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PROVEN FUND Managers

1st Quarter 2018 Economic Analysis - Jamaica

Gross Domestic Product (Real GDP)

For the quarter ended December 2017, real GDP grew by an estimated 1.1% relative to the corresponding quarter in 2016. The Goods Producing, and Services industries grew by an estimated 1.2% and 1.1%, respectively. The main contributors to growth in the Goods Producing Industries were the Mining & Quarrying, Manufacturing and Construction sectors that grew by 14.7%, 0.3% and 0.7% respectively. The Mining & Quarrying industry benefitted from higher production levels at the alumina plants. The Manufacturing industry's performance was attributed to increased output from both the Food, Beverages & Tobacco and Other Manufacturing sub-industries. The Construction industry's performance reflected increased activities in the building construction components. This significant improvement, however, was negated by a 1.1% decrease in the Agriculture, Forestry, & Fishery industry due to unfavourable weather conditions during the quarter. This contraction in Agriculture, Forestry, & Fishery was driven primarily by a 10.7% reduction in growth in Traditional Export Crops.

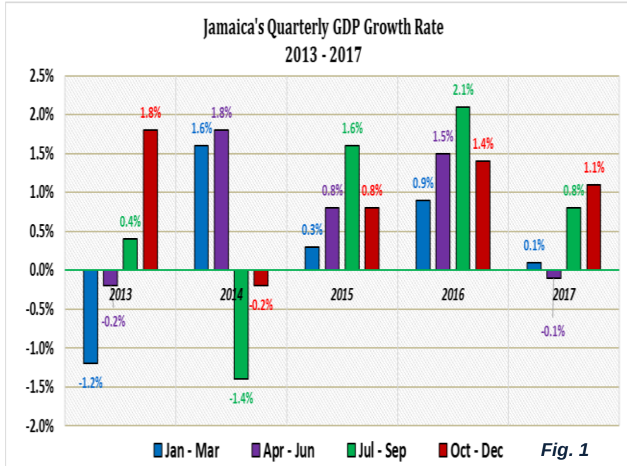


Fig. 1

All sub-categories of the services industry saw improved quarter on quarter performance. The sub-categories which estimated to have recorded the largest increases in the services industry are the Hotels & Restaurant and Other Services industries which recorded increases of 5.8% and 1.4%, respectively. Whilst the increase in the Other Services sub-category was due to higher recreational, cultural & sporting activities, the Hotel and Restaurant sub-category grew due a 13.7% increase in stopover arrivals with a smaller average length of stay of 7.7 days when compared to the average of 8.2 days as at February 2017.

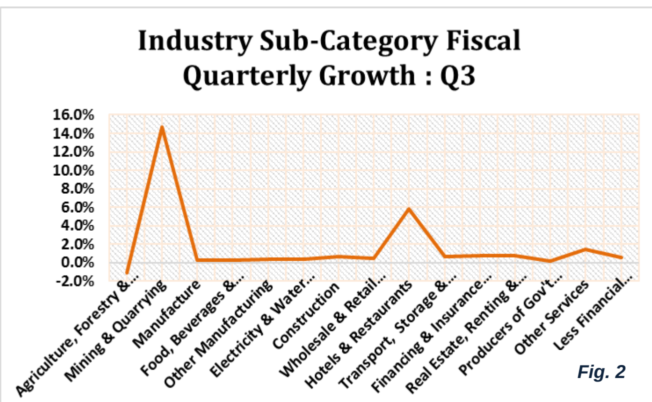


Fig. 2

The total labour force for October 2017 decreased by 0.5% or 6,500 persons to 1.35M persons when compared to the same month last year. The total employed labour force increased by 27,000 persons to 1.21M persons over the same month in the previous period. The total unemployed labour force went in the opposite direction and fell by 33,700 persons to 1.21M persons over the same month in the previous period. This net increase translated to a lower unemployment rate for October 2017 of 10.4% compared to 12.9% in October 2016.

Fiscal Accounts

Total revenues and grants for the fiscal period April to February 2018 stood at J$476.14B, 2.4% or J$11.05B over the budgeted J$465.09B. Total expenditure was 3.0% or J$15.21B below the budgeted J$499.97B at J$484.76B. This translated to a fiscal deficit of J$8.61B, 75.3% or J$26.B ahead the budgeted deficit of J$34.87B. The primary surplus, over the same period, was 22.2% over the budgeted J$95.54B at J$116.78B.

Lower than budgeted expenditure in tandem with the strong revenue performance have contributed to the primary balance outturn exceeding target. Against this backdrop of strong revenue performance, the GOJ, in the face of damage to infrastructure from excessive rainfall as well as the adverse impact of crime, utilized the increased fiscal space to address the damage to infrastructure, including roadways; and to facilitate the declaration of certain areas as Zones of Special Operations (ZOSO), with the aim being to significantly reduce crime.

This 11-month performance has placed the government in good stead in achieving its estimated budget surplus of J$1.77B and primary balance of J$132B for the fiscal year ended March 31, 2018. With the new precautionary SBA with the IMF, the GOJ is expected to continue to practice fiscal discipline and keep debt on its downward trajectory.

The success of the government's debt reduction strategy is dependent on their maintenance of fiscal prudence and consistency while improving GDP growth in a challenging economic climate.

Foreign Exchange

The JMD/USD foreign exchange (FX) rate as at the end of March 29, 2018 stood at J$125.98, representing a 0.98% in depreciation, YTD (January 2, 2018: J$124.76). Supported by measures to strengthen the operation of the foreign exchange market including a lowering of the foreign exchange surrender requirements and a more transparent auction system for interventions by the Bank of Jamaica, the local currency appreciated by 2.9% for FY 2017/18 through end-December 2017. For the 2017 calendar year, the local currency appreciated by 2.7% compared to a depreciation of 6.7% for the previous calendar year.

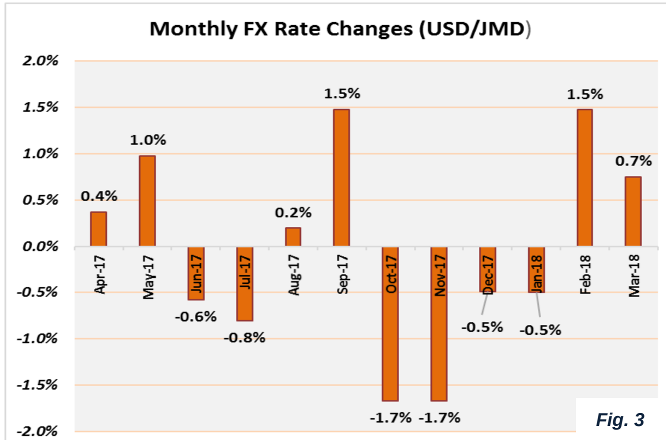
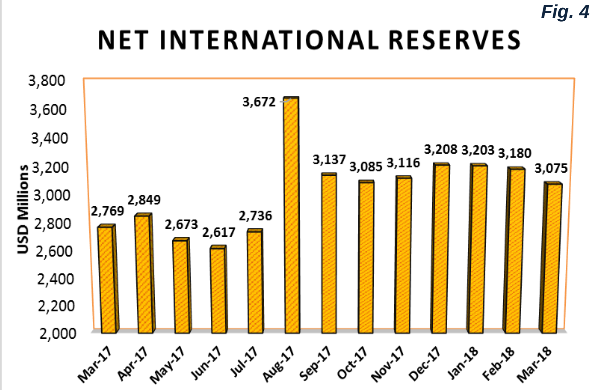


Fig. 3

On March 13th, 2018, the BOJ conducted its first exercise in which they pre-announced, up to 4-weeks ahead, the quantity of FX that it intended to sell or buy to the market every Wednesday of each week under their new FX Intervention & Trading Tool (B-FXITT). It was announced that they would sell US$20M to authorised dealers and cambios for the month of March 2018. The Bank will publish a report from each operation on the same day, including the weighted average exchange rate arising from the operation, and will also introduce the publication of midday weighted average exchange rates. This move is in line with the IMF's recommendation for Jamaica to institute a FX auction to gradually phase out the use of surrender requirements. This system is expected to smooth excessive currency market volatility.

Fig. 4



The Net International Reserves (NIR) has improved by US$305.40M as at March 2018, from US$2.77B to US$3.07B, over the same month last year and was US$101M below the projected US$3.18B. March's reserves in weeks of goods imports stands at 38.83 weeks. The NIR remains above the 12 weeks international benchmark. The relative stability in the local currency will mean less frequent intervention in the foreign exchange market by the Bank of Jamaica and should support high NIR levels. ***During the quarter, the dollar moved to as low as J$124.55 JMD/USD to as high as J$128.86. Based on the outturn so far, we are maintaining our initial view that the local currency will fluctuate between -1% (appreciation) to 3% (devaluation) for the calendar year.***

Inflation

The trailing 12-month inflation rate was 4.6% to February 2018, above the 3.5% as at February 2017. Lower inflation was experienced in the previous year due primarily to the impact of subdued international crude prices on fuel cost and domestic transportation. With more strident increases in oil price, we expect inflation to increase in the current year.

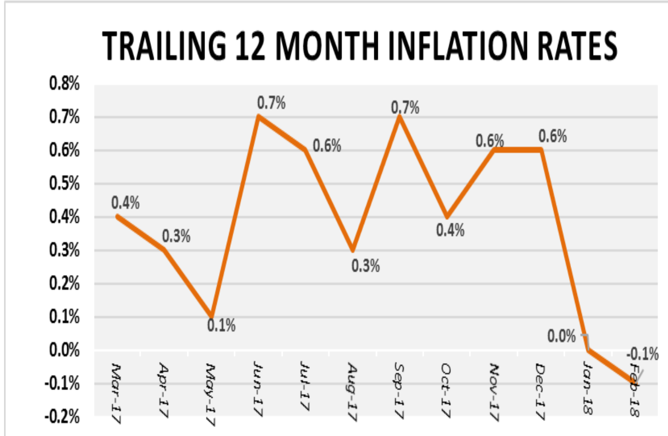


Fig. 5

Inflation for the fiscal year 2017/18 is forecasted to fall within the target range of 4-6% and the overall risks are viewed to be balanced over the next four months. The main upside risks to the inflation forecast are higher than expected increases in agricultural commodity prices, higher than anticipated international grain and oil prices, adverse weather and stronger than anticipated demand conditions. The major downside risks include quicker than anticipated recovery of the agricultural sector following flood rain damage, lower than projected international commodity prices and weaker than anticipated demand.

Interest Rates & Money Market

Interest Rates

Following a series of reductions, the Bank of Jamaica (BOJ) maintained its policy signal rate at 2.75% at its last announcement in March reflecting its continued accommodative stance. BOJ's decision to maintain an accommodative policy stance is aimed at supporting further credit expansion and faster GDP growth.

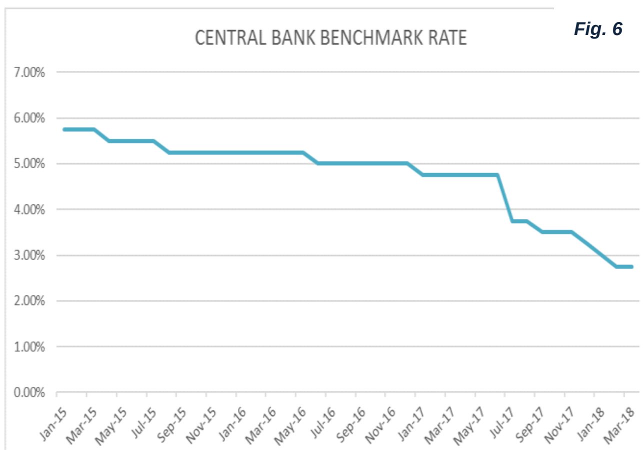


Fig. 6

When adjusted for expected inflation, the policy rate remains negative in real terms in a context of high liquidity in financial markets. The BOJ considers these conditions to be appropriate at this time given the weaker-than-desirable pace of credit expansion. The policy stance has supported downward adjustments to yields on medium and long-term GOJ bonds in recent times and these downward adjustments are expected to flow through to loan rates.

In contrast to the BOJ, the United States Federal Reserve (FED) increased the Federal Funds Rate by 25 basis points on March 21, 2018. The new benchmark range is now between 1.5% and 1.75%. With the decline in the interest rate differential between USD and JMD rates, there are concerns that portfolio switching could result in increased demand for USD assets. However, The Central Bank has put measures in place to discourage this by requiring Commercial Banks place a large portion of their US$ holdings with the Central Bank. Additionally, the Central Bank has also ceased paying interest on US$ holdings, which will ultimately result in Commercial Banks paying a lower interest rate on US$ deposits. Slower depreciation of the JMD since last year will also reduce the incentive to convert. ***It is our belief that the benchmark rate will remain at 2.75% for the following quarter. With expectation of the policy signal rate being unchanged, we do not expect market rates to vary much from current levels in the short run***.

Money Market

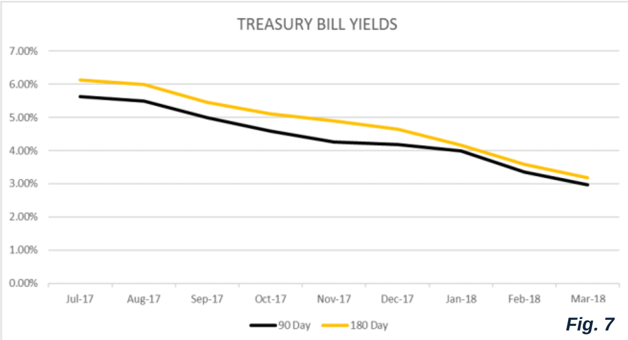


Fig. 7

Treasury bill (T-Bill) yields for the quarter trended between one and two percentage points above the benchmark rate. When compared to the quarter prior, yields have lowered slightly. The 90-day T-Bill yield ended at 2.98% for the quarter. This is down from 4.18% as at end of Q4 2017. Similarly, the 180-Day T-Bill yield ended at 3.17%% for the quarter, down from 4.63%% in the quarter prior. The 30-day T-Bill auction has been discontinued.

Stock Market

Fig. 8 YTD STOCK MARKET MOVEMENTS			
MAIN MARKET			
MAJOR WINNERS		**MAJOR LOSERS**	
VMIL	+35.5%	CBNY	-75.61%
BRG	+18.8%	MIL	-15.23%
NCB	+13.9%	KPREIT	-13.64%
JUNIOR MARKET			
MAJOR WINNERS		**MAJOR LOSERS**	
CAC	+257%	AMG	-30.33%
KREMI	+167%	FOSRICH	-18.04%
AFS	+164%	EPLY	-16.67%

YTD AVG. INDUSTRY MOVEMENTS		
	Main Market	**Junior Market**
Other	16.41%	-.45%
Manufacturing	5.17%	4.82%
Finance	3.41%	12.78%

Stock price appreciation has slowed significantly in 2018, with the Main Index increasing just 2.13%, while the Junior Market Index rose by 8.3% to the end of March. This is subdued relative to the 14.1% increase in the Main market and 13.7% rise in the Junior Market over the same period in 2017. The slowdown in the stock market would not be in line with expectations given the lower domestic interest rates. We note however that liquidity events last year would have helped to support price appreciation. Currently, we believe that investors are more cautiously seeking investment opportunities. Liquidity is being conserved in anticipation of the IPO's of Medicanja, Wigton Wind Farms, KIW International, Mayberry Jamaican Equities Limited to name a few. On a YTD basis, 6 out of the 10 junior market firms classified in the manufacturing industry experienced YTD gains, with AMG[1], BPOW[2], CFF[3] and SRA[4] making YTD losses. Though SALF[5] grew by 11.56% YTD, the larger market cap WISYNCO, had more bearing on the main market average and as such its YTD loss pulled down the overall industry average. The year to date outturn is slightly below our projections of annual growth between 10-15% but we believe that the listing of the potential IPO's in the 2nd and 3rd quarter will help to boost equity returns and spur overall market

[1] AMG Packaging & Paper Company Limited
[2] Blue Power Group Limited
[3] Caribbean Flavours & Fragrances Limited
[4] Sweet River Abattoir & Supplies Company
[5] Salada Foods Jamaica Limited

activity. We are maintaining the view that growth will be primarily driven by the manufacturing, financial and Tourism industry. Our expectation is that with improved macroeconomic variables and increasingly positive prospects for the Jamaican economy, the stock market will continue to benefit through an expansion of listed securities, domestic participation and continued profitability of its listed companies. ***Additionally, higher dividend yields continue to close in on, and in some cases, surpass BOJ benchmark rates, which we believe will continue to be a critical driver of investor interest in the stock market.***

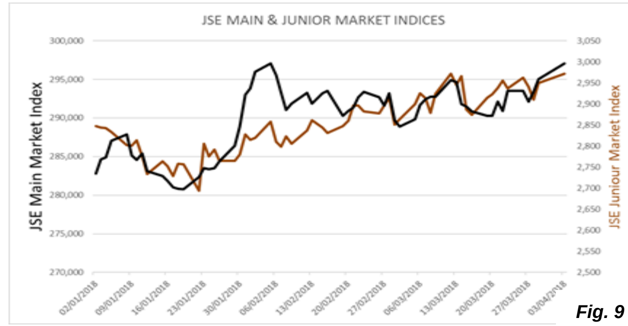
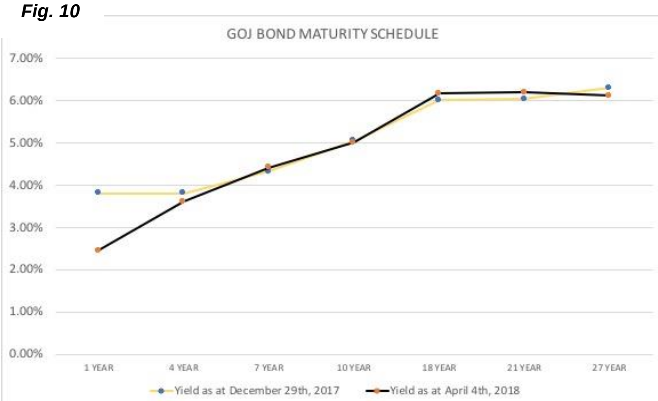


Fig. 9

Fig. 10



Bond Market

The Global bonds markets was eventful during the first quarter, with a new Fed Chair and US President on a mission to protect the US' interest at all cost. The Fed's new chair- Jerome Powell is expected to pursue more aggressive interest rate hikes as long as the US economy continues to strengthen. In his first appearance, Chairman Powell delivered a testimony that was widely interpreted as "hawkish" in its tone. This resulted in significant volatility in emerging market bonds. The recent 25 bps rate hike on March 21, which brought the Fed Funds rate within the target range of 1.50% - 1.75% triggered a falloff in EM bond prices, while Treasury yields rose 2-3 bps across the curve. What has dominated the market however is President Trump instigating what could be a trade war among the major economies. President Trump recently imposed China with $60Bn in import tariffs and has threatened that more measures against countries perceived as hurting US manufacturers are on the horizon. While the rate hike would have been priced into the market, we believe that these political events will result in even more volatility for bond prices.

During the first quarter of the year, GOJ global bonds yields have remained relatively smooth, observing marginal increases. The marginal increase in the bond yields are a result of slight bond price decreases, which is reflective of the decrease in demand for medium term GOJ bonds arising from BOJ's current inflation target of 4%-6%. Yields on other maturities in the 4-10-year bucket declined by less than 31 basis points, while the 7-year, 18-year and 21-year all increased by more than 9 basis points. Improved confidence stemming a from the fiscal discipline being showcased by the GOJ, adherence to the targets set under the Precautionary Stand-By Agreement (PSBA) with the IMF, as well as the country's improving economic prospects will continue to support GOJ Global Bond prices. However, rising interest rates in the US as well as politicking could result in increased volatility in prices; especially in light of higher US benchmark rates.