1.9.9.8

THE PRIVATE SECTOR ORGANISATION OF JAMAICA

ANNUAL REPORT ON THE JAMAICAN ECONOMY

Published May 1999

Publication Design and Typesetting:
The Private Sector Organisation of Jamaica
39 Hope Road, Kingston 10. Tel: 978-6795/6/8

PSOJ PUBLICATIONS

	Published
Jamaica Economic Review 1984	1985
Jamaica Economic Review 1985	1986
Jamaica Economic Review 1986	1987
Jamaica Economic Review 1987	1988
Jamaica Economic Review 1988	1989
Annual Report on the Jamaican Economy 1989	1990
Annual Report on the Jamaican Economy 1990	1991
Annual Report on the Jamaican Economy 1991	1992
Annual Report on the Jamaican Economy 1992	1993
Annual Report on the Jamaican Economy 1993	1994
Annual Report on the Jamaican Economy 1994	1995
Annual Report on the Jamaican Economy 1995	1996
Annual Report on the Jamaican Economy 1996	1997
Annual Report on the Jamaican Economy 1997	1998
A Policy Framework for Economic Development in Jamaica	1985
A Policy Framework for Economic Development in Jamaica *- A Progress Report*	1992
Economic Analysis & Public Policy I *- Foreign Trade Policy*	1986
Economic Analysis & Public Policy II *- The Role of Government in the Jamaican Economy*	1987
Economic Analysis & Public Policy III *- Exchange Rate Policy for Economic Growth & Development*	1987
Economic Analysis & Public Policy IV *- Why the JCTC should be dismantled*	1989
Economic Analysis & Public Policy V *- Social Policy*	1990
PSOJ/USAID *Business Behaviour Survey*	1993
PSOJ/USAID *Business Behaviour Survey*	1994
Alternative Monetary Regimes for Jamaica	1995

Keep your bottom line in the black.

Advertise in the business paper that's well read!

The Financial Gleaner. Every Friday.

The Gleaner

Readership 307,000. (Source: 1998 All Media Survey' Market Research Services Limited.)

TABLE OF CONTENTS

LIST OF TABLES

OVERVIEW OF ANNUAL ECONOMIC REPORT 1998

Throughout 1998 the government maintained essentially the same economic policies that had been in place since late 1995. These policies have featured high real and nominal interest rates and an emphasis on controlling the growth of money supply and preventing a depreciation of the exchange rate. The policies have resulted in a continuing declinė in the inflation rate and very little downward movement in the nominal value of the Jamaican dollar. However, the policies have taken quite a toll on some sections of the economy and the society and it is by no means clear that we have counted the full cost of them as yet.

The manufacturing and construction sectors have been hard hit by the policies and both contracted in output in 1998, the manufacturing sector having done so for the fourth consecutive year. Construction was recording its third successive year of decline. Despite the intervention of FINSAC, many locally owned financial institutions continue to experience some difficulties. While the restructuring and closure of a number of the intervened institutions has gained speed in 1998, there remain some fundamental questions about how the FINSAC debt load will be absorbed by the government and how it will be serviced in the coming years. It is also not completely clear as to how the resuscitation of the commercial banking sector can be completed without a significant reduction in interest rates.

In this regard, it is heartening to note that the Minister of Finance, in his 1999/2000 budget speech made the reduction of nominal interest rates a key component of the fiscal programme for the coming year. The reduction of interest rates will be a key factor in the government's plan to lower its domestic debt servicing costs, even though it will be borrowing a large amount of money to finance the 1999/2000 budget. The last 6 or 7 years have seen a strong and steady build up in the domestic debt and a corresponding increase in the cost of servicing it. This has in turn put considerable and increasing strain on the fiscal accounts, which have incurred large deficits over the last 3 years. Strong action to follow through on the planned reductions in interest rates

OVERVIEW OF ANNUAL ECONOMIC REPORT 1998

will therefore be of great help in restoring fiscal balance.

Some sectors of the economy have, however, managed to grow in 1998 and these include mining, tourism and basic services like electricity and water. However the expansion in these sectors was not enough to offset the contraction in others and the economy, as a whole, produced 0.7% less goods and services in 1998 than it did in 1997. This is the third consecutive year in which the economy has contracted and the lack of growth is beginning to have an impact on the society. The gas price demonstrations of mid-April 1999 are the most poignant evidence of these social stresses that we have had to date. Here again, the planned reductions in interest rates may help to revive investment and growth if they are implemented as programmed. The government must be congratulated for meeting its inflation targets for the calendar and fiscal years, which came at 7.9% and 6% respectively.

The major challenge facing the policymakers is to translate the lower inflation that they have achieved into strong and sustainable economic growth. It is not clear exactly how this will be done, but it must involve bringing a halt to the deterioration in the fiscal deficit and returning to a balanced budget or a fiscal surplus. The authorities will also have to hold the confidence of the international capital market as borrowing in hard currency is going to be an ongoing part of the government's fiscal programme. A credible medium term plan for servicing and retiring the FINSAC debt which has been incurred in the rescue of companies in the financial sectors is required. These debts amount to between J$90 and J$100 billion and have not yet come fully into the central government's financial statements. They represent a large liability which will make a significant call on government's resources at some point in the not too distant future.

Outlook

The course of events in 1999 will depend, to a large extent, on the government's ability to achieve its programmed reduction in interest rates because so much seems to depend on this. The improvement in the fiscal position which is forecast for this financial year will depend to a large extent on lower interest rates to control the servicing cost of the

OVERVIEW OF ANNUAL ECONOMIC REPORT 1998

domestic debt. A recovery in private investment and hence in economic output, the possibility that a significant reduction in interest rates may require a trade off in some other aspect of government policy, namely that with regard to the exchange rate. Lower real interest rates may require a more flexible approach to the exchange rate than the government has demonstrated in the recent past. Herein may lie the fundamental contradiction in the present policy objectives and it is very difficult to imagine how the economy will be shifted into a growth mode without this contradiction being resolved.

will also depend heavily on a reduction in both nominal and real interest rates. There is It is quite possible therefore that 1999 will be another holding year in which the economy will perform similarly to the way it did in 1998. This is even more likely to be the case if the government is successful in meeting its borrowing target in the international market and if there is no major outflow of private capital from Jamaica. Such an outcome would also assume a fairly minimal impact on tourism from the April gas price demonstrations and a fairly moderate rise in international oil prices.■

1. THE WORLD ECONOMY REVIEW 1998-1999

International economic and financial conditions have deteriorated considerably over 1998 and 1999 as recessions have deepened in many Asian emerging market economies and in Japan, and as Russia's financial crisis has raised the spectre of default. Negative spillovers have been felt in world stock markets, emerging market interest spreads, acute pressures on several currencies, and further drops in already weak commodity prices. Among the industrial countries of North America and Europe, the effects of the crisis on activity have been small so far but are beginning to be felt, especially in the industrial sector (see Table 1). World growth of only 2% is now projected for 1998, a full percentage point less than expected in IMF's May 1998 World Economic Outlook and well below trend growth. Chances of any significant improvement in 1999 have also diminished, and the risks of a deeper, wider and more prolonged downturn have increased.

World Trade

The prospects for world trade and output in 1998 have been clouded, to some degree, by the Asian financial crisis. Projections for economic growth have been scaled down markedly in Asia. The five countries, Indonesia, Korea, Malaysia, the Philippines and Thailand which are at the core of the crisis, are expected to record average GDP growth of 3% or less in 1998. As intra-Asian trade and investment links have developed dynamically over the last decades, more than half of Asia's trade was intra-regional in 1996; the repercussions of the crisis are foremost within the region. Intra-regional trade, which has more than tripled since 1990, could even decrease.

World trade volume in goods and services, as supplied from the preliminary indicators of the International Monetary Fund, was projected to grow at 3.7% in 1998 (6 percentage points below 1997's outcome) as compared with 4.6% in 1999 (2.2 percentage points below the growth rate in 1996). The moderate projected recovery in 1999 is premised on the sustained overall growth in the advanced economies of North America and Europe.

THE WORLD ECONOMY REVIEW 1998-1999

Oil

Successive agreements among oil-producing countries in the Spring of 1998 to cut production led to only temporary increases in oil prices, with market skepticism persisting about the effectiveness of the cuts. Prices fell to a 1998 low in the middle of June in real terms, the lowest level since 1973. Prices rebounded somewhat following fresh pledges of production cut-backs by oil-exporting countries in late June, but declined again in August. On the basis of future market quotations for the rest of the year oil prices in 1998 as a whole are projected to be 30% lower, on average, than in 1997, with only a partial recovery projected for 1999.

Inflation and Commodity Prices

The prices of many non-fuel commodities weakened further between May and August 1998 by about 9% on average, following some stabilization in early 1998, as the situation in Asia and other emerging markets deteriorated. They are now projected to be about 12% lower on average in 1998 than in 1997, and to show little upward movement in 1999.

With the weakness of primary commodity prices adding to the downward pressures on the broader price level arising from enhanced competition from Asia, most of the advanced economies have moved closer to price stability. This has led to a projected inflation rate for advanced economies at 1.7% in 1998 and 1999.

Inflation in developing countries continue to be subdued, with inflation for 1998 and 1999 projected at 10.3% and 8.3% respectively. However, activity in the transition countries as a group is now expected to stagnate in both 1998 and 1999 mainly as a consequence of the Russian crisis. This has therefore led to a projected inflation rate of 29.5% in 1998 and 34.6% in 1999.

Trade Development

In terms of world trade agreements there have not been many in 1998. However the United States has been challenging the European Union to comply with a World Trade Organisation

THE WORLD ECONOMY REVIEW 1998-1999

(WTO) ruling to reform its banana import regime, which the United States contends violates the European Union's WTO obligations.

This approach would provide the EU with an opportunity to prove its contention that its new measures, scheduled to be implemented on January 1, 1999, are consistent with the WTO. At the same time, this approach will preserve the right of the United States to suspend concessions within the WTO prescribed time frames. In preparation for exercising these rights, the United States has readily begun to receive public comments on the November 10, 1998 proposal to impose prohibitive duties on selected products that the United States imports from the EU.

World Economic Outlook 1999

Growth has continued to be well sustained overall in the advanced economies of the North America and Europe, but with significant changes in the relative growth performance. In the United States, growth eased to below its potential rate in the second quarter of 1998 after registering its highest rate for almost two years in the first quarter, but final domestic demand remained robust. Growth has also slowed in the United Kingdom and Canada. In continental Europe the recovery has gained momentum since early 1997, underpinned by strengthening domestic demand. Recent IMF indicators, including strong business and consumer confidence and improvements in labour market conditions, suggest that the near-term growth prospects in the European Union remain favourable.

However, growth prospects have been marked down significantly for Asia, Russia, and to a lesser extent for many emerging market countries in other regions, including oil and other commodity exporters, as a direct consequence of the reduction in oil and non-fuel commodity prices. Growth in the world economy is now projected at 2% in 1998, 2¼ percentage points lower than projected in 1997. In 1999 global growth is projected to pick up moderately to 2½%; a modest turnaround of growth in Asia, including Japan, is projected to be offset by a slowing of expansions in North America and, to a lesser extent, in Europe, with

THE WORLD ECONOMY REVIEW 1998-1999

the developing countries outside of Asia, and the transition countries, showing little or no improvement. The impact of the emerging market crisis is the main factor contributing to the projected slowdown in world trade growth to 3¾ in 1998, markedly lower than the exceptionally high 1997 growth rate, with only a moderate pick-up predicted in 1999. The trade growth now projected for 1998 and 1999 is similar to that experienced during 1992-93.

THE WORLD ECONOMY REVIEW 1998-1999

Overview of the World Economy (Annual percent change unless otherwise noted)	1996	1997	Current Projections 1998	1999
WORLD OUTPUT	**4.2**	**4.1**	**2.0**	**2.5**
Advanced economies	3.0	3.1	2.0	1.9
Major industrial countries	2.8	2.9	2.1	1.9
United States	3.4	3.9	3.5	2.0
Japan	3.9	0.8	-2.5	0.5
Germany	1.3	2.2	2.6	2.5
France	1.6	2.3	3.1	2.8
Italy	0.7	1.5	2.1	2.5
United Kingdom	2.2	3.4	2.3	1.2
Canada	1.2	3.7	3.0	2.5
OTHER ADVANCED ECONOMIES	**3.8**	**4.2**	**1.4**	**2.3**
Industrial countries	2.8	2.9	2.3	2.0
European Union	1.7	2.7	2.9	2.5
Euro Area	1.6	2.5	3.0	2.8
Newly industrialized Asian economies	6.3	6.0	-2.9	0.7
DEVELOPING COUNTRIES	**6.6**	**5.8**	**2.3**	**3.6**
Africa	5.8	3.2	3.7	4.7
Asia	8.2	6.6	1.8	3.9
ASEAN-4[1]	7.1	3.7	-10.4	-0.1
Middle East and Europe	4.7	4.7	2.3	2.7
Western Hemisphere	3.5	5.1	2.8	2.7
COUNTRIES IN TRANSITION	**-1.0**	**2.0**	**-0.2**	**-0.2**
Central and Eastern Europe	1.6	2.8	3.4	3.6
Excluding Belarus and Ukraine	3.7	3.2	3.7	4.1
Russia	-5.0	0.9	-6.0	-6.0
Transcaucasus and Central Asia	1.6	2.1	4.1	3.8
WORLD TRADE VOLUME (GOODS AND SERVICES)	**6.8**	**9.7**	**3.7**	**4.6**
IMPORTS				
Advanced economies	6.4	9.0	4.5	4.7
Developing countries	9.3	9.8	1.0	4.6
Countries in transition	10.0	8.2	3.5	3.5
EXPORTS				
Advanced economies	6.0	10.3	3.6	4.2
Developing countries	8.8	10.9	3.9	5.5
Countries in transition	7.0	6.9	5.3	5.9
COMMODITY PRICES				
Oil[1]				
In SDRs	23.7	-0.2	-29.2	10.4
In U.S. dollars	18.4	-5.4	-31.1	9.3
Nonfuel[2]				
In SDRs	3.3	2.0	-11.6	1.4
In U.S. dollars	-1.2	-3.3	-13.9	0.4
CONSUMER PRICES				
Advanced economies	2.4	2.1	1.7	1.7
Developing countries	14.1	9.1	10.3	8.3
Countries in transition	41.4	27.9	29.5	34.6
SIX-MONTH LIBOR (IN PERCENT)[3]				
On U.S. dollar deposits	5.6	5.9	5.7	5.7
On Japanese yen deposits	0.7	0.7	0.7	0.6
On deutsche mark deposits	3.3	3.4	3.7	...
On Euro deposits	...	...	...	3.7

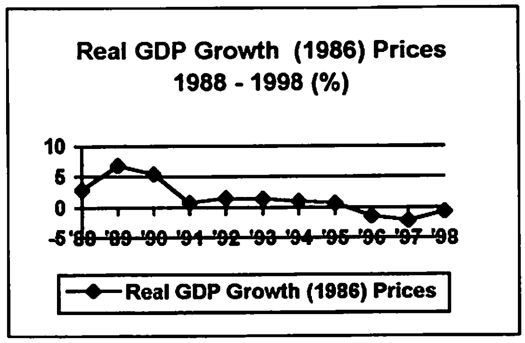
Note:
Real effective exchange rates are assumed to remain constant at the levels prevailing during July 27 - August 24, 1998, except for the bilateral rates among ERM currencies, which are assumed to remain constant in nominal terms.
[1] Simple average of spot prices of U.K. Brent, Dubai, and West Texas Intermediate crude oil. The average price of oil in U.S. dollars a barrel was $19.27 in 1997; the assumed price is $13.28 in 1998 and $14.51 in 1999.
[2] Average, based on world commodity export weights.
[3] London interbank offered rate.

2. GROSS DOMESTIC PRODUCT

Introduction

High interest rates continued to negatively impact the productive sector, even though there has been a slow and small reduction in real lending rates towards the end of 1998. The economy contracted by 0.7% in 1998, registering the third consecutive decline after contracting by 1.7% in 1996 and 2.4% in 1997. The restrictive monetary policy being pursued by the Central Bank since 1996 caused severe tightness in the financial market and fostered investment in government paper rather than in the real sector. It was anticipated that the programmed reduction in interest rates during 1998 would have helped to lower the costs of financing without jeopardising the achievement of lower inflation. The end result was that the weighted average loan rate of commercial banks fell from 35.00% at the end of 1997 to 32.88% at the end of 1998, while point to point inflation was reduced from 9.2% for 1997 to 7.9% for 1998. There was consequently only a marginal reduction in real lending rates.

Figure 2.1



There was positive growth in the service sectors and a slight upturn in the output of the tradable goods sector. Mining and quarrying grew by 2.6%, electricity and water by 6.4% and transport, road and communication by 5.6%. However, the manufacturing sector contracted for the fourth consecutive year and registered a decline of 4.2% due primarily to high interest costs and, to a lesser extent, to competitive pressures from imports. Further, total agricultural production fell by 0.3% compared with a 14.6% decline in 1997.

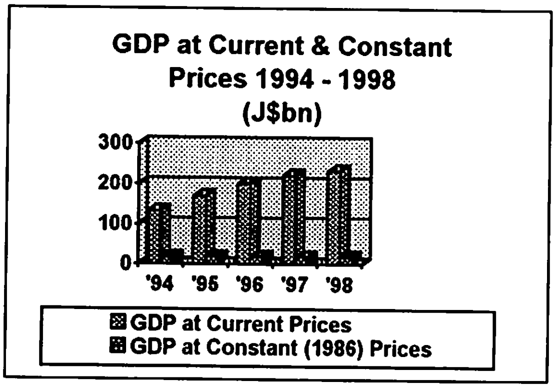
Balance of Payment Developments

There were significant improvements on the balance of payments accounts as the deficit on the current account was reduced

GROSS DOMESTIC PRODUCT

in 1998. Further, net capital movement increased from US$247.8M in 1997 to US$352.8M in 1998. This contributed to the reserves at the Bank of Jamaica (BOJ) increasing by US$29.6M in 1998 compared with a reduction of US$152.1M for the previous year. The trade deficit decreased from US$1,120.8M in 1997 to US$1,101.9M due to a 6.4% reduction in exports and a 4.5% decline in imports.

Figure 2.2



Value of the Jamaican Dollar

The nominal value of the domestic currency declined slightly, with the exchange rate moving from J$36.59 for US$1.00 to J$37.16 for US$1.00. However, towards the end of the year, pressure on the Jamaican dollar began to rise as government's failure to raise its budgeted borrowing on the international capital markets led to a relative shortage of foreign exchange in the local market. In the first quarter of 1999, the Jamaican dollar declined further to a rate of about J$38.30 for US$1.00.

Interest Rates

High real interest rates continued to be a cause for concern throughout the year. This resulted from the continuation of the high interest rate policy by the central bank despite the move to increase liquidity by lowering the cash reserve requirement of the commercial banks. In an attempt to increase liquidity, the liquid assets reserve ratio was reduced from 47% to 45% and then to 43% at the beginning of August and November respectively.

High interest rates on government paper, and liquidity constraints brought on by the financial sector restricted the ability of the commercial banking system to provide reasonably priced credit for investment purposes. However, nominal interest rates continued to decline somewhat with the Treasury Bill rate falling from 28.9% in December 1997 to 23.5% in December 1998.

GROSS DOMESTIC PRODUCT

However, real interest rates were still too high to significantly stimulate investment ventures from the private sector. The continuation of high real interest rates has negatively impacted the loans to the productive sector and has resulted in a reduction in total commercial banks' loans from J$55,241.858M as at November 1997 to J$43,692.494M as at November 1998.

THE PRODUCTIVE SECTOR

Agriculture

As was mentioned earlier, the drought conditions of 1997 negatively impacted agricultural production during the first half of 1998. The end result is that total agricultural production fell by 0.3% in 1998 compared with a 14.6% decline in 1997. The share of agriculture in the tradable goods sector increased, reflecting increased output in domestic food crop production. Thus, the production of condiments, yams, potatoes, fruits and other tubers recorded increases between January and September 1998.

During the crop year ended July 1998, the volume of sugar cane milled declined by 6.0% to 2.3 million tonnes, while the amount of sugar produced fell by 21.2% to 186,154 tonnes owing to the drought conditions of the previous year. However, the volume of sugar exported increased by 21.5% to 149,900 tonnes between January and September 1998, while receipts from exports declined by 7.1% to US$94.7M due to price reductions.

The drought conditions of 1997 adversely affected coffee production and resulted in a 16.6% decline in coffee beans delivered to the processing plants during the crop year August 1997 to July 1998. Thus, only 21,135 tonnes of coffee beans were delivered to processing plants. During the year, the government made concerted efforts to avert the continued fallout in coffee production and to that end has put in place funding to aid the ailing sub-sector.

Whereas the production of bananas and citrus declined by 21% and 25.7% respectively during the first nine months of 1998, cocoa production continued its exponential rate of increase and registered a 48.9% increase in cocoa beans delivered to processing plants. This comes on top of the 24.4% expansion in cocoa production for the 1997 crop year due to

GROSS DOMESTIC PRODUCT

an increase in the price per box in at the beginning of the 1997 crop year.

Mining

Preliminary data shows a continuation of the upward trend in the production of bauxite and alumina evidenced in 1997. Total bauxite production increased by 5.5% to 12.65 million tonnes in 1998, the highest level since 1974. Crude bauxite for export rose by 10.4% above its 1997 level to 4.02 million tonnes in 1998, owing to new management arrangements and a more stable labour environment.

Alumina production increased by 1.4% to a new record level of 3.44 million tonnes in 1998 and export volume expanded by 1.8% to 3.48 million tonnes. Despite the expansion in export volumes, gross receipts declined from US$735.0 million in 1997 to an estimated US$685.0 million in 1998 due to sluggish international market conditions associated with the economic turbulence of Asia.

In July 1998, the government, trade unions and bauxite companies signed "The Manley Accord" – a Memorandum of Understanding – with a view to improving industrial relations and the investment climate in the bauxite/alumina sector. This led to substantial improvements in labour relations in the second half of the year and the authorities will be pushing for similar agreements in other areas of the economy in 1999.

Manufacturing Sector

The manufacturing sector continued to suffer from high financing costs and contracted by 4.2% in 1998 to register its fourth consecutive year of decline. During the year, processed food, chemicals and chemical products recorded small increases; but sharp declines in the output of beverages and tobacco, petroleum, and cement resulted in an overall decline. The reduction in manufacturing output was primarily due to high interest costs and the continuing real appreciation of the Jamaican dollar. To a lesser extent, the liberalization of imports and reduced customs duties, which rendered domestic goods less price competitive to imported goods, also affected manufacturing.

Exports of manufactured goods declined by 11.6.0% to US$220.82 million during 1998 and the share of manufactured goods in exports declined from 18.0% in

GROSS DOMESTIC PRODUCT

1997 to 17.1% in 1998. Thus, the manufacturing sector continued to suffer from neglect and if something is not done to avert the negative impact of high interest costs in a liberalized and open economy, this trend is likely to continue. With the fallout within the manufacturing sector, imports of manufactured goods increased from US$879.885 million in 1997 to US$908.525 million in 1998, an increase of 3.3%.

SERVICES

Financial Sector

Several policy initiatives were implemented during 1998 in an attempt to aid recovery in the financial sector. However, the anticipated impact of most of these policy initiatives have been slow and uncertain. The government initiated a reduction in the lending rates of its development banks from 18% to 13% in May 1998 and the BOJ embarked on a programmed reduction in the cash reserve ratio of the commercial banks. The programmed reduction in the cash reserve ratio will release approximately J$6.4 billion in liquidity to commercial banks over eighteen months or less and is expected to lead to further reductions in lending rates.

FINSAC continued to be very active during the year but with a view to consolidating its purchases of non-performing loans and financial sector companies that were deemed insolvent. An interesting point to note is that the FINSAC-controlled Workers Bank placed its parent company in receivership owing to its extensive exposure to the Corporate Group. Commercial banks' credit to the goods-producing sectors declined by 22.8% between January and September 1998 compared with a decline of 13.3% in the comparative period of 1997, reflecting the slowdown in financial activities resulting from the acquisition of non-performing loans by FINSAC. Credit to the service sector registered a 37.0% reduction, compared with a decline of 3.5% for the first nine months of 1997.

Tourism

During the first eleven months of 1998 total visitor arrivals fell slightly by 0.2% to 1.7 million visitors, but total stopover

GROSS DOMESTIC PRODUCT

arrivals rose by 3.1% to 1.1 million. The US continued to be a major market for Jamaica's tourism product and increased its share of stopover visitor arrivals from 61.8% in 1997 to 67.9% in 1998. The average length of stay of visitors in all types of accommodation increased from 10.4 nights to 10.7 nights during the eleven- month period, but the average length of stay in hotels fell slightly to 6.9 nights from 7 nights. Due mainly to the increase in stopover visitor arrivals, gross estimated expenditure between January and November 1998 increased to US$1.1 billion. This sector did experience real growth in 1998.

Outlook for 1999

The economy registered its third consecutive year of decline in economic activity during 1998, declining by 0.7%. Whereas growth was recorded in the output of the utilities, tele-communications, water, electricity and mining sectors, the agricultural, manufacturing, construction and the financial sectors experienced declines during 1998. Further, the increased competition from imported goods continued to add to the woes of the domestic productive entities, a development facilitated by high local interest rates and a local currency which has appreciated considerably in real terms, since the mid - 1990's.

The 1999/2000 budget has suggested that there is little likelihood of economic growth in 1999. The huge domestic borrowing that is planned will continue to crowd out the private sector and dampen private investment. Interest rates will remain high in real and nominal terms, further inhibiting private business activity. A low level of public capital expenditure will not help to expand output either. In fact, economic growth is unlikely as long as the high interest rate policy remains in place.■

3. BALANCE OF PAYMENTS

Introduction

The Balance of Payments (B.O.P.) is the record of the transactions of the residents of a country (in this case Jamaica) with the rest of the world. There are two (2) main accounts in the balance of payments: the current account and the capital and financial account. The current account records trade in goods and services, as well as transfer payments. Services include freight, royalty and interest payments. Services also include compensation to employees, net investment income, the interest and profits on our assets abroad less the income foreigners earn on assets they own in Jamaica. Transfer payments consist of remittances, gifts and grants. The trade balance simply records trade in goods. Adding trade in services and net transfers to the trade balance we arrive at the current account. The capital and financial account records capital transfers and transactions i.e. the purchases and sales of assets, such as stocks, bonds and land, investments and loan principal inflows and repayment and foreign reserves.

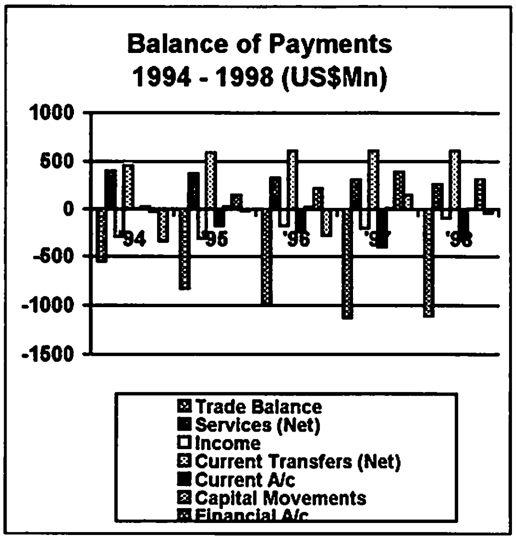
The format of the BOP report is based on the fifth edition of the IMF's Balance of Payments manual. Preliminary estimates on the BOP for 1998 compared with the revised 1997 figures are provided in Table 3.1. In contrast to the deterioration recorded in 1997, 1998 saw marked improvements in the BOP. Notably for 1998 there were the following improved performances:

- an improvement of US$18.9 Mn in the merchandise trade;
- a US$107.6Mn reduction in the income account deficit and
- a build up of US$41.5Mn in Bank of Jamaica's International Reserves.

This performance has resulted in a US$77.8 Mn improvement in the current account for 1998 which ended with a deficit of US$322.8Mn compared with the deficit of US$400.6 Mn in 1997. The reduction in the current account deficit was due in part to the substantial reduction in oil prices which took place in 1998, which affected the decline in bauxite and alumina prices. An even

BALANCE OF PAYMENTS

Figure 3.1



Merchandise Trade

For the review period January to December 1998, the merchandise trade account recorded a trade deficit of US$1,101:9Mn. This represents an improvement of US$18.9Mn compared to the corresponding period in 1997. Preliminary estimates on the BOP for 1998, compared with the revised 1997 figures are provided in Table 3.1. In contrast to the negative performance recorded in 1997 there were significant improvements in 1998. The marked improvement was largely attributed to the reduction in net exports of US$74.2Mn.

The Goods or Merchandise trade balance for 1998 consisted of exports totalling US$1,590.4Mn and imports of US$2,692.3Mn. However the outcome of 1997 revealed exports and imports of US$1,699.1Mn and US$2,819.9Mn respectively, thus both sub-accounts of 1998 declined relative to the outcome of 1997, falling by US$108.7Mn and US$127.6Mn respectively.

The greater reduction in imports relative to exports over the 1997/1998 period has therefore led to a US$18.9Mn improvement in the trade deficit from US$1,120.8Mn in 1997 to US$1,101.9Mn in 1998. The sharp reduction in the import bill is as a direct result of the decline in expenditure on raw materials (down US$75.667Mn) and Capital goods (down by US$105.99Mn) in 1998 relative to the 1997 experience. This decline is an off-shoot of what is happening in the wider economic environment, and resulted from the reduction in petroleum based imports of 28.3% in 1998 due mainly to the fall in international oil prices.

BALANCE OF PAYMENTS

The decline in capital goods imports was primarily due to the fact that two airplanes were imported into the island in 1997 but no others came in 1998. Earnings from traditional and non-traditional exports declined in 1998 when compared to the corresponding period of 1997. Traditional and non-traditional exports for 1998 amounted to US$840.6Mn and US$399.65Mn respectively compared with US$945.40Mn and US$408.18Mn in 1997. This thus represents a decline of US$104.77Mn and US$8.53Mn in both sub-accounts for the 1998 period. The significant decline in alumina earnings was spurred by a reduction in world alumina prices which took place in the latter half of 1998. The decline in earnings took place even though export volume rose slightly.

Services

On the services account, a net surplus of US$261Mn was recorded in the January - December 1998 period, which was US$46.6Mn lower than in the comparable period of 1997. The decrease in net service earnings was influenced by the travel and other services sub-accounts. Net contributions from travel declined by US$39.7Mn to US$909.8Mn, as the expansion in gross tourism receipts was counterbalanced by an increase in expenditure by Jamaicans travelling abroad. The growth in travel receipts was influenced mainly by a 4.0% improvement in arrivals of foreign national stop-over visitors. Net payments of US$367.2Mn were recorded on the other services account, US$12.7Mn lower than in the comparable period of 1997. These declines were partially offset by a US$5.8Mn compression in net payments for transportation services resulting mainly from a fall in freight charges on imports.

Income

The income account recorded a deficit of US$93.6Mn in 1998, which was significantly lower than the deficit of US$201.2Mn for the comparable period of 1997. Compensation to employees increased by US$18.2Mn while net investment income outflows were US$89.4Mn less than in the corresponding period of 1997. The investment income

BALANCE OF PAYMENTS

out-turn was due largely to the reduced profitability of foreign companies operating in Jamaica, particularly the mining companies.

Net Current Transfers

Net current transfers of US$611.7Mn were recorded in 1998, US$2.1Mn less than in the comparable period of 1997. Net inflows to the private sector grew by US$0.5Mn while those to the official sector fell by US$2.6Mn.

Current Account

For the January to December 1998 period, the current account of the balance of payments recorded a deficit of US$322.8Mn compared with the deficit of US$400.6Mn in 1997. The performance in 1998 was influenced by significant improvements in the goods and income sub-accounts, which were partially offset by marked reductions in the Services as well as Capital and Financial sub-accounts. This improved performance of 1998 as compared to 1997 is not necessarily reflective of a marked improvement in the competitiveness of the currency but is rather attributed to the developments on the international market.

Capital and Financial Account

The capital and financial account recorded net inflows of US$6.6Mn and US$316.2Mn respectively in 1998. The balance on the financial account represented a decline of US$75Mn when compared to the previous year. This decline was attributed to the official sector, which registered a net deficit of US$57.7Mn relative to the net surplus of US$43.1Mn in the previous period. The 1998 out-turn was due to an increase of US$209.7Mn in official debt payments and a reduction of US$46.2Mn in foreign borrowings. The increase in net private investments however, which rose by US$219.4Mn, was enough to cover the official investments and current account deficits. This led to a build-up of US$41.5Mn in the Net International Reserves (NIR) of the Bank of Jamaica (BOJ) compared with the draw down of US$152.1Mn in the 1997 period.

BALANCE OF PAYMENTS

1994-1998

Table 3.1

	Jan-Dec '94	Jan-Dec '95	Jan-Dec '96	Jan-Dec '97	Jan-Dec '98
Goods balance	-551.2	-829.4	-994.2	-1120.8	-1101.9
Exports	1548.0	1796.0	1721.0	1699.1	1590.4
Imports	2099.2	2625.4	2715.2	2819.9	2692.3
Services - Net	401.6	374.2	326.1	307.6	261.0
Transportation	-196.2	-246.0	-270.2	-287.4	-281.6
Foreign Travel	889.5	921.2	935.2	949.5	909.8
Other Services	-291.7	-301.0	-338.9	-354.5	-367.2
Income	-294.1	-309.5	-177.4	-201.2	-93.6
Compensation of employees	41.4	46.5	47.3	53.7	71.9
Investment Income	-335.5	-356.0	-224.7	-254.9	-165.5
Current Transfers (Net)	450.6	592.0	607.8	613.8	611.7
Private	440.7	554.8	573.9	590.8	591.3
Official	9.9	37.2	33.9	23.0	20.4
Current Account	6.9	-172.7	-237.7	-400.6	-322.8
Net Capital Movements	21.7	24.1	21.1	9.4	6.6
Private	3.5	3.6	2.4	2.4	2.4
Official	18.2	20.5	18.7	7.0	4.2
Financial A/c	-28.6	148.6	216.6	391.2	316.2
Other Official Investment	-127.4	-97.0	-144.7	43.1	-57.7
Other Private Investment	436.3	265.3	639.9	196.0	415.4
Changes in Reserves	-337.5	-19.7	-278.6	152.1	-41.5

BALANCE OF PAYMENTS

Outlook for 1999

The direction in the Balance of Payments for 1999 would be significantly influenced by the movements within the sub-accounts.

Merchandise Trade

Its outcome will depend on the direction in the prices of the major export commodities, namely alumina, as well as the extent to which recovery in output is made in traditional and non-traditional exports. This, to a large degree, will be influenced by the level of modernization within the different export sectors as well as the extent to which Asian economies recover, given the central authorities' stabilization attempt in the foreign exchange market.

The volume of imports is expected to be restricted given tight liquidity management by both households and government alike. In addition, the upward trend in world oil prices will impact negatively on the value of imports. As such, a slight contraction in the volume of imports is expected, and a similar movement in the value of exports is expected.

Services and Net Transfers

Tourism earnings is expected to remain flat while the level of transfers is expected to remain high given the relative buoyancy of the US and UK economies.

Current Account

Movement in this account will be greatly influenced by the extent of the imbalance in the Merchandise Trade. For 1998 it was the improvement in the income sub-account which significantly created an improvement in the Balance of Payment for the period January to December 1998. Whether or not this trend (that is, the reduction in the repatriation of profits) will continue for 1999 is highly dependent on the level of restructuring of companies, namely those in the mining industry.

Capital & Financial Account

Private investment inflows will be affected by the extent to which interest rate falls. A significant reduction in interest rates would shift portfolio balances highly weighted toward foreign currency. With

BALANCE OF PAYMENTS

With the government's continuation in the quarterly reduction of the cash reserve ratio, the expectation for 1999 with respect to interest rate reduction could mimic the trend achieved for the latter part of 1998. This, as a result, could see the Net International Reserves moving marginally downwards. This could have implications for the ability of the government to borrow US$400Mn on the international capital market, as well as the maintenance of a stable J$/US$ exchange rate.■

4. EXTERNAL TRADE

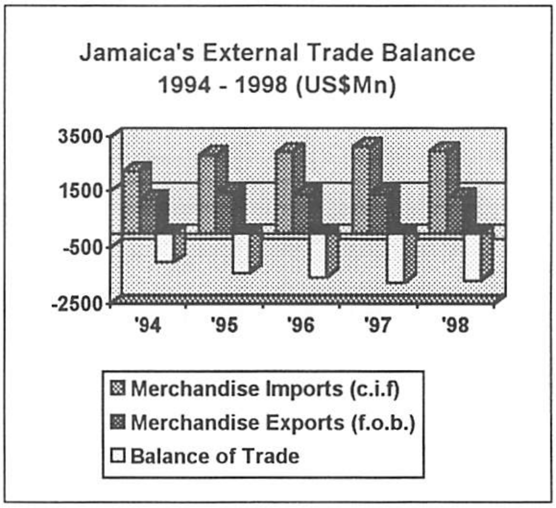
Introduction

There was an improvement in the balance of trade in goods and services in 1998. The trade deficit was reduced by US$56.6Mn or 3.3% relative to the out-turn of 1997. This was the result of greater reduction in the value of imports relative to exports.

The narrowing in the merchandise trade deficit was due to a 4.9% reduction in the value of imports to US$2,960.64Mn. Consumer Goods was the only category of imports showing an increase. Imports of items to be used as Raw Materials/Intermediate Goods and Capital Goods fell by 4.8% and 16.1% respectively, reflecting the general down-turn in economic output.

Earnings from exports in 1998 fell by US$95.8Mn or 6.9% compared to the similar period in 1997. All categories of exports declined in 1998 relative to 1997: Major Traditional, Other Traditional, Non-Traditional and Domestic Exports. In general, drought and high interest rates were a major contributing factor to the increase in food imports, as well as the decline in exports.

Figure 4.1



Exports

For the review period January to December 1998, total exports (f.o.b) were valued at US$1,290.34Mn, a reduction of US$95.79Mn relative to the outcome of the corresponding period in 1997. Of this total amount, US$1,240.28Mn accounted for domestic exports while the remaining US$50.06Mn came from re-exports.

Contributing to the decline in total exports were reductions of US$87.92Mn, US$16.85MN and US$8.53Mn in major traditional, other traditional and non-traditional exports respectively.

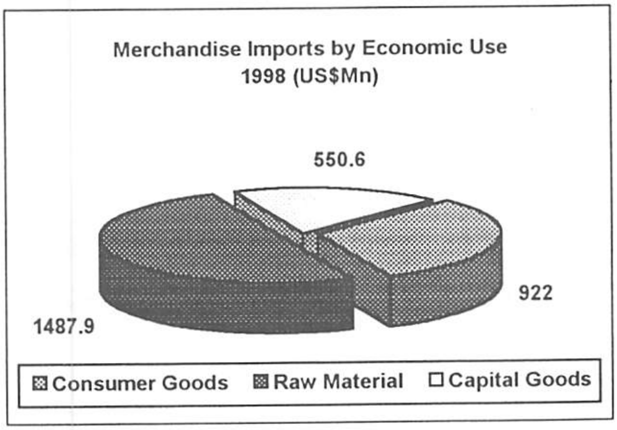
EXTERNAL TRADE

These were marginally counteracted by an increase of US$17.51Mn in re-exports. The reduction in the major traditional group continues to reflect mainly the effect of depressed international prices on the value of alumina exports. During the review period, earnings from alumina dropped by US$76.37Mn despite an increase in export volume. Earnings from sugar and banana exports were also lower than in the 1997 period, falling by US$7.3Mn and US$12.48Mn respectively. This stemmed from decline in both the average price and export volume. A decrease of US$17.28Mn in earnings from coffee was responsible for the reduction in the value of other traditional exports which marginally offsetting increases in cocoa, pimento and gypsum. Crude Material exports, which declined by US$73.91Mn or 10% in the 1998 period, were largely accountable for the decline in the non-traditional category. A US$20.11Mn increase in export earnings from beverages and tobacco was the main countervailing influence.

Imports

Total imports (c.i.f.) for the January to December 1998 review period stood at US$2,960.64Mn, a US$152.4Mn reduction compared to the outcome in 1997. The US$152.4Mn reduction in imports was strongly influenced by the decline in raw materials of US$75.7Mn and capital goods of US$105.9Mn. The raw materials import category continues to be influenced by the decline in fuel prices on the international market, while the capital goods import category continues to be influenced by the reduction in Transport and Equipment.

Figure 4.2



Consumer goods, however, were up US$29.2Mn mainly through increases in food and other non-durables, albeit a contraction in motor vehicle imports.

EXTERNAL TRADE

During 1998 motor vehicle imports, as it relates to consumer goods, were US$31.21Mn lower than for the comparable period in 1997. A major contributor to the increased importation in food and non-durables could be the lower commodity prices in the international market.

Caricom Trade

In 1998 imports from CARICOM were valued at US$310.9Mn while US$47.7Mn were earned from total exports. The major items imported from CARICOM include Food, Minerals, Fuels and Lubricants. Food and chemicals were the main items exported. At the end of the 1998 period the trade deficit stood at US$265.2Mn, down from US$270.3Mn in the 1997 period.

Outlook for 1999

Exports

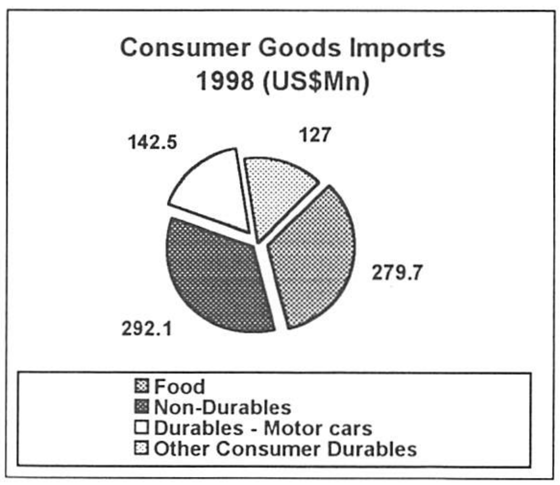
The outlook for 1999 is expected to follow the similar declining trend for 1998. The extent to which exports are likely to improve in the short to medium term will depend strongly on the level of added human capital and technology made to the respective export driven sectors. The problems that the industry faces are as follows:

(i) extended periods of drought

(ii) high interest rates, and

(iii) the likely removal of preferential arrangement on bananas with the increased competitiveness of our South, Central and Latin American counterparts.

Figure 4.3



EXTERNAL TRADE

Table 4.1 External Sector US$Mn

	Jan-Dec 97	Jan-Dec 98
Total Exports (F.O.B.)	**1386.20**	**1290.30**
Major Traditional Exports	**872.20**	**784.20**
Bauxite	72.80	81.00
Alumina	651.70	575.30
Sugar	101.90	94.60
Bananas	45.80	33.30
Other Trad. Exports	**73.20**	**56.40**
Non-Trad. Exports	**408.20**	**399.60**
Re-Exports	**32.60**	**50.10**
Total Imports (C.I.F)	**3113.00**	**2960.60**
Trade Balance	**-1726.80**	**-1670.30**

Alumina and bauxite could see marginal improvements in export earnings if international prices improve. Sugar and bananas are likely to decline given the likely level of restructuring necessary to re-engineer growth. The movement in non-traditional exports will be influenced by government's policy directed toward the given sector.

Imports

Given the restrictive monetary policy adopted by the government, consumption borrowing will be discouraged thus reducing the demand for consumer durables. However, given the negative external shock to world oil prices, commodity prices are likely to increase. As such, the movement in the import bill will depend on the level of the trade off between import value and volume.

Of equal significance to the reduction in imports is the extent to which our infant industries develop and become more competitive, amidst a growing atmosphere of increased international competition. Although government has recently decided to ban all imports of meat, the poultry, agriculture, dairy industries are at a competitive disadvantage due in no small part to domestic economic policy.■

5. MONEY AND BANKING

Base Money

Base money declined by 0.8% during 1998. This indicates increased tightening of the financial system and compares well with the increase of 13.3% registered for 1997. Base money management continues to be the focus of the BOJ's monetary policy and the main tool by which it controls money supply growth.

Currency issue increased from J$14.2 billion to J$15.24 billion between the end of December 1997 and the end of December 1998, an increase of 7.3%. This is an improvement over the increase of 14.9% recorded during 1997. Commercial Banks' Accounts declined from J$19.92 billion at the end of December 1997 to J$18.23 billion at the end of December 1998, an 8.5% fall. This decline was primarily due to a reduction of the cash reserve ratio - the share of deposits which the banks are required to maintain in non-interest bearing accounts at the BOJ.

Money Supply

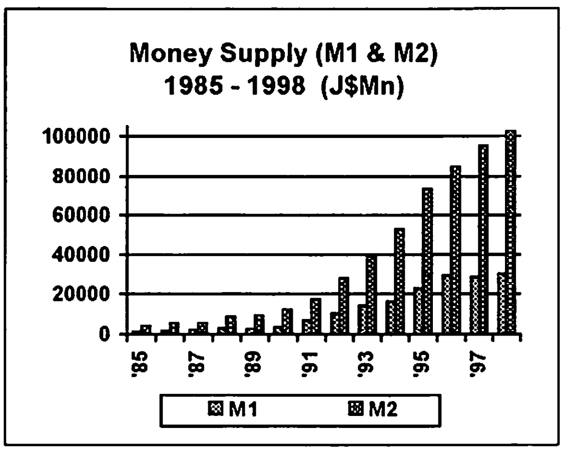
The nominal stock of broad money (M2) increased from J$95.60 billion at the end of December 1997 to J$102.63 billion at the end of December 1998. This increase of 7.3% over the 1997 stock, indicates a slowdown in money supply growth from the 13.6% increase recorded in 1997, and resulted primarily from the slight contraction in the monetary base. Narrow money (M1) increased by 5.8% to J$30.27 billion at the end of 1998. Whereas the "currency with the public" component of M1 increased by 8.5% to J$13.49 billion, the "demand deposits" component increased by 3.7% to J$16.78 billion. "Quasi money" increased from J$66.98 billion at the end of 1997 to J$72.36 billion at the end of 1998, an increase of 8.0% which is greater than the rate of increase of M1 and M2. Time and savings deposits increased by 19.1% and 4.4% to J$19.60 billion and J$52.76 billion respectively.

MONEY AND BANKING

Table 5.1 Money Supply: 1985 – 1998 (J$Million)

YEAR	M1	TIME DEPOSITS	SAVINGS DEPOSITS	QUASI MONEY	M2
1985	1210.4	1091.7	2007.5	3009.2	4309.6
1986	1667.6	1183.3	2646.8	3830.1	5497.7
1987	1874.8	1119.4	2646.6	3766.2	5641.0
1988	2908.8	1625.5	4365.8	5991.3	8900.1
1989	2739.4	1843.5	4882.7	6726.2	9465.6
1990	3516.0	2281.8	5499.0	7780.8	11296.8
1991	6867.1	2464.2	8135.2	10599.4	17466.5
1992	10283.6	4409.8	13124.0	17533.8	27817.4
1993	14398.7	6340.5	18179.6	24520.1	38918.8
1994	16374.0	12042.8	24733.2	36776.0	53150.0
1995	23227.7	15839.7	34550.2	50389.9	73617.6
1996	29166.5	17204.3	38576.7	55781.0	84947.5
1997	28623.8	16453.7	50527.1	66980.8	95604.6
1998	30273.5	19599.9	52755.5	72355.4	102628.9

Figure 5.1



Credit to the public sector more than doubled, increasing from J$41.33 billion at end of 1997 to J$85.23 billion at year end, while credit to the private sector declined by 17.5% from J$42.16 billion to J$34.79 billion over the same period.

This indicates an increasing and drastic crowding out of private sector credit by the public and points to the serious imbalance in public finances.

Loans and Advances

The total assets at commercial banks stood at J$164.03 billion at the end of November 1998 compared to J$143.60 billion at the end of the corresponding period in 1997 and J$148.34 billion at the end of December 1997. Thus total assets at commercial banks increased by 14.2% between November 1997 and November 1998, and by 10.6% over the eleven

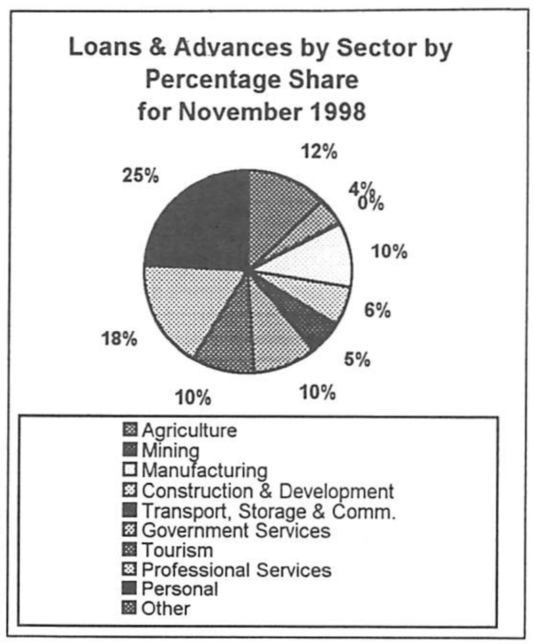
MONEY AND BANKING

months ending November 1998. Loans and advances accounted for J$55.24 billion (38.5%), J$59.00 billion (39.8%) and J$43.69 billion (26.6%) of total assets at the end of November 1997, December 1997 and November 1998 respectively. Thus, both the value of credit by the commercial banking system and the percentage of assets extended as credit at November 1998 declined over those for November 1997 and December 1997.

Total deposits with commercial banks increased from J$108.56 billion at the end of November 1997 and J$109.31 billion at the end of December 1997 to J$116.07 billion at the end of November 1998. Thus, loans and advances as a percentage of total deposits declined from 50.9% at November 1997 and 54.0% at December 1997 to 37.6% at November 1998. This goes to show the continued contraction in lending activities and the extent of the problem is underscored by the fact that loans and advances have declined for the period under review, despite a growth in deposits.

Personal loans continued to dominate the loan portfolio of the commercial banking system and increased from 20.2% of loans at the end of November 1997 to 24.2% at the end of November 1998. Loans for professional and other services also increased their share and relative importance and they moved from 11.9% to 17.3% over the same period. They ranked second at the end of November 1998 as opposed to third for the corresponding period of 1997. Loans to manufacturing, government, tourism, and construction accounted for 10.2%, 10.0%, 9.8% and 6.0% respectively at the end of November 1998. Table 5.2 gives further details on the allocation of loans on advances.

Figure 5.2



MONEY AND BANKING

Table 5.2 **Loans & Advances by Sector**

Sectors	Nov. 1997	Share (%)	Nov. 1998	Share (%)
Agriculture	2524.90	4.5	1964.62	4.5
Mining	198.92	0.4	146.23	0.3
Manufacturing	5808.90	10.5	4466.10	10.2
Construction & Development	3649.02	6.6	2615.83	6.0
Transport, Storage & Comm.	3840.86	7.0	2321.73	5.3
Government Services	7061.43	12.8	4379.86	10.0
Tourism	4292.56	7.8	4259.46	9.8
Professional Services	6590.19	11.9	7557.75	17.3
Personal	11168.55	20.2	10576.12	24.2
Other	10106.53	18.3	5404.79	12.4
Total	**55241.86**	**100.0**	**43692.49**	**100.0**

Commercial Banks' Liquidity

Commercial banks started the year with the 47% statutory reserve ratio that has been in effect since June 1995. This high reserve ratio has resulted in high real lending rates and a relatively wide spread between deposit and lending rates. As a move to increase liquidity and accelerate the reduction in commercial banks lending rates, the central bank has embarked on a gradual reduction in the legal reserves. This move is intended to result in the cash reserve ratio declining by about 8% over nine to eighteen months, with an initial 2% reduction at the beginning of August 1998 and at least a 1% reduction per quarter thereafter. So far, the ratio declined to 45% at the beginning of August 1998 and then to 43% at the beginning of November 1998. It was reduced to 41% at the beginning of February 1999.

The reduction in the cash reserve ratio from 25% to 21% has resulted in increased liquidity. However, the conversion of the excess liquidity to loans has been slow, as the actual liquidity ratio of commercial banks has declined slightly from 50.6% at the end of 1997 to 50.1% at the end of 1998. Thus, excess liquidity has increased from 3.6% at the end of 1997 to 7.1% at the end of 1998, a reversal of the contraction in excess liquidity recorded for 1997. The essential difference between the position at the end of 1998 and that at the end of 1997 is that the increase in liquidity was caused mainly by the reduction in the cash reserve ratio. The apparent excess liquidity of

MONEY AND BANKING

commercial banks masks the severe liquidity problems which some institutions are experiencing as the BOJ has been counting institutions' holdings of repos as part of their statutory reserves and the cash surpluses of some institutions are concealing the shortages in others.

Interest Rates

The yield on Treasury Bill rates declined during 1998, falling from 30.17% in January to 23.52% in December. This rate is still relatively high when compared to the inflation rate of 7.9% and continues to encourage investment in government paper at the expense of investment in the real sector. The reduction was due to a gradual reduction in the BOJ's Repo rate from 29% in December 1997 to 22% in December 1998.

Weighted average lending rates at commercial banks fell from 34.96% at December 1997 to 32.98% at December 1998, while weighted deposits rates increased from 14.06% to 15.54% over the same period. This signifies a reduction in the spread from 20.9% to 17.44% and came in the second half of the year in response to the increase in liquidity caused by the reduction in the cash reserve ratio. As the rate of inflation declined form 9.2% in 1997 to 7.9% in 1998, real lending and deposit rates moved from 25.76% and 4.86% to 25.08% and 7.64% respectively. Table 5.3 gives details on lending and deposits rates on a quarterly basis.

Table 5.3 **Commercial Banks' Loan and Deposit Rates, 1996 - 1998**

Rates	1996				1997				1998			
	Q1	Q2	Q3	Q4	Q1	Q2	Q3	Q4	Q1	Q2	Q3	Q4
Installment Credit	59.66	62.46	58.03	64.09	57.53	57.18	56.65	56.65	56.12	55.71	55.81	54.87
Mortgage Credit	25.47	26.75	25.51	21.45	10.48	14.74	14.74	10.46	10.43	10.42	10.43	10.40
Personal Credit	49.53	50.75	50.62	47.86	43.35	39.58	38.08	38.20	36.62	35.49	34.64	33.87
Commercial Credit	40.97	40.05	39.77	37.11	31.94	35.01	33.01	33.63	33.72	34.35	31.42	30.39
Local Govt. & Pub. Entities	14.77	15.06	15.00	14.21	14.65	15.89	15.85	21.75	22.65	22.64	19.82	19.09
Central Govt.	28.73	30.76	38.58	38.78	35.86	20.65	19.53	18.30	15.46	28.92	22.33	26.52
Avg. Weighted Loan Rate	43.86	44.23	42.74	42.16	36.09	37.54	35.02	34.96	35.23	36.28	33.72	32.98
Avg. Weighted Deposit Rate	26.14	26.04	23.73	20.79	15.47	12.46	11.80	14.06	17.04	17.70	13.56	15.54
Avg. Lending Rate	58.27	59.95	58.50	55.22	47.92	44.95	44.22	44.17	44.17	43.67	40.33	38.80

MONEY AND BANKING

Stock Market Developments

Stock market activities intensified during the middle of the year and the index increased from 19,846.67 at the close of December 1997 to 25,331.51 at the close of July 1998. The index then trended downwards to the monthly low of 18,940.89 at the close of November and then rose to 20,593.32 at the end of 1998. The rise in the value of the index was triggered to a large extent by movements in the value of a few stocks with a very large market capitalization. Thus, the index increased by 5.7% between December 1997 and December 1998 and exhibited more volatile movement during 1998 than in 1997.

Both the volume and value of shares traded fell, declining from 905.42 million units valued at J$4,594.42 million traded in 1997 to 604.55 million units valued at J$2,064.24 million in 1998. Thus, the average value of units traded declined from J$5.07 in 1997 to J$3.41 in 1998 due to the 33.2% and 55.1% decline in volume and value. This signals a slowdown in stock market activity and might have resulted from diminishing investor confidence. The continuing fall-out in the financial sector and the continuing contraction in economic activity would have affected this in turn. Table 5.4 gives the value and volume trade and the index value between 1989 and 1998.

Figure 5.3

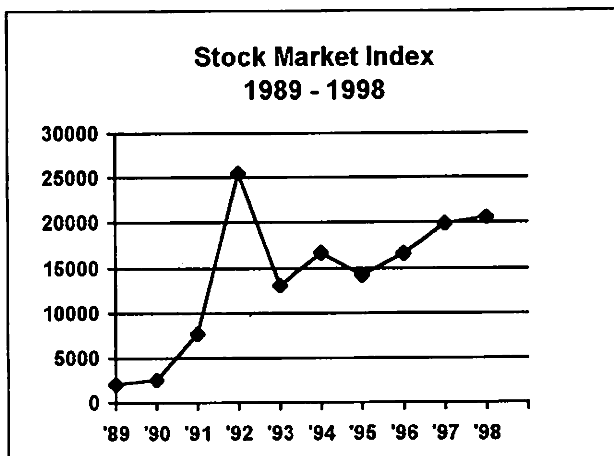


Table 5.4 **Stock Exchange Index, 1989 - 1998**

Year	Volume	Value (J$)	Index
1989	95.202.452	516.456.318	2,075.85
1990	57.960.234	230.781.846	2,539.36
1991	144.259.019	1.156.608.055	7,681.50
1992	395.900.000	4.688.400.000	25,475.90
1993	567.454.280	8.346.769.977	13,099.68
1994	741.754.077	5.155.463.519	16,676.74
1995	3.565.612.318	11.560.535.279	14,266.99
1996	560.528.182	4.629.395.414	16,615.99
1997	905.418.910	4.594.418.367	19,846.67
1998	604.545.158	2.064.243.797	20,593.32

MONEY AND BANKING

Foreign Exchange Developments

Deposits into foreign currency accounts declined by 2.1% from US$7,581.11 million in 1997, while withdrawals from these accounts increased by 1.4% from US$7,151.41 million. Despite the increase in withdrawals and the reduction in deposits, total amounts deposited to these accounts continued to be higher than withdrawals as deposits and withdrawals during 1998 amounted to US$7,418.41 million and US$7,251.59 million respectively. Thus, there was a continuing build up in foreign currency accounts.

Foreign currency accounts at commercial banks, building societies and merchant banks amounted to US$1,036.72 million at the end of December 1998, an increase of 1.6% over the amount of US$1,020.46 million at the end of 1997. The relative share deposited with these institutions shifted slightly with commercial banks accounting for 79.7% at the end of 1998, a marginal increase over the 79.2% at the end of 1997. Whereas building societies marginally increased their share from 17.5% at the end of 1997 to 17.6% at the end of 1998, merchant banks registered a marginal decline from 2.8% to 2.7% over the same period.

The nominal value of the domestic currency remained relatively stable and fluctuated between exchange rates of J$36.28 for US$1.00 and J$37.45 for US$1.00. Thus, at the end of the year, the exchange rate was J$37.16 for US$1.00 compared with J$36.59 for US$1.00 for the previous year and J$35.03 for US$1.00 for 1996. However, towards the end of the year pressure on the Jamaican dollar began to rise as government's failure to raise its budgeted borrowing on the international capital market led to a relative shortage of foreign exchange in the local market. The Bank of Jamaica did not intervene in the foreign exchange market as regularly as in 1997, allowing some slippage in the exchange rate.

The Financial Sector

The problems within the financial sector continued in 1998 and the government continued to intervene in an attempt to avert a total collapse of the sector. In January 1998, the Minister of Finance and Planning, through FINSAC, assumed

MONEY AND BANKING

temporary control of Caldon Finance Merchant Bank, Workers Savings & Loans Bank, Corporate Merchant Bank and Capital Assurance Building Society. Thus, the problems associated with the financial sector were originally underestimated, as the government has now rendered assistance to the majority of banking entities.

During the year the government also took greater control of Dyoll Life Insurance, Mutual Life and Eagle Insurance, as these entities fell into deeper financial trouble. Talks ensued about merging these entities just as the government was proceeding with the merger of four FINSAC controlled banks, Workers Saving & Loan Bank, Citizens Bank, Horizon Merchant Bank and Eagle Commercial Bank, to form the Union Bank.

The FINSAC intervention has cost approximately $88 billion so far, up from the $55 billion reported at the end of 1997. This will impact on the 1999/2000 fiscal budget to the tune of at least $8 billion as the interest cost is estimated to be in excess of $16 billion per annum. NCB has been the major beneficiary of the FINSAC intervention as they have received some $19.5 billion worth of assistance during February 1998.

At the beginning of the second half of the year two new primary dealers, Sigma Investment Management Systems Limited and George & Brandy Limited, were appointed. Horizon Merchant Bank ceased trading, thus the number of primary dealers increased to fourteen.

Outlook for 1999

There will be many challenges facing the financial sector during 1999 as the size of the bad loan portfolio has increased and clients have become insolvent due to high interest costs. The government has announced its resolve to reduce the public sector deficit to 4.6% of GDP in the coming budget. If this resolve is carried through, it will serve to free up resources for private sector investment. However, there is cause for concern as this is a mammoth task that might demand increased taxation. The pending move by the government to tax interest on securities at source is an indication that

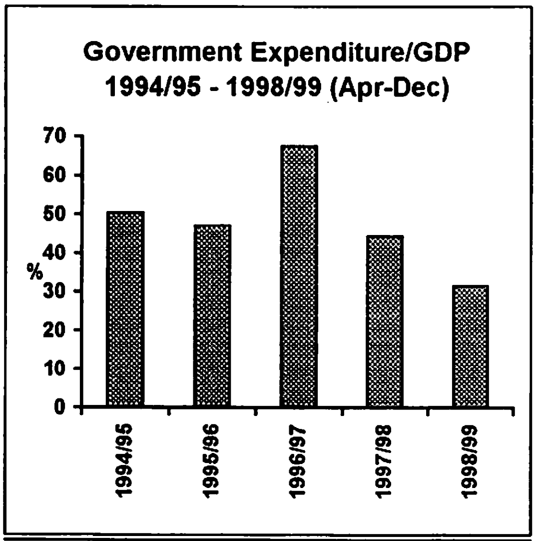
MONEY AND BANKING

the government will be tightening its tax system. The move to increase liquidity by reducing the cash reserve ratio will impact positively on the financial sector and should accelerate a reduction in lending rates. Nonetheless, FINSAC will no doubt become a strain on the budget and could account for in excess of J$8 billion of the 1999/2000 budget. Given that NCB, the largest commercial bank, is not lending due to its large portfolio of non-performing loans and the possibility of government continuing to crowd out investment, the sector will face a major challenge as it struggles to return to growth in 1999.■

6. FISCAL POLICY

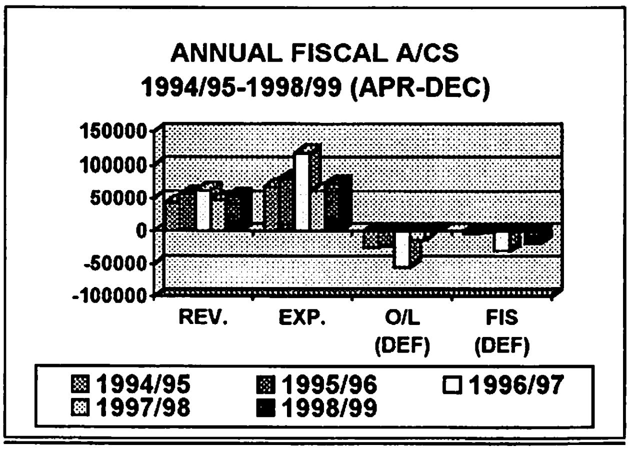
The 1998/99 J$130.092 billion fiscal budget was presented in April 1998. This $130.092 billion budget represents increases of 22.1% and 13.1% over the original and revised estimates respectively for 1997/98, reflecting a significant real increase in government consumption. FINSAC costs did not come directly onto the budget in 1998/99. With this huge increase in expenditure, the government has increased its share of GDP from the 52% projected for the 1997/98 fiscal year (FY) to about 60% for FY 1998/99.

Figure 6.1



The budget projected recurrent expenditure at $85.079 billion, 65.4% of estimated expenditure for the 1998/99 fiscal year, compared with original estimates of $65.251 billion and revised estimates of $71.657 billion for the previous year represented increases of 30.4% and 18.7% respectively on original and revised expenditure for 1997/98. Interest payment amounted to $34.437 billion or 40.5% of projected recurrent expenditure, compared to $21.670 billion or 33.2% and $24.250 billion or 33.8% of original and revised recurrent expenditure respectively for the 1997/98 fiscal year. The increase in recurrent expenditure as a share of overall expenditure (65% in 1998/99 versus 62% in 1997/98) has been strongly influenced by the sharp increase in interest payments. This has resulted from the increase in domestic borrowing and the very high real rates of interest, which are paid on these loans.

Figure 6.2



FISCAL POLICY

Capital expenditure accounted for $45.013 billion or 34.6% of expenditure estimates for 1998/99 compared to estimates and revised estimates of $41.332 billion and $43.394 billion or 38.8% and 37.7% of total expenditure for the previous year respectively. This reduction in the share of capital expenditure will impact the government's ability to improve or expand infrastructure and brings into question the government's commitment to accelerating the pace of capital formation.

Fiscal Accounts And The Budget

The fiscal performance was mixed. The following points highlight the main points of fiscal performance during 1998:

- Preliminary data from the Ministry of Finance for the nine months to December 1998 indicates that Revenue and grants increased by 12.5% over the same period in 1997 to J$54.593 billion, but was 12.1% below the budgeted revenue of J$62.122 billion. This outcome can be attributed to the 14.4% growth in tax revenue and the 10.5% increase in capital revenue, as non-tax revenue, bauxite levy and grants declined by 1.0%, 2.3% and 16.9% respectively. After the budget was tabled, a number of commentators expressed the view that the revenue projections were too ambitious and could not be realized in an environment of falling inflation and declining output. This has indeed turned out to be the case.

Table 6.1

Annual Fiscal Accounts 1995/96 - 1998/99 (J$Millions)

	95/96	%GDP	96/97	%GDP	97/98	% GDP	Apr-Dec 98/99	% GDP
Revenue	58,081.56	34.2	63,100.2	36	48,261.5	23.55	54588.5	23.55
Expenditure	81,341.06	47	118368.1	67.4	90,625.9	44.21	73080.9	31.53
Overall Deficit/Surplus	-23,259.5	13.7	-55267..9	31.5	-19,629.4	9.58	1009.9	0.44
GDP = (J$Mn)	169,652.2		175500		204,982		231778.7	
Fiscal Deficit/Surplus	-1,760.19	1.04	-31192.2	17.77	6,074.8	2.96	-18492.4	-7.98

FISCAL POLICY

- Preliminary data indicates that total expenditure between April and December 1998 increased by 5.8% to J$73.081 billion and was 1.8% below the budgeted amount of J$74.404 billion. The rate of increase is in line with the rate of inflation and therefore indicates that the government is trying to contain real increases in its expenditure. The containment of expenditure was due mainly to a 36.0% decline in capital expenditure, as recurrent expenditure increased by 2.9% owing primarily to a 10.8% increase in programmes.

- Preliminary data for the first nine months of the 1998/99 fiscal year indicates that the fiscal deficit declined by 9.9% to J$18.488 billion, but was 50.5% above the budgeted deficit of J$12.282 billion. Unless there is a dramatic recovery in the revenue inflows in the last quarter of the fiscal year, the fiscal deficit will be in the range of 9-11% of GDP, slightly higher than was the case last fiscal year.

Figure 6.3

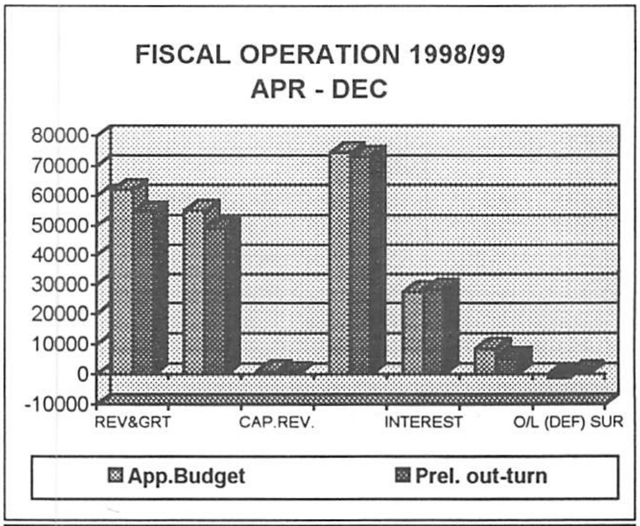


Table 6.2 provides summary information on fiscal operations for the first nine months of 1998/99 and its comparative period. Note should be taken that the figures provided are preliminary and may be revised when the financial year comes to an end and a complete audit of expenditure and revenue is undertaken.

FISCAL POLICY

Table 6.2 Summary of Fiscal Operations 1998/99 (J$M)

	Actual Apr-Dec 1997/98	Approved Budget Apr-Dec 1998/99	Preliminary Apr-Dec 1998/99
Revenue & Grants	**48,548.4**	**62,121.6**	**54,592.8**
Tax Revenue	42,926.0	55,086.0	49,099.6
Non-Tax Revenue	2,369.5	2,666.5	2,345.3
Bauxite Levy	2,189.0	2,331.3	2,139.0
Capital Revenue	455.9	1,122.9	503.6
Grants	608.0	914.9	505.3
Expenditure	**69,075.6**	**74,404.4**	**73,080.9**
Recurrent Expenditure	**55,827.9**	**65,492.8**	**67,423.1**
Interest	19,269.8	27,465.8	28,340.7
Capital Expenditure	**9,787.7**	**8,427.9**	**5,397.6**
Amortization	22,739.5	27,723.5	26,595.3
Overall Surplus/(Deficit)	**-7229.9**	**-1,328.2**	**1,014.1**
Fiscal Surplus/(Deficit)	**-20,527.2**	**-12,282.4**	**-18,488.1**

The 1998/99 budget was contingent on an expansion of the tax revenue base by virtue of improving compliance. Due to the economic downturn and falling profits in several sectors of the business community, tax revenue was 10.9% below the budgeted amount of J$55.086 billion. Similarly, collections of non-tax revenue, capital revenue and grants were 12.0%, 55.2% and 44.8% below the projected amounts.

Interest expenditure on the domestic debt at $23.833 billion, was 55.5% above the $15.327 billion recorded for the comparative period of 1997/98, while interest on the foreign debt increased by 14.2% from J$3.943 billion to J$4.503 billion. Further, interest on domestic debt was 4.7% above the budgeted J$22.778 billion, compared to interest on foreign debt being 3.9% below the budgeted amount of $4.688 billion for the period April to December 1998. The higher than expected interest on domestic debt was due to the higher than programmed domestic borrowings and higher than programmed domestic interest rates, while the lower than expected interest expense on the foreign debt was due to the reduced

FISCAL POLICY

amount obtained from the international capital markets as well as the general reduction in international interest rates.

Total loan receipts during the nine months stood at J$46.098 billion compared to J$36.037 billion for the corresponding period of 1997, an increase of 27.9%. While external loan receipts for the same period increased by 3.5% to J$11.436 billion, they were still below the budgeted amount. Domestic loan receipts increased by 38.7% to J$34.661 billion to make up for the lower than expected external loan receipts and the lower collections from tax revenue and grants. Thus, external loan receipts were 37.4% or J$6.837 billion below projection and domestic loan receipts were 69.9% or J$14.257 billion above projection. This indicates an increase in the crowding out of private sector borrowing by the government and might very well be a major reason for continuing contraction in the economy.

Amortization was 4.1% below the target of J$27.723 billion due to the amortization of domestic debt being 7.7% below the target of J$16.031 billion. Whereas the amortization of domestic debt decreased by 5.2% from $15.597 billion between April and December 1997, total amortization and the amortization of external debt increased by 17.0% and 65.2% respectively.

Outlook for 1999

Indications are that the fiscal results for 1998/99 will reveal a large deficit and will result in an increase in the stock of government debt and the continued crowding-out of private sector investments by keeping domestic interest rates relatively high. The budget for fiscal year April 1999 to March 2000 indicates that the government intends to spend J$160 billion but government plans that the fiscal deficit will be reduced to 4.5% of GDP. This will be quite a challenging target, as there are questions surrounding the sources of revenue which can be used to finance the 1999/2000 budget. Increased taxes are likely but they may not be large enough to bring about the reduction in the deficit which has been programmed.

FISCAL POLICY

Despite the difficulty of curbing government spending the government will have to contain costs, reduce public sector waste and increase compliance in order to maintain a fiscal deficit within 4.5% of GDP. This is critical, as any move to add new taxes or increase existing tax rates may lead to less compliance and social unrest.

Given an anticipated budget deficit of between 9-11% of GDP at the end of fiscal 1998/99, the failure to raise funds on the international capital market and an allocation of approximately J$8.0 billion from the 1999/2000 budget for FINSAC costs, the government's targeted fiscal deficit is unlikely to materialize. Further, the budgeted expenditure for 1999/2000 will not be less than J$160 billion. This budget will lead to further crowding out of investment activity and the possibility of yet another year of economic contraction.■

7. INFLATION

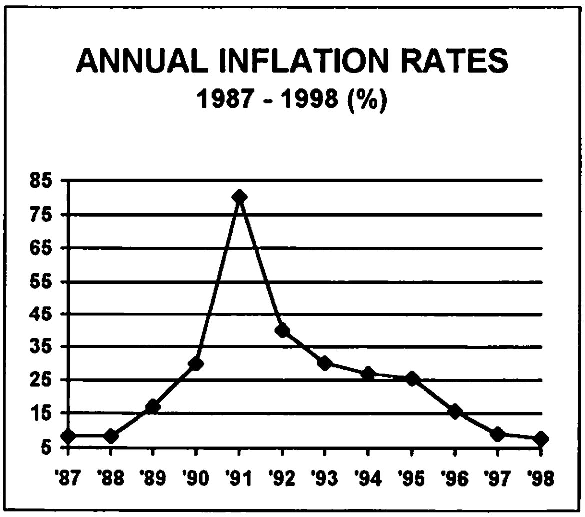
Introduction

Inflation represents the persistent or sustained rise in the price level. It is this definition of inflation that Milton Friedman and other noted economists use when they make statements such as "inflation is always and everywhere a monetary phenomenon". A measure of such a change is the Consumer Price Index (CPI), used to reflect the representative basket of goods through which changes in the price level are ascertained. For 1998 the inflation rate stood at 7.9%, a continuance of the downward trend from 15.8% in 1996 and 9.2% in 1997.

The key economic variable through which inflation responds is the monetary base and hence the Bank of Jamaica's handling of its the monetary policy directly impacts on the level of inflation in the economy. From 1996 to 1998 the nominal measure of monetary base expanded by 12.43%, with a 13.3% expansion between 1996 and 1997 counterbalanced by a 0.8% contraction between 1997 and 1998.

Jamaica's inflation rate of 7.9% represents the lowest recorded in over a decade (see Figure 7.1). Although commendable there still exists a marked differential in rates between ourselves and our trading partners. The consumer prices provided by the IMF shows that in 1998 the level of inflation in the United States, Canada and the United Kingdom stood at 1.6%, 13% and 2.8 % respectively. However, for the less advanced economies such as the Dominican Republic, Barbados and Trinidad & Tobago the inflation rates, as reported by their central banks, stood at 5%, 1.53% and 6.52% (November 1998) respectively.

Figure 7.1



INFLATION

Inflation trends for 1998

For the fiscal year 1998/99, the Government of Jamaica projected an inflation rate of 6-8% with the monthly target set at 0.7%. In 1998, October recorded the lowest level of inflation of -0.3%, compared with June's outcome of 1.8%, the highest for the year. Half as many months registered inflation rates outside of government's projected 0.7%, as compared to those that fell within the projected range, (see Table 7.1).

Table 7.1

Months	Inflation Rate/(%)	Variance
Jan.	0.7	(0.0)
Feb.	0.1	(-0.6)
Mar.*	0.8	(-0.2)
Apr.	0.4	(-0.3)
May*	0.8	(0.1)
Jun.*	1.8	(1.1)
Jul.*	1.1	(0.4)
Aug.*	1.0	(0.3)
Sep.	0.1	(-0.6)
Oct.	-0.3	(-1.0)
Nov.	0.1	(-0.6)
Dec.*	1.0	(0.3)

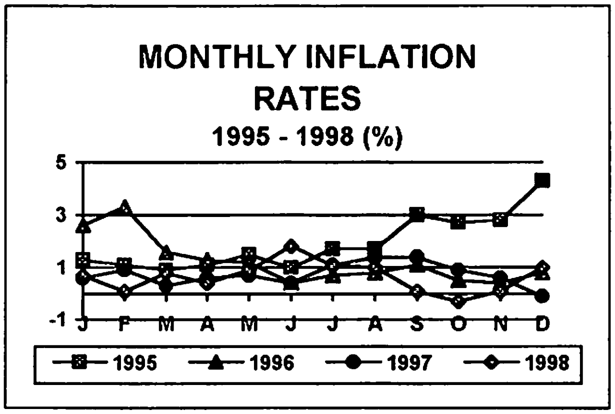
* *Months falling outside of Government's projected inflation rate of 0.7%.*
Base Period January 1998 = 100

The average inflation rate for the four quarters of 1998 stood as follows:

Qtr. 1. - 0.53%
Qtr. 2. - 1.00%
Qtr. 3. - 0.73%
Qtr. 4. - 0.27%

The high mean inflation rate recorded for the second quarter of 1998 was influenced strongly by an increase in the tax levied on each litre of gasoline, as well as tax incentives contained in the 1998/99 budget. This one shot increase affected prices mainly through increased transportation cost. With no further internal or external price shock the average inflation rate per quarter thereafter trended downwards.

Figure 7.2



INFLATION

Factors: Internal and External

The lower level of inflation and expectations thereof were influenced by factors both domestic and external to the Jamaican economy.

Domestic Factors

1. Contraction in the rate of growth of money supply and thus the monetary base growth rate in 1998 as compared to prior periods of the 90's.
2. The financing of the fiscal deficit, which took the form of both local and foreign borrowing through the issue of bonds. This restrained liquidity growth, reduced consumption and investment expenditure (at least in the short term) and as a consequence lowered the overall demand in the economy.
3. The high interest rates (nominal and real), which resulted from the aggressive open market operations of the Bank of Jamaica, also reduced the demand for money balances by private agents, including investors. This had the effect of tempering overall demand in the local economy.
4. The condition in the labour market was characterised by frequent job losses notably in the bauxite, sugar, bananas, manufacturing and poultry industries as well as the financial sector. This created a heightened atmosphere of job insecurity, with a resultant shift in resources weighted more towards earning assets such as savings accounts with commercial banks and credit unions as well as the procurement of short to medium term investment portfolios. This thus depressed the demand for items included in the basket of goods used to represent the CPI.
5. Government's firm commitment to grant wage increases to the extent of the inflationary outlook of the economy, i.e. to grant wages comparable to the inflation rate. This served to lower the demand pull component of inflation.

External Factors

1. World commodity prices for 1998, e.g. oil, have remained very weak and non-fuel commodity prices have weakened further relative to 1997. This positive supply shock has resulted in the reduction of the cost-push component of inflation.

INFLATION

2. The slowdown in global growth prospects, as a result of, (1) the recessions in the East Asian emerging market economies, (2) the August crisis in Russia and (3) the more recent turmoil in Brazil, has contributed to further weakening of net exports in Jamaica's balance of trade position. This has led to a reduction in income to the export industry and as such resulted in a fall in expenditure and thus a contraction in consumer demand in the local economy.

Outlook for 1999

For 1999 Government is expected to continue pursuing its tight monetary policy of the past three (3) years in order to temper the inflationary demand by private agents. This, however, has the effect of reducing both consumer and investor spending in the short to medium term, contracting the tax base and negatively impacting on the revenue side of the fiscal account.

Alternately, the upward trending in world oil prices coupled with the added tax on domestic petrol will push prices upward. The implication here is that the tax measure has only a one time effect on prices, however, prices will continue to rise if, and only if, world oil prices continue trending upwards.

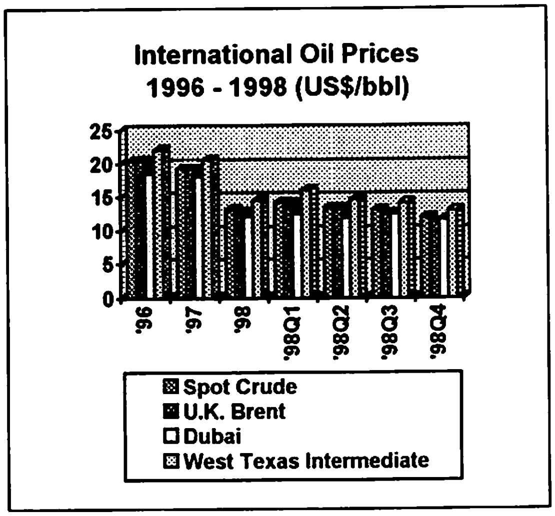
The overall effect of an upward trend in world oil prices will significantly outweigh the contraction in demand by economic agents. This has led to an expected outlook of about 7% - 9% for 1999.■

8. ENERGY

International Oil Market

The price of oil declined for the second consecutive year due to increasing supplies and a reduction in global demand for oil. Consequently, there was a 32.2% reduction in the price of spot crude in 1998 compared with a reduction of 5.4% for 1997. Thus, the price of spot crude averaged US$13.07 per barrel in 1998 compared to US$19.27 and US$20.37 per barrel in 1997 and 1996 respectively.

Figure 8.1



The price per barrel of UK Brent, Dubai and West Texas Intermediate declined by 33.5%, 33.2% and 30.0% to US$12.72, US$12.09 and US$14.42 respectively during 1998. These reductions are more significant than in 1997 as the price per barrel of UK Brent, Dubai and West Texas Intermediate declined by 6.5%, 2.4% and 7.0% to US$19.12, US$18.10 and US$20.59 respectively in 1997. Table 8.1 gives average spot prices for selected crude oils.

Local Consumption

The volume of petroleum imports increased by 4.6% from 19.5 million barrels in 1997 to 22.9 million barrels in 1998. Petrojam Refinery's importation of crude oil and refined products increased by 5.7% from 10.5 million barrels in 1997 to 11.1 million barrels in 1998. The Refinery took advantage of the decline in world prices by increasing its importation of refined products by 9.7% from 5.4 million barrels in 1997 to 5.9 million barrels in 1998.

Despite the increase in volume of imports, the total value of exports declined from US$354.13 million in 1997 to US$306.86 million in 1998, a decline of 27.3%. The value of imports by bauxite companies declined by 29.6% from US$141.08 million in 1997 to US$99.30 million in 1998, while the value of crude oil and refined products imported by the Refinery declined by 29.0% from US$213.05 million in 1997 to US$151.35 million in 1998.

ENERGY

Table 8.1 Average Spot Prices For Selected Crude Oils

	Unit (US)	1996	1997	1998	98Q1	98Q2	98Q3	98Q4
Spot Crude	$/BBL	20.37	19.27	13.07	14.16	13.28	13.00	11.85
U.K. Brent	$/BBL	20.45	19.12	12.72	14.08	13.28	12.45	11.10
Dubai	$/BBL	18.54	18.10	12.09	12.46	11.93	12.42	11.56
West Texas Intermediate	$/BBL	22.13	20.59	14.42	15.96	14.64	14.12	12.90
(Spot crude is an equally weighted average of U.K. Brent, Dubai and West Texas Intermediate.)								

Petrojam's output declined by 2.3% (0.9 million barrels) during 1998 owing to closure for three weeks in January 1998, closure since October 1998 as a result of fire to a smelting plant and the increased importation of refined products to take advantage of falling international prices. Total production for 1998 amounted to 5.1 million barrels compared with 5.3 million barrels in 1997.

The average billing prices of most petroleum products on the local market increased in 1998 owing to a tax on gasoline effected in April 1998 and increased production costs. Whereas fuel oil and liquid petroleum registered price reductions of 24.9% and 18.2% respectively, the price per litre of premium, unleaded and diesel oil declined by 4.4%, 3.4% and 2.2% respectively. Therefore, Jamaican consumers did not reap the full benefit of the reduction in international oil prices.

Table 8.2 Volume and Value of Petroleum Imports, 1996 -1998

	1996		1997		1998	
	Volume (BBLS)	Value (US$M)	Volume (BBLS)	Value (US$M)	Volume (BBLS)	Value (US$M)
REFINERY						
Crude Oil	5,113,600	106.624	5,131,200	94.000	5,198,400	59.257
Refined Products	6,165,200	148.527	5,412,300	119.051	5,936,800	92.094
Sub-Total	**11,278,800**	**255.151**	**10,543,500**	**213.051**	**11,135,200**	**151.351**
BAUXITE COMPANIES						
Fuel Oil	7,490,500	114.120	8,961,900	141.078	9,054,000	99.302
Total Imports	**18,769,300**	**369.271**	**19,505,400**	**354.129**	**22,868,200**	**306.860**
Total Imports	18,769,300	369.271	19,505,400	354.129	22,868,200	306.860

ENERGY

Electricity Sales

Total electricity sales increased by 7.2% to 2,466.1 megawatts in 1998 from 2,281.0 megawatts in 1997. This is an increase over the previous year when total sales grew by 6.4% form 2,144.7 megawatts in 1996, and a continuation in the expansion of electricity sales. Table 8.3 gives further details on electricity sales between 1995 and 1998.

Both sales for commercial and private uses have increased over the past three years, with private usage increasing at a faster rate than commercial usage. Whereas electricity sales for commercial purposes increase by 4.8% to 1,464.8 megawatts in 1998, electricity sales for domestic or private use increased by 11.1% to 981.3 megawatts in 1998. Commercial and domestic (private) usage during 1997 increased by 5.1% and 8.4% to 1,398.0 megawatts and 883.0 megawatts respectively.

Tale 8.3 **Electricity Sales, 1995 - 1998**

	1995	1996	1997	1998
Total Sales (TS) – M.W.H.	1,997.8	2,144.7	2,281.0	2,446.1
Commercial Sales (CS) – M.W.H.	1,262.0	1,330.1	1,398.0	1,464.8
Private Sales (PS) – M.W.H.	735.8	814.6	883.0	981.3
% Change – TS		7.4	6.4	7.2
% Change – CS		5.4	5.1	4.8
% Change – PS		10.7	8.4	11.1

Outlook for 1999

The OPEC cartel members have committed themselves to cut the supply of crude oil in an attempt to halt the rapid decline in international oil prices and it is being argued on the international circles that oil prices will increase. This will definitely impact local prices and will have an inflationary impact. The increase in price will be steep as the cartel members are seeking to restore the 1996 price per barrel, that is some 82.9% above the current price. Therefore, given the recent increase in gas taxes, consumers should expect prices to increase during 1999.

The Government introduced a revision of Tariff Schedules which allows the JPSCo.

ENERGY

to make faster adjustments in the rates charged to its customers. Given that international oil prices are expected to increase, consumers should expect these increases to be passed on by increases in their fuel rates.

Improvements in the energy sector are expected as the Ministry of Mining and Energy is drafting an Energy Sector Development Plan in order to implement the Energy Policy. Further, there should be more discussions on additional privatization within the energy sector. To this end, the divestment of Petrojam and the JPSCo are events that may move forward to 1999.■

9. MANUFACTURING

The manufacturing sector continued to suffer from high financing costs and contracted by 4.2% in 1998 to register its fourth consecutive year of decline. During the year, processed food, chemicals and chemical products recorded small increases; but sharp decline in the output of beverages and tobacco, petroleum, and cement resulted in an overall fall in the sectoral output. The reduction in manufacturing output was primarily due to high domestic interest costs and also to the continuing lack of competitiveness in local production. The situation was worsened by developments in South East Asia where the currency devaluations have made the exports of these countries so much more competitive in the Jamaican market.

The government continued its initiatives to restore growth to the manufacturing sector. To this end the administration lowered the lending rates at its development banks from 18% to 13%, and mounted a special programme of assistance for the garment industry. These efforts did not have a significant impact in 1998.

Food Processing

Data on poultry meats for the first six months of 1998 indicate that production declined by 34.86% from 22,719,000 kilograms in 1997 to 14,799,000 kilograms in 1998. Sugar production also registered a significant decline of 20.43% as sugar production declined from 230,000 metric tonnes in 1997 to 183,000 metric tonnes in 1998. Between January and September 1998 the production of condensed milk increased by 9.11% from the 11,986 tonnes recorded for the first nine months of 1997.

Beverages & Tobacco

Like the food processing sub-sector, there were significant reductions in the beverages and tobacco production due to cost constraints imposed by the continued high interest rates. Consequently, between January and September, aerated water, cigars and beer & stouts declined by 37.34%, 16.60% and 4.04% respectively, while the production of cigarettes marginally increased by 0.23% over the same period. Rum & alcohol production

MANUFACTURING

litres in 1997 to 23.630 million litres in 1998.

Petroleum Products

There were reductions in most products within this sub-sector as only diesel & fuel oils registered an increase in production, increasing by 4.29% to 538.3 million litres in 1998. Gasoline, turbo-fuel/kerosene and other petroleum products declined by 2.32%, 21.48% and 55.34% respectively. Table 9.1 contains further details on actual production.

Table 9.1 Production of Selected Commodities

Sub-Sector / Commodities	Unit	1997	1998	% Change
Food Processing				
Poultry Meats**	000 kg	22,719	14,799	-34.86
Animal Feeds				
Condensed Milks*	Tonnes	11,986	13,078	9.11
Flour	000 kg			
Sugar	met. Ton.	230	183	-20.43
Molasses	000 kg			
Beverages & Tobacco				
Rum & Alcohol	000 litres	22,634	23,630	4.40
Beer & Stout*	000 litres	50,778	48,725	-4.04
Aerated Water*	000 litres	21,817	13,671	-37.34
Cigarettes*	000	854,000	856,000	0.23
Cigars*	000	16,525	13,781	-16.60
Chemical Products				
Fertilizers	Tonnes			
Paint*	000 litres	5,855	5,494	-6.17
Sulphuric Acid	Tonnes			
Aluminium Sulphate	Tonnes			
Salt – NaCl	Tonnes			
Non-Metallic Minerals				
Cement	Tonnes	577,300	558,100	-3.33
Glass Bottles	Tonnes			
Petroleum Products				
Gasoline	'000 litres	142,300	139,000	-2.32
Diesel & Fuel Oils	'000 litres	538,300	561,400	4.29
Turbo-Fuel/Kerosene	'000 litres	71,700	56,300	-21.48
Other Petroleum Products	'000 litres	35,600	15,900	-55.34

* Data available for January to September.

** Data available for January to June.

MANUFACTURING

Manufacturing Exports

Export of manufactured goods declined by 11.6.0% to US$220.82 million during 1998 and the share of manufactured goods in exports declined from 18.0% in 1997 to 17.1% in 1998. The decline reflects the continuing lack of competitiveness in the manufacturing sector. The high real lending rates have taken a toll on the working capital of the firms in the sector and sharp increases in local costs have made it difficult for the sector to compete in both the local and foreign market. With the fallout within the domestic manufacturing sector, imports of manufactured goods increased from US$879.885 million in 1997 to US$908.525 million in 1998, an increase of 3.3%. This was due in part to an appreciation in the real exchange rate and to increases in domestic labour costs.

Outlook for 1999

If both real and nominal interest rates are not reduced during 1999, the manufacturing sector will continue to experience declines in most sub-sectors as high financing costs continued to have a negative impact on the working capital and profitability of the productive sector. Further, the sector will continue to suffer from intense competition with imported goods due to lower international prices and lower import duties. The capacity of firms in the manufacturing sector to recover will depend on the extent to which they can use internally generated funds, or new equity, to finance the re-tooling and re-organisation of their production facilities. Unless there is a significant shift in the current policy direction, this may be the only route back to profitability and growth in the sector. A few companies have begun to make the transition but many others will have to do likewise if the sector is to halt the current decline.■

10. MINING

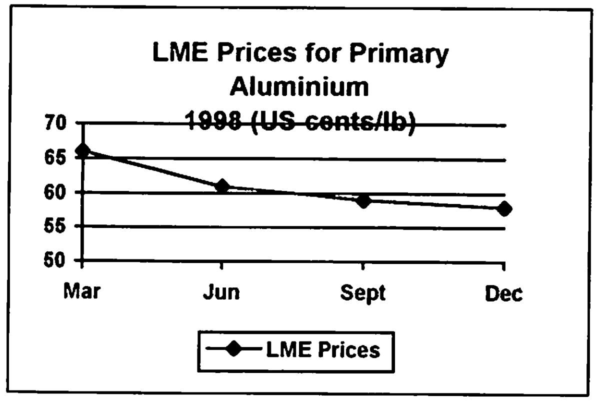
International Metal Industry

The IMF index for Metals indicates that the average price of metal products declined by 15.1% in 1998 compared to an increase of 8.7% in 1997. The actual market prices of metal products indicate that all metal products with the exception of iron ore experienced a fall in prices. Whereas the price of iron ore increased by 3.5%, the price of copper, aluminium, tin, nickel, zinc and lead declined by 27.3%, 10.0%, 5.6%, 33.2%, 22.1%, and 15.4% respectively. These significant reductions resulted from the slowdown of some Asian and other developing economies, which has negatively impacted the demand for consumer durables in the world market.

Domestic Production

Preliminary data indicates a continuation of the upward trend in the production of bauxite and alumina evidenced in 1997. Total bauxite production increased by 5.5% to 12.65 million tonnes in 1998, the highest level since 1974. This increase is a slowdown in growth as total bauxite production in 1997 increased by 6.9% over the level of production registered for 1996.

Figure 10.1



Crude bauxite production increased by 10.7% to 4.03 million tonnes, while alumina production increased by 1.4% to a new record level of 3.44 million tonnes in 1998. Thus, there was acceleration in the growth of the production of crude bauxite as the rate of growth during 1997 was 2.8%. Further, there was a deceleration in the growth of alumina production as production increased by 7.5% to 3.39 million tonnes in 1997.

Crude bauxite for export rose by 10.4% above its 1997 level to 4.02 million tonnes in 1998, due to new management arrangements and a more stable labour environment. This is an acceleration in

MINING

the growth rate as crude bauxite exports for 1997 increased by 2.6% to 3.64 million tonnes.

Alumina export volume expanded by 1.8% to 3.48 million tonnes. This deceleration in the growth rate of 6.9% for 1997 reflects the sluggish international market conditions in the metal industry.

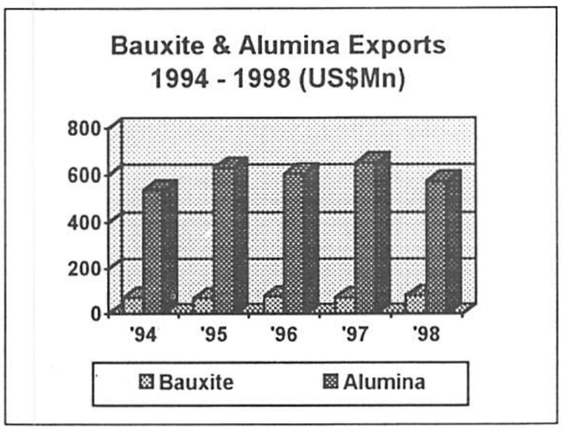
Total bauxite export volume increased by 5.7% to 12.72 million tonnes compared to an expansion of 6.4% to 12.03 million in 1997. Thus, total bauxite export volume continued to show growth and continues to be the sector recording the highest rate of growth in output.

In July 1998, the government, trade unions and bauxite companies signed "The Manley Accord" – a Memorandum of Understanding – with a view to improving industrial relations and the investment climate in the bauxite/alumina sector. This led to substantial improvements in labour relations in the second half of the year and the authorities will be pushing for similar agreements in other areas of the economy in 1999.

Foreign Exchange Earnings

Despite the expansion in export volumes, gross receipts are expected to decline from US$735.0 million in 1997 to an estimated US$685.0 million in 1998 due to sluggish international market conditions associated with the economic turbulence of Asia. This 6.8% reduction in expected receipts is a result of falling international prices due to increased competition in the international metal industry and does not compare favourably to the 4.6% increase recorded for 1997.

Figure 10.2



The economy is projected to retain approximately U$274 million for 1998 compared to US$294 million in 1997. The estimated retention will pay for

MINING

wages, investment, and the Government levies and is based on a rate of 40% of the earnings of the bauxite industry.

Outlook for 1999

The economic fallout in several Asian countries has resulted in a lowering of the prices of metal products on the international market. However, the expected return to growth in most of these Asian countries will serve to increase the demand for alumina and bauxite. World demand for these products should increase during 1999 and, if so, Jamaica may be able to increase its export volume of crude bauxite and alumina. Further, with the USA implementing measures to protect its metal industry from cheaper imports, Jamaica will stand to benefit from increased export volumes to the US. World prices are also expected to continue their decline as competition in the world metal industry intensifies.

With world prices expected to remain soft, the prospects for increased earnings by this industry in 1999 are not good. The relative competitiveness of the Jamaican production facilities will play a part in determining whether or not the country is able to attract additional investment in the bauxite/alumina industry. A significant expansion of the existing production facilities is critical to the long term viability of the Jamaican bauxite/alumina industry. There is also the prospect that a further increase in production may not yield a significant increase in earnings.■

11. TOURISM

World Tourism

Provisional figures provided by the World Tourism Organisation revealed a continued expansion in international tourist activity for 1998. During the 1998 period tourist arrivals increased, albeit marginally by 0.84% compared with the increase of 4.2% in 1997. The fall in increased output could be attributed to the relative instability in the international market, as a direct consequence of the financial turmoil in South East Asia, Russia and Brazil, which has translated into lower net disposable income in these important regions.

There is a growing competitiveness in the international tourism market as countries try to meet the growing demands of tourists by effecting novel ideas in order to woo increased visitor arrivals. These include:

1. eco-tourism development;
2. developing and maintaining traditional attractions, as well as implementing modern attraction sites; and
3. the emergence of countries with a strong and attractive cultural outlook with particular focus on medicinal herbs and spices.

Table 11.1 Growth Prospects of International Tourism World and Regional Picture, 1996 - 1998 - Tourist Arrivals - Millions

Region	*Actual Data*	*Estimates*		*Yearly Change %*	
	1996	**1997**	**1998**	**1996/97**	**1997/98**
Africa	21.5	22.8	24.9	6.05	9.21
Americas	116.1	120.8	120.1	4.05	-0.58
East Asia/Pacific	87.3	93.0	86.9	6.53	-6.56
Europe	351.2	363.0	372.5	3.36	2.62
Middle East	14.2	15.5	15.6	9.15	0.65
South Asia	4.5	4.9	5.1	8.89	4.08
World	594.8	620.0	625.2	4.24	0.84

TOURISM

Jamaica's Development and Performance in 1998

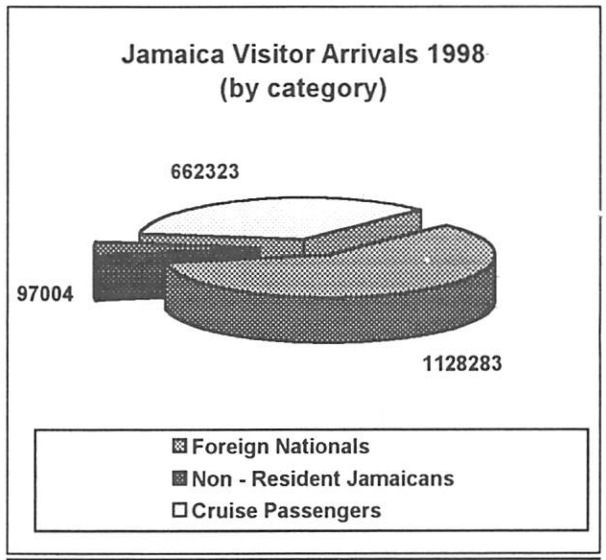
The sector continued to show signs of growth amidst the chilling economic environment that pervaded in 1998. The negative external shock on the world economy, as a direct consequence of the Asian and Russian crises, depleted net disposable income to the rest of the world. This thus reduced the likely prospect of increased growth in the sector. In addition, the opening up of other more competitive tourist destinations, namely by our nearest neighbour, Cuba, reduced likely tourism inflows to the country. There were also domestic factors that contributed to or influenced tourist arrivals throughout 1998.

These were mainly:

(i) poor physical infrastructure;
(ii) tourist harassment and the incidents of crime against tourists;
(iii) the cut in the budget allocation to the sector for advertising on the eve of the winter tourist season; and
(iv) the re-financing difficulties faced by the sector amidst the high real interest rates.

In spite of these negative influences there was continued investment in the sector as construction began on the Ritz Carlton Hotel in Montego Bay, Beaches in Westmoreland and SuperClub's Hedonism III in Runaway Bay.

Figure 11.2



Visitor Arrivals in 1998

Tourist arrivals were flat for 1998. Growth of 2.8% in stop-over arrivals was offset by a 5.3% decline in cruise ship visitors. Cruise ship arrivals fell by 13.3% with ship calls down to 422 versus 487 calls last year. However, the estimated visitor expenditure for 1998 was US$1.196 billion or 4.91% above the earnings for 1997.

TOURISM

Table 11.2 Tourism Performance in Jamaica for 1998

Month	*Foreign Nationals*	*Non-Resident Jamaicans*	*Total Stop-Over Arrivals*	*Cruise Passenger Arrivals*							
				Mobay # of calls		*Ocho Rios # of calls*		*Port Antonio # of calls*		*Total Calls # of calls*	
Jan.	93671	4846	98517	13	9557	31	58407	1	433	45	68417
Feb.	94386	4894	99280	18	17396	26	48245	1	478	46	66723
Mar.	106924	5550	112474	14	9840	37	64707	0	-	51	74547
Apr.	102038	7903	109941	11	7822	28	57780	0	-	39	65602
May	91777	5286	97063	11	7525	16	35399	1	43	28	42967
Jun.	97432	9875	107307	8	5433	17	40489	0	-	25	45922
Jul.	108214	12212	120426	9	7543	18	45652	0	-	27	53195
Aug.	100018	9909	109927	9	6415	15	38592	0	-	24	45007
Sep.	69362	6169	75531	8	4229	15	34796	0	-	23	39025
Oct.	75696	6558	82254	5	3047	16	34013	0	-	22	37134
Nov.	88730	5739	94469	11	7956	23	44037	0	-	34	51993
Dec.	100035	18063	118098	23	16366	35	66792	0	-	58	83158
Totals	**1128283**	**97004**	**1225287**	**140**	**103129**	**277**	**568909**	**3**	**954**	**422**	**673690**

Total stop-over arrivals for 1998 stood at 1,225,287 relative to the 1,192,194 outcome of 1997 when a growth of 2.6% was achieved. Of the 1,225,287 total stop-over arrivals for 1998, 97,004 were non-resident Jamaicans (down from 106,795 in 1997) with the remaining 1,128,283 visitors being foreign nationals (up from 1,085,399 in 1997). The largest group of stop-over arrivals by region in 1998 came from the United States of America (U.S.A.) with 67.7%, Europe with 17.4%, and the remaining 14.9% largely from Latin America, Japan and the Caribbean. Compared to the outcome of 1997, USA stop-over arrivals increased by 3.1%, with a marginal 1% increase by European visitors. Deteriorating economic conditions in Latin America and Japan, however, led to a 7.2% and 31.7% reduction respectively in stop-over arrivals from these countries.

TOURISM

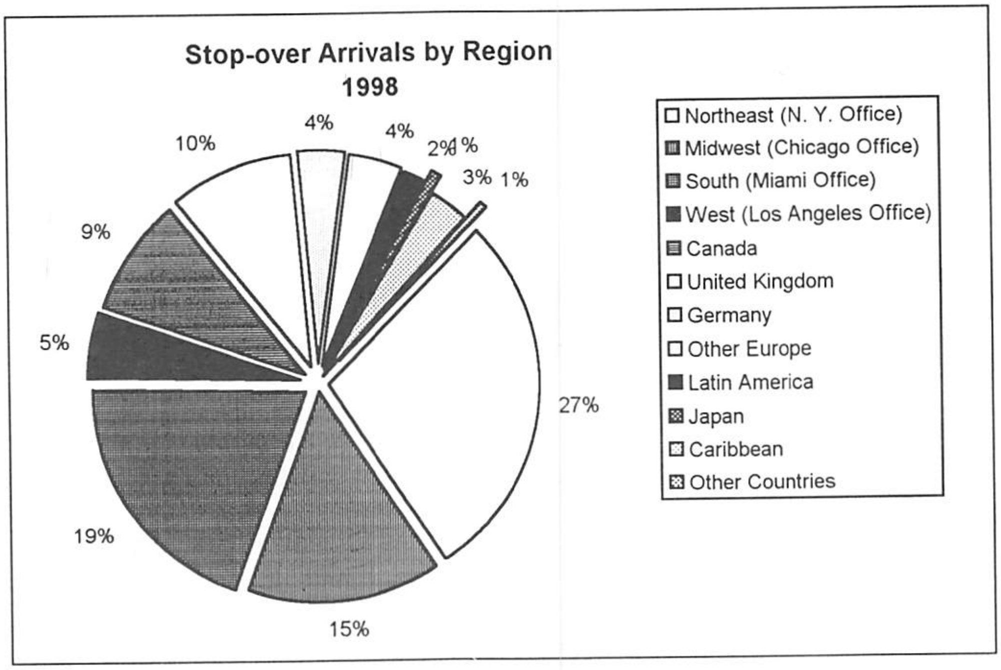
Cruise ship passengers for 1998 fell significantly by 38,009 visitors to 673,690 relative to the outcome of 711,699 in 1997. Of the 422 calls made in 1998 compared to 487 in 1997, 140 were made in Montego Bay compared with 227 in 1997, 277 in Ocho Rios relative to 255 in 1997 and 3 in Port Antonio compared with 2 in 1997.

Table 11.3 **Stopover Arrivals by Region**

Region	*Jan-Dec '96*	*Jan-Dec '97*	*Jan-Dec '98*
U.S.A.			
Northeast (N.Y. Office)	328629	339189	348826
Midwest (Chicago Office)	165702	170832	178777
South (Miami Office)	224268	231735	241240
West (Los Angeles Office)	55247	62582	60487
TOTAL USA ARRIVALS	**773846**	**804338**	**829330**
OTHERS			
Canada	102215	99226	109802
United Kingdom	114417	116390	116552
Germany	36509	33480	43018
Other Europe	57440	60762	53119
Latin America	18721	20682	19187
Japan	22280	15775	10781
Caribbean	31070	34768	36818
Other Countries	5951	6750	6680

TOURISM

Figure 11.2



Caribbean Tourism

Provisional figures from the Caribbean Tourism Organisation reveal that overall tourist stop-over arrivals to the Caribbean for 1998 grew modestly relative to the comparable period of 1997. Caribbean destinations recorded strong growth in arrivals during the winter months (January to April) relative to the performance of 1997, namely Belize (up 16.8%), the Dominican Republic (up 16.3%), St. Kitts and Nevis (up 26.6%) and Turks and Caicos Islands (up 19.7%).

The strong winter performance was not repeated in the Summer months (May to October). The main influence could be attributed to the devastating effects of Hurricanes George and Mitch. All territories were affected whether directly or indirectly with the major ones being Antigua, Montserrat, Anguilla, British Virgin Islands, Haiti, Cuba and the Dominican Republic. Despite this factor, increased growth in arrivals were recorded in territories such as Cuba (up 21%), Martinique (up 10.6%), and Trinidad & Tobago (up 12.2%) relative to the 1997 performance.

Cruise tourism grew by approximately 30% in 1998 relative to the 1997 experience with the greatest percentage

TOURISM

increase in Cruise passenger arrivals taking place in St. Kitts and Nevis. Aruba, however, accounted for the greatest percentage decline over the 1998 period relative to the similar period in 1997. This increase in performance with respect to Cruise passenger and stop-over arrivals is partly as a result of new berth capacity in addition to the strong advertising campaign undertaken by the Caribbean Tourism Organisation to market the Caribbean in North America.

Table 11.4 **Cruise Passenger Arrivals - 1997 & 1998**

Destination	*Period*	*1998*	*1997*	*% change*
Antigua and Barbuda	Jan-Dec	336066	285489	17.7
Aruba	Jan-Oct	183102	210937	-13.2
Bahamas	Jan-Dec	1729894	1751140	-1.2
Barbados	Jan-Dec	506610	517888	-2.2
Bermuda	Jan-Dec	188331	181886	3.5
Cayman Islands	Jan-Dec	852527	866609	-1.6
Cozumel (Mexico)	Jan-Sep	840370	785512	7.0
Curacao	Jan-Dec	231222	214685	7.7
Dominica	Jan-Sep	175739	157129	11.8
Grenada	Jan-Dec	265875	246612	7.8
Jamaica	Jan-Dec	673690	711699	-5.3
Puerto Rico	Jan-Dec	1243442	1227367	1.3
St. Kitts and Nevis	Jan-Dec	308214	205476	50.0
St. Lucia	Jan-Dec	372068	310213	19.9
St. Maarten	Jan-Dec	881448	885956	-0.5
St. Vincent and G'dines	Jan-Nov	24476	24567	-0.3
Trinidad and Tobago	Jan-Sep	24988	25857	-3.4
US Virgin Islands	Jan-Dec	1615518	1618956	-0.2

TOURISM

Table 11.5 Tourist (Stopover) Arrivals in the Caribbean in 1998

Destination	*Period*	*Tourist Arrivals*	*% Change*		
			Overall	*Winter✧*	*Summer✧*
Anguilla	Jan-Dec	43874	1.6	4.3	-0.4
Antigua & Barbuda	Jan-Nov	182774	-5.0	2.5	-10.7
Aruba	Jan-Dec	647437	-0.4	-0.1	-0.5
Bahamas	Jan-May	697496	-7.3	-7.0	-8.6
Barbados	Jan-Dec	512397	8.5	15.6	4.8
*Belize****	Jan-Dec	94928	9.0	16.8	3.8
Bermuda	Jan-Dec	368749	-2.9	-3.1	-2.8
Bonaire	Jan-Dec	61740	-1.7	1.8	-3.7
Cancun (Mexico)	Jan-Sep	2317189	11.4	13.2	9.7
Cayman Is.	Jan-Dec	404205	6.0	6.4	5.8
Cozumel (Mexico)	Jan-Sep	325417	14.4	12.9	15.7
Cuba	Jan-Aug	936212	18.0	15.5	21.0
Curacao	Jan-Dec	198570	-3.2	-1.4	-4.1
Dominica	Jan-Sep	49684	-0.5	1.3	-1.9
*Dominican Republic**	Jan-Dec	2334493	6.9	16.3	1.4
Grenada	Jan-Dec	115794	4.6	0.2	7.2
*Guadeloupe***	Jan-Jun	74143	-8.4	-10.0	-3.9
Guyana	Jan-Aug	47301	-9.8	-21.8	0.7
Jamaica	Jan-Dec	1225287	2.8	2.9	2.7
Martinique	Jan-Dec	548672	6.9	2.2	10.6
*Puerto Rico***	Jan-Dec	1063901	4.6	5.3	4.2
St. Eustatius	Jan-Dec	8636	1.2	0.9	1.4
St. Kitts & Nevis	Jan-Nov	84528	8.5	26.6	-3.3
St. Lucia	Jan-Dec	252237	1.5	3.9	0.2
St. Maarten	Jan-Dec	458486	4.4	13.9	-1.7
St. Vincent & G'dines	Jan-Dec	67228	3.2	15.4	-2.6
Trinidad & Tobago	Jan-Oct	285348	8.1	3.2	12.2
Turks & Caicos Is.	Jan-Dec	105925	14.8	19.7	11.7
*US Virgin Is.****	Jan-Dec	523402	2.9	4.9	1.5
TOTALS		**14036053**	**100.1**	**162.3**	**70.4**

✧Winter: January - April; Summer: April - December
**Foreign Visitor Departures **Hotel Registrations Only ***Air Arrivals Only*

TOURISM

Outlook for 1999

Tourism growth, if achieved, is expected be low during 1999. Overall, Caribbean Tourism moved sluggishly for 1998, even Barbados with consistent growth over the past five years, saw a fall in tourist earnings by 3% in the first quarter of 1999.

Although reeording a strong performance for the first quarter of 1999, the local industry has to take into account the impact of the riots and the incidents of crimes against tourists. The question therefore is 'will the industry hold or lose ground for the remainder of the season?'.

Also of equal significance is the strong competition coming from Cuba, Cozumel and Cancun in Mexico, which from all indications have pulled in the highest growth in visitor arrivals for 1998 in the region. In addition to the Cuban and Mexican factor is the Summer Olympics in Sydney (Australia) next year which could pull tourists away from the country and the Caribbean region this year.

Although reduced occupancy levels were recorded for 1998 this was counterbalanced by increased visitor stay. Whether or not this trend continues for 1999 will depend on the steepness of the discounts offered by hoteliers.

In spite of the difficulties in the industry, it still remains one of the fastest growing sectors in the very short run. One of the major thrusts expected to spearhead the development for the twenty first century is the Port Royal Project, which could serve as a major catalyst for other similar initiatives.■

12. GRAPHIC ECONOMIC DATA

Table 12.1

COMMERCIAL BANKS' LOAN AND ADVANCES BY SECTOR (1992 - 1998) J$Mn							
Sectors	**1992**	**1993**	**1994**	**1995**	**1996**	**1997**	**1998**
Agriculture	1117.1	1416.7	2038.5	1879.0	2247.8	2541.3	1977.0
Manufacturing	2119.9	3027.0	3867.2	6092.6	7310.5	5898.6	4002.0
Construction	2473.9	3321.1	4616.1	5587.2	4692.0	4070.1	2540.1
Mining	73.4	118.1	236.4	354.1	320.7	245.6	191.0
Tourism	1027.8	2000.1	2912.1	3830.4	4682.2	4336.0	4260.4
Transport	1137.7	2163.6	3026.9	4399.9	3810.4	3845.8	1901.2
Government Service	813.2	1299.4	2674.3	3353.0	5240.4	8736.3	4716.4
Others	3340.1	8275.7	10928.9	18373.0	24266.0	27671.4	21497.7
Total	14095.1	23614.7	32294.4	45864.2	54566.1	59342.1	43083.8
Source: Bank of Jamaica							

Figure 12.1

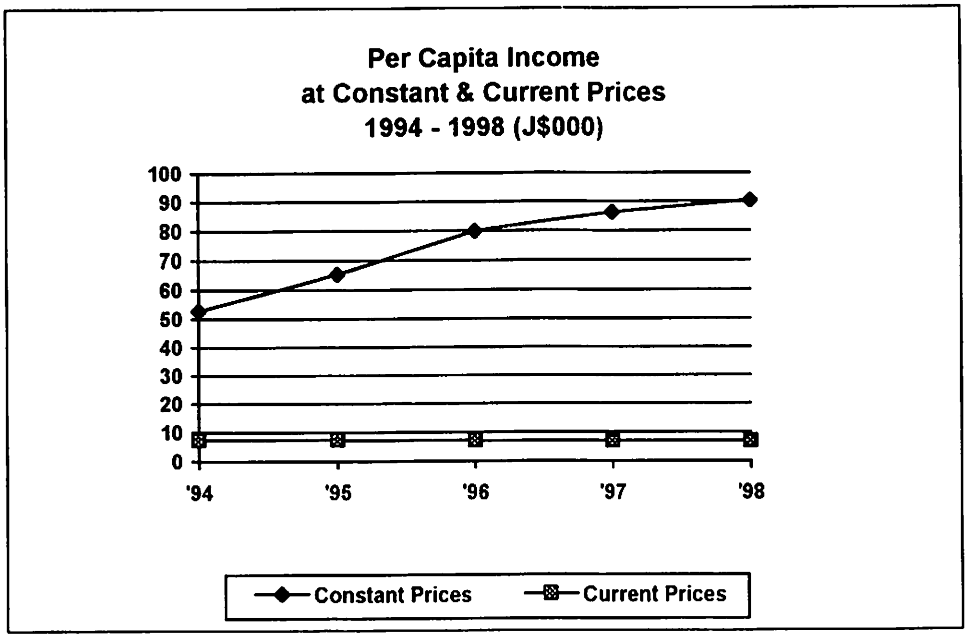


Figure 12.2

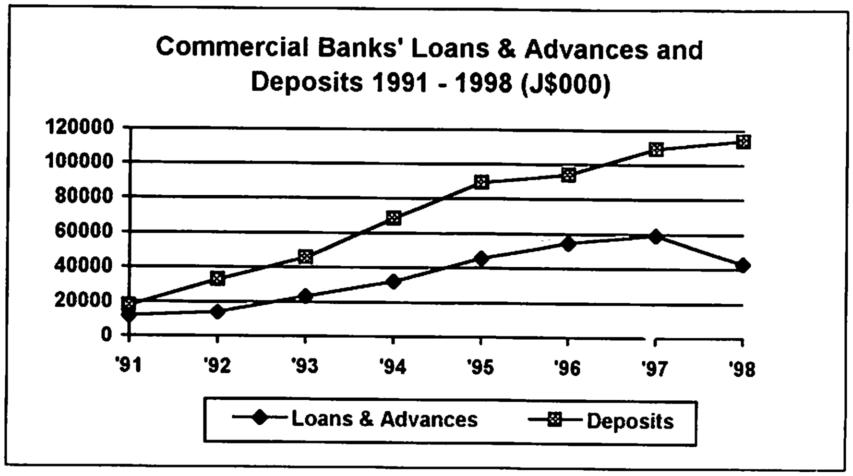


Figure 12.3

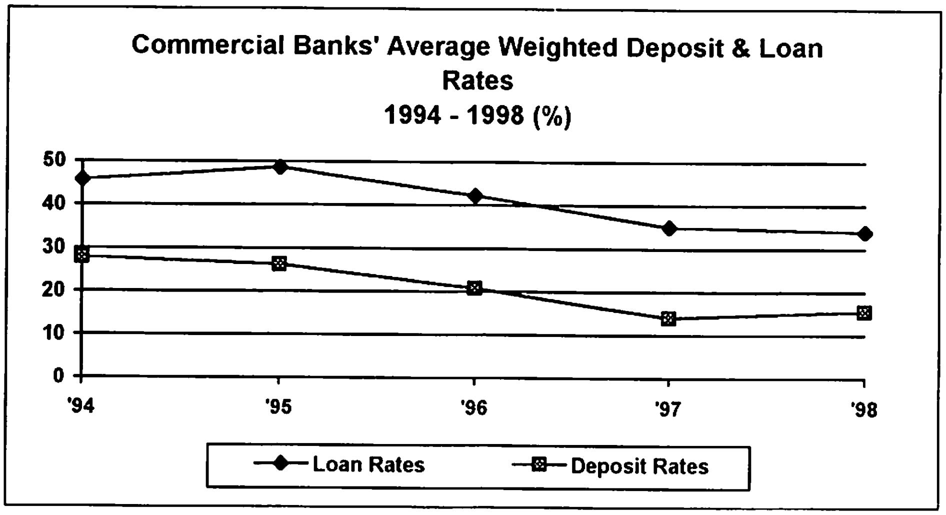


Figure 12.4

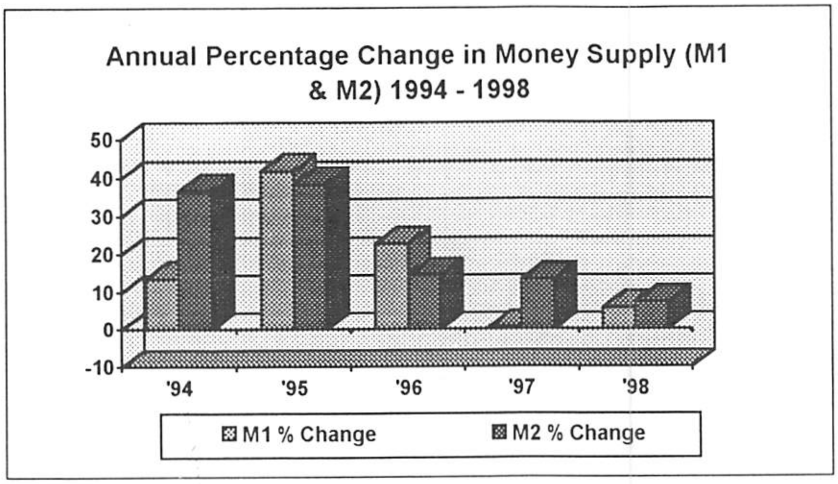


Figure 12.5

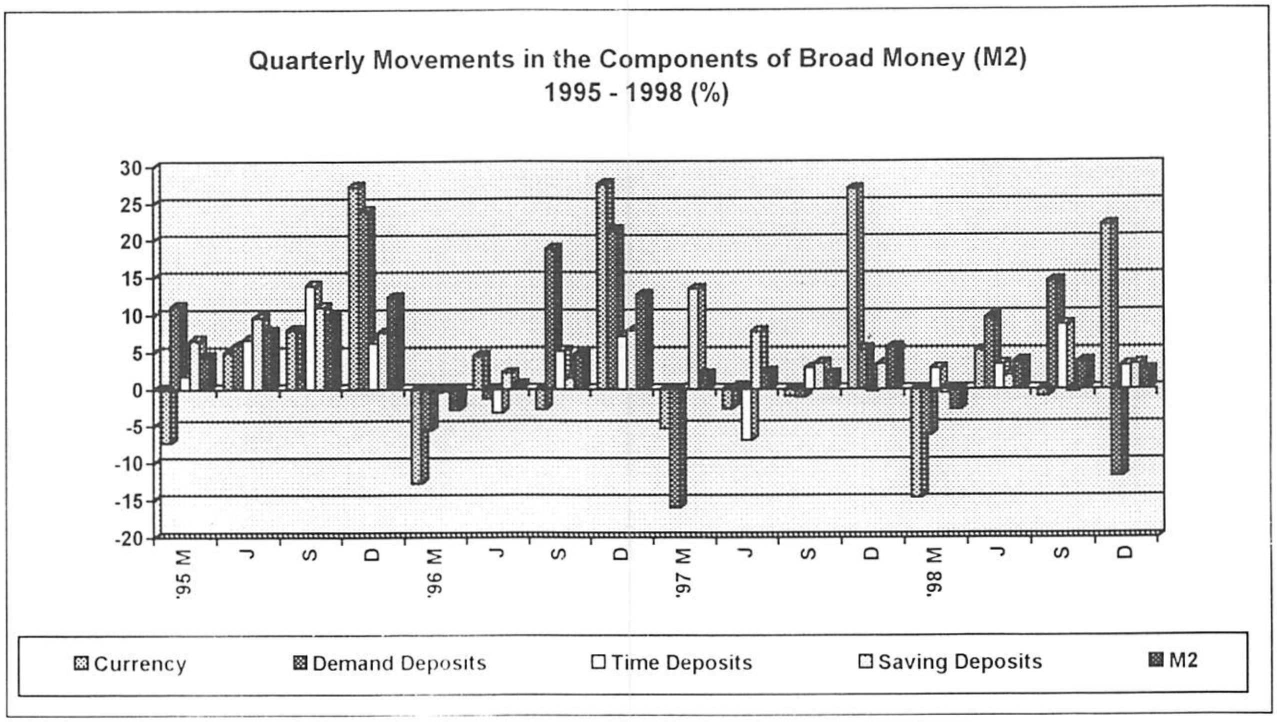


Figure 12.6

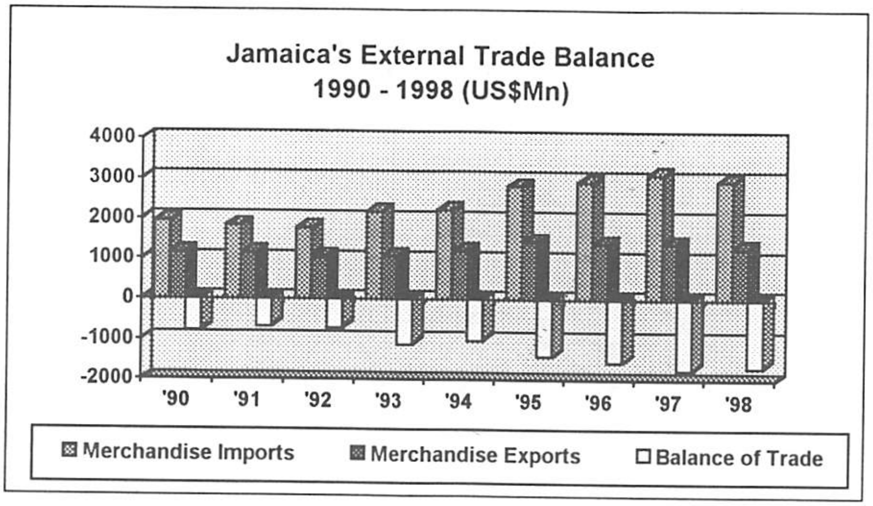


Figure 12.7

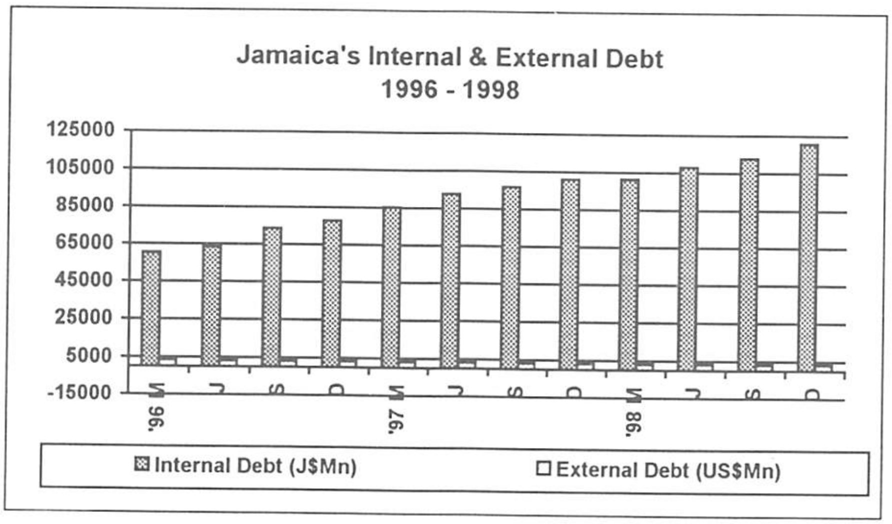


Figure 12.8

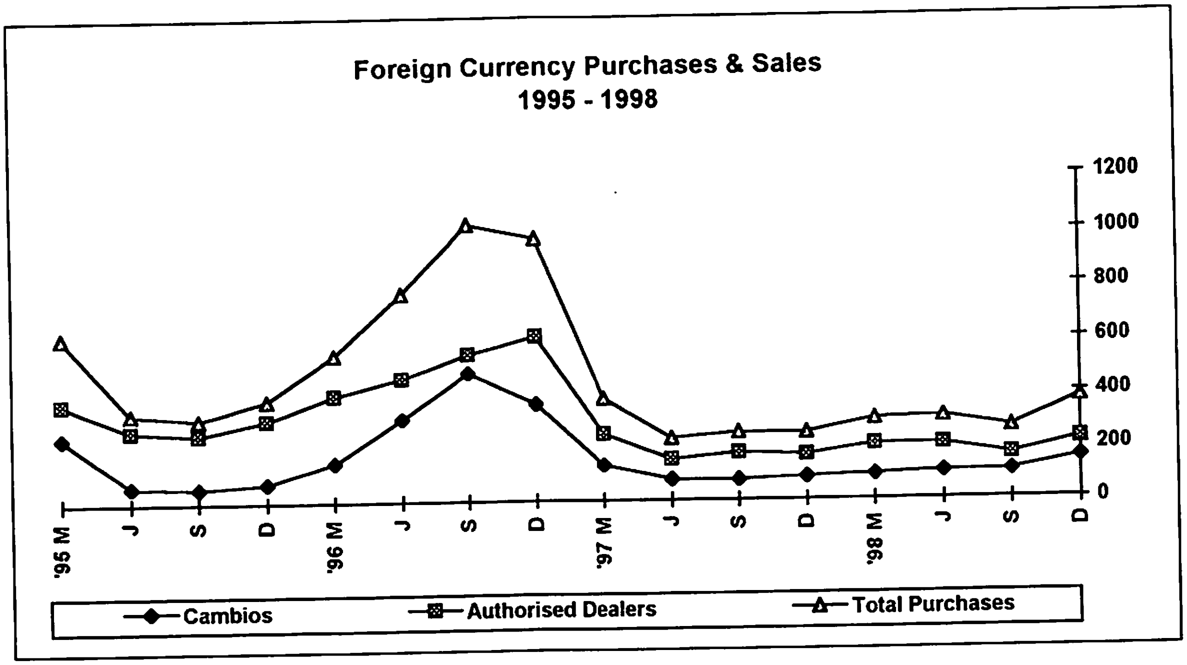


Figure 12.9