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October 13, 1988

To: Members of the Executive Board

From: The Secretary

Subject: Trinidad and Tobago - Staff Report for the 1988 Article IV Consultation

Attached for consideration by the Executive Directors is the staff report for the 1988 Article IV consultation with Trinidad and Tobago.

This subject, together with Trinidad and Tobago's request for a purchase under the compensatory financing facility (EBS/88/208, 10/13/88), will be brought to the agenda for discussion on a date to be announced.

Mr. Elson (ext. 8477) or Mr. Gronlie (ext. 7157) is available to answer technical or factual questions relating to this paper prior to the Board discussion.

Att: (1)

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INTERNATIONAL MONETARY FUND

TRINIDAD AND TOBAGO

Staff Report for the 1988 Article IV Consultation

Prepared by the Staff Representatives for the 1988
Article IV Consultation with Trinidad and Tobago

Approved by J. Ferrán and Eduard Brau

October 13, 1988

Contents

I. Introduction

The 1988 Article IV consultation discussions with Trinidad and Tobago were initiated in Port-of-Spain during June 11-24 and were completed during August 18-September 3, 1988. 1/ The representatives of Trinidad and Tobago in the discussions included the Prime Minister, who is also Minister of Finance and the Economy; the Minister of Planning and Mobilization; the Minister in the Ministry of Finance and the Economy; the Governor of the Central Bank; and other senior officials from government agencies and selected state enterprises. The staff representatives in one or both rounds of discussions were Messrs. Elson (Head-WHD), Clark (EP-WHD), Gronlie, Karlik, and Khor (all WHD), Mrs. Muttardy (RES), Mrs. Sosa (WHD), Mr. Huh (ETR), and Ms. Rubin and Ms. Rowles (both secretaries-WHD). Mr. Hospedales, Alternate Executive Director for Trinidad and Tobago, participated in the policy discussions.

The previous consultation discussions with Trinidad and Tobago were held in July 1987, and the staff report (SM/87/238) was considered by the Executive Board on October 28, 1987. On that occasion, Executive Directors commended the authorities for the efforts made to counter the effects of the decline in the price of oil in 1986, but they expressed concern about the persistence of sizable external and domestic imbalances. Directors underscored the need to implement promptly a comprehensive program of adjustment and structural reform to lay the basis for the resumption of sustained economic growth. In particular, Directors urged the authorities to take action to strengthen public savings through wage restraint, tax reform, and a restructuring of the public enterprises. Directors also recommended that action be taken to encourage upward flexibility of interest rates and to seek further improvements in competitiveness.

II. Background

The weakening of the price of petroleum, Trinidad and Tobago's principal export commodity, in the early 1980s gave rise to widening imbalances in the economy. In 1984 and 1985 cutbacks in public investment helped reverse the deterioration of the public finances, while exchange and trade controls were imposed in an effort to reduce the external current account deficit. The reduction in the external and domestic imbalances during this period was associated with a sharp contraction in economic activity and a rise in unemployment. During 1984-85, real GDP fell by 11 percent, and by 1985 was nearly 25 percent below the level at the beginning of the decade; unemployment, in turn, rose from 11 percent in 1983 to 15 percent in 1985 (Table 1). While the external current account deficit narrowed over the period 1984-85 mainly because of a drop in imports, the capital account deteriorated and

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1/ Trinidad and Tobago continues to avail itself of the transitional arrangements under Article XIV.

Trinidad and Tobago's overall balance of payments continued to be in deficit. Consequently, net official international reserves declined by about US$1 billion during 1984-85 from a level of US$2 billion at the end of 1983.

Table 1. Trinidad and Tobago: Selected Macroeconomic Indicators

(Annual percentage changes)

	1984	1985	1986	Prel. 1987	Proj. 1988
Gross domestic product at current market prices	-0.1	-3.2	-5.4	-5.9	0.1
Gross domestic product at 1985 prices	-7.1	-3.9	-3.8	-4.8	-4.0
GDP deflator	7.6	0.8	-1.7	-1.2	4.2
Unemployment rate (in percent)	12.8	15.2	16.6	21.6	25.0
Period averages					
Retail prices	13.3	7.7	7.7	10.8	9.3
Weekly earnings	14.4	7.4	1.8	4.3	3.0
Real weekly earnings	0.9	-0.3	-5.5	-5.9	-5.8
Realized petroleum price (in U.S. dollars per barrel)	27.1	27.7	17.0	19.1	16.3

Sources: Central Bank of Trinidad and Tobago; Central Statistical Office; Ministry of Finance and the Economy; and Fund staff estimates.

In order to arrest the worsening balance of payments position, in December 1985 the Trinidad and Tobago dollar was devalued from TT$2.40 per U.S. dollar to TT$3.60 per U.S. dollar except for imports of essential goods (roughly 25 percent of imports). The budget for 1986 had provided for a sizable increase in capital spending to support economic growth but, following the collapse of international oil prices in the first half of 1986, fiscal outlays were reduced sharply; public investment spending was cut to less than half the level of the previous year, and transfers (including those to the public enterprises) were trimmed back by 16 percent. Nevertheless, the overall deficit of the nonfinancial public sector more than doubled to 11.5 percent of GDP in

1986 (Table 2). In addition, the operation of the preferential exchange rate regime resulted in central bank exchange losses equivalent to about 4 percent of GDP.

The external current account deficit rose from 2 percent of GDP in 1985 to 14 percent of GDP in 1986, while the overall deficit of the balance of payments nearly tripled to almost US$700 million; at the end of 1986, the net international reserves of the Central Bank had fallen to US$314 million, or the equivalent of about three months of 1987 imports. Real GDP declined by nearly 4 percent in 1986, and adjusted for the effect of the deterioration in terms of trade by nearly 14 percent, while the unemployment rate rose to over 16.5 percent.

The administration which took office in December 1986 adopted immediately a number of adjustment measures, including (a) the elimination of the preferential exchange rate, (b) a reduction in the government wage bill through the suspension of cost-of-living allowances (COLAs) granted in previous years and merit pay increases for 1987, and (c) a set of revenue measures expected to yield the equivalent of 1.5 percent of GDP. The Government also took action to reduce the dependence of the public enterprises on budgetary transfers to meet their debt service obligations and operating deficits. Notwithstanding the new tax measures, central government revenue actually declined in 1987 as a further drop in economic activity weakened non-oil tax collections. However, sizable spending cuts reduced total expenditure by more than revenue and the public sector deficit narrowed from 11.5 percent of GDP in 1986 to 8.3 percent of GDP in 1987.

Following a decline in private deposits in 1986, the growth in bank liabilities to the private sector recovered somewhat in 1987. All of the growth in private financial savings in 1987, however, was accounted for by an increase in private bank capital and reserves, as the holdings of money and quasi-money continued to decline. Total credit expansion exceeded by a significant amount the growth in liabilities of the financial system, resulting in a loss of net international reserves of the Central Bank of US$240 million (Table 3). The expansion of credit reflected, in addition to the financing of the government deficit, an increase in net central bank credit to the commercial banks, both in the form of liquidity support and a reduction in reserve requirements that sought to allow commercial banks to purchase treasury bills from the Government, after the Central Bank had reached its statutory limit on lending to the Government.

Because of the continued access by commercial banks to financing from the Central Bank, there was no significant upward movement of interest rates in 1987. Thus, yields on most financial instruments remained below the average rate of inflation. However, there was some increase in the interest rate spread in the financial system, reflecting not only the persistence of high operating costs, but also the need for financial institutions to improve their capital and reserve position in the face of continued deterioration of their loan portfolio.

Table 2. Trinidad and Tobago: Summary Central Government Operations

	1984	1985	1986	1987	1988 Budget	1988 Proj.
(In millions of Trinidad and Tobago dollars)						
Total revenue	6,580	6,612	5,289	5,207	5,114	4,735
Petroleum revenue	2,760	2,468	1,681	2,098	2,025	1,649
Other	3,820	4,144	3,608	3,109	3,089	3,086
Taxes on income	2,280	2,123	1,785	1,528	1,534	1,373
Taxes on goods and services	574	640	595	598	760	702
Taxes on international trade	481	629	500	385	410	436
Nontax revenue	421	667	660	519	329	516
Other	64	85	68	79	56	59
Total expenditure	8,171	7,484	6,541	6,313	7,410	5,851
Current	6,211	5,823	5,469	5,547	5,854	5,142
Wages, salaries, and contribution to NIS	2,586	2,563	2,578	2,212	2,370	2,335
Goods and other services	471	419	416	493	502	387
Interest	266	280	476	561	593	561
Domestic	81	78	145	239	236	236
External	185	202	331	322	357	325
Transfers and subsidies	2,888	2,562	1,999	2,281	2,389	1,860
Capital	1,960	1,661	1,071	766	1,556	709
Capital formation	1,107	1,287	604	379	1,140	441
Transfers and net lending	853	374	467	387	416	267
Overall balance	-1,591	-872	-1,252	-1,106	-2,296	-1,116
Financing	1,591	872	1,252	1,106	2,296	1,116
External	457	326	-210	64	571	501
Domestic	1,134	546	1,462	1,042	1,725	615
Memorandum item						
Overall public sector deficit	-1,554	-969	-2,001	-1,367	...	-1,134
(In percent of GDP at market prices)						
Total revenue	34.6	35.9	30.3	31.8	31.1	28.9
Petroleum revenue	14.5	13.4	9.6	12.8	12.3	10.0
Other	20.1	22.5	20.7	19.0	18.8	18.8
Taxes on income	12.0	11.5	10.2	9.3	9.3	8.4
Taxes on goods and services	3.0	3.5	3.4	3.6	4.6	4.3
Taxes on international trade	2.5	3.4	2.9	2.3	2.4	2.7
Nontax revenue	2.2	3.6	3.8	3.2	2.0	3.1
Other	0.4	0.5	0.4	0.6	0.5	0.4
Total expenditure	42.9	40.6	37.5	38.5	45.1	35.7
Current	32.6	31.6	31.4	33.8	35.6	31.3
Wages, salaries, and contribution to NIS	13.6	13.9	14.8	13.5	14.4	14.2
Goods and other services	2.5	2.3	2.4	3.0	3.0	2.4
Interest	1.4	1.5	2.7	3.4	3.6	3.4
Domestic	0.4	0.4	0.7	1.4	1.4	1.4
External	1.0	1.1	1.9	2.0	2.2	1.9
Transfers and subsidies	15.2	13.9	11.5	13.9	14.5	11.3
Capital	10.3	9.0	6.1	4.7	9.4	4.3
Capital formation	5.8	7.0	3.5	2.3	6.9	2.7
Transfers and net lending	4.5	2.0	2.7	2.4	2.5	1.6
Overall balance	-8.4	-4.7	-7.2	-6.7	-13.9	-6.8
Memorandum item						
Overall public sector deficit	-8.2	-5.3	-11.5	-8.3	...	-6.9

Sources: Ministry of Finance and the Economy; and Fund staff estimates.

Table 3. Trinidad and Tobago: Summary Accounts of the Central Bank and the Financial System

	TT$2.4 = US$1		TT$3.6 = US$1			
	1983	1984	1985	1986	1987	Proj. 1988
	(In millions of Trinidad and Tobago dollars)					
	I. Central Bank of Trinidad and Tobago					
Net international reserves	4,756.7	2,977.1	3,597.6	1,131.3	268.9	-172.8
Other external assets	416.8	665.6	1,169.2	1,128.1	1,052.7	979.7
Net domestic assets	-4,268.9	-2,763.6	-3,923.3	-1,386.3	-502.9	22.5
Net claims on public sector	-1,618.5	-491.3	-185.3	1,157.7	1,325.9	1,795.5
Central Government	-1,627.7	-507.2	-226.9	1,052.9	1,210.9	1,623.4
Rest of public sector	9.2	15.9	41.6	104.8	115.0	172.1
Official capital and surplus	-930.5	-891.3	-2,410.1	-1,693.4	-1,266.7	-1,140.6
Other	-1,719.9	-1,381.0	-1,327.8	-850.6	-562.1	-632.4
Currency issue	904.6	879.0	844.3	873.1	818.7	829.4
	II. Consolidated Financial System					
Net foreign assets	4,979.0	3,408.5	4,642.2	2,251.5	1,393.9	781.1
Net domestic assets	4,646.8	6,684.5	5,762.3	7,361.4	8,330.4	9,068.4
Net claims on public sector	-1,937.3	-784.7	-406.5	1,079.6	2,048.9	2,535.4
Central Government	-1,809.3	-740.0	-392.2	824.9	1,453.0	1,908.0
Rest of public sector	-128.0	-44.7	-14.3	254.6	595.9	627.4
Credit to private sector	8,487.3	9,115.9	9,138.3	8,735.7	9,015.0	9,335.5
Other	-1,903.2	-1,646.7	-2,969.5	-2,453.9	-2,733.5	-2,802.5
Liabilities to the private sector	9,625.8	10,092.9	10,404.6	9,612.8	9,724.1	9,849.5
	(Annual percentage change) 1/					
Net domestic assets	39.0	21.2	...	15.4	10.1	7.6
Credit to the public sector	21.3	12.0	3.7	14.3	10.1	5.0
Credit to the private sector	15.8	6.5	0.2	-3.9	2.9	3.3
Liabilities to the private sector	11.4	4.9	3.1	-7.6	1.2	1.3
	(In percent of GDP at market prices)					
Net domestic assets	24.4	35.1	31.3	42.2	50.8	55.3
Credit to the public sector	-10.2	-4.1	-2.2	6.2	12.5	15.4
Credit to the private sector	44.6	49.5	49.6	50.1	55.0	56.9
Liabilities to the private sector	50.5	53.0	56.5	55.1	59.3	60.0

Sources: Central Bank of Trinidad and Tobago; and Fund staff estimates.

1/ In relation to liabilities to the private sector at the beginning of the year.

The external current account deficit narrowed by nearly 8 percentage points of GDP in 1987 to 6.5 percent of GDP, as imports declined by more than 20 percent (in U.S. dollar terms), reflecting intensified controls on imports, a further real effective depreciation of the Trinidad and Tobago dollar, and a continued decline in economic activity (real GDP contracted by 4.8 percent in 1987). The unification of the exchange system in early 1987 and the continued depreciation of the U.S. dollar against other major currencies brought about a real effective depreciation of the Trinidad and Tobago dollar of 13.5 percent during 1987 (Chart 1).

The external capital account registered a small net inflow in 1987 following three years of net outflows, and the overall balance of payments deficit narrowed to US$233 million, mainly financed by the use of Trinidad and Tobago's SDR holdings and reserve position in the Fund; at the end of 1987, the Central Bank's net international reserves stood at US$75 million (equivalent to less than four weeks of merchandise imports at the level projected for 1988).

The external public debt rose from 34.5 percent of GDP in 1985 to 50 percent of GDP in 1987, while debt service obligations reached 28 percent of merchandise exports in 1987, up from 15 percent in 1985 (Table 4). Over the same period, interest payments as a proportion of exports of goods and services rose from 6 percent to 8.5 percent. Because a significant proportion of Trinidad and Tobago's external debt is denominated in currencies other than the U.S. dollar, a large part of the increase in debt service costs reflected the weakening of the U.S. dollar against other major currencies.

With the softening of international oil prices during the first half of 1988, Trinidad and Tobago's external and fiscal positions have weakened again. Notwithstanding a temporary income tax surcharge and increases in a number of indirect taxes, central government revenue during the first half of 1988 fell 17 percent below budgetary estimates because of the fall in oil prices and the effects of a further decline in economic activity. Total expenditure remained at about the level of the first half of 1987, and the government deficit through June 1988 was the equivalent of 3.4 percent of GDP, compared with near equilibrium in the corresponding period of 1987. Part of the public sector financing requirement was covered with a bond placement of US$75 million in the Japanese market, but fully two thirds of the government deficit was financed by central bank credit. As a consequence, the net international reserves of the Central Bank declined by nearly US$80 million during the first half of 1988.

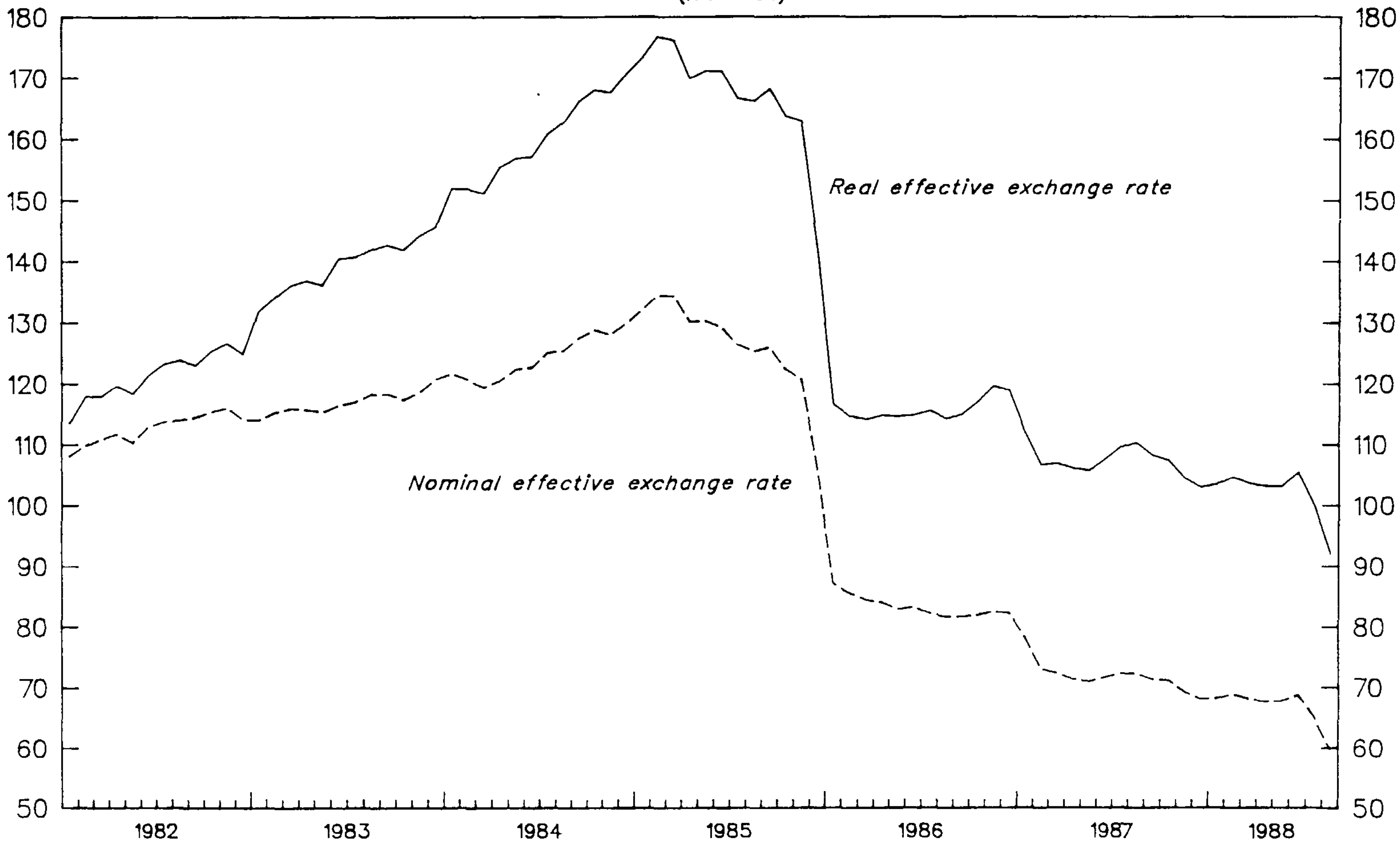
In the face of these developments, the authorities adopted a series of adjustment measures in July-August 1988 which included an increase in the central bank lending rate from 7.5 to 8.5 percent, a devaluation of the Trinidad and Tobago dollar from TT$3.60 to TT$4.25 per U.S. dollar, cuts in recurrent budget allocations equivalent to 2.5 percent of

CHART 1

TRINIDAD AND TOBAGO

REAL AND NOMINAL EFFECTIVE EXCHANGE RATE[1]

(1980=100)



Sources: Central Statistical Office and International Monetary Fund.

[1] An increase(decrease) in the index denotes appreciation(depreciation).

Table 4. Trinidad and Tobago: Summary Balance of Payments

	1984	1985	1986	1987	Proj. 1988
	(In millions of U.S. dollars)				
Current account	-500.0	-97.1	-632.9	-268.9	-199.4
Trade balance	220.6	560.9	-108.4	239.5	290.3
Exports	2,137.9	2,155.3	1,357.7	1,400.0	1,344.8
Of which: petroleum	1,680.6	1,674.7	955.9	985.9	795.3
Imports	-1,917.3	-1,594.4	-1,466.1	-1,160.5	-1,054.5
Services (net)	-637.4	-597.3	-486.4	-469.0	-460.7
Of which: interest on public debt	-148.6	-152.6	-140.3	-139.4	-167.7
Transfers (net)	-83.2	-60.7	-38.1	-39.4	-29.0
Capital account	-242.0	-146.5	-50.8	36.4	-53.0
Private (net)	-261.6	-235.2	-111.1	0.5	-30.9
Direct investment	113.2	1.2	-3.9	54.5	49.0
Other 1/	-374.8	-236.4	-107.2	-54.0	-45.8
Public (net)	19.6	88.7	60.3	35.9	-56.2
Central Government 2/	81.2	61.3	-58.2	58.1	34.1
Rest of public sector	-61.6	27.4	118.5	-22.2	-90.3
Overall balance	-742.0	-243.6	-683.6	-232.5	-252.4 3/
Memorandum items					
Public external debt, end of year	1,437	1,650	1,810	2,022	1,883 5/
Public debt service payments	389.5	320.5	323.2	396.6	471.5
Net international reserves of Central Bank	1,240.5	999.3	314.3	74.7	...
	(In percent of GDP)				
Current account	-9.7	-2.0	-14.1	-6.5	-5.2
Trade balance	4.3	11.7	-2.4	5.8	7.5
Exports	41.6	45.0	30.2	33.7	34.3
Imports	-37.3	-33.3	-32.6	-28.0	-27.3
Services and transfers	-14.0	-13.7	-11.7	-12.2	-12.7
Public external debt	27.9	34.5	40.3	50.0	55.4
Public debt service (as percent of exports)	18.2	14.9	23.8	28.3	35.1
Gross international reserves of Central Bank (in months of imports) 4/	9.4	8.3	4.1	1.4	...

Sources: Central Bank of Trinidad and Tobago; Central Statistical Office; and Fund staff estimates.

1/ Includes net errors and omissions.
2/ Includes net external lending operations.
3/ Includes unfinanced gap of US$202 million.
4/ In relation to imports of the following year.
5/ Excludes rescheduling and gap financing.

GDP, and an increase in the excise duty on gasoline to yield 0.5 percent of GDP on an annual basis. In addition, around TT$700 million was cut from the budgetary allocation for capital outlays, in line with the underexecution of the investment program that occurred in the first half of 1988.

III. Summary of Policy Discussions

The policy discussions focused on the short-term adjustment measures that would help to stem the loss of foreign reserves by the Central Bank and on the elements of a medium-term economic program that would provide the basis for the resumption of sustained economic growth and the restoration of external viability. These discussions served to frame an economic program that eventually could be supported by the use of Fund resources.

1. Medium-term outlook

There was general agreement between the authorities and the staff that an economic recovery strategy for Trinidad and Tobago would need to be cast in terms of a comprehensive medium-term program for adjustment and structural reform. It was recognized that, given the present structure of the economy, Trinidad and Tobago's economic and financial position will continue to be under pressure during the next few years because of the weakness and uncertainty of world energy markets and the likelihood that petroleum production may continue to decline over the near term with the gradual depletion of existing oil reserves. Additional pressures arise because of the burden imposed by the increase in external debt in recent years.

The authorities explained that in the past year the Government had elaborated a medium-term adjustment program for 1989-91 after consultations with representatives of all major sectors of the economy. The key objective of the program is the restoration of positive economic growth by 1990-91 to be achieved by means of a significant increase in domestic savings and investment. Investment is targeted to rise from an average of less than 20 percent of GDP in 1985-87 to 24 percent (still less than the investment ratio at the beginning of the decade) by the end of the period. This recovery would be supported by a significant improvement in the public finances designed to reduce the overall public sector deficit from around 8 percent of GDP in 1987 to an estimated 7 percent of GDP in 1988, around 4 percent of GDP in 1989 and about 1.5 percent of GDP in 1991. Consistent with this fiscal improvement and a recovery of private sector savings, the external current account deficit was projected to decline from 6.5 percent of GDP in 1987 to about 4 percent of GDP in 1989 and 1990 and to around 2.5 percent of GDP in 1991; at the same time, the gross international reserves of the Central Bank would be restored to the equivalent of at least three months of imports.

To achieve the fiscal objectives of the program, the authorities would adopt a wide range of revenue and expenditure measures, including a tax reform to be initiated in 1989 aimed at widening the tax base and shifting the burden of taxation from income to consumption (mainly through the introduction of a value-added tax), further reductions in the government wage bill, and a sizable cutback in budgetary transfers to the state enterprises. The authorities also will seek increased interest rate flexibility to stimulate financial savings, as well as exchange rate flexibility, combined with a liberalization of trade and exchange restrictions, to improve competitiveness and promote non-oil exports.

While most of the investment drive would be expected to come from the private sector, the authorities explained that they intended to implement a public sector investment program which would call for outlays amounting to around 6 percent of GDP over the period 1989-91. This investment program would support the development of agriculture, energy, manufacturing, and tourism. While some projects and their financing have yet to be identified, around one third of the investment program for the period 1989-91 is related to four major projects in the chemical and energy sectors, for which financing is currently being arranged: a new methanol plant, a natural gas production facility on the south coast, a natural gas liquids recovery plant, and a secondary oil recovery project.

The medium-term balance of payments projections discussed with the authorities assume that the international commodity prices for Trinidad and Tobago's exports would evolve along the lines suggested in the most recent WEO exercise, and that the export volume of crude oil and petroleum products would bottom out in 1990-91 on account of the favorable effects of increased secondary recovery activity. The export projections also assume that additional capacity in the chemical sector would come on stream in 1989 (ammonia) and 1992 (methanol). Imports in real terms would grow after 1989 in line with economic activity and the projected price increases for Trinidad and Tobago's suppliers.

The resulting current account deficit and the sizable debt repayment obligations which peak at around US$440 million in 1990 imply that Trinidad and Tobago would face significant financing gaps of around US$400 million in 1989 and US$437 million in 1990 (Table 5). These gaps would decline to US$210 million in 1991 and about US$80 million in 1992. The authorities indicated that they had approached commercial banks and official creditors about the possibility of rescheduling or refinancing maturities falling due during the four-year period beginning September 1988. This debt relief is expected to cover about three fourths of the external financing gap over the next few years. In

Table 5. Trinidad and Tobago: Medium-Term Balance of Payments Projections

	1989	1990	1991	1992	1993
(In millions of U.S. dollars)					
Current account	-178	-165	-106	-22	2
Trade balance	314	330	382	463	472
Exports	1,389	1,445	1,564	1,722	1,819
Of which: petroleum	775	809	893	931	964
Imports	-1,075	-1,115	-1,182	-1,259	-1,347
Services (net)	-462	-463	-454	-450	-432
Of which: interest on public debt	-198	-215	-222	-227	-217
Transfers (net)	-30	-32	-34	-36	-38
Capital account	-169	-189	-42	-37	31
Private (net)	60	70	85	100	115
Direct investment	60	70	85	100	115
Other	--	--	--	--	--
Public (net)	-229	-259	-127	-137	-84
Central Government	-154	-191	-70	-128	-125
Rest of public sector	-75	-68	-57	-9	41
Overall balance	-347	-354	-147	-59	33
Financing	347	354	147	59	-33
Change in official external assets (increase -)	-55	-82	-63	-19	-22
Financing gap	402	437	211	78	-11
Memorandum items					
Public external debt 1/	2,313	2,490	2,574	2,515	2,420
Public debt service payments	567	605	435	460	314
Gross official international reserves (in months of imports)	1.7	2.5	3.0	3.0	3.0
(In percent of GDP)					
Current account	-4.5	-4.1	-2.4	-0.5	—
Trade balance	7.9	8.0	8.7	9.9	9.4
Exports	35.1	34.9	35.6	36.8	36.3
Imports	-27.2	-27.8	-26.9	-26.9	-26.9
Services and transfers	-12.4	-12.0	-11.1	-10.4	-9.4
Public external debt	58.5	60.2	58.7	53.8	48.3
Public debt service (in percent of exports of goods and nonfactor services)	34.5	35.2	23.4	22.6	14.6
Memorandum items					
Petroleum price (in U.S. dollars per barrel)	17.0	17.6	18.2	18.9	19.5
Growth in real GDP (in percent)	-1.0	1.0	2.5	3.0	3.5

Sources: Central Bank of Trinidad and Tobago; Central Statistical Office; and Fund staff estimates.

1/ Includes borrowing required to fill financing gaps.

the view of the authorities, the remainder could be filled mainly by new borrowing from multilateral organizations. Taking into account the financing required to cover the balance of payments gap, Trinidad and Tobago's external debt would rise gradually to a peak of 60 percent of GDP in 1990, but would then decline to 48 percent of GDP by 1993.

Trinidad and Tobago's external position remains sensitive to variations in the export price of crude oil and petroleum products; a change of US$1 per barrel with respect to the price assumptions incorporated in the medium-term scenario would alter export revenue by US$56 million (around 1 percent of GDP) a year, on average, over the period 1989-93.

2. Domestic economic policies

a. Fiscal policy

On the basis of the actions taken by the authorities in mid-1988 to contain the fiscal deficit and limit the government's domestic borrowing requirement during the remainder of 1988, as well as the net effect of the recent devaluation, it was estimated that the overall central government deficit in 1988 would be virtually unchanged in terms of GDP relative to 1987 (around 7 percent). Meanwhile, the public sector deficit would narrow from 8.3 percent of GDP in 1987 to about 6.9 percent of GDP in 1988.

In the discussions, it was recognized that the public sector's overall financial result in 1988 would depend crucially on the ability of the rest of the public sector (in particular the state enterprises) to adjust to the sharp cutback in transfers in the budget, from the equivalent of 10.5 percent of GDP in 1987 to 7.9 percent of GDP in 1988. The authorities explained that the improvement in the financial performance of the enterprises was being achieved on the basis of recommendations of the Commission on Public Enterprises that had been established last year, which call for wide-ranging reforms, including financial restructuring, divestiture, and closure in some cases. In addition, some enterprises in the export sector were expected to benefit from stronger international prices for their products, as well as from the recent currency devaluation. The authorities further noted that, on the basis of the example set by the Central Government, wage restraint was being exercised throughout the public sector, including a substantial curtailment of overtime. The authorities noted that the proposed adjustments could reduce employment in the public sector, but they believed that the entities affected by the cuts had no alternative to an adjustment of their operations in the present circumstances.

The authorities considered that the need for prompt action to reduce the overall fiscal deficit was dictated by the Government's reduced access to foreign financing. Moreover, the staff and the authorities shared the view that domestic financing should be constrained so as to minimize the loss of net international reserves of the Central Bank in the second half of 1988.

In the area of tax policy, the authorities emphasized the importance of the measures introduced earlier this year to restructure the income and petroleum tax regimes with a view to stimulating production and employment. The reform of the petroleum tax regime included incentives for secondary oil recovery (workovers) and a downward revision of the supplemental petroleum tax (SPT), both actions designed to stimulate additional production. Under the revised SPT, it is assumed that production from existing operations (taxed at current rates) declines, while additional production (taxed at lower rates) increases. The tax rate would eventually be consolidated in 1992.

In the area of public sector wage policy, the authorities informed the staff that the Industrial Court had recently handed down a decision that called for the reinstatement of cost-of-living adjustments (COLAs) that had been suspended since the beginning of 1987 and an additional increase in wages and salaries of government employees of 2 percent effective January 1989. The retroactive cost of this decision was estimated to be in the region of TT$700 million. The authorities indicated that they were reviewing various options to deal with the Court's decision, but in any event they did not intend to make any cash outlays on account of the decision in either 1988 or 1989 because of the Government's weak fiscal position. The authorities were prepared to seek offsetting salary adjustments by legislative action, if necessary, to prevent any increase in the overall wage bill of the Government.

Looking beyond 1988, the authorities were considering certain schemes to reduce the public sector wage bill which would involve accelerated retirement and voluntary separation. These programs would be introduced before the end of 1988 and were targeted to reduce public sector employment by around 10,000 workers. In such an event, the budgetary savings (net of increased pensions) would amount to some TT$210 million (around 1 percent of GDP). However, this savings would not be realized immediately because of the payment of separation allowances required by law. Further reductions in the overall fiscal deficit would be expected to come from lower transfers to the public enterprises and an improvement in the tax effort.

b. Monetary policy

The authorities were concerned about the poor growth of private financial savings, the loan recovery problems of banks, and the weak financial position of many nonbank institutions. The authorities recognized that monetary policy had been excessively expansionary, as it had accommodated the Central Government's large domestic borrowing requirement and the financing needs of commercial banks that were faced with difficulties in satisfying their legal reserve requirements. However, the authorities expected that central bank credit expansion would be reduced with the improvements being sought in the fiscal position and by efforts to cut back loans to the commercial banks through increases in the central bank lending rate, a strengthening of bank supervision, and greater interest rate flexibility.

The authorities were considering further monetary measures to improve the efficiency of the banking system and strengthen the incentives for financial saving. In this connection, they were studying the possibility of phasing out the secondary reserve requirement (which provides a captive market for budget financing through treasury bills) and increasing the yield on treasury bills to levels comparable to that on short-term bank deposits. In their view, these changes would help reduce the large spread between lending and deposit rates arising from the effects of the primary and secondary reserve requirements, higher loan-loss provisions in response to deteriorating portfolios, the high cost of labor, and inefficiencies in the financial system. In general, the authorities felt that interest rates needed to rise further in present circumstances, although they feared that a significant increase in interest rates could aggravate the already precarious financial position of many businesses and worsen the loan recovery of the banks.

c. Wage and price policies

The authorities recognized that the sharp increase in unemployment in recent years--from 11 percent of the labor force in 1983 to about 25 percent in mid-1988--reflected to a large extent the downward stickiness of wages; indeed, wage levels in the manufacturing sector had risen sharply in real terms through 1985. Since then, however, they had declined by around 5.5 percent a year. The authorities observed that, based on the normal three-year wage contracts registered with the Ministry of Energy and Labor in 1987, the average annual wage increase negotiated for 1987-89 was estimated to be 3 percent; moreover, in contrast with previous years, cost-of-living allowances have been discontinued.

The authorities considered that the recent decline in real wages had been a necessary adjustment to the present circumstances of the country. They explained that as part of the adjustment measures introduced in August 1988 salaries of nonunionized managerial workers in the state enterprises had been reduced, while the practice of providing allowances for employees acting temporarily in higher paid jobs was curtailed. In this regard, they believed that further real wage reductions might be needed in certain sectors, including the public sector.

With the exception of sharp increases in food prices immediately following the exchange rate adjustments of December 1985 and January 1987, retail price increases have moderated markedly since 1983: by mid-1988 the 12-month increase in retail prices had been reduced to around 5-6 percent from 15 percent at the end of 1983. The impact of the August 1988 currency devaluation on domestic prices was expected to be modest given the weak demand situation and the low rate of wage increases provided in recent wage contracts.

The authorities considered that prices should generally be determined by the interplay of market forces and that the incidence of controls would remain limited. For the most part, price controls are set in terms of a markup over costs. In this regard, the authorities confirmed that the maximum limit for prices subject to control would be fully adjusted for the cost effects of the recent devaluation.

3. External sector policies

The devaluation of the Trinidad and Tobago dollar from TT$3.60 to TT$4.25 per U.S. dollar in August 1988 is estimated to have reduced the real effective value of the currency to around 50 percent of the level prevailing at the beginning of 1985 when the value of the U.S. dollar had reached its peak against other major currencies. In the view of the authorities, the recent exchange rate adjustment had restored an adequate level of external competitiveness, and they were confident that this situation would be preserved, given the reduced wage pressures. The authorities indicated that they attached importance to maintaining an adequate exchange rate in the future, but felt that frequent adjustments would tend to reduce confidence and encourage speculation against the Trinidad and Tobago dollar.

The authorities explained that the tightening of exchange and trade controls in recent years should be regarded as temporary and that their intention was to reestablish an exchange system free of restrictions as external conditions improved and the adjustment program began to take hold. They also drew attention to the simplification of the exchange control system in 1988, and the introduction of greater flexibility in the system through the provision of annual exchange allocations (Trade Allocation Certificates) for each importer registered at the Central Bank. They further explained that exchange allocations for invisibles were authorized on the basis of bona fide requests.

The authorities indicated that they intended to liberalize the system of exchange allocations for imports, which constitutes an exchange restriction subject to the Fund's approval under Article VIII, 1/ with a view to establishing an exchange system free of restrictions during the period of their medium-term program. They also explained that the so-called Negative List which covers imports subject to licensing requirements would be substantially reduced; however, for some items removed from the list, an increase in customs duty rates would be required to maintain an adequate level of protection.

The authorities were of the view that the policy of granting import duty exemptions mostly to inputs used in the production of goods for the domestic market has led to a bias toward inefficient import substitution and should be revised in order to improve resource allocation. In this

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1/ Trinidad and Tobago does not maintain any exchange restrictions under the transitional arrangements provided in Article XIV of the Fund Agreement.

connection, they were giving consideration to limiting such exemptions in the future mainly for the production of goods for the export market.

In order to foster the development of export industries that would take advantage of Trinidad and Tobago's improved competitive position, the authorities emphasized the importance of foreign investment, including joint ventures with domestic state enterprises. To this end, they recognized that the approval of investment applications by the Industrial Development Corporation needed to be streamlined further and that the Aliens Landholding Act should be modified to remove certain legal restrictions that have hampered foreign investment.

Over the next few years, Trinidad and Tobago faces a heavy concentration of foreign (mostly commercial) debt service obligations. Therefore, the authorities intend to seek a restructuring of commercial bank and official debt for the period through August 1992, and they would pursue a prudent debt management policy that would give emphasis to borrowing from multilateral lending institutions. In this regard, they indicated that Trinidad and Tobago was expected to have its eligibility for World Bank lending restored in 1989; the country had been graduated from Bank lending in the 1970s because of its (then) high per capita income.

IV. Staff Appraisal

Since the early 1980s, Trinidad and Tobago's economic and financial position has suffered a serious deterioration largely as a result of the decline in international oil prices. Real GDP has contracted by more than one fourth, the unemployment rate has more than doubled to 25 percent, and net international reserves have declined sharply to critically low levels.

During 1984-85, the authorities took measures to bring aggregate expenditure more clearly in line with the reduced oil export earnings; they curtailed sharply public capital outlays and adjusted the exchange rate, but also increased their reliance on exchange and trade restrictions. Trinidad and Tobago's internal and external imbalances were reduced in those years, but they widened again in the wake of the oil price collapse in 1986.

The administration which took office in late 1986 renewed the adjustment effort, mainly by tightening fiscal policy and unifying the exchange system at the more depreciated rate. As a result, the fiscal and balance of payments performance improved in 1987. However, economic activity and employment continued to contract, and the financial system weakened further because of bank loan recovery problems and a decline in private financial savings.

Faced by a renewed decline in international oil prices in 1988, the authorities have recently introduced significant corrective actions involving a further depreciation of the Trinidad and Tobago dollar, sizable budget cuts, and an increase in the central bank lending rate. At the same time, the Government announced the broad framework of a medium-term adjustment program for the period 1989-91. The staff welcomes these actions and would stress that a comprehensive adjustment program is needed to strengthen the balance of payments and to lay the foundations for sustained economic growth and external viability. Such a program must comprise not only measures to reduce Trinidad and Tobago's large internal and external imbalances, but also major actions to diversify the structure of the economy.

In the fiscal area, the authorities intend to bring about a substantial reduction in the overall public sector deficit through cuts in the public sector wage bill, improvements in public enterprise efficiency, and a reform of the tax system. The plan of the Government to curtail spending on wages and salaries is based on a voluntary severance and accelerated retirement scheme, but the authorities should be prepared to take additional action if this scheme does not yield the desired results. Up to now, improvements in the operating balances of the public enterprises have been imposed by cutbacks in transfers by the government budget. However, in order to ensure that this approach continues to result in improvements in the overall public sector position, efforts should be made to strengthen the Government's monitoring and control of public enterprise operations.

As regards tax reform, the staff supports the authorities' objective to simplify the tax system to make it easier to administer and to shift the tax burden from income to expenditure. Efforts should be made in this exercise to improve the structure of incentives for non-oil export production without resorting to subsidies and to limit the scope of customs duty exemptions.

Monetary and credit policies should be geared to strengthening the net international reserve position of the Central Bank and improving the efficiency and soundness of financial intermediaries. A reduction in the fiscal imbalance will be critical in reducing pressures on the Central Bank, but increased interest rate flexibility also is needed. The recent increase in the central bank lending rate was an important step in this direction, but further action may be required. The authorities also should allow for more competitive yields on short-term government paper, which would help improve the earnings of commercial banks and promote flexibility of interest rates more generally, thereby improving the efficiency of financial markets. To deal with the problems faced by financial intermediaries, the authorities should strengthen the supervisory function of the Central Bank.

The recent exchange rate adjustment was an important step that provided additional incentives for export expansion and efficient import substitution. However, the exchange rate will need to be kept under review in the light of other policy adjustments, as well as ongoing cost-price and balance of payments developments. In this connection, exchange rate policy will have to be geared to the achievement of the desired improvement in the external accounts over the medium term, in the context of an exchange system free of restrictions. At the same time, quantitative and other restrictions on imports need to be phased out, with a view to encouraging the production of tradeable goods.

In the next few years, Trinidad and Tobago faces a bunching of repayment obligations to commercial banks, and a refinancing or rescheduling of these obligations, in the context of an adequate adjustment program, will be needed to ensure a viable balance of payments. The authorities should use the time period of relief that would be provided by the rescheduling to improve the fiscal situation so that the country can meet its debt obligations on a sustained basis in the future. It also is important that Trinidad and Tobago pursue a prudent debt management policy over the next few years in order not to exacerbate its already high debt service burden. A careful selection of public sector investment projects and greater recourse to multilateral lending institutions should help achieve this objective.

Trinidad and Tobago maintains a restriction on import payments subject to approval under Article VIII. The authorities have stated that this restriction is temporary, and the staff urges the authorities to eliminate this restriction as quickly as possible. In the absence of a clearly defined program for its elimination, no approval of this restriction is proposed at the present time.

It is recommended that the next Article IV consultation be held on the standard 12-month cycle.

Trinidad and Tobago - Relations with the Fund and World Bank
(As of August 31, 1988)

a. Fund Relations

I. Membership Status

(a) Date of membership: July 17, 1963
(b) Status: Article XIV

(A) Financial Relations

II. General Department (General Resources Account)

(a) Quota: SDR 170.1 million

	Millions of SDRs	Percent of Quota
(b) Total Fund holdings of Trinidad and Tobago currency:	170.1	100.0
(c) Reserve tranche position	--	--

III. SDR Department

(a) Net cumulative allocation: SDR 46.2 million

(b) Holdings: None

(c) Current designation plan: None

IV. Current stand-by and special facilities

Trinidad and Tobago has not used Fund resources to date.

(B) Nonfinancial Relations

V. Exchange rate: Pegged to the U.S. dollar since August 17, 1988 at TT$4.25=US$1.00.

VI. Effective October 1983 a foreign exchange budget for imports was introduced whereby importers must obtain exchange approval from the Central Bank before an import license can be activated.

VII. The last Article IV consultation was concluded on October 28, 1987 (SM/87/238); the Executive Board did not approve Trinidad and Tobago's exchange restrictions on that occasion.

b. Relations with the World Bank

As a result of the decline in per capita income in recent years, it is expected that Trinidad an Tobago will become eligible for World Bank lending in 1989. No World Bank loan has been approved since 1979.

A World Bank mission is expected to travel to Trinidad and Tobago before the end of the year to begin the preparations for policy-based lending.

TRINIDAD AND TOBAGO - Basic Data

GDP at market prices (1987)	SDR 3,523 million US$4,555.6 million TT$16,401 million
GDP at market prices per capita (1987)	SDR 2,895

	1985	1986	Prel. 1987	Proj. 1988
Origin of GDP		(percent)		
Agriculture	3.8	4.3	4.6	...
Petroleum	26.1	21.8	23.1	...
Manufacturing	6.6	8.2	8.8	...
Construction	10.6	10.3	10.4	...
Government	14.9	16.1	14.2	...
Other	58.0	39.3	38.9	...
Ratios to GDP				
Exports of goods and nonfactor services	50.9	35.4	39.1	40.6
Imports of goods and nonfactor services	45.3	43.2	37.9	37.8
Current account of the balance of payments	-2.0	-14.3	-6.4	-4.6
Central administration revenues	35.9	30.3	31.8	28.9
Central administration expenditures	40.6	37.5	38.5	35.7
Central administration savings	3.3	-1.0	-2.2	-2.6
Central administration overall balance	-4.7	-7.2	-6.7	-6.8
Overall public sector surplus or deficit	-5.3	-11.5	-8.3	-6.9
External public debt (end of year)	34.5	40.3	50.0	55.4
Gross national savings	15.8	9.8	13.1	14.2
Gross capital formation	17.1	22.8	19.1	18.6
Change in money and quasi-money (end of year)	48.6	46.7	49.1	49.1
Annual changes in selected indicators				
Real GDP	-3.9	-3.8	-4.8	-4.0
GDP at current prices	-3.2	-5.4	-5.9	0.1
Domestic expenditures (at current prices)	-7.9	5.3	-13.3	-1.2
Gross capital formation	-28.1	26.7	-21.5	-2.1
Consumption	-2.0	0.6	-11.1	-0.9
GDP deflator	0.8	-1.7	-1.2	4.2
Consumer price (period average)	7.7	7.7	10.8	9.3
Central government revenues	0.5	-20.1	-1.6	-9.1
Central government expenditures	-8.4	-12.6	-3.5	-7.3
Liabilities to private sector 1/	3.1	-7.6	1.2	1.3
Money	-0.5	-1.2	--	—
Quasi-money	2.4	-6.6	-0.7	0.1
Net domestic assets of the financial system 1/	...	15.6	10.3	7.6
Credit to public sector	3.9	14.2	10.2	5.0
Credit to private sector	0.2	-3.9	1.9	4.1
Merchandise exports (in U.S. dollars)	0.8	-37.0	3.1	-3.9
Merchandise imports (in U.S. dollars)	-16.8	-8.0	-20.8	-9.1

	1985	1986	Prel. 1987	Proj. 1988
Central government finances	(Trinidad and Tobago dollars)			
Revenues	6,611.5	5,288.6	5,207.3	4,735.0
Expenditures	7,484.0	6,541.0	6,313.1	5,851.0
Current account surplus or deficit (-)	789.0	-180.0	-340.0	-407.0
Overall surplus or deficit (-)	-872.0	-1,252.0	-1,105.8	-1,116.0
External financing (net)	325.7	-261.0	166.0	501.0
Balance of payments	(U.S. dollars)			
Merchandise exports	2,155.3	1,357.7	1,400.0	1,344.8
Merchandise imports	-1,594.4	-1,466.1	-1,160.5	-1,054.5
Investment income (net)	-306.6	-239.5	-279.6	-278.7
Other services and transfers (net)	-351.4	-285.0	-228.8	-211.0
Balance on current account	-97.1	-632.9	-268.9	-199.4
Official capital	88.7	74.6	7.5	-56.2
Financial system	57.0	38.0	23.5	-5.0
Private capital, including errors and omissions	-292.2	-163.3	5.4	8.2
Changes in reserves (increase -)	243.6	683.6	232.5	252.5 2/

International reserve position	Dec. 31 1985	1986	1987	Aug. 1988
	(in millions of SDRs)			
Central Bank (net)	909.8	257.0	52.7	-55.5
Financial system (net)	885.1	265.9	76.9	2.2 3/
Gross official reserves	920.4	322.9	102.8	51.6

Social and Demographic Indicators	
Area	5,128 km2
Agricultural land (% of total)	25
Population	1.2 million (1987)
Rate of growth	1.5 (1983-87)
Density (1986)	
Population per km^2	230
Population per km^2 of arable land	428
Population Characteristics	
Life expectancy at birth (1980)	69
Male	67
Female	72
Infant mortality (1983) (percent)	15.6
Child death rate (aged 1-4, percent)	1
Health (1983)	
Population by physician	1,400
Population per hospital bed	200
Income Distribution (1973)	
% of national income, highest quintile	53
lowest quintile	3
Access to Safe Water (1983)	
% of dwellings - urban	97
rural	77
Access to Electricity (1983)	
% of population - urban	92
rural	76
Per capita electricity of generation	2.450 kwh
Nutrition (1983)	
Per capita calorie intake (per day)	2,915
Per capita protein intake (grams per day)	73
Education (percent)	
Adult literacy rate (1980)	97.2
Primary school enrollment (1983)	96
Secondary school enrollment (1973)	76

1/ As a percent of liabilities to the private sector at the beginning of the period. In 1985, the change in net domestic assets excludes the effect of the revaluation of the foreign assets held by the Central Bank.

2/ Includes unfinanced gap.

3/ As of June 30, 1988.

Trinidad and Tobago--Statistical Issues

1. Outstanding Statitiscal Issues

a. Real sector

At present, no data for industrial production or labor market statistics are reported to the Bureau of Statistics. However, there has been a marked improvement in the currentness of the reporting of national accounts at current prices over the past year. There is a need for a review of the methodology relating to unit values for foreign trade, which have tended to show erratic movements.

b. Government finance

Data in both the August 1988 IFS and the 1987 Government Finance Statistics Yearbook (GFSY) cover operations of consolidated central goverment only through 1981. No data for local governments are published in the GFSY. The lack of currentness of government finance statistics is due to the absence of reply to the annual GFS questionnaire for several years.

2. Coverage, Currentness, and Reporting of Data in IFS

The table below shows the currentess and coverage of data published in the country page for Trinidad and Tobago in the August 1988 issue of IFS. The data are based on reports sent to the Fund's Bureau of Statistics by the Central Statistical Office and the Central Bank. The currentness of some of the data needs improvement.

Status of IFS Data

		Latest Data in August 1988 IFS
Real Sector	- National Accounts	1985
	- Prices: CPI	Q3 1987
	- Production: Crude Petroleum	Q2 1987
	- Employment	n.a.
	- Earnings	n.a.
Government Finance	- Deficit/Surplus	1981
	- Financing	1981
	- Debt	1981
Monetary Accounts	- Monetary Authorities	February 1988
	- Deposit Money Banks	December 1987
	- Other Banking Institutions	Q3 1986

Interest Rates	- Discount Rate	April 1988
	- Bank Lending/Deposit Rates	April 1988/ December 1987
	- Bond Yields	April 1988
External Sector	- Merchandise Trade: Values	September 1987
	Prices	Q4 1986
	- Balance of Payments	1987
	- International Reserves	June 1988
	- Exchange Rates	June 1988

3. Technical Assistance Missions in Statistics (1985 to present)

Subject	Date
Balance of Payments	July 1986