

NEW CONFIDENTIAL ECONOMIC BULLETIN

PRIVATE SECTOR ORGANISATION OF JAMAICA

Monthly Analysis of the Jamaican Economy

Vol. I No. 8; May 1996

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Overview

The past month has been a very eventful one, with some interesting new developments emerging in the economy. The Minister of Finance made a key announcement when he declared that government expenditure would be cut if the \$8.3 billion of additional revenue that was included in the 1996/97 budget, could not be collected. This was very good news on the inflation front, as it suggested that government would not be borrowing from the Bank of Jamaica to support its expenditure and would not increase its debt further to accommodate a shortfall in this area. However, the Prime Minister has thrown some cold water on Dr. Davies statement by reaffirming his confidence that the \$8.3 billion will be collected. This is extremely unlikely and the Prime Minister must be getting advice to this effect from his technocrats, if not from the Finance Minister himself.

Inflation has been coming down some-what faster than we had anticipated and it is now possible that 1996 calendar year inflation could fall below 20% and fiscal year inflation could be in the mid-teens. This can only happen if the reported declines in the rate of growth of money supply continue and, if the government lives up to its promises, they should.

The implications of this for business could be quite

severe, as the cost -push pressures in the economy are still quite strong. Companies will have to pay particular attention to labour costs as the labour movement has not made a significant downward adjustment in their inflationary expectations and are still expecting settlements in line with those of the recent past. It will be extremely difficult to pass on these costs to the consumer and the impact on the bottom line is likely to be decidedly negative. Utility costs are also likely to go up soon and this will have repercussions on cost throughout the economy.

While there has, in the recent past, been a great deal of agonising by companies in the domestic market, those in the export sector will also be feeling the pinch this year. With the exchange rate appreciating by 4.5% in May and local inflation still running at about 31% on a point to point basis, the export sector (tourism included) is going to have a tough time absorbing and controlling their costs. Although an adjustment in the exchange rate may be unavoidable in the medium term, there is little prospect of this happening before the next election, which is unlikely to be held before the next 12 to 15 months.

One of the consequences of the present policy framework is already becoming apparent. Imports were up 20% in the first two months of this year to equal roughly twice the value of merchandise exports. Non-bauxite exports actually declined by about US\$5 million. The apparel sector also registered a decline in exports over this period which is a very worrying sign as this has been the star performer of the non-traditional export sector. The recent appreciation of the currency is likely to reinforce these trends, boosting imports and impeding exports.

The revaluation was prompted by the Bank of Jamaica's selling of some of their Net International Reserve holdings as these were accumulating too rapidly. The high T-bill rates are proving to be very attractive to holders of hard currency as inflows continue to be strong. There is little prospect of rates falling any time soon, as recent issues have offered

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fixed returns of over 42% until November of this year when they will float in line with Tbill rates. Government has also come out with a new instrument, an Investment Debenture, the first tranches of which will be issued in June.

Net International Reserves

During April, the Net International Reserves registered a US\$33.1 million increase over the US\$496.3 million balance held at the end of March. This implies that the Net International Reserves rose by 8.7% and 16.2% respectively during April and over the first four months of 1996. These movements compare with a 2.14% fall and a 7.04% increase over similar periods in 1995. However in March 1995, there was a US\$62.7 million or 16.7% rise in the Net International Reserves which was not as alarming then, since it followed a US\$35.6 million decline in (February) the previous month.

The implications for the current level of increase in the Net International Reserves will be reflected in a rise in money supply and an increase in its growth rate which could have inflationary effects on the economy if the funds expended to purchase foreign currency are not mopped up instantly.

The authorities contend that the increase in the Net International Reserves resulted from the Bank of Jamaica honouring its obligation to purchase certain levels of foreign exchange from authorized dealers and cambios. During this month there was a significant increase in the levels of inflows to the system which gave rise to the level of intake by Bank of Jamaica.

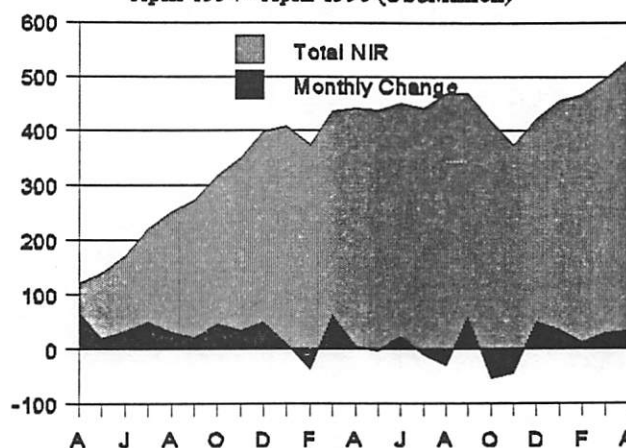
Foreign Exchange Accounts

The estimated stock position of foreign exchange accounts at the end of April stood at US\$739.03 million that is US\$37.0 million or 5.3% more than for March. This indicates a 1996 first four months increase of only US\$1.73 million, since from December 1995 - first quarter's monthly stocks have remained relatively flat.

In the midst of all this, the number of lay-offs and redundancies continues to grow as companies seek to increase their efficiency and prepare themselves to deal with an extended period of high interest rates, relatively high inflation and economic stagnation or decline.

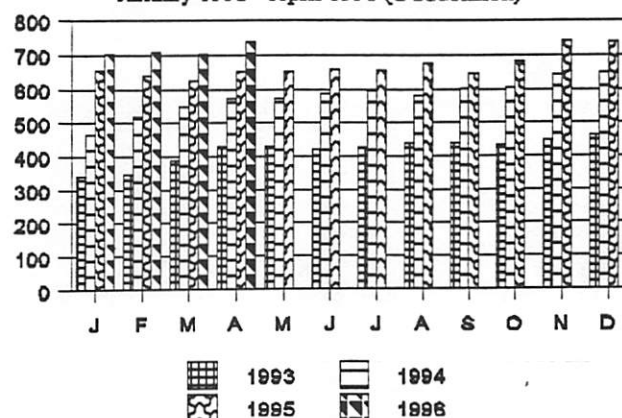
CHANGES IN INTERNATIONAL RESERVES

April 1994 - April 1996 (US\$Million)



FOREIGN CURRENCY ACCOUNTS

January 1993 - April 1996 (US\$Million)



None-the-less, the pattern of stock flows for the first four months of 1996, are relatively similar to those of 1995, only main difference being 1996 has seen a higher level of stocks than 1995.

It is assumed that the high interest rate policy is one of the major contributors to the buoyancy of foreign exchange inflows. As this policy is slated to continue

for some time yet it should be reasonable to expect continued buoyant inflows of foreign currency in the near future.

Exchange Rate

As May closes, the exchange rate is actually experiencing an appreciation. The Jamaican dollar has been exchanging at J\$38.35 to J\$38.78 to the US\$. The scenario at the end of May is the reverse of that which existed at the end of April, when the exchange rate of the J\$ to the US\$ was actually depreciating and edging over the J\$40.00 to US\$1.

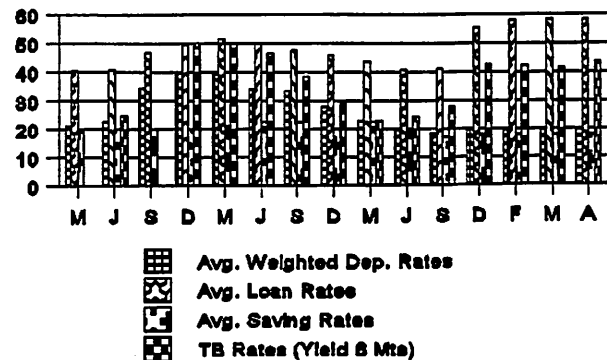
May's appreciation in the exchange rate was started and influenced strongly by Bank of Jamaica's decision to sell foreign exchange from its Net International Reserves holdings. This was done ostensibly to slow the growth of the Net International Reserves which was proceeding ahead of schedule. Since the increase in foreign exchange inflows is believed to be influenced by arbitrage activities its reliability and sustainability could be very fragile. With supplies apparently flush now, all the users of foreign exchange should garner their supplies now to tide them over the usually leaner months of September/October.

As the trade data for January to February show a declining trend in export earnings, while imports values continue to almost double export earnings, even with tourism showing some positive trends, there is bound to be an adverse effect on the Balance of Payment later on in the year. One is forced to wonder how long private transfers will continue to finance this growing trade gap

Interest Rates

There was no LRS offer made in May however, there were three issues of Tbills, which consisted of two for J\$500 million each and one for J\$900 million. These issues were all over subscribed - the J\$500 million for 25 days by 50% and the other two by up to 200%. The average yield was 45.50% from the 25 days issue and 42.49% on the other two issues which were for 183 and 191 days each. With the 6 months issue in

Comparative Interest Rates
of Commercial Banks (1993, 1994, 1995 and 1996)



April offering 44-45%, the yield in May is showing a slight decline so one is prompted to question if this is the beginning of a slow decline in the rates as well as if this is the pace at which the decline will be maintained.

During April, however, commercial rates continued their upward movement.

Fixed deposit rates moved up 2 percentage points at the higher end of the range while saving and loan rates remained the same as in March.

Currently, high interest rates are serving as an attraction to increased inflows of foreign exchange - which is contributing to a revaluation of the local currency while it is creating havoc with business and investments. Yet government remains committed to this high interest rate policy and reactions to the recent revaluation confirm their belief that this is the way to go. This and the Net International Reserves seem to be the cornerstone of their policy to hold the exchange rate until after the general elections.

Inflation

The movement in the CPI for April showed a 1.3% rate of inflation for the month. This follows a 1.6% and 3.3% rise in March and February respectively. The rate in April signifies a downward trend in the inflation levels. For the first four months of 1996, the inflation rate rose by 8.8%. If this is being compared with the government's projection of 11-15% for the calendar year - rates need to be below 1% per month

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for the rest of the year to achieve this target. The annual rate for the calendar year could be about 20% or just below that.

The point to point rate for April 1995 to 1996 is 33.3% showing a steadily increase trend given a point to point rate of 25.6% in December 1995.

Base Money

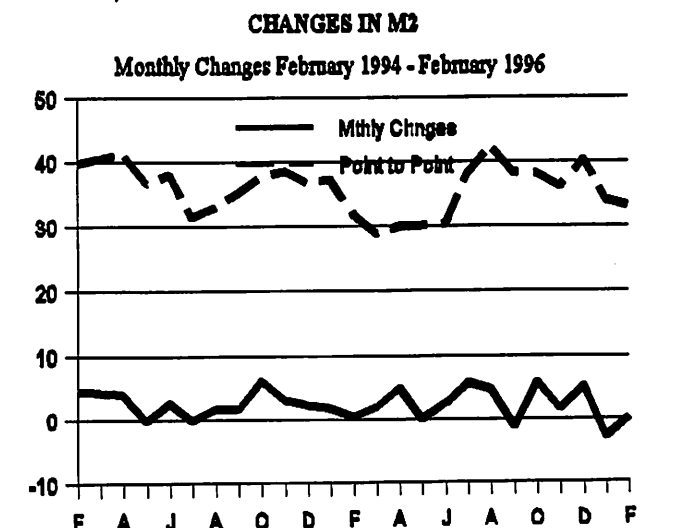
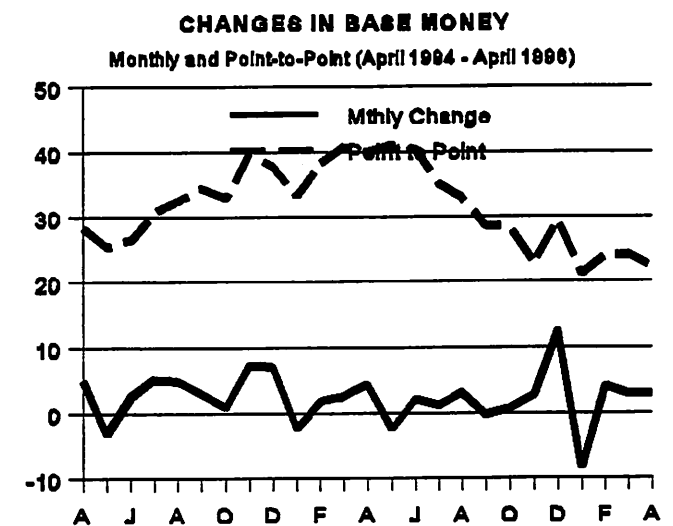
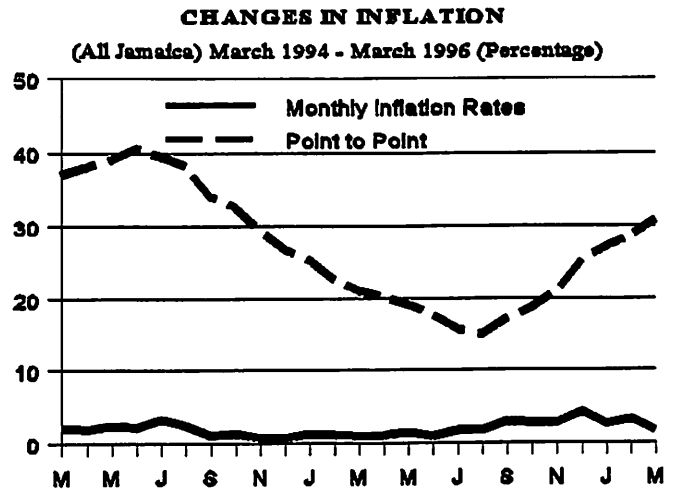
The increase in base money during April was 2.83%, just marginally lower than the increase of 2.89% experienced in March. This however saw the point-to-point change declining by 2 percentage points, that is to 22.3% in April compared with 24.2% in March. The point to point trend has been maintained in the lower twenties since January indicating a moderating trend in 1996 when compared with the similiar period in 1995, which showed point to point changes of 33.2% to 40.2%.

Since January 1996, while the level of currency issue has been steadily trending upwards, the cash reserves of FIA institutions and Building Societies have been constantly adjusting and fluctuating and this has moderated the increasing effect of the rise in currency issues on the overall base money.

Money Supply

After a decline of 2.8% in Money Supply (M2) in Janauary, February saw a marginal rise of 0.27%. This brought the point to point change to 33.64% which is indicating a move back to the declining trend of late 1995 which was broken in December by the influence of seasonal demand on this variable.

This trend is encouraging as sustained declines in the rate of money supply growth are critical in reducing the rate of inflation. Though the detail have not been made public the Ministry of Finance is claiming that monthly money supply growth has been very low for the first 4 months of 1996. If so, this bodes well for reducing inflation.



Tourism

During April, tourist arrivals showed a 5.5% increase compared with April 1995. Of the 149,663 arrivals, there were 89,030 stop over visitors and 60,633 cruise passengers - these increasing by 2.9% and 9.7% respectively, when compared with April 1995. For the four months January to April 1995 and 1996 compared, the 1996 period saw 630,797 tourists arriving. This amounted to an 8.3% rise in arrivals, cruise passengers improving by 8.9% and stop-overs by 7.9%.

Expenditure figures for January to February amounted to US\$172.00 million which was 8.31% more than the similar period in 1995.

As the arrivals up to April, have shown improvement over last years figures, the tourism product is also experiencing some boost in areas of accommodation, transportation and in attractions. During May - the first family all inclusive 100 rooms Suite Spa opened in Montego Bay; Air Jamaica opened its air route to London/Europe and restoration work on the old Folly Estate in Portland was initiated.

Despite the overall positive experiences of the sector, the smaller hotels and the U-Drive sector complain of severe pressure on their profitability and are urging action from government to maintain their viability.

Merchandise Trade

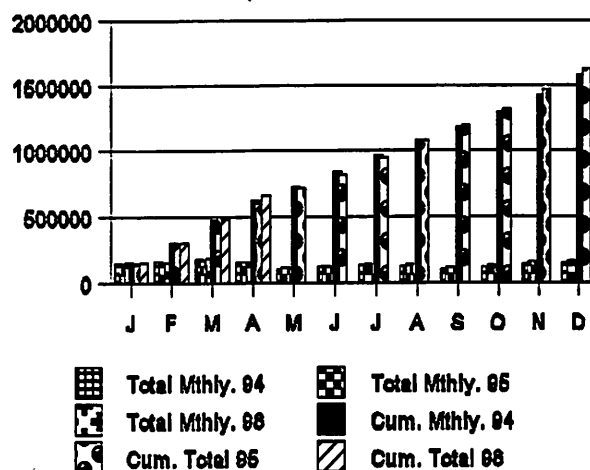
The trade data for January and February 1996 show imports totalling US\$462.9 million and exports of US\$230.3 million, which resulted in a trade gap of US\$232.6 million. Compared with the similar period in 1995, imports have risen by US\$77.9 million or by 20.3%, exports by US\$26.5 million or by 13%, and the trade gap widened by US\$51.4 or by 28.4%.

Contributing to the out turn for the current period were the following factors:

Exports: The major traditional exports sector

TOURIST ARRIVALS

1994, 1995 and 1996



showed a 27% overall increase in earnings with only sugar showing a decline. Bauxite and Alumina showed increases in both export volumes and earnings. Earnings of both the non-traditional and other traditional sectors fell by 4.8% and 17.8% respectively.

It is interesting to note that the increase in bauxite/alumina earnings of approximately US\$30 million was more than the overall increase in exports, highlighting the decline in the other export sectors.

Imports: Consumer goods imports rose by 42.5%, while raw material and capital goods increased by 15.7% and 8.5% respectively. Raw materials imports other than fuel rose by 18.8%. Imports of motor cars formed 19.2% of the total consumer goods imported for the period.

The trade deficit with Caricom has begun to accumulate. At the end of February 1996, Imports from Caricom stood at US\$31.3 million with exports at US\$7.2 million leaving a gap of US\$24.1 million, of which US\$23.15 million accrues to Trinidad and Tobago.

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BALANCE OF PAYMENTS PROFILE: US\$Mn

	Merchandise	Services	Transfers	Current A/c	Capital A/c	NIR A/c
Dec '95	-1342.60	508.20	579.30	-255.10	278.50	421.31
Jan-Feb '95	-181.20	69.60	99.30	-12.30	-12.50	373.13
Jan-Feb '96	-232.60	125.90	91.10	-15.60	61.80	467.52

MONTHLY MACRO-ECONOMIC INDICATORS

(December 1994 - April 1996)

MONTHS	BASE MONEY		NET INT'L RESERVE	FOREX ACCTS.	INFLATION		TOURIST ARRIVALS			CHANGES IN M2 (MONEY SUPPLY)	
	Mthly Chng.	Point to Point	Total NIR	Total Balances	Mthly Chng	Point to Point	Total Visitors	Stop-overs	Cruise	Mthly Chng.	Point to Point
Dec.94	7.07	37.83	397.92	649.76	0.7	26.80	147290	94127	53017	2.31	36.57
Jan. 95	-2.13	33.19	408.70	655.12	1.3	25.40	138969	81385	57570	1.85	37.22
Feb.	1.79	38.18	373.13	640.34	1.1	22.70	140787	86147	54281	0.55	31.82
Mar	2.64	40.85	435.30	625.15	0.9	21.20	164222	96378	67844	1.99	28.89
Apr	4.43	40.01	440.41	652.66	1.1	20.76	141814	86552	55262	4.93	30.01
May	-2.43	41.09	437.55	651.42	1.5	19.20	106772	71945	34827	0.00	30.16
Jun.	2.17	40.51	449.89	656.38	1.0	17.80	118253	87480	30773	2.70	30.22
Jul. 95	1.17	35.06	440.35	654.51	1.7	15.80	138624	101244	36780	5.88	38.15
Aug	3.21	32.95	411.23	676.25	1.7	15.10	133198	90747	42451	4.84	42.44
Sept	-0.17	28.69	468.05	646.13	3.0	17.20	110372	66663	43709	-1.29	38.19
Oct.	0.69	28.49	416.42	682.86	2.7	18.80	128394	72803	55591	6.03	38.04
Nov.	2.71	22.87	373.22	740.06	2.8	21.20	148839	77419	71419	1.73	36.11
Dec.95	12.81	29.46	421.31	737.30	4.3	25.50	157819	100183	57636	5.53	40.40
Jan 96	-8.46	21.08	455.79	702.00*	2.6	27.22	150561	86184	64377	-2.78	34.00
Feb.	4.17	23.91	467.52	708.00*	3.3	29.94	150355	94449	55906	0.27	33.14
Mar.	2.89	24.21	496.26	702.00	1.6	30.8	180218	108407	71811	-----	-----
Apr.	2.83	22.30	529.37	739.03*	1.3	33.3	149663	89030	60633	-----	-----

* Provisional

Source: Compiled from National Statistics as Supplied by Bank of Jamaica, Planning Institute of Jamaica and Jamaica Tourist Board.