

TRINIDAD AND TOBAGO TRENDS AND PROSPECTS

-A PERIOD OF ADJUSTMENT-

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- A PERIOD OF ADJUSTMENT -

In 1984, Trinidad and Tobago, a small open economy which for the past decade has experienced the prosperity associated with oil producing countries, finds itself faced with the urgent need for economic adjustment.

Signs of decline were present since 1979 when crude oil production began to decrease, and were reinforced by 1982 when the rate of increase of government oil revenues declined significantly. However, with major capital projects in mid-stream, Government budgets in the \$9 billion range, foreign exchange reserves approaching \$8 billion and citizens' expectations rising, it was difficult to even contemplate restraint, much more adjustment. In the period 1980 - 1982 therefore, the economy was characterized by increases in government spending despite declining rates of increases in revenues. This coupled with the gloomy outlook for both the traditional petroleum sector and the new petro-based industries, began to affect the rest of the economy. In 1983 and 1984 therefore, the Government, as principal actor in the economy, has resorted to several adjustment policies in which decreased capital expenditure, increased foreign borrowing, tight foreign exchange budgeting and incomes and wages restraint, figure prominently.

In order to highlight the economic need for adjustment in Trinidad and Tobago, trends in the major sectors of the economy will be outlined briefly, following which, the adjustment measures mentioned above will be discussed.

The Petroleum Sector

Crude Oil production declined at an average annual rate of 6.9 per cent from the peak production of 83.7 million barrels in 1978 to 58.4 million barrels in 1983. This fall was largely due to the natural decline of mature wells coupled with the absence of any major discovery during the period. In the first half of 1984 there was a slight increase in crude oil production. This was mainly attributed to the success of workover activity carried out in 1983 in conjunction with incremental flows from new marine wells. This increase however, is likely to be short-term and crude oil production in the next year or two is expected to be only marginally above at the 1983 level.

Since 1982 the petroleum sector experienced a sharp decline in domestic refining as refinery throughput slumped to 8.76 million cubic metres, 13 per cent lower than the level achieved in 1981 and the lowest recorded since refining capacity was expanded in 1957. This was due mainly to adverse trends in the international demand for residual fuel oil, coupled with problems associated with the domestic operations of Texaco Trinidad Incorporated. The decline in refinery operations has continued into the first half of 1984 when throughput was marginally lower than that for the first half of 1983. On 31st August 1984, Government announced its decision to purchase the Texaco refinery. The levels of future refinery activity will hinge on the specific arrangements associated with this decision.

There have been no increases in official oil prices since 1979. For the latter half of 1984 and continuing into 1985, prices are expected to remain stable at best, with the possibility of a decline if OPEC responds to the erosion of its market share by uncontrolled increases in its own output.

The Trinidad and Tobago economy is so structured, that developments in the petroleum sector, which are externally determined, act indirectly as the drive-mechanism for the entire system through government revenues.

Government

Developments in the petroleum sector since 1980 have resulted in a steady decline in petroleum taxes to the government. Over the period 1974 - 1980, total revenue from the oil sector increased at an average annual rate of 18.1 per cent, compared to an increase of 1 per cent in 1981 and decreases of 23 per cent and 25 per cent in 1982 and 1983, respectively. Over the 1974 - 1980 period also, petroleum taxes accounted for an average of 65 per cent of total government recurrent revenue. Its contribution then fell sharply from 62 per cent in 1981 to 38 per cent in 1983. The contribution of personal income taxes to Government recurrent revenue increased in importance, from 12 per cent in 1979 to 43 per cent in 1982 before falling to 25 per cent in 1983. Total Government revenue for 1983 amounted to \$6,481 million representing a 5 per cent decrease over 1982, compared to an almost negligible increase in 1982.

The trend of falling government revenues over the 1980 - 1983 period have not been matched by a commensurate fall in recurrent expenditure. While the average increase in recurrent expenditure for the 1974 - 1980 period was 29.1 per cent, for the period 1980 - 1983 expenditure continued at a relatively high level and increased at an average annual rate of 27.7 per cent. In 1983 however, the increase of 10 per cent was lower than the 65 per cent¹ and 14 per cent increases recorded in 1982 and 1981, respectively.

Government capital expenditure increased at an average annual rate of 41.7 per cent over the 1974 - 1980 period compared to an average of 6.9 per cent over the 1980 - 1983 period. This latter average however represents a combination of declining increases between 1980 and 1982 and an actual decrease of 21 per cent in 1983.

In 1983 Government experienced a deficit of \$14 million on current account operations and an overall deficit of \$2,857 million. This compares with the fiscal outturn in 1982 when current account operations resulted in a surplus of \$931 million and an overall deficit of \$2,652 million. In the first half of 1984 the deficit on government's cash flow operations amounted to \$1,111 million compared to a cash flow deficit of \$1,173 million in the corresponding period of 1983.

¹ This extraordinarily high increase was due to large retroactive wage payments.

The Non-Oil Economy

Total Fertilizer production has increased from 372.8 thousand tonnes in 1974 to 939.7 thousand tonnes in 1982 or an average annual increase of 12.2 per cent. This period was characterized by growing international demand, rising prices and increased local plant capacity. In 1983, despite the softening of world prices, local production increased by 36 per cent and exports increased by 43 per cent over 1982 levels. In 1984 however, fluctuating international market conditions resulted in relatively high production and export levels in the first quarter, followed by lower levels in the second quarter. Market conditions are expected to improve in the third quarter and for 1984 and 1985, production and exports are expected to increase.

Trinidad and Tobago's 1,200 metric tonnes per day Methanol plant began commercial operations in June 1984. The international methanol market is currently characterised by excess supply, sluggish demand and low prices and conditions are not expected to improve in the near future.

The production of Iron and Steel in Trinidad and Tobago has experienced several set-backs since its inception in 1982. In that year output amounted 512.6 thousand tonnes and exports to 155.6 thousand tonnes while in 1983 output increased to 676.1 thousand tonnes and exports to 190.5 thousand tonnes. The future of this venture remains clouded although the international market is expected to improve slowly.

The level of production in the Light Manufacturing sector, as measured by movements in the Index of Domestic Production,² increased at an average annual rate of 7.2 per cent between 1977 - 1980 then declined to an average annual growth rate of 1.9 per cent between 1980 - 1983. During the latter period several sub-sectors recorded production decreases although increases were recorded in the 'Electricity', 'Chemicals and Non-metallic Materials', 'Food Processing' and 'Assembly and related' sub-sectors. The general fall in output since 1981 has occurred against the background of poor conditions in domestic, regional and international markets.

The Services sectors of the economy recorded high growth rates over the 1974 - 1978 period and continued at relatively high rates between 1979 to 1982, before showing significant declines in 1983. Given the general downturn in the economy gross output in the services sectors is expected to decline.

Since 1972 when the agriculture sector attained high production levels, performance, has generally been poor. The export crops in particular have shown no signs of increased output. Sugar production declined for the seventh consecutive year in 1983 while the production of cocoa, coffee and citrus has also been marked by declines. Over this period, domestic agriculture has however shown some encouraging signs, with meat, milk and poultry production increasing considerably since 1981.

² Index excluding oil and sugar (Base = 1977).

Inflation

Trinidad and Tobago has experienced double digit inflation since 1973. The steady rate of increase in prices over the 1973 - 1980 period was reversed in 1981 and 1982 when there was a deceleration in the rate of price increases. In 1983 however, owing to the marked reduction of government subsidies and increased indirect taxes, prices increased by 16.7 per cent. This level of price increase is expected to prevail in 1984 and 1985.

The Financial System

The financial system has played a significant role in the expansion of the economy over the 1974 - 1982 period, and as evidenced by trends in 1983, is likely to play an equally important role in the necessary economic adjustment.

Over the period 1974 - 1979, the financial system experienced buoyant growth of its monetary resources and relatively easy liquidity owing to the increasingly large deficit on the government's domestic budget. Over this period the net sales of foreign exchange to the private sector also increased significantly but the net effect on the system was expansionary. The money supply, total commercial banks' deposits and credit to the private sector increased at average annual rates of 35 per cent, 29 per cent and 31 per cent, respectively, over the 1974 - 1979 period.

By 1980 the slowdown in the growth of the government domestic budget deficit and the continued increase in net sales of foreign exchange, combined to dampen the excessive growth rates in the principal monetary aggregates. This declining trend was interrupted in 1982 when, due mainly to large public sector wage payments, the significant increase in the domestic budget deficit served as a short-term stimulus to the financial system. By 1983 however, the underlying declining trend was reflected in an 8 per cent decrease in the money supply and a mere 5 per cent increase in aggregate commercial bank deposits. The liquidity position tightened considerably, particularly during the second half of the year and while private sector credit for the year increased by 18 per cent, for the latter half of the year the annualised increase was only 7 per cent.

Credit conditions in the banking system tightened further in 1984. For the first half of the year, the money supply decreased by 4.5 per cent while total commercial bank deposits and credit to the private sector increased at the relatively low rates of 5 per cent and 3.6 per cent respectively. By the end of June, average excess liquidity had fallen to 1.8 percent.

THE BALANCE OF PAYMENTS

The balance on the Merchandise account moved from a surplus of \$823 million in 1975 to its peak surplus of \$1,434 million in 1980 then declined to a surplus of \$1,217 million in 1981 before moving to a deficit position in 1982. In that year exports fell by 11 per cent and

imports increased by 40 per cent, resulting in a deficit of \$1,360 million. In 1983, while exports declined by a further 8 per cent, the increase in imports declined to 10 per cent, resulting in a reduced deficit of \$1,117 million.

The balance on the Services account moved from a deficit in 1974 to a surplus of \$227 million in 1975 after which it slowly deteriorated to a deficit of \$337 million in 1979. Since that year the services account has remained 'in the red' with the estimated deficit of \$994 million in 1983 representing a significant increase over the \$393 million deficit recorded in 1982.

Except for 1976, the the Capital account has over the 1975 - 1983 period, consistently recorded substantial surpluses. except for 1976. These capital inflows mainly represent a net foreign source of funds to the direct investment enterprises and foreign borrowings by the private and public sector.

Overall therefore, between 1974 - 1981, there was a surplus on the Balance of Payments. This surplus increased at an average annual rate of 11.5 per cent, but by 1982 there was an adverse swing to an overall deficit position of \$527 million. In 1983 the deficit was estimated at \$2,168 million representing a four-fold increase over the 1982 deficit.

THE ADJUSTMENT PROCESS

The policy of adjustment is clearly enunciated in the 1984 Budget Speech.

"The Government, as prime mover in the economy, unhesitatingly accepts the responsibility for giving the lead in the process of adjustment. In the face of less buoyant revenues, public expenditure must be contained. However, the imperative of providing public goods and satisfying legitimate aspirations for basic amenities must continue ... but this must not be at the expense of our responsibility to maintain the creditworthiness of the country and to protect its foreign reserves. These objectives will be reconciled by a judicious mix of revenue and expenditure measures and by prudent borrowing both locally and abroad.

A major burden of adjustment will also rest on each and every citizen injudicious expenditures, wasteful consumption and our more ostentatious habits must be contained".

Government Capital Expenditure

One of the major adjustment processes, though not specifically elucidated by any Government statement, is necessary reduction of Capital expenditure. In 1983 Government's capital expenditure amounted to \$2,888 million representing a decrease of 20 per cent over the 1982 level, compared with an average annual increase of 37 per cent over the 1974 - 1982 period. This trend is supported by proposals in the 1984 Budget

which projects a further 20 per cent decrease in capital expenditure based on a minimum slate of Capital projects as identified in the Report by the Development Plan Task Force³. On the basis of this elimination or delayed implementation of mainly infrastructural projects, it is estimated that Government capital expenditure will be further scaled down by approximately 23 per cent in 1985.

Foreign Borrowing

Increased foreign borrowing by Government is another policy which has been clearly stated as necessary to the adjustment process. In 1983 Government's fiscal deficit amounted to \$2,857 million of which 83 per cent was financed by a drawdown of Long-Term Development (LTD) Funds and Accumulated Cash Balances, 10 per cent through net local borrowings and 7 per cent through net foreign borrowings. In 1984 the Government deficit is projected at approximately \$2 billion, and although the drawdown of Cash and LTD Funds will finance the greater population, Government plans to borrow close to \$0.5 billion abroad. By May 1984, over 50 per cent of this planned borrowing has been achieved, with international market reaction reported to be favourable. In 1985 however, when Government savings will be exhausted, despite the planned reduction in expenditure, Government's overall borrowing requirement will be appreciably increased.

3 Report of the Task Force appointed by Cabinet to formulate a multi-sector development plan for the Republic of Trinidad and Tobago (August 1983).

Exchange Control

The prudent management of our declining foreign exchange reserves is clearly viewed by Government and the Monetary Authorities as one of the important adjustment processes. With effect from October 10th 1983 the Central Bank introduced a system of import budgeting, the stated objectives were as follows:-

- (i) to slow the rate of decline of the foreign exchange reserves
- (ii) to achieve a better allocation of foreign exchange among competing uses, with priority being given to imports of raw materials and capital goods.
- (iii) to build up a comprehensive data-base on imports and importers

This policy has been reasonably successful. In 1983 total imports amounted to \$6,044 million representing a decrease of 10 per cent over the 1982 level, while the import bill for the first four months of 1984 totalled \$1,445 million, 39 per cent lower than for the corresponding period in 1983. Over this latter period all major categories of imports fell although the decline in Machinery and Transport Equipment, which fell by 60 per cent is attributable to the sharp fall in public sector capital spending. The country's foreign exchange reserves, which declined from \$7,169 million at the end of 1982 to \$4,991mn at the end of 1983, continued to decline in 1984. In the first quarter of 1984, the net foreign exchange reserves decreased by 21

per cent compared to a decrease of 17 per cent in the first quarter of 1983 while in the second quarter of 1984, the decrease of 8 per cent was also higher than the 6 per cent decrease recorded in the second quarter of 1983.

Salary Increases

Restraint in Wage and salary increases appears as another process ordered by the downturn of the economy and sanctioned by Government as part of the overall package of economic adjustment measures. In 1983 the Index of Average Weekly Earnings For All Employees and the Index of Minimum Wage rates For Production And Ancillary Workers in all sectors of the economy, continued to increase at the relatively high rates of 18.4 per cent and 18.1 per cent respectively. However a significant decline in wage and salary increases offered to employees is clearly noticeable in all industrial negotiations undertaken in 1984, and although this may lead to an increasing number of industrial disputes, this policy is likely to continue into 1985.