamaica Tourist Board (JTB) in both traditional and non-traditional markets, as well as the redeployment of cruise vessels from the Mediterranean given security concerns in that region and the emergence of SARS in other competing destinations. The industry also benefited from continued improvements of the major docking facilities across the Island since 1999. In addition, accelerated economic growth coupled with improved consumer confidence in the USA had a positive effect on visitor arrivals.

Whereas visitor arrivals from the USA, the Island's main tourist market grew by 5.2 per cent during 2003, there were more significant improvements from Europe and the UK. There was a marked increase of 29.3 per cent in arrivals from Europe in the year, relative to a decline of 0.9 per cent in 2002, facilitated by increased charter flights from that region. The growth in visitor arrivals from Europe was associated with the marketing efforts of the JTB, as well as, the introduction of European hotel franchises in Jamaica since 2001. Arrivals from the UK, Jamaica's second largest tourist market, increased by 18.3 per cent in 2003, relative to 2002, and accounted for 11.3 per cent of total stopovers. Visitor arrivals from Spain, Germany and Italy also experienced significant increases in 2003.

Table 40

Visitor Arrival Statistics

	1/ 2002	2/ 2003	% Change
Total Stop-overs	1 266 972	1 350 284	6.6
Foreign National Stopovers	1 179 083	1 262 108	7.0
Long-stay	1 110 325	1 186 780	6.9
Short-stay	68 758	75 328	9.6
Non-resident Jamaican stopovers	87 889	88 176	0.3
Cruise Passengers & Armed Forces	**865 419**	**1 132 596**	**30.9**
Total Visitors	**2 132 391**	**2 482 880**	**16.4**
Gross Estimated Expenditure (US$M)	**1 209.0**	**1 327.7**	**9.8**

1/ Revised
2/ Estimates

Source: Jamaica Tourist Board

The growth in stopover arrivals to Jamaica lagged slightly behind the performance of the region's tourism in the first half of 2003[21]. For the period January to June 2003, stopover visitor arrivals to Jamaica increased by 7.0 per cent, compared with 7.7 per cent growth for selected Caribbean destinations. The performance of the region was influenced mainly by respective increases of 18.0 per cent, 15.0 per cent and 10.0 per cent in stopover arrivals to the Dominican Republic, Cuba and Barbados.

Other Services

The deficit of US$426.4 million on the *other services* sub-account in 2003 was marginally below the deficit of US$434.3 million in 2002. Total outflows on this sub-account contracted by US$4.9 million to US$770.9 million, the impact of which was complemented by an expansion of US$3.0 million to US$344.5 million in total

[21]Information unavailable for most of the countries beyond June 2003.

inflows. The reduction in outflows was associated with lower financial and communications services charges, the effect of which was partly countered by an expansion in outflows related to other business services. The lower financial service charges were associated with Government's limited external borrowing, while the expansion in other business services was partly as a result of increased payments associated with the growth in the travel sector.

6.2.3 Income

The *income account* recorded a deficit of US$633.3 million in 2003, relative to a deficit of US$605.5 million in the previous year. *Net investment income* outflows grew by US$21.2 million to US$708.8 million, while net inflows for *compensation to employees* fell by US$6.6 million to US$75.5 million. The deterioration in the *investment income* sub-account was largely attributable to a contraction in the interest earnings of the BOJ, which was affected by a significant reduction in the average stock of its gross foreign assets and the continued lowering of international interest rates since 2001 (see **International Economic Developments**). There was also an increase in interest payments on Government's external debt. Inflows representing compensation to Jamaicans for work abroad fell by US$2.1 million to US$108.9 million in 2003, while there was an increase in payments to non-residents for work performed in Jamaica.

6.2.4 Current Transfers

Current transfers continued to grow in 2003, led primarily by increased inflows to the private sector, largely remittances. For the review period, net inflows of *current transfers* amounted to US$1 135.0 million, an increase of US$48.1 million (4.4 per cent), relative to 2002. Net inflows to the private sector grew by US$71.0 million (7.3 per cent), while net inflows to the public sector contracted by US$22.9 million (21.3 per cent) (see **Table 41**).

Gross inflows to the private sector increased to US$1 361.9 million (11.4 per cent) in 2003, relative to US$1 222.8 million in 2002, the effect of which

Table 41

Current Transfers (US$M)

	1/ 2002	2/ 2003	Change
TOTAL RECEIPTS	**1 337.9**	**1 453.8**	115.9
General Government	115.1	91.9	-23.2
Private Sector	1 222.8	1 361.9	139.1
Postal System	0.7	1.2	0.5
Financial System	509.0	591.3	82.3
Remittance Companies	620.9	675.8	54.9
Other	92.1	93.6	1.5
TOTAL PAYMENTS	**251.0**	**318.8**	67.8
General Government	7.5	7.2	-0.3
Private Sector	243.5	311.6	68.1
Financial System	205.3	273.9	68.6
Other	38.2	37.7	-0.5
NET CURRENT TRANSFERS	**1 086.9**	**1 135.0**	48.1

1/ Revised
2/ Estimates

was partly offset by an expansion of US$68.1 million (30.0 per cent) in gross private sector outflows. The growth in private remittance inflows in 2003 reflected, *inter alia*, the marketing efforts of financial institutions and the traditional remittance companies, which were geared towards increasing access to the service. Despite a decline in the share of inflows attributed to the remittance companies in 2003, these companies remained the most popular choice for the transmittal of funds. Remittance companies accounted for 49.6 per cent of remittance inflows in 2003, relative to 50.8 per cent in 2002. Conversely, the share of total private remittance inflows accounted for by financial institutions increased to 43.4 per cent in 2003, compared with 41.6 per cent in 2002. This improvement reflected increased effort on the part of one financial institution to expand its market share. With regard to the Government sector, the level of gross inflows declined by US$23.2 million, due mainly to a fall-off in the value of grant receipts. Outflows of US$7.2 million represented a decrease of US$0.3 million over 2002.

6.2.5 Capital and Financial Account

The *capital account* recorded a deficit of US$17.1 million in 2003, marginally above the US$16.9 million deficit recorded for 2002, while the *financial account* recorded a lower surplus of US$1 020.4 million (see **Table 36**). The performance of the *financial account* represented a

decline of US$114.7 million, when compared with the previous year, influenced by a substantial fall-off in net *other official investment* inflows.

The *other official investments* sub-account recorded net outflows of US$367.8 million in 2003, relative to net inflows of US$77.1 million in the previous year. Gross investment inflows to the sector declined by US$449.6 million to US$109.6 million in 2003, while gross official payments of US$477.3 million were US$4.7 million lower than in 2002 (see **Table 42**). The fall-off in gross inflows in 2003 was associated with the Government's not borrowing externally in the context of unfavourable international market conditions.

Table 42

Other Official Investment Flows (US$M)

	1/ 2002	2/ 2003	Change
GROSS OFFICIAL INFLOWS	**559.1**	**109.6**	-449.6
Donor Countries	0.0	0.0	0.0
Multilateral Institutions	162.6	0.0	-162.6
Other Assistance	300.0	50.0	-250.0
Project Loan	96.5	59.6	-37.0
GROSS OFFICIAL OUTFLOWS	**482.0**	**477.3**	-4.7
Government Direct	481.1	476.8	-4.3
Bank of Jamaica	0.9	0.5	-0.4
NET OFFICIAL INVESTMENTS	**77.1**	**-367.8**	**-444.9**

1/ Revised
2/ Provisional

The level of net *other private investments* rose by US$141.7 million to US$956.0 million, relative to 2002, reflecting Government's borrowing in US dollars on the domestic market, which in turn fostered private inflows to facilitate these transactions. The performance of this category was partly offset by a decline of US$7.7 million in net inflows of foreign direct investments (FDI) to US$373.5 million, relative to 2002. Lower FDI inflows in 2003 were associated with a general slowdown in new investments in the telecommunications and financial sectors. The private sector surplus was insufficient to finance the deficits on the *capital* and *current* accounts. Consequently, there was a draw down of US$432.1 million in the NIR to US$1 168.6 million at the end of 2003.

The decline in the country's net official foreign exchange reserves in 2003 largely reflected a contraction of US$446.9 million in official gross foreign assets (see **Table 43**), partially offset by a reduction of US$14.8 million to US$31.3 million in official gross foreign liabilities. The fall in the NIR of BOJ reflected the purchase of foreign exchange from the Bank by the Government for the settlement of a maturing Eurobond during the first quarter of the year and relatively high intervention sales to stem instability in the foreign exchange market during the first half of the year. In this context, the level of gross reserves for Jamaica at end December 2003 stood at US$1 199.9 million, representing an estimated 12.4 weeks of imported goods and services.

Table 43

Foreign Exchange Reserves (US$M)

	1/ 2002	2/ 2003	Change
GROSS FOREIGN ASSETS	**1 646.8**	**1 199.9**	-446.9
Bank of Jamaica	1 643.1	1 196.3	-446.8
Central Government	1.5	1.5	0.0
Other official Institutions	2.2	2.1	-0.1
GROSS FOREIGN LIABILITIES	**46.1**	**31.3**	-14.8
OFFICIAL NET INTERNATIONAL RESERVES	**1 600.7**	**1 168.6**	-432.1

1/ Revised
2/ Provisional

6.3. Foreign Exchange Management

6.3.1. Foreign Exchange Receipts and Payments

Foreign exchange receipts for 2003 were US$1 360.5 million, a decline of US$32.3 million or 2.3 per cent relative to 2002. The major sources were market purchases of US$647.8 million and purchases of GOJ loan proceeds of US$410.1 million (see **Table 44**).

Combined surrenders to the BOJ of US$320.9 million from authorised dealers and cambios during 2003 were above that of 2002, due to an 8.3 per cent increase in surrenders from cambios. Notwithstanding a decline in market purchases in 2003, the increased cambio surrenders to BOJ

reflected an increase in the percentage surrendered by that group. The lower volume surrendered by authorised dealers is consistent with the decline in market purchases as the percentage surrendered by them remained unchanged.

In addition to funds purchased through the surrender arrangement, the BOJ purchased US$327.0 million from the market, during 2003, relative to US$180.4 million in 2002. Approximately 69.0 per cent of the total transactions were brokered with authorised dealers during several bouts of tight Jamaica dollar liquidity, which emerged at different intervals during the year.

The sale to the BOJ of GOJ foreign currency loan proceeds totalled US$410.1 million in 2003, relative to US$545.8 million in 2002. The lower inflows during the review period occurred in a context where financial sector loans from multilateral agencies (World Bank, Inter-American Development Bank, Caribbean Development Bank), which were US$162.5 million in 2002 were not repeated in 2003. In a context where there was deterioration in confidence in emerging market sovereign bonds, the Government focussed on raising foreign currency loans in the regional and domestic capital markets.

During 2003, the GOJ made one public and four private offers of US dollar denominated bonds on the domestic capital market. The public offer was a three (3) year local US dollar bond issued in September with a coupon of 11.75 per cent per annum. The GOJ raised US$176.9 million from this bond which replaced a US$99.6 million Promissory Note which matured. This bond has an extendible feature which allows investors an additional two years before redemption. The four private issues resulted in the Government raising US$150.1 million from three commercial banks.

One Eurobond was issued in the CARICOM region during 2003, resulting in the GOJ raising US$50 million. This bond which was arranged by RBTT Merchant Bank, Trinidad and Tobago was issued in October at a non-taxable coupon of 9.0 per cent per annum. The bond is scheduled to mature in October 2008.

Purchases by the BOJ from the bauxite sector during 2003 were US$189.4 million, relative to US$163.8 million during 2002. The increase in purchases by the Bank reflected an increase in sales by these entities to fund their local operations and royalty payments. The increase in royalty payments is consistent with the new bauxite levy regime agreed with the sector during January 2003. This new regime includes, *inter alia*, the gradual removal of the bauxite levy and increased royalty payments from the sector, to conform to international best practice.

Table 44

Sources of Foreign Exchange (US$M)

	Inflows		Change	
	2002	2003	($)	(%)
Exports & Services	**655.6**	**837.2**	**181.78**	**27.73**
Bauxite Receipts	163.8	189.4	25.63	15.65
Direct Purchases	**491.7**	**647.8**	**156.15**	**31.76**
Surrender to BOJ				
- authorised dealers	171.0	169.0	-2.00	-1.17
- cambios	140.3	151.9	11.59	8.26
other purchases	180.4	327.0	146.56	81.25
Purchase of GOJ Loan Proceeds	**545.8**	**410.1**	**-135.66**	**-24.86**
- eurobond	295.6	49.8	-245.77	-83.15
- local US$ bond	25.0	326.4	301.37	1 205.48
- other loans	225.2	34.0	-191.26	-84.93
Grants	6.3	0.0	-6.32	-100.00
Divestment	72.2	0.0	-72.24	-100.00
Other Receipts*	113.0/1	113.2	0.14	0.12
Total Cash Inflow	**1 392.8**	**1 360.5**	-32.30	**-2.32**

1/ Revised
** includes income earned on foreign assets and funds lodged to sundry GOJ accounts at the BOJ*

Foreign exchange payments of US$1 807.2 million during 2003 were higher by US$154.1 million or 9.3 per cent relative to 2002. Foreign currency debt payments increased by 11.6 per cent, while direct sales increased by 8.8 per cent relative to 2002 (see **Table 45**).

The increased foreign currency debt payments were largely influenced by increased principal payments during the year. Bullet payments of □200 million in February and US$99.6 million in September represented 49.3 per cent of principal payments in 2003. In comparison, bullet payments comprised 37.0 per cent of principal payment in 2002.

Direct sales to the foreign exchange market during 2003 totalled US$739.3 million, reflecting an increase of US$59.7 million or 8.8 per cent relative to 2002. The higher sales were consistent with the Bank's commitment to maintain orderly conditions in the foreign exchange market.

Table 45

Uses of Foreign Exchange (US$M)

	Outflows		Change	
	2002	2003	($)	(%)
Public Debt	**891.0**	**994.4**	**103.4**	**11.6**
- Principal	545.2	636.2	90.9	
- Interest	345.8	358.2	12.4	
Direct Sales	679.6	739.3	59.7	8.8
Other Payments	**82.5**[/1]	**73.5**	-9.0	**-10.9**
Total Cash Outflow	**1 653.1**	**1 807.2**	154.1	**9.3**

[/1] *Revised*

6.3.2. Bank of Jamaica International Reserves

The net international reserves (NIR) of the BOJ declined by US$432 million during 2003 resulting in a stock of US$1 165 million as at 31 December 2003. The decline was influenced mainly by the net repayment of US$584.3 million on GOJ's foreign currency debts.

The NIR declined during every quarter of 2003, with the exception of the September quarter. The significant decline in the March quarter was due to the redemption of the □200 million 10.0 per cent 2003 Eurobond. Consequently, the NIR declined by US$257.3 million during the March quarter. The US$212.3 million decline in the June quarter reflects significant sales to the market. During the September quarter, the NIR recorded an increase of US$55.2 million mainly due to the net receipts from GOJ's foreign currency debt issues (see **Table 46**).

Total foreign liabilities declined from US$46.1 million at end-December 2002 to US$31.4 million at end-December 2003. The reduction emanated from the Bank's quarterly payments to the IMF during 2003.

6.3.3. Reserve Management

6.3.3.1. Earnings on Foreign Assets

Bank of Jamaica's total foreign assets of US$1 196.3 million at end December 2003 were US$446.7 million or 27.2 per cent less than the previous year. The year-end positions largely reflect the average holdings of US$1 198 million and US$1 713 million for 2003 and 2002 respectively.

Table 46

Net International Reserves (NIR) of the BOJ (US$M)

	2002 Dec.	2003 Mar.	June	Sept.	Dec.	Annual Change ($)
NIR	1 597.0	1 339.7	1 127.4	1 182.6	1 165.0	-432.0
Gross Foreign Assets	1 643.1	1 382.2	1 165.2	1 216.7	1 196.3	-446.7
Foreign Liabilities	46.1	42.5	37.8	34.0	31.4	-14.7

Foreign investment income declined by US$21.2 million to US$37.5 million in 2003. The 30 per cent decrease in average holdings of foreign assets, coupled with lower short-term interest rates during 2003 were the primary reasons for the fall in earnings. Income earned over the period translated to a return on investment of 3.1 per cent per annum, compared to a return of 3.3 per cent per annum in 2002. **Table 47** below provides details of earnings by asset class for the years 2002 and 2003.

Table 47

Foreign Investment Income For Year Ended 31 December

	2002		2003	
ASSETS	**US$M**	**(%)**	**US$M**	**(%)**
Euro Dollar Deposits	17.85	30.44	8.05	21.47
U.S. Agency Bonds	37.47	63.89	26.51	70.69
Reserve Fund	0.53	0.90	1.46	3.89
Other	2.80	4.77	1.48	3.95
Total	58.65	100.00	37.50	100.00
Portfolio Return		3.3		3.1
Average Income Earning Assets	1 713		1 198	

Pound and the Canadian dollar influenced modest increases in the bank's holdings of these currencies. However, the GOJ's foreign currency debt structure continued to influence the maintenance of a heavily overweight position in US dollar denominated investments. **Table 48** shows the distribution of foreign assets by currency at 31 December 2002 and 2003.

6.3.3.3. Investment Strategy

As in previous years and consistent with the Bank's policy guidelines, time deposits and bonds dominated the portfolio throughout 2003. **Table 49** shows the comparative breakdown by asset class as at end December 2002 and 2003.

Throughout most of the year, financial markets in the U.S. were volatile. The mixed performance of various economic indicators, coupled with geopolitical tension and fears of terrorism contributed to this volatility. Treasury yields fell to new lows by June but reverted by end of July to levels similar to those recorded at end 2002. This has resulted in increased uncertainty among fixed rate investors.

Table 48

Currency Composition of Foreign Assets as at End of Period

	Currency (M)		US$ Equivalent (M)		%age Share	
	2002	**2003**	**2002**	**2003**	**2002**	**2003**
US$	1 606.32	1 088.18	1 606.32	1 088.18	97.77	90.96
Euro	8.21	26.37	8.61	33.22	0.52	2.78
British Pound	2.68	28.15	4.31	50.23	0.26	4.20
Canadian $	32.87	28.69	20.80	22.20	1.27	1.85
Yen	239.24	258.71	2.01	2.41	0.12	0.20
Other	-	-	1.00	0.09	0.06	0.01
TOTAL FOREIGN ASSETS			**1 643.06**	**1 196.33**	**100.00**	**100.00**

6.3.3.2. Asset Distribution

The weakening of the US dollar was the most significant and persistent feature of the major foreign exchange markets in 2003. The dollar depreciated against all the major currencies during the year, suffering a 22 per cent and 12 per cent decline against the euro and the yen, respectively. The relative strength of the Euro, the British

Table 49

Distribution of Investments by Asset Class at 31 December

	2002		2003	
ASSET CLASS	**US$M**	**(%)**	**U$SM**	**(%)**
Cash				
BHA	136.20	8.29	75.72	6.33
Euro Dollar Deposits	27.53	1.68	56.79	4.75
U.S. Agency Bonds	829.64	50.49	563.67	47.11
Reserve Fund	609.27	37.08	458.20	38.30
	40.42	2.46	41.95	3.51
TOTAL FOREIGN ASSETS	**1 643.06**	**100.00**	**1 196.33**	**100.00**

6.3.4. The Foreign Exchange Market

The Bank of Jamaica's foreign exchange market management was severely challenged during 2003. The impact of these challenges manifested in the Jamaica dollar depreciating against its three major counterpart currencies - the United States Dollar, the Canadian Dollar and the Great Britain Pound. At 31 December 2003, the weighted average US dollar selling rate was US$1.00 = J$60.62, a depreciation of 15.9 per cent when compared to US$1.00 = J$50.97 at the end of 2002. For 2002, the weighted average US dollar selling rate had depreciated by 7.0 per cent.

The major factors contributing to the depreciation during the year were:

- Downturn in market confidence triggered by prolonged uncertainty regarding fiscal performance.
- Increased speculative demand arising from the potential adverse effect of the US/Iraq war.
- Resurgent pressures associated with seasonal demand.

The depreciating momentum that developed in December 2002 continued throughout the March quarter of 2003, with the market exhibiting a protracted period of instability. Trends in the foreign exchange market during the quarter reflected waning market confidence triggered by awareness of further deterioration in the fiscal accounts and the subsequent revision of the outlook on Jamaica's sovereign debt from stable to negative by Standard and Poor's in December 2002. Additionally, there were uncertainties regarding the Government's ability to refinance a maturing Eurobond, which was scheduled for payment in February 2003. Consequent on these factors, the demand for foreign currency remained high, influencing a 9.4 per cent depreciation in the weighted average selling rate to end the quarter at US$1.00 = J$56.24. The sharpest depreciation of 4.4 per cent was experienced during March. The adjustment in the quarter compares with a depreciation of 0.4 per cent for the corresponding period in 2002. The Bank of Jamaica moved decisively to stem the precipitous depreciation in the exchange rate, augmenting US dollar supply and implementing tighter monetary policy measures.

The instability continued into the first six-weeks of the June quarter with the exchange rate depreciating by 16.3 per cent to peak at US$1.00 = J$67.22 on 16 May. Following an announcement by the Prime Minister aimed at restoring confidence in the domestic economy, the market turned and continued appreciating. By the end of the quarter, the exchange rate was US$1.00 = J$59.00 reflecting an appreciation of 13.9 per cent relative to 16 May, and a depreciation of 4.7 per cent for the quarter. As is customary in periods of excess demand for foreign currency, the Bank maintained its presence in the market by selling foreign exchange.

During the September quarter, the foreign exchange market was fairly stable with the weighted average selling rate depreciating by 1.2 per cent ending the quarter at US$1.00 = J$59.71. The stability was underpinned by tight Jamaica Dollar liquidity conditions and the absence of the negative market psychology that had permeated the market prior to 16 May. Where conditions warranted, timely intervention by the Central Bank resulted in the market displaying immediate and positive responses.

At the onset of the December quarter, there were resurgent pressures in October associated with seasonal demand for foreign currency facilitated by net maturities on Government instruments. This resulted in a 1.2 per cent depreciation to US$1.00 = J$60.44 by end-October. The Central Bank maintained a strong presence during that month alleviating periods of tight US dollar supply. For the rest of the quarter, stability returned to the foreign exchange market which was manifested in a weighted average selling rate of US$1.00 = J$60.62 at end year relative to US$1.00 = J$60.44 at end-October.

Foreign exchange purchases and sales reported by authorised dealers and cambios in 2003 were lower than in 2002, with purchases and sales reflecting decreases of 10.9 per cent and 10.7 per cent, respectively. Average daily purchases and sales

volumes during the year were US$35.1 million and US$34.7 million, respectively, compared to US$39.7 million and US$39.2 million reported during 2002.

Authorised dealers' market share decreased by 1.4 percentage points accounting for 62.7 per cent of the total foreign exchange market trading during 2003, with cambios accounting for 37.3 per cent. Within this, inter-dealer trading remained significant, albeit a lower share than in 2002, averaging US$12.35 million daily and accounting for approximately 38.9 per cent of total market activity compared to 45.0 per cent in 2002.

The instability in the foreign exchange market during the year was also evident in a widening of the trading spread. On average, the market traded at a 0.5 per cent spread during 2003 up from 0.3 per cent in 2002. The increased spread was more pronounced in the March and June quarters, which reflected average spreads of 0.5 per cent and 0.7 per cent, respectively.

Table 50

Purchases and Sales of Foreign Exchange[22] (US$M)

	Purchases		Sales	
Quarter	**2002**	**2003**	**2002**	**2003**
March	2 148.1	2 646.3	2 164.0	2 631.9
June	2 393.7	2 204.1	2 368.2	2 183.8
September	2 742.3	1 911.8	2 718.7	1 884.5
December	2 590.4	2 040.1	2 508.7	2 012.6
Total	**9 874.4**	**8 802.3**	**9 579.7**	**8 713.0**

[22] *Includes BOJ intervention*

6.3.5. Cambios

The Central Bank conducted two hundred and fifty-one (251) inspections during 2003 in accordance with its objective of ensuring the efficiency and integrity of the cambio system. The adherence to the Bank of Jamaica's Operating Guidelines for cambios was the measure by which all cambios were monitored and supervised by the Central Bank. In addition, there was continued focus on the cambios' compliance with their obligations under the Money Laundering legislation. As part of the country's fight against money laundering and terrorist financing activities, particular attention was directed at their adherence to 'Threshold Transactions' and 'Suspicious Transactions' reporting and the 'Know Your Customer' procedures.

In June 2003 the Designated Authority for reporting purposes under the Money Laundering Act was changed from the Director of Public Prosecutions to the Chief Technical Director, Financial Investigations Division, Ministry of Finance and Planning by Ministerial Order.

During the year, eleven (11) cambios were licensed while six (6) were closed. Of the six (6) cambios closed, three relinquished their licences voluntarily, while the other licences were revoked by the Bank of Jamaica for non-compliance with the BOJ Operating Guidelines and the Money Laundering legislation. At the end of 2003, there were one hundred and forty-eight (148) cambio locations in operation, an increase of five (5) relative to 2002. The number of entities increased by two (2) moving to sixty-nine (69) in 2003. These cambios are distributed across the island with 22.3 per cent in Kingston and St. Andrew, 17.6 per cent in St. James, 13.5 per cent in St. Ann, and 9.5 per cent in Westmoreland as at end-December 2003.

The Central Bank also continued to conduct 'fit and proper' assessments of significant shareholders, directors and managers of cambios. Through this process, eighty (80) persons were assessed. This compares to a total of seventy-seven (77) in 2002.

The following table provides comparative data on the status of cambio licences for years 2002 and 2003.

Table 51

Status of Cambio Licences as at 31 December

	2002	**2003**
Applications Received	28	27
Applications Approved	13	11
Applications Pending	4	5
Cambios Closed	6	6
Total Cambios Licensed	143	148
Number of Entities	67	69

7. PRODUCTION AND PRICES

7.1 Production

The Statistical Institute of Jamaica (STATIN) indicated that, the Jamaican economy grew by 2.1 per cent (see **Table 52**). The estimated expansion in real Gross Domestic Product (GDP) represented the fifth consecutive year of positive economic growth. The most significant impetus to growth emanated from services, which accounted for an estimated 72.0 per cent of real GDP in 2003.

Table 52

Gross Domestic Product Sectoral Growth Rates

	Jan - Dec 2003 (%)
1. GOODS	1.6
AGRICULTURE FORESTRY & FISHING	5.7
MINING & QUARRYING	4.8
MANUFACTURING	-1.0
CONSTRUCTION & INSTALLATION	1.1
2. SERVICES	2.4
BASIC SERVICES	3.4
Electricity & Water	4.7
Transport Storage & Communication	3.0
OTHER SERVICES	2.1
Distributive Trade (Wholesale & Retail)	1.3
Financing & Insurance Services	6.6
Real Estates & Business Services	1.3
Producers of Government Services	0.0
Miscellaneous Services	4.9
Households & Private Non-Profit Instit.	0.3
3. IMPUTED SERVICE CHARGES	2.8
TOTAL GDP	2.1

The expansion in the goods producing sectors during the year principally reflected strong performance in **agriculture** and **mining**. For services, **financing & insurance**, **miscellaneous, electricity & water** and **transport, storage & communication** were the main areas of growth.

The value added of the **agriculture** sector grew by 4.4 per cent in 2003, compared with the decline of 7.0 per cent recorded in 2002. This expansion contributed an estimated 6.0 per cent of overall growth in GDP, and stemmed from the *domestic agriculture* sub-sector, as the *export agriculture* sub-sector is estimated to have contracted during the year.

Information from the Ministry of Agriculture indicate that, for 2003, domestic crop production increased by 13.9 per cent, relative to 2002 (see **Table 53**). The growth in domestic agriculture during the year represented a recovery from the impact of the May/June and September 2002 flood rains that caused a decline of 12.0 per cent in domestic agriculture production in that year. Agriculture production was also enhanced by the favourable weather conditions experienced throughout 2003, which resulted in marked increases in the yields of most crops, in particular vegetables. Despite the overall growth in domestic agriculture, several factors served to moderate the performance of the sector. Among these were the scarcity of planting materials, in particular legumes, badly damaged farm roads, poor germination of selected vegetable seeds and higher cost of inputs.

With regard to export agriculture, the export volume of traditional agriculture crops declined by an estimated 5.3 per cent in 2003, relative to 2002 (see **Table 54**). Banana and coffee exports experienced another year of decline, contracting by 2.5 per cent and 12.4 per cent, respectively, in the review year. For coffee, the industry was faced with significant increases in the cost of inputs such as pesticides, fertilizers, labour and transportation. Sugar cane production fell by 7.8 per cent during the year, relative to 2002, attributed to a lower level of replanting at the beginning of the 2002/03 crop year. Partly offsetting the decline in banana and coffee were estimated increases in the volumes of citrus and cocoa exported.

Table 53

Production (000'tonnes)			
Crop Group	**Jan -Dec 2002**	**Jan - Dec 2003**	**Growth (%)**
Yams	148.2	152.2	2.8
Vegetables	136.0	171.8	26.3
Other tubers	33.1	35.6	7.5
Fruits	38.0	46.6	22.6
Condiments	22.0	26.2	18.9
Plantains	20.9	20.2	-3.3
Potatoes	25.4	30.3	19.3
Legumes	5.5	5.5	0.8
Cereals	1.8	2.0	16.4
Total	**431.6**	**491.5**	**13.9**

Source: Ministry of Agriculture

Table 54

Exports (000'tonnes)			
Crop	**Jan -Dec 2002**	**Jan - Dec 2003**	**Growth (%)**
Banana	39.9	37.9	-5.1
Citrus	4.8	5.8	20.9
Cocoa	0.7	1.0	35.8
Coffee	1.6	1.4	-12.3
Pimento	0.5	0.3	-45.7

Source: Bank of Jamaica

The output of the **mining** sector expanded in 2003, contributing an estimated 6.0 per cent of the growth in GDP. This growth reflected a general increase in capacity utilisation in the sector to approximately 96.3 per cent, up from approximately 90.8 per cent in 2002. Alumina production in 2003 grew by 5.7 per cent, relative to 2002, while crude bauxite production declined by 5.3 per cent in the year. In relation to exports, alumina volumes increased by 7.0 per cent, while bauxite volumes declined by 6.6 per cent. The increase in alumina production partly reflected normalisation in output in 2003 following the impact of the May/June 2002 flood rains. Conversely, the decline in the production of crude bauxite partly reflected inclement weather conditions in the December 2003 quarter.

Value added in the **manufacturing** sector contracted marginally by 1.0 per cent in 2003, the second successive decline since 2001. The contraction in value added stemmed from the other *manufacturing* sub-sector, as the *food, beverages & tobacco* sub-sector is estimated to have grown marginally during the year. The estimated decline in *other manufacturing* was mainly attributable to the performance of petroleum refining activities, given the closure of Petrojam for scheduled maintenance in the June 2003 quarter. Estimated reductions in the textile & wearing apparel, leather and paper industries, augmented the decline in petroleum refining. Growth in the *food, beverages & tobacco* sub-sector was driven primarily by the food processing and non-alcoholic beverages industries, partly offset by estimated declines in the sugar, molasses & rum, alcoholic beverages and tobacco groups. The increase in food processing related to poultry meat, edible oils and flour (see **Table 55**). The decline in alcoholic beverages may have reflected lower consumer demand, resulting from price increases over the period January to April 2003.

Table 55

Production (000'tonnes)			
Items	**Jan -Dec 2002**	**Jan - Dec 2003**	**Growth (%)**
Poultry Meat	67.6	76.4	13.0
Edible Oils	14.7	17.9	22.0
Cornmeal	11.1	12.3	10.9
Condensed Milk	14.5	13.9	-4.3
Flour	126.9	130.0	2.4
Animal Feeds	369.4	363.7	-1.5
Sugar	175.2	158.4	-9.6

Source: Planning Institute of Jamaica

The **construction & installation** sector is estimated to have expanded by 1.1 per cent in 2003, following growth of 2.3 per cent in 2002. The expansion in the sector reflected four consecutive years of real economic growth. The industry grew consistently throughout the four quarters of the year, with the September quarter registering the strongest growth. The growth in the sector was partly inferred from a real expansion of approximately 40.0 per cent in commercial bank loans extended to construction during 2003. In addition, continued work on the Highway 2000 and the Northern Coastal Highway Improvement projects enhanced construction during the year. These were complemented by capital expenditure by the National Works Agency (NWA) on roads and capital expenditure by the utilities companies. The latter included the installation and expansion of transmission pipes, plant upgrade, transformer rehabilitation,

expansion of generating capacity and extension of electrical wires. Notwithstanding the growth emanating from the above-mentioned projects, there may have been a lower level of activity in the residential segment of the market. There were respective declines of 23.7 per cent and 46.3 per cent in housing starts and completions in 2003, relative to 2002, by the National Housing Trust (NHT), the major provider of residential houses in Jamaica. The reduction in residential construction in 2003 followed from substantial housing development schemes in 2002.

With respect to services, all the sub-sectors, with the exception of **Government**, are estimated to have improved in 2003. The **transport, storage and communication** sector grew by 3.0 per cent for the year and, given its weight in GDP, was the second largest contributor to the economic expansion. Much of this dynamism was fuelled by the expansion of the communication sub-sector, in particular mobile telephone networks. In this context, the total number of telephone lines in service (mobile and 'plain old telephones') was estimated to have grown by approximately 13.0 per cent during the year, relative to 2002. For the transport sub-sector, growth was inferred, in part, from a 16.5 per cent increase in visitor arrivals in 2003, relative to the previous year. Additionally, cargo movements over the Island's main seaports, as well as, the number of ships calling at Jamaican ports is estimated to have grown by approximately 0.8 per cent and 1.9 per cent, respectively, relative to 2002.

For the **electricity & water** sector, growth of 4.7 per cent in 2003 was reflected in expansions of 5.0 per cent and 3.5 per cent in total electricity generation and sales, respectively. Electricity sales categorized as "industrial" and "other" increased by 5.4 per cent and 0.8 per cent, respectively, during the year. This buoyancy is attributed to the constant renovation and expansion exercises that have been implemented by the main power company over the years. In particular, additional generating capacity was installed in 2002. Augmenting the growth in the *electricity* sub-sector was an increase of 3.9 per cent in water production in 2003, relative to the previous year.

The **distributive trade** sector is estimated to have grown by 1.3 per cent in 2003, continuing the trend observed since 2000. The growth in the sector partly reflected an estimated real increase of 7.4 per cent in consumption tax receipts, relative to 2002. In addition, the real stock of loans extended by commercial banks to the sector increased by 56.3 per cent. Growth was also enhanced by the recovery in agriculture production during the year. Conversely, the estimated real reduction of 2.3 per cent in merchandise imports had a negative impact on growth in the sector.

An expansion of 6.6 per cent in the real value added of **financing & insurance** services during the year was underpinned by growth in the *banking institutions, other financial institutions* and *insurance* sub-sectors. The growth of banking institutions primarily reflected the performance of commercial banks, which offset the decline in the value added of the Bank of Jamaica and merchant banks. However, relative to 2002, the value added of the Bank of Jamaica improved.

For the review year, increased returns on investments and loans & advances in commercial banks were the main impulses generating growth in the *banking institutions* sub-sector. During 2003, commercial bank loans and advances grew in real terms by 19.1 per cent, which contributed to the buoyancy in the interest income of these institutions. Over the same period, money market average interest rates and commercial bank weighted average loan rates rose by approximately 504 and 106 basis points, respectively. These gains were complemented by an increase in commercial banks' non-interest income.

As indicated by the performance of the tourism industry, value added in **miscellaneous** services is estimated to have expanded by 5.1 per cent, relative to 2002. The major factor contributing to the performance of the tourism industry during the year was an increase of 16.5 per cent in visitor arrivals. Growth in visitor arrivals was driven primarily by increases of 30.8 per cent and 6.6 per cent in cruise and stopover arrivals, respectively. Visitor expenditure also increased by 9.6 per cent

in 2003, relative to the previous year (see **Balance of Payments**).

Outlook

For 2004, forecast for the Jamaican economy is growth within the range of 2.0 - 3.0 per cent. This projection is predicated on positive expectations for the goods producing, as well as services sectors. The most notable developments in the economy are expected to be derived from the anticipated acceleration of growth in **mining, financing & insurance** and **construction**, as well as continued growth in **agriculture** and **miscellaneous** services.

The main challenge to growth could stem from a continuation of the dry spells observed since the start of 2004, given its implications for the **agriculture** sector and the sector's linkages to the **distributive trade** and **manufacturing**. In addition, growth in the **financing & insurance** sector will depend on a stable macroeconomic environment. However, the external environment is expected to remain favourable as growth accelerates among Jamaica's major trading partners in the context of continued low inflation.

7.2. Prices

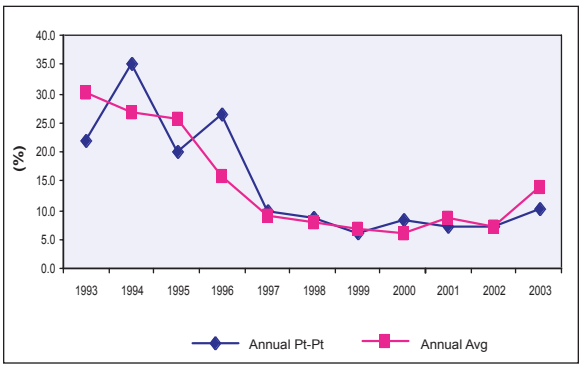
7.2.1. Overview

Following six consecutive years of single digit inflation, prices increased by 14.1 per cent in 2003, relative to inflation of 7.3 per cent in 2002. This outturn was influenced by a number of factors including exchange rate movements, international commodity prices, Government revenue measures and administered price adjustments. The annual average inflation for the year was 10.3 per cent, 3.2 percentage points higher than that of the previous year (see **Chart 15**).

Price deflation of 0.4 per cent was observed in the March 2003 quarter. The deflation in this quarter resulted from significant declines in the prices of agricultural produce due to increased supplies. However, there were strong inflationary impulses in the second quarter, reflecting an outturn of 6.0 per cent. Inflation in the June quarter was fuelled by the widening of the General Consumption Tax (GCT) base, effected on May 1, 2003, to include some previously zero-rated and exempt items, increases in international oil and other commodity prices and sharp exchange rate depreciation. With tightened monetary policy in the second half of the year, the inflation outturn moderated in the September and December quarters, with respective outturns of 4.6 per cent and 3.4 per cent. Lagged and second round effects of the factors that prevailed in the June quarter, increases in transportation costs, as well as seasonal increases in school related expenses dominated the inflationary process in the September quarter. In the December quarter, inflation was driven by the effect of price increases in crude oil and grains in the international market, as well as, administered price adjustments.

Chart 15

Jamaica's Headline Inflation Rate



The higher inflationary pressures reflected increased underlying or core inflation, calculated using the trimmed mean approach. For the year, core inflation was 8.1 per cent, or 4.7 percentage points higher than that recorded for 2002 (see **Chart 16**). Monthly movements in core inflation increased in the first half of 2003. However, with the tightening of monetary policy, there was a moderation in this trend towards the end of the year (see **Chart 17**).

Chart 16

CPI and Core Inflation (y-o-y)

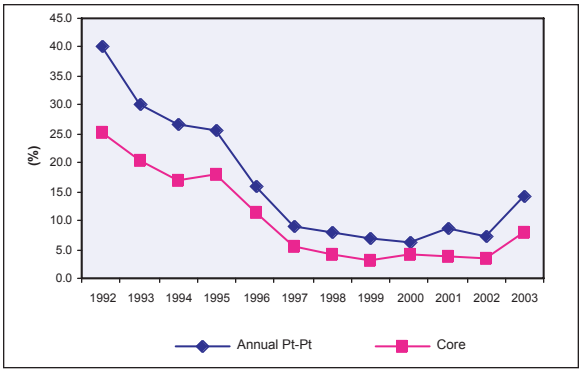
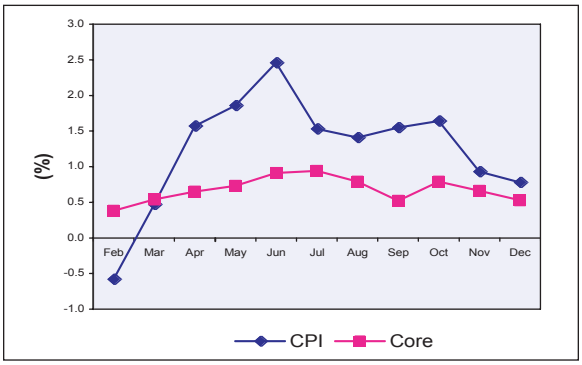


Chart 17

CPI and Core Inflation (m-t-m)



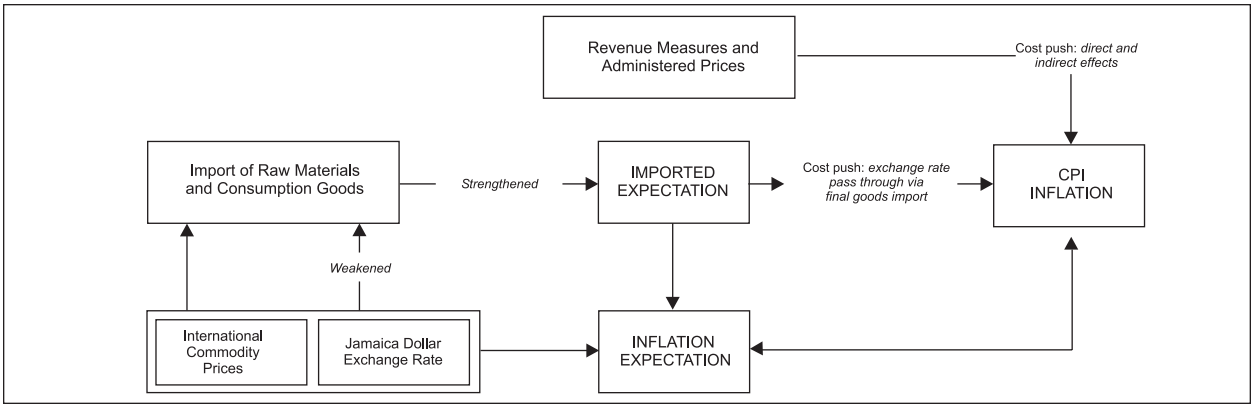
7.2.2. Factors Affecting Inflation

The major shocks to inflation were the significant disruption to the foreign exchange market, adjustments in government revenue measures and administered prices, increases in international oil and other commodity prices and to a lesser extent, inflation expectations (see **Flow Diagram**).

The weighted average selling rate of the Jamaica Dollar in US dollar terms declined by 15.9 per cent in 2003 compared to 7.0 per cent in 2002. The pace of depreciation accelerated in the first half of the year, with the exchange rate moving by 14.2 per cent over the January to May period. The rate of depreciation, however, slowed in the second half of the year, as a result of tighter monetary policy action by the Bank. Consequently there was lagged effect of the pass-through to prices. Approximately 8.5 percentage points of the annual inflation was the result of exchange rate movements.

Other factors influencing inflation in 2003 were adjustments in government revenue measures and administered prices, introduced in the June quarter. The Government revenue measures influenced price increases in various basic consumer goods and services such as food, healthcare, cigarettes, and household items. Upward adjustments in the minimum wage and increased administered prices in the transportation sector also provided significant impetus to inflation.

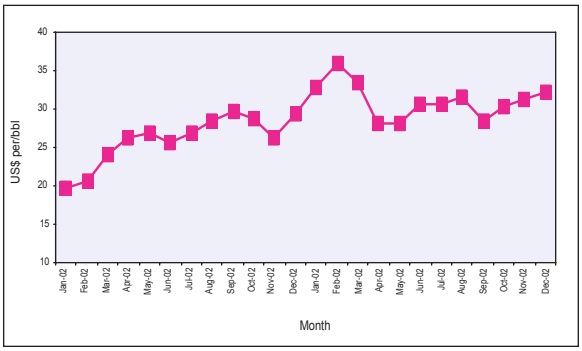
Flow Diagram
Factors Affecting Inflation in 2003



Movements in international commodity prices had an unfavourable effect on domestic prices. The price of the benchmark West Texas Intermediate (WTI) crude oil rose by 10.8 per cent in 2003, relative to an increase of 38.0 per cent in 2002 and a reduction of 36.4 per cent in 2001. The average price of crude in 2003 was approximately US$31.00 per barrel, relative to US$26.00 per barrel in 2002 (see **Chart 18**). The increase in the price of crude oil had a noticeable effect on the prices of domestic household and automotive fuels, as well as utility rates.

Chart 18

Monthly Oil Prices



The rise in the prices of vegetable oils (see **Chart 19**), on the world market also had an unfavourable effect on domestic prices. These increases were influenced by heightened world demand, coupled with reduced output in the major producing areas. The annual average increases in the prices of groundnut oil and soybean oil in 2003 were 80.9 per cent and 21.9 per cent, respectively (see **Table 56**). These compared to price increases of 1.0 per cent and 28.3 per cent, respectively, in 2002.

Chart 19

Annual Soybean Oil Prices

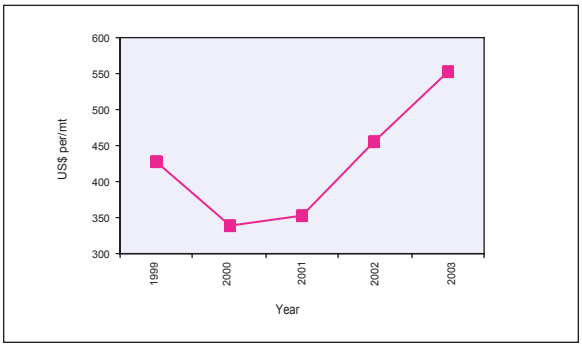


Chart 20

Annual Wheat Prices

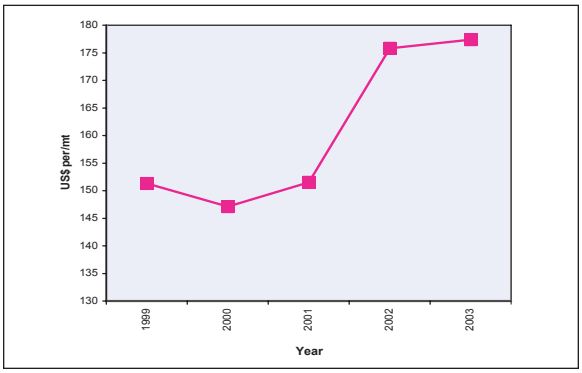


Table 56

International Prices of Selected Commodities
Annual Averages (US$)

Commodity	Units	2002	2003	Annual Average (%)
Vegetable Oils				
Coconut Oil	$/mt	421.0	467.3	11.0
Groundnut oil	$/mt	687.1	1243.2	80.9
Soybean Oil	$/mt	454.3	553.9	21.9
Grains				
Soybean meal	$/mt	175.2	210.9	20.4
Soybean	$/mt	212.7	264.0	24.1
Maize	$/mt	99.3	105.4	6.1
Sorghum	$/mt	101.7	106.5	4.7
Wheat Canada	$/mt	175.8	177.4	0.9
Rice (A1)	$/mt	150.2	151.5	0.9
Raw Materials				
Cotton, 'A'	¢/kg	101.9	139.9	37.3
Rubber, US	¢/kg	90.7	122.5	35.1
Fertilizer-TSP	$/mt	133.1	179.4	34.8
Zinc	¢/kg	77.9	82.8	6.3

Increases in international grain prices also had an adverse impact on domestic prices. In particular, soybean prices in 2003 were higher on average by approximately 20.0 per cent, relative to 2002 (see **Table 56**). This primarily reflected adverse weather conditions in major producing countries, as well as, increased global demand. Supplies of grains such as wheat and corn were affected by a significant drought in the Midwest region of the United States of America, a major producing area.

The increase in prices in the review period was also influenced by inflation expectations of producers, traders and consumers. Waning confidence and instability at the beginning of the

year led to increased speculation against the Jamaica Dollar. The depreciation in the Jamaica Dollar influenced the price setting behaviour of producers and traders, which translated into domestic prices.

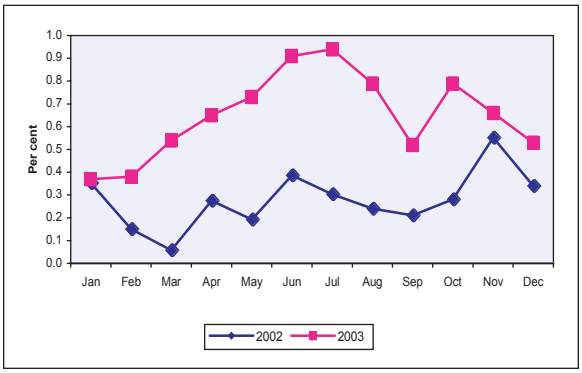
Significant growth in the agriculture sector during 2003 had a moderating effect on inflation in contrast to previous years, due in part to improved weather conditions and significant rehabilitative efforts in the sector. This led to significantly lower inflation being recorded in the agriculture related sections of the CPI basket, relative to 2002 (see **Table 58**). Additionally, the containment of money growth, particularly in a context of increased demand pressures in the second half of the year, also assisted in moderating inflation in 2003.

7.2.4. Core Inflation

Core inflation increased to 8.1 per cent in 2003 from 3.4 per cent in 2002. On a monthly basis, core inflation in 2003 was consistently above the rate that obtained in the previous year (see **Chart 21**). This measure was particularly high in the June and September quarters, in the context of rapid exchange rate movements.

Chart 21

Monthly Core Inflation: 2002 & 2003



As a consequence of the rapid depreciation, the Bank of Jamaica severely tightened monetary policy. Subsequent to this adjustment, core inflation moderated towards the end of the year (see **Chart 21**). The increase in core inflation in the second half of the year was 4.3 per cent, relative to 3.6 per cent recorded in the first half of the year. The pace of reduction in the latter half year was constrained by the inflationary impact of unprogrammed monetary injection resulting from greater than expected Government financing needs. The outturn of this measure for the December quarter was 1.9 per cent, relative to 2.3 per cent recorded in the two previous quarters.

Table 57

Decomposition of Inflation Outturn: Calendar Year 2003

	Inflaton (%)	Contribution (%)
NON- CORE	**6.0**	**42.6**
Food & Drink	3.1	21.9
Meat, Poultry & Fish	1.2	8.7
Baked Products Cereals & B'fast Drinks	1.0	7.4
Dairy Products	0.8	5.8
Transportation	1.2	8.3
Fuels/Other Housing Expenses	1.1	7.8
Miscellaneous Expenses	0.9	6.6
Other	-0.3	-1.9
CORE	**8.1**	**57.4**
TOTAL	**14.1**	**100.0**

7.2.5. Contribution to Inflation

The largest contributors to the increase in the CPI in 2003 were the *Food & Drink, Transportation* and *Miscellaneous Expenses* sub-indices, accounting for 47.8 per cent, 13.3 per cent, and 10.5 per cent of the total inflation out turn, respectively (see Table 58). The *Fuels & Other Household Supplies* and the *Housing & Other Housing Expenses* sub-indices, each contributed 9.4 per cent.

Within the *Food & Drink* sub-index, the *Meat, Poultry & Fish* sub-group increased by 11.9 per cent, providing the main impetus to the expansion of the sub-index. In addition, there were price stimuli to the *Baked Products, Cereals & Breakfast Drinks* and *Dairy Products Oils & Fats* sub-groups, which increased by 19.0 per cent and 19.1 per cent, respectively. The increased prices of vegetable oils and grains in the international market affected these sub-groups. Other changes of note within

the *Food & Drink* sub-category were the increase of 15.7 per cent and 19.7 per cent in the *Meals Away From Home* and the *Other Food & Beverage* sub-categories, respectively. Price increases in these sub-groups had a second round effect on the *Meals Away From Home* sub-category. While the rise in the *Other Food & Beverages* sub-index was associated with increases in the prices of patties, aerated water, as well as increased tax associated with alcoholic drinks. Price increases in the agriculture related categories of *Starchy Food* and *Vegetables & Fruits* were lower than the previous years, due to increased output of the agricultural sector (see **Production**).

The increase in the *Transportation* sub-index of 28.6 per cent was due mainly to significant increases in bus and taxi fares. Additionally, the increases in international oil prices, also contributed to the increase in the *Transportation* sub-index.

The contribution of the *Miscellaneous Expenses* sub-category to inflation was due mainly to revenue enhancement measures of the Government. The widening of the GCT base, as well as exchange rate movements and the introduction of a 2.0 per cent customs user fee ("cess") all contributed to the increase in prices of many items within this group. Of note, was the average increase of 29.3 per cent in the price of cigarettes. Additionally, during the year there were noticeable increases in the cost of tuition, examination fees and textbooks.

Prices in the *Fuels & Other Household Supplies* sub-index were primarily influenced by international oil prices, revenue measures and the exchange rate, contributing 9.4 per cent to inflation. The *Fuels* sub-group, which increased by 27.6 per cent was primarily affected by increased price of cooking gas and kerosene. The *Other Household Supplies* sub-group increased by 12.5 per cent, was mainly affected by the widening of the GCT base.

The *Housing & Other Housing Expenses* sub-index was affected primarily by administered price adjustments. Administered price changes were

Table 58

Jamaica - Component Contribution to Inflation
2002 vs 2003

Groups and Sub-groups	Group Weights	Price Inflation (%) 2002	Price Inflation (%) 2003	Contribution to Inflation (%) 2002	Contribution to Inflation (%) 2003
FOOD & DRINK	0.5563	7.8	11.2	60.6	47.8
- Meals Away From Home	0.0741	4.1	15.7	4.2	8.4
- Meat Poultry & Fish	0.1613	4.9	11.9	10.3	13.9
- Dairy Products Oils & Fats	0.0668	3.3	19.1	3.0	9.2
- Baked Products Cereals & Breakfast Drink	0.0864	8.7	19.0	10.5	11.9
- Starchy Foods	0.0525	10.3	0.7	7.5	0.3
- Vegetables & Fruits	0.0650	25.7	-6.5	23.1	-3.0
- Other Food & Beverages	0.0502	2.8	19.7	1.9	7.2
FUELS & OTHER HOUSEHOLD SUPPLIES	0.0735	2.2	20.7	2.7	9.4
- Household Supplies	0.0482	3.5	12.5	2.3	4.3
- Fuels	0.0253	1.2	27.6	0.4	5.0
HOUSING & OTHER HOUSING EXPENSES	0.0786	15.2	16.7	16.2	9.4
- Rental	0.0209	6.8	13.4	2.0	2.0
- Other Housing Expenses	0.0577	17.8	17.6	14.2	7.4
HOUSEHOLD FURNISHINGS & FURNITURE	0.0283	5.4	8.5	2.0	1.7
- Furniture	0.0068	10.8	11.4	1.0	0.6
- Furnishings	0.0215	3.2	7.3	1.0	1.1
HEALTHCARE & PERSONAL EXPENSES	0.0697	5.0	11.5	4.9	5.8
PERSONAL CLOTHING FOOTWEAR & ACC.	0.0507	3.9	6.0	2.8	2.1
- Clothing Materials	0.0055	5.6	1.6	0.4	0.1
- Readymade Clothing & Accessories	0.0242	1.8	4.6	0.6	0.8
- Footwear	0.0159	4.6	8.9	1.0	1.0
- Making & Repairs	0.0051	10.2	6.6	0.7	0.2
TRANSPORTATION	0.0644	2.2	28.6	2.0	13.3
MISCELLANEOUS EXPENSES	0.0785	8.2	18.5	8.9	10.5
ALL GROUPS	1.0000	7.3	14.1	100.0	100.0

related to increased rental rates, higher utility rates, a rise in artisans' fees and an increase in the minimum wage. The higher utility rates reflected, in particular, a rebalancing of telephone rates.

7.2.6. Regional Inflation

Inflation in the Other Towns was marginally higher than in the other regions. For the year, the indices for the **Other Towns**, **KMA** and **Rural Areas** increased by 14.8 per cent, 14.4 per cent and 13.3 per cent, respectively. This outturn revealed that inflation in the KMA and Other Towns exceeded the overall increase in the All Jamaica index, while the changes in the Rural Areas had a moderating effect. On the contrary, inflation in 2002 in the Rural Areas was higher than in the other two regions (see **Chart 22**).

The disparity in price movements across the regions in 2003 was mirrored in four of the eight groups, with the most significant divergence in *Fuels & Other Household Supplies* (see **Table 59**). This category reflected respective increases of 31.4 per cent, 14.9 per cent and 10.1 per cent in the **KMA**, **Other Towns** and **Rural Areas**. Within *Fuels & Other Household Supplies*, the widest deviation was reflected in the *Fuels* sub-group. The greater increase in the *Fuels* sub-group in the KMA was caused in part by a significant increase in the price of kerosene, which was not experienced in the other regions.

Chart 22

Regional Inflation 2002 and 2003

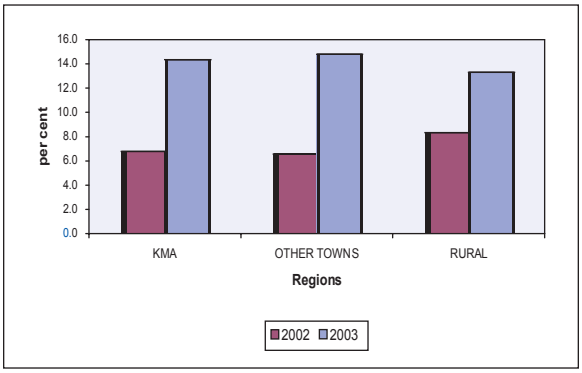


Table 59

Regional Inflation

Groups / Sub-groups	Weight in CPI	KMA (%)	Other Towns (%)	Rural (%)
FOOD & DRINK	0.5563	9.8	13.2	11.7
- Meals Away From Home	0.0741	13.8	18.0	17.7
- Meat Poultry & Fish	0.1613	11.0	12.0	12.9
- Dairy Products Oils & Fats	0.0668	15.9	22.8	20.8
- Baked Products Cereals & Breakfast Drink	0.0864	16.3	21.2	20.9
- Starchy Foods	0.0525	-1.4	1.6	1.4
- Vegetables & Fruits	0.0650	-8.3	-4.0	-5.6
- Other Food & Beverages	0.0502	16.1	19.8	23.9
FUELS & OTHER HOUSEHOLD SUPPLIES	0.0735	31.4	15.0	10.1
- Household Supplies	0.0482	11.5	14.9	12.5
- Fuels	0.0253	50.1	15.0	8.1
HOUSING & OTHER HOUSING EXPENSES	0.0786	16.9	16.1	17.1
- Rental	0.0209	14.6	8.5	8.5
- Other Housing Expenses	0.0577	17.8	17.0	18.1
HOUSEHOLD FURNISHINGS & FURNITURE	0.0283	6.7	9.1	9.9
- Furniture	0.0068	1.8	16.2	16.0
- Furnishings	0.0215	8.7	5.9	6.8
HEALTHCARE & PERSONAL EXPENSES	0.0697	10.1	14.1	12.4
PERSONAL CLOTHING FOOTWEAR & ACC.	0.0507	6.7	5.7	5.5
- Clothing Materials	0.0055	1.8	1.1	1.4
- Readymade Clothing & Accessories	0.0242	5.8	5.4	3.1
- Footwear	0.0159	10.2	6.2	9.1
- Making & Repairs	0.0051	4.6	7.2	9.2
TRANSPORTATION	0.0644	32.9	26.4	22.7
MISCELLANEOUS EXPENSES	0.0785	16.0	18.8	23.1
ALL GROUPS	1.0000	14.4	14.8	13.3

8. BANKING AND CURRENCY OPERATIONS

8.1. Banking Services

The Bank of Jamaica carries out a variety of activities that support the local payments and settlement systems and provides oversight to these systems. The Bank provides a wide range of banking services to the government, commercial banks, primary dealers and other regional central banks. Limited over-the-counter services are also provided to the general public. As fiscal agent, the Bank also administers new borrowings in the domestic and Treasury Bill and bond markets.

The Bank continues to provide vaulting and settlement services to the Jamaica Central Securities Depository (JCSD), a wholly owned subsidiary of the Jamaica Stock Exchange. It also facilitates the settlement of regional payments through the CARICOM bilateral arrangements and the exchange of CARICOM currencies.

8.2. Payment Transactions

The automated clearing house through which local cheques are cleared and settled and the central bank-owned electronic funds transfer system, the Customer Inquiry and Funds Transfer System (CIFTS) for the settlement of interbank obligations are the two main payment systems in operation locally. For cheques, multilateral netting takes place twice daily and balances settled on the books of the Central Bank while CIFTS payments are settled gross. Both cheque and CIFTS payments are settled in Central Bank assets at the end of day through a deferred settlement arrangement.

In Jamaica, payments are effected mainly by cash, cheques, cards (debit, credit, stored value) and interbank transfers. New electronic payment instruments have been introduced and a wide array of banking products and services are being delivered through electronic banking (e-banking) channels. Despite these developments, cheques remain the most commonly used payment form in Jamaica as they are used for a wide variety of payment transactions, retail and wholesale.

During the year the Bank provided cheque clearing and settlement facilities (automated and manual) for 13.6 million Jamaica Dollar items valued at J$2 009.6 billion. This compares to 11 million items valued at J$1 735.5 billion exchanged through the clearing in 2002. US dollar items totalling US$2.3 billion were exchanged locally through the clearing. This represents an increase of 16 percent over the US$2.0 billion exchanged in 2002. These foreign items are not settled using Central Bank assets. They are settled bilaterally on a net basis by wire transfers to/from overseas correspondent bank accounts held by the clearing banks.

The local currency items processed through the clearing house represent a fraction of the overall cheque usage as they exclude those items encashed or deposited at the bank on which they were drawn. Proprietary transactions in 2003 were approximately J$1 200 billion, accounting for almost 40 per cent of total local currency cheques paid.

During the year 25 085 large value payments[24] valued at J$1 700.7 billion were executed electronically through CIFTS. This compares with 21 548 CIFTS payments valued at J$1 359.7 billion in 2002, an increase by volume and value of 16 per cent and 25 per cent, respectively. The combined value of Jamaica Dollar payments effected by cheques and via CIFTS in 2003 was approximately J$5 000 billion.

[24]Interbank electronic funds transfer payments.

8.2.1 Payment System Developments

The Bank of Jamaica is committed to ensuring the integrity and efficiency of the payment system as a critical element of its mandate to ensure the soundness and stability of the Jamaican financial system. Over the years there have been significant developments both initiated and facilitated by the Bank to enhance the efficiency of the payment and settlement systems. In keeping with this commitment and in an effort to standardize local clearing processes, the clearing banks, led by the Bank of Jamaica, amended the Clearing House Rules in December 2003 to allow the inclusion in the local clearing of Sterling, Canadian and Euro items issued by or drawn on local commercial banks. As for USD items, these instruments will be settled bilaterally on a net basis by wire transfers to/from correspondent bank accounts or by drafts.

The hold period for non-U.S. dollar foreign items averaged thirty days and varied among banks. The expansion of the range of eligible items puts the major foreign currencies on equal footing, reduces settlement risk and allows for the reduction and synchronization of the hold and recourse periods on these items to six business days. The new Rules took effect in January 2004.

8.3. Currency Operations

8.3.1. Currency Distribution System

In 2003, the currency distribution system was rationalized with the closure of the two currency agencies in Mandeville and Montego Bay. Since then, all currency issues and redemptions are done directly from the Bank's offices in Kingston. This centralization of the currency operations has resulted in significant cost savings for the Bank.

8.3.2. Banknotes Issued

During the year, 171.3 million notes were issued valued at $73.0 billion or 26.5 per cent more than 2002. Of these, 123.9 million pieces or 72.3 per cent were new notes (see **Table 60**). The dominance of new notes continued to reflect the Bank's clean note policy, which acts as a deterrent to counterfeiting. Additionally, it illustrates the relatively short average useful lives of the lower denominations, $100 and $50, as 87.3 per cent and 96.1 per cent, respectively, of these notes issued were new.

8.3.3. Coins

The value of coins issued in 2003 rose by only 2 per cent, relative to 2002, as coins valued at $426.2 million were put into general circulation compared with $417.8 million in the previous year. A total of 34.4 million coins valued at $256.8 million was redeemed during the year, resulting in a net increase of $169.42 million in the value of coins in circulation.

Demand for the $1 coin remained strong with 31.6 million pieces going into circulation. This however, was 8 per cent lower than the 34.3 million pieces issued in 2002. Nonetheless, the figure reflects the continued high demand for this coin by the retail sector as it has assumed the role traditionally undertaken by the one cent, ten cent and twenty-five cent coins in change-making in commerce.

Table 60

Banknotes Issued in 2003 - By Category
(in millions of pieces)

	Total Notes		New Notes		ATM Fit	
Denom	**Pieces**	**%**	**Pieces**	**% of Total**	**Pieces**	**% of Total**
$1000	42.82	100	25.34	59.20	17.48	40.80
$500	46.50	100	24.75	53.20	21.75	46.80
$100	56.86	100	49.64	87.30	7.22	12.70
$50	25.12	100	24.14	96.10	0.98	3.90
TOTAL	**171.30**	**100**	**123.80**	**72.30**	**47.15**	**27.73**

8.3.4. Currency Redemptions and Processing

A total of 162.5 million banknotes valued at $68.1 billion was redeemed to the Central Bank during 2003. The Bank processed 161.1 million notes, valued at $67.4 billion during the period under review. This was 17 per cent more than the 136.5 million pieces processed in 2002. Of this amount 113.3 million pieces or 70 per cent were deemed unfit for reissue and were destroyed. The remaining 47.8 million notes were re-classified as ATM-Fit and subsequently reissued. In the previous year, 69 per cent of notes processed were determined to be unfit and were destroyed on-line.

8.3.5. Currency In Circulation

Currency in circulation at end December 2003 was valued at $29.8 billion, an increase of 20.9 per cent over that recorded in 2002. Banknotes accounted for 95.6 per cent and coins 4.4 per cent of the total. **Charts 23 and 24** show the denominational breakdown of banknotes in circulation. The $1000 notes valued at $18.91 billion, accounted for 66.5 per cent of total banknotes in circulation compared to 62.7 per cent at end 2002. The $500 denomination valued at $6.8 billion accounted for 24.1 per cent compared to 27.2 per cent at December 2002, while the $100 notes and $50 notes valued at J$2.0 billion and J$503.7 million accounted for 7.0 and 1.8 per cent respectively at end 2002.

Chart 23
Comparision of Decimal Notes in Circulation as at 31 December 2003 (By Value)

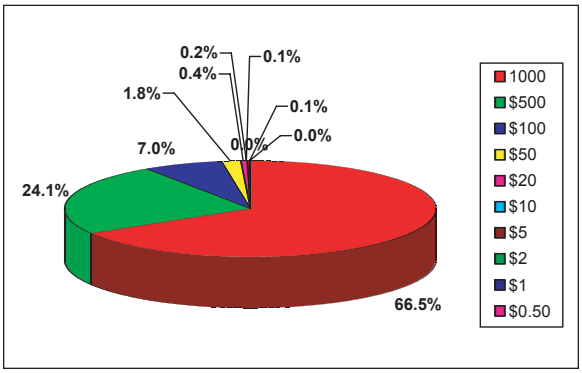
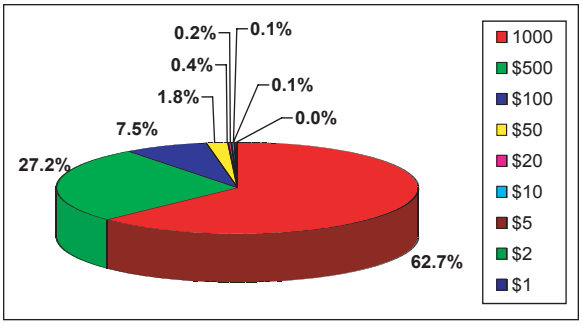


Chart 24
Composition of Decimal Notes in Circulation as at 31 December 2002 (By Value)



8.3.6. Public Education And Counterfeit Detection

During the year the Bank continued its public education programme, mainly through seminars to train large-volume cash handlers in banknote authentication techniques. This remains a major plank of the Bank's anti-counterfeit strategy. Participants were drawn mainly from the banking, insurance and public sector institutions. An indication of the effectiveness of this programme may be gleaned from the counterfeit statistics for 2003 and 2002 as set out in **Table 61**.

The number of counterfeit $1 000, $500 and $100 notes detected in processing by the Bank of Jamaica increased by 53 per cent, that is, from 1 560 notes in 2002 to 2 381 in 2003. Of significance, however, is the fact that most of the counterfeits were detected by the commercial banks upon presentation at their counters (79 per cent in 2003 compared to 71 per cent in 2002). The commercial banks detected 90.6 per cent and 72.7 per cent, by value, in 2003 and 2002, respectively. Despite the 53 per cent increase in the number of counterfeit notes detected in processing, the value of these increased by only 26 per cent, from $1.3 million in 2002 to $1.6 million in 2003. This is attributable to increased recognition by the public of the security features in the $1000 note. Consequently, counterfeiters have resorted to targeting the $100, which they now perceive as a 'softer' target. As a result, the number of counterfeit $100 notes detected in 2003 increased by 511%.

Table 61

Counterfeit Notes Processed by Bank of Jamaica
2003

Denomination $	Counterfeits detected in lodgements by BOJ		Counterfeits confiscated by financial institutions		Total Processed by BOJ	
	Value	Pieces	Value	Pieces	Value	Pieces
1 000	90 000	90	1 348 000	1 348	1 438 000	1 438
500	29 500	59	106 000	212	135 500	271
100	35 200	352	32 000	320	67	672
TOTAL	**154 700**	**501**	**1 486 000**	**1 880**	**200**	**2 381**
% of TOTAL	**9.4**	**21.0**	**90.6**	**79.0**	**1 640 700**	**100**

Counterfeit Notes Processed by Bank of Jamaica
2002

Denomination $	Counterfeits detected in lodgements by BOJ		Counterfeits confiscated by financial institutions		Total Processed by BOJ	
	Value	Pieces	Value	Pieces	Value	Pieces
1 000	291 000	291	842 000	842	1 133 000	1 133
500	59 500	119	99 000	198	158 500	317
100	4 600	46	6 400	64	11 000	110
TOTAL	**355 100**	**456**	**947 400**	**1 104**	**1 302 500**	**1 560**
% of TOTAL	**27.3**	**29.2**	**72.7**	**70.8**	**100**	**100**

9. FINANCIAL LEGISLATION

9.1. The Bank of Jamaica Act

Amendments to establish the regulatory framework for remittance companies were tabled in Parliament during the last two months of 2003 and passed into law on 13 February 2004. The proposed amendments will make provisions:

(i) for persons currently carrying out, or intending to provide, money transfer and remittance services, to obtain authorization from the Minister of Finance and Planning to continue with or to commence the provision of these services;
(ii) for such persons to operate solely in accordance with the directions to be issued by the Minister of Finance and Planning through the Bank of Jamaica;
(iii) for the creation of the necessary offences and the imposition of fines and penalties for breaches of theses offences.

The proposed amendments seek to implement a regime that accords a level of supervision similar to that in place for cambios/bureaux de change. This is because money transfer and remittance agents and agencies do not take deposits and are not repositories of the savings and investments of the public. As such, the level of supervision applicable to deposit-taking institutions supervised by the Bank of Jamaica is not required.

By placing money transfer and remittance agents and agencies within a regulatory framework, Jamaica will also be addressing one of several mandates imposed on it for the fulfilling of its international obligations to combat money laundering. The Financial Action Task Force's 40 **Revised** recommendations which are applicable to cooperating states, requires states to ensure that "at a minimum, businesses providing money or value transfer or of money or currency changing, should be licensed or registered and subject to effective systems for monitoring and ensuring compliance with national requirements to combat money laundering and terrorist financing."

<u>The Banking (Licence Fees) Regulations, 2003</u>
These Regulations, which were promulgated on 5 November 2003, replace The Banking (Licence Fees) (Forms of Application) Regulations, 1973.

<u>The Financial Institutions (Licence Fees) Regulations, 2003</u>
These Regulations were promulgated on 27 February 2003 and will bring licensees under the Financial Institutions Act in line with banks and building societies in that they will now be required to make annual licence fee payments.

As at December 2003, work was proceeding in relation to the following items of legislation:

<u>The Building Societies (Licence Fees) Regulations</u>
These Regulations will be revised to bring the fees payable by building socieites in line with the applicable fees under the Licence Fees Regulations under the Banking Act and the Financial Institutions Act which were promulgated in 2003.

<u>The Banking (Capital Adequacy) Regulations and the Financial Institutions (Capital Adequacy) Regulations</u>
These regulations seek to establish a risk-based method of assessing the capital adequacy of banks and licensed financial institutions, with the requisite capital requirement being prescribed by the risk attaching to the institutions assets.

<u>The Banking (Qualification of Auditors) Regulators</u>
These regulations will create a framework for ensuring that auditors who are proposed as the statutory auditors of financial institutions are independent of the institutions being audited.

The Banking (Credit Classification and Provisioning) Regulations
These regulations relate to the measures that banks are required to take in assessing credit, taking security and making provisions for the possibility of default.

The Cooperative Societies (Amendment) Bill
This amendment to the Cooperative Socieities Act will firstly restrict the deposit-taking activities of cooperative societies to those cooperative societies which operate as credit unions. Secondly, the amendment will bring credit unions under the regulatory ambit of the Minister of Finance and the Bank of Jamaica.

The Bank of Jamaica (Credit Union) Regulations
These regulations will establish the Bank's operational jurisdiction over credit unions and make provision for matters such as licensing, capital, reserves, prohibited business, remedial and intervention processes, and the role of credit union associations.

The Bank of Jamaica (Building Societies) (Amendment) Regulations

These Regulations were previously reported as having been passed into law. However, it was subsequently realized that despite having been gazetted, these Regulations had not in fact been tabled in the Senate for approval. The legislative process in this regard will therefore need to be restarted and these Regulations resubmitted to the Parliament for approval.

These Regulations will increase the Bank of Jamaica's ability to regulate these institutions. They are intended to:

(a) incorporate some of the amendments already effected to the Banking Act and Financial Institutions Act in March 2002 including introducing a regime for building societies to pay penalties for certain breaches of the law;
(b) correct inconsistencies in the existing regulations and update fines;
(c) simplify the arrangement of the Regulations.

Related Legislative amendments being worked on as at December 2003 include the following:

The Money Laundering Act

The Money Laundering Regulations

The Money Laundering Act is being amended to incorporate requirements mandated by the Financial Action Task Force's (FATF) revised 40 Anti-money Laundering recommendations and the FATF's recommendations for Combating the Financing of Terrorism. Cabinet approved drafting instructions for revisions to the Money Laundering Act and the Regulations thereunder in October 2003. The Money Laundering Regulations are being revised to provide more specific details of the anti-money laundering practices and procedures that financial institutions are expected to have in place.

There will also be consequential amendments to the financial legislation following on the amendment of the Money laundering laws. For instance, there will be amendments to enhance the ability to share information with other Supervisory Authorities and law enforcement agents, and to allow Supervisory Authorities to take regulatory action in response to non-compliance with the money laundering laws.

The Terrorism Prevention Bill

Given recent developments in the world, Jamaica is obliged to act in concert with other nations in combating terrorism, including fully implementing United Nations and international instruments relating to terrorism. The Bill will among other things, specifically impose reporting and other procedural requirements on financial institutions to minimise or totally remove the possibility of the services of the financial sector being used in any way to facilitate the financing of terrorist activities. The Bill was tabled in Parliament during October 2003 and is currently before the Joint Select Committee of Parliament.

10. ADMINISTRATION

10.1 Overview of the Year 2003

In 2003 the Bank's management continued the process of institutional strengthening aimed at creating an organizational structure with an appropriate mix of skills, competences and experience, capable of providing the technical and administrative support, which would allow the Bank to achieve its mission critical objectives. Accordingly, during the year, the Bank recruited and trained staff consistent with the organization's strategic objectives and endeavoured to maintain a work environment that is healthy, safe and conducive to productive work.

10.2 Staffing

According to proposed legislations, which would require the Bank to supervise and regulate credit unions, as well as, money transfer and remittance agencies, the Financial Institutions Supervisory Division was assigned responsibilities to supervise credit unions; while the Financial Markets Sub-division was assigned the supervision of remittance companies and money transfer agencies. In preparation for these additional responsibilities, the Bank's establishment was increased from 475 as at 1 December 2002 to 511 during 2003.

To meet the expanded supervisory requirements and other operational objectives, the Bank recruited 34 permanent and 13 contract officers in 2003. The recruited officers included 11 persons with postgraduate qualifications and 24 with undergraduate degrees, while the remaining 12 had a combination of secretarial/administrative and clerical skills. It is to be noted that of the 47 persons recruited 27 had competences in economics, financial analysis and auditing, while 8 had specialized skills in information technology and engineering.

As at 31 December 2003, the number of incumbents totalled 472. This compared to 446 at 31 December 2002. The incumbents at the end of 2003 comprised 446 permanent employees and 26 contract officers, relative to 426 permanent employees and 20 contract officers as at the end of 2002. The staff turnover 2003 was 4.24 per cent, compared with 4.6 per cent in 2002, continuing the trend of low attrition rates experienced by the Bank in recent years.

10.3 Training & Development

During the review period, the Bank's Training Institute continued to provide targetted training interventions aimed at increasing organizational effectiveness and the efficiency of the Bank's staff. Training programmes implemented during the period emphasized the use of best practices and advances in information technology in support of the Bank's mission critical objectives. The menu of training interventions inclusive of seminars, workshops and conferences conducted during the year, covered information system management; economic modelling, analysis and forecasting; human resource management, occupational health and safety, as well as human relations skills. In addition, specialized training in electrical power generation and management and security system management was conducted during the year. The latter programmes provided technical support to the Management's initiative of ensuring the efficient and cost effective maintenance of the Bank's plant and physical infrastructure.

The Training Institute partnered with the Federal Reserve Bank of Atlanta, the Financial Stability Institute of Switzerland, the MIS Training Institute of Massachusetts and Regional Central Banks in hosting several In-Country training

programmes during the year. The programmes conducted included:

- Corporate Governance and Operational Risk Management,
- Management Assessment of Proficiency,
- Fundamentals of Enterprise Network Security and Security Audit of TCP/IP Network,
- 14th Annual Conference of Regional Central Banks' Information Systems Specialists,
- VI Conference of Central Banks Human Resource Managers,
- XXI Annual Conference of the Caribbean Group of Bank Supervisors.

In-Country training programmes which involve the use of specialist trainers, local and overseas, provide a cost effective method of delivering training to a larger number of Bank staff, other regional central bankers and practitioners in the local financial sector.

In addition to the menu of training programmes provided by the Bank's Training Institute, members of staff attended specially targetted overseas training programmes and participated in attachments at several overseas institutions, notably the International Monetary Fund, the Bank for International Settlements, the Bank of Canada and the Bundesbank. For the year 2003, 376 members of staff participated in 132 training programmes that were conducted locally and overseas.

10.4 Plant and Physical Infrastructure

In 2003 the Bank continued the phased programme of plant and infrastructure rehabilitation, which commenced in 2000. During the year, several floors were refurbished to accommodate increased staff within the Financial Institution Supervisory Division and the Financial Markets Sub-division. In addition, the Bank, being cognizant of the need for increased security to minimize risk to staff, visitors, equipment and other assets, as well as, the physical plant, upgraded the security infrastructure consistent with new and improved security technology.

Against the background of the expected Occupational Health and Safety Legislation to be implemented by the Government of Jamaica, the Bank intensified its efforts in ensuring an environmentally safe, healthy and secure workplace for staff and visitors. Accordingly, during the year the Bank installed a new chiller, which uses a non ozone-depleting refrigerant and replaced the banned Halon Fire suppressant system with environmentally friendly Inergen and FM200, which are non-ozone depleting fire suppressant systems.

10.5 Industrial and Staff Relations

During the review year, the Bank of Jamaica enjoyed a calm and productive industrial relations environment, as has been the case in recent years. Notably, the Bank's staff participated in several local sporting competitions, as well as the Regional Central Bank Games. In the latter competition held in the Bahamas, the Bank of Jamaica retained the championship trophy and also won several individual prizes for outstanding performances. The second year of the two-year Salary and Benefits Agreement between the Bank's Management and the unionized staff represented by the Bustamante Industrial Trade Union (BITU) is in effect and will expire on 31 March 2004.

11. COMPENSATION OF EXECUTIVE MANAGEMENT

Salary Range of Executive Management		**$5,370,181 - $8,321,216**
Allowances of Executive Management		
(a)	Governor	$1 440,000
(b)	Deputy Governors	$319,195

Notes

Executive Management includes the Governor and three (3) Deputy Governors. In the case of the Governor, a maintained residence and an official car are provided, as is customary for Governors of the Bank of Jamaica. For Deputy Governors a fully maintained motor vehicle is provided. Each member of the Executive Management is eligible for benefits including a non-contributory pension plan, health insurance, life insurance, and staff loans.

12. CALENDAR OF MONETARY POLICY DEVELOPMENTS

10/01/03 The Bank of Jamaica instituted a "Special Deposit" requirement for Commercial Banks and institutions licensed under the Financial Institutions Act. Each institution was required to place cash deposits with the Central Bank equivalent to 5% of its Jamaican Dollar prescribed liabilities.

10/02/03 The Bank of Jamaica introduced a special five-month open market instrument, which earned interest at 30% per annum. This instrument was introduced in a context of significant Jamaica dollar liquidity and protracted instability in the foreign exchange market.

14/02/03 The Bank of Jamaica withdrew the special five- month open market instrument, which was introduced on 10 February 2003. The decision to remove this instrument came against the background of tight Jamaica dollar liquidity and the appreciation in the exchange rate over the previous four days. The removal was also in response to representations made to the Bank of Jamaica by financial institutions and understandings reached with respect to the development of foreign exchange market protocols.

19/03/03 Interest rates on Bank of Jamaica's 180-day, 270-day and 365-day open market instruments were increased to 19.65 per cent, 21.50 per cent and 24.0 per cent, respectively.

26/03/03 Interest rates on Bank of Jamaica 30-day, 60-day, 90-day, 120-day, 180-day, 270-day and 365-day open market instruments were increased to 15.00 per cent, 15.30 per cent, 20.00 per cent, 24.00 per cent, 33.15 per cent, 34.50 per cent and 35.95 per cent, respectively.

25/04/03 Interest rates on Bank of Jamaica 180-day, 270-day and 365-day open market instruments were reduced to 28.00 per cent, 32.50 per cent and 33.00 per cent, respectively.

19/05/03 The interest rate applicable to overdrafts on accounts held with the Bank of Jamaica was increased to 65.0 per cent per annum.

24/06/03 Interest rates on Bank of Jamaica 180-day, 270-day and 365-day open market instruments were reduced to 26.50 per cent, 29.50 per cent and 30.00 per cent, respectively.

08/07/03 Interest rates on Bank of Jamaica 270-day and 365-day open market instruments were reduced to 27.50 per cent and 28.00 per cent, respectively.

04/08/03 Interest rates on Bank of Jamaica 90-day, 120-day, 180-day, 270-day and 365-day open market instruments were reduced to 18.00 per cent, 22.00 per cent, 25.00 per cent, 25.75 per cent and 26.00 per cent, respectively.

09/09/03	Interest rates on Bank of Jamaica 120-day, 180-day, 270-day and 365-day open market instruments were reduced to 21.00 per cent, 23.50 per cent, 23.75 per cent and 24.00 per cent, respectively.
17/10/03	Bank of Jamaica withdrew its 270-day and 365-day instruments from open market trading.
29/10/03	Bank of Jamaica returned its 270-day and 365-day instruments to open market trading at 23.75 per cent and 24.00 per cent respectively.
10/12/03	Interest rates on Bank of Jamaica 90-day 120-day, 180-day, 270-day and 365-day open market instruments were reduced to 17.00 per cent, 20.00 per cent, 21.00 per cent, 22.00 per cent and 23.00 per cent, respectively.

AUDITORS' REPORT

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Chartered Accountants

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TO BANK OF JAMAICA

Auditors' Report

Pursuant to Section 43(1) of the Bank of Jamaica Act, we have audited the financial statements, set out on pages ii to xxix, and have obtained all the information and explanations which we required. The financial statements are the responsibility of the Bank's management. Our responsibility is to express an opinion on the financial statements based on our audit.

We conducted our audit in accordance with International Standards on Auditing. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatements. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall presentation of the financial statements. We believe that our audit provides a reasonable basis for our opinion.

In our opinion, proper accounting records have been kept and the financial statements, which are in agreement therewith and have been prepared in accordance with International Financial Reporting Standards, give a true and fair view of the state of affairs of the Bank as at December 31, 2003, and of its results of operations and cash flows for the year then ended and comply with the provisions of the Bank of Jamaica Act.

KPMG Peat Marwick

March 24, 2004

Balance Sheet
December 31, 2003

	Notes	2003 J$'000	2002* J$'000
ASSETS			
Foreign assets			
Notes and coins		22,013	7,821
Cash resources	3	9,221,708	8,030,773
Interest in funds managed by agents		2,533,834	2,066,358
Investments	4	60,099,207	72,147,227
International Monetary Fund - Holding of Special Drawing Rights		3,198	39,917
		71,879,960	82,292,096
Local assets			
Notes and coins		44,374	36,429
Investments	5	78,308,002	59,512,481
International Monetary Fund - Quota Subscription	6	2,454,750	1,886,832
Investment property	7	87,000	108,500
Investments in financial institutions	8	3,210	3,210
Due from Government and Government Agencies	9	4,563,331	5,868,513
Property, plant and equipment	10	1,629,927	1,384,709
Employee benefits	11	837,200	763,300
Other	12	1,447,268	1,430,393
		89,375,062	70,994,367
		161,255,022	153,286,463

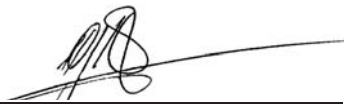
*Restated (see note 26)
The accompanying notes form an integral part of the financial statements.

Balance Sheet (cont'd)
December 31, 2003

	Notes	2003 J$'000	2002* J$'000
LIABILITIES, CAPITAL AND RESERVES			
Liabilities			
Notes and coins in circulation	13	29,424,600	24,364,753
Deposits and other demand liabilities	14	55,602,295	70,498,753
Securities sold under repurchase agreements	15	56,705,566	47,732,400
International Monetary Fund - Allocation of Special Drawing Rights	16	3,203,044	2,462,006
Foreign liabilities	17	332,588	304,174
Employee obligations	11	474,400	443,200
Other	18	13,112,117	5,181,307
		158,854,610	150,986,593
Capital and reserves			
Share capital	19	4,000	4,000
General reserve fund	20	20,000	-
Special stabilisation account	21	329,600	287,244
Other reserves	22	2,046,812	2,008,626
		2,400,412	2,299,870
		161,255,022	153,286,463

The financial statements on pages 2 to 29 were approved by the Board of Directors on March 24, 2004 and signed on its behalf by:


Governor
Derick Milton Latibeaudiere


Acting Division Chief, Finance and Technology
Herbert A. Hylton


Director, Accounting Services Department
Angela E. Foote

*Restated (see note 26)
The accompanying notes form an integral part of the financial statements.

Statement of Income and Expenses
Year ended December 31, 2003

	Notes	2003 J$'000	2002* J$'000
Operating income			
Interest		18,508,389	11,822,369
Foreign exchange gain, net	23	11,415,229	4,960,555
Other		110,637	24,822
Total		30,034,255	16,807,746
Operating expenses			
Interest		21,635,766	15,929,735
Salaries, pension scheme contributions, and staff and post retirement benefits	24	895,245	709,745
Currency expenses		290,858	282,522
Property expenses, including depreciation		223,916	242,975
Other operating expenses		290,509	258,976
Total	25	23,336,294	17,423,953
Net operating profit/(loss)		6,697,961	(616,207)
Other gains/(losses)			
Bad debts, net		(1,269)	(5,196)
Gain/(loss) on remeasurement of staff loans and promissory note		106,157	(36,049)
Loss on revaluation of securities		(363,923)	(33,401)
Gain on disposal of fixed assets		583	1,805
Gain on disposal of investment property		6,458	-
Change in value of investment property		8,724	2,332
Expenditure on behalf of Government of Jamaica not reimbursed	9	(89,181)	(163,237)
Net profit/(loss) for the year		6,365,510	(849,953)
Transferred to pension equalisation reserve	22(c)	(73,900)	(122,500)
Transferred to general reserve fund		(6,291,610)	(972,453)

*Restated (see note 26)
The accompanying notes form an integral part of the financial statements.

Statement of Changes in Equity
Year ended December 31, 2003

	Share capital J$'000 (Note 19)	General reserve fund J$'000 (Note 20)	Special stabilisation account J$'000 (Note 21)	Other reserves J$'000 (Note 22)	Total J$'000
Balances at December 31, 2001: As previously reported using Jamaica GAAP	4,000	20,000	264,690	931,154	1,219,844
Effect of first-time adoption of International Financial Reporting Standards (IFRS) [note 26(a)]	-	(488,687)	-	643,719	155,032
Net loss due from consolidated fund	-	488,687	-	-	488,687
Balances at December 31, 2001 as restated using IFRS	4,000	20,000	264,690	1,574,873	1,863,563
Restated net loss for the year [note 26(b)]	-	(849,953)	-	-	(849,953)*
IAS 16 – Property, plant and equipment	-	-	-	126,012	126,012*
IAS 19 – Employee benefits	-	-	-	122,500	122,500*
IAS 39 – Financial instruments – Recognition and measurement	-	-	-	185,241	185,241*
Transfer from coins in circulation	-	-	22,554	-	22,554*
Restated net loss due from consolidated fund	-	829,953	-	-	829,953
Restated balances at December 31, 2002	4,000	-	287,244	2,008,626	2,299,870
Net profit for the year	-	6,291,610	-		6,291,610*
IAS 16 – Property, plant and equipment	-	-	-	154,313	154,313*
IAS 19 – Employee benefits	-	-	-	73,900	73,900*
IAS 39 – Financial instruments – Recognition and measurement	-	-	-	(190,027)	(190,027)*
Transfer from coins in circulation	-	-	42,356	-	42,356*
Net profit due to consolidated fund (note 9)	-	(6,271,610)	-	-	(6,271,610)
Balances at December 31, 2003	4,000	20,000	329,600	2,046,812	2,400,412

* Total recognised gains J$6,372,152,000 (2002: loss J$393,646,000).
The accompanying notes form an integral part of the financial statements.

Statement of Cash Flows
Year ended December 31, 2003

	2003 J$'000	2002 J$'000
Cash provided by operating activities:		
Net profit/(loss) for the year	6,365,510	(849,953)
Adjustments to reconcile net profit/(loss) for the year to net cash provided/(used) by operating activities:		
Depreciation	84,063	117,907
Gain on disposal of property, plant and equipment	(583)	(1,805)
Gain on disposal of investment property	(6,458)	-
Unrealised exchange gain on overseas securities	(524,429)	188,391
Employee benefits, net	(42,700)	(90,200)
Change in fair value of investment property	(8,724)	(2,332)
Transfer from coins in circulation	42,356	22,554
Unrealised exchange gain on International Monetary Fund - Quota subscription	(567,918)	(88,125)
Unrealised exchange loss on International Monetary Fund - Allocation of SDR's	741,038	114,990
Net cash provided/(used) by operating activities	6,082,155	(466,073)
Cash flows from investing activities:		
International Monetary Fund - Holding of Special Drawing Rights	36,719	28,978
Interest in funds managed by agents	(467,476)	(215,981)
Foreign currency denominated investments	12,048,020	642,133
Local currency denominated investments	(18,461,119)	(12,487,524)
Proceeds of disposal of investment property	36,958	-
Due from Government and Government Agencies	(4,966,428)	4,049,545
Additions to property, plant and equipment	(175,792)	(109,847)
Additions to investment property	(276)	(10,668)
Repayment of investment in promissory notes	-	150
Proceeds of disposal of property, plant and equipment	1,407	2,570
Other assets	(16,875)	2,563,617
Net cash used by investing activities	(11,964,862)	(5,537,027)
Cash flows from financing activities:		
Notes and coins in circulation	5,059,847	1,996,963
Deposits and other demand liabilities	(14,896,458)	(11,879,600)
Securities sold under repurchase agreements	8,973,166	9,286,147
Foreign liabilities	28,414	12,453
Other liabilities	7,930,810	(398,352)
Net cash provided/(used) by financing activities	7,095,779	(982,389)
Net increase/(decrease) in cash resources	1,213,072	(6,985,489)
Cash resources at beginning of year	8,075,023	15,060,512
Cash resources at end of year	9,288,095	8,075,023
Cash resources at end of year comprise:		
Foreign notes and coins	22,013	7,821
Foreign currency cash resources	9,221,708	8,030,773
Local notes and coins	44,374	36,429
	9,288,095	8,075,023

The accompanying notes form an integral part of the financial statements.

Notes to the Financial Statements
December 31, 2003

1. Identification

Bank of Jamaica (hereafter "the Bank") was established under the Bank of Jamaica Act (hereafter "the Act"). The Act was most recently amended effective December 23, 2003 [see note 2(f)].

The principal objects of the Bank, as set out in the Act, are to issue and redeem notes and coins; to keep and administer the external reserves of Jamaica; to influence the volume and conditions of supply of credit so as to promote the fullest expansion in production, trade and employment, consistent with the maintenance of monetary stability in Jamaica and the external value of the currency; to foster the development of money and capital markets in Jamaica; and to act as banker to the Government of Jamaica.

2. Basis of preparation and significant accounting policies

(a) Basis of preparation:

Jamaica adopted International Financial Reporting Standards (IFRS) effective July 1, 2002. Consequently, there have been significant changes in the accounting policies followed in these financial statements compared with those used in previous years. As a result, the comparative figures have been restated to conform with the provisions of IFRS.

The financial statements have been prepared in accordance with the provisions of the Bank of Jamaica Act, International Financial Reporting Standards (IFRS) adopted by the International Accounting Standards Board (IASB), interpretations issued by the International Financial Reporting Interpretations Committee of the IASB and practice statements issued by the Institute of Chartered Accountants of Jamaica.

IFRS 1, *First-time adoption of IFRS*, has been applied before its effective date of January 1, 2004 in the preparation of the Bank's financial statements. An explanation of the effects of adopting IFRS on the equity, results of operations and financial position is provided in note 26.

The preparation of the financial statements in accordance with IFRS requires management to make estimates and assumptions that affect the reported amount of assets, liabilities, contingent assets and contingent liabilities at the balance sheet date and the income and expenses for the year then ended. Actual amounts could differ from these estimates.

The financial statements are presented in Jamaica dollars and are prepared under the historical cost convention, except for the inclusion of available-for-sale investments, investment property and certain classes of property, plant and equipment at fair value.

(b) Foreign currencies:

The rate of exchange of the Jamaica dollar for the United States dollar is determined by the average of the weighted average rate at which the commercial banks trade in US dollars and the rate at which the Bank itself buys US dollars. The rates of exchange for other currencies are derived from the US$ rate, thus determined, using rates published by the Federal Reserve Bank and the Financial Times.

Foreign currency balances at the balance sheet date are translated at the rates of exchange prevailing at that date. Transactions in foreign currencies are converted at the rates of exchange ruling at the dates of those transactions.

Notes to the Financial Statements (cont'd)
December 31, 2003

2. Basis of preparation and significant accounting policies (cont'd)

(b) Foreign currencies (cont'd):

Gains and losses arising from fluctuations in exchange rates are included in the statement of income and expenses.

(c) Financial instruments:

(i) Classification of investments:

Management determines the classification of investments at the time of purchase and takes account of the purpose for which the investments were purchased. Investments are classified as originated loans and receivables and available-for-sale.

Originated loans and receivables are created by the Bank by providing money to a debtor other than those created with the intention of short-term profit taking. Originated loans and receivables are recognised on the day they are transferred to the Bank.

Available-for-sale instruments are those that are not held for trading purposes, or originated by the Bank. Available-for-sale instruments are recognised on the date the Bank commits to purchase the instruments. From this date, any gains and losses arising from changes in fair value of the instruments are recognised in equity.

(ii) Measurement:

Financial instruments are measured initially at cost, including transaction costs.

Subsequent to initial recognition, all available-for-sale investments are measured at fair value, except that any instrument that does not have a quoted market price in an active market and whose fair value cannot be reliably determined, is stated at cost, including transaction costs, less impairment losses.

All non-trading financial liabilities and originated loans and receivables are measured at amortised cost, less impairment losses. Amortised cost is calculated on the effective interest rate method. Premiums and discounts, including initial transaction costs, are included in the carrying amount of the related instrument and amortised based on the effective interest rate of the instrument.

Based on the above guidelines, the Bank's investments are measured as follows:

[i] Loans are classified as originated loans and receivables and are stated at cost (amortised cost), less provision for losses and impairment as appropriate.

[ii] Government of Jamaica securities purchased on the primary market and interest-bearing deposits are stated at historical or amortised cost.

[iii] Government of Jamaica securities purchased on the secondary market are classified as available-for-sale and measured at fair value.

Notes to the Financial Statements (cont'd)
December 31, 2003

2. Basis of preparation and significant accounting policies (cont'd)

(c) Financial instruments (cont'd):

(ii) Measurement (cont'd):

[iv] US Government bonds purchased on the primary market are classified as originated loans and those purchased on the secondary market are classified as available-for-sale. US Government bonds are measured at amortised cost for originated loans and fair value for available-for-sale securities.

[v] Securities sold under repurchase agreements:

A repurchase agreement ("Repo") is a short-term transaction whereby securities are sold with simultaneous agreements for repurchasing the securities on a specified date and at a specified price. Repos are accounted for as short-term collateralised borrowing and are carried at cost.

The difference between the sale and repurchase considerations is recognised on an accrual basis over the period of the agreements, using the effective yield method, and is included in interest.

[vi] Investments in financial institutions:

Investments in financial institutions are stated at cost less provision for losses. A provision for loss is made where, in the opinion of the directors, there has been a permanent impairment in the value of an investment. Consolidated financial statements are not prepared because the directors are of the view that, at this time, the cost is out of proportion to the benefit to be derived having regard to, *inter alia*, the nature of the activities of the investees. The only remaining subsidiary is in voluntary liquidation (see note 8).

(iii) Fair value measurement principles:

The fair value of financial instruments classified as available-for-sale is based on their quoted market price at the balance sheet date without any deduction for transaction costs. Where a quoted market price is not available, the fair value of the instrument is estimated using pricing models or discounted cash flow techniques or a generally accepted alternative method.

Where discounted cash flow techniques are used, estimated future cash flows are based on management's best estimates and the discount rate is a market related rate at the balance sheet date for an instrument with similar terms and conditions. Where pricing models are used, inputs are based on market related measures at the balance sheet date.

(iv) Gains and losses on subsequent measurement:

Gains and losses arising from a change in the fair value of available-for-sale assets are recognised directly in equity. When the financial assets are sold, collected or otherwise disposed of, the cumulative gain or loss recognised in equity is transferred to the statement of income and expenses.

Notes to the Financial Statements (cont'd)
December 31, 2003

2. Basis of preparation and significant accounting policies (cont'd)

(c) Financial instruments (cont'd):

(v) Cash resources:

Cash resources, including short-term deposits with maturities ranging between three and twelve months from balance sheet date, are shown at cost.

(vi) Other assets:

These are stated at their cost, less impairment losses.

(vii) Other liabilities:

Other liabilities, including provisions, are stated at their cost. A provision is recognised in the balance sheet when the Bank has a legal or constructive obligation as a result of a past event, it is probable that an outflow of economic benefits will be required to settle the obligation, and a reliable estimate of the amount can be made. If the effect is material, provisions are determined by discounting the expected future cash flows at a rate that reflects current market assessments of the time value of money and, where appropriate, the risks specific to the liability.

(viii) Derecognition:

A financial asset is derecognised when the Bank loses control over the contractual rights that comprise that asset. This occurs when the rights are realised, expired or are surrendered. A financial liability is derecognised when it is extinguished.

Available-for-sale assets that are sold are derecognised and corresponding receivables from the buyer for the payment are recognised as of the date the Bank commits to sell the assets.

Originated loans and receivables are derecognised on the day they are transferred by the Bank.

(d) Property, plant and equipment:

(i) Items of property, plant and equipment are stated at cost less accumulated depreciation and impairment losses, except for freehold land and buildings which are stated at market value.

(ii) Property, plant and equipment are depreciated on the straight-line method at annual rates estimated to write off the assets over their estimated useful lives. Leasehold property is amortised in equal instalments over the shorter of the lease term and the property's estimated useful life. Land, works of art, statues and museum coins are not depreciated. The depreciation rates are as follows:

Buildings	5% and 10%
Leasehold property	Shorter of lease term and useful life
Furniture, plant and equipment	10%
Computer and software	20%
Motor vehicles	20%

Notes to the Financial Statements (cont'd)
December 31, 2003

2. Basis of preparation and significant accounting policies (cont'd)

(e) Notes and coins in circulation:

The nominal value of numismatic coins sold is included in notes and coins in circulation. The net proceeds from such sales are included in the statement of income and expenses.

Notes and coins in circulation is stated after a deduction of 25% of the value of coins in circulation in accordance with the Bank of Jamaica (Value of Coins in Circulation) Order 1973, as permitted under Section 22 of the Act. The deductions are credited to the special stabilisation account.

(f) Taxation:

Section 46 of the Act, which exempted the Bank from income tax, stamp duties and transfer tax, was repealed on December 23, 2003 (see note 1). The Bank is still exempt from income tax under Section 12(b) of the Income Tax Act. The Bank's supplies are substantially exempt from general consumption tax (GCT); it incurs GCT at standard rates on taxable supplies acquired.

(g) Employee benefits:

Employee benefits are all forms of consideration given by the Bank in exchange for service rendered by employees. These include current or short-term benefits such as salaries, NIS contributions, annual leave, and non-monetary benefits such as medical care and housing; post-employments benefits such as pensions and medical care; other long-term employee benefits such as termination benefits.

Employee benefits that are earned as a result of past or current service are recognised in the following manner: Short-term employee benefits are recognised as a liability, net of payments made, and charged as expense. The expected cost of vacation leave that accumulates is recognised when the employee becomes entitled to the leave. Post employment benefits are accounted for as described below.

Employee benefits comprising pensions and other post-employment assets and obligations included in these financial statements have been actuarially determined by a qualified independent actuary, appointed by management. The appointed actuary's report outlines the scope of the valuation and the actuary's opinion. The actuarial valuations were conducted in accordance with IAS 19, and the financial statements reflect the Bank's post-employment benefit asset and obligations as computed by the actuary. In carrying out their audit, the auditors relied on the actuary's report.

The cost of employee benefits is the cost to the Bank of its administration of, and contributions to, the pension scheme established to provide retirement benefits, and its payments to pensioners to supplement the basic pensions to which pensioners are entitled under the rules of the scheme (see note 11). The contributions are a percentage of the members' salaries; the percentage is determined by the scheme's actuaries using the *aggregate actuarial cost* method. The contributions are charged to income as they fall due; administration costs are charged when incurred; and supplemental payments are charged when paid.

The Bank's net obligation in respect of the defined benefit pension plan is calculated by estimating the amount of future benefits that employees have earned in return for their service in the current and prior periods; that value is discounted to determine the present value, and the fair value of any plan assets is deducted. The discount rate is determined by reference to the yield at the balance sheet date on long-term government bonds with maturities approximating the terms of the Bank's obligation. The calculation is performed by a qualified actuary, using *the projected unit credit method*.

Notes to the Financial Statements (cont'd)
December 31, 2003

2. Basis of preparation and significant accounting policies (cont'd)

(g) Employee benefits (cont'd):

When the benefits of the plan are improved, the portion of the increased benefit relating to past service by employees is recognised as an expense in the statement of income and expenses on a straight-line basis over the average period until the benefits become vested. To the extent that the benefits are vested immediately, the expense is recognised immediately in the statement of income and expenses.

All actuarial gains and losses as at January 1, 2002, the date of transition to IFRS, were recognised. In respect of actuarial gains and losses that arise subsequent to January 1, 2002 in calculating the Bank's obligation in respect of the plan, to the extent that any cumulative unrecognised actuarial gain or loss exceeds ten percent of the greater of the present value of the defined benefits obligation and the fair value of plan assets, that portion is recognised in the statement of income and expenses over the expected average remaining working lives of the employees participating in the plan. Otherwise, the actuarial gain or loss is not recognised.

Where the calculation results in a benefit to the Bank, the recognised asset is limited to the net total of any unrecognised actuarial losses and past service costs and the present value of any future refunds from the plan or reductions in future contributions to the plan.

(h) Statutory transfer of profits and losses:

Section 9 of the Act provides for each financial year's net income to be credited, or net loss charged, to the General Reserve Fund, and for the balance on the General Reserve Fund in excess of five times the Bank's authorised share capital to be transferred to the Consolidated Fund. Likewise, any losses not covered by reserves are required by the Act to be funded by Government out of the Consolidated Fund.

(i) Investment property:

Investment property is stated at fair value determined annually by an independent registered valuer. Fair value is based on current prices in an active market for similar properties in the same location and condition. Any gain or loss arising from a change in fair value is recognised in the statement of income and expenses. In carrying out their audit, the auditors relied on the valuators' report.

3. Cash resources

	2003 J$'000	2002 J$'000
Current accounts and money at call with foreign banks	9,024,572	7,831,276
Current accounts with local banks	197,136	199,497
	9,221,708	8,030,773

4. Foreign currency denominated investments

	2003 J$'000	2002 J$'000
Originated securities:		
US Government bonds	20,107,054	22,616,496
Available-for-sale securities:		
US Government bonds	6,663,425	7,553,888
Barbados Government bond	36,631	29,557
	26,807,110	30,199,941
Short-term deposits with foreign banks	33,292,097	41,947,286
	60,099,207	72,147,227

Notes to the Financial Statements (cont'd)
December 31, 2003

5. Local currency denominated investments

	2003 J$'000	2002 J$'000
Originated securities:		
Jamaica Government Securities:		
Local registered stock	60,060,232	53,467,012
Bonds	5,038,547	-
Debentures	10,619,264	3,748,381
	75,718,043	57,215,393
Available-for-sale securities:		
Jamaica Government Securities:		
Local registered stock	2,202,536	2,296,562
Treasury bills	227	526
Bonds	14,634	-
Debentures	372,562	-
	2,589,959	2,297,088
	78,308,002	59,512,481

6. International Monetary Fund – Quota Subscription

This represents the portion of Jamaica's fee for membership of the International Monetary Fund (IMF), based on its quota, which was paid by the Bank (the other portion having been subscribed by the Government of Jamaica).

Quotas are reviewed every five years, when adjustments may be considered.

	SDR'000	2003 J$'000	2002 J$'000
Amount subscribed (net of reserve tranche of J$Nil):			
At beginning of year	31,125	1,886,832	1,798,707
Effect of exchange rate fluctuation	-	567,918	88,125
At end of year	31,125	2,454,750	1,886,832

7. Investment property

	2003 J$'000	2002 J$'000
Balance at beginning of year	108,500	95,500
Additions	276	10,668
Disposals	(30,500)	-
Increase in fair value	8,724	2,332
Balance at end of year	87,000	108,500

Notes to the Financial Statements (cont'd)
December 31, 2003

8. Investments in financial institutions

	2003 J$'000	2002 J$'000	Equity holding %	Latest audited financial statements	Retained earnings/ (deficit) J$'000
Subsidiary company:					
Jamaica Export Credit Insurance Corporation Ltd. (in voluntary liquidation)	3,200	3,200	100.00	31.12.96	45,106
Other:					
Development Bank of Jamaica Limited	10	10	17.35	31.03.97	(263,614)
	3,210	3,210			

By virtue of Section 23(j) of the Act, the Bank is empowered to, with the approval of the Minister, subscribe to, hold and sell shares in any corporation which, with the approval, or under the authority, of the Government, is established for the purpose of promoting the development of a money market or securities market in Jamaica or of improving the financial machinery for the financing of economic development.

9. Due from Government and Government Agencies

	Dec. 31, 2002 J$'000	Movements during the year: Advances/ Losses J$'000	Profit/ Settlements J$'000	Charged to expenses J$'000	Dec. 31, 2003 J$'000
Expenditure on behalf of Government:					
Payment of exchange losses and interest on foreign liabilities [see (b) below]	-	89,181	-	(89,181)	-
Other expenditure on behalf of Government		1,690	-	-	1,690
Withholding tax refund due	-	1,120,411	-	-	1,120,411
Accrued interest on Government securities	4,000,183	8,653,363	(4,000,183)	-	8,653,363
Overdrafts – Government and Government Agencies	-	133,735	-	-	133,735
Net loss payable to Consolidated Fund as previously reported under JGAAP	942,357	-	(942,357)	-	-
IFRS adjustments	925,973	-	(231)	-	925,742
Net profit payable to Consolidated Fund	-	-	(6,271,610)	-	(6,271,610)
	5,868,513	9,998,380	(11,214,381)	(89,181)	4,563,331

(a) By virtue of Section 36 of the Act, the Bank is empowered to make advances to the Government up to thirty percent of the estimated revenue of Jamaica for that financial year of the Government, which are to be repaid within three months after the financial year. Where advances are not duly repaid, the power of the Bank to grant further advances in any subsequent financial year is not exercisable until the outstanding advances are repaid.

Advances made to the Government during the Bank's financial year ended December 31, 2003 amounted to $Nil (2002: $Nil) which was Nil% (2002: Nil%) of the estimated revenue of Jamaica for the year of J$134 billion (2002: J$108 billion).

Notes to the Financial Statements (cont'd)
December 31, 2003

9. Due from Government and Government Agencies (cont'd)

(b) Exchange losses paid and interest on foreign liabilities comprise:

(i) advances to cover exchange losses realised on repayment of Government of Jamaica foreign liabilities, and

(ii) interest paid on Government of Jamaica foreign liabilities.

(c) Government is required by the Act to pay to the Bank, out of the Consolidated Fund, the losses incurred by the Bank. Section 9 (3) provides that if, in the opinion of the Minister, a payment to the Bank to clear the losses cannot be made from the Consolidated Fund, then such losses may be cleared by the issue to the Bank of securities charged to the Consolidated Fund.

10. Property, plant and equipment

	Freehold land and buildings J$'000	Leasehold property J$'000	Furniture, plant and equipment J$'000	Motor vehicles J$'000	Work-in-progress J$'000	Total J$'000
At cost or valuation:						
December 31, 2002	1,032,300	1,208	619,436	75,924	23,809	1,752,677
Additions	47,387	-	63,628	28,577	36,200	175,792
Revaluation	154,313	-	-	-	-	154,313
Transfers	-	-	23,809	-	(23,809)	-
Disposals/write-offs	-	-	-	(4,588)	-	(4,588)
December 31, 2003	1,234,000	1,208	706,873	99,913	36,200	2,078,194
At cost	-	1,208	706,873	99,913	36,200	844,194
At valuation	1,234,000	-	-	-	-	1,234,000
	1,234,000	1,208	706,873	99,913	36,200	2,078,194
Depreciation:						
December 31, 2002	-	669	346,631	20,668	-	367,968
Charge for the year	-	115	66,999	16,949	-	84,063
Eliminated on disposals/write-offs	-	-	-	(3,764)	-	(3,764)
December 31, 2003	-	784	413,630	33,853	-	448,267
Net book values:						
December 31, 2003	1,234,000	424	293,243	66,060	36,200	1,629,927
December 31, 2002	1,032,300	539	272,805	55,256	23,809	1,384,709

The Bank's land and buildings were revalued in 2002 and 2003 by The C. D. Alexander Company Realty Limited, Real Estate Broker, Appraiser and Auctioneer on the open-market, existing-use basis. The surplus arising on revaluation, inclusive of depreciation no longer required, is included in property revaluation reserve (note 22).

11. Employee benefits

The Bank operates a non-contributory defined benefit pension scheme, and medical and life insurance schemes for all its permanent eligible employees and funds retirement benefits, except as set out at (e) below. Benefits under the pension scheme are computed by reference to final salary. The assets of the scheme, which are held separately from those of the Bank, are under the control of a board of trustees, with day-to-day management by employees of the Bank.

Notes to the Financial Statements (cont'd)
December 31, 2003

11. Employee benefits (cont'd)

(a) Employee benefits asset/obligation:

	Asset		Obligation	
	2003 J$'000	2002 J$'000	2003 J$'000	2002 J$'000
Present value of funded obligations	1,133,400	1,057,800	-	-
Present value of unfunded pension obligations, medical and life insurance	-	-	652,200	458,500
Fair value of plan assets	(3,710,400)	(3,063,700)	-	-
Unrecognised actuarial losses/(gains)	531,500	122,200	(177,800)	(15,300)
Unrecognised assets due to limitation	1,208,300	1,120,400	-	-
Net (asset)/obligation at end of year	(837,200)	(763,300)	474,400	443,200

(b) Movements in the net (asset)/obligation recognised in the balance sheet:

	Asset		Obligation	
	2003 J$'000	2002 J$'000	2003 J$'000	2002 J$'000
Net (assets)/obligations at January 1	(763,300)	(640,800)	443,200	410,900
Contributions	(21,300)	(21,800)	(35,500)	(26,700)
(Credit)/expense recognised in the statement of income and expenses	(52,600)	(100,700)	66,700	59,000
Net (assets)/obligations at end of year	(837,200)	(763,300)	474,400	443,200

(c) Expense recognised in the statement of income and expenses:

	Asset		Obligation	
	2003 J$'000	2002 J$'000	2003 J$'000	2002 J$'000
Current service costs	35,100	29,500	11,700	9,200
Interest on obligation	130,400	110,700	55,000	49,800
Expected return on plan assets	(306,000)	(263,500)	-	-
Change in disallowed assets	87,900	22,600	-	-
Total included in staff costs	(52,600)	(100,700)	66,700	59,000
Actual return on plan assets	17.65%	14.06%	-	-

(d) Principal actuarial assumptions at the balance sheet date (expressed as weighted averages)

	2003 %	2002 %
Discount rate at January 1	12.5	12.5
Expected return on plan assets at January 1	10.0	10.0
Future salary increases	8.0	8.0
Future pension increases	0.0	0.0
Medical claims growth	12.5	11.0

(e) The Bank granted increases to pensioners as a supplement to the pensions paid by the scheme. An actuarial valuation disclosed that for the scheme to take over these supplemental payments currently being paid by the Bank, in addition to increases proposed with effect from December 31, 2001, a special contribution of J$168,700,000 would be required from the Bank as of the valuation date. No provision for this lump sum amount is included in the financial statements, as the scheme is already overfunded.

Notes to the Financial Statements (cont'd)
December 31, 2003

11. Employee benefits (cont'd)

(e) (cont'd)

In addition, the Bank granted a further supplement to pensioners: these supplemental pension payments amounted to J$30,613,059 for the year (2002: J$26,398,260), all of which have been included in staff costs in the statement of income and expenses.

12. Other assets

	2003 J$'000	2002 J$'000
Items in process of collection	20,203	10,658
Overdrafts	13,584	7,504
Staff and ex-staff loans, including interest receivable	765,728	711,374
Stock of unissued notes and coins	496,465	466,352
Accrued interest receivable other than on GOJ securities	372,558	489,910
Promissory notes	109,217	121,207
Other	26,137	20,661
	1,803,892	1,827,666
Less: provision for losses	(356,624)	(397,273)
	1,447,268	1,430,393

13. Notes and coins in circulation

	2003 J$'000	2002 J$'000
Notes	28,435,801	23,503,021
Coins	988,799	861,732
	29,424,600	24,364,753

Section 21 of the Act requires the Bank to hold assets of an amount in value sufficient to cover the value of the total amount of notes and coins in circulation as defined in that section. The assets held shall include, *inter alia*, (a) gold; (b) "hard currency" cash, bank balances or securities issued by a foreign government or international financial institution of which Jamaica is a member; or (c) Special Drawing Rights. Specified assets held by the Bank, as at December 31, 2003, were 2.44 (2002: 3.38) times the value of notes and coins in circulation at that date.

14. Deposits and other demand liabilities

	2003 J$'000	2002 J$'000
Government and Government agencies	2,530,657	5,031,889
Commercial banks and specified financial institutions	28,525,936	19,904,820
International Money Fund	58,828	58,828
Certificates of deposit	22,397,787	40,168,140
Others	2,089,087	5,335,076
	55,602,295	70,498,753
Jamaica dollar equivalent of foreign currency deposits	9,063,798	9,167,084
Jamaica dollar deposits	46,538,497	61,331,669
	55,602,295	70,498,753

Notes to the Financial Statements (cont'd)
December 31, 2003

14. Deposits and other demand liabilities (cont'd)

Deposit liabilities of the Bank include cash reserves held in connection with the Bank's supervision of the prudential requirements of commercial banks and specified financial institutions under the provisions of section 28 of the Act, section 14 of the Banking Act and section 14 of the Financial Institutions Act.

In relation to its management of liquidity in the financial system, the Bank may, under section 28A of the Bank of Jamaica Act, require commercial banks and specified financial institutions to make special deposits with it in the form of cash or specified securities. Cash so deposited is also included in deposit liabilities of the Bank; securities so deposited are, however, excluded from the Bank's liabilities, as title is not transferred and the Bank merely holds them in safekeeping.

At the balance sheet date, the following obtained:

	2003 J$'000	2002 J$'000
Amounts included in deposit liabilities of the Bank, representing statutory reserves	25,488,221	17,165,653

15. Securities sold under repurchase agreements

As part of the process of controlling liquidity in the financial system, the Bank acquires funds from or makes funds available to financial institutions and this is effected by entering into short-term agreements with the institutions. The Bank, on taking delivery of the funds, delivers certificates evidencing transfer of interest in securities and agrees to repurchase them on a specified date and at a specified price ('repos'). When the Bank makes funds available, it receives securities and agrees to resell them on a specified date at a specified price ('reverse repos').

At the balance sheet date, certificates evidencing temporary transfer of interest in the following securities were delivered as repos:

	2003 J$'000	2002 J$'000
Jamaica Government Securities:		
Local registered stocks	51,674,103	45,973,554
Investment debentures	1,278,298	1,758,846
Investment bonds	3,753,165	-
	56,705,566	47,732,400

16. International Monetary Fund - Allocation of Special Drawing Rights

This represents the Bank's obligation for Special Drawing Rights (SDRs) allocated to it. This allocation does not change unless there are cancellations or further allocations. There have been no further allocations or cancellations during the year (2002: Nil) and, accordingly, the changes arise from exchange rate fluctuations.

	SDRs'000	2003 J$'000	2002 J$'000
At beginning of year	40,613	2,462,006	2,347,016
Effect of exchange rate fluctuation	-	741,038	114,990
At end of year	40,613	3,203,044	2,462,006

Notes to the Financial Statements (cont'd)
December 31, 2003

17. Foreign liabilities

	2003 J$'000	2002 J$'000
Borrowings - Principal	310,536	284,839
- Accrued interest	5,229	4,570
Unsettled balances on bilateral accounts for Caricom trade	16,823	14,765
	332,588	304,174

18. Other liabilities

	2003 J$'000	2002 J$'000
Interest payable	12,756,663	4,119,616
Staff and staff-related expenses	141,239	124,846
Other [see (i)]	214,215	936,845
	13,112,117	5,181,307

(i) Other includes provisions broken down as follows:

	2003 J$'000	2002 J$'000
Balance at beginning of year	148,733	143,558
Provisions made during the year	68,985	158,975
Provisions used during the year	(57,539)	(153,800)
Balance at end of year	160,179	148,733

19. Share capital

Section 8 of the Act provides for the capital of the Bank to be J$4,000,000, which has been paid by Government of Jamaica.

20. General Reserve Fund

Section 9 of the Act provides that the Bank shall establish and maintain a General Reserve Fund:

(a) to which, at the end of each financial year, the net income for that year shall be transferred or the net losses charged;

(b) from which shall be paid to the Consolidated Fund the amount by which, at the end of the financial year, the balance thereon exceeds five times the Bank's authorised share capital;

(c) into which should be paid from the Consolidated Fund at the end of the financial year, the amount by which the Bank's net loss exceeds the balance in the General Reserve Fund.

21. Special stabilisation account

The special stabilisation account is maintained at 25% of the coins in circulation as a reserve against coins that are unlikely to be redeemed.

Notes to the Financial Statements (cont'd)
December 31, 2003

22. Other reserves

This represents the following:

	2003 J$'000	2002 J$'000
Securities revaluation reserve [see (a)]	84,856	274,883
Property revaluation reserve [see (b)]	1,124,756	970,443
Pension equalisation reserve [see (c)]	837,200	763,300
	2,046,812	2,008,626

(a) This represents the unrealised gains/losses on the revaluation of available-for-sale investments.

(b) The property revaluation reserve represents the surplus arising on the revaluation of certain freehold properties (see note 10).

(c) The pension equalisation reserve represents the pension surplus arising on the actuarial valuation, under IAS 19, of the Bank's pension scheme. Annual changes in the value of the scheme are shown in the statement of income and expenses, then transferred to this reserve.

23. Foreign exchange gain

	2003 J$'000	2002 J$'000
Net unrealised gain on translation of foreign currency assets and liabilities and realised gain on settlement of foreign assets and foreign liabilities	11,822,287	5,130,009
Exchange loss on purchases and sales of foreign currency	(407,058)	(169,454)
	11,415,229	4,960,555

24. Employee numbers and costs

The number of employees at the end of the year was 473 (2002: 420) full-time and 39 (2002: 26) contract. The related costs for these employees were as follows:

	2003 J$'000	2002 J$'000
Salaries and wages	754,152	647,756
Statutory payroll contributions	46,210	45,703
Pension, medical and life insurance [see note 11(b)]	14,100	(41,700)
Uniforms	16,759	8,687
Staff welfare	42,735	34,157
Other	21,289	15,142
	895,245	709,745

Notes to the Financial Statements (cont'd)
December 31, 2003

25. Operating expenses

Operating expenses include the following charges:

	2003 J$'000	2002 J$'000
Depreciation	84,063	117,907
Auditors' remuneration	4,650	4,500
Payments for redundancies	62	2,311

26. Effects of first-time adoption of IFRS

As stated in note 2(a), these are the Bank's first financial statements prepared in accordance with IFRS.

An explanation of how the transition from Jamaica GAAP (JGAAP) to IFRS has affected the Bank's financial position, results of operations and cash flows is set out in the following tables and the notes that accompany the tables.

(a) Reconciliation of 2001 reserves:

	General reserve fund J$'000	Other reserves J$'000	Total J$'000
IAS 10 – Events after the balance sheet date [f(i)]	427,189	-	427,189
IAS 16 – Property, plant and equipment [f(ii)]	-	185,925	185,925
IAS 19 – Employee benefits [f(iii)]	229,900	-	229,900
Transfers	(640,800)	640,800	-
IAS 38 – Intangible assets [f(iv)]	(165,973)	-	(165,973)
IAS 39 – Financial instruments – Recognition and measurement [f(v)]	(366,916)	(183,006)	(549,922)
IAS 40 – Investment property [f(vi)]	27,913	-	27,913
	(488,687)	643,719	155,032

(b) Reconciliation of 2002 net loss:

	J$'000
Net loss as previously reported under JGAAP	1,389,546
IAS 10 – Events after the balance sheet date [f(i)]	(427,189)
IAS 19 – Employee benefits [f(iii)]	(90,200)
IAS 38 – Intangible assets [f(iv)]	(47,656)
IAS 39 – Financial instruments – Recognition and measurement [f(v)]	30,357
IAS 40 – Investment property [f(vi)]	(4,905)
Net loss as restated under IFRS	849,953

Notes to the Financial Statements (cont'd)
December 31, 2003

26. Effects of first-time adoption of IFRS (cont'd)

(c) The summarised effects of (a) and (b) on the Bank's financial statements for the year ended December 31, 2002 and in the preparation of an opening IFRS balance sheet at January 1, 2002 (the Bank's date of transition) are as follows:

	January 1, 2002			December 31, 2002		
	Previously reported under JGAAP J$'000	Effect of transition to IFRS J$'000	IFRS J$'000	Previously reported under JGAAP J$'000	Transition to IFRS J$'000	IFRS J$'000
ASSETS						
Notes and coins	9,223	-	9,223	7,821	-	7,821
Cash resources	15,012,093	-	15,012,093	8,030,773	-	8,030,773
Interest in funds managed by agents	1,850,377	-	1,850,377	2,066,358	-	2,066,358
Investments [f(v)]	72,992,293	(202,933)	72,789,360	72,655,168	(507,941)	72,147,227
International Monetary Fund - Holding of Special Drawing Rights	68,895	-	68,895	39,917	-	39,917
Total foreign assets	89,932,881	(202,933)	89,729,948	82,800,037	(507,941)	82,292,096
Notes and coins	39,196	-	39,196	36,429	-	36,429
Investments [f(v)]	47,005,030	19,927	47,024,957	59,422,058	90,423	59,512,481
International Monetary Fund - Quota Subscription	1,798,707	-	1,798,707	1,886,832	-	1,886,832
Investment property [f(vi)]	-	95,500	95,500	-	108,500	108,500
Investments in financial institutions	3,360	-	3,360	3,210	-	3,210
Due from Government and Government Agencies [f (i), (ii), (iii),(iv), (v) and (vi)]	8,599,418	488,687	9,088,105	4,942,540	925,973	5,868,513
Property, plant and equipment [f(ii)]	1,152,334	118,338	1,270,672	1,148,454	236,255	1,384,709
Employee benefits	-	640,800	640,800	-	763,300	763,300
Other [f(iii)]	4,499,716	(505,706)	3,994,010	1,945,984	(515,591)	1,430,393
Total local assets	63,097,761	857,546	63,995,307	69,385,507	1,608,860	70,994,367
Total assets	153,030,642	654,613	153,685,255	152,185,544	1,100,919	153,286,463
LIABILITIES, CAPITAL AND RESERVES						
Notes and coins in circulation	22,367,790	-	22,367,790	24,364,753	-	24,364,753
Deposits and other demand liabilities	82,378,353	-	82,378,353	70,498,753	-	70,498,753
Securities sold under repurchase agreements	38,446,253	-	38,446,253	47,732,400	-	47,732,400
International Monetary Fund - Allocation of Special Drawing Rights	2,347,016	-	2,347,016	2,462,006	-	2,462,006
Foreign liabilities	291,721	-	291,721	304,174	-	304,174
Employee obligations [f(iii)]	-	410,900	410,900	-	443,200	443,200
Other	5,979,665	(400,006)	5,579,659	5,181,307	-	5,181,307
Total liabilities	151,810,798	10,894	151,821,692	150,543,393	443,200	150,986,593
Capital and reserves	4,000	-	4,000	4,000	-	4,000
General Reserve Fund	20,000	-	20,000	-	-	-
Other reserves [f(ii) and (v)]	1,195,844	643,719	1,839,563	1,638,151	657,719	2,295,870
Total capital and reserves	1,219,844	643,719	1,863,563	1,642,151	657,719	2,299,870
Total liabilities, capital and reserves	153,030,642	654,613	153,685,255	152,185,544	1,100,919	153,286,463

Notes to the Financial Statements (cont'd)
December 31, 2003

26. Effects of first-time adoption of IFRS (cont'd)

(d) The summarized effects of (b) on the Bank's statement of revenue and expenses for the year ended December 31, 2002 are as follows:

	Previously reported under JGAAP	Effect of transition to IFRS	IFRS
	J$'000	J$'000	J$'000
Operating income			
Interest [f(i)]	11,795,186	27,183	11,822,369
Foreign exchange gain, net	4,960,555	-	4,960,555
Other	24,822	-	24,822
Total	16,780,563	27,183	16,807,746
Operating expenses			
Interest [f(i)]	16,329,741	(400,006)	15,929,735
Salaries, pension scheme contributions, staff and post retirement benefits [f(iii)]	853,293	(143,548)	709,745
Currency expenses	282,522	-	282,522
Property expenses and depreciation [f(vi)]	245,548	(2,573)	242,975
Other operating expenses	258,976	-	258,976
Total	17,970,080	(546,127)	17,423,953
Net operating loss	(1,189,517)	573,310	(616,207)
Other gains/(losses)			
Bad debts, net	(5,196)	-	(5,196)
Gain/(loss) on remeasurement [f(iii)]	-	(36,049)	(36,049)
Loss on revaluation of securities	(33,401)	-	(33,401)
Gain on disposal of fixed assets	1,805	-	1,805
Change in value of investment property [f(vi)]	-	2,332	2,332
Expenditure on behalf of Government of Jamaica not reimbursed	(163,237)	-	(163,237)
Net loss for the year	(1,389,546)	539,593	(849,953)

(e) Effect on statement of cash flows:

There were no material adjustments between the cash flow statement presented under IFRS and the cash flow statement presented under previous JGAAP.

Notes to the Financial Statements (cont'd)
December 31, 2003

26. Effects of first-time adoption of IFRS (cont'd)

(f) Notes to IFRS adjustments:

(i) This represents adjustments relating to the Bank's and the Ministry of Finance's September 6, 2002 agreement. Some changes, which affected 2001 balances, were eliminated from 2001 and shown in 2002 to comply with IAS 10.

(ii) This arose on the revaluation of certain freehold properties, which were carried at cost under JGAAP, but are now carried at market value.

(iii) Employee benefits:

(a) The basis on which doubtful debt provision was made under JGAAP has changed from applying a percentage to overdue balances, to comparing the collateral values to outstanding balances and then provide for shortfalls.

(b) Pension asset on defined pension benefit scheme, and obligations under medical and life insurance schemes are recognised under IFRS based on valuation results of the schemes carried out by independent actuaries. These were not recognised under JGAAP.

(iv) Certain items that were carried as deferred asset, but did not meet the definition of asset under IFRS have been written-off.

(v) Financial instruments – Recognition and measurement:

(a) Investments were carried at fair value under JGAAP. Under IFRS, investments classified as originated loans are carried at amortised cost. The resultant difference between fair value under JGAAP and amortised cost under IFRS is taken to securities revaluation reserve.

(b) Interest is charged at concessionary rates on staff loans. IFRS requires that such loans be re-measured, using market rates, and the interest concession by the Bank should be recorded as a cost.

(v) This represents the reclassification of certain freehold properties, from property, plant and equipment, to investment property under IAS 40. The properties are now carried at market value and the change in market value is taken to the statement of income and expenses.

27. Capital commitments

At the balance sheet date, the Bank had commitments for capital expenditure as under:

	2003	2002
	J$'000	J$'000
Authorised and contracted	36,639	32,803
Authorised but not contracted	13,540	13,211
	50,179	46,014

28. Contingent liabilities

At December 31, 2003, the Bank was a defendant in various relatively minor suits claiming damages. The Bank is of the view that the claims are generally without merit and will not result in any significant losses to the Bank. There are no lawsuits pending with the Bank as plaintiff as at December 31, 2003.

Notes to the Financial Statements (cont'd)
December 31, 2003

29. Financial instruments

A financial instrument is any contract that gives rise to both a financial asset of one enterprise and a financial liability or equity instrument of another enterprise.

(a) Fair value of financial instruments:

Fair value is the arm's length consideration for which an asset could be exchanged or a liability settled, between knowledgeable, willing parties, who are under no compulsion to act and is best evidenced by a quoted market price, if one exists.

Determination of fair value:

The financial instruments held at the balance sheet date are: cash resources, interest in funds managed by agents, foreign and local currencies denominated investments, other assets, due from Government and Government Agencies, deposits and other demand liabilities, securities sold under repurchase agreements, International Monetary Fund – Allocation of Special Drawing Rights, foreign liabilities and other liabilities.

The fair value of foreign and local currencies denominated investments is assumed to be equal to the estimated market values as provided in notes 4 and 5, respectively. These values are obtained on the basis outlined in note 2(c)(iii).

The fair value of certain short-term financial instruments was determined to approximate their carrying value.

No fair value has been estimated on the amount due from Government and Government Agencies, as there is no practical means of estimating its fair value.

(b) Financial instrument risk:

Exposure to foreign currency, interest rate, credit, market, liquidity and cash flow risks arises in the ordinary course of the Bank's business. No derivative instruments are presently used to manage, mitigate or eliminate exposure to financial instrument risks.

(i) Foreign currency risk

Foreign currency risk is the risk that the value of a financial instrument will fluctuate due to changes in foreign exchange rates. At the balance sheet date, the Bank's net exposure to foreign exchange rate fluctuations was as follows:

	2003 J$'000	2002 J$'000
Foreign currency assets	74,615,244	84,700,824
Foreign currency liabilities	(12,665,353)	(11,993,082)
Net foreign currency assets	61,949,891	72,707,742

	2003	2002
Buying exchange rates at December 31:		
US$1 to J$	60.40	50.52
UK£1 to J$	107.77	81.31
CDN$1 to J$	46.74	31.98
€ to J$	76.09	52.98

At March 24, 2004, the buying exchange rates were US$1 to J$60.77, UK£1 to J$112.43, CDN$1 to J$45.62 and € 1 to J$73.69.

Notes to the Financial Statements (cont'd)
December 31, 2003

29. Financial instruments (cont'd)

(b) Financial instrument risk (cont'd):

(ii) Interest rate risk:

Interest rate risk is the risk that the value of a financial instrument will fluctuate due to changes in market interest rates. The Bank manages this risk by monitoring interest rates daily and ensuring that, even though there is no formally predetermined gap limits, to the extent practicable, the maturity profile of its financial assets is matched by that of its financial liabilities.

The following table summarises the carrying amounts of balance sheet assets, liabilities and equity to arrive at the Bank's interest rate gap based on the earlier of contractual repricing and maturity dates.

	2003						
	Within 3 months J$'000	Three to 12 months J$'000	Over 12 months J$'000	Payable after notice J$'000	Non-rate sensitive J$'000	Total J$'000	Weighted average interest %
Assets							
Notes and coins	-	-	-	-	66,387	66,387	-
Cash resources	-	-	-	-	9,221,708	9,221,708	-
Interest in funds managed by agents	-	-	-	2,533,834	-	2,533,834	3.79
Foreign currency denominated investments	33,292,095	-	26,807,112	-	-	60,099,207	2.46
International Monetary Fund - Holding of Special Drawing Rights	-	-	-	-	3,198	3,198	-
Local currency denominated investments	1,904,412	5,108,873	71,294,717	-	-	78,308,002	24.80
Investment property	-	-	-	-	87,000	87,000	-
International Monetary Fund – Quota Subscription	-	-	-	-	2,454,750	2,454,750	-
Investments in financial institutions	-	-	-	-	3,210	3,210	-
Due from Government and Government agencies	-	-	-	-	4,563,331	4,563,331	-
Property, plant and equipment	-	-	-	-	1,629,927	1,629,927	-
Employee benefits	-	-	-	-	837,200	837,200	-
Other assets	-	-	-	-	109,217	1,338,051	1,447,268
Total assets	35,196,507	5,108,873	98,101,829	2,643,051	20,204,762	161,255,022	7.82
Liabilities							
Notes and coins in circulation	-	-	-	-	29,424,600	29,424,600	-
Deposits and other demand liabilities:							
Jamaica dollar equivalent of foreign currency deposits	1,095,042	-	-	7,968,756	-	9,063,798	0.58
Jamaica dollar deposits	13,804,426	11,459,362	-	17,670,745	3,603,964	46,538,497	15.08
Securities sold under repurchase agreements	21,136,364	35,569,202	-	-	-	56,705,566	26.85
International Monetary Fund – Allocation of Special Drawing Rights	-	-	-	-	3,203,044	3,203,044	-
Foreign liabilities	-	-	310,536	-	22,052	332,588	8.4
Employee obligations	-	-	-	-	474,400	474,400	-
Other liabilities	-	-	-	-	13,112,117	13,112,117	-
Capital and reserves	-	-	-	-	2,400,412	2,400,412	-
Total liabilities	36,035,832	47,028,564	310,536	25,639,501	52,240,589	161,255,022	12.73
Total interest rate sensitivity gap	(839,325)	(41,919,691)	97,791,293	(22,996,450)	(32,035,827)	-	-
Cumulative gap	(839,325)	(42,759,016)	55,032,277	32,035,827	-	-	-

Notes to the Financial Statements (cont'd)
December 31, 2003

29. Financial instruments (cont'd)

(b) Financial instrument risk (cont'd):

(ii) Interest rate risk: (cont'd)

	2002						
	Within 3 months J$'000	Three to 12 months J$'000	Over 12 months J$'000	Payable after notice J$'000	Non-rate sensitive J$'000	Total J$'000	Weighted average interest %
Assets							
Notes and coins	-	-	-	-	44,250	44,250	-
Cash resources	-	-	-	-	8,030,773	8,030,773	-
Interest in funds managed by agents	-	-	-	2,066,358	-	2,066,358	3.09
Foreign currency denominated investments	41,969,288	10,063	30,167,876	-	-	72,147,227	3.70
International Monetary Fund - Holding of Special Drawing Rights	-	-	-	-	39,917	39,917	-
Local currency denominated investments	168	5,170,994	52,131,973	-	2,209,346	59,512,481	17.57
International Monetary Fund – Quota Subscription	-	-	-	-	1,886,832	1,886,832	-
Investment property	-	-	-	-	108,500	108,500	-
Investments in financial institutions	-	-	-	-	3,210	3,210	-
Due from Government and Government agencies	-	-	-	-	5,868,513	5,868,513	-
Property, plant and equipment	-	-	-	-	1,384,709	1,384,709	-
Employee benefits	-	-	-	-	763,300	763,300	-
Other assets	-	-	-	121,207	1,309,186	1,430,393	0.22
Total assets	41,969,456	5,181,057	82,299,849	2,187,565	21,648,536	153,286,463	6.15
Liabilities							
Notes and coins in circulation	-	-	-	-	24,364,753	24,364,753	-
Deposits and other demand liabilities:							
Jamaica dollar equivalent of foreign currency deposits	3,458,235	-	-	5,708,849	-	9,167,084	2.21
Jamaica dollar deposits	27,082,793	15,260,347	-	15,126,562	3,861,967	61,331,669	7.37
Securities sold under repurchase agreements	31,134,327	16,598,073	-	-	-	47,732,400	17.68
International Monetary Fund – Allocation of Special Drawing Rights	-	-	-	-	2,462,006	2,462,006	-
Foreign liabilities	-	-	284,839	-	19,335	304,174	8.30
Employee obligations	-	-	-	-	443,200	443,200	-
Other liabilities	-	-	-	-	5,181,307	5,181,307	-
Capital and reserves	-	-	-	-	2,299,870	2,299,870	-
Total liabilities	61,675,355	31,858,420	284,839	20,835,411	38,632,438	153,286,463	8.89
Total interest rate sensitivity gap	(19,705,899)	(26,677,363)	82,015,010	(18,647,846)	(16,983,902)	-	
Cumulative gap	(19,705,899)	(46,383,262)	35,631,748	16,983,902	-	-	

(iii) Credit risk:

Credit risk is the risk of loss arising from a counter-party to a financial contract failing to discharge its obligations.

Credit risk in the foreign currency investment portfolio is managed by restricting the holdings of investments substantially to US Government securities, other highly rated sovereign issues, Jamaica Government US$ debentures and placements in highly rated supranational institutions.

Notes to the Financial Statements (cont'd)
December 31, 2003

29. Financial instruments (cont'd)

(b) Financial instrument risk (cont'd):

(iii) Credit risk (cont'd):

Credit risk for local securities is managed by investing primarily in Government of Jamaica securities. Other credit exposures consist mainly of staff loans for housing and motor vehicles.

Exposures to credit risk attaching to financial assets are monitored through credit rating and lending limits, which are regularly reviewed. In addition, securities issued or guaranteed by the Government of Jamaica are required to collateralise advances to financial institutions. Mortgages and liens are obtained for housing and motor vehicle loans to staff, respectively.

Cash resources are held in financial institutions which management regards as strong and there is no significant concentration. The Bank's significant concentrations of credit exposure by geographical areas (based on the entity's country of ownership) are as follows:

	2003 J$'000	2002 J$'000
Jamaica	78,622,100	60,344,073
U.S.A. and other industrialised countries	71,316,693	82,075,462
Barbados	36,631	29,557
Multilateral Institutions	2,457,948	1,926,749
Other	617,573	458,600
Total financial assets	153,050,945	144,834,441

Current credit exposure is the amount of loss that the Bank would suffer if every counterparty to which the Bank was exposed were to default at once; this is represented substantially by the carrying amount of financial assets shown on the balance sheet.

(iv) Market risk:

Market risk is the risk that the value of a financial instrument will fluctuate as a result of changes in market prices, whether those changes are caused by factors specific to the individual security, its issuer or factors affecting all securities traded in the market.

The Bank manages market risk on its foreign asset portfolio through:

- Its investment policy, which prescribes the quality of the issuer and limits investments to specific foreign government securities that are deemed to be virtually risk free.
- Its diversification of the portfolio into various instruments while limiting the maximum permitted exposure to any one security or issuer.
- Its policy of holding securities to maturity which in essence eliminates the possibility of loss arising from fluctuations in market price.

Notes to the Financial Statements (cont'd)
December 31, 2003

29. Financial instruments (cont'd)

(b) Financial instrument risk (cont'd):

(iv) Market risk (cont'd):

Market risk on the Bank's local asset portfolio of investments is minimised by restricting investments to securities issued or guaranteed by the Government of Jamaica.

(v) Liquidity risk:

Liquidity risk, also referred to as funding risk, is the risk that the Bank will encounter difficulty in converting its securities to cash at, or close to, its fair value or in raising funds to meet its commitments. Prudent liquidity management implies maintaining sufficient cash and marketable securities, and ensuring the availability of funding through an adequate amount of committed standby credit facilities to meet commitments.

The Bank's exposure to liquidity risk to meet foreign liabilities, as an institution, is limited due to the minimal amount owed to overseas creditors/lenders. Management of liquidity risk relates primarily to the availability of liquid foreign resources to sell to the Government of Jamaica and its agencies to repay their creditors and lenders. The Bank manages this risk through a combination of:

- Budgetary procedures to identify the timing of Government foreign payments.
- Scheduling the maturity of foreign deposits to coincide with the demands of Government and its Agencies.
- Maintaining a portion of its foreign assets in cash or near cash as precautionary funds to meet unforeseen demands.

The Bank, like all central banks, has no real liquidity risk in relation to its domestic financial obligations.

(vi) Cash flow risk:

Cash flow risk is the risk that future cash flows associated with a monetary financial instrument will fluctuate in amount.

The Bank manages this risk through budgetary measures ensuring, as far as possible, that financial assets and liabilities are matched to mitigate any significant adverse cash flows.