SPEECH TO THE CARIBBEAN ASSOCIATION OF INVESTMENT AND FINANCIAL ADVISORS BY

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WE ARE A PEOPLE OF GREAT POTENTIAL

I am fascinated by science.

One of the many fascinating facts in the biological sciences is the fact that embryos of remarkably different species are astonishingly similar.

This was a fact known by early 19^{th} century scientists:

You cannot easily distinguish between species by looking at the embryos of mammals, birds, reptiles, or fish in the early stages.

However, we know that embryos eventually become very different animals.

What makes the difference is the DNA in each of those embryonic cells, which contain the code for their development.

Some have DNA of elephant, others the DNA of an ANT.

Applying the metaphor to Jamaica, in my capacity of Minister of Finance, I have always thought that Jamaica has elephant DNA.

We, like other Caribbean countries, have the capacity to become economically great.

And, as far as the Ministry of Finance is concerned, we will achieve this by a focus on policies and programmes geared towards:

- Achievement and maintenance of Economic Independence
- Economic Expansion for All
- Protection of the Vulnerable

ECONOMIC INDEPENDENCE

Economic Independence means many things and I will have a lot to say about this over time.

Economic independence is not an absence of inter-dependence.

Jamaica is a small, open economy where trade in goods and services as a percentage of GDP is very high at over 60%. There will always be inter-dependence.

Economic independence, however, means among other things, not being dependent on creditors for our basic needs.

Economic independence requires us to manage our economy in such a way that we create the fiscal space to pursue priorities.

Economic independence requires that policy-making does not just consider today, but it also considers tomorrow.

Economic independence requires long-term thinking.

The pathway to achieving and maintaining economic independence must also take account of our context and realities.

A significant feature of the Jamaican and Caribbean reality is that we are subject to natural disasters, hurricane, windstorms, flooding, drought and even earthquakes, from time to time.

According to data from the Association of Caribbean States there were 165 natural disasters in the Caribbean between 1990 and 2008.

Natural disasters have a fiscal cost, and sometimes a profoundly large fiscal cost.

Natural disasters can result in unplanned public expenditure or the reallocation of already committed financial resources to reconstruct, repair and/or rehabilitate roads, bridges and public buildings and to provide support to victims.

Budgetary revenues also fall in natural disasters as, on a net basis, economic activity is often curtailed.

As a consequence, governments often face budgetary pressures at exactly the wrong time and flows of foreign exchange decline as tourism is often affected.

As a result, central bank reserves come under pressure, the need to borrow domestically and overseas increases at a time when interest rates are probably moving upwards as a response to the effects of disaster.

In short, as we have experienced in Jamaica and the Caribbean, the scale of natural disasters can overwhelm public resources.

Instead of using absolute values, damage is better expressed as percentages of GDP of the countries affected by disasters in each year to allow for comparisons across time.

According to a paper written by Omar Bello from Economic Commission for Latin America and the Caribbean (ECLAC), the Caribbean is the region, within the Americas, in which disaster damage, on average, has represented the largest share of GDP, surpassing 8% seven times between 1972 and 2010. The damage to Grenada in 2004 and Dominica in 2017 was estimated at 200% of GDP.

Today, and for the next 18 months Jamaica is in a Precautionary Stand-By Arrangement with the IMF. Within the context of this program with the Fund, we have access to significant resources should we need them.

As we move towards the end of this monitored, program relationship with the IMF with the commensurate stand-by line of credit that it offers, it is important that we consider measures that can moderate the fiscal impact of natural disasters.

Natural disasters have the potential to set small countries back for years. Jamaica has done too much work, made too many sacrifices to leave us completely exposed, in a post IMF-Program environment, to the potential fiscal impact of natural disaster.

While we won't be able to insulate ourselves completely our ambition for economic independence must mean that we do all that we can.

OUR CURRENT PROTECTION IS INADEQUATE

Today, public bodies usually insure their assets.

For example, the NHT pays over J$1 billion in premiums each year to cover the houses on which it has mortgages.

The Port Authority spends approximately $200 million in premium each year to cover hurricane, flood, earthquake exposure for all of its facilities and assets.

However, the Central Government has no analogous coverage for the assets across Ministries and Departments, no coverage for the hundreds of public buildings, police stations, schools, libraries, offices, roads, highways and bridges where the value at risk is in the trillions of Jamaican dollars.

There is no provision to provide cover for these assets on a commercial basis; instead consecutive governments of Jamaica have always opted for self-insurance, which means meeting the costs of natural disaster out of recurrent expenditure.

The question is whether we should continue to operate in that way as the evidence suggests that the frequency and intensity of natural disasters are increasing.

THE WAY FORWARD

The appropriate approach for the Caribbean at this time must consist of the appropriate mix of disaster risk mitigation, adaptation and financing strategies.

There is a lot of innovation internationally and regionally in each of these areas but today I will focus on the financing component.

Among the suite of financial strategies that Jamaica must consider are:

(a) Negotiation of Contingent Credit Facilities for Natural Disasters with multilateral institutions.

These would provide credit financing and rapid cash disbursement in the aftermath of a natural disaster on pre-agreed terms.

The last thing that any government wishes to do in the immediate aftermath of a natural disaster is to be negotiating for financing at that point.

Instead, negotiate beforehand, and be in a position that the Jamaica can drawdown on liquid resources immediately after a disaster.

The advantage of this approach is that the fiscal costs in the years preceding a natural disaster are minimal.

The disadvantage, of course, is that the drawdown would be loan funds.

(b) Catastrophe Bonds

Another product for Jamaica and Caribbean countries to consider is Catastrophe Bonds or 'Cat' Bonds.

Cat Bonds are risk-transferring securities that can be used by a country to transfer the risk of a catastrophic event, over a multi-year period, to the international capital markets.

The Country sponsoring the Cat bond pays an annual premium and the Cat bonds pays out on the occurrence of a natural disaster that meets the agreed criteria.

An advantage of Cat bonds is that they provide payout triggered by the severity of an event rather than by dollar estimates of damages so payouts can happen quickly once the trigger has been met allowing governments to provide emergency relief.

A disadvantage is that Cat bonds require budgetary space to fund premiums and designing the appropriate trigger can be difficult

(c) <u>Natural Disaster Sovereign Fund</u>

Jamaica could also consider allocating a portion of the budget each year to fund a natural disaster sovereign fund, until the fund was of sufficient size that can be used in the event of a natural disaster.

(d) <u>Accessing Climate Financing for Adaptation and Mitigation to build resilience</u>

Global climate funds have mushroomed in size, number and complexity over the past few years. They offer scope to provide project financing for countries to improve resilience, which in the long run reduce cost of disaster risk management.

None of these is a silver bullet and none can be used exclusively or for one period of time. The point is that Jamaica needs the appropriate mix of solutions that can meet our needs and that we can afford and that are continuously applied.

Perhaps too there is need to collaborate with other Caribbean countries to diversify risks and thereby reduce the costs.

Public Financial Management Policy Strategy for Natural Disaster Risk

Given our focus on economic independence, prior to the end of the Precautionary Stand-By Arrangement with the IMF Jamaica will develop, with the technical assistance of our partners, a Public Financial Management Policy for Natural Disaster Risk combined with a ten-year operational plan for its implementation.

This Policy will consider Jamaica's fiscal realities, our natural disaster fiscal exposure, the pros and cons of various solutions available, our resource envelope and existing literature. The policy will improve understanding of fiscal risks of natural disaster, and recommend appropriate financial management of natural disaster risk including the implementation of various financing strategies.

We must be reminded that Economic Independence for Jamaica requires us to carry our umbrella.

INSTITUTIONAL CAPITAL IS CRUCIAL FOR ECONOMIC EXPANSION

Expansion of Jamaica’s economy is a crucial imperative and institutional capital can play a critical role.

By “institutional capital”, I mean money that is held by pension funds, insurance companies, collective investment schemes and security dealers all of which are regulated, in addition to unregulated pools of capital that are managed professionally by third party managers.

According to the 2017 Financial Stability Report from the Bank of Jamaica:

The asset base of the Non Deposit Taking Financial Institutions was approximately J$1.7 trillion as at end-September 2017.

Non-Deposit taking Financial Institutions include pension funds, collective investment schemes, securities dealers, life insurance companies and general insurance companies and so we can take this number as a proxy for the institutional capital available in Jamaica.

It is made up of:

- The on-balance sheet and off-balance sheet funds under management by security dealers which was approximately J$1.1 trillion as at end-September 2017

- Private pension funds, which had J$0.5 trillion of assets under management at the end of 2017.

- Life insurers, which had approximately $300 billion of assets.

- General insurers had approximately $75 billion of assets

There is some overlap as, for example, pension funds have investments with security dealers but in unique dollars the Bank of Jamaica publication reports a total of J$1.7 trillion of institutional capital in Jamaica.

By comparison the Financial Stability Report stated that the asset base of Deposit Taking Institutions was J$1.5 trillion.

So, the non-banking financial sector is larger than the banking financial sector and with assets heading fast towards $2 trillion Jamaican dollars.

We want to ensure that while macro prudential stability is maintained and entrenched, the regulatory framework for the non-bank financial sector provides a foundation that allows for the deepening of financial inclusion and the acceleration of economic expansion.

The reduction in government borrowing—public debt now projected to fall below 100 percent of GDP by end March 2019— creates real opportunities to accelerate our efforts to convert and re-direct savings into investment, job creation and economic empowerment for all Jamaicans.

In the near term this will involve a focus on a revised investment framework for pension funds and insurance companies.

In parallel, we will focus on creating opportunities for improved access to credit and financial services to support business and entrepreneurial activity across the board, as envisaged in the National Financial Inclusion Strategy.

I am pleased to announce that Bank of Jamaica has retained the services of Mr. David Marston, former Senior Advisor and Chief Risk Officer of the IMF, current member of the Eminent Persons Group of the G-20 and a Jamaican, to support Governor Wynter in leading these initiatives.

The intention is for a consultative process that will lead to actionable policy, legislative and reform initiatives to accelerate and deepen the role of finance and institutional capital in supporting inclusive economic expansion while maintaining financial sector stability.

CONCLUDING REMARKS