ANNUAL REPORT

2006

Report and Statement of Accounts for the
Year Ended 31 December 2006

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.

The Governor

Bank Of Jamaica
Nethersole Place
Kingston, Jamaica, W.I.

30 March 2007

Dr. The Hon. Omar Davies
Minister of Finance & Planning
Ministry of Finance
30 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 2006 and a copy of the Statement of the Bank's Accounts as at 31 December 2006 duly certified by the Auditors.

Yours sincerely,

Derick Latibeaudiere

PRINCIPAL OFFICERS

GOVERNOR
The Hon. Derick Latibeaudiere, O.J.

SENIOR DEPUTY GOVERNOR
Mrs. Audrey Anderson, C.D.

DEPUTY GOVERNORS

1.	Mr. Rudolph Muir	-	General Counsel & Bank Secretary
2.	Mrs. Myrtle Halsall	-	Research & Economic Programming and Banking & Market Operations Divisions
3.	Mrs. Gayon Hosin	-	Financial Institutions Supervisory Division
4.	Mr. Livingstone Morrison	-	Finance & Technology, Payments System, Investment and Risk Management Division

GENERAL MANAGER
Mr. Kenloy Peart

DIVISION CHIEFS

1.	Mrs. Natalie Haynes	-	Banking & Market Operations Division
2.	Mr. John Robinson	-	Research & Economic Programming Division
4.	Mrs. Faith Stewart	-	Payments System, Investment and Risk Management

FINANCIAL CONTROLLER
Mr. Herbert Hylton - Finance & Technology Division

DEPUTY GENERAL COUNSEL
Mr. Randolph Dandy - Senior Legal Counsel, Legal Department

CHIEF INTERNAL AUDITOR
Mrs. Evadnie Sterling - Internal Audit Department

BOARD OF DIRECTORS

CONTENTS

ABBREVIATIONS

ABM	Automated Banking Machines
ACH	Automated Clearing House
ACP	African, Pacific and Caribbean (countries)
AFI	Approved Financial Institutions
AML/CFT	Anti-money Laundering and Counter-Financing of Terrorism
ARC	Accounts Receivable Conversion
ASBA	Association of Supervisors of the Banks of the Americas
ASEAN	Association of South-East Asian Nations
BCP	Basel Core Principles
BIS	Bank for International Settlements
BITU	Bustamante Industrial Trade Union
BLADEX	Banco Latino Americano de Exportaciones
BOC	Bank of Canada
BoE	Bank of England
BOJ	Bank of Jamaica
BoJ	Bank of Japan
BOP	Balance of Payments
BP	British Petroleum
Bpd	Barrels per day
Bps	Basis points
CAD	Current Account Deficit
CAP	Clarendon Alumina Production
CAR	Capital Adequacy Ratio
CARICOM	Caribbean Community
CARTAC	Caribbean Technical Assistance Centre
CBERA	Caribbean Basin Economic Recovery Act
CD	Certificates of Deposit
CEO	Chief Executive Officer
CET	Common External Tariff
CFATF	Caribbean Financial Action Task Force
CGBS	Caribbean Group of Banking Supervisors
c.i.f.	Cost, insurance and freight
CIFTS	Customer Inquiry Funds Transfer System
CPI	Consumer Price Index
CSD	Central Securities Depository
CSM	Caribbean Single Market
CSME	Caribbean Single Market and Economy
DBJ	Development Bank of Jamaica
DOFPA	Drug Offences Forfeiture of Proceeds Act
DTI	Deposit-taking Institutions
ECB	European Central Bank
EU	European Union
EWS	Early Warning System
Ex-Im Bank	National Export-Import Bank of Jamaica
FATF	Financial Action Task Force
FCIBS	FirstCaribbean Building Society
FDI	Foreign Direct Investment
Fed	Federal Reserve (US)
FIA	Financial Institutions Act
FID	Financial Investigations Division
FIFA	Fédération Internationale de Football Association
FISD	Financial Institutions Supervisory Division
FISIS	Financial Institutions Supervisory Information System

ABBREVIATIONS (Cont'd.)

FOMC	Federal Open Market Committee
FSAP	Financial Sector Adjustment Programme
FSD	Financial Stability Department
FY	Fiscal Year
GBP	Great Britain Pound
GDP	Gross Domestic Product
GOJ	Government of Jamaica
IAIS	International Association of Insurance Supervisors
IASB	International Accounting Standards Board
ICC	International Cricket Council
IEA	International Energy Agency
IFRS	International Financial Reporting Standards
IMF	International Monetary Fund
IOSCO	International Organization of Securities Commission
IPCP	Index of Primary Commodity Prices
JBA	Jamaica Bankers Association
JCSD	Jamaica Central Securities Depository
JNBS	Jamaica National Building Society
JSE	Jamaica Stock Exchange
KMA	Kingston Metropolitan Area
KYC	Know Your Customer
LRS	Local Registered Stocks
MLA	Money Laundering Act
MLR	Money Laundering Regulation
MOU	Memorandum of Understanding
NDA	Net Domestic Assets
NHT	National Housing Trust
NIBJ	National Investment Bank of Jamaica
NIR	Net International Reserves
NPL	Non-Performing Loans
OCC	Office of the Comptroller of Currency
OMO	Open Market Operations
OPEC	Organization of Petroleum Exporting Countries
PC Bank	People's Cooperative Bank
PCMB	Pan-Caribbean Merchant Bank
PD	Primary Dealers
PEP	Politically Exposed Persons
POCA	Proceeds of Crime Act
POS	Point of Sale
REPD	Research and Economic Programming Division
RTGS	Real Time Gross Settlement
SIPS	Systemically Important Payments System
SWIPS	System-wide Important Payment System
T&T	Trinidad and Tobago
UK	United Kingdom
UN	United Nations
US	United States
VMBS	Victoria Mutual Building Society
WASR	Weighted Average Selling Rate
WTI	West Texas Intermediate (crude oil)
WTO	World Trade Organization

1. Overview

The Bank of Jamaica (BOJ) eased monetary policy on a number of occasions in 2006. This was against the background of broadly favourable domestic macroeconomic conditions, growing investor confidence and supportive international developments. The foreign exchange market was relatively stable in 2006, reflecting the impact of improved investor confidence in the last half of the year. Domestic GDP growth accelerated, driven by a rebound in agricultural production and robust growth in tourist arrivals. In addition, all indicators of the health of the domestic financial system remained strong in 2006, while the system remained resilient to shocks. Externally, world growth also accelerated, while oil prices increased at a slower pace than in 2005, both of which contributed to a broadly positive balance of payments outturn. Given the confluence of positive developments, the Bank was able to constrain core inflation for the calendar year, which underpinned a fall in headline inflation.

The sharp fall in headline inflation to 5.8 per cent in 2006 from 12.9 per cent in 2005 was the most significant change in the macroeconomic environment during the year. It represented the first single-digit calendar year outturn since 2002 and the lowest such outturn since 1981. Core inflation also fell to 3.4 per cent in 2006 from 5.2 per cent in 2005. The fall in inflation was influenced in part by a relatively strong expansion in agricultural supply, which fostered significant reductions in the prices of agricultural products. However, the trend decline in the prices for agricultural food items was somewhat offset by higher meat prices, associated with supply shortages. In addition, the price of consumer staples rose significantly during the year, reflecting the impact on domestic prices of increases in the price of wheat on the international market. There were also upward adjustments to critical production inputs such as electricity rates, minimum wage and cement prices.

An important contributor to the moderation in inflation was continued stability in the foreign exchange market during 2006. The weighted average selling rate (WASR) of the US dollar depreciated by 3.8 per cent relative to 4.6 per cent in 2005. The stability in the market was underpinned by a confluence of factors including judicious intervention by the Bank, improvements in the economic outlook, a significant decline in world oil prices in the last quarter of the year that tempered the impact of fuel-related imports on US dollar demand, a pause in monetary tightening in the US in August and strong foreign currency inflows from tourism, remittances and foreign direct investments.

Notwithstanding the overall stability, intermittent demand pressures emerged in the foreign exchange market during the year. The instability was related to seasonal imbalances over the course of the year as well as secondary market trading of public and privately issued bonds. In the context of an increased appetite for US dollar denominated assets, given the steady narrowing in the interest rate differential since the start of the year, these bond offers were deemed to be attractive.

The Bank resumed the loosening of monetary conditions in the second quarter of the year. There were heightened inflationary expectations during the first quarter of 2006,

prompting the Bank to hold interest rates at levels in effect since May 2005. In addition, the tightening of monetary policy by the Federal Reserve in the United States served to reduce the acceptable differential between domestic rates and those in the external markets. As concerns about real rates dissipated and the general outlook for the economy improved, the Bank removed the 270-day and 365-day tenors from the spectrum of open market instruments on 18 April 2006. This was followed by the removal of the remaining Special Deposit requirement on 01 May 2006, which had been in effect since January 2003. Beginning 12 May 2006, the Bank reduced interest rates on its open market instruments on four occasions.

Consistent with the overall easing of monetary policy, market-determined interest rates generally declined during the year. There were also reductions in commercial bank deposit rates as well as building societies' mortgage rates. Commercial banks' average loan rates, however, rose marginally for the year.

There was a general acceleration in the growth of the monetary aggregates in 2006. The growth in the monetary base was higher than that for 2005, largely reflected in an increase of 18.7 per cent in currency issue, compared with 10.0 per cent in 2005. This acceleration occurred in the context of overall buoyancy in economic activity as well as the easing of monetary policy. The growth in the monetary base emanated from an increase in the Bank's net international reserves (NIR), the impact of which was partly offset by a decline in the net domestic assets (NDA) of the BOJ. The decline in the NDA reflected an increase in Government balances at the Bank as well as net placements on open market instruments.

Consistent with the acceleration in base money, broad money supply increased by 13.6 per cent in 2006, relative to an expansion of 8.6 per cent in 2005. With the exception of time deposits, all the components of broad money supply recorded accelerated growth rates. An increase in commercial bank credit to the private sector and a build-up in the net foreign assets of the BOJ were the main sources of the monetary expansion. The growth in private sector credit accelerated to 29.6 per cent in 2006 from 13.4 per cent in 2005, reflecting significantly faster growth in local currency loans and advances. The bulk of this expansion was related to personal loans but there was also increased lending to the major productive sectors of the economy, particularly **Distribution, Manufacturing** and **Construction**.

Other financial institutions also experienced significant loan growth in 2006. Loans and advances provided by the licensees under the Financial Institutions Act (FIA) experienced robust growth for the year. While there was an overall deceleration in the growth rate of mortgage loans provided by building societies, the expansion remained buoyant in 2006. Moreover, the number of new mortgage loans increased by 17.4 per cent during the review period, higher than the increase of 11.5 per cent for 2005. The continued growth in credit union membership during the year contributed to an increase of 21.6 per cent in loans for the year.

Facilitated by the expansion in credit within the economy as well as favourable weather conditions, real Gross Domestic Product (GDP) is estimated to have grown by 2.5 per cent for the year. This followed average growth of 1.3 per cent over the period 2000 - 2005. The expansion in the economy was reflected in both the goods producing and services sectors. The main areas of growth were **Agriculture, Forestry & Fishing** and **Miscellaneous Services** (particularly tourism). **Construction & Installation** and **Manufacturing**, however, declined. **Agriculture, Forestry & Fishing** grew significantly by 15.9 per cent in 2006 after two consecutive years of

significant declines and was the largest contributor to GDP growth. The expansion of the sector was attributable to favourable weather conditions throughout the year, but was also driven by improved labour productivity and increases in banking system credit. Value-added in **Miscellaneous Services** expanded significantly above trend in 2006 due to strong growth in the tourism industry. This was largely associated with significant expansions in both stopover and cruise ship arrivals. The growth of the tourism industry was facilitated by a notable increase in the number of hotel rooms, air carriers and new attractions, supported by aggressive promotions.

The contraction in **Construction & Installation**, which followed six consecutive years of moderate growth, was associated with a shortage of cement on the domestic market during the first three quarters of the year. For **Manufacturing**, the contraction was attributed to a significant decline in *Food, Beverages & Tobacco*, which offset moderate growth in *Other Manufacturing.*

The current account deficit (CAD) of the Balance of Payments is estimated to have widened by a marginal US$17.7 million to US$1 096.4 million in 2006. Relative to GDP, the current account deficit, however, improved to 10.3 per cent in 2006 from 11.1 per cent in 2005. Notably, the improvement relative to GDP occurred in spite of an increase in imports associated with a sharp jump in estimated foreign direct investments (FDI) flows for the year. In the context of the higher imports, the deterioration in the CAD largely reflected an increase in the merchandise trade deficit.

Expenditure on imports expanded by US$816.4 million in 2006, the largest annual increase on record. This growth was driven by significant increases in the importation of machinery & transport equipment, food, manufactured goods, mineral fuels and chemicals. The overall growth in imports largely reflected the impact of increases in the price of imported commodities, particularly oil. Crude oil prices, as measured by the West Texas Intermediate index, rose by 17.0 per cent in 2006, which followed the 36.2 per cent growth in 2005.

Export growth, which was largely driven by an expansion in receipts from alumina exports, partly offset the impact of the expansion in imports on the merchandise trade balance. The increase in earnings from alumina benefitted from growth of 16.8 per cent in the average realised price of the ore.

More than adequate financing for the current account deficit was provided by net private and official investment inflows. The NIR consequently increased by US$230.1 million to US$2 317.6 million at 31 December 2006, with gross reserves representing 17.9 weeks of imported goods and services.

Central Government operations generated a deficit equivalent to 5.5 per cent of GDP for the period April to December 2006, relative to the budgeted deficit of 4.2 per cent of GDP. The deviation from budget reflected a shortfall in revenue and grants as well as higher than budgeted expenditure. While revenue and grants were below budget, they exceeded the intake for the comparable period in 2005, reflecting normal growth in the tax base as well as an improvement in Government's collection efficiency. The deviation of revenues from budget, therefore, reflected lower than targetted receipts from the Accounts Receivable Conversion (ARC) Programme. Recurrent expenditure exceeded budget because of higher than planned spending on wages and salaries and interest payments on domestic debt.

The higher than budgetted deficit was mainly financed from the domestic market. Higher than programmed

net issue of domestic debt instruments over the period was partly offset by higher than budgetted net foreign amortization, the latter reflecting Government's pre-funding of its foreign debt obligations by the raising of a US$250.0 million Eurobond issued in the last quarter of F/Y 2005/06. Partly reflecting the impact of the Central Government debt raising, Jamaica's debt stock expanded by 9.3 per cent over the first nine months of the fiscal year. The debt stock at end December consequently was $925.8 billion, or 133.2 per cent of GDP, compared with 134.3 per cent at end March 2006.

All indicators of the health of the banking system remained strong in 2006. The system continued to maintain comfortable liquidity margins, with liquid assets ratios for domestic and foreign currencies remaining well above the required minimum. There were also further improvements in commercial banks' asset quality as non-performing loans, as a per cent of total loans, fell to 2.6 per cent at end-2006, compared with 2.9 per cent at end-2005. At year end, all licensees maintained primary and risk weighted capital ratios above the minimum requirements. Profit margins also remained strong, albeit marginally below the level for 2005.

In addition, the system remained resilient to shocks. The banking sector's exposure to foreign exchange risk declined in 2006, consequent on a reduction in the overall foreign currency net open position to capital. Similarly, the ratio of the dollar change in profits, to interest rates, an indicator of interest rate risk, remained relatively low during the year. The Bank's early warning system indicated a general improvement in risk relating to the macroeconomy, given the positive outturn for inflation.

As the Bank remained responsive to market developments and evolution of international standards, both on and off-site supervision of financial institutions continued to evolve in 2006. The **Standards of Best Practices for Credit Risk and Market Risk Management** was upgraded and a new overarching **Standard on Effective Corporate Governance and Risk Management** was well advanced at year-end. On-site examination also involved enhanced reviews of information systems infrastructure and disaster recovery and business continuity arrangements and an expanded scope of review of licensees' framework for anti-money laundering and counter-financing of terrorism (AML/CFT). The BOJ also made further revisions to its 2004 'Guidance Notes for the Prevention and Detection of Money Laundering and Terrorist Financing Activities' during the year.

In terms of legislative developments, the Minister of Finance and Planning, in April 2006, approved the granting of a commercial banking licence to Pan Caribbean Merchant Bank Limited (PCMB). The Minister also issued an Order under Section 2 of the Banking Act in August 2006, designating the sale, issue and distribution of 'stored value cards' as "banking business".

The BOJ continued the process of drafting and updating the Omnibus Bill in 2006. This bill seeks to consolidate the Banking Act, the Financial Institutions Act and the BOJ (Building Societies) Regulations, along with related subsidiary financial legislation. The Bank simultaneously promoted the reconfiguration of groups, of which deposit-taking entities are a part, to form financial structures that will facilitate effective monitoring and regulation by the BOJ.

In the continuous pursuit of enhancing the structure and operations of the institution, three Deputy Governors were appointed to the senior management of the Bank during the year. Their areas of appointment were the Finance & Technology, Payment Systems, Investment and Risk

Management Divisions, the Banking & Market Operations and Research and Economic Programming Divisions, and the Financial Institutions Supervisory Division. The Bank also settled a two-year wage agreement, which took effect on 01 April 2006, consistent with the guidelines of the second Memorandum of Understanding for Public Sector Entities and Statutory Bodies.

The Bank, in 2006, continued to fulfil its statutory obligation to meet currency requirements. In this context, two banknote sorters were acquired to replace those already in operation. The upgrade to the currency processing facilities is to enhance the Bank's capability to maintain its clean note policy and the counterfeit surveillance system. The new technology also strengthened internal controls by reducing the manual handling of banknotes during sorting.

An IMF team prepared an *Interim Staff Report Under Intensified Surveillance* in July 2006. In this report, the team recognised that the economy was making a gradual recovery from shocks and that progress was being made in reducing high debt, albeit at a slower pace than envisaged earlier. The findings of a Financial Sector Assessment Programme (FSAP), conducted in 2005, were also published in March 2006. The report noted that the financial system appeared well capitalized and supervision was considerably strengthened in recent years, although financial institutions continued to operate in a risky macroeconomic environment.

For 2007, the Bank is expecting the continuation of the favourable macroeconomic environment that characterised 2006. In particular, the maintenance of single digit inflation is programmed in 2007. Critical to this outcome are continued strong real sector performance to underpin foreign exchange market stability, continued fiscal consolidation and prudent monetary management by the Central Bank.

2. The Financial System

2.1. Monetary Policy Management

2.1.1. Introduction

In 2006, the Bank of Jamaica eased its policy stance on six occasions. This was against the background of favourable local macroeconomic conditions, supportive international developments and growing local and international investor confidence. Consequently, the Bank constrained core inflation to 3.4 per cent for the calendar year which underpinned a fall in headline inflation to 5.8 per cent. This was the lowest headline inflation outturn in 25 years.

2.1.2. Developments and Challenges

During the first quarter of 2006, the Bank held interest rates at levels in effect since May 2005. This was against a background of heightened inflation expectations which ensued from an acceleration in inflation in the final half of 2005. Over that period, inflation was affected by rising global oil prices as well as the impact on the real economy of three major hurricanes. This triggered concerns about real rates leading to instability in the foreign exchange market as investors increased their demand for instruments that provided a hedge against inflation.

The Bank resumed the easing of monetary policy in the second quarter of 2006. This was in a context where concerns for real rates had dissipated as macroeconomic indicators such as GDP growth and inflation steadily improved. This engendered stability in the foreign exchange market. These positive occurrences in the domestic economy were also supported by favourable international developments such as falling oil prices and the pause in US Fed rate hikes. In addition, the Government issued a 30-year bond on the international capital market, putting less upward pressure on domestic interest rates.

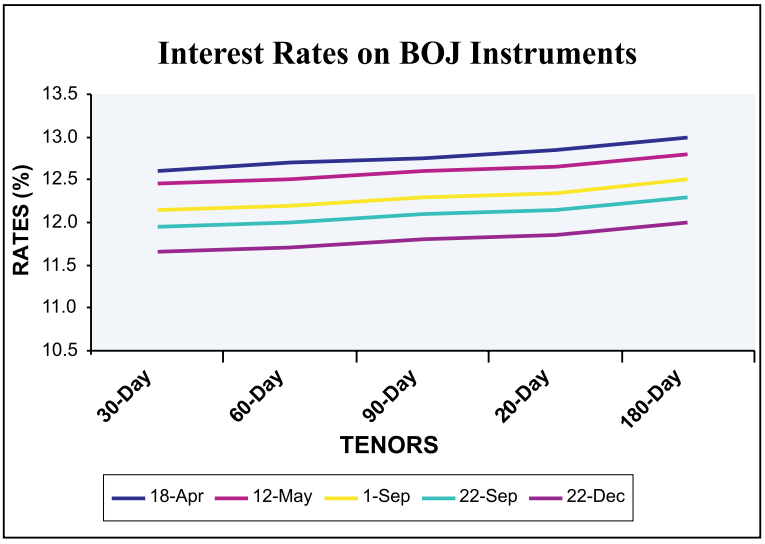
Interest rates on open market instruments were reduced on four occasions during the year. Prior to the resumption of interest rate reductions, the 270-day and 365-day tenors were removed from the spectrum of open market instruments on 18 April 2006, effectively shortening and further normalizing the yield curve. The Bank also removed the remaining 1.0 per cent Special Deposit requirement on 1 May 2006 which had been in effect since January 2003.

2.1.3. Base Money Management

The monetary base expanded by 17.3 per cent in 2006, compared to 9.7 per cent in 2005 and 11.7 per cent in the financial programme. The expansion emanated largely from a US$230.1 million increase in the Bank's net international reserves (NIR). This was partially offset by a decline in the net domestic assets (NDA) due to an increase in Government balances at the Bank and net placements on BOJ open market instruments. The expansion in the base was largely reflected in a net increase of 18.7 per cent in currency and an increase of 12.9 per cent in the local currency cash reserves of the commercial banks (see **Table 1B**). The deviation in the monetary base from programme was mainly due to a greater than anticipated increase in the NIR, largely attributed to strong inflows from tourism, remittances and private capital.

During the first quarter of the year, the monetary base contracted by 11.8 per cent, reflected mainly in net currency redemption following the high seasonal demand in the December 2005 holiday spending period. The ensuing liquidity was absorbed through open market operations as well as a build-up in Government accounts from debt raising in the domestic market. The build-up in the Government accounts also reflected the proceeds of a US$250 million bond which the Government issued on 28 February 2006. However, this did not have an impact on domestic liquidity as the funds were held

Chart 1:



in foreign currency and used to finance external debt payments.

In keeping with the improvements in the macro-environment in the first two quarters of the year, there was heightened demand for domestic assets especially during the third quarter. To this end, investors opted to sell the BOJ foreign currency to facilitate their participation in Government domestic debt offers. Consequently, the NIR increased by US$232.0 million in the September quarter.

The base expanded in the final quarter in keeping with the economic activities of the period. In the context of seasonal demand for notes and coins and foreign exchange, there was a net unwinding of OMO instruments. The expansion in the base was not deemed to be inflationary given that this occurred in tandem with increased demand in the economy. Additionally, a large portion of the increase was held in the vaults of commercial banks.

Table 1A

BANK OF JAMAICA - BASE MONEY TARGETS
STOCKS J$M
December 2006

	TARGET	OUT-TURN	DEVIATION FROM TARGET
Net International Reserves (US$)	2 043.8	2 317.6	273.8
NET INT'L RESERVES (J$)	136 096.6	153 862.1	17 765.5
NET DOMESTIC ASSETS	-80 879	-95 886.7	-15 007.7
MONETARY BASE	55 217.8	57 975.5	2 757.8

Table 1B

BANK OF JAMAICA - SUMMARY FLOWS J$M	2005 Total	2006 Jan - Mar	Apr - Jun	Jul - Sept	Oct - Dec	2006 Total
Net International Reserves (US$)	**228.9**	**-9.3**	**31.9**	**232.0**	**-24.5**	**230.1**
NET INT'L RESERVES (J$)	**14 191.8**	**-605.5**	**2 100.2**	**15 400.2**	**-1 623.9**	**15 271.0**
-Assets	17 800.8	1 3293.4	-5 244.8	12 051.4	-5 019.7	15 080.2
-Liabilities	-3 609.0	-13 898.8	7 345.0	3 348.7	3 395.8	190.8
NET DOMESTIC ASSETS	**-9 829.7**	**-5204.4**	**-757.4**	**-13 030.6**	**12 279.2**	**-6 713.2**
Net Claims on Public Sector	**5 130.9**	**2394.7**	**-40.3**	**-5 753.7**	**1 476.8**	**-1 922.5**
- Central Govt. Deposits	276.1	-18 254.1	308.1	-6 197.9	2 825.4	-21 318.6
- Govt. Securities	-3 796.1	-2 003.4	5 490.2	2 290.2	-385.2	5 391.8
- Other	8 650.8	22 651.9	-5 838.6	-1 846.0	-963.4	24 787.9
Net Credit to Banks	**4 207.1**	**-35.0**	**1583.9**	**-563.4**	**-417.5**	**568.1**
Open Market Operations	**-19 114.4**	**-7 551.1**	**-2 080.4**	**-6 580.9**	**11 261.9**	**-4 950.5**
Other	**-53.3**	**-13.0**	**-220.6**	**-132.6**	**-42.0**	**-408.3**
MONETARY BASE	**4 362.1**	**-5 809.9**	**1 342.8**	**2 369.6**	**10 655.3**	**8 557.8**
- Currency Issue	3 246.4	-5 930.1	1 020.0	1 408.9	10173.9	6 672.8
- Cash Reserve	809.6	559.4	408.0	814.7	-86.2	1 695.8
- Current Account	306.1	-439.2	-85.2	146.0	567.5	189.2
Memo:						
NIR Stock (US$MN) e.o.p.)	2 087.4	2 078.1	2 110.0	2 342.0	2 317.6	
Growth in Monetary Base (%)	9.7	-11.8	3.1	5.3	22.5	17.3
Inflation (%)	12.9	0.1	2.8	2.4	1.0	5.8

Table 2

BOJ OPEN MARKET OPERATIONS RATES (%) 2006	18 Apr	12 May	1 Sept	22 Sept	22 Dec
30-Day	12.60	12.45	12.15	11.95	11.65
60-Day	12.70	12.50	12.20	12.00	11.70
90-Day	12.75	12.60	12.30	12.10	11.80
120-Day	12.85	12.65	12.35	12.15	11.85
180-Day	13.00	12.80	12.50	12.30	12.00

Table 3

MONEY SUPPLY, M3* (DOMESTIC AND FOREIGN CURRENCY) (J$MN.)				
	COMPONENTS OF MONEY SUPPLY			
	2005 (J$M)	2006 (J$M)	2005 %	2006 %
Money Supply (M2)*	**16 889.0**	**28 655.1**	**8.0**	**12.6**
Money Supply (M1)*	**4 913.4**	**14 710.2**	**7.2**	**20.2**
Currency in Circulation	2 987.1	6 150.7	11.2	20.8
Demand Deposits	1 926.3	8 559.5	4.7	19.9
Quasi Money	**11 975.6**	**13 944.9**	**8.3**	**9.0**
Savings Deposits	8 233.6	12 905.6	7.7	11.1
Time Deposits	3 741.9	1 039.2	10.4	2.6
Other Deposits	4 799.4	8 462.8	11.9	18.7
Total Money Supply (M3)*	**21 688.4**	**37 117.8**	**8.6**	**13.6**
	SOURCES OF MONEY SUPPLY			
Net Foreign Assets	**1 894.8**	**8 664.8**	**1.7**	**15.6**
Bank of Jamaica	14 224.7	15 270.7	12.4	19.1
Commercial Banks	-12 329.9	-6 605.9	1346.1	49.9
Loans and Advances to Private Sector	**11 809.6**	**29 630.0**	**13.4**	**29.6**
Local Currency	5 970.5	23 941.1	10.5	38.0
Foreign Currency	5 839.0	5 688.9	18.6	15.3
Net Claims on Public Sector	**12 188.6**	**-11 521.1**	**6.8**	**-6.0**
Net Claims on Financial Institutions	**-424.7**	**767.7**	**4.2**	**-7.3**
BOJ Open Market Operations	**-19 114.4**	**-4 950.5**	**14.6**	**3.3**
Other Items (Net)	**15 334.5**	**14 267.8**	**141.3**	**19.7**
TOTAL	**21 688.4**	**37 117.8**	**8.6**	**13.6**

2.2. Money Supply

During 2006, broad money supply (M3*)[1] increased by 13.6 per cent from 8.6 per cent in 2005 (**see Table 3**). With the exception of time deposits, all the components of M3* reflected a faster rate of growth. The overall growth in M3* was influenced by increased economic activity.

Currency in circulation and demand deposits, (Narrow Money or M1*), increased by 20.2 per cent, relative to 7.2 per cent in 2005. Growth in currency in circulation accelerated to 20.8 per cent in 2006 from 11.2 per cent in 2005. Demand deposits grew by 19.9 per cent relative to an increase of 4.7 per cent in 2005. The acceleration reflected a 28.7 per cent increase in deposits denominated in local currency as there was continued reduction in the foreign currency component. The decline in the foreign currency component of demand deposits was consistent with the strong demand for Jamaica Dollars observed during the year.

Quasi money (Savings and Time deposits) grew by 9.0 per cent in 2006 relative to 8.3 per cent in 2005 (see **Table 3**). This outturn mainly reflected faster growth in both the local and foreign currency components of savings deposits, consistent with the improved macroeconomic environment. Time deposits grew, albeit at a slower rate.

During the review year, an increase in banking sector credit to the private sector and a build-up in the net foreign assets (NFA) of the BOJ were the main sources of monetary expansion. Growth in private sector credit, excluding private debentures, accelerated to 25.4 per cent in 2006 from 19.2 per cent in 2005. The significantly faster growth in loans and advances to the

1 M3* is defined as M2* plus Other Deposits. M2* represents banking system domestic and foreign currency liabilities to the private sector in the form of notes and coin as well as demand, time and saving deposits. Other deposits are largely comprised of commercial banks reserves.

private sector reflected acceleration in the use of local currency credit in the context of aggressive marketing of personal loans by commercial banks and increased lending to the **Manufacturing, Distribution** and **Construction & Land Development** sectors (**see Commercial Banks**). The increase in the NFA of the BOJ resulted mainly from net purchases of foreign currency from the market. The major countervailing influences on money supply were a net build-up in deposits by the public sector and a reduction in the net foreign assets of commercial banks. The build-up in deposits by the public sector reflected the proceeds from debt raising activities on the international capital markets and to a lesser extent the domestic market. The relatively stable foreign exchange market conditions which prevailed during the year influenced the reduction in the net foreign assets of commercial banks.

2.3. Commercial Banks

2.3.1. Overview

During 2006, the assets of the commercial banking sector grew at a faster rate than in 2005. This acceleration was largely reflected in a faster rate of growth in the banks' holdings of securities and cash & bank balances. There was also continued robust growth in loans and advances, albeit at a slower rate than in 2005. The faster rate of growth in assets was largely financed from local currency deposits which recorded a significant expansion, partly influenced by higher economic activity. During the year there was an improvement in the banks' asset quality, attributed to continued decline in past due loans.

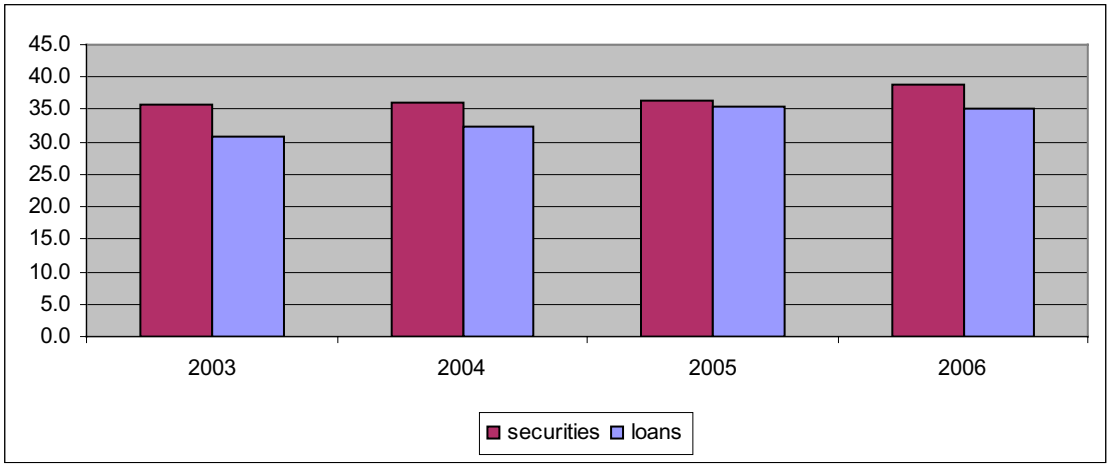
2.2.2. Assets and Liabilities

The commercial banking sector's asset base increased by 17.3 per cent in 2006, relative to an expansion of 6.7 per cent in 2005 and largely reflected growth in the holdings of securities (see **Table 4**). The faster rate of growth in the banks' holdings of securities[2] largely reflected a significant increase in the institutions' holdings of BOJ securities and foreign currency denominated securities. The institutions increased their holding of BOJ securities at lower rates of return in the context of Central Government's reduced demand for banking system loans in 2006. This lower demand for financing from the banking sector coupled with the narrowing of the interest rate differential between Jamaica Dollar and US dollar denominated assets influenced a build-up in the institutions' holdings of foreign currency securities. As a consequence, commercial banks' holdings of securities continued to dominate the institutions' asset portfolio, accounting for 38.8 per cent of total assets at end-December 2006, relative to 36.2 per cent at end-December 2005 (see **Chart 2**).

A relatively sharp increase in the institutions' cash & bank balances also contributed to the faster rate of growth in the sector's asset base. This expansion was mainly reflected in increased placements of foreign currency with overseas banks and was possibly for precautionary reasons, given a significant build-up in the sectors' liabilities denominated in foreign currency.

During 2006, growth in the banks' stock of loans (net of provisioning) slowed to 16.5 per cent from 17.2 per cent in 2005[3]. This deceleration was largely reflected in a slower rate of growth in foreign currency-denominated loans (see **Table 4**). Given this slowdown, the stock of loans as a proportion of total assets, reflected a marginal reduction to 35.3 per cent at end December 2006 from 35.5 per cent at end-December 2005 (see **Chart 3**).

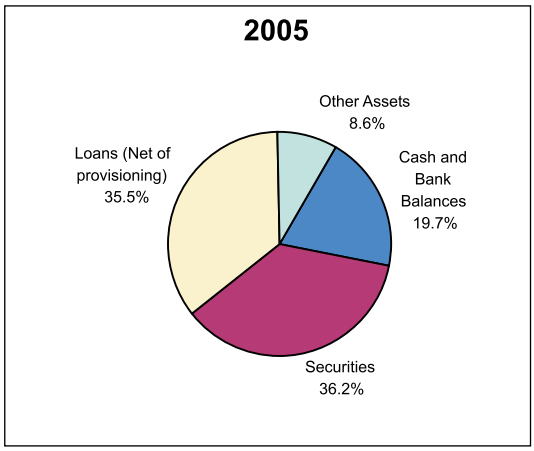
Chart 2: Loans and Securities as a Proportion of Total Commercial Banks' Assets



2 Total Securities = Investments + Securities Purchased for Resale

3 The stock of loans refers to gross loans net of International Financial Reporting Standards (IFRS) provisions for losses.

Chart 3: The Composition of Commercial Banks' Assets at 31 December 2005 and 31 December 2006



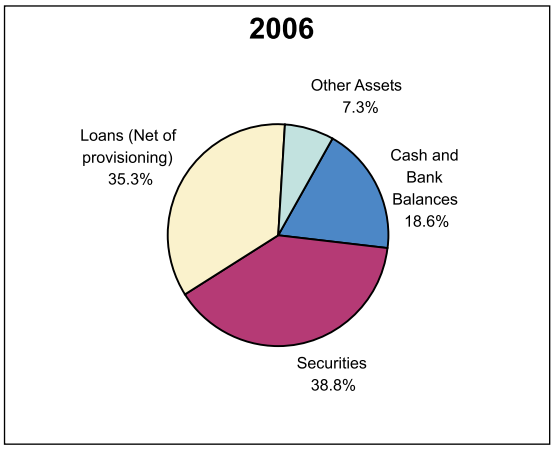


Table 4

COMMERCIAL BANKS
SUMMARY OF ASSETS AND LIABILITIES
(J$MN)

	Stock 2006	Flows 2004	Flows 2005	Flows 2006	% 2004	% 2005	% 2006
ASSETS (1)	**427 098.9**	**31 637.8**	**22 944.7**	**62 876.2**	**10.2**	**6.7**	**17.3**
Cash and Bank Balances	79 543.9	3 419.4	-6 557.2	7 759.1	4.6	-8.4	10.8
Placements with Overseas Banks	*34 781.6*	10 026.4	-2 682.3	5 083.0	44.9	-8.3	17.1
Investments	158 733.0	10 810.1	10 522.5	31 471.6	10.2	9.0	24.7
-Domestic Currency	106 103.2	8 259.4	5 021.7	15 160.8	10.6	5.8	16.7
BOJ securities	42 099.0	11 341.0	6 511.8	11 603.2	89.7	27.2	38.0
Jamaica Government Securities	57 370.4	-17 859.7	223.2	2 506.5	-24.6	0.4	4.6
Other Public Sector	820.8	-542.1	-555.6	-433.3	-23.1	-30.7	-34.5
Other Local	5 813.0	2 677.1	-1 157.7	1 484.4	95.3	-21.1	34.3
-Foreign Currency	52 629.8	2 550.7	5 500.8	16 310.8	9.0	17.8	44.9
o.w. Ja. Gov. Foreign Securities	*41 778.5*	2 091.0	4 334.3	7 921.6	7.6	14.7	23.4
Securities Purchased for resale	7 180.9	797.3	-1 227.6	2 448.2	15.4	-20.6	51.7
Loans (Net of provisioning)	150 578.9	14 994.6	18 971.7	21 338.9	15.7	17.2	16.5
Domestic	92 057.9	5 884.8	9 266.4	14 939.0	9.5	13.7	19.4
Foreign	61 391.2	8 334.1	9 460.1	6 414.8	22.4	20.8	11.7
Accounts Receivable	6 509.2	-854.7	1 458.1	-523.6	-13.3	26.2	-7.4
Fixed Assets	8 055.9	467.9	176.8	333.0	6.6	2.3	4.3
Other Assets	16 497.1	2 003.2	-0 399.7	0 049.1	13.5	-2.4	0.3
LIABILITIES & CAPITAL	**427 098.9**	**31 637.8**	**22 944.6**	**62 876.2**	**10.2**	**6.7**	**17.3**
Deposits	282 925.5	29 415.7	18 074.4	36 660.6	14.8	7.9	14.9
Domestic	175 855.3	16 539.2	9 363.0	26 976.9	13.4	6.7	18.1
Foreign	107 070.3	12 876.5	8 711.4	9 683.8	17.0	9.8	9.9
Due to Bank of Jamaica	182.6	62.2	4.5	-51.9	37.1	2.0	-22.1
Due to Commercial banks	38 591.8	11 462.7	3 885.4	11 600.3	98.4	16.8	43.0
Overseas banks	*31 197.3*	8 434.1	675.2	10 577.9	73.3	3.4	51.3
Due to Specialised Institutions	4 211.4	-5 039.1	94.9	286.4	-56.8	2.5	7.3
Securities sold under Repurchase Agreements	13 132.2	-15 317.6	-5 808.7	-3 397.7	-40.7	-26.0	-20.6
Other Liabilities	36 141.3	4 265.2	3 046.8	10 783.2	23.6	13.7	42.5
Capital Account	51 914.1	6 788.7	3 647.3	6 995.2	19.7	8.8	15.6

(1) Assets exclude contingent accounts
Data account for provisioning
Investments and Cash and Bank Balances adjusted to reflect reclassification of
Certificates of Deposits from "other accounts designated as liquid" to BOJ securities

The expansion in the banks' asset base was financed largely from deposits (see **Table 4**). In the context of relatively stable foreign exchange market conditions, increased borrowings from overseas banks also contributed to the financing. The acceleration in the growth of deposits was reflected in a build-up in deposits held by both the private and public sectors (see **Table 5)**. Expansion in these deposits was partly influenced by increased economic activity and a reduction in unemployment. The significant increase in public sector deposits was largely reflected in time deposits held by Other Public Sector Entities and demand deposits held by Central Government.

There was continued slowdown in the growth in foreign currency private sector deposits, reflecting the relatively stable foreign exchange market conditions that prevailed during most of 2006 (see **Table 6**). As a consequence, there was a decline in the ratio of foreign currency private sector deposits to total private sector deposit liabilities. This ratio declined to 27.3 per cent at end-2006 from 30.0 per cent at end-2005 and was the lowest since the 26.5 per cent recorded in January 2003.

Table 5

COMMERCIAL BANKS
TOTAL DEPOSITS
(J$M)

	Stocks 2006	Flows 2004	Flows 2005	Flows 2006	% 2004	% 2005	% 2006
Deposits	284 879.8	30 310.9	17 412.8	38 156.9	14.8	7.6	15.5
Private Sector	221 194.9	24 816.6	13 901.9	22 504.4	15.5	7.5	11.3
Demand /1	51 665.6	9 087.7	1 926.4	8 559.5	28.3	4.7	19.9
Savings	128 700.3	11 662.3	8 233.6	12 905.7	12.2	7.7	11.1
Time	40 829.0	4 066.6	3 741.9	1 039.2	12.7	10.4	2.6
Public Sector	36 166.9	4 012.7	-1 182.0	14 514.0	21.3	-5.2	67.0
Other	27 518.0	1 481.6	4 692.9	1 138.4	7.3	21.6	4.3

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

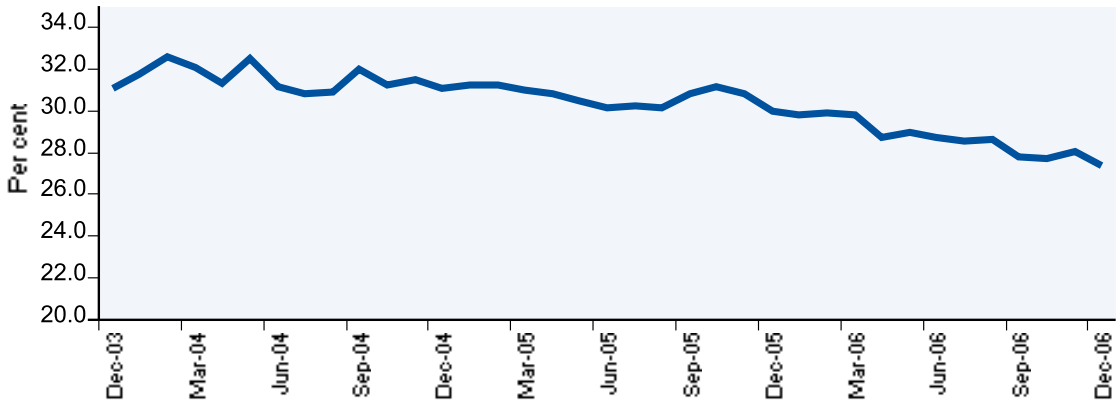
Table 6

COMMERCIAL BANKS
LOCAL AND FOREIGN CURRENCY DEPOSITS /1
(PRIVATE SECTOR)
(J$M)

	Stocks 2006	Flows 2004	Flows 2005	Flows 2006	% 2004	% 2005	% 2006
Private Sector Deposits	221 194.9	24 816.6	13 901.9	22 504.4	15.5	7.5	11.3
Local Currency	146 012.1	14 951.4	10 721.8	20 394.2	15.0	9.3	16.2
Foreign Currency	75 182.8	9 865.2	3 180.1	2 110.2	16.4	4.5	2.9

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

Chart 4: Foreign Currency Deposits to Total Deposits
December 2003 to 2006



2.3.3. Loans and Advances

The stock of commercial bank loans and advances at end-December 2006 reflected a slower rate of increase of 15.9 per cent, relative to an expansion of 16.7 per cent in 2005 (see **Table 7**). This slower rate of growth largely reflected significant reduction in commercial bank loans to the public sector. In real terms, however, the growth in loans and advances accelerated to 6.7 per cent in 2006, compared to 1.0 per cent in 2005. The growth in loans and advances was in the context of further investment in the real economy, particularly in **Manufacturing**, **Distribution** and **Construction & Land Development**. The stock of loans outstanding to the private sector continued to dominate the commercial banks' loan portfolio, accounting for 80.9 per cent at end-December 2006, compared to 74.7 per cent at end-December 2005.

The commercial banks' private sector loan portfolio **(excluding debentures)** grew by 25.4 per cent in 2006, relative to an increase of 19.2 per cent in 2005. The growth in 2006 was primarily reflected in **Personal Loans, Distribution** and **Manufacturing**. The expansion in **Personal Loans** continued to reflect aggressive marketing by the banks. The higher growth in loans to **Distribution** was mainly influenced by a large loan.

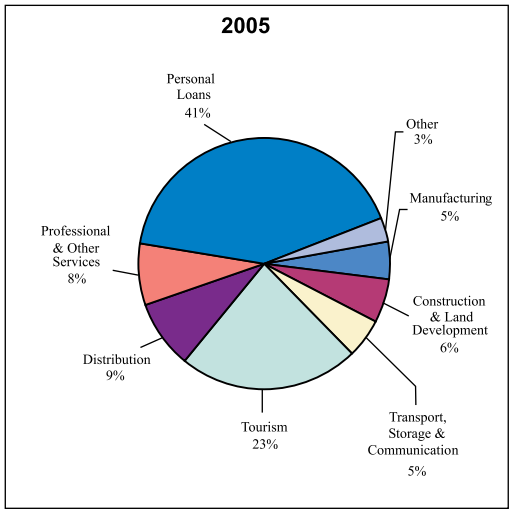
Table 7

COMMERCIAL BANKS
TOTAL LOANS AND ADVANCES
(J$MN)

	Stocks 2005	Stocks 2006	Flows 2004	Flows 2005	Flows 2006	% 2004	% 2005	% 2006
Public Sector	**32 551.1**	**27 937.2**	**2 299.0**	**2 740.6**	**-4 613.9**	**8.4**	**9.2**	**-14.2**
Other Financial Institutions	**871.5**	**1430.4**	**157.7**	**282.8**	**558.9**	**36.6**	**48.0**	**64.1**
Private Sector*	**98 930.2**	**124 081.6**	**11 762.2**	**15 960.6**	**25 151.3**	**16.5**	**19.2**	**25.4**
Agriculture and Fishing	1 831.6	2 298.4	-194.1	604.1	466.8	-13.7	49.2	25.5
Mining and Quarrying	253.0	643.5	-185.0	29.6	390.5	-45.3	13.2	154.3
Manufacturing	4 678.0	7 534.6	283.6	931.6	2856.5	8.2	24.9	61.1
Construction & Land Development	5 512.3	8 045.5	695.0	-363.4	2533.2	13.4	-6.2	46.0
Transport, Storage & Communication	5 209.2	3 705.8	-803.3	-3 524.4	-1 503.5	-8.4	-40.4	-28.9
Tourism	22 917.7	24 282.3	3 833.3	7 175.9	1 364.6	32.2	45.6	6.0
Distribution	8 651.0	11 900.4	-496.6	1 897.2	3 249.5	-6.8	28.1	37.6
Professional & Other Services	7 680.8	9 237.2	1 012.8	1 485.9	1 556.4	19.5	24.0	20.3
Personal Loans	41 159.7	55 916.7	7 514.7	7 729.9	14 757.0	29.0	23.1	35.9
Electricity, Gas & Water	746.3	190.1	-15.9	-23.3	-556.2	-2.0	-3.0	-74.5
Entertainment	274.1	291.2	137.4	33.1	17.1	132.5	13.7	6.2
Overseas Residents	16.4	35.9	-19.8	-15.5	19.5	-38.3	-48.6	118.8
TOTAL	**132 352.9**	**153 449.2**	**14 218.8**	**18 984.0**	**21 096.3**	**14.3**	**16.7**	**15.9**

Loans to **Construction & Land Development** recorded strong growth consistent with increased investment spending in the sector, following the shortage of cement. **Personal Loans, Tourism, Distribution** and **Professional & Other Services** continued to dominate the share of private sector loans outstanding, increasing marginally to 81.7 per cent as at 31 December 2006, relative to 81.3 per cent at end December 2005 (see **Chart 5**).

Chart 5: Distribution of Private Sector Loans and Advances at 31 December 2005 and 31 December 2006



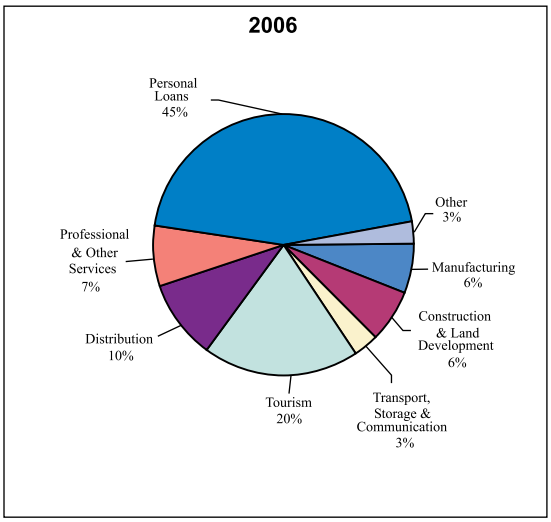


Table 8

COMMERCIAL BANKS FOREIGN CURRENCY LOANS AND ADVANCES (US$000)								
	Stocks 2005	Stocks 2006	Flows 2004	Flows 2005	Flows 2006	% 2004	% 2005	% 2006
Public Sector	**245 927**	**234 068**	**40 978**	**54 021**	**-11 859**	**27.2**	**28.1**	**-4.8**
Other Financial Instituions	**12 480**	**17 320**	**3 496**	**4 206**	**4 840**	**73.2**	**50.8**	**38.8**
Private Sector*	**599 331**	**664 729**	**79 083**	**59 518**	**65 398**	**17.2**	**11.0**	**10.9**
Agriculture	4 185	5 960	-589	3 315	1 775	-40.4	381.0	42.4
Mining & Quarrying	14	5 178	-4 689	14	5164	-100.0	100.0	101.0
Manufacturing	24 495	57 086	10 195	-4 042	32 591	55.6	-14.2	133.1
Const., & Land Development	40 518	57 373	-4 383	4 909	16 855	-11.0	13.8	41.6
Transport, Storage & Comm.	35 181	32 957	8 802	-86 869	-2 224	7.8	-71.2	-6.3
Electricity, Gas & Water	10 018	15	-46	-281	-10003	-0.4	-2.7	-99.9
Distribution	54 268	52 203	11 559	23 167	-2 065	59.1	74.5	-3.8
Tourism	345 770	348 368	35 308	113 135	2 598	17.9	48.6	0.8
Entertainment	1 911	01 650	1 602	110	-261	805.0	6.1	-13.7
Professional & Other Services	36 456	42 072	15 793	4 467	5 616	97.5	14.0	15.4
Personal Loans	46 515	61 813	5 531	1 593	15 298	14.0	3.5	32.9
Loans to Overseas Residents	0	54	0	0	54	0.0	0.0	1.0
TOTAL	**857 738**	**916 117**	**123 557**	**117 745**	**58 379**	**20.0**	**15.9**	**6.8**

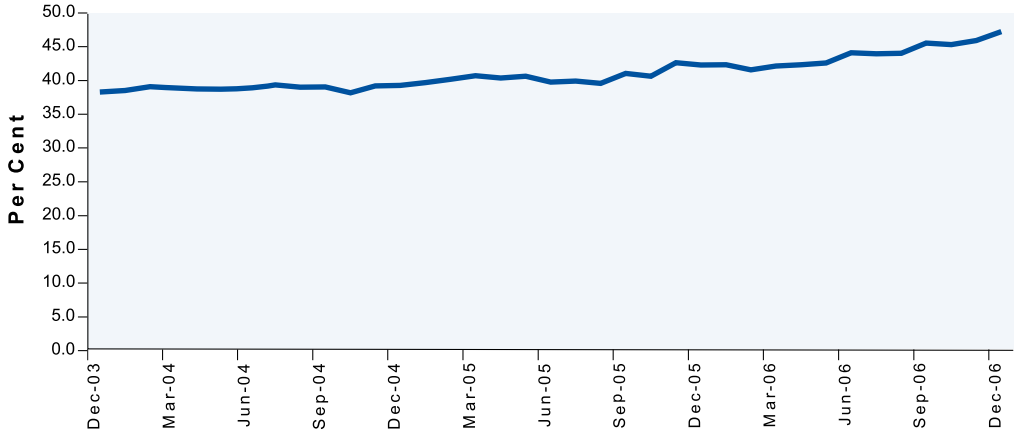
**Private sector loans excluding debentures*

Loans and advances denominated in foreign currency grew at a slower rate of 6.8 per cent in 2006. This deceleration was influenced by a reduction in foreign currency loans to the public sector as foreign currency loans to the private sector grew by 10.9 per cent, in line with the outturn for 2005. The growth in foreign currency loans to the private sector largely reflected an expansion in loans to **Manufacturing**; **Construction & Land Development** and **Personal Loans** (see **Table 8**). There was continued growth in foreign currency loans to **Tourism,** albeit at a slower rate. This deceleration reflected the repayment of loans previously obtained by hotels. Significant net repayments were reflected within **Electricity, Gas & Water** and **Transport, Storage & Communication**. The proportion of foreign currency loans to total loans and advances decreased to 40.0 per cent at end-December 2006 from 41.6 per cent at end-December 2005.

The ratio of non-performing loans to total loans declined marginally to 2.2 per cent at end-December 2006, from 2.3 per cent at end December 2005[4]. The ratio of commercial banks' loans to deposits increased to 47.2 per cent at end-December 2006, from 42.3 per cent at end-December 2005 (see **Chart 6**).

4 Non-performing loans are classified as loans past due for three months and over. The international maximum benchmark for non-performing loans is 10.0 per cent.

Chart 6: Commercial Bank Advance to Deposits Ratio
December 2003 to December 2006



2.3.4. Liquid Assets

Total liquid assets of the commercial banks increased by $17 100.0 million or 30.3 per cent in 2006[5]. As a consequence, there was an increase in the ratio of average liquid assets to prescribed liabilities to 42.3 per cent at end-December 2006 from 38.4 per cent at end-December 2005. The increase in this ratio largely reflected higher holdings of BOJ open market instruments (see **Table 9**). With the increased holdings of securities, the banks' excess reserves increased to $31 700.0 million at end-December 2006 from $23 100.0 million at end-December 2005.

5 In 2006, the statutory cash reserve and liquid asset requirements for commercial banks remained unchanged at 9.0 per cent and 23.0 per cent, respectively.

Table 9

COMMERCIAL BANKS LIQUID ASSETS						
	2004	2005		2006		
	Dec	Dec	Mar	Jun	Sep	Dec
Statutory Liquidity (%)						
Cash Reserve Ratio	9.0	9.0	9.0	9.0	9.0	9.0
Liquid Assets Ratio	23.0	23.0	23.0	23.0	23.0	23.0
Average Liquid Assets Holdings (%)	38.4	38.4	41.0	43.9	43.8	42.3
Liquid Assets (J$BN)						
Notes and Coins	5.8	6.0	3.5	3.3	3.7	6.5
Current Account	0.4	1.1	0.4	0.2	0.3	1.3
Cash Reserve	12.3	13.1	13.7	14.1	14.9	14.8
Treasury Bills	1.0	1.0	1.1	1.3	1.6	1.2
Local Registered Stocks*	3.1	0.2	4.4	3.8	3.9	1.2
Other Government Securities	1.0	4.1	3.5	1.6	0.9	1.3
BOJ Open Market Instruments	29.0	31.1	40.1	48.0	52.1	47.5
Total	52.6	56.7	66.7	72.3	77.3	73.8
Prescribed Liabilities (J$BN)	136.8	145.8	152.1	156.6	165.6	164.7
Excess Reserves	21.1	23.1	28.2	32.8	34.4	31.7

**Net of securities pledged as collateral*

2.3.5. Interest Rates and Spreads

For 2006, there were reductions in the rates of return on commercial banks' deposits and rates in the money market, consistent with the easing of monetary policy (see **Table 10**). However, there was an increase in commercial banks' overall average loan rate. Accordingly, there was a widening of the overall spread by 61 basis points (see **Table 10**). The widening in the overall spread was reflected in an increase in the spread on loans extended to other public sector entities, influenced by an increased demand for loans by these institutions (see **Table 11**). There was also a sharp decline in the spread on mortgage loans.

Table 10

INTEREST RATES IN THE DOMESTIC MARKET (End of Period)	2004 Dec	2005 Dec	2006 Mar	Jun	Sep	Dec
COMMERCIAL BANKS						
INTEREST RATE SPREAD	**11.68**	**11.96**	**12.16**	**12.25**	**12.60**	**12.57**
Overall Average Weighted Loan Rate	**17.72**	**17.32**	**17.54**	**17.60**	**17.83**	**17.59**
Foreign Currency Average Weighted Loan Rate	**9.13**	**9.50**	**9.69**	**9.77**	**9.78**	**9.76**
Overall Average Weighted Deposit Rate	**6.04**	**5.36**	**5.38**	**5.35**	**5.23**	**5.02**
Demand	3.31	3.23	2.99	2.87	2.79	2.86
Savings	5.71	4.87	4.87	4.82	4.75	4.64
Time	7.78	7.00	7.17	7.17	6.88	6.60
Certificates of Deposit						
1-month	7.71	6.58	6.95	7.65	6.75	6.36
3-month	8.45	7.42	7.49	7.37	7.21	6.98
12-month	7.17	7.05	7.35	6.77	6.79	6.71
Foreign Currency Average Weighted Deposit Rate	**3.32**	**3.29**	**3.25**	**3.22**	**3.29**	**3.26**
Demand	3.27	3.07	2.96	2.76	2.67	2.28
Savings	2.27	2.21	2.28	2.27	2.21	2.21
Time	5.27	5.12	5.01	5.02	5.12	5.01
GOJ 6-MONTH TREASURY BILL RATE	**14.94**	**13.55**	**13.18**	**12.82**	**12.49**	**12.31**
BOJ 180-DAY REPURCHASE AGREEMENT RATE	**14.30**	**13.00**	**13.00**	**12.80**	**12.30**	**12.00**
PRIVATE MONEY MARKET RATE	**14.10**	**13.75**	**13.35**	**12.70**	**12.40**	**11.85**

Table 11

COMMERCIAL BANK INTEREST RATE SPREADS (BY SECTOR)	2004 Dec	2005 Dec	2006 Mar	Jun	Sep	Dec
OVERALL AVERAGE WEIGHTED LOAN RATE	**17.72**	**17.32**	**17.54**	**17.60**	**17.83**	**17.59**
OVERALL AVERAGE WEIGHTED DEPOSIT RATE	**6.04**	**5.36**	**5.38**	**5.35**	**5.23**	**5.02**
OVERALL SPREAD	**11.68**	**11.96**	**12.16**	**12.25**	**12.60**	**12.57**
Installment Credit	17.82	17.89	17.33	16.82	16.08	16.63
Mortgage	14.12	15.03	19.56	19.92	20.29	8.07
Personal	24.15	23.80	23.73	23.92	23.85	22.62
Commercial	8.09	8.70	8.44	8.50	8.63	8.34
Central Government	12.23	11.27	10.92	10.84	10.72	8.81
Other Public Sector	5.59	6.27	6.37	6.69	6.91	7.10

2.4. Other Financial Intermediaries

1.1.1. Financial Institutions Act Licensees (FIAs)

The asset base of the FIA licensees recorded marginal growth in 2006, following a sharp decline in 2005[6]. There was robust growth in loans and advances, securities purchased with a view to resale as well as cash and bank balances in commercial banks.

However, these increases were partly offset by a decline in the institutions' holdings of securities. The FIAs continued to hold a high level of foreign currency assets in their portfolio. The expansion in the asset base was facilitated by an increase in deposits and, to a lesser extent, an increase in the capital base, primarily of one institution.

Table 12

ASSETS AND LIABILITIES OF FIAs (J$M)

	Stock December 2006*	Flows 2005	Flows 2006	% Change 2005	% Change 2006
Assets (1)					
Cash and Bank Balances with Commercial Banks	2 080.2	-803.6	241.5	-30.4	13.1
Balances with Other Financial Institutions	6.2	0.5	0.5	10.2	8.3
Balances with Bank of Jamaica	759.2	-208.7	224.2	-28.1	41.9
Investments	26 898.3	-6 471.5	-2 679.8	-18.0	-9.1
Securities Purchased a with View to Resale	3 060.0	92.3	564.3	3.8	22.6
Loans & Advances (net of provision)	11 098.0	1 273.2	2 476.3	17.3	28.7
Accounts Receivable	1 545.8	-317.9	555.7	-24.3	56.1
Other Assets	460.7	476.1	48.1	749.5	11.7
TOTAL	**45 908.3**	**-5 959.6**	**1 430.9**	**-11.8**	**3.2**
Liabilities and Capital					
Deposits	14 017.0	703.6	1 877.1	6.2	15.5
Balances due to Commercial Banks	854.5	-133.9	39.2	-14.1	4.8
Balances due to Specialised Institutions	305.3	40.9	-31.7	13.8	-9.4
Borrowings from Other Financial Institutions	1 663.0	-21 315.3	26.7	-92.9	1.6
Securities sold under Repurchase Agreements	19 812.0	13 751.6	-1 894.1	172.9	-8.7
Other Liabilities	1061.5	-329.4	331.2	-31.1	45.3
Capital & Reserves	8 195.1	1 323.0	1 082.6	22.9	15.2
TOTAL	**45 908.3**	**-5 959.6**	**1 430.9**	**-11.8**	**3.2**
Memorandum Items					
Foreign Currency Assets	29 849.0	-6 566.5	34.0	-18.0	0.1
Foreign Currency Liabilities	14 193.3	-21 205.1	1 290.2	-62.2	10.0

(1) Assets exclude contingent accounts

** Provisional Data*

6 Includes Merchant Banks and Trust Companies.

2.4.1.1. Assets & Liabilities

At end-December 2006, the assets of the FIAs totalled $45 908.3 million, reflecting an expansion of 3.2 per cent for the calendar year, compared to a decline of 11.8 per cent in 2005. This growth was largely reflected in **Loans & Advances (net of provision)** which increased by 28.7 per cent, significantly above the expansion of 17.3 per cent recorded during 2005. Consequently, the loans to asset ratio increased to 24.2 per cent at end-December 2006 from 19.4 per cent at end 2005, reflecting the continued realignment of the institutions' asset portfolio towards loans. This expansion in loans primarily reflected an increase in domestic currency loans, which was in sharp contrast to the previous year, when the majority was foreign currency loans. **Securities Purchased with a View to Resale** and **Accounts Receivable** also recorded strong growth during the calendar year.

The impact of the expansion in loans of the FIAs was significantly offset by a 9.1 per cent decline in the entities' holdings of investments. The reduction during 2006 largely reflected declines in the entities' holdings of both domestic and foreign currency denominated Government of Jamaica (GOJ) securities. Consequently, investment holdings accounted for 58.6 per cent of the asset portfolio at end-December 2006, a lower proportion than the 66.5 per cent recorded a year earlier.

The foreign currency assets of the entities remained relatively flat during the review year, relative to a decline of 18.0 per cent in 2005. Consequently, the ratio of foreign currency assets to total assets fell to 65.0 per cent at end 2006 from 67.0 per cent at end 2005.

Continued growth in deposits was the main source of funding for the increase in total assets of the FIAs. Deposits expanded by 15.5 per cent during the review year compared with an increase of 6.2 per cent during 2005. This growth continued to primarily reflect an increase in foreign currency deposits.

The FIAs' capital base grew by 15.2 per cent in 2006 relative to growth of 22.9 per cent during 2005, reflecting expansions in paid-up and assigned ordinary shares, retained earnings and revaluation reserves (see **Table 12**). The growth in the capital base during 2006 largely emanated from adjustments made by one institution.

2.4.1.2. Sectoral Distribution of Loans

Loans extended by the FIAs to the private sector recorded buoyant growth of 31.7 per cent during 2006 relative to an expansion of 36.9 per cent during 2005. Consequently, the share of private sector loans to total loans increased to 96.7 per cent at end December 2006 (see **Table 13**). There was a continued decline in the proportion of public sector loans, largely driven by net repayments of loans from Government entities during the review period.

Table 13

SECTORAL DISTRIBUTION OF LOANS AND ADVANCES OF INSTITUTIONS LICENCED UNDER THE FINANCIAL INSTITUTIONS ACT (J$M)

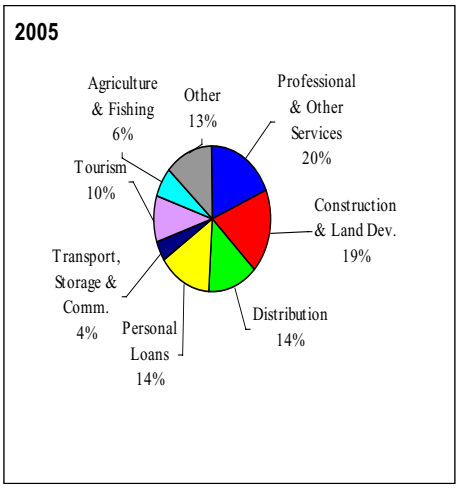
	2005 Stock	Share of Total (%)	Annual Change in Stock	2006* Stock	Share of Total (%)	Annual Change in Stock
Public Sector	**475.7**	**5.5**	**-208.3**	**360.0**	**3.2**	**-115.8**
Financial Institutions	**9.4**	**0.1**	**-180.8**	**10.5**	**0.1**	**1.1**
Private Sector	**8 185.2**	**94.4**	**2 206.7**	**10 776.3**	**96.7**	**2 591.1**
Agriculture & Fishing	531.0	6.1	215.5	1037.0	9.3	506.0
Mining & Quarrying	27.5	0.3	7.1	19.9	0.2	-7.6
Manufacturing	474.8	5.5	205.5	423.5	3.8	-51.2
Construction & Land Development	1 489.2	17.2	223.2	1 663.9	14.9	174.7
Transport, Storage & Communication	361.3	4.2	-66.6	609.2	5.5	247.9
Tourism	847.2	9.8	511.6	995.8	8.9	148.6
Distribution	1 132.2	13.1	211.2	1 874.6	16.8	742.5
Professional & Other Services	1 548.8	17.9	27.4	1 324.8	11.9	-224.0
Personal Loans	1 174.6	13.5	524.4	1 984.3	17.8	809.7
Electricity, Gas and Water	177.3	2.0	1.0	10.2	0.1	-167.1
Entertainment	71.8	0.8	2.9	106.3	1.0	34.5
Overseas Residents	349.6	4.0	343.6	726.7	6.5	377.1
TOTAL	**8 670.3**	**100.0**	**1 817.7**	**11 146.7**	**100.0**	**2 476.5**

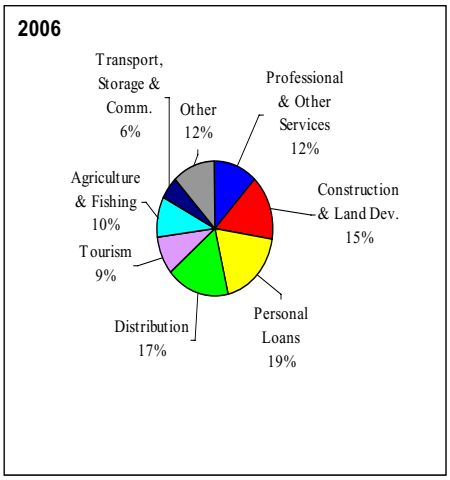
** Provisional*

Totals include provisions for loan losses

Similar to the commercial banks, **Personal Loans** continued to account for the largest proportion of the increase in credit, consistent with the aggressive marketing of these loans by the institutions. Loans to **Distribution** and **Agriculture & Fishing** also recorded buoyant growth during the review year. With the exception of loans to **Professional & Other Services**, **Electricity, Gas & Water**, **Manufacturing** and **Mining & Quarrying**, all other categories of loans recorded increases in credit during 2006 (see **Table 13**).

Chart 7: Distribution of Private Sector Loans and Advances





Consistent with the rapid growth in **Personal Loans** during 2006, there was a significant increase in its share of total loans. There were also increases in the share of outstanding loans to **Distribution, Agriculture & Fishing** and **Transport, Storage and Communication** while all other loan categories declined during the review year (see **Chart 7**).

There was an improvement in the quality of the FIAs' loan portfolio during the review period as evidenced by a decline in the ratio of past due loans (over three months) to total loans to 4.4 per cent at end-2006 from 5.0 per cent at end-2005[7].

2.4.2. Building Societies

The assets of the building societies grew at a significantly faster rate during 2006 than in 2005. This expansion was largely reflected in a faster rate of growth in the institutions' holdings of investments. Mortgage loans remained buoyant, although there was a deceleration in the growth rate. The faster rate of growth in assets was largely facilitated by higher rates of increases in savings fund, borrowings from specialized institutions and the entities' capital base.

Table 14

ASSETS AND LIABILITIES OF BUILDING SOCIETIES (J$M)

	STOCK December 2005	STOCK December 2006	FLOW Annual Change 2005	FLOW Annual Change 2006	Per Cent Change 2005	Per Cent Change 2006
ASSETS						
Cash and Balances with Commercial Banks	12 009.8	13 783.0	990.7	1 773.1	9.0	14.8
Balances with Other Financial Institutions	1.0	1517.4	1.0	1 516.4	0.0	151 636.8
Balances with Bank of Jamaica	1 373.6	1 609.6	107.1	236.0	8.5	17.2
Investments (net of provision)	20 270.4	23 689.6	1 566.8	3 419.1	8.4	16.9
Securities Purchased with View to Resale	14 431.8	14 248.2	-462.8	-183.6	-3.1	-1.3
Loans and Advances (net of provision)	35 865.4	43 380.1	7 169.5	7 514.7	25.0	21.0
- of which Mortgages	35 054.3	42 357.5	6 960.5	7 303.2	24.8	20.8
Accounts Receivables	2 626.2	4 264.3	-684.2	1 638.1	-20.7	62.4
Fixed Assets	1 960.2	2 142.3	134.5	182.1	7.4	9.3
Other Assets	728.5	914.6	105.4	186.1	16.9	25.5
TOTAL	**89 267.1**	**105 549.1**	**8 927.9**	**16 281.9**	**11.1**	**18.2**
LIABILITIES and CAPITAL						
Savings Fund	64 076.2	73 585.1	5 284.4	9 508.9	9.0	14.8
Due to Bank of Jamaica	0.0	0.0	0.0	0.0	0.0	0.0
Due to Commercial Banks	1659.0	2864.1	821.1	1 205.1	98.0	72.6
Due to Specialized Institutions	3 284.3	6 054.4	1 420.5	2 770.1	76.2	84.3
Due to Other Financial Institutions	1418.4	1563.0	768.6	144.6	118.3	10.2
Securities Sold Under Repurchase Agreement	0.0	0.0	0.0	0.0	0.0	0.0
Other Liabilities	2 463.2	2 906.1	-328.1	442.9	-11.8	18.0
Capital and Reserves	16 366.1	18 576.4	961.3	2 210.3	6.2	13.5
TOTAL	**89 267.1**	**105 549.1**	**8 927.9**	**16 281.9**	**11.1**	**18.2**
INDICATIVE RATIOS (Per Cent)						
Liquid Assets : Total Assets	12.9	12.7				
Liquid Assets : Savings Fund	17.9	18.3				
Advance : Savings Fund	57.0	59.8				
Mortgage Loans : Savings Fund	54.6	57.6				

7 This compares to the international benchmark of 10.0 per cent.

At end-2006, the total assets of the building societies amounted to $105 549.1 million, reflecting acceleration in the growth of assets to 18.2 per cent from 11.1 per cent in the previous year. The faster rate of growth in the asset base during the review year was mainly reflected in a significant expansion of 16.9 per cent in the institutions' holdings of investments relative to the increase of 8.4 per cent increase for 2005. This acceleration was predominantly reflected in their holdings of domestic currency GOJ securities as well as debentures and investment shares. There was also an increase in the institutions' holdings of foreign currency denominated securities issued by Governments and institutions.

There was continued strong growth of 20.8 per cent in loans and advances in 2006, albeit slower than the 24.8 per cent in 2005. The growth in the review year reflected continued buoyancy in the local real estate market. **Loans and Advances** continued to account for the dominant share of the increase in the institutions' asset base. The significant increase in loans during 2006 facilitated a 2.8 percentage point increase in the advance to savings fund ratio. In addition, the mortgage loans to savings fund ratio increased to 57.6 per cent at end-2006 from 54.6 per cent at end-2005 (see **Table 14**).

The major source of financing continued to be **Savings Fund** with an increase of 14.8 per cent in 2006 relative to the increase of 9.0 per cent for 2005. Of this increase in the deposit base, 62.9 per cent represented growth in domestic currency savings. The expansion in the institutions' liabilities also reflected a faster rate of growth in balances due to specialized institutions and commercial banks. There was also acceleration in the growth of the capital accounts which largely reflected increases in permanent capital, capital shares and the entities' retained earnings.

2.4.2.1. New Mortgage Loans

There was an increase in both the value and number of mortgage loans in 2006. The value of the new mortgage loans increased by 17.0 per cent during 2006 vis-à-vis an increase of 21.3 per cent in the previous year. This slowdown reflected a decline in the value of new *Commercial* and *Residential* mortgages while *Agricultural & Other* mortgages tripled during the review year. The reduction in residential mortgages could be linked to an increase in the mortgage limit of the National Housing Trust (NHT).

The number of new mortgage loans increased by 17.4 per cent during the review period, higher than the increase of 11.5 per cent for 2005. The increase in mortgage loans largely reflected significant growth within the *Residential* and *Agricultural & Other* categories, as there was a slight decline in the number of new commercial loans extended during the review year. Consistent with similar growth in both the value and volume of new mortgage loans, the average size of these loans at end-2006 remained at the $2.5 million recorded at end-2005.

In the context of a highly competitive mortgage market, where there were frequent promotions highlighting preferential rates, the overall weighted average loan rate fell by 87.0 basis points during the review year to 13.85 per cent at end-2006. This outturn also occurred against the background of generally positive market fundamentals and a trend decline in market interest rates.

Table 15

Building Societies New Mortgage Loans

	Stock 2005	Stock 2006	Flow 2005	Flow 2006	% Change 2005	% Change 2006
Value of New Accounts (J$M)						
Residential	8 110.9	9 084.6	1 101.2	973.7	15.7	12.0
Commercial	355.1	109.6	240.8	-245.5	210.7	-69.1
Agricultural & Other	402.2	1 184.0	212.9	781.8	112.5	194.4
TOTAL	**8 868.2**	**10 378.2**	**1 554.9**	**1 510.0**	**21.3**	**17.0**
Number of New Accounts						
Residential	3 250	3 587	185.0	337	6.0	10.4
Commercial	36	28	6.0	-8	20.0	-22.2
Agricultural & Other	252	539	174.0	287	223.1	113.9
TOTAL	**3 538**	**4 154**	365.0	**616**	**11.5**	**17.4**
Overall Weighted Average Loan Rate (%)	14.71	13.85	-0.91	-0.87		

2.5. Development Banks

2.5.1. Development Bank of Jamaica

The Development Bank of Jamaica (DBJ), in 2006, expanded its size primarily as a result of a merger with the National Investment Bank of Jamaica (NIBJ) on 01 September 2006. There was no change in the mandate or operations of the institution arising from the merger. Consequently, the DBJ continued to provide medium and long term financing at concessional interest rates via Approved Financial Institutions (AFIs)[8] as well as the People's Co-operative (PC) Banks. Loan approvals and disbursements declined for the year. However, there was a sharp increase in the stock of loans outstanding, consequent on the acquisition of NIBJ's loan portfolio. The DBJ's operations during the year resulted in profits of $299.9 million, which was 156.3 per cent above that recorded for 2005.

Total assets of the DBJ increased by 50.0 per cent in 2006 (see **Table 16**). This expansion mainly reflected increases in repurchase agreements, receivables and prepayments, outstanding loans, as well as cash and bank balances. Total loans to financial institutions increased by 35.9 per cent resulting from the incorporation of the NIBJ loans. This outturn reflected decreases of 36.5 per cent and 2.1 per cent in loans to PC Banks and AFIs, respectively. At end-2006, the outstanding stock of loans to these institutions stood at $6 130.6 million, representing 64.0 per cent of loans to financial institutions. During the year, there was also a 44.5 per cent reduction in outstanding loans relating to the GOJ infrastructural loan programme.

On the liability side, there was an expansion of 106.2 per cent in long-term loans and an increase of 48.2 per cent in shareholders' equity. There were, however, declines in short-term and other liabilities.

Table 16

DEVELOPMENT BANK OF JAMAICA
ASSETS AND LIABILITIES
(J$M)

	2005	2006	Change	% Change
ASSETS				
Cash and Bank Balances	279.2	2 029.0	1 749.8	626.7
Receivables and Prepayments	6 994.7	10 322.6	3 327.9	47.6
Investments	74.6	628.5	553.9	742.5
Securities - Resale Agreements	201.9	4 640.5	4 438.6	2 198.4
Loans to Financial Institutions	7 043.5	9 575.2	2 531.7	35.9
-Loans to Co-operative Banks	757.5	481.1	-276.4	-36.5
-Loans to AFIs	5 769.2	5 649.5	-119.7	-2.1
-Other Loans	516.8	3 444.6	2 927.8	566.5
GOJ Infrastructural Loan Programmes	5 732.2	3 184.2	-2 548.0	-44.5
Other Assets	0.0	0.0	0.0	0.0
Fixed Assets	384.2	690.2	306.0	79.6
TOTAL	**20 710.3**	**31 070.2**	**10 359.9**	**50.0**
LIABILITIES AND SHAREHOLDERS' EQUITY				
Shareholder's Equity	5 398.0	7 998.7	2 600.7	48.2
Current Liabilities	1 196.3	1 376.8	180.5	15.1
Long-term Liabilities	10 149.0	20 922.7	10 773.7	106.2
Short-term Liabilities	2 368.4	383.1	-1 985.3	-83.8
Other Liabilities	1 598.6	388.9	-1 209.7	-75.7
TOTAL	**20 710.3**	**31 070.2**	**10 359.9**	**50.0**

8 These include commercial and merchant banks.

Loan Approvals and Disbursements

During 2006, local currency loan approvals amounting to $1 186.4 million were 11.3 per cent more than in 2005, while those denominated in foreign currency declined by 78.9 per cent (see **Table 17**). Approvals in local currency were mainly for the Manufacturing and Agro-Industry sectors, which accounted for 49.6 per cent and 25.6 per cent of total local currency loan approvals, respectively (see **Table 18**). These were the only sectors to reflect an increase in approvals relative to 2005.

Local currency and foreign currency loan disbursements both declined relative to 2005. The reduction reflected a 58.2 per cent decline in the foreign currency component. Foreign currency loan disbursements amounted to US$2.8 million, a decline of 58.2 per cent. The tourism sector accounted for 94.2 per cent of outstanding foreign currency loans. Local currency loan disbursements amounted to $907.8 million, a 7.0 per cent decline relative to 2005. Manufacturing, Agriculture and Other Services accounted for 42.9 per cent, 25.5 per cent, and 19.3 per cent of the disbursements, respectively (see **Table 18**).

Table 17

LOAN APPROVALS AND DISBURSEMENTS TO AFI's AND PC BANKS BY SECTOR
JANUARY - DECEMBER 2006

APPROVALS	Local Currency J$M			Foreign Currency US$M		
Sector	2005	2006	% change	2005	2006	% change
Agriculture	348.9	77.3	-77.8	0	0	0
Agro-Industry	151	303.4	100.9	0	0	0
Manufacturing	238.2	588.3	147.0	0	0	0
Mining & Quarrying	78.9	72.7	-7.9	0	0	0
Other Services	138.7	111.4	-19.7	0.2	0.2	0
Tourism	110	33.3	-69.7	12.6	2.5	-80.2
Total	1 065.7	1 186.4	11.3	12.8	2.7	-78.9

DISBURSEMENTS	Local Currency J$M			Foreign Currency US$M		
Sector	2005	2006	% change	2005	2006	% change
Agriculture	320.1	231.4	-27.7	0	0	0
Agro-Industry	265.6	57.6	-78.3	0	0	0
Manufacturing	173.7	389.9	124.5	0	0	0
Mining & Quarrying	94.7	0	-100.0	0	0	0
Other Services	0.8	175.5	21 837.5	0	0.2	
Tourism	121	53.3	-56.0	6.7	2.6	-61.2
Total	975.9	907.8	-7.0	6.7	2.8	-58.2

Table 18

LOAN APPROVALS AND DISBURSEMENTS TO AFI's AND PC BANKS BY SECTOR JANUARY - DECEMBER 2006								
	PROPORTIONS							
	APPROVALS				DISBURSEMENTS			
	Local Currency	Foreign Currency	Local Currency	Foreign Currency	Local Currency	Foreign Currency	Local Currency	Foreign Currency
	2005		2006		2005		2006	
Sector								
Agriculture	32.7	0	6.5	0	32.8	0	25.5	0
Agro-Industry	14.2	0	25.6	0	27.2	0	6.3	0
Manufacturing	22.4	0	49.6	0	17.8	0	42.9	0
Mining & Quarrying	7.4	0	6.1	0	9.7	0	0	0
Other Services	13	0	9.4	7.4	0.1	0	19.3	5.8
Tourism	10.3	0	2.8	92.6	12.4	100	5.9	94.2

2.5.2. National Export-Import Bank of Jamaica

In 2006, the National Export-Import Bank of Jamaica (Ex-Im Bank) continued to provide trade financing and medium term loans to the export sector, complemented by export credit insurance and other related services. In keeping with the main strategic initiative to grow its loan portfolio, loan disbursements in 2006 exceeded $4.0 billion, 78.0 per cent above the amount disbursed in 2005.[9] This was achieved primarily through an expansion in productive business activities of existing clients, improved marketing activities and the targetting of new sub-sectors primarily within the bauxite and tourism industries. Financing for the year partly came from a US$10.0 million medium term loan from Banco Latinoamericano de Exportaciones (BLADEX).

In terms of new business, the Ex-Im Bank is in the final stage of preparation for the launch of its Domestic Credit Insurance, a facility which is expected to come on stream by mid-2007 and which is proposed to be accompanied by short-term working capital discounting financing. This proposal came against the background of a demand for the product.

In light of the approaching end to its existing Strategic Plan, the Ex-Im Bank started the process of formulating its new three-year Strategic Plan 2007/2010, which will continue to focus on extending trade financing to facilitate sustainable economic development. With this new plan, the Ex-Im Bank is expected to continue to support viable medium term loan projects and products with export potential, which will allow local companies to effectively compete with their international counterparts.

2.5.2.1. Review of Lending Operations

In 2006, the Ex-Im Bank disbursed local and foreign currency loans of J$2.7 billion and US$27.5 million, respectively, bringing total disbursements to J$4.4 billion or 78.0 per cent above that for 2005. Growth was recorded in both local and foreign currency loans. The expansion in foreign currency loans was primarily attributable to the Ex-Im Bank's financial support for the importation of cement and the increased utilization under the **Cuban Line of Credit**. Simultaneously, a strong demand for pre-shipment financing and medium term loans to facilitate production and the acquisition of capital equipment, contributed to the increase in demand for local currency loans.

Table 19 - Local Currency Disbursements

FACILITIES	Jan. - Dec. 2005	Jan. - Dec. 2006	Flow	Change
	J$MN	J$MN	J$MN	%
Bankers' Export Credit Facility	409.5	470.4	60.9	14.9
Export Credit Facility	675.9	650.0	-25.9	-3.8
Insurance Policy Discounting Facility	69.2	44.1	-25.1	-36.3
Pre-Shipment/ CoPack Facilities	285.7	790.2	504.5	176.6
Apparel Sector Financing	21.8	23.4	1.6	77.3
Modernization Fund for Exporters	122.0	207.1	85.1	69.8
Small Business Facility	114.3	209.7	95.4	83.5
Ornamental Fish	1.5	0.7	-0.8	-53.3
General Trade Line	0.0	238.6	238.6	100.0
JEA/ExBed	16.8	18.5	1.7	10.1
Information Communication Technology (ICT)	1.1	0.3	-0.8	-72.7
Total	**1 717.8**	**2 653.0**	**935.2**	**54.4**

9 In 2004 the Ex-Im Bank developed a strategic plan which outlined several initiatives it intended to pursue over a three year period.

Local currency loans increased by 54.4 per cent, relative to 2005, largely attributed to increased demand for the pre-shipment facility, which registered a 176.6 per cent increase over the previous year (see **Table 19**). The medium term facilities namely the **Modernization Fund for Exporters** and the **Small Business Facility** also recorded strong growth in 2006, as small and medium size companies sought to modernize their businesses and streamline their financial operations. Demand for the total export credit insurance facility remained flat at approximately $1.0 billion in 2006 despite the rebound in the level of non-traditional exports.[10]

Food and Beverage continued to be the major beneficiary of the Ex-Im Bank's local currency funding, accounting for 37.0 per cent of total approved loans at end-2006. Additionally, a 67.0 per cent increase in loan disbursement to **Agro Processing**, coupled with more than 100.0 per cent increase in funding to **Distribution/Services** and **Other Manufacturing**, contributed to the overall increase in utilization in 2006 (see **Table 20**).

Table 20 - Approved Loans by Industry

Industry	January - December 2005		January – December 2006	
	J$	%	J$	%
Agro Processing	468.1	27.3	812.7	30.6
Food & Beverage	955.5	55.6	982.3	37.0
Textile & Apparel	22.6	1.3	26.4	1.0
Other Manufacturing	134.7	7.9	344.5	13.0
Distribution/Services	136.9	7.8	473.3	17.8
Mining	-	-	13.6	0.5
Total	**1 717.8**	**100**	**2 652.8**	**100.0**

10 The total export credit insurance facility represents the sum of Bankers' Export Credit Facility and Export Credit Facility.

Table 21 - Foreign Currency Disbursements

Facility	US$MN 2005	US$MN 2006	Change US$	Variance %
Lines of Credit	9.8	20.5	10.7	109.0
Bankers Export Credit Facility	0.7	0.9	0.3	44.0
Cuban Line of Credit	-	4.6	4.6	100.0
Export Growth Initiative Fund	1.0	1.4	0.4	35.0
Total	**11.5**	**27.4**	**16.0**	**139.1**

Foreign currency disbursements were driven by **Lines of Credit**, which increased by US$10.7 million or 109.0 per cent in 2006, relative to 2005. This exceptional performance was due mainly to the Ex-Im Bank's financial support to facilitate the importation of cement. The **Cuban Line of Credit**, which was suspended in 2005 as a result of operational problems, was reinstated in 2006, and recorded loan disbursements of US$4.6 million **(**see **Table 21).**

2.6 Financial Stability Assessment of Deposit-Taking Institutions ((DTIs)

2.6.1 Overview

In 2006, the BOJ conducted stress tests of the resilience of deposit-taking institutions (DTIs) to adverse hypothetical shocks using the institutions' financial statements and prudential data as at the end of each quarter. Hypothetical losses incurred by DTIs were assumed to erode buffer capital first, with losses in excess of buffer capital absorbed by statutory capital.[11] Stress test results on aggregate DTIs revealed more than adequate shock-absorption capacity following hypothetical shocks to credit, exchange rate, interest rate and liquidity. Positive results were also obtained from the Bank's early warning system (EWS).

2.2.2 Credit Risk Stress Test Results

Aggregate DTIs were resilient to potential deterioration in credit quality during 2006, due to the low levels of NPLs as well as high levels of capitalization.[12] In the context of an improvement in credit quality during 2006, there were less than 1.0 percentage point declines in capital adequacy ratios (CARs) of the commercial banks, FIA licensees and building societies sub-sectors as a result of hypothetical 10.0 per cent and 30.0 per cent increases in NPLs.

The DTI sector was also resilient to a hypothetical 30.0 per cent decline in performing loans to the private sector. This occurred despite relatively strong concentrations in personal loans as well as, to a lesser extent, loans to the distribution and tourism sectors. There was a less than 0.5 per cent decline in aggregate CAR following shocks to performing loans for all loan categories. 'Personal loans to domestic residents' was the only category to experience declines in CAR above 1.0 per cent in stress tests conducted at the end of each quarter in 2006. However, the declines in CAR for this category as a result of the shocks did not exceed 2.0 per cent at the end of each quarter in 2006.

11 Buffer capital or excess capital comprises retained earnings, unappropriated profits and specified revaluation reserves.

12 Resilience is determined by the capital adequacy ratio remaining above the 10.0 per cent ratio following extreme but plausible hypothetical shocks.

2.2.3 Foreign Exchange Risk Stress Test Results

The exposure of DTIs to foreign exchange risk declined during 2006, consequent on a reduction in the overall foreign currency net open position to capital. This improvement in foreign currency risk exposure was against the background of sharp declines in the US dollar-denominated net open positions held by some institutions over the September and December quarters. In addition, the CAR remained above the 10.0 per cent benchmark when the impact of hypothetical depreciations in the exchange rate on the banking sector balance sheet was assessed.

2.2.4 Interest Rate Risk Stress Tests

The DTI sector was robust to hypothetical interest rate shocks during 2006. Capital buffer levels were more than sufficient to offset the adverse effect of potential interest rate increases. Stress tests results indicate that capital adequacy of the sector was unchanged following hypothetical shocks to both domestic and international interest rates at the end of each quarter in 2006.

2.2.5 Liquidity Risk (Interest Rate) Stress Test

The banking sector was resilient to hypothetical liquidity shocks during 2006. At the end of each quarter, the system did not suffer a decline in CAR under the interest rate shocks applied. Specifically, for cases where increases in interest rates resulted in a loss in net interest income for the sector, buffer capital was sufficient to absorb this loss and prevent a decline in CAR levels.

2.2.6 Liquidity Risk (Deposit Withdrawal) Stress Tests

Deposit withdrawal risk did not pose a meaningful source of risk to the banking sector during 2006. In addition, none of the sub-sectors appeared susceptible to a possible sudden withdrawal of deposits during the year, although specific institutions were slightly adversely affected under the most extreme shocks applied. The robustness of the banking sector to the hypothetical sudden declines in deposit levels reflected the strong liquidity position of the sector throughout 2006.

2.6.7 Early Warning System (EWS) Stress Test Results

The value of the Bank's macro-prudential index, which comprises 18 key macroeconomic indicators, improved during 2006 in a context of the general improvement in macroeconomic fundamentals.[13] In addition, the value of the Bank's micro-prudential index, comprising 21 key financial ratios indicators for each DTI sub-sector, remained broadly stable in 2006. The system's ability to withstand shocks was also supported by the fact that both the macro-prudential index and the micro-prudential index recorded values well below the levels that obtained during the 1996 to 1999 financial crisis.

13 The Bank's macro-prudential index is used to assess the macroeconomic environment in which DTIs operate.

3. Money Market Operations

3.1. Bank of Jamaica Operations

During 2006, the issuance of Certificates of Deposit (CDs) continued to be the main tool of monetary policy implementation. Primary Dealers (PDs) and commercial banks remained the main conduits through which CD were issued. Primary dealers accounted for 63.3 per cent of placements during the year.

Primary Dealer Monitoring and Assessment

The number of PDs remained unchanged at 15 at the end of the year. The monitoring of PDs continued in 2006 through the examination of institutions' performance under the following criteria:

- subscriptions to GOJ primary issues;
- holdings of BOJ open market instruments (CDs);
- the operation of their current account at the Bank of Jamaica in accordance with the account agreement; and
- timely submission of reports on financial market activity to the Bank.

In order to enhance the implementation of monetary policy, the Bank, following discussions with the PDs, embarked on re-designing the processes and instruments used for liquidity management. In this regard, by mid-2007, the process of applying for OMO instruments will be done electronically. The improvement in the security features of the certificates, the establishment of the appropriate legal framework and enhanced market protocols will support the increased tradability of these instruments. The objective however, is that the issuance of OMOs will be dematerialized once the Central Securities Depository for fixed income securities is implemented 2008.

Liquidity Management

There was an increase of $4 964.8 million in the stock of CDs in 2006. However, interest payments from maturing OMO instruments amounted to $23 773.4 million. Consequently, there was a net injection of $18 768.4 million through OMOs (see **Table 22**). The net injection from these flows along with net purchases of foreign currency by the Bank supported the net issue of GOJ domestic instruments, particularly in the second half of the year. The proceeds of the net issue were accumulated in GOJ accounts held at the BOJ.

Table 22

Bank of Jamaica Open Market Operations in Certificates of Deposit 2006 (in J$mn)

	March	June	September	December
Net Absorption(+)/Injection (-)	1 053.8	(5 660.3)	2 227.1	(16 389.3)

Data include principal and interest payments

Monetary policy was implemented in a generally benign macroeconomic environment during 2006, which allowed the Bank to reduce interest rates on all tenors of OMOs, as well as discontinue offering 270-day and 365-day instruments. These actions spurred subscriptions to the 180-day instrument, partly financed by the proceeds from maturing 270 and 365-day instruments. In this context, it was observed that the proportion of 180-day placements to total placements increased in 2006 relative to 2005 (see **Table 23**). The increased demand for this tenor also reflected the need for instruments which qualify as liquid assets. Notwithstanding the demand for the 180-day tenor, the 30-day tenor continued to dominate the take-up profile for OMOs, as it provided on-going cash flow for treasury management purposes.

By end-December 2006, maturities occurring within 30-days to 90-days accounted for approximately 63.1 per cent of the total $154 757.0 million in outstanding open market liabilities. This compares with maturities within the similar range as at end-December 2005 being 44.2 per cent of the $149 806.5 million in open market liabilities (see **Table 24**).

Table 23

Take-up Ratios (%) in Selected Open Market Instruments
Quarterly Profile for 2005 & 2006

	Issue Tenor	March	June	September	December
2	30-day	39.4%	40.8%	40.5%	48.5%
0	90-day	7.1%	7.3%	10.9%	15.6%
0	180-day	4.5%	8.7%	8.3%	7.2%
5	365-day	38.3%	36.1%	28.7%	15.6%
	Other*	10.7%	7.2%	11.6%	13.0%
		March	June	September	December
2	30-day	45.2%	39.2%	49.3%	44.4%
0	90-day	9.4%	10.3%	11.3%	10.1%
0	180-day	5.3%	33.5%	29.6%	38.3%
6	365-day	27.1%	9.5%	n/a	n/a
	Other*	12.9%	7.4%	9.7%	7.1%

n/a indicates that the tenor was withdrwan from offer.
* 'Other' includes the take-up in the 60-day, 120-day and 270-day tenors.

Table 24

Maturity Profile of Bank of Jamaica Open Market Liabilities
Quarterly Cumulative Profile for 2006

Time left to Maturity	Dec-05	Mar-06	Jun-06	Sep-06	Dec-06
⩽ 30-days	17.3%	31.8%	22.4%	23.4%	25.8%
⩽ 60-days	32.3%	47.5%	31.5%	43.4%	43.4%
⩽ 90-days	44.2%	56.0%	39.2%	58.1%	63.1%
⩽ 120-days	62.9%	66.9%	50.4%	65.5%	79.1%
⩽ 180-days	79.2%	74.5%	74.1%	90.7%	100.0%
⩽ 270-days	94.3%	83.8%	89.9%	100.0%	...
⩽ 365-days	100.0%	100.0%	100.0%	...	...
OMO Liabilities Outstanding (J$ mn):	149,806.5	157,357.6	159,438.1	166,018.9	154,757.0

3.2. Interest Rates

The favourable macroeconomic environment during 2006 facilitated further reductions in domestic interest rates. In this regard, the BOJ effected reductions ranging from 95 basis points on the 30-day tenor to 100 basis points on the 180-day tenor (see **Table 25**).

Table 25

Rates on Selected OMO Instruments (%) (December 2005- December 2006)					
End Month	**30 days**	**90 days**	**180 days**	**270 days**	**365 days**
December '05	12.60	12.75	13.00	13.25	13.60
January	12.60	12.75	13.00	13.25	13.60
February	12.60	12.75	13.00	13.25	13.60
March	12.60	12.75	13.00	13.25	13.60
April	12.60	12.75	13.00	n/a	n/a
May	12.45	12.60	12.80	n/a	n/a
June	12.45	12.60	12.80	n/a	n/a
July	12.45	12.60	12.80	n/a	n/a
August	12.45	12.60	12.80	n/a	n/a
September	11.95	12.10	12.30	n/a	n/a
October	11.95	12.10	12.30	n/a	n/a
November	11.95	12.10	12.30	n/a	n/a
December '06	11.65	11.80	12.00	n/a	n/a

n/a tenors removed as at 18 April 2006

During the March 2006 quarter, the Bank's OMO rates remained unchanged despite the moderation in inflation relative to the December 2005 quarter. This action reflected the Bank's conservative monetary policy stance in response to investors' concerns about real rates following the sharp increase in inflation in 2005, as well as the potential effects of escalating international oil prices. There were also concerns about the Jamaica - US interest rate differential, given the trend increase in US policy interest rates.

However, during the subsequent quarters, these concerns dissipated in light of the continued moderation in inflation and declining oil prices which influenced a steady improvement in investor confidence. Conditions were also bolstered by the fact that the Government had completed its external borrowing requirements for the 2006/2007 fiscal year with the successful Eurobond offer of US$250.0 million in February, followed by the presentation of a fiscal budget that was generally viewed as attainable. Further, the prospects for the attainment of single digit inflation for 2006 became more apparent as deflation of **0.1** per cent and **0.2** per cent were recorded in October and November, respectively. These developments combined with improved prospects for economic growth supported reductions in OMO rates during the June and December quarters. The reductions were effected on four occasions during the period, resulting in rates on the 30-day and 180-day tenors closing the year at 11.65 per cent and 12.00 per cent, respectively, relative to 12.60 per cent and 13.00 per cent on the respective tenors at end-December 2005 (see **Chart 8**). Notably, interest rates on OMOs at end-2006 represented the lowest in 15 years.

Consistent with the reduction in BOJ policy rates, market-determined rates declined during the year. In this regard, the 180-day Treasury Bill yield at end-2006 was 12.31 per cent, relative to 13.55 per cent at end- 2005. Similarly, average yields on the 90-day Treasury Bill declined to 12.26 per cent at end- 2006 from 13.34 per cent at end-2005 (see **Chart 8**). The general decline in market-determined interest rates was also evident at the long-end of the GOJ yield curve. The weighted average yield of 14.05 per cent on a 20-year LRS issued in the December quarter compared favourably with the outturn of 14.31 per cent on an 11-year LRS issued in the June quarter.

Chart 8

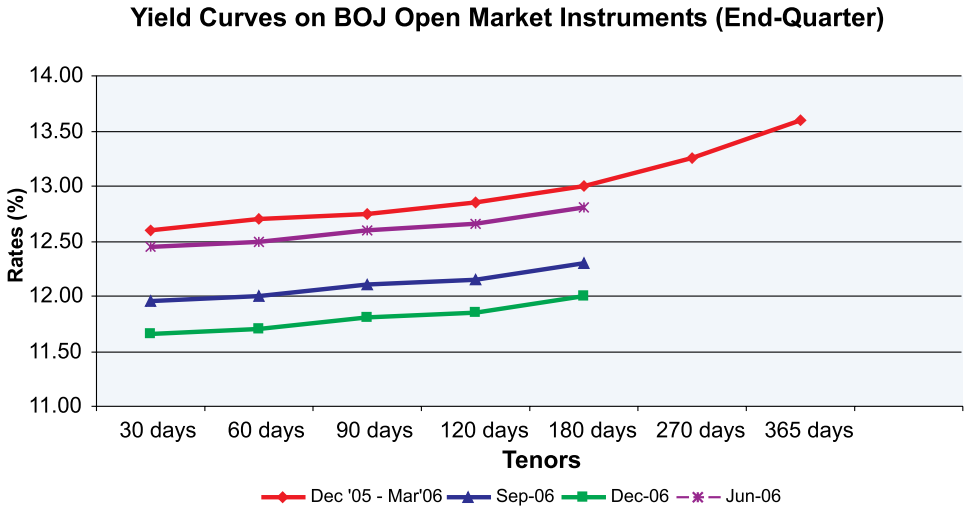


Chart 9

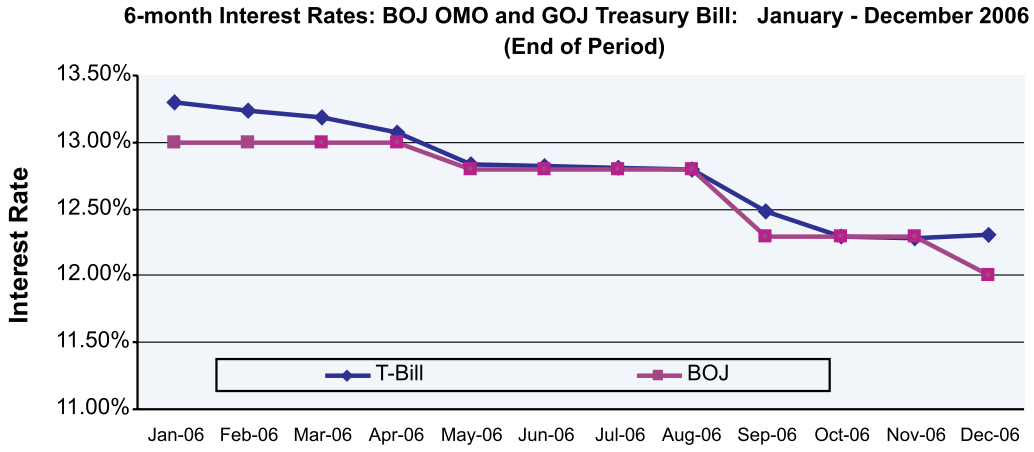


Table 26

Weighted Average Treasury Bill Yields (End Period - 2006)		
End Month	**3-month**	**6-month**
January	12.82%	13.30%
February	12.83%	13.24%
March	13.16%	13.18%
April	12.79%	13.07%
May	12.67%	12.84%
June	12.64%	12.82%
July	12.62%	12.81%
August	12.68%	12.79%
September	12.44%	12.49%
October	12.12%	12.30%
November	12.09%	12.28%
December	12.26%	12.31%

In 2006, the Main JSE Index declined by 3.7 per cent to 100 677.96 points, while the All Jamaica Composite and the Select Index increased by 2.2 per cent and 2.9 per cent, respectively (see **Chart 10**). Despite weak stock market returns during the first half of the year, improved investor outlook contributed to a moderate rebound in the equities market in the September quarter and robust gains in all indices during the last quarter of the year. For the December quarter, the Main JSE Index gained 16.6 per cent, relative to growth of 1.3 per cent for the September quarter and an average decline of 9.5 per cent over the previous two quarters (see **Chart 11**).

Chart 10

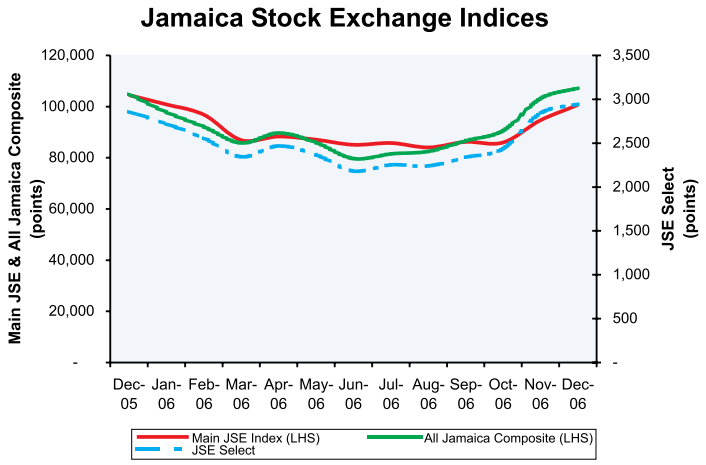
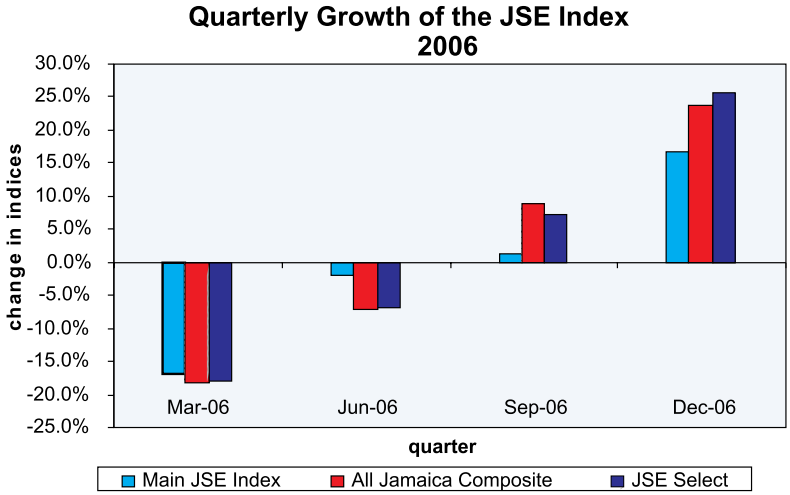


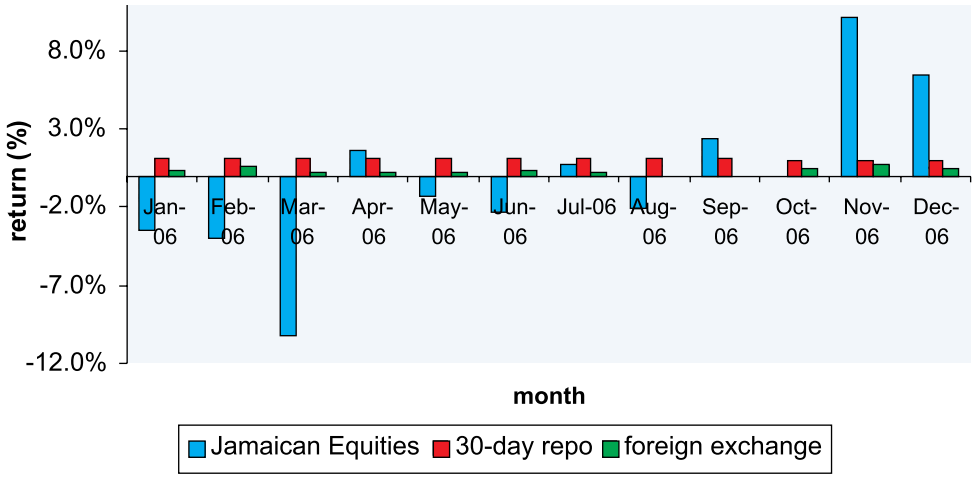
Chart 11



During the first half of the year, the stock market continued the downturn that was observed for most of 2005, returning an average monthly loss of 3.3 per cent to investors, relative to more attractive monthly returns of 1.1 per cent and 0.4 per cent from fixed income and foreign currency investments, respectively (see **Chart 12**).[14] The weak stock market performance during the first half of the year reflected dampened investor interest due to relatively poor earnings results for many of the listed companies. Investor sentiment worsened during the June quarter as a result of the cement shortage, which restricted revenue growth for some entities in the manufacturing and retail sectors. The relatively low returns on equity investments also coincided with the increased attractiveness of foreign currency investments, due to successive increases in policy rates in the developed economies during May and June.

Chart 12

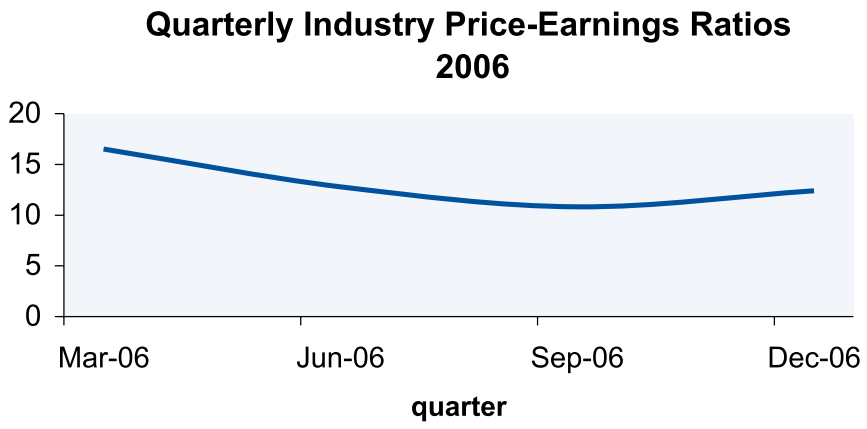
Monthly Returns From Equities, Fixed Income and Foreign Exchange 2006



14 The secondary 30-day repo rates and the rate of depreciation of the Jamaica Dollar vis-à-vis the US dollar are used as proxies for fixed income and foreign currency investments, respectively.

The stock market rebounded during the second half of the year, attributable to improved investor outlook regarding the prospects for increased profits. This was in a context of sustained improvements in the macroeconomic fundamentals, as well as expansion plans and restructuring exercises by a number of the listed companies in order to maximize the earnings potential of their operations. In addition, investor sentiment was positively influenced by interest rate reductions by the BOJ during the period. In anticipation of a continuation of the lower interest rate environment, some financial companies re-structured their operations to strengthen earnings from core and non-interest income business activities. Against this background, there were large share price appreciations for several listed companies in the manufacturing and financial sectors as well as increases in price/earnings valuations (see **Chart 13**).[15] Specifically, this occurred in a context where several of the companies reported favourable earnings results during the December quarter. In addition, increased participation by some investors in anticipation of large cash payments in the latter part of the quarter contributed to the overall performance. [16] The improvement in the price/earnings ratio represented a reversal of the downward trend in the ratio since the start of the year (see **Chart 13**).

Chart 13



15 Industry P/E ratios is the ratio of the current share price divided by the earnings per share over the last four quarters.

16 Some investors anticipated large cash payments for share offers in respect of DB&G and Courts in the December quarter.

Stocks from the financial, manufacturing, and conglomerate categories were among the best performers in terms of price movements in 2006 (see **Table 27**). The improved investor interest in these stocks had a strong impact on the performance of the Main JSE Index as they accounted for the bulk of market capitalization**.** The stocks with the largest declines were from the manufacturing, insurance, communication and 'other' categories (see **Table 28**).

Table 27

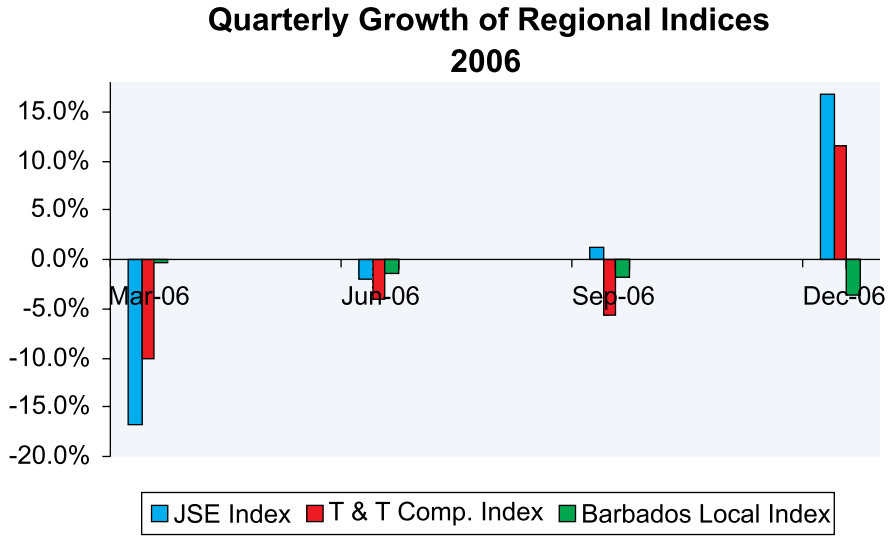
Top Ten Share Price Performers in 2006		
	Price at end 2006 ($)	**Price Change (%) 2006**
Financial Sector		
DB&G	28.00	24.40
NCB	23.65	17.6
FCIB Ja	26.00	27.84
Manufacturing		
Ja Broilers	5.00	22.25
Salada	40.00	299.60
Kingston Wharves	7.94	32.33
Conglomerates		
Carreras	40.00	50.00
JPG	33.40	27.21
Lascellles	275.10	20.66
Tourism		
Jamaica Pegasus	13.90	54.44

Table 28

Ten Largest Declining Stocks in 2006		
	Price at end 2006 ($)	Price Change (%) 2006
Insurance		
Guardian Holdings	240.00	-33.33
Dyoll Group	0.90	-51.35
Manufacturing		
Goodyear Ja.	8.50	-23.63
Mobay Ice	6.50	-42.96
Trinidad Cement	84.50	-19.52
Conglomerates		
Grace Kennedy	63.50	-27.39
Communication		
Cable and Wireless	1.01	-31.76
Gleaner Company	1.99	-23.46
Tourism		
Ciboney	0.07	-22.22
Other		
Palace Amusement	31.45	-40.32

The other major stock exchanges in the region registered weak performances during 2006. For Barbados and Trinidad & Tobago, the composite indices declined by 6.8 per cent and 9.2 per cent, respectively (see **Chart 14**). The declines in the indices occurred in a context of a higher inflation and interest rate environment. However, similar to the performance of the Main JSE Index, the T&T Composite Index recorded robust gains in the December quarter, largely reflecting the strong performance of cross-listed stocks.

Chart 14


Quarterly Growth of Regional Indices
2006
15.0%
10.0%
5.0%
0.0%
-5.0%
-10.0%
-15.0%
-20.0%
Mar-06
Jun-06
Sep-06
Dec-06
JSE Index
T & T Comp. Index
Barbados Local Index

5. Supervision Of Deposit -Taking Financial Institutions

5.1. Introduction

The Bank of Jamaica is charged with the supervision and periodic examination of deposit-taking financial institutions pursuant to provisions under Section 34A of the Bank of Jamaica Act. The supervised population comprises:

- Commercial banks licensed under the Banking Act;
- Merchant banks licensed under the Financial Institutions Act
  (FIA licensees); and
- Building Societies governed by the Building Societies Act and the Bank of Jamaica (Building Societies) Regulations.

Additionally, credit unions have been designated by the Minister of Finance as 'specified financial institutions' under the Bank of Jamaica Act, as a preliminary step towards placing these institutions under the supervisory regime of the Bank. This specification currently enables the Bank to obtain information on their operations. Regulations to establish a formal supervisory framework for these entities have been drafted after extensive discussion with sector representatives, and are expected to be presented before Parliament during 2007 (see **Legislative Developments**).

Regulatory responsibility for non-deposit-taking financial institutions rests with the Financial Services Commission which has supervisory oversight of insurance companies, securities dealers, unit trusts, pension management companies and mutual funds (see **Supervisory Cooperation and Interaction**).

5.2. Legislative Framework

The major pieces of legislation and supporting regulations governing the operations of the licensed deposit taking institutions are shown in **Table 29**.

Table 29 – Overview of Legislative Framework

Type of Legislation	Title of 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 Banking (Establishment of Branches) Regulations • The Banking (Amalgamation and Transfers) Regulations • The Banking (Capital Adequacy) Regulations • The Banking (Licence Fees) Regulations • The Financial Institutions (Establishment of Branches) Regulations • The Financial Institutions (Amalgamation and Transfers) Regulations • The Financial Institutions (Capital Adequacy) Regulations • The Financial Institutions (Licence Fees) Regulations • The Building Societies (Licences) Regulations

Licensees also have statutory responsibilities which may or may not be peculiar to their nature of business, which devolve from other pieces of legislation. These include, but are not limited to, the Companies Act, the Deposit Insurance Act, Drug Offences (Forfeiture of Proceeds) Act, the Money Laundering Act and related regulations as well as guidance notes issued by the Supervisory Authority (see **Legislative Developments**).

5.3. Supervisory Methodology

Supervisory responsibilities are discharged through the Financial Institutions Supervisory Division (FISD) of the Bank. The supervisory methodology combines annual on-site examinations along with on-going off-site monitoring, which allows for continuous and timely review of developments in the financial condition of supervised entities both at the institutional level as well as at the systemic level.

Each licensee is examined once per year as required by statute or more frequently, if deemed necessary by the Supervisor of Banks. Traditionally, the on-site examination incorporated reviews and assessments of key areas of a licensee's operations, in particular, capital adequacy, asset quality, liquidity, earnings performance, management oversight and the overall risk management framework within which the institution operates, inclusive of anti-money laundering and anti-terrorism financing arrangements. As the Bank remains responsive to market developments and evolution of international standards, the on-site supervisory approach has continued to evolve, and now also encompasses:

- A more risk-based approach to supervision which involves enhanced off-site and pre-examination procedures, with increased scrutiny on licensees' corporate governance frameworks, risk management and operational/group structures. The outcome of these assessments identifies those areas that pose the greatest potential risk to each institution's operations and determines the institution's overall risk rating, as well as the level and focus of supervisory resources to be assigned to examination (see Section 4.5);
- Enhanced reviews of information systems infrastructure as well as disaster recovery and business continuity arrangements; and
- An expanded and deepened scope of review of licensees' framework for anti-money laundering and for combating the financing of terrorism and fraud (AML/CFT) in order to ensure that policies, controls, etc., remain in keeping with heightened international obligations under United Nations (UN) Security Council Resolutions, and other international standards promulgated by the Financial Action Task Force (FATF)[17] and the Caribbean Financial Action Task Force (CFATF)[18] of which Jamaica is a member.

Off-site assessments were primarily facilitated by prudential returns which licensees were required to submit to the Bank at stated intervals (weekly, monthly, quarterly, annually), but also entailed reviews of audit and other external reports. The off-site review involved analysis of the prudential returns for trends in operations and financial condition and also included an 'early warning system' whereby various financial and prudential indicators were monitored and subjected to scenarios and stress tests to allow for forward looking assessments to facilitate pro-active supervisory responses. In this regard, the Financial Stability Department (FSD) of the Research and Economic Programming Division (REPD) of the Bank generated forecasts and scenario/stress tests. The FSD, in collaboration with FISD, reviewed and assessed prudential information system vulnerabilities arising from financial contagion, macro-economic policy and real sector developments, in addition to other exogenous influences.

17 FATF is an inter-governmental body established in 1989, whose purpose is the development and promotion of national and international policies to combat money laundering and terrorist financing.

18 CFATF is an organization of thirty states of the Caribbean Basin which agree to implement common counter measures to address criminal money laundering.

Integral features of the supervisory approach also included reviewing compliance with legal requirements and prudential regulations as well as the provision of formal guidance through the dissemination of best practice standards and guidelines. Additionally, the approach also promoted the highest degree of disclosure through the Bank's publication of quarterly unaudited balance sheet data for each licensee and a suite of prudential indicators for each financial sub-sector and the combined deposit-taking system.

The Central Bank provided feedback from its various reviews and assessments to licensees' management and boards through a combination of formal meetings, official correspondence and formal written reports on examination findings. These highlighted issues of concern requiring remedial actions within specified time frames as was necessary. Where there was evidence of 'unsafe and unsound' practices, the Bank utilized sanction powers/measures as provided under the respective financial legislation and in accordance with its supervisory "Ladder of Enforcement" which sets out the graduated series of supervisory actions in response to specified prudential concerns.

5.4. Current Issues in Banking Supervision

During 2006, the Bank continued to focus on near to medium-term priorities for the further development of the regulatory and supervisory framework, viz:

- Achievement of full compliance with the recently revised Basel Core Principles for Effective Banking Supervision (BCPs);
- Advancing implementation of an effective regulatory framework to facilitate effective consolidated/conglomerate supervision of financial groups which include a deposit-taking entity;
- Promotion of enhanced risk management frameworks in deposit-taking entities;
- Establishment of the legal and supervisory framework for Basel II implementation in Jamaica by 2010; and
- Continued development/enhancement of supervisory techniques and methodologies, specifically with regard to the full implementation of risk-based supervision.

These near-to-medium term plans and priorities were influenced by many factors, including:-

1. ***Results of the IMF/World Bank 2005 Financial Sector Assessment Programme (FSAP).*** During 2005, Jamaica underwent a financial sector assessment by the IMF/World Bank. The final Report issued in early 2006 indicated that the Bank was fully or largely compliant with twenty-two (22) of the twenty-five (25) BCPs (as originally issued in 1997), the international benchmark against which bank supervisory agencies are assessed. The need for a comprehensive consolidated supervisory framework was the major area identified by the IMF/World Bank for further improvement by the Supervisory Authority, an area in which considerable progress has already been made (see **Consolidated and Conglomerate Supervision of Financial Groups)**.

2. ***Revision of the Basel Core Principles.*** Subsequent to the FSAP exercise conducted in 2005, the Basel Committee on Banking Supervision comprehensively revised the Core Principles, which were ratified by the Committee Members and officially issued in October 2006[19]. The revised BCPs seek to achieve greater consistency with other Basel as well as global best practice standards issued since publication of the original text in 1997, thereby facilitating greater convergence in international approaches. Such standards include the new Basel II capital adequacy framework as well as those issued by other international standard setting bodies such as FATF, the International Association of Insurance Supervisors (IAIS), the International Organization of Securities Commission (IOSCO) and the International Accounting Standards Board

19 The Basel Committee on Banking Supervision is the international standard setting body for banking supervisors worldwide. The Committee is represented by central banks and bank regulators from Belgium, Canada, France, Germany, Italy, Japan, Luxemburg, the Netherlands, Spain, Sweden, Switzerland, United Kingdom and the United States.

(IASB). The entrenchment of the following principles also serve as an endorsement of the Bank's current supervisory priorities and near term action plan, which place similar emphasis on these themes:

- Effective consolidated supervision;
- Greater transparency on the part of licensed entities as well as supervisors;
- Strong corporate governance and risk management frameworks in banking entities; and
- Enhanced supervisory approaches and techniques (facilitated by appropriate and adequate information systems).

3. ***Developments in banking and financial markets.*** Local, regional and global developments in banking and financial markets led to further consolidation of the banking and financial sector as well as increased competitiveness. These developments heightened supervisory focus on conglomerate issues including the need for increased information sharing arrangements as well as greater level of cooperation and harmonization of standards among regulators (local and overseas). Such developments also heightened the need for greater promotion of enhanced risk management frameworks in banking entities.

5.4.1. ***Programme for Achievement of Full Compliance with Revised Core Principles***

During 2006, the Bank continued the process of drafting and updating the Omnibus Bill which seeks to consolidate the Banking Act, the Financial Institutions Act and the BOJ (Building Societies) Regulations, along with related subsidiary financial legislation. The objective is to remove inconsistencies in the existing legal requirements for deposit-taking entities and minimize regulatory arbitrage opportunities. The Omnibus Bill will also seek to enhance the legislative framework to facilitate full compliance with the revised BCPs (see **Electronic Money Order**).

5.4.2. ***Consolidated and Conglomerate Supervision of Financial Groups***

Significant advancements were made during 2006 in laying the foundation for full implementation of consolidated/conglomerate supervision. The BOJ continued to promote the reconfiguration of groups of which deposit-taking entities are a part, to form financial structures that will facilitate effective monitoring and regulation by the Bank. Financial groups were, for the most part, far advanced in their restructuring exercises, the critical first step in the implementation of conglomerate supervision. The Bank also made significant progress in the development of a legal framework for conglomerate supervision, as part of the Omnibus Bill. The proposed legislation is intended to allow the Supervisory Authority to regulate not only the activities of the licensed deposit-taking entity, but also of the financial holding company, as well as facilitate supervisory reach to the entire financial group of which the licensee is a part.

5.4.3. ***Promotion of Enhanced Risk Management Frameworks***

Notwithstanding the continued strong financial performance of the deposit-taking sector, the Supervisory Authority recognized the need for further strengthening of the corporate governance and risk management frameworks in licensed entities, particularly in preparation for adoption of the Basel II Capital Adequacy framework. In this regard, the Supervisory Authority in 2006, sought to further promote the establishment of comprehensive risk management processes through the systematic revision of the suite of existing Standards of Best Practices for Effective Risk Management for updating and re-issuance to the industry. In that regard, considerable work was done in upgrading the Standards of Best Practices for Credit Risk and Market Risk Management. In addition, drafting of a new overarching standard on 'Effective Corporate Governance and Risk Management' was well advanced at year end. As is customary, these Standards will be provided to the industry for comments prior to finalisation and issue.

5.4.4. *Basel II Implementation*

The Basel Committee introduced a new capital adequacy framework, '*International Convergence of Capital Measurement and Capital Standards: A Revised Framework (Basel II)'* in 2004 for adoption by internationally active banks in its member countries by end-2007. The framework is based on three (3) Pillars: -

- Pillar I – Quantitative Measurement of Capital
- Pillar II – Supervisory Review
- Pillar III – Transparency and Disclosures

During 2006, the Supervisory Authority fine-tuned its *Roadmap for Basel II Implementation,* which is expected to be implemented in four phases by end 2010, viz:

- Phase I – implementation of preconditions for Basel II, including full compliance with the Revised Core Principles, including implementation of consolidated supervision;
- Phase II – implementation of Pillar II;
- Phase III – implementation of Pillar III; and
- Phase IV – full adoption of Basel II with the implementation of Pillar I.

During the year under review, particular emphasis was placed on Phase I of the *Roadmap*, including identification of requisite legal enhancements to be made as well as in the areas of the new framework to which national discretion may be applied. This work will continue in 2007, with increased dialogue with the industry. The Supervisory Authority also engaged in extensive dialogue with other regulators among the Caribbean Group of Banking Supervisors (CGBS), aimed at achieving greater levels of understanding and harmonization of approaches to Basel II implementation.

5.4.5. *Development of Supervisory Techniques and Methodologies*

The tremendous increase in the size and complexity of banking business globally has mandated the re-examination of supervisory approaches and methodologies to ensure that deposit-taking entities continue to be effectively supervised. As such, risk-based approach to supervision has now become an international standard. Risk-based supervision focusses on understanding the material risks faced by a supervised entity, and the way in which such risks are managed. It places greater emphasis on the oversight functions of a banking entity resident in the board and senior management, financial analysis, risk management, compliance and internal audit.

The BOJ has, in principle, always been risk-focussed in its approach, but in 2006 began the process of formal adoption of risk-based supervision in line with evolving international standards. The process will continue in 2007.

5.5.1. *Revision of the Bank of Jamaica AML/CFT Guidance Notes*

During 2006 the Bank of Jamaica made further revisions to its 2004 'Guidance Notes for the Prevention and Detection of Money Laundering and Terrorist Financing Activities', which will be issued to the industry in early 2007. These amendments included, inter alia,:

- Further guidance on procedures to combat the financing of terrorism as a result of the passage of Jamaica's Terrorism Prevention Act;
- Enhanced identification requirements when dealing with high risk customers, accounts opened by intermediaries, politically exposed persons (PEPs) and countries with inadequate AML/CFT frameworks; and
- More detailed guidance/directives as regards record-keeping, monitoring and compliance standards as well as employee integrity and awareness.

5.6. Supervisory Cooperation and Interaction

5.6.1. *Financial Regulatory Council*

The Financial Regulatory Council (the Council) was established in 2000 with the mandate to develop policies and strategies to facilitate greater co-ordination and information sharing between the various supervisory and related agencies operating in the Jamaican financial sector. The conduct of the Council is guided by a Memorandum of Understanding signed by each member that addresses a range of common issues including, information sharing. The Council comprises the following members:

- The Governor of the Bank of Jamaica, Chairman;
- The CEO, Financial Services Commission;
- The CEO, The Jamaica Deposit Insurance Company;
- The Financial Secretary; and
- The Solicitor-General

The Council continued to meet during 2006 to examine issues affecting the financial industry as well as issues specific to corporate groups comprising financial entities which are supervised by the Bank of Jamaica and the Financial Services Commission.

5.6.2. *Regional Interaction*

5.6.2.1. *The Caribbean Group of Banking Supervisors*

The Bank continued to administer the Secretariat for the Caribbean Group of Banking Supervisors (CGBS), through a unit in the FISD[20]. The Central Bank of Trinidad & Tobago currently holds the Chair of the Group under a two-year term which is scheduled to end January 2007. During the year the Secretariat organized a number of regional training programmes with international providers as well as the annual conference held in Aruba during May 2006. The Secretariat, with the assistance of the Bank of Jamaica's Information Systems Department, developed enhancements to the CGBS's restricted website (extranet) which is maintained at the Bank (see **International Interaction**).

5.6.2.2. *Information Sharing*

The Bank is one of the signatories to a formal **Information Sharing Agreement** (an MOU), originally signed by eight CGBS members to facilitate cross border cooperation between home and host supervisory authorities for regional banking entities. During 2006, another two regional jurisdictions joined as signatories to the Agreement.

5.6.2.3. *Regional Joint Examinations*

The Bank was one of three regional central banks that participated in a technical assistance initiative coordinated by the **Caribbean Technical Assistance Centre (CARTAC)**[21]**.** This involved a senior examiner participating in an examination team comprising regional and international supervisory experts, in the review of a state owned development bank in a regional jurisdiction.

5.6.2.4. *Caribbean Financial Action Task Force*

In another area of regional involvement, the Deputy Supervisor of Banks continued to serve as the Principal Contact for Jamaica in respect of the **CFATF**. During the year, the Bank jointly coordinated with that organisation, their 'Third Compliance Conference on Anti-Money Laundering, Combatting the Financing of Terrorism and Fraud'. This conference which was held in Jamaica had over 200 participants from 14 regional territories (including Jamaica) spanning a range of industries impacted by AML/CFT (e.g. financial sector, accounting, legal, law enforcement).

20 The CGBS was established in 1983 under the aegis of the Central Bank Governors of member countries of the Caribbean Community (CARICOM), with the specific mandate to co-ordinate the enhancement of bank supervisory practices in the English speaking Caribbean, consistent with internationally accepted standards. The CGBS was later extended to banking supervisors from non-CARICOM Caribbean territories and now comprises membership from fourteen regional jurisdictions, nine of which are presently core members of CARICOM.

21 CARTAC is a regional resource which provides technical assistance and training in core areas of economic and financial management at the request of participating countries. CARTAC operates as a project of the United Nations Development Programme (UNDP) with the IMF serving as the executing agency.

5.6.3. *International Interaction*

The Bank maintained interaction with the Basel Committee on Banking Supervision both in its own capacity and in its role of Secretariat for the CGBS. During the year the Bank provided comments during the consultative stage, on Basel Committee's supervisory guidance on 'Sound Credit Risk Assessment and Valuation of Loans' and 'Home-host Information Sharing for Effective Basel II Implementation'.

The Bank also participated in international conferences including the Basel Committee's biennial 'International Conference of Banking Supervisors'. In its capacity as Secretariat for CGBS, the Bank prepared and submitted the CGBS' contribution to the Basel Committee's 'Report on International Developments in Banking Supervision' (published in September 2006).

5.7. Administrative Developments

Throughout 2006, the Bank of Jamaica was also involved in the development of an upgraded information technology solution to underpin bank supervision functions. This new Financial Institutions Supervisory Information System (FISIS), developed by external providers, will see bank supervision processes supported by a browser-enabled system running on an Oracle database. During October 2006, Bank commenced implementation of FISIS with commercial banks requested to participate in a parallel run which involved the dual submission of prudential returns via the existing system and FISIS. A notable feature of FISIS is that, where prescribed validation rules are not met, the system will reject institutions' attempts to submit data with appropriate error messages being conveyed.

FISIS also employs data warehouse technology which will enable the use of business intelligence tools for BOJ's reporting and analytical needs. The system is expected to be sufficiently scalable and flexible to accommodate future and evolving supervisory needs such as Basel II and enhancements in consolidated supervision, as well as support the Bank's proactive supervisory stance. It is expected that full implementation for all reporting institutions will be completed by the end of March 2007.

5.8. The Supervised Deposit Taking System

Both the number and market composition of licensed deposit-taking entities (commercial banks, FIA licensees and building societies) remained unchanged during the year (see **Tables 30 and 31**). In April 2006, the Minister of Finance approved the granting of a licence under the Banking Act to **Pan Caribbean Merchant Bank Limited (PCMB)**. At year end the actual issue of the commercial bank license was pending the appropriate change of name of PCMB. PCMB's existing licence under the Financial Institutions Act is to be surrendered.

Table 30 - Market Composition – Number of Deposit-taking Entities*

Supervised Entities	2002	2003	2004	2005	2006
Commercial Banks	6	6	6	6	6
FIA Licensees	10	7	5	5	5
Building Societies	4	4	4	4	4
Total	**20**	**17**	**15**	**15**	**15**

* The proposal by the Minister of Finance for assumption by the Bank of Jamaica of full supervisory responsibility for credit unions which numbered forty-eight at year end-2006, will result in significant expansion of the supervised deposit-taking system (see **Credit Unions**).

Table 31 Licensed Deposit-Taking Institutions as at 31 December 2006

Sub-sector	Institution Name	*Related Deposit-taking Institution*
Commercial Banks	Bank of Nova Scotia Jamaica Limited	*Scotia Jamaica Building Society*
	Citibank N. A.	*Citimerchant*
	FirstCaribbean International Bank (Jamaica) Limited	*FirstCaribbean International Building Society*
	First Global Bank	
	National Commercial Bank Jamaica Limited	
	RBTT Jamaica Limited	
FIA Licensees	Capital & Credit Merchant Bank Limited	
	Citimerchant	*Citibank N. A.*
	DB&G 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	
	Scotia Jamaica Building Society	*Bank of Nova Scotia Jamaica Limited*
	Victoria Mutual Building Society	

5.8.1. System Performance Review

5.8.1.1. Overview

Aggregate assets for all licensed deposit-taking institutions expanded by 15.8 per cent to total $590.8 billion as at 31 December 2006. This surpassed the 5.8 per cent increase reported for 2005 and 12.0 per cent in 2004. Current growth was largely funded from increased deposits and borrowings as well as, to a lesser extent, equity, all of which facilitated expansion in loans and investment portfolios.

Commercial banks maintained their market dominance accounting for an increased share of system assets: 75.1 per cent at end-2006 relative to 73.7 per cent at end-2005[22]. Building societies had the second highest market share of 17.9 per cent at end-2006, slightly higher than the 17.5 per cent at end-2005. In contrast, FIA Licensees market share declined to 7.9 per cent at end-2006, relative to 8.8 per cent at end-2005. This decline was influenced significantly by a strategic balance sheet restructuring that was being undertaken by one licensee (see **Table 32**).

22 Assets are shown net of provision for losses under International Financial Accounting Standards but include guarantees/letters of credits etc.

Table 32

MARKET SHARE OF LICENSED DEPOSIT TAKERS						
	31-Dec-04		31-Dec-05		31-Dec-06	
	J$BN	%	J$BN	%	J$BN	%
Commercial Banks	350.5	72.7	375.9	73.7	438.4	75.1
Building Societies	80.4	16.7	89.3	17.5	105.6	17.9
FIA Licensees	51.1	10.6	44.9	8.8	46.7	7.9
SYSTEM TOTAL	482.0	100.0	510.1	100.0	590.7	100.0

All commercial banks reported larger asset bases, with Bank of Nova Scotia Jamaica Limited and National Commercial Bank Jamaica Limited remaining market leaders. Both accounted for over 70.0 per cent of the asset growth for that sub-sector in 2006 (62.0 per cent in 2005). Of the $62.6 billion growth in assets, deposits funded 58.6 per cent while borrowings funded 26.8 per cent.

While the two larger building societies, Jamaica National Building Society (JNBS) and Victoria Mutual Building Society (VMBS), maintained market leadership of that sub-sector, First Caribbean International Building Society (FCIBS) was able to increase its share to 4.4 per cent at end-2006 from 2.8 per cent at end-2005, influenced by a heightened presence in the mortgage market and increased funding from related companies during the year. This resulted in growth in FCIBS' assets by over 86.8 per cent and contributed to an overall asset accretion of $16.3 billion or 18.2 per cent in the building societies sub-sector compared to $8.9 billion or 11.1 per cent in 2005. Growth was reflected mainly in new mortgages funded from deposit inflows and borrowings.

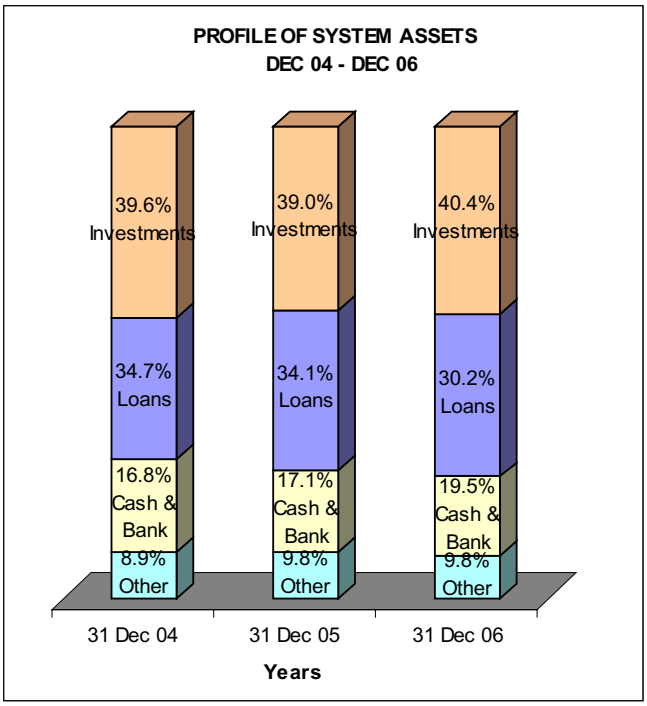
In contrast to the previous year, FIA Licensees reported growth in assets of $1.9 billion or 4.0 per cent (contraction of $6.2 billion or 12.1 per cent in 2005). Of the five licensees, two reported contraction in assets during the review year.

The foreign currency denominated portion of total system assets, grew by US$331.0 million or 10.3 per cent in 2006 as against US$35.0 million or 1.1 per cent during 2005. These assets were funded from an increase of US$413.0 million in foreign currency liabilities of which incremental overseas borrowings accounted for US$237.0 million or 57.3 per cent, while new deposits contributed US$159.0 million or 38.5 per cent. Commercial banks and building societies both reported expansion in foreign currency portfolios by US$314.0 million and US$50.0 million, respectively, while FIA Licensees recorded contraction of US$33.0 million.

5.8.1.2. ***Balance Sheet Profile***

Investments and loans were the fastest growing asset categories within the system during 2006. However, investments continued to account for the largest share, with $233.8 billion, at end-2006 relative to $198.8 billion at end-2005. This reflected annual growth of 17.6 per cent as compared to growth of 39.0 per cent during 2005 (see **Chart 15).**

Chart 15



The system's stock of loans and advances (net of provisions for losses) grew by $31.3 billion to $208.6 billion at end-2006. This represented 34.7 per cent of total assets, up from 34.1 per cent at end-2005. Commercial banks continued to exhibit the most significant increment in credit, accounting for $21.4 billion, followed by building societies with $7.5 billion and FIA licensees with $2.5 billion.

Of the $31.3 billion in incremental credit in the system, domestic currency loans represented 74.7 per cent compared to 60.7 per cent at year-end 2005. Foreign currency loans (inclusive of accretion due to revaluations) expanded by US$81.0 million as against growth of US$133.0 million in 2005. At end-December 2006, the foreign currency portfolio represented 33.2 per cent of total loans (34.6 per cent at end-2005). Of the US$1.0 billion foreign currency loan portfolio, advances to non-foreign currency earners represented 20.4 per cent, similar to end 2005.

On the liabilities side of the balance sheet, deposit inflows accelerated during the year, growing by 14.9 per cent to $370.5 billion, compared to an increase of 8.1 per cent in 2005. All sub-sectors benefitted from new inflows, with the commercial banks dominating the system with $36.7 billion, followed by building societies, $9.5 billion and FIA Licensees, $1.9 billion. Borrowings grew at a faster rate than deposits, increasing by $19.0 billion to $104.6 billion. New deposits funded approximately 60.0 per cent of incremental assets while borrowings funded 23.0 per cent.

Of new deposits, domestic currency accounted for $32.2 billion compared to $13.3 billion recorded in 2005. This represented 67.1 per cent of inflows, up from 55.1 per cent recorded the previous year. Foreign currency deposits grew by US$0.2 billion compared to growth of US$83.0 million at end-2005.

5.8.1.3. Liquidity

The system continued to maintain comfortable liquidity margins in 2006 with liquid assets ratios well above the required minimum in relation to both domestic and foreign currencies[23]. The ratio of domestic currency liquid assets ratio was 37.7 per cent at year-end, above the 34.5 per cent recorded at the end of 2005.

Most licensees maintained liquidity ratios well above requirements in all currencies. There were, however, a few exceptions during the year, where some institutions failed to maintain the required Liquid Assets level as a result of inaccuracies in computation of reservable liabilities. There were also instances of failure to credit respective cash reserve accounts in a timely manner. Consequently, applicable penalties were imposed on the shortfalls under the respective Acts/ Regulations at the rate of 45.0 per cent on domestic currency and 20.0 per cent on foreign currencies.

23 The statutory minimum cash reserve and liquid assets ratios for domestic currency and foreign currencies (required to be held in US Dollar, Canadian Dollar and Pound Sterling) remained at 9 per cent and 23 per cent, respectively, throughout the year. Building Societies that satisfy a residential mortgage threshold of 40 per cent in relation to respective deposit bases qualify for a lower cash reserve ratio of 1 per cent and liquid asset requirement of 5 per cent.

5.8.1.4. Asset Quality

There was further improvement in asset quality in 2006, notwithstanding growth of $0.3 billion (5.9 per cent) in non-performing loans (NPL). Non-performing loans, 3 months and over, totalled $5.4 billion, representing 2.6 per cent of total loans as against 2.9 per cent and 3.0 per cent at end-2005 and end-2004, respectively. However, coverage for specific provisions as per IFRS accounting principles as well as prudentially required loan loss reserves slipped slightly to 99.8 per cent as against 100.0 per cent at the end-2005.

5.8.1.5. Capital

Shareholders' equity for the banking system grew by $10.3 billion or 15.0 per cent, generated primarily from retained earnings, but also reflected an external injection and increments arising from fair value accounting of investments. The narrower statutory capital base comprising permanent forms of equity was strengthened by $6.0 billion or 12.3 per cent, representing transfers from realised profits to mandatory and discretionary statutory reserve funds. One licensee also benefitted from an external injection of $1.3 billion from its parent company.

At year end, all licensees maintained primary and risk weighted capital ratios above the minimum requirements. As the rate of asset growth out-paced that of capital base, the system reflected a marginal contraction in the primary ratio to 9.3 per cent compared to 9.6 per cent at end-2005, which continued to be comfortably above the 6.0 per cent required minimum. The risk weighted Capital Adequacy ratio of 17.3 per cent also remained well above the required minimum of 10 per cent and compares to 18.9 per cent at end-2005.

5.8.1.6. Profitability

Profit margins for 2006 remained strong but marginally below the performance for 2005. This was influenced by the continued fall in market interest rates and the continued significance of investments, combined with the increasing proportion of higher cost borrowing, relative to the cost of deposits. Based on unaudited earnings and expenditure results submitted to the Bank of Jamaica, a system pre-tax profit margin of 25.2 per cent was recorded, relative to 26.0 per cent for 2005, and a return on assets of 3.3 per cent compared to 3.4 per cent for 2005.

Incremental revenue largely comprised interest income from loans and advances of $4.0 billion and investments of $1.0 billion. This was complemented by non-interest income of $1.8 billion from service charges.

Expenses grew by $5.7 billion (11.4 per cent) which was marginally faster than revenue increase of $6.9 billion (10.6 per cent) leading to the slight depression in profit indicators. Significant growth in expense categories were interest on deposits of $1.1 billion, borrowings of $1.4 billion and staff expenses of $1.3 billion.

5.9. Credit Unions

5.9.1. *Supervisory Framework*

During 2006, significant progress was made towards finalization of the draft Bank of Jamaica (Credit Unions) Regulations, to pave the way for submission to Parliament. It is anticipated that the Regulations, which will specify the principles for supervision (inclusive of a licensing regime) will be promulgated during 2007 (See **Financial Legislation**).

5.9.2. *Supervisory Developments*

During the year, the Bank continued its preparatory work in sensitizing credit unions to the requirements of the new supervisory regime and the licensing process that will be implemented under the imminent Regulations. In that regard, credit unions continued to furnish monthly and quarterly prudential returns to the Bank to allow for on-going monitoring of each entity and to enable the Supervisor to keep abreast of the developments in the sub-sector. In addition, the on-site examination programme for credit unions

continued with the completion of the first round during the first half of the year. There was, however, one credit union for which the inaugural first round on-site examination had to be aborted and rescheduled to 2007 due to the unavailability of accurate data to allow for meaningful assessment of its operations. The second round of on-site examinations commenced in the latter half of 2006 and is scheduled to continue in 2007 as the Bank seeks to update its records to inform the decisions regarding recommendations to be made to the Minister for licensing of credit unions. The Bank has continued to provide feedback to the credit unions examined by way of exit review meetings convened with the Board and management of each entity. This is to facilitate the taking of necessary corrective action to address the issues of supervisory concerns prior to introduction of the licensing process under the Regulations.

Audited financial statements, which are also used to enhance Bank of Jamaica's assessment, were submitted by 43 of the 48 credit unions for financial year ended December 2005. Efforts are being made to obtain the outstanding financials from the remaining 5 credit unions.

The Department of Cooperatives and Friendly Societies (which has responsibility for registering cooperative societies, including credit unions), confirmed that during 2006, no new cooperative with deposit taking capability was registered and no mergers occurred. Consequently, the number of credit unions were confirmed at 48 at the end of 2006.

5.9.3. *Credit Union Performance Highlights*

There was continued growth reported in credit union membership during the year, with total membership of 874,471 at end-2006, up from 811,655 at end-2005. The increased membership contributed to the asset growth in the credit union sub-sector with total assets of $38.6 billion reported as at December 2006. This represented an increase of $5.9 billion over 2005 (see **Table 33**).

Loans continued to represent the major asset category and increased by $21.6 per cent to $25.9 billion at end-2006 compared to $21.3 billion at end-2005. Total loans accounted for 67.1 per cent of the assets portfolio at the end of the year, an increase over the 65.3 per cent share as at end-2005. Incremental loan demand was funded by an augmentation in overall savings by 19.2 per cent to $30.4 billion. Loans accounted for 85.5 per cent of total savings compared to 83.7 per cent in 2005.

Table 33

Select Credit Union Data 2002-2006

Year End	No. of Credit Unions	Membership	Total Savings ($BN)	Total Loans ($BN)	Loans/Savings Ratio (%)	Total Assets ($BN)
2002*	56	680,338	16.4	11.1	68.0	20.0
2003*	52	728,447	19.0	13.3	69.7	23.8
2004	50	759,532	22.5	17.4	77.3	28.6
2005	48	811,655	25.5	21.3	83.5	32.6
2006	48	874,471	30.4	25.9	85.5	38.6

*Source of data: Jamaica Co-operative Credit Union League

Table 34

ANNUAL PRUDENTIAL INDICATORS OF COMMERCIAL BANKS, LICENSEES UNDER THE FINANCIAL INSTITUTIONSACT (FIA) AND BUILDING SOCIETIES
31-Dec-06

	COMMERCIAL BANKS			FIA LICENSEES			BUILDING SOCIETIES			System Total (aggregation of all 3 sectors)		
	Dec-04	Dec-05	Dec-06	Dec-04	Dec-05	Dec-06 [b]	Dec-04	Dec-05	Dec-06	Dec-04	Dec-05	Dec-06
Number of institutions in operation	**6**	**6**	**6**	**5**	**5**	**5**	**4**	**4**	**4**	**15**	**15**	**15**
J$MN												
[1]**Total Assets** (incl. contingent accounts)	350,463	375,857	**438,437**	51,124	44,914	**46,733**	80,401	89,331	**105,617**	481,988	510,102	**590,787**
[2]**Total Assets** (excl. contingent accounts)	341,278	364,221	**427,099**	50,437	44,477	**45,908**	80,339	89,267	**105,549**	472,054	497,965	**578,556**
Cash & Bank Balances	78,342	71,785	**79,544**	3,391	2,379	**2,846**	12,286	13,383	**16,910**	94,019	87,547	**99,300**
Investments [incl. Securities Purch.] (net of prov.)	122,699	131,995	**165,914**	38,452	32,072	**29,958**	33,598	34,702	**37,937**	194,749	198,769	**233,809**
Total Loans (gross)	113,369	132,095	**153,449**	6,853	8,670	**11,147**	29,279	36,523	**44,036**	149,501	177,288	**208,632**
Total Loans (net of IFRS prov.) [a]	110,268	129,240	**150,579**	6,781	8,622	**11,098**	28,696	35,865	**43,380**	145,745	173,727	**205,057**
Total Deposits	228,190	246,265	**282,926**	11,436	12,140	**14,017**	58,792	64,076	**73,585**	298,418	322,481	**370,528**
Borrowings (incl. repos)	53,959	54,773	**71,557**	32,151	24,495	**22,635**	3,352	6,362	**10,482**	89,462	85,630	**104,674**
Non-Performing Loans [NPL] (3 mths & >)	3,020	3,071	**3,408**	148	432	**493**	1,319	1,628	**1,534**	4,487	5,131	**5,435**
Provision for Loan Losses	4,098	4,048	**4,288**	155	140	**152**	882	944	**982**	5,135	5,132	**5,422**
[3] **Capital Base**	30,678	33,373	**38,055**	3,554	4,749	**5,205**	6,525	10,805	**11,686**	40,757	48,927	**54,946**
Contingent Accts [Accept., LC's & Guarantees]	9,185	11,636	**11,338**	687	437	**825**	62	64	**68**	9,934	12,137	**12,231**
Funds Under Management	0	0	**0**	176	168	**193**	0	0	**0**	176	168	**193**
Repos on behalf of or for on-trading to clients	0	n/a	**n/a**	0	n/a	**n/a**	0	n/a	**n/a**	0	n/a	**n/a**
%												
Rate of Asset [1] Growth	9.5%	7.2%	**16.6%**	15.1%	-12.1%	**4.0%**	22.4%	11.1%	**18.2%**	12.0%	5.8%	**15.8%**
Rate of Deposit Growth	14.8%	7.9%	**14.9%**	38.1%	6.2%	**15.5%**	18.9%	9.0%	**14.8%**	16.3%	8.1%	**14.9%**
Rate of Loans Growth (gross)	14.3%	16.5%	**16.2%**	15.7%	26.5%	**28.6%**	22.1%	24.7%	**20.6%**	15.8%	18.6%	**17.7%**
Rate of Capital Base Growth	17.2%	8.8%	**14.0%**	4.2%	33.6%	**9.6%**	18.6%	65.6%	**8.2%**	16.1%	20.0%	**12.3%**
Rate of NPL (3 Mths &>) Growth	-2.6%	1.7%	**11.0%**	-3.3%	191.9%	**14.1%**	-8.1%	23.4%	**-5.8%**	-4.3%	14.4%	**5.9%**
Investments :Total Assets [1]	35.0%	35.1%	**37.8%**	75.2%	71.4%	**64.1%**	41.8%	38.8%	**35.9%**	40.4%	39.0%	**39.6%**
Loans (net of prov.):Total Assets [1]	31.5%	34.4%	**34.3%**	13.3%	19.2%	**23.7%**	35.7%	40.1%	**41.1%**	30.2%	34.1%	**34.7%**
Fixed Assets:Total Assets [1]	2.2%	2.1%	**1.8%**	0.3%	0.4%	**0.7%**	2.3%	2.2%	**2.0%**	2.0%	1.9%	**1.8%**
Liquidity												
Average Domestic Currency Cash Reserve: Average Prescribed Liabilities [4]	9.0%	9.0%	**9.0%**	9.1%	9.0%	**9.0%**	1.0%	1.0%	**1.0%**	7.1%	7.0%	**7.0%**
Average Domestic Currency Liquid Assets: Average Domestic Prescribed Liabilities [4]	38.4%	38.1%	**42.3%**	127.2%	39.7%	**33.6%**	24.8%	23.8%	**24.4%**	35.9%	34.5%	**37.7%**
Asset Quality												
Prov. For Loan Losses:Total Loans (gross)	3.6%	3.1%	**2.8%**	2.3%	1.6%	**1.4%**	3.0%	2.6%	**2.2%**	3.4%	2.9%	**2.6%**
Prov. For Loan Losses: NPL (3 Mths &>)	135.7%	131.8%	**125.8%**	104.7%	32.4%	**30.8%**	66.9%	58.0%	**64.0%**	114.4%	100.0%	**99.8%**
NPL (3 Mths &>):Total Loans (gross)	2.7%	2.3%	**2.2%**	2.2%	5.0%	**4.4%**	4.5%	4.5%	**3.5%**	3.0%	2.9%	**2.6%**
NPL (3 Mths &>): (Total Assets [1] + Provision for loan losses)	0.9%	0.8%	**0.8%**	0.3%	1.0%	**1.1%**	1.6%	1.8%	**1.4%**	0.9%	1.0%	**0.9%**
Capital Adequacy												
Deposits + Borrowings: Capital (:1)	9.3	9.1	**9.4**	12.4	7.8	**7.2**	9.7	6.6	**7.3**	9.6	8.4	**8.7**
Capital Base:Total Assets [1]	8.8%	8.9%	**8.7%**	7.0%	10.6%	**11.1%**	8.1%	12.1%	**11.1%**	8.5%	9.6%	**9.3%**
[5] Capital Adequacy Ratio [CAR]	17.7%	17.9%	**16.1%**	14.2%	25.4%	**21.2%**	14.5%	20.5%	**20.5%**	16.7%	18.9%	**17.3%**
NPL (3 mths &>):Capital Base+Prov for loan losses	8.7%	8.2%	**8.0%**	4.0%	8.8%	**9.2%**	17.8%	13.9%	**12.1%**	9.8%	9.5%	**9.0%**
Profitability												
[6] Pre - tax Profit Margin (for the Calendar Quarter)	21.2%	25.3%	**22.6%**	24.3%	27.6%	**20.2%**	44.2%	18.0%	**27.5%**	25.8%	24.2%	**23.3%**
Pre - tax Profit Margin (for the Calendar Year)	21.6%	26.6%	**25.9%**	15.8%	27.6%	**21.2%**	26.7%	22.4%	**23.5%**	22.1%	26.0%	**25.2%**
Return on Average Assets (for the Calendar Quarter)	0.7%	0.9%	**0.8%**	0.6%	0.7%	**0.5%**	1.7%	0.6%	**0.8%**	0.9%	0.8%	**0.7%**
Return on Average Assets (for the Calendar Year)	3.0%	3.7%	**3.5%**	1.4%	2.6%	**2.3%**	3.9%	2.8%	**2.8%**	3.0%	3.4%	**3.3%**
[7] Income Assets/Expense Liabilities (as at 31 December)	101.2%	101.6%	**102.7%**	107.3%	113.7%	**115.1%**	109.0%	110.3%	**108.4%**	103.1%	104.2%	**104.7%**

Notes:
n/a not applicable

- Based on unaudited data submitted to BOJ by supervised institutions up to 01 February 2007. Prior years indicators may have revisions arising from amendments, which in instances include IFRS restatements.

[a] - Effective January 2004, the Bank of Jamaica revised its reporting requirements in line with International Financial Reporting Standards (IFRS) and in this regard the following change was effected:
The composition of "Provision for Loan Losses" has been segregated into two (2) distinct components being:
i) provision for losses computed in accordance with IFRS; and
ii) any incremental provisioning necessary under prudential loss provisioning requirements.
Consequently, "Total Loans (net of prov.)" represents gross loans net of IFRS loan loss provisions per (i) above

[b] - During April 2006, the Minister of Finance approved the granting of a licence under the Banking Act to Pan Caribbean Merchant Bank Limited (PCMB), which will be issued once the appropriate change of name of PCMB is effected.

[1] Total Assets and Liabilities reflected net of Provision for Losses and include Contingent Accounts (Customer Liabilities for Acceptances, Guarantees and Letters of Credit). In keeping with IFRS, Total Assets and Liabilities were redefined to include Contingent Accounts and in this regard, Current Year Ratios were computed in accordance with this principle and prior years were restated.
[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 institution.
- Building Societies: (Permanent Capital Fund + Deferred Shares + Capital Shares + Reserve Fund + Retained Earnings Reserved Fund) less impairment by net losses of individual society.
[4] Prescribed Liabilities include:
(i) deposit liabilities, (ii) reservable borrowings and interest accrued and payable on (i) & (ii).
[5] Capital Adequacy Ratio (CAR): Qualifying Capital (Tier 1 + Tier 2 capital items less prescribed deductions) in relation to Risk Weighted Assets and Foreign Exchange Exposure.
- As at December 2004, the Bank of Jamaica implemented new Quarterly Capital Adequacy Returns which provide more precise ratios. Therefore, ratios prior to December 2004 were estimated.
[6] Data includes extraordinary income/expenditure and adjustments for prior period.
[7] Income Assets comprise FC Cash Reserves, Placements, Investments, Repo Assets and Loans less Non-Performing Loans (3 months & over).
Expense Liabilities comprise Deposits and Borrowings including Repo Liabilities (from BOJ, Banks, OFI etc).

Statutory Reserve Requirements :

	COMMERCIAL BANKS			FIA LICENSEES			BUILDING SOCIETIES**		
	Dec-04	Dec-05	Dec-06	Dec-04	Dec-05	Dec-06	Dec-04	Dec-05	Dec-06
Required Special Deposit Ratio *	5.0%	1.0%	n/a	5.0%	1.0%	n/a	n/a	n/a	n/a
Required Cash Reserve ratio	9.0%	9.0%	9.0%	9.0%	9.0%	9.0%	1% / 9%	1% / 9%	1% / 9%
Required Liquid Assets ratio (incl Cash Reserve)	23.0%	23.0%	23.0%	23.0%	23.0%	23.0%	5% / 23%	5% / 23%	5% / 23%

* 5% Special Deposit requirement imposed on Commercial Banks and FIA Licensees in Jan 2003 pursuant to Section 28 A (1) of the Bank of Jamaica Act.
Effective 1 March 2005, the required Special Deposit Ratio was reduced to 3%, followed by a second reduction to 1% on 16 May 2005.
Effective 1 May 2006, the Special Deposit Ratio was removed.
** 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.

6. Supervision Of Cambios and Remittance Companies

In 2006, the Bank continued to regulate cambios and remittance companies in keeping with its mandate under the BOJ Act. This was achieved through on-site inspection and in-house monitoring of the operations of all cambios and primary agents (companies licensed in Jamaica to offer the service as agents of remittance companies domiciled overseas).

The major objective of the on-site inspections was to assess the entities' adherence to the BOJ Operating Directions relevant to each entity type and the anti-money laundering legislation. This was achieved through semi-annual visits to licensed locations to conduct examination of the records and operations of these entities.

Through in-house monitoring, the BOJ ensured that:

- All requirements were satisfied prior to the issue of operating licences including the assessment of relevant personnel under the BOJ 'fit and proper' criteria;
- The requirements for renewal of licences were satisfied; and
- The entities adhered to daily reporting requirements of the BOJ.

The Bank continued to assess operators of cambios and remittance companies under the 'fit and proper' criteria during 2006, to ensure the integrity of the persons who are being authorised to offer these services. In this regard, 95 persons were assessed in relation to cambios while 185 were assessed in relation to remittance companies. This compares to 122 and 402 in 2005 for cambios and remittance companies, respectively[24].

6.1. Cambios

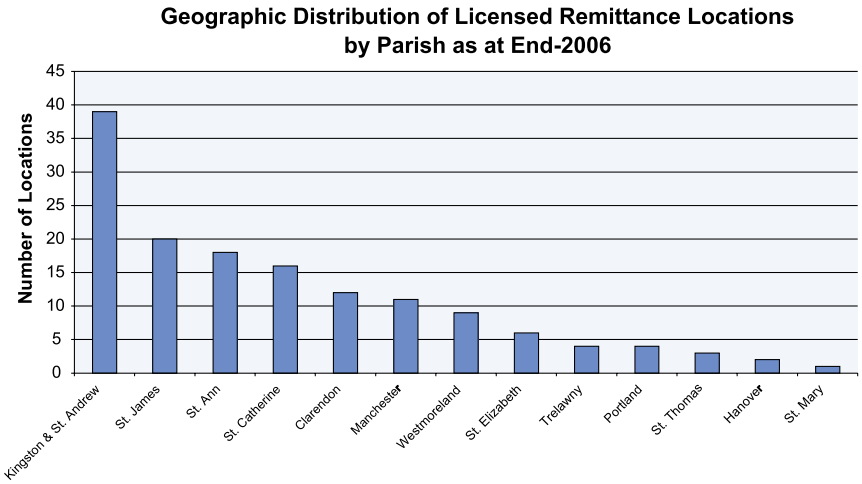
During 2006, 2 new cambio locations were approved while 6 were closed due to the voluntary surrender of the licences by the operators. This brought the number of cambio locations at the end of the review year to 145, representing 66 entities. This compares to 148 locations representing 69 entities at end-2005 (see **Table 35)**. Kingston and St. Andrew continued to account for the largest concentration of cambios (26.9 per cent) in 2006 (see **Chart 16).**

Table 35

Status of Cambio Licences as at 31 December 2006		
	2005	2006
New Locations Licensed	13	3
Locations Closed	3	6
Number of Locations	148	145
Number of Entities	69	66

24 Directors and majority shareholders holding 10 per cent or more of the shares of the each company and the manager of each proposed location

Chart 16



6.2. Remittance Companies

The number of licenced primary agents declined to 13 at end-2006 from 17 at end-2005 as 4 primary agents ceased operations during 2006 (see **Table 36**).

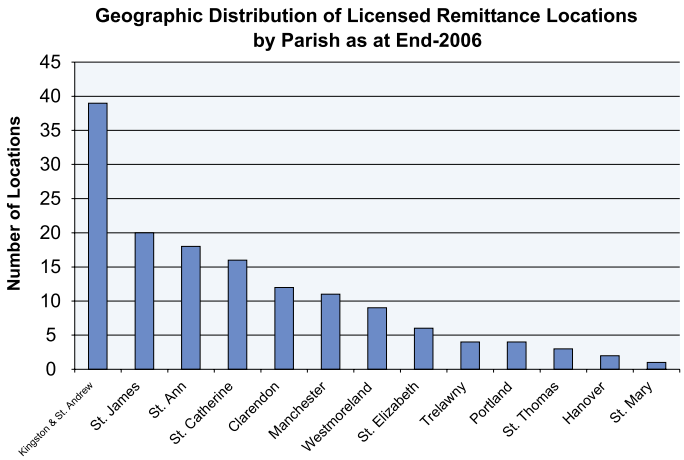
Table 36

Status of Remittance Licences as at 31 December 2006		
	2005	**2006**
New Locations Licensed	253	174
Locations Closed	0	22
Number of Locations	253	405
Number of Primary Agents	17*	13

** of which 10 were licensed*

These primary agents operated from 405 locations island-wide at end-2006 as against 253 at the end of 2005. Kingston and St. Andrew accounted for the largest concentration with 21.2 per cent at end-2006 as against 23.7 per cent at end-2005 (see **Chart 17**).

Chart 17



7.1. International Economic Developments

7.1. 1 Overview

Global economic growth is estimated to have accelerated by 0.4 percentage point to 5.2 per cent in 2006, reflecting faster expansion among the major industrialised economies, particularly the USA and the Euro area. There was moderation in the rate of expansion in the emerging market economies in 2006, influenced by a deceleration in growth in Developing Asia. Despite the deceleration, China and India recorded the highest rate of economic growth in the world. Growth also accelerated in the Caribbean region in 2006, driven principally by Trinidad & Tobago.

World inflation continued to increase in 2006, albeit marginally, due mainly to the lagged effects of higher energy prices. Annual average inflation in the advanced economies increased by 0.1 percentage point in 2006, led by Japan and the UK. Inflation in the developing countries, however, decelerated by 0.1 percentage point, relative to 2005.

Commodity prices rose at a slower rate in 2006. In particular, oil prices increased by 17.0 per cent for the year, relative to a 36.2 per cent growth in 2005. Non-fuel commodity prices rose by 28.5 per cent, mainly influenced by a significant increase in metal prices.

The currencies of selected advanced economies reflected mixed changes, relative to the US dollar in 2006. The Euro and the Great Britain Pound (GBP) appreciated against the dollar in the context of a faster pace of monetary tightening in the two countries as well as concerns relating to macroeconomic imbalances in the USA. On the other hand, the Japanese Yen and the Canadian dollar weakened against the US dollar in 2006. The Canadian dollar weakened as declines in oil prices in the second half of the year affected export revenues, while the depreciation of the Yen reflected the relatively weak economic performance of that country as well as increases in US/Japan interest rates differentials.

Trade negotiations in 2006 were generally unfavourable. There was a breakdown in World Trade Organisation (WTO) trade talks in mid-July, as members failed to agree on issues related to agriculture. A request by the USA for an extension of the waiver regarding the Caribbean Basin Economic Recovery Act (CBERA) was denied by the WTO. More positively, Jamaica and five other CARICOM member states brought the Caribbean Single Market (CSM) into effect on 30 January 2006.

7.1. 2 Industrial Countries

Real GDP growth among the advanced economies accelerated by 0.5 percentage point to 3.0 per cent in 2006, relative to the growth in 2005. With the exception of Canada, the selected advanced economies all recorded a faster rate of growth (see **Table 37**).

There was an acceleration in real output growth in the USA to 3.4 per cent, largely reflecting the expansion in the first and fourth quarters as growth slowed considerably during the second and third quarters of 2006. The slowdown in growth in the third quarter may have reflected the impact of increases in energy prices and monetary policy tightening. The overall increase in economic activity for the year was influenced by an improvement in net exports, largely related to the depreciation of the US dollar against the currencies of its major trading partners. While consumption expenditure increased by 3.2 per cent, this was at a slower pace than in 2005. Similarly, growth in private investment spending slowed to 4.6 per cent, compared with 5.4 per cent in 2005. This was influenced by a reduction of 4.2 per cent in residential investment.

For the other industrialized economies, the faster rate of economic expansion was primarily the result of growth in investment spending.

In particular, the German economy recorded an acceleration in growth, associated in part with that country's hosting of the 2006 Fédération Internationale de Football Association (FIFA) World Cup. The acceleration in the UK's growth rate was mainly driven by private consumption. The expansion in the Japanese economy in 2006 was driven by increased private fixed capital investment, in the context of strong growth in the profits of corporate entities and bank credit. In contrast, the deceleration in real GDP growth in Canada reflected a decline in exports in the context of the slowdown in the US economy in the second and third quarters as well as a fall in oil prices in the latter part of the year.

The average unemployment rate among the advanced economies declined by 0.4 percentage point to 5.6 per cent in 2006. Unemployment in the USA fell by 0.5 percentage point to 4.5 per cent, reflecting job growth in the services industries. The unemployment rate in the Euro area also fell to 7.9 per cent, compared with 8.6 per cent in 2005. For Canada, the reduction in the unemployment rate to 6.3 per cent, from 6.8 per cent in 2005, reflected growth of 2.1 per cent in employment, the fastest pace since 2002, and was concentrated in services.

The acceleration in inflation that began in 2005 among the major developed economies continued into 2006, and was principally due to higher inflation in the UK and Japan. In the UK, the annual average inflation rate accelerated by 0.3 percentage point to 2.3 per cent, reflecting the impact of increases in energy related prices and tuition fees. The fairly significant acceleration in Japan was also influenced by higher prices of energy related products and, to a lesser extent, commodity imports. There was, however, a deceleration in inflation in the USA and Canada to 3.2 per cent and 2.0 per cent in 2006, respectively, relative to 3.4 per cent and 2.2 per cent in 2005. These declines were influenced by reductions in crude oil prices over the last half of the year. Inflation remained stable in the Euro area.

Inflation among the advanced economies was constrained by monetary tightening by the major central banks. In the USA, the Federal Reserve (Fed) raised interest rates four times by 25 basis points (bps) on each occasion to 5.25 per cent by the middle of the year. Similarly, the Bank of Canada (BOC) increased rates in the first half of 2006 by an overall 100 bps to 4.25 per cent. Both the Fed and the BOC stopped tightening monetary policy in the second

Table 37

INDUSTRIAL ECONOMIES
Real GDP, Consumer Prices and Unemployment Rates
(Annual percentage change and per cent of labour force)

Country	GDP		Unemployment Rate		Inflation Rate		Current Account (% of GDP)	
	2005	2006*	2005	2006*	2005	2006	2005	2006*
Advanced Economies	2.5	3.0	6.0	5.6	2.3	2.4		
USA	3.2	3.4	5.1	4.5	3.4	3.2	-6.4	-6.6
UK	1.9	2.7	4.8	5.3	2.0	2.3	-2.2	-2.4
Euro area	1.4	2.6	8.7	7.9	2.2	2.2	0.2	-0.1
Canada	2.9	2.8	6.8	6.3	2.2	2.0	2.3	2.0
Japan	1.9	2.1	4.4	4.1	-0.2	1.4	3.6	3.7

Source: The World Economic Outlook, September 2006, Statistics Offices of individual countries
** Estimates*

half of the year in the context of a fall in inflation expectations. In Europe, the Bank of England (BoE) increased rates twice in the last half of the year, while the European Central Bank (ECB) increased rates five times throughout the year. The Bank of Japan (BoJ) also raised rates in mid July to 0.25 per cent, after holding the rate at zero since early 2001.

Table 38

ADVANCED ECONOMIES: EXCHANGE RATES				
	US Dollars per unit of national currency		%Change	
	2005	2006	2005	2006
Canadian Dollar	0.83	0.88	7.24	6.79
Japanese Yen/[1]	110.0	116.30	-1.73	-5.71
Pound Sterling	1.82	1.84	-0.62	1.21
Euro	1.25	1.26	0.20	0.88

1 Expressed as local currency per unit of US dollars.
Source: US Federal Reserve

The currencies of selected industrialised economies reflected mixed movements against the US dollar in 2006. The GBP and the Euro appreciated by 1.2 per cent and 0.9 per cent, respectively, relative to the US dollar. However, the US dollar appreciated against the Yen and Canadian dollar by 5.7 per cent and 6.8 per cent, respectively (see **Table 38**). The strengthening of the GBP and the Euro relative to the US dollar reflected investors' concerns about the sustainability of the US current account deficit as well as the relatively faster pace of monetary tightening by the ECB and the BoE during the last half of 2006. The depreciation of the Canadian dollar reflected the impact of falling oil prices on Canadian export earnings during the latter months of the year. In addition, the foreign exchange market reacted to an announced plan by the government to introduce a tax on the earnings of foreign owned trust funds. For the Japanese Yen, the depreciation against the US dollar reflected the response of private capital flows to widening interest rate differentials, as well as a comparatively lower growth performance.

7.1.3. Developing Economies

The average growth rate among the developing countries remained robust at 7.3 per cent in 2006 (see **Table 39**). This rate, while being marginally below that of 2005, represented an improvement relative to the annual average of 6.3 per cent over the period 2001 to 2005. All regions, with the exception of the Western Hemisphere and the Middle East, experienced slight deceleration in growth. The acceleration in growth for the Western Hemisphere region largely reflected the performance of Trinidad & Tobago, Brazil, Mexico. Jamaica also experienced significant improvements in its growth rate, relative to the previous year.

There was a deceleration in the rate of growth of the Asian economies to 8.7 per cent in 2006 from 9.0 per cent in 2005. The slowdown in growth was the result of a moderation in demand from the USA. Notwithstanding the moderation, growth within this region remained the fastest in the world. China and India continued to experience significant growth rates despite attempts at controlling investment spending through monetary tightening and administrative controls.

Table 39

Selected Developing Countries
Real GDP & Consumer Prices
(Annual Per cent Change)

Country	GDP		Inflation Rate**	
	2005	2006*	2005	2006*
Developing Countries	**7.4**	**7.3**	**5.3**	**5.2**
Western Hemisphere	**4.3**	**4.8**	**6.3**	**5.6**
Latin America				
Argentina	9.2	8.0	9.6	10.9
Brazil	2.3	3.2	6.9	4.2
Chile	6.3	5.2	3.1	3.5
Colombia	5.2	5.2	5.0	4.7
Costa Rica	5.9	6.5	13.6	13.0
Dominican Republic	9.3	9.0	4.2	7.8
Ecuador	4.7	4.4	2.1	3.3
Mexico	3.0	4.4	4.0	3.5
Paraguay	2.9	3.5	6.8	8.6
Uruguay	6.6	6.5	4.7	6.3
Venezuela	9.3	7.5	15.9	13.7
Caribbean				
Antigua & Barbuda	5.0	7.1	2.1	3.5
Barbados	3.9	3.5	6.0	6.3
Dominica	3.4	3.0	1.6	1.5
Guyana	-3.0	3.5	6.9	7.5
Jamaica	1.4	2.5	15.3	8.6
St. Kitts & Nevis	6.7	5.2	3.6	2.0
St. Lucia	5.4	6.0	3.9	5.5
Trinidad & Tobago	7.9	12.5	6.9	7.7
Developing Asia	**9.0**	**8.7**	**3.5**	**3.8**
China	10.2	10.7	1.8	1.5
India	8.5	8.3	4.0	5.6
Indonesia	5.6	5.2	10.5	13.0
Malaysia	5.2	5.5	3.0	3.8
Philippines	5.0	5.0	7.6	6.7
Thailand	4.5	4.5	4.5	4.9
Middle East	**5.7**	**5.8**	**7.7**	**7.1**

Sources: The World Economic Outlook, September 2006,
Regional Economic Outlooks
Statistics Offices of individual countries,
*Estimates, **Annual average

Growth in the Caribbean accelerated in 2006 in the context of continued high oil prices as well as strong foreign and local investment activities related to the Cricket World Cup and recovery from an over-active hurricane season in 2005. Due primarily to high oil prices, Trinidad & Tobago retained its position as the fastest growing economy in the region since 2001. The acceleration in growth in most Caribbean countries was related to increased activity in the construction sector as the region prepared for the ICC Cricket World Cup in 2007. There was a marked turn-around in economic activity in Guyana as that economy recovered from the effects of severe flooding in 2005.

Inflation in developing countries decelerated by 0.1 percentage point to 5.2 per cent in 2006. This reflected significant monetary tightening in the Western Hemisphere, in the context of the implementation of formal inflation targetting regimes in some Latin American countries. Average inflation rates for the Caribbean, however, rose, due to the adverse effects of increases in oil prices. Inflation in Developing Asia also accelerated slightly, reflecting double-digit inflation in the ASEAN-4 region, due to a sharp rise in administered fuel prices in Indonesia[25].

3.3.4. Commodity Markets

For 2006, commodity prices, as measured by the IMF's Index of Primary Commodity Prices (IPCP), increased by 22.0 per cent, following a 29.2 per cent rise in 2005. The increase in the IPCP was attributed to significant growth in both energy (19.3 per cent) and non-fuel (28.5 per cent) commodity prices. With respect to non-fuel prices, the prices of agricultural raw materials went up by an average of 10.7 per cent, reflecting the impact of increases in grain prices, while metal prices grew by an average of 56.5 per cent in 2006, following an increase of 26.4 per cent in 2005 (see **Table 40**).

Table 40

SUMMARY OF WORLD COMMODITY PRICES

Annual Average per cent change

	2005	2006
All Primary Commodities	29.2	22.0
1. Non-fuel Commodities	10.3	28.5
1.1 Edibles	1.6	9.5
(a) Food	-0.4	9.9
(b) Beverages	21.0	6.3
1.2 Industrial Inputs	17.6	42.6
(a) Agricultural Raw Materials	1.5	10.7
(b) Metals	26.4	56.5
2. Energy	38.7	19.3
Petroleum /1	36.1	17.0

Sources: The World Economic Outlook, September 2006,

/1 West Texas Intermediate measure

25 The ASEAN-4 are the four least developed countries (LDCs) and economies in market-based transition in South-East Asia –Cambodia, Lao People's Democratic Republic (PDR), Myanmar and Vietnam

The increase in metals prices was largely associated with growth in the prices of copper, zinc and nickel, reflecting robust demand from China as well as supply concerns (in the context of historically low inventory levels) and deterioration in ore quality. Aluminium prices also increased on average by 35.4 per cent in 2006.

The food sub-index of the non-fuel group increased by 9.9 per cent in 2006, reflecting a significant rise in the price of grains. The average price of wheat, which increased by 26.4 per cent in 2006, was influenced primarily by the worst drought to affect Australia in a century. Corn prices rose by 23.5 per cent, largely due to unfavourable weather in the US Midwest, in addition to strong demand for corn as an input into ethanol production.

Crude oil prices, as measured by the West Texas Intermediate index, averaged US$66.09 per barrel in 2006, representing an increase of 17.0 per cent relative to 2005. Oil prices reached a record high of US$77.03 per barrel on 14 July 2006. This increase was primarily due to growth in demand and continued supply uncertainty in the context of geopolitical tensions in the Middle East and Nigeria.

Growth in demand in 2006 was slightly lower than that recorded in 2005. The International Energy Agency (IEA) reported an increase of 0.9 per cent in world demand to 84.4 million barrels per day (bpd) in 2006, following an increase of 1.5 per cent in 2005. Oil consumption increased in China and the Middle East but fell slightly in Europe and Japan. The overall increase in oil demand for 2006 was underpinned by buoyant global activity in the first two quarters of the year, associated, in part, with an acceleration in economic growth in the USA during the first half of 2006, relative to the similar period in 2005.

World supply also rose by a similar 0.9 per cent over the year to 85.4 million bpd, a slight deceleration from the 1.0 per cent growth rate in 2005. This expansion occurred in the context of increased supply from non-Organization of Petroleum Exporting Countries (OPEC) producers such as Canada, the UK and Russia. Despite the overall balance in the world market for crude oil, excess demand pressures were evident among the OECD countries where inventory levels fell in the fourth quarter by about 0.45 million barrels more than the normal seasonal decline.

The oil market was also adversely affected by speculation amidst concerns related to the intensification of the tension over the Islamic Republic of Iran's nuclear programme. The market was also affected by the outbreak of fighting in Lebanon and Israel in August and the closure of a large Alaskan oil field by BP Corporation. Continued violence in the Nigerian oil-producing region and security threats to Iraqi oil infrastructure also contributed to market fears about potential supply shortages.

Some easing of geopolitical tensions, slowing economic growth and favourable winter temperatures contributed to oil prices falling by 14.9 per cent in the fourth quarter. This prompted OPEC to announce production cuts of 1.2 million bpd in October and 0.5 million bpd in December.

7.1.5. International Trade Developments

7.1.5.1. The Caribbean Single Market (CSM)

Jamaica was one of six CARICOM member states (Barbados, Belize, Guyana, Jamaica, Suriname and Trinidad & Tobago) to officially endorse the Caribbean Single Market (CSM) on 30 January 2006 in Kingston. Antigua & Barbuda, Dominica, Grenada, St. Kitts & Nevis, St. Lucia and St. Vincent & the Grenadines joined on 3 July. The CSM is intended to provide more opportunities to produce and sell the region's goods and services, as well as attract investment. This will be achieved through the creation of a single economic space among the participating member states. Competitive production achieved from regional integration is also expected to lead to a greater variety and quantity of products and services to trade with other countries. The CSM is expected to become the Caribbean Single Market and Economy (CSME) on 01 January 2009.

7.1.5.2. The World Trade Organization (WTO)

A meeting of the Trade Negotiations Committee was held in Geneva from 28 June to 01 July 2006 at the WTO headquarters to discuss "modalities" in agriculture and industrial products. These included formulas for cutting tariffs and subsidies in agriculture. A discussion of the Work Programme on Small Economies was also on the agenda for this meeting. This programme was established to address trade-related issues identified for the fuller integration of small, vulnerable economies into the multilateral trading system.

Deadlock among G-6 countries on matters relating to market access and domestic support forced the suspension of the negotiations at the end of July. The suspension of talks threatens the benefits expected to accrue to the Caribbean, including the reduction of agricultural distortions, the duty-free/quota-free package for least-developed countries' exports and "aid for trade".

7.1.5.3. Trade Preferences

Several preferential market access schemes in which Caribbean countries have participated continued to come under threat from both developing and developed countries. A further request by the USA for an extension of the Caribbean Economic Basin Recovery Act (CBERA) was denied by the WTO's Council for Trade in Goods[26]. In addition, the European Union's request for an extension of the waiver for the tariff rate quota for bananas of the African, Caribbean and Pacific (ACP) countries was blocked because of diverging views on the issue. On the positive side, an extension for the CARIBCAN Initiative was granted until 31 December 2011.

The reform of the EU-ACP Sugar Regime began on 01 July 2006. The reform process involves, *inter-alia*, a 39.0 per cent price cut over four years, with a 5.0 per cent reduction in 2006. ACP producers were granted €40.0 million in 2006 and are to receive an additional €165.0 million in 2007 to assist in cushioning the impact of the reforms. The ACP and Less Developed Countries have, however, called for a slower phase-in of the reform, as well as for more assistance.

26 The Caribbean Basin Economic Recovery Act and the Caribbean Basin Trade Partnerships Act (CBTPA) were collectively known as the Caribbean Basin Initiative (CBI). A request for the extension of the waiver regarding the CBERA , which expired in 2005 was denied in 2006. The CBTPA will expire in 2008.

7.1.5.4. PetroCaribe Initiative

On 14 August 2006, Jamaica and Venezuela signed several bilateral development loans agreements under the PetroCaribe Initiative. These loans include funding for the construction of a leg of Highway 2000 and the expansion of the Petrojam Oil Refinery. Amendments were also made to the original Agreement to regularise an additional 2 500 bpd supplied to Air Jamaica. Under the PetroCaribe Initiative, which was signed on 6 September 2005, Venezuela ships 21 000 barrels of oil daily to Jamaica, but allows the Government to withhold 40 per cent of the cost as a loan repayable in 25 years at an interest rate of one per cent per annum.

7.1.5.5. Cement Tariff

In the context of cement shortages in early 2006 and growing demand for the product in the construction sector, the Government of Jamaica (GOJ), on 08 March 2006, announced the reduction of duties on the importation of cement to the Common External Tariff (CET) rate of 15.0 per cent[27]. The GOJ subsequently removed all duties until June 2007. The Trade Board had projected the annual shortfall in the industry at approximately 300 000 metric tonnes.

27 In 2004, the Government imposed safeguard duties of 25.8 per cent, in addition to the 15.0 per cent common external tariff on cement imports, to ensure a US$100.0 million investment in Carib Cement Company Limited.

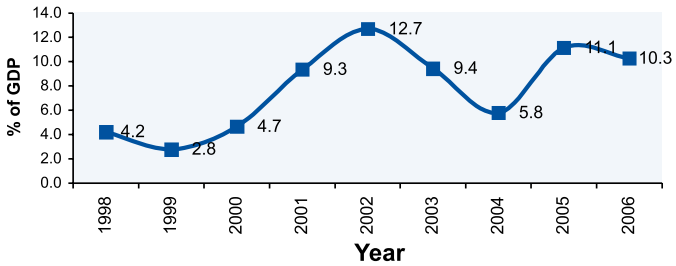
7.2. Balance of Payments

7.2.1. Overview

The current account deficit of Jamaica's balance of payments (BOP) is estimated to have widened marginally by US$17.7 million to US$1 096.4 million (10.3 per cent of GDP) in 2006. The deterioration in the current account reflected increases in the deficits on the merchandise trade and income accounts, partly offset by higher surpluses on the current transfers and services accounts. The wider deficit on the merchandise trade balance largely reflected the impact of increases in the prices of imported commodities, particularly oil, which was partially offset by growth in receipts from alumina exports, tourism and private transfers. The latter benefitted from stronger growth in the major developed and emerging market economies (see **International Economic Developments**).

Chart 18

Jamaica: Current Account Deficit to GDP



More than adequate financing for the current account deficit was provided by net private and official investment inflows. In this context, the NIR of the BOJ increased by US$230.1 million to US$2 317.5 million at 31 December 2006, with gross reserves representing 17.9 weeks of imported goods and services.

Table 41

SUMMARY OF BALANCE OF PAYMENTS (US$M)			
	2005[1/]	2006[2/]	Change
CURRENT ACCOUNT	**-1078.7**	**-1096.4**	**-17.7**
A. GOODS BALANCE	**-2581.3**	**-2944.8**	**-363.5**
Exports (f.o.b.)	1664.3	2117.3	453.0
Imports (f.o.b.)	4245.6	5062.0	816.4
B. SERVICES BALANCE	**600.1**	**802.4**	**202.3**
Transportation	-273.8	-322.2	-48.4
Travel	1295.7	1613.9	318.2
Other Services	-421.8	-489.2	-67.4
GOODS & SERVICES BALANCE	**-1981.2**	**-2142.3**	**-161.1**
C. INCOME	**-675.9**	**-680.6**	**-4.7**
Compensation of employee	88.5	101.0	12.5
Investment income	-764.4	-781.6	-17.2
D. CURRENT TRANSFERS	**1578.4**	**1726.5**	**148.1**
General Government	137.0	130.2	-6.8
Other Sectors	1441.4	1596.4	155.0
2. CAPITAL & FINANCIAL A/C	**1078.7**	**1096.4**	**17.7**
A. CAPITAL ACCOUNT	**-2.7**	**2.0**	**4.7**
General government	0.3	4.5	4.2
Other Sectors	-3.0	-2.6	0.4
B. FINANCIAL ACCOUNT	**1081.4**	**1094.4**	**13.0**
Official Investment	409.0	578.0	169.0
Private Investments[3/]	901.3	746.6	-154.8
Reserves[4/]	-228.9	-230.1	-1.2

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

7.2.2. Merchandise Trade

The deficit on the merchandise trade account expanded by US$363.5 million in 2006 (see **Table 41**). This reflected an increase of US$816.4 million (19.2 per cent) in spending on imports (f.o.b.), which was partly offset by an expansion of US$453.0 million (27.2 per cent) in earnings from exports. The growth in imports and exports in 2006 both exceeded the respective five-year historical average growth rates of 7.3 per cent and 1.7 per cent.

Exports

The growth in total export earnings was influenced primarily by a 29.5 per cent expansion in earnings from **General Merchandise Exports**. **Goods Procured in Ports** also increased in 2006, while there was a marginal contraction in **Free-zone Exports**. The increase in earnings from **General Merchandise Exports** emanated from expansions in all categories, in particular *Non-Traditional and Major Traditional Exports* (see **Table 42)**.

Table 42

TRADITIONAL & NON-TRADITIONAL EXPORTS (US$M)

	2005 1/	2006 2/	Change	% Change
GENERAL MERCHANDISE EXPORTS	**1531.5**	**1983.5**	**452.0**	**29.5**
DOMESTIC EXPORTS	1501.7	1947.8	446.1	29.7
Major Traditional Exports	1100.6	1256.9	156.4	14.2
Bauxite	98.8	113.3	14.5	14.7
Alumina	920.3	1040.5	120.3	13.1
Sugar	76.8	89.7	12.9	16.8
Bananas	4.7	13.4	8.7	185.8
Other Traditional Exports	59.5	80.8	21.3	35.8
Citrus	1.6	2.8	1.2	77.8
Cocoa	1.4	2.0	0.7	50.8
Coffee	17.3	32.1	14.8	85.3
Pimento	2.9	1.4	-1.4	-50.6
Rum	34.3	41.0	6.7	19.6
Gypsum	2.1	1.5	-0.6	-30.1
Non Traditional Exports	341.6	610.0	268.4	78.6
RE-EXPORTS	29.8	35.7	5.9	19.7
FREEZONE EXPORTS	**56.8**	**54.1**	**-2.7**	**-4.7**
GOODS PROC. IN PORTS	**76.0**	**79.7**	**3.7**	**4.9**
GRAND TOTAL	**1664.3**	**2117.3**	**453.0**	**27.2**

1/ Revised

2/ Estimates

The performance of *Major Traditional Exports* in 2006 reflected increased earnings from all commodities, in particular alumina. Growth in alumina export earnings was attributed to a 16.8 per cent increase in the average realised price. However, the effect of this was partly offset by a 3.2 per cent decline in the volume exported. Movement in alumina prices resulted from continued strong demand for aluminium from China (see **International Economic Developments**) and a reduction in supply, the latter being associated with the closure of a number of smelters in the United States and Germany. The decline in the volume of alumina exports largely reflected disruptions in production due to technical problems at Windalco and Alpart.

With respect to other major exports, bauxite export earnings grew by 14.7 per cent in 2006, principally reflecting an 11.9 per cent increase in volume. This occurred in the context of capacity expansion in the industry (see **Production and Prices**). In addition, the value of sugar exports expanded by 16.8 per cent in 2006, reflecting a 24.1 per cent growth in export volume, the effect of which was partly offset by a 5.9 per cent decline in prices. Increased export volume resulted from the normalization in production activities following the disruptions caused by adverse weather during the 2004/05-crop year. The fall in the price of sugar was influenced by the implementation of the first phase of the price cuts under the European Union (EU) sugar regime on 01 July 2006. Earnings from banana exports were also estimated to have tripled in 2006, reflecting a normalisation in production and export activities, following the destruction of the crop by Hurricane Ivan in 2004.

Total earnings from O*ther Traditional Exports* increased by 35.8 per cent in 2006, mainly influenced by coffee exports (see **Table 42**). Coffee exports benefitted from increased production, consequent on the favourable weather conditions since the passage of Hurricane Ivan in 2004. The value of *Non-Traditional Exports* expanded by 78.6 per cent to US$610.0 million in 2006, principally reflecting normalisation in the export of mineral fuel, which had been affected by the extended closure of the Petrojam oil refinery in 2005. In the context of the global increase in metal prices, the export of 'waste and scrap metal' also emerged as one of the most significant non-traditional exports in 2006.

Imports

Total expenditure on imports (c.i.f.) increased by US$919.0 million in 2006, representing the largest annual increase on record. This occurred in the context of a sharp increase in estimated FDI for the year. This expansion emanated primarily from an increase of US$911.0 million in the value of **General Merchandise Imports**, which reflected robust growth in the importation of *Mineral Fuels, Machinery & Transport Equipment, Chemicals, Manufactured Goods and Food* (see **Table 43**). Spending on *Machinery & Transport Equipment*, which accounted for 28.5 per cent of the increase in general merchandise imports, was influenced by the purchase of motorbuses, cars and a power barge. The increase in *Food, Manufactured Goods and Fuel* imports reflected the growth in the prices of these commodities in 2006 (see **International Economic Developments)**. Mineral fuels remained the largest category of imports and represented 16.5 per cent of GDP in the review year.

Table 43

VALUE OF IMPORTS BY SITC (C.I.F.) (US$MN)

	2005[1/]	2006[2/]	Change	% Change
TOTAL GENERAL IMPORTS	**4739.4**	**5650.4**	**911.0**	**19.2**
0. FOOD	602.9	616.8	13.9	2.3
1. BEVERAGE. & TOBAC.	55.9	68.4	12.4	22.2
2. CRUDE MATS.	79.2	82.4	3.3	4.1
3. MINERAL FUELS	1360.1	1758.5	398.4	29.3
4. ANI. & VEG. OIL	27.7	25.2	-2.5	-8.9
5. CHEMICALS	555.3	680.4	125.1	22.5
6. MANUF. GOODS	637.8	696.1	58.3	9.1
7. MACH. & TRANSP.	870.0	1130.1	260.1	29.9
8. MISC. MANUF. GOODS	477.2	510.8	33.6	7.1
9. MISC. COMMDS.	73.3	81.8	8.4	11.5
FREEZONE	**15.5**	**19.0**	**3.5**	**22.3**
GOODS PROC. IN PORTS	**112.3**	**116.8**	**4.5**	**4.0**
GRAND TOTAL	**4867.3**	**5786.3**	**919.0**	**18.9**

1/ Estimates

7.2.3. Services

Net earnings from **Services** increased by an estimated US$202.3 million in 2006, influenced primarily by an expansion in the surplus *on Travel* (see **Table 41**). There were partial offsetting increases in the deficits on *Other Services* and *Transportation.*

Transportation

Net payments for transportation services were estimated at US$322.2 million in 2006, an increase of US$48.4 million, relative to 2005. The widening of the deficit on *Transportation* stemmed from an increase of US$117.5 million in gross payments, mainly associated with freight charges on higher volumes of imported goods. Partially offsetting the growth in these payments was an increase of US$69.2 million in inflows, influenced largely by a significant expansion in stopover visitor arrivals.

Travel

Gross earnings from visitor expenditure were estimated to have increased by 16.1 per cent to US$1 887.3 million (17.7 per cent of GDP) in 2006. This was partly offset by an estimated increase of US$24.0 million in the total expenditure of Jamaicans travelling overseas.

The expansion in earnings from tourism mainly reflected respective increases of 17.7 per cent and 13.5 per cent in cruise visitor and stopover arrivals (see **Table 44**). Total visitor arrivals in 2006 surpassed three million for the first time in Jamaica's history. Tourism earnings also benefitted from an increase of 8.5 per cent in the average daily expenditure of stopover visitors.

Increased marketing and promotional activities, coupled with additional airlift capacity, influenced the growth in tourist arrivals. This coincided with an increase in the number of attractions, including the return of a major music festival, Reggae Sunsplash, as well as the addition of two new hotels. A relatively inactive hurricane season in 2006 as well as the diversion of business from Cancun and Cozumel, which had been affected by hurricanes in 2005, also contributed to the growth in visitor arrivals.

Table 44

VISITOR ARRIVAL STATISTICS ('000s)			
	2005[1/]	2006 [2/]	% Change
Total Stopovers	**1478.7**	**1678.9**	**13.5**
Foreign National Stopovers	1387.0	1578.2	13.8
Non-resident Jamaican Stopovers	91.7	100.7	9.9
Cruise Passengers & Armed Forces	**1135.8**	**1336.5**	**17.7**
Total Visitors	**2614.5**	**3015.4**	**15.3**
Average Daily Expenditure (US$)	**102.9**	**111.7**	**8.5**
Gross Estimated Expenditure (US$M)	**1545.1**	**1887.3**	**22.2**

[1/] *Revised*

[2/] *Provisional*

All the major source markets recorded increases in stopover visitor arrivals in 2006. For the second consecutive year, arrivals from the USA, Jamaica's main source market, exceeded one million. Visitor arrivals from this market grew by 12.5 per cent and coincided with additional airlift to the Island. Visitor arrivals from Canada and Europe expanded by 31.4 per cent and 17.1 per cent, respectively. The introduction of new and chartered airlines from Toronto and Halifax primarily accounted for the improved performance from Canada. With respect to Europe, the expansion largely reflected growth in stopover arrivals from the United Kingdom, Jamaica's second largest source market. This expansion was principally related to the introduction of service by Virgin Airlines in the middle of the year, as well as increased promotion of the Island in Europe.

The growth in cruise passenger arrivals was mainly influenced by a 10.8 per cent increase in the number of ship calls to the Island during the year. This performance occurred in the context of the diversion of vessels from other ports, in particular Cancun, in the aftermath of the passage of Hurricane Ivan. The growth in calls also benefitted from a relatively inactive hurricane season, as well as the commencement of service in June 2006 by the *Freedom of the Seas*, the largest cruise ship in the world.

Growth in stopover arrivals to Jamaica compared favourably with the average for the Caribbean in 2006 (see **Table 45**). Jamaica outperformed the average for the region in relation to growth in cruise passenger arrivals (see **Table 46**).

Table 45

Stopover Visitor Arrivals (Selected Caribbean Countries)			
	2005	**2006**	**% Change**
Bahamas*	1 270.2	1 276.4	0.5
Barbados	547.3	563.2	2.9
Dominican Republic	3 691.9	3 965.1	7.4
Jamaica	**1 478.7**	**1 678.9**	**13.5**
Martinique	484.2	502.1	3.7
St Lucia	318.1	302.5	-4.9
Total	**7 790.4**	**8 288.2**	**6.4**

Source: Caribbean Tourism Organization
**Jan-Oct*

Table 46

Cruise Visitor Arrivals (Selected Caribbean Countries)			
	2005	**2006**	**% Change**
Bahamas**	2 681 664	2 509 263	-6.4
Barbados*	397 462	351 574	-11.5
Cayman Islands	1 798 788	1 930 136	7.3
Jamaica	**1 135 843**	**1, 336 453**	**17.7**
St. Lucia	394 364	359 593	-8.8
St. Maarten	1 488 461	1 438 211	-3.4
Total	**7 896 852**	**7 925 320**	**0.4**

Source: Caribbean Tourism Organization
**Jan-Sep*
***Jan-Oct*

Other Services

The deficit on *Other Services* widened by US$67.4 million in 2006, principally influenced by an expansion of US$65.5 million in outflows[28]. The estimated expansion in outflows mainly reflected an increase of US$58.1 million in payments for other business services, mainly associated with growth in visitor arrivals during the year.

28 *Other services* include communication, computer & information, other business and Government services.

7.2.4. Income

The deficit on the income account widened by US$4.7 million in 2006. This higher deficit largely reflected an expansion of US$17.2 million in net investment income outflows, influenced primarily by respective increases of US$36.0 million and US$14.2 million in the imputed profit remittances of the direct investment companies and official interest payments (see **Table 41**). An increase of US$33.2 million in BOJ's interest income from its foreign assets partially offset the higher payments.

7.2.5. Current Transfers

The surplus on the current transfers account increased by US$148.1 million in 2006 (see **Table 47**). This improvement reflected growth of 7.7 per cent in gross private inflows, supported by a decline in gross private outflows. In contrast, gross official inflows fell by 4.6 per cent due primarily to the non-repetition of grant flows associated with hurricane relief in 2005. Gross official outflows remained relatively flat in 2006 when compared with 2005. The performance of private transfers coincided with the acceleration in world growth in 2006, relative to the previous year.

Table 47

CURRENT TRANSFERS (US$MN)			
	2005[1/]	**2006[2/]**	**Change**
TOTAL RECEIPTS	**1935.8**	**2066.5**	**130.7**
General Government	142.1	135.3	-6.8
Private Sector	1793.7	1931.2	137.6
TOTAL PAYMENTS	**357.3**	**340.3**	**-17.1**
General Government	5.1	5.1	0.0
Private Sector	352.2	335.1	-17.1
NET CURRENT TRANSFERS	**1578.4**	**1726.5**	**148.1**

1/ Revised
2/ Estimates

Remittance companies continued to be the major conduit for private transfers in 2006, accounting for 51.0 per cent of total inflows, relative to 53.6 per cent in 2005. The share of inflows through the

financial system expanded to 39.8 per cent in 2006, from 36.7 per cent the previous year. For the postal system, the share remained flat in 2006, while the share attributed to other agencies declined to 9.1 per cent from 9.6 per cent in 2005.

7.2.6. Capital and Financial Account

The capital account recorded a surplus of US$2.0 million in 2006, relative to a deficit of US$2.7 million in 2005. The surplus on the financial account increased by US$13.0 million in 2006 largely reflecting a US$169.0 million increase in official investments (see **Table 41**).

Table 48

FOREIGN EXCHANGE RESERVES (US$MN) As at 31 December	2005[1/]	2006[2/]	Change
GROSS FOREIGN ASSETS	**2 176.7**	**2 406.8**	**230.1**
Bank of Jamaica	2 169.0	2 399.1	230.1
Central Government	0.8	0.8	0.0
Other Official Institutions	6.9	6.9	0.0
GROSS FOREIGN LIABILITIES	**81.6**	**81.6**	**0.0**
NET INTERNATIONAL RESERVES	**2 095.1**	**2 325.2**	**230.1**
Weeks of estimated imports of goods and services	18.9	17.9	

1/ Revised

2/ Provisional

Net *official investment inflows* increased by US$169.0 million in 2006 stemming from a reduction of US$395.4 million in payments, which was partly offset by a fall of US$226.4 million in gross official receipts (see **Table 49**). The fall in total outflows was principally associated with a decline in GOJ debt payments, which was supported by lower outflows from the Bank. The decline in gross official investment inflows reflected the non-repetition of international borrowing to finance the operations of Air Jamaica, the national airline, as well as a reduction in Government activities on the international bond market. Gross official inflows included a Eurobond for US$250.0 million.

Within the financial account, net private and official investment inflows of US$578.0 million and US$746.6 million, respectively, were more than sufficient to finance the deficit on the current account. In this context, there was a build-up of US$230.1 million in the NIR. This reflected an increase of US$230.1 million in the country's gross foreign assets to US$2 399.1 million at end December 2006, representing an estimated 17.9 weeks of imported goods and services (see **Table 48**).

Table 49

OFFICIAL INVESTMENT FLOWS (US$MN)	2005[1/]	2006[2/]	Change
GROSS OFFICIAL INFLOWS	**1 442.7**	**1 216.3**	**-226.4**
Donor Countries	0.0	0.0	0.0
Multilateral Institutions	0.0	0.0	0.0
Other Assistance	1 375.3	1 099.1	-276.2
Project Loan	67.4	117.2	49.8
GROSS OFFICIAL OUTFLOWS	**1 033.7**	**638.3**	**-395.4**
Government Direct	647.2	398.9	-248.3
Bank of Jamaica	386.5	239.4	-147.1
NET OFFICIAL INVESTMENTS	**409.0**	**578.0**	**169.0**

1/ Revised

2/ Provisional

7.3. Foreign Exchange Management

7.3.1. Bank of Jamaica International Reserves

The stock of gross foreign assets of the Bank of Jamaica was US$2 399.1 million as at end-2006, US$230.1 million above the level at end- 2005 (see **Table 50**). The growth in the stock was largely attributed to net foreign currency purchases from the market.

Table 50

BANK OF JAMAICA GROSS FOREIGN ASSETS	
As At end-December 2006 US$MN	
Opening Gross Foreign Assets (GFA)	2,169.0
Inflows	1,825.2
Outflows	(1,592.9)
/1 Adjustment to GFA	(2.3)
Closing Gross Foreign Assets	2,399.1

/1 - Unrealized loss on foreign currencies and other investments.

Bank of Jamaica's foreign liabilities as at end-2006 remained unchanged at US$81.6 million, relative to end-2005. The foreign liabilities peaked at US$294.8 million during the March quarter, as a result of the GOJ's issue of a US$250 million Eurobond (see **Table 51**). These funds were held on deposit with the Central Bank and were utilized during subsequent quarters for amortization of external debt by the GOJ.

Given the changes in the gross foreign assets and liabilities, the net international reserves (NIR) of the BOJ was US$2 317.5 million at end-2006, reflecting an increase of US$230.1 million, relative to end-2005. The strongest growth in the reserves occurred in the September quarter. This happened in the context of improved inflows to the foreign exchange market, which facilitated the Bank's net purchase of US$245.9 million from the market. By the end of the quarter the stock was US$2 342.0 million**.** In the December quarter, the NIR declined by US$24.4 million reflecting relatively higher foreign currency debt payments during that quarter.

Table 51

BANK OF JAMAICA NET INTERNATIONAL RESERVES (NIR) (end of period) US$MN						
	2005 Dec.	2006 Mar.	June	Sept.	Dec.	Annual Change ($)
NIR	2087.4	2078.1	2110.1	2342.0	2317.5	230.1
Gross Foreign Assets	2169.0	2372.9	2293.2	2474.7	2399.1	230.1
Foreign Liabilities	81.6	294.8	183.2	132.7	81.6	0.0

Foreign Exchange Inflows and Outflows

Inflows

Foreign exchange inflows to BOJ for 2006 totalled US$1 825.2 million, US$722.2 million lower than in 2005. The decline in inflows in 2006 reflected lower levels of debt raising by way of GOJ foreign currency bonds, relative to the total offered in 2005. Purchases from the market during 2006 represented the primary source of inflows (see **Table 52**).

Total market purchases amounted to US$1 005.2 million, increasing marginally by US$4.2 million relative to 2005. These purchases accounted for approximately 55.1 per cent of total inflows and comprised US$430.6 million and US$574.6 million purchased under the surrender arrangement and through the trading room, respectively[29].

The purchase of foreign currency from GOJ Eurobond proceeds by the Bank amounted to US$447.4 million for the year, with all sources, excepting G*rants,* declining relative to 2005. In particular, total GOJ bond receipts amounted to US$340.5 million in 2006, relative to US$780.2 million in 2005.

Purchases of US$259.9 million from the bauxite sector during 2006 were US$38.9 million higher than in 2005. This increase was in a context where the sector continued its expansion projects.

29 Under the surrender arrangement, authorized dealers and cambios agree to sell to the BOJ 5% -10% of their purchases from the clients segment of the market.

Table 52

Inflows of Foreign Exchange US$MN	Inflows 2005	Inflows 2006	Change ($)
Bauxite Receipts	**221.0**	**259.9**	**38.9**
Market Purchases	**1 001.0**	**1 005.2**	**4.2**
Surrenders to BOJ			
- Authorised Dealers	231.2	293.4	62.2
- Cambios	134.8	137.2	2.5
Other purchases	635.0	574.6	-60.4
GOJ Foreign Currency Receipts	**1 223.5**	**447.4**	**-776.2**
- Eurobond	542.7	248.2	-294.5
- Local/Regional US$ bond	246.5	92.3	-154.2
- Other loans	430.7	83.9	-346.9
of which Air Jamaica	*321.5*	*0.0*	*-321.5*
Grants	3.6	23.0	19.4
Other Receipts*	**101.9**	**112.8**	**10.8**
Total Cash Inflow	**2 547.4**	**1 825.2**	**-722.2**

*** Includes income earned on foreign assets, net prudential reserve inflows and funds lodged to sundry GOJ accounts at the BOJ.**

Outflows

Foreign currency outflows for 2006 totalled US$1 592.9 million, US$641.1 million lower than the value for 2005 (see **Table 53**). Outflows from all categories with the exception of 'other payments' declined. Public sector debt payment of US$893.5 million, approximately US$257.0 million lower than in 2005, accounted for the largest decline in a context where there were no Eurobond bullet payments in 2006.

During 2006, Air Jamaica Limited withdrew its remaining deposits of US$59.4 million. This was significantly lower than the drawdown of US$264.3 million in 2005, and largely accounted for the decline of $224.3 million in the *Other GOJ Payments* category relative to 2005.

The BOJ sold US$572.9 million to the market in 2006, US$168.3 million lower than the volumes in 2005. The lower sales occurred in a context of the relative foreign exchange market stability experienced during most of the year.

Table 53

Outflows of Foreign Exchange
US$MN

	Outflows		
	2005	**2006**	**Change**
Public Sector Debt	**1 150.5**	**893.5**	**-257.0**
- Principal	730.3	447.9	-282.4
- Interest	420.3	445.6	25.4
Other GOJ Payments	332.5	108.2	-224.3
Direct Sales	741.2	572.9	-168.3
Other Payments	9.9	18.3	8.4
Total Cash Outflow	**2 234.0**	**1 592.9**	**-641.1**

7.3.2. Reserve Management

Performance

The gross foreign assets of the Bank of Jamaica amounted to US$2 399.1 million at the end-December 2006, an increase of US$230.1 million or 10.6 per cent, relative to end-December 2005 (see **Table 55**). Foreign income of US$106.0 million was US$33.4 million or 46.1 per cent more than in 2005 (see **Table 54**). This was due mainly to the increase in average foreign assets holdings, a partial restructuring of the bond portfolio and increases in short-term foreign interest rates during the year. Income earned over the period translated to a return on investment of 4.67 per cent per annum compared to a return of 3.49 per cent per annum in 2005.

Table 54

FOREIGN INVESTMENT INCOME FOR YEAR ENDED 31 DECEMBER				
	2005		2006	
ASSETS	**US$MN**	**%**	**US$MN**	**%**
Money Market Investments	37.10	51.14	50.28	47.44
Bond Holdings	27.03	37.26	45.11	42.56
External Fund	1.75	2.41	3.35	3.16
Other	6.67	9.19	7.25	6.84
TOTAL	**72.55**	**100.00**	**105.99**	**100.00**
Portfolio Return	**3.49**		**4.67**	
Average Income Earning Assets	**2 079**		**2 271**	

The Fed Funds rate increased by a total of 100 basis points during the year, ending marginally above expectations at 5.25 per cent per annum. These developments set the interest rate floor in the target market and served to create opportunities for managing the portfolio towards a higher rate of average return. Income on the money market investments, which contributed 47.4 per cent of total income for the period, was driven by investments in United States Agency Bonds, Eurodollar deposits and to a lesser degree, Auction Rate Certificates.

Investment Strategy

There were no significant changes to the Bank's investment strategy during the year (see **Table 55**). However, there was continued focus on attainment of the Bank's stated objectives which are prioritized as follows: (i) maintenance of liquidity, (ii) preservation of capital and (iii) maximization of returns. In this context, the portfolio remained biased towards US dollar-denominated positions which enabled the Bank to respond to the intervention needs of the foreign exchange market as well as to satisfy the Government's foreign exchange requirements for debt service payments.

The capacity to carefully measure and manage the risk of the fixed income portfolio became paramount as the year witnessed lacklustre bond market conditions that relied heavily on tactical security selection. Duration changes were accomplished primarily through selective trading and product diversification.

Portfolio Distribution

The Bank increased its bond holdings to 40.4 per cent from 37.6 per cent in a context where the benchmark 10-year United States Treasury yield moved to a high of 5.25 per cent at end-June from a low of 4.34 per cent per annum in January (see **Table 55**). As yields in the bond markets increased, the environment provided an opportunity for repositioning of the Bank's bond portfolio to optimize its value in the medium term.

Table 55

Distribution of Investments by Asset Class at 31 December				
	2005		2006	
ASSETS	US$MN	%	US$MN	%
Money Market Investments	1 256.45	57.93	1 183.88	49.35
Bond Holdings	815.57	37.60	968.87	40.38
Balance Held Abroad	53.87	2.48	128.77	5.37
External Fund	43.15	1.99	117.59	4.90
TOTAL	2 169.04	100.00	2 399.11	100.00
Average Income Earning Assets	2 079		2 271	
Portfolio Return %		3.49		4.67

During the second half of the year there was limited volatility along the Treasury curve as the 10-year benchmark traded within a tight range of 4.55 per cent per annum – 5.00 per cent per annum. During this period any small upward pressure on yields was viewed as a buying opportunity in what became characterized as a low yield market. In response to market weakness, the bond strategy employed included the extension of call options and stringent duration management. At 31 December 2006, the bond portfolio had an effective duration of 2.46 years and a weighted average yield to maturity of 5.57 per cent.

Throughout the year the portfolio shifted towards a more defined barbell structure. Currently 56.0 per cent of the investment portfolio is concentrated in the short term and 25.0 per cent in the long term[30].

7.3.3. The Foreign Exchange Market

The foreign exchange market was relatively stable during 2006, as evidenced by a slower pace of depreciation as well as a lower level of market sales by the Bank. The weighted average selling rate (WASR) of the US dollar depreciated by 3.8 per cent, relative to 4.6 per cent in 2005, while sales to the market were lower by US$168.3 million. The slower pace of depreciation occurred in a context of favourable macro-economic conditions, particularly in the June and September quarters. At end-2006, the WASR was US$1.00 = J$67.15 compared to US$1.00 = J$64.58 at end-2005. The Jamaica Dollar also depreciated by 4.5 per cent against the Canadian dollar and 16.1 per cent against the Great Britain Pound, with the latter being influenced by monetary tightening in the United Kingdom.

Following a depreciation of 1.40 per cent in the March 2006 quarter, the rate of depreciation in the WASR slowed in the June and September quarters to 0.81 per cent and 0.03 per cent, respectively. Foreign exchange market stability during these two quarters was

30 A "barbell" structure is a bond holding strategy with less exposure to medium term maturities, and relatively greater weight on long and short term maturities.

underpinned by a confluence of positive factors including:

- Improvements in the domestic economic outlook owing to favourable outturns in key macroeconomic variables such as inflation and fiscal performance;
- Significant decline in world oil prices, which tempered the impact of fuel-related imports on US dollar demand; and
- A pause in monetary tightening in the US, since August 2006.

These conditions contributed to increased inflows to the market and anchored selling rates around an average of US$1.00 = J$65.87 for the 6-month period.

Notwithstanding the overall stability, transient demand pressures emerged around the end of the June quarter. This was partly associated with the issue of an 11.00 percent 10-year US dollar bond by the Jamaica Public Service Company Limited. In the context of an increased demand for US dollar denominated assets, given the steady narrowing in the interest rate differential since the start of the year, this bond offer was deemed to be attractive. The pause in the benchmark Fed Funds Rate following sustained increases over a 2-year period, resulted in the abatement of concerns regarding further narrowing in the Jamaican - US interest rate differential. Consequently, by the middle of the September quarter, this resulted in investors converting US dollars for investment in Jamaica Dollar assets. This was manifested in a reduction in the reported foreign currency position of authorized dealers from a long position of US$80.2 million at end-June to a short position of US$33.2 million at end-September. In addition, strong FDI flows boosted supply during the quarter, evidenced by per diem purchases of US$26.3 million, relative to US$24.8 million and US$20.5 million in the June 2006 quarter and September 2005 quarter, respectively.

The December quarter, on the other hand, was characterized by seasonal excess demand for foreign currency to pay for imports as well as to satisfy dealers' demand to cover short positions. In this context, the Bank augmented supply of foreign currency to the extent of US$224.7 million, approximately 40.0 per cent of total market sales in 2006. This was significantly below sales of US$416.4 million for the comparative period of 2005. Notwithstanding market sales by the Bank, the WASR depreciated by 1.6 per cent during the December quarter, the sharpest quarterly change for 2006. The level of exchange rate depreciation in the December 2006 quarter, however, was lower than the 2.6 per cent depreciation for the corresponding period of 2005.

Foreign currency transactions reported by authorized dealers and cambios in 2006 were significantly higher than in 2005, with purchases and sales reflecting increases of 25.3 per cent and 25.4 per cent, respectively (see **Table 56**). Excluding intervention, average daily purchase and sales volumes during 2006 were US$46.7 million and US$46.8 million, respectively, compared to US$36.2 million for both average daily purchases and sales volumes during 2005 (see **Table 57**). Authorized dealers registered a 5.0 percentage point reduction in market share in 2006, thereby accounting for 63.3 per cent of total foreign exchange sales, with cambios accounting for 36.7 per cent.

Table 56

Purchases and Sales of Foreign Currency (US$MN)				
Quarter	**Purchases**		**Sales**	
	2005	**2006**	**2005**	**2006**
March	2 177.4	2 897.9	2 156.9	2 878.8
June	2 328.2	3 071.8	2 453.4	3 045.7
September	2 517.5	3 217.0	2 500.4	3 326.9
December	2 754.0	3 067.2	2 680.6	3 027.5
TOTAL	**9 777.1**	**12 254.0**	**9 791.2**	**12 278.9**

Includes BOJ Intervention

Table 57

Daily Average Trading Volumes (US$MN)						
2006						
	Purchases			**Sales**		
Quarter	**From Earners**	**Inter-Dealer**	**Total**	**To End-Users**	**Inter-Dealer**	**Total**
March	23.5	19.9	43.4	23.3	19.9	43.2
June	24.8	22.6	47.4	23.6	23.3	47.0
September	26.3	23.9	50.2	28.0	23.9	51.9
December	27.1	18.8	45.8	26.4	18.8	45.2
Average per diem	**25.4**	**21.3**	**46.7**	**25.3**	**21.5**	**46.8**
2005						
Quarter	**From Earners**	**Inter-Dealer**	**Total**	**To End-Users**	**Inter-Dealer**	**Total**
March	22.0	13.3	35.3	21.9	13.0	34.9
June	21.2	14.8	36.0	23.2	14.7	37.9
September	20.8	14.8	35.6	20.7	14.6	35.3
December	22.1	15.6	37.7	20.5	16.0	36.5
Average per diem	**21.5**	**14.6**	**36.2**	**21.6**	**14.6**	**36.2**

Data exclude BOJ Intervention

8.1. Production

Overview

Jamaica's Gross Domestic Product (GDP) grew at a rate of 2.5 per cent for the review year, following seven consecutive years of marginal growth, averaging 1.3 per cent (see **Chart 19**). This growth emanated primarily from agriculture and tourism, which in total contributed in excess of 70.0 per cent to the overall GDP outturn (see **Table 58**). The increased activity occurred in the context of a stable macroeconomic environment, characterized by declining inflation, stable financial markets, an improvement in external competitiveness, favourable weather conditions as well as relatively strong external demand. In this context, business expectations improved significantly in the latter half of the year. Further, growth reflected the impact of foreign direct investments in the economy, improvements in productivity in certain sectors as well as post hurricane recovery. Growth was, however, affected by supply constraints in the construction industry.

Chart 19

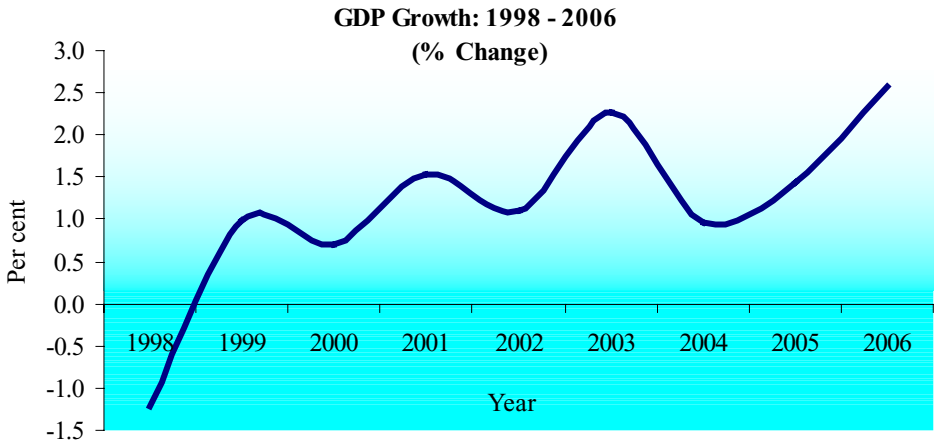


Table 58

SECTORAL CONTRIBUTION TO GDP GROWTH (%)		
Sectors	**Jan –Dec 2006**	**Contribution (2006)**
1. GOODS	1.1	14.7
AGRICULTURE FORESTRY & FISHING	15.9	39.9
MINING & QUARRYING	1.7	3.9
MANUFACTURING	-2.4	-13.0
CONSTRUCTION & INSTALLATION	-2.2	-8.5
2. SERVICES	3.2	91.4
BASIC SERVICES	4.4	31.4
Electricity & Water	3.7	5.5
Transport, Storage & Communication	4.7	26.0
OTHER SERVICES	2.8	60.0
Distributive Trade (Wholesale & Retail)	1.4	12.3
Financing & Insurance Services	2.1	7.1
Real Estates & Business Services	2.4	4.9
Producers of Government Services	0.1	0.3
Miscellaneous Services	10.4	34.0
Households & Private Non-Profit Instit.	0.4	0.1
3. LESS IMPUTED SERVICE CHARGES	2.3	6.1
TOTAL GDP	2.5	100.0

Source: STATIN

Sectoral Developments

Expansion in the economy was reflected in both the goods producing and services sectors. For the goods producing sector, growth was displayed in **Agriculture, Forestry & Fishing** and **Mining & Quarrying**, as **Construction & Installation** and **Manufacturing** recorded declines**.** Within services, **Miscellaneous Services, Transport, Storage & Communication** and **Electricity & Water** were the main areas of growth.

After two consecutive years of sizable declines due to adverse weather, **Agriculture, Forestry & Fishing** grew significantly by 15.9 per cent and was the largest contributor to GDP growth (see **Chart 20**). **Agriculture, Forestry & Fishing** expanded consistently throughout the year, registering the strongest growth of 22.9 per cent in the March quarter. Growth occurred in both the D*omestic* and *Export Agriculture* sub-sectors. Activity within the industry was driven by improved labour productivity and increased banking system credit to the sector (see **Chart 21**). With regard to output per hectare, the ratio surpassed levels obtained in 2005, driven largely by improved farming practices, such as the introduction of green house farms, hydroponics and better irrigation systems[31].

31 Output per hectare increased to 13.2 tonnes relative to 12.6 tonnes in 2005.

Chart 20

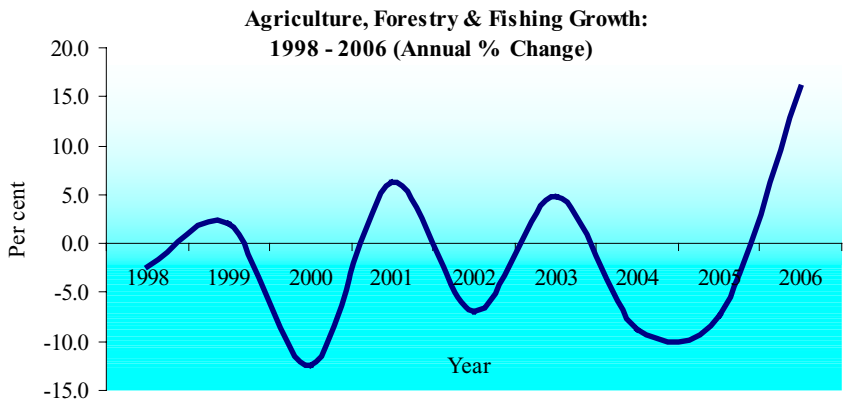
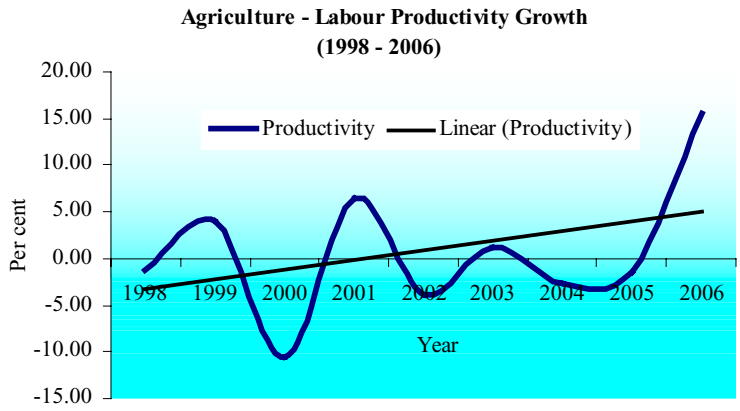


Chart 21



Growth in production was also attributable to the favourable weather conditions experienced island-wide since the start of 2006, which influenced increased crop establishment and yields.

Domestic crop production is estimated to have grown by 19.4 per cent (see **Table 59**). All crop groups, with the exception of cereals recorded increases within the year. In particular, there was considerable growth in the production of plantains, representing output from newly established fields following damage to farms by hurricanes in 2004 and 2005.

Table 59

SELECTED DOMESTIC CROP PRODUCTION

Crop Group	Production ('000 tonnes) 2005	2006	% Change
Yams	107.2	123.0	14.6
Vegetables	145.1	167.1	12.1
Other tubers	27.6	35.6	29.2
Fruits	34.7	45.9	32.4
Condiments	27.1	30.1	11.1
Plantains	8.9	22.0	145.6
Potatoes	33.0	36.0	9.3
Legumes	4.9	5.5	12.1
Cereals	1.92	1.90	-1.6
Total	**391.7**	**467.8**	**19.4**

Source: Ministry of Agriculture

However, the sector's performance was challenged by the limited availability of tractor service for land preparation and increases in the cost of inputs such as fertilizers, pesticides and some planting materials. The continued high level of praedial larceny also hampered the sector's performance.

Export Agriculture improved by 46.1 per cent in 2006, reflecting considerable recovery in citrus and banana production. Both industries were devastated by Hurricane Ivan in 2004 and were further affected by adverse weather conditions in 2005. With the improvement in weather conditions in 2006 and improved farming practices, production accelerated in the review year (see **Table 60**).

Table 60

SELECTED EXPORT CROP PRODUCTION

Crop	2005	2006	% Change
	Exports[1] ('000tonnes)		
Banana	11.6	31.8	175.2
Citrus	4.1	10.2	147.0
Cocoa	0.7	0.5	-17.5
Coffee	1.0	1.2	15.8
Pimento	0.5	0.5	10.0
	Production (000'tonnes)		
Sugar cane[2]	1445.2	1671.5	8.3

Sources: ***Bank of Jamaica Estimates & Sugar Corporation of Jamaica***

There was a moderate increase of 1.7 per cent in **Mining & Quarrying** during the review year, representing a deceleration in growth when compared to the previous year. This slower rate of growth was partly associated with the marginal growth of 0.3 per cent in alumina production, compared to 1.6 per cent in 2005. This lower output was influenced by prolonged labour disputes during the first half of the year and technical problems at one of the alumina plants during the third quarter. As a result, the capacity utilisation rate for alumina registered a marginal decline to 92.5 per cent compared to 92.8 per cent during 2005. The impetus for growth within the sector emanated primarily from bauxite production. For the year, crude bauxite production grew considerably by 12.3 per cent, reflective of an increase of approximately 11.0 per cent in capacity. However, the capacity utilisation rate for bauxite expanded marginally to 91.0 per cent from 90.0 per cent in 2005.

Following six consecutive years of moderate growth, economic activity in **Construction & Installation** contracted in 2006. Construction activity within the first three quarters of the year was affected by the shortage of cement on the domestic market, stemming from internal problems at the sole cement plant. These factors resulted in the postponement of a number of new construction projects and delays in existing projects. The situation was further exacerbated by a shortage of cement on the international market and lengthy delays in imports. Against this background, the sector recorded an average quarterly decline of 4.1 per cent over this period. Activity on the domestic market accelerated in the December quarter with the normalisation of cement supply from local production and imports. In this context, the sector grew by 1.6 per cent in the December quarter. This growth was, however, insufficient to offset the declines registered over the first three quarters of the year.

Manufacturing recorded a second consecutive year of contraction in 2006, registering a decline of 2.4 per cent. This decline was against an average growth of 0.1 per cent recorded over the previous five years. The outturn was attributed to a significant decline in *Food, Beverages & Tobacco*, which offset moderate growth in O*ther Manufacturing*. The weak performance of the sector was partly attributed to the non-competitive nature of some industries, which resulted in the relocation of a number of manufacturing companies out of Jamaica. There were also significant increases in labour cost in this industry in the context of declining productivity.

Growth in *Other Manufacturing* was mainly attributed to the normalisation of production at the petroleum refining plant following reduced output in 2005. The reduction in 2005 was due to the extended closure of the plant for maintenance in the first two

quarters of that year. For 2006, reduced activities within the chemical and non-metallic mineral industries tempered the improvement in the sub-sector in 2006. Production within the chemical industry was affected by the closure of a major fertilizer factory in June 2006 along with reduced demand for the product. There was also a reduction in paint output arising from the fallout in demand from the construction industry. In this context, the production of chemicals contracted by 2.6 per cent, relative to growth of 8.4 per cent in 2005. Activity within the non-metallic mineral industry was affected by the temporary closure of the sole cement plant. Accordingly, cement production declined by 9.6 per cent compared to growth of 4.5 per cent the previous year.

The reduction in F*ood, Beverages & Tobacco* was reflected primarily in the tobacco and non-alcoholic beverages industries, partly offset by increases in food processing and alcoholic beverages. The decline in tobacco reflected the closure and relocation of the sole cigarette factory to another jurisdiction within the Caricom Single Market. The improvement in food processing stemmed primarily from increased output of poultry meat, edible oils & fats and animal feeds (see **Table 61**). The performance of poultry meat and animal feeds was attributed to increased consumer demand for chicken products. The growth in the output of edible oils reflect an increase in local production, as there was a reduction in imports due to technical problems faced by overseas producers. With regard to alcoholic beverages, growth was primarily driven by the improvement in beer and stout production, arising from domestic promotion as well as growth in export markets.

Expansion in **Electricity & Water** was in line with the average growth of 3.4 per cent observed over the last five years. This expansion was primarily facilitated by the installation of a 50 Megawatt barge at one of the private electricity producers during the March quarter. As a result, total electricity generation for the review year increased by 4.3 per cent, while sales increased by 2.7 per cent. Capacity utilization remained low in the year at 56.1 per cent, slightly below the utilization of 57.8 per cent in 2005. Moderating the growth in the sector was a marginal decline of 0.1 per cent in water production in 2006, relative to the previous year. High rates of capacity utilization continued in the water sub-sector, averaging 98.3 per cent over the last two years.

Table 61

Selected Food Processing Items

	Production ('000tonnes)		
Item	**2005**	**2006**	**% Change**
Poultry Meat	101.5	104	2.5
Edible Oils	16.7	21.1	26.5
Cornmeal	11.6	11.2	-3.6
Condensed Milk	15.1	11.4	-24.5
Flour	135.4	129.3	-4.5
Animal Feeds	367.6	378.2	2.9
Sugar	126.1	142.8	13.3

Source: Planning Institute of Jamaica

During 2006, there was a continuation of the robust growth observed in **Transport, Storage & Communication** since the early 1990's. Notably, the sector recorded consistent growth in all quarters. Demand for sea and air transport was the main driver of growth. Within R*ailway, Road, Water & Air Transport*, growth reflected the on-going expansion of the Island's port facilities, which, given Jamaica's strategic location and competitive advantage, translated into increased transhipment activities during the year. This was facilitated by the US$26.6 million infrastructural development programme by the Kingston Wharves Limited, which commenced within the year. The programme involved the expansion of berth capacity to accommodate larger vessels and a 50.0 per cent increase in storage facility. For the year, domestic cargo movements through the main seaports and the number of ships calling at Jamaican ports grew by 9.1 per cent and 7.8 per cent, respectively. Additionally, the introduction of new airline carriers to the Island facilitated an increase in demand. This contributed to the improvement of 15.3

per cent in visitors when compared to 2005. Further, during the year the number of charter flights from Canada and the United States increased, with US Air expanding the number of its flights from four to eight per week to facilitate the diversion of passengers from Cancun to Jamaica. Generally, the performance of the sector reflected a favourable international economic environment for trade and travel, facilitated by increased airlift capacity to Jamaica and the expansion of port facilities. These translated into an overall improvement in labour productivity in 2006 after two years of decline.

There was a significant improvement in the real value-added of **Financing & Insurance Services** in 2006, when compared to its average growth of 0.4 per cent recorded over the last five years. This improvement primarily reflected the performance of B*anking Institutions*, in particular commercial banks and insurance (See **Supervision of Deposit Taking Financial Institutions)**.

Reflecting the performance in tourism, value added in **Miscellaneous Services** significantly expanded above trend by 12.3 per cent in 2006, relative to average growth of 2.4 per cent recorded over the last five years. The major factor contributing to the performance of the tourism industry was an increase of 13.5 per cent in total stopover arrivals, led by an expansion of 13.8 per cent in foreign national arrivals. Cruise ship arrivals also improved by 17.7 per cent during the year. Against this background, visitor expenditure increased by 22.2 per cent in 2006 (see **Balance of Payments**).

The demand for the Island's tourism product continued to improve against the background of growth in Jamaica's main source markets. This expansion was supported by an increase of 5.0 per cent in the number of hotel rooms, with the completion of Sandals Whitehouse and Bahia Principe Hotels in the year, as well as additional room capacity at Couples Resort. Furthermore, the refurbishing of properties and product upgrades as well as promotions by stakeholders supported the growth. Also, new airlift to the Island stimulated increased arrivals. The tourism industry continued to be the main recipient of banking system credit to the productive sectors.

8.2. Prices

8.2.1. Overview

Consumer price inflation fell sharply to 5.8 per cent in 2006 from 12.9 per cent in 2005. This represented the first single-digit calendar year outturn since 2002 and the lowest since 1981. Core inflation also fell to 3.4 per cent in 2006 from 5.2 per cent in 2005.

The out-turn for headline inflation for the review year was influenced by a sequence of favourable domestic and international factors. These included strong expansion in agricultural supply, relative stability in the exchange rate and modest increases in international oil prices, with sharp reversals in the latter part of the year. On the other hand, there were increases in administered prices and supply constraints in the fishing and beef industries. Nonetheless, the predominance of positive shocks precipitated the realization of a 25-year low in annual inflation.

Domestic Factors influencing Inflation

Supply Conditions

Agricultural output was positively affected by intensified planting activities in 2006 in the aftermath of the 2005 tropical Atlantic hurricane season, the most active on record. These efforts were reinforced by the increased use of new technology such as greenhouses and hydroponics and a particularly uneventful hurricane season. In this context, there was increased output of tubers and vegetables which resulted in lower prices for major crops such as yellow yam, sweet potato, tomato, pumpkin, cabbage and lettuce. As a consequence, Starchy Foods and Vegetables & Fruits of the Consumer price Index (CPI) decreased by 3.7 per cent and 9.3 per cent, respectively, in 2006. The impact of these movements offset some of the inflationary impulses in the other components of the Food & Drink category and from administered prices.

Beef and fish prices rose by approximately 33.0 per cent and 10.0 per cent, respectively. This reflected supply constraints and rising input costs associated with the increased prices for energy and grains. Supply in the beef industry declined in a context of low breeding stocks, with production declining by 20.1 per cent to 10 391 tonnes in 2005 from 13 096 tonnes during the 2001-2005 period. The fishing industry was affected by the exit of a significant player in the domestic market due to the redirection of its output to the export market. Higher priced imports were used to fill the void. Largely as a result of these developments, Meat, Poultry & Fish accounted for nearly one-third of the year's inflation (see **Table 63**).

Administered Prices

The annual adjustment to the national minimum wage was 16.7 per cent in 2006 and primarily affected household helpers and gardeners whose minimum wages moved to $2,800.0 from $2,400.0 per 40-hour work week. A 15.0 per cent increase in minimum wage was also granted to industrial security guards. As a result, their minimum wages moved to $4,140.0 from $3,600.0 for a 40-hour workweek. These increases were reflected in *Housing & Other Housing Expenses*, which was responsible for approximately 12.0 per cent of inflation in the year (see **Table 63**).

External Factors Influencing Inflation

The most significant external impetus to inflation was the movement in the international prices of petroleum products. The average price of the benchmark West Texas Intermediate (WTI) crude oil rose by 17.0 per cent to average US$66.09 per barrel in 2006. This followed the sharp increase of 36.2 per cent in 2005. However, there was significant volatility in crude oil prices over the year as prices fell sharply towards the end of the year from a nominal peak of US$77.03 per barrel in July (see **International Developments**). 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.

Table 62

STYLIZED DECOMPOSITION OF INFLATION OUTTURN: CALENDAR YEAR 2006		
	INFLATION (%)	CONTRIBUTION (%)
NON- CORE	**2.40**	**41.7**
Agricultural Commodities		
–Meat, Poultry & Fish	1.47	25.6
–Starchy Foods/ Vegetables	-0.59	-10.2
Other Food		
–Baked Prods/Dairy Prods	1.0	17.4
International Commodities		
–Household Fuel/Petrol	0.06	1.0
Administered Prices		
–Minimum Wage	0.12	2.1
Other	*0.34*	*5.8*
CORE	**3.36**	**58.3**
TOTAL	**5.76**	**100.0**

8.2.3. Core Inflation

Core inflation was contained at 3.4 per cent in 2006, below the 5.2 per cent attained in 2005[32]. For the greater part of the year, core inflation was relatively stable and consistently below the rate that obtained in the previous year. However, this lower level of core inflation in a context of lower overall price impulses resulted in a higher proportion of core relative to overall inflation. Underlying inflation was 58.3 per cent of headline inflation in 2006 (see **Table 62**).

32 measured by the change in the trimmed mean index

8.2.4. Contribution to Inflation

The movement in the CPI in 2006 was largely reflected in increases in *Food & Drink*, *Housing & Other Housing Expenses* and *Fuels & Other Household Supplies*. These sub-indices expanded by 5.3 per cent, 9.0 per cent and 8.1 per cent, contributing 55.3 per cent, 11.7 per cent and 8.9 per cent, respectively, to the year's outturn (see **Table 63**).

Within *Food & Drink*, the main impetuses to price increases were reflected in *Meat, Poultry & Fish*, *Baked Products, Cereals &*

Breakfast Drinks and *Dairy Products, Oils & Fats*. *Meat, Poultry & Fish* rose by 12.4 per cent and contributed 31.6 per cent to the year's inflation. This increase reflected the impact of supply constraints in the meat industries in addition to the impact of higher energy prices on processing and storage. *Baked Products, Cereals & Breakfast Drinks,* which increased by 9.6 per cent, accounted for 13.0 per cent of overall inflation and was principally affected by increases in the cost of wheat and flour which led to higher prices for baked products. Countervailing impetus from *Starchy Foods* and *Vegetables & Fruits* moderated the full impact of inflation from the group.

The main sub-group that contributed to inflation in *Housing & Other Housing Expenses* was *Other Housing Expenses*, which increased by 7.7 per cent. The primary contributor was electricity rates, consequent on the movements in international oil prices and annual adjustments in energy charges. Similarly, *Fuels & Other Household Supplies* was also affected by the impact of international oil price movements. The *Fuels* sub-component was affected by increases in the cost of household fuels while in the case of *Household Supplies*, the price of ice increased due to higher energy costs. The 16.7 per cent increase in the minimum wage and sharp movements in cement prices, consequent on problems in the industry, also added upward impetus to *Housing & Other Housing Expenses*.

Table 63

JAMAICA: COMPONENT CONTRIBUTION TO INFLATION; 2006

	Group Weights	*Inflation (%) 2006*	*Weighted Inflation*	*% Contribution to Inflation*
FOOD & DRINK	**55.6**	**5.3**	**3.51**	**55.3**
- Meals Away From Home	7.4	5.7	0.42	6.7
- Meat Poultry & Fish	16.1	12.4	2.00	31.6
- Dairy Products, Oils & Fats	6.7	8.0	0.53	8.4
- Baked Products Cereals & Breakfast Drinks	8.6	9.6	0.83	13.0
- Starchy Foods	5.3	-3.7	-0.19	-3.1
- Vegetables & Fruits	6.5	-9.3	-0.61	-9.6
- Other Food & Beverages	5.0	10.3	0.52	8.2
FUELS & OTHER HOUSEHOLD SUPPLIES	**7.4**	**8.1**	**0.56**	**8.9**
- Household Supplies	4.8	7.0	0.34	5.4
- Fuels	2.5	8.8	0.22	3.5
HOUSING & OTHER HOUSING EXPENSES	**7.9**	**9.0**	**0.74**	**11.7**
- Rental	2.1	14.2	0.30	4.7
- Other Housing Expenses	5.8	7.7	0.44	7.0
HOUSEHOLD FURNISHINGS & FURNITURE	**2.8**	**9.0**	**0.23**	**3.7**
- Furniture	0.7	12.9	0.09	1.4
- Furnishings	2.2	6.8	0.15	2.3
HEALTHCARE & PERSONAL EXPENSES	**7.0**	**7.4**	**0.51**	**8.1**
PERSONAL CLOTHING FOOTWEAR & ACCESSORY	**5.1**	**5.8**	**0.29**	**4.6**
- Clothing Materials	0.6	3.8	0.02	0.3
- Ready-made Clothing & Accessories	2.4	5.5	0.13	2.1
- Footwear	1.6	5.3	0.08	1.3
- Making & Repairs	0.5	9.8	0.05	0.8
TRANSPORTATION	**6.4**	**0.5**	**0.03**	**0.5**
MISCELLANEOUS EXPENSES	**7.9**	**5.8**	**0.46**	**7.2**
ALL GROUPS	**100.0**	**5.8**	**6.34**	**100.0**

Source: STATIN & BOJ's Calculations

8.2.5. Regional Inflation[33]

Inflation was higher in *Other Towns* compared with *Rural Areas* and *Kingston Metropolitan Area* (*KMA*). In 2006, the index for *Other Towns* increased by 7.0 per cent, while the indices for *Rural Areas* and *KMA* increased by 5.2 per cent and 5.6 per cent, respectively.

This difference was largely reflective of disproportionate increases in *Food & Drink* in *Other Towns* with the main areas of deviation being reflected in *Meat, Poultry & Fish* and *Baked Products, Cereals & Breakfast Drinks* (see **Table 64**).

Table 64

REGIONAL INFLATION

Groups / Sub-groups	Weight in CPI	KMA (%)	Other Towns (%)	Rural (%)
FOOD & DRINK	0.5563	**5.0**	**7.9**	**4.3**
- Meals Away From Home	0.0741	2.6	8.5	9.4
- Meat Poultry & Fish	0.1613	12.2	13.7	11.9
- Dairy Products Oils & Fats	0.0668	6.8	9.2	8.7
- Baked Products Cereals & Breakfast Drink	0.0864	9.3	11.7	8.8
- Starchy Foods	0.0525	-9.9	7.0	-3.9
- Vegetables & Fruits	0.0650	-3.1	-10.5	-14.9
- Other Food & Beverages	0.0502	10.0	10.5	10.6
FUELS & OTHER HOUSEHOLD SUPPLIES	0.0735	**7.1**	**8.3**	**9.4**
- Household Supplies	0.0482	6.1	6.8	8.4
- Fuels	0.0253	7.6	9.1	10.0
HOUSING & OTHER HOUSING EXPENSES	0.0786	**9.6**	**7.4**	**8.9**
- Rental	0.0209	16.9	2.6	2.6
- Other Housing Expenses	0.0577	6.8	7.9	9.5
HOUSEHOLD FURNISHINGS & FURNITURE	0.0283	**11.8**	**6.1**	**8.2**
- Furniture	0.0068	28.8	3.6	5.1
- Furnishings	0.0215	3.3	7.4	9.9
HEALTHCARE & PERSONAL EXPENSES	0.0697	**7.8**	**7.3**	**6.6**
PERSONAL CLOTHING FOOTWEAR & ACC.	0.0507	**3.6**	**7.7**	**7.0**
- Clothing Materials	0.0055	2.6	2.5	6.8
- Readymade Clothing & Accessories	0.0242	2.8	5.5	7.8
- Footwear	0.0159	2.6	10.6	4.8
- Making & Repairs	0.0051	9.5	9.3	10.6
TRANSPORTATION	0.0644	**0.0**	**1.2**	**1.2**
MISCELLANEOUS EXPENSES	0.0785	**6.2**	**5.5**	**5.6**
ALL GROUPS	1.0000	**5.6**	**7.0**	**5.2**

Source: STATIN

33 The KMA refers to the Corporate Area, Spanish Town and Portmore, the Other Town to the parish capitals and major towns while the Rural Areas refers to the smaller towns.

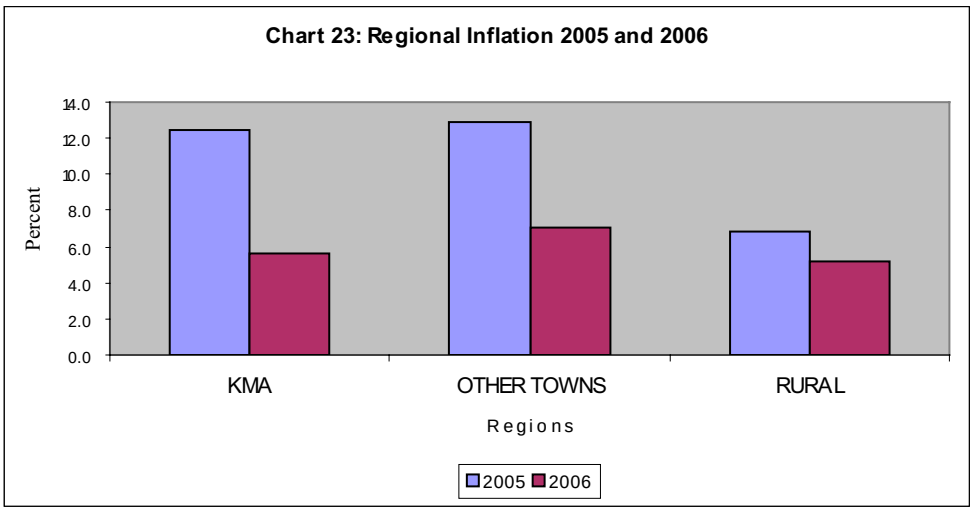


Chart 23: Regional Inflation 2005 and 2006
14.0
12.0
10.0
8.0
6.0
4.0
2.0
0.0
Percent
KMA
OTHER TOWNS
RURAL
Regions
2005
2006

9.1. Central Government Performance

For the period April to December 2006, Central Government operations generated a deficit of $38 419.8 million or 5.5 per cent of GDP, relative to the budgeted deficit of $30 731.7 million or 4.2 per cent of GDP (see **Tables 65** and **66**). The deviation from budget reflected a shortfall in revenue and grants and higher than budgeted expenditure. The primary surplus ratio was 5.2 per cent of GDP, compared to the target of 5.6 per cent, reflecting the shortfall in revenues while, the current deficit was 3.4 per cent of GDP, significantly above the target of 1.9 per cent, as revenues (excluding capital revenue) were insufficient to cover recurrent expenditure. The interest payments to GDP ratio was 10.7 per cent, relative to the target of 9.8 per cent, as there was a greater than projected issue of instruments with quarterly interest payments.

Chart 24

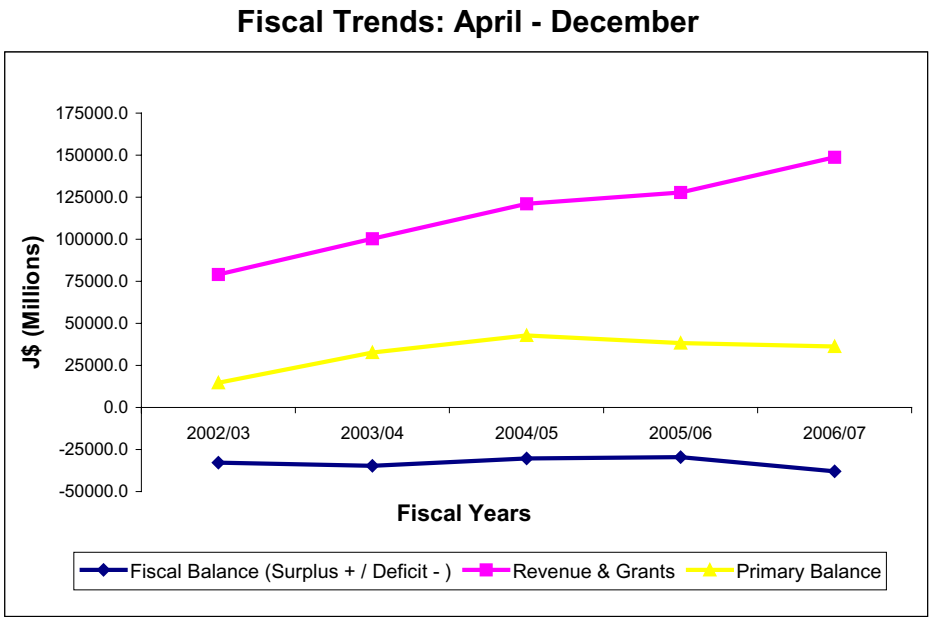


Table 65

CENTRAL GOVERNMENT SUMMARY ACCOUNTS
FY 2006/07
(J$MN)

	FY 2006/07 Q1 - Q3	Target Q1 - Q3	Variance	Per Cent
Revenue & Grants	**148 292.9**	**154 225.0**	**-5 932.0**	**-3.8**
Revenue	**146 803.2**	**151 065.7**	**-4 262.5**	**-2.8**
Tax Revenue	132 388.5	137 031.6	-4 643.1	**-3.4**
Non-Tax Revenue	10 070.8	8 542.0	1 528.8	**17.9**
Bauxite Levy	3 038.3	2 904.8	133.5	**4.6**
Capital Revenue	1 305.6	2 587.3	-1 281.8	**-49.5**
Grants	1 489.8	3 159.3	-1 669.5	**-52.8**
Expenditure	**186 712.7**	**184 956.7**	**1 756.0**	**0.9**
Recurrent Expenditure	168 880.9	162 190.5	6 690.4	**4.1**
Programmes	36 350.7	35 522.5	828.2	**2.3**
Wages & Salaries	58 265.6	54 883.6	3 382.0	**6.2**
Interest	74 264.6	71 784.4	2 480.2	**3.5**
Domestic	53 987.0	51 629.3	2 357.7	**4.6**
Foreign	20 277.5	20 155.0	122.5	**0.6**
Capital Expenditure	17 831.8	22 766.2	-4 934.4	**-21.7**
Fiscal Balance	**-38 419.8**	**-30 731.7**	**-7 688.0**	**25.0**
Current Balance	**-23 383.3**	**-13 712.1**	**-9 671.2**	**70.5**
Primary balance	**35 844.8**	**41 052.7**	**-5 207.9**	**-12.7**

Table 66

FISCAL PERFORMANCE RATIOS
FY 2006/07
(%)

	FY 2006/07 Q1 - Q3	Target Q1 - Q3
Borrowing Requirement/GDP	**5.5**	**4.2**
Current Balance/GDP	**-3.4**	**-1.9**
Primary Balance/GDP	**5.2**	**5.6**
Interest Payments/GDP	**10.7**	**9.8**
Fiscal Stability Ratio	**-1.3**	**-1.2**
Non-Interest Expenditure	**16.2**	**15.4**

Key

Current Balance = Current Revenue-Current Expenditure

Primary Balance = Total Revenues-Total Expenditures less Interest Payments

Fiscal Stability Ratio = (Overall Balance/ Total Revenue) - 1

International Benchmarks

BR greater than **3% of GDP** often indicates serious fiscal imbalance

FSR closer to zero indicates more stable government finances

Negative CB ratio of less than 1% indicates dissaving or a need for fiscal adjustment as the public sector is borrowingfor consumption

PB ratio above zero indicates major fiscal adjustment to cover interest on past obligations

** Recurrent Expenditure includes programmes, wages and salaries and interest payments.*

For the FY to December 2006, total revenue and grants were 3.8 per cent below budget, but exceeded the level for the comparable 2005/06 period by 16.0 per cent. The deviation from budget reflected a 3.4 per cent shortfall in tax revenue consequent on lower than targeted receipts from the Accounts Receivable Conversion (ARC) Programme, reflected in the categories *Production and Consumption* and *Income and Profits*. On the other hand, there were higher than targeted receipts from *International Trade*.

Total expenditure for April to December 2006 was $1 756.0 million or 0.9 per cent above budget, reflecting higher than targetted recurrent expenditure tempered by lower than budgeted capital expenditure. Recurrent expenditure was 4.1 per cent above budget, reflecting higher than planned spending in all areas, particularly wages and salaries and domestic interest payments. Lower than budgeted capital expenditure largely reflected timing issues.

Table 67

C-Effeciency Ratio
April - December
(J$ Millions)

	2003/04	2004/05	2005/06	2006/07*	3 YR AVG
Consumption	319,356.7	345,987.8	405,010.8	475,100.8	356,785.1
GCT	26,503.7	31,415.1	35,044.0	42,397.4	30,987.6
GCT/Consumption (%)	8.3	9.1	8.7	8.9	8.7
Standard Rate (%)	15.0	15.0	16.5	16.5	15.5
C-Efficiency Ratio (%)	**55.3**	**60.5**	**52.4**	**54.1**	**56.1**

* For Fiscal Year 2006/07, consumption figures used are BOJ estimates

Despite the lower than budgeted tax revenue, the overall collection efficiency of the tax system improved. The C-Efficiency ratio for April to December 2006 was 54.1 per cent, compared to 52.4 per cent for the corresponding period of FY 2005/06 (see **Table 67**)[34]. The moderate increase in the ratio for FY to December reflected an improvement in the collection of tax arrears relative to the comparable period in FY 2005/06.

Financing

In a context where the Government raised US$250.0 million through a Eurobond issue prior to the start of the fiscal year, Government debt raising was largely confined to the domestic market, during the period April to December, reflected in the higher than budgeted net issue of domestic debt instruments. This was partly offset by higher than budgeted net foreign amortization, which partly reflected a delay in project loan receipts.

34 The C-Efficiency ratio is the share of value-added tax (VAT) revenue in consumption

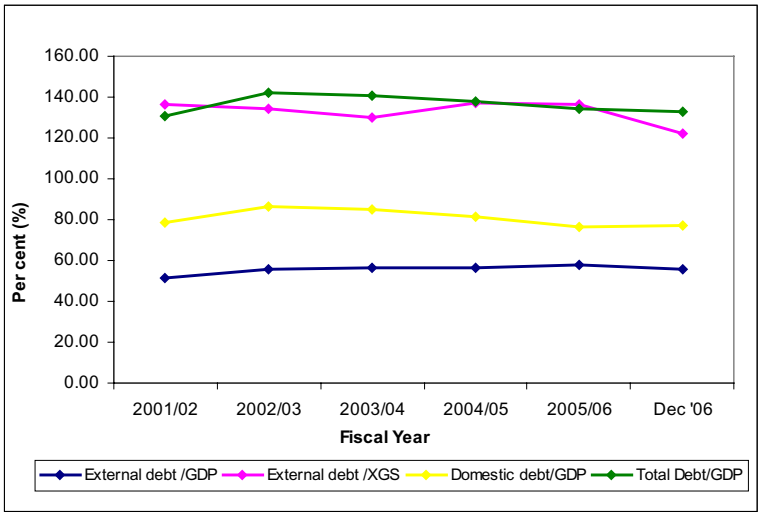
Debt Analysis

Jamaica's debt stock expanded by 9.3 per cent to $925.8 billion in the first nine month of the fiscal year. Based on Bank of Jamaica estimates, the debt stock at end-December 2006 was 133.2 per cent of GDP, relative to 134.3 per cent end-March 2006 (see **Chart 25**). The expansion in the stock reflected increases of 11.2 per cent and 6.7 per cent in the domestic debt stock and external debt stock, respectively. At end-December, the domestic debt stock was 77.2 per cent of GDP, compared to 76.5 per cent at end March 2006. The external debt stock was 56.0 per cent of GDP compared to 57.8 per cent of GDP at end-March 2006.

period increased to 9.8 years compared to the average of 4.2 years estimated for the comparable period in the previous fiscal year. The increase in the average age of new debt reflected a greater reliance on instruments with maturities of above 5 years, which resulted in a lengthening in the maturity profile of the debt stock and a reduction in refinancing risks. Consequent on the lowering of interest rates during the FY to December 2006, the weighted average interest rate on new domestic debt issues fell to 12.96 per cent at end-2006 from 13.45 per cent at end-2005. During the period, the foreign currency-linked portion of the domestic debt portfolio declined to 13.8 per per cent from 16.0 per cent at end-March 2006, thereby reducing currency risk in the debt portfolio.

Chart 25

Selected Fiscal Indicators



Domestic Debt

The increase in domestic debt in the fiscal year largely reflected the higher than budgetted fiscal deficit. In a context where investors continued to seek hedged instruments in FY 2006/07, Government debt offers were primarily skewed towards variable rate instruments, which accounted for 67.4 per cent of the financing raised (see **Table 68**). Consequently, the variable rate component of the domestic debt increased to 59.8 per cent relative to 53.0 per cent at end March 2006[35]. The weighted average age of debt issued in the current

35 Note that the 2006/07 Debt Strategy had a target of 40.0 per cent for variable rate debt.

Table 68

GOJ PUBLIC OFFERS OF INSTRUMENTS (EXCLUDING T-BILLS) APRIL - DECEMBER									
	Number of Offers			Value of Offers (J$ millions)			Proportion of Total (%)		
	2004/05	2005/06	2006/07	2004/05	2005/06	2006/07	2004/05	2005/06	2006/07
Variable Rate	3	11	9	6 635.4	45 493.9	72 916.9	8.1	57.2	67.4
Fixed Rate	16	12	16	61 537.0	18 429.0	32 190.5	75.3	23.2	29.8
US$ Instruments	2	2	1	13 508.7	15 657.3	3 057.8	16.5	19.7	2.8
TOTAL	21	25	26	81 681.1	79 580.3	108 165.2	100.0	100.0	100.0
Short-term and Medium-term	17	16	5	73 696.0	60 858.0	21 674.6	90.2	76.5	20.0
Long-term	4	9	21	7 985.2	18 722.3	86 490.6	9.8	23.5	80.0
TOTAL	21	25	26	81 681.1	79 580.3	108 165.2	100.0	100.0	100.0
				2004/05	2005/06	2006/07			
Weighted Average Age of New Debt (yrs.)				2.7	4.2	9.8			
Weighted Average Interest Rate on New Debt (%)				16.69	13.45	12.96			

External Debt

The increase in external debt in the fiscal year largely reflected growth in Government guaranteed debt to US$915.3 million from US$737.4 million at end March 2006 (see **Table 69**). This was primarily due to the issue of a US$200 million Eurobond by Clarendon Alumina Production Ltd. (CAP). Consequently, the proportion of bonds in the external debt portfolio increased to 59.5 per cent from 57.3 per cent at end March, while the proportion of multilateral/bilateral debt fell to 33.5 per cent from 36.0 per cent. The external debt continued to be predominantly composed of long-term fixed rate interest instruments in the FY 2006/07 period.

Table 69

External Debt by Borrower Category March 2006 - December 2006 (in millions of US dollars)				
	March	**June**	**Sept.**	**Dec.**
Central Government	4 826.4	4 871.4	4 874.3	4 878.7
Government Guaranteed	737.4	736.4	743.1	915.3
BOJ	3.7	3.7	1.9	1.7
Total	**5 567.4**	**5 611.5**	**5 619.3**	**5 795.6**

Source: Ministry of Finance

10. Economic Outlook

The prospect for 2007 is for continued strengthening of the domestic economy, underpinned by stronger growth, relatively low inflation and a continuation of stable financial markets. In spite of anticipated moderation in world growth, the Jamaican economy should continue to benefit from a favourable international environment. Growth will also reflect the significant investments in construction, mining and tourism in 2006. It is also expected that there will be additional investments in these sectors in 2007. Relatively low domestic interest rates and projected continued expansion in loans should augur well for growth. Developments in the macroeconomic environment will be greatly enhanced by continued confidence in the economy and lower inflation expectations.

The possibility of heightened volatility in crude oil prices and adverse weather conditions are threats to the positive economic outlook. However, the risks are balanced. In this context, monetary policy will continue to focus on maintaining single digit inflation and stable financial markets.

10.1. International Economy

World output growth for 2007 is projected to decelerate by 0.4 percentage point from 4.8 per cent in 2006. This outlook mainly reflects a 0.5 percentage point deceleration in growth for the advanced economies to 2.5 per cent. Additionally, real GDP growth among the developing economies is expected to moderate to 7.2 per cent, below the 7.3 per cent expansion recorded in the previous year.

World inflation is expected to decelerate in 2007, largely reflecting inflation of 1.8 per cent for the advanced economies, which compares favourably with the 2.4 per cent recorded for 2006. Inflation in the developing economies is projected to decelerate to 5.0 per cent from 5.2 per cent in the previous year. The moderation in world inflation is expected to be influenced by the reduction in inflationary pressures from oil prices. Average oil prices are expected to remain broadly at the same level as in 2006. However, the prices of selected food commodities, in particular grains, are expected to continue the upward trend which began in 2006. Limited spare capacity in the market for metals is expected to contribute to continued increases in the prices of these commodities.

Within the global financial market, interest rates are not expected to rise sharply given the anticipated moderation in inflation. In particular, the Federal Reserve is expected to maintain its target rates at end-2006 levels for at least the first half of 2007. Against this background, emerging market bonds, particularly Jamaica's sovereign bonds, should continue to trade favourably as investors search for higher returns.

Trade negotiations under the Doha Development Agenda of the WTO resumed on 7 February 2007. The agenda includes several issues of importance to Jamaica, particularly special and differential treatment, special safeguard measures for the Small Vulnerable Economies group and phased tariff reductions for non-agricultural products. Given the expiration of several trade agreements, such as the Caribbean Basin Economic Recovery Act (CBERA) and the Cotonou Agreement, the negotiation of replacement arrangements is expected to pose challenges for Jamaica during 2007[36].

10.2. Real Sector

The Jamaican economy is expected to grow within the range of 3.0 per cent to 3.5 per cent in 2007. In spite of the anticipated moderation in world growth, it is projected that there will be continued buoyant demand for Jamaica's exports, particularly services. Significant

36 The Caribbean Basin Economic Recovery Act and the Caribbean Basin Trade Partnerships Act (CBTPA) were collectively known as the Caribbean Basin Initiative (CBI). A request for the extension of the waiver regarding the CBERA, which expired in 2005 was denied in 2006. The CBTPA will expire in 2008.

public and private investments, improving credit conditions, and a general amelioration in the domestic macroeconomic environment, will be the major factors underlying the growth impetus.

Economic growth is anticipated in both the goods producing and the services sectors. Notably, stronger growth is forecasted for the goods producing sectors, mainly **Mining**, **Agriculture** and **Construction**. Within the construction sector, the normalization of supplies of construction materials on the domestic market should facilitate the plethora of projects planned for 2007. These include the construction of four hotels, the expansion of the Petrojam refinery as well as the on-going expansion of the Norman Manley International Airport. Favourable weather conditions and improved farming techniques should boost production in **Agriculture.** The services sector is expected to grow, chiefly due to anticipated expansion in **Miscellaneous Services** and **Basic Services**. **Miscellaneous Services** should continue to exhibit strong growth through an expansion in its major component, *Hotels, Restaurants and Clubs*. Tourism is expected to benefit from additional room capacity, increased airlift and advertising relative to last year. Growth in this sector is anticipated to have a positive effect on **Transportation.**

10.3. Inflation

The maintenance of single digit inflation is anticipated in 2007. Critical to this outcome will be a strong real sector performance to underpin foreign exchange market stability and the containment of excessive monetary impulses. In this context, core inflation is expected to remain broadly in line with its long run average of 4.0 per cent. Domestic food prices are expected to remain relatively stable in the context of increased agricultural production. The lower anticipated inflation in the global economy is expected to result in reduced imported inflation on domestic prices. It is not expected that oil prices will increase significantly given recent trends and greater use of alternative energy sources.

10.4. Monetary Policy

Within the context of the monetary programme for fiscal year 2007/08, the Bank will target inflation within the range of 6.0 per cent to 7.0 per cent. Against this background, and given the trends in output, fiscal accounts and international interest rates, the Bank will continue its conservative monetary policy stance. The relatively high real interest rates should encourage continued demand for domestic financial assets and hence it is not expected that there will be undue pressure on the exchange rate. In any event, continued strong inflows especially from remittances and the services sector, as well as the Bank's substantial stock of reserves should reduce any risk of instability.

11.1. Banking Services

During 2006, the Bank continued to provide a variety of banking services to its customers. The Bank's customers include the Government, licensed financial institutions, primary dealers, selected brokers of the Jamaica Central Securities Depository (JCSD) and regional central banks. The Bank continued to provide operational support to the Systemically Important Payment Systems (SIPS) in Jamaica. The SIPS are the Automated Clearing House (ACH) and the Customer Inquiry Funds Transfer System (CIFTS). The ACH is owned and operated by the six commercial banks while the CIFTS is owned and operated by the Bank.

With regard to the ACH, the Bank operates in the following capacities:

- Participant - negotiating cheques drawn on commercial banks as well as sending and receiving electronic files with the cheque data to and from the ACH Operator;
- Settlement Bank - effecting the settlement of clearing balances on the accounts of commercial banks;
- Providing oversight to the Payments System; and
- Supervising the manual clearing process for items that do not qualify for the ACH as well as foreign currency cheques which qualify for domestic clearing.

The CIFTS is a medium for the electronic transfer of funds between the accounts held at the BOJ by commercial banks, primary dealers and the participants of the JSCD.

In providing banking services to the Government, the Bank continued to effect the settlement of GOJ primary issues in the domestic securities market, the redemption of GOJ Treasury Bills and the payment of external and domestic debt obligations. Services provided to other customers included settlement of open market operations, equities traded on Jamaica Stock Exchange (JSE), the issue and redemption of currency and regional payments through Caricom bilateral arrangements. Limited over-the-counter services, including the exchange of mutilated Jamaica Dollar notes, the redemption of coins and the purchase of foreign currencies, were provided to the general public.

Notwithstanding the relatively restricted level of its interface with customers, the Central Bank, being cognizant of the possibility that its services could be exposed to the risk of money laundering and of other persons wishing to use the system to facilitate the commission of some other financial crime, upgraded its Anti-Money Laundering and Combating the Financing of Terrorism (AML/CFT) policy in July 2006. This process involved the appointment of a senior compliance officer, the training and sensitization of staff as regards their roles in the AML/CFT procedures and enhancement of the Bank's 'Know Your Customer' (KYC) requirements. Under this policy the Bank is required to file Threshold Transactions and Suspicious Transactions reports to the Designated Authority and observe KYC requirements. The Financial Investigations Unit of the Ministry of Finance is the Designated Authority.

11.2. Currency Operations

In 2006, the Bank continued to fulfil its statutory obligation to meet the currency requirements of the Jamaican society. In discharging this function, the Bank upgraded its currency processing facilities to enhance its capability to maintain its clean note policy and the counterfeit surveillance system. Accordingly, the Bank acquired two advanced currency sorting machines (BPS 3000 banknote sorters) to replace those already in operation (BPS 1000). These new machines have improved the rate of processing redeemed notes as it relates to:

- Determining their authenticity;

- Identifying the notes suitable for further circulation; and
- Destroying unfit banknotes.

Additionally, this new technology will strengthen internal controls by reducing the manual handling of banknotes during sorting.

Currency in Circulation

Total currency in circulation at the end-2006 was valued at $42.8 billion, an increase of 15.8 per cent relative to 2005. Of this amount, banknotes represented $40.8 billion or 95.5 per cent, up from $34.4 billion or 94.4 per cent at end-2005 (see **Table 70**). The $1 000 denomination amounted to $29.2 billion or 71.5 per cent of total currency in circulation. The $500 note accounted for 20.5 per cent of total notes in circulation.

Table 70

BANKNOTES IN CIRCULATION AS AT END-DECEMBER

(In Billions of Dollars)

DENOMINATION	2005	2006	% CHANGE
$1,000	23.99	29.21	21.76
$500	7.35	8.39	14.15
$100	2.37	2.49	5.06
$50	0.48	0.55	14.58
*OTHERS	0.2	0.2	0.00
Total	34.39	40.84	18.75

** Notes ($20, $10, $5, $2, $1 & $0.50) which have been withdrawn from active circulation.*

Coins in circulation were valued at $1.9 billion, an increase of 15.7 per cent relative to 2005. The $20 coin with a value of $720.3 million represented 37.4 per cent of the total. This denomination recorded a 20.5 per cent expansion in circulation, largely because of its relatively higher purchasing power. The values of the 25 cent and 10 cent denominations in circulation increased by 4.4 per cent and 5.5 per cent, respectively, relative to 2005.

Currency Issued

During 2006, the Bank issued 281.3 million pieces of banknotes valued at $131.2 billion. This value represented an increase of 18.8 per cent above the value of notes issued in 2005. The $1 000 and $500 denominations accounted for 61.7 per cent and 29.9 per cent respectively, of total value.

Coins issued in 2006 were valued at $514.1 million, an increase of 13.2 per cent relative to 2005. The demand for the $5 coin increased by 17.0 per cent while that for the $10 and $1 coins increased by 13.8 per cent and 13.7 per cent, respectively. On the other hand, demand for the 25 cent coin declined by 4.7 per cent relative to the previous year.

Banknotes Redeemed and Sorted

The Bank redeemed 271.7 million pieces of banknotes valued at $124.8 billion during 2006. This represented an increase of 16.2 per cent relative to 2005 when total redemptions were valued at $107.4 billion.

A total of 233.6 million banknotes were sorted during the year. Of this number, 101.5 million pieces or 43.5 per cent were deemed fit for re-issue to the public. During the sorting process 63.1 per cent of the notes identified as unfit for re-issue were $100 and $50 notes, reflecting the relatively high usage of these denominations which are used mainly in low value transactions. Consequently, these denominations have short average useful lives and high replacement rates.

Incidence of Counterfeiting

In 2006, the value of counterfeit banknotes detected amounted to $3.3 million relative to $2.1 million in 2005. Of this figure, the financial institutions detected 73.2 per cent upon presentation at their counters, while the remaining 26.9 per cent was detected by the BOJ. The denomination most affected was the $1 000 note which accounted for 65.9 per cent of the total. The quality of the counterfeits remained poor as the perpetrators continued to find it difficult to reproduce the security features embedded in the notes. As part if its anti-counterfeiting strategy, the Bank continued to offer training to the stake-holders during 2006.

Chart 26

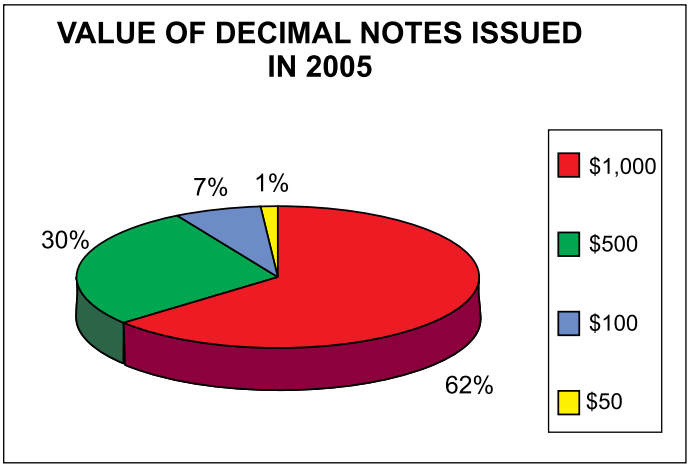
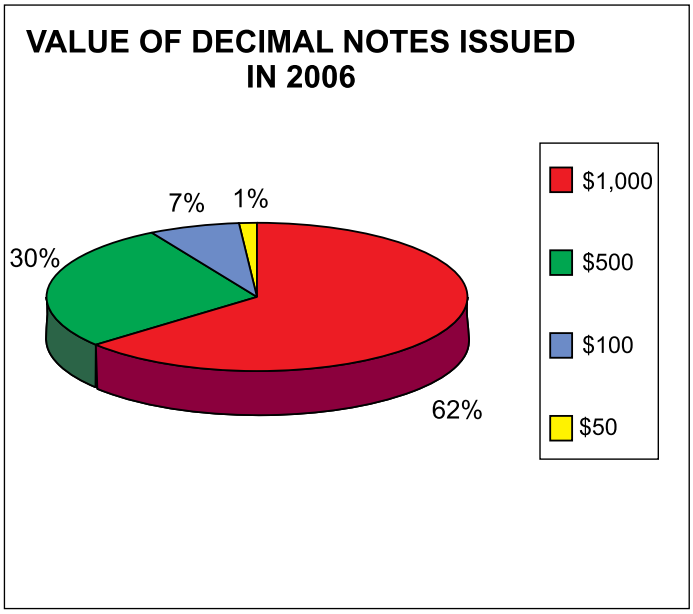


Chart 27



12. Payments System Developments

12.1. Payments System

During 2006 the Bank of Jamaica focussed on payments system reform as well as general oversight of the payment systems that are a vital part of the financial infrastructure.

Payments System Reform - In relation to the payments system reform project, the Bank commenced the technological procurement phase for the Real Time Gross Settlement (RTGS) and the Central Securities Depository (CSD) systems inclusive of all related linkages. The establishment of the supporting legal framework continued and in the last quarter the development of the oversight function was pursued as a major priority.

General System Oversight - The level of activities in the two systemically important payment systems (SIPS)[37], the Automated Clearing House (ACH) and the Customer Inquiry and Funds Transfer System (CIFTS), during the period under review served to confirm the growing importance of these systems in the payments infrastructure[38]. The total value of payments made through these channels in 2006 was in excess of J$6.0 trillion, approximately 16 per cent more than in 2005.

In addition to general oversight of the SIPS, there was ongoing review of activities and developments in retail systems that are of system-wide importance (SWIPS). This is in full recognition of the fact that these systems are used to facilitate a large volume of small-value transactions usually occurring at Points of Sale (POS), through Automated Banking Machines (ABM) or over the counter. Our review showed that during this period the total value of ABM and POS transactions was approximately $167 billion, a significant increase of approximately 30 per cent over 2005.

The existing payment systems operated smoothly and efficiently during the year under review, even as we pursued our reform objectives. Details pertaining to payments system reform and system oversight are presented in the following subsections.

PAYMENTS SYSTEM REFORM

Consistent with international best practice, the Bank of Jamaica has responsibility for the promotion of safety and efficiency of the national payments and securities settlement systems. It is in this context that the following reform objectives are being pursued:

1. Implementation of modern mechanisms that can safely and cost effectively support transfer of monetary value;
2. Establishment of the appropriate legal framework to support the reformed payments and securities settlement system; and
3. Enhancement of the oversight function for payments and securities settlement systems.

The reform agenda is being pursued in several phases which in many instances will run concurrently. These are:

1. Inception
2. Establishment of Legal Framework
3. Diagnostic and System Design
4. Establishment of the Oversight Function
5. Solution Procurement
6. Documentation and Strategic Implementation
7. RTGS & CSD Systems Implementation

We have completed the Inception and Diagnostic phases and are currently in the Solution Procurement Phase, with work continuing on the establishment of the Legal Framework and the Oversight Function. The project is scheduled for completion in the third quarter of 2008.

37 A Systemically Important Payment System (SIPS) is any system which, if it is insufficiently protected against risk, can trigger disruptions in the financial markets or widely across the economy.

38 CIFTS, owned and operated by the Bank of Jamaica, facilitates the electronic transfer of funds between financial institutions with settlement accounts at the Central Bank.

Solution Procurement

During the year, the scope of the reform project was expanded to include the establishment of a CSD as a replacement for the depository solution that was being developed by the Jamaica Central Securities Depository (JCSD). The change was necessary to ensure that the CSD satisfies the critical requirements for full integration with the RTGS system. This solution will guarantee smooth functioning of the payments and securities settlement system in accordance with internationally established standards of safety and security in the reformed environment.

Establishment of Legal Framework

In order to ensure that an appropriate legal framework is established to support the reformed payments and securities settlement system, the scope for legal reforms has been agreed and work on the Payment Systems Act, which is the major piece of legislation, is currently in progress. The Bank has developed the Drafting Instructions to be issued to the Chief Parliamentary Counsel. Appropriate modifications to the Bank of Jamaica Act have also been initiated, while amendments to the various pieces of legislation governing electronic issuance and trading of GOJ securities are being actively pursued. It is in this context that the Electronic Transactions Act will provide the legal framework for electronic transactions in general and is regarded as a pivotal step in the payment system reform agenda.

Establishment of Oversight Function

In 2006 the Bank continued the process of the re-engineering of the payments systems to meet international standards and best practices. The scope of oversight will be enhanced to be proportionate to the assessed potential risks of each payment system. The function will address two broad categories of payment systems:

- Systems that are important in terms of their impact on financial stability, referred to as SIPS; and
- Systems primarily important for public confidence and therefore of system-wide importance, referred to as SWIPS.

The Central Bank-owned and operated CIFTS, which supports the electronic transfer of large value inter-bank transactions, and the ACH, which facilitates the electronic processing and settlement of cheques, are the two designated SIPS. These systems are widely used and are the primary payment mechanisms for the financial system. As disruptions in these systems can have systemic implications, the oversight function for these systems is being established as a priority. The appropriate oversight methodologies for SWIPS are being developed concurrently.

GENERAL SYSTEMS OVERSIGHT

During 2006 the Bank continued to perform general oversight of payment systems which focussed on system utilization for the clearing and settlement of financial transactions. The oversight activities covered:

- The ACH;
- CIFTS;
- Retail Payment Systems; and
- The Clearing of Selected Foreign Currency Items.

CHEQUE PROCESSING SYSTEMS - LOCAL CURRENCY ITEMS

Cheques remain the most commonly used non-cash payment form in Jamaica in 2006, with the ACH being the major cheque-processing system. Total cheque payments, comprising ACH and proprietary transactions, increased by 19.5 per cent to $4.483 billion in 2006 from $3.752 billion in 2005.

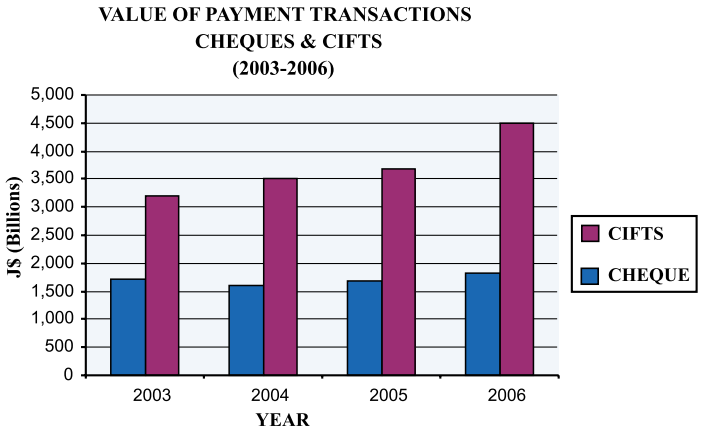
In 2006, 10.7 million transactions valued at $2.226 trillion were processed through the ACH, compared to 10.8 million items valued at $1.960 billion in 2005. The value of proprietary cheque transactions in 2006 totalled $2.257 billion, an increase of 25.9 per cent over 2005[39].

39 Proprietary transactions are those items encashed or deposited at the bank on which they are drawn.

a) Customer Inquiry and Funds Transfer System (CIFTS)

In 2006, transactions valued at $1 830 billion were processed through CIFTS, representing an increase of 8.4 per cent relative to 2005. The average value of CIFTS transactions in 2006 was $80.1 million, an increase of 16.9 per cent over the average of $68.6 million in 2005. However, the volume of CIFTS transactions decreased by 7.2 per cent to 22 853, relative to 2005. The combined value of Jamaica Dollar payments made by cheques and CIFTS amounted to $6.314 trillion, reflecting significant growth of 16.0 per cent over 2005 (see **Chart 28**).

Chart 28



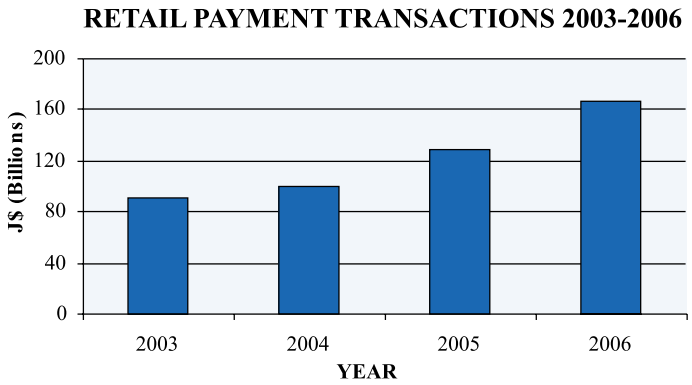
b) Retail Payment Systems

The retail payment system review focusses on card payments made at ABM and POS terminals. The total value of ABM and POS transactions (proprietary and non-proprietary) in 2006, was J$166.97 billion, an increase of 29.5 per cent over 2005.

ABM transactions of J$111.32 billion accounted for 65.0 per cent of the total (see **Chart 29**).

At the end of 2006 there were 372 ABMs and 13 609 POS terminals. This reflected increases of 42 ABMs and 1 589 POS terminals during the year. Commercial banks processed approximately 15 million ABM and POS transactions (non-proprietary) across the MultiLink network, an increase of 14.5 per cent relative to 2005.

Chart 29



Source: Commercial Banks & MultiLink

Clearing of Selected Foreign Currency Items

The Bank facilitated the manual exchange of selected foreign currency items issued by or drawn on local commercial banks. Eligible items were denominated in US dollars, Canadian dollars, Great Britain Pounds and Euros. Foreign currency items cleared locally are not settled in the Central Bank but are settled bilaterally on a net basis by wire transfers between correspondent bank accounts. These accounts are held by clearing banks in the respective currencies.

Foreign currency items equivalent to approximately US$3.8 billion were cleared locally in 2006 (see **Table 71**). This represents an increase of approximately 31 per cent over the US$2.9 billion exchanged in 2005. US dollar items continued to dominate, accounting for more than 95 per cent of foreign currency items.

Table 71

FOREIGN CURRENCY ITEMS CLEARED

(VALUE)

Currency Units (Millions)	2004	2005	2006
USD	2 400	2 770	3 679
CDN	18.37	20.79	24.71
GBP	57.70	53.13	71.33
Euro	1.06	5.46	6.51

13. Financial Legislations

DEVELOPMENTS

Electronic Money Order pursuant to the Banking Act, 1992

On 11 August 2006 the Minister of Finance and Planning, by way of Ministerial Order, designated the sale, issue and distribution of stored value cards as "banking business" pursuant to his powers under Section 2 of the Banking Act. The Order defines electronic money and covers any card-based electronic purse that bears the common feature of allowing the holder thereof to either receive the funds loaded on the card at a later date from an automated banking machine or to use the card via point of sale technology at participating merchants.

PENDING AMENDMENTS TO FINANCIAL LEGISLATION

The Cooperative Societies (Amendment) Bill

This Bill will seek to restrict the deposit-taking activities of cooperative societies to those which operate as credit unions. Secondly, it will seek to bring credit unions under the regulatory ambit of the Minister of Finance and the Bank of Jamaica.

Omnibus Statute

The Bank is in the process of reviewing legislation governing the operations of deposit-taking entities (i.e. the Banking Act, Financial Institutions Act and the Building Societies Act) with a view to consolidating these pieces of legislation into one consolidated statute. In so doing, it is intended that any existing inconsistencies between these statutes will be removed and this will ensure a more synchronized progression of updates to the laws governing the deposit-taking industry. This initiative is also intended to implement enhancements that will bring the regulation of the banking sector in line with the recently issued revised Basel Core Principles as well as to ensure that the relative provisions in relation to consolidated and conglomerate supervision are appropriately robust[40]. Revisions to the financial legislation will also focus on current issues such as outsourcing, as well as the proposed role of credit bureaux, provisions for electronic reporting and enhancing powers as regards the investigation and prosecution of illegal deposit-taking activities. Currently, the Bank is finalizing a working paper on the matter which will inform the subsequent submission to Cabinet to commence the legislative process.

PENDING FINANCIAL REGULATIONS

The Banking (Form of Application) Regulations

The Financial Institutions (Form of Application) Regulations

These regulations will comprise the prescribed application form under the respective Acts. The earlier format of licence fees regulations under the Banking Act and the Financial Institutions Act that dealt with both licence fees and the prescribed form of application was not retained. It was felt that the matter of the prescribed application form should be addressed via separate regulations so that the periodic upgrading of this form would not disrupt the licence fees aspect of the regulatory regime. These regulations will also include enhancements to the application form to capture from applicants certain basic particulars that were not captured by the old forms as well as enhancements to bring them in line with the revised Core Principles.

The revised form will also require the principals signing on behalf of the applicant company to certify that the information given in the form is accurate to the best of their knowledge and belief. Similar reforms to the application form under the Building Societies Act will be subsequently effected.

40 The Basel Core Principles II are the global standards for prudential regulation and supervision of banking systems.

The Building Societies (Licence Fees) Regulations

These regulations will be revised to bring the fees payable in line with the applicable fees under the 2003 Licence Fees Regulations under the Banking Act and the Financial Institutions Act.

The Banking (Qualification of Auditors) Regulations

These regulations will create a framework for ensuring that auditors, who are proposed as the statutory auditors of financial institutions, are independent of the financial institutions being audited.

The Banking (Credit Classification and Provisioning) Regulations

These regulations will formally impose the measures that banks are required to take in assessing credit, taking security and making provisions for the possibility of default.

The Bank of Jamaica (Credit Union) Regulations

The new regulations will bring the operations of credit unions fully under the BOJ's prudential supervisory regime. These regulations will therefore, among other things, cover licensing, capital, reserves, prohibited business, remedial and intervention processes and the role of credit union associations.

NON-FINANCIAL LEGISLATIVE ACTS DEVELOPMENTS

The Terrorism Prevention Act, 2005

In March 2006, the Chief Technical Director of the Financial Investigations Division (FID) of the Ministry of Finance, was, by way of Ministerial Order, designated the Designated Authority under the Terrorism Prevention Act for the purposes of receiving reports from reporting entities under that Act. This designation of the FID is a major step forward in the satisfaction of requirements identified out of the 2005 CFATF AML/CFT Mutual Evaluation as matters for Jamaica's attention.

The Terrorism Prevention Act came into effect on 6 June 2005. This Act, among other things, specifically imposes reporting and other operational control requirements on financial institutions to minimise the possibility of the services of the financial sector being used in any way to facilitate the financing of terrorist activities. The passage of this Act is a major step in the satisfaction of Jamaica's obligations to act in concert with other nations in combating terrorism, including fully implementing United Nations Resolution 1373 (2001) and other international instruments relating to terrorism.

The Electronic Transactions Act

This Act was passed by Parliament in the latter part of 2006 and will come into effect on the day appointed by the relevant Minister.

The Act deals with matters such as: -

- Electronic signatures;
- Formation and validity of contracts;
- Information retention requirements;
- Certification of the Service Provider;
- Liability of Intermediaries;
- Admissibility and evidential weight of information on electronic form; and
- Offences and Penalties.

The Ministry of Commerce, Science and Technology is spearheading the introduction of this Act as the first step to establishing an environment for the pursuit of e-commerce. Due to the impact this Act will have on financial services, particularly those that are transacted electronically, the Bank of Jamaica took an interest in the provisions to be included in this Act. The Bank of Jamaica met with the Jamaica Bankers' Association (JBA) and subsequently provided the Ministry with comments on the then Bill.

PENDING NON-FINANCIAL LEGISLATIVE AMENDMENTS

The Bank of Jamaica is involved in the process of formulating certain items of non-financial legislation.

(i) Payments and Settlement System Legislation

The Bank of Jamaica in conjunction with the JBA, is spearheading the introduction of legislation to deal with the regulation of the payments and settlement system of Jamaica. This legislation will formally establish the legal framework for the oversight of the payment and settlement systems and will address matters such as: -

(i) the finality of payments;
(ii) the effect of insolvency on payments already in the system; and
iii) upgrading of the settlement infrastructure by, inter alia, allowing for real-time gross settlement.

Drafting instructions prepared in consultation with a foreign legal expert are being finalized for submission to the Chief Parliamentary Counsel through the Ministry of Finance & Planning.

Passage of this Legislation will be the first step in ensuring that Jamaica's payments and settlement system operates in accordance with the Bank for International Settlements (BIS) Core Principles for Systemically Important Payment Systems. These Core Principles are the standards for payment systems used by international agencies such as the World Bank and the International Monetary Fund (IMF), to assess the safety and soundness of payment systems generally.

(ii) The Proceeds of Crimes Act (POCA)

POCA was passed by the Parliament in early 2007 and will come into effect on the day approved by the relevant Minister.

During the 2004/2005 legislative year a policy decision was taken to pursue the enhancements to the Anti-Money Laundering Framework through the passage of the Proceeds of Crimes Act (POCA). This statute will be based on the UK Proceeds of Crime Act and will be similar to the UK scheme of criminal and civil forfeiture. On its enactment, the POCA will target all serious offences and in respect of convictions for such offences, will make available to prosecutors the post conviction options of forfeiture of any benefits derived from commission of a crime or forfeiture based on the presumption of "criminal lifestyle". The POCA will also seek to address all the loopholes currently hampering investigative and prosecutorial efforts to combat money laundering that exist under the current Drug Offences Forfeiture of Proceeds Act (DOFPA) and under the Money Laundering Act (MLA). On the passage of the POCA, the MLA and the Regulations thereunder and the DOFPA will be repealed. On the passage of the POCA, the reporting and other obligations that now obtain for financial institutions under the MLA and MLR will be transferred to the AML provisions under the POCA.

(iii) The Financial Investigations Division Act (FIDA)

The passage of this Act will satisfy Jamaica's obligation to comply with recommendation 26 of the (FATF) 40 (revised) recommendations which states that: -

"Countries should establish a Financial Intelligence Unit that serves as a national centre for the receiving, analysis…and dissemination of suspicious transaction reports and other financial information regarding money laundering or terrorist financing".

Allied to this recommendation is the FATF advisory that such unit when established, should consider applying for membership in the Egmont Group[41].

41 "*The Egmont Group is an informal group of financial intelligence units (FIUs) established in 1995. The group was so named for the location of the first meeting at the Egmont-Arenberg Palace in Brussels. The goal of this group is to provide a forum for FIUs to improve support to their respective national anti-money laundering programmes. This support includes expanding and systemizing the exchange of financial intelligence information, improving expertise and capabilities of personnel of such organizations, and fostering better communication among FIUs through application of technology*." Source: Information Paper on FIUs and the Egmont Group – (See the FATF web site at WWW.fatf-gafi-org or see www1.oecd.org/fatf/ctry-orgpages/org-egmont_.htm

(iv) Terrorism Prevention (Reporting Entities) Regulations

These Regulations will be promulgated under the Terrorism Prevention Act and will outline the operational controls that must be maintained by financial institutions particularly when contemplating the commencement of a business relationship or one-off transaction. As such, these regulations will therefore largely mirror the Know Your Customer (KYC) obligations contained in the regulations under the Money Laundering Act and will therefore require financial institutions to establish and maintain appropriate procedures in relation to identification, record-keeping (minimum 5 years retention period), internal controls, communication, and training of employees. These Regulations will also prescribe the requisite Declaration Forms for transactions which the reporting entity knows or suspects is one that constitutes a terrorism offence; and for the quarterly reports as to whether or not the reporting entity is holding property in respect of a person who is on the United Nations list of designated terrorists or in respect of a person who has links with terrorists or terrorist groups or organizations.

14. Administration

14.1. Overview

In 2006, the Bank's Senior Management Team was further strengthened by the appointment of three (3) Deputy Governors. Effective 01 April 2006, Mrs. Myrtle Halsall and Mrs. Gayon Hosin, were confirmed in the positions of Deputy Governors, Banking & Market Operations and Research and Economic Programming Divisions, and Financial Institutions Supervisory Division, respectively. Mr. Livingstone Morrison, previously on secondment to the Sugar Company of Jamaica, was appointed as Deputy Governor with responsibility for Finance and Technology, Payment Systems, Investment and Risk Management effective 12 September 2006.

At end-2006, the Bank's staff complement was five hundred and thirty-one (531) officers comprising four hundred and sixty-six (466) permanent, twenty-one (21) contract and forty-four (44) project staff. During the year, thirty-nine (39) permanent employees and eighteen (18) contract officers were recruited. These included seven (7) persons with postgraduate degrees, twenty-one (21) with undergraduate degrees, while the remaining twenty-nine (29) had a combination of tertiary and professional qualifications. The rate of staff turnover in 2006 increased by 2.3 percentage points to 8.2 per cent. This increase was influenced in part, by staff retirements and resignations.

During 2006, the two-year agreement between the Bank's management and unionized staff represented by the Bustamante Industrial Trade Union (BITU) expired. Following an intense period of negotiation involving the Bank's management, the BITU and Ministry of Finance & Planning, a settlement was agreed for the period 01 April 2006 to 31 March 2008. The agreement which took effect on 01 April 2006 falls within the guidelines of the second Memorandum of Understanding for Public Sector Entities and Statutory Bodies.

14.2. Training and Development

The Bank's Training Institute continued to facilitate the enhancement of skills and competencies of staff members. Four hundred and twelve (412) staff members participated in one hundred and thirty-five (135) training programmes. Of this number, fifty-one (51) participated in local off-site programmes, while thirty-six (36) attended specially targetted overseas programmes. The Institute also expanded and deepened training for functionaries in the financial sector at the local and regional levels. The menu of training activities inclusive of seminars, workshops, courses, conferences and attachments, covered a number of areas ranging from leadership and management, to information technology, technical and behavioural skills.

In 2006, the Institute hosted several *In-Country* programmes. In-Country programmes have become anticipated training events primarily because of the geographic reach and considerable expertise, as well as the wide exposure made available to a larger number of employees at lower per capita cost. During the year, the Institute welcomed sixty-three (63) participants from fifteen (15) countries across the Caribbean to In-Country programmes. Participating countries included Anguilla, Antigua and Bermuda, Aruba, Curacao, Barbados, Belize, British Virgin Islands, Guyana, Netherlands Antilles, St. Kitts and Nevis, St. Lucia, St. Vincent and the Grenadines, The Bahamas, The Cayman Islands and Trinidad & Tobago.

In addition to In-Country and Institute sponsored programmes, there were collaborations with several overseas institutions. These included joint training with the Association of Supervisors of the Banks of Americas (ASBA); Office of the Comptroller of the Currency (OCC); Basel Committee on Bank Supervision; the Caribbean Financial Action Task Force (CFATF) and the Caribbean

Group of Bank Supervisors (CGBS) primarily with respect to financial supervisory training. Joint arrangements were also organized and facilitated with the Board of Governors of the Federal Reserve System (USA); the Financial Stability Institute of the Bank of International Settlements; International Monetary Fund (IMF) and the World Bank. Of particular significance was a workshop for Caribbean Regulators of Money Services Businesses and a seminar on Pillar 2 of the new Basel Accord and its implementation.

14.3. Plant and Physical Infrastructure

A number of infrastructure development projects were implemented in 2006. These included: a Financial Institutions Supervisory Information System, a Business Intelligence model and videoconferencing facility. The Bank's on-going programme of infrastructure upgrading and modernization significantly enhanced the organization's capacity to deliver improved and more efficient services.

In 2006, the Bank continued and intensified efforts at ensuring adherence to occupational safety and health standards. In this regard, the Administration and Technical Services Division and Information Systems Department, in collaboration with the Bank's Disaster Management Committee re-evaluated the Bank's disaster management and business continuity plans. In addition, an aggressive education programme on disaster management and preparedness was maintained throughout the year. Simultaneously, the Bank continued its programme of plant renovation and maintenance, ensuring that the quality of indoor air and water as well as the work environment were safe for staff and visitors and were consistent with international standards and best practice.

15. Compensation of Executive Management

		$		$
Salary Range of Executive Management		6 164 113	-	10 006 262
Allowances of Executive Management				
(a)	Governor	2 551 500		
(b)	Deputy Governors	457 590		

Notes

Executive Management includes the Governor, the Senior Deputy Governor, four (4) Deputy Governors and a General Manager. 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. The Deputy Governors and General Manager are provided with fully maintained motor vehicles. Each member of the Executive Management is eligible for benefits including a non-contributory pension plan, health insurance, life insurance and staff loans.

18/04/06 The Bank suspended the acceptance of placements on its open market operations (OMO) instruments with tenors of 270 days and 365 days, until further advised. The OMO instruments, along with corresponding interest rates, that remained on offer were 30-days: 12.6 per cent; 60-days: 12.70 per cent; 90-days: 12.75 per cent; 120-days: 12.85 per cent; and 180-days: 13.00 per cent.

01/05/06 The Bank removed the requirement that deposit-taking institutions must hold some portion of their assets as a Special Deposit with the Central Bank. This requirement was introduced in January 2003 to stabilize the financial markets. The initial deposit requirement was set at 5 per cent of prescribed liabilities and this was reduced to 1 per cent in two steps between February and May 2005. The significant improvement in macroeconomic conditions and the positive outlook for fiscal year 2006/07 allowed for the return of the remaining deposits. The sum due to financial institutions as at 28 April 2006 was J$1 564.1 million.

12/05/06 Interest rates on Bank of Jamaica 30-day, 60-day, 90-day, 120-day and 180-day open market instruments were reduced to 12.45 per cent, 12.50 per cent, 12.60 per cent, 12.65 per cent and 12.80 per cent, respectively.

01/09/06 Interest rates on Bank of Jamaica 30-day, 60-day, 90-day, 120-day and 180-day open market

instruments were reduced to 12.15 per cent, 12.2 per cent, 12.30 per cent, 12.35 per cent and 12.50 per cent, respectively.

22/09/06 Interest rates on Bank of Jamaica 30-day, 60-day, 90-day, 120-day and 180-day open market instruments were reduced to 11.95 per cent, 12.00 per cent, 12.10 per cent, 12.15 per cent and 12.30 per cent, respectively.

22/12/06 Interest rates on Bank of Jamaica 30-day, 60-day, 90-day, 120-day and 180-day open market instruments were reduced to 11.65 per cent, 11.70 per cent, 11.80 per cent, 11.85 per cent and 12.00 per cent, respectively. This policy action came against the background of continued robust economic performance and favourable medium term economic outlook.

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TO BANK OF JAMAICA

Report on the Financial Statements

Pursuant to Section 43(1) of the Bank of Jamaica Act, we have audited the accompanying financial statements of Bank of Jamaica (the Bank), set out on pages *iii* to *xxxv*, which comprise the balance sheet as at December 31, 2006, and the statements of income, changes in capital and reserves and cash flows for the year then ended, and a summary of significant accounting policies and other explanatory notes.

Management's Responsibility for the Financial Statements

Management is responsible for the preparation and fair presentation of the financial statements in accordance with International Financial Reporting Standards and the Bank of Jamaica Act. This responsibility includes designing, implementing and maintaining internal controls relevant to the preparation and fair presentation of financial statements that are free from material misstatements, whether due to fraud or error, selecting and consistently applying appropriate accounting policies, and making accounting estimates that are reasonable in the circumstances.

Auditor's Responsibility

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 comply with ethical requirements and plan and perform the audit to obtain reasonable assurance as to whether or not the financial statements are free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on the auditor's judgment, including the assessment of the risks of material misstatement of the financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal controls relevant to the Bank's preparation and fair presentation of the financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the Bank's internal control. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of accounting estimates made by management, as well as evaluating the overall presentation of the financial statements.

Report on the Financial Statements (cont'd)

We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our audit opinion.

Opinion

In our opinion, the financial statements give a true and fair view of the financial position of Bank as at December 31, 2006, and of its financial performance, changes in capital and reserves and cash flows for the year then ended in accordance with International Financial Reporting Standards, and comply with the provisions of the Bank of Jamaica Act.

We have obtained all the information and explanations which, to the best of our knowledge and belief, were necessary for the purposes of our audit. In our opinion, proper accounting records have been maintained and the financial statements are in agreement with the accounting records.

KPMG Peat Marwick

March 28, 2007

Balance Sheet
December 31, 2006

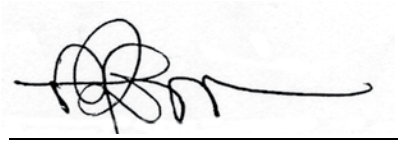
	Notes	2006 J$'000	2005 J$'000
ASSETS			
Foreign assets			
Notes and coins		9,862	5,236
Cash and cash equivalents	3	8,668,203	15,863,272
Interest in funds managed by agents		7,872,232	2,789,112
Investments	4	144,043,862	120,561,845
International Monetary Fund - Holding of Special Drawing Rights		17,874	395
		160,612,033	139,219,860
Local assets			
Notes and coins		34,840	44,796
Investments	5	86,791,126	81,794,037
International Monetary Fund - Quota Subscription	6	2,999,595	2,906,624
Investment property	7	87,082	87,000
Investments in financial institution	8	3,200	3,200
Due from Government and Government Agencies	9	13,838,500	12,941,466
Property, plant and equipment	10	1,943,685	1,612,658
Employee benefits	11	2,673,200	1,591,400
Other	12	3,017,197	2,562,762
		111,388,425	103,543,943
		272,000,458	242,763,803

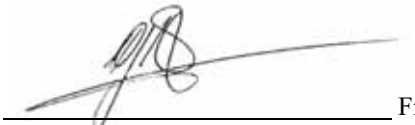
Balance Sheet (cont'd)
December 31, 2006

	Notes	2006 J$'000	2005 J$'000
LIABILITIES, CAPITAL AND RESERVES			
Liabilities			
Notes and coins in circulation	13	42,282,010	35,643,220
Deposits and other demand liabilities	14	62,170,029	40,319,676
Open market liabilities	15	150,711,491	147,206,515
International Monetary Fund - Allocation of Special Drawing Rights	16	3,913,978	3,792,666
Foreign liabilities	17	123,086	184,513
Employee benefits obligation	11	788,700	656,600
Other	18	7,468,240	11,952,415
		267,457,534	239,755,605
Capital and reserves			
Share capital	19	4,000	4,000
General reserve fund	20	20,000	20,000
Special stabilisation account	21	481,423	416,102
Other reserves	22	4,037,501	2,568,096
		4,542,924	3,008,198
		272,000,458	242,763,803

The financial statements on pages 3 to 35 were approved for issue by the Board of Directors on March 28, 2007, and signed on its behalf by:


Governor
Derick Milton Latibeaudiere


Deputy Governor
Livingstone Morrison


Financial Controller
Herbert A. Hylton

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

Income Statement
Year ended December 31, 2006

	Notes	2006 J$'000	2005 J$'000
Operating income			
Interest		20,276,685	18,833,573
Foreign exchange gain, net	23	4,530,385	4,230,382
Other		78,781	50,771
Total		24,885,851	23,114,726
Operating expenses			
Interest		22,613,220	23,481,006
Salaries and other staff costs	24	1,316,476	1,047,631
Currency expenses		700,957	566,002
Property expenses, including depreciation		428,721	366,853
Other operating expenses		305,624	290,819
Total	25	25,364,998	25,752,311
Operating loss		(479,147)	(2,637,585)
Other gains/(losses)			
Pension, medical and life insurance	11(c)	874,800	(107,800)
Impairment provision, net		3,170	(2,567)
Loss on remeasurement of staff loans and promissory note		8,193	(49,212)
Loss on revaluation of securities		(274,278)	(33,943)
Gain on disposal of property, plant and equipment		635	1,650
Expenditure on behalf of Government of Jamaica not reimbursed	9	(132,491)	(91,449)
Profit/(loss) for the year		882	(2,920,906)
Transferred to pension equalisation reserve	22(c)	(1,051,100)	(17,000)
Transferred to general reserve fund		(1,050,218)	(2,937,906)

Statement of Changes in Capital and Reserves
Year ended December 31, 2006

	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, 2004	4,000	20,000	376,637	3,793,902	4,194,539
Loss for the year	-	(2,937,906)	-	-	(2,937,906)*'
Transfer of surplus on defined benefit pension scheme	-	-	-	42,200	42,200*'
Change in fair value of available-for-sale securities	-	-	-	(1,268,006)	(1,268,006)*'
Transfer from coins in circulation	-	-	39,465	-	39,465
Loss due from consolidated fund (note 9)	-	2,937,906	-	-	2,937,906
Balances at December 31, 2005	4,000	20,000	416,102	2,568,096	3,008,198
Loss for the year	-	(1,050,218)	-	-	(1,050,218)*'
Transfer of surplus on defined benefit pension scheme	-	-	-	1,081,800	1,081,800*'
Loss on property, plant and equipment recognized in income statement	-	-	-	(3,089)	(3,089)*'
Change in fair value of available-for-sale securities	-	-	-	390,694	390,694*'
Transfer from coins in circulation	-	-	65,321	-	65,321
Loss due from consolidated fund (note 9)	-	1,050,218	-	-	1,050,218
Balances at December 31, 2006	4,000	20,000	481,423	4,037,501	4,542,924

*' - Total recognised gains of J$ 419,187,000 (2005: losses of J$4,163,712,000).
The accompanying notes form an integral part of the financial statements.

Statement of Cash Flows
Year ended December 31, 2006

	Note	2006 J$'000	2005 J$'000
Cash flows from operating activities:			
Profit/(loss) for the year		882	(2,920,906)
Adjustments for:			
Depreciation	10	208,221	157,556
Gain on disposal of property, plant and equipment		(635)	(1,650)
Employee benefits, net		(919,000)	15,600
Unrealised exchange gain		(3,743,542)	(3,293,517)
Unrealised exchange gain on International Monetary Fund - Quota subscription		(92,971)	(167,904)
Unrealised exchange loss on International Monetary Fund - Allocation of SDR's		121,312	219,088
Interest income		(20,276,685)	(18,833,573)
Interest expense		22,613,220	23,481,006
Operating profit before changes in other assets and other liabilities		(2,089,198)	(1,344,300)
Interest received		19,135,899	19,042,376
Interest paid		(27,891,037)	(21,699,216)
Other assets		184,198	47,280
Other liabilities		793,642	(370,139)
Due from Government and Government Agencies		655,337	(1,651,943)
Net cash used by operating activities		(9,211,159)	(5,975,942)
Cash flows from investing activities:			
International Monetary Fund - Holding of Special Drawing Rights		(17,479)	4,088
Interest in funds managed by agents		(4,972,544)	(58,443)
Foreign currency denominated investments		(18,659,191)	(19,438,330)
Local currency denominated investments		(4,642,559)	3,499,849
Additions to investment property		(82)	-
Additions to property, plant and equipment	10	(557,654)	(154,188)
Proceeds of disposal of property, plant and equipment		15,952	10,342
Net cash used by investing activities		(28,833,557)	(16,136,682)
Cash flows from financing activities:			
Notes and coins in circulation		6,704,111	3,291,374
Deposits and other demand liabilities		21,056,338	(1,963,540)
Open market liabilities		3,504,976	21,391,690
Foreign liabilities		(65,057)	(74,243)
Net cash provided by financing activities		31,200,368	22,645,281
Net (decrease)/increase in cash and cash equivalents		(6,844,348)	532,657
Cash and cash equivalents at January 1		15,913,304	15,903,561
Effect of exchange rate fluctuation on cash held		(356,051)	(522,914)
Cash and cash equivalents at December 31		8,712,905	15,913,304
Cash and cash equivalents at December 31 comprise:			
Foreign notes and coins		9,862	5,236
Foreign cash and cash equivalents		8,668,203	15,863,272
Local notes and coins		34,840	44,796
		8,712,905	15,913,304

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

BANK OF JAMAICA

Notes to the Financial Statements
December 31, 2006

1. Identification

Bank of Jamaica (hereafter "the Bank") was established under the Bank of Jamaica Act (hereafter "the Act") amended on December 8, 2004. The Bank is domiciled in Jamaica and its registered office is located at Nethersole Place, Kingston.

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. Statement of compliance, basis of preparation and significant accounting policies

(a) Statement of compliance:

The financial statements are prepared in accordance with the provisions of the Bank of Jamaica Act and International Financial Reporting Standards (IFRS) and their interpretations, adopted by the International Accounting Standards Board (IASB).

(b) Basis of preparation:

The financial statements are presented in Jamaica dollars (J$) which is the Bank's functional currency and are prepared on the historical cost basis, except for the inclusion of available-for-sale investments, investment property and certain classes of property, plant and equipment at fair value.

The accounting policies set out below have been applied consistently to all periods presented in these financial statements and comply in all material respects to IFRS.

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

Accounting estimates and judgements

Judgements made by management in the application of IFRS that have significant effect on the financial statements and estimates with a significant risk of material adjustment in the next financial year are discussed below:

(a) Pension and other post-retirement benefits

The amounts recognised in the balance sheet and income statement for pension and other post-retirement benefits are determined actuarially using several assumptions. The primary assumptions used in determining the amounts recognised include expected long-term return on plan assets, the discount rate used to determine the present value of estimated future cash flows required to settle the pension and other post-retirement obligations and the expected rate of increase in medical costs for post-retirement medical benefits.

BANK OF JAMAICA

Notes to the Financial Statements (cont'd)
December 31, 2006

2. Statement of compliance, basis of preparation and significant accounting policies (cont'd)

(b) Basis of preparation:

Accounting estimates and judgements (cont'd)

(a) Pension and other post-retirement benefits (cont'd)

The expected return on plan assets is assumed after considering the long-term historical returns, asset allocation and future estimates of long-term investment returns. The discount rate is determined based on the estimate of yield on long-term government securities that have maturity dates approximating the terms of the company's obligation; in the absence of such instruments in Jamaica, it has been necessary to estimate the rate by extrapolating from the longest-tenor security on the market. The estimate of expected rate of increase in medical costs is determined based on inflationary factors. Any changes in these assumptions will impact the amounts recorded in the financial statements for these obligations.

It is reasonably possible, based on existing knowledge, that outcomes within the next financial year that are different from these assumptions could require a material adjustment to the carrying amount reflected in the financial statements.

(c) 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 U.S. 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.

Monetary assets and liabilities denominated in foreign currencies at the balance sheet date are translated at the foreign exchange rates prevailing at that date. Transactions in foreign currencies are translated at the foreign exchange rates ruling at the dates of those transactions.

Gains and losses arising on fluctuations in exchange rates are included in the income statement.

(d) 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 loans and receivables and available-for-sale securities.

BANK OF JAMAICA

Notes to the Financial Statements (cont'd)
December 31, 2006

2. Statement of compliance, basis of preparation and significant accounting policies (cont'd)

(d) Financial instruments (cont'd):

(i) Classification of investments (cont'd):

Loans and receivables are non-derivate financial assets acquired by the Bank with fixed or determinable payments and which are not quoted in an active market. An active market is one where quoted prices are readily and regularly available from an exchange, dealer, broker or other agency and those prices represent actual and regularly occurring market transactions on an arm's length basis. Loans and receivables are recognised on the day they are acquired by the Bank.

Other financial instruments held by the Bank are classified as available-for-sale. Available-for-sale instruments are recognised on the date the Bank commits to purchase the instruments.

(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 [note 2 (k)].

All non-derivate, non-trading financial liabilities and 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 loans and receivables and are stated at cost (amortised cost), less provision for losses and impairment as appropriate.

[ii] Local currency denominated Government of Jamaica securities which do not have a quoted market price in an active market and whose fair values cannot be reliably determined, and interest-bearing deposits are stated at historical or amortised cost.

[iii] Local currency denominated Government of Jamaica securities with quoted prices in an active market are classified as available-for-sale and measured at fair value.

[iv] US Government bonds are classified as available-for-sale and are measured at fair value.

BANK OF JAMAICA

Notes to the Financial Statements (cont'd)
December 31, 2006

2. Statement of compliance, basis of preparation and significant accounting policies (cont'd)

(d) Financial instruments (cont'd):

(ii) Measurement (cont'd):

[v] 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 amounts involved are not material to the bank. 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, except for impairment losses and, in the case of monetary items such as debt securities, foreign exchange gains and losses. When the financial assets are sold, collected or otherwise disposed of, the cumulative gain or loss recognised in equity is recognised in the income statement.

(v) Cash and cash equivalents:

Cash and cash equivalents are shown at cost.

(vi) Other assets:

Other assets are stated at amortised cost, less impairment losses [note 2 (k)].

BANK OF JAMAICA

Notes to the Financial Statements (cont'd)
December 31, 2006

2. Statement of compliance, basis of preparation and significant accounting policies (cont'd)

(d) Financial instruments (cont'd):

(vii) Other liabilities:

Other liabilities, including provisions, are stated at amortised cost.

(viii) Provision:

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.

(ix) 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.

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

(e) Property, plant and equipment:

(i) Owned assets:

Items of property, plant and equipment are stated at cost less accumulated depreciation and impairment losses [note 2 (k)], except for freehold land and buildings which are stated at market value.

Cost includes expenditures that are directly attributable to the acquisition of the asset. The cost of self-constructed assets includes the cost of materials and direct labour and any other costs directly attributable to bringing the asset to a working condition for its intended use.

The cost of replacing part of an item of property, plant and equipment is recognised in the carrying amount of the item if it is probable that the future economic benefits embodied within the part will flow to the bank and it can be measured reliably. The costs of the day-to-day servicing of property, plant and equipment are recognised in profit or loss as incurred.

The market value of freehold land and building is the estimated amount for which a property could be exchanged on the date of valuation between a willing buyer and a willing seller in an arms' length transaction.

BANK OF JAMAICA

Notes to the Financial Statements (cont'd)
December 31, 2006

2. Statement of compliance, basis of preparation and significant accounting policies (cont'd)

(e) Property, plant and equipment:

(ii) Depreciation:

Property, plant and equipment are depreciated on the straight-line basis at annual rates estimated to write down the assets to their residual value 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 estimated useful lives are as follows:

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

The depreciation methods, useful lives and residual values are reassessed at the reporting date.

(f) 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 income statement.

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.

(g) Taxation:

Section 46 of the Act, which exempted the Bank from income tax, stamp duties and transfer tax, was repealed on December 23, 2003. 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.

(h) Employee benefits:

Employee benefits comprise 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 vacation leave, and non-monetary benefits such as medical care and life insurance; post-employment benefits such as pension and medical care; other long-term employee benefits such as termination benefits.

BANK OF JAMAICA

Notes to the Financial Statements (cont'd)
December 31, 2006

2. Statement of compliance, basis of preparation and significant accounting policies (cont'd)

(h) Employee benefits (cont'd):

(i) General 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.

(ii) Defined-benefit scheme and post employment benefits:

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. 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.

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 income statement.

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.

BANK OF JAMAICA

Notes to the Financial Statements (cont'd)
December 31, 2006

2. Statement of compliance, basis of preparation and significant accounting policies (cont'd)

(h) Employee benefits (cont'd):

(ii) Defined-benefit scheme and post employment benefits: (cont'd)

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.

(i) 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.

(j) Investment property:

Investment property is stated at fair value determined by management and based on an initial valuation by an independent registered valuer. Fair value is based on market value, being the estimated amount for which the property could be exchanged on the date of valuation between a willing buyer and a willing seller, in an arms length transaction, after proper marketing wherein the parties had acted knowledgeably, prudently and without compulsion.

Any gain or loss arising from a change in fair value is recognised in the income statement. In carrying out their audit, the auditors relied on the valuators' report.

(k) Impairment:

The carrying amounts of the Bank's assets are reviewed at each balance sheet date to determine whether there is any indication of impairment. If any such indication exists, the asset's recoverable amount is estimated at each balance sheet date. An impairment loss is recognised whenever the carrying amount of an asset or its cash-generating unit exceeds its recoverable amount. Impairment losses are recognised in the income statement.

When a decline in the fair value of an available-for-sale financial asset has been recognised directly in equity and there is objective evidence that the asset is impaired, the cumulative loss that has been recognised directly in equity is recognised in the income statement even though the financial asset has not been derecognised. The amount of the cumulative loss that is recognised in the statement of income and expenses is the difference between the acquisition cost and current fair value, less any impairment loss on that financial asset previously recognised in the income statement.

BANK OF JAMAICA

Notes to the Financial Statements (cont'd)
December 31, 2006

2. Statement of compliance, basis of preparation and significant accounting policies (cont'd)

(k) Impairment (cont'd):

(i) Calculation of recoverable amount:

The recoverable amount of loans receivable is determined as indicated in accounting policy note 2(d)(ii).

The recoverable amount of the Bank's investment in loans and receivables and other assets is calculated as the present value of expected future cash flows, discounted at the original effective interest rate inherent in the asset. Receivables with a short-term duration are not discounted.

The recoverable amount of other assets is the greater of their net selling price and value in use. In assessing value in use, the estimated future cash flows are discounted to their present value using a pre-tax discount rate that reflects current market assessments of the time value of money and the risks specific to the asset.

For an asset that does not generate largely independent cash inflows, the recoverable amount is determined for the cash-generating unit to which the asset belongs.

(ii) Reversals of impairment:

An impairment loss in respect of loans and receivables carried at amortised cost is reversed, if the subsequent increase in recoverable amount can be related objectively to an event occurring after the impairment loss was recognised. For all other assets, an impairment loss is reversed, if there has been change in the estimate used to determine the recoverable amount.

An impairment loss in respect of an investment in an equity instrument classified as available-for-sale is not reversed through the income statement. If the fair value of a debt instrument classified as available-for-sale increases and the increase can be objectively related to an event occurring after the impairment loss was recognised in the statement of income and expenses, the impairment loss shall be reversed, with the amount of the reversal recognised in the income statement.

An impairment loss is reversed only to the extent that the asset's carrying amount does not exceed the carrying amount that would have been determined, if no impairment loss had been recognised.

BANK OF JAMAICA

Notes to the Financial Statements (cont'd)
December 31, 2006

2. Statement of compliance, basis of preparation and significant accounting policies (cont'd)

(l) Adoption of new and revised IFRS and interpretations

(i) During the year, the following revised and new IFRS were effective:

IFRS 6	Exploration for Evaluating of Mineral Resources	January 1, 2006
IFRIC 4	Determining whether an Arrangement Contains a Lease	January 1, 2006
IFRIC 5	Rights to Interest Arising from Decommissioning, Restoration and Environmental Rehabilitation Funds	January 1, 2006
IAS 19 Amendments	Actuarial Gains & Losses, Group Plans and Disclosures	January 1, 2006
IAS 39 Amendments	The Fair Value Option	January 1, 2006
IAS 39 Amendments	Financial Instrument Cash Flow Hedge Accounting for Forecast Intra-group Transactions	January 1, 2006
IAS 39 Amendments	Financial Guarantee Contracts	January 1, 2006

IAS 19 amendments resulted in additional disclosures as indicated at note 11. There were no changes resulting from the adoption of the other new standards and interpretations.

(ii) At the date of authorisation of the financial statements, there were certain standards and interpretations which were in issue but were not yet effective. The standards and interpretations, which are effective for accounting periods beginning on or after the dates indicated below, and the dates are as follows:

IFRIC 8	Scope of IFRS 2	May 1, 2006
IFRS 7	Financial Instruments: Disclosure	January 1, 2007
IFRIC 6	Liabilities arising from Participating in a Specific Market – Waste, Electrical and Electronic Equipment	December 1, 2006
IFRIC 7	Applying the Restatement Approach under IAS 29 Financial Reporting in Hyper-Inflationary Economies	March 1, 2006
IFRIC 9	Reassessment of Embedded Derivatives	June 1, 2006
IFRIC 10	Interim Financial Reporting	November 1, 2006
IFRIC 11	Group and Treasury Share Transactions	March 1, 2007
IFRS 8	Operating Segments	January 1, 2009
IFRIC 12	Service Concession Arrangement	January 1, 2008

BANK OF JAMAICA

Notes to the Financial Statements (cont'd)
December 31, 2006

2. Statement of compliance, basis of preparation and significant accounting policies (cont'd)

(l) Adoption of new and revised IFRS and interpretations (cont'd)

(ii) (cont'd)

The adoption of IFRS 7 is expected to result in additional disclosures for financial instruments. Except for these additional disclosures, the adoption of these standards and interpretations are not expected to have a material impact on the financial statements.

(m) Related party balances and transactions:

A party is related to the Bank if:

(i) directly or indirectly the party:

- controls, is controlled by, or is under common control with the Bank;
- has an interest in the Bank that gives it significant influence over the Bank, or
- has joint control over the Bank;

(ii) the party is a member of the key management personnel of the Bank.

(iii) the party is a close member of the family of any individual referred to in (i) or (ii) above;

(iv) the party is a post-employment benefit plan for the benefit of employees of the Bank, or any entity that is a related party of the Bank.

A related party transaction is a transfer of resources, services or obligations between related parties, regardless of whether a price is charged.

3. Cash and cash equivalents

	2006 J$'000	2005 J$'000
Current accounts and money at call with foreign banks	8,435,900	15,614,567
Current accounts with local banks	232,303	248,705
	8,668,203	15,863,272

4. Foreign currency denominated investments

	2006 J$'000	2005 J$'000
Available-for-sale securities:		
US Government bonds	64,747,867	52,027,554
Barbados Government bond	36,999	37,494
	64,784,866	52,065,048
Short-term deposits with foreign banks	79,258,996	68,496,797
	144,043,862	120,561,845

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Notes to the Financial Statements (cont'd)
December 31, 2006

5. Local currency denominated investments

	2006 J$'000	2005 J$'000
Loans and receivables:		
Jamaica Government Securities:		
Local registered stock	49,511,938	42,451,484
Available-for-sale securities:		
Jamaica Government Securities:		
Local registered stock	15,524,300	22,619,164
Treasury bills	2,043	85,101
Investment bonds	16,273,817	5,309,389
Investment debentures	4,734,154	11,123,941
Registered bond	744,874	204,958
	37,279,188	39,342,553
	86,791,126	81,794,037

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	2006 J$'000	2005 J$'000
Amount subscribed (net of reserve tranche of J$Nil):			
At beginning of year	31,125	2,906,624	2,738,720
Effect of exchange rate fluctuation	-	92,971	167,904
At end of year	31,125	2,999,595	2,906,624

7. Investment property

	2006 J$'000	2005 J$'000
Investment property	87,082	87,000

The carrying amount of the investment property is the fair value of the property arrived at by management, who took account of the location of the property. The property was initially valued by C. D. Alexander Limited, registered independent valuator having an appropriate recognised professional qualification and recent experience in the location and category of the property being valued, in 2003 at $87,000,000. The fair value arrived at by management was determined having regard to recent market transactions for similar properties in the same location as the Bank's investment property and was not materially different from that of the independent valuator in 2003 [note 2 (j)]. Direct operating expenses during the year were $2,635,712 (2005: $1,137,136).

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Notes to the Financial Statements (cont'd)
December 31, 2006

8. Investments in financial institution

	2006 J$'000	2005 J$'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

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.

During the year, the Board approved a grant to EX-IM Bank equivalent to the net liquidation proceeds upon completion of the winding up of the subsidiary company, less the par value of shares held by the Bank.

9. Due from Government and Government Agencies

	Dec. 31, 2005 J$'000	Movements during the year: Advances/ Losses J$'000	(Settlement)/ Profit J$'000	Charged to expenses J$'000	Dec. 31, 2006 J$'000
Expenditure on behalf of Government:					
Payment of interest on foreign liabilities [see (b) below]	-	132,491	-	(132,491)	-
Other expenditure on behalf of Government	2,299	15,240	-	-	17,539
Withholding tax refund due	4,797,736	1,597,469	-	-	6,395,205
Accrued interest on Government securities	5,873,385	6,375,538	(5,873,385)	-	6,375,538
Net profit payable to/net loss due from Consolidated Fund	2,268,046	1,050,218	(2,268,046)	-	1,050,218
	12,941,466	9,170,956	(8,141,431)	(132,491)	13,838,500

(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.

Except for temporary overdrafts, no advances were made to the Government during the Bank's financial years ended December 31, 2006 and 2005.

(b) Interest on foreign liabilities comprises interest paid on Government of Jamaica foreign liabilities.

BANK OF JAMAICA

Notes to the Financial Statements (cont'd)
December 31, 2006

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

(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
Cost or valuation:						
December 31, 2004	1,263,437	1,208	811,401	115,978	7,340	2,199,364
Additions	14,708	95	79,462	48,419	11,504	154,188
Transfers	4,666	-	2,674	-	(7,340)	-
Disposals/write-offs	-	-	(2,375)	(21,361)	-	(23,736)
December 31, 2005	1,282,811	1,303	891,162	143,036	11,504	2,329,816
Additions	12,187	5,899	397,242	54,770	87,556	557,654
Transfers	4,176	-	3,001	-	(7,177)	-
Disposals/write-offs	(14,482)	-	(1,995)	(17,288)	-	(33,765)
December 31, 2006	1,284,692	7,202	1,289,410	180,518	91,883	2,853,705
At cost	65,174	7,202	1,289,410	180,518	91,883	1,634,187
At valuation	1,219,518	-	-	-	-	1,219,518
	1,284,692	7,202	1,289,410	180,518	91,883	2,853,705
Depreciation:						
December 31, 2004	63,212	841	487,961	22,633	-	574,647
Charge for the year	64,192	62	77,572	15,730	-	157,556
Eliminated on disposals	-	-	(1,915)	(13,130)	-	(15,045)
December 31, 2005	127,404	903	563,618	25,233	-	717,158
Charge for the year	64,348	652	117,989	25,232	-	208,221
Eliminated on disposals	(1,475)	-	(1,995)	(11,889)	-	(15,359)
December 31, 2006	190,277	1,555	679,612	38,576	-	910,020
Net book values:						
December 31, 2006	1,094,415	5,647	609,798	141,942	91,883	1,943,685
December 31, 2005	1,155,407	400	327,544	117,803	11,504	1,612,658
December 31, 2004	1,200,225	367	323,440	93,345	7,340	1,624,717

The Bank's land and buildings were revalued in 2003 by The C. D. Alexander Company Realty Limited, Real Estate Broker, Appraiser and Auctioneer on the open-market, existing-use basis. A revaluation was not done during the year as management was of the opinion that there was no significant change in the value of the land and buildings. The surplus arising on revaluation, inclusive of depreciation no longer required, is included in property revaluation reserve (note 22).

BANK OF JAMAICA

Notes to the Financial Statements (cont'd)
December 31, 2006

11. Employee benefits

The Bank operates a non-contributory defined benefit pension scheme, as well as medical and life insurance schemes, for all its permanent eligible employees and funds supplemental 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.

(a) Pension assets:

	2006 J$'000	2005 J$'000
Present value of funded obligations	(2,187,500)	(1,638,700)
Fair value of plan assets	6,051,300	5,326,300
Unrecognised amount due to limitation	(285,900)	(968,400)
Unrecognised actuarial gains	(904,700)	(1,127,800)
Recognised assets	2,673,200	1,591,400

(i) Movements in the liability for defined benefit obligations recognised in the balance sheet:

	2006 J$'000	2005 J$'000
Balance at beginning of year	(1,638,700)	(1,449,500)
Benefits paid	83,700	41,600
Service and interest costs	(256,800)	(234,200)
Actuarial gain	(375,700)	3,400
Balance at end of year	(2,187,500)	1,638,700

(ii) Movements in plan assets:

	2006 J$'000	2005 J$'000
Fair value of plan assets at January 1	5,326,300	4,199,100
Contributions paid	30,700	25,200
Expected return on plan assets	583,000	461,000
Benefits paid	(83,700)	(41,600)
Actuarial gain	195,000	682,600
Fair value of plan assets on December 31	6,051,300	5,326,300

Plan assets consist of the following:

Government of Jamaica securities	5,645,300	4,781,600
Certificates of deposit	20,000	115,000
Real estate	58,000	47,000
Other	328,000	382,700
	6,051,300	5,326,300

BANK OF JAMAICA

Notes to the Financial Statements (cont'd)
December 31, 2006

11. Employee benefits (cont'd)

(a) Pension assets (cont'd):

(iii) Credit recognised in the income statement:

	2006 J$'000	2005 J$'000
Current service costs	(57,200)	(55,600)
Interest on obligations	(199,600)	(178,700)
Expected return on plan assets	583,000	461,000
Past service cost	(300)	(100)
Changes in disallowed assets	682,600	(211,200)
Net actuarial losses	42,600	1,600
	1,051,100	17,000
Actual return on pension plan assets	12.9%	21.4%

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

	2006 %	2005 %
Discount rate	12.0	12.5
Expected return on plan assets	11.0	11.0
Future salary increases	9.0	9.0

The overall expected long-term rate of return of assets is 10%. The expected long-term rate of return is based on an inflation rate of 7% and real rate of investment return of 4%.

(v) Historical information

Defined benefit pension plan

	2006 J$'000	2005 J$'000	2004 J$'000	2003 J$'000	2002 J$'000
Present value of the defined benefit obligation	(2,187,500)	(1,638,700)	(1,449,500)	(1,133,400)	(1,057,800)
Fair value of plan assets	6,051,300	5,326,300	4,199,100	3,710,400	3,063,700
Surplus in plan	3,863,800	3,687,600	2,749,600	2,577,000	2,005,900
Experience adjustments arising on plan liabilities	(384,800)	(278,000)	97,900	(38,100)	(46,600)
Experience adjustments arising on plan assets	195,000	682,600	36,200	349,000	167,300

BANK OF JAMAICA

Notes to the Financial Statements (cont'd)
December 31, 2006

11. Employee benefits (cont'd)

(b) Post-retirement obligations:

Present value of obligations and recognised liability

(i) Movements in the liability for defined benefit obligations:

	2006 J$'000	2005 J$'000
Balance at beginning of year	(656,600)	(573,600)
Expenses recognised in statement of income and expenses	(176,300)	(124,800)
Contributions paid	44,200	41,800
Balance at end of year	(788,700)	(656,600)

(ii) Expense recognised in the income statement:

	2006 J$'000	2005 J$'000
Current service costs	(22,500)	(24,700)
Interest on obligations	(130,900)	(92,600)
Past service costs	(100)	(100)
Net actuarial losses recognised in the year	(22,800)	(7,400)
	(176,300)	(124,800)

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

	2006 %	2005 %
Discount rate	12.0	12.5
Medical claims growth	11.0	11.0

Assumptions regarding future mortality are based on the PA(90) mortality table for pensioners (British mortality tables), but with each age rated down by six years.

(iv) Historical information

Post-employment medical benefits

	2006 J$'000	2005 J$'000	2004 J$'000	2003 J$'000	2002 J$'000
Present value of obligations	1,443,900	1,069,600	761,500	652,200	458,500
Experience adjustments arising on plan liabilities	(30,100)	78,300	30,200	(73,700)	(14,000)

BANK OF JAMAICA

Notes to the Financial Statements (cont'd)
December 31, 2006

11. Employee benefits (cont'd)

(c) Assumed health care cost trend have a significant effect on the amounts recognised in profit or loss. A one percentage point change in assumed healthcare cost trend rates would have the following effects:

	One percentage point increase J$'000	One percentage point decrease J$'000
Effect on the aggregate service and interest cost	9,900	(7,200)
Effect on the defined benefit obligation	64,000	(49,000)

(d) The estimated pension contributions expected to be paid into the plan during the next financial year is J$32,520,000.

(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.

In addition, the Bank granted a further supplement to pensioners: these supplemental pension payments amounted to J$39,205,660 for the year (2005: J$37,654,484), all of which have been included in staff costs in the income statement.

12. Other assets

	2006 J$'000	2005 J$'000
Items in process of collection	824	14,872
Overdrafts	1,285	7,833
Staff and ex-staff loans, including interest receivable (note 26)	1,016,659	983,414
Stock of unissued notes and coins	937,168	1,114,285
Accrued interest receivable other than on GOJ securities	1,336,711	698,078
Promissory notes	65,173	81,339
Other	76,516	97,601
	3,434,336	2,997,422
Less:		
Re-measurement of promissory note	(7,060)	(10,570)
Impairment and re-measurement of staff and ex-staff loans	(410,079)	(424,090)
	3,017,197	2,562,762

13. Notes and coins in circulation

	2006 J$'000	2005 J$'000
Notes	40,837,740	34,394,915
Coins	1,444,270	1,248,305
	42,282,010	35,643,220

BANK OF JAMAICA

Notes to the Financial Statements (cont'd)
December 31, 2006

13. Notes and coins in circulation (cont'd)

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, 2006, were 3.8 (2005: 3.91) times the value of notes and coins in circulation at that date.

14. Deposits and other demand liabilities

	2006 J$'000	2005 J$'000
Government and Government agencies	19,976,955	3,599,887
Commercial banks and specified financial institutions	31,967,984	28,826,793
International Money Fund	65,895	63,852
Others	10,159,195	7,829,144
	62,170,029	40,319,676
Jamaica dollar equivalent of foreign currency deposits	16,286,254	14,712,408
Jamaica dollar deposits	45,883,775	25,607,268
	62,170,029	40,319,676

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, section 14 of the Financial Institutions Act and section 31 of the Building Societies Regulations.

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 Bank was not holding any specified securities in lieu of cash deposits.

At the balance sheet date, the following obtained:

	2006 J$'000	2005 J$'000
Amounts included in deposit liabilities of the Bank, representing statutory reserves	27,075,462	25,579,437

15. Open market liabilities

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. Receipt of funds is evidenced by the Bank issuing, to the depositor, Certificates of Deposit.

BANK OF JAMAICA

Notes to the Financial Statements (cont'd)
December 31, 2006

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 (2005: Nil) and, accordingly, the changes arise from exchange rate fluctuations.

	SDRs'000	2006 J$'000	2005 J$'000
At beginning of year	40,613	3,792,666	3,573,578
Effect of exchange rate fluctuation	-	121,312	219,088
At end of year	40,613	3,913,978	3,792,666

17. Foreign liabilities

	2006 J$'000	2005 J$'000
Borrowings - Principal	109,444	171,142
- Accrued interest	2,865	3,505
Unsettled balances on bilateral accounts for Caricom trade	10,777	9,866
	123,086	184,513

18. Other liabilities

	2006 J$'000	2005 J$'000
Interest payable	6,479,372	11,757,189
Staff and staff-related expenses	220,232	149,526
Other	768,636	45,700
	7,468,240	11,952,415

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 the 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.

BANK OF JAMAICA

Notes to the Financial Statements (cont'd)
December 31, 2006

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.

22. Other reserves

This represents the following:

	2006 J$'000	2005 J$'000
Securities revaluation reserve [see (a) and note 29]	242,634	(148,060)
Property revaluation reserve [see (b)]	1,121,667	1,124,756
Pension equalisation reserve [see (c)]	2,673,200	1,591,400
	4,037,501	2,568,096

(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, net

	2006 J$'000	2005 J$'000
Net unrealised gain on translation of foreign currency assets and liabilities and realised gain on settlement of foreign assets and foreign liabilities	4,953,990	4,062,437
Exchange (loss)/gain on purchases and sales of foreign currency	(423,605)	167,945
	4,530,385	4,230,382

24. Employee numbers and costs

The number of employees at the end of the year was 466 (2005: 469) full-time and 21 (2005: 21) contract. The related costs for these employees were as follows:

	2006 J$'000	2005 J$'000
Salaries and wages	1,110,549	882,601
Statutory payroll contributions	69,277	59,256
Uniforms	18,318	4,699
Staff welfare	63,226	53,786
Other	55,106	47,289
	1,316,476	1,047,631

BANK OF JAMAICA

Notes to the Financial Statements (cont'd)
December 31, 2006

25. Operating expenses

Operating expenses include the following charges:

	2006 J$'000	2005 J$'000
Depreciation	208,221	157,556
Auditors' remuneration	5,950	5,390
Payments for redundancies	1,692	-

26. Related party balances

The Bank has a related party relationship with its board of directors, the members of the Executive Council and the Bank of Jamaica pension scheme. Membership of the Executive Council is limited to fifteen (15) persons.

The balance sheet includes balances arising in the ordinary course of business, with related parties, as follows:

	2006 J$'000	2005 J$'000
Loans (included in note 12)	64,257	55,621

The interest rate applicable to the above loans range from 3% - 5%. In addition, a deemed taxable income is computed on the interest saved by virtue of the concessionary interest rate. No non-executive director receives emoluments or is in receipt of a BOJ staff loan.

The income statement includes income earned from/expenses incurred in transactions with related parties, in the ordinary course of business, as follows:

	2006 J$'000	2005 J$'000
Interest expense – pension scheme	12,230	48,640
Interest income – Executive Council	1,690	1,202
Pension scheme	77,073	67,797

Executive Council compensation is as follows:

	2006 J$'000	2005 J$'000
Short-term employee benefits included in staff costs (note 24)	91,710	86,177

27. Commitments

At the balance sheet date the Bank had:

(a) Capital commitments as follows:

	2006 J$'000	2005 J$'000
Authorised and contracted	62,331	77,908
Authorised but not contracted	43,207	402,140
	105,538	480,048

BANK OF JAMAICA

Notes to the Financial Statements (cont'd)
December 31, 2006

27. Commitments (cont'd)

(b) Operating lease commitment payable as follows:

	2006	2005
	J$'000	J$'000
Within one year	3,093	2,811
Subsequent years	11,260	14,353
	14,353	17,164

28. Contingent liabilities

At December 31, 2006, 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, 2006.

29. Financial instruments

A financial instrument is any contract that gives rise to 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 and cash equivalents, 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, open market liabilities, International Monetary Fund – Allocation of Special Drawing Rights, foreign liabilities and other liabilities.

The fair value of foreign and local currency 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(d)(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.

BANK OF JAMAICA

Notes to the Financial Statements (cont'd)
December 31, 2006

29. Financial instruments (cont'd)

(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:

	2006 J$'000	2005 J$'000
Foreign currency assets	164,934,337	142,821,121
Foreign currency liabilities	(20,389,212)	(18,753,438)
Net foreign currency assets	144,545,125	124,067,683

Exchange rates at December 31:

	2005	2006
US$1 to J$	66.95	64.40
UK£1 to J$	131.12	110.68
CDN$1 to J$	57.46	55.25
€ to J$	88.35	76.26

At March 28, 2007, the exchange rates were US$1 to J$67.61, UK£1 to J$132.58, CDN$1 to J$58.39 and €1 to J$90.13.

(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, at least, 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.

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Notes to the Financial Statements (cont'd)
December 31, 2006

29. Financial instruments (cont'd)

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

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

	2006						
	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	-	-	-	-	44,702	44,702	-
Cash and cash equivalents	-	-	-	-	8,668,203	8,668,203	-
Interest in funds managed by agents	-	-	-	7,872,232	-	7,872,232	4.0
Foreign currency denominated investments	79,258,996	-	64,784,866	-	-	144,043,862	5.0
International Monetary Fund - Holding of Special Drawing Rights	-	-	-	-	17,874	17,874	-
Local currency denominated investments	3,875,679	1,354,463	81,560,984	-	-	86,791,126	14.0
International Monetary Fund – Quota Subscription	-	-	-	-	2,999,595	2,999,595	-
Investment property	-	-	-	-	87,082	87,082	-
Investments in financial institutions	-	-	-	-	3,200	3,200	-
Due from Government and Government agencies	-	-	-	-	13,838,500	13,838,500	-
Property, plant and equipment	-	-	-	-	1,943,685	1,943,685	-
Employee benefits	-	-	-	-	2,673,200	2,673,200	-
Other assets	-	-	-	-	3,017,197	3,017,197	-
Total assets	83,134,675	1,354,463	146,345,850	7,872,232	33,293,238	272,000,458	7.23
Liabilities							
Notes and coins in circulation	-	-	-	-	42,282,010	42,282,010	-
Deposits and other demand liabilities:							
Jamaica dollar equivalent of foreign currency deposits	4,890,611	-	-	11,395,643	-	16,286,254	-
Jamaica dollar deposits	30,123,156	-	-	15,760,619	-	45,883,775	-
Open market liabilities	93,726,459	-	-	56,985,032	-	150,711,491	12.59
International Monetary Fund – Allocation of Special Drawing Rights	-	-	-	-	3,913,978	3,913,978	-
Foreign liabilities	-	-	109,444	-	13,642	123,086	8.20
Employee benefits obligation	-	-	-	-	788,700	788,700	-
Other liabilities	-	-	-	-	7,468,240	7,468,240	-
Capital and reserves	-	-	-	-	4,542,924	4,542,924	-
Total liabilities	128,740,226	-	109,444	84,141,294	59,009,494	272,000,458	6.98
Total interest rate sensitivity gap	(45,605,551)	1,354,463	146,236,406	(76,269,062)	(25,716,256)	-	
Cumulative gap	(45,605,551)	(44,251,088)	101,985,318	25,716,256	-	-	

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Notes to the Financial Statements (cont'd)
December 31, 2006

29. Financial instruments (cont'd)

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

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

	2005						
	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	-	-	-	-	50,032	50,032	-
Cash and cash equivalents	-	-	-	-	15,863,272	15,863,272	-
Interest in funds managed by agents	-	-	-	2,789,112	-	2,789,112	4.2
Foreign currency denominated investments	68,496,797	-	52,065,048	-	-	120,561,845	4.39
International Monetary Fund - Holding of Special Drawing Rights	-	-	-	-	395	395	-
Local currency denominated investments	5,228	12,650,578	69,138,231	-	-	81,794,037	15.2
International Monetary Fund – Quota Subscription	-	-	-	-	2,906,624	2,906,624	-
Investment property	-	-	-	-	87,000	87,000	-
Investments in financial institutions	-	-	-	-	3,200	3,200	-
Due from Government and Government agencies	-	-	-	-	12,941,466	12,941,466	-
Property, plant and equipment	-	-	-	-	1,612,658	1,612,658	-
Employee benefits	-	-	-	-	1,591,400	1,591,400	-
Other assets	-	-	-	81,339	2,481,423	2,562,762	-
Total assets	68,502,025	12,650,578	121,203,279	2,870,451	37,537,470	242,763,803	7.35
Liabilities							
Notes and coins in circulation	-	-	-	-	35,643,220	35,643,220	-
Deposits and other demand liabilities:							
Jamaica dollar equivalent of foreign currency deposits	4,401,395	-	-	10,311,013	-	14,712,408	-
Jamaica dollar deposits	10,255,269	-	-	15,351,999	-	25,607,268	-
Open market liabilities	63,678,960	83,527,555	-	-	-	147,206,515	14.04
International Monetary Fund – Allocation of Special Drawing Rights	-	-	-	-	3,792,666	3,792,666	-
Foreign liabilities	-	-	171,142	-	13,371	184,513	8.25
Employee benefits obligation	-	-	-	-	656,600	656,600	-
Other liabilities	-	-	-	-	11,952,415	11,952,415	-
Capital and reserves	-	-	-	-	3,008,198	3,008,198	-
Total liabilities	78,335,624	83,527,555	171,142	25,663,012	55,066,470	242,763,803	8.52
Total interest rate sensitivity gap	(9,833,599)	(70,876,977)	121,032,137	(22,792,561)	(17,529,000)	-	
Cumulative gap	(9,833,599)	(80,710,576)	40,321,561	17,529,000	-	-	

BANK OF JAMAICA

Notes to the Financial Statements (cont'd)
December 31, 2006

29. Financial instruments (cont'd)

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

(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.

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 and cash equivalents 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:

	2006 J$'000	2005 J$'000
Jamaica	87,644,939	82,616,536
U.S.A. and other industrialised countries	159,979,723	138,680,227
Barbados	36,999	37,494
Multilateral Institutions	3,017,469	2,907,018
Other	372,508	275,488
Total financial assets	251,051,638	224,516,763

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.

BANK OF JAMAICA

Notes to the Financial Statements (cont'd)
December 31, 2006

29. Financial instruments (cont'd)

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

(iv) Market risk (cont'd):

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.

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.