MEDIUM-TERM DEBT MANAGEMENT STRATEGY

For the period 2011/2012 – 2013/2014

Government of Jamaica

Ministry Paper No.

April 28, 2011

Prepared by: The Ministry of Finance and the Public Service

Government of Jamaica

Medium-Term Debt Management Strategy (MTDS) (for the period 2011/2012 – 2013/2014)

and

Annual Borrowing Plan (for Fiscal Year 2011/2012)

Ministry of Finance and the Public Service
April 2011

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I. FOREWORD

1. The Government of Jamaica (GOJ) is pleased to develop and publish its updated Medium-term Debt Management Strategy (MTDS) using the framework developed by the International Monetary Fund (IMF) and the World Bank, to help countries develop their MTDS. The MTDS embodies the Government's desire and commitment to proactively manage the public debt and increase transparency. In execution of the debt strategy, the Government is in the process of drafting legislation for a Public Debt Management Act (PDMA), to replace more than twenty public debt-related pieces of legislations. The new Act will seek to maintain transparency in the management of the public debt.

2. The Government has also introduced a Fiscal Responsibility Framework (FRF) to address fiscal challenges. The FRF is at the centre of public financial management reforms, which includes the establishment of a Centralized Treasury Management System (CTMS). This strengthened legal, institutional and fiscal policy framework will facilitate achievement of the objectives of the *Debt Management Strategy*.

3. The *Debt Management Strategy* outlines the Government of Jamaica's (GOJ) objectives, strategies and plans for the management of public debt over the medium-term. It provides a review of the achievements and developments during the previous year, taking into account the composition of the debt portfolio, the fiscal operations, developments in the macro-economy and the domestic and international capital markets. It will also promote lower cost and prudent levels of risk to the public debt.

II OVERVIEW OF DEBT MANAGEMENT IN JAMAICA

4. During the 1980s and 1990s debt management functions were executed by the Bank of Jamaica (BOJ), the Ministry of Finance and the Public Service (MOFPS) and the Accountant General's Department (AGD). However, a policy decision was taken to centralize debt management functions within the MOFPS with the establishment of the Debt Management Unit (DMU) on April 1, 1998. These developments coincided with the BOJ's decision to focus on its primary role of maintaining stability in the monetary and financial systems.

5. The DMU was mandated to raise adequate levels of financing on behalf of the GOJ at minimum costs, to develop and implement strategies, while maintaining risk at an acceptable level.

6. The new organisational arrangement of the DMU resulted in a clear allocation of responsibility among the MOFPS, the BOJ and the AGD. Responsibility for the core debt management functions - debt policy and strategy formulation, implementation and analyses, debt-raising activities, debt recording, monitoring and some payment functions fully resided within the DMU. The BOJ acts as an agent for the MOFPS and is responsible for effecting external debt payments, conducting auctions for Treasury Bills and accepting applications for all primary market issues of government domestic securities. The Accountant General's Department has responsibility for treasury operations, including the servicing of the public debt.

7. Strong co-ordination of the MOFPS with the BOJ and the AGD are critical for effective debt management, particularly in the context of monetary and fiscal policy. The co-ordination of debt management with fiscal and monetary policies is undertaken within the context of the Government's macroeconomic framework, designed to lower inflation, achieve macroeconomic stability, sustainable growth and development.

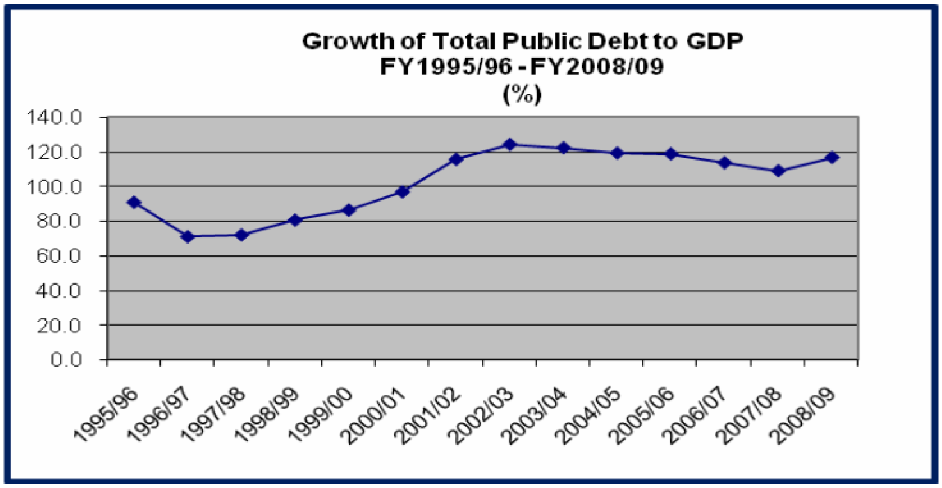
8. Jamaica emerged out of the decade of the 1980s with a heavy external debt burden. Consequently, debt management focused on the management of the external debt portfolio. The domestic debt has evolved largely as a result of a decline in external borrowing. However, foreign exchange shortage, domestic currency devaluation and other macroeconomic conditions created debt servicing difficulties and pressure on the fiscal resources. As a result, in the early 1990's, it was deemed necessary to increase the reliance on domestic borrowing. During this period, the stock of domestic debt increased more than tenfold moving from $11,868.6 million at end-March 1991 to $139,203.7 million at end-March 1999. Contingent liabilities played a significant part in the growth of the domestic debt, particularly the assumption of debt related to the financial sector crisis of the late 1990s, which accounted for 40% of GDP.

9. In 1997, Jamaica commenced activities on the International Capital Markets (ICM) to access funds for budgetary financing. This move heralded a substantial change in the structure of the debt portfolio with external debt being dominated by debt from private creditors, mainly global bonds, as loans from multilateral and bilateral sources continued to decline over the next 10 years.

The increasing domestic debt comprised fixed and floating rate medium to long-term Local Registered Stocks (LRS), short to medium-term debentures, Treasury Bills, US$-denominated domestic bonds, US$-indexed bonds, and commercial loans.

10. Jamaica's Debt-to-GDP increased considerably between FY 1996/97 and FY 2002/03, when the ratio increased by 52.9% moving from 71.3% of GDP at the end of FY 1996/97 to 124.3% at the end of FY 2002/03 (Chart 1).

Chart 1



11. With the ballooning of the debt, bunching of maturities and the increasing cost of servicing the domestic debt, by FY 2009/10, the government took the decision to execute a liability management exercise to realign the domestic debt portfolio in relation to the maturity structure, which involved a voluntary debt exchange marketed as the Jamaica Debt Exchange (JDX).

12. The main characteristics of the JDX, which sought to exchange all market issued Jamaica and United States Dollar local securities were:

- A par-for-par exchange offer with no "haircuts";
- Voluntary exchange of over 350 market issued domestic bonds valued at approximately $701.5 billion for 25 new benchmark bonds;
- Voluntary exchange of short dated high yielding interest bearing securities for longer dated securities with significantly lower yields;
- Extension of the maturity profile of the domestic debt portfolio in order to lower the refinancing risks;
- Achievement of substantial cost savings;
- Issue of an appropriate mix of fixed, variable and USD securities; and
- The introduction of new CPI-Indexed Investment Bonds.

13. Following execution of the JDX, the results revealed a participation rate of 99.2% from investors. This included 100% participation from the financial institutions and represented $695.60 billion of the total eligible bonds.

III REVIEW OF THE PUBLIC DEBT PORTFOLIO FY 2010/11

14. During FY 2010/11, the Government continued its management of the public debt within the framework prescribed by its annually reviewed debt management strategy and was successful in the efforts to finance the budget at minimum borrowing costs, minimize foreign currency exposure of the domestic debt portfolio, and extend the maturity structure in order to maintain prudent levels of risk.

15. At the end of the fiscal year, the stock had increased in nominal terms by 9.5% over FY 2009/10 and showed a significant reduction in the growth rate when compared to the increase of 19.5% at the end of FY 2009/10 over FY 2008/09.

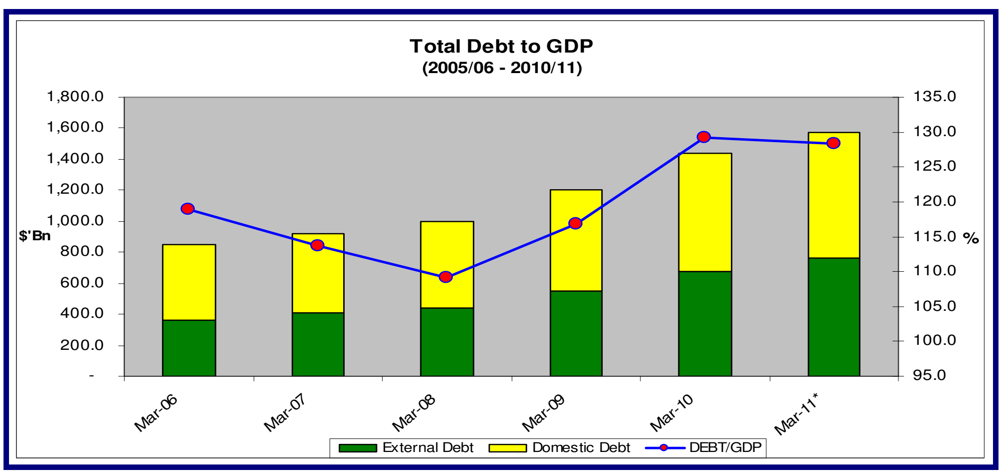
Debt Stock

16. At the close of FY 2010/11, Jamaica's total public debt increased to $1,570.4 billion or 128.3% of GDP. This represented a 9.5% increase compared with $1,434.8 billion or 129.3% of GDP at end of FY 2009/10. The stock movement over the review period was attributable to:

- Financing of the fiscal deficit;
- Disbursements on existing external loans;
- Increase in loans from multilateral creditors;
- Assumption of debts of the Sugar Company of Jamaica; and
- Issue of securities to BOJ for capitalized interest on former FINSAC Bonds.

17. Chart 2 illustrates the growth of the total debt stock during the period FY 2005/06 to FY 2010/11, together with the Debt to GDP ratio.

Chart 2



Domestic

18. At the end of FY 2010/11, central government domestic debt stood at $809,370.0 million or 66.1% of GDP, a net increase of 6.7%, when compared with $758,700.4 million or 68.4% of GDP at the end of FY 2009/10. In addition, explicit domestic guarantees stood at approximately J$26,405.1 million or 2.2% of GDP at end FY 2010/11.

External

19. At the end of FY 2010/11, the stock of public and publicly-guaranteed external debt peaked to US$8,874.8 million (J$760,998.3 million) or 62.2% of GDP, an increase of 17.5% over the stock at end FY 2009/10. Contributing to this increase is the raising of US$400.0 million on the International Capital Markets to pre-finance the repayment of the US$400 Million 11.75% Bond which matures in May 2011.

Debt Composition

Domestic

20. As a result of the JDX, by the end of FY 2010/11, the structure of the domestic debt had changed significantly when compared with FY 2008/09. The stock comprises FR and VR Benchmark Bonds, CPI-Indexed Investment Notes, Treasury Bills, Commercial Loans and USD and Euro Loans (Charts 3 and 4).

Chart 3

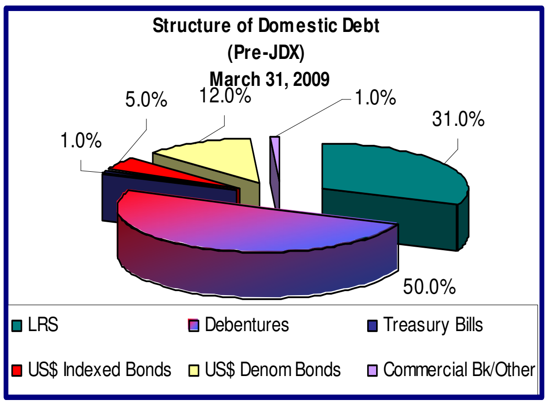
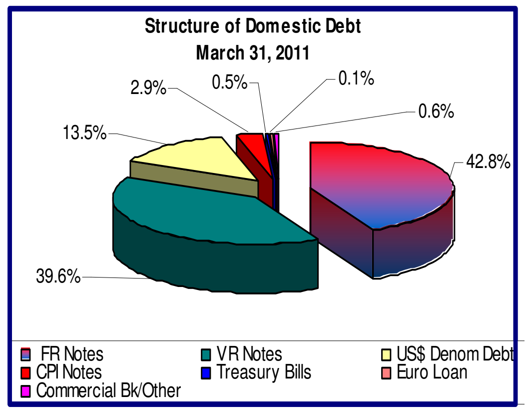


Chart 4



External

21. At end-FY 2010/11, Bond issues of US$4,200.0 million represented the largest creditor category of Jamaica's public sector external debt, accounting for 47.3% of the portfolio. Overall, bond issues increased by 10.4% over FY 2009/10. Bilateral and multilateral obligations accounted for 46.4% of external debt compared to 45.1% in FY 2009/10. Consequent on the Government's focus on securing more funding from official creditors, multilateral indebtedness increased by 25.9% to US$3,109.5 million, when compared with the previous period (Charts 5 and 6).

Chart 5

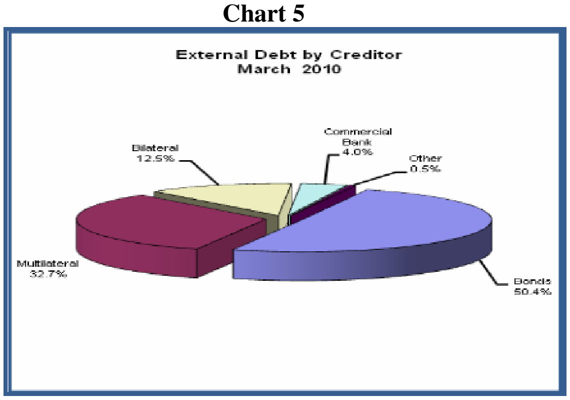
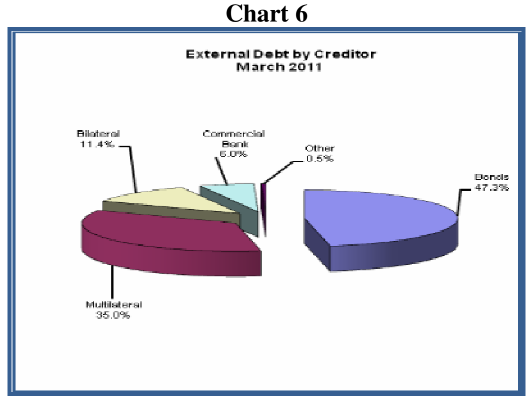


Chart 6



Maturity Profile

22. The Government successfully issued long dated securities in both the domestic and external markets. This was facilitated by the successful reopening of long-term fixed rate Benchmark bonds and the sourcing of loans from the multilaterals.

Domestic Debt

23. During FY 2010/11, the maturity profile of the domestic portfolio showed marginal improvement at the short end of the curve. By the end of the year debt scheduled to mature within one year had declined to 5.8% compared to 10.1% at the end of FY 2009/10. In the one to five year segment, 51.1% was scheduled to mature compared with 42.2% at the end of FY 2009/10; debt scheduled to mature after 5 years accounted for 43.1% compared to 47.7% at the end of FY 2009/10 (Charts 7 and 9).

External Debt

24. At the end of FY 2010/11, of the total external debt outstanding, 21.6% had maturities of up to 5 years, compared with 27.2% at the end of FY 2009/10, 32.8% had maturities of 5-10 years up from 23.6% in March 2010; and 45.6% had maturities in excess of 10 years down from 49.2% in March 2010. The external debt portfolio therefore continues to be largely long-term and consistent with minimizing and effectively managing rollover risk (Charts 8 and 10).

Maturity Profile

Chart 7

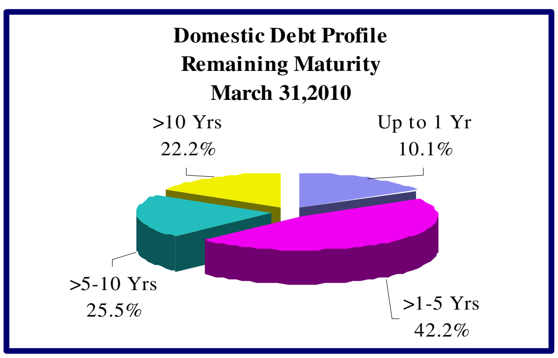


Chart 9

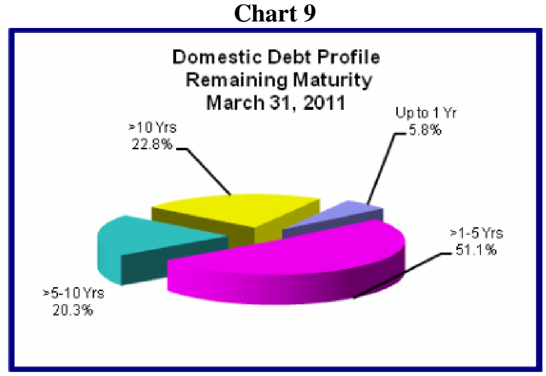


Chart 8

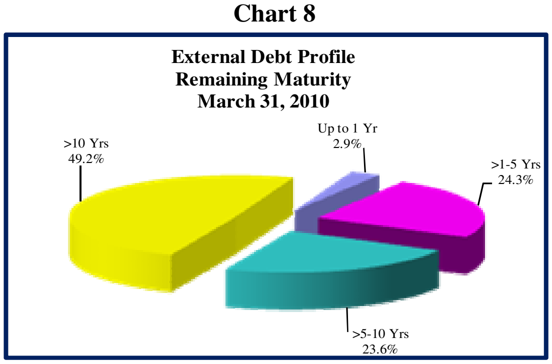
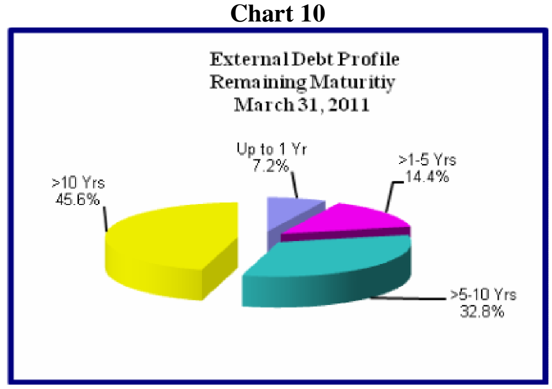


Chart 10



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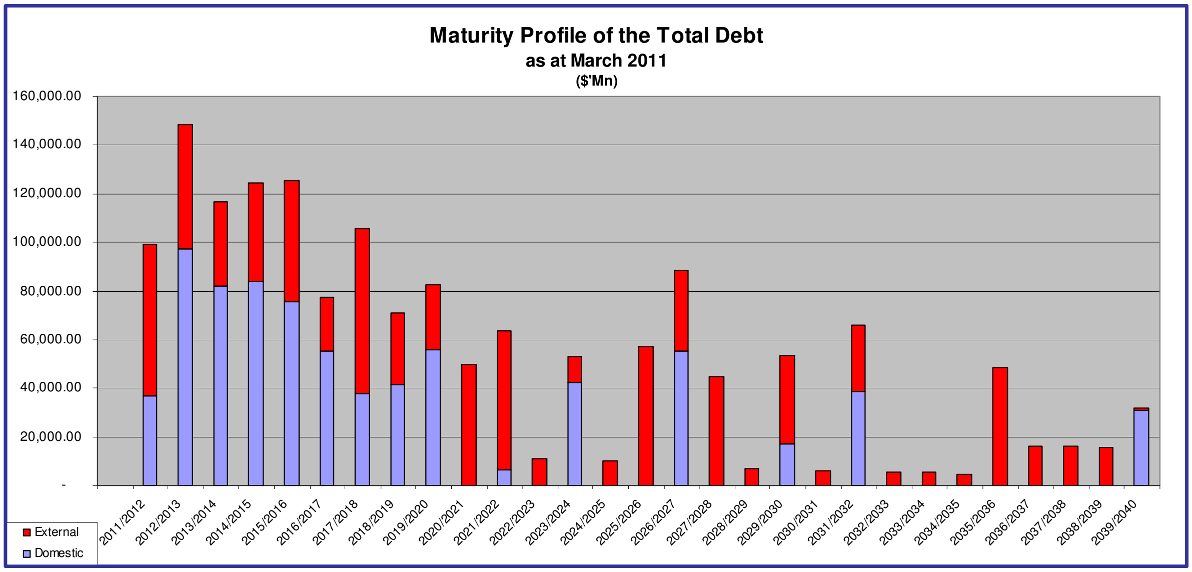


Currency Composition

Domestic

25. At the end of FY 2010/11 the foreign currency component of the debt stock had increased marginally to $109,282.9mn or 13.5% compared to $99,675.5mn or 13.1% at the end of FY 2009/10 (Chart 12). The Government has not issued any US$-Denominated Bond or US$-Indexed Bond in the domestic market since the JDX, consistent with the objectives of the debt strategy. However, during the review period the Government assumed US$96.2 million in Sugar Company of Jamaica debt.

External

26. At the end of FY 2010/11, US dollar denominated debt accounted for 82.4% of the external debt compared with 79.2% at the end of FY 2009/10. Further, at the end of FY 2010/11, the proportion of the debt denominated in Euros represented 13.6% compared with 16.1% at the end of FY 2009/10. Yen-denominated loans represented 2.1% of the external stock, while other currencies accounted for 1.9% at the end of FY 2010/11 (Chart13).

Chart 12

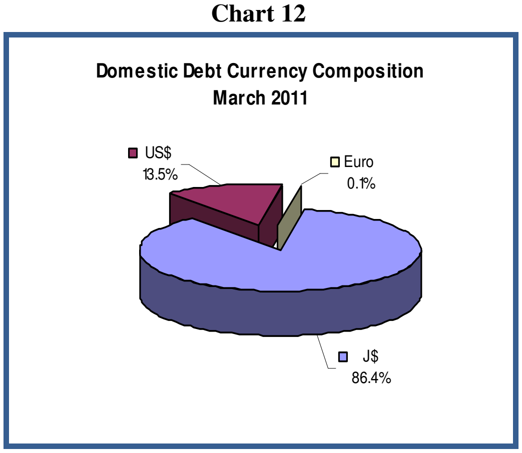
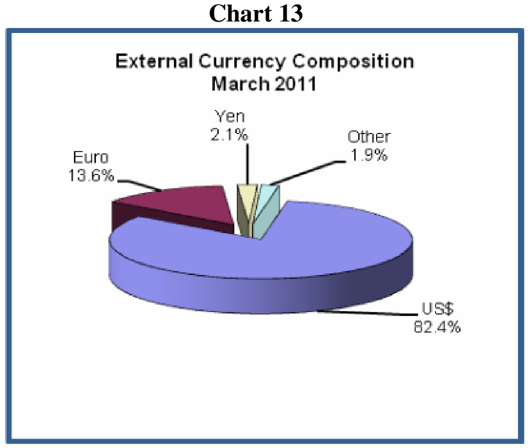


Chart 13



Interest Rate Structure

Domestic

27. At the close of FY 2010/11, 59.8% of the domestic debt was on a fixed rate basis, while 40.2% was contracted on a floating interest rate basis. This compares favourably over FY 2009/10 where the fixed interest rate component of the domestic portfolio stood at 56.4% (Table 1).

External

28. At the end of FY 2010/11, 76.2% of the external debt was fixed rate and 23.8% was variable rate (Table 1).

Table 1

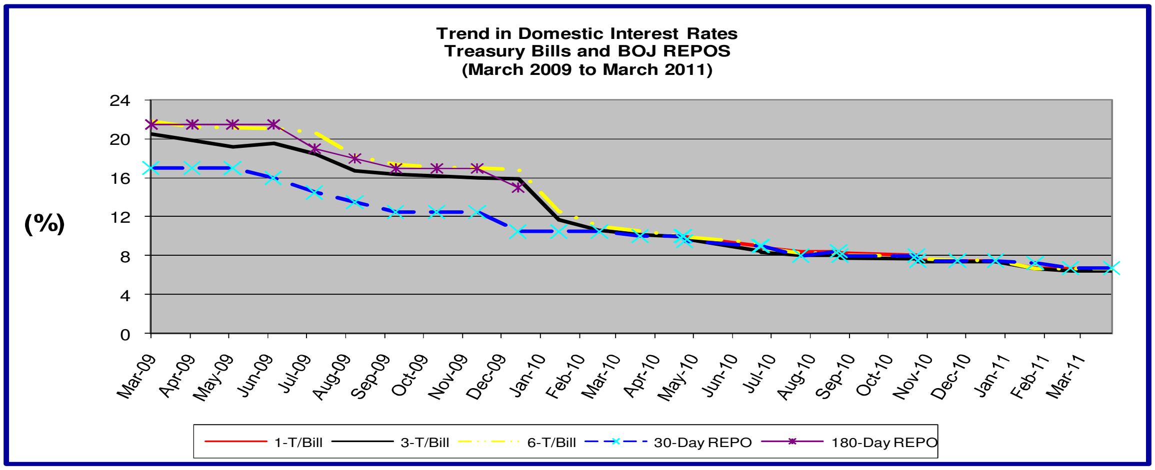
Interest Rate Structure As at March 2011 (%)		
	External Debt	**Domestic Debt**
Fixed Rate	76.2	59.8
Variable Rate	23.8	40.2
Total Debt	**100.0**	**100.0**

Interest Rates

Domestic

29. During FY 2010/11, all signal interest rates in the domestic market declined to new historically low levels. By the end of FY 2010/11, the interest rate on the signal BOJ 30-day open-market instrument had moved from 17.00% p.a. at the end of March 2009, to 6.75% p.a. Concurrently, the average yields on the 3 and 6-month Treasury Bills trended downwards, moving from 20.51% p.a. and 21.77% p.a. respectively at the end of March 2009, to 6.46% p.a. and 6.63% p.a. respectively at the end of March 2011 (Chart 14).

Chart 14



International

30. During FY 2010/11, international interest rates remained low as a result of the prolonged global financial crisis. This had a positive impact on interest payments on variable rate loans, resulting in lower-than-projected interest payments. Base interest rates, such as the US 3-month LIBOR, were reduced to a low of 0.31% p.a. as at March 2011, compared to 1.27% at end March 2009.

31. Jamaica's bonds performed well compared to other emerging market issuers during FY 2010/11. The trading levels of the Government's Eurobonds were sustained at exceptionally high levels. At the end of March 2011 the bid prices of all Jamaica Bonds were above par and the yields tightened relative to the benchmark US Treasury Note. This is an indication of investors' confidence in Jamaica and that there is a demand for the country's Bonds (Charts 15 and 16).

Chart 15

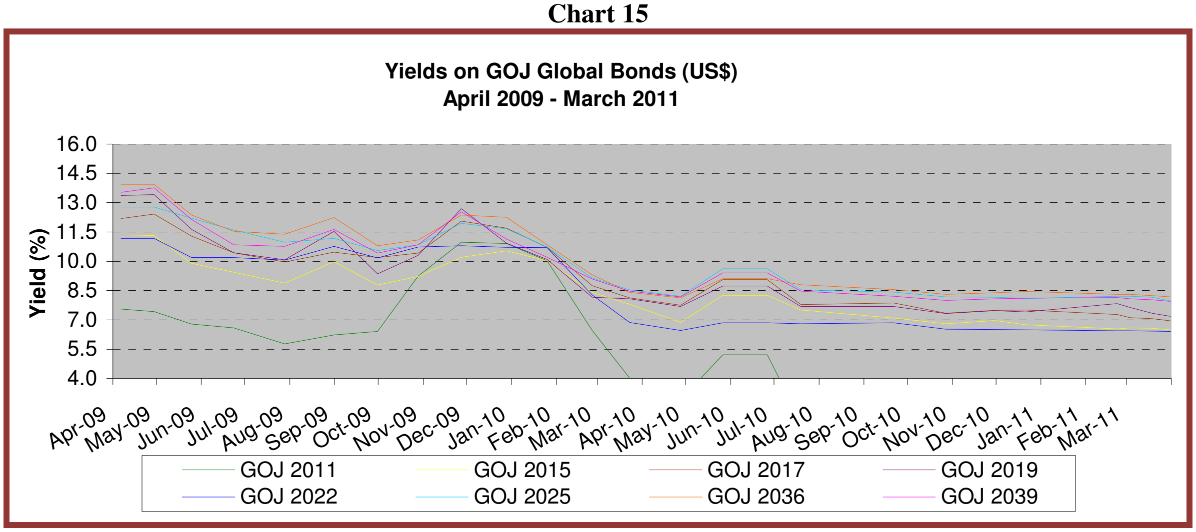
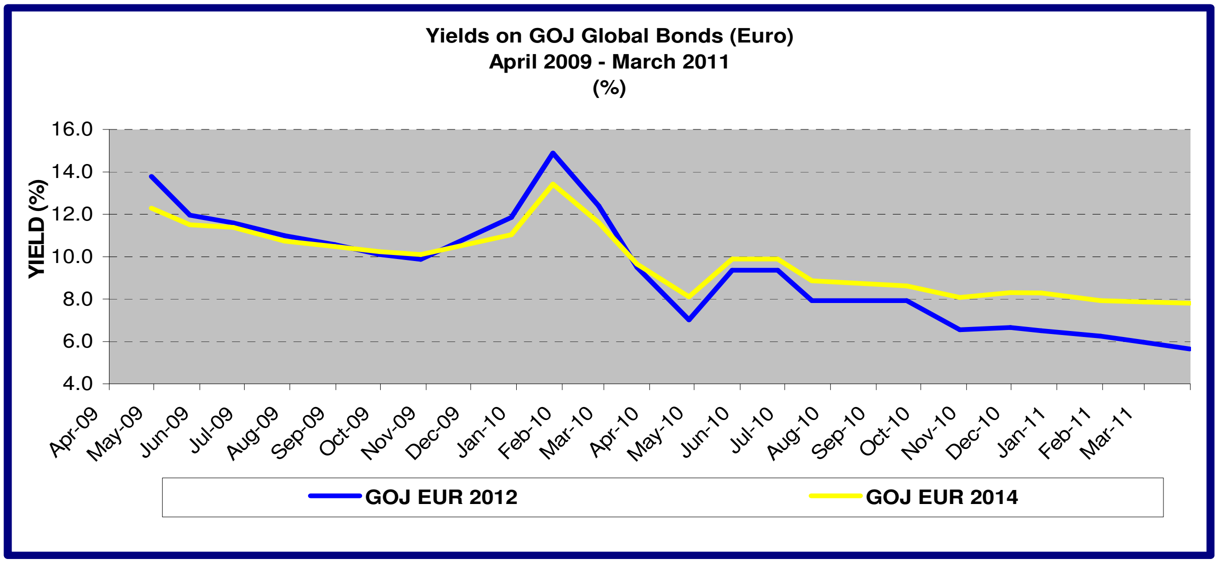


Chart 16



Debt Issuance

Domestic

32. Gross new debt issued during FY 2010/11 amounted to $126,005.0mn, compared with budgeted financing requirement of $117,971.5mn. The total raised during this period represented a significant reduction of $122,840.37 million or 49.4% when compared to the amount raised in FY 2009/10. Of this amount, $117,717.3mn was issued into the market; a reduction of $254.2mn or 0.2% when compared with the budgeted amount of $117,971.5mn for FY2010/11. The other securities issued were of a non-cash nature and represented the Government's assumption of certain debts the on behalf of the Sugar Company of Jamaica.

33. As a consequence of the gradual but consistent interest rate reduction during FY 2010/11, there was low investor demand for variable rate notes. As a result, fixed rate debt issued during the period increased significantly to 99.0%, up from 87.5% at the end of March 2010.

34. During FY 2010/11, new debt issued in the domestic market had 69.9% maturing within 5 years, compared with 87.6% in FY 2009/10. There was measured success in extending the maturity structure, as debt issues maturing after 5 years increased significantly to 30.1%, up from 12.4% at the end of FY 2009/10 (Tables 2 and 3).

Table 2

Interest Rate Structure of New Domestic Debt Issued During F/Y2010/11		
	Total	**%**
FR	124,707.0	99.0
VR	1,298.0	1.0
Total	**126,005.0**	**100.0**

Table 3

Maturity Structure of New Domestic Debt Issued During F/Y 2010/11 Original Maturities ($mn)					
	Up to 1 Year	**>1-5 Years**	**>5-10 Years**	**>10 Years**	**Total**
Issues	20,738.4	67,383.3	18,484.8	19,398.5	126,005.0
%age	**16.4**	**53.5**	**14.7**	**15.4**	**100.0**

External

35. During FY 2010/11, the Government received loans from multilateral and commercial sources. Multilateral policy-based loans contracted during the period totaled $400.0 million. In February 2011, Jamaica successfully raised US$400.0 million on the International Capital Markets by reopening its 8.0% 2019 Global Bond at a yield of 7.95%. The increase in the size of the 8.0% 2019 to US$750 million meets specific liquidity and structural requirements for placement in the JP Morgan Emerging Market Bond Index (EMBI).

36. Fifty percent of the new external debt issuance was contracted on a fixed rate basis with a maturity of greater than five to ten years. The remaining issuance which was contracted on a variable rate basis has maturities in excess of ten years (Tables 4 and 5).

Table 4

Interest Rate Structure of New External Debt Issued During FY 2010/11 (US$Mn)		
	Total	**%**
FR	400	50
VR	400	50
Total	**800**	**100**

Table 5

Issued during F/Y 2010/11 (US$Mn)	< 1 year	1-5 years	>5-10 years	>10 - 15 years	Total
Multilateral	0.0	0.0	0.0	400.0	400.0
IDB	0.0	0.0	0.0	400.0	400.0
IBRD	0.0	0.0	0.0	0.0	0.0
Bonds	0.0	0.0	400.0	0.0	400.0
Total	**0.0**	**0.0**	**400.0**	**400.0**	**800.0**
Percentage	0.0	0.0	50.0	50.0	100.0

Debt Indicators

37. Table 6 below shows indicators for FY 2009/10 and FY 2010/11.

Table 6

Jamaica: Debt Ratios (%)	F/Y2009/10	F/Y2010/11
Total Debt / GDP	129.3	128.3
External Debt / GDP	60.9	62.2
Domestic Debt / GDP	68.4	66.1
External Debt Service / XGS	12.1	11.5
Total Interest Payments / GDP	17.0	10.5
Total Debt Service / Total Revenue	119.3	73.2
Total Debt Service / Total Expenditure	85.0	59.2
Total Interest Payments / Tax Revenue	71.0	45.8
Total Interest Payments / Total Expenditure	44.8	32.9
Total Amortization / Total Revenue	56.5	32.5
Total Amortization / Total Expenditure	40.2	26.2

External Debt Forgiveness

38. Under the Commonwealth Debt Initiative, the United Kingdom has over the years provided debt relief to Jamaica under its various debt initiatives. Accordingly, in FY 2010/11, Jamaica received debt forgiveness in the aggregate amount of £2.41 million. Jamaica was granted this debt forgiveness based on an assessment of selected indicators from the Government's Medium Term Framework (MTF) and the National Development Plan (Vision 2030).

Country Rating

39. Annual rating reviews were conducted on Jamaica's credit standing by the rating agencies Moody's Investors Service (Moody's), Standard and Poor's (S&P) and Fitch Ratings during the fiscal year. In December 2010, S&P re-affirmed Jamaica's long-term foreign and local currency sovereign rating "B-" and maintained its "Stable" outlook. This was followed in January 2011 by Moody's re-affirming Jamaica's long-term foreign currency local currency credit ratings of "B3". Moody's maintained its "Stable" outlook for Jamaica. Finally, in February 2011, Fitch Ratings also re-affirmed Jamaica's foreign and local currency default rating of "B-" and assigned a "Stable" outlook.

40. The ratings were supported by the country's relatively high level of institutional strength, the Government's ongoing commitment to fiscal discipline and to maintaining investor confidence and stability, its proven ability to face exogenous shocks, willingness to pay and political stability.

IV. RISK ANALYSIS

41. The structure of the debt portfolio has inherent risks associated with market conditions and the macroeconomic environment. Risk mitigation strategies have been consistently employed to insulate the portfolio from potential shocks. These strategies include the suspension of issuance of US$-denominated and US$-indexed bonds in the domestic market, as well as the extension of the "Average Time to Refixing" of new debt.

Foreign Exchange Risk

42. At the end of FY 2010/11, 82.4% of the external debt was denominated in US$, while 13.5% of the domestic debt was also US$-denominated. Jamaica's public debt faces ongoing risk arising from cross currency parity changes which is inherent in the external debt component of the debt portfolio. This has been reduced over time as the US Dollar, the currency in which the external debt is reported, continues to maintain its prominence as the principal currency with respect to the other major currencies i.e. Euros, Japanese Yen, Renminbi Yuans and Great Britain Pounds. In addition, the domestic portfolio has benefited from the introduction of CPI-Indexed Investment Notes and the discontinuation of US$ Indexed Bonds as this has substantially reduced the level of foreign exchange exposure in the domestic portfolio. However, with a foreign currency component of approximately 55.4% at the end the review period, Jamaica's public debt exhibits a high level of foreign exchange risk which may be alleviated through an increase in domestic currency borrowing.

Box 1. Foreign Exchange Risk

Foreign Exchange Risk is the possibility that the Government could sustain losses occurring from adverse movements in foreign exchange rates among currencies represented in the debt stock.

The level of exposure to this risk depends on the proportion of the debt stock that is denominated in foreign currency. However, the potential negative impact of this risk may be mollified through proper management. Methods to alleviate the impact may include execution of forward exchange contracts and hedging mechanisms.

Essentially, the extent of exposure to this risk would depend on the long-term stability in the foreign exchange rate market and the potential to maintain long-term sustainability.

Refinancing Risk in the Domestic Portfolio

43. The JDX had the desired effect of smoothing maturities along the domestic yield curve, thereby significantly decreasing refinancing risk in the debt stock. At March 31, 2011, 5.8% of the outstanding domestic debt was scheduled to mature within one year down from 10.08% at the end of March 2010. Debt scheduled to mature after 10 years increased from 22.2% at the end of March 2010 to 22.8% at the end of March 2011.

Refinancing Risk in the External Portfolio

44. In keeping with the debt strategy objectives of extending the maturities of the debt and minimizing rollover risk, the external debt has traditionally been contracted on a long term basis and therefore continues to be largely long-term with low rollover risk.

45. During FY 2010/11, 88.4% of the debt was at the long end of the curve. Of the total external debt outstanding at the end of March 2011, 27.2% will mature in 5 years, up from 18.9% at the end of the previous year; while 49.2% had maturities in excess of 10 years, an increase from 47.3 % in FY 2009/10.

Box 2. Refinancing/ Rollover Risk

Refinancing risk measures the exposure of the debt portfolio to unusually high interest rates at the point at which debt is being refinanced. In extreme cases, when this risk is too high, debt managers are unable to roll over maturing obligations.

The following indicators measure the exposure to this risk:

- The redemption profile of the outstanding debt; that is, the sequence of principal payments arising from the outstanding stock of debt.
- Proportion of the debt stock falling due within a particular period.
- Proportion of the debt stock falling due within a particular period adjusted by liquid assets; that is, 'liquid cushions' in the form of FX reserves or cash balances that reduce the Government's vulnerability to refinancing risk.
- Average time to maturity.

Interest Rate Risk

46. The Government was able to achieve its debt strategy objective of reduced interest costs over the medium-term through an increase in the fixed rate component of the domestic debt and through significantly reduced external interest rates. This had the effect of reducing the level of interest rate risk which has been inherent in the domestic portfolio.

47. The external component of the debt which is predominantly on a fixed rate basis has traditionally had a low level of interest rate risk. Internationally, interest rates remained low as a result of the prolonged global recession. This however had a positive impact on interest payments on variable rate loans, resulting in lower than projected interest payments. Base interest rates such as the US 3-month LIBOR were reduced to the historically low level of 0.25% p.a. as at January 2010. The US 3-month LIBOR increased marginally and stood at 0.3% p.a. at the end of March 2011.

Box 3. Interest Rate Risk

Interest Rate Risk refers to the susceptibility of the debt portfolio to higher market interest rates. The impact of this risk may cause interest rates on variable and fixed rate debts that are maturing to be re-priced.

The impact of this risk on the public debt stock may be controlled through the degree of prudence exercised by the Debt Management Unit. This may include the new debt issue being done on the premise of current debt stock and the desire of continuity towards a balanced debt portfolio. Furthermore, debt officers would take into consideration the volatility and direction of rate changes; the slope of the interest rate yield curve and the basis for re-pricing at rollover dates. Hence, the creation of variable or fixed rate instruments would be predicated on these considerations.

Liquidity Risk

48. The Government's financing requirements have in the past been adversely affected by varying degrees of liquidity risk. In these circumstances severe challenges are experienced in raising adequate financing from the market through debt issuances, even when there are more than adequate funds available. The market may resist buying the Government securities for reasons including uncertainty in the macroeconomic outlook.

49. The Government has sought to mitigate this risk by building reserves to protect the adequacy of the cash flow. Although there is potential to earn from short term deposits of these reserves, the carrying cost may be prohibitive, and therefore strategic management of the reserves would have to be employed.

Box 4. Liquidity Risk

Liquidity Risk is the probability that the Government may not raise adequate financing to satisfy its budgetary requirements. The risks may be due to insufficient liquidity or the investing community deeming the security to be unattractive.

The attractiveness of the securities to investors may be negatively affected by the following:

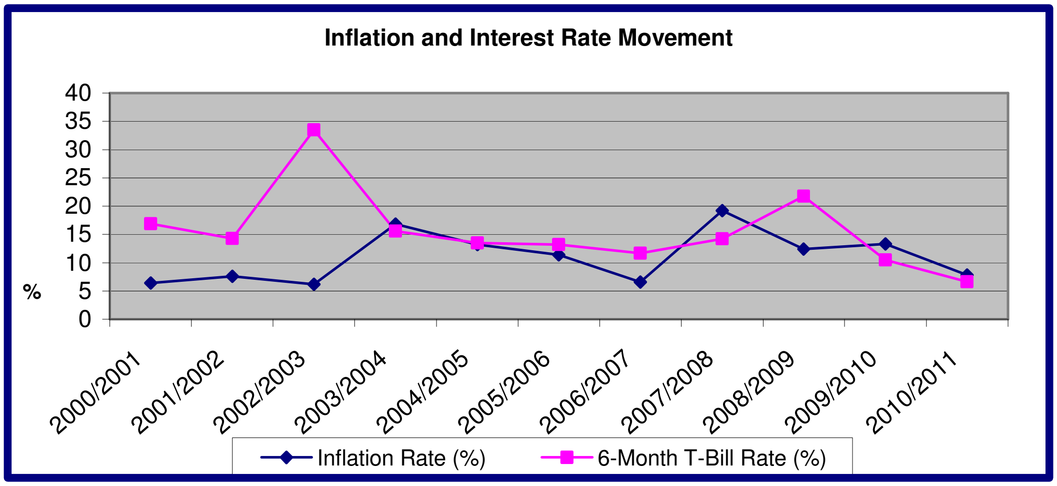
(a) return on investment not reflecting the appetite of the investors along the yield curve.
(b) uncertainty among investors arising from the socio-political environment.
(c) instability created by geo-political events in the global environment could disrupt the credit market

However, this risk may be mitigated through the building of cash buffers, using designated reserves.

Inflation Risk

50. Jamaica, as a small open economy, is prone to volatile inflation rates, which are strongly influenced by such factors as exposure to the pass-through effects of international commodity price movements and adverse weather conditions. Given the theoretically demonstrated direct relationship between inflation and interest rates, increases in the inflation rate will increase market rates thus negatively impacting bond pricing and trading on the secondary market (Chart 17).

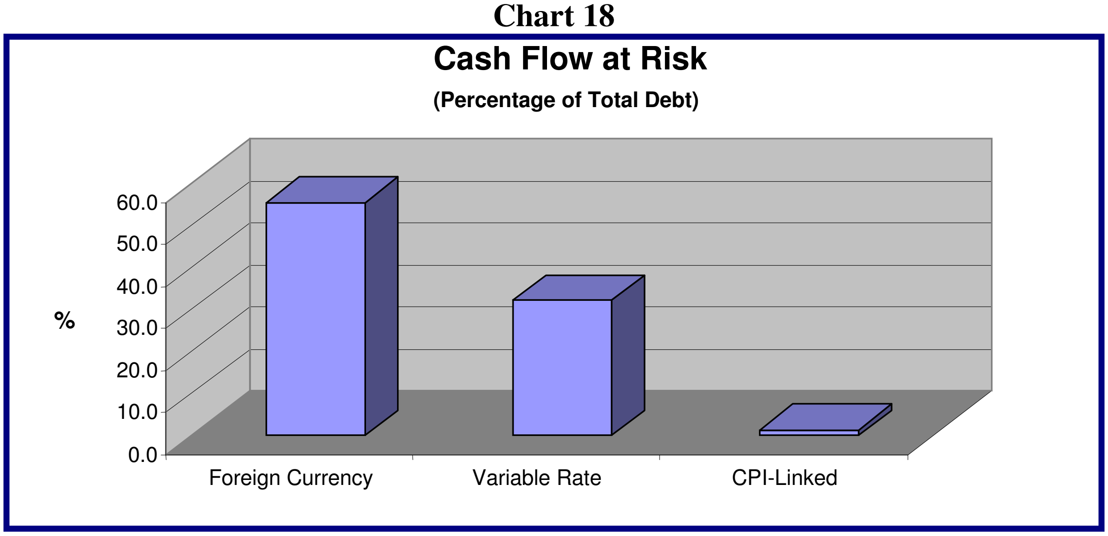
Chart 17



Cash Flow at Risk

51. The variable rate and foreign currency bonds have the highest risk in the debt portfolio. Given the small proportion of the CPI-linked bonds in the portfolio, i.e. 1.5%, the risk to the cash flow is minimal. Currently, all external debt, US$-denominated bonds issued in the local market, variable rate bonds and CPI-linked bonds have the potential to negatively impact the cash flow, as the macroeconomic variables, such as inflation, devaluation and interest rates are subject to change. The variables that may impact the cash flow from a domestic debt standpoint are illustrated in Chart 18.

Chart 18



V. REVIEW OF THE DEBT MANAGEMENT STRATEGY 2010/2011

52. The *Debt Management Strategy* outlined the Government of Jamaica's objectives, strategies and plans for the management of the domestic and external debt liabilities for the fiscal year and the medium-term. It provided a review of the achievements and developments during FY 2009/10 taking into account the composition of the debt portfolio, the fiscal operations and developments in the macro-economy and in the domestic and international capital markets.

53. During FY 2010/11 the Debt Management Strategy sought to:

- Minimize debt service cost;
- Increase the fixed-rate proportion of the domestic debt portfolio;
- Maintain the maturity profile of the debt;
- Minimize foreign currency exposure of the domestic debt portfolio;
- Maintain the number of benchmark bonds;
- Support and improve the development of the secondary market;
- Increase the transparency and predictability of debt issuance and operations;
- Continue to engage the multilateral institutions and the bilateral creditors;
- Enhance consultation with market players and rating agencies;
- Restructure the Debt Management Unit; and
- Implement legislation governing debt.

Minimise Debt Service Cost

54. The execution of the Jamaica Debt Exchange (JDX) in February 2010 led to greater access to multilateral sources of financing, which contributed to sustained reduction in domestic interest rates. Yields on GOJ 6-month Treasury Bills moved from a high of 10.49% at the end of FY 2009/10 to 6.63% in March 2011. The current yields on Treasury Bills are the lowest in 30 years.

Increase the Fixed-Rate Proportion of the Domestic Debt Portfolio

55. The Government achieved considerable success in the realization of this objective. The fixed rate portion of the domestic debt increased from 56.4% at end-March 2010 to 59.8% at end-March 2011, thereby exceeding the strategy target of 58.4%. This strategic move has reduced the potential interest rate risk on the domestic debt portfolio.

Maintain the Maturity Profile of the Debt Portfolio

56. The objective of maintaining the maturity profile of the debt portfolio was achieved during the review period; this achievement was realised following the execution of the Liability Management Programme with respect to the domestic debt portfolio in FY 2009/10. At March 31, 2011, 5.8% of the outstanding domestic debt was scheduled to mature within one year, 51.0% between one and five years; and the remaining 43.1% after five years. This is a significant improvement over the previous period, as at the end-March 2010, 10.1% of the total domestic debt outstanding was scheduled to mature within one year, while 47.7% had maturities of five years and over.

57. At March 31, 2011, 21.6% of the external debt was scheduled to mature in 1-5 years, 32.8% in 5-10 years, and 45.6% in excess of 10 years. The external debt portfolio, therefore, continues to be largely long-term and consistent with minimizing and effectively managing rollover risk.

Minimize Foreign Currency Exposure of the Domestic Debt Portfolio

58. The stated objective of reducing the foreign currency component of the domestic debt from 13.1% to 12.0%, to reduce the exposure of the domestic portfolio to exchange risks, was not achieved, as the actual outturn at end-March 2011 was 13.5%. Although no new US$-denominated securities were issued in the domestic market during the review period, the Government assumed Sugar Company of Jamaica's (SCJ) debt denominated in US$.

Maintain the Number of Benchmark Bonds

59. During the review period, of the four Bonds that matured two were replaced with new Benchmark notes. This decision was consistent with prudent debt management, as all borrowing requirements were satisfied by early February.

Support and Improve the Development of the Secondary Market

60. With the dematerialisation of all eligible GOJ securities in the JamClear-CSD, settlement and trading transactions are now completed in real time and on a safe platform, thereby supporting increased efficiency and reducing operational risks to both the participants in the depository and the Government. Strategic and prudent reopening of the Benchmark Bonds has contributed to increased market liquidity, thereby supporting improved price discovery in the secondary market.

Increase the Transparency and Predictability of Debt Issuance and Operations

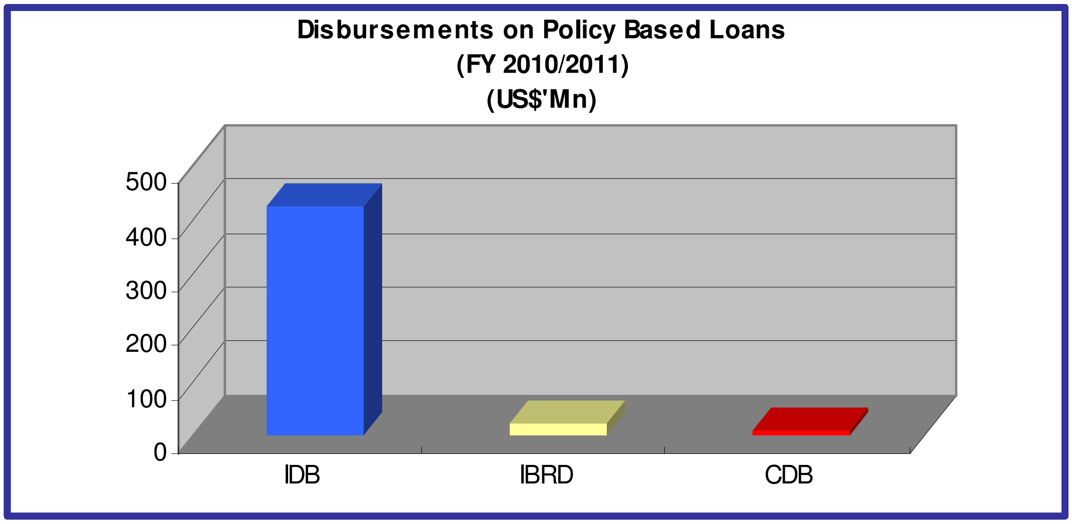
61. The objective of maintaining transparency in debt issuance was achieved by the provision of up-to-date information to the market through regular postings to the MOFPS website (www.mof.gov.jm/dmu) and constant communication to the investing community. During the year, the Government continued to publish comprehensive, timely and reliable information on the performance and management of the public debt, thereby ensuring greater predictability and accountability.

62. The Government published schedules of upcoming market issues and the results. Information on the debt strategy, operations and key debt data including stock of debt, interest rate structure, currency and creditor composition, monthly interest rate schedules and other relevant investor information were also published on the MOFPS' website. Prior to the start of the review period, the schedule of Treasury Bill issues for the fiscal year was published as planned. The schedule of market issues was published on a monthly basis up to October 2010. This was followed by a 5-month schedule for the remainder of the fiscal year.

Continue to engage the Multilateral Institutions and the Bilateral Creditors

63. The debt strategy to engage the multilateral and bilateral creditors continued during FY 2010/11. This approach was geared towards securing more cost effective financing for infrastructure development projects. These loans covered a wide spectrum of the economic sector, ranging from agriculture, information technology, rural development and road rehabilitation. Concessional policy-based loans for budgetary support were disbursed by the Inter-American Development Bank (IDB), the World Bank and Caribbean Development Bank (CDB) (Chart 19).

Chart 19



Enhanced Consultations with Market Players and Rating Agencies

64. The Government did not host its usual investor conference calls with the international and domestic markets. However, there were numerous meetings, presentations and investor fora with the public and private sectors in the domestic market, two Non-Deal Road Shows – one in Europe in October 2010 and another in the United States in February 2011. This was preparatory to the Government's re-entry into the International Capital Markets, following the onset of the global financial crisis.

Restructuring of the Debt Management Unit

65. The objective to restructure the Debt Management Unit along the functional lines of a Front, Middle and Back office model was not realized during the review period. However, significant advances in this regard were made and it is envisaged that this strategy objective will be achieved by mid-FY 2011/12.

Implement Legislation Governing Debt Management

66. Implementation of legislation governing debt management was not achieved during the review period, although considerable progress in developing this omnibus legislation has been made. The draft Public Debt Management Bill is currently at an advanced stage, preparatory to the entry into the Houses of Parliament for consideration and final approval. It is anticipated that the PDMA will be passed into law during the first quarter of FY 2011/12.

VI. TOWARDS A MEDIUM TERM DEBT MANAGEMENT STRATEGY (MTDS)

67. The IMF and World Bank have jointly developed a multifaceted framework to help countries develop a more systematic approach to their Medium-term Debt Management Strategy (MTDS). This framework encapsulates a comprehensive approach to the formulation of a debt strategy, identifying possible constraints through the dynamics of macroeconomic variables; costs/risks trade-offs and market conditions relative to debt management. It involves the process of providing analysis on all feasible alternatives while taking into consideration all relevant costs and risks.

68. Prior to the use of the MTDS Toolkit, the medium-term debt strategies developed by the GOJ outlined the Government's objectives, strategies and plans for the management of the public debt for the fiscal year and the medium-term. The former Debt Management Strategies provided a review of the achievements and developments during the previous year taking into account the composition of the debt portfolio, the fiscal operations and developments in the macro-economy and in the domestic and international capital markets.

69. The MTDS Toolkit assists in informing the appropriate borrowing strategy, which includes the issuance of debt instruments with certain characteristics (i.e. interest rate, maturity profile, and currency composition) with the objective of achieving a desired cost-risk profile. This will seek to facilitate development of the domestic capital markets. The MTDS Toolkit provides a quantitative framework to inform the choice of debt instruments to be issued.

70. The primary objectives of the MTDS are:

- Ensuring that the funding needs of the Government are met;
- Minimizing the cost of debt in the medium - term and the long term;
- Keeping risks in the debt portfolio at acceptable levels; and
- Promoting the development of the domestic debt market.

71. In general terms, the scope of the MTDS will include Central Government domestic and external debt, as well as the publicly-guaranteed external debt. Explicit domestic guarantees, although not included, are closely monitored and reported to the House of Representatives on a periodic basis. The amendment of the Financial Administration and Audit Act (FAA Act), as well as the enactment of the PDMA will support increased monitoring of explicit liabilities. Cost/risk analysis will be applied to new proposals for both central Government obligations and Government guarantees

VII. ASSESSMENT OF THE MACROECONOMIC ENVIRONMENT

Macroeconomic Environment

72. In evaluating the alternative debt strategies, the current macroeconomic outlook and medium-term fiscal policy framework were examined in order to assess their potential impact on the strategy options. The macroeconomic framework underpinning the MTDS is that of the macroeconomic programme.

Economic Activity

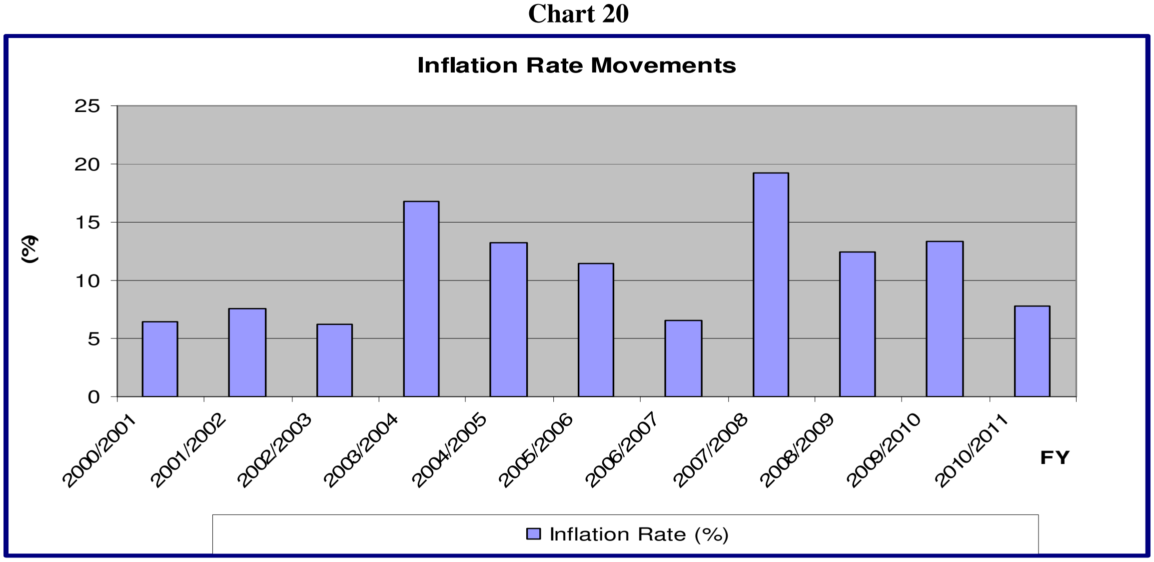
73. Economic growth remains negative, even though there are signs of improvement. Following a 2.5% decline in real growth in FY 2009/10, GDP was expected to grow by 0.6% in FY 2010/11; however, there was a decline of 0.7% for FY 2010/11. Despite this negative projection, tourism continues to show remarkable resilience, with stop-over arrivals attaining record levels in July and August. In addition, good weather conditions facilitated growth in the agricultural sector, while the mining sector has improved with the reopening of the West Indies Alumina Company Ewarton plant in June 2010. The sugar industry will receive a substantial boost in investment upon conclusion of the sale of the Government-owned sugar factories.

74. Unemployment remains high and was recorded at 12.4% at April 2010. At the same time, however, there have been some recent positive developments in the labour market, with positive job growth for the first time in four quarters. The FY 2009/10 outturn for the external current account deficit was 7.5 % and is projected to end FY 2010/11 at 8.3 %. Net International Reserves (NIR) stood at US$2,515.7mn at the end of FY 2010/11, a US$763.8mn increase over the US$1,751.9mn recorded at the end of FY 2009/10. There are signs of improvement in remittance flows and export earnings.

Inflation

75. Inflation has fallen significantly since 2008. The inflation rate for calendar year 2010 was 11.7% in comparison to the 10.2% that obtained for calendar year 2009. However, the outturn for FY 2010/11 is 7.8 %, 5.5% below the 13.3% recorded for FY 2009/10 (Chart 20).

Chart 20



Exogenous Shocks

76. Jamaica is vulnerable to most kinds of disasters, particularly floods and hurricanes. The inflation rate is strongly influenced by international commodity prices. In 2010, prices for both oil and non-oil commodities increased considerably, reflecting a combination of strong demand growth and supply shocks. These could have serious implications for the fiscal revenue. It is expected that this upward pressure in commodity prices will continue in 2011.

Public Finances

77. Despite the economic challenges the country faces, the Government remains resolute in meeting the medium term fiscal targets. In light of this, the Government has taken steps to implement a set of structural reforms: namely the Public Sector Reform, Tax Reform, and Public Expenditure Management, which aim at entrenching fiscal discipline and bolstering transparency. These reforms will help to ensure that the gains achieved to date will be sustained and deepened over the medium-term. The Central Government primary balance for FY 2010/11 was $53.4bn or 4.4% of GDP, compared to an outturn of $67.5bn or 6.1% of GDP for FY 2009/10 (Table 7).

78.

Table 7

Macroeconomic Indicators

	2008/09	**2009/10**	**2010/11**	**2011/12**	**2012/13**	**2013/14**
GDP, Prices and Employment						
Real GDP Growth (%)	-1.7	-2.5	-1.0	1.5	2.0	2.0
Inflation Annual Pt to Pt (%)	12.4	13.3	7.8	7.0	6.5	6.5
End of Period Exchange Rate	88.82	89.51	85.85	…	…	…
Unemployment rate (%)	10.8	11.4	…	…	…	…
Government Operations (in % GDP)						
Budgetary Revenue	26.9	27.1	25.7	25.9	24.7	24.7
Budgetary Expenditure	34.2	38.0	31.8	31.6	30.6	29.1
Primary Expenditure	22.0	21.0	21.3	21.8	20.5	19.8
Interest Payments	12.2	17.0	10.5	9.8	10.1	9.3
Budget Balance	-7.3	-10.9	-6.1	-4.6	-3.5	-2.3
Of which: Primary Fiscal Balance	4.9	6.1	4.4	4.2	4.2	4.9
Public Debt	116.8	129.3	128.3	126.1	125.2	113.8
External Sector						
Current Account Balance	-18.4	-7.5	-8.3	-6.7	-6.0	-5.5
Of which: exports of goods, f.o.b.	17.0	11.2	10.4	13.6	14.6	15.6
Of which: imports of goods, f.o.b.	50.0	35.4	33.7	37.4	39.3	41.2
Net International Reserves (in US$Mn)	1,628.6	1,751.9	2,515.7	1959.2	2,184	2,205

Financial Market

79. Domestic financial market conditions remain stable. At the end of FY 2010/11, the 6-month Treasury Bill rate declined to 6.63%, 386 basis points, from the 10.49% recorded for the same period in FY 2009/10. In addition, the BOJ has cut its open market rates to 6.75%, accommodating market trends. The Financial System Support Fund (FSSF) remains untapped indicating that financial institutions have weathered the impact of the JDX well.

VIII. DESCRIPTION OF ALTERNATIVE BORROWING STRATEGIES AND SCENARIOS

Four alternative Borrowing Strategies were evaluated in the 2011 MTDS

80. These strategies were analysed to determine the impact of changes in exogenous factors on Jamaica's public debt profile in the future to facilitate the decision making process of determining strategies that best reflect preferences for costs or risks.

Strategy I: Continue strategic path to a balanced portfolio

81. This strategy follows the current debt management practices of refinancing all maturing external bonds with new debt from external commercial and the multilateral sources, while the level of new domestic borrowing is based on financing the fiscal deficit.

82. This strategy also supports access to fixed rate long term funds from multilateral sources and in the current low interest rate borrowing environment, it is anticipated that funding from this source will continue in the short term, resulting in cost savings. The Government stands to benefit from lower debt servicing cost, notwithstanding the potential for foreign exchange risk.

83. Securities to be issued in the domestic market will be a combination of fixed and variable rate securities, together with a limited issue of CPI-Indexed Bonds to satisfy investors appetite. The issuance Strategy for these securities will be to minimize both roll-over and interest rate risks. With approximately 56.9% of the domestic debt scheduled to mature in the next five years, the strategy will include issuing securities along the yield curve with maturities greater than five years. The Government, being mindful that investors may resist some long-term securities, will employ the use of general reserves to guarantee adequacy of the cash flow.

84. The Government is aware that inherent in continuation of the existing strategy are potential foreign exchange, refinancing and demand side risks. Trade-off to these risks include some qualitative factors such as the development of the domestic capital market, a wide and diversified investor base comprising both local and foreign investors. The rationale for employing this Strategy is the achievement of a balanced portfolio over the medium term.

85. Strategy I will also promote the Government's objective of supporting and improving the development of the secondary market, through reopening of Benchmark Bonds through the auction mechanism, for greater price discovery.

Strategy II: More External Commercial Financing

86. Under this strategy, the share of market-based external fixed-rate financing is increased. The strategy assumes that all external financing will be on commercial terms and that some variable-rate domestic currency debt will be replaced with external commercial financing.

Strategy III: More Long-term Variable Rate Debt

87. This strategy option allowed for fixed-rate domestic debt to be replaced with longer term variable-rate domestic debt. The objective of this strategy is to lengthen the maturity in order to reduce the rollover risk in the medium-term as debt service payments are projected to increase within the next 3-5 years. The use of long-term variable-rate debt is to take advantage of potential reductions in the domestic interest rates during the medium-term, as the Government moves towards economic growth within the context of a balanced fiscal budget.

Strategy IV: More Long-Term Fixed-Rate Domestic Debt

88. Under this strategy, domestic debts maturing in the short-term (i.e. the next two to three years) are replaced with longer-term fixed-rate domestic securities. The objective of this strategy is to lengthen the maturity profile without increasing the interest risk which is inherent in Strategy III, and reduce the potential refinancing risks.

89. Table 8 presents a summary of the objectives underpinning the four (4) Strategy Alternatives, their implementing implications and the trade-offs involved.

Table 8

Overview of Debt Management Strategies

	S_I– Continue Strategic Path to Balanced Portfolio	S_{II} – More External Commercial Loans	S_{III} – More long-term Variable Rate Domestic Debt	S_{IV} – More long-term Fixed Rate Domestic Debt
Objective	Maintaining the Status Quo	Reduce refinancing & liquidity risks	Reducing Refinancing Risks	Reducing the Interest Rate and Refinancing Risks
Implementation	1. External Debt Financing replaces External Maturities 2. Domestic Financing covers deficit financing	External Financing on Commercial terms	More Variable Rate, Long term Domestic Debt	More Fixed Rate , Long term Domestic Debt
Trade-off	FOREX risks	Higher FOREX risks	Higher Interest Rate risks	Higher debt Service Costs over a long period, with Reduced Interest Rate risks

Description of Alternative Scenarios (Shocks)

90. The Borrowing Strategies were subjected to stress testing, under the following four (4) scenarios:

- **Increased domestic interest rate**: Under this scenario, interest rates on the domestic debt are increased across the board by 600 basis points. This upward shift in the yield curve is justifiable on the grounds that it is largely consistent with conditions prior to JDX and are, therefore, possible.
- **Higher interest payments on external debt:** Assuming continued volatility in the global financial markets and limited access to cheaper external financing sources, this scenario increases interest rates on foreign currency debt by 200 basis points.
- **Devaluation:** A one-off devaluation of 30.0% in FY 2011/12, followed by the trajectory of devaluation projected under the baseline. This shock may be probable in circumstances of rising oil and commodity prices on the international market, and Jamaica being a small, open economy, is susceptible to these exogenous shocks.
- **Combined scenarios:** This scenario combines an upward shift in the domestic and external yield curves, as well as devaluation. Over the medium-term, the domestic yield curve is shifted upwards by 300 basis points and the external yield curve is also shifted upwards but by only100 basis points. Additionally, a devaluation of 15.0% is applied in FY 2011/12.

Cost/Risk Analysis of Alternative Borrowing Strategies

91. The costs of alternative borrowing strategies under different stress tests were represented by:

(1) annual interest payments as a percentage of GDP; and
(2) total debt stock as a percentage of GDP.

92. The Interest-to-GDP ratio increases as maturities are lengthened and official external financing is replaced with financing on market terms (Table 10). The baseline strategy, therefore, dominates all other strategies with respect to costs and risks, if measured by Interest-to-GDP ratio. However, this ratio does not account for the rollover risks that result from the current bunching of debt repayments in the medium-term.

Table 9

Scenarios \ Strategies	S_I– Continue Strategic Path to Balanced Portfolio	S_{II} – More External Commercial Loans	S_{III} – More long-term Variable Rate Domestic Debt	S_{IV} – More long-term Fixed Rate Domestic Debt
Interest Cost / GDP (%)				
Baseline	9.2	9.4	9.4	9.4
Domestic Interest Rates increased by 6.0%	12.7	12.3	13.0	13.1
External Interest Rates increased by 2.0%	9.6	10.1	9.8	9.8
Devaluation of J$ by 30% in F/Y 2011/12	11.9	11.8	12.3	11.2
Domestic Interest Rate increased by 3.0%, External Interest Rates increased by 1.0% and a 15.0% Devaluation of the J$	11.9	12.0	12.2	12.2
RISKS (Deviation from Baseline)				
Domestic Interest Rates increased by 6.0%	3.5	2.9	3.6	3.7
External Interest Rates increased by 2.0%	0.4	0.7	0.4	0.4
Devaluation of J$ by 30% in F/Y 2011/12	2.7	2.4	2.9	1.8
Domestic Interest Rate increased by 3.0%, External Interest Rates increased by 1.0% and a 15.0% Devaluation of the J$	2.7	2.6	2.8	2.8

More external commercial debt

93. Financing in foreign currency is, from the perspective of interest costs, less expensive than financing in domestic currency. The increase in interest costs under Strategy II relative to the Baseline Strategy as a result of the devaluation may be mitigated over time as interest rates under Strategy II are lower when compared to the baseline. More external commercial debt increases Jamaica's exposure to a devaluation shock, in particular if measured by the Debt-to-GDP ratio as shown in Table 10.

Table 10

Debt-to-GDP (%)				
Scenarios \ Strategies	S_I– Continue Strategic Path to Balanced Portfolio	S_{II} – More External Commercial Loans	S_{III} – More long-term Variable Rate Domestic Debt	S_{IV} – More long-term Fixed Rate Domestic Debt
Baseline	102.3	103.2	102.6	102.7
Domestic Interest Rates increased by 6.0%	113.7	113.5	114.3	114.4
External Interest Rates increased by 2.0%	103.5	105.1	103.9	104.0
Devaluation of J$ by 30% in F/Y 2011/12	124.8	125.8	125.7	123.3
Domestic Interest Rate increased by 3.0%, External Interest Rates increased by 1.0% and a 15.0% Devaluation of the J$	118.6	119.8	119.0	119.2
RISKS (Deviation from Baseline)				
Domestic Interest Rates increased by 6.0%	11.5	10.3	11.6	11.7
External Interest Rates increased by 2.0%	1.3	1.9	1.3	1.3
Devaluation of J$ by 30% in F/Y 2011/12	22.5	22.7	23.1	20.6
Domestic Interest Rate increased by 3.0%, External Interest Rates increased by 1.0% and a 15.0% Devaluation of the J$	16.3	16.6	16.4	16.4

Increasing the share of domestic variable rate debt

94. The share of domestic variable rate debt in the debt portfolio is high under Strategy III. The portfolio would be particularly vulnerable to an increase in domestic interest rates. The shock would raise the interest cost by 3.6 % of GDP (Table 9). The interest risk becomes even more apparent when evaluating the percentage of debt to be re-fixed within one year (Table 11). Under Strategy III, more than 50 % of Jamaica's debt would be subject to re-fixing within a given year under all scenarios. ***Increasing the share of domestic variable rate debt, would further expose the debt portfolio to interest rate shocks.***

Table 11

Percentage of Debt to be Re-fixed in One Year				
Strategies / Scenarios	S_I– Continue Strategic Path to Balanced Portfolio	S_{II} – More External Commercial Loans	S_{III} – More long-term Variable Rate Domestic Debt	S_{IV} – More long-term Fixed Rate Domestic Debt
Baseline	44.0	39.0	51.5	40.1
Domestic Interest Rates increased by 6.0%	44.0	38.4	52.5	39.6
External Interest Rates increased by 2.0%	44.0	38.8	51.6	40.0
Devaluation of J$ by 30% in F/Y 2011/12	42.3	37.0	50.3	38.2
Domestic Interest Rate increased by 3.0%, External Interest Rates increased by 1.0% and a 15.0% Devaluation of the J$	43.1	37.6	51.2	38.9

More long-term Fixed Rate Domestic Debt

95. Under Strategy IV, interest costs would increase by 0.2 % of GDP relative to the baseline (Table 9). However, only approximately 40% of the debt would be subject to re-fixing in one year. In addition, the rollover risk would be reduced as principal payments would fall by about 2% of GDP in the medium-term. While demand for longer term fixed-rate instruments might be limited, issuing more instruments with these characteristics could be useful for reducing key risks inherent in Jamaica's current debt portfolio. However this strategy may be resisted by some market players, as there still exists a fairly high propensity to keep short funding positions.

IX. SELECTION OF BORROWING STRATEGY

96. Following extensive stress testing of the alternative strategies, the decision was taken to pursue Strategy I: **Continue Strategic Path to a Balanced Portfolio**. This will therefore focus on a continuation of the current debt management practices of refinancing all maturing external debt with new debt from external sources, combined with domestic borrowing along all segments of the yield curve. A limited amount of variable rate bonds and CPI-Indexed bonds will also be issued in the local market.

97. The analysis has shown that the share of variable rate debt in the portfolio is already high; therefore increasing the share of variable rate debt, as in Strategy III, would increase the exposure to interest rate shocks. Under this Strategy, the portfolio would be particularly vulnerable to an increase in domestic interest rates.

98. Under Strategy IV, increasing the share of fixed-rate long-term debt increases costs but reduces interest and rollover risk through fixed rates and extended maturities. Although interest costs would increase by 0.2% of GDP relative to the baseline, rollover risk would be reduced as principal payments would fall by about 2% of GDP in the medium-term. The additional risk associated with this option is the possible resistance by market players to an increased offering of long term debt securities, as there is still a fairly high propensity to maintain short funding positions. This would lead to potential liquidity risk to the cash flow.

99. With the lowering of domestic market interest rates in recent months, there has been a convergence of yields with those from external sources. Nevertheless, more external commercial debt would increase Jamaica's exposure to foreign exchange risk.

X. THE DEBT MANAGEMENT STRATEGY 2011/2012 AND IMPLEMENTATION METHODOLOGY

100. The objectives of the *Debt Management Strategy* continue to ensure that the funding needs of the Government are met at minimum cost in the medium and the long-term; while keeping risks in the debt portfolio at acceptable levels and promoting the development of the domestic debt market.

101. More specific objectives for FY 2011/12 are to:

- Restructure the Debt Management Unit;
- Pursue enactment of legislation governing debt management;
- Create and improve Benchmark Bonds along the Domestic Market Yield Curve;
- Issue New Domestic Bonds through the Auction Mechanism;
- Support and enhance the development of the Domestic Market;
- Generate reserves, to provide some flexibility in issuing long term instruments;
- Explore the feasibility of external liability management operations;
- Enhance communication with market players and rating agencies;
- Continue to engage multilateral institutions and bilateral creditors; and
- Apply rigid cost-risk analyses to Government Guarantees and Contingent Liability.

Restructuring of the Debt Management Unit

102. The current organisational structure of the DMU has limitations with respect to improving the efficiency of debt management. The restructuring of the Unit along the lines of Front, Middle and Back offices has therefore been recommended to achieve improvements in efficiency.

103. A detailed assessment of the requirements and measures needed to transform the Unit into a well-functioning office along the lines of international best practice has been completed. Assistance in this regard has been provided by the multilateral institutions and the Commonwealth Secretariat. The restructuring will facilitate additional analytical reporting on the Government's debt, improve efficiency by specialization of functions and enhance capacity building in the area of debt management. It is expected that the restructured unit will be fully operational by mid FY 2011/12.

Pursue Enhacment of Legislation Governing Debt Management

104. Work on the draft public debt management bill is currently at an advanced stage, and it is anticipated that the comprehensive PDMA will become a reality during the first quarter of FY 2011/12. The current law relating to public debt management is distributed among more than twenty (20) discrete pieces of legislation, some dating back to as early as the 1940s.

105. It is therefore being proposed that the existing Loan Act of 1964 and the various subsidiary loan acts be repealed and replaced with the PDMA, which would represent a coherent and comprehensive piece of legislation that takes a strategic approach to public debt management and reflects international best practice.

106. The proposed PDMA will speak to the Debt Management Committee (DMC) that has been established to among other things enhance the governance structure for public debt management. The DMC is a high-level advisory committee mandated to ensure policy co-ordination in the preparation of the debt strategy and to clarify and distinguish the roles and responsibilities of the official bodies concerned with public debt management.

107. The proposed PDMA will complement the recent legislative amendments to the Financial Administration and Audit (FAA) Act and the Public Bodies Management and Accountability (PBMA) Act which were undertaken within the context of the Fiscal Responsibility Framework. The amendments empower the Minister of Finance and the Public Service to improve the management of public finances through addressing the weaknesses in the current fiscal policy and administrative systems in Jamaica.

Creation and Improvement of Benchmark Bonds along the Domestic Market Yield Curve

108. Implementation of the MTDS will involve the issuance of four (4) new Benchmark Bonds and the reopening of a number of existing Bonds during FY 2011/12. The strategy also contemplates replacing domestic bonds maturing over the next two to three years with new long term bonds. In order to achieve this, a balanced issuance strategy for new Bonds will be executed targeting maturities ranging from 9 to 35 years, including amortizers. This objective will not only promote secondary market trading and enhance liquidity in the benchmark bonds, but is also geared towards the attainment of a balanced portfolio.

Issue New Domestic Bonds through the Auction Mechanism

109. Use of the auction mechanism to promote competitiveness through the bidding process for efficient price discovery will be maintained. Auctions will be conducted on a regular basis with issues along a wide spectrum of the domestic market yield curve (Figure No. 31). The auction of Treasury Bills will be managed in the Treasury Bill Module in the JamClear-CSD, commencing in the first quarter of FY 2011/12. During this financial year a review of the system will be finalized to facilitate the reopening of existing issues by auction through the CSD.

Support and Enhance the Development of the Domestic Market

110. The Government is committed to the development of the domestic market in order to foster a deeper and liquid market for local GOJ securities. This will be facilitated through the provision of technical assistance from the multilateral institutions. Following the dematerialization of Government of Jamaica securities in the JamClear-CSD, the platform has now been created for increased settlement efficiencies between the Government and market participants. The stage is now set for further development of the secondary market, through consultations with the BOJ, FSC and other key stakeholders on adjustments to certain regulations and limitations, such as prudential requirements in the local bond market, as well as the development of the private Reverse Repurchase Agreement (Repo) market. Consultations towards the establishment of a trading platform for domestic bonds will continue with the BOJ.

Generate reserves to provide some flexibility in issuing long term instruments

111. Implementation of the MTDS requires the issuance of long term fixed rate domestic securities. In order for this strategy objective to be successful, the need to build domestic reserves is critical, as the local market may exhibit a high propensity for short term securities, which has the potential to compromise the cash flow requirements. The pre-funding of future cash flow requirements will militate against this eventuality and provide the Government with the flexibility to execute the strategy.

Explore the feasibility of external liability management operations

112. Consistent with ensuring effective and proactive debt management the Government will seek to execute a market-friendly transaction, market conditions permitting, with the objective of smoothing the maturities of the external debt and reducing interest rate costs. Liability Management tools, including buy-backs and interest rate swaps of high cost external bonds for lower costs, will be employed.

Enhance Communication with Market Players and Rating Agencies

113. The Strategy includes the hosting of semi-annual investors' conference calls with the domestic and international capital market players. Consultations with the domestic market will be geared towards the process of implementing the debt strategy to assist with achieving the objectives of the Government's borrowing plan. The Government will host quarterly investors' fora with the investing community.

114. The Government will host investor presentations in North America. These presentations will provide information on the Government's medium-term macroeconomic programme and the status of the targets outlined therein. Scheduled dialogue with the Government's investor base is geared towards fostering greater awareness and transparency of debt operations and debt management objectives.

Continue to Engage Multilateral Institutions and Bilateral Creditors

115. The Government will continue discussions with the multilateral institutions and their affiliates to secure longer tenor and more cost effective financing for infrastructure development projects and for budgetary support. The strategy to seek cost effective financing from bilateral sources will continue during FY 2011/12.

Apply rigid cost/risk analyses to Government Guarantees and Contingent Liabilities

116. The impending PDMA, together with recent amendments to the FAA Act, make provisions for new requests for Government Guarantees to be subject to appropriate risk assessments, rigid monitoring and the payment of a risk fee. Resources will be provided to assist with execution of the strategy objective.

XI. ANNUAL BORROWING PLAN

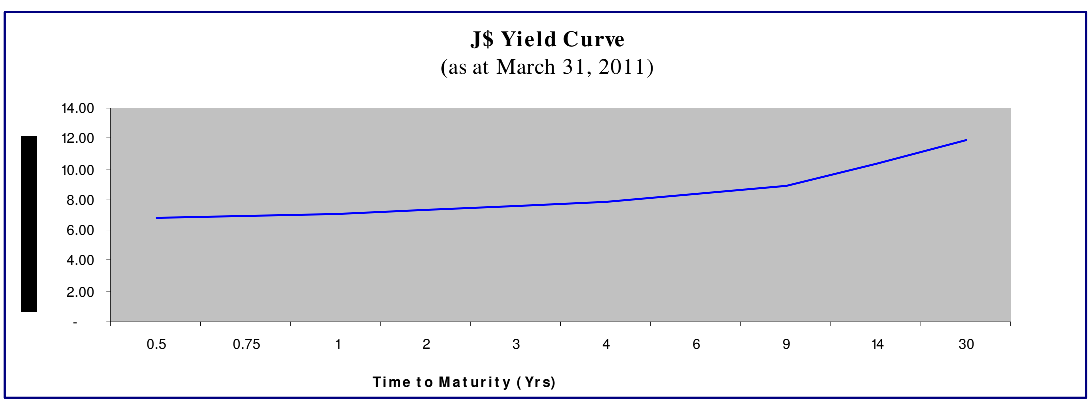
117. The Annual Borrowing Plan (ABP) is developed on the basis of the Debt Management Strategy and the Estimates of Expenditure, as tabled in the House of Representatives for FY 2011/12. The plan will allow prospective investors the opportunity to adjust their portfolios ahead of time in order to participate in Government issued securities. The borrowing requirement for the fiscal year is approximately **$140,778.2mn** broken down as follows (Table 12):

Table 12

Domestic Funding Source and Issuance Strategy			
Local Capital Market			**J$97,002.8Mn**
	2010/11	**2011/12**	
		Lower Limit %	**Upper Limit %**
Fixed Rate	98.9	93.5	95.0
Variable Rate	1.1	4.0	4.5
CPI-Indexed	-	0.1	0.5
External Funding Source			
Multilateral:			
World Bank		US$100.0Mn	
IDB		US$220.0Mn	
Other Sources:			
Existing Project Loans		US$183.4Mn	

118. **Issuance Strategy for Domestic Debt.** The Government will issue four (4) new long-term Fixed Rate Benchmark Notes with maturities ranging from 9 to 30 years, together with the reopening of existing Benchmark Notes along the J$ Market Yield curve (Chart 21). In addition to the securities listed above, the Government will issue on a monthly basis, three (3) series of Treasury Bills.

Chart 21



XII. CONCLUDING REMARKS

119. The development and implementation of the Medium-term Debt Management Strategy, in conjunction with Government's *Medium-term* Expenditure Framework, should aid in the transformation of the current Central Government debt portfolio into a fully optimized and balanced portfolio, characterized by sustainable levels of refinancing, interest rate and foreign exchange risks. The success of the MTDS is therefore contingent on the successful rollout of all the components that form a part of the overall Fiscal Responsibility Framework. The MTDS Analytical Tool will help to quantify the cost and risks associated with different scenarios on the alternative borrowing strategies that will support, enhance and preserve a balanced portfolio under a variety of alternative business environments.

Audley Shaw, MP
Minister of Finance and the Public Service
April 28, 2011

A C R O N Y M S

ABP	-	Annual Borrowing Plan
AT	-	Analytical Tool
BOJ	-	Bank of Jamaica
CDB	-	Caribbean Development Bank
CDI	-	Commonwealth Death Initiative
CG	-	Central Government
CTMS	-	Central Treasury Management System
DFID	-	Department for International Development
DMU	-	Debt Management Unit
EMBI	-	J.P. Morgan Emerging Market Bond Index
FAA Act	-	Financial Administration and Audit Act
FR	-	Fixed Rate
FRF	-	Fiscal Responsibility Framework
FSC	-	Financial Services Commission
FSSF	-	Financial System Support Fund
GDP	-	Gross Domestic Product
GOJ	-	Government of Jamaica
GSDA	-	Government Securities Dematerialization Act
IBRD	-	International Bank for Reconstruction and Development (also, The World Bank)
ICM	-	International Capital Markets
IDB	-	Inter-American Development Bank
IMF	-	International Monetary Fund
JamClear-CSD	-	Jamaica Clearing and Settlement Assured in Real Time, Central Securities Depository
JDX	-	Jamaica Debt Exchange
LRS	-	Local Registered Stocks
MOFPS	-	Ministry of Finance and the Public Service
MTDS	-	Medium Term Debt Management Strategy
NIR	-	Net International Reserves
PBMA	-	Public Bodies Management and Accountability Act
PDMA	-	Public Debt Management Act
SBA	-	Stand-by Arrangement
SCJ	-	Sugar Company of Jamaica
S & P	-	Standard & Poor's
TSA	-	Treasury Single Account
VR	-	Variable Rate
WINDALCO	-	West Indies Alumina Company

XIV. GLOSSARY

Amortization
Amortization refers to principal repayments on loans. These repayments reduce the borrowed money by portions, which are usually fixed amounts expressed as a percentage of the whole. Most of the domestic debt has a bullet repayment - the entire principal is repaid at maturity rather than gradually over the term of the loan.

Auction
An auction is a system by which securities are bought and sold on a competitive bidding process. The auctions are conducted on a multiple-price-bidding basis, which means that the successful investor will receive stocks at the price he bids.

Benchmark Issues
Issues of securities that are sufficiently large and actively traded, such that their prices serve as reference for other issues of similar maturities.

Commonwealth Debt Initiative (CDI)
A programme of the Government of the United Kingdom launched in 1997 to cancel the debt of poor to middle-income Commonwealth countries that are committed to international development targets.

Consolidated Fund
The Consolidated Fund is the principal Government account to which all Government revenues must be deposited and from which expenditure, via warrants, is withdrawn.

Contingent Liabilities
The potential obligations of the Government, as guarantor, having provided a form of security to the lender for a loan or credit facility on behalf of a public sector entity.

Debt Service Payments
Debt service payments cover interest charges on a loan. Some sources also include amortization under debt service payments. These payments liquidate the accrued interest (and loan obligations if amortization is included).

JP Morgan Emerging Markets Bond Index (EMBI)
The EMBI is a benchmark index for measuring the total return performance of international government bonds issued by emerging market countries. Inclusion in the index requires that the debt be more than one year to maturity, have more than $500 million outstanding, and meet stringent trading guidelines to ensure that pricing inefficiencies don't affect the index.

Eurobond
A bond underwritten by international investors and sold in countries other than the country of the currency in which the issue is denominated. Jamaica issued a five-year, US$200mn Eurobond in July 1997, its first ever.

Inflation-Indexed Bonds
Inflation-Indexed bonds are securities with the principal linked to the Consumer Price Index. The principal changes with inflation, guaranteeing the investor that the real purchasing power of the investment will keep pace with the rate of inflation. Although deflation can cause the principal to decline, at maturity the investor will receive the higher of the inflation-adjusted principal or the principal amount of the bonds on the date of the original issue.

Local Registered Stock (LRS)
The term refers to medium and long term debt instruments issued by Government. LRS is issued both to finance Government operations and to support macroeconomic and monetary objectives. Since October 1999, LRS has been offered to the market using the auction system.

Par
Par is the nominal or face value of a security. A bond being issued at par, for example at $100, is worth the same $100 at maturity.

Project Loan
The term refers to loans, which fund capital development activities. The term capital refers to lasting systems, institutions and physical structures. Project loans are typically funded from foreign sources by bilateral/multilateral institutions.

Public Debt Charges / Public Debt
Public debt refers to the loan obligations of Central Government. The obligations of Government entities are also included if such entities are unable to meet their obligations. The entities, however, are then indebted to the Central Government. Public debt charges are interest payments on the loan obligations and include related incidental expenses such as service fees, late payment penalties and commitment fees.

Schedule B/Shelf Registration Statement
A facility with the US Securities Exchange Commission, which allows for the registration of securities intended to be issued in the future.

Sovereign Rating
A sovereign rating is an assessment of the default risk for medium and/or long-term debt obligations issued by a national Government (denominated in foreign currency), either in its own name or with its guarantee. Ratings are produced by independent agencies (Moody's Investors Service, Standard & Poors and others). The ratings provide a guide for investment risk to capital market investors.

Treasury Bill
Treasury Bills are instruments designed to provide Government with short-term financing to meet temporary cash needs arising from fluctuations in cash revenue. Treasury Bills are no longer limited in use to this strict interpretation. They are now being used by Government as a tool in its open market operations for liquidity management.

US Dollar Indexed Bonds
Interest and principal are protected from adverse changes in the exchange rate as adjustments are made for movements in Jamaica dollar vis-à-vis the US dollar.

Interest payments are made on a fixed rate basis on the exchange rate adjusted principal.

The index for measuring the applicable rate of exchange has been the 10-day moving average selling rate as published by the Bank of Jamaica 10 days prior to the respective due dates. Interest and principal are generally payable in Jamaica dollars. US Dollar Indexed Bonds were introduced in July 1999.

Yield Curve

A line graph showing the interest rates at specific points in time by plotting the yields of all securities with the same risk but with maturities ranging from the shortest to the longest available. The resulting curve shows if short-term interest rates are higher or lower than long-term interest rates.

XV. ACKNOWLEDGEMENT

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APPENDIX I
SIGNIFICANT DEVELOPMENTS IN DEBT MANAGEMENT

▪ July 1997	– Jamaica's entry into the International Capital Markets
▪ March 1998	– Initial sovereign rating by Moody's Investors Service
▪ April 1, 1998	– Establishment of the Debt Management Unit
▪ April 1998	– Consolidation and centralization of debt management functions within the Ministry of Finance and Planning
▪ June 1999	– Long-Term Savings Accounts introduced
▪ June 1999	– Implementation of 15% tax on interest withheld at source
▪ July 1999	– US$ indexed-linked bonds introduced in the domestic market
▪ October 1999	– Auction system for the sale of Local Registered Stocks (LRS) introduced
▪ November 1999	– Initial sovereign rating by Standard & Poor's
▪ April 2000	– First publication of the *Debt Management Strategy*
▪ April 2000	– Implementation of 25% tax on interest withheld at source
▪ March 2001	– Jamaica included as case study in IMF/World Bank publication of *Guideline for Public Debt Management*, as implementing prudent debt management practices consistent with the Guidelines
▪ April 2001	– First 12-year LRS sold by auction. A total of six 12-year LRS' issued by auction during FY 2001/02
▪ May 2001	– First 10-year global Eurobonds issued
▪ December 2001	– First 20-year Eurobonds issued
▪ December 2001	– Schedule B Registration Statement filed with the United States' Securities and Exchange Commission (US SEC)
▪ February 2002	– "Shelf" Registration Programme established with the US SEC
▪ June 2003	– First 15-year LRS sold by auction
▪ September 2003	– First 30-year LRS sold by auction
▪ April 2004	– Launch of quarterly Investors' Conference Call
▪ November 2004	– Publication of quarterly financing requirements
▪ March 2005	– Jamaica selected as a member of the Steering Committee on the Latin American and Caribbean Debt Group
▪ May 2005	– Jamaica ended its borrowing relationship with the IMF by fully repaying all outstanding debt to that institution
▪ June 2005	– Air Jamaica, the national airline, successfully accessed the international and regional capital markets
▪ February 2006	– First 30-year global Eurobonds issued
▪ March 2007	– First 32-year amortizing Eurobonds issued
▪ October 2007	– First large and liquid bond with eligibility to the JP Morgan Emerging Bond Index (EMBI)
▪ January 2010	– Launch of the Jamaica Debt Exchange (JDX)
▪ February 2010	– Exchange of 350 small bonds to 25 liquid benchmark bonds
▪ February 2010	– Dematerialization of GOJ Securities
▪ February 2011	– Second GOJ Global Bond to enter the EMBI