



**Introduction**

The economic turnaround which started in 2000 following four years of declining aggregate output continued into 2001 with an estimated 2 percent growth being achieved. In fact, the economy was growing at a faster rate during the first half of 2001 before the occurrence of several shocks which created major setbacks. The main shocks were caused by social unrest in July, followed by the September 11 disaster in the USA and severe flood damage caused by Hurricane Michelle in November. These shocks slowed the economy and disrupted somewhat the performance of other macroeconomic variables. In particular, there was a marked deterioration in the fiscal balance, and the current account deficit of the balance of payments also widened as tourism was affected by the publicity impact of the events mentioned above, among other things. The fiscal deterioration calls for further fiscal expenditure restraint in order to maintain the overall macroeconomic stability that has so far been achieved.

In general, the Bank of Jamaica maintained its tight monetary policy stance in order to keep inflation under control and the exchange rate stable, but at the same time there was some easing as the minimum required cash reserve ratio in commercial banks continued to be reduced. Despite the widening of the external current account deficit, the build-up of international reserves continued due to significant capital inflows which included some Government borrowing abroad. The debt/GDP ratio declined slightly but debt service continues to impose a major burden on the economy.

**Output Performance**

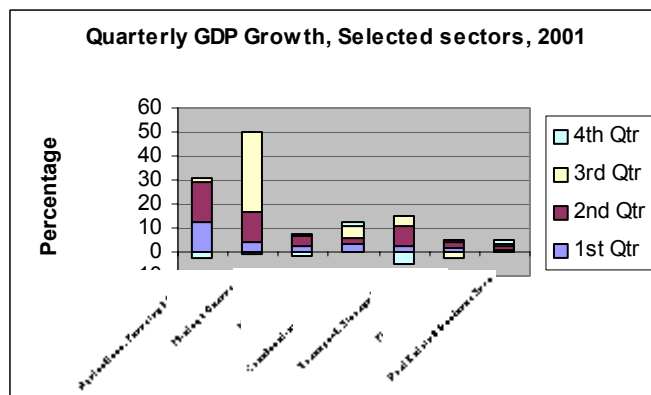
According to preliminary estimates, output grew by 2 percent in 2001. This represents an improvement in growth over the performance in 2000 when output increased by 1 percent. The output performance for 2001 was significantly set back by the major shocks that occurred in the second half of the year. GDP growth for the first three quarters of the year, measured on an annualized basis, amounted to 2.6

percent, 4.7 percent and 3.9 percent, respectively, while the economy contracted by 1.3 percent in the fourth quarter.

The main sectors responsible for the 2001 growth were agriculture, forestry and fishing, and mining and quarrying, with construction also making an important contribution (Figure 1). Under the influence of good weather conditions, agriculture grew by 12.3 percent and 17.2 percent, in the first and second quarters, respectively. Mining and quarrying production grew by 12.0 percent and 34.0 percent in the second and third quarters, respectively, still on the rebound following the return to operation of the Gramercy plant in the USA, which had been out of operation since 1999. Manufacturing, which had been on the decline during the 1990s, also showed significant growth in the early part of 2001, expanding by 4.0 percent in the second quarter. All three of these sectors, however, contracted during the last quarter of the year.

On the whole, the service sectors did less well than the goods producing sectors with transport, storage and communication being the leading service sector in terms of growth in the early part of the year. However, this sector contracted in the last quarter, ending up with 2.4 percent growth in the year as a whole. Growth was more modest in real estate and business services, financial services and government services while electricity and water recorded a small decline.

**Figure 1**



Tourism, the leading service sector in the country, was severely affected by the shocks which occurred in Jamaica in 2001. In the period January – April 2001, stopover arrivals grew by 4.9 percent and growth continued to be positive until June (Table 1). However, in July, coinciding with the social unrest in Kingston that month, stopover arrivals declined by 4.8 percent and the changes continued to be negative for the rest of the year. Consequently, arrivals dropped by 8.0 percent in the May-December period and by 3.5 percent during January-December. The drop in tourist arrivals peaked in September and October when it measured 20.0 and 20.7 percent respectively. However, the decline in tourist business for the year as a whole has been less severe than was predicted following the September 11 events in the USA.

**Table 1**  
**Tourist Arrivals**  
**January - December**  
**2001**

Months	Total Stopover Arrivals	Percentage Change
Jan-Apr.	484,164	4.9 %
September	63,508	-20.0 %
October	69,799	-20.70%
November	82,782	-14.9 %
May-Dec.	792,352	-8.0 %
Jan-Dec.	1,276,516	-3.5 %
December	106,575	-8.8 %

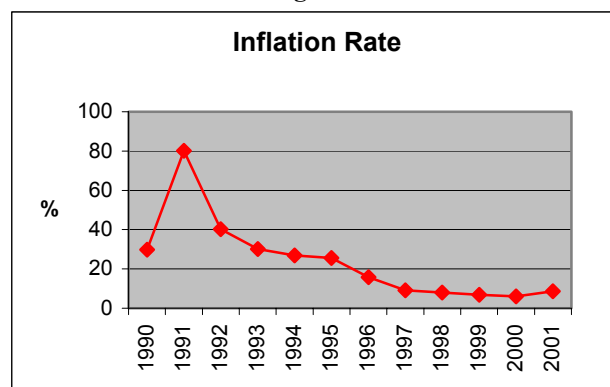
Cruise ship arrivals also showed deterioration in 2001, declining by 7.4 percent in 2001 relative to 2000. This outcome was attributable not only to the shocks mentioned above, but also to a reduction in the number of cruise ship calls in Jamaica.

### Money & Banking

The Bank of Jamaica continued to pursue a tight monetary policy with base money declining marginally during the year ending January 2002 and money supply (M2) rising by 8.7 percent during the year ending November 2001. Meanwhile, the inflation rate also measured an estimated 8.7 percent in 2001. Commercial bank loans, which had gone through a period of decline during the late 1990s when the economy was contracting, grew by 17.7 percent in the year ending November 2001. The

leading sectors borrowing were transport, storage and communication where loans rose by 192.4 percent, and government services which increased its commercial bank borrowing by 53.9 percent. Meanwhile, commercial bank loans to agriculture and mining declined by 21.4 percent and 15.0 percent, respectively. Near-banks (merchant banks, trust companies and finance houses) also recorded increases in loans, amounting to 13.4 percent in 2001.

**Figure 2**



The Bank of Jamaica also continued the process of lowering the minimum liquid assets requirement for banks from 31 percent in November 2000 to 27 percent at the beginning of 2002, with a view to bringing about a narrowing of interest rate spreads between loan rates and deposit rates. However, the banking system continued to hold significant excess reserves. Loan rates showed some reduction over the past year but they are still at relatively high levels in nominal and real terms. The average loan rate declined from 31.7 percent to 26.6 percent and the *weighted* average loan rate declined from 22.2 percent to 19.5 percent.

A major objective of the GOJ is to achieve low interest rates in order to stimulate investment and growth and reduce the fiscal burden of debt service. In general, interest rates have declined at a slower rate than originally forecast. The six-month average weighted yield on GOJ treasury bills declined from 19.4 percent in January 2001 to 17.1 percent in January 2002, still significantly higher than the 14 percent forecast for March 2001 (Table 2). The downward stickiness of the interest rate is partly due to Bank of Jamaica intervention in the foreign exchange market to support the Jamaican Dollar.

**Table 2**  
**Selected Interest Rates**

Accounts	Jan-01	Jan-02
Savings Deposits (Average Rate)	<b>9.86</b>	<b>9.08</b>
Loan Rate (Average Rate)	<b>31.67</b>	<b>26.63</b>
G.O.J Treasury Bills (Weighted Avg.) Yield (6 months)	19.41	17.08
BOJ Reverse Repurchase Rates (percent) *	<b>16.45</b>	<b>14.25</b>
	<b>Nov-00</b>	<b>Nov-01</b>
Weighted Fixed Deposits Rate	12.23	10.26
Weighted Loan Rate	22.17	19.53

\* Apply to 30 days

### Fiscal Operations

The fiscal balance showed some slippage in 2000/01, following the significant improvements achieved in the previous year. By December 2001, it was evident that there would be some fiscal deterioration caused by the shocks that occurred during the year. For example, the social unrest that occurred in July had caused an unanticipated increase in Government expenditure for heightened security and tourism promotion to counteract the adverse publicity. In recognition of this fiscal slippage, the IMF and the GOJ agreed to revise the fiscal deficit target under the SMP from 2.8 percent to 4.1 percent of GDP.

Provisional estimates of fiscal performance for April to December 2001 show the deficit to be 12.7 percent above the revised target. Revenue and grants measured J\$73.8 billion, amounting to 1.9 percent below the SMP target, while total expenditure measured 1.1 percent above the SMP target. This also represented a tripling of the deficit relative to that of the corresponding period of the previous year. On the revenue side, there were significant reductions in taxes on income and profits of bauxite/alumina and other companies, and taxes on interest. The General Consumption Tax and stamp duty on traded goods also saw significant declines. In terms of expenditure, programmes were down by 3.3 percent relative to forecasts and wages and salaries were also down slightly but interest payments were above forecast by 4.5 percent, reflecting the failure to achieve forecast reductions in interest rates, as indicated earlier. In light of these provisional indicators, it will be necessary to introduce further

fiscal contraction in the final quarter of FY 2001/02 if the SMP deficit target is to be achieved. Up to February 2002, a 1.3 percent revenue shortfall, relative to the SMP target, was being projected for FY 2001/02 as a whole. Consequently, the GOJ faces the task of achieving a substantial expenditure contraction in the final quarter of the financial year.

### External Performance

The current account of the Jamaica balance of payments showed a sharp deterioration in 2001, the deficit widening by US\$361.4 million or 125 percent over the 2000 value (see Table 3). However, this deterioration was amply covered by an increase in net capital inflows, resulting in a large build up in reserves.

**Table 3**  
**The Balance of Payments**

Accounts	2000	2001*	percent Change
<b>Current Account</b>	<b>-288.6</b>	<b>-650.0</b>	<b>-125.2</b>
<b>Goods balance</b>	<b>-1353.5</b>	<b>-1580.0</b>	<b>-16.7</b>
Exports (f.o.b)	1554.6	1451.6	-6.6
Imports (f.o.b)	2908.1	3031.6	4.2
<b>Service Balance</b>	<b>594.0</b>	<b>546.4</b>	<b>-8.0</b>
Travel	1123.9	1073.2	-4.5
<b>Income</b>	<b>-349.9</b>	<b>-488.7</b>	<b>-39.7</b>
<b>Current Transfers</b>	<b>820.8</b>	<b>872.3</b>	<b>6.3</b>
Official	147.9	62.9	-57.5
Private	672.9	809.4	20.3
<b>Financial Account</b>	<b>286.4</b>	<b>662.4</b>	<b>131.3</b>
Other Official Investment	383.7	653.4	70.3
Other Private Investment (incl. Errors & omissions)	422.0	880.3	108.6

\* Provisional

The major traditional exports increased in earnings, mainly as a result of the doubling of bauxite exports as the Gramercy refining plant in the USA returned to full operation. Alumina exports also increased but sugar and banana export earnings declined significantly. Non-traditional exports declined, leading to an overall reduction in goods exports of 7 percent. While goods exports declined, total merchandise imports increased by 4 percent, contributing further to the widening deficit. There was growth in all the end-use categories of imports,

especially raw material and capital goods imports. The increases in raw material and capital goods imports are consistent with an upturn in economic activity in the major productive sectors.

The service balance declined by 8 percent as both travel and transportation earnings contracted. The balance of income flows also declined by 40 percent as the net outflow of investment income increased substantially. International transfers continued to contribute positively to the performance of the balance of payments. The balance of international transfers increased by 6 percent with net private transfers growing by 20 percent and making up for a significant reduction in net official international transfers. On the capital account, net capital inflows exceeded a billion and a half US Dollars, leading to a build up of net international reserves of US\$871 million in 2001. Contributing to capital inflows in 2001 were GOJ external bond issues totaling US\$825 million and net private investment (including errors and omissions) amounted to US\$880 million. As a consequence of these changes, net international reserves almost doubled in 2001 reaching US\$1.8 billion by January 2002. The estimated gross reserves were equivalent to 34 weeks of goods import coverage.

### Debt

The national public debt of Jamaica is projected to decline to 130 percent of GDP by the end of FY 2001/02, down from 140 percent a year earlier. The changes in debt indicators are consistent with the strategy being pursued by the GOJ of replacing high priced domestic debt with less expensive external debt. High debt and debt service continue to place a significant burden on the Jamaican economy. Debt service as a ratio of exports of goods and services is estimated to be a manageable 14 percent, but interest

payments over the 2001/02 financial year estimated to be 49 percent of total Central Government revenue and grants. The high interest payments severely limit the resources available for social and other government spending and accounts for the high primary surplus of around 10 percent of GDP.

### Outlook

Jamaica has prospects for a strengthening of the growth process if current trends persist. Some important factors that may contribute to further growth include the return of tourist arrivals to pre-September 11 levels, continued increases in manufacturing output and rising output in the volatile agriculture industry. The completion of the rehabilitation process in the financial sector following the crisis of the 1990s will contribute significantly to the economy, not only in terms of value added but also by helping to foster increased confidence and a more favorable investment climate. Another important consideration will be the performance of the international economy which is showing more upbeat signs at the present time compared to last year. This will help to boost major export prices and improve the prospects for higher tourist arrivals.

Further lowering of interest rates in Jamaica could also contribute substantially to greater macroeconomic stability and economic growth. In the wake of the shocks to the economy in 2001, fiscal pressures have increased and a period of further fiscal restraint in FY 2002/03 is inevitable if macroeconomic stability is to be maintained and growth promoted.

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