Analyzing the Sustainability of Public Sector Debt in Trinidad and Tobago

CENTRAL BANK OF TRINIDAD & TOBAGO

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45th Annual Monetary Studies Conference , Kingston, Jamaica, October 2-4 2013
www.central-bank.org.tt

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OUTLINE

- Review of Fiscal Performance
- Debt Sustainability
- Methodology
- Results
- Risks/Vulnerabilities
- Recommendations
- Conclusion

Review of Fiscal Performance

- Since 2009, Government annual spending has exceeded annual earnings.
- Spending over the last 5 years has been 40.1 per cent higher when compared to 5 years prior.

Table 1: Trinidad and Tobago Fiscal Indicators (2004-2013)

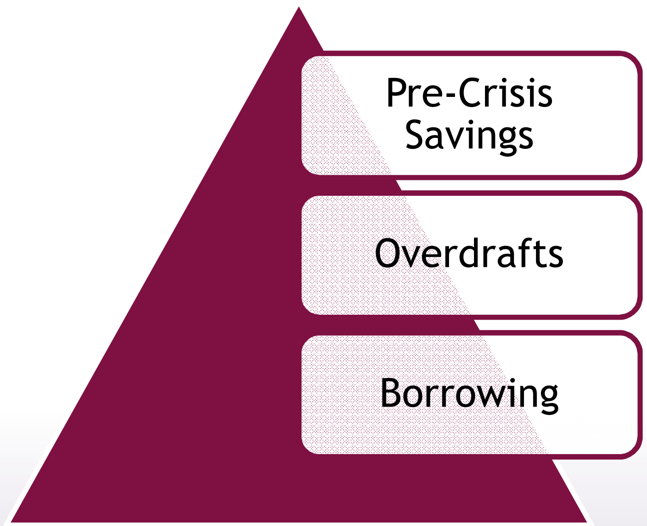
	2004	2005	2006	2007	2008	TOTAL	2009	2010	2011	2012	2013	TOTAL
	(In TT$ Millions)											
Revenue	20.6	29.6	38.9	40.1	56.8	186.1	39.0	43.9	47.5	48.9	50.7	230.1
Expenditure	19.1	27.2	37.1	39.8	53.9	177.1	45.7	43.7	48.6	50.7	59.5	248.2
Sup/Def	1.5	2.4	1.8	0.3	3.0	9.0	-6.7	0.2	-1.1	-1.8	-8.8	-18.1
Non-Energy Def	-7.3	-10.8	-17.5	-16.1	-20.6	-72.2	-26.0	-22.5	-28.4	-28.3	-34.5	-139.8

Objective: Fiscal stimulus & Financial Bailout

Table 2: Fiscal Balance as a per cent of GDP

	2008/ 2009	2009/ 2010	2010/ 2011	2011/ 2012	2012/ 2013P
	In Per cent of GDP				
Non-Energy Balance	-19.3	-17.5	-20.0	-18.8	-20.4
Overall Balance (without CLICO)	-5.0	0.1	-1.4	-1.4	-3.8
CLICO Support	1.4	2.7	0.6	2.6	6.7
Overall Balance (with CLICO)	-6.4	-2.6	-2.0	-4.1	-10.5

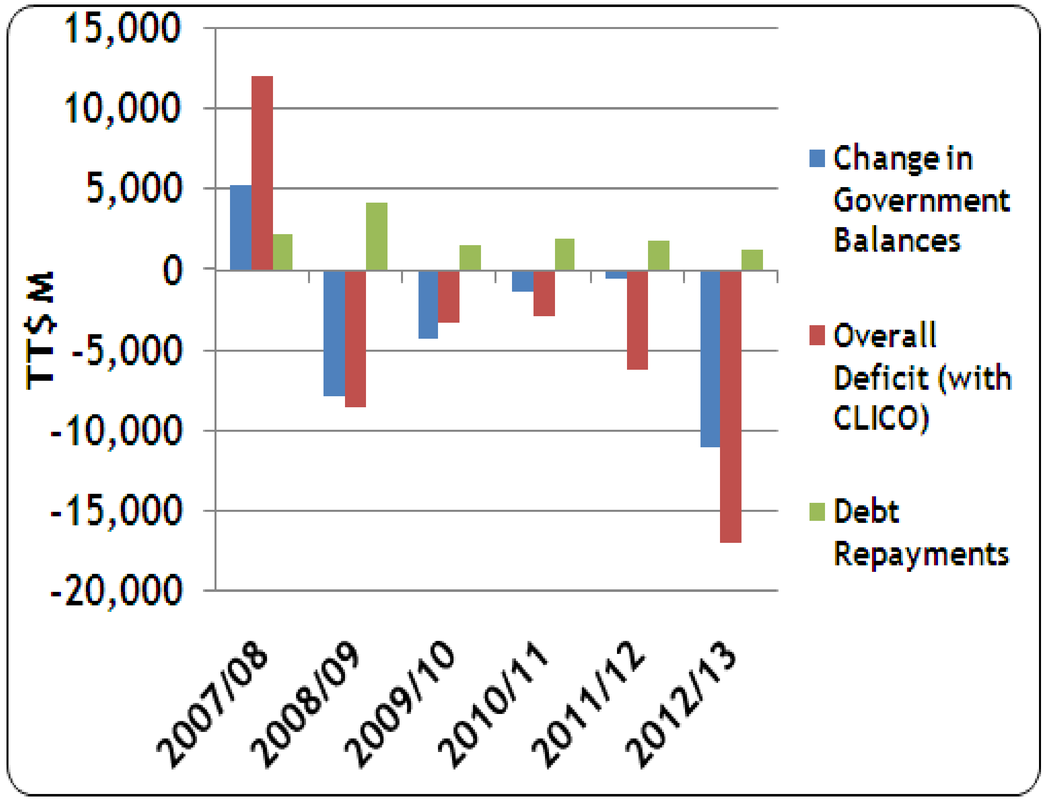
Financing



Impact on Government's Cash Balances

- In the initial years after the crisis, fiscal savings proved adequate to meet debt payments and finance deficits.
- But as CLICO financing increased, cash balances deteriorated and could not adequately finance deficit spending.
- Government borrowing increased sharply in the latter years.

Figure 1: Impact on Government's Cash Balances



Impact on Public Debt

**Figure 2a:
Impact of CLICO Bailout on Public Debt (% of GDP)**

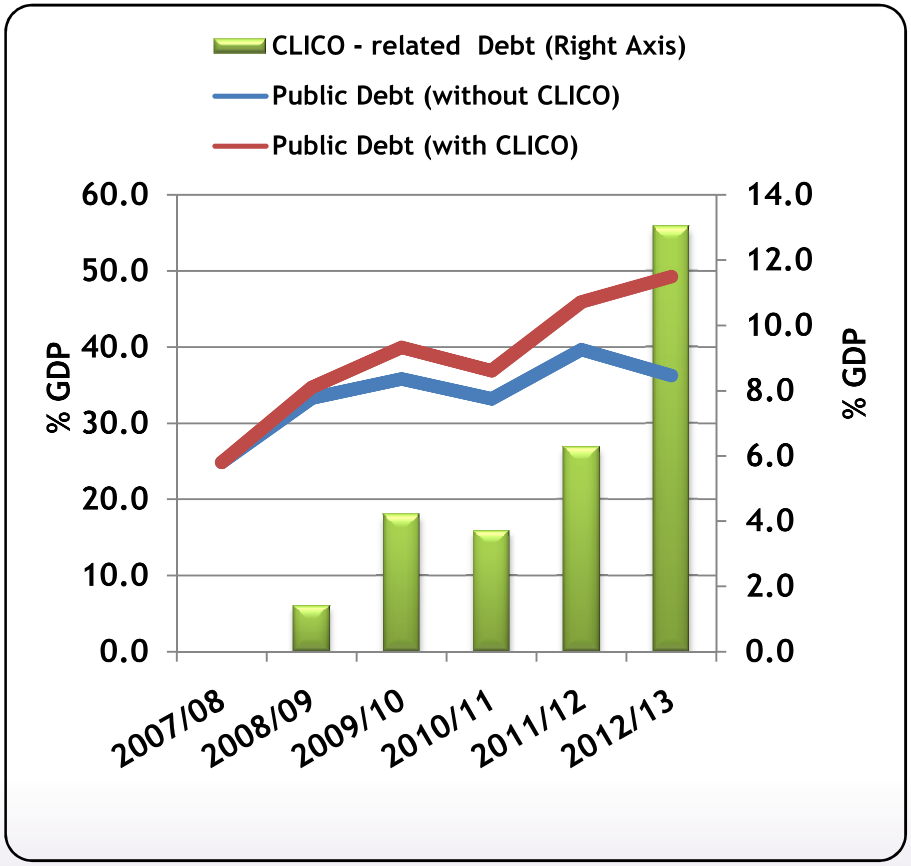
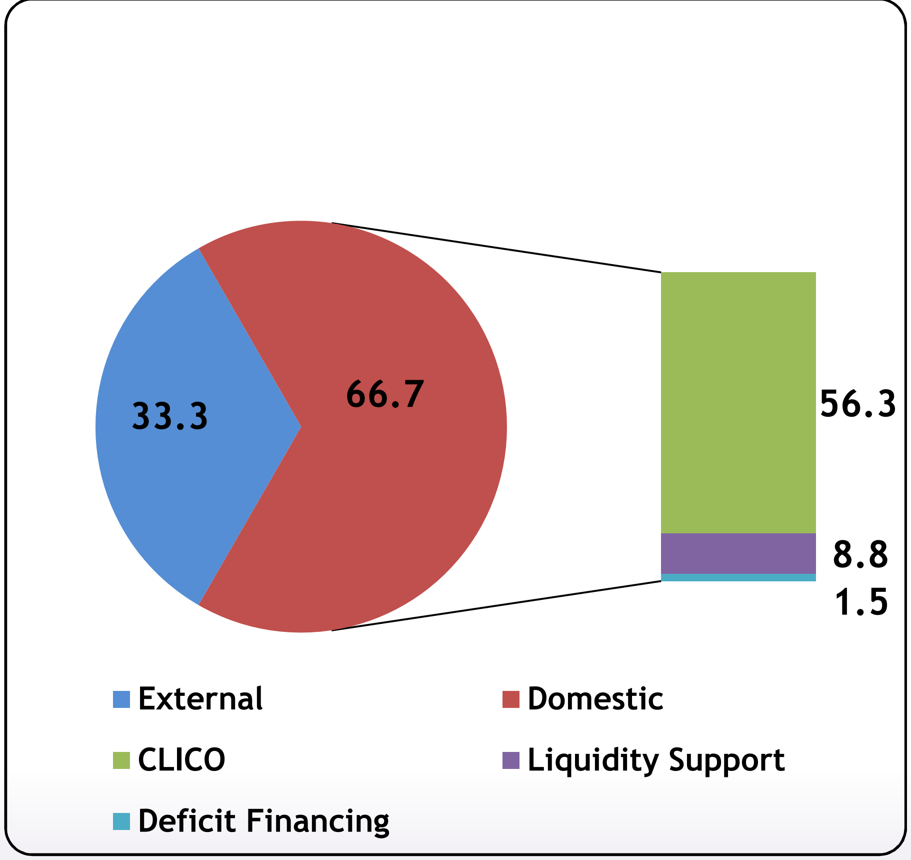


**Figure 2b:
Central Government Sources of Borrowing (2009-2013) - (Per cent)**



Why is Debt Sustainability Important?

What is debt sustainability?

A country's capacity to finance its policy agenda and service the ensuing debt without unduly large adjustments that may compromise its macroeconomic stability and/or that of its economic partners.

Why is it important? – A high level of debt:

- ❑ Constrains Government's social expenditure
- ❑ Reduces a country's ability to withstand shocks
- ❑ Threatens Investment Grade Ratings which increase borrowing costs
- ❑ Increases likelihood for painful austerity and adjustment measures
- ❑ Reduces welfare of future generations

Current Situation

TRADITIONAL INDICATORS	FY2012/13 (Per cent)
Fiscal Balance/GDP	-4.2
Public Debt/GDP	48.6
Public Debt/Exports	69.5
Public Debt/Revenue	142.7
Public Debt Service/GDP	17.2
Public Debt Service/Revenue	50.2
Public Sector Domestic Debt/GDP	40.6
Public Sector External Debt/GDP	8.6
Public Sector Domestic Debt/Total Debt	82.5
Public Sector External Debt/Total Debt	17.5
Public Sector External Debt/Reserves	22.8
Public Sector External Debt Service/Exports	1.0
Average Time to Maturity (Years)	8.7

DSA Methodology

IMF DSA Framework for MACs

- One of many DSA tools
- Identifies the primary balance required to stabilize the debt to GDP ratio
- Determines the gross financing needs
- Decomposes the change in public debt by looking at the debt dynamics
- Illustrates the impact of various shocks on the most realistic scenario

Focus of this Paper

- Public sector DSA template only

- Three (3) Scenarios Examined:
  - Baseline (Proposed Borrowings)
  - Unchanged Primary Deficit (passive)
  - Balanced Budget in 2016 (active)

- The following stress tests are examined:
  - Lower real GDP growth
  - Larger primary deficit
  - Increase in real interest rate
  - 10% increase in contingent liabilities
  - Negative commodity Price Shock (Oil & Gas)
  - Combination shock

Definitions

Definition of Debt

All liabilities that require payment(s) of interest and/or principal by the debtor to the creditor at a date, or dates, in the future.

Coverage of Public Sector

Central Government plus state enterprises and statutory authorities

Treatment of Contingent Liabilities

All explicit guarantees are included in the stock of debt as well as the CLICO –related debt (implicit contingent liability)

Baseline Fiscal Framework

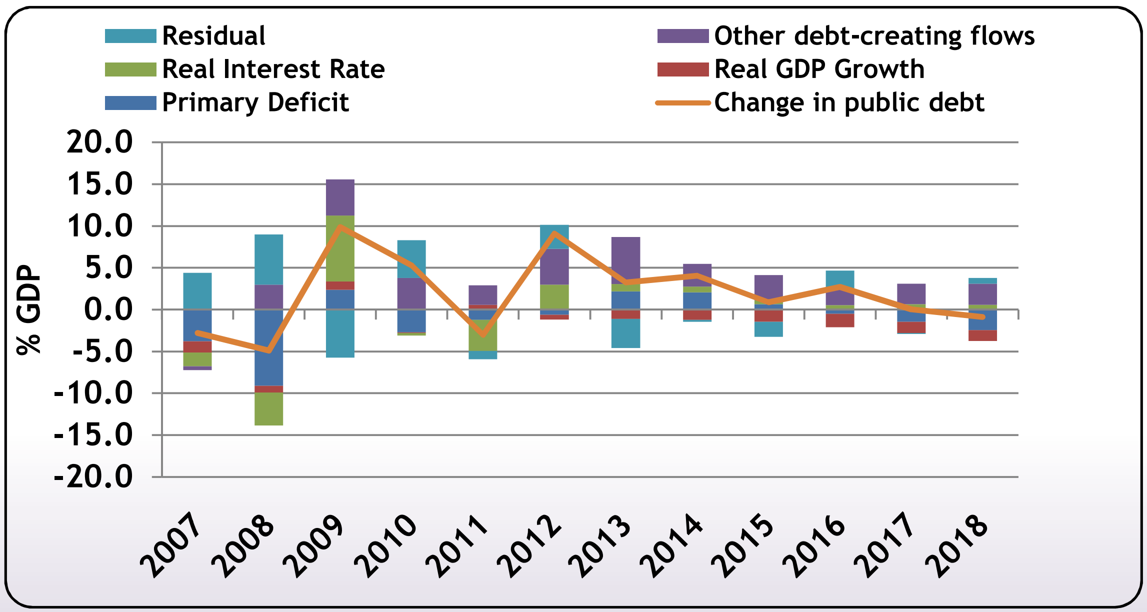
	2011/ 2012	2012/ 2013	2013/ 2014	2014/ 2015	2015/ 2016	2016/ 2017	2017/ 2018
	In per cent of GDP (Fiscal Year)						
Revenue	32.7	34.2	33.6	32.6	33.6	33.8	34.1
Energy	17.7	0.0	17.8	17.1	17.1	17.1	17.1
Non-Energy	14.9	0.0	15.9	15.5	16.5	16.7	17.0
Expenditure	33.9	38.4	37.5	35.7	35.6	34.8	34.1
Current	29.3	33.0	32.6	30.8	30.7	29.9	29.2
Wages & Salaries	4.9	6.2	5.5	5.1	5.7	5.6	5.8
Goods & Services	4.7	5.1	5.4	5.1	5.3	5.2	5.1
Interest Payments	1.8	2.0	1.8	1.8	1.9	1.9	1.9
Transfers & Subsidies (excl. HSF)	17.9	19.7	19.9	18.7	17.9	17.3	16.3
Capital	4.6	5.3	4.9	4.9	4.9	4.9	4.9
Primary Balance	**0.6**	**-2.2**	**-2.1**	**-1.2**	**-0.1**	**0.9**	**1.9**
Non-energy balance	**-18.9**	**-38.4**	**-21.7**	**-20.1**	**-19.1**	**-18.1**	**-17.1**
Overall balance (incl. CLICO)	**-1.2**	**-4.2**	**-3.9**	**-3.0**	**-2.0**	**-1.0**	**0.0**

Public Debt - Baseline scenario

Debt, Economic and Market Indicators

	Actual			Projections					Debt Stabilizing Primary Balance
	2003-2011	2012	2013	2014	2015	2016	2017	2018	
	(In per cent of GDP)								1.8
Gross Public Debt	37.0	46.0	48.6	53.3	54.2	56.7	56.9	57.0	
Gross Public Financing Needs	6.1	13.4	16.8	16.9	13.1	12.7	11.1	9.6	
	(In Per cent)								
Real GDP Growth	4.8	1.5	2.5	2.6	2.9	3.2	2.5	2.5	
Inflation rate (GDP Deflator)	7.7	-2.5	2.9	3.0	3.3	3.5	3.7	4.0	
Nominal GDP Growth	11.4	2.6	3.6	5.5	10.7	2.3	6.4	6.5	
Effective interest rate	7.6	5.5	5.0	4.5	4.3	4.7	5.0	5.2	

Figure 3
Debt Creating Flows
(Per cent of GDP)



Balanced Budget Fiscal Framework

	2011/ 2012	2012/ 2013	2013/ 2014	2014/ 2015	2015/ 2016	2016/ 2017	2017/ 2018
	In per cent of GDP (Fiscal Year)						
Revenue	32.7	34.2	33.6	32.6	33.6	33.8	34.1
Energy	17.7	0.0	17.8	17.1	17.1	17.1	17.1
Non-Energy	14.9	0.0	15.9	15.5	16.5	16.7	17.0
Expenditure	33.9	38.4	37.5	34.7	33.7	33.0	32.5
Current	29.3	33.0	32.6	29.8	28.8	28.1	27.6
Wages & Salaries	4.9	6.2	5.5	5.1	5.7	5.6	5.8
Goods & Services	4.7	5.1	5.4	5.0	4.9	4.8	4.7
Interest Payments	1.8	2.0	1.8	1.8	1.8	1.8	1.8
Transfers & Subsidies (excl. HSF)	17.9	19.7	19.9	17.8	16.4	15.9	15.5
Capital	4.6	5.3	4.9	4.9	4.9	4.9	4.9
Primary Balance	**0.6**	**-2.2**	**-2.1**	**-0.2**	**1.8**	**2.8**	**3.4**
Non-energy balance	**-18.9**	**-38.4**	**-21.7**	**-20.1**	**-19.1**	**-18.1**	**-17.1**
Overall balance (incl. CLICO)	**-1.2**	**-4.2**	**-3.9**	**-2.0**	**-0.0**	**0.9**	**1.6**

Assumptions for Alternative Scenarios

Unchanged Deficit	Balanced Budget
FY2014 budget deficit (3.6% of GDP) stays unchanged until FY2018	Expenditure envelope leads to fiscal balance by FY2015/2016
No restriction in growth of spending on goods & services	Limiting growth in spending on Goods & Services
Payments of subsidy arrears but no removal of fuel subsidy	Payments of subsidy arrears and full removal of fuel subsidy by FY2018
Other transfers & Subsidies growing by inflation	Growth in other transfers does not exceed 3.5% in any given year
Capital spending remains at FY2014 budget (4.9% of GDP)	Capital expenditure kept at FY2014 budgeted (4.9% of GDP)

Alternative Scenarios

Figure 4a
Public Debt
(Per cent of GDP)

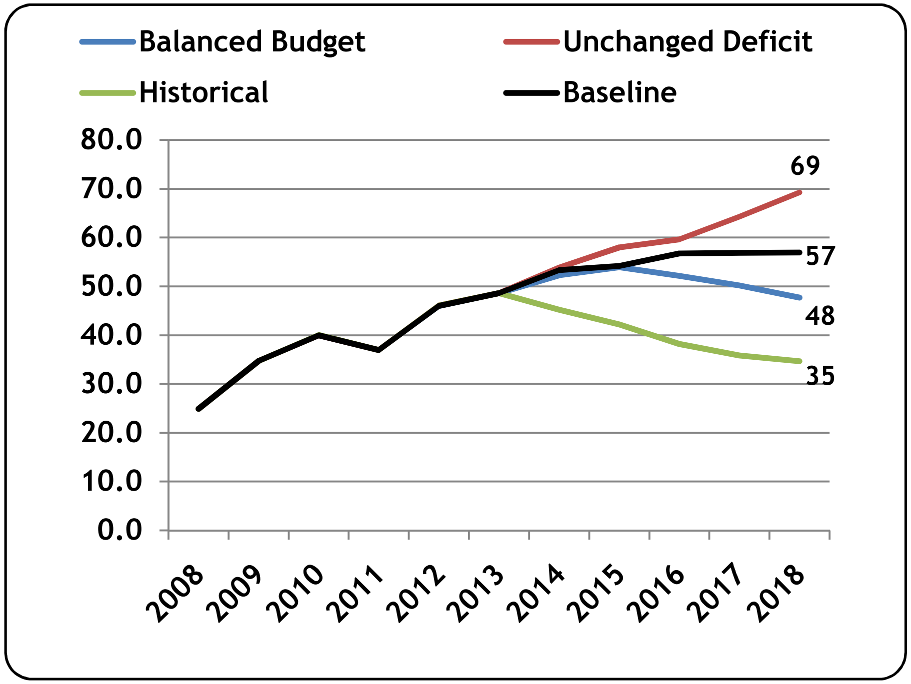
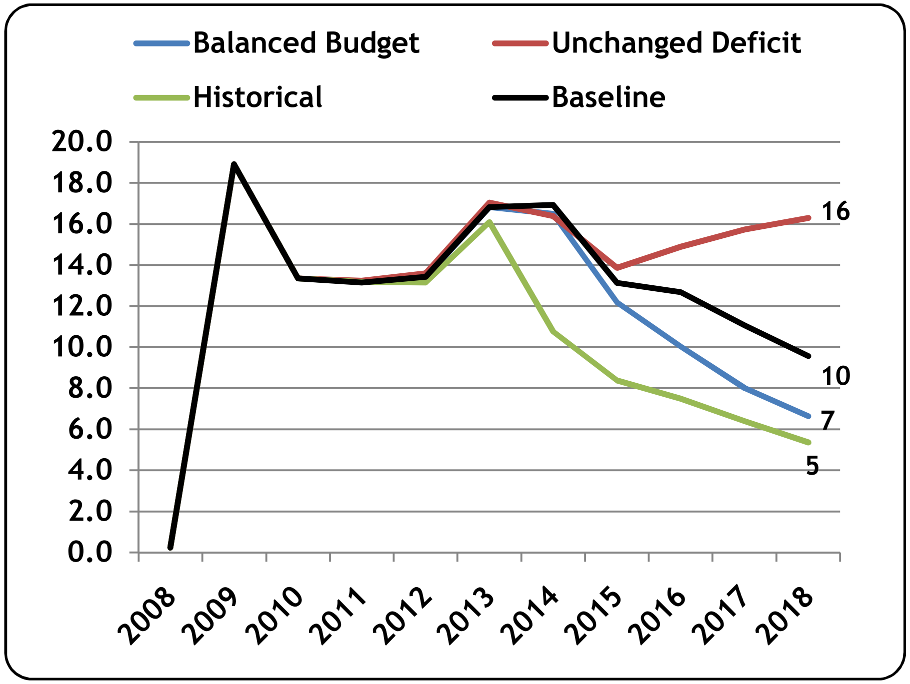


Figure 4b
Gross Financing Needs
(Per cent of GDP)



Stress Tests

Public Debt/GDP

Figure 5a

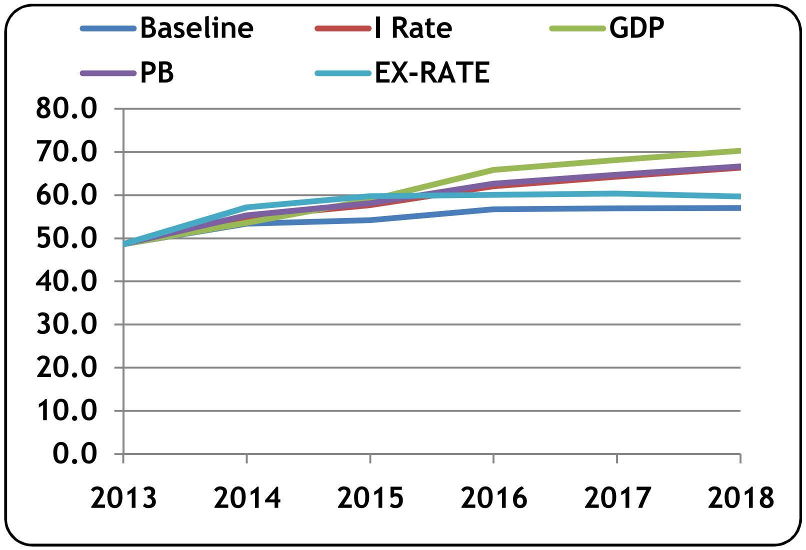


Figure 5b

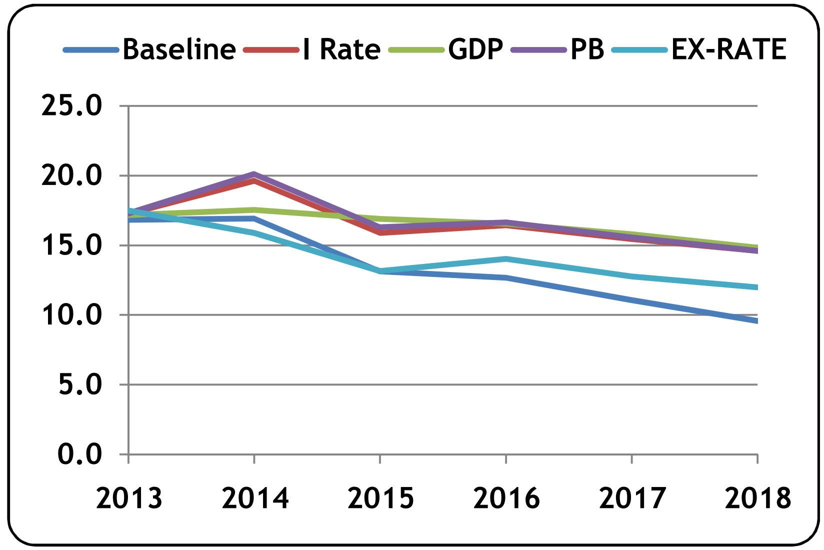


Figure 5c

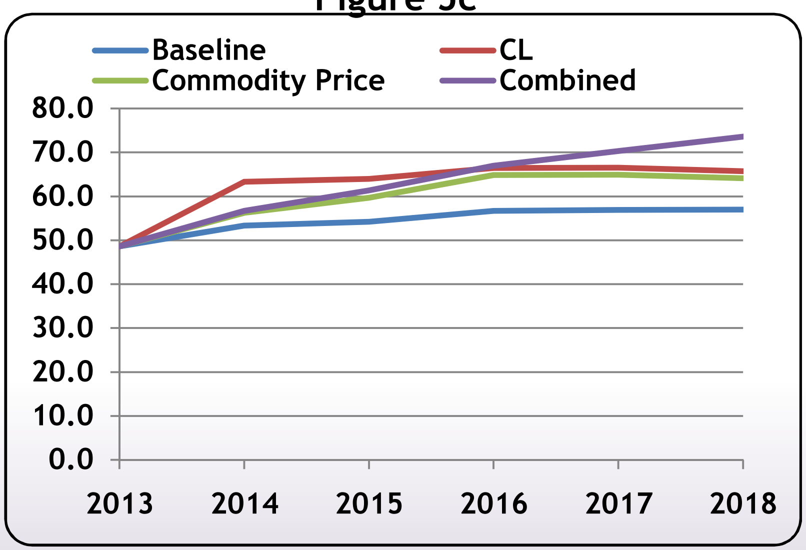
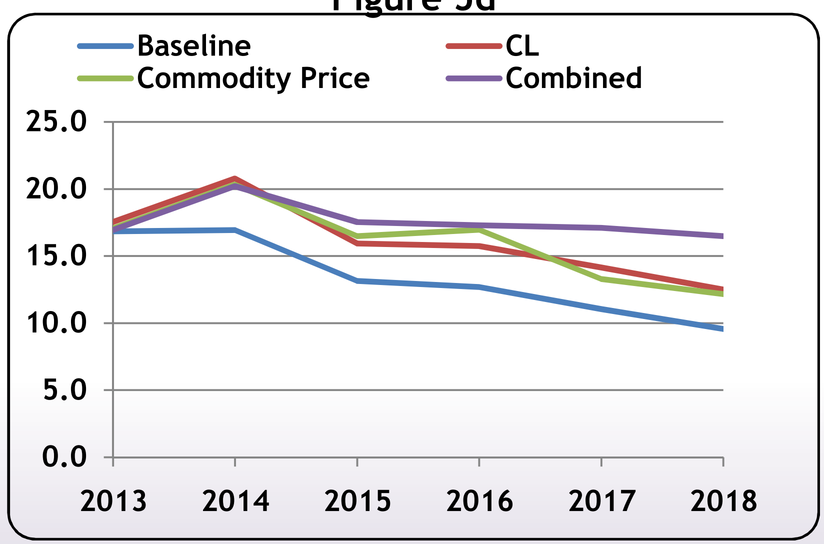


Figure 5d



Gross Financing Needs/GDP Debt

Debt Stabilizing Primary Balance

Scenario/Shock	Debt/GDP FY2018	Gross Financing Needs	DSPB Required
Baseline	**57.0**	**9.6**	**1.8**
i shock	65.6	14.6	3.9
Growth shock	70.3	14.8	1.5
PB shock	66.6	14.6	1.7
CL (10%) shock	65.7	12.7	1.7
30% Dep. shock	59.6	12.0	1.6
Combined (i +g+pb)	73.6	16.5	4.1
Comm. Price shock	64.2	12.2	1.7
Unchanged PB	**70.0**	**16.3**	**2.8**
Balanced Budget in FY2016	**47.7**	**6.8**	**1.6**

Debt Thresholds

- Reinhart & Rogoff (2009 & 2011) define debt thresholds into four(4) brackets:
  - 0% to 30% (low)
  - 30% to 60% (moderate)
  - 60% to 90% (high)
  - Over 90% (very high)

RR Intervals	WB Income Group	Main Economic Activity
0-30% Low		
Suriname	Upp-middle	Commodity Exporter
30-60% Moderate		
The Bahamas	High	Tourism
Trinidad &Tobago	High	Commodity Exporter
60-90% High		
Barbados	High	Tourism
Belize	Low-middle	Tourism
Dominica	Upp-middle	Tourism
Guyana	Low-middle	Commodity Exporter
St. Lucia	Upp-middle	Tourism
St. Vincent/Gren.	Upp-middle	Tourism
> 90% Very High		
Antigua/Barbuda	Upp-middle	Tourism
Grenada	Upp-middle	Tourism
Jamaica	Upp-middle	Tourism
St. kitts/Nevis	Upp-middle	Tourism

Summary of DSA Results

- In the most realistic scenario, the debt to GDP ratio reaches a high of 57% in FY2018 which is below the benchmark (60%). For long-run sustainability a primary balance of at least 1.8% is required.
- But when standard and customized shocks are applied (except exchange rate)the benchmark is breached.
- The no policy change scenario lead to debt ratios in excess of 60% even without the consideration of any shock.
- The balanced budget scenario leads to a debt to GDP ratio below 50% by the end of FY2018.

Fiscal Risks/Vulnerabilities

- The economy is vulnerable to shocks
  - Financial sector crises
  - Natural disasters

- Growth is hinged on the execution of Government Capital Projects – recent experience point to a slower than expected implementation rate

- Government Revenues are volatile (oil/gas price volatility)

- Unsustainable growth in transfers & subsidies

- Contingent Liability risks

Risks in the debt portfolio

Figure 6a

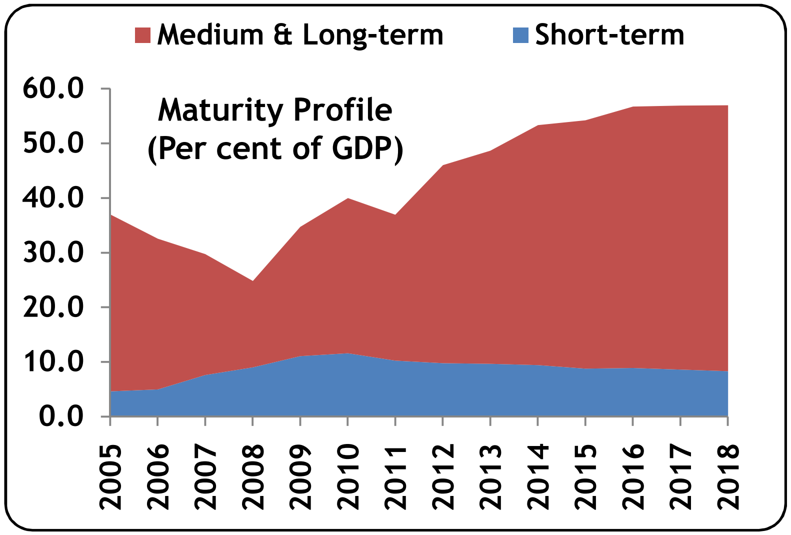


Figure 6b

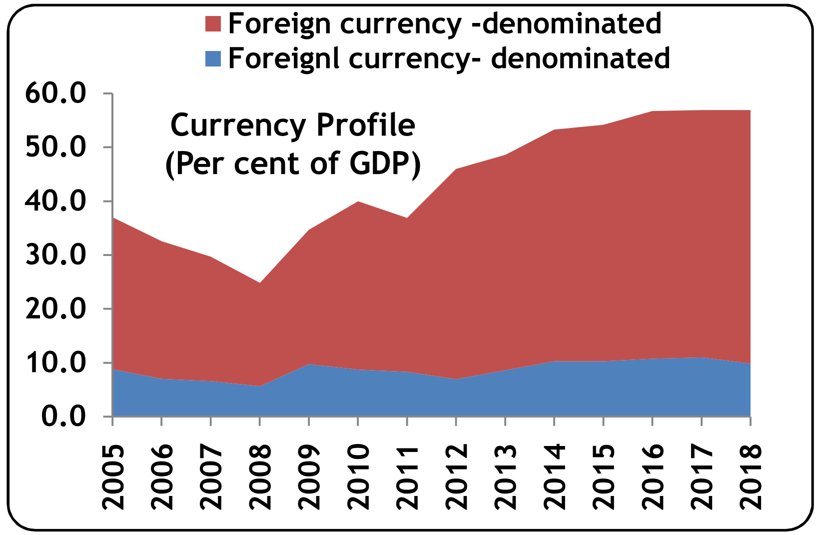


Figure 6c

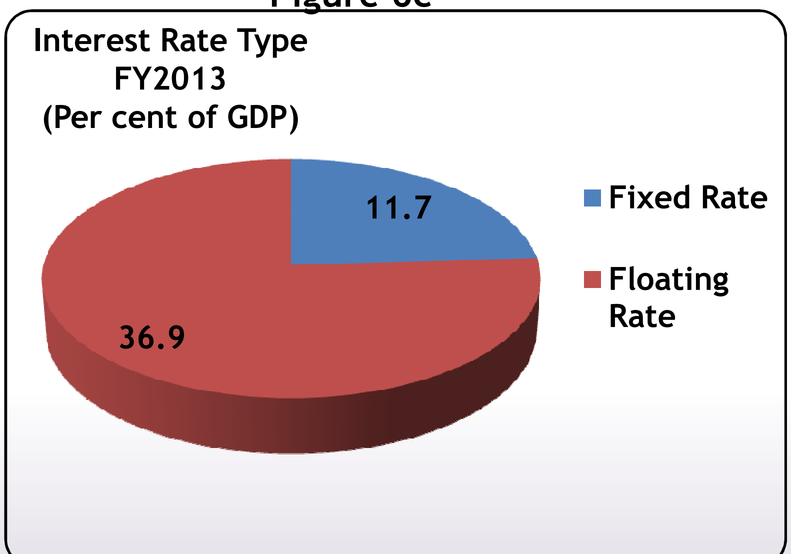
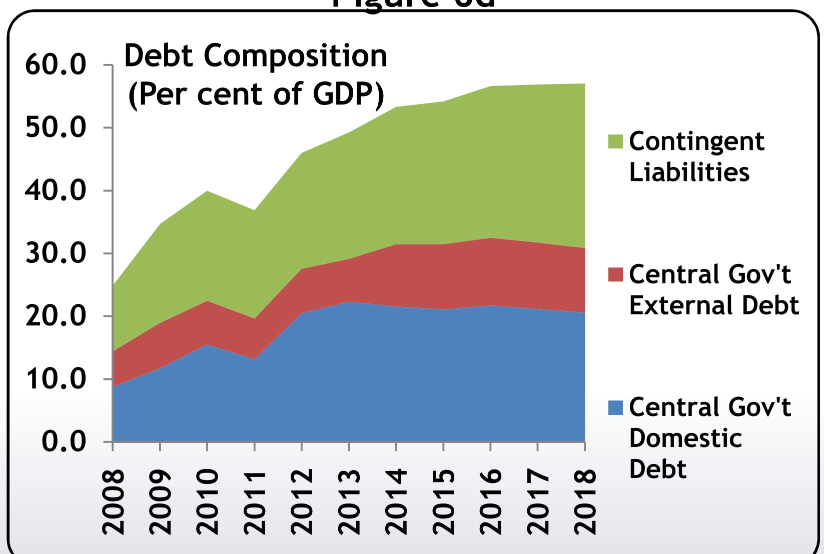


Figure 6d



Institutional Risks

- No formal Debt Management Strategy
- No Annual Borrowing Plan/Bond Issuance Calendar
- Financing decisions made opportunistically without reference to Debt Strategy, Borrowing Plan or established priorities
- Financing decisions often driven by SOEs and Line Ministries without MOF&E input
- Decisions made without reference to debt maturity profile or Borrowing Limits

Recommendations

- Government should aim to balance its budget by FY2016
- Formulation of MTDS
- Greater risk analysis
- Liability Management Operations
- Improvements in Debt recording
- Formulation of ABP & Bond Calendar
- Explore innovative financing instruments

Conclusion

- Public debt in T&T is expected to increase in the medium-term albeit at a slower rate that in the period 2009-2013.
- Gross financing needs are projected to decline on account of a gradual improvement in the fiscal accounts mainly owing to expenditure adjustments in particular transfers & subsidies.
- Public debt is projected to remain within sustainable levels in the medium-term but there are various risks to be addressed.
- Given these downside risks & vulnerabilities, adopting an expenditure envelope that leads to balanced budget by 2016 would free up space to respond to shocks and limit the impact on debt.

Thank you for your attention