

**STATEMENT BY HON AUDLEY SHAW
MINISTER OF FINANCE AND THE PUBLIC SERVICE**

Mr. Speaker,

1. The intensification of the global financial crisis since September has underscored Jamaica's vulnerability to changes in the external economic environment. The country faces an up-hill challenge if it is to maintain domestic stability in FY 2009/10 and restore the conditions that can support recovery and sustainable growth into the medium-term.
2. The recession in the global economy is expected to persist throughout this fiscal year. In particular, the US economy is projected to contract by 2.0 to 3.0 per cent in FY 2009/10, relative to growth of 1.1 per cent in FY2008/09. In the context of the continued weakness in the global economy, international commodity prices are expected to decline while the international capital markets are not expected to re-open to Jamaica until 2010. Against this background, the domestic economy will be adversely affected by a decline in exports, particularly bauxite/alumina, and a reduction in capital inflows.
3. The immediate challenges that we face are the financing gaps in the fiscal and external accounts. The revenue targets for FY2009/10 are going to be difficult to attain in the context of a shrinking economy while the achievement of the expenditure targets depends crucially on a reduction in debt service costs. Furthermore, any additional domestic borrowing arising from a slippage in either revenue or expenditure will place upward pressure on interest rates. The current situation points to the need for some alteration to the fiscal programme as well as an urgent infusion of foreign capital.
4. The technical analysis by GOJ officials (and supported by the IMF staff in their Article IV discussions with us) is that unless there is this influx of new capital, Jamaica's ability to remain current on its international obligations will deteriorate sharply this year. Also, without the assurance that these resources offer, the improvement in investor confidence that is necessary to underpin a reduction in

interest rates will not occur. Maintaining order in the foreign exchange market and reducing borrowing costs are both crucial elements in building a stable environment that is friendly to investment, job creation and growth.

5. In the external accounts, the main challenges for this year arise from the sharp fall in inflows of approximately US\$1.0 billion related to bauxite/alumina exports, tourism and remittances. The impact of this fallout will be felt right across the economy. The reduction in mining activity will be especially hard on Government revenue. In the first quarter of this fiscal year, the contribution to Government revenue for mining activity was some 97% less than it was a year ago. Over the next few years, the reduction in export earnings will be compounded by proposed changes to the Petrocaribe agreement which are likely to result in reduced credit for fuel imports, more difficulty in funding development projects and could deprive Jamaica of US\$100 m to US\$150 m per annum in official credit.

Why the IMF?

6. **Mandate:** The IMF is the multilateral institution that is best placed to respond to crises such as the one the world is undergoing. It has the reach, the information and the technical expertise to assess the needs of each member country and to continuously oversee the recovery process.
7. **Resources:** Over a long period of relative buoyancy in the world economy, Fund resources were underutilized resulting in a large unused cache of loanable funds. Even so, given the potential size of the liquidity needs of member countries, its resources have been strengthened by approximately US\$1.0 trillion through commitments by the G-20 as well as recent issues of debt instruments to countries willing to invest a part of their reserves with the Fund.
8. **Responsiveness:** The Executive Board, management and staff of the IMF are in emergency mode. Their operations are focused on addressing the global crisis. Consequently, at all levels, there is a strong disposition to extend support to Jamaica and similarly placed countries. Between November 1 2008 and May 31 2009, 25 countries have accessed Fund facilities to the value of US\$33.0 billion

and further commitments to over 30 countries amounting to US\$123.0 billion are in the pipeline.

9. **Facilities:** In the extraordinary context of a global economic downturn, the Fund is prepared to depart substantially from its traditional menu and modalities of support. This includes the possibility of extending loans for fiscal support and the front-loading of any agreed support rather than the standard release of funds in tranches after meeting specific targets. The current stance of the IMF management provides a window of opportunity to obtain support on terms that were hitherto unthinkable.

10. **Reputation:** An increased inflow of both official and private capital could depend crucially on the presence of an IMF commitment, even if the funds are never used. Both the World Bank and the IDB are inclined to follow the lead of the IMF and to condition their support on IMF assistance. If the downturn persists, medium term viability will depend on the availability and use of Fund support.

How much is needed?

11. Passive balance of payments projections point to a financing gap of US\$600 - US\$800 million in 2009/10. A general allocation of SDRs – that is, the distribution of SDR 250 billion among all member countries - has been approved by the Board of the Fund and is likely to be ratified by the Board of Governors. Jamaica's share of this allocation would boost resources available to the Bank of Jamaica by approximately US\$320 million before the Annual IMF/World Bank Meetings in early October.

12. The conclusion of a Stand-By Arrangement by September, in which the Fund is expected to commit the equivalent of 300 per cent of quota (US\$ 1200 m) over two years, would provide Jamaica with the wherewithal to meet all its external commitments. It would be expected that at least US\$400 million of the Stand-By Arrangement would be available 'up front'. This pool of convertible funds and the endorsement of the Fund would also smooth the flow of approximately

US\$400 million to US\$500 million from other multilateral sources and make the IMF funds a truly precautionary arrangement.

What terms can be anticipated?

13. The traditional conditionalities that accompanied IMF borrowing arrangements are no longer in practice. Such terms in the past included ‘prior actions’ such as exchange rate action, legislation, etc. and structural changes such as liberalization. These lending arrangements led to denial of ownership by borrowing countries and the development of a political stigma around IMF arrangements.
14. While IMF support is more liberal and more focused on the general evolution of policy rather than discrete steps, there has been no lowering of the standard with respect to the need for presentation of an internally consistent set of projections and policies. It is important to emphasize that Fund support is being sought for a programme defined and presented by Jamaica.
15. The Government has already entered into several agreements with other multilaterals which support a programme of reform in the public sector, the provision of social and economic infrastructure and a range of programmes to enhance human development. This implies that the measures advanced by the authorities for closing financing gaps in the public sector will be consistent with commitments given to other multilaterals.
16. Exploratory discussions have been taking place with the staff of the IMF since their visit to Jamaica in June for annual Article IV consultations. There are essentially three areas that they would like to see strengthened as part of a foundation for medium term sustainability:
 - a. consolidation of public enterprises i.e. a structured approach to minimizing the impact of these enterprises on the accumulation of debt. This would include divestment, mergers and improvements to their governance that would minimize financial losses;
 - b. the formulation of a debt strategy for the medium term that will relieve the extraordinarily high debt service burden; while the Government has always worked towards achieving the objectives of its annually reviewed

debt strategy, there is scope for bringing social partners into agreement to enable more equitable burden sharing;

- c. steps towards limiting the size of future deficits: These will include legislating guidelines for fiscal responsibility, streamlining the civil service and enhancing tax administration.

17. These areas are not new and are already being pursued by the Administration. The key issue for immediate consideration among stakeholders is the need for a compression of Government spending in the current fiscal year to meet the limits set by available revenue and borrowing. These are decisions that would have to be made with or without an IMF programme. However, the inflows associated with IMF support will make such adjustments easier and set the stage for a more sustainable fiscal path into the future.

Cabinet Decision

18. The Cabinet met yesterday to consider the report of the IMF discussions to date and to assess the current trends in the economy.

19. The general conclusion reached was that given the objective reality of:

- a) the fall out in foreign exchange earnings and foreign capital flows;
- b) the lack of access to the international capital market; the linkage of flows from other international lending institutions to an IMF Agreement;
- c) the prospect of a severe contraction in the local economy beyond the present crisis,

Jamaica has no real option at this time but to return to a borrowing relationship with the IMF.

20. Accordingly, Cabinet yesterday authorized the Minister of Finance and the Public Service to make a formal application to the IMF to seek to borrow up to 300 % of quota (Approximately US\$1.2 billion) in a Stand-by Arrangement.

21. We propose to have further discussions on these issues with the staff of the Fund during the course of next week and to keep Jamaica informed on the substance of these talks. We expect to complete the preparatory work and documentation by mid-August and to make a formal submission to the Executive Board of the IMF when it resumes in September.

22. We are acutely aware of the apprehension that many feel in our approaching the IMF and we will continue to consult with our stakeholders as far as practicable so that we can all be assured that we move together as one towards a more prosperous future.

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