

20 December 2018

BANK OF JAMAICA LOWERS POLICY RATE

Bank of Jamaica announces its decision to lower the policy interest rate (the rate offered on overnight placements with Bank of Jamaica) by **25 basis points to 1.75 per cent**.

Inflation

This decision reflects the Bank's most recent assessment that inflation could now fall below the lower limit of the 4.0 per cent to 6.0 per cent target in the latter half of 2019 and early 2020. There is also some risk that inflation could fall below 4.0 per cent at December 2018.

The inflation rate at November 2018, as reported by the Statistical Institute of Jamaica, was 4.1 per cent, lower than the 4.7 per cent recorded at October 2018 and the 4.9 per cent at November 2017.

At the Bank's last assessment in November 2018, inflation was projected to approach the upper end of the 4.0 per cent to 6.0 per cent target by June 2019 and trend thereafter to the middle of the target range. Over the short term, the key sources of upward price pressures were expected to emanate from (1) continued improvements in domestic demand and (2) increases in utility rates consequent on an assumption that international oil prices would remain elevated for the next two quarters. One of the main downside risks to the November 2018 forecast that would cause inflation to be lower than projected was that international oil prices could be lower than anticipated.

Those downside risks have since materialised, with crude oil prices for October and November 2018 falling significantly below the Bank's forecast. In addition, the likelihood is increasing that oil prices will remain at their current low levels (approximately 30 per cent below the previous forecast) and this intensifies the risk of inflation breaching the lower limit of the Bank's target over the near term. Declines in domestic agricultural prices, associated with an expected recovery in crop production in the December 2018 quarter, could intensify this risk over the very short term.

Meanwhile, all measures of underlying inflation at November 2018 continued to be low, lending support to an assessment that recent improvements in domestic demand have not stimulated inflationary pressures in Jamaica.

Other Economic Variables

Over the near term, the domestic economy is likely to continue to reflect some slack (i.e., projected GDP growth is less than the Bank's estimate of potential GDP growth). In the medium term, growth prospects are heavily contingent on the continued expansion of construction and agriculture, which both carry some downside risk.

There is a downside risk to domestic growth from potentially weaker external demand signalled by the revision downwards in the US Federal Reserve's growth outlook, notwithstanding its decision this week to increase its policy rate. There is also a downside risk to domestic growth as the pace of expansion in private sector credit extended by deposit-taking institutions in October 2018 was lower than Bank of Jamaica's forecast and showed signs of weakening. Credit to the private sector expanded year over year by 16.3 per cent at October 2018, slightly lower than the growth of 16.4 per cent at September 2018 but above the 11.6 per cent at October 2017.

Bank of Jamaica's decision to lower the policy rate is therefore aimed at stimulating a pick-up in the rate of expansion in private sector credit, which should lead to higher economic activity, which will support inflation being maintained in the target range of 4.0 per cent to 6.0 per cent.

Other macroeconomic indicators continue to be positive. Foreign reserves are above the level deemed to be adequate, market interest rates are low, labour market conditions are improving and fiscal performance continues to be strong.

The next policy decision announcement date is 20 February 2019.