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Growth with Crosswinds Aplenty

Overview

The Trinidad and Tobago economy returned to growth in the 4th quarter of 2009 according to latest estimates. After four consecutive quarterly declines, the Central Bank of Trinidad and Tobago (CBTT) forecasted that GDP in the 4th quarter of 2009 rose by 1.3 percent. Republic Bank's estimate also shows positive growth. The quarter's growth was driven primarily by high commodity prices and production in the energy sector. Nonetheless, persistent challenges faced by key non-energy sectors serve as a drag on economic resurgence and suggest that growth prospects are tenuous going forward. The unem-

ployment rate is estimated to have climbed marginally to approximately 6.0 percent in the 4th quarter as key non-energy sectors continued to face weak demand conditions. The CBTT's interest rate reduction strategy picked up steam in the last quarter but did little to boost loan growth or stop the year-long decline in the stock market. On the external front, despite the strong demand for US dollars in 2009, reserves were still in a healthy position at the end of the year and this country's import cover actually increased as a result of a decline in imports.

TRINIDAD AND TOBAGO KEY ECONOMIC INDICATORS

Indicator	2008	2008.4	2009.4 p/e
Real GDP (% Change)	2.3	-2.6	2.5
Retail Prices (% Change)	12.0	3.3	0.16
Unemployment Rate (%)	4.6	3.9	6
Fiscal Surplus/Deficit (\$M)	12,132.70	-599.00	Surplus
Bank Deposits (% Change)	13.4	3.9	12.4
Private Sector Bank Credit (% Change)	17.9	4.5	0.08
Net Foreign Reserves (US\$M)	11,271.00	11,271.00	10,100.00
Exchange Rate (TT\$/US\$)	6.22/6.29	6.22/6.28	6.32/6.36
Stock Market Comp. Price Index	842.93	842.93	765.28
Oil Price (WTI) (US\$ per barrel)	99.57	58.4	76.06

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

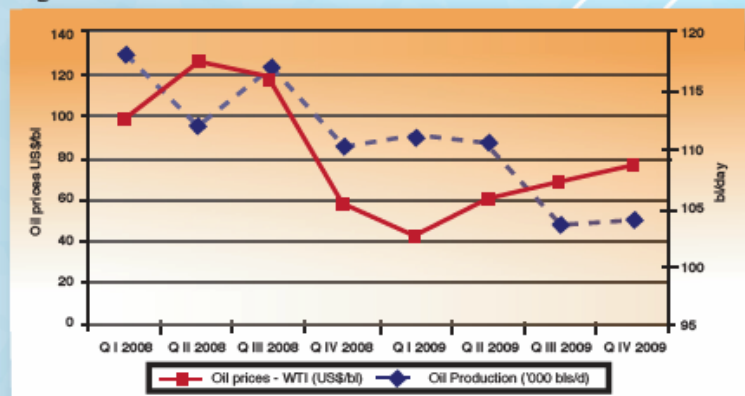
p - Provisional Data

e - Republic Bank Limited Estimate

Energy sector

The stabilization of the energy sector continued in the 4th quarter, with some recovery in production levels and commodity prices finishing the year on a positive note. Methanol (US\$331/tonne – fob Rotterdam) and ammonia (US\$298/tonne – fob Caribbean) both recorded their highest quarterly price averages for the year, and with production of 1,657,899 and 1,354,319 metric tonnes respectively for the quarter, are returning to their pre-recession levels. Crude oil prices climbed to US\$76.06 per bl. in the October to December period (its highest average since quarter III 2008) resulting in a 2009 average price of US\$61.66 per bl. The benefits of rising prices were tempered by reduced output as production averaged only 104,000 barrels per day during the quarter (Figure 1). Natural gas prices rallied to US\$4.47 per thousand cubic feet, giving an average of US\$4.06 per thousand cubic feet for 2009. Production jumped to a daily average of 4,331 million cubic feet for the quarter due to increased demand spurred by higher petrochemical production and

Figure 1: Oil Price & Production



Source: CBTT & Ministry of Energy & Energy Industries

the start-up of some of the plants comprising Methanol Holdings Trinidad Limited's (MHTL) AUM complex.

Non-energy sector

Following the estimated 6.8 percent contraction of the non-energy sector in the 3rd quarter, anecdotal evidence suggests the trend continued through the 4th quarter as many key sectors faced difficult circumstances. The dearth of major projects, and delays in the resumption of government's home construction thrust, have seen the continued decline in the construction sector, clearly evident by the trend in cement sales (Figure 2). The manufacturing sector's challenging time persisted as well, with the available data for the 4th quarter showing a continuation of the sharp fall-off in non-energy exports (Figure 3).

Fiscal position

With three of the four quarters recording deficits, the fiscal year ending September 2009, saw an overall deficit of \$7.4 billion representing 5.3 percent of GDP. This result was not a surprise and in fact government has already penciled in a 5.4 percent deficit for the current fiscal year. With commodity prices consistently higher than the budgeted prices of US\$55 per barrel for oil and US\$2.75 per thousand cubic feet for natural gas, the October – December quarter could see a surplus which augurs well for the rest of the 2009/2010 fiscal year.

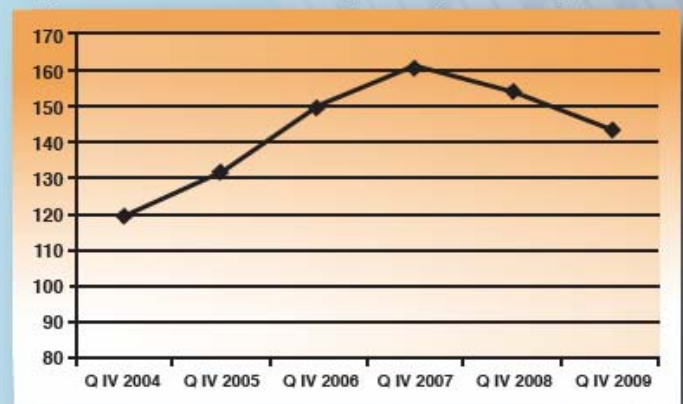
Monetary policy

The prevailing low interest rate environment in leading economies and falling inflation rates at home gave the CBTT the leeway to continue its interest rate reduction strategy. With the year-on-year inflation rate falling to 1.3 percent in December (average inflation for 2009 was 7 percent) the Bank lowered the 'Repo' rate three times taking it from 6.25 percent at the end of September to 5.0 percent in January. With year-on-year inflation climbing to 3.7 percent in January and the 'Repo' rate currently at its lowest historical point, it was not surprising that the CBTT left the rate unchanged in its March 'Repo' rate announcement.

The ensuing fall in commercial bank interest rates saw the prime lending rate cut to 10.25 percent in the quarter. Commercial banks have lowered their prime lending rate to 9.50 percent in February. Nevertheless, loan growth continues to struggle. The value of consumer loans outstanding in the 4th quarter 2009 grew by just 1.9 percent over the previous quarter and actually declined by 0.4 percent from the same period in 2008. The stock market didn't benefit either, with the Composite Index falling by 22.3 points from October to December, to end the quarter and the year at 765.28, a 9.2 percent decline from 2008.

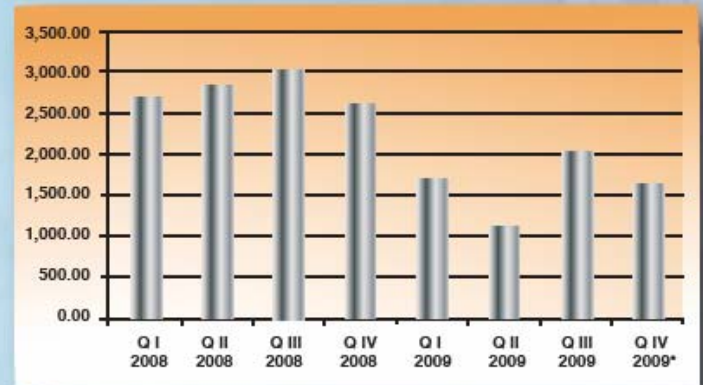
The selling rate for US dollars increased to TT\$6.36 as demand for the currency remained high at year's end. During the year, net

Figure 2: Cement Sales – 4th Quarter ('000 tonnes)



Source: CBTT & Trinidad Cement Limited

Figure 3: Non-energy Exports (TT\$ Mn)



Source: Central Statistical Office
* Republic Bank estimate

foreign reserves fell by over US\$700 million to close 2009 at an estimated US\$10,100 million, representing over 12 months of import cover.

Outlook

Notwithstanding likely growth in the 4th quarter, the economy faces significant and varied crosswinds and there is no guarantee of sustained growth in the first half of 2010. Despite the end of year economic expansion in the USA and UK, T&T's and the region's key trading partners, growth is spotty at this time and is not likely to impact regionally until the 2nd half of this year. The construction and manufacturing sectors will both struggle to achieve any growth in the near term. Further, the current drought affecting the Caribbean promises to negatively affect all the main drivers of economic activity throughout the region, particularly agriculture and tourism. Ultimately, T&T's growth prospects in the short term depend on the resurgence of the energy sector as only this can overcome the likely sub-par performance of other sectors of the economy.



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Caribbean Update

Cautious Optimism in the Caribbean

After the turbulence of 2009, the Caribbean region is hoping for recovery this year. Recovery depends largely on growth in the developed economies which is being facilitated by stimulus spending. The global downturn saw the region experience overall negative growth of -0.1 percent in 2009 (Table 1). Falling tourist arrivals, remittances and foreign direct investment have led to deterioration in the fiscal balances and debt situation of many CARICOM countries. However, with the improvements in the USA and European economies, the region is anticipating a return to growth in 2010. Tourism, along with ongoing public spending are expected to see growth of approximately 2.3 percent, according to the World Bank.

Table 1

GDP Growth Rates (%)		
	2009	2010
World Economy	-2.2	2.7
Caribbean	-0.1	2.3
Trinidad & Tobago	-3.0	2.0
Barbados	-5.3	-1.0
Guyana	2.3	4.4
Jamaica	-3.5	0.5
Antigua & Barbuda	-6.6	-1.1
Grenada	-7.7	0.8
Saint Lucia	-3.8	1.0

Source: World Bank Report 2010,
Various Budget Speeches & Central Bank Reports.

Barbados

Like most of the tourism-dependent islands of the Caribbean, Barbados was severely affected by the downturn, with GDP falling by 5.3 percent in 2009. Waning tourist arrivals have seen falling investment activities, resulting in rising unemployment rates which reached 10 percent by the end of 2009. The deteriorating economic situation has resulted in a widening of the fiscal accounts, as government sought to cushion the economy from the global downturn. This resulted in a fiscal deficit of BB\$564.6 million or 8.4 percent of GDP for 2009, up from 6.4 percent in the previous year. Inflation rates, on the other hand, have moderated from 8.6 percent at

the end of 2008 to 3.1 percent at the end of 2009. These trends are likely to continue in 2010, albeit at a slower rate as the Central Bank anticipates a small decline in GDP. Stable commodity prices and partial recovery in some of the main tourist markets will help augment downward pressures.

Grenada

Early estimates suggest that the Grenadian economy declined by 7.7 per cent in 2009, a reversal from growth of 2.2 per cent in 2008. This development reflects declines in major sectors of the economy, with stay-over tourist arrivals during January to November 2009, declining by 12.8 percent, when compared to the same period last year. With foreign direct investment declining, construction-related activity fell by over 50 percent. Despite these setbacks, there were some positives, as agriculture increased by 9.3 percent and cruise ship arrivals increased by 21.5 percent, for the period January to November 2009. The inflation rate is estimated to have slowed to 1.0 percent, compared to an increase of 8.2 percent in 2008. Coupled with the implementation of VAT earlier this year and a marginal recovery in tourism, the Grenadian economy is projected by the Government to grow by 0.8 percent in 2010.

Guyana

Unlike other CARICOM members, Guyana's economy expanded by 2.3 percent in 2009, marking the fourth year of consecutive growth. A large part of this growth is attributed to public infrastructural projects. One such project is a road to Brazil which should soon open up new economic opportunities, especially in light of the deteriorating economic conditions in nearby Venezuela. Agriculture is on the rebound, with rice production increasing by 9.2 percent in 2009. These improvements saw a balance of payments surplus of US\$234.4 million, increasing the country's external reserves position to a historic high of US\$628 million. Going into 2010, economic activity is projected to pick up on account of the Amaila Falls hydropower project and the oil exploration initiative in the Takutu basin. These developments, as well as an improvement in the country's finances should see the economy attain a growth rate of 4.4 percent in 2010.

Cuba

Notwithstanding the negative impact of the global downturn on nickel prices and the damage brought by 3 successive hurricanes on the agricultural sector in 2008, Cuba still managed a growth rate of 1.4 percent in 2009. Assisted by the relaxing of USA restrictions, tourist arrivals increased by 3.3 percent for the period January to September 2009, while agriculture recovered marginally by 4.4 percent. Apart from these improvements, the shortage of hard currency remains Cuba's main economic problem with a number of drastic measures being adopted to reduce the pressures on foreign reserves. These included the implementation of power cuts, suspension of foreign debt payments and the slashing of food imports from the USA. According to the U.S.-Cuba Economic Trade Council, imports fell 26 percent in 2009 to US\$528 million, after peaking at US\$710 million the year before. These stringent measures have alleviated some of the pressures on foreign reserves. Looking ahead, with the easing of restrictions by the USA administration, remittances from Cuban-Americans are anticipated to increase and, coupled with improvements in tourism, growth is projected to increase by 1.9 percent in 2010.

The Region

Jamaica's economy remains one of the most severely affected in the region. The economy contracted by 3.5 percent in 2009, as bauxite and alumina production fell. According to official figures, alumina production plummeted by 65 percent in the last quarter of 2009 alone. The country's debt situation deteriorated even further, with 55 percent of revenues consumed by debt service payments. Domestic debt alone climbed to 120 percent of GDP at the end of 2009, which saw government restructuring its debt and seeking assistance from the IMF. Consequently, US\$1.27 billion was provided in February 2010, to help alleviate the mounting debt problems. In respect of the OECS countries, high, public-sector debt will continue to affect the region's economic growth potential. Most of the countries are already on standby agreements with the IMF and while such assistance has not come with the traditionally strict austerity measures, depressed global demand will see slow economic recovery.

Haiti by far remains the most in need of international assistance. The earthquake in January claimed more than 200,000 lives and cost billions of dollars in damage to the country's infrastructure.

Outlook

Looking ahead, many countries remain cautiously optimistic, as the global economy emerges from the recession, however fears remain as to the strength of the recovery. Will it be U-shaped, or is the prospect of a double-dip recession more likely? Volatility remains as governments attempt to deal with the fallout imposed by the global downturn. Tourism, the mainstay of most Caribbean economies, is expected to pick up but to remain weak and with increased taxes levied on long-haul flights departing the United Kingdom, arrivals from this market will be affected. Nevertheless, with the USA posting positive growth rates in the 3rd and 4th quarters of 2009, most CARICOM members are anticipating a return to growth in 2010. Unfortunately, any recovery is likely to be lethargic, as most of the region's main economic drivers remain weak.



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Making the Case for Indigenous Business Development


To a large extent, directly and indirectly, the region has grown dependent on foreign firms for investment, employment, government revenue and growth.

The business landscape of the Caribbean is characterized by (i) large, foreign-owned companies (ii) sizeable governments across many sectors from tourism to energy and (iii) an indigenous business sector, which with few exceptions is still very small. In circumstances in which Caribbean governments are fiscally strained and multinational firms are finding it difficult to raise finance for investment, might a larger indigenous business sector not be useful in helping to cushion the external shock stemming from the global downturn? We suggest it can be. A strong regional indigenous private sector can assist not only to help provide protection against external shocks but to boost domestic wealth creation.

To a large extent, directly and indirectly, the region has grown dependent on foreign firms for investment, employment, government revenue and growth. This is not surprising given the size of such investments as might be gleaned from Table 1. The financial crisis and weak external markets however are making it difficult for some foreign multinational companies to raise funding and to invest in the Caribbean at this time.

In the case of governments, many are finding it difficult to make ends meet and this is also having adverse effects on the economies and societies as unemployment rises.

Table 1
Foreign Direct Investment and Gov't. Exp. (2008)



Country	FDI (%GDP)	Gov't Exp. (%GDP)
Guyana	15.4	47.7
Jamaica	9.7	34.3
Bahamas	11.1	20.2
Trinidad & Tobago	7.2	23.9

Source: IDB

The argument presented here, by no means asserts that a well-developed, indigenous private sector could replace the functions of government or the multi-national companies. Rather, the argument is that indigenous businesses can play a stronger role in complementing the other two sectors in ensuring more sustainable growth.

In many countries in the region, governments play a very active role. Partly because the indigenous business sector has traditionally been weak, governments are forced to maintain a very strong presence in the market. Public utilities were usually the target, but many regional governments are involved in other lines of



business including airlines and sugar refineries. Regional governments are still compelled to provide fiscal support to the economy on regular occasions. The development of a robust domestic business sector could help reduce this burden on state resources and free significant portions of state financing for infrastructural and other purposes.

Throughout the region the private sector is led by multi-national corporations through their subsidiaries and branches. Multi-nationals generally have access to greater capital flows than the average Caribbean firm. This allows them to invest in large projects that are at times beyond the means of domestic companies. Even though the bulk of their profits are repatriated, multinationals (directly and indirectly) employ large portions of the region's labour force and contribute significantly to regional growth. In unfavourable economic times however, multi-nationals may be forced to rationalize their global operations. This can result in adverse consequences for the region as they may reduce their investment spending and labour force in the region. With a vibrant indigenous business sector, the region will likely generate a greater percentage of its own growth. This could ease the reliance on foreign-based companies and governments for domestic economic growth.

Additionally, successful development of indigenous business could bring to market new goods and services, likely creating a springboard for the formation of new industries. In a supportive environment, entrepreneurs and investors would be encouraged to develop and invest in new ideas and innovations. The business ideas that prove viable would induce more new firms to enter the market, while also creating opportunities for providers of ancillary services, resulting eventually in the development of new industries. In addition to creating greater choice, this would create more sources of income for the region.

Building Caribbean enterprise is by no means a simple undertaking. It requires the investment of considerable thought, effort and resources. A few companies have already shown the way. However, if the region is willing to make some change in the way it does business, the benefits are likely to more than compensate for the costs.

It is important to note that such a push would require a multi-sectoral approach. Government policy must encourage the business fraternity to explore opportunities within the non-traditional sectors. This would involve some incentives being made available to promote investment in specific sectors or could also entail the use of targeted stimulus packages to fledgling industries. Thorough analysis must be performed to ensure that the competencies and resources of a country can support, over the long term, the sectors that are tagged for development. Failure to do so can have disastrous effects as notable amounts of scarce resources are at stake. Multilateral

institutions and organisations, such as the International Finance Corporation (IFC), European Union (EU), Caribbean Development Bank (CDB), to name a few, also have a role to play in supporting activities that have greater private sector participation than hitherto.

Small and medium-size enterprises (SMEs) must be nurtured and encouraged to grow, since they are the likely source of future large-sized firms. SMEs account for over 90 percent of all businesses globally and in most countries they employ a large percentage of the labour force, operate across many sectors and contribute significantly to economic growth. Of vital importance though, is the wealth of new ideas and innovations they create, which provide fertile ground from which high-performing firms can grow. Unfortunately, less than half of all start-ups survive beyond five years, while only a fraction of them is able to develop into large firms.

The importance of SMEs dictates that the Caribbean seek to improve their success rate by ensuring that promising projects are adequately financed, and have access to appropriate technology. The aim should be to transform small companies into national companies and to transform national companies into regional and international companies.

The global economic downturn is providing a grim reminder of the region's vulnerability and its dependence on North America and Europe for investments, markets and for its growth. In the face of this harsh reality the region has the chance to initiate a process of significant change to its economies. The development of the domestic business sector cannot be reasonably expected to totally replace the role played by the government and multi-national companies, but can be a strong third pillar in support of overall economic development. Vibrant domestic enterprises would not be totally immune to external shocks but they can be

expected to act as a buffer when shocks occur, by maintaining some level of economic activity and slowing the rise of unemployment. This initiative should be placed at the top of the agenda of Caribbean policy makers.



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