Analysis

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Jamaica

Macroeconomic Developments[1]

RATINGS ARE CONSTRAINED BY HIGH PUBLIC-SECTOR DEBT BURDEN

Despite the constraints imposed by the burden of a large public-sector debt, the Jamaican authorities continue to respond successfully to shocks in a challenging environment. The economy remained on a positive growth path in 2003 for the fifth year in a row. GDP growth for FY 2003/04 is estimated to have reached 2.2% buoyed, by strong growth in the country's main tradable sectors, bauxite/alumina and tourism. The authorities estimate that economic activity will continue to expand above 2% in the current fiscal year. Significant ongoing investments in mining and tourism combined with increasing worker remittances are expected to be the main factors sustaining growth momentum over the medium term.

By mid-2003, the authorities had successfully faced another speculative attack on the Jamaican dollar using all tools at their disposal, including interest rate hikes, use of international reserves, the fluctuation of the nominal exchange rate, and moral suasion from the Rt Honourable Prime Minister PJ Patterson. Although the pass-through from nominal devaluation to inflation has declined somewhat in the 1990s, it remains high in Jamaica. As a result, inflation for FY 2003/04 more than doubled from historical levels to about 16.5%, with year-end 2003 inflation at 14.1%. Increases in international agricultural commodity prices and new tax measures also contributed to push inflation to these levels. Inflation is expected to return to single-digit levels by the end of the current fiscal year.

The current strengthening of the exchange rate reflects an improvement in the credibility of fiscal policy. After reaching a peak of J$69.6 per US$ in May 2003 partly fuelled by expectations of fiscal slippage, the exchange rate has remained broadly stable at around J$60 per US$. The gradual easing of monetary policy has been reflected in the lowering of benchmark interest rates 15 times over a 12-month period, going from 35.95% in March 2003 to 17.95% in March 2004. For the Bank of Jamaica, open market interest rates are another sign of the return of investor confidence.

Nevertheless, the Jamaican economy remains vulnerable to adverse external shock, acts of nature, and shifts in investor confidence, particularly that of resident investors. While the government's room for policy maneuver remains limited, the authorities continue to demonstrate their commitment to make the necessary adjustments in the wake of negative shocks while servicing the public-sector debt in full and on timely basis. Nonetheless, the risk that the ongoing fiscal consolidation efforts could be destabilized with another severe combination of negative shocks remains.

1. *The Government's fiscal year runs from April 1st until March 31st.*

Politics/Social Developments

SOCIAL DIALOGUE WILL LIMIT PUBLIC WAGE EXPANSION

The government of Jamaica (GoJ) is led by the People's National Party (PNP), currently in an unprecedented fourth term in office. The PNP has a comfortable majority in Parliament with 34 seats while the opposition Jamaican Labor Party (JLP) holds the remaining 26. The next election is constitutionally due by October 2007. The GoJ and representatives of civil society are engaged in an ongoing dialogue to ensure fiscal sustainability with high growth and further reduction in poverty.

Within this framework, the GoJ and the Jamaican Confederation of Trade Unions (JCTU) signed a memorandum of understanding (MOU) agreeing to a two-year "wage restraint" from 1st of April 2004 until 31st of March 2006. Public-sector wages amounted to 12.1% of GDP and 64.5% of non-debt fiscal expenditures in FY 2003/04, down from 14% of GDP and 67.1% in FY 2002/03 respectively. Even in the face of recurrent negative shocks and ongoing fiscal consolidation, the government has increased the share of public spending devoted to critical sectors such as health and education, where the wage component is the highest. In addition to a wage cap, the MOU mandates employment restraint, curtailing of expenditures, the meeting of monetary and fiscal targets, and the development of an efficient public sector. The MOU is important because it overrides existing contracts between employers and workers and emphasizes that the unions are a major contributor to the social dialogue and that they are committed to the government's macroeconomic strategy.

Government Finance and Debt

GOVERNMENT MEETS FISCAL TARGETS IN FY 2003/04

The GoJ is striving to achieve a budget surplus by FY 2006/2007as a means to begin reducing its large debt burden. Its medium-term budget framework for FY 2004/2005 aims at cutting the overall central government deficit in the current fiscal year by almost half the 5.6% of GDP outturn in FY 2003/2004. The government has established the target of a balanced budget by next fiscal year and increasing surpluses in the years thereafter. These efforts at fiscal consolidation are to be accompanied by increasing the already sizeable primary surplus — 12.5% of GDP posted in FY 2003/2004.[2]

The authorities' fiscal response combines constant revenue efforts, rationalization, and containment of expenditures. Tax revenues in 2003 increased substantially above the expansion of nominal GDP. Tax revenues, which account for nearly 90% of total revenues on a calendar-year basis, increased by 28.4%, well above the 18.3% nominal increase in GDP. [3] The revenue-to-GDP ratio reached 28.7% of GDP, one of the highest in the region. According to Moody's own calculations, the tax elasticity to nominal output is about unity, after controlling for discretionary tax measures.

The higher increase in tax collection in FY 2003/2004 thus reflects a tax package enacted with the budget at the beginning of the last fiscal year. The tax package included tax-rate increases and a broadening of the tax base for consumption and import taxes in addition to further improvements in tax management. The package yields some 3% of GDP on an annual basis. For FY 2004/2005 the authorities plan to continue to improve efficiency in tax collection and tax administration to sustain the tax burden. Primary expenditures posted a nominal increase of only 4.2% in FY 2003/2004 while wages increased broadly in line with inflation[4]. The rationale for Jamaica's rating incorporates the expectation that, if needed, the GoJ will enact and implement additional revenue measures to minimize slippages from the fiscal consolidation targets.

Given the large weight of interest payments on the debt as a share of revenues as well as a share of expenditures, maneuverability is, and is likely to remain, very limited. Total interest payments on public debt (in J$ equivalent) represent 58% of total revenues, 67% of tax revenues and 49% of total expenditures. The authorities, however, continue to respond promptly and adequately to shocks to the budget in a constantly challenging domestic as well as external environment. The authorities' commitment to servicing the government's debt is highlighted by a sizeable primary surplus. Higher taxation and expenditure containment allowed the government to post a primary surplus equivalent to 70% of interest payments on public debt.

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2. *The authorities' fiscal targets are on fiscal year basis.*
3. *The results are broadly the same when looking at fiscal year basis. Tax revenue increased by 27.3% and nominal GDP by 16.6% in FY 2003/2004 compared with the previous fiscal year.*
4. *On calendar year basis, primary expenditure increased by 7.7% and wages increased slightly above inflation.*

DOMESTIC DEBT ROSE BY 14% IN FY 03/04

The overall nominal deficit of 5.6% of GDP posted by the GoJ in FY 2003/2004 was financed mostly in the domestic market.[5] At the end of March 2004, the stock of public-sector debt stood at J$693,885.6 million or 142.4% of GDP. This represents an increase of 15.4% over the stock at the end of March 2003. However, the rate of growth was slower than the 21% increase recorded in FY 2002/2003 compared with the previous fiscal year. The main factors accounting for the increase in FY 2003/2004 include the sharp depreciation of the exchange rate, the issuance of securities in lieu of interest payments on BoJ/FINSAC debt, assumption of enterprises debts, issuance of securities to cover BoJ losses, GoJ guarantees, and net issuance of bonds in domestic and international markets.

The domestic debt increased by 14% in FY 2003/2004. The foreign-currency component of the domestic debt increased while the share of medium- to long-term instruments declined, reflecting the issuance of shorter-term securities in response to market conditions. The increase in dollar-indexed bonds took place in the first half of the year in support of the BoJ efforts to stabilize the foreign exchange market. The main holders of GoJ securities remained the merchant banks, trust companies and brokers. Most of the new domestic debt issued in FY 2003/2004 was contracted at fixed exchange rates. Nearly 60% of the total domestic debt outstanding is at a fixed rate. New fixed-rate debt was issued for the fiscal year at an average rate of 29.7% compared with a projection of 16.95% that reflects the volatility in the foreign exchange market and a shift in resident investors' confidence.

At the end of March 2004, the stock of public and publicly guaranteed external debt stood at J$276,314.3 million ($4.5 billion) equivalent to 56.7% of GDP. The increase was due largely to the issuance of approximately $352 million in bonds in the regional and international capital markets, which exceeded gross amortization for the fiscal year and exchange-rate adjustments. The share of loans from official creditors has declined steadily while the share of bondholders has increased. Bonds issued in the international capital market represent a significant component of the external debt stock, accounting for 43.8% of the stock at the end of FY 2003/2004 compared to 38.6% at the end of FY 2002/2003. The US dollar remains the predominant currency in which external loans and bonds are denominated. The loans from official creditors were contracted at highly concessional interest rates with long tenures. The average interest rate on those loans ranged from 2% to 4%. The average interest rate on bonds was 10.79% in FY 2003/2004 declining marginally from the previous fiscal year. The external-debt portfolio remains predominantly long term. Of the total external debt outstanding at the end of FY 2003/2004, 24.5% had maturities up to 5 years and 23% had maturities in excess of 10 years.

PEER COMPARISON: JAMAICA GOVERNMENT DEBT RATIO BALANCED BY HIGH PRIMARY SURPLUS

The debt of the GoJ at nearly five times general government[6] revenues is one of the highest among the B-rated countries. Only Lebanon's is worse. Jamaica's ratio of general government debt to general government revenues is higher than lower B-rated countries such as Honduras, Bolivia, Dominican Republic and Uruguay. The ratio stood at nearly four times revenues for Honduras, about two and a half times for Bolivia, about three and a half times for Dominican Republic and just over four times for Uruguay. A combination of major currency, banking and debt crises sharply deteriorated the general government-debt-to-revenue ratio of the Dominican Republic and Uruguay in the recent past. Bolivia's ratio continues to deteriorate at a relatively rapid pace, reflecting a widening fiscal deficit that is increasingly being financed within the domestic market. Of this grouping, only Honduras' ratio has improved, partly reflecting external debt forgiveness. Jamaica's ratio has steadily deteriorated over the last five years, reflecting a number of factors, including exchange rate adjustments, assumption of debts of state-owned enterprises, and the cost of the rescue of the financial system in addition to the still-high overall fiscal deficit.

At about 7% of GDP,[7] Jamaica's general government fiscal deficit is somewhat in between Bolivia's 8.3% and Dominican Republic's 2.4%, and higher than Uruguay's 4.4% and Honduras' 5.5%. Because the country continues to run massive primary surpluses, Jamaica's deficit is explained by its high interest debt burden. The 12.5% of GDP primary surplus posted in FY 2003/2004[8] is about three times that of Brazil, and several times the primary surplus of most of the B-rated countries.

5. On a calendar-year basis, the deficit was 7.1% of GDP.

6. The subnational governments in Jamaica have no significant revenues of their own and their expenditures are covered nearly completely with transfers from the central government. The subnational governments have no outstanding debt of their own. The debt of the central administration includes guarantees and also includes about 30% of GDP equivalent as the cost of the financial sector rescue in 1997. Although the National Insurance Scheme (NIS) is not included, the ratio etc and after government please insert becasue the NIS has no cash deficit. The ratios calculated using fiscal data from the central administration are in the case of Jamaica a good approximation to the concept of general government.

7. On a calendar-year basis.

8. The primary surplus for calendar year 2003 was 10.1% of GDP.

External Vulnerability and Liquidity

WHILE COMPARATIVELY STRONG, KEY INDICATORS MAY DETERIORATE QUICKLY

The ability to sustain favorable external vulnerability and liquidity indicators continues to be a supporting factor for Jamaica's ratings. The ratio is highly sensitive to changes in the level of international reserves. This, in turn, depends on the authorities' access to international capital markets and the need to use reserves to defend the exchange rate. The external vulnerability indicator deteriorated in 2003 to 87.1% from a very comfortable ratio of 67.7% in 2001 and 79% in 2003, largely reflecting the defense of the currency in mid-2003. Current account earnings, driven mostly by worker remittances and tourism receipts, have begun to expand at a faster pace. In 2003, higher prices for aluminum and higher volume of mineral exports also contributed to the increase in current account earnings. Tourism arrivals have surpassed the pre-9/11 levels and per capita spending is increasing. Worker remittances, bauxite alumina exports and tourism receipts will be the drivers of current account earnings. FDI flows into the traditional tradable sectors will finance an important share of the still-high external current account deficit. The government intends to access the international capital market if conditions permit.

PEER COMPARISON: EVEN AS LIQUIDITY DETERIORATES, JAMAICA REMAINS STRONGER THAN PEERS

Liquidity and vulnerability indicators deteriorated in 2003 but remain better than other B-rated countries in the Caribbean region and in South America. Although the external vulnerability ratio of Jamaica increased in 2003, it is still below 100% of international reserves and the authorities are rebuilding reserves. A sustained improvement of the ratio in 2004 will fundamentally depend on the stability of the exchange rate. At 87.1% in 2003, the ratio compares well with that of the Dominican Republic's 741%, Bolivia at 167%, and Uruguay's 192%.

Jamaica's liquidity ratio (defined as short-term liabilities in BIS banks to total assets in BIS banks) has also deteriorated, albeit slightly. At 39.4%, the ratio compares well with that of B3-rated Dominican Republic, which reached 67.9% in 2003 and that of Bolivia, which reached 80%. Jamaica's debt service ratio, at about 10% of current account receipts, compares well to Bolivia's and Uruguay's debt service ratio of about 40% of current account receipt, but it is higher than the very low debt service ratio of the Dominican Republic, which remains under 5% of current account earnings. The total external debt to current account earnings of Jamaica remains under 100%, reflecting a combination of expanding current account earnings and a broadly stable level of public-sector debt at about $ 4.0 billion. The ratio compares well with that of Honduras, 146%, Bolivia, 236%, and Uruguay 338%. Jamaica's ratio is nearly twice as high as that of the Dominican Republic.

The ratio of total external debt[9] to total current account receipts for Jamaica fell to 93.7% in 2003 from 108.8% in 2003, reflecting a combination of higher current account receipts and a decline in the total stock of external debt at the end of calendar year 2003. The external debt statistics of Jamaica are not compiled in full agreement with the External Debt Guide for Compilers and Users, in the sense that they include foreign currency-denominated debt issued in international markets that is in the hands of residents. Anecdotal evidence indicates that at least half and as much as 75% of the nearly $2.0 billion in GoJ internationally issued bonds are held by residents. The total debt service ratio has also improved and remains under 20% of total current account earnings. Both ratios compare well with other B-rated countries in the Caribbean basin.

Rating History: Jamaica

Rating Action	Date	Foreign Currency Bonds and Notes Long-term	Foreign Currency Bank Deposits Long-term	Local Currency Government Bond Ratings Long-term
Rating Downgraded	May 27, 2003	B1	B2	Ba2
Review for Downgrade	April 17, 2003	Ba3	B1	Baa3
Assigned	March 30, 1998	Ba3	B1	Baa3

9. There are no official debt statistics for private sector external debt and short-debt. The total debt then includes figures from World Bank Global Development Finance statistics for those categories and Moody's own estimates. Both the external debt of the private sector and the short-term debt are small in relative and absolute terms. The bulk of the external debt is the public sector debt.

Related Research

Special Comments

Moody's Sovereign Ratings: A Ratings Guide, March 1999 (43788)

A Quantitative Model for Local Currency Government Bond Ratings, September 2003 (79404)

A Quantitative Model for Foreign Currency Government Bond Ratings, February, 2004 (81176)

Rating Methodology

Revised Country Ceiling Policy, June 2001 (67679)

To access any of these reports, click on the entry above. Note that these references are current as of the date of publication of this report and that more recent reports may be available. All research may not be available to all clients.

Jamaica

Report Date(s)	1998	1999	2000	2001	2002	2003	2004F
Economic Structure and Performance							
Nominal GDP (US$ Bil.)	7.5	7.5	7.6	7.8	8.0	7.3	7.6
Population (Mil.)	2.5	2.6	2.6	2.6	2.6	2.6	2.7
GDP per capita (US$)	2951.1	2936.5	2962.4	2998.7	3057.9	2768.1	2867.5
GDP per capita (PPP basis, US$)	3421.8	3481.2	3605.5	3754.3	3774.0	—	—
Nominal GDP (% change, local currency)	6.0	7.6	11.9	8.8	8.6	18.3	9.5
Real GDP (% change)	0.0	0.9	0.8	1.5	1.1	2.2	2.5
Inflation Rate (CPI, % change Dec/Dec)	7.9	6.8	6.1	8.7	7.3	14.1	7.0
Gross Investment/GDP (%)	26.2	24.4	27.0	29.8	33.2	27.6	27.8
Gross Domestic Saving/GDP (%)	14.8	16.8	14.8	11.2	9.5	9.6	9.3
Nominal Exports of G & S (% change, US$ basis)	7.1	1.9	6.3	-7.3	-3.0	-8.5	3.8
Nominal Imports of G & S (% change, US$ basis)	0.7	-1.9	12.0	4.2	6.0	-0.2	8.5
Openness of the Economy (%) [1]	93.7	93.3	100.5	97.8	97.2	102.8	104.9
Government Finance							
Gen. Gov. Revenue/GDP (%)	25.7	27.5	29.7	27.1	26.5	28.7	28.5
Gen. Gov. Expenditures/GDP (%)	32.2	33.0	29.9	32.3	34.8	33.9	32.4
Gen. Gov. Financial Balance/GDP (%)	-6.6	-5.5	-0.2	-5.2	-8.4	-7.1	-3.9
Gen. Gov. Primary Balance/GDP (%)	5.3	7.7	11.8	8.5	5.9	10.0	13.2
Gen. Gov. Direct Debt/GDP (%)	114.9	130.7	150.0	132.1	140.5	139.4	132.2
Gen. Gov. Direct Debt/Gen. Gov. Revenue (%)	432.0	439.5	499.6	487.2	531.0	485.4	463.6
Gen. Gov. Int. Pymt/Gen. Gov. Revenue (%)	46.2	47.7	40.5	50.5	54.2	59.8	59.0
Gen. Gov. FC & FC-indexed Debt/Gen. Gov. Debt (% only)				48.9	51.5	51.6	52.0
External Payments and Debt							
Current Account Balance (US$ Bil.)	-0.3	-0.2	-0.4	-0.8	-1.1	-1.0	-1.0
Current Account Balance/GDP (%)	-4.4	-2.9	-4.8	-9.8	-14.0	-13.7	-13.4
External Debt (US$ Bil.)	4.1	4.0	4.3	5.2	5.2	4.8	4.8
External Debt/GDP (%)	55.0	53.0	56.0	66.5	65.2	65.7	62.5
External Debt/CA Receipts (%) [2]	82.1	78.7	74.6	90.2	108.8	93.7	85.0
Net Foreign Direct Investment/GDP (%)	3.8	5.7	5.2	6.8	5.6	6.2	5.9
Official Forex Reserves (US$ Bil.)	0.7	0.6	1.1	1.9	1.6	1.3	1.3
Nominal Exchange Rate (local currency/US$)	37.1	41.3	45.4	47.3	50.8	59.8	—
Short-term External Debt/Total External Debt (%)	13.7	20.3	17.1	13.6	13.0	10.4	10.9
Interest Paid on External Debt (US$ Bil.)	0.3	0.3	0.3	0.4	0.4	0.4	0.4
Amortization Paid on External Debt (US$ Bil.)	0.5	0.5	0.3	0.4	0.5	0.5	0.6
Net Foreign Assets of Domestic Banks (US$ Bil.)	0.1	0.3	0.4	0.4	0.5	0.5	
Monetary, Vulnerability and Liquidity Indicators							
Domestic Credit (% change, Dec/Dec)	34.6	18.1	-1.8	-35.3	30.0	64.4	35.0
Domestic Credit/GDP (%)	37.2	40.9	35.8	21.3	25.5	35.5	38.0
M2/Official Forex Reserves (X)	4.4	5.7	3.1	1.8	2.2	2.6	3.0
Debt Service Ratio (%) [3]	15.0	14.5	10.3	12.4	18.8	17.4	16.0
External Vulnerability Indicator (%) [4]	156.0	223.1	105.9	67.7	79.0	87.1	82.3
International reserves	708.8	553.8	1053.6	1899.0	1644.2	1194.8	1300.0
Liquidity Ratio (%) [5]	46.0	65.8	42.7	39.1	33.6	39.4	—
"Dollarization" Ratio (%) [6]	25.5	25.3	26.7	28.1	30.2	31.6	33.1
"Dollarization" Vulnerability Indicator (%) [7]	67.8	69.1	53.4	34.8	41.9	45.8	48.4
M2 (% change, Dec/Dec)	7.7	12.2	13.0	8.6	12.0	10.5	11.0
Short-Term Nominal Interest Rate (%, Dec 31)	15.6	13.5	11.6	9.6	8.6	8.5	8.6
Total External Debt/Forex Reserves (%)	567.7	708.7	398.0	260.0	291.1	422.8	366.9
Total Liabilities due BIS Banks/Total Assets Held in BIS Banks (%)	48.2	56.1	47.4	44.2	48.5	50.9	—

Notes:
[1] Sum of Exports and Imports of Goods and Services/GDP (%)
[2] Current Account Receipts
[3] (Interest + Current-Year Repayment of Principal)/Current Account Receipts (%)
[4] (Short-Term External Debt + Currently Maturing Long-Term External Debt + Nonresident Foreign Currency Deposits Over One Year)/Official Foreign Exchange Reserves (%)
[5] Liabilities to BIS Banks Falling Due Within One Year/Total Assets Held in BIS Banks (%)
[6] Total Foreign Currency Deposits in the Domestic Banking System/Total Deposits in the Domestic Banking System (%)
[7] Total Foreign Currency Deposits in the Domestic Banking System/(Official Foreign Exchanges Reserves + Foreign Assets of Domestic Banks) (%)

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