Monetary Policy Press Statement:
QMPR Press Conference

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Introduction

Good morning, ladies and gentlemen and welcome to the first Quarterly Monetary Policy Report press conference for 2022. As you know, the fourth wave of the COVID-19 pandemic appears to be receding and therefore the prospects for the Jamaican economy remain generally positive. Economic activity and employment continue to rebound, inflows into the foreign exchange market are buoyant and the country's international reserves have remained strong. Recent developments in domestic inflation and the outlook for inflation are however an ongoing source of concern for the Bank. These developments have prompted the Bank to pursue stronger measures to influence a return of inflation to the Bank's target of 4 per cent to 6 per cent in the near term.

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

Monetary Policy Decisions

You may recall that in December 2021, the Bank increased its policy rate by 50 basis points to 2.50 per cent. With that adjustment, the policy rate was increased by a total of 200 bps for calendar year 2021, along with accompanying measures. The Bank also adjusted the FX net open position (NOP) limits for deposit-taking institutions (DTIs) in December to support its fight against destabilizing movements in the exchange rate. With these policy adjustments, we noted that while interest rates in the money markets have increased, banks remained relatively liquid and, for the most part, have not passed on the policy rate increases to their customers who hold deposits

with them. This means that to the public J$ assets/deposits have not become more attractive compared to US$ assets, leading to a preference for foreign assets and pressure on the foreign exchange market. Of further concern, the prospects of earlier and stronger monetary policy tightening by our major trading partners, notably the United States, may result in capital outflows which could cause pressures on the exchange rate if domestic monetary policy is not appropriately aligned.

The Bank's Monetary Policy Committee (MPC) met on Wednesday and Thursday of last week and voted unanimously to increase the policy rate by 150 bps to 4.00 per cent, effective today, 21 February. The Committee also decided to pursue stronger measures to contain Jamaican dollar liquidity expansion and to maintain stability in the FX market. Some of these actions include issuing longer tenor open market instruments, direct FX sales to the energy sector and ensuring adherence to FX investment limits by regulated financial institutions.

These stronger policy actions should result in a tightening of liquidity, an improvement in the preference for J$ assets and consequently greater stability in the foreign exchange market. In turn this will take some pressure off inflation.

Let me now go into more details about recent developments in inflation and the inflation outlook.

Inflation

As we are aware, the inflation rate for the 12 months leading up to January 2022, as released on Tuesday by the Statistical Institute of Jamaica,

was 9.7 per cent, representing the sixth successive month that inflation has been above the Bank's target range of 4.0 to 6.0 per cent.

The January 2022 outturn mainly reflected high energy-related inflation, due to increases in electricity rates. In addition, the prices for processed foods and services accelerated due to the continued lagged and second round impact of higher international grains and freight costs which, as you know, have been the principal contributors to rising inflation over the past few months.

Going forward, the MPC anticipated that, without further, stronger policy actions, inflation will continue to breach the upper limit of the Bank's target range over the next 10 to 12 months and will peak in the range of 9.0 to 11.0 per cent over this period. This inflation forecast assumes the continued lagged impact of international commodity and shipping prices. Of note some further pressures from energy prices are expected in the coming months. Agricultural food prices are also expected to support inflation. We anticipate that the further tightening of monetary policy will influence a return of inflation to the 4.0 to 6.0 per cent target range in the latter part of 2022.

The near-term risks to the inflation forecast are assessed to be balanced, which means that actual inflation should track in line with the forecast. The factors that could cause the inflation rate to be lower than projected include weaker than projected global growth as well as weaker domestic demand, arising from renewed challenges associated with the pandemic. On the upside, there remains the possibility of a higher pass through from imported inflation as inflation expectations remain high. Left unchecked, underlying demand pressures could also begin to threaten the

stability of the foreign exchange market, diminishing the prospects of inflation returning to the target range.

Developments in the Foreign Exchange Market

In relation to the foreign exchange market, as at 16 February 2022, the exchange rate was J$157.42 to US$1, representing an annual point to point depreciation of 4.0 per cent. This is a slower pace of depreciation than what occurred over the same period of last year. Moreover, since the beginning of 2022, the exchange rate has depreciated by 1.5 per cent, significantly slower than the 6.1 per cent for the similar period in 2021.

The deceleration in the pace of depreciation versus last year, reflects the actions taken by the Bank in response to the higher than targeted inflation. Specifically, since the beginning of the year, the Bank sold US$301.9 million to the market via B-FXITT, compared to US$88.7 million for the corresponding period of 2020. In addition, Bank of Jamaica sold US$115.3 million directly to the energy sector.

The Bank's actions have ensured that foreign currency flows continue to be healthy and that businesses and individuals in Jamaica who require foreign exchange have been able to access it. For the calendar year to 03 February 2022, the daily purchases of US dollars by authorised dealers and cambios averaged approximately US$37.2 million, 12% higher than the average of US$33.3 million recorded over the same period last year. At the same time, however, daily sales to end users over the same period averaged close to US$30.5 million, 26% above the $24.2 million recorded a year earlier.

At 16 February 2022, Jamaica's gross international reserves were substantial, amounting to US$4.3 billion, and representing the equivalent of 140 per cent of the level considered adequate.

Outlook for the Jamaican Economy

The most recent real GDP data published by STATIN indicated that domestic economic activity expanded by 5.8 per cent for the September 2021 quarter, compared with the expansion of 14.2 per cent in the June 2021 quarter and the contraction of 10.6 per cent a year earlier. This outturn represents a continued recovery in economic activity for the country.

The labour market also continues on a path of improvement. The latest data released by STATIN indicated an unemployment rate of 7.1 per cent at October 2021, 3.7 percentage points lower than the rate at October 2020 and, of note, 0.1 percentage point below the country's pre-pandemic unemployment level in October 2019.

Real GDP growth for FY2021/22 is still projected to be within the range of 7 to 10 per cent before moderating in the range of 2 to 4 per cent for FY2022/23, given the impact of stronger than expected improvements in the economies of Jamaica's main trading partners. In this context, the key drivers of this rebound are the services industry, particularly tourism and related sectors, notwithstanding setbacks from the Omicron variant of the coronavirus. The GDP forecast also assumes that the temporary disruption to production at one of Jamaica's main alumina plants will be resolved by June 2022.

The risks to the growth forecast are skewed to the downside, suggesting the possibility of slower growth. Growth in tourist arrivals and related activities could be lower than currently projected, given the potential impact of efforts to control the pandemic. Also, the impact of the shortage of key raw materials and the impact of higher inflation on real incomes could have an adverse impact on GDP growth.

The Bank projects that gross foreign currency reserves will continue to remain healthy. This will be supported by a current account deficit of the balance of payments ranging between 0.5 and 1.0 per cent of GDP, a sustainable level by traditional measures. The performance of the balance of payments is expected to be supported by a further recovery in the tourism sector.

Developments in the Financial Sector

Looking at the financial sector, DTIs balance sheets remain robust, adequately capitalized and in compliance with prudent liquidity standards. The pace of loan growth, while remaining positive, has continued to slow due to the moderating impact of the pandemic. The stock of private sector loans and advances recorded year-on-year growth of 7.9 per cent at November 2021, compared to growth of 16.5 per cent at February 2020 (prior to the crisis). At the same time, non-performing loans remain well below our threshold for concern and continue to be fully provided for by the system.

Concluding Statement

Ladies and gentlemen, I wish to reaffirm Bank of Jamaica's commitment to fulfilling its mandate of price stability. The Bank will

aggressively pursue all options within its sphere of influence in an effort to ensure a return of inflation to the target range of 4 to 6 per cent. The Bank will closely monitor the economic environment and stands ready to expand its suite of measures at subsequent policy meetings, if necessary, in order to achieve this objective.

Thank you and I will now take questions.