BANK OF JAMAICA

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Remarks at Blast Off 2011 Seminar themed "Rekindle the Passion" hosted by the Jamaica Association of Insurance and Financial Advisors (JAIFA)

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Ladies and Gentlemen,

Thank you for inviting me to join you in your 'Blast Off' and for giving me an opportunity to share with you my view of the economic outlook for 2011.

Had I been offered this opportunity last year, I would have sketched a picture of an economy that was struggling to come to terms with the impact of a global recession. Output and employment were declining and were expected to fall further. Even as incomes were falling, inflation was being driven by new tax measures as the Government tried desperately to keep up with the heavy burden of debt payments. The only bright spot that I would have relied on to motivate you would have been the potential benefits of a radical debt initiative that was still in the design stage and the likelihood of strong international support if Jamaica could commit to a new path of fiscal and debt sustainability.

I'm glad to be able to join you at the start of 2011 because this time the outlook is different. I hope that you will fully understand what I mean in a few minutes.

As advisors all, you would know that a large part of the value that you bring to your clients consists of an informed view of the kind of changes that we can expect in our economic environment – what will happen to inflation, incomes, the exchange rate, interest rates, taxation and so on. All financial plans depend on these inputs. In designing or choosing financial products for your clients, you seek to protect them from some of the risks to which they are exposed and, where applicable, you find a way for them to share in the proceeds of activities that are profitable and expanding.

I claim, as a kind of financial advisor myself, that inflation is the single most important variable affecting your future, the value of your products, the perceived value of your services and your own financial plans. Inflation is the continuous, inexorable and sometimes rapid increase in the prices of the things we need to enjoy a decent life or even merely to survive day by day. It eats away at our savings and makes nonsense of long-term financial plans. And it has a direct link to those other variables that planners contend with such as growth, interest rates and the exchange rate.

I don't have to tell you this. This is the shared experience of everybody in modern day Jamaica. No doubt you hear it from your clients every day. Let me put it another way: a policy with a face value of $100,000 purchased by a young graduate 40 years ago is worth considerably less than 1,000 of those same dollars at his retirement. In actual fact, the value of 100,000 of today's dollars in terms of 1971 dollars is $177.22.

So, where is the other $99,000 or so of purchasing power? Where has it gone?

On the face of it, nowhere. The underwriter will still faithfully pay over the face amount or cash surrender value which could still be nominally $100,000. But the expectation that this lump sum could have bought a house or provided an adequate source of investment income well into retirement is worse than a broken promise. Time and inflation changed the price of everything except his savings.

As it turned out, from the day the policy or contract was signed, the value of the Jamaica Dollar has been steadily falling. A dollar buys less each day. Sometimes the impetus has come from some unexpected shortage of goods which causes the supplier to hike prices. The ability to sustain demand at these higher prices has been helped by the bargaining power of workers who claim higher wages and salaries to compensate for the increased cost of living. Property owners charge higher rent, owners of capital charge higher interest and demand higher profits and earners of foreign exchange hold out for higher exchange rates. The Government too plays a role. It borrows more to pay higher wages and distribute more financial support and if, instead, the Government were to resort to borrowing from the Central Bank, it would be simply printing more money to fund its activities thus adding fuel to the inflation fire. At the end of the day, those without the ability to adjust their incomes to match inflation – such as pensioners, workers on fixed income and those with little income or property – become progressively poorer and their savings worth less and less. Thus a princely $100,000 policy in 1971 eventually becomes little more than a funeral grant today.

When will this erosion of value stop? It will not stop entirely. Everywhere in the world prices change as the relative value of goods and services change and as basic exhaustible resources become scarcer. But, as happens in the developed world and increasingly in emerging market economies, it is possible to conduct our affairs so that inflation is hardly a factor in our long-term plans. The formula is simple enough although very challenging to put into practice.

First, we need to stabilise public finances. We need to stop the process that demands that we keep borrowing just to keep servicing past borrowing. We need to leave people with as much money in their pockets as possible and cease paying more employees than necessary to produce fewer and fewer goods and services. That process has begun in the public sector and an encouraging degree of progress was made in 2010. The Jamaica Voluntary Debt Exchange (JDX) provided a jump start by reducing annual debt serving costs by over $40 billion and has relieved cash flow requirements by extending the maturity of Government securities. The grace period that this has provided is allowing time for the implementation of a series of reforms - from divestment, expenditure management and tax administration to overall resizing of government – that will see the Government's borrowing requirement eliminated in three years. It is a strong commitment to stakeholders, local and foreign, who are monitoring progress carefully.

The fiscal consolidation and financial discipline represented by these reforms is a key component of a stable low-inflation environment.

Second, the Central Bank has a key role to play. Many low-inflation countries have modified their governance arrangements such that the Central Bank takes ‘independent’, or non – political, responsibility for achieving the inflation target that the country sees as desirable. The Bank is then left to make the necessary periodic adjustments to its monetary policies so as to achieve this objective and reports to the country through Parliament at regular intervals. It has worked well elsewhere and is being advocated by strong voices in the local private sector. We at the Bank endorse this direction and have already begun to rearrange our internal operations to meet this new expectation. By March 2011, we expect the 12-month inflation rate to fall to about 8 per cent, well within the target range announced for the fiscal year. We at the Bank of Jamaica will do what is required of us to see that rate fall further and remain at a stable single-digit rate for the foreseeable future.

But much depends on what the public views as an acceptable rate of inflation. Jamaica has experienced an average annual rate of inflation of about 15% over the past 50 years. Our main trading partner, the USA, has averaged about 4% over the same period. We need, as consumers, parents, financial planners and advisors to make our voices heard and help to forge a consensus on how much inflation is too much and oblige our public administrators to operate within our expectations. If some find an easy inflation hedge at the expense of those on fixed contracts, we all lose in the end because the injustice of it will become intolerable to those at the losing end of events.

The burden of fostering a low inflation environment rests not only on the Government. As you blast off into your own spheres of endeavour – as you ramp up your productivity and do more in a day using less fuel and less paper – you help to keep costs from continuously rising. Productivity improvements are the single most effective way to grow income while keeping prices stable. It thus becomes a business objective, a managerial guidepost and a personal resolution. At the end of the day, your actions, your voices and your advice will be invaluable inputs into the mix that keeps Government and central bankers true to their promise and you true to your clients.

Plan for success this year and rest assured that we will do our part to maintain the integrity of those plans.

Thank you.