Bank of Nova Scotia Jamaica Limited 1997

ECONOMIC OVERVIEW

The 1997 performance of the Jamaican economy was highlighted by certain positive achievements. The most outstanding of these was the substantial deceleration in the rate of inflation from 22.76% for the year ending October 31, 1996 to 9.98% for the corresponding period of 1997.

Other achievements included:-

- Price stabilization
- Reduction of growth in money supply
- A slow down in the growth of imports
- Continuation of relatively high levels of capital inflows
- A further build up in the Net International Reserves (NIR)
- A relatively stable exchange rate
- Continued growth in inflows of remittances.

Despite these achievements, the economy showed few signs of recovery. The continued downturn in the real sector was reflected in reduced export levels coupled with falling imports of raw material and related capital goods. Prospects for growth were also affected by Government's tight monetary policy.

The agricultural sector declined overall, due mainly to the effects of drought on domestic crops. Sugar production fell below the 1996 level, while banana exports were lower than in 1996. Manufacturing output also dropped below the levels attained in 1996. This sector suffered from a combination of high interest rates, high utility costs, low domestic demand and competition from cheaper imports. As a result, some operations down sized, while others were forced to close. However, Tourism, one of the main service sectors, recorded an increase in earnings during the year.

THE FINANCIAL SECTOR

The financial sector experienced significant difficulties during the year, mainly as a result of the Government's tight monetary policy and deficiencies in the management of some financial institutions. Lack of confidence in the commercial banking sector produced runs on a number of smaller commercial banks.

Problems in the insurance industry continued into 1997 mainly because of the mismatch of company assets and liabilities. Short term liabilities were used to finance costly long-term assets. With the downturn in the economy, and the slowing of inflation, the high real interest rates resulted in a liquidity crisis in the insurance industry.

The Financial Sector Adjustment Company (FINSAC) was formed by Government to provide financial support for the financial sector, in recognition of its critical role in economic growth and development. FINSAC will likely help to enhance the viability and efficiency of the sector, in addition to restoring its public confidence.

Government has now, through FINSAC, become a direct participant in commercial banking. The overall health of the financial sector will depend on the Government's fiscal and monetary policies. The current policy direction will perhaps lead to further consolidation of the sector.

OUTLOOK

Tight fiscal policy is expected to help consolidate the inflation gains attained in 1997. The transition to a lower inflation environment, which was the focal point of Government policy in 1997, required a significant growth trade-off. As the lower inflation trend becomes well established, appropriate adjustments must be made to foster economic growth and development, while maintaining an environment of stability.

There is much optimism that the productive sectors will stabilize. At the micro level, there are indications of increasing levels of capital utilization and re-tooling by firms. While it may not be possible to remove all the disincentives, the Government is committed to supporting the sector through fiscal incentives, training and technical assistance programmes, and aggressive investment and trade promotion activities. As well, the Government has stated its commitment to remedy infrastructural deficiencies.