20 February 2023

BANK OF JAMAICA INCREASES CASH RESERVE REQUIREMENTS AND MAINTAINS POLICY RATE

At its meeting on 16 and 17 February 2023, the Monetary Policy Committee (MPC) unanimously decided to **increase by one percentage point (pp) the domestic and the foreign currency Cash Reserve Requirements (CRRs) applicable to deposit-taking institutions (DTIs), effective 01 April 2023.** This decision represents a part of the central bank's efforts aimed at underpinning the return of inflation to the target range of 4.0 to 6.0 per cent.

Currently, DTIs are required to hold a minimum of 5.0 per cent of their Jamaican dollar-denominated prescribed liabilities and 13.0 per cent of their foreign currency-denominated prescribed liabilities as cash reserves at the central bank. The domestic currency CRR had been reduced progressively from 12.0 per cent at the start of 2019 to 5.0 per cent in the context of an extended period of low and stable inflation. The Bank had also maintained a constant differential between the domestic currency CRR and the foreign currency CRR over much of the period. With this adjustment, **the domestic currency CRR will be increased to 6.0 per cent and the foreign currency CRR will move to 14.0 per cent.**

The MPC also decided to maintain the policy interest rate (the rate offered to DTIs on overnight placements with BOJ) at 7.0 per cent and continue to maintain relative stability in the foreign exchange market.

The decisions were informed by the MPC's view that, while incoming data were generally favourable for the inflation outlook, risks to inflation had become elevated. Jamaica's inflation rate of 8.1 per cent at January 2023 was below the rate of 9.4 per cent at December 2022. Core inflation (which excludes food and fuel prices from the CPI) also decelerated to 7.1 per cent at January 2023 from 8.5 per cent at December 2022. The pace of monetary tightening by the United States (US) Federal Reserve Board (Fed) also appeared to be slowing, as expected, and future rate increases by the Fed will likely be moderate. The key external drivers of headline inflation, such as grains, fuel and shipping prices, continued to decline and the forecasts for these variables have been lowered. Inflation expectations continued to track downward.

In this context, consistent with global consensus forecasts for a fall in commodity prices and the Bank's overall monetary policy stance, and in the absence of any new shocks, inflation is projected to continue to decelerate in 2023. This forecast envisages that annual inflation will fall within the Bank's inflation target range of 4.0 to 6.0 per cent by the December 2023 quarter and remain generally at that level over the medium-term.

The near-term risks to the inflation outlook are however elevated and skewed to the upside. In a context where the domestic economy continues to grow, labour market shortages carry the potential for future wage adjustments that can put upward pressure on inflation. The projected level of liquidity in the financial system, if left unchecked, poses material risks to the achievement of the inflation target as well as to the maintenance of stability in the foreign exchange market. Higher inflation could also ensue from a worsening in supply chain conditions and higher commodity prices if there are further geo-political disruptions. On the downside, weaker than expected global growth could negatively affect domestic demand and some projected adjustments to regulated prices may not materialize.

In the context of these risks, the Committee concluded that to further underpin inflation returning to the target range and to underwrite continued stability in the foreign exchange market, the additional precautionary liquidity control measure of increasing the CRR was required.

In terms of the macroeconomic outlook, the Jamaican economy continues to grow strongly. Gross domestic product (GDP) for fiscal year 2022/23 is now projected in the range 4.0 to 5.5 per cent, exceeding the upper limit of the range previously anticipated by the Bank. The GDP outturn for the September 2022 quarter was higher than the Bank had anticipated and there are signs that the economy continued to expand for the December 2022 quarter and for the March 2023 quarter to date. GDP growth for FY2022/23 is being driven by the services industry, particularly tourism.

For FY2023/24, GDP growth is projected to moderate somewhat, as income growth among Jamaica's main trading partners normalises to pre-COVID rates.

In the absence of new shocks, future monetary policy decisions aimed at returning inflation to the Bank’s target range, including further adjustments to the cash reserve requirement, will depend on the state of liquidity in the financial system and the continued pass-through effect of monetary policy on deposit and loan rates. The decisions will also depend on the MPC seeing more pass-through of international commodity price reductions to domestic prices and on the Fed continuing to slow its policy rate increases.

Bank of Jamaica will continue to closely monitor the global and domestic environments for potential risks that could further threaten the attainment of Jamaica’s inflation target.

A summary of the Monetary Policy Committee’s discussions, which influenced the monetary policy decision, has been published on the Bank’s website at https://boj.org.jm/core-functions/monetary-policy/policy-schedule/summary-of-decisions/.

The date of the next policy decision announcement is 29 March 2023.

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