BANK OF JAMAICA

MINUTES OF THE

MONETARY POLICY COMMITTEE MEETINGS

HELD VIRTUALLY

ON

TUESDAY, 28 SEPTEMBER 2021 AND WEDNESDAY, 29 SEPTEMBER 2021

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Minutes of the Monetary Policy Committee ("MPC/the Committee") meetings held virtually on Tuesday, 28 September 2021 (Briefing Meeting) at 9:00 a.m. and continued on Wednesday, 29 September 2021 (Decision/Communication Meeting), at 10:00 a.m. via GoToMeeting.

Attendance

The following members of the Committee were present:

Mr. Richard Byles	Chairman
Dr. Wayne Robinson	Senior Deputy Governor
Mr. Robert Stennett	Deputy Governor
Dr. Nadine McCloud	Appointed Member, MPC
Mr. David Marston	Appointed Member, MPC

Other attendees:

Ms. Carey-Anne Williams	Division Chief, REPD[1]
Mrs. Sharon Miller-Betty	Deputy Division Chief, REPD
Mrs. Natalie Haynes	Deputy Governor[2]
Mr. Taffi Bryson	Director, Market Operations and Analysis Department[3]
Ms. Tanisha Ennis	Executive Coordinator, Governor's Office
Ms. Arlene Tomlinson	Senior Director, Board/Management Secretariat
Mrs. Karelle Tyrell[4]	Head, Monetary Policy Communication Unit, REPD
Ms. Shannon Spencer	Monetary Policy Committee Secretary

1.0 Call to Order and Apologies

1.1 On 28 September 2021, the Chairman called the meeting to order and welcomed all to the fourth meeting of the MPC. There were no apologies for absence.

[1] The Bank's Research and Economic Programming Division.
[2] In attendance at the meeting on 28 September 2021 only.
[3] In attendance at the meeting on 28 September 2021 only.
[4] In attendance at the meeting on 29 September 2021 only.

2.0 Confirmation of the Minutes of the Previous Meeting

2.1 The minutes of the meeting held on 08 September 2021 to review and approve the minutes of meetings held on 17 and 18 August 2021 were confirmed by Mr. David Marston and seconded by Dr. Nadine McCloud.

3.0 Matters Arising

3.1 The investigation into the increase in rental prices & drivers of growth in the construction sector

3.1.1 At the meeting of May 2021, the Committee had requested an investigation into the rental housing market in the context of a notable increase in housing rental prices in March 2021. The MPC had also enquired about the main factors supporting the notable growth in the construction sector.

3.1.2 Ms. Carey-Anne Williams reported that there was a delay in the finalisation of a Memorandum of Understanding (MOU) between the Bank of Jamaica ("BOJ/the Bank") and key stakeholders. As a result, the updates would be provided to the MPC as soon as the MOU was signed and the data procured and assessed.

3.2 Presentation on Jamaica's Medium Term Potential Output

3.2.1 Mr. Robert Stennett presented a recent paper published by the Bank on Jamaica's medium term potential output. The objective of the presentation was to identify the factors that underlined the Bank's medium term projection for real GDP growth. The paper utilised a production function to examine the level and rate of change in Jamaica's potential GDP (a measure of Jamaica's maximum level of sustainable output or the level of GDP consistent with a stable inflation rate) over the medium term. The paper estimated and projected the potential factor inputs (total factor productivity (TFP), human capital, labour supply and capital stock).

3.2.2 The presentation showed that human capital (proxied by the average number of years of schooling provided to the average school child) had improved steadily from 8.5 years in 2000 to 9.75 years in 2020. Based on the trend, the analysis projected that years of schooling would continue to improve marginally over the medium term. However, the years of schooling was low compared to other developed economies, which implied that more policy initiatives might be needed to drive a substantial increase in Jamaica's human capital. The analysis abstracted from the impact of the uneven access by segments of the school population to online education (the so-called 'scarring effects' of the Covid-19 pandemic). The Bank would also be assessing the implications for potential output growth of the recently announced Government of Jamaica (GOJ) Sixth Form

Pathway Programme, which increases the minimum number of years in school for all secondary school students from five to seven.

3.2.3 Since the global financial crisis in 2008, Jamaica's capital stock has been on a downward trajectory, a trend exacerbated by the adverse impact of the COVID-19 pandemic on investment flows into the economy. Notwithstanding the assumption of reasonably strong growth in investments in the future, the potential capital stock over the forecast period (2021-2025) was projected to continue declining, given that the investment flows were insufficient to exceed the assumed rate of depreciation in the stock.

3.2.4 The projection for potential labour supply was constrained by the assumption that the working-age population would remain constant over the projection horizon. Still, this impact was projected to be partly offset by a recovery in the labour force participation rate. The projection for the working-age population was informed by STATIN's population projection which, among others, envisaged a reduction in the female fertility rate. For the labour force participation rate, the Bank anticipated that this would normalise to approximately 65.0 per cent following the COVID-19 shock. In the context of a projected recovery in economic activity and employment following the Covid-19 pandemic, the unemployment gap (the difference between the non-accelerating inflation rate of unemployment (NAIRU) and actual unemployment) was projected to close by about mid-2023. The Bank estimated the long-run NAIRU to be 5.8 per cent. Finally, the average number of hours worked per employee in Jamaica had been relatively constant before the onset of the Covid-19 pandemic but fell by 8.0 per cent during the pandemic. This shock reflected the impact of restrictions on movement over the period as workers generally worked fewer hours. Over the forecast horizon, the Bank's projection assumed that the average working hours per person would normalise and remain stable at the legislated 40 hours work-week.

3.2.5 Potential total factor productivity (TFP) was estimated to be constant before the pandemic but fell during the pandemic due, perhaps, to some workers' inability to transition to remote work arrangements. However, for the forecast, the Bank assumed that potential TFP would grow at an average rate of 0.5 per cent per quarter over the next five years. This view reflected the expected impact on TFP of the government's ongoing reform programme, particularly the current push to accelerate the digitization of some activities.

3.2.6 Given the factor inputs' projections, potential output was forecasted to recover in 2021 and grow at an average annual rate of 1.7 per cent over the medium term.

However, the average growth in potential GDP reflected the effect of the recovery in 2021 and 2022 and, abstracting from these years, the average medium-term growth was lower than 1.7 per cent.

3.2.7 The presentation pointed to the need for an aggressive programme to encourage investments into the economy to lift the prospects for medium-term growth.

4.0 Monetary Policy Matters

4.1 Risk Assessment for Macroeconomic Projections and Monetary Policy Recommendations

4.1.1 The Bank staff's assessment of risks to the August 2021 macroeconomic projections and monetary policy recommendations were presented by Mrs. Miller-Betty. The assessment recounted the forecasts provided in August 2021, presented recent developments and highlighted the risks to the forecasts, particularly for inflation.

4.1.2 At the assessment in August 2021, the Bank's staff had reported to the MPC that inflation would breach the upper limit of the Bank's target range over the forecast horizon. Inflation was projected to average 5 ½ to 6 ½ per cent over the next two years. This inflation outlook was underpinned by (i) the lagged impact of increases in international commodity (i.e. grains and energy) and shipping prices; (ii) upward adjustments in selected regulated prices; (iii) a recovery in domestic demand; (iv) relatively stable inflation expectations and (v) annual declines in agricultural food price inflation. Over the medium term, the Bank had projected that, conditional on the gradual tightening of monetary policy, inflation would trend towards the mid-point of the target range.

4.1.3 Commodity prices (WTI crude oil and average grains prices) were projected to remain elevated but were expected to commence declining by the end of the September 2021 quarter in the context of a more balanced oil market as OPEC and non-OPEC producers eased supply restrictions. Similarly, grains prices (soybean, wheat, corn) were projected to fall by 1.1 per cent over the next two years due to a rebound in global supplies, partly offset by the impact of adverse weather conditions in Brazil.

4.1.4 Based on recent developments, the inflation forecast was likely to be revised upwards. Inflation at August 2021 was 6.1 per cent, which was higher than the Bank's forecast and above the upper end of the target range of 4.0 per cent to 6.0 per cent. The deviation from the forecast reflected the impact of adverse weather conditions on agricultural commodity prices. Also, the increases in the prices for several items in the CPI basket suggested that the lagged impact of the

rise in commodity prices was higher than expected. In this context, core inflation at August 2021 was 7.8 per cent, which was higher than the 3.4 per cent recorded at August 2020. The higher than expected level of inflation was projected to take a year to dissipate and, by then, would worsen inflation expectations. In particular, one-year-ahead inflation expectations, measured by a survey of Jamaican businesses in July 2021, deteriorated to 7.4 per cent, compared to 7.0 per cent at June 2021. The JMD GOJ yield curve also signalled that inflation expectations in the September 2021 quarter was rising, which was inconsistent with the assumption of the normalising of expectations that underpinned the August 2021 inflation forecast.

4.1.5 The recent trends in energy prices (oil and LNG) relative to the Bank's forecast suggested net upside risks to the inflation projection. LNG prices were above forecast, while WTI crude oil prices were below projection. The variance in WTI crude oil prices reflected the weak outlook for global fuel demand and an appreciation of the US dollar. In this regard, the projection for crude oil prices may be revised downwards. On the other hand, the variance in LNG prices reflected expectations of contractions in global supply and higher natural gas consumption in the context of colder winter temperatures in 2021. In this regard, the projection for LNG prices may be revised upwards. Freight prices also continued to rise, suggesting an upside risk to the Bank's inflation forecast.

4.1.6 The recent performance of grains prices, relative to the Bank's forecast, suggested downside risks to the inflation projection. Average grains prices tracked below forecast due to better than anticipated weather conditions and an appreciation in the US dollar. Over the next two years, corn and soybean prices were likely to be lower than the forecast due to larger than expected increases in global supplies and slower demand growth in China. Wheat prices were likely to trend below the previous projection due to a rebound in European wheat production.

4.1.7 The Bank had projected a recovery in domestic economic activity in the range of 7.0 per cent to 10.0 per cent for fiscal year (FY) 2021/22. Growth was projected to moderate within the range of 2.0 per cent to 4.0 per cent for FY2022/23. This outlook was primarily driven by the performance of selected industries (Tourism and related sectors, and Construction) over the next year and the lagged impact of accommodative monetary policy conditions.

4.1.8 The projection for real GDP growth for FY2021/22 was likely to be revised downwards due to a deterioration in the outlook for Agriculture, Forestry & Fishing, Mining & Quarry. In particular, the risk to the projection for the Mining sector

reflected the impact of a fire on operations at the Jamalco alumina plant. For FY2022/23, growth in real GDP was likely to be revised slightly upwards, relative to the August 2021 projection. The global growth outlook, which supports the projections for the growth in domestic GDP, was also likely to be revised downwards amid rising COVID-19 cases, the spread of the Delta variant and uneven vaccination rates.

4.1.9 Inflation among Jamaica's main trading partners (TP Inflation) as of July 2021 was slightly above the Bank's projection due to supply shortages and demand pressures related to the re-opening of economies. TP inflation was likely to remain in line with the Bank's projection over the next two years.

4.1.10 The Bank had projected that the current account deficit (CAD) of the balance of payments would average 2.0 per cent of GDP for FY2021/22 to FY2022/23, which reflected a deterioration compared to the outturn of 1.1 per cent of GDP for FY2020/21. This projection was mainly driven by higher commodity prices and higher import volumes in the context of the recovery in the domestic economy. For FY2021/22, a CAD of 2.2 per cent of GDP was projected. It was not likely that the projected current account would change.

4.1.11 The Bank's gross international reserves (GIR) were projected to improve in FY2021/22 due to the impact of the International Monetary Fund's (IMF) Special Drawing Rights (SDR) allocation in August 2021. The GIR was projected to remain adequate relative to the benchmark "Assessing Reserve Adequacy" (ARA) metric. The risks to the GIR were skewed to the upside, given the buoyancy in foreign exchange inflows in August 2021.

4.1.12 In response to the MPC's signal of an imminent tightening of monetary policy, all private money market rates and most GOJ Treasury Bill (T-bills) rates increased for the quarter, relative to end-June 2021. However, short-term interest rates generally remained within the Bank of Jamaica's policy corridor over the September 2021 quarter.

4.1.13 Given the foregoing assessment, the Bank's staff recommended that the Bank of Jamaica reduce its level of monetary policy accommodation via a suite of measures. The staff recommended that the Bank increase the policy rate, continue measures to contain Jamaican dollar liquidity expansion and ensure that movements in the exchange rate do not threaten the inflation target. Finally, consistent with meeting its inflation target sustainably in the medium term, the staff

recommended that the Committee signal that it was prepared to continue to guide negative real interest rates to more sustainable levels at subsequent policy meetings, subject to inflation and other macroeconomic data evolving as projected.

4.1.14 The presentation concluded with an assessment of the macroeconomic impact of raising nominal interest rates progressively over time. The assessment included the impact of the proposed policy measure on real GDP growth, the exchange rate and inflation.

4.2 Financial Market Update and Short-Term Outlook

4.2.1 Mr. Taffi Bryson presented on recent developments in the financial markets and provided a short-term outlook. Recent open market operations (OMOs) were aimed at tightening liquidity, consistent with the Bank's monetary policy stance. This absorption of liquidity followed the Bank's provision of liquidity between March 2020 and December 2020 in response to the impact of the COVID-19 virus on financial markets.

4.2.2 Liquidity management by the Bank seeks to ensure that orderly conditions are maintained in both the money and foreign exchange (FX) markets. The Bank typically utilises its weekly 30-day FR CD operations (but deploys other instruments such as US dollar Indexed Bonds and longer tenor FR CDs) to absorb Jamaican dollar liquidity.

4.2.3 Liquidity, as measured by current account balances held at the Bank by commercial banks and primary dealers (PDs), averaged J$73.9 billion over the calendar year to August 2021. The primary source of this liquidity was the Bank's purchase of USD from the market via the surrender window, partly offset by net absorption through the government of Jamaica operations.

4.2.4 Liquidity was, however, concentrated in the banking system. This concentration represents a constraint on the efficiency of the monetary transmission mechanism.

4.2.5 As reported earlier, short term interest rates remained within the Bank's interest rate corridor for the review period. Between January 2021 and July 2021, rates on GOJ T-bills and BOJ 30-day FR CDs trended downwards, which suggested that liquidity was more than adequate over this period, particularly in the context of the ongoing scarcity of liquid financial instruments. An uptick in money market rates in August 2021 reflected the combined impact of relatively attractive capital market

investment opportunities, the change in the Bank's policy posture towards liquidity management, and the Bank's forward guidance on interest rates.

4.2.6 Of the GOJ bond issues over the first half of 2021, primary dealers and commercial banks preferred shorter tenors, while insurance companies preferred longer tenors. There was a general increase in the weighted average yields on the issues over time.

4.2.7 As measured by indicative bids and offers, the yields at the long end of the yield curve increased marginally between June 2021 and August 2021, while those on the short end of the curve remained reasonably stable. The upward movement in yields was particularly evident in the indicative yields for the 2031 (10 years) and the 2037 (16 years) instruments. This steepening of the yield curve supported the view that investors expected higher inflation in the medium term. The MPC expressed the view that given the shallowness of the Jamaican financial market, this measure of inflation expectations, while indicative has limitations.

4.2.8 Concerning the foreign exchange market, the exchange rate continued to exhibit two-way movement. For the calendar year to August 2021, the weighted average selling rate (WASR) depreciated by 6.2 per cent (J$9.44) and reflected an average monthly depreciation of 0.7 per cent. The depreciation mainly reflected seasonal demand pressures in January, April and July 2021. In general, episodes of appreciation in the WASR corresponded with increased short positions of the DTIs while episodes of depreciation corresponded with increased long positions. To maintain order in the FX market, the Bank injected US dollar liquidity amounting to US$198.8 million via the intervention window during the review period.

4.2.9 In terms of the near-term outlook, the Bank expects the money market to reflect continued efforts by some institutions to position for Jamaican dollar investment obligations and opportunities. An uptick in Jamaican dollar liquidity was expected in October 2021, associated with the maturity of a BOJ US dollar Indexed note (amounting to J$25 billion) and higher seasonal FX purchases through the Bank's surrender arrangements. The impact of these liquidity injections was projected to be partially offset by a seasonal increase in the currency issued towards the end of the quarter. BOJ would also be actively absorbing Jamaican dollar liquidity through the utilisation of longer tenor instruments.

4.3 Discussion

4.3.1 The Committee expressed concern about the structural issues that existed in the JMD money and FX markets and the potential constraints that these issues placed

on the effectiveness of the monetary policy transmission mechanism and BOJ's ability to manage inflation effectively. To better understand these structural issues, the Committee requested that the Bank's staff conduct a study and report the results at a future MPC meeting.

4.3.2 It was also noted that the recommended policy adjustment involved a package of measures in the money and the FX market, which, taken together, were expected to have a significant impact on inflation expectations.

4.3.3 The Committee queried, in a context where most of the projected inflationary pressures in Jamaica stemmed from external price pressures (i.e. the pass-through of international commodity prices and shipping prices) whether the recommendation to raise the policy rate was appropriate at this point in time. This query was also against the backdrop of a weak domestic economy. It was noted that, even though the initial impact of international commodity prices could be temporary, higher inflation expectations could result in higher than previously anticipated inflation outcomes. In addition, the recent significant increase in core inflation suggested that the effects of these shocks would persist. The Committee discussed that it was important for the Bank to take a proactive approach to manage the risks of higher than expected inflation to safeguard and secure sustainable long-term growth. The MPC acknowledged that these policy actions would result in a trade-off between short term growth and more sustainable growth in the medium term. Additionally, the Committee noted that, although the economy was below pre-pandemic levels, there was much optimism that economic activity would normalise quickly over the ensuing quarters.

4.3.4 The Committee enquired whether supplementary approaches existed to measure inflation expectations, compared with the survey data and the information in the yield curve. The view was that, since heightened inflation expectations were highlighted as a significant risk to inflation, more focus should be placed on identifying other measures of inflation expectations. It was noted that this question would be continually kept under consideration but that there were currently no other feasible data sources.

4.3.5 Following the discussions, the meeting ended on 28 September 2021 at 11:55 a.m.

THE COMMITTEE RECONVENED ON 29 September 2021 AT 10:00 a.m.:

5.0 Monetary Policy Decision

5.1 On 29 September 2021, the Committee accepted and adopted the assessment of risks presented by Bank staff.

5.2 Based on the discussions on 28 and 29 September 2021, the Chairman invited the Committee to vote on the proposed package of measures:

(i) increase the policy interest rate by 100 bps to 1.50 per cent and;
(ii) maintain measures aimed at moderating inflation expectations, including the containment of Jamaican dollar liquidity expansion and ensuring that movements in the exchange rate do not threaten the inflation target.

5.3 The Committee **unanimously voted** in favour of the proposed package of measures

5.4 The Committee **unanimously voted** in favour of the propositions.

6.0 Summary of Decisions made at the meeting (Monetary Policy Communication)

6.1 It was noted that under section 34FG(4) of the Bank of Jamaica Act, the Committee is required to publish on the Bank's website a summary of decisions made at its meetings. Following the monetary policy decision, the Committee discussed the following documents: (i) Summary of Monetary Policy Discussion and Decision and (ii) the Monetary Policy Press Release.

6.2 The Committee **unanimously approved** (i) the Summary of Monetary Policy Discussion and Decision and publication of the same on the Bank's website and (ii) the Monetary Policy Press Release for distribution to the media and publication on the Bank's website, subject to changes which were agreed.

6.3 The documents, as revised, were **approved**.

7.0 Any other Business

7.1 There was no other business raised for discussion.

8.0 Adjournment of the Meeting

8.1 There being no other business, the Chairman adjourned the meeting on 29 September 2021 at 11:52 a.m.

SUMMARY OF APPROVALS/DECISIONS

The table below summarises the decisions and approvals made by the Committee.

ITEM NO.	DESCRIPTION	APPROVALS/DECISIONS
1.	Agreement by MPC to increase the Policy Rate by 100 bps to 1.50% and other accompanying measures.	**APPROVED-Meeting of 29 September 2021**
2.	Summary of Monetary Policy Discussion and Decision-September 2021	**APPROVED-subject to amendments agreed on at the meeting of 29 September 2021**
3.	Monetary Policy Press Release	**APPROVED-subject to amendments agreed on at the meeting of 29 September 2021**