BANK OF JAMAICA

News Release

Quarterly Press Briefing
Hon. Derick Latibeaudiere, Governor, Bank of Jamaica
15 August 2007

Good Morning Ladies and Gentlemen:

First, let me welcome you to our third quarterly briefing for 2007. I will start the discussion by focusing on inflation.

Inflation

Inflation for the June 2007 quarter was 1.9 per cent. This was slightly below the range that I outlined in my last presentation. It was also much lower than the seasonal average of 3.3 per cent for the past five years. This fall was largely due to unexpected buoyancy in domestic agricultural supplies, which caused the prices of starchy foods to decline. The inflation out-turn for the quarter brought the annual measure of inflation at June to 5.6 per cent, the lowest since November 2006.

Ladies and Gentlemen, it is also important to note that underlying inflation for the quarter was 1.0 per cent. This was in line with the Bank's expectation, and suggests that annual core inflation is moderating. Other measures that exclude the impact of agricultural and fuel prices also support the view that underlying inflation is moderating. In Box 1 of the Quarterly Report, we have provided a brief discussion of the reasons these other measures are now being reported, and we welcome your feedback on the issues raised in the Box.

For the September quarter, headline inflation is projected in the range of 2.0 -3.0 per cent. This is above the outturn for the June quarter but below the 5-year seasonal average. The Bank expects that seasonal declines in agricultural supplies over the quarter should exert upward pressure on food prices. In addition, recent developments in the international market for oil suggest that energy-related prices in Jamaica are likely to be adversely affected. Finally, exchange rate movements over the previous 2 quarters, as well as the movements in this quarter to date, suggest a slight upward impact on domestic prices.

The Bank's forecast of inflation for the full fiscal year, however, remains largely unchanged. Inflation in the 6-7% range for FY 2007/08 is conditioned on continued fiscal restraint as well as the normal evolution of the global economy.

We believe that the main near term risks to the inflation outlook remain the impact of adverse weather conditions and developments in the international market for oil. Another possible risk may emanate from the domestic foreign currency market, which has been experiencing some pressures as a result of reductions in foreign currency inflows and increased Jamaica Dollar liquidity.

Foreign Exchange Market

This leads me to recent developments in the foreign exchange market. While exchange rate movements over the June quarter were relatively moderate, the market experienced intermittent bouts of instability, particularly in June. For the quarter, the exchange rate depreciated by 1.1 per cent, slightly above the 0.96 per cent depreciation in the March 2007 quarter. For the calendar year to June, however, the value of the Jamaica Dollar declined by 2.1 per cent against the US dollar, which was below the 2.2 per cent depreciation for the comparable period of 2006.

Ladies and Gentlemen, the movement of the Jamaica Dollar against the US dollar, when taken in the broader context of the movement of the major currencies against each other, is relatively small. You would be aware that the US dollar depreciated against the Canadian dollar by 9.6 per cent between January and June 2007. The dollar also lost between 2.4 percent and 2.5 per cent of its value against the Euro and the British pound over the same period. The 2.1 per cent change in the value of the Jamaican currency would rank as relatively stable when compared with the movement of the US dollar against other major currencies.

Returning to conditions in the domestic foreign exchange market, the Bank's view is that the intermittent pressures that emerged during the review quarter were mainly associated with a contraction in net private capital inflows. The fall in net private capital inflows largely reflected portfolio switching by investors in the context of a narrowing in the interest rate differential between Jamaica Dollar bonds and US dollar denominated bonds. External financing activities by a public sector company in June, as well as increased demand from selected private sector entities to facilitate dividend payments, also acted as triggers for increased instability in the market over the quarter.

To moderate the pressures in the foreign exchange market during the quarter, the Bank sold foreign currency and offered a special variable rate Jamaica Dollar instrument in June. These actions served to reduce the excess Jamaica Dollar liquidity which was evident for some institutions. The variable rate instrument also had the welcome effect of prompting additional US dollar sales to the Bank by the market.

In the context of these developments, the NIR declined by US$90.5 million during the quarter to US$2.24 billion at end-June 2007. However, gross foreign exchange reserves remain adequate by conventional measures. At end-June 2007, these reserves represented approximately 17.8 weeks of projected goods and services imports.

For the September 2007 quarter, the Bank expects that periodic gaps will emerge in the foreign exchange market. This is in the context of continued reversals in interest rate spreads on emerging market bonds, and domestic liquidity conditions that can facilitate speculative forces, even as the central government moves to align its debt strategy with best practices. The Bank for its part remains committed to maintaining stability in the foreign exchange market and to ensure that broad monetary conditions are consistent with low, stable core inflation.

Real Sector Developments

Let me now turn to the issue of growth in the Jamaican economy. The Bank's estimate of Gross Domestic Product (GDP) for the June 2007 quarter indicated growth in the range of 1.5 per cent to 2.0 per cent. Most sectors in the economy are estimated to have grown, with the exception of mining and miscellaneous services, which includes tourism.

Importantly, some of this expansion in the economy is related to ongoing recovery of the construction and manufacturing sectors and upgrading of facilities at the both sea and airports.

Looking forward, output in the September 2007 quarter is projected to expand at a faster pace than in the June 2007 quarter, but perhaps slower than the expansion recorded in the September 2006 quarter. The Mining & Quarrying and the Construction & Installation sectors should lead this growth. Other sectors expected to contribute to the economy's expansion include the Distributive Trade, Miscellaneous Services, Electricity & Water and Agriculture, Forestry & Fishing.

In summary, on the macroeconomic front, the main challenge that the Bank is expected to face in ensuing quarters is the impact of the recent narrowing in interest rate differentials on net private capital flows. The path of oil prices also poses some concern. However, the Bank remains committed to ensuring price and exchange rate stability to underpin the country's goals of further growth and development.

Thank you