NEW CONFIDENTIAL ECONOMIC BULLETIN

A Monthly Analysis of the Jamaican Economy Vol. 7 No. 6, June 2001

Overview

The violence in West Kingston a week and a half ago (July 6th-8th), has occupied a great deal of media time and there has been much speculation about the possible impact of it in both the short and medium term. Apart from the disruption to businesses that operate downtown, and indeed for a couple days, those that operate uptown as well, there are going to be negative consequences for the economy as a whole. The extent of the negative impact will be determined to a large extent by the degree to which tourist arrivals and expenditure are affected by the negative international press that the incident attracted. Not much has been said about the role that the 10-12% growth in tourism last year played in the achievement of the 0.8% growth that was recorded in 2000. It has long been accepted in academic circles that growth in exports of goods and services is what drives growth in the overall Jamaican economy. From this perspective, last year's strong growth in tourism, the highest growth rate in many years, was probably a pivotal factor in the marginal growth that was achieved.

This year, even before the recent violence, tourism was facing the challenge of a weakening US and world economy and more aggressive marketing by competing destinations here in the Caribbean. The industry still achieved moderate growth in the first few months of 2001 but at roughly half the rate that prevailed in 2001. The negative press is likely to depress arrivals at least temporarily, thereby lowering even further the growth rate of the industry this year. With the exports of goods down by 11.6% in the first quarter of 2001, the outlook for export driven growth this year begins to look rather bleak. It is still too early to quantify the effect of the demonstrations but there can be little doubt that there will be a negative impact on the overall level of growth that will be recorded this year.

Economic growth is also likely to be inhibited by the recent trend in interest rates which have been heading upwards since last month. In June, the 6 month T-Bill rate moved up from 14.35% in May to 16.2% and in July, the most recent LRS issue, saw rates moving from just over 17% in June to between 18.09 and 19.83% for the 2004 and 2008 tenors. The recent rate increases seem to be the BOJ's response to heavy demand for US dollars which has seen them intervening in the foreign exchange market on a sustained basis over the last couple of months. The upturn in interest rates has started a bit earlier than we had expected based on the experience of previous years, but we will have to wait and see just how far and how quickly they will rise from here on. The players in the stock market do not seem to expect rates to go much higher in the short run as that market has reversed its downward movement and resumed a more moderate pace of growth.

International bond markets have been rocked in recent weeks by economic difficulties in Argentina and fears of a default by that country on its international debt. Although at the time of writing, bond prices have been staging a bit of a recovery, the market is likely to remain pretty volatile as Argentina struggles to overcome its severe fiscal problems. Jamaican bonds have suffered a relatively small decline in price during this period of uncertainty but government officials must be counting their good fortune at having approached the market before this most recent upheaval. It is likely to be very difficult and costly to raise debt in the international bond markets until Argentina returns to some form of stability.

In This Issue

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Net International Reserves

NIR continues record breaking surge - US$1.54bn

The Net International Reserves (NIR) of the central bank continued its record breaking performance for June 2001. The total stock of NIR at the central bank stood at a record US$1,540.51Mn (provisional) for the month. This represents a monthly increase of US$59.9Mn, compared to the record increase of US$198.82Mn reported for May. The current level of the NIR represents a record 27.33 weeks of imports, compared to the record 15.07 weeks of imports for June 2000.

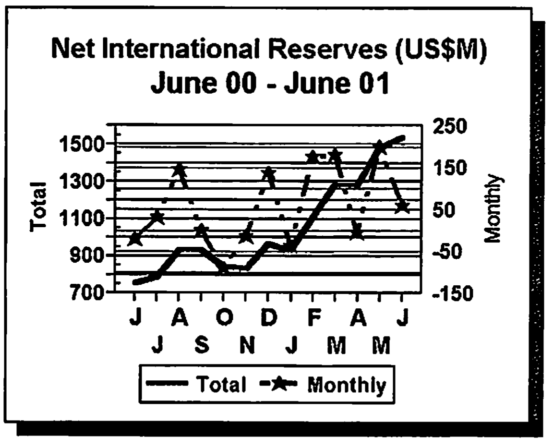

Figure 1: Net International Reserves

In the twelve months to the end of June 2001, the NIR increased by a record US$784.03Mn. This is in stark contrast to the US$165.91Mn increase for the same period ending June 2000. Inflows of US$128.34M in loan receipts, mainly from a second US$ bond issue at the end of May, contributed to NIR out-turn for June. Further divestment proceeds from the sale of the remaining FINSAC assets and draw-down of the second tranche of multilateral loans may improve the level of the NIR during the latter part of the year, though this may be tempered somewhat by debt obligations. The government's current success in the international bond market indicates that they may have little difficulty achieving the SMP NIR target of US$1,555Mn for the end of fiscal year 2001/02, although heavy intervention in the foreign exchange market could cause it to be misused.

Foreign Currency Deposits

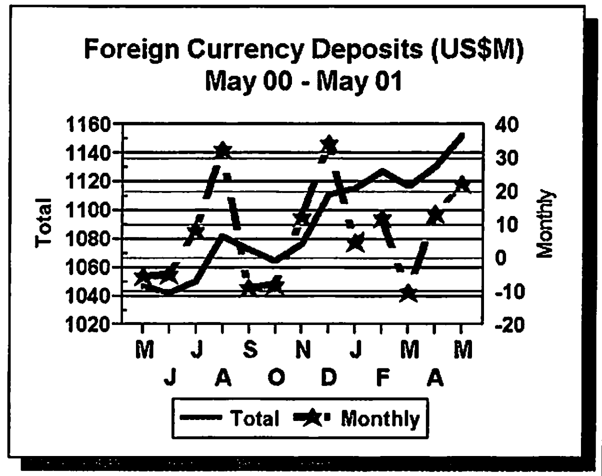

Figure 2: Foreign Currency Deposits

Foreign currency deposits attain another record - US$1.15bn

Preliminary BOJ statistics indicate that the total stock of foreign currency deposits increased by US$22.2M to a record US$1,152.64M, at the end of May 2001. This is in comparison to the US$1,130.48M reported at the end of April 2001. In the twelve months to May 2001, the stock of foreign currency deposits increased by US$105.4M (10.06%) compared with the US$81.4M (8.42%) increase for the same period in 2000. Commercial banks, merchant banks and building societies balances (excluding deposits on B accounts) were at US$929.84M, US$90.13M and US$132.67M respectively, representing increases of 8.26%, 44.12% and 5.47% over the corresponding period the previous year.

Foreign Exchange Rates

FX market slightly volatile during June

The foreign exchange market (J$/US$) continued to experience slight volatility during June 2001. The pressure which had been exerted on the market during the latter part of May 2001, was reduced during the first seven days of trading in June, by heavy central bank intervention. The intervention reduced the rate from J$45.82 on June 1st to J$45.70 on June 11th. However, continued increased demand for US$

subsequently led to the rate trading mostly between J$45.76 and US$45.80 during the latter part of the month, ending at J$45.82. Low liquidity in the US$ fixed income market due to continued purchase of Government of Jamaica Global Bonds, may have contributed to the increased demand. Central bank intervention has so far provided just enough liquidity to maintain relative market stability.

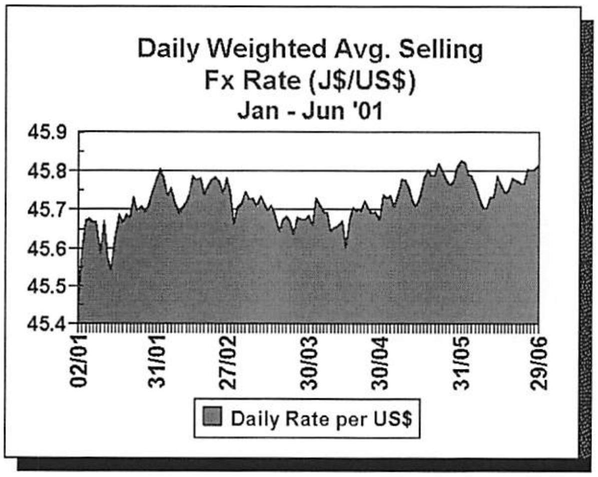

Figure 3: Daily J$/US$ Movements

J$ advance against US$ and GB£ but decline against CAN$

The Jamaican dollar had a better performance against the currencies of its major trading partners, in comparison to the previous Month. The domestic currency advanced against the US$ and GB£, but declined against the CAN$ - advancing by J$0.01 against the US$ and J$0.52 against the GB£, while declining by J$0.22 against the CAN$. This compares with the J$ declining against the US$ and CAN$, while advancing against the GB£ - J$0.15 against the US$, J$0.43 against the Canadian dollar and J$0.59 against the GB£ respectively - for the previous month.

The first six months of the calendar year has seen the J$ decline against the US$ and CAN$ while gaining against the GB£ - losing J$0.29 and J$0.29 while gaining J$2.84 respectively. This compares with losses of J$1.14 and J$0.30 while gaining J$3.25 respectively, for the similar period in 2000.

The weighted average selling rate of the Jamaican dollar to the US dollar for June 2001 was $45.77, which was the same as the average for May. The 12 month movement of this rate indicates a loss of $3.26 to the US dollar, compared with a loss of J$3.55 over the corresponding period in 2000.

The weighted average selling rates of the local currency vis-a-vis its major trading partners as at July 12th, 2001 were:
US$1 = J$45.78
CDN$1 = J$29.86
GB£ = J$63.89

Short-term Forecasts

The exchange rate at the end of June 2001 was $45.82, J$0.07 above the upper end of our "forecast" range of $45.73 - $45.75. Low liquidity levels in the US$ fixed income market led to increased pressure on the dollar, which were somewhat offset by central bank intervention. The relative stability that has prevailed in the market (J$/US$) for the first six months is by far the best performance over the past three years - the J$ lost only $0.29 in 2001 compared with $1.14 and $1.81 for the similar periods in 2000 and 1999. This translates into 0.63%, 2.77% and 4.86% respectively.

If this performance is maintained throughout the remainder of the year, barring external shocks - we could see the long awaited achievement of the interest rate targets, which are so critical to fiscal policy and investment.

Relative exchange rate stability may be expected to continue over the short term

The short term exchange rate forecasts have been updated, based on current market conditions (*Table 1*).

Table 1: Short Term Exchange Rate Forecasts for the end of the Months of July, August and September 2001 (J$/US$).

	Forecast	Actual	Difference
Jan	45.71 - 45.88	45.77	0.00
Feb	45.82 - 45.89	45.78	-0.04
Mar	45.78 - 45.82	45.68	-0.10
Apr	45.68 - 45.70	45.67	-0.01
May	45.72 - 45.74	45.83	0.09
Jun	45.73 - 45.75	45.82	0.07
Jul	45.81 - 45.83		
Aug	45.86 - 45.88		
Sep	45.94 - 45.96		

Interest Rates

Interest rates continued to trend downwards during the month of June, with the exception of the six-month Treasury Bill (T-Bill) rate. The benchmark six month treasury bill yield increased by 0.74 percentage points from 15.46 % in May, to 16.20% in June (*Table 2*). The market determined T-Bill rate has trended upwards due to low liquidity levels caused mainly by government's local debt issues, and the selling of foreign exchange in the market. In contrast, the 30 Day reverse repurchase was reduced twice, and was down by 0.50 percentage points from 14.75% in May to 14.25% in June. The longer term repo (365 days) was reduced once, by 0 .6 percentage points, and currently stands at 15.9%. The hike in 6-month T-bill yields means they have only declined by 3.96 percentage points year-to-date, in 2001 and 1.27 percentage points over the twelve months to date. The 30-day repo rate is down 2.2 percentage points year-to-date, and 2.75 percentage points over the twelve months to June.

6-month t-bill yield up by 0.74 basis points to 16.20% in June.

30-day repo down to 14.25% in June.

Table 2: Selected Interest Rates

	Mar	Apr	May	Jun
30 Day Repo	15.5	15.50	14.75	14.25
365 Day Repo	17.75	17.75	16.5	15.9
Avg. Savings Deposit	9.84	9.84r	9.5	9.45
Avg Loan Rate	31.33	31.21r	30.88	30.67
6 Month T-Bill Yield	16.87	16.50	15.46	16.2
12 Month T-Bill Yield	17.86	16.93	16.93	16.93

Average savings deposit and lending rates followed the trend of the declining repo rates, falling by 0.05 and 0.21 percentage points respectively. This had led to a decline in the spread between these two rates of 0.16 percentage points, to 21.22%.

Interest rates continue to trend down and are at their lowest levels since the early nineties. The surprising rise in the six-month T-Bill rate may be a temporary outlier, caused by possible short term liquidity constraints. The maturity of a number of government paper during July and the lagged effect of the June reduction in the cash reserve ratio, may improve liquidity conditions, though this may be constrained by income tax returns. The lowering of the 30-day repo twice during June is an indication that the government

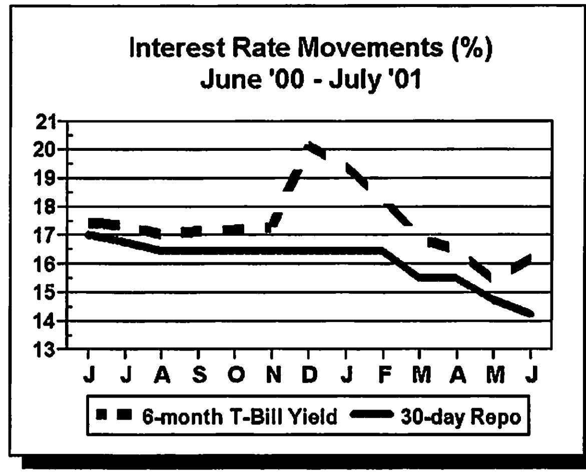

Figure 4: Interest Rate Movements

is still committed to reducing interest rates, in an attempt to achieve the interest rate targets. This may see the T-Bill rate return to its downward trend in July. Nevertheless, the most difficult period for interest rates may be approaching, based on past trends, and it remains to be seen what action government will take, and how the market will react, based on its expectations.

Inflation

Inflation rate 0.8% in May, 2.8% year to date, 6.2% pt-to-pt

The all Jamaica 'All Group' Consumer Price Index for May 2001 was 1,380.4, compared to the 1,370.0 reported for the previous month. This translates into a 0.8 percent inflation rate for May, following 0.4 percent and 0.5 percent in April and March respectively. The Calendar year-to-date rate is 2.8 percent, compared to 2.7 percent the previous year. The point-to-point rate is 6.2% compared to 9.2% in 2000.

The major contributor to May's increase was a 0.3 percent increase in the heavily weighted Food and Drink group, and a 1.8 percent increase for the Fuels and Household Supplies group. Higher prices for Vegetables and Fruit (0.7%) and Other Food and Beverages (0.6%) were the main contributor to the rise in the Food and Drink index, while a 1.8 percent increase in Fuels was responsible for the corresponding increase in the Fuels and Other Household Supplies.

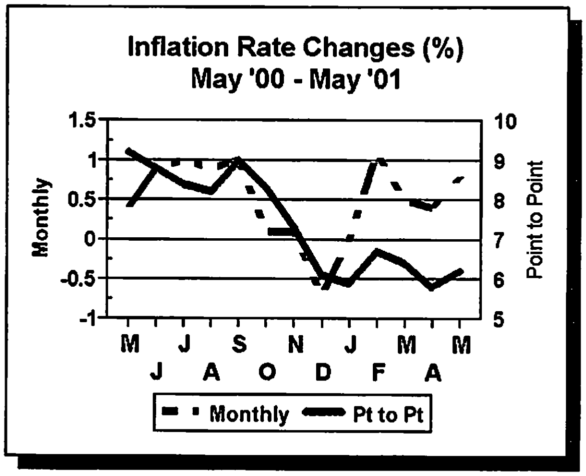

Figure 5: Inflation Rate Changes

The inflation rate for the fiscal year is 1.2% compared to 1.4% for the previous fiscal year. The inflation rate is expected to remain in single digits, and the inflation target for the 2001/02 fiscal year of 6.5% may be achieved. Continued tighter monetary policy and more favorable weather conditions compared to last year may contribute this out-turn. While OPEC has given the assurance that they will do what it takes to keep oil prices within the US$22.00 to US$28.00 range, fluctuating prices could still have a negative impact on Jamaica's inflation out-turn. The June bus fare hike may see a jump in that month's inflation out-turn. A possible hike in telephone and water rates during the latter part of the year, and seasonal back-to-school increases may also have a negative impact later during the year.

Base Money and Money Supply

Provisional figures from the BOJ showed that the monetary base declined by 0.9% to J$31,075.73M at the end of June 2001, from the J$31,351.28M recorded at the end of May 2001. For the period June 2000 to June 2001, there was a 1.8% decline, compared with the 3.7% decline recorded for the previous period. The lowering of the cash reserve ratio for commercial banks to 11% on June 1st, may have contributed to the out-turn for June.

Base money down 0.9% in June, -1.8% pt-to-pt

The nominal money supply stock increased by 0.1% at the end of April 2001 (provisional), as measured by the M2 (local and foreign currency) monetary aggregate. The M2 monetary aggregate recorded J$133,880.24M at the end of April 2001, compared with J$133,790.57M recorded at the end of March 2001. Increases in the demand deposits and savings components of money supply were responsible for this increase, which offset the marginal decline in the time and currency with the public components of the M2. The nominal money supply grew by 7.67% from April 2000 to April 2001, in contrast to the 17.0% growth recorded for the previous period. This partially reflects the fact that the authorities have continued to maintain a tighter monetary policy stance, in order to keep inflation under control.

M2 up 0.1% in April, 7.7% pt-to-pt

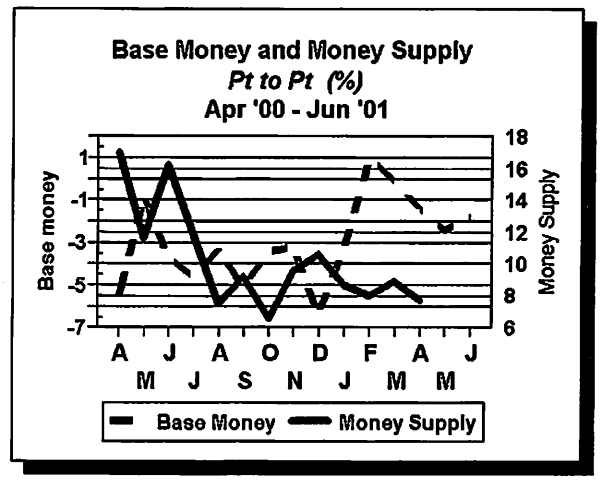

Figure 6: Base Money and Money Supply Movements

Current base money and money supply trends may be expected to continue throughout 2001, in line with the government's commitment of tighter monetary policy and base money targeting, to achieve the inflation targets. Further lowering of the cash reserve ratio during the year may facilitate government's continued control of base money and money supply.

Production of Selected Commodities

Mining: Total alumina production for the month of May 2001 was 315,690 metric tonnes. This represented increases of 2.29% and 4.97% over production figures for 2000 and 1999 respectively. Total year- to-date production was 1,541,484 metric tonnes, 2.87% and 6.24% above the year-to-date outcomes of 2000 and 1999 respectively.

Alumina prod up 2.87%, Bauxite up 55.47%, Jan-May

Total Crude Bauxite production was 310,823 metric tonnes, 47.99% more and 4.22% less than production in May 2000 and May 1999, respectively. The year-to-date production of Crude Bauxite was 1,494,771 metric tonnes, 55.47% above and 8.68% below 2000 and 1999's production figures respectively.

Alumina exports were 291,107 metric tonnes for the review period, which represented a 6.65% and a 1.93% reduction compared to the export figures for May 2000, and May 1999 respectively. The year-to-date alumina exports amounted to 1,487,643 metric tonnes, 4.17% below and 4.82% above 2000 and 1999 export figures, respectively.

Exports of crude bauxite for May 2001 were 264,723 metric tonnes and represented an increase of 26.84% and a decline of 19.95% compared to recorded exports in May 2000 and May 1999, respectively. Total year-to-date exports were 1,490,292 metric tonnes, 49.92% above and 9.91% below the corresponding period in 2000 and 1999, respectively.

Sugar: Total sugar production for May 2001 was 17.79% above that of May 2000, recording 30,590 tonnes in comparison to the 25,970 tonnes recorded in the corresponding 2000 period. This is the first positive performance for sugar production in 2001, and may well be signaling recovery from adverse weather conditions in during 2000.

Banana up 36%, Sugar up 17.8%, in May

Banana: Total Banana production for May 2001 was 35.96% above that of May 2000. May's production was 4,310 tonnes compared to the 3,170 tonnes produced in May 2000. Banana production has been on the rebound since the beginning of 2001, and appears to have fully recovered from the adverse weather conditions of 2000.

Cement up 40.5% in June

Cement: Total cement production for June 2001 was 40.52% above that of June 2000. Production for June 2001 recorded 51,073 tonnes compared with 36,345 tonnes in June 2000. June's production was 5.7% below the 54,183 tonnes produced in May. The total year-to-date production was 304,721 tonnes, 27.62% above production over the similar period in 2000.

External Trade

Trade deficit widen by US$80M, Exports down US$46M

The deficit on the external trade account widened by US$80.38M over the first quarter of calendar year 2001, in comparison to the corresponding period in 2000. Total goods imports (c.i.f.) increased by US$34.33M (4.1%), while total goods exports (f.o.b.) declined by US$46.05M (- 11.6%) *See Table 3.*

Exports: Total goods exports (f.o.b.) for the review period were valued at US$352.29M, down US$46.05M. The decline of US$32.55M (-9.5%)

	Jan-Mar 00	Jan-Mar 01	Change	% Change
Total Exports (fob)	**398.34**	**352.29**	**-46.05**	**-11.56**
Major Traditional	232.79	215.20	-17.59	-7.56
Other Traditional	172.74	190.04	17.30	10.02
Non-Traditional	80.67	67.28	-13.39	-16.60
Re-Exports	10.83	7.52	-3.31	-30.56
Freezone Exports	47.48	35.48	-12.00	-25.27
Goods Procured in Ports	9.30	7.80	-1.50	-16.13
Total Imports (cif)	**832.06**	**866.39**	**34.33**	**4.13**
Consumer Goods	219.13	225.73	6.60	3.01
Raw Materials	422.31	454.94	32.63	7.73
Capital Goods	149.87	157.92	8.05	5.37
Free-zone Imports	31.26	19.69	-11.57	-37.01
Goods Procured in Ports	9.50	8.10	-1.40	-14.74
Trade Balance	**-433.72**	**-514.10**	**-80.38**	**18.53**

Table 3: External Trade, January - February 2001

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in general merchandise exports was largely responsible for this out-turn, which was influenced by respective declines of US$17.58M (-7.6%), US$13.39M (-16.6%) and a US$1.73M (10.0%) increase, in major-traditional, non-traditional and other-traditional exports respectively.

Earnings from alumina, sugar and bananas down 8%, 32% and 12% resp.

Decreased earnings of US$13.67M (-8.0%), US$13.87M (-31.9%) and US$0.63M (-12.3%) from alumina, sugar and bananas respectively, were responsible for the decline in the major traditional group. These declines continued to offset the strong rebound in bauxite, which increased by US$10.58M (80.9%) over the period. The rebound in bauxite may be attributed to the return to normal operations at the Gramercy plant, leading to a 41.42% increase in volume, while benefiting from a 28.0% increase in price. Alumina earnings continued to be affected by weaker demand, leading to a slump in price (-6.7%) and volume (-1.4%). Alumina production actually increased by 2.5% in March, but suffered from a 13.0% price slump. Sugar and Bananas were both down by 7.2% and 21.8% in price respectively. The price slump in bananas is having a significant impact, as volume had actually increased by 11.83% over the first quarter.

Continued strong growth in earnings from coffee (33.2%) and an improved performance from Rum (30.2%) were mainly responsible for the positive out-turn in the other traditional exports subgroup, which increased by 10.0%. However, coffee prices have begun to weaken, which led to a 26.3% decline in exports for March.

The 16.6% downturn in non-traditional exports was largely driven by declines in crude materials (-1.7%), food (14.8%), chemicals (-30.8%), and miscellaneous manufactures (-25.1%) exports.

Imports: Total imports (C.I.F.), for the first quarter, were valued at US$551.29M, an increase of US$36.12M over the corresponding period in 2000. An increase of US$47.29 (6.0%) in merchandise purchases was largely responsible for this out-turn, which was partially offset by an US$11.56M (-37.0%) decline in free-zone imports.

Within the general merchandise category, the C.I.F. value of raw materials increased by US$32.63M or (7.7%). The increase in raw material imports was reflective of a US$36.02M (13.2%) rise in the value of other raw material imports. Of great significance is the US$3.38M (-2.3%) decline in the fuel import bill, which mainly reflected a 21.0% decline for fuel used in bauxite operations. There was a 25.5% reduction for March 2001. In comparison, the first quarter in 2000 had recorded a US$78.98M (128.7%) increase in the fuel import bill, over the corresponding 1999 period.

Fuel import bill down 2.3%, raw materials up 7.7%, capital goods up 5.4%

The capital goods category increased by US$8.06M (5.4%), mainly reflecting a US$23.27M (34.7%) increase in machinery, while all other sectors declined by more than 14.0%, with motor cars declining by a whopping 94.4%. Consumer goods increased by US$6.6M (3.0%), reflecting increases in Food US$4.12M (6.4%) and Durables US$1.57M (1.8%). Most of the above increase in consumer goods came about in the last month of the quarter, advancing by US$5.58M (7.3%).

Balance of Payments

Current A/C deficit widen by US$58M

The current account recorded a deficit of US$134.1M for the first quarter of calendar year 2001, in contrast to the deficit of US$33.1M recorded for the corresponding period in 2000. This resulted in a decline of US$101.0M on the balance for the review period. However the current account showed slight improvement for the fiscal year ending March 2001, with the deficit declining by US$3.4M.

The deficit on the goods balance widened by US$73.4M for the first quarter. This out-turn resulted from a US$27.3M increase in imports (f.o.b.) and an US$46.1M decline in exports (f.o.b.) for the review period (*Table 4*).

Services a/c balance up US$1.9M

The services account balance declined by US$1.9M increase for the review period. This was due to increased transportation charges (US$3.7M) and costs for other services (US$10.5M). These costs were sufficient to offset increased net travel receipts of US$12.3M.

For the income account, a negative US$37.9M change in investment income accounted for the US$36.2M decline. The US$10.5M increase in net current transfers was influenced by an expansion in private transfer flows of US$24.7M which was partially offset by US$14.2M contraction in official transfers. Private transfer flows continue to reflect strong remittance inflows which increased by US$26.9M (27.9%), while the contraction in official transfers reflects the absence of exceptional payments for cellular licenses in 2000.

The improvement in the capital and financial account mainly reflected activity in the financial account, which increased by US$106.7M. The surplus on the Other Official and Private Investment accounts together with the capital account were more than sufficient to offset the deficit on the current account, resulting in a US$316.8M increase in reserves.

Outlook - The First Six Months and Beyond

NIR expected to remain buoyant

The NIR has continued its tremendous record breaking run through the first half of 2001. Loan inflows of over US$570 million and purchases of over US$670 million have been responsible for this out-turn through the first half 2001. While the NIR may not be expected to increase as much during the second half of the year - due to debt obligations - further divestment proceeds from the sale of FINSAC assets, bond issues and the draw-down of loans from the multilateral organizations, should keep the reserves buoyant. There should be little difficulty in achieving the SMP NIR target of US$1,555 million for fiscal year 2001/02. However,

Table 4: Balance Of Payments (US$M), January to March 2001

	Jan-Mar 00	Jan-Mar 01	Change	% Change
Current A/C	-33.1	-134.1	-101	305.14
Goods Balance	-317.4	-390.8	-73.4	23.13
Exports (fob)	398.4	352.3	-46.1	-11.57
Imports (fob)	715.8	743.1	27.3	3.81
Service Balance	174.8	172.9	-1.9	-1.09
Transportation	-47.7	-51.4	-3.7	7.76
Travel	292.9	305.2	12.3	4.20
Other Services	-70.4	-80.9	-10.5	14.91
Income	-93.6	-129.8	-36.2	38.68
Compensation	3.8	5.5	1.7	44.74
Investment	-97.4	-135.3	-37.9	38.91
Current Transfers	203.1	213.6	10.5	5.17
Official	34.5	20.3	-14.2	-41.16
Private	168.6	193.3	24.7	14.65
Capital & Fin. A/C	33.1	134.1	101	305.14
Net Capital Movement	9.1	3.4	-5.7	-62.64
Official	7.3	2.5	-4.8	-65.75
Private	1.8	0.9	-0.9	-50.00
Financial A/C	24	130.7	106.7	444.58
Other Official Investment	156.7	114.3	-42.4	-27.06
Other Private Investment	120.6	333.2	212.6	176.29
Reserves	-253.3	-316.8		

heavy central bank intervention may be required during the last four months of 2001, to stem potential volatility and maintain relative stability in the foreign exchange market, if interest rates are to continue their downward trend. This may somewhat offset the strong growth in the NIR.

Relative FX market stability may be expected over short term

The foreign exchange market (J$/US$) has shown the most resilience since 1998, depreciating by only 0.63% or J$0.29 over the first half of 2001. This compares with declines of 2.77% and 4.86% over the first half of the two previous years. However, most of the damage to the domestic currency has occurred over the second half of previous years, depreciating by 7.09% ($3.02), and 6.29% ($2.45) for 2000 and 1999 respectively. However, compared with previous years, the economy may be adjudged to be in better shape, and investor confidence, one of - if not the most - important market forces, has improved somewhat. The government's record breaking NIR levels has lent credence to the position that the dollar is backed - at least to some extent - and that this may well lead to maintenance of a relatively stable market over the usually volatile last four months, while allowing interest rates to fall. That credibility was lacking the previous three years.

Interest rate decline may depend on FX stability

The first half of 2001 has seen the government consistently reducing interest rates *(see Interest Rates)*, in tandem with its SMP agreement. Although a similar pattern was followed for the first half of each of the past three years, before stagnating or being reversed in the latter half of the year, the out-turn in 2001 seems as if it is on the threshold of being reversed, although only time will tell. The possibility of a relatively stable foreign exchange market during the latter half of the year, may be "*the key*" to the reversal of previous trends. This of course is being helped by improved liquidity conditions, lower U.S. interest rates and a consistent inflation rate. The slight hiccup in the downward trend of the market determined 6-month T-Bill rate may be temporary. Even if the authorities are unable to achieve the SMP target of 12.9% by the end of this fiscal year, consistently reducing the rates throughout the entire year, and getting as close to the SMP target as possible, will significantly improve market confidence, investment and government's fiscal program.

No major change expected in monetary policy

The authorities may not expected to make any significant changes in monetary policy, as they work toward achieving the inflation target. Thus tighter control of base money and money supply may be expected to continue throughout the rest of the year. If the improved weather conditions during the first six months of 2001 continues throughout the year, this should temper inflationary pressures from the heavily weighted food and drink group compared to last year. The inflationary shock from higher world oil prices has been tempered, with oil prices actually falling over the past two months.

Building Foreign Exchange Credibility?

During the first half of 1999, the NIR had actually declined year-on-year, by US$15.3 million, to the end of June 1999. At the end of the first half of 2000, despite increasing by US$165.9 million year-on-year, and attaining a record level the previous month, these achievements might have come too late in the year. Further, there were the added problems of a record breaking increase in the import fuel bill and an ill-fated US$ bond issue during the latter half, both of which brought tremendous pressure to bear on the local currency. However at the end of the first quarter of 2001, not only had the NIR achieved record levels and easily surpassed the SMP target, but the year-on-year increase was US$582.8 million - only US$170 and US$8 million, less than the entire stock of NIR at the end of the first half of 2000 and 1999 respectively. At the end of the first half of 2001, the NIR is US$784 million (or twice) above June 2000, and US$949 million above June 1999. Meanwhile, interest rates have attained their lowest levels in over ten years. These developments may have improved the government's credibility (albeit at a very high cost to the economy), to simultaneously maintain a relatively stable exchange rate, while lowering interest rates, over the upcoming latter half of the year - a feat not achieved for quite some time.

This was mainly driven by higher inventory levels and the recent resumption of oil exports by Iraq. Further, OPEC has committed to maintaining oil prices within US$22 and US$28 for the remainder of the year.

No change in economic fundamentals

The major economic fundamentals - as captured by the external trade and balance of payments accounts - have not shown any improvement in their overall out-turn through the first quarter. However, their composition may have changed somewhat, which may point to the reversal of some trends during the latter part of the year.

-ve out-turn in exports may be reversed toward latter part of 3rd qtr, with possible recovery in alumina

For the external trade account, the major weakness over the first quarter was the 11.6% decline in goods exports, compared with a 15% expansion this time last year, over the period in 1999. A weaker than expected out-turn from alumina, - which accounts for almost half the export earnings from external trade (44.7% for the first quarter) - a continued decline in sugar and nontraditional exports, were responsible for this out-turn (*see External Trade*). Weaker world prices and consequently lower volume, have affected earnings from both alumina and sugar. Sugar may be expected to recover somewhat towards the third quarter (overall production up 18% in May), given more favorable weather conditions, although prices are expected to remain weak. Alumina prices could rebound somewhat during the third quarter, with a possible improvement in the U.S. Economy during that period. A rebound in alumina prices could single-handedly reverse the negative trend of exports, given its heavy contribution to overall earnings. Of course, the converse is also true.

Another significant feature of the first quarter external trade data, is the composition of imports. While imports are still expanding, the expansion is much slower (4.1%) than last year this time (16.8%). The most significant feature of this out-turn is the decline in the fuel import bill. The increase in the first quarter fuel bill stood at a whopping US$78.98 million in 2000, which is more than twice the increase for total goods imports in the first quarter of 2001. Put another way, it is only US$1 million less than the first quarter increase in the value of total trade for 2001. The fuel bill has actually declined by US$3.38 million (-2.3%), which is mainly due to world oil prices being maintained within OPEC's US$22 to US$28 price band. A possible continuation of this trend throughout the remaining three quarters may see a declining growth in overall imports, and less pressure on the foreign exchange market especially during the last quarter.

Imports of raw materials for food (14.3%) and other raw materials (11.0%) have expanded somewhat, which may be indicating a slightly expanding economy, although it is still too early to be conclusive. Imports of construction capital goods are down 22.5%, indicating a weak construction sector over the first quarter, and imports of motor cars declined by 94.4%. However, overall capital goods have increased, and if these trends continue throughout the year, may be indicators that the economy is jump-starting.

The deficit on the balance of trade may be expected to widen even further over the second quarter, as imports continue to outweigh exports. However, there may be a possible third quarter recovery in exports, which may temper the decline in the balance somewhat. The widening trade balance may be expected to continue impacting negatively on the current account balance, at least through the third quarter of 2001.

Table 5: Major Macro-Economic Indicators
January 1999 - June 2001

	BM		M2		NIR	Fx Dep	CPI		Tourism	J$/US$	Tbill	Loan	Sav	Dom Debt	Fx Debt
	M	P	M	P	US$M	US$M	M	P	P		%	%	%	J$M	US$M
Jan-99	-3.7	0.0	-0.6	8.3	578.0	977.3	0.4	7.5	9.65	37.45	22.62	38.46	12.25	132,782.90	3,289.40
Feb	0.6	-0.5	0.8	9.9	578.5	921.1	-1.1	6.3	7.95	37.75	21.85	38.47	12.19	136,282.96	3,264.90
Mar	-3.7	-2.8	1.2	12.0	581.5	960.3	0.5	5.4	17.98	38.23	21.67	38.60	12.09	139,203.68	3,215.70
Apr	0.8	-3.0	20.8	11.0	587.4	979.3	-0.1	5.5	-0.09	38.27	21.32	39.00	12.33	146,554.27	3,184.30
May	-4.2	-7.8	3.9	14.2	590.5	965.8	0.9	5.6	-0.09	38.61	21.32	39.00	12.33	147,911.39	3,167.00
Jun	-0.1	-8.5	2.1	11.8	590.6	956.8	1.3	5.0	3.43	38.96	20.16	37.89	11.96	148,688.52	3,161.80
Jul	1.7	8.2	3.6	15.5	487.0	1,032.6	1.2	5.1	-0.67	39.47	20.04	36.50	11.50	153,193.82	3,036.00
Aug	-0.7	-7.1	4.7	18.5	490.8	1,033.3	1.1	5.1	2.70	39.71	20.63	36.50	11.50	158,948.56	3,030.10
Sep	-1.6	-8.7	-0.7	15.6	526.2	1,014.7	0.3	5.3	9.28	39.88	19.21	35.92	11.50	161,571.93	3,035.00
Oct	0.4	-9.2	2.6	18.5	492.8	1,016.2	0.8	6.4	14.64	40.05	19.19	33.92	11.38	163,443.11	3,076.00
Nov	0.6	-4.5	-0.5	19.5	506.7	949.3	1.0	7.4	15.45	40.57	19.19	33.92	11.38	168,730.78	3,049.30
Dec	16.5	4.0	3.0	19.1	450.2	956.5	0.5	6.8	-2.66	41.27	22.03	33.92	11.38	176,717.47	3,024.10
Jan-00	-12.5	-5.5	-0.5	19.2	453.1	990.1	0.2	7.8	-1.47	41.75	20.54	33.92	11.38	178,340.93	2,971.00
Feb	-2.3	-8.2	0.2	18.5	590.6	1,057.6	0.4	8.2	12.10	42.25	20.05	33.92	11.38	175,492.98	3,133.10
Mar	-2.8	-7.4	0.9	18.1	703.5	1,047.1	0.7	8.4	12.05	42.15	17.96	33.92	11.38	175,322.74	3,164.80
Apr	2.9	-5.5	1.2	17.2	744.0	1,052.9	1.0	9.6	12.76	42.07	17.58	33.67	11.38	176,599.44	3,098.20
May	0.6	0.8	-0.7	11.9	776.3	1,047.3	0.4	9.2	16.93	42.29	17.64	33.67	10.90	177,180.13	3,054.70
Jun	3.6	3.7	1.6	16.2	756.5	1,042.1	0.9	8.8	10.89	42.51	17.47	33.00	10.11	181,578.09	3,053.70
Jul	0.8	4.6	-0.3	11.8	788.7	1,050.3	1.0	8.5	9.20	42.70	17.32	33.00	10.11	189,222.03	3,018.60
Aug	0.6	-3.3	0.9	7.7	935.5	1,082.5	0.9	8.2	23.29	42.89	17.04	32.75	10.11	189,666.78	3,003.80
Sep	-3.4	-5.1	1.8	9.1	935.5	1,072.4	1.0	9.0	7.58	43.85	17.13	31.50	9.96	184,337.90	3,208.60
Oct	1.4	-3.4	0.3	6.6	845.7	1,065.0	0.1	8.3	7.60	44.71	17.13	31.67	9.86	181,507.81	3,208.81
Nov	0.9	-3.2	1.1	9.6	831.7	1,077.1	0.1	7.3	9.88	45.08	17.28	31.67	9.86	184,795.00	3,265.20
Dec	12.7	-6.4	2.4	10.6	969.3	1,111.3	-0.7	6.1	8.20	45.48	20.16	31.67	9.86	187,520.03	3,375.30
Jan-01	-9.5	-3.2	-0.3	8.7	931.2	1,115.7	0.0	5.9	10.07	45.67	19.41	32.18	9.86	193,616.74	3,492.06
Feb	1.9	1.0	-0.5	8.0	1,106.6	1,128.5	1.1r	6.7r	2.82	45.76	18.27	32.18	9.86	190,384.80	3,636.78
Mar	-3.8	-0.1	1.4	8.9	1,286.3	1,117.3	0.5r	6.4	-0.08	45.70	16.88	31.33	9.84	215,084.05	3,620.40
Apr	1.6	-1.4	0.1	7.7	1,281.8	1,130.5	0.4	5.8	4.24	45.68	16.50	31.21r	9.84	n/a	n/a
May	-0.5	-2.4	n/a	n/a	1,480.6	1,152.64	0.8	6.2	n/a	45.77	15.46	30.88	9.50	n/a	n/a
Jun	-0.9	-1.8	n/a	n/a	1,540.5	n/a	n/a	n/a	n/a	45.77	16.2	30.67	9.45	n/a	n/a

<u>Key:</u>

BM - Base Money	M2 - Money Supply
NIR - Net International Reserves	FX Dep - Foreign Exchange Deposit
CPI - Consumer Price Index	Tourism - Total Tourist Arrivals
Tbill - 6-month Treasury Bill Yield	Loan - Average Loan Rate
Save - Average Savings Deposit Rate	M - Monthly percentage Change
P - Point-to-Point Percentage Change	r - Revised
n/a - Not Available	

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