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Jamaica: 2007 Article IV Consultation—Staff Report; Staff Supplement; Public Information Notice on the Executive Board Discussion; and Statement by the Executive Director for Jamaica

Under Article IV of the IMF's Articles of Agreement, the IMF holds bilateral discussions with members, usually every year. In the context of the 2007 Article IV consultation with Jamaica, the following documents have been released and are included in this package:

- the staff report for the Article IV consultation, prepared by a staff team of the IMF, following discussions that ended on February 16, 2007**,** with the officials of Jamaica on economic developments and policies. Based on information available at the time of these discussions, the staff report was completed on April 11. 2007. The views expressed in the staff report are those of the staff team and do not necessarily reflect the views of the Executive Board of the IMF;
- a staff supplement of April 20, 2007 updating information on recent developments;
- a Public Information Notice (PIN) summarizing the views of the Executive Board as expressed during its April 30, 2007 discussion of the staff report that concluded the Article IV consultation; and
- a statement by the Executive Director for Jamaica.

The policy of publication of staff reports and other documents allows for the deletion of market-sensitive information.

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INTERNATIONAL MONETARY FUND

JAMAICA

Staff Report for the 2007 Article IV Consultation

Prepared by the Staff Representatives for the 2007 Consultation with Jamaica

Approved by Caroline Atkinson and Anthony Boote

April 11, 2007

Background. Jamaica is a large Caribbean economy with high debt and a complex financial system. In 2004 the government adopted a medium-term plan to reduce debt through fiscal consolidation.

Developments. Recent economic performance has been remarkably strong: growth of nearly 3 percent during FY 2006/07 (April to March) was the best in over a decade; annual inflation fell to 6 percent in January, compared to the target of 9½ percent for FY 2006/07; and external reserves reached historical highs before declining some in recent months. The overall improved economic picture notwithstanding, the budget deficit target for FY 2006/07 was likely missed by a large margin, mostly on account of higher expenditures.

Policy recommendations. The key issue is debt reduction, where progress has not lived up to expectations laid out in the authorities' medium-term plan. Discussions focused on the need to reinvigorate the debt strategy. The staff urged the authorities to seize the opportunity afforded by today's still benign external environment to build up resilience to shocks, while initiating deep structural reforms to anchor the debt strategy.

- **Fiscal policy**. Measures to increase the central government primary surplus and improve the resiliency of the debt profile to shocks.
- **Monetary and exchange-rate policies**. Build on the developing credibility of monetary policy by introducing greater flexibility to both exchange and interest rates.
- **Financial sector**. Enhance the supervision of activities exposed to interest rate risk. Maintain vigilance against pyramid schemes.
- **Structural reforms**. Make the debt strategy durable through reforms to the tax system, public wage and employment, public entities, the financial sector, and the business environment.

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I. INTRODUCTION

1. **Jamaica adopted an ambitious medium-term program of fiscal consolidation in 2004 to reduce public debt from over 140 percent of GDP to 100 percent by 2009**. Under this program, the government aimed to raise the central government primary balance to 13¾ percent of GDP during FY 2004/05 (compared to 7⅓ percent two years earlier) and to keep it broadly at that level throughout the medium term. Although fiscal targets have not been fully met each year since (including on account of natural disasters), some progress was made during 2004–05 in reducing debt, which currently stands at about 132 percent of GDP.[1]

2. **Exposure to the risk of shocks, nevertheless, remains pronounced—a situation that the authorities are managing delicately**. Jamaica's public debt is still very high in international comparison (Figure 1). The debt is sensitive to exchange rate as well as domestic interest rate changes. And, with the pace of money demand growth lower than that of reserve accumulation, the outstanding stock of short-term central bank sterilization bills has increased markedly since 2003. With inflation declining and motivated by debt costs and the adverse impact on growth, the Bank of Jamaica (BOJ) has steadily lowered interest rates, while also seeking to keep its sterilization bills sufficiently attractive against increased U.S. rates. The bulk of Jamaica's current account deficit is financed by sustainable foreign direct investment. Nevertheless, private flows and external public borrowing remain significant. In this regard, the still benign global conditions have been important in helping maintain this delicate balance.

3. **Elections may be imminent and are expected to be closely fought**. In early 2006, Ms. Simpson-Miller emerged victorious in an internal contest for the leadership of the governing People's National Party (PNP) and took over as prime minister. General elections are constitutionally required by October 2007. While there is a grace period of three months, the elections may also be called earlier. A recent poll shows both the PNP and the opposition Jamaica Labor Party enjoying the support of 31–32 percent of registered voters, with most of the remainder still undecided.[2]

4. **Fund advice to Jamaica has in recent years reinforced the authorities' own home-grown policy framework**. Noting the high sensitivity of the debt dynamics to macroeconomic volatility and market sentiment, past consultations have emphasized the importance of fiscal consolidation in creating a virtuous cycle of reduced debt and improved living standards. The authorities have been advised to use monetary policy preemptively to

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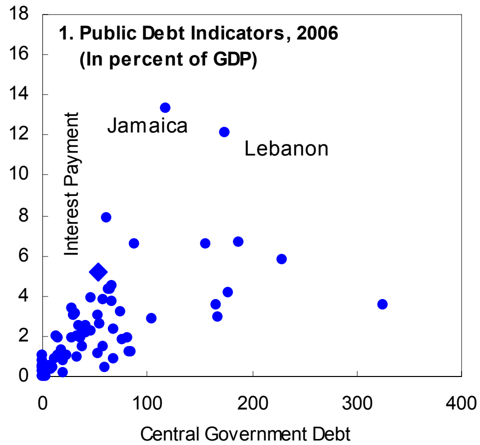
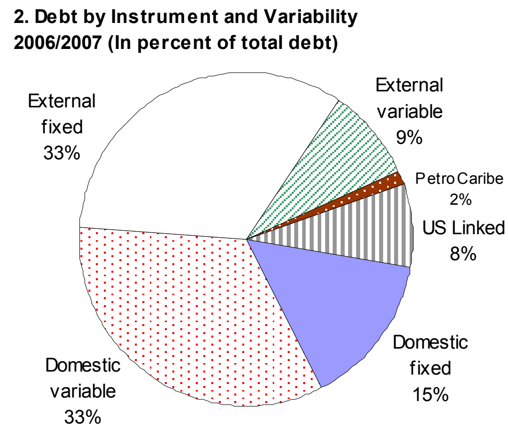
[1] Excluding a recent bond (amounting to about 3 percent of GDP) to pre-finance FY 2007/08 obligations.

[2] Jamaica Gleaner, January 22, 2007.

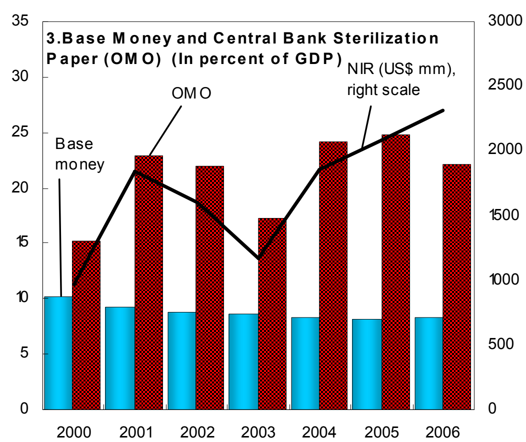
Figure 1. Jamaica: Key Macroeconomic Indicators

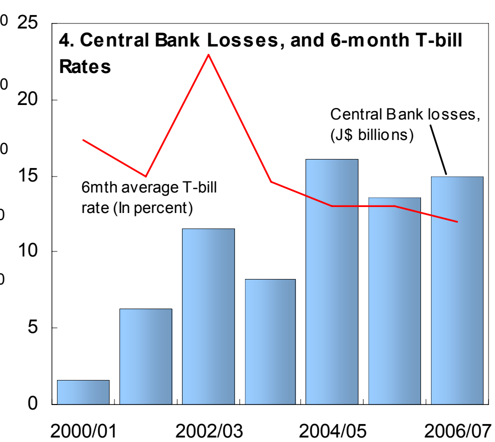
Jamaica's high debt burden is sensitive to exchange rates and domestic interest rates,...



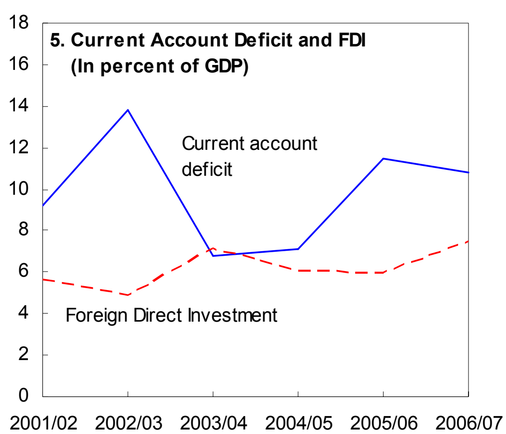


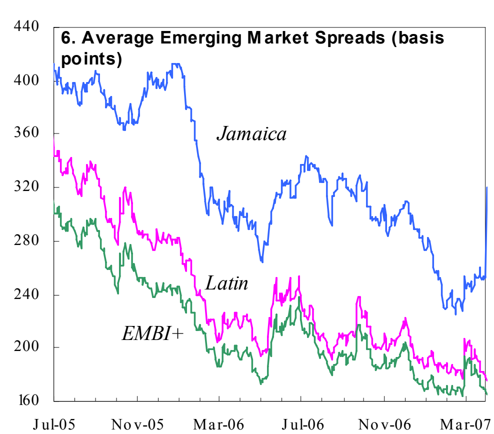
...while central bank losses reflect the costs of sterilizing reserves,...





...which have increased since 2003 in a benign external evironment.



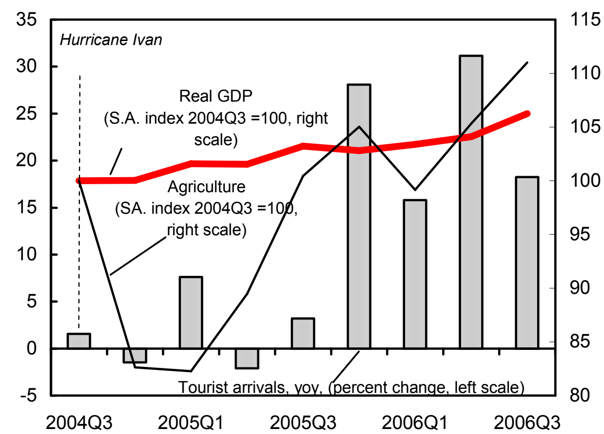


Sources: National authorities; and Fund staff estimates.

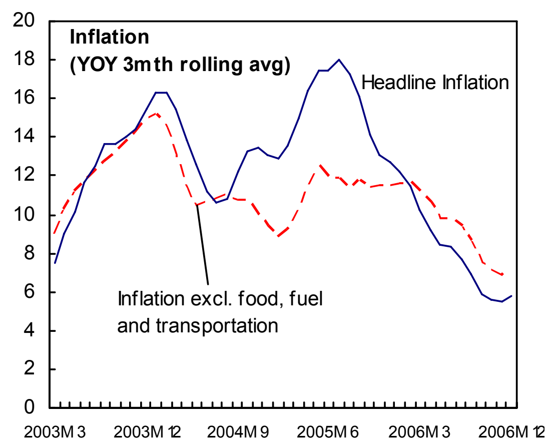
ease pressures. While there has generally been consensus between the Fund and the authorities on overall objectives, views have differed at times on the extent and timing of specific policy actions.

II. Recent Developments

5. **Jamaica is estimated to have achieved its best growth performance in over a decade this past year**. Underpinned by agriculture and tourism, real economic growth of almost 3 percent is estimated for FY 2006/07 (which runs from April to March), up from 2 percent the previous year and 0.4 percent the year before.



6. **The BOJ has successfully lowered inflation without constraining the economic recovery**. Annual inflation has fallen to 6 percent, compared to the FY 2006/07 target of 9½ percent and a recent high of over 19 percent in September 2005.



7. **The external current account balance is improving**. The FY 2006/07 current account deficit is estimated at 10½ percent of GDP—down from 11½ percent the previous year, due to strengthening exports, as well as robust remittances and tourism.

8. **The exchange rate remained broadly stable during 2006 but came under some pressure early this year**. Through most of 2006, capital inflows enabled the BOJ to purchase foreign exchange in the market without putting excessive pressures on the exchange rate. All in all, the nominal bilateral rate vis-à-vis the U.S. dollar depreciated by under 4 percent (year-on-year) during 2006. At the same time, with inflation declining, the BOJ steadily eased monetary policy by removing special deposit requirements for banks and reducing interest rates in three steps during May–December 2006. Annual base money growth accelerated to 17.3 percent at end-2006, compared to 9.3 percent a year earlier. With the local currency yield premium virtually non-existent, however, markets became unsettled in January 2007 in anticipation of a large redemption of government bonds. The BOJ issued special bills to mop up liquidity and stepped up sales of foreign exchange even as it allowed the exchange rate to depreciate at a somewhat quickened pace for some time. Reserves continued to decline some through February but the exchange rate has remained broadly stable again in recent weeks.

9. **Financial sector soundness indicators remain robust despite a search for high yields**. A worrisome development has been the apparent growth of unregulated foreign currency trading schemes promising spectacularly high returns. Bank credit to the private sector has been expanding at double digit rates in real terms annually. Nevertheless, prudential indicators for both banks and other regulated financial institutions remain sound.

10. **The overall strong economic picture notwithstanding, the budget deficit target for FY 2006/07 was likely missed by a large margin, mostly on account of higher expenditures**. Revenues increased markedly over last year, but have still been short of the ambitious targets set out in the budget. More substantively, expenditures for the year as a whole are likely to have exceeded budgeted amounts by at least 1¾ percentage points of GDP, and possibly by as much as 2½ percentage points of GDP. As a result, the primary surplus has fallen to about 8–8¾ percent of GDP and the debt ratio likely declined only marginally, if at all.

11. **Mid-year expenditure increases occurred in a number of categories**. Parliament recently approved supplementary estimates for higher wages, pensions, and travel allowances as well as for other current items, including natural disaster insurance premia. A new two-year wage agreement with unions accommodated larger wage increases for nurses and teachers than had been expected. Other expenditure overruns reflect a variety of factors, including voter registration and increased security spending in connection with the Cricket World Cup.

	FY 2006/07 (Ten Months)			FY 2006/07 (Full year)		
	Budget	Act.	Dev.	Budget	Rev.	Dev.
	(In percent of GDP)					
Budget balance	-4.3	-5.4	-1.1	-2.7	-4.7	-2.0
Revenue and grants	24.0	23.7	-0.3	30.4	30.1	-0.3
Non-interest current expenditure	13.9	14.9	1.1	16.5	18.0	1.5
Of which: wages and salaries	8.4	9.1	0.7	10.1	11.0	0.9
Interest expenditure	10.9	11.5	0.5	12.8	13.5	0.7
Capital Expenditure	3.5	2.7	-0.8	3.7	3.3	-0.5
Memo: GDP (in billions of J$)	722	709		722	709	

All in all, non-interest current expenditures were increased by 1.5 percentage points of GDP. Interest payments are also likely to have ended the year about ¾ percentage points of GDP higher than budgeted. To some extent, the expenditure increases were offset in the supplementary estimates by lower capital spending but the latter is likely to be a statistical aberration—the authorities estimate that J$5 billion (0.7 percent of GDP) in capital spending may be underreported for this year due to teething problems with new reporting procedures, which resulted in delays in the verification of some donor-funded projects. Including these amounts as FY 2006/07 expenditures could lead to a deficit as much as 2¾ percent of GDP higher than originally budgeted.

12. **Exposure of the public debt to changes in exchange rates and interest rates has increased in recent years**. Presently, Jamaica's public debt is almost evenly split between domestic and foreign currency denominations while variable rate instruments account for

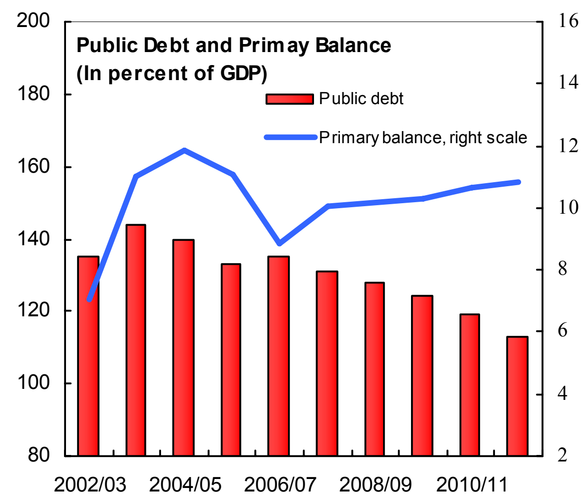
Figure 2. Jamaica: Prudential Indicators of the Financial System, 2001–06
(Year-end, in percent)

Sources: National authorities; and Fund staff estimates.
1/ Includes, in addition, building societies and merchant banks/finance companies.
2/ The 2006 figure for securities firms is as of end-September.

about 40 percent of the total portfolio.[3] About three quarters of the debt stock is owed to private creditors, including, in particular, the domestic financial system (commercial banks, merchant banks, security dealers and others). Over the past two years, the share of the debt that is sensitive to exchange rate movements increased by 1½ percentage points while the interest-sensitive portion increased by almost 8 percentage points.

III. Medium-Term Outlook

13. **The outlook depends critically on the authorities' commitment to reducing debt**. Given that little, if any, progress was made in reducing debt during FY 2006/07, a resumption of progress during this fiscal year would ensure continued confidence in the authorities' strategy. This, in turn, would help sustain the currently favorable domestic economic conditions and enable further progress at debt reduction over the medium term. On the other hand, insufficient progress in tackling the debt problem could, through its potential impact on confidence, leave open the possibility of a reversal in the dynamics in the wake of even a small shock. This, in turn, could create a situation where the authorities' strategy could quickly unravel.

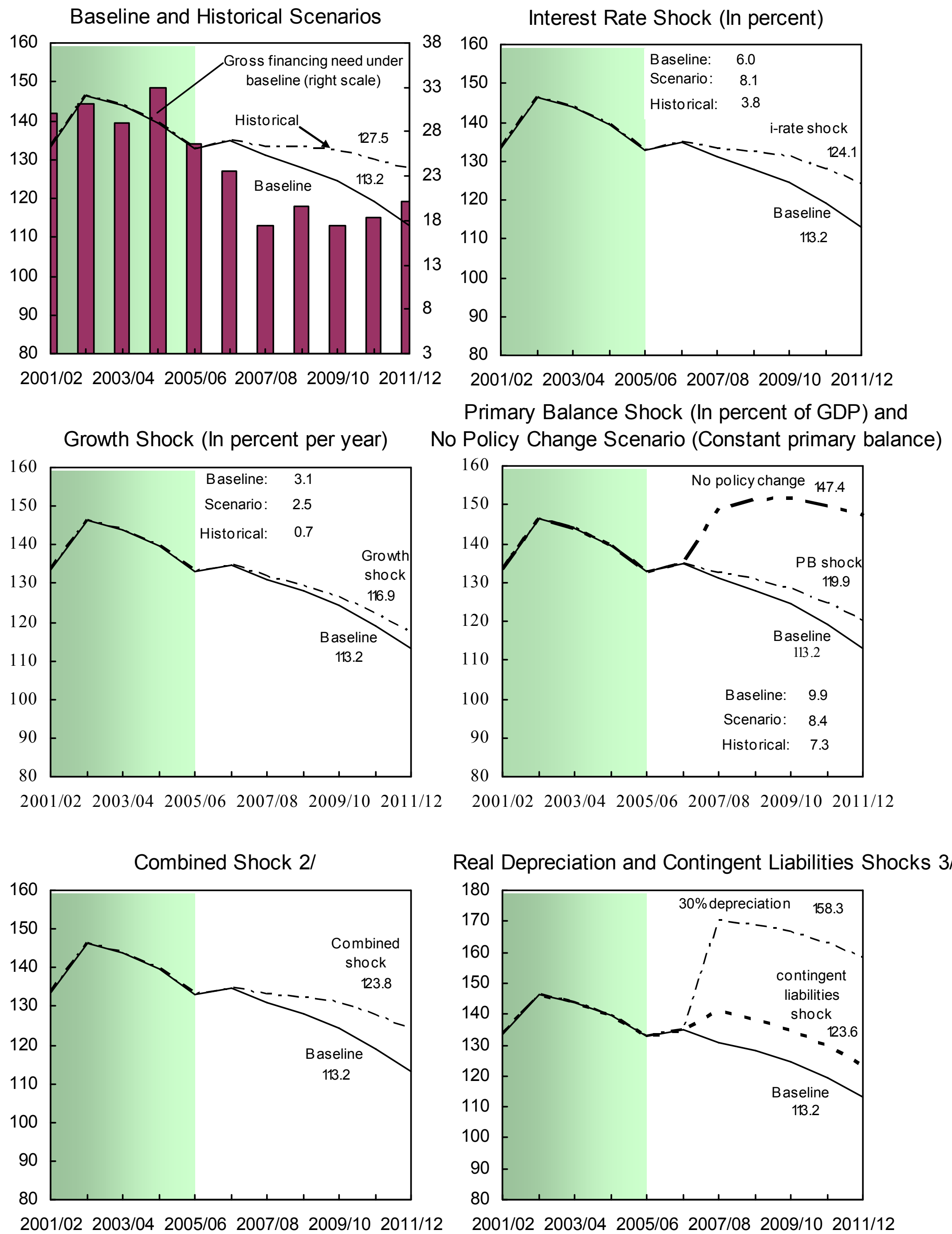


14. **An illustrative scenario prepared by the staff suggests that debt could come down to about 113 percent of GDP by 2012 with decisive policy action**. Raising and maintaining the primary surplus at 10–10½ percent of GDP would, in combination with fiscal discipline of extra-budgetary entities, enable a gradual reduction in the debt ratio. To the extent that the primary surplus were higher—say, along the lines envisaged in the authorities' original strategy—the debt ratio would be commensurately lower. The debt reduction would remain robust to exogenous shocks of limited magnitude (Figure 3). For example, a permanent interest rate shock one-half standard deviation of the historical average would significantly slow the pace of decline, but would still leave debt 10 percentage points of GDP lower in five years.

15. **The analysis also underscores the critical role of confidence, including in the context of a financial system that remains exposed to risks**. A 30 percent weakening of the currency, for example, would lead the debt ratio to quickly climb to 170 percent of GDP. Thereafter, if all other factors remained equal, the debt ratio would resume declining, albeit to a level still significantly higher than at present. However, a confidence shock of such

[3] The share of variable debt in domestic currency debt is higher (see Box 1).

Figure 3. Jamaica: Public Debt Sustainability: Bound Tests 1/
(Public debt in percent of GDP)



Sources: International Monetary Fund, Country desk data, and staff estimates.
1/ Shaded areas and the Baseline projection line represent actual Central Government Debt data. Individual shocks are permanent one-half standard deviation shocks. Figures in the boxes represent average projections for the respective variables in the baseline and scenario being presented . Ten-year historical average for the variable is also show n. For FY 2006/07, debt includes a US$350 million bond issued in March 2007 for prefinancing.
2/ Permanent 1/4 standard deviation shocks applied to real interest rate, grow th rate, and primary balance.
3/ One-time real depreciation of 30 percent and 10 percent of GDP shock to contingent liabilities occur in 2006, w ith real depreciation defined as nominal depreciation (measured by percentage fall in dollar value of local currency) minus domestic inflation (based on GDP deflator).

magnitude is unlikely to remain an isolated event without other concurrent or second-round effects placing further upward pressures on debt. In this regard, recent increased exposure of the public debt to interest rate shocks is of particular concern. Risks also stem from the financial sector, where security dealers (often part of conglomerates that include banks) remain dependent on short-term borrowed household funds.

IV. Report on Policy Discussions

16. **Against this background, the overarching theme of the discussions was the importance of reinvigorating the debt reduction strategy, while also guarding against short-run vulnerabilities**. The challenges are to: (i) seize the opportunity afforded by today's still benign external environment to build up resistance to shocks; and, (ii) increase the durability of the debt strategy by initiating deep structural reforms to strengthen public finances and foster sustained growth.

A. Fiscal Policy

17. **Discussions revolved around the FY 2006/07 outturn and on policies to strengthen the fiscal position in FY 2007/08**. The authorities expressed their own disappointment at the budgetary outturn but also emphasized the importance of keeping an appropriate perspective on the slippage and its implications for the debt dynamics. In particular, while debt-related vulnerabilities in Jamaica were real, the authorities argued that risks were exaggerated to some extent, since measured GDP was significantly underestimated. Nevertheless, looking ahead, they expressed firm commitments to reduce the deficit and bring the debt ratio down—they saw markets demanding progress in these respects.

18. **The mission advised raising the primary surplus back to at least 10 percent of GDP in FY 2007/08, from 8¾ percent currently**. The mission commended the authorities on collecting sizeable tax arrears during FY 2006/07. It noted, however, that the resulting stock reduction, together with the existence of numerous specific taxes, implied that revenues could decline by up to 1.2 percent of GDP in FY 2007/08 without additional measures. Raising the primary surplus by a further 1.2 percent of GDP would thus imply an effort equivalent to 2.4 percent of GDP. Of this amount, savings of 1.1 percentage points could accrue on account of the one-off Cricket World Cup related spending in the FY 2006/07 budget. At the same time, part of these savings (up to 0.7 percent of GDP) could be offset by the need to take into account in the FY 2007/08 budget the as-yet unreported capital spending (which the authorities are planning to do). Thus, measures amounting to just under 2 percent of GDP would likely be required.

19. **The mission suggested several options to fill the gap**. Fundamental expenditure reforms are generally more durable over the long term but realizing savings from public employment reform will take time (see paragraph 29). The mission, therefore, saw scope,

over the short-term to rely on revenue measures to: (i) reduce exempted items from the General Sales Tax; (ii) retire or substantially eliminate discretionary exemptions for imports; and (iii) raise specific taxes eroded by inflation. On expenditures, the mission recommended administrative steps to keep temporary workers and overtime in check. It also suggested that there may be some scope to roll back a larger portion of the FY 2006/07 increase in capital expenditures.

20. **The authorities explained that they would carefully review the staff's proposals**. They considered it premature to arrive at a definitive position on the FY 2007/08 deficit but were confident of an improvement over FY 2006/07. They indicated, however, that trimming capital spending would be challenging, given, in particular, the continuing need to repair infrastructure damage. As regards revenues, while agreeing to explore options, the authorities underscored the need to strike a delicate balance during an election year. However, they were pleased that recent tax administration reforms being supported by CARTAC and Fund technical assistance were bearing fruit and were confident on the potential for additional revenue gains from this source. In this regard, the mission noted the importance of carrying through the major reforms recommended by the technical assistance mission, including restructuring the organizational structure of tax administration.

21. **The mission underscored the contributions that public enterprise reform could play in reducing debt**. It noted with concern the deterioration of the financial positions of key perennial loss-makers even as the balances of some other public entities were turning out better than expected. In particular, the available data through September 2006 indicated that the combined deficits of the Jamaica Urban Transit Company (JUTC), the Sugar Company and Air Jamaica amounted to almost 1 percent of GDP more than had been expected. The mission saw scope to reduce capital spending by public entities in FY 2007/08 after the large expansion over the past year. Such consolidation would also enable more of the concessional PetroCaribe funds currently going to finance off budget entities to replace expensive central government debt.

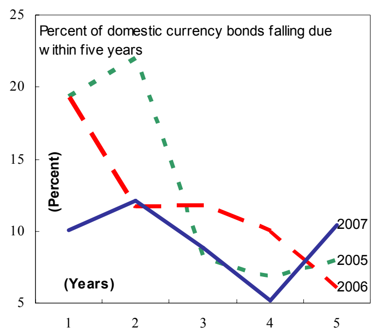
22. **The authorities explained that they were taking steps to address the problems of the large loss-makers**. There had recently been a senior management change in the JUTC and an initiative was underway to divest the Sugar Company. As regards Air Jamaica, they explained that they had recently endorsed a comprehensive restructuring plan to rehabilitate the airline over three years.

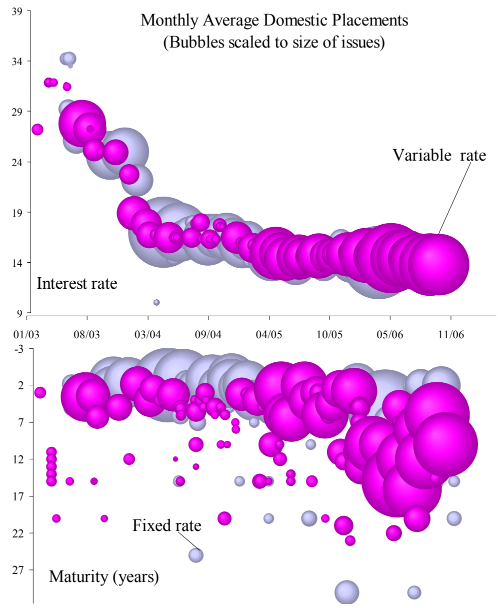
23. **Effective debt management will remain important in improving resilience to shocks**. The mission noted that a shift toward issuing variable rate instruments significantly increased the risks to the budget of interest rate shocks, especially given a prospective tightening of global liquidity. The mission suggested that interest savings from variable debt appeared modest and that it would be worth exploring again whether fixed rate debt of longer maturity could be issued at limited additional cost (Box 1).

Box 1. Jamaica: Debt Management

The optimal sovereign debt portfolio is the result of a complicated decision-making process, which no single model can capture entirely. Nevertheless, a simple partial equilibrium framework can still provide some useful insights. Using such an approach, this box examines the relative costs and benefits to the Jamaican government of issuing variable versus fixed rate domestic debt.

Background. The market premium for fixed rate debt increased in 2003 when interest rates were raised sharply to defend the currency. Thereafter, even as prices declined, the authorities have favored issuing variable rate instruments. Variable rate debt now accounts for 70 percent of total outstanding domestic currency debt (compared to 50 percent in 2005) and it amounts to about 48 percent of GDP currently (an increase of 13 percentage points of GDP since 2005).





Analysis. Increasing variable rate debt enabled the authorities to reduce roll-over risk (by extending maturities) and also lower the interest bill but at the cost of increased exposure to interest rate risk. With the narrowing of interest margins between the two types of debt and the increased maturity at which fixed rate debt can now be placed (see table below), the benefits have mostly dissipated while the costs remain large:

- Aggregate data suggests that the interest savings from currently shifting an additional 13 percent of GDP in debt from fixed to variable rate would amount to under 0.1 percent of GDP annually. Looking more closely at individual issuances that isolate differences in timing and maturity suggests that the savings could be less than half that amount.
- The risks and potential costs of an interest shock are, however, significant. The current 12-month standard deviation of 37 basis points for domestic interest rates suggests that there is approximately a one in six chance that even the meager savings could be undone entirely. If interest rates increased suddenly by 18 percentage points as they did in 2003, the costs of having shifted 13 percentage points of GDP in debt to variable rate instruments would initially amount to 2½ percent of GDP annually.
- At the same time, the costs of extending the maturity of fixed rate debt are limited. Regression estimates of the slope of the yield curve suggests that between 2005 and now, the increase in maturity of fixed rate debt by one year cost, on average, between 20 to 30 basis points.

Jamaica: Domestic Currency Bonds

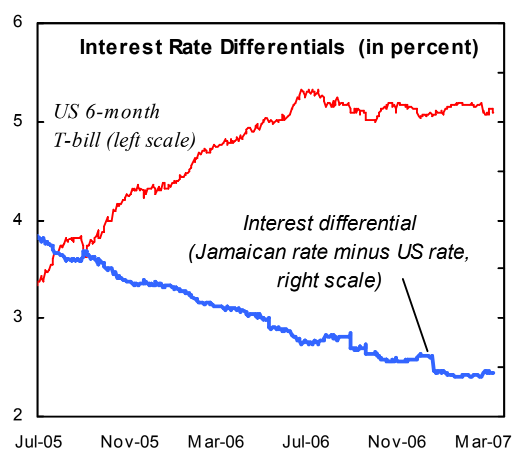
	2005	2007	Difference
Weighted interest rate (percent)			
Fixed debt	17.7	14.8	-2.9
Variable debt	16.7	14.2	-2.5
Difference	1.1	0.6	
Maturity (years)			
Fixed rate	5.0	7.7	2.8
Variable rate	10.9	10.5	-0.3
Difference	(5.9)	(2.8)	

Sources: Jamaican authorities; and Fund estimates.

B. Monetary and Exchange Rate Policy

24. **The primary aim of monetary policy remains price stability**. The authorities explained that their policy framework targeted inflation above all other objectives. At the same time, they emphasized the need to remain mindful of the fiscal costs of high interest rates and to maintain competitiveness. With inflation declining rapidly, the authorities had seized what they saw as opportunities to reduce interest rates in FY 2006/07 and accommodate a larger expansion in base money than had been envisaged. The mission agreed that inflation should remain the main objective of monetary policy. At the same time, if exchange rate movements become too predictable (thus creating incentives for the market to make one-way bets) and the interest differential vis-à-vis the U.S. dollar fell too far, there was a risk of large destabilizing portfolio shifts.

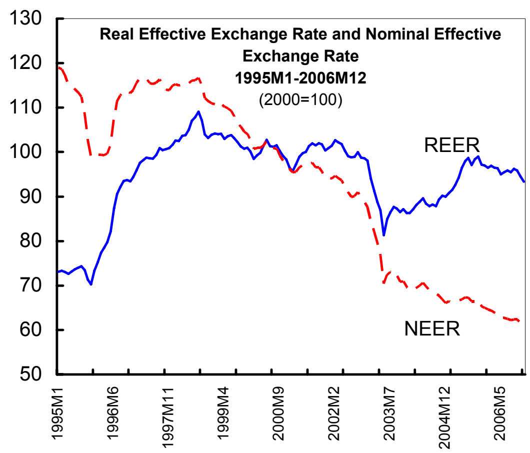
25. **The mission suggested that flexible use of all its instruments would allow the BOJ a greater degree of independence in pursuing inflation objectives**. The mission argued that in practice, this would imply accommodating pressures for the exchange rate to strengthen during periods of sustained capital inflows. This would create more room to pursue the inflation target while also limiting sterilization costs from adding to the government debt. Flexibility would also require a willingness to increase as well as decrease interest rates—indeed, given the recently unsettled financial markets, there could currently be a case for preemptively increasing rates. More generally, flexibility would avoid creating incentives for the market to make one-way bets and would build on the developing credibility of monetary policy. Greater flexibility would also allow for smaller and less wrenching adjustments over time.

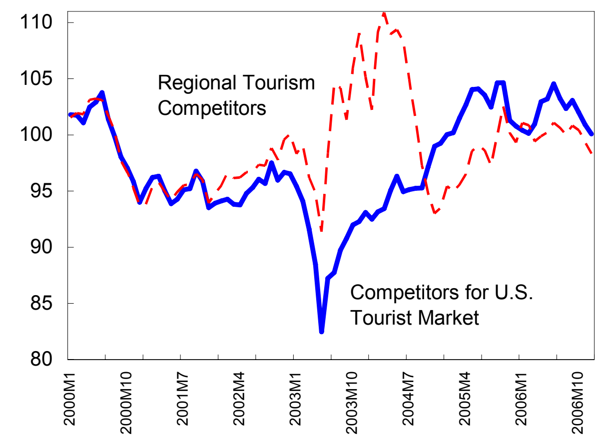


26. **While agreeing that flexibility eased the tasks of the BOJ in pursuing its objectives, the authorities also emphasized the realities on the ground**. They noted that the BOJ did not seek to target any particular exchange rate path but rather found itself in positions of having to intervene in the foreign exchange market to meet demand for domestic liquidity. Limitations in market structure and behavior after years of financial volatility often led banks to seek out the BOJ to sell foreign exchange. The authorities also noted that frequent and sharp movements in the key financial variables had significant costs to businesses and the population in a small open island economy subject to shocks.

27. **There was agreement that the current level of the exchange rate appeared broadly appropriate from competitiveness considerations**. The trade-weighted real

effective exchange rate as well as tourism-competitor based measures of the real exchange rate were in line with historical levels (recent unit labor cost data are not available). Furthermore, exports and tourism earnings were performing robustly and the current account deficit was projected to improve further over time as the large infrastructure and tourism projects underway bore fruit.





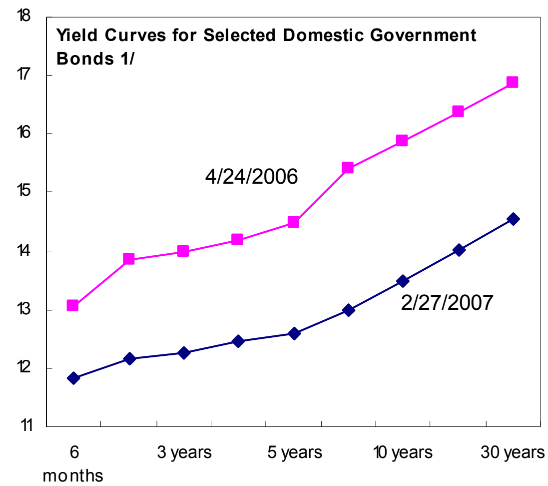
C. Financial Sector

28. **Progress being made now in strengthening the financial sector will help prepare for changed circumstances in future**. A draft Omnibus Banking Bill incorporates a number of key FSAP recommendations, and the BOJ has taken steps to prepare for the early introduction of Basel II standards while also strengthening risk monitoring capacity. Similarly, insurance supervisory capacity has been enhanced considerably by new hiring; progress is being made on the regulation of private pension schemes; and, work is underway to develop a set of coherent regulations governing collective investment schemes. Other notable achievements this past year have included parliamentary passage of the Proceeds of Crime Act, which will, inter alia, strengthen the legal regime to combat money laundering.

29. **The mission welcomed efforts to enforce regulations and encouraged continued enhanced supervision of activities vulnerable to interest rate risk**. The authorities have vigorously pursued unregulated trading schemes for breaches of the securities act. Continued vigilance against pyramid schemes and more high level warnings about the dangers of speculative investment schemes are, however, warranted and there may be need to strengthen the technical capacity to conduct forensic investigations and prosecute, if and when, evidence of fraud does emerge. The authorities are making progress on refining repo margins for security dealers and, consistent with the 2005 FSAP recommendations, the mission advised setting new requirements, on average, above current levels. Introducing more risk-sensitive capital requirements on security dealers would also enhance their resilience (Box 2).

Box 2. The Rewards and Risks of the Repo Business

The securities sector in Jamaica has had a great run, taking advantage of the high yield on government paper. Prompted by a confluence of factors, including regulatory and temporary tax advantages, the sector has grown to play a large role in the financial system, with assets amounting to half of GDP and liabilities exceeding bank deposits. The impressive growth has largely come from the repo business—short-term borrowing from households through hold-in-custody repurchase arrangements (repos) to fund investment in long-term government paper. The net interest income generated from the difference between short- and long-term interest rates has been the main source of profits.

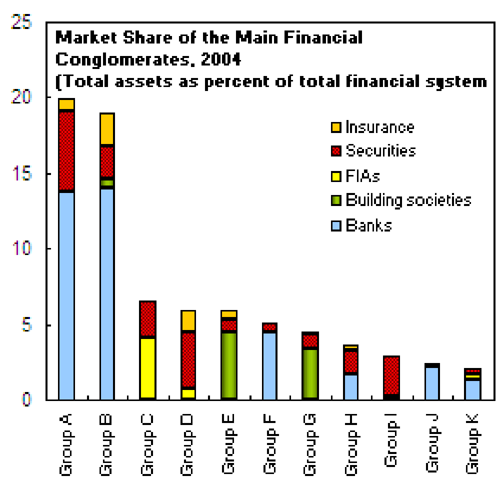


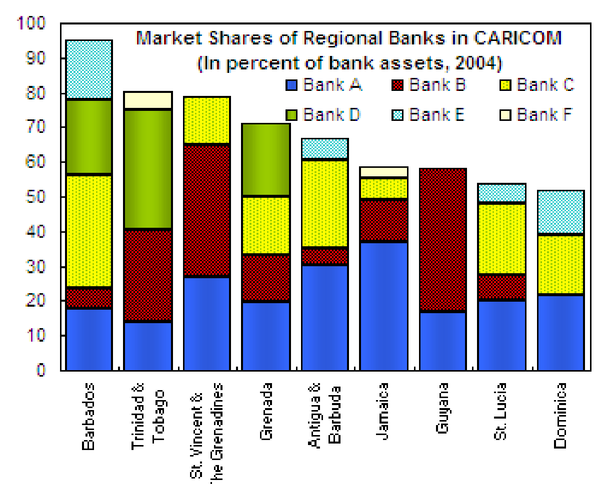
Sources: Bloomberg and Bank of Jamaica website.
1/ The yield for 6 months on 4/24/06 is proxied by 6-month TB yield issued around the same time.

The repo business has recently lost some of its luster. With the flattening and downward shift of the domestic yield curve, average annual returns on assets fell to 1.8 percent in the year to September 2006, compared to 2.4 percent the previous year.

The sector remains significantly exposed to interest rate and roll-over risk. A rise in long-term interest rates reduces the value of fixed rate assets and a sharp rise in short-term rates squeezes profitability, given the need to continuously roll over repo agreements with households. Legal ambiguities on the control rights over the underlying securities could exacerbate risks.

The potential spillovers could be important, given the extent of financial conglomeration in Jamaica and the linkages among Caribbean countries. Within Jamaica, 65 percent of the securities market is accounted for by securities firms that belong to the eleven financial conglomerates that dominate the domestic financial system. Within the conglomerates, the importance of the securities arm varies, ranging from 2 percent of the total group assets to 91 percent. Moreover, many of these conglomerates are active regionally. Broadly, while financial markets in the Caribbean remain segmented as measured by price convergence, they remain closely linked through ownership channels, with for example, the same six banks accounting for more than 50 percent of assets in nine countries.





Finally, the mission urged the authorities to prioritize developing and testing crisis management systems.

D. Structural Reforms

30. **Deep structural reforms would reinforce the debt strategy**. The mission noted that, with room for maneuver limited, a variety of circumstances had derailed the fiscal plan each year over the past few years. With debt still high, there was, however, little room for slippage, going forward. The mission indicated that this suggested the need to step back and reinvigorate the overall strategy to make it robust to the pressure points that appeared to emerge every year. Toward that end, the mission recommended beginning preparations now to implement deep reform in a number of areas (Figure 4):

- **The tax system**. There exists significant consensus in Jamaica on the need to reform and simplify the tax system by unifying rates, reducing the number of taxes and streamlining allowances and exemptions. The mission suggested that the issue of tax incentives was, in particular, critical, given their fiscal costs.

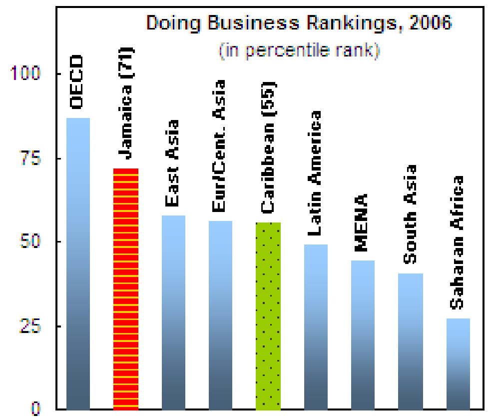
- **Public sector wage and employment policies**. During 1995–2003, the public sector headcount rose by over 40 percent. As part of the austerity program adopted in 2004, the wage bill temporarily decreased as nominal wages were frozen in agreement with unions without addressing the issue of employment. The pick-up in the wage bill again, however, suggests that this approach is not sustainable and requires a multi-year plan of fundamental reform.

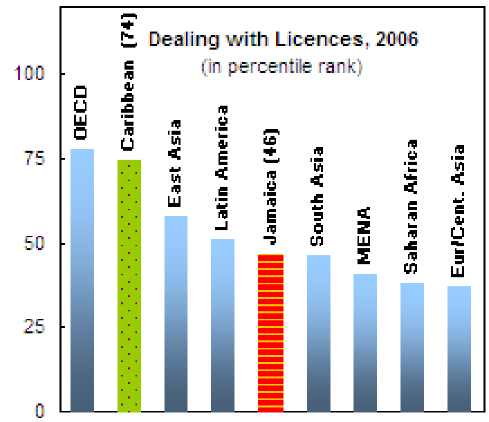
- **Public entities**. Jamaica has a multitude of off-budget public entities, some of which are vehicles for public policy while others are commercial ventures. Although the entities' expenditures are monitored, their operations, overall balances, and debt obligations are not consolidated into a unified framework amenable to formulating and assessing the overall direction of fiscal policy. As initial steps, the mission recommended preparation of a fiscal ROSC and offered Fund assistance on assessing major fiscal risks from public enterprises. It also suggested that additional Fund technical assistance could be helpful for putting in place a consolidated public sector accounting framework.

- **Financial sector**. Legislation to clarify the legal framework for repos and to empower the Financial Services Commission to obtain information for consolidated supervision and to impose penalties would be helpful. There is also scope to continue to strengthen inter-agency collaboration for supervision and regulation of conglomerates, including by developing a protocol for joint on-site inspection. The authorities are also encouraged to explore with their counterparts in other Caribbean countries the options for strengthening regional supervision.

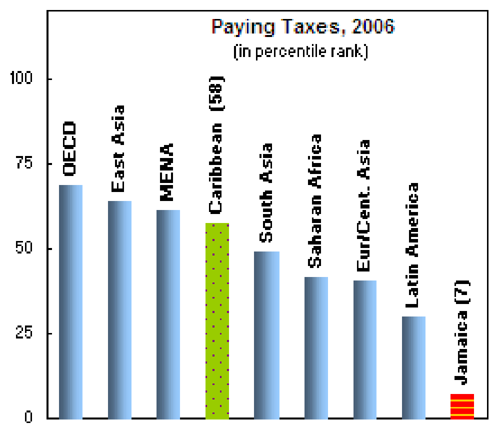
Figure 4. Jamaica: Structural Priorities 1/

Jamaica ranks well overall in creating a business environment but red tape is an issue...





...and the tax system is, in particular, inefficient and costly...



Estimated Tax Gap, 1995-2004 2/
(In percent of GDP)

	Corporate Income Taxes	Import-related Taxes	Total
Caribbean (average)	**5.6**	**5.3**	**10.8**
Dom. Republic	4.0	3.9	7.9
Trinidad & Tobago	3.3	2.4	5.7
Jamaica	6.2	3.9	10.1
ECCU	5.4	5.8	11.1
Other	6.1	5.7	11.8

...and there is significant scope to improve government effectiveness.

Governance Indicators
(Percentile ranking) 1/

	Government Effectivenss	Regulatory Quality	Rule of Law	Voice & Accountability	Political Stability
Jamaica	**51.2**	**60.4**	**37.2**	**63.3**	**34.9**
Caribbean	68.9	66.3	65.2	66.5	67.5
Bahamas, The	86.6	77.2	88.9	87.4	75.0
Barbados	85.6	77.7	88.4	86.0	88.7
Dom. Republic	41.1	45.5	33.3	51.7	47.6
Trinidad & Tobago	63.6	69.8	52.7	59.9	43.4
ECCU	74.8	75.4	71.1	75.8	81.0

Sources: World Bank Doing Business Database; World Bank Governance Database; and Fund staff estimates.

1/ Percentile rank indicates the percent of countries worldwide that rate below the selected country or regional average (calculated using simple average).

2/ Difference between what statuatory rates would imply collection to be and actual collection. Assumes corporate sector income accounts for 1/4 of GDP.

- **Business environment**. The authorities are encouraged to review the scope for reducing red tape and streamline government, including by consolidating and eliminating duplicate requirements, institutions and functions.

31. **The authorities reaffirmed their commitment to undertake structural reforms**. They explained that they were working with the Inter-American Development Bank to strengthen the business climate. They agreed that the system of tax incentives merited review and reiterated their ongoing efforts to strengthen public enterprises.

V. Staff Appraisal

32. **The Jamaican authorities have secured some notable policy successes during the past year**. Economic growth is at its best in a long time and the current account deficit is on an improving trend. The authorities have also succeeded in sharply reducing inflation and in bringing about a recovery in revenue collections after the decline recorded last year. A number of important financial sector reforms are proceeding apace.

33. **Against this background, the substantial breach of the deficit target in FY 2006/07 and resulting lack of progress at reducing debt are unfortunate**. The authorities have tended to rely on stop gap measures, such as a wage freeze, to help achieve their fiscal and debt objectives. Developments this past year have shown that policies to anchor ambitious medium-term programs should look beyond just short run exigencies to deep and long-lasting reforms.

34. **The authorities are, therefore, advised to initiate, while conditions still remain benign, deep reforms that can deliver sustained and durable debt reduction**. The medium-term program adopted in 2004 is now in need of a fundamental reinvigoration. Toward that end, the upcoming elections provide an opportunity to create the broad political consensus necessary to carry through with long standing reforms. The authorities are encouraged to set in place a renewed strategy to reform the tax system; address public employment; and, undertake a comprehensive reassessment of the size and appropriate role in the economy of the public sector. The latter, in conjunction with other steps to improve the business environment, will foster private sector led growth, which remains indispensable for bringing down the burden of indebtedness.

35. **The authorities will also need to remain vigilant against vicissitudes in market conditions and sentiments, and in this regard, their commitment to reduce the deficit in FY 2007/08 is welcome**. The authorities are urged to aim for a primary surplus of at least 10 percent of GDP and take the measures necessary to credibly deliver on such a target. They will also need to continue to pursue public enterprise reform. They could consider Fund technical assistance in creating a framework to identify risk from off-budget entities,

preparing a Fiscal ROSC, and putting in place a consolidated public sector accounting framework.

36. T**he limited room for fiscal policy maneuverability in Jamaica reinforces the need for flexible monetary and exchange rate policies and for further strengthening the financial sector**. The authorities' readiness to increase interest rates, if and when necessary, is important in this respect. This, in turn, underscores the benefits of improving the resiliency of the debt profile and the financial sector to interest rate shocks. At the same time, vigilance against the dangers of unregulated speculative investment schemes, strengthening consolidated supervision, and prioritizing the development and testing of crisis management systems remain critical.

37. **It is recommended that the next Article IV consultation take place within the standard 12-month cycle**.

Table 1. Jamaica: Selected Economic Indicators 1/

	2004/05	Prel. 2005/06	Staff Projections 2006/07	2007/08	2008/09	2009/10	2010/11	2011/12
			(Annual percentage changes)					
GDP, prices, and employment								
Real GDP	0.4	2.0	2.9	3.0	3.1	3.2	3.2	3.2
Nominal GDP	11.0	17.0	10.3	9.4	9.3	8.7	8.5	8.5
Consumer price index (end of period)	13.2	11.4	6.6	6.0	5.5	5.2	5.2	5.2
Consumer price index (average)	12.7	15.1	7.1	6.3	6.0	5.3	5.2	5.2
Exchange rate (end of period, in J$/US$)	0.9	6.2	…	…	…	…	…	…
End-of-period REER (percent change, appreciation +)	5.2	4.1	…	…	…	…	…	…
Unemployment rate (in percent)	12.2	11.3	…	…	…	…	…	…
			(In percent of GDP)					
Government operations 1/								
Budgetary revenue	31.2	29.0	30.1	28.9	28.8	28.5	28.5	28.5
Budgetary expenditure	36.7	32.7	34.8	33.8	33.2	31.5	30.6	29.6
Primary expenditure	19.4	18.0	21.2	20.7	20.4	20.0	19.6	19.4
Interest payments 2/	17.4	14.7	13.5	13.1	12.8	11.5	10.9	10.1
Gap	0.0	0.0	0.0	1.8	1.8	1.8	1.8	1.8
Budget balance	-5.5	-3.6	-4.7	-3.1	-2.6	-1.2	-0.3	0.7
Of which: primary fiscal balance	11.9	11.1	8.8	10.0	10.2	10.3	10.7	10.9
Off-budget expenditure 3/	3.1	1.2	1.4	1.2	0.0	0.6	0.5	0.5
Overall fiscal balance	-8.6	-4.8	-6.1	-4.3	-2.6	-1.9	-0.8	0.2
Public debt	139.6	133.0	134.9	131.0	128.0	124.4	119.2	113.2
External sector								
Current account balance	-7.2	-11.4	-10.5	-9.4	-9.3	-7.1	-5.6	-5.2
Of which: exports of goods, f.o.b.	17.5	17.8	19.5	19.1	17.8	17.1	16.7	16.1
Of which: imports of goods, f.o.b.	41.2	44.4	46.2	44.6	44.3	42.3	41.0	40.6
Net international reserves (in millions of US$)	1,902	2,078	2,220	2,300	2,350	2,400	2,450	2,500
		(Changes in percent of beginning of period broad money) 4/						
Money and credit								
Net foreign assets	7.5	1.8	3.3	4.8	...	...	...	...
Net domestic assets	2.7	6.8	9.5	4.6	...	...	...	...
Of which: credit to the central government	0.5	-8.5	1.8	15.0	...	...	...	...
Broad money	10.3	8.6	12.9	9.4	...	...	...	...
Velocity (ratio of GDP to broad money)	2.6	2.8	2.7	2.7	...	...	...	...
Memorandum items:								
Nominal GDP (in billions of Jamaican dollars)	550	643	709	776	848	922	1,001	1,086
Exchange rate (end of period, J$/US$)	61.5	65.3	…	…	…	…	…	…

Sources: Jamaican authorities; and Fund staff estimates and projections.

1/ Based partly on assumptions provided by the authorities. Fiscal years run from April 1 to March 31. Public debt is central government debt including debt assumed from public entities, plus guaranteed public entity debt, plus PetroCaribe debt. For FY 2006/07, the debt includes US$350 million bond issued for prefinancing. Cash-flow savings from the PetroCaribe agreement with Venezuela are managed by an extrabudgetary Fund that lends to both budgetary and off-budget entities.

2/ Includes capitalized interest payments on previous year's BoJ Special Issue bonds.

3/ Includes debt issued to BOJ to cover its cash losses, and debt related to off-budget projects financed initially by the private sector.

4/ Including valuation adjustments.

Table 2. Jamaica: Summary of Central Government Operations
(In billions of Jamaican dollars)

		Prel.	Budget	Revised	Staff Projections 1/				
	2004/05	2005/06	2006/07	2006/07	2007/08	2008/09	2009/10	2010/11	2011/12
Budgetary revenue and grants	171.5	186.7	219.2	213.3	224.1	244.3	263.2	285.6	309.9
Tax	153.0	165.7	198.9	193.3	204.2	223.0	240.1	260.5	282.7
Nontax	14.4	20.3	16.6	16.7	17.4	18.5	20.1	21.9	23.7
Grants	4.2	0.7	3.7	3.2	2.5	2.7	2.9	3.2	3.5
Budgetary expenditure	201.8	210.0	238.7	246.7	262.4	281.6	290.8	306.0	321.3
Primary expenditure	106.4	115.6	146.3	150.6	160.4	172.7	184.5	196.6	211.2
Wage and salaries	63.5	63.1	72.8	78.2	86.7	93.3	97.7	102.1	108.6
Other expenditure	32.1	40.8	46.5	49.3	52.7	55.6	60.4	65.5	71.1
Capital expenditure	10.8	11.7	27.0	23.2	21.0	23.8	26.3	29.0	31.5
Interest	95.4	94.4	92.4	96.0	102.0	108.9	106.4	109.4	110.1
Domestic	75.3	71.5	66.3	69.2	71.1	79.1	75.0	76.5	75.7
Current	72.6	65.4	61.5	64.4	65.3	72.9	75.0	76.5	75.7
BoJ special issue bonds 2/	2.6	6.1	4.8	4.8	5.8	6.2	0.0	0.0	0.0
External	20.1	22.9	26.1	26.8	30.9	29.8	31.3	32.8	34.4
Gap /3	0.0	0.0	0.0	0.0	14.3	14.9	16.2	17.6	19.1
Budget balance	**-30.2**	**-23.3**	**-19.4**	**-33.4**	**-24.0**	**-22.4**	**-11.4**	**-2.8**	**7.7**
***Of which:* primary balance**	**65.2**	**71.1**	**73.0**	**62.6**	**78.0**	**86.5**	**94.9**	**106.6**	**117.8**
Off-budget expenditure	17.3	7.4	10.1	10.1	9.0	0.0	5.7	5.1	5.1
BoJ cash losses 4/	13.4	7.4	10.1	10.1	7.4	0.0	5.7	5.1	5.1
Deferred financing 5/	3.9	0.0	0.0	0.0	1.6	0.0	0.0	0.0	0.0
Overall balance	-47.5	-30.8	-29.6	-43.5	-33.1	-22.4	-17.1	-7.9	2.6
Financing /6	47.5	30.8	29.6	43.5	33.1	22.4	17.1	7.9	-2.6
External financing	7.8	20.7	-8.8	13.3	-21.0	3.2	3.3	3.4	3.5
Domestic financing	38.5	10.1	35.4	30.3	54.1	19.2	13.9	4.5	-6.0
Banking system	1.0	-11.9	43.3	4.0	38.7	13.2	6.1	5.7	5.7
Others	37.5	22.0	-7.9	26.2	15.4	6.0	7.8	-1.2	-11.8
Divestment	1.3	0.0	3.0	0.0	0.0	0.0	0.0	0.0	0.0

Sources: Jamaican authorities; Fund staff estimates and projections.

1/ The starting point for the projections is FY 2006/07. The projections assume approximately 0.7 percent of GDP in capital expenditure in FY 2006/07 are carried over to FY 2007/08.

2/ Accrued interest on previous year's BoJ Special Issue bonds is contractually paid to the BoJ through debt issuance the following year. Beginning in 2008/09 the central government pays this interest concurrently, which results in two payments in FY 2008/09.

3/ To be filled with measures.

4/ Refers to operating losses of the Bank of Jamaica, not covered by the BOJ Special Issue Bonds.

5/ Debt issued upon assuming public investment projects carried out by the private sector.

6/ For FY 2006/07 and FY 2007/08, composition reflects the impact of external borrowing for pre-financing.

Table 3. Jamaica: Summary of Central Government Operations
(In percent of GDP)

		Prel.	Budget	Revised	Staff Projections 1/				
	2004/05	2005/06	2006/07	2006/07	2007/08	2008/09	2009/10	2010/11	2011/12
Budgetary revenue and grants	31.2	29.0	30.3	30.1	28.9	28.8	28.5	28.5	28.5
Tax	27.8	25.8	27.5	27.3	26.3	26.3	26.0	26.0	26.0
Nontax	2.6	3.2	2.3	2.4	2.2	2.2	2.2	2.2	2.2
Grants	0.8	0.1	0.5	0.5	0.3	0.3	0.3	0.3	0.3
Budgetary expenditure	36.7	32.7	33.0	34.8	33.8	33.2	31.5	30.6	29.6
Primary expenditure	19.4	18.0	20.2	21.2	20.7	20.4	20.0	19.6	19.4
Wage and salaries	11.6	9.8	10.1	11.0	11.2	11.0	10.6	10.2	10.0
Other expenditure	5.8	6.4	6.4	7.0	6.8	6.5	6.5	6.5	6.5
Capital expenditure	2.0	1.8	3.7	3.3	2.7	2.8	2.9	2.9	2.9
Interest	17.4	14.7	12.8	13.5	13.1	12.8	11.5	10.9	10.1
Domestic	13.7	11.1	9.2	9.8	9.2	9.3	8.1	7.6	7.0
Current	13.2	10.2	8.5	9.1	8.4	8.6	8.1	7.6	7.0
BoJ special issue bonds 2/	0.5	0.9	0.7	0.7	0.7	0.7	0.0	0.0	0.0
External	3.7	3.6	3.6	3.8	4.0	3.5	3.4	3.3	3.2
Gap 3/	0.0	0.0	0.0	0.0	1.8	1.8	1.8	1.8	1.8
Budget balance	**-5.5**	**-3.6**	**-2.7**	**-4.7**	**-3.1**	**-2.6**	**-1.2**	**-0.3**	**0.7**
***Of which:* primary balance**	**11.9**	**11.1**	**10.1**	**8.8**	**10.0**	**10.2**	**10.3**	**10.7**	**10.9**
Off-budget expenditure	3.1	1.2	1.4	1.4	1.2	0.0	0.6	0.5	0.5
BoJ cash losses 4/	2.4	1.2	1.4	1.4	1.0	0.0	0.6	0.5	0.5
Deferred financing 5/	0.7	0.0	0.0	0.0	0.2	0.0	0.0	0.0	0.0
Overall balance	-8.6	-4.8	-4.1	-6.1	-4.3	-2.6	-1.9	-0.8	0.2
Budgetary principal payment	24.3	21.8	17.4	17.4	13.1	16.9	15.5	17.6	20.4
Domestic	18.9	16.6	15.1	14.7	8.8	11.8	13.8	16.1	16.3
External	5.4	5.1	2.3	2.7	4.3	5.1	1.7	1.5	4.1
Memorandum items:									
Deposit draw-down (in percent of GDP)	0.0	0.0	0.0	2.3	3.1	0.0	0.0	0.0	0.0
Public debt 6/	139.6	133.0	126.1	134.9	131.0	128.0	124.4	119.2	113.2
Of which: cumulative PetroCaribe debt	...	0.1	2.1	2.1	4.1	5.8	7.3	8.7	9.8
Gross financing (in percent of GDP)	32.9	26.5	21.5	23.5	17.3	19.5	17.4	18.4	20.2
GDP (in billions of J$)	550	643	722	709	776	848	922	1,001	1,086

Sources: Jamaican authorities; Fund staff estimates and projections.

1/ The starting point for the projections is FY 2006/07. The projections assume approximately 0.7 percent of GDP in capital expenditure in FY 2006/07 are carried over to FY 2007/08.

2/ Accrued interest on previous year's BoJ Special Issue bonds is contractually paid to the BoJ through debt issuance the following year. Beginning in 2008/09 the central government pays this interest concurrently, which results in two payments in FY 2008/09.

3/ To be filled with measures.

4/ Refers to operating losses of the Bank of Jamaica, not covered by the BOJ Special Issue Bonds.

5/ Debt issued upon assuming public investment projects carried out by the private sector.

6/ Central Government debt including debt assumed from public entities, plus guaranteed public entity debt, plus PetroCaribe debt. Includes US$350 million bond issued in March 2007 for prefinancing. Cash-flow savings from the PetroCaribe agreement with Venezuela are managed by an extrabudgetary Fund that lends to both budgetary and off-budget entities.

Table 4. Jamaica: Summary of the Public Debt 1/

		Prel.	Staff Projections					
	2004/05	2005/06	2006/07	2007/08	2008/09	2009/10	2010/11	2011/12
	(In billions of Jamaican dollars)							
Debt stock								
Public debt	767	855	957	1,016	1,086	1,147	1,192	1,229
Government debt	727	798	868	893	931	962	985	998
Domestic 2/	449	483	514	548	573	591	601	600
Of which : US$ linked	85	77	74	77	79	81	83	86
External 3/	278	315	354	345	358	371	384	398
Official	103	121	121	113	104	95	88	81
Commercial	174	194	233	232	255	276	296	317
PetroCaribe external debt	...	1	15	32	50	68	87	107
Government guaranteed debt	41	57	74	91	106	117	121	124
External	32	48	62	78	93	103	106	109
Domestic	8	9	12	12	13	14	14	15
Domestic currency debt	373	415	451	484	506	524	532	530
Foreign currency debt	310	364	432	455	500	542	577	613
US$ linked debt	85	77	74	77	79	81	83	86
	(In percent of GDP)							
Debt stock								
Public debt	139.6	133.0	134.9	131.0	128.0	124.4	119.2	113.2
Government debt	132.2	124.0	122.4	115.1	109.7	104.4	98.4	91.9
Domestic 2/	81.7	75.1	72.4	70.7	67.5	64.1	60.1	55.3
Of which : US$ linked	15.4	12.0	10.5	9.9	9.3	8.8	8.3	7.9
External 3/	50.5	49.0	50.0	44.5	42.2	40.2	38.4	36.6
Official	18.8	18.8	17.1	14.5	12.2	10.3	8.8	7.5
Commercial	31.7	30.1	32.9	29.9	30.0	29.9	29.6	29.2
PetroCaribe external debt	...	0.1	2.1	4.1	5.8	7.3	8.7	9.8
Government guaranteed debt	7.4	8.9	10.4	11.7	12.4	12.7	12.1	11.4
Domestic currency debt	67.8	64.5	63.6	62.4	59.7	56.8	53.2	48.8
Foreign currency debt	56.3	56.6	60.9	58.7	59.0	58.8	57.7	56.5
US$ linked debt	15.4	12.0	10.5	9.9	9.3	8.8	8.3	7.9
Change in the debt/GDP ratio	-4.2	-6.5	1.9	-4.0	-3.0	-3.6	-5.2	-6.0
Memorandum items:								
Total debt (in billions of US$)	12.5	13.1	14.1	14.5	15.1	15.5	15.7	15.8
Of which: foreign currency debt	5.0	5.6	6.4	6.5	6.9	7.3	7.6	7.9
Government guaranteed debt issues (U.S. dollar millions):		280	315	204	164	115	90	70
(in Jamaican dollar billions)		18	21	14	12	9	7	5
Of which								
Air Jamaica		280	70	70	70	70	70	70
Petrojam/PCJ		0	0	80	80	45	20	0
Ports authority		0	45	50	10	0	0	0
GDP (in billions of J$)	550	643	709	776	848	922	1,001	1,086

Sources: Jamaican authorities; Fund staff estimates and projections.

1/ Central Government debt including debt assumed from public entities, plus guaranteed public entity debt, plus PetroCaribe debt. Includes US$350 million bond issued in March 2007 for prefinancing. Cash-flow savings from the PetroCaribe agreement with Venezuela are managed by an extrabudgetary Fund that lends to both budgetary and off-budget entities.

2/ Includes annually 0.3 percent of GDP for contingencies and assumed domestic debts.

3/ Includes US$350 million bond issued in March 2007 for prefinancing.

Table 5. Summary Accounts of the Bank of Jamaica 1/

	2003/04	2004/05	2005/06	Staff Proj. 2006/07	Staff Proj. 2007/08
	(In billions of Jamaican dollars)				
End-of-period stocks 1/					
Net international reserves	**96**	**118**	**136**	**150**	**161**
Net domestic assets	**-59**	**-76**	**-92**	**-100**	**-106**
Net claims on public sector	76	95	97	109	122
Net claims on central government 2/	68	78	55	56	95
Net credit to commercial banks	-14	-13	-11	-9	-10
Net credit to other financial institutions	-1	-1	-1	-1	-1
Open market operations	-108	-144	-157	-174	-188
Other item net (incl. valuation adj.)	-12	-14	-20	-25	-30
Base money	**36**	**42**	**44**	**50**	**55**
Currency in circulation	21	24	26	31	34
Liabilities to commercial banks	16	18	17	19	21
Fiscal year flows 1/					
Net international reserves	**20.5**	**22.1**	**18.0**	**14.8**	**10.7**
Net domestic assets	**-16.8**	**-16.7**	**-16.0**	**-8.3**	**-5.7**
Net claims on public sector	11.9	19.3	1.6	12.5	13.2
Net claims on central government 2/	11.5	9.3	-22.7	1.2	38.7
Net credit to commercial banks	-1.2	1.1	1.7	1.5	-0.5
Net credit to other financial institutions	0.1	-0.1	0.0	-0.1	-0.1
Open market operations	-22.1	-35.6	-13.5	-17.0	-13.3
Other items net	-5.5	-1.4	-5.9	-5.2	-5.0
Base money	**3.7**	**5.5**	**2.0**	**6.5**	**5.0**
Currency in circulation	3.3	2.9	2.7	5.1	3.0
Liabilities to commercial banks	0.4	2.5	-0.7	1.4	2.1
	(Change in percent of beginning-of-period base money)				
Net international reserves	**63.1**	**61.1**	**43.2**	**33.9**	**21.3**
Net domestic assets	**-51.8**	**-46.0**	**-38.5**	**-18.9**	**-11.3**
Net claims on public sector	36.7	53.4	3.8	28.7	26.4
Net credit to commercial banks	-3.7	3.0	4.1	3.5	-1.1
Net credit to other financial institutions	0.2	-0.3	0.0	-0.2	-0.1
Open market operations	-67.9	-98.3	-32.4	-39.0	-26.5
Other items net	-17.0	-3.8	-14.1	-11.9	-9.9
Base money	**11.3**	**15.1**	**4.7**	**15.0**	**10.0**
Currency in circulation	10.2	8.1	6.4	11.7	5.9
Liabilities to commercial banks	1.2	7.0	-1.7	3.3	4.1
Memorandum item:					
Net international reserves (in millions of US$)	1,569	1,915	2,078	2,220	2,300

Sources: Bank of Jamaica; and Fund staff estimates.

1/ Fiscal year runs from April 1 to March 31.
2/ Includes net unclassified and BoJ operating loss from the previous fiscal year.

Table 6. Jamaica: Summary Monetary Survey 1/

	2003/04	2004/05	2005/06	Staff Proj. 2006/07	Staff Proj. 2007/08
	(In billions of Jamaican dollars)				
End-of-period stocks 1/					
Net foreign assets	102	116	120	128	140
Net domestic assets	89	94	108	130	142
Net claims on public sector	165	179	191	203	216
Of which: central government	147	148	136	140	179
Open market operations	-83	-110	-116	-116	-125
Credit to private sector	80	93	106	133	155
Other 3/	-73	-68	-73	-91	-104
Liabilities to private sector (M3)	191	210	229	258	282
Money supply (M2)	125	139	154	173	193
Foreign currency deposits	66	71	75	84	89
Fiscal year flows 1/					
Net foreign assets	14.2	14.4	3.8	7.6	12.3
Net domestic assets	17.9	5.2	14.4	21.8	12.0
Net claims on public sector 2/	13.8	13.8	12.3	12.0	13.2
Of which: central government	15.4	1.0	-11.9	4.0	38.7
Open market operations	-13.7	-26.9	-5.7	-0.1	-9.5
Credit to private sector	25.2	13.0	13.1	27.5	22.0
Other 3/	-7.3	5.3	-5.4	-17.6	-13.7
Liabilities to private sector (M3)	32.1	19.6	18.2	29.4	24.3
	(Change in percent of beginning-of-period M3)				
Net foreign assets	9.0	7.5	1.8	3.3	4.8
Net domestic assets	11.3	2.7	6.8	9.5	4.6
Net claims on public sector 2/	8.7	7.2	5.9	5.3	5.1
Of which: central government	9.7	0.5	-8.5	1.8	15.0
Open market operations	-8.6	-14.1	-2.7	-0.1	-3.7
Credit to private sector	15.9	6.8	6.2	12.0	8.5
Other 3/	-4.6	2.8	-2.6	-7.7	-5.3
Liabilities to private sector (M3)	20.2	10.3	8.6	12.9	9.4
Memorandum items:					
Monetary base (millions of Jamaica dollars)	36.2	41.6	43.6	50.1	55.2
M3/monetary base	5.3	5.1	5.2	5.1	5.1
Net foreign assets (in millions of US$)	1676	1895	1843	1887	2001
M3 velocity	2.6	2.6	2.8	2.7	2.7

Sources: Bank of Jamaica; and Fund staff estimates and projections.

1/ Fiscal year runs from April 1 to March 31.
2/ Includes Bank of Jamaica operating balance.
3/ Includes net credit to nonbank financial institutions, capital accounts, valuation, adjustment, securities sold under repurchase agreements, and net unclassified assets.

Table 7. Jamaica: Summary Balance of Payments
(In millions of U.S. dollars)

			Staff Projections					
	2004/05	2005/06	2006/07	2007/08	2008/09	2009/10	2010/11	2011/12
Current account	-644	-1,166	-1,127	-1,058	-1,109	-895	-753	-736
Trade balance	-2,124	-2,716	-2,858	-2,872	-3,160	-3,180	-3,248	-3,458
Exports (f.o.b.)	1,567	1,809	2,085	2,149	2,124	2,155	2,226	2,271
Imports (f.o.b.)	3,691	4,524	4,943	5,022	5,284	5,336	5,474	5,729
Fuel (c.i.f.)	987	1,558	1,535	1,574	1,661	1,707	1,768	1,818
Exceptional imports (incl. FDI-related)	316	273	661	521	549	391	304	354
Other	2,388	2,694	2,747	2,927	3,073	3,237	3,401	3,557
Services (net)	570	643	742	845	955	1,110	1,246	1,372
Transportation	-182	-290	-322	-311	-323	-302	-296	-312
Travel	1,178	1,372	1,529	1,649	1,793	1,949	2,102	2,266
Of which: tourism receipts	1,457	1,619	1,799	1,930	2,088	2,258	2,426	2,606
Other services	-426	-439	-466	-493	-515	-538	-559	-582
Income (net)	-599	-682	-776	-861	-815	-831	-857	-857
Current transfers (net)	1,508	1,589	1,766	1,830	1,911	2,007	2,107	2,208
Government (net)	175	130	105	86	80	84	88	88
Private (net)	1,333	1,459	1,661	1,744	1,831	1,923	2,019	2,120
Capital and financial account	977	1,342	1,269	1,138	1,159	945	803	786
Capital account (net)	2	-3	1	1	1	1	1	1
Financial account (net)	975	1,346	1,268	1,137	1,158	944	802	785
Direct investment (net)	538	608	750	622	662	534	450	449
Central government (net)	235	367	199	-306	44	45	45	45
Other official (net) 1/ 2/	…	12	204	733	379	343	247	250
Of which: PetroCaribe	…	12	214	233	229	228	227	225
Private (net)	202	359	114	88	73	22	61	41
Of which: unidentified flows	-136	395	0	0	0	0	0	0
Overall balance/change in NFA	333	177	142	80	50	50	50	50
Memorandum items:								
Net international reserves	1,902	2,078	2,220	2,300	2,350	2,400	2,450	2,500
(in weeks of imports of GNFS)	18	17	17	17	17	17	17	16
Current account (in percent of GDP)	-7.2	-11.4	-10.5	-9.4	-9.3	-7.1	-5.6	-5.2
Exports of goods (in percent change)	6.8	15.4	15.3	3.1	-1.2	1.5	3.3	2.0
Imports of goods (in percent change)	11.9	22.6	9.2	1.6	5.2	1.0	2.6	4.7
Tourism receipts (in percent change)	4.0	11.1	11.1	7.3	8.2	8.2	7.4	7.4
GDP (in millions of U.S. dollars)	8,949	10,183	10,698	11,261	11,937	12,622	13,346	14,112

Sources: Jamaican authorities; and Fund staff estimates.

1/ In 06/07 and beyond, consists of borrowing by public entities for infrastructure projects, Air Jamaica, and bauxite expansion.

2/ Includes counterpart to the inflow for the government's pre-financing in March 2007 and in 2005/06.

Table 8. Jamaica: Selected Vulnerability Indicators

	2003/04	2004/05	Prel. 2005/06 1/	Proj. 2006/07
Key economic and market indicators				
Real GDP growth (in percent)	1.9	0.4	2.0	2.9
CPI inflation (period average, in percent)	12.9	12.7	15.1	7.1
Short-term (ST) interest rate (in percent)	16.0	13.5	13.0	12.8
EMBI secondary market spread (bps, end of period)	551	405	301	...
Exchange rate NC/US$ (end of period)	60.8	61.5	65.3	...
External sector				
Exchange rate regime	Managed float			
Current account balance (percent of GDP)	-6.8	-7.2	-11.4	-10.5
Net FDI inflows (percent of GDP)	7.1	6.0	6.0	7.0
Exports (percentage change of US$ value, GNFS)	11.0	5.1	9.5	12.4
Real effective exchange rate (1995/96=100; end of period)	115.3	121.3	126.3	…
Gross international reserves (GIR) in US$billion	1.6	1.9	2.4	2.5
GIR in percent of ST debt at remaining maturity (RM)	327.7	352.6	679.6	435.8
GIR in percent of ST debt at RM and banks' FX deposits.	97.2	113.6	148.7	135.8
Net international reserves (NIR) in US$billion	1.6	1.9	2.1	2.2
Total gross external debt (ED) in percent of GDP	54.5	56.4	54.7	59.6
Of which : ST external debt (original maturity, in percent of total ED)	0.0	0.0	0.0	0.0
ED of domestic private sector (in percent of total ED)	...	...	...	...
ED to foreign official sector (in percent of total ED)	47.1	43.7	36.0	27.8
Total gross external debt in percent of exports of GNFS	123.4	130.7	131.8	134.3
Gross external financing requirement (in US$billion) 2/	0.8	1.1	1.7	1.4
Public sector (PS) 3/				
Overall balance (percent of GDP)	-9.9	-8.6	-4.8	-6.1
Primary balance (percent of GDP)	11.0	11.9	11.1	8.8
Debt-stabilizing primary balance (percent of GDP) 4/	10.0	9.0	5.0	3.6
Gross PS financing requirement (in percent of GDP) 5/	29	33	27	24
Public sector gross debt (PSGD, in percent of GDP) 5/	144	140	133	135
Of which : Exposed to rollover risk (in percent of total PSGD) 6/	17	17	12	...
Exposed to exchange rate risk (in percent of total PSGD) 7/	54	51	52	...
Exposed to interest rate risk (in percent of total PSGD) 8/	42	43	40	...
Public sector net debt (in percent of GDP)	126	121	118	...
Financial sector (FS) 9/				
Capital adequacy ratio (in percent)	14.0	17.7	17.9	16.1
NPLs in percent of total loans	3.1	2.7	2.3	2.2
Provisions in percent of NPLs	125.0	135.7	131.8	125.8
Return on average assets (in percent)	4.3	3.0	3.7	3.5
Return on equity (in percent)	39.0	26.9	30.8	29.7
FX deposits held by residents (in percent of total deposits)	38.1	38.8	39.5	37.8
FX loans to residents (in percent of total loans, net of provisions)	39.0	41.3	42.7	40.8
Net open forex position (in percent of capital) 10/	25.7	30.8	13.1	21.6
Public sector debt held by FS (percent of total FS assets)	32.7	25.0	24.2	20.0
Credit to private sector (percent change)	40.0	20.0	20.0	30.0
Memorandum item:				
Nominal GDP in billions of U.S. dollars	8.3	8.9	10.2	10.8

Sources: Bank of Jamaica, Ministry of Finance, STATIN; and Fund staff estimates and projections.

1/ Staff estimates, projections, or latest available observations.
2/ Current account deficit plus amortization of external debt.
3/ Public sector covers central government only.
4/ Based on averages for the last five years for the relevant variables (i.e., growth, interest rates).
5/ FY 2006/07 debt reflects a US$350 million bond issued in March 2007 for pre-financing for FY 2007/08.
6/ ST debt and maturing medium- and long-term debt, domestic and external, excluding external debt to official creditors.
7/ Debt in foreign currency or linked to the exchange rate, domestic and external, excluding external debt on concessional terms.
8/ ST debt and maturing medium-and long-term debt at variable interest rates, domestic and external.
9/ Financial sector includes commercial banks only. Data in calendar year.
10/ Sum of on-and off-balance sheet exposure.

Table 9. Jamaica: Public Sector Debt Sustainability Framework, 2001/02-2011/12
(In percent of GDP, unless otherwise indicated)

		Actual					Projections						Debt-stabilizing primary balance 9/
		2001/02	2002/03	2003/04	2004/05	2005/06	2006/07	2007/08	2008/09	2009/10	2010/11	2011/12	
1	**Baseline: Public sector debt 1/**	**133.3**	**146.3**	**143.7**	**139.6**	**132.9**	**134.9**	**131.0**	**128.0**	**124.4**	**119.2**	**113.2**	
	Of which : foreign-currency denominated	69.9	69.1	71.8	65.9	61.1	62.6	58.5	57.4	56.4	55.4	54.3	
	Government guaranteed debt 1/	4.0	7.0	7.2	7.4	8.9	12.5	15.8	18.3	20.0	20.7	21.2	
	Central government debt 1/	**129.2**	**139.3**	**136.6**	**132.2**	**124.0**	**122.4**	**115.1**	**109.7**	**104.4**	**98.4**	**91.9**	**4.4**
2	Change in Central Government debt	1.7	10.0	-2.7	-4.4	-8.1	-1.6	-7.3	-5.4	-5.3	-5.9	-6.5	
3	Identified debt-creating flows (4+7+12)	-4.2	9.2	-4.2	-3.8	-9.8	-5.4	-6.3	-7.2	-6.9	-7.4	-8.0	
4	Primary deficit	-7.4	-5.2	-9.3	-8.7	-9.9	-7.4	-8.9	-10.2	-9.7	-10.1	-10.4	
5	Revenue and grants	27.0	28.1	29.4	31.2	29.0	30.1	28.9	28.8	28.5	28.5	28.5	
6	Primary (noninterest) expenditure	19.6	22.9	20.1	22.5	19.1	22.7	20.0	18.6	18.9	18.4	18.2	
7	Automatic debt dynamics 2/	3.2	14.4	5.0	4.9	0.1	2.0	2.6	3.0	2.8	2.7	2.4	
8	Contribution from interest rate/growth differential 3/	1.2	3.2	-3.6	4.1	-4.8	2.0	2.6	3.0	2.8	2.7	2.4	
9	Of which contribution from real interest rate	2.3	5.9	-1.2	4.6	-2.4	5.3	5.9	6.3	6.0	5.8	5.3	
10	Of which contribution from real GDP growth	-1.0	-2.6	-2.3	-0.5	-2.4	-3.3	-3.3	-3.3	-3.2	-3.0	-2.9	
11	Contribution from exchange rate depreciation 4/	2.0	11.2	8.6	0.8	4.9	...	...	...	...	...	...	
12	Other identified debt-creating flows	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	
13	Privatization receipts (negative)	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	
14	Recognition of implicit or contingent liabilities	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	
15	Other (specify, e.g. bank recapitalization)	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	
16	Residual, including asset changes (2-3) 5/	5.8	0.8	1.5	-0.6	1.6	3.8	-1.0	1.8	1.6	1.5	1.4	
	Public sector debt-to-revenue ratio 1/	493.4	521.3	489.4	447.2	457.9	448.6	453.5	444.6	435.9	417.5	396.5	
	Gross financing need 6/	30.1	31.2	28.9	32.9	26.5	23.5	17.3	19.5	17.4	18.4	20.2	
	in billions of U.S. dollars	2.4	2.6	2.4	2.9	2.7	2.5	2.0	2.3	2.2	2.5	2.8	
	Scenario with key variables at their historical averages 7/						**134.9**	**133.3**	**133.2**	**132.3**	**130.0**	**127.5**	**4.6**
	Scenario with no policy change (constant primary balance) in 2005-2010						**134.9**	**133.2**	**132.9**	**131.7**	**129.1**	**126.2**	**4.1**
	Key Macroeconomic and Fiscal Assumptions Underlying Baseline												
	Real GDP growth (in percent)	0.9	2.2	1.9	0.4	2.0	2.9	3.0	3.1	3.2	3.2	3.2	
	Average nominal interest rate on public debt (in percent) 8/	11.5	12.7	15.7	14.1	13.0	12.0	11.8	12.2	11.4	11.4	11.2	
	Average real interest rate (nominal rate minus change in GDP deflator, in percent)	2.0	5.0	-0.7	3.6	-1.7	4.9	5.5	6.2	6.1	6.2	6.0	
	Nominal appreciation (increase in US dollar value of local currency, in percent)	-4.0	-12.9	-10.3	-0.9	-5.8	...	...	...	...	...	...	
	Inflation rate (GDP deflator, in percent)	9.5	7.6	16.4	10.5	14.7	7.1	6.3	6.0	5.3	5.2	5.2	
	Growth of real primary spending (deflated by GDP deflator, in percent)	11.1	19.0	-10.4	12.3	-13.3	22.0	-9.2	-4.1	4.7	0.6	1.8	
	Primary deficit	-7.4	-5.2	-9.3	-8.7	-9.9	-7.4	-8.9	-10.2	-9.7	-10.1	-10.4	

1/ Central government and government guaranteed debt on gross basis. From FY 2002/03, includes debt issued to the BoJ to cover its cash losses and related capitalized interest. FY 2006/07 debt includes US$350 million in prefinancing. The primary balance includes budgetary primary balance and Bank of Jamaica losses. Debt dynamics only drive Central Government debt, not Government Guaranteed debt.

2/ Derived as [(r - p(1+g) - g + ae(1+r)]/(1+g+p+gp)) times previous period debt ratio, with r = interest rate; p = growth rate of GDP deflator; g = real GDP growth rate; a = share of foreign-currency denominated debt; and e = nominal exchange rate depreciation (measured by increase in local currency value of U.S. dollar).

3/ The real interest rate contribution is derived from the denominator in footnote 2/ as r - π (1+g) and the real growth contribution as -g.

4/ The exchange rate contribution is derived from the numerator in footnote 2/ as ae(1+r).

5/ For projections, this line includes exchange rate changes.

6/ Defined as public sector deficit, plus amortization of medium and long-term public sector debt, plus short-term debt at end of previous period.

7/ The key variables include real GDP growth; real interest rate; and primary balance in percent of GDP. Includes Government Guaranteed debt.

8/ Derived as nominal interest expenditure divided by previous period debt stock.

9/ Assumes that key variables (real GDP growth, real interest rate, and other identified debt-creating flows) remain at the level of the last projection year.

Table 10. Jamaica: External Debt Sustainability Framework, 2001/02-2010/11
(In percent of GDP, unless otherwise indicated)

		Actual					Projections						Debt-stabilizing non-interest
		2001/02	2002/03	2003/04	2004/05	2005/06	2006/07	2007/08	2008/09	2009/10	2010/11	2011/12	current account 6/
1	**Baseline: External debt 1/**	**53.6**	**49.8**	**54.5**	**56.4**	**54.7**	**59.6**	**57.8**	**58.2**	**58.1**	**57.0**	**55.8**	**-2.3**
2	Change in external debt	4.7	-3.7	4.7	1.8	-1.7	4.9	-1.8	0.4	-0.1	-1.1	-1.2	
3	Identified external debt-creating flows (4+8+9)	2.1	7.4	0.2	-2.7	-1.4	2.0	2.2	2.0	1.1	0.5	0.3	
4	Current account deficit, excluding interest payments	6.2	10.1	3.3	3.5	7.9	6.3	4.6	4.8	2.7	1.4	1.2	
5	Deficit in balance of goods and services	15.4	19.8	14.9	17.4	20.4	19.8	18.0	18.5	16.4	15.0	14.8	
6	Exports	39.9	39.4	44.2	43.1	41.5	44.4	44.2	43.3	42.9	42.8	42.4	
7	Imports	55.3	59.2	59.1	60.5	61.8	64.2	62.2	61.7	59.4	57.8	57.2	
8	Net nondebt creating capital inflows (negative)	-5.6	-4.8	-7.1	-6.0	-6.0	-7.0	-5.5	-5.5	-4.2	-3.4	-3.2	
9	Automatic debt dynamics 1/	1.5	2.2	4.1	-0.2	-3.3	2.7	3.1	2.7	2.6	2.5	2.3	
10	Contribution from nominal interest rate	3.1	3.7	3.5	3.7	3.5	4.2	4.8	4.5	4.3	4.2	4.0	
11	Contribution from real GDP growth	-0.4	-1.1	-1.0	-0.2	-1.0	-1.5	-1.7	-1.7	-1.7	-1.7	-1.7	
12	Contribution from price and exchange rate changes 2/	-1.2	-0.4	1.5	-3.7	-5.9	...	...	...	...	...	...	
13	Residual, incl. change in gross foreign assets (2-3) 3/	2.6	-11.2	4.5	4.6	-0.3	3.0	-4.0	-1.6	-1.2	-1.7	-1.5	
	External debt-to-exports ratio (in percent)	134.3	126.4	123.4	130.7	131.8	134.3	130.7	134.5	135.3	133.2	131.5	
	Gross external financing need (in billions of U.S. dollars) 4/	**1.1**	**1.9**	**0.9**	**1.1**	**1.7**	**1.5**	**1.6**	**1.8**	**1.2**	**1.0**	**1.4**	
	in percent of GDP	13.7	22.6	10.3	12.6	16.8	13.8	14.5	15.0	9.3	7.5	9.8	
	Scenario with key variables at their historical averages 5/						**59.6**	**55.4**	**53.7**	**52.4**	**50.6**	**49.0**	**-5.2**
	Key Macroeconomic Assumptions Underlying Baseline												
	Real GDP growth (in percent)	0.9	2.2	1.9	0.4	2.0	2.9	3.0	3.1	3.2	3.2	3.2	
	GDP deflator in U.S. dollars (change in percent)	2.4	0.8	-3.0	7.3	11.6	2.1	2.2	2.8	2.5	2.5	2.5	
	Nominal external interest rate (in percent)	6.5	7.2	7.0	7.3	7.1	8.1	8.5	8.2	7.9	7.7	7.4	
	Growth of exports (U.S. dollar terms, in percent)	-8.4	1.7	11.0	5.1	9.5	12.4	4.9	3.7	5.0	5.3	4.9	
	Growth of imports (U.S. dollar terms, in percent)	2.3	10.2	-1.2	10.3	16.4	9.0	2.1	5.1	1.7	2.9	4.7	
	Current account balance, excluding interest payments	-6.2	-10.1	-3.3	-3.5	-7.9	-6.3	-4.6	-4.8	-2.7	-1.4	-1.2	
	Net nondebt creating capital inflows	5.6	4.8	7.1	6.0	6.0	7.0	5.5	5.5	4.2	3.4	3.2	

1/ Includes a US$350 million bond issued in March 2007 for prefinancing.

2/ Derived as [r - g - r(1+g) + ea(1+r)]/(1+g+r+gr) times previous period debt stock, with r = nominal effective interest rate on external debt; r = change in domestic GDP deflator in US dollar terms, g = real GDP growth rate, e = nominal appreciation (increase in dollar value of domestic currency), and a = share of domestic-currency denominated debt in total external debt.

3/ The contribution from price and exchange rate changes is defined as [-r(1+g) + ea(1+r)]/(1+g+r+gr) times previous period debt stock. r increases with an appreciating domestic currency (e > 0) and rising inflation (based on GDP deflator).

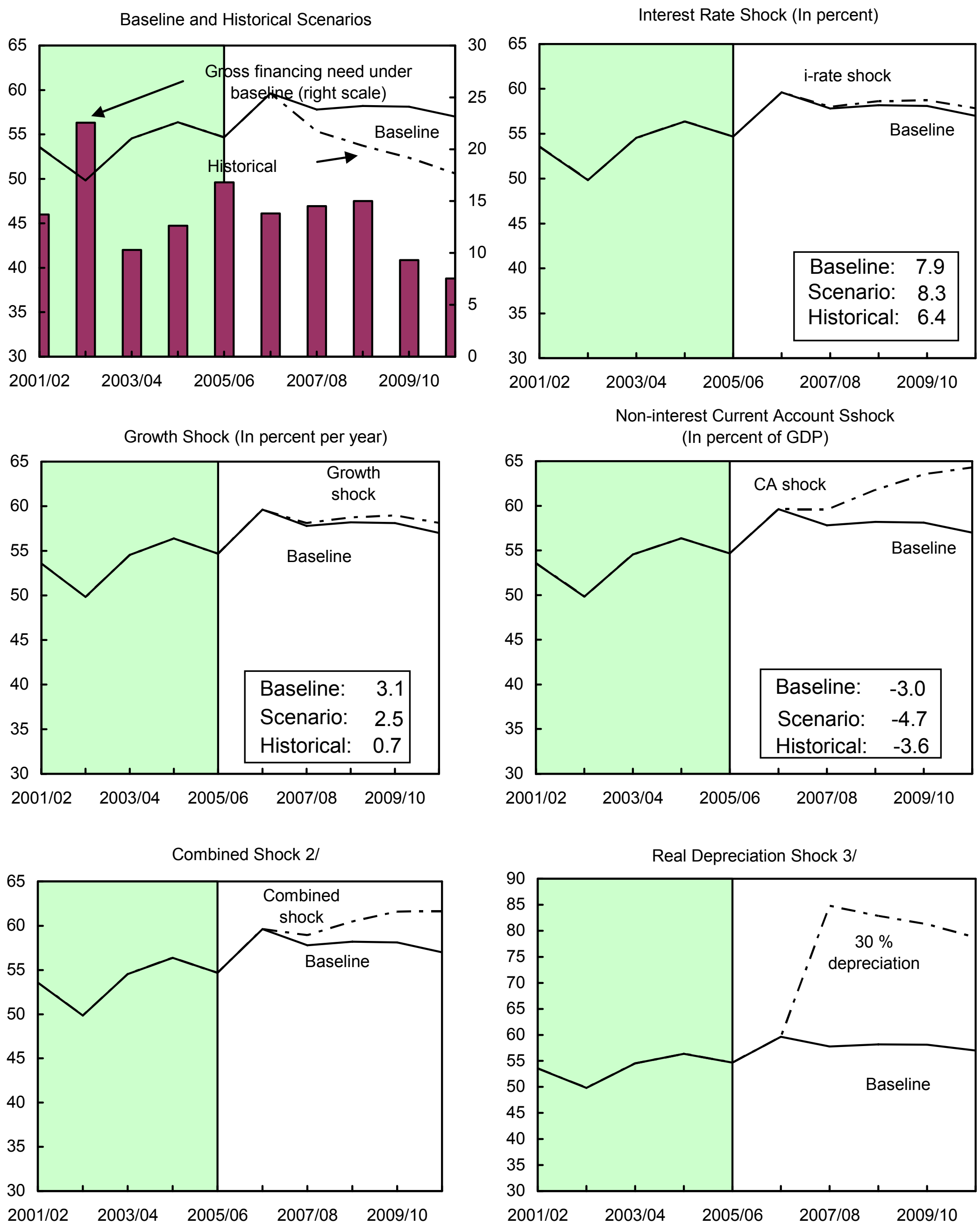
4/ For projection, line includes the impact of price and exchange rate changes.

5/ Defined as current account deficit, plus amortization on medium- and long-term debt, plus short-term debt at end of previous period.

6/ The key variables include real GDP growth; nominal interest rate; dollar deflator growth; and both non-interest current account and non-debt inflows in percent of GDP.

7/ Long-run, constant balance that stabilizes the debt ratio assuming that key variables (real GDP growth, nominal interest rate, dollar deflator growth, and non-debt inflows in percent of GDP) remain at their levels of the last projection year.

Figure 5. Jamaica: External Debt Sustainability: Bound Tests 1/
(External debt in percent of GDP)



Sources: International Monetary Fund, Country desk data, and staff estimates.

1/ Shaded areas represent actual data. Individual shocks are permanent one-half standard deviation shocks. Figures in the boxes represent average projections for the respective variables in the baseline and scenario being presented. Ten-year historical average for the variable is also shown.

2/ Permanent 1/4 standard deviation shocks applied to real interest rate, growth rate, and current account balance.

3/ One-time real depreciation of 30 percent occurs in 2007.

APPENDIX I. BACKGROUND AND SUMMARY OF APPENDICES

Discussions. The 2007 Article IV consultation discussions were held in Kingston during February 5–16, 2007. The mission met with Finance Minister Omar Davies, Governor Derick Latibeaudiere, Financial Secretary Colin Bullock, other senior officials, representatives of the private sector, and the opposition. The staff team comprised Sanjaya Panth (Head), Jinqqing Chai, Chris Faircloth and Rafael Romeu (all WHD); and, Piyabha Kongsamut (PDR). Ms. Atkinson (WHD) joined the team for the final discussions, as did Mr. Fried (Executive Director) and Ms. Morgan (OED).

Exchange arrangement. Jamaica has accepted the obligations of Article VIII, Sections 2, 3, and 4, and maintains an exchange system free of restrictions on payments and transfers for current transactions. Beginning September 17, 1990, the external value of the Jamaican dollar has been determined in an interbank market operated by commercial banks. Jamaica's exchange regime is classified by the Fund as a managed float with no pre-determined path.

Fund Relations. Jamaica has no outstanding purchases or loans. The last financial arrangement was an Extended Fund Arrangement for the period 12/11/92 to 03/16/96 totaling SDR$109 million (of which SDR$77.8 million was drawn). The post of the resident representative in Jamaica was closed in August 1997.

Technical Assistance. In 2006, a CARTAC/FAD mission evaluated tax and customs administration performance and prepared a set of recommendations to strengthen the operations of the Jamaica Tax Administration. The Fund has also provided TA on banking supervision and national accounts methodology in recent years.

Statistical Issues. Data provision to the Fund is adequate for surveillance purposes despite weaknesses in national accounts and the lack of producer price and international investment position (IIP) data. Efforts are being made to improve the national accounts, including through updating the base year. The authorities are also in the process of revising their CPI weightings and preparatory work is underway to begin compiling IIP data. This latter effort has been supported by the Caribbean Regional Technical Assistance Center (CARTAC) and the European Union.

Relations with the World Bank Group. At March 30, 2007, the active portfolio of the Bank stood at US$139 million, of which US$53 million remains undisbursed. The Country Assistance Strategy (CAS) for Jamaica was approved by the WB Executive Board on May 10, 2005. The CAS proposes financial assistance of up to US$150 million between 2006 and 2009 in support of: (i) accelerating inclusive economic growth, (ii) improving human development and opportunity, and (iii) preventing and reducing crime.

Relations with the Inter-American Development Bank. As of February 2007, Jamaica's outstanding debt to the IDB stood at US$637 million, of which US$607 million were public sector loans and US$30 million were loans to the private sector. In August 2006, the IDB approved a new country strategy for the 2006–09 period. The principal areas of focus are: (i) private sector development; (ii) value for money; and (iii) reducing vulnerability to natural disasters.

Appendix I. Jamaica—Fund Relations
(As of February 28, 2007)

I. Membership Status: Joined: February 21, 1963; Article VIII

II. General Resources Account:	**SDR Million**	**% Quota**
Quota	273.50	100.00
Fund holdings of currency	273.55	100.02
Reserve position	0.00	0.00
Holdings exchange rate		

III. SDR Department:	**SDR Million**	**% Allocation**
Net cumulative allocation	40.61	100.00
Holdings	0.17	0.42

IV. Outstanding Purchases and Loans: None

V. Latest Financial Arrangements:

Type	Approval Date	Expiration Date -	Amount Approved (SDR Million)	Amount Drawn (SDR Million)
EFF	Dec. 11, 1992	Mar. 16, 1996	109.13	77.75
Stand-By	Jun. 28, 1991	Sep. 30, 1992	43.65	43.65
Stand-By	Mar. 23, 1990	May 31, 1991	82.00	82.00

VI. Projected Payments to Fund:

(SDR Million; based on existing use of resources and present holdings of SDRs):

	Forthcoming				
	2007	2008	2009	2010	2011
Principal					
Charges/Interest	1.29	1.73	1.72	1.73	1.73
Total	1.29	1.73	1.72	1.73	1.73

VII. Implementation of HIPC Initiative: Not Applicable

VIII. Implementation of Multilateral Debt Relief Initiative (MDRI): Not Applicable

IX. Exchange Rate Arrangements:

The external value of the Jamaican dollar has been determined in an interbank market operated by commercial banks beginning September 17, 1990. The Jamaican dollar has depreciated significantly since then, though not in a uniform trend. At January 31, it was trading at around J$67 to the U.S. dollar. At the conclusion of the 2004 Article IV consultation for Jamaica, it was found that a multiple currency practice arose from the implementation of the surrender requirement where authorized foreign exchange dealers and cambios are required to surrender at least 5 percent—but not more than 10 percent—of their purchases of U.S. dollars, Canadian dollars and pound sterling to the Bank of Jamaica (BOJ). This surrender requirement is effected based on the previous day's average selling rate for the U.S. dollar, the Canadian dollar and the pound sterling, respectively, against the Jamaican dollar (referred below as "surrender rates"). In 2004, the surrender rates had resulted in the cross rates between the U.S. dollar and the Canadian dollar and between the U.S. dollar and the pound sterling to differ periodically (for more than five days) by more than 1 percent from the midpoint spot exchange rates for those two currency pairs in their principal markets. While such differences were observed in 2004 leading to a finding that a multiple currency practice arose, the previously identified broken cross rate arising from the currency surrender requirement is no longer apparent since this time. Therefore, there is no evidence that a multiple currency practice arises from the surrender requirement.

X. Last Article IV Consultation and Program Relations:

Jamaica is under intensified surveillance whereby staff monitor the implementation of the economic strategy formulated by the authorities without reaching prior understandings with the Fund. The last Article IV consultation was completed by the Executive Board on March 24, 2006 (IMF Country Report Nos. 06/158 and 06/157). Interim staff reports are prepared for information of the Executive Board in-between Article IV consultations (IMF Country Report Nos. 06/324, 05/219, and 05/61).

XI. Technical Assistance:

Department	**Dates**	**Purpose**
FAD	September 2006	Tax and Customs Administration
MAE	May 1995	Review of deposit insurance scheme
	October–December 1995	Banking supervision
	February–June 1996	Banking supervision
	September 1996	Banking crisis and restructuring
	October 1996	Banking supervision
	February 1997	Central bank accounting
	May 1997	Banking supervision
	August 1997	Banking supervision
	January 1998	Banking supervision
	April 1998	Public debt management
	May 1998	Financial sector restructuring
	April 2001	Banking supervision
	January 2002	Banking supervision
STA	September 1996	Multisector statistics assessment

XII. **Resident Representative**:

The post of the resident representative was closed on August 1997.

Appendix II. Jamaica—Relations with the World Bank

(As of March 30, 2007)

The new Country Assistance Strategy (CAS) for Jamaica was discussed by the WB Board of Executive Directors on May 10, 2005. The document proposes financial assistance of up to US$150 million between 2006 and 2009, as well as technical and advisory services. The CAS will support the Government's own Medium Term Socioeconomic Policy Framework for 2004-2009 with lending, analytical, and technical assistance to accelerate inclusive economic growth, improve human development and opportunity, and help prevent and reduce crime. It was prepared in collaboration with the government and was widely consulted and discussed with other donors, representatives of the private sector, CBOs, Chambers of Commerce, trade unions, and academic institutions. As part of the assistance program, the Bank will undertake analytical work including a Poverty Assessment, a Financial Sector Assessment Program (jointly with the International Monetary Fund), a Country Fiduciary Assessment (jointly with the Inter-American Development Bank), and a Diagnostic of the Investment Climate. The Bank Group assistance program will include support from the International Finance Corporation (IFC), focused on investment in infrastructure, the financial sector, services and other sectors, and the Multilateral Investment Guarantee Facility (MIGA), focused on development of the financial sector and key infrastructure.

A. Projects

The Jamaica **Reform of Secondary Education Project II** was approved in March 2003 for US$39.8 million. In support of Jamaica's fifteen-year program to reform secondary education, the Project will improve the quality, and equity of secondary education, and expand access to upper secondary education, as well as strengthen the capacity of the central ministry, and regional offices to manage, and monitor the reform. The components of the Second Reform of Secondary Education Project will: 1) finance grants to selected secondary schools, on the basis of annual work programs, and budgets for activities designed to improve student outcomes, as well as direct costs associated with preparing, and implementing school improvement plans. Technical assistance will support the preparation of a school improvement plan manual, and training materials, while training assistance in school development, and management will be provided; 2) finance centrally coordinated activities that complement the bottom up approach, and support all-age schools not eligible for school improvement grants (SIGs), to rally national literacy programs, and mathematics, by providing tools for teachers to diagnose the specific learning problems, enriching libraries and media centers, and supporting counseling for at-risk youths; 3) provide access to upper secondary school, by securing excess capacity in independent secondary schools, through construction of new schools, and extension of existing selected schools; and, 4) support the Ministry of Education, and regional offices in the implementation of the above components, as their role shifts from centralized, to one responsive to school-based demands for technical assistance, and continuous support on monitoring outcomes.

The Jamaica **HIV/AIDS Prevention and Control Project** was approved in August 2002 for US$15 million. The HIV/AIDS Prevention and Control Project for Jamaica is part of the Second Phase Multi-Country HIV/AIDS Prevention and Control Adaptable Program Lending (APL) for the Caribbean Region, which provides loans and/or credits to governments in the

Region to finance their HIV/AIDS programs. Jamaica has met the five eligibility criteria for country participation. This project aims to support selected activities of Jamaica's HIV/AIDS National Strategic Plan (NSP). Using a multi-sectoral approach, it assists the Government of Jamaica in curbing the spread of the HIV epidemic through 1) the expansion of preventive programs targeted to high-risk groups as well as the general population; 2) the strengthening of treatment, care, and support for persons living with HIV/AIDS (PLWHA); and 3) the strengthening of Jamaica's multisectoral capacity to respond to the epidemic

The Jamaica **Social Safety Net Project** was approved in February 2002 for US$40 million. The Social Safety Net Project is supporting the Government's efforts to transform the social safety net into a fiscally sound, and efficient system of social assistance for the poor, and vulnerable groups. The components will: 1) finance conditional grants for poor children (up to age 17), eligible under the program. Direct costs regarding schooling, and health care delivery will be financed by those grants, conditioned on regular health clinic visits for children up to the age of six not enrolled in school, and for children on school attendance up to the age of seventeen; 2) finance conditional grants to poor pregnant/lactating mothers, elderly poor over the age of sixty-five, and poor disabled, and destitute adults under the age of sixty-five, eligible under the program. Benefits will be conditional on regular health clinic visits for adult beneficiaries; and, 3) strengthen the institutional capacity of the Ministry of Labor and Social Security, and institutions involved in the operation, and streamlining of the social safety net in Jamaica. Support will be provided for enrollment mechanisms of temporary employees, hired for data processing, including as well the financing of the necessary technology information equipment, and software. Technical assistance, will support implementation of the scoring formula, based on data from the Survey of Living Conditions, namely at the early stages, when the scoring formula will require periodic review, and refinement. Also included are training, and promotion assistance, project management costs, and, monitoring, and evaluation systems.

The Jamaica **National Community Development Project** was approved in April 2003 for US$15 million. The National Community Development Project aims at providing basic services and creating temporary employment opportunities for the poorest groups in Jamaica. To this end, several subprojects have been identified as priority by these communities for funding by the Jamaica Social Investment Fund (JSIF). The project components include: 1) financing of demand-driven, and community-implemented socioeconomic infrastructure works, and activities, through subprojects that include construction, and rehabilitation of basic infrastructure, and social super-structure facilities. Community assessments will be implemented, to ensure appropriate skills (or ability to acquire skills), and resources availability to manage the proposed community-contracted works; 2) financing for technical assistance, training, and strengthening programs to JSIF, and the various entities to be involved in the project, particularly to support the Community Based Contracting (CBC) system. Financing will also be provided for additional consultants to support implementation of community contracting; and, 3) funding for goods required to facilitate subproject supervision, monitoring, and community training.

The Jamaica **Inner City Basic Services for the Poor Project** was approved in March 2006 for US$29.3 million. The project development objective is to improve quality of life in 12 Jamaican inner-city areas and poor urban informal settlements through improved access to basic urban infrastructure, financial services, land tenure regularization, enhanced community capacity and improvements in public safety. Specifically, the project will: (a) increase access and improve the quality of water, sanitation, solid waste collection systems, electricity, roads, drainage and related community infrastructure for over 60,000 residents of poor urban informal settlements through capital investments and innovative arrangements for operations and maintenance; (b) facilitate access to microfinance for enterprise development and incremental home improvement for entrepreneurs and residents in project areas; (c) increase security of tenure for eligible households in project areas; and (d) enhance public safety through mediation services, community capacity building, skills training and related social services.

B. Economic and Sector Work

During 2003 and 2004, the Bank prepared a Country Economic Memorandum focused on issues related to accelerating inclusive economic growth and, during 2004 and 2005, a Public Expenditure Review examining public expenditure allocation priorities and public sector reform issues in Jamaica's tight fiscal environment. In addition, a study on growth and competitiveness issues in the Caribbean recently completed by the Bank provides the Government with insights and policy recommendations for improving the competitiveness of the economy. The dissemination of these reports represented a key instrument for policy discussion with the Government on the country's development priorities and the Bank's assistance strategy.

A Poverty Assessment currently under preparation will provide an updated assessment of poverty levels and will focus on poverty and the labor market, and the link between crime and violence and poverty. Work on a Country Fiduciary Assessment (CFA), in collaboration with the Inter-American Development Bank, is underway to help strengthen public financial management and procurement. It will also help to provide a sound basis for the harmonization and alignment with the country's procurement and financial management systems. To help create a positive enabling environment for private sector driven growth, the Bank is also undertaking a Diagnostic of Investment Climate which will provide policy recommendations complementary to the recently completed study on growth and competitiveness issues in the Caribbean.

The Bank will continue the informal monitoring of macroeconomic developments given the vulnerability of the economy. This will be done within the context of the results based monitoring framework agreed between the Government and the donors. In addition, the Bank will undertake just-in-time policy notes to follow-up on specific findings and recommendations of the studies undertaken during the CAS period and other issues jointly identified with the authorities.

In addition to the country specific analytical work, Jamaica will benefit from ongoing and planned regional studies. A Caribbean regional study on Crime, Violence and Social Exclusion would focus on the impact of crime on tourism, investment, poverty, and social cohesion. This would be a multi-sectoral endeavor aimed at developing recommendations that would draw on experience from successful interventions in Brazil and elsewhere. The Bank has completed a Social Protection Strategy Review paper for the Caribbean, including a focus on Jamaica. The objective of the strategy is to strengthen the Bank's ability to support clients on social protection through: (i) better understanding the key socio-economic risks, existing country-level social protection programs, coverage and implementation gaps, and outstanding country-level needs; (ii) stronger coordination with country counterparts and donors; and (iii) more strategic emphasis on the Bank's comparative advantage in the region. A Caribbean regional study on Migration, Remittances and the Diaspora will examine the impact of migration and its implications for public policy decisions surrounding the financing of higher education and skills development; the impact, facilitation, and potential leverage of remittance flows; and the potential for the growth of niche markets among the diaspora. This work will be undertaken in close collaboration with other donors, most notably the IDB. Additional planned regional studies cover issues related to pension reform, health financing, and the infrastructure and financial sectors

C. Financial Relations[1]

(In millions of U.S. dollars)

Project	Original Amount	Available	Disbursed Outstanding
National Community Development Project	15.0	2.5	12.5
JM - Reform of Secondary Education Project II	39.8	7.3	5.2*
JM – Inner City Basic Services for the Poor Project	29.3	28.4	0.9
HIV/AIDS Prevention and Control Project (Second Phase)	15.0	3.0	7.6
Social Safety Net Project	40.0	12.1	26.8
Total	**139.10**	**53.3**	**53.0**

1/ Amounts may not add up to Original Principal due to changes in the SDR/US exchange rate since signing.
* Project restructured.

Disbursements and Debt Service (Fiscal Year Ending June 30)

	Actual							Projections
	2000	2001	2002	2003	2004	2005	2006	2007
Total disbursements	65.1	97.6	82.4	85.0	11.3	8.5	21.7	10.9
Repayments	70.1	56.9	45.7	44.9	47.4	43.4	39.7	34.1
Net disbursements	-5.0	40.7	36.7	40.1	-36.1	-34.9	-17.9	-23.1
Interest and fees	22.8	21.6	20.3	21.9	18.9	17.5	20.5	21.6

Appendix III. JAMAICA—Relations with the Inter-American Development Bank

Jamaica joined the Inter-American Development Bank (IDB) in 1969. Since then, the IDB has approved 95 loans (78 projects) to Jamaica amounting to US$1.8 billion and 179 technical cooperation operations totaling US$59.6 million. IDB financial assistance has supported a wide range of infrastructural, environmental and social sector projects with a view to enhancing Jamaica's human resource and absorptive capacity and strengthening the foundation for private sector-led growth. In addition, the IDB has supported reforms aimed at strengthening the institutional and regulatory environment.

The IDB is the leading lender to Jamaica among multilateral development partners. As of February 2007, Jamaica's outstanding debt to the IDB stood at US$637 million, of which US$607 million were public sector loans and US$30 million were loans to the private sector. The total represents 11 percent of public external debt and half of multilateral debt. Nevertheless, the IDB's share of total public external debt—like that of most other multilateral and bilateral agencies—has declined since 2003.

Table 1. IDB Outstanding Debt

Type	Amount (US$m.)
Public Sector	606.9
Private Sector	30.0
Total Debt Outstanding	636.9

As of February 2007, the Bank's portfolio consisted of 10 investment loans valued at US$217.8 million, and 28 non-reimbursable technical cooperations (TC) valued at US$13.0 million. Forty-three percent of the IDB project funds and fifty-two percent of the TC funds have been disbursed, leaving some US$130.5 million available for disbursement.

Table 2. Major Ongoing Projects

Project Category	Number	Amount (US$m.)	Percent Disbursed
Projects in execution	10	217.8	43
Private sector loans	1	5.0	0
IIC loans	1	10.0	35
TCs in execution	28	13.0	52

Over time, growing government current expenditures—particularly on interest payments and wages and salaries—have crowded out capital expenditures. The reduction in the government's investment program caused budgetary allocations to IDB-supported projects to fall far short of that needed for a normal pace of implementation, particularly in the period from 2002/03 to 2004/05. This slowed project execution and extended project lifetimes, delayed or prevented the achievement of development objectives, and increased the ratio of project administration and financial costs to disbursements (Table 3).

Table 3. Number of Projects by Implementation Progress Category

	2002	2003	2004	2005	2006
Highly Satisfactory	0	0	0	0	0
Satisfactory	10	7	6	7	7
Unsatisfactory	3	6	7	4	3
Very unsatisfactory	0	0	0	2	0
TOTAL	13	13	13	13	10

In recognition of this, and in order to make the IDB portfolio of projects more consistent with available fiscal space, the government and IDB have collaborated to rationalize the portfolio through partial cancellation of loans while trying to minimize the impact of cancellations on the likely achievement of the portfolio's development objectives. In October 2004, the government and IDB agreed to cancel US$49.8 million in loan resources from nine out of the 13 projects. In 2006, the government and IDB made further partial cancellations of US$10 million. In FY2006/07, government capital expenditures have increased and IDB-supported projects have received better budget allocations, resulting in an improved pace of project implementation.

In August 2006, the IDB approved a new country strategy for the 2006–09 period. In view of the aforementioned fiscal space issue, the new strategy de-emphasizes public sector investment lending and instead focuses on policy-based lending, grant modalities, and lending to the private sector. The principal areas of focus are: (i) private sector development; (ii) value for money; and (iii) reducing vulnerability to natural disasters.

Growing repayments from lending in the late 1990s and the constraints on disbursements on investment projects caused by the lack of fiscal space have resulted in negative net loan flows since 2005 (Table 4).

Table 4. Net Flow of IDB Convertible Currencies
(US$ million)

	2003	2004	2005	2006	2007[4]
a. Loan disbursements	26.4	80.8	12.8	25.9	62.4
b. Repayments (principal)	52.7	52.3	51.2	64.1	70.0
c. **Net loan flow (a–b)**	**-26.3**	**28.5**	**-38.4**	**-38.2**	**-7.7**
d. Interest and charges	31.2	29.1	29.8	28.0	31.3
e. **Net cash flow (c– d) 1/**[5]	**-58.5**	**-2.7**	**-73.6**	**-70.6**	**-42.4**

[4] Projected figures.
[5] e. includes subscriptions.

Table 5. Total Projected Debt Service, 2007–11
(Millions of U.S. dollars equivalent)

	2007	2008	2009	2010	2011
Principal	70.0	70.0	67.1	62.4	50.1
Interest	31.3	30.4	28.1	25.0	22.3
Total	**101.3**	**100.4**	**95.2**	**87.4**	**72.4**

Appendix IV. Jamaica—Statistical Issues

Data provision to the Fund is adequate for surveillance purposes despite weaknesses in national accounts and the lack of producer price and international investment position data. In early 2003, Jamaica started participating in the Fund's General Data Dissemination System (GDDS), which provides participants with a framework for the development of the statistical system. Jamaica should now focus its efforts on improving its data and dissemination practices by moving towards the goal of subscribing to the Special Data Dissemination Standards (SDDS) over the medium term.

Key websites for statistics on Jamaica:

Bank of Jamaica:	**http://www.boj.org.jm/**
Ministry of Finance and Planning:	**http://www.mof.gov.jm/**
Planning Institute of Jamaica:	**http://www.pioj.gov.jm/**
Statistical Institute of Jamaica:	**http://www.statinja.com/**

National accounts

There are significant weaknesses in the national accounts and other real sector data. In regard to GDP estimates, concerns relate both to its level and growth rate. Addressing these shortcomings has been hindered, *inter alia*, by insufficient legal authority granted to the Statistical Institute of Jamaica (STATIN) to collect source data, as well as by institutional weaknesses, and a lack of resources. However, efforts are being made to improve the national accounts, including through updating the base year. Assistance on national accounts methodology has been provided by Statistics Canada and by a STA technical assistance mission in June 2001. The first publication of quarterly national accounts was issued in August 2002.

Prices

Expenditure weights of the consumer price index (CPI) are derived from a household expenditure survey carried out in 1984, with the base for the index being January 1988, resulting in an apparent inconsistency. STATIN is in the process of updating weights based on a household survey conducted in 2004–05 and the revamped CPI is expected to be released in 2007.

Production

No data on industrial production, wholesale or producer prices, import volumes, or export and import prices have been reported for publication in the *International Financial Statistics (IFS)* in recent years.

Government finance statistics

These data are available at:
Debt: http://www.mof.gov.jm/dmu/
Budget: http://www.mof.gov.jm/programmes/em/fpmu/default.shtml

Fiscal data is not currently reported for publication in the *IFS*. In 2005, the authorities reported data for 2003, in *GFSM 2001* format, for publication in the 2005 GFS *Yearbook*.

Monetary and financial statistics

Monetary statistics published by the Bank of Jamaica (BOJ) are sectorized, classified, and valued in accordance with international standards, and are provided to the Fund in a timely manner. Currently, information on deposit money banks and monetary authorities is being reported on a regular basis. The BOJ initiated the submission of monetary and financial statistics based on standardized report forms in March 2007.

Balance of payments

The BOJ compiles and disseminates balance of payments statistics on a monthly and annual basis. Detailed annual balance of payments data are reported by the BOJ for publication in the Balance of Payments Statistics Yearbook (BOPSY) and the IFS. At present, the BOJ does not compile International Investment Position (IIP) statistics although it has begun preparatory work with assistance from the Caribbean Regional Technical Assistance Center (CARTAC) and the European Union.

JAMAICA: TABLE OF COMMON INDICATORS REQUIRED FOR SURVEILLANCE AS OF MARCH 28, 2007

	Date of latest observation	Date received	Frequency of Data[6]	Frequency of Reporting[6]	Frequency of publication[6]
Exchange Rates	03/27/07	03/28/07	D	D	D
International Reserve Assets and Reserve Liabilities of the Monetary Authorities[1]	12/06	02/07	M	M	M
Reserve/Base Money	02/07	03/07	M	M	M
Broad Money	12/06	02/07	M	M	M
Central Bank Balance Sheet	12/06	02/07	W	W	W
Consolidated Balance Sheet of the Banking System	12/06	02/07	M	M	M
Interest Rates[2]	02/07	03/07	M	M	M
Consumer Price Index	01/07	03/07	M	M	M
Revenue, Expenditure, Balance and Composition of Financing[3] – General Government[4]	02/07	03/07	M	M	M
Revenue, Expenditure, Balance and Composition of Financing[3]– Central Government	02/07	03/07	M	M	M
Stocks of Central Government and Central Government-Guaranteed Debt[5]	02/07	03/07	M	M	M
External Current Account Balance	11/06	3/07	M	M	M
Exports and Imports of Goods and Services	11/06	3/07	M	M	M
GDP/GNP	Q4/06	04/07	Q	Q	Q
Gross External Debt	02/07	03/07	M	M	M

[1]Includes reserve assets pledged or otherwise encumbered, as well as net derivative positions.
[2] Both market-based and officially-determined, including discount rates, money market rates, rates on treasury bills, notes and bonds.
[3] Foreign, domestic bank, and domestic nonbank financing.
[4] The general government consists of the central government (budgetary funds, extra budgetary funds, and social security funds), and state and local governments.
[5] Including currency and maturity composition.
[6] Daily (D), Weekly (W), Monthly (M), Quarterly (Q), Annually (A), Irregular (I); Not Available (NA).

INTERNATIONAL MONETARY FUND

JAMAICA

Staff Report for the 2007 Article IV Consultation
Supplementary Information

Prepared by the Staff Representatives for the 2007 Consultation with Jamaica

Approved by Caroline Atkinson and Anthony Boote

April 20, 2007

1. **This supplement provides an update on the fiscal outturn for FY 2006/07 and the authorities' budget proposal for FY 2007/08**. The new information reinforces the thrust of the staff appraisal contained in the staff report (4/11/07).

2. **Recent data releases suggest that the growth momentum may be slowing but inflation remains on target**. Real manufacturing activity appears to have weakened toward the end of 2006. Tourist arrivals for the first three months of 2007 have also been lower than anticipated. Real economic growth for FY 2006/07 may, therefore, be somewhat lower than the 3 percent expected earlier. Annual consumer price inflation, meanwhile, ended the fiscal year at 6½ percent, down from 11½ percent the previous year. International reserves recovered in March to reach US$2.3 billion, just shy of the all time high reached at end-2006.

3. **As anticipated in the staff report (4/11/07), the budgetary outturn for FY 2006/07 was weaker than indicated by data available earlier**. The authorities now estimate that J$5.5 billion (0.8 percent of GDP) in capital spending occurred in FY 2006/07 on central government projects funded by donors and PetroCaribe that were not picked up by the normal reporting process for spending. Preliminary information also suggests that revenues are likely to have ended the year somewhat lower than expected earlier. All in all, the overall budget deficit for FY 2006/07 is now estimated at 5.7 percent of GDP, compared to 4.7 percent of GDP indicated by earlier data (see tables 1 & 2). The primary balance is also now correspondingly lower. The earlier debt data had, however, already picked up the obligations associated with the higher capital spending and, therefore, debt estimates remain broadly unchanged from the staff report (4/11/07).

4. **The draft FY 2007/08 budget submitted to parliament recently envisages an improvement in the primary balance by about 2 percent of GDP, to 10¼ percent of GDP under staff definitions**. Parliamentary debate on the government's budget proposal commenced on April 12. In their presentation of the FY 2007/08 budget, the authorities are

recognizing under capital spending J$12.5 billion associated with previous years.[1] Staff presentations in the attached tables have allocated these amounts to the appropriate earlier years and, therefore, capital spending as well as the overall balance differ from the authorities' official budget presentations.

5. **The FY 2007/08 budget sets a high bar for tax administration and envisages new capital expenditures to replace one-off spending in FY 2006/07**. The budget includes two tax measures (cigarette tax and environmental levy on imports) expected to yield 0.2 percent of GDP. At the same time, a new exemption to the existing Customs User Fee will lead to some loss in revenue. Nevertheless, the authorities are hoping to increase total tax revenues by 1½ percentage points of GDP, to 28½ percent in FY 2007/08 by strengthening tax administration, including improving procedures to verify refunds. The budget envisages the expenditure-to-GDP ratio at 34¼ percent in FY 2007/08, down by about 1¼ percentage points from FY 2006/07. Budgeted amounts, however, still allow for an increase in capital spending if the one-off nature of the FY 2006/07 Cricket World Cup spending (estimated at around 1.1 percent of GDP) is taken into account. The new capital spending is broad-based but with some concentration in the areas of transportation, public works, and education.

6. **The staff welcomes the planned improvement in the primary balance but considers that achieving it will require additional tax policy or expenditure measures.** Such measures (see staff report of 4/11/07, paragraph 19) will need to be implemented earlier rather than later in FY 2007/08 to secure the planned adjustment within the fiscal year**.** While strengthened tax administration has already delivered measurable successes in FY 2006/07, generating sufficient additional resources from this source alone will likely become increasingly difficult.

7. **The authorities' efforts to regularize the budget recording and reporting procedures are welcome and should continue**. The provision made in the FY 2007/08 budget for past expenditures undertaken through special financing schemes exemplifies the authorities' existing commitment to fiscal transparency. At the same time, it also highlights the potential benefits of carrying out a thorough review of fiscal standards and codes, creating a framework to identify risk from off-budget entities, and putting in place a stronger consolidated public sector accounting framework.

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[1] This figure includes the J$5.5 billion referred to in paragraph 3 and J$0.4 billion in FY 2005/06, as well as other amounts for deferred financing (see footnote 3 in table 2) and the take-over of public entity debt.

Table 1. Jamaica: Summary of Central Government Operations
(In billions of Jamaican dollars)

	2004/05	2005/06	2006/07		2007/08	
			Staff Rpt. (4/11/07)	Rev.	Staff Rpt. (4/11/07)	Budget 4/
Budgetary revenue and grants	171.5	186.7	213.3	211.6	224.1	243.1
Tax	153.0	165.7	193.3	192.5	204.2	221.9
Nontax	14.4	20.3	16.7	17.3	17.4	17.9
Grants	4.2	0.7	3.2	1.8	2.5	3.3
Budgetary expenditure	201.8	210.4	246.7	251.7	262.4	265.6
Primary expenditure	106.4	116.0	150.6	154.9	160.4	164.2
Wage and salaries	63.5	63.1	78.2	78.7	86.7	88.5
Other expenditure	32.1	40.8	49.3	49.1	52.7	49.3
Capital expenditure	10.8	12.0	23.2	27.2	21.0	26.3
Interest	95.4	94.4	96.0	96.8	102.0	101.5
Domestic	75.3	71.5	69.2	70.3	71.1	70.5
Current	72.6	65.4	64.4	65.5	65.3	64.7
BoJ special issue bonds 1/	2.6	6.1	4.8	4.8	5.8	5.8
External	20.1	22.9	26.8	26.5	30.9	31.0
Gap	0.0	0.0	0.0	0.0	14.3	0.0
Budget balance	**-30.2**	**-23.7**	**-33.4**	**-40.1**	**-24.0**	**-22.6**
***Of which:* primary balance**	**65.2**	**70.7**	**62.6**	**56.7**	**78.0**	**78.9**
Off-budget expenditure	17.3	7.4	10.1	10.1	9.0	9.0
BoJ cash losses 2/	13.4	7.4	10.1	10.1	7.4	7.4
Deferred financing 3/	3.9	0.0	0.0	0.0	1.6	1.6
Overall balance	-47.5	-31.2	-43.5	-50.2	-33.1	-31.6
Financing	47.5	31.2	43.5	50.2	33.1	31.6
External financing	7.8	20.7	13.3	13.3	-21.0	-21.0
Domestic financing	38.5	10.5	30.3	37.0	54.1	52.6
Banking system	1.0	-11.9	4.0	4.0	38.7	38.7
Others	37.5	22.4	26.2	33.0	15.4	13.9
Divestment	1.3	0.0	0.0	0.0	0.0	0.0

Sources: Jamaican authorities; Fund staff estimates and projections.

1/ Accrued interest on previous year's BoJ Special Issue bonds is contractually paid to the BoJ through debt issuance the following year.
2/ Refers to operating losses of the Bank of Jamaica, not covered by the BOJ Special Issue Bonds.
3/ Debt issued upon assuming public investment projects carried out by the private sector under the deferred financing facility. The government has been authorizing amounts under this facility since 1997. Staff presentations have been including the debt incurred as “off budget spending” at the time of debt issuance. Starting in FY 2005/06, the authorities also started including (in their own budget presentations, to which adjustments are made here to avoid double-counting) amounts under capital expenditure at the time debt service first begins. The schedule according to which the authorities incorporate this spending in their budget presentation was recently revised and they are undertaking a review of the historical data to help ensure continuing consistency between different presentations.
4/ Staff presentation of authorities' draft budget.

Table 2. Jamaica: Summary of Central Government Operations
(In percent of GDP)

	2004/05	2005/06	2006/07		2007/08	
			Staff Rpt. (4/11/07)	Rev.	Staff Rpt. (4/11/07)	Budget 5/
Budgetary revenue and grants	31.2	29.0	30.1	29.8	28.9	31.3
Tax	27.8	25.8	27.3	27.1	26.3	28.6
Nontax	2.6	3.2	2.4	2.4	2.2	2.3
Grants	0.8	0.1	0.5	0.3	0.3	0.4
Budgetary expenditure	36.7	32.7	34.8	35.5	33.8	34.2
Primary expenditure	19.4	18.0	21.2	21.8	20.7	21.2
Wage and salaries	11.6	9.8	11.0	11.1	11.2	11.4
Other expenditure	5.8	6.4	7.0	6.9	6.8	6.4
Capital expenditure	2.0	1.9	3.3	3.8	2.7	3.4
Interest	17.4	14.7	13.5	13.7	13.1	13.1
Domestic	13.7	11.1	9.8	9.9	9.2	9.1
Current	13.2	10.2	9.1	9.2	8.4	8.3
BoJ special issue bonds 1/	0.5	0.9	0.7	0.7	0.7	0.7
External	3.7	3.6	3.8	3.7	4.0	4.0
Gap 3/	0.0	0.0	0.0	0.0	1.8	0.0
Budget balance	**-5.5**	**-3.7**	**-4.7**	**-5.7**	**-3.1**	**-2.9**
***Of which:* primary balance**	**11.9**	**11.0**	**8.8**	**8.0**	**10.0**	**10.2**
Off-budget expenditure	3.1	1.2	1.4	1.4	1.2	1.2
BoJ cash losses 2/	2.4	1.2	1.4	1.4	1.0	1.0
Deferred financing 3/	0.7	0.0	0.0	0.0	0.2	0.2
Overall balance	-8.6	-4.8	-6.1	-7.1	-4.3	-4.1
Budgetary principal payment	24.3	21.8	17.4	17.4	13.1	13.1
Domestic	18.9	16.6	14.7	14.7	8.8	8.8
External	5.4	5.1	2.7	2.7	4.3	4.3
Memorandum items:						
Deposit draw-down (in percent of GDP)	0.0	0.0	2.3	2.3	3.1	3.1
Public debt 4/	139.6	133.0	134.9	134.7	131.0	130.6
Of which: cumulative PetroCaribe debt	...	0.1	2.1	2.1	4.1	4.1
Gross financing (in percent of GDP)	32.9	26.6	23.5	24.5	17.3	17.1
GDP (in billions of J$)	550	643	709	709	776	776

Sources: Jamaican authorities; Fund staff estimates and projections.

1/ Accrued interest on previous year's BoJ Special Issue bonds is contractually paid to the BoJ through debt issuance the following year.
2/ Refers to operating losses of the Bank of Jamaica, not covered by the BOJ Special Issue Bonds.
3/ Debt issued upon assuming public investment projects carried out by the private sector under the deferred financing facility. The government has been authorizing amounts under this facility since 1997. Staff presentations have been including the debt incurred as “off budget spending” at the time of debt issuance. Starting in FY 2005/06, the authorities also started including (in their own budget presentations, to which adjustments are made here to avoid double-counting) amounts under capital expenditure at the time debt service first begins. The schedule according to which the authorities incorporate this spending in their budget presentation was recently revised and they are undertaking a review of the historical data to help ensure continuing consistency between different presentations.
4/ Central Government debt including debt assumed from public entities, plus guaranteed public entity debt, plus PetroCaribe debt. Includes US$350 million bond issued in March 2007 for prefinancing. Cash-flow savings from the PetroCaribe agreement with Venezuela are managed by an extrabudgetary Fund that lends to both budgetary and off-budget entities.
5/ Staff presentation of authorities' draft budget.

INTERNATIONAL MONETARY FUND
Public Information Notice
EXTERNAL RELATIONS DEPARTMENT

Public Information Notice (PIN) No. 07/50
FOR IMMEDIATE RELEASE
May 4, 2007

International Monetary Fund
700 19th Street, NW
Washington, D. C. 20431 USA

IMF Executive Board Concludes 2007 Article IV Consultation with Jamaica

On April 30, 2007, the Executive Board of the International Monetary Fund (IMF) concluded the 2007 Article IV consultation with Jamaica.[1]

Background

Jamaica's economy is estimated to have achieved its best growth performance in over a decade during FY 2006/07, which ended on March 31, 2007. Notwithstanding some recent moderation of momentum, the economy is estimated to have expanded by just under 3 percent in real terms, up from 2 percent the previous year and 0.4 percent the year before. While tourist arrivals have recently weakened, they were robust through December 2006 and agricultural activity has rebounded sharply after the weather-related shocks encountered during 2004–05.

Inflation has fallen significantly. Annual consumer price growth fell to 6½ percent at end-FY 2006/07, compared to a target of 9½ percent and a recent high of 19 percent in September 2005. The rebound in agriculture, which weighs heavily in the consumer price basket, has contributed to the decline in headline inflation.

[1] Under Article IV of the IMF's Articles of Agreement, the IMF holds bilateral discussions with members, usually every year. A staff team visits the country, collects economic and financial information, and discusses with officials the country's economic developments and policies. On return to headquarters, the staff prepares a report, which forms the basis for discussion by the Executive Board. At the conclusion of the discussion, the Managing Director, as Chairman of the Board, summarizes the views of Executive Directors, and this summary is transmitted to the country's authorities.

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On the external front, the current account deficit is estimated to have strengthened by 1 percent of GDP in FY 2006/07 to 10½ percent of GDP, largely on account of increased exports alongside robust tourism receipts and remittances. Capital inflows enabled a sharp build up in net international reserves (NIR) through 2006 and they currently remain broadly at historical highs.

However, fiscal targets for FY 2006/07 were missed by a wide margin notwithstanding the overall strong economic context. The fiscal slippage is primarily attributable to higher expenditures, although revenues also fell short of the ambitious target set out in the budget. A variety of mid-year expenditure increases were approved in a supplementary budget, mainly relating to agreed public sector wage increases and higher interest costs. As a result, budgetary expenditures for the 2006/07 fiscal year as a whole are estimated to have exceeded fiscal targets by 2½ percent of GDP. Little progress was made in reducing public debt—which stands at about 132 percent of GDP (excluding a recent bond to pre-finance FY 2007/08 obligations).

Monetary policy remains focused on containing inflation while also seeking to engender a sustainable reduction in interest rates. With inflation declining, the Bank of Jamaica eased monetary policy during FY 2006/07 by removing special deposit requirements on banks and reducing interest rates in three steps during May–December, to 12 percent on six-month instruments currently.

Financial sector soundness indicators for regulated entities remain robust despite a search for high yields. With (ex post) real rates of return on treasury bills declining sharply, financial institutions have sought out profitable lending opportunities and bank credit to the private sector has increased markedly. Nevertheless, prudential indicators for both banks and other regulated financial institutions remain sound. However, anecdotal evidence suggests that there has also been an apparent rise in unregulated investment schemes promising very high returns.

Executive Board Assessment

Executive Directors commended the authorities for recent policy successes and noted the strong economic growth in 2006/07, and the declining trend in the current account deficit. The authorities have also succeeded in sharply reducing inflation and bringing about a recovery in revenue collections after their decline in FY 2005/06.

Nevertheless, Directors expressed concern regarding the substantial breach of the deficit target in FY 2006/07, which related in part to one-off expenditures, and the limited progress in reducing the very high debt burden. They considered the medium-term macroeconomic program adopted in 2004 now in need of a fundamental reinvigoration. In this context, Directors saw the need for a broad political consensus to carry through the reforms necessary to secure sustained debt reduction.

Directors viewed fostering private sector led growth as critical to reducing the debt burden. Toward that end, they encouraged the authorities to reform the tax system, and to move ahead with reforms of the civil service aimed at improving efficiency. They also considered that steps to improve the business environment would raise the growth and employment impact of private sector investment.

Directors welcomed the planned improvement in the FY 2007/08 primary budget target as a promising start and an important signal of the authorities' continuing commitment to debt reduction. However, while welcoming progress at strengthening tax administration, Directors noted that it would be challenging to achieve the authorities' revenue objectives through such means alone. Most Directors recommended additional tax and expenditure actions to secure the budgetary objectives. To improve fiscal control and transparency, several Directors encouraged the authorities to continue the process of consolidating the operations of off-budget entities into a single unified framework.

Directors encouraged the authorities to continue to pursue public enterprise reform and strengthen the framework to formulate and assess the overall direction of fiscal policy. They recommended preparation of a fiscal Report on the Observance of Standards and Codes, Fund technical assistance to help improve public financial management, and to put in place a consolidated public sector accounting framework.

Directors pointed to the improving credibility of monetary policy in Jamaica and underscored the benefits of increased monetary and exchange rate flexibility. Given fiscal dominance in Jamaica, Directors considered exchange and interest rate flexibility crucial to allowing the Bank of Jamaica greater independence in pursuing inflation objectives.

Directors welcomed progress in financial sector reforms as an important element to guard against swings in market conditions and sentiments. Looking forward, they underscored the benefits of the authorities' efforts to improve the resilience of the debt profile to interest rate shocks. Directors also called for increased vigilance over speculative investment schemes, and recommended continued efforts to strengthen consolidated supervision, and prioritizing the development and testing of crisis management systems.

Public Information Notices (PINs) form part of the IMF's efforts to promote transparency of the IMF's views and analysis of economic developments and policies. With the consent of the country (or countries) concerned, PINs are issued after Executive Board discussions of Article IV consultations with member countries, of its surveillance of developments at the regional level, of post-program monitoring, and of ex post assessments of member countries with longer-term program engagements. PINs are also issued after Executive Board discussions of general policy matters, unless otherwise decided by the Executive Board in a particular case.

Jamaica: Selected Economic Indicators 1/

	2003/04	2004/05	2005/06	2006/07
	(Annual percentage changes)			
GDP, prices, and employment				
Real GDP	1.9	0.4	2.0	2.7 - 2.9
Nominal GDP	18.5	11.0	17.0	10.3
Consumer price index (end of period)	16.8	13.2	11.4	6.6
Consumer price index (average)	12.9	12.7	15.1	7.2
Exchange rate (end of period, in J$/US$)	8.6	0.9	6.2	3.5
End-of-period REER (percent change, appreciation +)	-0.8	5.2	4.1	…
	(In percent of GDP)			
Government operations 1/				
Budgetary revenue	29.4	31.2	29.0	29.8
Budgetary expenditure	36.8	36.7	32.7	35.5
Primary expenditure	18.4	19.4	18.0	21.8
Interest payments 2/	18.5	17.4	14.7	13.7
Gap	0.0	0.0	0.0	0.0
Budget balance	-7.4	-5.5	-3.7	-5.7
Of which: primary fiscal balance	11.0	11.9	11.0	8.0
Off-budget expenditure 3/	2.4	3.1	1.2	1.4
Overall fiscal balance	-9.9	-8.6	-4.8	-7.1
Public debt	143.7	139.6	133.0	134.7
External sector				
Current account balance	-6.8	-7.2	-11.4	-10.5
Of which: exports of goods, f.o.b.	17.7	17.5	17.8	19.5
Of which: imports of goods, f.o.b.	39.7	41.2	44.4	46.2
Net international reserves (in millions of US$)	1,569	1,902	2,078	2,329
	(Changes in percent of beginning of period broad money) 4/			
Money and credit				
Net foreign assets	9.0	7.5	1.8	3.3
Net domestic assets	11.3	2.7	6.8	9.5
Of which: credit to the central government	9.7	0.5	-8.5	1.8
Broad money	20.2	10.3	8.6	12.9
Velocity (ratio of GDP to broad money)	2.6	2.6	2.8	2.7
Memorandum items:				
Nominal GDP (in billions of Jamaican dollars)	495	550	643	709
Exchange rate (end of period, J$/US$)	60.8	61.5	65.3	67.6

Sources: Jamaican authorities; and IMF staff estimates and projections.

1/ Based partly on assumptions provided by the authorities. Fiscal years run from April 1 to March 31. Public debt is central government debt including debt assumed from public entities, plus guaranteed public entity debt, plus PetroCaribe debt. For FY 2006/07, the debt includes US$350 million bond issued for prefinancing. Cash-flow savings from the PetroCaribe agreement with Venezuela are managed by an extrabudgetary Fund that lends to both budgetary and off-budget entities.
2/ Includes capitalized interest payments on previous year's BoJ Special Issue bonds.
3/ Includes debt issued to BOJ to cover its cash losses, and debt related to off-budget projects financed initially by the private sector.
4/ Including valuation adjustments.

Statement by Jonathan Fried, Executive Director for Jamaica
and Murna Morgan, Senior Advisor to Executive Director
April 30, 2007

My authorities wish to express their appreciation to the staff for the frank, open and constructive discussions that have characterized the Article IV consultations in recent years. The staff's assessment of the overarching challenge facing Jamaica - fiscal and debt sustainability - coincides with that of the authorities. There is broad agreement not only on what is desirable but what is feasible, which reflects greater understanding by the staff of some of the constraints faced. My authorities place tremendous value on the Fund's role in monitoring and assessing Jamaica's home-grown medium-term macroeconomic policy framework and look forward to continued cordial dialogue, collaboration and support.

Recent Economic Developments

Economic performance in 2006/07 was somewhat mixed. Notwithstanding higher oil prices, Jamaica's inflation rate dropped sharply to 6.6 percent (compared with a projected 9 percent), significantly lower than the 11.4 percent recorded in 2005/06 and 13.2 percent for 2004/05. This outcome mainly reflected lower prices for agricultural products following recovery in the agriculture sector. Following an average growth of 1.3 percent for the period 2000-05, economic activity expanded by 2.5 percent in 2006, and though moderate, was the highest in 11 years. The catalysts for this expansion were a higher level of investment by the public sector in much needed infrastructure and activities related to the Cricket World Cup, as well as private investment mainly in the tourism sector; the recovery in agriculture which benefited from favorable weather conditions and implementation of measures to increase production and productivity; continued strong growth in the tourism industry; and a generally favorable external environment. In keeping with this increase in economic activity, unemployment declined in 2006. The foreign exchange market remained relatively stable, the external accounts improved marginally, and augmented by significant capital inflows, international reserves grew. Notwithstanding these positive developments, Jamaica's budgeted fiscal target was not met.

Fiscal Policy and Debt

Jamaica's 2006/07 central government operations realized a fiscal deficit of 5.7 percent, significantly higher than budgeted. Although revenue performance was better than in 2005/06, it underperformed relative to budget projections. Expenditure was above budget due to higher than programmed public sector wage increases, interest payments and increased capital expenditure on Cricket World Cup related activities and on-going road works. Jamaica's allocation for participation in the new World Bank sponsored Caribbean Catastrophic Risk Insurance Facility was not contemplated in the budget.

My authorities appreciate the staff's concern about the increase in the public sector wage bill and wish to assure the Board that due cognizance has been given to fiscal prudence. However, after a two-year wage freeze in the context of higher than projected inflation during the period, an acceptable compromise had to be reached with public sector workers, and this was signaled by the authorities. Jamaica has been losing skilled workers, in particular nurses and teachers, to recruitment by offshore employers. Faced with the reality of the international marketability of these professionals, my authorities were not prepared to risk domestic deterioration of basic services and the consequent social instability. As a consequence, the government opted to front-load the agreed two-year wage adjustment under the second memorandum of understanding (MOU II) between the government, public sector workers and the represented trade unions. This accommodation resulted in a much larger than programmed wage bill, a necessary trade-off to enable the government to retain qualified, skilled professionals to provide necessary public services at acceptable levels. As a result, in 2007/08 there will be a reduction in the rate of growth in wages.

The Jamaican authorities acknowledge that the large debt burden poses serious challenges to the country's long-term growth and development. Accordingly, the major thrust of the medium-term macroeconomic program has been fiscal consolidation and improved management of the debt dynamics. The generation of double digit primary surpluses has been an integral part of the fiscal consolidation effort for many years. Despite widespread doubts, Jamaica has generated and maintained high primary surpluses, averaging 10 percent over the past five years. This is a clear demonstration of the authorities' commitment to fiscal discipline and preparedness to tackle the debt problem. This has not been without costs. One of the policy challenges constantly faced, therefore, is finding the right balance between reasonable levels of capital expenditure, long advocated by the staff, and the generation of double digit primary surpluses.

Monetary and Exchange Rate Policies

The central bank – the Bank of Jamaica (BOJ) – and the staff are in full accord regarding the need for flexibility in the use of all monetary policy instruments and for increased independence, to facilitate the bank's pursuit of its inflation objective. The BOJ fully intends to maintain flexibility in the conduct of exchange rate policy. The BOJ's intervention in the foreign exchange market is limited to smoothing exchange rate fluctuations while providing sufficient liquidity to the market to meet demands. The BOJ does not target a particular exchange rate path, nor does it predetermine rates and makes no judgment as to what the rate should be. Accordingly, interventions take place using current market-determined exchange rates.

Regarding the issue of interest rates, the BOJ has demonstrated its willingness to increase as well as decrease interest rates when necessary. The central bank does not share the staff's view that the recent market volatility presents a case for a preemptive increase in interest rates. Variable rate debt accounts for 60 percent of the domestic debt and the staff has rightly noted that this presents increased risks and increased potential costs if there is an interest rate shock. With that in mind, rate increases by the central bank must be based on a need to correct genuine disequilibria in the market.

From the BOJ's perspective, the instability in the foreign exchange market in January 2007 arose from transitory demand pressures and portfolio switching in the context of limited domestic assets, and that it created no major disequilibrium in the financial market. Moreover, with continued lower inflation in the first three months of 2007 and increased investor confidence, the BOJ's assessment is that the situation does not justify a pre-emptive increase in rates.

The current monetary policy stance is consistent with achieving the programmed core inflation. The authorities' position has been vindicated by the results of the treasury bill auctions in March 2007, which saw further declines in these market-determined rates. In addition, in March 2007, Jamaica successfully tapped the international capital markets and pre-financed its 2007/08 external borrowing program with a new 32-year bond with a yield of 8.125 percent.

Notwithstanding these developments, the BOJ stands ready to increase the interest rates, if conditions in the market dictate.

Financial Sector

The staff noted that by all indicators, the health of the financial sector remains strong and that Jamaica has made progress in strengthening regulations. Mindful of its costly experience with the sector and its severe and long-term impact on the debt and fiscal performance, the Jamaican authorities, in consultation with stakeholders, will continue their efforts to ensure effective regulation of the financial sector. Work is ongoing to improve the legislative framework and strengthen the institutional structure of the sector.

In 2006, the BOJ advanced work to reform the payments system. Following extensive consultations with stakeholders, legislation is being drafted to provide for (a) the regulation and operation of a national payments system for which the BOJ will have regulatory oversight; and (b) the establishment of a central securities depository for fixed income securities to allow for the immobilization, electronic trading and settlement of these securities. The depository will be operated by the BOJ.

Structural Reforms

Successful implementation of structural reforms is necessary to achieve the medium-term macroeconomic objectives and for reinforcing the fiscal consolidation and debt reduction strategy. It is within this context that my authorities remain committed and have been advancing a comprehensive structural reform program, including reforms in the areas of financial sector, tax administration, public administration, labor market and the business environment. The authorities agree with the staff that the time is opportune to re-evaluate the overall strategy and welcome the staff's advice, and the recommended technical assistance.

Tax reform: In addition to ongoing reform measures to improve tax administration, the 2007/08 budget outlined the authorities' commitment to an additional tax reform effort. Jamaica plans to consolidate payroll deductions during the current fiscal year. In addition to the benefits of simplification and increased efficiency to be derived, consolidation will allow for resource allocation to areas of greatest need in the context of changing priorities. Given the developmental role of education, the sector will receive an increased share of consolidated collections.

Public Enterprises Reform: The Jamaican authorities agree that a number of public sector entities – Air Jamaica, the Jamaica Urban Transit Company and the Sugar Company of Jamaica – have been a drain on the public purse. The authorities have taken steps to restructure their operations in order to improve their financial performance in the short- to medium-term. Air Jamaica and the Jamaica Urban Transit Company are currently implementing business plans approved by Cabinet and are aimed at a gradual reduction in the existing levels of losses. In the case of the sugar company, the assets are in the process of being divested, and a change in ownership is anticipated during the current fiscal year.

Business Environment: In recent years, Jamaica has benefited from an unprecedented level of FDI. However, it appears that the text-book trickle down effect of these investments has not been fully realized. Jamaica is taking steps to assist small- and medium-size domestic enterprises to maximize the benefits of these investments and to expand their participation in the economy. A comprehensive program of financial and technical assistance will be implemented during this fiscal year. Resources from the highly concessional Petrocaribe funds will be made available through the development banks to the productive sector – manufacturing, tourism and related services, as well as agriculture/agri-business and agro-processing. This will be supported by the provision of technical assistance in business planning and product development.

With the support of development partners, Jamaica has made progress in creating an enabling environment for private sector-led growth. Despite this progress, my authorities recognize that work remains to further improve the business climate through increased efficiency and effectiveness of regulations. As a result, legislative and administrative steps will continue to be taken to streamline the work of the various agencies and government departments involved, including a delegation of appropriate authority from the Ministerial level to the authorities involved. With assistance from the USAID in collaboration with the local private sector, a Development and Investment Manual has been prepared to guide developers, professionals, the private sector, civil society and government officials.

Conclusion

Jamaica's medium-term growth prospects are positive but there are many challenges. These are daunting, but they are not insurmountable. My authorities have demonstrated their willingness and preparedness to make significant and sometimes painful decisions. They remain steadfast in their commitment to fiscal sustainability, particularly through improvements to the debt dynamics, to place Jamaica on a path to long-term sustained economic development. Hence, the 2007/08 budget and the medium-term programs are designed to return the fiscal balance and debt to a downward path. Jamaica places a high value on its hard-earned credibility, and the confidence of the local and international markets and investment community in general. Accordingly, the authorities will continue to pursue policies and programs aimed at enhancing macroeconomic stability, infrastructure development and improved global competitiveness, as a basis for expanding growth and raising the standard of living of Jamaicans.