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EBS/88/188

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August 30, 1988

To: Members of the Executive Board  
From: The Secretary  
Subject: Jamaica - Request for Stand-By Arrangement

Attached for consideration by the Executive Directors is a paper on Jamaica's request for a stand-by arrangement equivalent to SDR 82 million, which will be brought to the agenda for discussion on a date to be announced. Draft decisions appear on page 27.

Mr. Elson (ext. 8477) or Mr. Decarli (ext. 7161) is available to answer technical or factual questions relating to this paper prior to the Board discussion.

Att: (1)



INTERNATIONAL MONETARY FUND

JAMAICA

Request for Stand-By Arrangement

Prepared by the Western Hemisphere Department

(In consultation with Exchange and Trade Relations,  
Fiscal Affairs, Legal, and Treasurer's Departments)

Approved by M. Caiola and S. Kanasa-Thanan

August 30, 1988

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## I. Introduction

Discussions on an economic program for fiscal year 1988/89 <sup>1/</sup> that could be supported by the use of Fund resources were held by Fund staff with the Jamaican authorities on several occasions in Kingston and at Fund headquarters during the period February-July 1988. The staff team in the discussions consisted of Mr. Elson (Head), Mr. Decarli, Mrs. Schmitz, Mr. Terrier (all WHD), Mr. De Zoysa (FAD), Mr. Weerasinghe (ETR), Miss Coles and Mrs. Tollaksen (Secretaries, WHD). The team was assisted by Mr. Hill, the Fund resident representative in Jamaica. The representatives of Jamaica included the Prime Minister, who is also Minister of Finance, the Governor and Deputy Governors of the Bank of Jamaica, the Accountant General, the Minister of Mining, Energy, and Tourism, and other officials.

In the attached letter, dated August 22, 1988, the Jamaican authorities request a stand-by arrangement for the period through November 1989 (approximately 14 months) in an amount equivalent to SDR 82 million (about 48 percent of quota on an annual basis). The letter specifies Jamaica's economic program for the current fiscal year; policies for the next fiscal year will be specified in a review of the arrangement to be completed by end-April 1989, which conditions purchases after that date. The proposed arrangement would be financed in the ratio of one to two from ordinary and borrowed resources.

It is proposed that the amount of the stand-by arrangement be made available in six purchases as presented in Table 1 and Attachment IV. Repurchases due over the period mid-September 1988-November 1989 are equivalent to SDR 176 million, or SDR 94 million more than purchases under the proposed stand-by arrangement. Thus, purchases of the full amount under the arrangement would result in a reduction of Fund credit to Jamaica from 270 percent of quota at end-August 1988 (of which 53 percent of quota under special facilities) to 206 percent of quota at end-November 1989 (28 percent of quota under special facilities).

Jamaica has had almost continuous arrangements with the Fund since 1977. Under the last stand-by arrangement, covering the period March 1987-May 1988, all purchases for SDR 85 million were made as scheduled. <sup>2/</sup>

## II. Background

In the early 1980s Jamaica received large-scale external financing in connection with an economic program supported by an extended arrangement from the Fund. The program ran into difficulties because of the

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<sup>1/</sup> Jamaica's fiscal years run from April to March.

<sup>2/</sup> Information on Jamaica's relations with the Fund is presented in Attachment I.

Table 1. Jamaica: Projection of IMF Position during Period of Stand-By Arrangement

	1988						1989			
	Outstanding Aug. 31, 1988	Board Approval Sept.	Oct.-Dec.	Jan.-Mar.	Apr.-June	July-Sept..	Oct.-Nov.			
(In millions of SDRs)										
<u>Transactions under tranche policies (net)</u>	<u>7.7</u>	<u>-9.8</u>	<u>-24.0</u>	<u>-10.3</u>	<u>-21.4</u>	<u>0.5</u>				
Purchases	13.7	13.7	13.7	13.7	13.7	13.5				
Ordinary resources	4.6	4.6	4.6	4.6	4.6	4.4				
Borrowed resources	9.1	9.1	9.1	9.1	9.1	9.1				
Repurchases	-6.0	-23.5	-37.7	-24.0	-35.1	-13.0				
Ordinary resources	-3.9	-14.1	-15.1	-14.6	-13.8	-8.3				
Borrowed resources	-2.1	-9.4	-22.6	-9.4	-21.3	-4.7				
<u>Transactions under special facilities (net) 1/</u>	<u>-9.1</u>	<u>-9.1</u>	<u>-9.1</u>	<u>-9.1</u>	<u>--</u>	<u>--</u>				
Purchases	--	--	--	--	--	--				
Repurchases	-9.1	-9.1	-9.1	-9.1	--	--				
<u>Total Fund credit outstanding (end of period)</u>	<u>393.2</u>	<u>391.8</u>	<u>372.9</u>	<u>339.8</u>	<u>320.4</u>	<u>299.0</u>	<u>299.5</u>			
Under tranche policies 2/	316.0	323.7	313.9	289.9	279.6	258.2	258.7			
Special facilities 1/	77.2	68.1	59.0	49.9	40.8	40.8	40.8			
(In percent of quota)										
<u>Total Fund credit outstanding (end of period)</u>	<u>270.2</u>	<u>269.3</u>	<u>256.3</u>	<u>233.5</u>	<u>220.2</u>	<u>205.5</u>	<u>205.8</u>			
Under tranche policies 2/	217.2	222.5	215.7	199.2	192.2	177.5	177.8			
Special facilities 1/	53.0	46.8	40.6	34.3	28.0	28.0	28.0			

Source: IMF.

1/ Compensatory Financing Facility.

2/ Ordinary and borrowed resources.

collapse of Jamaica's bauxite industry, but also because of the financial policies pursued and a growing overvaluation of the Jamaica dollar. In the 1983-85 period, economic programs supported by stand-by arrangements from the Fund continued to be negatively affected by a persistent decline in bauxite exports; nonetheless, progress was made in reducing fiscal imbalances and competitiveness was restored by allowing the Jamaica dollar to depreciate under a foreign exchange auction system.

In 1986/87 the price of petroleum fell and international interest rates moderated, tourism performed strongly, and the demand for Jamaica's bauxite and alumina improved. As a consequence of these external developments and improved domestic policies, Jamaica's financial imbalances were substantially reduced. Real GDP rose by close to 4 percent after a decline of a similar magnitude the previous year, while the average annual rate of inflation moderated to 11 1/2 percent from 24 percent. The overall public sector deficit was reduced to 5 1/2 percent of GDP (from 13 percent in 1985/86) and the external current account deficit declined to 3 percent of GDP from 11 percent (Table 2).

Throughout the mid-1980s, Jamaica's stabilization efforts have been reinforced by structural reforms generally aimed at improving the conditions for export-led growth, which have been supported by policy and project loans from the World Bank. The restoration of external competitiveness has been complemented by a significant liberalization of the import licensing system. With the overhauling of the individual income tax and the corporate tax in 1986, the tax system was made more equitable and efficient. A program for the simplification of import duties is being implemented and the Government intends to replace a number of indirect taxes by a general consumption tax. In the financial area, reform has focused on increasing the reliance on market-oriented instruments and policies to control credit aggregates.

### III. Performance Under the 1987/88 Program

The 1987/88 stand-by program (which was supported by a stand-by arrangement for SDR 85 million approved in March 1987) aimed at a further improvement in Jamaica's economic performance, including a consolidation of the external position in the context of a stable exchange rate regime. The overall public sector deficit was to be further reduced, and the growth of credit and monetary aggregates was to be slowed significantly.

Performance under the stand-by arrangement was generally satisfactory, with all performance criteria being met and all purchases taking place as scheduled <sup>1/</sup> (Table 3). Output growth is estimated to

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<sup>1/</sup> During the program period, a number of modifications were introduced to adapt performance criteria to unforeseen developments (EBS/87/152, 7/8/87, pp. 20-22; and EBS/87/217, 10/15/87, pp. 16-17).

Table 2. Jamaica: Selected Economic Indicators

	1983/84	1984/85	1985/86	1986/87	1987/88		1988/89
					Prog. 1/	Prel.	Program
(Percentage annual change)							
Real GDP	1.7	-1.4	-3.7	3.9	1.1	5.5	4.7
Nominal GDP	23.3	30.1	26.8	15.7	9.1	12.7	12.2
GDP deflator	21.3	31.9	31.7	11.4	7.9	6.8	7.2
Consumer price index							
Annual average	14.7	29.7	24.2	11.4	9.6	6.9	7.0
End of period	21.1	29.7	19.8	7.7	7.0	7.8	7.0
Domestic interest rate (in percent) 2/	13.9	17.7	20.0	14.4	...	15.5	...
Broad money	25.0	20.0	24.3	23.6	10.3	21.1	17.0
(In percent of GDP)							
Overall public sector balance 3/	-19.6	-15.1	-13.2	-5.6	-4.5	-5.4	-2.8
Of which:							
Central government deficit	-15.8	-6.3	-5.3	-1.4	-2.2	--	0.4
Rest of public sector	-1.9	-3.0	-1.0	1.5	2.4	--	1.3
Bank of Jamaica losses	-1.9	-5.8	-6.9	-5.7	-4.7	-5.4	-4.5
External current account balance	-9.1	-10.9	-11.2	-2.8	-3.8	-4.5	-3.1
Memorandum items							
Nominal GDP (in millions of Jamaica dollars)	7,577	9,856	12,496	14,459	15,750	16,307	18,292
Real effective exchange rate index (1980=100) 4/	75.1	63.9	68.1	68.2	73.9	67.5	...
Average annual exchange rate J\$ per US\$	2.47	4.36	5.65	5.50	5.50	5.50	5.50

Sources: Bank of Jamaica; and Fund staff estimates.

1/ As presented in EBS/87/152 (7/8/87).

2/ Weighted average deposit rate of the commercial banks.

3/ Measured as the use of foreign and domestic financing by the public sector, which includes the losses of the Bank of Jamaica.

4/ End of period.



Table 3. Jamaica: Compliance with Quantitative Performance Criteria

	1987												1988		
	March			June			September			December			March		
	Prog.	Actual	Margin	Prog.	Actual	Margin	Prog.	Actual	Margin	Prog.	Actual	Margin	Prog.	Actual	Margin
(In millions of U.S. dollars)															
Net international reserves <u>1/</u>	-576	-560	16	-463	-445	18	-473	-453	20	-466	-446	20	-396	-382	14
Net external debt disbursements <u>2/</u>	38	-59 <u>3/</u>	97	76	-14 <u>3/</u>	90	78	-22 <u>3/</u>	100	93	-70	163	115	-11 <u>4/</u>	126
Gross disbursements of external public debt of 1-5 years maturity <u>5/</u>	133	113	20	171	146	25	208	149	59	251	152	99	293	239	54
Increase in the stock of short-term external public debt <u>6/</u>	25	19	6	45	30	15	45	16	29	45	14	31	45	36	9
Stock of external payments arrears	25	1	24	--	--	--	--	--	--	--	--	--	--	--	--
(End of period, in millions of Jamaica dollars)															
Net domestic assets of the Bank of Jamaica <u>7/</u>	4,044	4,009	35	3,435	3,395	40	3,558	3,458	100	3,606	3,566	40	3,160	3,130	30
Overall public sector financing requirement <u>8/</u>	746 (940)	644 <u>3/</u>	102	738 (997)	451 <u>3/</u>	287	976 <u>3/</u>	697 <u>3/</u>	279	1,019 (1,310)	906	113	1,256 <u>9/</u>	1,252 (1,464)	4
Central Government financing requirement <u>8/</u>	2,113 (1,210)	1,095	18	1,282 (1,416)	1,128	154	1,570 <u>3/</u>	1,272 <u>3/</u>	298	1,756 (1,889)	1,640	116	1,809 (2,072)	1,638	181

Sources: Technical Memorandum of Understanding; Jamaican authorities.

- 1/ Targets adjustable upward for any cumulative excess of net external debt disbursements over programmed amounts.
- 2/ Peters to medium- and long-term debt contracted by the public sector or the private sector with government guarantee (excluding project loans by multilateral and other official development agencies). Figures refer to cumulative change from March 31, 1986. Any excess in net disbursements over programmed amounts (which are US\$20 million below these limits) is to be added to net international reserves.
- 3/ Revised.
- 4/ Adjusted to exclude impact of debt equity conversion.
- 5/ Figures refer to cumulative change from March 31, 1986.
- 6/ In relation to the end-of-year 1986 level.
- 7/ Ceilings adjustable downward for any excess of net external debt disbursements over programmed amounts.
- 8/ Cumulative change from March 31, 1986. Adjustable upward (downward) for any excesses (shortfalls) over programmed disbursements of project-related foreign inflows; there was a maximum for the upward adjustment of the ceiling on the overall public sector financing requirement which was equal to the Jamaica dollar equivalent of US\$10 million. In parentheses are the respective ceilings before adjustment for shortfalls over programmed disbursements of project-related foreign inflows. The ceiling on the overall public sector financing requirement was also adjustable upward in the event of the purchase of the Clarendon alumina refinery plant. The allowable adjustment was equal to the cost of acquisition up to a maximum of US\$50 million.
- 9/ The ceiling was adjusted for the cost of the government's purchase of shares in JAMALCO which owns the Clarendon alumina refinery plant (J\$145 million).

have accelerated to 5.5 percent in 1987/88 from about 4 percent in 1986/87, with a strong expansion in bauxite/alumina exports (which were boosted by sustained increases in aluminum prices in international markets), nontraditional exports, tourism and construction. By year-end, the open unemployment rate declined to about 21 percent and the job-seeking rate to about 9 percent, the lowest levels registered in many years. The average rate of inflation fell to less than 7 percent. The 12-month rate of inflation rose to 8.4 percent by end-1987 because of scarcities of food products caused by floods, but moderated to 7.8 percent by March 1988.

The deficit of the overall public sector (including the losses of the Bank of Jamaica) declined only marginally from the previous year, to 5.4 percent of GDP, compared with 4.5 percent of GDP in the original program (which, however, did not include the cost of the purchase of shares in JAMALCO, for the equivalent of 0.9 percent of GDP). <sup>1/</sup> The origin of the deficit was substantially different from that initially envisaged, with the Central Government showing a small overall surplus instead of the programmed deficit and the losses of the Bank of Jamaica being substantially larger than programmed (Table 4). <sup>2/</sup>

Central government revenue rose by some 22 percent mainly because of large proceeds from the divestment of public enterprises to the private sector and buoyant collections from income taxes and customs duties, as well as sizable loan recoveries and transfers from public sector entities. Tax revenue rose by 15 percent, reflecting the rapid pace of economic activity and imports, the effect of income tax reforms enacted in 1986/87, and cutbacks in import duty exemptions introduced

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<sup>1/</sup> This transaction had not been contemplated in the original projections, but allowance was made in the first review of the program for a modification of the ceiling on the public sector financing requirement up to a maximum of J\$275 million (see EBS/87/152, 7/8/87, pp. 14-15). In the event, in March 1988 the Government purchased J\$145 million additional shares in JAMALCO, an alumina-refining venture with ALCOA, increasing its participation in the company from 6 percent to 50 percent. (The Government had operated JAMALCO's Clarendon plant since 1985, under a lease arrangement that expired in February 1988.) The purchase was paid with inventories the Government had accumulated in the company (J\$51 million) and the Government's obligation to make investments of J\$94 million in JAMALCO during the subsequent two years.

<sup>2/</sup> In 1987/88 there was an unexplained negative residual of some 0.8 percent of GDP in the public sector accounts which represented the balance of operations of the nonconsolidated public sector as well as errors and omissions in the computation of fiscal transactions. Improvements have been made in the measurement of central government transactions and the losses of the Bank of Jamaica in recent months. Regarding the rest of the public sector, ongoing work to improve the accounts is expected to be completed by December 1988.

Table 4. Jamaica: Public Sector Balances and Financing

	1983/84	1984/85	1985/86	1986/87	1987/88		1988/89
					Prog. 1/	Prel.	Program
(In millions of Jamaica dollars)							
Central Government 2/	-1,196.3	-624.3	-659.6	-203.5	-345.1	2.7	79.6
Rest of general government	72.0	167.6	190.3	154.5	320.0	156.4	153.1
Selected public entities	-93.4	-133.6	-138.7	243.8	233.0	286.0	136.1
Bank of Jamaica losses	-142.1	-576.0	-857.9	-822.0	-733.0	-875.4	-823.3
Other public sector							
on-lending 3/	-40.3	-51.9	-75.7	-172.3	-179.9	-186.6 4/	-45.4
Purchase of shares in JAMALCO	--	--	--	--	--	-145.0	61.6 5/
Others and discrepancy	-85.0	-267.0	-111.9	-10.3	--	-121.5	-73.7
<u>Overall public sector balance</u>	<u>-1,485.1</u>	<u>-1,485.2</u>	<u>-1,653.5</u>	<u>-809.8</u>	<u>-705.0</u>	<u>-883.4</u>	<u>-512.0</u>
Foreign financing 6/	1,078.1	886.1	800.6	-415.6	182.2	-99.2	16.5
Domestic financing 7/	407.0	599.1	852.9	1,225.4	522.8	982.6	495.5 5/
(In percent of GDP)							
Central Government 1/	-15.8	-6.3	-5.3	-1.4	-2.2	--	0.4
Rest of general government	1.0	1.7	1.5	1.1	2.0	1.0	0.8
Selected public entities	-1.2	-1.3	-1.1	1.7	1.5	1.8	0.8
Bank of Jamaica losses	-1.9	-5.8	-6.9	-5.7	-4.7	-5.4	-4.5
Other on-lending 2/	-0.5	-0.5	-0.6	-1.2	-1.1	-1.1	-0.2
Purchase of shares in JAMALCO	--	--	--	--	--	-0.9	0.3
Others and discrepancy	-1.2	-2.9	-0.9	-0.1	--	-0.8	-0.4
<u>Overall public sector balance</u>	<u>-19.6</u>	<u>-15.1</u>	<u>-13.2</u>	<u>-5.6</u>	<u>-4.5</u>	<u>-5.4</u>	<u>-2.8</u>
Foreign financing 6/	14.2	9.0	6.4	-2.9	1.2	-0.6	0.1
Domestic financing 7/	5.4	6.1	6.8	8.5	3.3	6.0	2.7
Memorandum items							
GDP (in millions of Jamaica dollars)	7,576.5	9,856.3	12,496.1	14,456.9	15,750.0	16,307.1	18,292.1
Overall public sector financing requirement 8/ (in millions of Jamaica dollars)	1,485.1	1,485.2	1,653.5	922.7	...	1,385.0	925.5
(In percent of GDP)	19.6	15.1	13.2	6.4	...	8.5	5.1

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

1/ As presented in EBS/87/152 (7/8/87).

2/ Includes accrued bauxite levy receipts earmarked to repay a 1982 advance (tolling arrangement) and on-lending to the private sector (pass-throughs).

3/ In 1983/84-1985/86 not all on-lending by the rest of the public sector is included, but only its two main components, which were financed by (a) World Bank disbursements to the Export Development Fund, and (b) IDB disbursements to the Rehabilitation Fund.

4/ Includes on-lending of US\$12.6 million to the cement company. The majority of the shares of this company were sold to private investors by end-June 1987.

5/ In 1988/89 the Government is committed to undertake investment expenditure of about J\$62 million on behalf of ALCOA to pay for shares the Government acquired in JAMALCO in 1987/88. The investment obligation is treated as a repayment of domestic debt.

6/ Includes changes in net foreign assets and in medium- and long-term foreign liabilities of the Bank of Jamaica.

7/ Includes changes in the net domestic assets of the Bank of Jamaica, except for those which are the counterpart of changes in its net foreign assets or in its medium- and long-term foreign liabilities.

8/ Definition used in technical memorandum of understanding for the proposed arrangement. This definition includes as financing the proceeds of divestment and does not include amortization linked to the tolling arrangement.

last year. Divestment proceeds amounted to J\$328 million (2 percent of GDP), most of which resulted from the sale of shares in the national telecommunications enterprise to a foreign company. Central government expenditure rose by about 15 percent mainly reflecting a 26 percent increase in capital outlays to J\$1,163 million (about 7 percent of GDP). Capital expenditure was some J\$300 million larger than projected, but the original program was based on a much lower estimate of proceeds from divestments (J\$50 million).

The overall surplus of the rest of the General Government remained at about the same level as in 1986/87, instead of increasing substantially as programmed, because the surplus of the National Insurance Fund was much less than anticipated as benefits were doubled at the start of the fiscal year.

The overall surplus of the public enterprises increased in 1987/88 mainly as a result of further improvement in the financial positions of the electricity company and the telecommunications company, and lower losses of the National Investment Bank of Jamaica. Divestment proceeds retained by public enterprises (from the sale of the Caribbean Cement Company and one hotel) amounted to about J\$133 million, approximately in line with program projections. Their capital expenditure (other than that financed by transfers from the Central Government) rose by about 20 percent from the previous year's level.

The losses of the Bank of Jamaica, which reflect mainly the difference between the interest paid on domestic and foreign liabilities and the income from its asset portfolio, accounted for most of the overall public sector deficit. These losses rose by some J\$50 million in 1987/88 to J\$875 million as an increase in the interest paid to local banks and public sector entities on certificates of deposit and other liabilities issued to absorb liquidity was only partially offset by a decline in net interest paid abroad.

In line with the improved economic prospects, private sector credit demand was buoyant throughout 1987/88, and the growth in banking system credit to the private sector accelerated to an annual rate of 34.5 percent in 1987/88, compared with 21 percent in 1986/87 (Table 5). In the face of strong credit demands, the Bank of Jamaica refrained from acting to reduce interest rates even though the rate of inflation had been on a declining trend. The Bank maintained its policy of offering its certificates of deposit at a pre-set rate (of 18 percent) <sup>1/</sup> in unlimited amounts at frequent auctions and kept the floor on interest rates of savings deposits unchanged at 15 percent (this floor had last been reduced, by 1 percentage point, in August 1986). The weighted deposit rate of commercial banks rose from 14.5 percent at end-March

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<sup>1/</sup> Except for a few instances, particularly in December 1987 when the rate was set at 20 percent. Meanwhile, treasury bills continued to be offered at auctions where the amount was pre-set, with average yields rising gradually over the program period.

Table 5. Jamaica: Monetary Accounts

	Level March 31 1988 1/	Changes During Period							1988/89 Prog.
		1983/84	1984/85	1985/86	1986/87	1987/88			
						Program 1/	Prel.		
(In millions of Jamaica dollars)									
I. Banking System									
Net international reserves	-2,843	-459	977	196	295	990	819	989	
Net domestic assets	10,680	1,133	-302	786	892	-380	492	291	
Net credit to Central Government	3,094	794	-656	191	299	-953	-1,243	-1,500	
Net credit to rest of public sector	-1,602	317	-163	-502	-619	-348	-232	-1,500	
Net Bank of Jamaica losses	1,697	142	576	858	822	733	875	823	
Net credit to other financial institutions	-932	-54	-102	-170	-313	-110	-159	-11	
Credit to private sector	4,238	480	124	313	545	295	1,098	985	
Medium- and long-term foreign liabilities	-3,024	-254	-332	-158	25	3	22	232	
Net unclassified	7,208 2/	-292	251	254	133	--	141	-238	
SIR allocation	310	--	--	--	--	--	--	--	
Liabilities to private sector	7,527	674	675	982	1,187	610	1,311	1,279	
Money	1,757	92	184	222	310	154	266	299	
Quasi-money	4,836	455	389	715	712	394	873	822	
Other	933	127	102	45	165	62	172	159	
II. Bank of Jamaica									
Net international reserves 3/	-2,556 4/	-556	1,063	346	305	990	984	990	
Net domestic assets	3,796	602	-1,000	-125	-158	-910	-829	-832	
Net credit to Central Government	1,484	739	-824	-224	-72	-1,216	-1,194	-1,413	
Net credit to rest of public sector	-1,167	415	-120	-393	-35	-348	-495	-1,413	
Net losses	1,697	142	576	858	822	733	875	823	
Net credit to banks	-1,731	-477	-318	-334	-672	-60	-198	-533	
Net credit to other financial institutions	-423	-2	1	-51	-208	-22	-113	51	
Medium- and long-term foreign liabilities	-2,956	-238	-328	-156	38	3	39	240	
Net unclassified	6,892 2/	23	13	175	-31	--	257	--	
SIR allocation	310	--	--	--	--	--	--	--	
Liabilities to private sector	930	46	63	221	147	80	155	158	
Currency in circulation	764	46	63	114	138	62	105	130	
Certificates of deposit	166	--	--	107	9	18	50	28	
(In percent)									
Banking system									
Net domestic assets 5/	...	42.0	-9.0	19.4	17.7	-6.4	7.9	3.9	
Net credit to the public sector 5/	...	46.4	-7.2	13.5	10.0	-9.6	-9.7	-9.0	
Credit to private sector	...	28.4	5.7	13.7	20.9	10.0	34.5	23.2	
Liabilities to private sector	...	25.0	20.0	24.3	23.6	10.3	21.1	17.0	
(In millions of Jamaica dollars)									
Memorandum items									
Financial savings of the private sector (percent)	12,218	1,043 (27.4)	1,051 (21.6)	1,391 (23.5)	2,239 (30.7)	...	2,681 (28.1)	2,566 (21.0)	
Net domestic assets of the Bank of Jamaica, proposed program definition 6/	5,049	1,045	-933	-123	218	...	-629	-664	

Sources: Bank of Jamaica; and Fund staff estimates.

1/ Program as presented in ERS/87/152 (7/8/87).

2/ Includes valuation adjustment of J\$5,375 million.

3/ Valued at accounting rates of J\$1.90 = US\$1 in 1983/84, J\$4.00 = US\$1 in 1984/85, J\$5.65 = US\$1 in 1985/86, and J\$5.5 = US\$1 in 1986/87, 1987/88, and 1988/89.

4/ Valued at accounting rates of J\$5.5 = US\$1 and US\$1.387 = SDR 1.

5/ Changes in relation to the stock of private sector liabilities at the beginning of the period.

6/ As defined under the proposed program: base money minus net international reserves of the Bank of Jamaica.

1987 to 15.5 percent at end-March 1988, while the weighted loan rate remained at 25.4 percent. High interest rates and improved business confidence apparently fostered a continued high level of demand for financial assets, and broad money grew by 21 percent, a substantial rise in real terms.

The Bank of Jamaica's net international reserves rose by US\$189 million during 1987/88 compared with a US\$55 million gain the previous year. More than half that improvement took the form of net repurchases to the Fund. The improvement in the overall balance of payments reflected a strengthening of the capital account, while the current account deficit rose to US\$133 million (US\$23 million more than programmed) from US\$73 million in 1986/87 (Table 6).

The widening of the external current account deficit in 1987/88 was mainly caused by an expansion of imports of more than US\$250 million (close to 25 percent). The growth of imports of capital goods (49 percent) and raw materials (29 percent) was related to a strong expansion of investment and restocking of inventories. Merchandise exports expanded by some US\$150 million (24 percent), mainly reflecting better prices for alumina and a sharp increase in textile/garment exports under the Caribbean Basin Initiative. Net tourism receipts also expanded (by 7.5 percent).

Net capital inflows in 1987/88 recovered from the low level of the previous year, reflecting mainly a shift from an outflow to an inflow of official capital. Furthermore, direct investment also increased substantially, including purchases by nonresidents of shares of the Caribbean Cement Company (US\$4.5 million) and the telecommunications company (US\$55 million).

#### IV. The Program for 1988/89

The economic program for 1988/89 is designed to foster export-led growth while reducing the reliance of the economy on foreign borrowing. Assuming that Jamaica will maintain its competitive position and its terms of trade will remain basically unchanged, real GDP is projected to grow by about 5 percent this year. Inflation, as measured by the average increase in the consumer price index, is projected to remain at about 7 percent.

##### 1. Domestic economic policies

###### a. Public finances

The fiscal program aims at reducing the overall public sector deficit from 5.4 percent of GDP in 1987/88 to 2.8 percent of GDP in 1988/89, in spite of a projected reduction in the proceeds from the divestment of public assets equivalent to about 1 percentage point of GDP. Part of the improvement is explained by the fact that the 1987/88

Table 6. Jamaica: Balance of Payments

(In millions of U.S. dollars)

	1983/84	1984/85	1985/86	1986/87	1987/88 Prog. 1/	1987/88 Prel.	1988/89 Prog.
<b>Current account balance</b>	<b>-278.6</b>	<b>-246.7</b>	<b>-248.1</b>	<b>-73.4</b>	<b>-110.0</b>	<b>-133.0</b>	<b>-103.1</b>
Trade balance	-528.9	-548.1	-494.8	-407.8	-485.0	-510.0	-535.3
Exports	721.8	671.3	539.3	622.6	633.0	774.0	871.5
Bauxite/alumina	477.2	381.6	283.8	306.6	339.0	384.0	421.2
Nontraditional, excluding CARICOM 2/	96.3	150.6	142.7	165.1	159.0	236.2	275.8
Other	148.3	141.1	112.8	150.9	135.0	153.8	174.5
Imports	1,250.7	1,221.4	1,034.1	1,030.4	1,118.0	1,284.0	1,406.8
Bauxite sector: fuel	136.7	100.4	56.3	31.9	53.0	33.2	34.9
Bauxite sector: other	79.0	80.1	49.3	36.0	87.0	31.5	35.1
Nonbauxite fuel	265.0	293.9	236.7	166.3	145.0	174.5	181.2
Nonbauxite nonfuel	770.0	747.0	691.8	796.2	833.0	1,044.8	1,151.6
Tourism, net	360.9	389.2	396.8	503.0	512	539.8	584.6
Interest payments, net	-262.0	-286.8	-308.7	-304.6	-289.0	-305.6	-300.6
Other services, net	-1.1	52.0	3.6	-12.4	-26.0	-22.7	-40.9
Transfers, net	152.5	147.0	155.0	148.3	178.0	165.5	184.2
Of which: official grants	...	37.4	38.4	25.8	...	38.0	59.7
<b>Capital account balance</b>	<b>-169.6</b>	<b>743.9</b>	<b>324.5</b>	<b>128.8</b>	<b>290.0</b>	<b>322.2</b>	<b>222.1 3/</b>
Official medium and long-term (net)	61.6	558.8	215.4	-9.0	213.0	140.2	122.5
Inflows	449.6	971.1	674.8	567.1	663.0	638.9	593.7
New money	338.6	436.0	443.0	252.3	470.0	418.0	489.3
Rescheduling	110.0	535.1	231.8	314.8	193.0	220.9	104.4
Outflows	-388.0	-412.3	-459.4	-576.1	-450.0	-498.7	-471.2
Official short-term (net)	...	...	...	...	...	17.0	...
Direct investment (net)	...	...	20.0	2.0	...	61.2	34.4
Other private capital (net), (including errors and omissions)	-231.2	185.1	89.1	135.9	77.0	103.8	65.2
<b>Overall balance</b>	<b>-448.2</b>	<b>497.2</b>	<b>76.4</b>	<b>55.4</b>	<b>180.0</b>	<b>189.2</b>	<b>119.0</b>
<b>Change in reserves (increase in   assets -)</b>	<b>306.0</b>	<b>-265.7</b>	<b>-61.9</b>	<b>-55.4</b>	<b>-180.0</b>	<b>-189.2</b>	<b>-180.0</b>
Assets	27.0	-125.6	-10.1	38.7	-39.0	-25.5	-12.8
Liabilities	278.0	-140.1	-51.8	-94.1	-141.0	-163.7	-167.2
IMF (net)	39.0	39.1	-19.4	-87.3	-103.1	-113.4	-147.2
Purchases	77.1	105.6	77.6	61.1	72.0	79.2	77.7
Repurchases	-38.1	-66.5	-97.0	-148.4	-175.1	-192.6	-224.9
Arrears	190.0	-111.2	-38.4	-32.6	-25.0	-1.2	...
Other	50.0	-66.0	6.0	25.8	-12.9	-49.1	-20.0
Other arrears	142.2	-231.5	-14.5	...	...	...	...
<b>Financing gap</b>	<b>...</b>	<b>...</b>	<b>...</b>	<b>...</b>	<b>...</b>	<b>...</b>	<b>61.0 4/</b>
<b>Memorandum items</b>							
Ratios to GDP (percent)							
Current account balance							
Including grants	-9.1	-10.9	-11.2	-2.8	-3.8	-4.5	-3.1
Excluding grants	...	-12.6	-13.0	-3.8	...	-5.8	-4.9
Ratios to exports of goods and services (percent) 4/							
Debt service (before rescheduling)	47.6	52.0	67.7	69.3	60.0	57.8	54.1
Debt service (after rescheduling)	39.8	27.4	49.5	47.6	47.1	44.4	44.9
Oil import price (U.S. dollars per barrel, c.i.f.)	...	...	26.4	14.5	15.4	17.5	17.0
Multinationals alumina price (U.S. dollars per metric ton)	179.2	153.4	138.4	137.1	141.6	202.1	217.1
Bauxite/alumina exports (millions of tons of bauxite equivalent)	9.6	7.7	6.0	7.1	7.6	7.2	7.4
Nonbauxite exports (percent change)	-6.4	19.3	-12.4	23.7	4.7	23.4	15.5
Tourism earnings (percent change)	13.3	6.4	3.7	24.9	7.4	7.3	8.0
Nonbauxite nonfuel imports (percent change)	-21.0	-3.0	-7.4	15.1	6.8	31.2	10.4

Sources: Bank of Jamaica; and Fund staff estimates.

1/ As presented in EBS/87/152 (7/8/87).

2/ Nontraditional exports comprise exports other than bauxite, alumina, sugar, and bananas.

3/ It is assumed that a rescheduling with the Paris Club on terms similar to those of the 1987 agreement would yield US\$61 million, raising the capital account surplus to US\$283 million and eliminating the financing gap.

4/ Includes receipts from tourism.

operations included a nonrecurrent purchase of shares in JAMALCO, which was equivalent to 0.9 percent of GDP. The remaining improvement is expected to result from the net effect of (a) a better performance of the Central Government, a decline in the losses of the Bank of Jamaica, and reduced on-lending to the private sector by official financial institutions; and (b) a decrease in the overall surplus of the public enterprises partly caused by an increase in capital expenditure (see Table 4). 1/

Central government operations are expected to yield an overall surplus equivalent to 0.4 percent of GDP in 1988/89, compared with approximate equilibrium in 1987/88 (Table 7). Revenue (inclusive of divestment) is expected to remain at 33 percent of GDP, while external grants are projected to double to 1.7 percent of GDP reflecting higher foreign assistance to the public sector investment program under the aegis of the Caribbean Group for Cooperation in Economic Development.

In 1988/89 the Government intends to complete a revision of the bauxite levy regime to simplify the tax administration and to provide greater incentives for production. Under the proposed new system, a reduced levy, which changes with the international price of alumina, would apply to companies producing at 100 percent capacity. In addition, a general consumption tax will be introduced with the budget for 1989/90. 2/

Central government expenditure is projected to increase by 0.4 percent of GDP to 33.2 percent, with both current and capital expenditure rising. Investment projects are being undertaken, under a three-year Public Sector Investment Program (PSIP), to improve the economic infrastructure in tourism and export-related industries and to rehabilitate social infrastructure for health and education. In this regard, the Jamaican authorities have emphasized programs which are to have significant benefits for low-income groups (Social Well-Being Program). The projected increase in current expenditure reflects in part the increased costs associated with the maintenance of the expanded economic and social infrastructure.

Although central government finances are projected to improve substantially during 1988/89, the Central Government was a net borrower from the banking system during the first quarter, partly because investment outlays, after reaching a peak in the last quarter of 1987/88,

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1/ The excess of the below-the-line measure of the deficit over the above-the-line measure (representing transactions of the nonconsolidated public sector as well as statistical discrepancies) was assumed to remain at the average Jamaica dollar level of the last three years.

2/ Administrative procedures for the introduction of this tax, including a revised business registry number system, have already been established and, in the second half of the current fiscal year, instructions will be issued to taxpayers regarding tax returns and appropriate documentation.



Table 7. Jamaica: Summary Operations of the Central Government

	1983/84	1984/85	1985/86	1986/87	1987/88		1988/89
					Prog. 1/	Prel.	Prog.
(In millions of Jamaica dollars)							
Revenue	1,794.7	2,686.0	3,150.7	4,361.1	4,413.2	5,029.5	5,705.6
Tax revenue	1,532.1	2,022.6	2,716.9	3,758.3	3,933.2	4,323.6	4,929.6
Nontax revenue	64.8	174.2	145.6	139.3	128.0	203.2	221.0
Bauxite levy	194.0	481.2	280.5	463.5	352.0	334.8	437.8 2/
Capital revenue	3.8	8.0	7.7	--	--	167.9	117.3
Proceeds of divestment	--	--	--	25.0	50.0	328.0	336.5
Grants	--	25.0	123.7	130.0	141.0	154.1	318.1
Expenditure	2,902.1	3,265.1	3,843.8	4,677.0	4,898.0	5,352.4	6,078.8
Current	2,394.0	2,817.9	3,253.0	3,755.0	4,026.0	4,189.3	4,708.8
Wages and salaries	967.0	1,072.0	1,083.0	1,260.0	1,334.0	1,335.4	1,499.0
Interest	780.0	1,000.9	1,303.0	1,515.0	1,545.0	1,612.0	1,721.5
Other	647.0	744.0	867.0	980.0	1,147.0	1,241.9	1,488.3
Capital and net lending	508.1	447.2	590.8	922.0	872.0	1,163.1	1,370.0
Pass-throughs 3/	88.9	70.2	90.2	42.6	51.2	156.5	201.8
Overall balance 4/	-1,196.3	-624.3	-659.6	-203.5	-345.1	2.7	79.6
Financing	1,196.3	624.3	659.6	203.5	345.1	-2.7	-79.6
Foreign	499.5	1,117.2	636.7	-151.7	648.1	387.0	549.1
Domestic	696.8	-492.9	22.9	355.2	-303.0	-389.7	-628.7
Banking system	790.0	-654.3	-53.8	-42.0	-789.0	-1,242.9	...
Other 5/	-93.2	161.4	76.7	397.2	486.0	853.2	...
(In percent of GDP)							
Revenue	23.7	27.2	25.2	30.2	27.1	30.8	31.2
Tax revenue	20.3	20.5	21.7	26.0	24.1	26.5	26.9
Nontax revenue	0.9	1.8	1.2	1.0	0.8	1.2	1.2
Bauxite levy	2.5	4.9	2.2	3.2	2.2	2.1	2.4
Capital revenue	--	0.1	0.1	--	--	1.0	0.6
Proceeds of divestment	--	--	--	0.2	0.3	2.0	1.8
Grants	--	0.3	1.0	0.9	0.9	0.9	1.7
Expenditure	38.3	33.1	30.8	32.4	30.0	32.8	33.2
Current	31.6	28.6	26.0	26.0	24.7	25.7	25.7
Wages and salaries	12.8	10.1	8.7	8.7	8.2	8.2	8.2
Interest	10.3	10.9	10.4	10.5	9.5	9.9	9.4
Other	8.5	7.5	6.9	6.8	7.0	7.6	8.1
Capital	6.7	4.5	4.9	6.4	5.3	7.1	7.5
Pass-throughs 2/	1.2	0.7	0.7	0.3	0.3	1.0	1.1
Overall balance	-15.8	-6.3	-5.3	-1.4	-2.1	--	0.4
Financing	15.8	6.3	5.3	1.4	2.1	--	-0.4
Net external	6.6	11.3	5.1	-1.0	4.0	1.6	2.1
Net domestic	9.2	-5.0	0.2	2.5	-1.9	-1.6	-2.5
Banking system	10.4	-6.6	-0.4	-0.3	-4.8	...	...
Other	-1.2	1.6	0.6	2.7	3.0	...	...

Sources: Ministry of Finance; and Fund staff estimates.

1/ As presented in EBS/R7/152 (7/8/87).

2/ Does not include receipts of J\$61.6 million earmarked for amortization of the Government's debt to ALCOA for the purchase of shares in JAMALCO.

3/ Guaranteed on-lending to the private sector.

4/ Overall balance on the basis of checks issued.

5/ Includes financing from nonbank financial institutions, the nonfinancial private sector and public sector entities, as well as the float item.

remained very high in the first quarter of this fiscal year. The authorities explained that this situation would start to be reversed during the second quarter, as investment outlays are expected to slow down with the completion of some projects, while disbursements (which usually lag behind execution) would accelerate.

The overall surplus of the rest of the general government is projected to remain in nominal terms at last year's level, thus declining slightly in relation to GDP. This decline would be the net result of an improvement in the overall position of the National Insurance Fund due to higher investment income, a shift in the national training institute's position (HEART) from a small surplus to a small deficit, and a reduction in the overall surplus of the National Housing Trust.

The combined overall surplus of the public enterprises is projected to decline to 0.8 percent of GDP this year from 1.8 percent of GDP in 1987/88. Their operating surplus is projected to increase somewhat, but the enterprises would not retain any portion of the proceeds from divestment of hotels (compared with a retention equivalent to 0.7 percent of GDP in 1987/88) and would raise capital expenditure (other than that financed by transfers from the Central Government) by 23 percent. The larger increases in capital expenditure would be carried out by the telecommunications company, the electricity company, and the Port Authority.

On-lending by the rest of the public sector is projected to decline to J\$45 million in 1988/89 from J\$187 million in 1987/88, partly because last year lending included direct borrowing by the Caribbean Cement Company (J\$69 million) which was privatized in June 1987 but was still included in the public sector for program monitoring purposes. In 1988/89 the public sector does not include the operations of the cement company. The rest of the decline in on-lending in 1988/89 is associated with reduced operations of the National Development Bank and the Jamaica Mortgage Bank.

The losses of the Bank of Jamaica are projected to decline from 5.4 percent of GDP in 1987/88 to 4.5 percent in 1988/89, owing to the reduction in the Bank's foreign liabilities that has been taking place.

During 1988/89 work will continue toward improving the Government's financial management system through an Administrative Reform Program (ARP), aimed at developing an integrated system of accounting, cash management, and financial reporting. This program is being implemented with financial and technical assistance from the World Bank. The authorities have undertaken to make further improvements in public sector accounting by the time of the mid-term review of the stand-by arrangement.

b. Monetary policy

The monetary program for 1988/89 envisages an expansion of broad money of about 17 percent, compared with 21 percent the previous year (see Table 5) <sup>1/</sup> with the declining trend in money velocity continuing to taper off. Consistent with the net international reserve target and the domestic financing needs of the public sector, the increase in bank credit to the private sector is projected to decelerate to an annual rate of 23 percent by the end of the fiscal year, compared with 35 percent during the previous 12 months. Ceilings have been established on the net domestic assets of the Bank of Jamaica (defined for program purposes as base money minus net international reserves) consistent with the projected rise in broad money and the net official international reserve target.

As credit growth accelerated in April-June 1988 (with credit to the private sector growing at an annual rate of 38 percent in the year ended June 1988 and the Government also borrowing in net terms from the banking system), the authorities decided to modify open market procedures to strengthen control over credit. On August 9, 1988 the Bank of Jamaica announced that it would discontinue the policy of offering certificates of deposit at periodic auctions at a pre-set interest rate, with the amount sold being determined by demand at that rate. Since that date the Bank has been offering pre-set amounts of its own CDs or the Government's treasury bills, with interest rates resulting from the bidding. <sup>2/</sup> The quantities offered are those deemed necessary to maintain the net domestic assets of the Bank of Jamaica within the established limits.

The authorities recognize the important role that positive interest rates have in promoting financial savings, but they believe that with the inflation rate having remained at an average of 7 percent for more than a year, there is room for a further decline in interest rates, including those on savings deposits. They have thus indicated that the floor on the interest rate on savings deposits would be modified from time to time in the light of developments in the auctions of Bank of Jamaica's CDs or government treasury bills.

In the first half of 1987/88 the Government started a program to convert external debt into domestic equity investment. Under the program, a prospective investor can use eligible debt of Jamaica acquired

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<sup>1/</sup> A broader measure of private sector holdings of financial assets (including broad money and holdings of government paper) would expand by 21 percent, compared with 28 percent in 1987/88.

<sup>2/</sup> With the elimination by March 1988 of the liquid assets requirement, which could be satisfied by holding Government's treasury bills but not Bank of Jamaica's certificates of deposit, the differences between these two financial instruments were blurred. The Bank of Jamaica has started to use both instruments in an equivalent manner for purposes of credit control.

at a discount in the secondary market to obtain local currency from the Bank of Jamaica to pay for part of an approved investment project. To avoid the monetary effects of the transaction, the Bank places special bonds (ten years' maturity and market-related interest rate) with domestic financial institutions. External debt converted in 1987/88 amounted to about J\$14 million, and conversions may increase to about J\$176 million in 1988/89. The pace of conversion will be managed in order not to strain the capacity of the domestic market to absorb debt instruments.

The Government intends to continue its program of financial sector reform in 1988/89. The second phase of the program will focus on improving the operations of nonbank financial institutions and expanding the market for private debt instruments.

c. Incomes and price policies

The authorities consider that wage guidelines have been useful in containing wage increases and, therefore, they have extended through March 1989 the 10 percent wage guideline that had been in effect since early 1987. Application of this guideline to the two-year contracts covering most central government employees has resulted in average annual increases of 9 percent in the central government wage bill in the 1987/88-1988/89 period. Wage increases for unionized private sector workers have not exceeded 10 percent a year.

A limited number of products, including basic foods, animal feed, and medicine, remain subject to price controls. The prices for these products will be adjusted to reflect changes in costs, and the scope of price controls will not be increased during the program period. The Jamaica Commodity Trading Corporation (JCTC), which is the sole importer of most of the products subject to price control, subsidizes the sale of certain essential goods for low-income groups with gains made on other products and transfers from the rest of the public sector. Under the sponsorship of the World Bank, a study is being conducted on the costs and benefits of JCTC's subsidy operations and, on the basis of this study, the JCTC's price and subsidy scheme would be reviewed before March 1989.

2. External sector policies

The deficit in the external current account is projected to decline to US\$103 million (3.1 percent of GDP) in 1988/89 from US\$133 million (4.5 percent of GDP) last year. The growth of both merchandise exports and imports is expected to decelerate substantially from the high growth rates of last year. Exports are projected to rise by 13 percent due to increased volume and unit value for alumina and continued expansion of nontraditional exports. Imports are projected to grow by 10 percent, as the inventory accumulation of the previous year levels off and the rise of aggregate demand slows. Tourism receipts are projected to grow by some 8 percent, slightly faster than in 1987/88. Net interest payments

abroad are expected to remain unchanged, while an increase in other net service payments should be offset by larger official grants.

Net capital inflows are projected at some US\$283 million, about US\$40 million less than last year. Following last year's exceptionally large inflows, direct investment and other net private capital inflows are projected to decline in line with lower divestment proceeds and slower pace of growth of private sector activity and imports. This decline, however, would be partially offset by an increase in disbursements of official loans from US\$435 million in 1987/88 to US\$490 million in 1988/89, as a result of substantial commitments of both balance of payments support and project loans made at meetings of the Caribbean Group for Cooperation in Economic Development.

Existing and prospective rescheduling agreements are expected to provide debt relief to Jamaica for some US\$165 million in 1988/89. Of this amount, US\$73 million corresponds to commercial bank loans, and US\$21 million to debt with Venezuela and Mexico, under rescheduling agreements completed in early 1987. In addition, Jamaica is requesting from official creditors under the auspices of the Paris Club a rescheduling of current maturities, including those in arrears since June 1, 1988, on terms similar to those of the 1987 rescheduling. With the completion of such agreement, Paris Club creditors are projected to provide debt relief to Jamaica for some US\$71 million during 1988/89. <sup>1/</sup>

Net official international reserves are targeted to improve by US\$180 million in 1988/89, similar to the 1987/88 increase. Such improvement would permit an increase in liquid reserves to about US\$100 million (equivalent to about four weeks of projected nonbauxite sector imports) by end-March 1989. Assuming that purchases are made as scheduled under the proposed stand-by arrangement, net repurchases to the Fund would be equivalent to US\$147 million in 1988/89.

Jamaica's outstanding medium- and long-term external debt (including obligations to the Fund) is projected to rise by only US\$20 million during 1988/89, declining in relation to GDP to 127 percent from 142 percent at the end of 1987/88. After rescheduling, official debt service payments would remain at about 45 percent of exports of goods and nonfactor services.

An important element of the program is the maintenance of the arrangement for allocating foreign exchange through a Dutch auction system. The authorities intend to continue to manage the auction system in such a way that all bona fide bids for foreign exchange are accepted and that there are no undue delays in the delivery of foreign exchange for those bids at or above the threshold price.

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<sup>1/</sup> Of which US\$10 million corresponds to obligations falling due in April and May 1988 which were rescheduled under an extension of the March 1987 agreed minute.

Under the auction system in operation since 1983, the Jamaica dollar depreciated substantially against the U.S. dollar through end-1985, but it has since then remained basically unchanged. An index of the real value of the Jamaica dollar in relation to a weighted average of the real value of trading partners' currencies <sup>1/</sup> has followed a similar pattern (Chart 1), indicating that Jamaica's competitiveness has remained virtually unchanged since December 1985, a judgement which appears to be corroborated by the continued good performance of nontraditional exports and tourism. Program projections assume no major changes in Jamaica's terms of trade, an average inflation rate in trading partner countries of 7 percent, and a similar inflation rate in Jamaica. These projections imply that competitiveness would be broadly maintained by keeping the value of the Jamaica dollar unchanged against the U.S. dollar, assuming no significant shifts in the value of the U.S. dollar against Jamaica's other trading partners.

As a safeguard against a possible erosion in competitiveness, the program provides that whenever the average index of the effective exchange rate over a three-month period indicates an appreciation of the Jamaica dollar of more than 5 percent over the level of June 1988, the Jamaica dollar will be allowed to depreciate as necessary to return to its real effective exchange value at the base date. Also, in case of underperformance under the target for net international reserves, the authorities intend to reduce the supply of foreign exchange in the auction, which would be expected to result in a depreciation of the Jamaica dollar.

Jamaica's exchange system involves certain restrictions on current international transactions, including limitations on profit remittances abroad under a debt-equity conversion scheme, limitations on travel expenditure and other personal services abroad, and a duty rebate of 7.5 percent on the f.o.b. value of exports of manufactured goods, which gives rise to a multiple currency practice. Also, the "Dutch" bidding system in the foreign exchange auction has intermittently given rise to a multiple currency practice. <sup>2/</sup>

Progress has been made and will continue to be made in 1988/89 toward the liberalization of exchange controls. On August 8, 1988 the basic allowance for foreign travel (other than for business and professional reasons) was raised from US\$150 to US\$300 per person and calendar year. Also, the annual limit per person on remittances of income from emigrants' property and remittances for family maintenance was raised from US\$1,000 to US\$2,000, and that for cash gifts was raised from US\$50 to US\$100. In addition, the 7.5 percent duty rebate scheme will be eliminated by April 1, 1989 with the implementation of the general consumption tax referred to above.

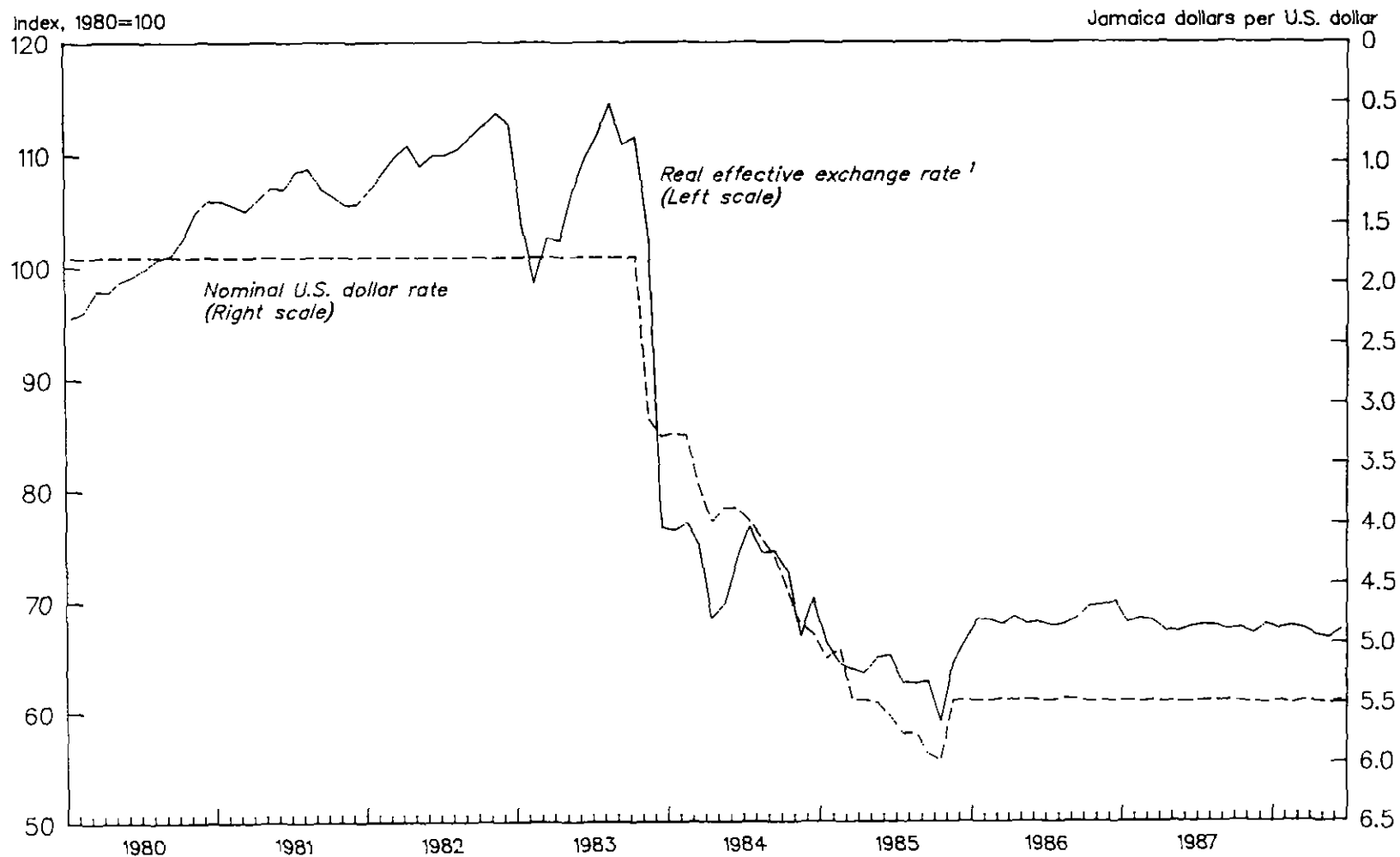
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<sup>1/</sup> The real effective exchange rate calculation used by the Fund for its Information Notice System.

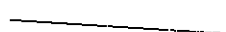
<sup>2/</sup> Jamaica's exchange and trade system is described in EBS/88/10 (1/22/88) and in SM/88/37 (2/9/88), pp. 50-52.

CHART 1  
JAMAICA

EXCHANGE RATE DEVELOPMENTS, JANUARY 1980 TO JUNE 1988



<sup>1</sup> Value of Jamaica dollar in terms of 1980 trade-weighted average of partner countries' currencies, adjusted for relative movements in consumer prices. Decline represents real depreciation of Jamaica dollar. Incorporates officially sanctioned dual market transactions and transactions in the black market during January–November 1983.





The Government intends to continue the customs duty reform program that was initiated in April 1987 under a World Bank sectoral adjustment loan. Maximum duties were reduced to 60 percent (20 percent for capital goods) on April 1, 1988. The ultimate objective is the simplification of the duty structure to a system of four rates ranging from 5 to 30 percent within four to five years.

#### V. Performance Criteria

The financial program described in the attached letter contains the following performance criteria, specified through March 1989 (Table 8):

1. A ceiling on the financing requirement of the overall public sector, defined to include as financing the proceeds of the divestment of public enterprises. This ceiling is designed to exclude the telecommunications company (TELECOM) from the public sector if the Government becomes a minority shareholder before end-October 1988. Also, this ceiling is adjustable downward (upward) for shortfalls (excesses) from projected disbursements of project-related foreign loans. There is a maximum allowable upward adjustment of US\$10 million.

2. A subceiling on the combined financing requirement of the Central Government and the Bank of Jamaica, adjustable downward (upward) for shortfalls (excesses) from projected disbursements of project-related foreign loans.

3. A ceiling on the net domestic assets of the Bank of Jamaica.

4. A floor for the stock of net international reserves.

5. A prescription that external arrears, defined to include undue delays in payments to nonresidents by the public sector and in the delivery of foreign exchange at the auction, will not be incurred.

6. A ceiling on net disbursements of medium- and long-term official foreign debt (excluding project loans) with a subceiling on gross disbursements of loans with one to five years' maturity. The ceiling on net debt disbursements has been set at US\$10 million above programmed amounts. However, any excess over programmed amounts will require an equivalent upward adjustment in the floor on net international reserves and downward adjustment in the ceiling on the net domestic assets of the Bank of Jamaica.

7. A ceiling on short-term external public debt, which provides for no increase from the stock as of March 31, 1988.

Under the program, exchange rate action is to be triggered by an appreciation in the real effective value of the Jamaica dollar of more than 5 percent as defined in the attached letter; in addition, under-performance under the floor on net international reserves requires that

Table 8. Jamaica: Proposed Quantitative Performance Criteria

	Program		
	September 1988	December 1988	March 1989
(In millions of U.S. dollars)			
Net international reserves <u>1/</u>	-437	-401	-285
Net external debt disbursements <u>2/</u>	38	65	47
Gross disbursements of external public debt of 1-5 years maturity <u>3/</u>	71	114	158
Stock of short-term external public debt <u>4/</u>	97	97	97
Stock of external payments arrears	--	--	--
(End of period, in millions of Jamaica dollars)			
Net domestic assets of the Bank of Jamaica <u>5/</u>	5,070	5,050	4,385
Overall public sector financing requirement <u>6/</u> <u>7/</u>	777	1,138 (1,095)	926 (772)
Central Government financing requirement <u>6/</u>	1,027	1,407	1,157

Sources: Technical Memorandum of Understanding.

1/ Targets adjustable upward for any cumulative excess of net external debt disbursements over programmed amounts.

2/ Refers to medium- and long-term debt contracted by the public sector or by the private sector with government guarantee (excluding project loans by multilateral and other official development agencies). Figures refer to cumulative change from April 1, 1988. Any excess in net disbursements over programmed amounts (which are US\$10 million below these limits) is to be added to net international reserves.

3/ Figures refer to cumulative change from April 1, 1988.

4/ Trade and suppliers' credits with original maturities of less than one year.

5/ Ceilings adjustable downward for any excess of net external debt disbursements over programmed amounts.

6/ Cumulative change from April 1, 1988. Includes Bank of Jamaica losses. Adjustable upward (downward) for any excesses (shortfalls) over programmed disbursements of project-related foreign loans; there is a maximum for the upward adjustment of the ceiling on the overall public sector financing requirement which is equal to the Jamaica dollar equivalent of US\$10 million.

7/ The ceilings in parentheses, which refer to the overall public sector financing requirement excluding the operations of the telecommunications company (TELECOM), will be effective if TELECOM is privatized before October 31, 1988.

the supply of foreign exchange in the auction be reduced, which would be expected to result in a depreciation of the Jamaica dollar.

The progress made in implementing the program will be assessed in a review to be completed by end-April 1989, which is also a performance criterion. In that review, understandings must be reached on performance criteria for the period of the arrangement beyond end-March 1989.

The customary performance criteria on overdue financial obligations to the Fund and on exchange restrictions, multiple currency practices, bilateral payments agreements inconsistent with Article VIII, and import restrictions for balance of payments purposes are applicable during the program period.

#### VI. Operations of the World Bank in Jamaica

Since 1980 the World Bank has substantially increased its lending to Jamaica through loans in support of policy reforms and directly productive projects. From 1980/81 to 1984/85 the Bank approved 17 operations totaling US\$376 million, with about one half of this amount corresponding to three Structural Adjustment Loans (SALs). <sup>1/</sup> The SALs were designed as medium-term programs to complement the stabilization efforts supported by the Fund, and were aimed mainly at promoting an expansion and diversification of exports, a liberalization of the economy, and improvements in public sector operations.

No new loan was approved by the Bank for Jamaica during 1985/86 because of concerns over the country's creditworthiness. However, Bank lending to Jamaica resumed in June 1987 with the approval of a package of four loans: two policy-based loans to support improvements in public enterprise operations (US\$20 million) and trade and financial sector reforms (US\$40 million); and two project loans in the areas of population and health (US\$10 million) and sugar rehabilitation (US\$34 million). Project loans in the areas of agriculture, power generation, education, and industrial development for US\$17 million were approved during 1987/88.

Gross disbursements averaged US\$54 million a year in the four years through June 1988, while repayments have risen rapidly to an estimated US\$58 million in 1987/88. At the end of June 1988 Jamaica's net indebtedness to the World Bank amounted to US\$508 million, or about 12 percent of Jamaica's external public debt.

During 1988/89, two policy-based loans for US\$50 million (with co-financing by developed trading partners for an identical amount), to support agricultural sector reform and trade and financial sector

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<sup>1/</sup> Jamaica's financial relations with the World Bank are summarized in Attachment II; data refer to the Bank's fiscal years (which run from July to June).

reforms, are expected to be approved and partly disbursed. Also, disbursements of project loans for administrative reform, agriculture, roads, health and education are expected to continue.

## VII. Medium-Term External Outlook

The Jamaican authorities have developed an economic strategy for the period 1988/89-1990/91 which is designed to maintain an average growth of real GDP of 3 1/2 to 4 percent a year while reducing Jamaica's debt service burden through further improvements in the overall fiscal position and export performance. This strategy has been endorsed by the World Bank and served as the basis for requesting financial assistance from bilateral and multilateral agencies participating in meetings of the World Bank's Caribbean Group for Cooperation in Economic Development in December 1987 and June 1988. The proposed public sector investment program (PSIP) amounts to J\$6.6 billion over 1988/89-1990/91 (around 12 percent of GDP per year, in line with the average public investment ratio in the past four years). The PSIP focuses on investment in economic infrastructure to sustain growth and on rehabilitating social infrastructure (Social Well-Being Program).

A revised medium-term external scenario, based on the Government's strategy and on recent developments, suggests that Jamaica's balance of payments will remain under pressure for several years. Debt service obligations (including those to the Fund and the World Bank) would remain large, and extraordinary financing would be required during the next few years.

Nonetheless, the scenario is based on progress toward easing the debt burden. Specifically, the ratio of external debt to GDP would be reduced from 127 percent in 1988/89 to 93 percent in 1993/94, and the ratio of debt service payments to exports of goods and nonfactor services from 45 percent to 28 percent. Achievement of these objectives would require a reduction in the external current account deficit in relation to GDP from 3.1 percent to 0.6 percent (Table 9).

The required improvement in the external current account could be attained with average nominal growth in exports of 6 percent per year and a similar nominal growth in imports, which would appear to be achievable if a flexible exchange rate policy is pursued to maintain export competitiveness and compensate for any possible increase in import demand resulting from the planned reduction in import duties. The average annual growth in the volume of bauxite/alumina, bananas and nontraditional exports would be 3 percent, 13 percent and 7 percent, respectively, while receipts from tourism would grow at an annual rate of around 7.5 percent over the medium term. At the same time, import volume would increase at an average rate of 2.5 percent a year.

Table 9. Jamaica: Medium-Term Balance of Payments Projections

(In millions of U.S. dollars)

	Prel. 1987/88	Prog. 1988/89	Projections				
			1989/90	1990/91	1991/92	1992/93	1993/94
Current account balance	-133	-103	-97	-84	-74	-46	-27
Trade balance	-510	-535	-579	-623	-656	-693	-733
Exports	774	872	920	968	1,032	1,097	1,167
Bauxite/alumina	384	421	420	421	439	457	476
Nontraditional, excluding CARICOM 1/	236	276	311	346	380	413	449
Other	154	175	189	201	213	227	242
Imports	1,284	1,407	1,499	1,591	1,688	1,791	1,900
Bauxite sector: fuel	33	35	40	42	44	46	48
Bauxite sector: other	32	35	43	46	48	50	52
Nonbauxite fuel	175	183	195	208	222	237	253
Nonbauxite nonfuel	1,045	1,154	1,221	1,295	1,374	1,458	1,547
Tourism, net	540	585	634	688	739	794	852
Interest payments, net 2/	-306	-301	-312	-325	-337	-330	-328
Other services, net	-23	-41	-27	-10	-5	1	1
Transfers, net	166	189	188	187	185	183	181
of which: official grants	38	60	60	60	60	60	60
Capital account balance	322	222 3/	128	76	101	96	106
Official medium and long-term, net	140	122	48	6	41	36	46
Inflows	639	594	500	407	374	372	372
New money	418	489	439	402	372	372	372
Rescheduling	221	104	61	5	2	--	--
Outflows	-499	-471	-452	-401	-333	-336	-326
Official short-term, net	17	--	--	--	--	--	--
Direct investment, net	61	34	30	30	20	20	20
Other private capital, net (Including errors and omissions)	104	65	50	40	40	40	40
Overall balance	189	119	31	-8	26	50	79
Change in reserves	-189	-180	-132	-134	-125	-109	-101
(Increase in assets -)							
Assets	-26	-13	-25	-30	-35	-40	-45
Liabilities	-163	-167	-107	-104	-90	-69	-56
IMF (net)	-113	-147	-99	-100	-86	-65	-50
Purchases	79	73	57	--	--	--	--
Repurchases	-192	-225	-156	-100	-86	-65	-56
Arrears	-1	--	--	--	--	--	--
Other	-49	-20	-8	-4	-4	-4	--
Financing gap	--	61 3/	101	142	99	59	22
Memorandum items							
Ratios to GDP (percent)							
Current account balance							
Including grants	-4.5	-3.1	-2.7	-2.2	-1.8	-1.0	-0.6
Excluding grants	-5.8	-4.9	-4.4	-3.8	-3.3	-2.4	-1.8
Public debt (medium- and long- term, end period)	142	127	119	112	106	99	93
Ratios to exports of goods and services (percent) 4/							
Public debt (medium- and long- term, end period)	254	236	222	210	200	189	180
Debt service (before rescheduling)	57.8	54.1	46.8	39.2	34.0	31.1	28.0
Debt service (after rescheduling)	44.4	44.9	...	...	...	...	...
Multinationals alumina price (U.S. dollar per metric ton)	202	217	198	192	196	201	206
Bauxite/alumina exports (millions of tons of bauxite equivalent)	7.2	7.3	7.6	7.7	7.8	8.0	8.0
Nonbauxite exports (percent change)	23.4	15.5	11.0	9.3	8.5	7.9	7.4
Tourism earnings (percent change)	7.3	8.0	8.1	8.1	7.1	7.1	7.0
Nonbauxite related imports (percent change)	31.2	9.6	6.0	6.2	6.2	6.2	6.2

Sources: Bank of Jamaica; and Fund staff estimates.

1/ Nontraditional exports comprise domestic exports other than bauxite, alumina, sugar and bananas.

2/ Includes interest payments on borrowing to cover the projected financing gaps.

3/ It is assumed that a rescheduling with the Paris Club on terms similar to those of the 1987 agreement would yield US\$61 million, raising the capital account surplus to US\$243 million and eliminating the financing gap.

4/ Includes receipts from tourism.

On the basis of gradually declining official capital inflows <sup>1/</sup> (including those resulting from already agreed reschedulings) and a conservative estimate of net private capital inflows, in the next five years there would be an external financing gap of about US\$425 million, with the gap averaging US\$115 million a year during the first three years and declining thereafter to about US\$40 million a year. These gaps would need to be filled by concessional aid and new reschedulings, as well as further financial arrangements from the Fund. The latter would be expected to be in amounts that would result in a continuing reduction in outstanding Fund credit.

#### VIII. Staff Appraisal

In fiscal year 1986/87, improvements in the external environment and in domestic policies helped Jamaica reduce its long-standing financial imbalances, and there was a resumption of economic growth. The Government's economic program for 1987/88, which was supported by a stand-by arrangement from the Fund approved in March 1987, aimed at a further improvement in Jamaica's economic performance in the context of a stable exchange rate regime.

Performance under the 1987/88 program was generally satisfactory, with all performance criteria being met and all purchases taking place as scheduled. Output growth accelerated to 5.5 percent led by an expansion of merchandise exports, tourism, and construction. The unemployment rate declined, and inflation moderated. At the same time, credit and import growth accelerated sharply, and the external current account deficit widened to 4.5 percent of GDP from 2.8 percent in the previous year; most of this increase was financed by private capital inflows, including those related to the divestment of public enterprises.

For the period 1988/89-1990/91 the Jamaican authorities have developed a growth-oriented adjustment strategy, which is designed to maintain an average growth of real GDP of 3 1/2 to 4 percent a year and a rate of inflation in line with that of trading partners, while reducing Jamaica's debt service burden. Consistent with this strategy, the economic program for 1988/89 aims at reducing the external current account deficit to 3 percent of GDP, on the basis of a further reduction in the overall public sector deficit and a significant slowing in the growth of bank credit to the private sector.

In the fiscal area, the Government intends to bring about a reduction in the overall fiscal deficit to 2.8 percent of GDP in 1988/89, while increasing expenditure to improve the economic infrastructure for export-led growth and to rehabilitate the social infrastructure to

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<sup>1/</sup> These inflows are larger than those assumed in EBS/88/10 (1/22/88) as they reflect amounts pledged by donors in the last two meetings of the Caribbean Group for Cooperation in Economic Development.

alleviate poverty. To attain these objectives, the Government is counting on continued proceeds from the divestment of public enterprises. It must be stressed, however, that divestment should be considered an exceptional source of revenue that does not obviate lasting fiscal measures. The staff, therefore, attaches importance to the authorities' intention to introduce a general consumption (value-added) tax with the budget for the coming fiscal year, and encourages the authorities in their efforts to further rationalize the import duty system and improve the efficiency of tax administration. On the expenditure side, it is important that the Government implements as quickly as possible its administrative reform program, which is expected to result in further improvements in budgetary control and monitoring.

Achievement of the program's price and balance of payments objectives requires an overall policy of credit restraint. Faced with the upsurge of credit to the private sector in April-June 1988, which was superimposed upon a large, temporary domestic financing requirement of the public sector, the authorities introduced modifications in open market procedures to improve control over credit. The recent efforts to rein in credit expansion will need to be pursued determinedly, and careful monitoring will be required to maintain credit policy on track. The essence of the new arrangement is the setting of the amount of open market sales at a level consistent with the overall credit program, allowing interest rates to be determined at the auction. Of course, it is possible that the resulting interest rates do not fit to the expectation of the authorities that interest rates should decline. In any event, consistent with the approach to credit management that has been adopted, the authorities should refrain from attempting to influence interest rates through administrative means. To reduce upward pressures on interest rates on a lasting basis, the most effective way would be additional action to strengthen the public finances.

Regarding incomes policies, restraint on wages should be exercised, within the 10 percent wage guideline recently extended through March 1989, in order to avoid an erosion of competitiveness. For the future, given the emphasis placed by the authorities on maintaining the exchange rate of the Jamaica dollar in terms of the U.S. dollar at its present level, the guideline may need to be reviewed to prevent that costs in Jamaica rise faster than in competitor countries.

Maintenance of Jamaica's competitiveness in the last three years has been consistent with stability in the value of the Jamaica dollar against the U.S. dollar, which has been helped by the depreciation of the U.S. dollar against other major currencies and a declining inflation rate in Jamaica. However, the authorities should follow closely developments in the balance of payments and indicators of competitiveness. In this connection, the staff notes the authorities' intention not to allow the Jamaica dollar to appreciate by more than a limited margin in real terms, and to reduce the supply of foreign exchange in the auction if needed to meet the program's net international reserve targets.

In view of the policies already adopted and those being implemented, the staff believes that the economic program of the Jamaican authorities deserves the support of the Fund in the form of a stand-by arrangement for the equivalent of SDR 82 million.



### IX. Proposed Decisions

The following draft decisions are proposed for adoption by the Executive Board:

1. Stand-By Arrangement

a. The Government of Jamaica has requested a stand-by arrangement for a period from September , 1988 to November 30, 1989 in an amount equivalent to SDR 82 million.

b. The Fund approves the stand-by arrangement set forth in EBS/88/188.

c. The Fund waives the limitation in Article V, Section 3 (b) (iii).

2. Exchange System

Jamaica retains restrictions in the making of payments and transfers for current international transactions and multiple currency practices, as described in EBS/88/10 and EBS/88/188, which are subject to the Fund's approval under Article VIII, Sections 2(a) and 3. Jamaica is implementing an economic program which contemplates liberalization of its exchange system, and, on this basis, the Fund grants approval for the retention of these exchange measures until April 30, 1989 or the completion of the next Article IV consultation, whichever is earlier.

Jamaica - Fund Relations

I. Membership status

- (a) Date of membership February 21, 1963.  
 (b) Status: Article VIII.

(A) Financial Relations (as of July 31, 1988)

II. General Department

- (a) Quota: SDR 145.5 million  
 (b) Total Fund holdings of Jamaica dollars:  
 SDR 555.9 million or 382.1 percent of quota  
 (c) Fund credit (i.e., Fund holdings of Jamaica dollars  
 subject to repurchase and charges):

	Millions of SDRs	As Percent of Quota
<u>Total Fund credit</u>	<u>410.4</u>	<u>282.1</u>
Of which: Under tranche policy	333.2	229.0
Credit tranches	101.6	69.8
Extended facility	231.6	159.2
Ordinary resources	53.4	36.7
Supplementary financing	19.6	13.4
Enlarged access resources	158.6	109.0
Under CFF	77.2	53.1

- (d) Reserve tranche position: None

III. Stand-by or extended arrangements and special facilities

- (a) Stand-by and extended arrangements during the last ten years:

Type	Date	Duration	Approved Amount (In millions of SDRs)	Amount Drawn (In millions of SDRs)	Amount Drawn (In % of quota)
EFF	6/09/78	3 years	200.0		
(augmented)	6/11/79		259.7	155.0	209.5
EFF	4/13/81	3 years	477.7	402.8	362.9
Stand-by	6/22/84	1 year	64.0	64.0	44.0
Stand-by	7/17/85	21 months	115.0	41.6	28.6
Stand-by	3/02/87	15 months	85.0	85.0	58.4

(b) Use of special facilities during the last five years:

CFF	6/26/84	SDR 72.6 million
CFF	3/02/87	SDR 40.9 million

IV. SDR Department

- (a) Net cumulative allocation: SDR 40.61 million
- (b) Holdings: SDR 0.01 million (0.04 percent of net cumulative allocation)

V. Administered Accounts

- (a) Trust Fund loans: None
- (b) SFF Subsidy Accounts: SDR 16.65 million

	Overdue Financial Obligations 8/11/88	Principal and Interest Due		
		1988	1989	1990
Principal	--	163.2	130.8	82.1
Repurchases	--	163.2	130.8	82.1
Trust Fund Repayments	--	--	--	--
Charges and interest including SDR and Trust Fund (provisional)	--	31.2	24.1	15.8
<u>Total</u>	<u>—</u>	<u>194.4</u>	<u>154.9</u>	<u>97.9</u>

(B) Nonfinancial Relations

VI. Exchange Rate Arrangement

In November 1983, Jamaica adopted a unified floating rate within an adjustable exchange rate band. An auction mechanism to determine rates was instituted in December 1983 and modified in March and November 1984. Since November 1985, the exchange rate has remained close to J\$5.5 per U.S. dollar.

VII. Article IV Consultation

The last Article IV Consultation was completed by the Executive Board on March 2, 1988 (EBM/87/34). Jamaica is on the standard 12-month cycle.

VIII. Technical Assistance

None since 1986.

IX. Resident Representative

Mr. John Hill, who has been resident representative since March 3, 1987, will be succeeded by Mr. Gilbert Terrier on September 1, 1988.

Jamaica: Financial Relations with the World Bank

(In millions of U.S. dollars)

	Outstanding as of June 30, 1988				
	Disbursed	Undisbursed	Total	Repayments	Net Outstanding
<u>Total IBRD</u>	<u>680.12</u>	<u>101.40</u>	<u>781.52</u>	<u>171.30</u>	<u>508.82</u>
Agriculture and forestry	60.27	20.60	86.87	19.45	40.82
Education	29.80	8.30	38.10	15.96	13.84
Population and rural development	23.54	9.49	33.03	10.41	13.13
Transportation	69.08	18.20	87.28	27.10	41.98
Power	69.44	19.18	88.62	33.28	36.16
Utilities	25.06	3.75	28.81	7.87	17.19
Program loan	30.00	--	30.00	13.86	16.14
EDF	64.40	--	64.40	17.14	47.26
SAL	251.40	--	251.40	13.77	237.63
Industrial development	24.02	11.35	35.37	5.56	18.46
Other	33.11	4.53	37.64	6.90	26.21
<u>IFC investments</u>	<u>12.25</u>	<u>4.29</u>	<u>16.54</u>	<u>6.01</u>	<u>6.24</u>
Net Disbursements During Fiscal Year 1/					
	Actual				Proj.
	1984/85	1985/86	1986/87	1987/88	1988/89
<u>Net disbursements (IBRD)</u>	<u>56.0</u>	<u>1.6</u>	<u>14.1</u>	<u>16.6</u>	<u>2.4</u>
Disbursements	75.3	23.7	52.8	64.0	60.0
Repayments	19.3	22.1	38.7	47.4	57.6

Source: IBRD.

1/ World Bank fiscal year (July 1-June 30).

## Jamaica: Selected Economic and Financial Indicators

	1983/84	1984/85	1985/86	1986/87	1987/88 Prog. 1/	1987/88 Prel.	Prog. 1988/89
(Annual percent changes, unless otherwise specified)							
National income and prices							
GDP at constant prices	1.7	-1.4	-3.7	3.9	1.1	5.5	4.7
GDP deflator	21.3	31.9	31.7	11.4	7.9	6.8	7.2
Consumer prices (period average)	14.7	29.7	24.2	11.4	9.6	6.9	7.0
External sector (in U.S. dollars)							
Exports, f.o.b.	-1.7	-6.7	-19.9	15.4	13.2	24.3	12.6
Imports, c.i.f.	-15.0	-2.3	-15.3	-0.2	9.1	24.7	9.6
Nonoil imports, c.i.f.	-20.1	-2.6	-10.4	12.3	8.8	29.3	10.5
Export volume	-3.5	16.9	-12.4	7.1	...	7.2	7.0
Import volume	-12.8	0.9	-9.1	8.0	...	16.3	4.8
Terms of trade	4.5	-17.5	-1.9	16.6	...	8.3	0.6
Nominal effective exchange rate (depreciation -) 2/	-34.2	-30.1	-6.2	-1.9	...	-1.5	...
Real effective exchange rate (depreciation -) 2/	-26.8	-14.9	6.5	0.1	...	-1.0	...
Central Government							
Revenue 3/	8.8	51.1	20.8	37.9	2.0	22.0	15.4
Total expenditures 4/	6.8	11.5	18.0	20.0	4.9	16.7	14.0
Money and credit							
Domestic credit (NDA) 5/	42.0	-9.0	19.4	17.7	-6.4	7.9	3.9
Public sector 6/	46.4	-7.2	13.5	10.0	-9.6	-9.7	-9.0
Private sector	16.0	7.5	7.7	10.8	4.8	17.5	13.1
Liabilities to private sector (M)	25.0	20.0	24.3	23.6	10.3	21.1	17.0
Velocity (GDP relative to M)	2.2	2.4	2.4	2.3	2.2	2.2	2.1
Interest rate (average commercial bank deposit rate)	13.9	17.7	20.0	14.4	...	15.5	...
(In percent of GDP)							
Central government deficit	15.8	6.3	5.3	1.4	2.2	--	0.4
Overall public sector deficit	19.6	15.1	13.2	5.6	4.5	5.4 7/	2.8
Foreign financing 8/	14.2	9.0	6.4	-2.9	1.2	-0.6	0.1
Domestic financing	5.4	6.1	6.8	8.5	3.3	6.0	2.7
Gross domestic investment	22.6	23.8	23.1	18.8	18.4	21.1	21.1
Gross national savings	13.5	13.2	11.4	15.4	14.6	16.6	18.0
External current account deficit							
Excluding grants	9.8	12.6	13.0	3.8	...	5.8	4.9
Including grants	9.1	10.9	11.2	2.8	3.8	4.5	3.1
External debt (end-period)							
Inclusive of use of Fund credit	91.1	136.2	163.5	136.1	...	142.0	127.0
Debt service ratio (in percent of exports of goods and services) 9/	39.8	27.4	49.5	47.6	47.1	44.4	44.9
Interest payments (in percent of exports of goods and services)	17.9	18.8	24.1	21.2	...	18.6	16.9
(In millions of U.S. dollars)							
Overall balance of payments	-448	497	76	55	180	189	180
Gross official reserves, end-period (in weeks of imports)	2	8	10	8	8	8	8
External payments arrears, end-period	418	72	34	1	--	--	--

1/ As presented in EBS/87/152 (7/8/87).

2/ March to March.

3/ Includes proceeds from divestment and grants.

4/ Includes guaranteed on-lending to the private sector.

5/ In relation to banking system liabilities to the private sector at the beginning of the period.

6/ Includes the losses of the Bank of Jamaica.

7/ Includes purchase of shares in JAMALCO for the equivalent of 0.9 percent of GDP.

8/ Includes changes in net foreign assets and in medium- and long-term foreign liabilities of the Bank of Jamaica.

9/ After rescheduling.

Jamaica: Schedule of Purchases During Period of Stand-by Arrangement

Amount	Schedule Availability Date	Conditions Necessary for Purchase <u>1/</u>
SDR 13.7 million	September , 1988	Board approval of program.
SDR 13.7 million	On or after November 20, 1988	Compliance with quantitative performance criteria as of September 30, 1988.
SDR 13.7 million	On or after February 20, 1989	Compliance with quantitative performance criteria as of December 31, 1988.
SDR 13.7 million	On or after May 20, 1989	Compliance with quantitative performance criteria as of March 31, 1989 and completion of program review.
SDR 13.7 million	On or after August 20, 1989	Compliance with quantitative performance criteria as of June 30, 1989.
SDR 13.5 million	On or after November 20, 1989	Compliance with quantitative performance criteria as of September 30, 1989

1/ Other than generally applicable conditions under the arrangement and nonquantitative performance criteria (including the performance clause on the exchange and trade system).

Jamaica: Summary of the 1988/89 Economic Program 1/

I. Main Objectives

1. External current account deficit to decline to 3.1 percent of GDP (from 4.5 percent in 1987/88).
2. Net international reserves to increase by US\$180 million.
3. Real GDP growth of 4 to 5 percent (5.5 percent in 1987/88).
4. Average inflation rate not to exceed 7 percent (same as previous year).

II. Main Assumptions

1. Weighted average inflation rate for trading partners of about 7 percent.
2. Average oil import price (c.i.f.) to decline to US\$17 per barrel (US\$17.5 the previous year).
3. Number of tourist stopover arrivals to increase by 6 percent.
4. Average price of alumina to increase by 7.4 percent.
5. Paris Club creditors to provide refinancing for US\$61 million.
6. Expansion of broad money of 17 percent (21 percent in 1987/88).

III. Principal Elements and Policies

1. Public finances

- a. Capital expenditure of the Central Government to increase by 18 percent (26 percent in 1987/88) and that of the public enterprises to increase by 23 percent (20 percent in 1987/88).
- b. Overall public sector deficit to decline to 2.8 percent of GDP (from 5.4 percent the previous year).
- c. Proceeds of divestment of public enterprises of about J\$340 million (1.8 percent of GDP).

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1/ A summary of projections for selected economic and financial indicators is provided in Attachment III.



- d. General consumption tax of the value-added type to be introduced by April 1989.
- e. The accounting, cash management and financial reporting systems to be improved in the context of the Government's administrative reform program.

2. Monetary policy

- a. Increase in bank credit to the private sector to be contained to 23 percent (35 percent in 1987/88).
- b. Flexible management of interest rates.
- c. Floor on interest rates on savings deposits to be changed from time to time in light of developments in the auction of Bank of Jamaica CDs or government treasury bills.
- d. Continuation of financial sector reform program to improve the operations of nonbank financial institutions and expand the market for private debt instruments.

3. Incomes policies

- a. Extension through March 1989 of the 10 percent wage guideline.
- b. Scope of price controls not to be increased.
- c. Government's review of the price and subsidy scheme of the Jamaica Commodity Trading Corporation to be completed before March 1989.

4. External sector policies

- a. Dutch auction system for foreign exchange to be maintained.
- b. Exchange rate action to be triggered whenever the average real effective exchange rate for the previous three months indicates an appreciation of the Jamaica dollar of more than 5 percent over the level of June 1988.
- c. Supply of foreign exchange in the auction to be reduced if there was underperformance under the floor on net international reserves in the previous quarter. Reduced supply would cause the Jamaica dollar to depreciate.
- d. Exchange controls liberalized on August 8 by doubling the allowance for certain foreign travel, the limit on certain remittances abroad, and the limit on cash gifts abroad.

- e. The 7.5 percent duty rebate for exports of manufactured goods to be eliminated by April, 1989 in connection with the introduction of the general consumption tax.

Jamaica--Stand-By Arrangement

Attached hereto is a letter, with annexed Technical Memorandum of Understanding, dated August 22, 1988 from the Prime Minister and Minister of Finance and the Governor of the Bank of Jamaica requesting a stand-by arrangement and setting forth:

(a) the objectives, policies, and measures that the authorities of Jamaica intend to pursue for the period of this stand-by arrangement; and

(b) understandings of Jamaica with the Fund regarding a review that will be made of progress in realizing the objectives of the program and of the policies and measures that the authorities of Jamaica will pursue for the period of this stand-by arrangement after March 31, 1989.

To support these objectives and policies the International Monetary Fund grants this stand-by arrangement in accordance with the following provisions:

1. For the period from September --, 1988 to November 30, 1989 Jamaica will have the right to make purchases from the Fund in an amount equivalent to SDR 82 million, subject to paragraphs 2, 3, 4, 5, and 6 below, without further review by the Fund.

2. (a) Purchases under this stand-by arrangement shall not, without the consent of the Fund, exceed the equivalent of SDR 13.7 million until November 20, 1988, the equivalent of SDR 27.4 million until February 20, 1989, the equivalent of SDR 41.1 million until May 20, 1989, the equivalent of SDR 54.8 million until August 20, 1989, and the equivalent of SDR 68.4 million until November 20, 1989.

(b) None of the limits in (a) above shall apply to a purchase under this stand-by arrangement that would not increase the

Fund's holdings of Jamaica's currency in the credit tranches beyond 25 percent of quota or increase the Fund's holdings of that currency resulting from purchases of borrowed resources beyond 12.5 percent of quota.

3. Purchases under this stand-by arrangement shall be made from ordinary and borrowed resources in the ratio of 1 to 2, provided that any modification by the Fund of the proportions of ordinary and borrowed resources shall apply to amounts that may be purchased after the date of modification.

4. Jamaica will not make purchases under this stand-by arrangement that would increase the Fund's holdings of Jamaica's currency in the credit tranches beyond 25 percent of quota or increase the Fund's holdings of that currency resulting from purchases of borrowed resources beyond 12.5 percent of quota:

(a) during any period in which the data at the end of the preceding quarter indicate that

(i) the ceiling on the financing requirement of the overall public sector described in paragraph 2 of the Technical Memorandum of Understanding annexed to the attached letter, or

(ii) the ceiling on the financing requirement of the Central Government including the losses of the Bank of Jamaica as described in paragraph 3 of the Technical Memorandum of Understanding annexed to the attached letter, or

(iii) the intention not to incur external payment arrears, as described and defined in paragraphs 4 and 5 of the Technical Memorandum of Understanding annexed to the attached letter, or

(iv) the ceiling on the stock of net domestic assets of the Bank of Jamaica as described in paragraph 6 of the Technical Memorandum of Understanding annexed to the attached letter, or

(v) the target for the net international reserve position of the Bank of Jamaica as described in paragraph 7 of the Technical Memorandum of Understanding annexed to the attached letter, or

(vi) the ceiling on increases in the stock of medium- and long-term external debt of the public sector described in paragraph 8 of the Technical Memorandum of Understanding annexed to the attached letter, or

(vii) the ceiling on gross disbursements of external debt of the public sector with an original maturity range of between one to five years described in paragraph 8 of the Technical Memorandum of Understanding annexed to the attached letter, or

(viii) the ceiling on the stock of short-term external debt of the public sector as described in paragraph 9 of the Technical Memorandum of Understanding annexed to the attached letter,

is not observed; or

(b) if Jamaica fails to implement the understandings on exchange rate measures as contemplated in paragraphs 10 and 11 of the Technical Memorandum of Understanding annexed to the attached letter; or

(c) during any period after April 30, 1989, until the review contemplated in paragraph 23 of the attached letter has been completed and suitable performance criteria for the remaining period of the arrangement after March 31, 1989 have been established, or after such performance criteria have been established, while they are not being observed; or

(e) during the entire period of this stand-by arrangement if Jamaica:

(i) imposes or intensifies restrictions on payments and transfers for current international transactions, or

(ii) introduces new multiple currency practices, or

(iii) concludes bilateral payments agreements which are inconsistent with Article VIII, or

(iv) imposes or intensifies import restrictions for balance of payments reasons.

When Jamaica is prevented from purchasing under this stand-by arrangement because of this paragraph 4, purchases will be resumed only after consultation has taken place between the Fund and Jamaica and understandings have been reached regarding the circumstances in which such purchases can be resumed.

5. Jamaica will not make purchases under this stand-by arrangement during any period of the arrangement in which Jamaica has an overdue financial obligation to the Fund or is failing to meet a repurchase expectation pursuant to the Guidelines on Corrective Action with respect to a noncomplying purchase.

6. Jamaica's right to engage in the transactions covered by this stand-by arrangement can be suspended only with respect to requests received by the Fund after (a) a formal ineligibility, or (b) a decision of the Executive Board to suspend transactions, either generally or in order to consider a proposal, made by an Executive Director or the Managing Director, formally to suppress or to limit the eligibility of Jamaica. When notice of a decision of formal ineligibility or of a decision to consider a proposal is given pursuant to this paragraph 6, purchases under this arrangement will be resumed only after consultation has taken place between the Fund and Jamaica and understandings have been reached regarding the circumstances in which such purchases can be resumed.

7. Purchases under this stand-by arrangement shall be made in the currencies of other members selected in accordance with the policies and procedures of the Fund, and may be made in SDRs if, on the request of Jamaica, the Fund agrees to provide them at the time of the purchase.

8. The value date for purchases under this stand-by arrangement involving borrowed resources will be determined in accordance with Rule G-4 (b) of the Fund's Rules and Regulations. Jamaica will consult the Fund on the timing of purchases involving borrowed resources in accordance with Rule G-4(d).

9. Jamaica shall pay a charge for this stand-by arrangement in accordance with the decisions of the Fund.

10. (a) Jamaica shall repurchase the outstanding amount of its currency that results from a purchase under this stand-by arrangement in accordance with the provisions of the Articles of Agreement and decisions of the Fund, including those relating to repurchases as Jamaica's balance of payments and reserve position improves.

(b) Any reductions in Jamaica's currency held by the Fund shall reduce the amounts subject to repurchase under (a) above in accordance with the principles applied by the Fund for this purpose at the time of the reduction.

(c) The value date of a repurchase in respect of a purchase financed with borrowed resources under this stand-by arrangement will be normally either the 6th day or the 22nd day of the month, or the next business day if the selected day is not a business day, provided that repurchase will be completed not later than seven years from the date of purchase.

11. During the period of the stand-by arrangement Jamaica shall remain in close consultation with the Fund. These consultations may include correspondence and visits of officials of the Fund to Jamaica or of representatives of Jamaica to the Fund. Jamaica shall provide the Fund, through reports at intervals or dates requested by the Fund, with such information as the Fund requests in connection with the progress of Jamaica in achieving the objectives and policies set forth in the attached letter and annexed technical memorandum of understanding.

12. In accordance with paragraph 23 of the attached letter Jamaica will consult the Fund on the adoption of any measures that may be appropriate at the initiative of the Government or whenever the Managing Director requests consultation because any of the criteria in paragraph 4 above have not been observed or because he considers that consultation on the program is desirable. In addition, after the period of the arrangement and while Jamaica has outstanding purchases in the upper credit tranches, the Government will consult with the Fund from time to time, at the initiative of the Government or at the request of the Managing Director, concerning Jamaica's balance of payments policies.

Kingston, Jamaica  
August 22, 1988

Mr. Michel Camdessus  
Managing Director  
International Monetary Fund  
700 19th Street, N.W.  
Washington, D.C. 20431

Dear Mr. Camdessus:

1. The Government of Jamaica hereby requests from the International Monetary Fund a 14-month stand-by arrangement, in an amount of SDR 82 million, in support of an economic program covering Jamaica's fiscal year beginning April 1, 1988. This program is consistent with the objectives of the Government's medium-term development program which covers the period 1988/89-1990/91.

2. Since the mid-1980s, the Government of Jamaica has been implementing wide ranging demand-management and supply-oriented measures to reduce economic and financial imbalances and to restructure the economy. Financial policies have focused on reducing the public sector deficit and raising private savings, while structural reforms have aimed at improving the conditions for export-led growth. A key element in these reforms was the evolution of the foreign exchange system from one based on a fixed exchange rate, under which the Jamaica dollar had become overvalued, to the present auction system. Since the adoption of the auction system, the Jamaica dollar has depreciated to the level of J\$5.5 per U.S. dollar, where it has remained stable in nominal terms for the last three years without loss of external competitiveness. This change in the foreign exchange regime was complemented by a significant liberalization of the import licensing system, an increase in limits for certain remittances, and the delegation of exchange control authority for all current transactions to commercial banks.

3. In the fiscal area, in the last two years the personal income tax was revised by unifying various marginal rates into a single tax rate of 33 1/3 percent, increasing the tax threshold, and broadening the tax base. The corporate tax rate was reduced to 33 1/3 percent and investment and depreciation allowances were adjusted. The resulting system of direct taxation is now more equitable, easier to administer, and more efficient in terms of revenue yields. In addition, a reform of the customs tariff regime has been initiated with the objective of establishing within four to five years a tariff system comprising four rates in the range of 5 to 30 percent. A new computer evaluation system has been introduced at all major ports of entry with a view to effecting improvements in customs assessment and collections. Inland revenue collections also have been improved by administrative changes involving the application of modern computer techniques and the recruitment and

training of revenue agents. On the expenditure side, the Government has contained the growth of recurrent expenditure and has started a major effort to improve the quality of the public investment program in terms of its preparation, execution, and monitoring. At the same time, the operations of the public enterprises have been made more efficient through restructuring, a more flexible management of tariffs and charges, and divestment of various entities to the private sector.

4. As a complement to fiscal restraint, the management of credit and monetary policy in recent years has aimed at a greater mobilization of financial savings and an improvement in the efficiency of financial intermediation. Financial savings have increased sharply in part as a result of a rise in real interest rates, which have become significantly positive. Moreover, the reform of the financial sector, which was initiated by the Government in 1986, has improved the allocation of financial savings between the public and private sectors and the control of the Bank of Jamaica over credit aggregates. This reform involved the gradual elimination of the liquid assets requirement for commercial banks and nonbanks, the introduction of remuneration on a part of the required cash reserves, and increased reliance on open market operations as an instrument of monetary and credit control.

5. In 1986/87 and 1987/88 the Jamaican economy made considerable progress toward sustained recovery under the impact of strong growth of merchandise exports, export-related investment and an expansion in tourism. This process was aided by favorable external developments in oil and alumina prices and continued efforts to reduce fiscal imbalances and improve external competitiveness. These efforts were framed in a program supported by a 15-month stand-by arrangement from the Fund in an amount of SDR 85 million under which Jamaica made all purchases as scheduled. Following two years of decline, real GDP expanded by about 4 percent in 1986/87 and by an estimated 5 1/2 percent in 1987/88, with the rate of unemployment declining and the average annual rate of inflation falling from 24 percent in 1985/86 to around 7 percent in 1987/88. Public sector capital expenditure is estimated to have increased by 20 percent in 1987/88, which was facilitated by a significant improvement in public savings and by proceeds from the divestment of public assets. The overall public sector deficit (including the losses of the Bank of Jamaica) was reduced from 13 percent of GDP in 1985/86 to about 5 1/2 percent of GDP in 1987/88.

6. The current account deficit of the balance of payments, which had fallen from about 11 percent of GDP in 1985/86 to about 3 percent of GDP in 1986/87, partly reflecting favorable oil price developments, widened again to about 4 1/2 percent in 1987/88. This latter development was largely the consequence of a rapid recovery in private sector economic activity, which was accompanied by a sharp expansion in credit and imports and coincided with a partial reversal of the aforementioned favorable oil price development. The larger current account deficit was financed by private capital inflows (including the proceeds from the divestment of the public assets mentioned above) which also



allowed for an improvement in the net international reserves of the Bank of Jamaica of US\$179 million in line with the objectives of the stand-by arrangement.

7. The Government of Jamaica has adopted a medium-term economic program (1988/89-1990/91) which is designed to promote sustained economic growth, while reducing Jamaica's debt service burden through further improvements in the overall fiscal position and export performance. This program has been endorsed by the World Bank and served as the basis for requesting financial assistance from bilateral and multilateral donor agencies participating in the World Bank's Caribbean Group for Cooperation in Economic Development. Real economic growth is targeted at about 3 1/2 to 4 percent per year, while the ratio of external debt to GDP has been projected to fall from 142 percent at end-1987/88 to 99 percent at end-1992/93 and the ratio of external debt service payments (after rescheduling) to exports of goods and nonfactor services would decline from 44 percent to 31 percent. Consistent with these targets, the external current account deficit (including grants) would decline from the equivalent of around 4 1/2 percent of GDP in 1987/88 to 1 percent of GDP by 1992/93.

8. The Government's medium-term economic program also seeks to improve the delivery of essential social services through increased public investment in the upgrading and expansion of infrastructure facilities for health, nutrition, education, employment, housing and water supply (Social Well-Being Program). The Government will make annual revisions of the program in the light of developments in the public finances and the availability of grants and concessional loans for social projects.

9. In line with the targets of the medium-term program, the Government intends to lower the external current account deficit (inclusive of grants) to the equivalent of 3.1 percent of GDP in 1988/89 (4.9 percent of GDP excluding grants). This target will be achieved through restrained fiscal and monetary policies which are aimed at moderating the growth in domestic expenditure and maintaining Jamaica's average rate of inflation (around 7 percent) in line with that of its trading partners in order to preserve a stable exchange rate for the Jamaica dollar in terms of the U.S. dollar.

10. The overall public sector deficit (including Bank of Jamaica losses) is targeted to decline to around 3 percent of GDP in 1988/89. Government tax revenues are projected to rise by 14 percent in 1988/89, reflecting continued economic growth and the improvements in tax structure and administration described earlier. During 1988/89, the Government will complete a revision of the bauxite levy regime which is intended to make the tax simpler to administer and to provide greater incentives for increased production. Moreover, the Government is taking steps to introduce, by April 1989, a general consumption tax of the value-added type to replace the present array of excise duties, retail sales tax, and other indirect taxes.

11. The divestment of public enterprises is expected to generate public sector revenues of at least J\$340 million (around 2 percent of GDP) in 1988/89. These resources would be obtained from the sale of government-owned hotels to foreign and domestic investors and of shares in the telecommunications enterprise (TELECOM) which began to be divested last year. To help provide financing for prospective buyers of the hotels, a special fund of around US\$30 million is being established with the participation of the United States (OPIC), Germany (DEG) and the World Bank (IFC).

12. The Government intends to maintain strict control over public expenditure through careful monitoring of the warrant system. The execution of public investment projects will be managed flexibly within the limit on the overall public sector deficit mentioned above, depending on the availability of revenue and financing, in particular divestment proceeds. Further improvements in expenditure control and monitoring will result from the modernization and streamlining of the budget management system which the Government is carrying out under its administrative reform program (ARP). The second phase of this reform, which is being supported technically and financially by the World Bank, will involve the introduction of a more streamlined budgetary system, as well as integrated accounting, cash management and financial reporting systems.

13. In connection with its program to improve budget management, the Government has developed a three-year public sector investment program (PSIP) for 1988/89-1990/91, which incorporates the Social Well-Being Program mentioned earlier. This multi-year investment program has been fully integrated into the Government's annual budget exercise. In light of the higher recurrent costs that will be generated by the PSIP over the medium term, especially in the social sectors, the Government intends to contain the growth in other current outlays to ensure that the rate of growth in overall recurrent expenditure is in line with the desired improvement in government savings over the medium term.

14. Progress will continue to be made in improving the reporting and monitoring of fiscal and monetary transactions. The Government has already taken steps to develop a direct (conventional) measurement of the central government borrowing requirement and the Bank of Jamaica losses. By December 1988 the Government will resolve the remaining problems relating to the institutional coverage of public sector operations, the reporting of public entity operations, and the measurement of the overall public sector borrowing requirement.

15. Public enterprise operations will be strengthened through appropriate price policies and management. Prices of goods and services provided by the public sector will be adjusted as necessary to ensure the achievement of the fiscal objectives of the program. With a view to improving the financial position of the Jamaican Commodity Trading Corporation (JCTC) in 1989/90, the Government also intends to carry out

a thorough review of its price and subsidy schemes before the end of the current fiscal year. Price controls are in place for certain products, including basic foods, animal feed, lumber and medicines, but controlled prices of these items will be adjusted as necessary at the wholesale and retail levels to reflect increases in costs. The scope of price controls will not be increased during the program period.

16. In the area of monetary policy, the Bank of Jamaica will ensure that the growth of domestic bank credit is maintained on a path consistent with the achievement of the program's balance of payments targets. In line with the objective of relying more on market mechanisms, the Bank of Jamaica has recently changed its procedures for open market operations whereby the yield on certificates of deposit, which compete with other government paper and time deposits in the banking system, will be determined by an auction process. In addition, *the Bank of Jamaica has increased the frequency of its open market operations and has lowered the minimum denomination of the financial instruments used in those operations.* Also, the minimum rate on savings deposits will be adjusted from time to time in accordance with the trend of interest rates for other financial instruments. In the next phase of the Government's financial sector reform to begin this year, the Government will take steps to make further improvements in the operations of the nonbanks and to expand the market for private debt instruments.

17. The Government recognizes the usefulness of a wage guideline in containing cost increases in Jamaica. Therefore, it has decided that the norm limiting increases in the "wage fund" to no more than 10 per cent a year for contracts agreed after January 1, 1987, which was established in Ministry Paper No. 6 of January 8, 1987, will continue in effect through March 1989.

18. Consistent with the objectives of the medium-term program, Jamaica's external public debt (including obligations to the IMF) is expected to increase by around US\$20 million in 1988/89 and by a similar amount in 1989/90. Continued access to exceptional financing will be required during these two years because of large debt repayments falling due. In the case of foreign commercial bank debt, all principal obligations falling due in the period from April 1, 1985 through March 31, 1990 were rescheduled in March 1987. Under the aegis of the Paris Club, official bilateral creditors will be requested to reschedule *a significant portion of principal and interest obligations falling due* in the period starting June 1988 through the end of the stand-by arrangement, under terms similar to those granted for the previous rescheduling. The proposed new rescheduling, together with donor country assistance arranged through the Caribbean Group for Cooperation in Economic Development, is expected to be sufficient to cover Jamaica's external financing requirement for 1988/89.

19. In order to permit commercial creditors to manage more efficiently their claims against Jamaica, while providing incentives for direct foreign investment in the country, the Government has launched a

debt/equity conversion scheme under which indebtedness of up to some US\$30-40 million held by commercial banks could be converted into equity each year over the next several years. However, the pace of debt conversion will be phased over time in line with the projected capacity of the domestic market to absorb the local-currency debt instruments to be issued in connection with the retirement of foreign debt.

20. Financial policies have been designed with the aim of maintaining a stable exchange rate for the Jamaica dollar during the period covered by the stand-by arrangement, a goal which is broadly in line with the maintenance of Jamaica's current level of competitiveness. The Government is prepared to adjust the exchange rate for the Jamaica dollar if needed to maintain an adequate level of external competitiveness and to ensure compliance with the balance of payments targets of the program.

21. The allocation of foreign exchange through the existing auction system, which has wide acceptance within the Jamaican community, will continue in effect. The Bank of Jamaica will monitor closely the operations of the auction to ensure that all bona fide bids for foreign exchange at the auction are satisfied and that there are no undue delays in the delivery of foreign exchange. The multiple currency practice that may arise from the auction because of the use of the "Dutch" bidding system currently used, under which those who bid for foreign exchange are required to pay the bid price rather than the marginal price if their bids are accepted, was temporarily approved by the Fund through May 31, 1988, and the Government seeks extension of this approval through the end of April 1989.

22. The Government will further liberalize exchange controls as the economy returns to a pattern of self-sustained growth and balance of payments viability. Accordingly, effective September 1, 1988, the basic allowance for foreign travel, other than for business and professional reasons, will be raised from US\$150 a person for each calendar year to US\$300 a person for each calendar year. At the same time, the limit on remittance of income from emigrants' property and remittances for family maintenance will be raised from US\$1,000 per person per year to US\$2,000 per person per year, while that for cash gifts will be raised from US\$50 per person per year to US\$100. In addition, the duty rebate scheme for exports of manufactured goods, consisting of a rebate of 7.5 percent of the value of eligible exports, will be eliminated by April 1, 1989 with the implementation of the General Consumption Tax mentioned earlier.

23. The Government of Jamaica believes that the policies set out in the foregoing paragraphs and further elaborated in the annexed Technical Memorandum of Understanding are consistent with the objectives of Jamaica's economic program. The Government will periodically consult with the Fund, in accordance with the Fund's policies on such consultations, about the progress being made in the implementation of the program described above and about any policy adaptations considered appropriate for the achievement of its objectives. In any event, the

Government will complete a review with the Fund not later than April 30, 1989 on the progress made in implementing the policies described in this letter and accompanying annex and, if necessary, will reach understandings on any additional measures as may be needed. In this review, the Government also will reach understandings with the Fund on the quantitative performance criteria for the period of the arrangement beyond March 31, 1989.

Yours sincerely,

/s/

Headley Brown  
Governor  
Bank of Jamaica

/s/

Edward P.G. Seaga  
Prime Minister and  
Minister of Finance and Planning

Technical Memorandum of Understanding (August 22, 1988)

1. This Memorandum describes more specifically certain key targets and policy understandings of the letter of the Government of Jamaica dated August 22, 1988, regarding Jamaica's economic program for the period through September 1989. Targets for the period after March 31, 1989 will be quantified during the review of the program specified in paragraph 23 of that letter.

2. The financing requirement of the overall public sector, for periods starting on March 31, 1988, will not exceed J\$926 million as of March 31, 1989. This financing requirement will not exceed J\$777 million as of September 30, 1988, and will not exceed J\$1,138 million as of December 31, 1988. For the purpose of this memorandum the overall public sector comprises the Central Government, the local governments, the Capital Development Fund, the Bank of Jamaica, certain selected public sector entities specified in the Annex, and other public sector entities. The financing requirement is defined as the sum of foreign financing and domestic financing of the overall public sector. Foreign financing is defined as the sum of net official foreign borrowing (excluding tolling and the reduction in external debt of the public sector resulting from the conversion of debt into equity), external proceeds of divestment and the change in short-term net foreign liabilities of the selected public entities, minus the change in net official international reserves, all valued at the exchange rate prevailing at the time of the transaction. Domestic financing is defined as the sum of (i) the change in banking system liabilities to the private sector and to other financial institutions, minus the increases in bank credit to the private sector and to other financial institutions, and in the net foreign assets and net unclassified assets of the commercial banks; (ii) the change in net credit of the nonbank financial institutions to the public sector; (iii) the change in the holdings of public debt instruments by the nonfinancial private sector, excluding government paper issued or credit extended to convert external debt into equity; and (iv) domestic proceeds of divestment. Public debt instruments held by the nonfinancial private sector are defined to include any financial obligations of the public sector.

The ceilings on the overall public sector financing requirement will be changed as indicated below if the Government becomes a minority shareholder in the Telecommunications company (TELECOM) before October 31, 1988. In that event, as TELECOM will cease to be considered a part of the public sector, the financing requirement of the overall public sector for periods starting on March 31, 1988, will not exceed J\$772 million as of March 31, 1989 and will not exceed J\$1,095 million as of December 31, 1989. Also, the ceilings on the overall public sector financing requirement will be subject to downward (upward) adjustment for any shortfalls (excesses) from the projected levels of disbursements of project-related foreign loans as set out in attached Table 1 (modified as indicated in the Table in the event that TELECOM ceases to be considered part of the public sector). At any test date,

the upward adjustment to the ceiling on the public sector financing requirement may not exceed by more than US\$10 million (or its Jamaica dollar equivalent) the projected level of project-related foreign loan disbursements.

3. The financing requirement of the Central Government, including the losses of the Bank of Jamaica, for periods starting on March 31, 1988, will not exceed J\$1,157 million as of March 31, 1989. This financing requirement will not exceed J\$1,027 million as of September 30, 1988, and will not exceed J\$1,407 million as of December 31, 1988 (Table 2). For the purpose of this paragraph, the financing requirement is defined to be the sum of net foreign borrowing of the Central Government (excluding tolling and the reduction in external debt of the Central Government resulting from the conversion of debt into equity) valued at the exchange rate prevailing at the time of the transactions, the external proceeds of divestment accruing to the Central Government and domestic financing of the Central Government. Domestic financing is defined as the sum of (i) the change in net credit to the Central Government from the banking system (including the losses of the Bank of Jamaica); (ii) the change in net credit to the Central Government from other financial institutions; (iii) the change in the holdings of public debt instruments by the nonfinancial private sector and public sector entities; and (iv) the domestic proceeds of divestment accruing to the Central Government. Government paper issued to convert external debt into equity will be excluded from the measure of domestic financing. The ceilings on the central government financing requirement, including the losses of the Bank of Jamaica, will be subject to downward (upward) adjustment for any shortfalls (excesses) from the projected levels of disbursements of project-related foreign loans as set out in Table 2. <sup>1/</sup>

4. The Central Government, the Bank of Jamaica and all other public sector entities will not incur any domestic or external payment arrears during the period of the stand-by arrangement. Domestic arrears are defined to include: a) checks which have been issued by the spending departments of the Central Government to residents and not released for payment within seven working days by the Accountant General; and b) a shortfall of payments by the Central Government and the Selected Public Entities into their respective earmarked accounts for external debt service payments. Arrears arise when the domestic counterpart of the full amount of the external debt service before rescheduling is not paid on the due date into these specified accounts. The measurement of domestic arrears related to external debt service payments will be reported monthly based on a debt service inventory that is classified

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<sup>1/</sup> In order to improve the statistical information available for conducting open market operations of the Bank of Jamaica, the Central Government will provide monthly reports on the following indicators of budget execution: warrants issued, expenditure committed, checks issued, and checks cashed.

according to obligations of the Central Government, the Bank of Jamaica, the Selected Public Entities and the other public sector entities.

5. External payment arrears are defined as all unpaid obligations vis-a-vis nonresidents (including overdue obligations of the Bank of Jamaica, the Central Government, and other public sector entities) and arrears in the foreign exchange auction system. Up to November 15, 1988 external payment arrears exclude the proposed refinancing of debt vis-a-vis Paris Club creditor countries specified in Table 3; the latter has been derived under the assumption that eligible payments will be rescheduled according to an Agreed Minute prior to November 15, 1988 on terms equivalent to those obtained under the rescheduling agreement with Paris Club creditors of March 1987. Overdue replenishment obligations by the Bank of Jamaica to the EDF also will be considered arrears. "Undue delays" arise when payments are made more than seven banking days beyond the date on which payments are due. Regarding debt service payments on external public debt, arrears in the external settlement of debt service will be identified on the basis of a comparison of the detailed debt service inventory mentioned earlier with the actual debt service payments recorded in the foreign exchange cash flow statement. Arrears in the foreign exchange auction system are defined by the difference between the stock of local currency deposits in the auction system on the last working day of each month and the cumulative value of successful bids in the previous four auctions. 1/

6. The stock of the net domestic assets of the Bank of Jamaica will not exceed J\$5,070 million on September 30, 1988; J\$5,050 million on December 31, 1988; and J\$4,385 million on March 31, 1989 (Table 4). These ceilings will be subject to downward adjustments for any cumulative excess of net external debt disbursements as specified in paragraph 8 below. For the purpose of this paragraph, the stock of the net domestic assets of the Bank of Jamaica is defined as the difference between (i) base money (i.e., the cash reserve and current account of the commercial banks at the Bank of Jamaica, plus currency issue, minus the currency holdings of the Bank of Jamaica); and (ii) the stock of net international reserves of the Bank of Jamaica as defined in paragraph 7 below. For the purpose of this paragraph, all foreign assets and liabilities, except those denominated in Special Drawing Rights (SDRs), will be converted into Jamaica dollars at the accounting rate of US\$1.00 = J\$5.50. Foreign assets and liabilities denominated in special drawing rights (SDRs) will be converted into Jamaica dollars at the accounting rate of SDR 1 = J\$7.629.

7. The net international reserve position of the Bank of Jamaica, which was negative US\$465 million on March 31, 1988, will not be less than: negative US\$437 million on September 30, 1988; negative US\$401

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1/ When a regularly scheduled auction does not occur because of a holiday, the number of auctions to be included in the arrears test would be reduced accordingly.



million on December 31, 1988; and negative US\$285 million on March 31, 1989 (Table 5). These net international reserve targets will be subject to upward adjustment for any cumulative excess over the projected net external debt disbursements specified in paragraph 8.

Foreign reserve assets of the Bank of Jamaica are defined to exclude the foreign assets of the Government of Jamaica and the foreign assets of the Export Development Fund. All foreign assets acquired in the form of swaps from foreign and domestic entities will be excluded from the foreign assets of the Bank of Jamaica. Swaps are defined as reversible purchases of foreign assets in exchange for domestic currency or obligations.

Foreign reserve liabilities of the Bank of Jamaica are defined to include (i) promissory notes related to prepayment of exports; (ii) any new borrowing by the Central Government, Bank of Jamaica, or any public sector entity with a maturity of less than one year not directly related to imports; and (iii) external payments arrears. All reserve liabilities shown in the attached Table 5 will continue to be treated as such, irrespective of any change in maturity. All assets and liabilities in SDRs will be converted into U.S. dollars at the accounting rate of SDR 1 = US\$1.387. Assets and liabilities in foreign currencies will be converted into U.S. dollars at cross exchange rates prevailing on March 31, 1988.

8. Any increase in the stock of medium- and long-term external debt of the public sector (defined as consisting of the central government, local governments, the group of selected public sector entities, any other public sector entity, the Bank of Jamaica, and the private sector with a government guarantee) from the level on March 31, 1988 in excess of US\$28 million as of September 30, 1988; US\$55 million as of December 31, 1988; and US\$37 million as of March 31, 1989 will lead to offsetting adjustments in the net domestic asset ceilings and the net international reserve targets described in paragraphs 6 and 7 above. Furthermore, the increase in this stock will not exceed a maximum of US\$38 million as of September 30, 1988; US\$65 million as of December 31, 1988; and US\$47 million as of March 31, 1989. Any reduction in the stock of medium- and long-term external debt of the public sector resulting from the conversion of debt into equity will be excluded from the measurement of debt flows under these ceilings. The gross disbursement of external debt of the public sector with an original maturity range of between 1-5 years, for periods starting on March 31, 1988, will not exceed US\$71 million as of September 30, 1988; US\$114 million as of December 31, 1988; and US\$158 million as of March 31, 1989. All projected changes in the stock of medium- and long-term external debt are set out in Table 3. For the purpose of these ceilings, the definition of debt (i) will exclude foreign reserve liabilities of the Bank of Jamaica; (ii) will exclude gross inflows during the program period associated with project financing by multilateral and other official development agencies; (iii) will include the repayment of arrears on debt; and (iv) will include disbursements

from the United States Economic Support Fund. External debt transactions will be expressed in U.S. dollars, with conversions from other currencies effected at the exchange rates prevailing when the loan is disbursed.

9. The stock of short-term external debt of the public sector, which was US\$97 million as of March 31, 1988, will not exceed that level at the end of any subsequent quarter through March 31, 1989. If TELECOM ceases to be considered as part of the public sector as described above in paragraph 2 above, only its publicly guaranteed short-term debt will be included in the stock of short term external debt of the public sector as of December 31, 1988 and March 31, 1989 (Table 6). Short-term debt is defined as trade and suppliers' credits with original maturities of less than one year.

10. In the event that the net international reserve (NIR) target during any program period is not attained for reasons other than a temporary shortfall in ESF or IBRD-SECAL disbursements that is reversible within the program period, the Bank of Jamaica will increase its net retentions from the foreign exchange auction market during the following quarter above previously programmed levels in order to facilitate attainment of the NIR target for that quarter. This increase in retentions is expected to trigger a depreciation of the Jamaica dollar that would strengthen the performance of the overall balance of payments.

11. During the program period, the exchange rate of the Jamaica dollar vis-a-vis the U.S. dollar will be adjusted as necessary; during the period through end-May 1989, whenever the average index of the real effective exchange rate of the Jamaica dollar for the most recent three-month period indicates a cumulative appreciation from the level of June 1988 of more than 5 percent, the domestic currency will be depreciated by that amount, within a period of no more than four foreign exchange auctions. The measure of the real effective exchange rate will be based on the index monitored by the Information Notice System of the Fund.

Table 1. Jamaica: Summary Public Sector Operations, 1987/88 and 1988/89

(In millions of Jamaica dollars, cumulative)

	1987/88	1988/89 1/					
		March 31, 1988- Sept. 30, 1988	March 31, 1988- Dec. 31, 1988	March 31, 1988- Dec. 31, 1988	March 31, 1988- Dec. 31, 1988	March 31, 1988- March 31, 1989	March 31, 1988- March 31, 1989
Overall balance	-1,385.0	-776.5	(-777.1)	-1,138.1	(-1,095.3)	-925.5	(-771.9)
Central Government 2/ 3/	-391.1	-628.5	(-628.5)	-812.6	(-812.6)	-333.9	(-333.9)
Bank of Jamaica	-875.4	-398.5	(-398.5)	-594.8	(-594.8)	-823.3	(-823.3)
Public entities 2/	334.6	259.2	(258.7)	305.7	(348.5)	289.2	(442.8)
Other public sector on- lending to the private sector	-186.6 4/	-22.8	(-22.8)	-34.2	(-34.2)	-45.4	(-45.4)
Other	-266.5	14.1	(14.1)	-2.2	(-2.2)	-12.1	(-12.1)
Overall financing requirement	1,385.0	776.5	(777.1)	1,138.1	(1,095.3)	925.5	(771.9)
Foreign 5/	314.4	283.9	(34.7)	545.3	(308.2)	282.7	(34.3)
Net official capital	1,033.4	437.4	(188.2)	897.9	(660.8)	1,083.5	(835.1)
Change in reserves	-1,036.8	-153.5	(-153.5)	-352.6	(-352.6)	-990.0	(-990.0)
Divestment proceeds	347.8	--	(--)	--	(--)	189.2	(189.2)
Domestic 5/	1,070.6	492.6	(742.4)	592.8	(787.1)	642.8	(737.6)
Banking system	581.7	79.1	(...)	76.7	(...)	139.1	(...)
Divestment proceeds	88.0	--	(--)	100.0	(100.0)	147.3	(147.3)
Other	400.5	413.5	(...)	416.1	(...)	356.4	(...)
Memorandum items							
Disbursement of foreign project loans	594.2	385.0	(375.0)	594.0	(579.4)	804.1	(762.8)
Debt-equity conversion	14.2	11.5	(11.5)	81.4	(81.4)	176.0	(176.0)

1/ Figures between parentheses exclude the transactions of the telecommunications company (TELECOM).

2/ Excludes divestment proceeds.

3/ Revenue does not include bauxite levy proceeds earmarked for amortization of foreign debt (colling arrangement).

4/ Includes on-lending to the Caribbean Cement Company that was privatized in June 1987.

5/ Excludes the reduction in foreign debt and the increase in domestic debt associated with the conversion of foreign debt into equity.

Table 2. Jamaica: Summary of Central Government Operations, 1987/88 and 1988/89

(In millions of Jamaica dollars, cumulative)

	1987/88	1988/89		
		March 31, 1988- Sept. 30, 1988	March 31, 1988- Dec. 31, 1988	March 31, 1988- March 31, 1989
Total revenue	5,117.8	2,554.3	3,928.5	5,946.7
Tax revenue	4,323.6	2,240.8	3,418.5	4,929.5
Nontax revenue	203.2	60.1	137.6	221.0
Bauxite levy	269.0	150.0	210.0	360.8
Capital revenue (including grants)	322.0	103.4	162.4	435.4
Total expenditure	5,508.9	3,182.8	4,741.1	6,280.6
Current expenditure	4,189.3	2,394.6	3,571.9	4,708.8
Capital expenditure	1,319.6	788.2	1,169.2	1,571.8
Of which: on-lending to the private sector	156.5	73.7	134.7	201.8
Overall balance	-391.1	-628.5	-812.6	-333.9
Financing requirement	391.1	628.5	812.6	333.9
<u>Memorandum items:</u>				
<u>Financing of on-lending</u>				
to the private sector	156.5	73.7	134.7	201.8
Net foreign disbursements	32.8	20.0	30.0	40.0
Gross disbursements	114.1	70.0	105.0	140.0
Amortization	81.3	50.0	75.0	100.0
Domestic financing	123.7	53.7	104.7	161.8
<u>Financing requirement of the Central Government, including the losses of the Bank of Jamaica</u>				
	1,266.5	1,027.0	1,407.4	1,157.2
Central Government	391.1	628.5	812.6	333.9
Bank of Jamaica	875.4	398.5	594.8	823.3
<u>Disbursement of foreign project loans</u>				
	298.3	254.1	375.1	486.2

Table 3. Jamaica: Cumulative Net Disbursement of Medium- and Long-Term External Debt, 1987/88 and 1988/89 <sup>1/</sup>

(In millions of U.S. dollars)

	March 31, 1987 March 31, 1988	March 31, 1988 Sept. 30, 1988	March 31, 1988 Dec. 31, 1988	March 31, 1988 March 31, 1989
<u>Inflows</u>	<u>532.4</u>	<u>260.2</u>	<u>401.2</u>	<u>508.1</u>
Bilateral	87.9	65.7	119.8	174.1
United States	67.3	48.0	71.1	93.2
Canada	7.7	4.0	7.0	10.0
United Kingdom	2.9	3.4	5.9	8.4
Germany	2.7	2.0	7.0	11.9
Japan	--	--	12.5	25.0
Other	7.3	8.3	16.3	25.6
Multilateral	69.7	--	13.5	32.0
World Bank	60.0	--	12.5	30.0
Other	9.7	--	1.0	2.0
Other	153.9	106.5	138.9	136.6
Rescheduling	220.9	88.0	129.0	165.4
<u>Outflows</u>	<u>-498.7</u>	<u>-232.7</u>	<u>-346.5</u>	<u>-471.2</u>
<u>Net disbursements</u>	<u>33.4</u>	<u>27.5</u>	<u>54.7</u>	<u>36.9</u>
<u>Memorandum item</u>				
Assumed refinancing	...	31.0	48.0	61.0

<sup>1/</sup> Excludes project-related financing. Includes debt of the private sector with public guarantee.

Table 4. Jamaica: Net Domestic Assets of the Bank of Jamaica  
1988/89

(In millions of Jamaica dollars)

	Actual 1988 March 31	Program		
		1988 Sept. 30	Dec. 31	1989 March 31
Net international reserves	-2,556	-2,403	-2,204	-1,566
Net domestic assets	5,049	5,070	5,050	4,385
Base money	2,493	2,667	2,846	2,819

Table 5. Jamaica: Net International Reserves of  
the Bank of Jamaica, 1988/89

(In millions of U.S. dollars)

	Actual 1988 March 31	Program		
		1988 Sept. 30	Dec. 31	1989 March 31
<u>Net international reserves</u>	<u>-464.9</u>	<u>-437.0</u>	<u>-400.8</u>	<u>-284.9</u>
<u>Assets</u>	<u>194.4</u>	<u>117.2</u>	<u>142.2</u>	<u>207.3</u>
Liquid	43.4	7.2	32.2	97.3
Nonliquid	151.0	110.0	110.0	110.0
<u>Liabilities</u>	<u>659.3</u>	<u>554.2</u>	<u>543.0</u>	<u>492.2</u>
IMF <sup>1/</sup>	617.8	523.8	516.6	470.8
Central Bank of Libya	28.0	24.0	20.0	20.0
Norway Consultancy Fund	0.4	0.4	0.4	0.4
Marubeni	9.0	6.0	6.0	1.0
CARICOM	4.1	--	--	--
Payment arrears	--	--	--	--

<sup>1/</sup> SDRs converted at the rate SDR 1 = US\$1.387.

Table 6. Jamaica: Stock of Short-Term External Public Debt, 1987/88

(In millions of U.S. dollars)

	At March 31, 1987	At March 31, 1988
<u>Total</u>	<u>79.96</u>	<u>96.93</u>
(Excluding Telecom)	(76.29)	(95.12)
Agricultural Credit Bank	--	--
Airports Authority of Jamaica	--	--
Air Jamaica Limited	0.70	0.20
F.I.D.C.O.	--	--
Jamaica Gypsum and Quarry	--	--
Jamaica Broadcasting Corporation	--	--
Jamaica Commodity Trading Corporation	12.95	31.45
Jamaica Public Service Company	--	--
Jamaica Sugar Holdings	0.18	--
Kingston Free Zone	--	--
Montego Bay Free Zone	--	--
National Investment Bank of Jamaica	0.07	1.54
National Water Commission	--	--
Petroleum Corporation of Jamaica/Petrojam	62.37	60.12
Port Authority	--	--
Sugar Industry Authority	--	--
Telecommunications of Jamaica (Telecom)	3.67	1.81
Urban Development Corporation	0.03	1.81



(Annex to Technical Memorandum of Understanding)

List of Selected Public Entities Monitored  
Under the Financial Program

1. Airports Authority of Jamaica
2. Air Jamaica Limited
3. Jamaica Broadcasting Corporation
4. Jamaica Commodity Trading Company Limited
5. Jamaica Merchant Marine Limited
6. Jamaica Mortgage Bank Limited
7. Jamaica Public Service Company Limited
8. Jamaica Railways Corporation
9. Jamaica Sugar Holdings Limited
10. National Hotels and Properties Limited
11. National Housing Corporation
12. National Investment Bank of Jamaica Limited
13. National Water Commission
14. Port Authority
15. Petroleum Corporation of Jamaica
16. Petrojam Limited
17. Sugar Industry Authority
18. Telecommunications of Jamaica (TELECOM)
19. Urban Development Corporation
20. Human Employment and Resources Training Trust
21. National Housing Trust
22. National Insurance Fund

