Monetary Policy Press Statement:
QMPR Press Conference

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Bank of Jamaica

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Ladies and gentlemen, good morning

On Monday, Bank of Jamaica announced its decision to maintain its policy rate at its historic low of 0.50 per cent per annum. The policy rate is that offered to deposit-taking institutions on overnight placements with the Bank.

The Bank believes that its current monetary policy stance is adequate to keep inflation within the target range but we will continue to review and assess our stance as time progresses. For the current fiscal year (FY2020/21) the point-to-point inflation rate is projected to be 4.5 per cent, while a slightly lower rate is projected for the next fiscal year. This forecast path is lower than our projection in February.

Our policy rate decision comes after arguably the most difficult two months for all Jamaicans and particularly those who have lost their jobs or had a family or friend fall victim to COVID-19. For us at BOJ, while we have been keeping a close eye on inflation, the sharp economic downturn has required us to devote much effort to ensuring the stability of the financial markets so that Jamaica can make a strong economic recovery when this challenging period comes to an end.

In that respect, the Bank has already implemented several initiatives to soften the unparalleled economic blow. These initiatives have centred around ensuring adequate liquidity in both the domestic and foreign exchange markets. Thus, last Friday (15 May) we announced our decision to lower the Jamaica Dollar cash reserve requirement for deposit-taking institutions (DTIs) by two (2) percentage points to the statutory minimum of 5 per cent of prescribed liabilities. This reduction, which is aimed at boosting liquidity levels in the financial system, became effective immediately and released approximately J$14 billion to DTIs. Simultaneously, we reduced the foreign currency cash reserve requirement for DTIs by two (2) percentage points to 13 per cent which returned about US$70 million to DTIs.

You will recall that previously, in addition to the regular facilities for liquidity assurance, the Bank has (i) removed the limits on the amounts that DTIs can borrow overnight, without being charged a penal rate, (ii) re-introduced a longer-term lending facility to DTIs for periods of up to six months, (iii) established a GOJ and BOJ bond buying programme, (iv) reactivated an intermediation facility to broker interbank lending, and (v) reactivated the Emergency Liquidity Facility that was initially established in 2015.

In the foreign exchange market our efforts have sought to encourage orderly conditions and included (i) raising the limit on the foreign currency net open positions of authorised dealers, (ii) direct sales to authorised dealers and cambios via B-FXITT, (iii) direct sales to the Jamaica Public Service Company and Petrojam, (iv) expanding the volume of foreign currency swap arrangements with authorised dealers, and (v) provision of a US dollar repo facility (US$170 million) to financial institutions. Foreign currency liquidity assistance provided to the financial market since the onset of the domestic crisis in March 2020 up to 15 May amounted to approximately US$338 million. Those are the initiatives of the BOJ to assist financial market stability over the past three months.

Inflation Outlook

Let me return to the matter of inflation and provide more details that informed our decision on Monday. The near-term inflation forecast that I highlighted earlier is impacted by two principal factors:

1. lower imported inflation; and
2. weaker demand conditions.

The expected fall in imported inflation is principally the result of projected lower oil and grain prices as well as generally lower inflation rates among Jamaica's main trading partners, particularly the US. These factors will cause lower rates of increase in retail prices and in domestic energy-related prices (in particular transport prices), despite a depreciated exchange rate.

The inflation forecast also takes into account the temporary stop in tourist arrivals and spending, and lower remittance inflows. These conditions will cause a deceleration in agricultural food prices as excess supplies will emerge for the duration of the period over which the tourism industry is closed. The COVID-19 pandemic is also likely to result in reduced domestic demand for several goods and services due to widespread job losses and elevated consumer uncertainty.

Over the medium-term (that is, three to five years ahead), inflation is projected to rise gradually to 5.0 per cent as the effects of the pandemic dissipates and the economic recovery regains full swing. I invite you to read the QMPR for additional details about the inflation forecast.

Risks to the Forecast

Notwithstanding the high degree of uncertainty around the duration of the crisis, over the next two years there is a stronger chance that inflation will be lower than the forecast that I have just outlined to you.

One of the factors that could cause inflation to be lower than anticipated includes even weaker domestic demand than expected because of a prolonged spread of the Coronavirus in Jamaica and abroad. In this event, we would also see international commodity prices staying lower for longer than we currently envisage. There is also the possibility that the administered price increases for water and electricity that we assumed, will not occur.

The main factors that could cause inflation to be higher than expected include a faster pace of depreciation in the exchange rate as well as higher agriculture prices resulting from adverse weather conditions. There is also a risk that the return to normalcy in the tourism sector could impact prices (particularly those related to agricultural produce).

Impact of COVID-19 on Jamaica's GDP and BOP

The economic outlook for Jamaica and the world is characterised by significant uncertainty, as we cannot determine the full intensity and duration of this global health crisis and the measures put in place by governments. We are seeing signs that the daily infection rates appear to be stabilizing in some countries, suggesting that we may be approaching the global peak of the outbreak of new cases. With these caveats, Bank of Jamaica's baseline forecast assumes that the virus will be largely contained by end-June 2020 and that the global economy will gradually re-open thereafter. I invite you to read the Box: **An Assessment of the COVID-19 Epidemiological Curve** in the QMPR for more details on the factors that informed this assumption.

In the context of these assumptions, the Bank projects that the Jamaican economy will contract in the range 4 - 7 per cent for FY2020/21. Specifically, our forecast is a contraction of 5.1 per cent for this fiscal year. We are anticipating a recovery of 2.5 – 5.5 per cent in FY2021/22. The projected contraction in FY2020/21 is broad-based but will be mainly reflected in *Hotels & Restaurants*, *Mining*, *Wholesale & Retail*, *Transport*, *Storage & Communication* and *Other Services*. Other industries, such as *Manufacturing* and *Distribution*, which have been impacted by the measures instituted locally, will also see a decline. We expect that economic growth will resume by the first half of next fiscal year as ports re-open, travel and tourism-related activities gradually resume, and related services and production in the other sectors of the economy are revived.

These drastic changes in the pattern of economic activity in Jamaica and abroad will be reflected in the balance of payments. The current account deficit of the balance of payments is projected to worsen by more than 5 percentage points of GDP in FY2020/21 to 7.5 per cent from the 2.3 per cent estimated for FY2019/20. This worsening mainly reflects the impact of the sudden stop in tourist arrivals and the slowdown in remittance inflows. In contrast, the merchandise trade deficit is projected to improve due to a decline in imports, particularly fuel, in the context of lower oil prices. The fall in the income of Jamaicans as well as a decline in FDI-related projects are also expected to constrain the importation of non-fuel consumer goods, raw materials and capital goods. The assumed gradual recovery of economic activity implies that the current account deficit will also improve gradually over the ensuing two years.

Ladies and gentlemen, if events unfold as we have envisaged, this shock to the external accounts implies that we have a significant financing gap and is reflected in the sharp depreciation of the Jamaican dollar over the past two months, despite the BOJ providing the market with over US$300 million. We must pace our interventions, for at this rate, the Bank could end up selling more than US$1 billion to the market over the course of the fiscal year, which is unsustainable. Be assured however, that with careful management, at US$3.1 billion at end-April 2020, the net international reserves of the Bank of Jamaica (NIR) are adequate to weather this storm.

In addition, the Government of Jamaica thought it prudent to put in place contingency arrangements by applying to the IMF for support of US$520 million under the rapid financing facility (RFI). The IMF Executive Board met on Friday, May 15th and approved the request for the loan. The proceeds of the loan are currently reflected in the gross reserves of the central bank. The Government can also use these RFI resources for budget support, should the need arise.

Concluding Statements

Ladies and gentlemen, we are, and have always been, a resilient people. While the heightened challenges associated with the COVID-19 outbreak remain an ongoing concern, we are confident that the measures that we have put in place at the Bank, alongside the aggressive fiscal stimulus measures being implemented by the Government, will serve to mitigate some of the impact on the economy and set us on a path to economic recovery. Bank of Jamaica remains true to its core mandate of ensuring that inflation remains low, stable and predictable and, at the same time, is prepared to take all necessary actions to ensure that Jamaica's financial system remains sound and well capitalized.

Thank you.