

PUBLIC FINANCE IN TRINIDAD AND TOBAGO

By

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FISCAL MANAGEMENT IN A DEVELOPING COUNTRY

There are basically three schools of thought prevailing in the academic world with respect to fiscal management of an economy. These have been categorised as (a) Keynesian, (b) Monetarists and (c) New Cambridge School approaches. To some the last school of thought is relatively new but to most it represents 'old wines in new bottles'. What I propose to do in the ensuing discussion is to attempt to analyse these approaches with special reference to a developing economy. Moreover, I wish to examine the overall fiscal management of certain economies in the Caribbean area to determine how far the policies have gone in diverting resources from lower priority use to higher ones, especially those stimulating economic growth.

The words 'fiscal policy'¹ are frequently used to mean government financial policies designed to benefit the economy largely by diverting resources from low priority areas to higher ones with a view to stimulating overall economic growth. In addition, it is recognized that fiscal policies can be used both in developed and developing countries to mitigate the effects of inflation and possibly control it. However, in the latter economies it is the general belief of many experts that fiscal policy has very limited, if any, usefulness as an instrument for cyclical stimulation of employment.

Keynes in his *General Theory* advocated that increased public spending financed by borrowing in times of a depression should be viewed as a positive instrument by which the aggregate level of income and employment could be increased without the danger of serious price inflation. Such policies tend to work fairly successfully in economies with well developed infrastructure, institutions and organized private manufacturing sectors. In developing countries without these basic facilities, one is not so sure that they would be as effective.

In challenging the theoretical base of contemporary Keynesian economics monetarists have questioned the latter's faith in fiscal measures as the principal tool to stabilise an economy in depressed conditions and effect economic growth. In their view, monetary rather than fiscal policies should be the main instrument for managing demand, i.e. keeping the nation's resources fully utilized without excessive price inflation.

Today, we know that the central concept of Keynes' analysis is a stable income-multiplier (or what comes to the same thing, a stable propensity to consume). Having a stable income multiplier means that a given change in the 'autonomous expenditure' — government spending, investment and exports — or in tax rates has a determinate effect on total spending and output in the economy. Based on these general principles, Keynesian arguments are that demand can be managed by changes in public expenditures and revenue and by stimulating or damping private investment. As regards monetary policy, Keynesians purport that its main role in economic management is to alter the volume of money in the system so as to alter the structure of interest rates (cost of money) to encourage and discourage investment (primary job creating investment). Keynesians seem to have attached little importance to controlling the volume of money in the system, apart from the effects on interest rates (cost of money). It is suggested that they do not believe that the volume of money in the hands of the public (money supply) at any given time has an important effect on total spending *per se*, because they hold that changes in the volume of money will be absorbed by changes in velocity of circulation.

In the opposing view (namely the monetarists), the quantity of money in the hands of the public largely determines total spending. The purported cornerstone of the monetarists' doctrine is the concept of a stable demand function for money (or a predictable income velocity of money). Predictable ("V") income velocity of circulation means that a given change in the volume of money has a determinate effect on total spending in the economy. The theory suggests that the volume of money in the hands of the public (money supply) largely determines total spending in nominal terms and therefore, the level of output and prices. Thus, control of the money supply by the appropriate authorities can in many ways be considered the main instrument of stabilization policy. In their opinion, fiscal policies can play a major supporting role.

A closer look at Keynesian principles suggests that the national budget is the principal instrument for regulating economic activity. When the national budget moves from a surplus position to an overall deficit (so to speak), the effect on total spending is presumed to be expansionary. Conversely, when the budget moves in the opposite direction (from deficit to surplus) the effect is presumed contractionary in conventional terms. Of course, in recent times one notices that this view does not necessarily prevail in an open economy where the budget surplus results from the windfall gains from the exports of the leading sector.

For monetarists, what is important is not necessarily the increase or decrease of expenditure or revenue, nor the deficit or surplus of the national budget, but their overall effects on the money supply. If the budget moves from balance to deficit and the latter is financed by borrowing from the public or banks, monetarists become concerned only if that borrowing involves an expansion of bank credit and thus of the money supply.

If the Central Bank takes no action to accommodate the Treasury or the Finance Ministry by expanding reserve money,² the increase in lending to the government by the public or the banks will probably be at the expense of lending to the private

economy, i.e. private borrowers will get less credit. In such a situation, monetarists claim that the cost of money (interest rates) will generally rise due to the increased demand for credit relative to supply. However, taking the economy as a whole, the overall effect of such policies would not be expansionary. If, however, the central monetary authorities decide to assist the government by expanding bank reserve assets to make room for financing the deficit, there would normally be an overall increase in bank credit and the volume of money in the system (i.e., provided the demand for such credit exists at the appropriate price). In this situation, one expects that the public and the banks will be in a better position to lend more to private borrowers as well as absorb additional government securities (debt). Interest rates (cost of money) will be relatively unaffected by the additional government financing, and taking the economy as a whole, the effects of the policy can be expansionary without inflation if the economy is operating well below full capacity. However, in a developing economy with small or even non-existent capital markets, a small manufacturing sector and few institutions, such policies can prove inflationary or seriously affect the balance of payments as shortfalls in goods and services are generally made up by massive imports to satisfy the excess demand brought on by the increased availability of credit from a highly liquid banking system.

If the national budget moves from balance to surplus (barring an unexpected windfall) and the surplus is used to retire government debt held by the public, the initial reduction in the money supply (argue the monetarists) will be cancelled out. On the other hand, should the surplus be used to retire debt held by the financial intermediaries (mainly the commercial banks) the effect would be to increase bank reserve assets which in the long run could lead to an expansion of bank credit and hence the volume of money in the system (the money supply) by a multiple of the amount of the initial surplus. The ultimate effect on total spending in such a situation would be clearly expansionary. For such actions to prove contractionary, the monetary authorities can sterilize the surplus, i.e., by placing it on fixed deposits with the Central Bank or foreign banking agencies abroad; placing it into special funds (once again fixed deposits) to be held in the Central Bank or using it to retire government debt by the Central Bank. Therefore, the way the budget deficit is financed or the surplus handled makes a marked difference to the way the economy is affected in the final analysis, the monetarists argue.

The third view which has recently surfaced to influence fiscal policy and the management of the economy is that of the 'New Cambridge School'. The new school suggests that there is a direct relationship between the public sector deficit and the current account of the balance of payments in an open economy; so the larger the public sector financial deficit the larger the deficit on the current account of the balance of payments.

Thus, once it is known what government borrowing requirements would be in any fiscal year or for any five-year development programme, one can reasonably forecast the deficit on current account of the balance of payments for the period. The thrust of the new school argument is that the net acquisition of financial assets by the public, private and overseas sector (i.e., balance of payments on current account) + (net capital

transfers) must sum to zero. This, coupled with the assertion that the private sector's net acquisition (personal and company sectors) is stable, suggests that any change in the budget deficit or public sector borrowing requirements must be reflected in the balance of payments on current account. Thus, any government that carelessly follows a principle of deficit financing to prime the economy of a small country (open economy) can be guilty of destroying the balance of payments in the long run.

The new school also contends that 'the private sector has a constant surplus over time, i.e., the M.P.S. of the private sector = 1. Therefore, if in the model $(S - I)$ is constant then $(X - M)$ current account of the balance of payments varies with changes in $(T - G)$, the government sector financial deficit. Thus, in the model, the balance of payments on current account is a simple linear function of $(T - G)$ government public sector deficit or surplus position. In this model the new school suggests that there are no leakages.

$$\begin{aligned}
 X - M &= (S - I) + (T - G) \\
 &= (S_p - I_p) + (S_b - I_b) + (T - G)
 \end{aligned}$$

$(S_p - I_p)$ = Personal Sector	
$(S_b - I_b)$ = Company Sector	
$(T - G)$ = Public Sector	
$(X - M)$ = Trade Balance	

A close examination of this model from a policy angle suggests that literally what the government has to do is simply fix a level for the balance of payments on current account and then set a target level of government surplus on deficit to achieve a desired balance of payments position. In this model T and G must of course vary simultaneously or else the policy makers would have to resort to 'short-term fine tuning of T and G to achieve their objectives.

The new model³ also suggests that the maintenance of internal balances and external balances in the economy requires a balance between domestic expenditure and domestic output which would leave room for imports and of course the balance of payments. They also intended that the balance of payments (current account) would be in deficit so long as domestic expenditure exceeds ($>$) domestic output. The immediate impact of fiscal policy in this situation falls primarily on 'internal balances' and monetary policy on 'external balances' and the balance of payments. But this applies only in the short-term. In the long-term, the New Cambridge School argues that the private sector would have constant surplus over time, so that the balance of payments on current account would reflect the public sector deficit or surplus position.

The problem with Keynesian expansion policy (the new School suggests) is that there is only one policy lever, 'demand expansion' by unbalancing the budget while there are two objectives, namely full employment and balance of payments equilibrium. Thus given the rule that there must be at least one policy lever for each objective, an additional policy lever is clearly required. If the authorities use deficit-financing to expand demand and revalue the currency at the same time, it would have

the authorities use deficit-financing to expand demand and revalue the currency at the same time, it would have the extra policy lever to keep the balance of payments in equilibrium.

However, recent experiences in Guyana, Jamaica and the United Kingdom (all open economies) confirm that the out-turn of such policies can be quite different to the expectations of the authorities.

Against these theoretical backgrounds, this paper attempts to examine the fiscal operations of the Trinidad and Tobago government in the period 1964-1975. The paper also attempts to trace the effect of the budget deficit in the period on base money (monetary base) and its overall effect on the economic system, e.g. inflation, employment. The budget deficit is either financed through the creation of base money and/or through sales of government securities outside the government sector (inclusive of the Central Bank). Because of its effects on these financial stocks, fiscal policy can be reinstated as the main channel of public influence on the economic system.

Fiscal policy, some would argue, already had this role in the economics of Keynes, but lost it in monetarist theory. However, the revival of fiscal policy in recent times has moved beyond orthodox Keynesian approach to include new developments in this field, i.e., a direct influence on the output market via stock in the system. In the new framework, most of the total impact and effects of fiscal policy can be attributed to its financial effects. Consequently, the paper also attempts to focus attention on the budget deficit and therefore expenditure and taxes in manufacturing the stock of base money and government securities in the economy. Moreover, in the examination of inflation in this developing economy it also intends to look at the deficit financed with base money generating the expansion of money and credit in the system. Thirdly, it traces the overall growth of the budget in the period, bearing in mind that the mere size of it can in the long run be inflationary even if it is balanced overtime. Finally, the paper analyses the growth of government debt in the period since a rapidly growing government debt and a large monetization of it can be considered sufficient conditions for fiscally generated inflation.

An examination of the fiscal operations of the Trinidad and Tobago government over the period 1964-1975 reveals that the size of the budget grew from a modest \$261m in 1964 to \$1,366.7m in 1974, an annual rate of growth of 14.0 per cent. In this period the authorities effected two five-year development plans designed to stimulate economic growth. The basic idea of the plans was to initially build the infrastructural base to transform the economy from a subsistence level to a semi-industrialised level. The plans also encompassed the restructuring and general improvement of the educational system (from primary through secondary to university level) to provide the personnel to service the economy. To effect the plan, the administration ran a deficit budget from 1964-1973 and spent \$1.419 billion on its capital programme. Out of this significant capital outlay, some \$1.125m was spent on the development programme.

The interesting feature of this fiscal operation in the period 1964-1975 is the fact that the Trinidad and Tobago government had a continuing surplus on its current

account throughout which clearly accounted for its overall creditworthiness on both domestic and foreign money markets. To be precise, the current account surplus expanded at an annual rate⁴ of 18.0 per cent in the period moving from \$16.7m in 1964 to \$603.5m in 1974. This suggests that the budget deficit was not generated by government dissaving through current account deficit, but was entirely determined by capital account expenditures mainly aimed at effecting the development programmes over the period. The Trinidad and Tobago authorities therefore seemed to have adopted a basic Keynesian stance in their approach to economic development in the 11 year period to 1974. But this fiscal policy, besides effecting the rapid development needed for the transformation of the economy, also had far reaching financial effects. The policy of deficit financing contributed substantially to the widening of the monetary base or the stock of base money in Trinidad and Tobago which moved from a modest \$45.9m in 1964 to \$482.4m in 1975 (an annual growth rate of some 14.4 per cent). However, as the development programme gathered pace and the size of the budget deficit grew, the growth of the stock of base money also expanded, rising to an annual growth rate of 25.5 per cent, i.e. from \$89.3m in 1968 to \$482.4m in 1975. This expansion of the monetary base created the conditions for the sharp expansion of bank credit which was needed to facilitate the flow of finished consumer durables from the manufacturers to the consumer. Bank credit in the period 1963-1975 rose from \$118.03m to \$880.863m representing an annual rate of 18.4 per cent. And, as the monetary base widened between the years 1968-1975, the rate of bank advances to individuals and business agents expanded at an annual rate of 21.7 per cent from \$212.475m to \$880.863m. The out-turn of the fiscal push in the period reviewed is that the money supply (M_1) increased at an annual rate of 18.9 per cent from \$138.3m to \$484.9m in the nine year period to 1975. Unfortunately, this marked expansion of demand through a fiscal push was not matched by a similar expansion of output in the real sector, hence the pressure on prices in the economy since late 1973.

TABLE 1 INDEX OF RETAIL PRICES (ALL ITEMS) (SEPTEMBER, 1960 = 100)

Year	Index as at 31 Dec.	Annual % Change All Items	% Change Food	M_1 Money Supply \$m	% Change Annual
1966	115.5	4.1	3.9	130.235	7.8
1967	117.9	2.1	1.5	136.736	5.0
1968	127.6	8.2	6.5	138.239	1.2
1969	130.8	2.5	2.4	146.918	6.2
1970	134.1	2.5	2.5	170.692	16.2
1971	138.8	2.5	3.5	196.3	15.0
1972	151.7	9.2	11.5	240.1	22.3
1973	174.2	14.8	19.0	242.3	0.8
1974	212.5	21.9	29.9	321.8	32.8
1975	248.6	17.0	16.9	484.9	50.6

Source: Central Statistical Office

The pressure on prices really began to manifest itself in 1972 following the social disturbance in 1970 and the consequent pump priming of the economy to take up the slack in private spendings. In 1968, however, the sharp upturn in prices resulted from the devaluation of the Trinidad and Tobago dollar (which was linked to the £ sterling) in November 1967. However, the sharp upturn in the years following 1970 can be correlated with the expansion of the monetary base and the consequent increase in the money supply M_1 as shown in Table 2.

TABLE 2 MONETARY BASE: BANK CREDIT: MONEY SUPPLY
(\$m)

Year	Monetary Base	% Change (Annual)	Bank Credit	% Change (Annual)	M_1	% Change
1966	66.255	19.1	178.098	6.4	130.235	7.8
1967	70.399	6.2	191.313	7.4	136.736	5.0
1968	89.286	26.8	212.475	11.0	138.339	1.2
1969	92.090	3.1	279.754	31.5	146.918	6.2
1970	105.598	14.7	334.660	19.6	170.692	16.2
1971	122.581	16.0	375.138	12.3	196.3	15.0
1972	134.533	9.7	521.097	38.9	240.1	22.3
1973	155.018	15.2	665.364	27.7	242.3	0.8
1974	306.060	97.4	676.414	1.7	321.8	32.8
1975	482.361	57.6	880.863	30.2	484.9	50.6

Source: Central Monetary Authorities

Of course any meaningful explanation of the causes of inflation in an open economy like Trinidad and Tobago must take into account such exogenous factors as the inflationary pressures emanating from the United States following the Vietnam war and the similar pressures from the U.K. and Europe. However, this paper only attempts to suggest that a fair amount of the inflationary pressures could have emanated from endogenous factors such as the expansionary fiscal policy and the liberal monetary stance.

Whether deficit financing is inflationary or not depends on how much money is created and what the money is used for in the system, e.g. consumption as against investment purposes. It also has to relate to agents' expectations about the movement of prices in the future and of course overall financial management of the economy. An increase in the money supply should not necessarily create inflationary pressures if it is matched by corresponding increases in the level of output. However, if the demand factors far outweighed the supply then such increases could be inflationary.

The extent to which inflation in Trinidad and Tobago may be ascribed to monetary, structural or fiscal causes, is still the subject of considerable debate. Whatever the result of that debate the fact still remains that a continuing rise in the price levels can only be supported by an increasing expansion in the money supply brought about by a similar expansion in credit.

CENTRAL GOVERNMENT FISCAL OPERATIONS

The basic objectives of the last five year development plan (1969-73) were: to increase the scale of total domestic saving (including both public and private sectors); to ensure that such saving is channelled into forms of investment which would facilitate the long-term growth and restructuring of the economy; to effect all necessary infrastructural development to facilitate the growth of industries, education and agriculture. To facilitate the smooth working of the development plan, the administration adopted a fiscal policy aimed at generating reasonable surplus on current account to finance the investment programme. An examination of the government fiscal operation in the period 1964-75 clearly shows that the administration did achieve its objective, but the surpluses on current account were insufficient to cover the rising cost of the capital programme, hence the need to borrow on both the domestic and foreign markets to make good the shortfall.

Recurrent Revenue

In the 11 year period from 1964-1975, recurrent revenue comfortably covered recurrent expenditure to show a surplus in every year as Table 3 clearly shows. However, the demands of the capital programme in the period forced the administration to borrow from domestic and foreign markets. As a result the Central Government gross 'public' debt rose from \$214.3m in 1964 to \$628.4m in 1975 which is an annual rate of growth of 11.8 per cent. Net domestic and foreign borrowing expanded at an annual rate of 14.0 per cent in the period 1964-75 which suggests that the authorities were in some way following a set plan.

Current Surplus

The policy of generating a reasonable surplus on current account through the period was easily achieved as the surplus grew at an annual rate of 18.0 per cent. However, this rate of expansion could be misleading since the windfall in oil revenue following the change in tax structure of oil companies in 1973-74 seemed to have made this growth rate much higher than would have normally obtained.

Central Government Revenue

Central Government current revenue⁵ grew at the annual rate of 14.8 per cent during the period 1964-75. Some 90 per cent of the current revenue came from tax yield while the remainder came from non-tax sources.

As clearly shown in Table 3, the most important source of tax revenue in the period reviewed was income taxes (accounting for over 44.0 per cent (avg.) in the

TABLE 3 CENTRAL GOVERNMENT REVENUE
(\$m)

Economic Classification	1964	1965	1966	1967	1968	1969	1970	1971	1972	1973	1974	1975P
Current Revenue	202.9	206.2	214.4	226.8	267.9	303.6	313.2	341.9	398.2	476.0	1,217.2	1,687.1
Tax Revenue ¹	183.4	185.0	190.6	197.5	234.7	262.9	280.6	314.5	370.4	448.6	1,190.0	1,625.2
Taxes on Foreign Trade	43.6	47.2	48.2	45.0	46.4	49.6	56.0	64.2	71.7	68.3	76.0	100.7
(i) Import Duties	43.4	47.0	48.0	44.8	45.2	49.4	55.8	64.0	71.4	68.0	75.7	100.4
(ii) Export Duties	0.2	0.2	0.2	0.2	0.2	0.2	0.2	0.2	0.3	0.3	0.3	0.3
Internal Taxes on Goods and Services	42.7	46.2	47.3	46.8	68.3	63.6	66.3	76.3	87.7	123.2	225.8	257.4
(i) Oil Royalties	21.9	25.7	26.7	25.7	34.9	24.8	24.2	29.9	27.4	49.9	158.2	178.4
(ii) Excise Duties	15.3	14.7	15.1	16.2	22.3	24.1	25.3	26.8	30.5	36.6	29.2	30.4
(iii) Purchase Tax	5.5	5.8	5.5	4.9	11.1	14.7	16.8	19.6	29.8	36.7	38.4	47.6
Taxes on Property	12.0	10.8	12.7	13.4	15.4	17.1	20.1	21.0	26.2	26.6	30.3	32.3
(i) Estate and Succession Duties	2.5	1.9	1.9	2.0	2.0	1.8	1.7	1.4	2.0	1.4	2.1	1.9
(ii) Taxes on Land and Buildings	1.7	1.8	2.0	2.3	2.4	2.7	4.5	3.3	3.1	4.9	5.8	4.6
(iii) Motor Vehicles Licences and Duties	7.8	7.1	8.8	9.1	11.0	12.6	13.9	16.3	23.1	23.3	22.4	25.8
Taxes on Income	79.4	75.4	76.8	86.5	99.4	126.0	132.2	145.9	172.4	215.3	643.7	1,218.4
(i) Corporate Income Tax	57.6	51.3	48.2	51.0	67.5	89.3	77.0	69.5	81.5	105.8	714.7	1,067.2
(a) Petroleum Companies	48.0	33.0	(32.4)	(35.8)	(46.2)	(64.8)	(48.1)	(39.8)	(52.9)	(57.3)	(657.0)	(936.6)
(ii) Personal Income Tax	21.8	24.1	27.8	28.0	28.6	30.6	39.9	52.2	69.0	89.5	106.6	134.0
(iii) Withholding Tax	-	-	0.8	7.5	3.5	6.0	5.5	12.1	9.0	6.6	7.2	17.0
(iv) Insurance Surrender Tax	-	-	-	-	-	0.1	0.2	0.2	0.1	0.1	0.2	0.2
(v) Unemployment Levy	-	-	-	-	-	-	9.6	11.9	12.8	13.3	15.0	-
Other Licences, Duties, Taxes, Betting and Entertainment	5.7	5.4	5.6	5.7	6.2	6.6	6.0	6.9	10.4	12.8	14.2	16.4
Non Tax Revenue	15.9	14.4	13.1	16.7	18.8	25.8	25.8	25.3	28.9	29.1	27.1	47.6
(i) Post Office	3.2	3.4	3.3	3.7	3.6	5.1	5.2	5.0	5.5	5.5	-	-
(ii) Interest*	3.6	3.2	1.2	3.6	5.6	9.0	9.5	10.5	10.4	10.7	14.0 ^E	-
(iii) Others	7.1	7.8	8.6	9.4	10.6	11.7	11.2	9.8	13.0	12.9	13.1	-
Other Revenue (Total) (non-tax)	5.5	4.8	10.6	12.5	14.3	14.7	16.1	13.8	11.6	11.0	15.1	14.3

Sources: Ministry of Finance; Central Statistical Office; Central Bank of Trinidad and Tobago;

¹ The Classification of Tax Structure Analysis for this Table is different from the normal Budgetary Classification.

r - revised p - provisional E - estimated.

period 1964-73 and 50.9 per cent in the period (1964-74). The next major sources were taxes on foreign trade, internal taxes on goods and services and property taxes.

It has been estimated that tax buoyancy in Trinidad and Tobago in the period reviewed was greater than 1. This suggests that tax revenue in the period grew at a faster rate than income. Such tax buoyancy meant that the government was able to increase its recurrent spending during the period with the knowledge that it would be financed by normal tax yield. It also suggested that the government was able to increase its spending without frequent recourse to the tax regulator during the period. Evidence shows that when the administration was forced to use the tax regulator, it fine-tuned indirect taxes, i.e. purchase taxes and motor vehicle licences and taxes. However, following the social disturbances in 1970 the administration introduced a new form of taxation known as the 'unemployment levy' to assist it to finance its crash programme aimed at taking up the slack in private spending. And, in 1974, the administration changed the structure of taxation on oil companies to reflect the sharp world-wide increase in the price of crude oil. This basic change in the system of taxation of the oil sector resulted in a dramatic change in the overall fiscal position of the government. Tax revenue rose from a modest \$435.3m in 1973 to \$1.175 billion in 1974.

Tax Structure

The tax system of Trinidad and Tobago consists of four basic taxes namely: *taxes on foreign trade* which include the components of import duties and export duties; *internal taxes on goods and services* which incorporate the components of oil royalty, excise duties and purchase tax; *taxes on property* which take in the components of estate and succession duties; taxes on lands and buildings; motor vehicles licences and duties; *taxes on income* which include the components of corporate income tax, personal income tax, withholding tax, insurance surrender tax and unemployment levy.

Revenue from taxation on incomes is by far the largest source of revenue with corporate income contributing the largest share of this source, i.e. corporate income tax on oil companies. This source of revenue represented 39.1 per cent in 1964 and rose to 42.2 per cent by 1969, 45 per cent in 1973 and 69.0 per cent in 1974. The sharp increase in 1974 is largely due to the increase in revenue obtained from oil companies as a result of the tax changes.

Taxes on Foreign Trade

Trinidad and Tobago with its large oil sector is unique among developing countries. It also has a relatively strong base because of the existence of a large oil refinery sector in the economy. Domestic production of crude oil, though on the upturn since 1974, is not sufficient to meet the demands of the oil refinery; as a consequence a substantial portion of crude oil used for this activity has to be imported. It is estimated that on average some 50.5 per cent of total imports between 1963-1972 was crude oil imports which are duty-free. Another 23.0 per cent of imports also entered the country duty-free to suggest that 73.5 per cent of imports

into the country is duty-free. In addition the administration has not taxed exports, primarily to assist the infant industries to get off the ground; as a consequence export taxes have hardly exceeded \$300,000 in any fiscal year.

Evidence shows that between one-fifth to one-quarter of tax revenue has its base in imports, and that imports tax revenue has literally held steady or declined with relation to the growth of tax revenue.

Petroleum taxes

In 1974 the government changed the system of taxation on oil companies to reflect the sharp increase in price of crude oil on world markets. The new tax system ensures that the Treasury will in future capture a substantial part of the profit of the oil producing companies in any financial/fiscal year. The principal changes introduced in the Petroleum Taxes Act of 1974 are as follows (1) whereas the taxable income of the petroleum companies was calculated on realized oil prices; it is now to be calculated on the basis of a tax reference price or the actual prices received whichever is the greater, effective from 1 January 1974. These prices have been set at US\$14.93 per barrel in the case of AMOCO-crude and US \$13.73 per barrel for Soldado crude oil. (2) Royalties would in future be assessed on the basis of the field storage value of crude oil. Currently the rates of royalty are between 10 per cent and 12½ per cent, but the new leases prescribe a rate of 15 per cent. (3) Exploration and production, refining and marketing are classified as separate businesses for the purposes of petroleum taxation. The new taxation meant that revenue from oil companies in 1974 rose to \$667m compared with \$57.3m in 1973 and \$52.9m in 1972.

Internal Taxes on Goods and Services

This category or source of taxation falls primarily on private consumption, hence the inclusion of purchase tax and excise tax. And a look at the table would show that these two components have been comparatively good earners for the treasury. Purchase tax has been used quite frequently in recent years as the main fine-tuning component of the tax regulator. As a consequence purchase tax revenue moved from a meagre \$5.5m in 1964 to \$38.4m in 1974 and a provisional \$47.6m in 1975. The increase in purchase tax revenue in the period 1972-1975 is due in part to an increase in the average purchase tax rates and also to an extension of the base by the inclusion of new chargeable items.

Income Taxes

As stated earlier, this is by far the largest source of tax revenue for the treasury. Normally governments pursue a vigorous income tax policy to effect a more equitable distribution of income in the system. However in the period 1964-75, evidence shows that this objective has not been achieved since there is a greater concentration of income in the hands of the upper income classes. Recent changes in the system of direct taxation with special emphasis on lower income groups are intended to redress this imbalance.

Income taxes on companies other than oil companies seemed to have held steady at around 9.5 per cent of total revenue in the period 1965-73. In fact this source of tax revenue seemed to have shown a slower growth rate than income taxes on individual (persons).

The sharp increase in salaries and wages since 1971 has netted a higher sum of revenue from personal income tax due to the fact that a great number of employed agents in the system moved into higher tax brackets. General taxes on incomes of both companies and individuals rose at an annual rate of 8.9 per cent in the period 1964-74. In the same period personal income tax expanded at an annual rate of 7.2 per cent.

The sharp rise in prices of most consumer durables has also contributed to a marked increase in some components of taxation, e.g. import duties, purchase taxes and taxes on lands and buildings.

The tax system of Trinidad and Tobago seems to be flexible and responsive to the requirements set by recurrent expenditure. This has been a source of comfort and strength for the authorities because they were able to plan the development programme with the knowledge that normal tax yields would comfortably cover recurrent spending and generate a surplus on current account which the records clearly uphold.

Expenditure

To thoroughly investigate fiscal management during the period 1964-75 one has to closely examine the expenditure side of the account and the financing of the budget-deficit over the period. As stated earlier, the government of Trinidad and Tobago seemed to have adopted a Keynesian stance to effect its development programmes in the period 1964-75. The buoyancy of main components of taxes suggests that the tax yield in each fiscal year was sufficient to cover recurrent spending and as a consequence the administration was able to achieve its aim of generating a comfortable surplus on current account in each year in the period 1964-75. During this period, recurrent expenditure expanded at an annual rate of 11.7 per cent moving from \$186.2m (1964) to \$613.7m 1975. Recurrent revenue, however, expanded at a faster rate, increasing at an annual rate of 14.8 per cent in the period reviewed. As a consequence the Central Government fiscal operation moved into a deficit position because of its rising expenditure on the capital account.

Capital Expenditure

Capital expenditure on the development programme which was maintained in spite of the higher cost of financing it expanded at an annual rate of 11.6 per cent between 1964 and 1975. The outlay covered traditional categories of general services which included the items of local government and others; community services which incorporated water and sewerage, drainage, highways and others; social services which included education, health and housing, economic services which took in agriculture, industry, tourism, transport and communication, fuel and power, research, acquisition of financial assets and others.

The bulk of expenditures went on the three main categories of social services, community services and economic services where the administration paid special attention to infrastructural development to effect its transformation of the economy from subsistence level⁶ to semi-industrial level.

Capital expenditure on housing moved from a modest \$5.6m in 1964 to \$22.3m in 1974; and outlays on education advanced from a mere \$2.6m in 1964 to \$37.9m by 1975. Capital spending on highway development only gathered pace in 1967, moving from \$4.3m then to \$24m in 1975. The government also maintained a relatively high level of capital spending on agriculture which moved from \$7.0m in 1964 to \$24m in 1975 but most of this went to bolster the declining sugar industry.

In recent years the outlay on the capital programme has accelerated with the acquisition by the government of the telephone company and other private companies in its overall development programme.

Consumption Outlays

One of the disturbing features of the growth of government spending in the period 1964-1974 has been the high proportion of revenue used to cover consumption outlay. This category includes the components of personnel emoluments, travel, pensions and national insurance; supplies and services; and current transfers. The first component expanded at an annual rate of 17.7 per cent in the 11 years to 1974, moving from \$60.5m in 1964 to \$336.0m in 1974. It accelerated at an even faster rate between 1969-73, rising at an annual rate of 27.5 per cent, i.e. from \$100.6m to \$336m. In the last five-year development the government had to accommodate two pay demands from its employees which accounted for the sharp rise in that period.

Spending on supplies and services accelerated at an annual rate of 7.2 per cent in the 11 years to 1974. However, in the period 1969-74 the annual rate of growth was 13.0 per cent, reflecting the price inflation affecting the economy.

Lastly, the component current transfers which go to local government expanded at an annual rate of 6 per cent in the 11 years to 1974. And between 1969 and 1974 this component moved from \$30m to \$60.8m.

Overall gross consumption outlays in the period 1964-74 expanded at an annual rate of 11.9 per cent moving from \$177.9m (1964) to \$571.2m (1974).

FINANCING OPERATIONS

In adopting its Keynesian stance to stimulate economic growth and restructure the economy, the administration expanded its budget-deficit at an annual rate of 12.4 per cent in the period 1964 to 1973. The deficit moved from \$33.8m in 1964 to \$130.5m by 1972, falling to \$68.5m in 1973. In 1974, the budget moved into positive surplus because of the windfall from receipts from the petroleum companies.

To finance this growing deficit, the administration's net domestic borrowing rose at an annual rate of 14.0 per cent in the period reviewed from \$27.9m in 1964 to

TABLE 4 CENTRAL GOVERNMENT EXPENDITURE

(\$m)

	1964	1965	1966	1967	1968	1969	1970	1971	1972	1973	1974	1975 ^P
1. Recurrent Expenditure	150.8	157.8	161.1	178.4	195.6	205.1	225.6	288.8	349.7	371.1	552.9	656.1
2. Current Transfers	35.4	32.1	39.2	24.9	23.7	30.0	33.9	38.9	43.9	54.2	60.8	89.0
3. Total Recurrent Expenditure	186.2	189.9	200.3	203.3	219.3	235.1	259.5	327.7	393.6	425.3	613.7	745.1
4. Loans to Statutory Bodies	--	--	--	10.0	8.8	13.7	13.2	14.4	16.3	19.3	54.3	56.1
5. Capital Expenditure (Total)	78.4	60.8	66.2	57.7	76.7	76.9	116.4	123.0	143.7	128.6	224.6	266.0
(i) Development Program	52.5	52.3	60.3	48.1	61.8	60.1	98.0	103.5	123.6	104.4	145.5	215.2
(ii) Cap. Repayment and Sinking Fund	8.8	8.5	5.9	9.6	14.9	16.8	18.4	19.5	20.1	24.5	79.1	50.8
(iii) Others	17.1	--	--	--	--	--	--	--	--	--	408.7	701.6
6. Appropriation to Special Fund	--	--	--	--	--	--	--	--	--	--	--	--
TOTAL OUTLAY	264.6	250.7	266.5	271.0	304.8	325.7	389.1	465.1	553.6	573.5	1,301.3	1,768.8
7. Consumption Outlay	177.9	178.5	188.3	190.0	202.7	220.0	240.3	306.3	337.5	454.6	571.2	686.6
(i) Personal Emoluments Travel, Pensions, NIS	60.5	63.5	83.3	89.0	95.3	100.6	110.4	158.8	206.3	237.4	336.0 ¹	395.5 ¹
(ii) Supplies and Services	82.0	82.9	65.8	76.1	83.7	89.4	96.0	108.6	87.3	141.9	174.4	202.1
(iii) Current Transfers	35.4	32.1	39.2	24.9	23.7	30.0	33.9	38.9	43.9	54.2	60.8	89.0

Sources: Ministry of Finance; Central Statistical Office; Central Bank of Trinidad and Tobago;

^Pprovisional

¹includes personal emoluments and overtime paid to Statutory Bodies (in addition to loans).

TABLE 5 CAPITAL EXPENDITURE (DEVELOPMENT PROGRAMME ETC.) TRINIDAD AND TOBAGO

(\$m)

	1964	1965	1966	1967	1968	1969	1970	1971	1972	1973	1974	1975 ¹
Total	62.5	57.8	60.3	54.9	66.8	60.0	98.2	103.0	123.0	104.4	154.2	216.0
GENERAL SERVICES	--	--	--	2.5	2.1	3.2	4.9	5.0	5.7	7.2	6.6	16.1
(i) Local Authorities	--	--	--	1.0	1.2	1.8	1.3	1.5	2.0	2.4	2.5	5.7
(ii) Others	--	--	--	1.5	0.9	1.4	3.6	3.5	3.7	4.8	4.1	10.4
COMMUNITY SERVICES	3.6	4.4	3.8	12.7	13.2	21.3	25.9	34.5	35.5	32.8	52.5	74.0
(i) Water and Sewerage	3.2	3.8	3.0	5.4	5.2	5.8	4.7	5.8	8.6	7.4	10.1	22.0
(ii) Drainage	--	--	--	0.7	1.0	1.3	1.0	1.3	1.4	1.5	11.6	3.4
(iii) Highways	--	--	--	4.3	4.0	8.9	10.2	14.0	11.7	7.3	18.7	24.0
(iv) Others	0.4	0.6	0.8	2.3	3.0	5.3	10.0	13.4	13.8	16.4	22.1	24.6
SOCIAL SERVICES	14.9	15.3	16.5	6.9	12.6	12.5	21.5	33.5	33.3	28.4	45.1	66.0
(i) Education	2.6	3.6	4.6	4.9	8.9	5.1	8.0	14.2	19.0	15.1	18.8	37.9
(ii) Health	6.7	7.0	6.9	0.4	0.4	0.8	1.1	0.9	3.3	3.3	4.0	10.9
(iii) Housing	5.6	4.7	5.0	1.6	3.3	6.6	12.4	18.4	11.0	10.0	22.3	17.2
ECONOMIC SERVICES	44.0	38.1	40.0	32.8	38.8	23.0	28.8	30.5	32.7	31.2	40.0	47.4
(i) Agriculture	7.0	7.2	9.5	10.4	11.6	14.4	11.2	12.2	14.8	18.2	23.2	24.0
(ii) Industry and Tourism	0.6	0.7	1.3	2.1	3.0	2.9	11.5	5.2	5.3	3.1	2.7	5.9
(iii) Transport and Communication	9.4	12.7	16.8	11.4	5.8	1.3	3.5	5.7	5.6	4.6	1.8	3.7
(iv) Fuel and Power	20.4	9.2	6.1	8.4	17.8	3.3	2.0	1.7	--	--	--	--
(v) Research	--	--	--	0.5	0.6	1.1	0.5	3.5	4.1	4.9	7.7	7.2
(vi) Other	6.6	8.3	6.3	--	--	--	--	2.2	2.9	0.4	4.6	6.6
Acquisition of Foreign Assets ¹	--	--	--	--	--	--	17.1	--	21.4	4.8	10.0	12.5
Adjustments	--	--	--	--	--	--	--	--	5.6	--	--	--

Source: Ministry of Finance

¹Purchase of equities in Private Companies

\$106.1m in 1972, falling to \$49.6m in 1974. In the same period, net foreign borrowing expanded at an annual rate of 14.0 per cent from \$28.4m in 1964 to \$65.9m in 1973, falling to \$47.3m 1974. The growth rate in domestic and foreign borrowing suggests that the authorities were conscious of the financial effects of expansion of government securities in the economy in general and on future taxpayers in particular.

Borrowing

Every decision by the Central Government to borrow on the local market represents a political will to divert additional resources to the public sector from the private sector and to use them to meet certain goals. On the other hand, the government decision to borrow externally, initially involves a net inflow of foreign currency, but subsequent repayments of loans would entail a transfer of resources from the domestic economy to foreign economies. Such drainage of badly needed hard currencies (foreign) normally affects the overall balance of payments. On the other hand, subsequent repayment of loans raised locally would entail a transfer of income from taxpayers to holders of debt (claims) in the economy. This (repayment of local loans) would clearly involve a redistribution of income, but there would be no strain on the balance of payments *per se*, and there need not be any net reduction in total income in the domestic economy.

In financing the deficit, the government expanded gross public debt at an annual rate of 12.3 per cent from \$136.7m in 1962 to \$636.0m in 1975. In this period, it expanded external debt (gross) at an annual rate of 7.8 per cent and gross internal debt at an annual rate of 21.0 per cent, which suggests that the aim of its overall debt management was to minimize the drain of foreign currencies from the economy in the future. The faster rate of growth of domestic debt (gross) meant initially that there was a marked transfer of resources from the private sector to the public sector, which possibly could account for the slow growth of investment spending by this sector during the period. This transfer of resources to the public sector meant a net expansion in the public sector to take up the output from its educational programme and to effect its overall infrastructural development.

Internal Debt

In its overall debt management, the administration in the period 1965-75 expanded internal long-term debt at an annual rate of 18.4 per cent from \$75.6m (1965) to \$310.4m in 1975. In the same period, it expanded its short-term internal debt at an annual rate of 11.5 per cent from \$32.4m in 1965 to \$101.2m. However, this expansion of short-term debt markedly increased the secondary reserves of the banking system to facilitate the consequent expansion of bank credit. This expansion in the secondary reserves coupled with the fact that government spending followed a similar trend suggests that the banking system primary reserves also expanded markedly as did the monetary base. The expansion in stock of base money and government securities facilitated the rapid growth of bank credit and the money supply in the period 1964-1975. The sharp expansion of bank credit also influenced the demand for imported goods to meet the shortfall in supply besides putting pressure on prices and output.

PUBLIC FINANCE IN TRINIDAD

TABLE 6
CENTRAL GOVERNMENT: FISCAL OPERATIONS
(\$m)

	1964	1965	1966	1967	1968	1969	1970	1971	1972	1973	1974	1975P
Current Revenue	202.9	206.2	214.4	226.8	267.9	303.6	313.2	341.9	398.3	476.0	1,217.2	1,687.1
Current Expenditure	186.2	189.9	200.3	203.3	219.3	235.1	259.5	327.7	393.6	425.3	613.7	745.1
Current Surplus	16.7	16.7	14.1	23.5	48.6	68.5	53.7	14.2	4.7	50.7	603.5	942.0
Capital Revenue	2.0	27.1	14.0	12.6	16.1	4.7	4.3	10.0	4.7	4.2	83.6	34.1
Capital Expenditure												
Development Programme	52.5	52.3	60.3	48.1	61.8	60.1	98.0	103.5	123.6	104.4	145.5	215.2
Loans to Statutory Bodies				10.0	8.8	13.7	13.2	14.4	16.3	19.3	54.3	56.1
Use of Special Funds											125.2	38.3
Overall Surplus (+) Deficit (-)	-33.8	-8.9	-32.2	-22.0	-5.9	-0.6	-53.2	-93.7	-130.5	-68.8	+362.1	+666.5
Financial Total	+33.8	+ 8.9	+32.2	+22.0	+ 5.9	+ 0.6	+53.2	+93.7	+130.5	+68.8	-362.1	-666.5
Gross Domestic Borrowing	+27.9	+14.5	+24.5	+10.2	+30.4	+22.0	+22.8	+43.7	+106.1	+45.1	+49.6	+ 37.0
Gross Foreign Borrowing	+28.4	+ 8.8	+10.8	+24.8	+26.2	+18.5	+ 7.7	+38.7	+ 44.5	+65.9	+ 47.3	+ 11.4
Capital Repayments and Sinking Fund	-25.9	- 8.5	- 5.9	- 9.6	-14.9	-16.8	-18.4	-19.4	- 20.1	-24.5	- 79.1	- 50.8
OTHERS	+ 3.4	- 5.9	+ 2.8	- 3.4	-35.9	-23.1	+41.1	+30.7	-	-17.7	- 96.4	- 0.8
Appropriation to Special Fund											-283.5	-663.3
(-) Increase (+) Decrease												

Sources: Ministry of Finance, Auditor General's Report 1974; Central Bank of Trinidad and Tobago, Provisional

Debt Burden

Most debts can be classified as burdens to those agents repaying them. But psychologically that strain can be eased if the funds raised are put to work on projects that yield a net return.

In analysing the debt burden of an economy one can use the indicator foreign debt servicing/net foreign assets. This indicator measures the proportion of net income in foreign exchange which is absorbed in servicing the foreign debt. The indicator is also used by the major world financial institutions to assess the creditworthiness of a country from time to time e.g. World Bank, Export-Import Bank, etc. During the period reviewed, the percentage of foreign debt servicing to net foreign assets averaged 19.7 per cent between 1969-1973 reaching a peak of 34.9 per cent in 1973. In the period 1974-1976 the average dipped to 6.2 per cent due mainly to a sharp rise in net foreign exchange earnings rather than a decline in foreign debt servicing. In fact the latter period witnessed a marked increase in foreign debt servicing. The data in these two periods suggest that Trinidad and Tobago was in serious straits in 1973 when its net foreign reserves dwindled to just \$67.1m while in the same year its foreign debt servicing increased sharply.

The position was reversed in 1974-1976 because the price of crude oil was increased substantially to allow Trinidad and Tobago's net foreign reserves to increase markedly as a consequence. The foreign debt burden was very small in the latter period and could well continue that way in the foreseeable future if the authorities continue to pay off their foreign debt quickly. It could rise sharply if the authorities decide to borrow heavily on foreign capital markets to finance such heavy capital projects as the aluminium smelter plant and the steel mill.

An examination of the deployment of funds raised on both domestic and foreign markets showed that they were used primarily to effect the development programme. The net returns were more schools, houses and in some instances more roads and the acquisition of certain private companies. It also involved a massive investment in human resources which paid rich dividends in the high standard of graduates coming from the secondary schools and higher educational institutions. However, an assessment of the administration's fiscal stance suggests that the main impact was on demand rather than supply, in spite of its generous fiscal incentives to the manufacturing sector. The weak performance of the private sector meant that there was a marked shortfall in the supply of job opportunities to match the increased demand brought about by the rise in school leavers and net increase in the population. To meet this shortfall, the public sector was deliberately expanded at an increasing rate in the period 1964-1975. However, many experts suggest that the capacity of the public sector to absorb more agents on the job market could be reaching saturation point, hence the need for a rethinking of the overall development policy.⁷

Creditworthiness

As noted earlier, the administration expanded external borrowing (net) at an annual rate of 14.0 per cent in the period 1964-1975. For this, the authorities had to meet the stiff conditions laid down by foreign institutions, e.g., that the particular

project generates a net return which would clear all cost; that the volume and maturity structure of its gross debt be such as to hold the overall burden of foreign debt repayments to within a reasonable proportion of net foreign exchange earnings, e.g. 20 per cent; that the burden of foreign debt repayments remains sustainable in light of the economy's growth and level of income.

The strength of the Central Government's financial position today clearly suggests that such conditions can be met in the immediate future. However, in the period 1971-73, the net foreign reserves of the government ran to such a low level that it threatened to markedly weaken the good credit record of the administration, a position which suggests that the authorities should always try to keep their foreign debt repayments well within the 20 per cent limit of net foreign exchange earnings.

TABLE 7 CENTRAL GOVERNMENT — PUBLIC DEBT 1963-1975

(\$m)					
As at 31st Dec.	Total	External	Internal	Cumulative Sinking Fund	Net Public Debt
Year	(1)	(2)	(3)	(4)	Col. (1) — Col. (4)
1962	136.7	72.7	64.0	33.7	103.0
1963	180.1	112.0	68.1	37.8	142.3
1964	214.3	121.0	93.3	42.4	171.9
1965	232.5	124.5	108.0	47.7	184.8
1966	266.1	136.3	129.8	53.1	213.0
1967	298.2	143.4	154.8	60.0	238.2
1968	338.8	157.2	181.6	63.8	275.0
1969	370.4	167.9	202.5	72.9	297.5
1970	392.6	158.2	234.4	78.0	314.6
1971	438.0	162.1	275.9	50.0	388.0
1972	533.1	199.2	333.9	67.0	466.1
1973	625.9	255.7	370.2	77.5	548.4
1974	628.4	241.4	387.3	89.9	592.5
1975	636.0	232.5	413.5	106.2	529.8

Deficit Financing and the Balance of Payments

The government of Trinidad and Tobago in its two five-year development plans adopted a Keynesian posture of deficit financing to expand economic activity in the economy. The objectives of the plans were, as stated earlier, to effect a more rapid rate of economic growth, restructure the economy from a subsistence level to a semi-industrialised level and train an increasing number of personnel locally to service the expanded public and private sectors. The effects of this fiscal policy on the balance of payments were damaging enough to make the country show an overall deficit on current account in the period 1964 to 1973. This position was only reversed when the authorities changed the system of taxation on oil companies and netted a substantial

(\$m)

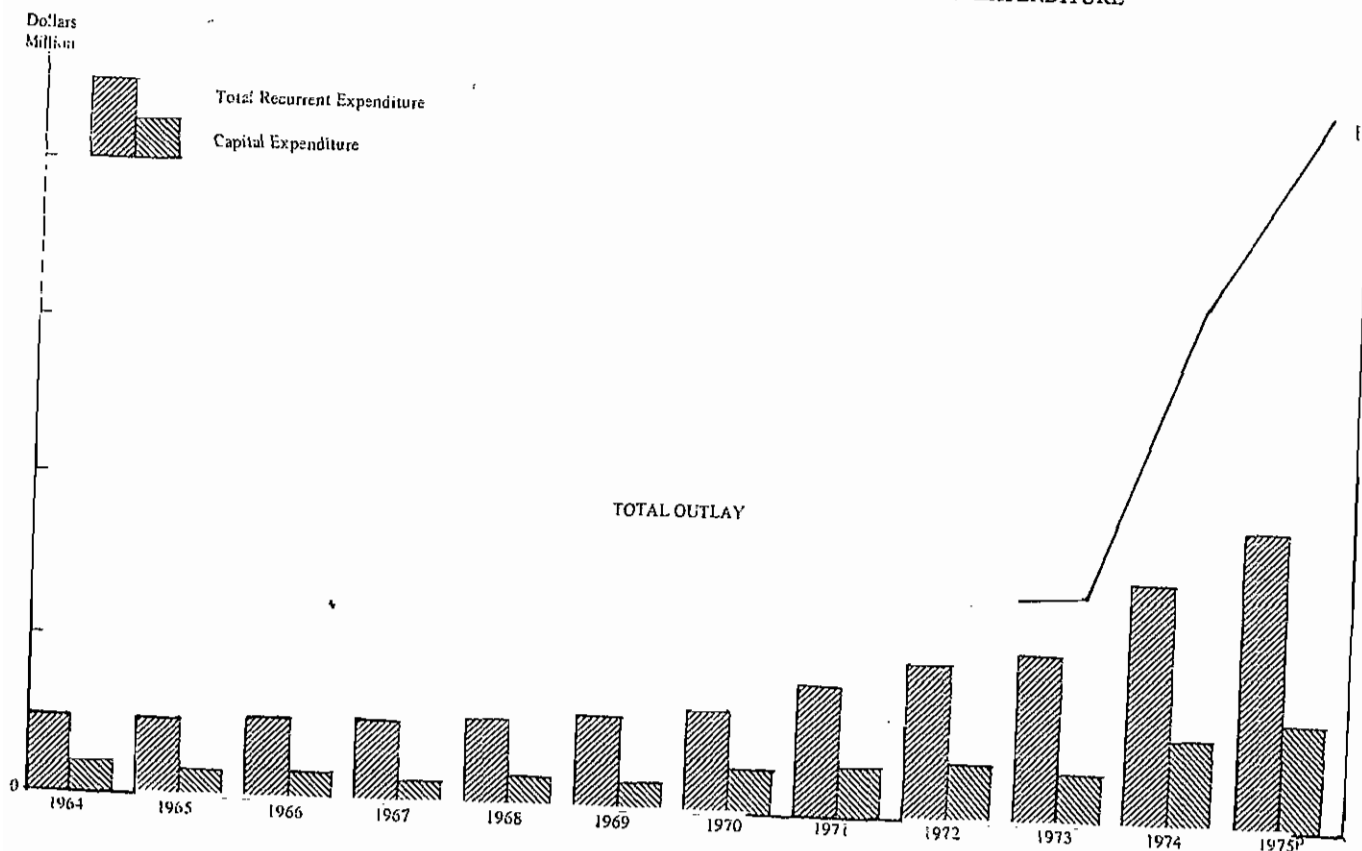
Debt Servicing

Year	Central Government Revenue (Total)	Total National Debt	Local Debt	External Debt	Local Interest	Amortization and Sinking Fund		Amortization and Sinking Fund	Net Foreign Exchange as at December	% (7) + (8) (9)	(5) + (6) + (7) + (8) (1)
						External Interest	Local Interest				
	(1)	(2)	(3)	(4)	(5)	(6)	(7)	(8)	(9)	(10)	(11)
1969	348.8	370.5	202.6	167.9	11.3	6.5	8.3	10.0	121.4	15.1	10.3
1970	389.1	392.6	234.4	158.2	12.4	7.5	9.1	10.8	106.6	18.7	10.2
1971	465.0	438.0	275.9	162.1	14.5	8.2	9.0	11.0	156.3	13.0	9.2
1972	553.6	533.1	333.9	199.2	16.9	11.8	10.6	8.1	110.4	16.9	8.6
1973	591.2	625.9	370.2	255.7	21.6	14.1	13.0	10.4	67.1	34.9	10.0
1974	1,806.4	628.7	387.3	241.4	25.8	16.0	25.4	63.1	768.3	11.5	7.2
1975	2,260.5	636.1	413.6	222.5	27.1	19.4	19.7	31.3	1,729.8	2.9	4.3
1976	2,541.7	617.4	483.6	133.8	28.4	24.2	13.9	89.2	2,415.6	4.3	6.1

Sources: Central Bank of Trinidad and Tobago; Ministry of Finance.

1964-1975P

FIGURE 1 TRINIDAD AND TOBAGO CENTRAL GOVERNMENT EXPENDITURE



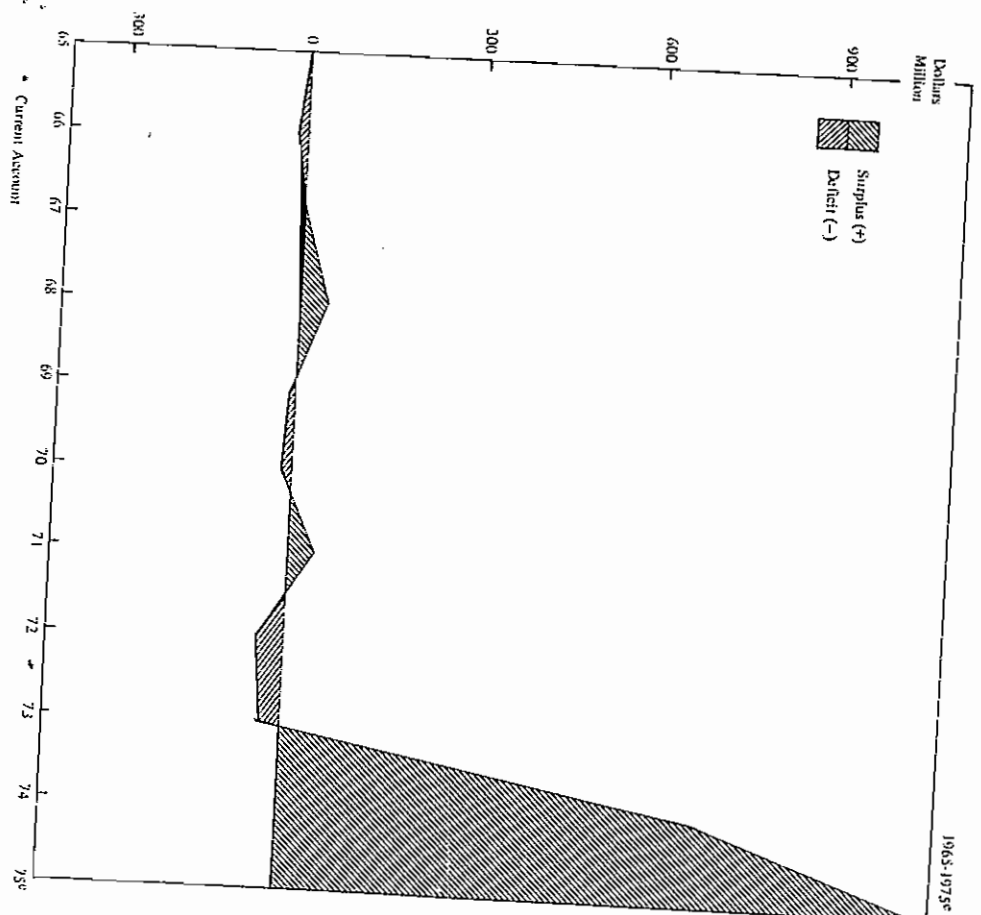
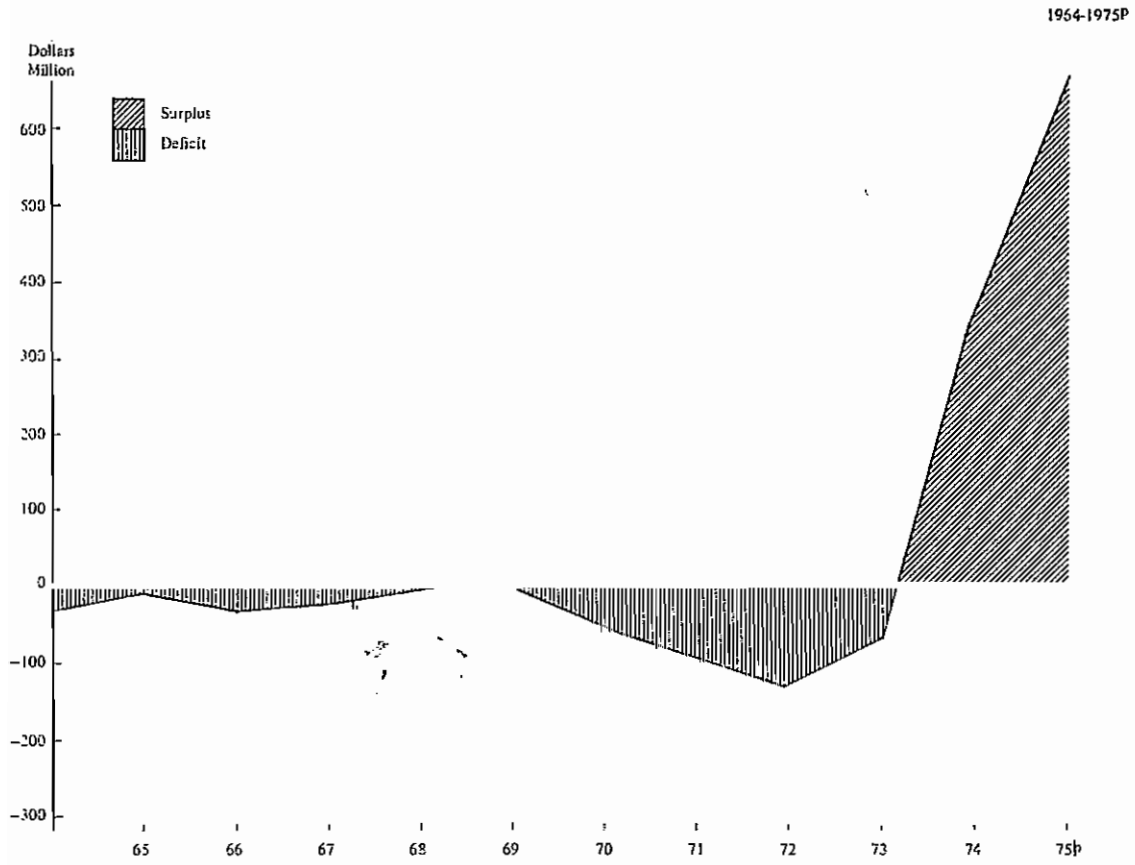
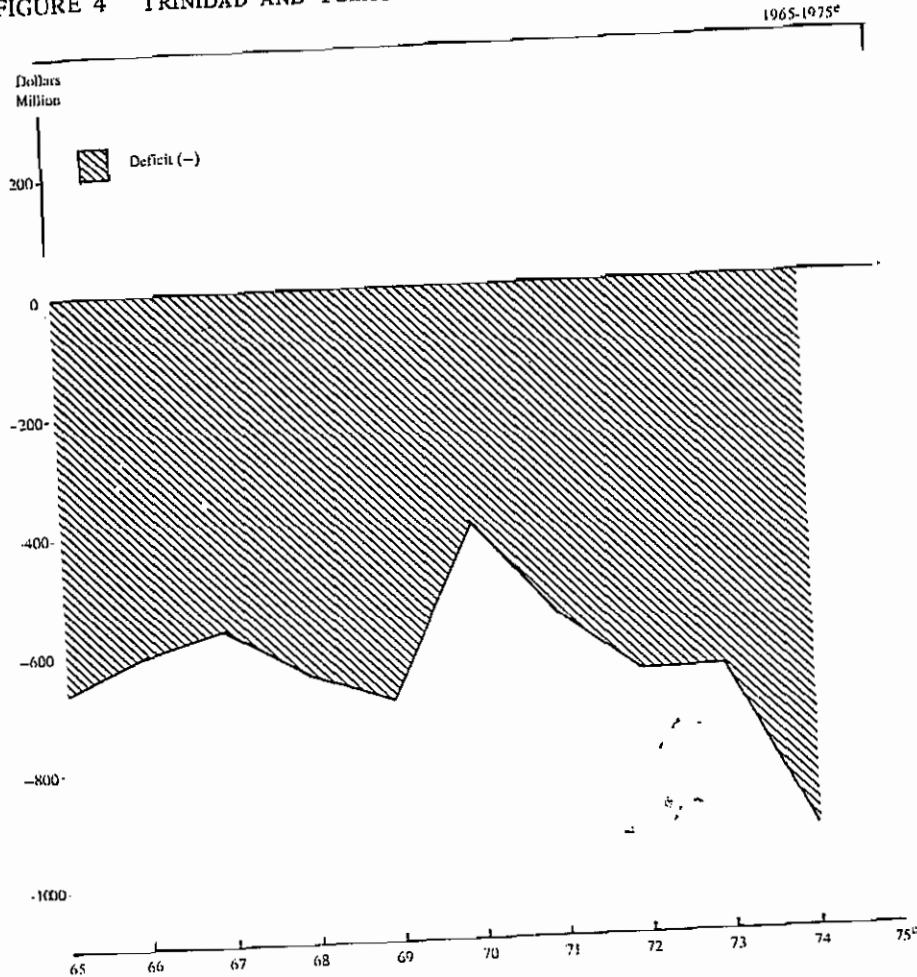


FIGURE 3 TRINIDAD AND TOBAGO BALANCE OF PAYMENTS (A/C)*

FIGURE 4 TRINIDAD AND TOBAGO BALANCE OF TRADE (EXCLUDING OIL)



windfall in oil revenue in 1974 and 1975 to turn the deficit on current account of the balance of payments into a comfortable surplus. The question this paper wishes to explore is whether there is a direct relationship between the public sector deficit and the overall position of the balance of payments in current account. The New Cambridge School suggests that such a relationship does exist and that once the financial operations of the public sector move in deficit, the likelihood is that there will be a corresponding deficit in the current account of the balance of payments. Thus, once the government decides on its overall deficit position in any given fiscal year, one can safely forecast the deficit of the current account of the balance of payments. They hold this view because they argue that the position of the private sectors always show a net surplus in any given financial year.

Because of lack of information one cannot analyse the performance of the private sector in the period 1964-1975. However, as the table on Central Government fiscal operations would show, the public sector did run a continuing deficit in the period 1964 to 1973. And during this period, the balance of payments on current accounts was in deficit on many occasions. For instance, the deficit on current account of the balance of payment⁸ moved from \$7.3m in 1964 to \$16.1m in 1966 and from \$6.4m in 1969 to \$15.6m in 1970 rising to \$45.6m in 1972, then dipping to \$32m in 1973. The position was reversed in 1974 when the public sector deficit was turned into a comfortable surplus of \$362.1m. In that year the balance of payments deficit on current account was sharply reversed to show a surplus of \$694.6m and this trend continued in 1975 when the public sector also showed an increased surplus. Chances are that in 1976 the situation would be the same if the public sector continued to show a surplus.

The evidence points to some loose correlation between the public deficit and borrowing requirements and the balance of payments on current account. Yet it is far too early yet to say that the theory put forward by the New Cambridge School really has made any substantial breakthrough in the field of economic theory and its application. However, evidence in the United Kingdom, Jamaica, Guyana and other open economies suggests that the argument should be taken seriously since all these countries are in similar balance of payments difficulties brought about by their heavy capital programme financed by deficit-financing (i.e. borrowing from both local and foreign market). Moreover, evidence also showed that revaluation of the currencies did not in any way improve the overall position of their balance of payments. As a matter of fact it worsened. Trinidad and Tobago could easily have been in a similar position if it did not have a major foreign-exchange earning sector in the oil industry. The windfall that accrued to the government following the changes in the system of taxation in 1974 saved the day. But the lesson one can learn from this new theory is that more careful management of fiscal operations of the public sector can go a long way towards conserving badly needed foreign exchange earnings.

The New Cambridge School, like the Monetarist, mainly advocates long-term planning based on sound financial policies in the public sector as a possible solution.

TABLE 9 BALANCE OF PAYMENTS SUMMARY

Item	\$ m										
	1965	1966	1967	1968	1969	1970	1971	1972	1973	1974	1975
Merchandise (net)	-106.4	-26.0	29.2	94.3	35.4	-132.6	-320.8	-370.6	-201.5	640.3	818.0
Services (net)	-32.8	-44.6	-52.2	-60.1	-84.0	-22.9	55.3	77.7	148.1	-50.3	-53.6
Required Transfers (net)	21.3	8.2	-2.0	-1.6	-2.1	-4.6	-8.7	-7.4	-17.7	-33.8	-45.9
Capital Movement (excluding reserves)	119.3	52.6	45.4	62.7	132.0	180.3	265.1	212.9	119.4	59.2	440.5
Errors and Omissions	5.9	-6.2	45.4	-49.8	-87.1	-35.8	52.0	41.8	-80.3	79.2	1,080.7
Overall Surplus or Deficit (-)*	-7.3	-16.0	4.1	45.5	-6.4	-15.6	42.9	-45.6	-32.0	694.6	-920.2
Merchandise (net) excluding oil exports +	-670.5	-606.5	-565.5	-644.9	-691.8	-400.8	-533.2	-657.1	-652.7	-920.2	-865.9
Overall Surplus or Deficit (-)†	-556.8	-598.5	-590.6	-693.7	-733.6	-283.8	-189.5	-331.1	-483.2	-865.9	-865.9

Source: C.S.O. Balance of Payments Estimates ¹1956-66; ²1966-72; ³1974

- †† B.O.P. (current account without oil)
- + B.O.T. (Balance of Trade excluding oil)
- * B.O.P. (current account including oil)

Merchandise - this figure reflects the trade balance i.e. exports, minus imports.
 Services - receipts of freight, transportation and travel, also interest received on investments abroad and other expenditures abroad.
 Unrequited Transfers - Remittances to individuals and institutions and Remittances Abroad. Also grants to government and contributions and pensions paid abroad by government.
 Capital Movement - Government and the private sector inflows and outflows of Capital.

CONCLUSION

The examination of the fiscal management of the Trinidad and Tobago economy for the period 1964 to 1975 highlighted a number of important lessons which Lesser Developed Countries (LDCs) can possibly learn in the years to come and the managers of the public sectors in the More Developed Countries (MDCs) can note. The first lesson is the need for far more planning to increase the overall effects of central government fiscal operations in the economy. The policy of deficit-financing to expand economic activities and effect the infra-structural development to transform the economy paid some dividends on the demand side but hardly affected the supply side in spite of the generous fiscal incentives offered to private sector. In addition, the policy seemed to have markedly influenced the expansion of base money in the monetary sector which facilitated the rapid expansion of the money supply was not matched by a corresponding expansion in the supply of goods and services and the demand pressures only served to push up prices of food, houses, land and motor vehicles. Possibly, the managers of the central government fiscal operations can look more closely at the overall financial effects of the fiscal policy to mitigate this adverse influence.

Another lesson that can be learned from this operation is the need to carefully examine the tax-yield of each component of taxes in order to get some prior knowledge of what the likely outturn of the central government fiscal operations on current account would be. The Trinidad and Tobago authorities were able to go ahead with their overall development plans because first, they knew that operations on current account would generate a surplus and secondly, that the spending on current account would be covered by the yield from taxes in any fiscal year. This markedly increased the creditworthiness of the Trinidad and Tobago authorities in the period 1964 to 1975 and assisted the government to finance the development programme by borrowing substantial sums of money on local and foreign markets.

The third lesson to be learnt is the need for meticulous debt-management policy. In the period 1964 to 1975 the Trinidad and Tobago authorities were able to switch a substantial proportion of their debt to local holders and away from foreign agents in order to minimize the drain of badly needed foreign exchange.

Lastly, (though it might be too early to argue this) there could be some loose relationship between overall public sector surplus/deficit and/or borrowing requirements and the balance of payments in current account. In addition, the policy lever of revaluing the currency upwards or downwards does not necessarily mean that the balance of payments would be improved in the long run or the short-term, e.g. Jamaica and Guyana. Careful planning of fiscal operations to control recurrent spending to the size of the normal tax yield and maintain a capital programme more tailored to the surplus generated on current account can possibly go a long way towards maintaining a healthy balance of payments position in the future. And, if the need for borrowing to finance an expansion of the capital programme arises, it might be wise to reduce recurrent spending even further to cover it.

In this way, most of borrowing could possibly be effected locally or very little would have to be borrowed externally.

FOOTNOTES

¹One has to admit that the definition of fiscal policy in this paper is somewhat restricted since it attempts to discuss primarily the financial policies of government *per se*. In effect what is implied as fiscal policy takes into account a policy mix of fiscal and liquidity policy aimed at influencing consumption, employment, income distribution and other goals.

²Reserve money implies bank reserves assets.

³The New Cambridge School seemed to have reversed the assignment rule as suggested by Mundell where fiscal and monetary policy take care of domestic demand management and exchange rate adjustments to the balance of payments. In the new model, changes in (T-G) public sector surplus or deficit determines the balance of payments and exchange rate adjustments determine the level of output in the system. The new school seems to concentrate more on the medium to long-term than short-term policy recommendations.

⁴Calculated by semi-log regression. All growth rate in this paper is calculated by semi-log regression. They do not represent annual changes.

⁵For analytical purposes, government revenue has been re-classified in a way different from the usual budgetary classification.

⁶The term subsistence level refers to the period 1900-1956 of Trinidad and Tobago's economic history. During this colonial period, the economy seems to have just limped along when compared to its rate of growth in the period 1962-1976. If one projects Trinidad and Tobago as a dual economy, i.e. in that a (large) subsistence sector co-existed with a modern sector (oil sector) in the period 1920-1956, then one can possibly see the point of subsistence level.

⁷Number of persons employed by government rose by 20,000 in the period 1970-1975 while in the same period private business increased their numbers employed by 3,000. Source: C.S.O. (Annual Statistical Digest 1974, No. 22).

⁸In 1967 and 1968 the B.O.P. (current account) moved into surplus. These were the years of the first Arab/Israeli war.