TRINIDAD AND TOBAGO

1. General trends

Contrary to expectations of an upturn in the economy of Trinidad and Tobago in 2010 based on the international economic recovery, real GDP declined by 0.3%, a relative improvement over 2009, when the economy contracted by 0.9%. Although the energy sector's performance was much better than the year before, it was not sufficient to compensate for the sluggish activity in the non-energy sector, in particular construction, manufacturing and retail services, due to the continuing decline in domestic demand. Headline inflation also posed a challenge to the authorities, increasing to as much as 14.2% year-on-year (compared with 1.3% at the end of 2009) as a result of domestic supply-side shocks. Nevertheless, by early 2011, the inflation rate started to trend downward. Prospects for a sustained recovery in economic growth still remain weak and growth of 2% is forecast for 2011.

According to preliminary estimates of the central bank based on data available up to the end of March 2011, the fiscal deficit for the year 2010/2011[1] will be smaller than expected (around 0.2% of GDP), as a result of lower-than-budgeted expenditure, coupled with higher revenues. The budget for fiscal year 2010/2011 projected a deficit of 5.4% of GDP, but the deficit may actually turn out to be around 2.5% of GDP. In 2010, the balance-of-payments current account recorded a surplus of US$ 2.89 billion or 18% of GDP. The surplus on the current account was closely linked to the recovery in energy and petrochemical prices.

In 2010, the policy mix consisted of an expansionary monetary and fiscal policy stance designed to stimulate economic activity. This combination of policies is expected to be maintained in 2011 provided that there is no resurgence in inflation.

2. Economic policy

(a) Fiscal policy

The outcome, thus far, of the government's fiscal operations in fiscal year 2010/2011 has not coincided with budget projections. The central government had forecast a deficit amounting to 5.4% of GDP. However, preliminary estimates by the central bank to 31 March 2011 indicate that the fiscal deficit was lower than expected (around 0.2% of GDP) owing to delayed spending on goods and services and on the capital programme. The government expects spending to increase throughout the remainder of the fiscal year as the capital expenditure programme gains momentum and the central government settles some more of its outstanding obligations, including debt to contractors and value added tax (VAT) refunds.

Revenue out-turn generally remained within budget estimates. Although receipts from the non-energy sector (estimated at 23% of GDP) were weak, higher oil receipts compensated for this shortfall bringing total revenue to TT$ 43.2 billion. The shortfall in revenue in the non-energy sector reflects the weak activity in the sector and the negative effects this had on VAT collections.

[1] The fiscal year runs from 1 October to 30 September.

Nevertheless, the government intends to maintain an expansionary fiscal stance to support the economic recovery and job creation. Thus, during the second half of the fiscal year, the problems that constrained expenditure will be corrected so that the overall deficit will be in line with the budget projections for the fiscal year. The unexpectedly strong surge in oil and gas prices augurs well for the government's fiscal position and the revised forecast by the government is for a fiscal deficit of 4% of GDP in 2010/2011. Trinidad and Tobago also maintains a Heritage and Stabilization Fund (HSF) as well as other development funds totalling $ 9.7 billion. This gives the country enough scope for fiscal stimulus without substantially impairing public solvency ratios. The government is expected to finance the deficit with a combination of savings and new external and domestic borrowing. Total public debt stood at 37% of GDP at the end of 2010.

(b) Monetary policy

Monetary policy management was challenged by weak economic activity in the non-energy sector in the aftermath of the global crisis, exacerbated by steep price increases, particularly for those agricultural crops that were hit by weather-induced supply shocks over the year. If food prices are stripped out, core inflation proves to be more modest at around 4% in 2010. With core inflation remaining more or less the same and faced with the persistent problem of weak growth in the other sectors of the economy, the central bank conducted monetary policy with the aim of reviving domestic economic activity. Monetary policy was somewhat accommodative (although excess liquidity caused the central bank to withdraw currency from the system), as the central bank reduced the repo rate six times between January and December 2010, bringing it down to 3.75% at the end of the year. The commercial banks responded by lowering their prime lending rate from 9.75% at the end of 2009 to 8.0% at the end of 2010. All other interest rates fell as well. The weighted average lending rate on all loans dipped to 9.93% in December from 10.25% at the end of 2009. Similarly, the weighted average deposit rates declined from 1.57% at the end of 2009 to 0.85% at the end of 2010. In 2011, this rate continued to slide further, reaching 0.72% at the end of the first quarter of 2011.

However, the lower interest rates did not stimulate borrowing and credit demand remained weak, particularly in the case of the business sector. Credit to major business categories such as manufacturing, construction, distribution and finance and insurance contracted. Only in the real-estate sector was there an increase in lending in 2010: by 7% year-on-year. In addition, there was a noticeable improvement in lending to consumers. Year-on-year, this category grew by 5.2% in 2010, and the growth continued in 2011 to stand at 3.9% in the first quarter. Disaggregated data show that loans for the purpose of debt consolidation and refinancing rose by 21.2% and 10.4%, respectively, as consumers took advantage of the lower interest rates. Since these were new loans with longer maturities, the consumer loan portfolio increased.

Given the low demand for credit by the business sector, excess liquidity existed in the financial system for most of the year. In November of 2010 the central bank therefore requested commercial banks to deposit a total of TT$ 2.0 billion in an interest-bearing account for 18 months. Additionally, the central bank removed TT$ 5.7 billion from the domestic system through net open-market activity and foreign-exchange sales. Bond issuance by the central government totalling TT$ 1.4 billion also helped to soak up liquidity from the financial system. The tightening of liquidity in late 2010 caused short-term interest rates to improve marginally. After declining to 0.28% in October 2010, the domestic three-month treasury bill rate moved up to 0.47% in April 2011.

In 2010, the monetary aggregates M1 and M2 grew strongly, by 33.4% and 21%, respectively, over 2009 levels. The expansion of M1 was fuelled by demand deposits, while growth in M2 reflected that of M1 and an increase in savings deposits. However, growth in the monetary aggregates slowed in the first few months of 2011. M1A increased by 16.2% in February 2011 year-on-year, compared with 38.1% in February 2010, year-on-year. The broader measure of the money supply, M2 also trended in a similar direction. On a twelve-month basis, M2 growth slowed to 6.9% in February 2011 from 22.1% in February 2010. This occurred because time deposits declined by 14.4% in February 2011. Similarly, foreign-currency deposits declined by 16.2% and savings deposits declined by 11.1% during the same period.

(c) Exchange-rate policy

The quasi-fixed exchange-rate regime remained unchanged in 2010 and the situation is expected to continue in 2011, supported by the central bank's strong reserves position. Rebounding international energy prices in 2010 buoyed energy-sector earnings leading to higher levels of foreign-exchange inflows. West Texas Intermediate (WTI) oil prices averaged US$ 79.41 per barrel in 2010, compared with US$ 61.66 per barrel in 2009. Estimates suggest the energy sector supplied US$ 2.5 billion of foreign currency to the market in 2010, compared with US$ 2.3 billion in 2009. Demand for foreign currency remained strong in 2010, although imports declined. During 2010, authorized intermediaries sold US$ 5.5 billion or 1.9% less to the public than in 2009. High international energy prices sustained export earnings in foreign currency and relieved some of the pressure on the foreign-exchange market, so that less intervention by the central bank was required. Therefore, the bank's sales amounted to US$ 1.5 billion,(18% less than in 2009). Nevertheless, these sales were 33.5% higher than the average for the last five years. In December 2010, the nominal exchange rate depreciated marginally, and the weighted average selling rate stood at US$ 1= TT$ 6.4018. By March 2011, the Trinidad and Tobago dollar depreciated marginally, and the rate stood at US$ 1= TT$ 6.4217. The real effective exchange rate also depreciated by 8.6% over the September 2010 to May 2011 period. This depreciation was the result of a steady reduction in domestic prices relative to those of the country's major trading partners.

3. The main variables

(a) Economic activity

Following two years of negative growth caused in large measure by the international financial crisis, and with this crisis abating, most major markets showed some recovery in 2010. However, the economy is estimated to have actually declined by 0.3% in 2010, compared with a real GDP decline of 0.9% in the previous year. Although activity in the energy sector increased, it could not compensate for the continued fall-off in domestic demand, which affected activity in construction, manufacturing and retail sales. The energy sector is estimated to have grown by 2.0%, while the other sectors in the economy combined are estimated to have recorded a decline of 2.3%. Energy sector growth was spurred by higher production of natural gas (3.2%), liquefied natural gas (LNG) (1.4%) and natural gas liquids (8.3%). However, there were reductions in the production of crude oil (8.3%), petroleum refining (16.7%) and petrochemicals (0.7%). The completion of most major government projects and the slow pace of starting new ones contributed to a 5.8% contraction in construction, while lower levels of retail and wholesale activity influenced a decline of 5.3% in commerce. Weather-related problems caused agriculture to decline by 14.8% in 2010.

Notwithstanding the increase in international prices, the volume of crude oil production decreased in 2010 compared with 2009. Refinery output averaged 129 thousand barrels per day in 2010. However, there were initial signs of an improvement in 2011. During 2010, BHP Billiton temporarily cut production from its Angostura field to install and upgrade infrastructure. The restart of natural gas production by BHP Billiton led to an increase in production to 4,337 mmcf/d from 4,200 mmcf/d in 2010. The strong performance in the energy sector is expected to continue in 2011. However, overall growth is expected to remain below potential owing to lagging consumer and business confidence.

(b) Prices, wages and employment

Inflationary pressures intensified in 2010, largely as a result of global food and commodity prices. The year-on-year inflation rate peaked at 14.2 % in August 2010 but eased to end the year at 13.2%. The major cause of inflation was high food prices due to weather conditions which led to crop damage and low yields. Domestic food price inflation is expected to rise in 2011 as prices for key global food items including wheat and dairy products, corn, oils and fats, and sugar have increased consistently in recent months. Core inflation has remained low, at a range consistently between 3% and 4% over the period. In 2011, as the effects of supply shocks subside and as long as domestic demand remains subdued, overall inflation should decline to single-digit levels. In March 2011, on a year-on-year basis, headline inflation declined to 9.4% compared with 10.7% in the previous month and 12.5% in January. Inflation is forecast to average 6.5% in 2011. However, if upward price pressures persist, then the inflation rate may overshoot this target.

The central government raised the minimum wage from TT$ 9.00 to TT$ 12.50 in its 2010/2011 budget. The government also settled its wage dispute with a major trade union, the Public Service Association (PSA), awarding a 5% salary increase and improved benefits. The labour relations climate remains tense, however, as other government worker-affiliated trade unions have rejected the 5% offer, and have threatened further action in the future.

Data on average weekly earnings show that wages in the manufacturing sector (as measured by the index of average weekly earnings) increased by 5.3% in 2010, compared with 9.0% in 2009.

Meanwhile, the unemployment rate stood at 6.4% in 2010 up from 5.9% in 2009. Although official estimates have not yet been released, as many as 17,600 jobs were lost in the construction sector and these account for the bulk of total job losses. Similarly, in agriculture, 7,900 jobs were lost. The job losses which occurred in 2010 were due mainly to the slowdown in the domestic economy.

(c) The external sector

In 2010, the balance-of-payments accounts registered an overall surplus of US$ 418.4 million, compared with a deficit of US$ 712.6 million in 2009. The strong performance of the external accounts owes much to a current account surplus of US$ 2.9 billion for the year, since the capital account remained in deficit. Higher commodity prices (oil, gas) and a decline in imports led to the surplus on the current account, including a merchandise trade balance of US$ 3.4 billion or 16.8% of GDP. The services account also recorded a surplus (US$ 514.7 million or 2.5% of GDP), which contributed to the positive balance on the current account. However, the capital and financial account (including net errors and omissions) showed an overall deficit of US$ 2.5 billion or 12.1% of GDP.

Net foreign direct investment declined to US$ 549.4 million in 2010, compared with US$ 709 million in 2009. Commercial bank assets held abroad increased by US$ 32.8 million in 2010, compared with an increase of US$ 675.2 million a year earlier. Central government principal repayments on external debt fell from US$ 330.9 million in 2009 to US$ 71.6 million in 2010 largely on account of a US$ 230 million bond placement made in September 2009. Total public debt service amounted to US$ 121.2 million, compared with US$ 434.4 million in 2009. At the end of 2010, gross official reserves stood at US$ 9.1 billion, representing over 14 months of goods imports.

The positive outlook of the balance of payments accounts is expected to continue in 2011. Boosted by high oil prices, the current account is expected to be in surplus again in 2011 (around 19.1% of GDP), but this performance will depend on the evolution of oil and gas prices for the remainder of 2011.