

ABSTRACT**THE EFFECTS OF EXCHANGE RATE POLICY
ON THE AGRICULTURAL SECTOR OF A SMALL OPEN ECONOMY:
THE CASE OF JAMAICA***Vincent Lyttle*

This thesis examines the effects of exchange rate policy on the agricultural sector of Jamaica over the period 1970-1990. The research and analysis involved the construction of an econometric model of the sector that recognised specific linkages of relative prices, income and monetary variables. The model was subjected to the analysis of the impact of exchange rate policies on agricultural factor costs, food prices, export competitiveness, profitability and supply, demand for and consumption of domestically produced food, and the demand for an consumption of imported food.

The study used data highly aggregated by commodity groups as well as proxies for some variables where direct measurements were impossible.

The empirical results obtained were quite revealing. Domestic inflation rates and labour productivity were the main determinants of wage rates in the agricultural sector. Farmgate prices were the major determinants of domestic retail prices, while the level of wages and exchange rate were the two main variables influencing farmgate prices. Domestic retail prices increased faster than wages indicating a decline in the purchasing power of wage earners.

Devaluation was found to improve export competitiveness and increase the profitability of exporting for all commodity groups. However, this improved levels of competitiveness and profitability within the agricultural sector ascribed to devaluation did not result in increased export supply of agricultural commodities because of structural constraints in the sector. The estimated coefficients of price elasticities of export supply ranged from a high

positive 1.6617 for yam to a negative value of 1.006 for vegetables. Relative price elasticities of domestic output were extremely low and insignificant, probably the result of the small variation and unchanging pattern of real prices between 1975 and 1981, which was associated with explicit price controls and the direct use of imports to control domestic prices.

The composition of imports for Jamaica appears to be based on sequential allocation dictated by political and economic priorities. Estimated price elasticities of imports were very low, with all estimated elasticities less than unity. The exchange rate did not have a significant effect on the food imports of Jamaica; exchange rate elasticities of imported goods were low.

The main policy implication of the study is that appropriate pricing policies must be developed so that some of the benefits derived from devaluation are passed on to farmers, who respond to farmgate prices and not domestic retail or export prices. Additionally, input and output price reform programmes should be accompanied by investment in physical and human capital, as well as in appropriate institutional structures to remove bottlenecks to production. Otherwise, significant long-term effects on agricultural growth cannot be expected from increased price incentives, as afforded by exchange rate policies.

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