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Challenges Aplenty

Overview

The adverse global economic trends that began to take root domestically in the fourth quarter of last year continued into 2009. Notwithstanding, as the energy sector grappled with low commodity prices, the first quarter registered GDP growth estimated at 2 percent, an improvement on the 3 percent contraction in the previous quarter. Oil prices averaged US$42.90 per barrel, in the first quarter down from US$58.35 just three months earlier, but by June rebounded to reach US$68 per barrel. The natural gas price averaged US$4.71 per mmscf from January to March, down from US$6.60. The unemployment rate, which averaged under 4 percent in the fourth quarter of 2008, is estimated at 4.50 percent for the first quarter as the number of lay-offs increased. The inflation rate initially fell off but in April edged back up to 11.9 percent (y-o-y) from 11.3 percent, providing additional challenges to the Central Bank. Responding to the Bank's policy signals, commercial banks lowered deposit and lending rates. Meanwhile, the stock market continued its downward slide. The Trinidad and Tobago Stock Exchange (TTSE) Composite Index closed the quarter at 821.82, 2.5 percent lower than the end of year value and fell further to 805.63 by the end of April.

TRINIDAD AND TOBAGO KEY ECONOMIC INDICATORS

INDICATORS	2008	2008.1	2009.1 p/e
Real GDP (% Change)	3.5	0.69	2.0
Retail Prices (% Change)	12	2.5	-0.3
Unemployment Rate (%)	4.6	5.3	4.5
Fiscal Surplus/ Deficit ($M)	9,817	1,997.00	-2,919
Bank Deposits (% Change)	16.6	2.4	4.8
Private Sector Bank Credit (% Change)	17.7	6	0.3
Net Foreign Reserves (US$M)	11,271.00	8,459.30	10,388.30
Exchange Rate (TT$/US$)	6.22/6.28	6.20/6.28	6.23/6.28
Stock Market Comp. Price Index	842.93	992.85	821.82
Oil Price (WTI) (US$ per barrel)	99.57	97.94	42.9

Source: - Central Bank of Trinidad and Tobago, TTSE, Energy Information Administration

p - Provisional Data

e - Republic Bank Limited Estimate

Energy Sector

Notwithstanding lower energy prices, the sector regained its footing somewhat in the first quarter of this year, following the plant shut-downs and production cuts which were triggered by plummeting energy prices at the end of 2008. With the exception of ammonia, production of methanol, natural gas and crude oil increased in the first quarter of 2009 (Table 1).

Table 1: Energy Production

	Quarter I '08	Quarter IV '08	Quarter I '09
Natural gas – mmscf /d	3,977.42	4,011.67	4,103.07
Crude oil – b/d	118,387	110,107	111,084
Methanol – metric tonnes / d	499,584	397,179	471,311
Ammonia – metric tonnes / d	406,028	562,491	560,539

Although they generally move together, the prices of oil and natural gas have been on divergent paths thus far this year. Gas prices have steadily trended down as a result of falling industrial demand and increased United States gas production. Prices averaged US$4.08 per mmscf in March and are expected to fall to an estimated US$3.86 in June. On the other hand, the crude oil price has climbed through the year, averaging US$47.94 per barrel in March, with a US$68 dollar average price expected in June (Fig. 1). While there are tentative signs of a modest recovery in oil prices, this seems to be largely based on the weak US dollar and speculative investors, as market fundamentals do not as yet support sustainable and strong price increases.

The local energy sector, stunted over the last year, with a number of projects deferred or being reconsidered, received a fillip this year with the completion of the Methanol Holdings Trinidad Ltd's 1850 tonnes per day ammonia plant. The plant, the first part of an AUM complex, began production in mid-April with the rest of the complex, 93 percent complete. Also on the industrial front, undaunted by the pullout of project partner Sural and ongoing protests by sections of the population, government forged ahead with the Alutrint aluminium smelter, breaking ground on the project site at La Brea. Work on the US$400 million plant, initially expected to last 28 months was halted following a high court decision in mid-June.

Figure 1: Oil & Gas Prices

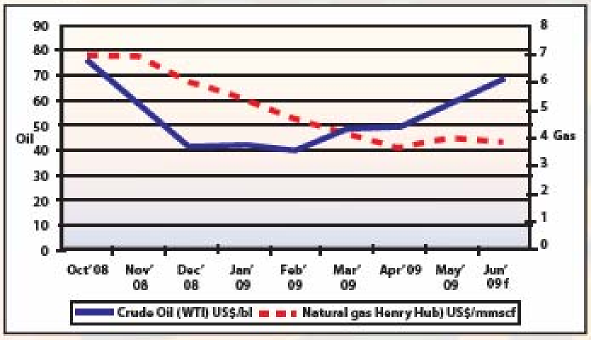


Figure 2: Fiscal Surplus / Deficit

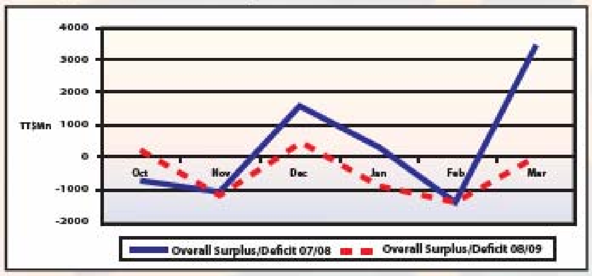
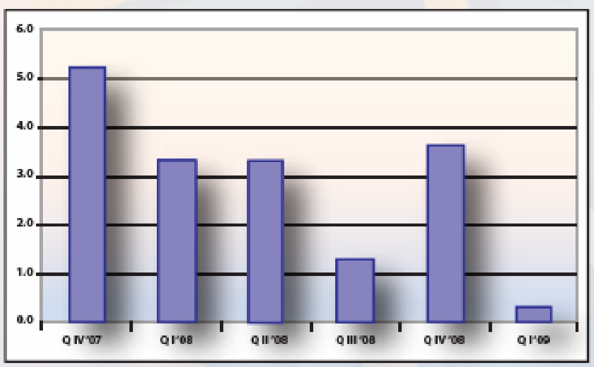


Figure 3: Private Sector Bank Credit (% chge.)



Fiscal Tightening

The decline in commodity prices impacted significantly on the country's fiscal position, with balances for the first half of the 2008/2009 fiscal year much weaker than the comparable 2007/2008 period. As expected, the disparity is reflected in the half-yearly balances which show a deficit of $2.9 billion this year, compared to a $1.9 billion surplus in the 2007/ 2008 period (Fig. 2).

Monetary Conditions

Encouraged by early indications of a downward inflation trend (the rate actually fell by 0.3 percent in the first quarter), the Central Bank of Trinidad and Tobago (CBTT) reduced its benchmark 'Repo' rate by 25 basis points in March and 50 basis points in April to 8.0 percent. Commercial banks responded in kind, reducing their prime lending rates from 13 percent. Initially, Republic Bank had the lowest prime rate of 12.50 percent - the first time that varying prime rates existed in the domestic banking sector. Further Central Bank actions, however, were stymied by a seemingly stubborn inflation rate, which in April, saw a reversal of the early 2009 trend. The year-on-year rate moved from 11.3 to 11.9 percent. With this country's food prices and overall inflation rate declining much more slowly than those of many other countries, the CBTT will want to be certain that the prevailing double digit inflation is abating before further interest rate reductions are induced.

With the general public and banks displaying increased prudence, private sector loans grew by just 0.3 percent in the first quarter of this year, down from 3.3 percent in the previous quarter (Fig. 3). One consequence of this has been a significant build-up of liquidity in the banking system. The CBTT itself acknowledged in its April *Monetary Policy Report*, that in the prevailing conditions, with interbank borrowing virtually non-existent, its benchmark 'Repo' rate is currently little more than a signalling mechanism. As part of its policy initiatives, the bank facilitated three bond issues of $0.5 billion, $1.0 billion and $0.3 billion, so far this year. The issues were all significantly oversubscribed, indicative of the high-liquidity environment.

Outlook

Crude oil price increases may well continue over the next quarter. However, the lift to government's coffers which they are likely to provide, while welcome, are unlikely to dissipate the fiscal challenges, as this country receives more of its revenue from gas and this latter price is expected to remain relatively low for some time. The Central Bank will be forced to walk a tightrope in respect of its stance on monetary policy between economic stimulation on the one hand and inflation control on the other.

Rising to the Challenge

The global downturn continues to hamper economic activity in the Caribbean, with the International Monetary Fund (IMF) downgrading economic projections for 2009, from 2.9 percent, to a negative 0.2 percent growth rate. Falling demand in the USA and the region's exposure to that economy has exacerbated the economic impact of the downturn on the region. Over the past few months, exports, tourism and remittances have all been affected and have led to deteriorating current account balances for the region. Indeed, the IMF is projecting a current account deficit of –5.1 percent in 2009 up from -2.8 percent in 2008 (Table 1). Furthermore, unemployment rates are also anticipated to increase, as tourism and construction activity begin to wane. These developments have forced countries to adopt fiscal incentive programmes to help stem the tide of the current downturn and lower the negative impact on the general population.

Table 1: Current Account Balance (% Change)

	2007	2008	2009
Caribbean	-1.5	-2.8	-5.1
Barbados	-5.2	-8.4	-7.2
Jamaica	-14.9	-15.3	-12.5
Guyana	-18.0	-20.8	-18.1
Trinidad & Tobago	24.8	26.8	7.4
Grenada	-41.9	-42.2	-32.9
Antigua & Barbuda	-33.4	-19.5	-18.6
St Kitts Nevis	-23.8	-24.2	-19.4

Source: IMF Global Economic Outlook Update 2009

Grenada

Grenada is struggling to meet the challenges of the global slowdown. Declining tourist arrivals and falling demand has seen the unemployment rate rise to 24 percent at the end of 2008. According to Finance Minister Nazim Burke, if global trends continue, the country could see an unemployment rate of 30 percent by the end of 2009. Further complicating matters is the country's high debt level (which stands at EC$1.8bn or 107 percent of GDP at end-2008), limiting government's fiscal policy. However, some relief is expected from the IMF, which is expected to grant a loan of approximately US$25.0 million this year. Government has also introduced an EC$20 million stimulus package in April 2009, in the hope of combating rising unemployment. The package is expected to create two thousand jobs and is aimed at those in the construction and agricultural sectors. Additionally, the government removed the National Reconstruction Levy and offered a tax amnesty to businesses and individuals.

Guyana

The Guyana goverment in February 2009, presented its largest fiscal budget to date. At US$637.4 million, it is 8 percent higher than the 2008 Budget and is expected to boost economic activity by 4.7 percent in 2009, up from 3.4 percent in the previous year. However, these projections seem highly optimistic according to the IMF, which sees a slower growth rate of 2.6 percent given the current state of the international economy. Investments in the country's energy sector are projected to slow, despite the heightened interest shown in 2008, as the global financial crisis has made it difficult to secure financing for such projects. In addition, falling bauxite prices and the termination of the EU sugar protocol in September 2009 are anticipated to stall economic activity even further.

Cuba

Despite the ravages inflicted by the 2008 hurricane season, the economy still managed to post a positive growth rate of 4.3 percent. However going into 2009, growth is expected to have slowed to around 2 percent, as the country's main exports continue to be negatively affected by the global slowdown. Nickel, the main foreign exchange earner, has seen prices plummet by more than 60 percent year-on-year in the first quarter of 2009. As a result, government expenditures have been reduced by 6 percent in 2009. Furthermore, the tourism sector is also anticipated to be negatively affected by the poor state of the global economy, especially visitors from the European Union. However, this is likely to be offset by increased arrivals from the USA, on account of the easing of travel restrictions to the island. Government is also pursuing its options in the energy sector, with the likes of Repsol (Spain), Norsk Hydro (Norway) and ONGC Videsh (India) all planning to drill exploratory wells in 2009, as well as Russian and Chinese firms showing great interest in the country's energy prospects in the Gulf of Mexico.

Barbados

With economic growth expected to decline by as much as 2 percent in 2009, the government has moved quickly to introduce a wide range of measures to help offset the effects of the downturn. In February, cabinet approved a BB$15 million Tourism Industry Relief Product (TIRP), which is aimed at preventing massive unemployment in the tourism sector due to falling tourist arrivals. The government also extended credit guarantees to medium sized businesses under the Small Business Guarantee Scheme. Traditionally, only firms with gross revenue of no more than BB$2 million qualified for such guarantees, but now firms with revenues reaching BB$4 million can access such funding. In light of the uncertainties placed on the regional financial system by the demise of Clico Investment Bank and the Stanford Financial Group, the Central Bank introduced a repurchase facility to provide additional liquidity to the commercial banks that need it.

The Region

With the main tourist markets (USA and EU) experiencing economic problems of their own, visitor arrivals from these countries have begun to fall. This has resulted in dwindling revenue streams and rising unemployment levels. While some of the islands are benefiting from falling commodity prices, for countries such as Guyana, Jamaica and Trinidad and Tobago these price movements have had a negative impact. In Jamaica, falling bauxite prices and tourism have led to a 0.6 percent decline in GDP in 2008 and government is projecting an even larger decline of -2.5 to -3.5 percent in 2009. For the countries of the Organisation of Eastern Caribbean States, the global downturn will prove difficult to 'ride out'; given the high level of debt of these countries. The average public sector debt in the OECS is now estimated at 93 percent of GDP and could worsen over the current year. The OECS and Trinidad and Tobago moved one step closer to an economic and political union, with a formal mechanism for the union announced in May 2009. While it is hoped that the union will strengthen the economies of member countries, critics argue that such a move could impede the development of the Caricom Single Market and Economy (CSME).

Outlook

Looking ahead, volatility in the international market will continue to hinder regional growth. Depressed demand and rising unemployment in the more developed countries have slowed inflows of foreign exchange into the region, placing a strain on the region's finances. These developments have led to various initiatives by several governments in the region, including access by some governments of loans from the International Monetary Fund (IMF). Unfortunately, however, financial strain is leading to heated quarrels amongst some regional countries on immigration and trade policies. Hopefully, these would be fully aired and solutions found at the upcoming Heads of Government Meeting in July.

Of Stimulus Packages, Government Intervention and Caribbean Business

by

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"Stimulus package", "government intervention", "bailouts", "credit crunch", "sub-prime mortgages" and "global meltdown," what do these phrases have in common? These are some of the catch-phrases which have come to be associated with the financial and global economic crisis affecting many developed countries including, the Caribbean's wealthy neighbours to the north. Unfortunately, we in the Caribbean have a tendency to "import" these terminologies wholesale and while we have not remained unscathed by the international turmoil, it is important to remember that our small and mainly island economies are unique in several respects and not without some possibilities of their own.

While some of the catch-phrases are no doubt relevant for the countries and circumstances in which they have arisen, they have little meaning for the local situation. Unfortunately, this does not prevent many of us from adopting these catch-phrases wholesale and interpreting them in a way that is not relevant to us. The USA and other developed countries beginning in 2007 faced specific challenges with the mortgage or housing crisis and all else that followed. Their governments fashioned responses costing billions of dollars in order to kick-start consumption and lending, which in turn are expected to stimulate economic growth.

One underlying assumption about that approach in the developed countries is that businesses would almost automatically return to growth as soon as consumption restarts and credit begins to flow. This approach is entirely applicable as those developed market economies boast a range of companies of all sizes that have been around for decades or longer. Most importantly these societies have for centuries appreciated the critical role of entrepreneurship and business in the achievement of a better standard of living for their citizens. Even their politicians and bureaucracies are highly appreciative and supportive of this dynamic.

Is this the case in Trinidad and Tobago or indeed the Caribbean? While we do have several successes, the truth is that the Caribbean environment really cannot be described as being "open for business". If there is any doubt, simply view the comparatively low ranking of Caribbean countries in the annual "Doing Business" report of the World Bank Group. The need therefore is not so much to stimulate consumption or for government takeover of Caribbean business in whole or in part. Instead, the need in the Caribbean is to stimulate production through the removal of the binding constraints to business development and through a pro-active approach in the growth of more businesses, especially Caribbean-owned ones.

To the extent that stimulus packages are necessary in the region, the goal must be to stimulate business expansion and innovation - not consumption. In our environment the need is, if anything, to minimize consumption, not stimulate it. It is not that all consumption is necessarily unimportant or "bad" but at this juncture of Caribbean development it is the stimulation of business which must be the first order of priority. As a region, we are still too far behind, especially if we are going to make good use of the various trade agreements which we have signed. In seeking growth, we must be careful not to simply stimulate consumer imports at the expense of scarce foreign reserves with the adverse exchange rate implications that can go with that. Lest we forget, business growth in turn generates taxes for government, employment, expenditure and income generation for the employed population. In other words, business expansion generates consumption.

In the case of Trinidad and Tobago and the Caribbean in general, the need is not for more government intervention. Rather, the need is for government support in the removal of the hindrances to business expansion and the promotion of a business-friendly environment.

"Bailouts" are part of the package which the USA and others have offered in the hope that they will return business to growth. In our context, apart from one business group which government is seeking to salvage, our banks and other business entities have not sought bailouts. Some may argue that these are early days yet but if a turnaround is not too long in coming then bailouts may not be necessary in the case of most Caribbean businesses. In any case, the capability of Caribbean governments to bail out failing businesses is severely restricted, even if such economic measures become necessary.

The major hindrance to the recovery in the USA is the reluctance of financial institutions to lend not only because they wish to retain whatever funds they receive for strengthening their capital base, but also because of the high risk environment which they face. Banks in Trinidad and Tobago are not in a similar position. Banks are well capitalised and are ready to lend though with a greater attention to the ability of individuals and businesses to acquire and repay additional debt.

In summary, the overriding point is that as business people we ought not to lose perspective. The world economy is indeed in crisis and this has major implications for the Caribbean. Nevertheless, if we are to successfully negotiate and surmount the many hurdles, we must be aware of our own strengths and challenges. To the extent that the Caribbean has not adequately embraced entrepreneurship, innovation and business in general, these remain areas of potential possibilities. Indeed, this business potential might strategically be viewed as a resource which, in the current context, might be activated to supplement the limited scope for fiscal expansion on the part of governments.

Now is not the time for business to retreat. It is not unusual these days to read or hear of all businesses being tarred with the brush of Enron, Lehman Brothers or the Stanford Group or some other failing and mismanaged business. This is unfair. There are businesses that are successful, that follow good management and corporate practices and which operate in the best interests of their stakeholders. These ought to be proud. Indeed such businesses have a responsibility to hold-up their flame to all who would wish to light their candle from them.

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