BANK OF JAMAICA

Monetary Policy Press Statement:
QMPR Press Conference

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19 August 2021

Introduction

Good morning, ladies and gentlemen and welcome to our Quarterly Monetary Policy Report press conference. I wish to begin by highlighting two major developments which serve as backdrop for the monetary policy decisions that the Bank published yesterday.

Firstly, the COVID-19 pandemic continues to be a major challenge for economic activity, both here in Jamaica and across the globe. In recent weeks we have witnessed an uncomfortable rise in cases, signalling the emergence of a third wave. Our economy will remain vulnerable to this pandemic until a significant proportion of the population has been vaccinated and the spread of the virus becomes contained. I wish to add my voice to those encouraging all to get vaccinated.

Secondly, since the start of 2021, we have been observing significant and rapid increases in the prices of some international commodities and services such as fuel, wheat, corn, soy, steel, lumber and shipping. These increases have been largely due to the impact of disruptions to global supply chains as well as increasing global demand as economies re-open from lockdowns associated with the pandemic. Although the prices of some commodities have started to fall from their peaks, we have begun to see increases in domestic transport-related costs, higher prices for processed foods and higher utility costs.

Given these developments, the Bank is now signalling that, while we have observed improvements within the Jamaican economy, including rising employment levels, buoyant inflows into the foreign exchange market and strong reserves, inflation is likely to breach the upper bound of the target range from as early as the September 2021 quarter. This experience of above-target inflation is similar to that of other central banks. Inflation in the US, for example, was 5.4 per cent at July 2021, more than twice its inflation target.

With this background, I will now speak in further detail to the Bank's latest monetary policy decisions.

Monetary Policy Decisions

The MPC met on Tuesday and Wednesday of this week and decided to maintain the policy rate at 0.50 per cent. However, consistent with meeting its inflation target sustainably in the medium term and, subject to inflation evolving as projected, the Committee also agreed to consider increasing the Bank's policy rate at its next meeting in September 2021. The Committee further decided to implement other measures aimed at moderating inflation expectations, including the containment of Jamaican dollar liquidity expansion. Finally, the Committee reiterated that, while the Bank does not target any specific level of the exchange rate, Bank of Jamaica will seek to ensure that movements in the exchange rate do not further threaten the inflation target.

The MPC's assessment is that inflation over the next 9 to 12 months will be higher than previously expected, breaching the upper bound of the Bank's target range from as early as the September 2021 quarter. The breaches are not, however, expected to persist beyond a year. In the context of this forecast, the MPC's decisions, including those to be taken in September, are designed to ensure that inflation will gradually fall back within the Bank's inflation target of 4.0 to 6.0 per cent in the shortest possible time.

Inflation

The inflation rate for the 12 months leading up to July 2021, as released on Monday by the Statistical Institute of Jamaica, was 5.3 per cent, within the Bank's inflation target but above the 4.3 per cent recorded for the previous month. This outturn largely reflected the impact of increased energy related costs as well as higher prices for processed foods. When compared with the 5.7 percent recorded at July 2020 however, the annual inflation rate at July 2021 was lower, a result of lower inflation for agricultural products.

Up to July 2021, the Bank continued to be successful in guiding inflation within the 4 to 6 per cent target range. Over the 36 months leading up to July, inflation has been below 6.0 per cent (which is the upper bound of the target range) on 34 occasions, or 94 per cent of the time. On the flip side, inflation fell below the lower end of the target over the period on 11 occasions.

Going forward, without further monetary policy action, the MPC anticipates that annualized consumer price inflation will evolve in the range of 6.0 to 7.0 per cent over the September 2021 quarter to the June 2022 quarter. Following the possible breaches of the upper limit of the Bank's target range over this period, inflation will gradually decelerate as the transitory effects of the pandemic fade.

The inflation forecast reflects the lagged impact of higher international commodity and shipping prices, a recovery in domestic demand and a temporary increase in inflation expectations. This outlook also contemplates the effects of one-off adjustments in selected regulated prices as well as further increases in house rental rates. In addition, headline inflation is projected to be affected by the lagged impact of energy prices. While international commodity and shipping prices are expected to remain elevated in the short term, they are projected to fall as demand/supply imbalances in the global economy continue to improve.

This outlook for inflation over the next two years is higher than the one shared with you in May 2021, a change that is primarily related to the MPC's updated view on the impact of the factors that I just described. The MPC believes that, for inflation to remain at 5.0 per cent over the medium term, there will be the need for the Bank to raise interest rates.

While there is some uncertainty surrounding the inflation forecast, especially given the emergence of new variants of the Corona virus, the near-term risks to this forecast are skewed to the upside. The upside risks, which could cause inflation to be higher, include higher than anticipated inflation expectations stemming from the shock to international commodity prices, as well as the impact of an adverse hurricane season on the supply of agricultural foods and prices. Already, we have witnessed the passage of Tropical Storm Grace and we will be assessing its impact on inflation, if any, over the coming weeks. On the downside, demand conditions could be weaker than anticipated because of lower global growth and tighter stringency measures, while there could a stronger than expected fall in commodity prices, all stemming from the emergence of the delta variant of the Corona virus. The prices for a number of commodities, including grains and oil, have already fallen from their recent peak levels.

Outlook for the Jamaican Economy

The most recent real GDP data published by STATIN indicated that domestic economic activity contracted by 6.7 per cent for the March 2021 quarter, compared with the contraction of 8.3 percent in the December 2020 quarter. This outturn represents another in a series of improvements, relative to the previous quarter.

The labour market also continues on a path of improvement. The latest data released by STATIN indicated an unemployment rate of 9.0 per cent at April 2021, down by 3.6 percentage points compared to the rate at July 2020, when the economy was experiencing the early stages of the pandemic. The decline in the unemployment rate reflected a reduction of 42 300 in the number of unemployed persons as well as a growth of 42 100 in the labour force.

Ladies and gentlemen, real GDP growth for FY2021/22 is now likely to be higher than we earlier anticipated, given the impact of stronger than expected improvements in the economies of Jamaica's main trading partners. The Bank is currently projecting that real GDP growth for this fiscal year will be in the range of 7 to 10 per cent, up from the 5 to 8 per cent we had indicated in May 2021. Leading indicators such as GCT flows and electricity consumption point to this rebound. The key drivers of this rebound are the tourism and related sectors, driven in large part by successful vaccination programmes in key source markets and our assumption of careful control of community spread in Jamaica. The Bank also anticipates continued strong growth in the construction sector.

The risks to this growth forecast are balanced. A faster pace of growth is possible if tourist arrivals and related activities rebound faster due to the pent-up demand that exists. The main downside risks to this growth projection relate to the domestic spread of the COVID-19 virus, the emergence of new variants of the COVID-19 virus and the accompanying measures to control it. If Jamaica's stringency measures are tightened and protracted, this could influence a slowdown in travel and disruptions in the production and distribution of goods.

Developments in the Financial Sector

Turning briefly to the financial sector, deposit-taking institutions' (DTIs) balance sheets continue to indicate that they are growing, properly capitalized and in compliance with prudent liquidity standards. Although the pace of loan growth has slowed due to the moderating impact of the pandemic, it continues to be positive. The stock of private sector loans and advances recorded year-on-year growth of 8.4 per cent at May 2021, compared to growth of 13.4 per cent a year earlier. At the same time, non-performing loans remain well below our threshold for concern and are fully provided for by the system.

Developments in the Foreign Exchange Market

In relation to the foreign exchange market, notwithstanding recent movements in the exchange rate, the pace of depreciation is better than we experienced last year. At 16 August 2021, the exchange rate was J$155.08 to US$1, representing a depreciation of 8.7 per cent for the calendar year to date. While this movement is still too high for comfort, it compares favourably with the 12.0 per cent depreciation that occurred over the same period of last year.

Even in this period of economic uncertainty, foreign currency flows have remained strong and business or individuals in Jamaica who require foreign exchange have been able to access it. For the calendar year to 16 August 2021, daily purchases of US dollars by authorised dealers and cambios averaged US$36.2 million, higher than the average of US$29.9 million recorded over the same period last year. At the same time, daily sales to end users excluding sales to BOJ averaged US$33.2 million since the start of 2021, above the average of US$26.6 million a year earlier.

For the calendar year to 16 August, the Bank has purchased US$1.1 billion from the market via market surrenders, which pays GOJ debt servicing and facilitates some energy imports. The Bank has also continued to intervene in the market when temporary shortfalls have been identified. Total B-FXITT flash sale operations and direct sales to the energy sector for the calendar year to 16 August has amounted to US$484.0 million. At 16 August 2021, Jamaica's gross international reserves remain healthy, amounting to US$4.2 billion (the equivalent of 128% of the level considered adequate).

Looking forward over the next two years, the Bank projects that the current account deficit of the balance of payments will remain at sustainable levels of about 2 – 4 per cent of GDP. This reflects the earlier mentioned expectations for a recovery in tourist arrivals and spending. While supported by the favourable outlook for the current account, our outlook for the gross reserves also anticipates the receipt of an IMF allocation of SDRs by end-September 2021. This allocation will boost the reserves by the equivalent of US$520 million (approximately). By any standard, Jamaica's foreign currency liquidity position will be more than sufficient to support the economy, if needed, in the foreseeable future.

Concluding Statement

Ladies and gentlemen, the macroeconomic outlook points to an even stronger improvement in real economic activity, relative to our previous assessment.

The outlook for inflation over the next year is, however, affected by the recent shock to international commodity prices. The ongoing COVID-19 pandemic continues to cast a cloud of uncertainty, notwithstanding global optimism about the deployment of vaccinations programmes.

In determining the stance of monetary policy, Bank of Jamaica will continue to closely monitor developments in the economy, particularly relating to inflation expectations, labour market conditions and the prices for international commodities and shipping costs. The Bank, through its Monetary Policy Committee, remains committed to ensuring that inflation remains low, stable and predictable, within the target range of 4.0 to 6.0 per cent and will consider increasing interest rates at its next meeting in September.

Thank you.