Fiscal Sustainability: The Case for Jamaica

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The paper assesses the sustainability of fiscal policy in Jamaica alongside a large public debt stock, albeit falling, in the context of an economic reform program. In addition, the paper examines the risks associated with the large public debt stock. Fiscal reaction functions are used to assess fiscal sustainability via an OLS, VAR, GMM and VECM models while the vulnerability of the public debt stock is evaluated using the IMF debt sustainability analysis (DSA) framework through shocks to real GDP, primary balance, interest rate, real exchange rate, and a combined shock. After the implementation of the country's economic reform program, the results show that fiscal policy in Jamaica is on a path to attain sustainability. However, after adjusting the sample to exclude the economic reform period, the findings show that fiscal policy in Jamaica is unsustainability. Further, the results indicate that in the long run a primary surplus of 4.8 per cent of GDP would be required to achieve a public debt-to-GDP ratio of 60 percent. The risk assessment of the public debt reveals that Jamaica's debt is most vulnerable to sharp exchange rate depreciations and that the overall risk to the public debt stock is high. Of note, the DSA results should be interpreted in the context within which the framework is created in that it does not account for all dynamics within the economy and therefore may overstate the extend of the impact. In light of the results and given that foreign currency debt accounts for approximately 60 percent of the public debt stock, it is critical to rebalance the debt portfolio in favour of domestic debt.

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***The views expressed are those of the author and does not necessarily reflect those of the Bank of Jamaica.**