# Republic Economic NEWSLETTER

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## Double Digit Differences

### The Story of Trinidad and Tobago's Economy

#### OVERVIEW

According to Central Bank's quarterly GDP statistics, Trinidad and Tobago's economy contracted by 2.9 percent in the second quarter of 2016 compared to the first quarter, significantly higher than the 1.0 percent contraction projected in our September edition. Following this difficult second quarter, all indications are that conditions deteriorated even more in the July – September period, with both the energy and non-energy sectors gearing down further. The third quarter registered a number of double-digit differences (3Ds) when compared to both the second quarter and the third quarter of 2015, with the vast majority of the 3Ds being of the unfavourable kind. In light of this, Republic Bank estimates that the economy contracted by 3.5 percent in the third quarter relative to the second. The unemployment rate is likely to have increased to 4.7 percent, up from the 4.4 percent recorded for the second quarter. The rising number of unemployed people, reduced consumer demand and slowing economic activity all served as a damper on inflation. While the gradual depreciation of the TT currency against the US dollar would have made all imports more costly, there were no state-initiated price increases during the quarter; (remember the fuel price increase and some of the other taxes and increases took effect in the fourth quarter). In this scenario, average prices were just 0.54 percent higher in the third quarter than the second.

#### TRINIDAD AND TOBAGO
#### KEY ECONOMIC INDICATORS

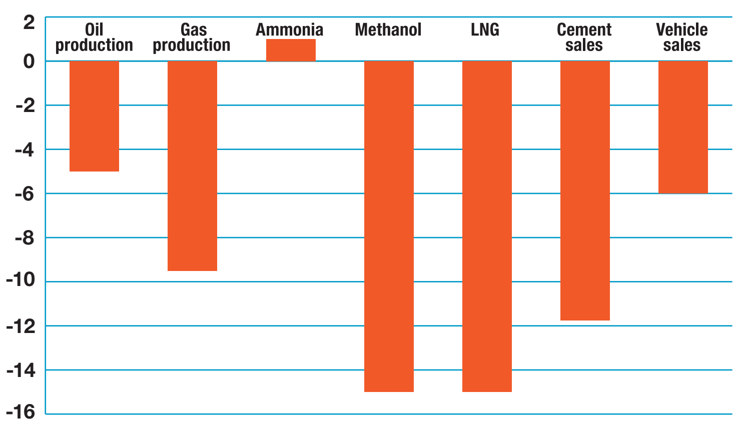
| INDICATOR | 2015 | 2015.3 | 2016.3 p/e |
|---|---|---|---|
| Real GDP (% change) | -0.6 | -0.3 | -3.5 |
| Retail Prices(% change) | 4.7 | 0.9 | 0.5 |
| Unemployment Rate (%) | 3.4 | 3.4 | 4.7 |
| Fiscal Surplus/ Deficit ($M) | -2,709.8 | -1,679.80 | -1,082.5 |
| Bank Deposits(% change) | -2 | -0.5 | -2.7 |
| Private Sector BankCredit (% change) | 1.4 | 1.2 | 0.4 |
| Net ForeignReserves (US$M) | 12,485.4 | 12,768.2 | 12,358.4 |
| Exchange Rate(TT$/US$) | 6.33 / 6.38 | 6.32 / 6.36 | 6.67/ 6.73 |
| Stock Market Comp. Price Index | 1,162.30 | 1,147.60 | 1,156.80 |
| Oil Price (WTI) (US$ per barrel) | 48.67 | 46.55 | 44.85 |
| Gas Price (Henry Hub) (US$ per mmbtu) | 2.63 | 2.76 | 2.88 |

**Source:**
Central Bank of Trinidad and Tobago, TTSE, EIA
p - Provisional data
e - Republic Bank Limited estimate

#### ENERGY SECTOR

Average West Texas Intermediate (WTI) crude oil prices, decreased in the third quarter by US 61 cents to US$44.85 per barrel while the average Henry Hub natural gas price increased by US 74 cents to US$2.88 per million British thermal units (mmBtu). Exploration activity picked up somewhat, with rig days and depth drilled increasing by 12 percent and 14.2 percent respectively. The decline in production continued however, with average crude output of 67,884 barrels per day (b/d) 5 percent lower than in quarter 2 and 11.2 percent lower than the same period in 2015 (Chart 1). Similarly, average gas production, at 3,048 million standard cubic feet per day (mmscf/d) represented a 9.7 percent decline from the previous quarter and a 19.6 percent falloff from a year ago. The reduced gas output impacted the downstream sector with ammonia production increasing by just 0.6 percent, while methanol and LNG production declined by 14.9 percent and 14.7 percent respectively compared to the second quarter. In recent months, oil and gas production would have been constrained partly due to planned shut downs by major producers. BHP Billiton's output was affected during preparations to bring its Greater Angostura field online in September, and bpTT shut down its Mahogany Bravo (B) hub as part of its preparations for the coming on-stream of its Juniper platform in 2017. Encouragingly, after hitting lows in August, oil production improved to 71,567 b/d in September and gas output increased to 3,193 mmscf/d. It should be noted however, that while gas production inched up further to 3,320 mmscf/d in October, oil production fell to 68,979 b/d.

**Chart 1:** Third quarter compared to the second quarter (% change)




**Sources:** Ministry of Energy and Energy Industries, Central Bank of Trinidad and Tobago

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## NON-ENERGY SECTOR

With private sector investment down and its biggest stimulator yet to kick start its infrastructure programme, the construction sector has been facing lean times for several quarters. Anecdotal evidence suggests that this trend continued through the third quarter. Following a brief increase in quarter two, cement sales fell by 11.9 percent in the third quarter of 2016 to just 127,185 tonnes, a figure 23.8 percent lower than the same period in 2015. The slowdown in manufacturing is also quite apparent. According to the Central Bank's Summary of Economic Indicators Bulletin the sector registered a capacity utilization rate of 68.6 percent in the second quarter which indicates that plants and factories are producing much less than they are capable of. That this figure is a 5 percent year-on-year reduction suggests the demand for manufactured goods is not only low but also declining. Of the sub-sectors, the Food, Drink & Tobacco producers were busiest with a capacity utilization rate of 75 percent followed by Chemicals and Non-Metallic Minerals (61.7 percent) and Assembly Type and Related Industries (45.2). In the absence of more recent data we believe this trend continued into the third quarter. The distribution sector has been facing declining activity as well, with varying levels of contraction across it sub-sectors. According to the CBTT's November 2016 Monetary Policy Report, supermarkets and grocery products was the one bright spot with 2.4 percent higher sales in the first half of 2016 compared to the first half of 2015. Not surprisingly, retail sales of hardware and construction materials fell significantly (27 percent), while household appliances, furniture and other furnishings had a more moderate decline of 3 percent. Indications are the weakness in the sector carried on into the second half of the year, with third quarter new vehicle sales 6.1 percent lower than in quarter two and 28.3 percent down from the corresponding 2015 period.

## MONETARY POLICY

In its November 25th monetary policy announcement, the Central Bank advised of its decision to maintain the 'Repo' rate at 4.75 percent. The decision was prompted primarily by weak domestic economic activity and subdued inflation pressures. In the third quarter, core inflation (year-on-year) increased from 2.0 percent in July to 2.3 percent in September, while food price inflation peaked in the quarter at 7.2 percent in August before falling to 6.2 percent in September. The end result was that average prices were just 3 percent higher in the third quarter this year than the same period in 2015. Private sector credit increased by just 0.4 percent from the second to the third quarter, but was 4.1 percent higher than a year ago, while consumer credit growth within the quarter was similarly weak at 0.5 percent but the September 2016 total was 7 percent higher than that of September 2015. Liquidity was lower in the second half of the year compared to the first, with commercial banks' excess reserves averaging $3.4 billion for most of November.

## RESERVES

This year, more than before, the foreign exchange market has been impacted by the prevailing weak economic activity in general and lower energy sector activity in particular. For the period January – October 2016, foreign exchange inflows from the energy sector totaled US$2,220.4 million, a 20 percent decline compared to the same period in 2015 (Table 1). In similar comparisons, purchases of foreign currency from the public by authorized dealers fell by 12 percent, while sales of foreign currency to the public declined by 24.4 percent. This country's foreign reserves, as represented by the net foreign position, increased from US$11,939.3 million in June to US$12,358.4 million in September, with the increase attributed to foreign currency loans secured by the government.

**Table 1:**

JAN. – OCT. 2016 COMPARED TO JAN. – OCT. 2015

| Indicator | % Change |
|---|---|
| Oil production | -10.6 |
| Gas production | -13 |
| LNG production | -14.9 |
| Rig days | - 40.4 |
| Cement sales | -21.1 |
| Vehicle sales | -12.9 |
| Energy exports + | -28 |
| Non-energy exports + | -20 |
| Purchases of foreign currency from the public | -12 |
| Sales of foreign currency to the public | -24.4 |

+ Jan. - Jun. comparison

**Sources:** Ministry of Energy and Energy Industries, Central Bank of Trinidad and Tobago

## OUTLOOK

With the expected roll-out of government's infrastructure programme and the prospect of increased output from the energy sector, the next six months are likely to see increased activity in the energy and construction sectors with direct and indirect spillover benefits for the manufacturing, distribution and finance, insurance and real estate sectors. While the increases are unlikely to be very strong, they will be notable in comparison to the declines of 2016. The combination of increased economic activity, new taxes, and a weakening currency should see stronger inflationary pressures in 2017. While the economy is unlikely to accelerate to the point where monetary policy needs to be tightened to prevent overheating, the 25 basis point increase in the US federal funds rate on December 14th puts pressure on the Central Bank to increase domestic interest rates.

The early part of 2017 has all possibility of being brighter than 2016. Indeed it would be hard-pressed not to be. While in some respects 2016 could be viewed as a transition year, economically it has been a difficult one, with each quarter worse than the one before. While the declines this year set the stage for some level of growth going forward, the extent of the declines could have negative consequences in 2017. At this time it is too early to tell what the final record of this year will be. However, based on the evidence thus far, the question needs to be asked; is it really possible for an economy to record so many 3Ds in so many significant areas for so much of the year, and not record a double digit difference in its GDP as well?



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# Trudging Along with Mounting Challenges

## OVERVIEW

Despite numerous challenges, the region continues to demonstrate resilience. The loss of correspondent banking relationships, global uncertainty surrounding 'Brexit', prolonged drought conditions and weak commodity prices were just some of the main challenges in 2016. In the face of these occurrences there have been some bright spots, with several countries (particularly tourism dependent economies) on track to record encouraging levels of GDP growth. Although the global economic environment remains very difficult for commodity based economies, Guyana is set to record another year of economic expansion. In terms of fiscal reform, Jamaica and Grenada continue to make commendable strides under IMF programmes. However, the Caribbean must approach the New Year with vigilance, as it is likely to provide additional challenges.

## BARBADOS

The Barbadian economy expanded by 1.3 percent in the first nine months of 2016, mainly due to growth in tourism, construction and business and other services. During the period, visitor arrivals increased by 5.7 percent year-on-year (y-o-y) with the majority of the growth coming from the US (11 percent) and Caribbean Community (Caricom) (13 percent). Tourism would likely be the main driver of growth in the fourth quarter, with the onset of the winter season. Although the performance of international and financial services sector was strong, it was challenged by global compliance issues. This was made evident by the 7.5 percent (y-o-y) fall in the number of licences granted to international companies in July. In addition, assets held by international banks declined by 16 percent (y-o-y) in June. On a positive note, the unemployment rate fell to 10.2 percent (y-o-y) in June, 2016 from 12 percent (y-o-y) in June, 2015. Based on tepid growth for the first three quarters of the year, the Central Bank of Barbados (CBB) reduced its growth forecast for 2016 from 1.5 percent to 1.4 percent.

## GRENADA

Grenada is expected to register 3.4 percent real GDP growth this year based on strong performances in the construction, tourism and transport and communication sectors. However, the agriculture sector contracted due to drought caused by the El Niño weather phenomenon. After years of deficits, the fiscal balance is expected to turn positive. This year, Grenada is forecasted to record a fiscal surplus of 1.9 percent of GDP from a fiscal deficit of 1.5 percent of GDP in 2015, due to increased economic activity, better tax collection efforts and tight fiscal management. Grenada continues to make progress under its Home Grown Programme and the IMF has approved the disbursement of US$2.7 million by December 22, 2016 after the Fifth Review under the Extended Credit Facility. Inflation is forecasted to average 2.1 percent for the year, as a result of higher prices for telecommunication services and the rebalancing of global oil prices. The financial system continued to strengthen its balance sheet and was able to reduce its non-performing loans ratio (NPLs) from 10 percent to 8.2 percent. Nevertheless, domestic credit was weak, as it declined by 5 percent during the first nine months of the year. After successful debt restructuring in 2015, total public sector debt is expected to fall from 100.1 percent of GDP in 2015 to 93.2 percent of GDP by the end of 2016.

## GUYANA

Real GDP growth is projected to slow down this year due to declines in output levels for both rice (-12.8 percent) and sugar (-18.7 percent). This year, the rice industry was negatively impacted by the loss of the Venezuelan market and weather-related challenges. The sugar industry was hampered by dry weather, late planting and frequent strikes. The Guyanese economy is expected to expand by 2.6 percent in 2016 with the quarrying and mining sector, projected to grow by around 33 percent. Gold prices were higher in 2016 than 2015 and production expanded as two foreign-owned companies reached full capacity and output from small and medium-sized miners increased. In terms of public finance, the actual fiscal deficit may be lower than the budgeted deficit of 5.5 percent of GDP, due to reduced capital expenditure, as some public sector projects were not initiated during the period. Net domestic credit of the banking system is expected to grow by 4 percent (y-o-y) by December, 2016 with household credit forecasted to grow by 9.1 percent (y-o-y). However, business credit will most likely be weaker. The banking sector was negatively impacted by global de-risking trends with locally owned banks losing approximately 37 percent of correspondent banking relationships by the end of 2016.

## CUBA

This year, the Cuban economy was buttressed by its tourism sector. However, unfavourable prices for its main exports (nickel and sugar) and declining oil subsidies from Venezuela placed a damper on the economy. Furthermore, growth was constrained by austerity measures such as energy rationing and reduced imports. No official data has been released for this year but growth is expected to be weaker than the 4.4 percent posted in 2015. On November 25, Cuba lost an Ex-President whose policies have defined the country for more than 50 years, with the death of Fidel Castro who passed away at the age of 90. Nevertheless, no major political instability is expected as his brother, Raùl, has been the president since 2006. Earlier in November, Donald Trump's victory in the US Presidential elections created some uncertainty with regard to future US-Cuba relations. While Mr. Trump has never fully leaned in favour of either rapprochement or the Republican's policy of isolation, he has stated that some of the recent policy changes under President Obama can be reversed if the people of Cuba do not get a "better deal". However, reversing the rapprochement could cause him to lose political support as many US businesses have lobbied for the removal of the embargo and some have already made investments to enter the Cuban market.

## SURINAME

The Surinamese economy is projected to contract significantly by 9 percent in 2016, after contracting by 2.7 percent in the previous year. This was mainly due to the closure of the Suralco alumina plant and the implementation of stringent fiscal measures. The Newmont Merian gold mine, which opened in October 1, should provide some ease to the domestic economy in 2017. With rapid increases in consumer prices and bouts of exchange rate depreciation, inflation increased to 77 percent in September and is expected to reach 60 percent by the end of 2016. The fiscal deficit was reduced to 6 percent of GDP by mid-2016, but fiscal policy loosened in the second half of the year as President Bouterse, knocked the IMF for not considering the social costs associated with the strict criteria under the two-year Stand-By Agreement (SBA). Public debt is projected to increase to 70 percent of GDP by the end of 2016 with the issuance of a $550 million government bond, for which the proceeds will be used to refinance existing debt from the state-owned oil company, Staatsolie and bilateral concessional loans.

## REGION

The Jamaican economy picked up in the third quarter, with real GDP growth of 2.3 percent (y-o-y). This was the strongest quarter of growth since early 2007 and it was mainly attributed to a 28.8 percent increase in agricultural output. The Jamaican economy has attained some stability since the IMF's Extended Fund Facility (EFF) was signed in 2013 and the IMF recently approved a US$1.64 billion three-year Stand-By Agreement to replace the current EFF, which was due to expire in early 2017. The current administration has already highlighted plans to cut public sector jobs in August, 2017 to fulfil part of its commitment to reduce the public-sector wage bill from 10 percent of GDP to around 9 percent under the current SBA. The labour market showed signs of improvement, as the unemployment rate fell from 13.7 percent in April to 12.9 percent in July.

Tourism was the main driver of growth for countries in the Organization of Eastern Caribbean States (OECS). During the first nine months of 2016, most OECS countries recorded healthy growth in tourist arrivals with the exception of Dominica, which registered a 6.4 contraction. In the second half of the year, 'Brexit' had generated some angst with regard to its potential negative impact on the number of UK and European Union (EU) visitors to the Caribbean. However, the true impact will not be known before the UK and EU negotiate new terms of agreement. The financial system continues to face significant challenges, with recent statistics from the Eastern Caribbean Central Bank (ECCB) revealing that private sector credit was weak for most of this year. In September, 2016, private sector credit contracted by 6.7 percent (y-o-y) compared to a contraction of 4 percent (y-o-y) in September, 2015.

## OUTLOOK

Looking ahead, the tourism-dependent nations are expected to experience economic growth in the first quarter of 2017, while commodity-exporters would generally still be challenged by weak commodity prices. The appreciation of the US currency would likely push down gold prices, while global energy prices are expected to remain weak, despite the Organization of Petroleum Exporting Countries (OPEC) decision to cut oil production. Next year, the world would get a better sense of the true impact of 'Brexit' when negotiations between the UK and the EU commence in March, 2017. If at the end of the process UK exports to the EU are stifled by new tariffs, this could constrict economic growth in the UK and subsequently result in fewer visitor arrivals for the Caribbean. With some countries in the region already suffering from weak credit growth and high non-performing loans (NPLs), the heightened global de-risking trends represents a clear and present danger. Some regionally-based banks have already lost correspondent banking relationships with foreign banks and this could continue in 2017, if the region does not move quickly to strengthen its Anti-Money Laundering/Combating the Financing of Terrorism (AML/CFT) framework to align with global standards.

# The Dawning of 2017

## Sunshine or Merely a Flicker of Hope?

With only a few days left in 2016, many businesses and households will no doubt be reflecting on how difficult a year it was for the domestic economy. Indeed the country has been pressed on all sides in 2016, with GDP projected to decline by 2.3 percent, public debt and the fiscal deficit rising to 61 percent of GDP and 5 percent of GDP, respectively and a tight foreign exchange market. We will not even mention the heightened fears of the population as it relates to crime… well not from this point onward. In this environment, many businesses were forced to cut costs to align with the realities of shrinking revenues, while some fell out of the market altogether. During the year, the government remained focused on fiscal consolidation, which saw the introduction of revenue-raising measures and the curtailment of expenditure in programmes such as GATE and the fuel subsidy. As necessary as these measures may be, they do result in increased hardship for certain segments of society. To no one's surprise, unemployment has been rising, reaching 4.4 percent in the second quarter of 2016 from 3.2 percent in the same period in 2015, with the strong possibility that it increased further over the rest of the year. In view of all this, it is natural and truly understandable, for the masses to look forward to the dawning of 2017 with the hope of some measure of relief. This article seeks to anticipate the type of economic environment we will likely face in 2017.

The government expects the domestic economy to expand by 1 percent in 2017, based on improved performances in energy and other major sectors such as manufacturing and construction. Based on the information available, we see this as a reasonable projection, providing that some momentum is gained with the public investment programme. Nevertheless, this level of growth is not expected to be sufficient to result in any significant boost in business profit, employment and government revenue.

Despite the optimism surrounding new production of oil and gas from BHP Billiton's Greater Angostura field in September 2016 and gas from BPTT's Juniper project, scheduled for late 2017, the domestic energy sector is not expected to experience major growth in 2017. Although both developments are expected to have a positive impact on the sector, it remains to be seen whether and to what extent these two events can at least arrest the slide in domestic energy production. Given that production from Juniper is anticipated to provide a much larger boost to the industry, any growth that the sector records in 2017, is likely to occur late in the year. In early December 2016, the governments of Venezuela and Trinidad and Tobago signed an agreement to monetise an initial one trillion cubic feet of gas from the Dragon gas field, which lies in Venezuelan waters. The field is estimated to have reserves in the region of 12-13 trillion cubic feet. Although this is expected to have a very positive effect on the domestic energy sector, first output is not expected before 2020.

As it relates to price, the U.S. Energy Information Administration projects oil prices to increase to an average of US$50 per barrel in 2017, compared to US$43 in 2016, while gas prices are expected to rise to US$3.12 per million British thermal units from US$2.50. In November, OPEC arrived at an agreement to cut supply by 1.2 million barrels a day by January 2017, as it seeks to end the glut on the global market. A few non-OPEC members, including Russia also agreed to cut an additional 600,000 barrels of their output. While this is encouraging news for the domestic economy, the substantial build-up of global inventories over the last two years and the potential for shale production to be stoked by a higher price environment, are anticipated to limit price increases. Additionally, if the new U.S. President acts on his campaign promise to seek to make the U.S. energy independent, there may be a continued drag on prices, since Shale production is likely to ramp up. The recent announcement of the largest oil find ever in the U.S. could embolden his policy stance.

Construction will likely register a stronger performance than all other major sectors in 2017. After what is expected to be a substantial contraction in 2016 (CSO projects a 7.6 percent fall), activity in the sector is anticipated to pick up appreciably in the succeeding year. In November 2016, the Housing Development Corporation (HDC) launched its first public private partnership (PPP) model housing project at a cost of $145 million. The Minister of Housing expects 800 new housing units to be built under the PPP model during the 2016 to 2018 period. Additionally, the 2016/17 budget identified a number of projects to be initiated or restarted in 2017 including, the Point Fortin Highway, Moruga Port, the Wallerfield to Manzanilla Highway and Crown Point International Airport. If meaningful momentum is achieved in these projects, not only will it result in growth and increased employment in the sector, but positive spillover effects are envisaged for other non-energy sectors. Nevertheless, the performance of the sector could be undermined by delays in these projects.

Still reeling from the fallout associated with the closure of the Arcelor Mittal steel plant in November 2015, the manufacturing sector is estimated to have shrunk by 5.7 percent in 2016. The sector is projected to experience a recovery in 2017. With construction activity likely to trend up during the year, the ensuing rise in demand for construction related products is expected to result in increased production in the chemicals and nonmetallic minerals segment of the manufacturing sector. At the same time, continued buoyant conditions in the regional tourism industry are expected to support the demand from CARICOM for this country's manufactured goods. CARICOM is Trinidad and Tobago's largest market for merchandise export.

With no significant boost in energy revenue foreseen in 2017 and the economy projected to record tepid growth, government's fiscal accounts are unlikely to see any substantial improvement during the year. In fact, it will be no surprise if government is unable to achieve the revenue target set for the 2016/17 fiscal year and thus, struggle to prevent further deterioration of its finances in 2017. In this regard, public debt may rise close to government's self-imposed ceiling of 65 percent of GDP in 2017, while the fiscal deficit could register at a level beyond the 3.9 percent anticipated.

The information at hand suggests that it is highly improbable that the country's reserves position will improve substantially in 2016, notwithstanding the forecasted moderate rise in energy prices. Low production levels are expected to limit foreign exchange earnings during the year. In this regard, the outlook is for the foreign exchange market to remain tight in 2017 with some improvement in 2018.

Although 2017 is expected to be a slightly better year for the domestic economy, for many it may seem or may actually be worse, since the bulk of the challenges confronting businesses and households are anticipated to linger and in some instances intensify. For instance, the low level of projected growth is not expected to significantly change the circumstances for companies in general. As such, the business environment will remain very challenging. Although increased activity in the construction sector is expected to boost employment in that sector, it may not offset the rising level of joblessness that may occur in other sectors. As a consequence, unemployment could increase in 2017. Further, it is normal for some of the spinoff opportunities which usually accompany expanding construction activity to occur with a time lag. In this regard, the related stimulus may not be felt in other sectors until late in the year or possibly early 2018. This is assuming of course, that there are no major delays in the execution of government's public investment programme. In short, the economic environment in 2017 is anticipated to be still very testing. If it's any consolation, at the end of that year, when we are looking forward to 2018 with hope, we are likely to be on the verge of a slightly brighter dawn.