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Trinidad and Tobago: 2005 Article IV Consultation—Staff Report; Public Information Notice on the Executive Board Discussion; and Statement by the Executive Director for Trinidad and Tobago

Under Article IV of the IMF's Articles of Agreement, the IMF holds bilateral discussions with members, usually every year. In the context of the 2005 Article IV consultation with Trinidad and Tobago, the following documents have been released and are included in this package:

- the staff report for the 2005 Article IV consultation, prepared by a staff team of the IMF, following discussions that ended on September 30, 2005, with the officials of Trinidad and Tobago on economic developments and policies. Based on information available at the time of these discussions, the staff report was completed on October 27, 2005. The views expressed in the staff report are those of the staff team and do not necessarily reflect the views of the Executive Board of the IMF.

- a Public Information Notice (PIN) summarizing the views of the Executive Board as expressed during its November 11, 2005 discussion of the staff report that concluded the Article IV consultation.

- a statement by the Executive Director for Trinidad and Tobago.

The documents listed below have been or will be separately released.

Statistical Appendix
Financial System Stability Assessment

The policy of publication of staff reports and other documents allows for the deletion of market-sensitive information.

To assist the IMF in evaluating the publication policy, reader comments are invited and may be sent by e-mail to publicationpolicy@imf.org.

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INTERNATIONAL MONETARY FUND

TRINIDAD AND TOBAGO

Staff Report for the 2005 Article IV Consultation

Prepared by the Staff Representatives for the 2005 Consultation with Trinidad and Tobago

Approved by Caroline Atkinson and G. Russell Kincaid

October 27, 2005

In a regional context, Trinidad and Tobago is an energy-rich economy with one of the higher income levels in the Caribbean but only average social indicators. It has a complex financial system, with well-developed banking, insurance and investment firms, enabling it to serve as a regional financial center and source of capital for Caribbean entities, including sovereigns.

Recent developments: Macroeconomic developments are being driven by a highly favorable external environment. Surging oil prices have strengthened the external current account balance, fueled the expansion of domestic absorption and contributed to high levels of liquidity in the financial system. The government's nonenergy deficit has expanded and there has been a recent up tick in inflation.

Fund relations: Trinidad and Tobago has accepted the obligations of Article VIII, Sections 2, 3, and 4. It maintains an exchange system free of restrictions on the making of payments and transfers for current international transactions. The Executive Board meeting concluding the 2004 Article IV consultations was held on October 22, 2004. A Financial Stability Assessment was carried out in 2005 and its findings are scheduled to be discussed by the Board together with this Staff Report.

Discussions: A staff team comprising Sanjaya Panth (head), Goohoon Kwon, Irineu de Carvalho, Rafael Romeu, and Wendell Samuel (all WHD) held discussions for the 2005 Article IV consultations in Port-of-Spain during July 14–26, 2005. The mission met with Hon. Conrad Enill, Minister in the Ministry of Finance; Governor Ewart Williams of the Central Bank of Trinidad and Tobago; other senior government officials; representatives of the private sector and labor unions; and the opposition party. Mr. Charles de Silva (OED) and Mr. Das (MFD), who led the 2005 FSAP missions to Trinidad and Tobago, joined the team for the final discussions.

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EXECUTIVE SUMMARY

Trinidad and Tobago is a small energy-rich Caribbean economy. The oil and gas sector, including downstream activities, currently accounts for about 40 percent of GDP, over 80 percent of exports, and approximately half of government revenues. However, its contribution to employment is less than 5 percent. Within the Caribbean, Trinidad and Tobago has become a major financial center and a source of capital for regional entities, including sovereigns.

The political balance is delicate. In recent years, political affiliation has largely split along ethnic lines. The current government, formed by the People's National Movement party, took office in early 2003 after three successive elections in as many years. The next elections are not due until 2007 but may be called earlier—the political environment is already charged in anticipation.

Macroeconomic performance and financial developments are being driven by a highly favorable external environment. Surging oil prices have strengthened the external current account balance, financed an expansion of aggregate demand, and contributed to high levels of liquidity in the financial system. The labor market has tightened significantly, and there are tentative signs that the economy is producing at, or near, capacity. Inflationary pressures have emerged—annual headline inflation stood at 7 percent in September, up from 2¾ percent a year and a half ago.

The nonenergy fiscal deficit has widened substantially, adding to demand pressures in the short-run and heightening exposure to long term vulnerabilities. Following an already expansionary stance in FY 2004/05, the budget for FY 2005/06 envisages a significant further widening of the nonenergy deficit (the overall deficit less energy revenues). This is due to a combination of lower nonenergy revenues (from reduced tax rates and increased allowances) as well as increases in non-interest expenditures. However, large overall surpluses are expected to continue on account of high energy prices. Staff advice focused on the benefits of saving a larger portion of the current high energy revenues and strengthening expenditure administration.

The strong external inflows and widening nonenergy fiscal deficits pose several challenges for monetary and exchange rate policy. In the short run, the priority remains to address the liquidity in the system stemming from the rising nonenergy deficit. In the long run, if oil prices remain at high levels, a real appreciation appears inevitable in the absence of sufficient fiscal tightening. In this context, the mission recommended moving toward greater nominal exchange rate flexibility.

The authorities' structural reform agenda is currently focused on tax and financial sector reform. The reform of nonenergy taxes aims to increase efficiency and predictability. Financial sector reforms, consistent with the FSAP recommendations, seek to strengthen supervision and consolidate Trinidad and Tobago's role as a regional financial center.

I. Introduction

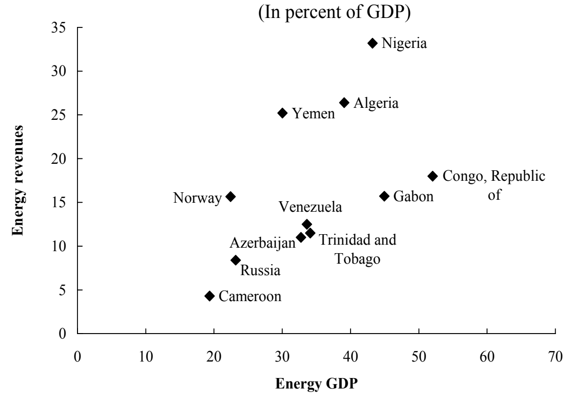
1. **Trinidad and Tobago is a small energy-rich Caribbean economy**. The oil and gas sector, including downstream activities, currently accounts for about 40 percent of GDP, over 80 percent of exports, and approximately half of government revenues. However, its contribution to employment is less than 5 percent. Within the Caribbean, Trinidad and Tobago has become a major financial center and a source of capital for regional entities, including sovereigns. Trinidad and Tobago is one of the larger Caribbean nations in terms of GDP and population. Its energy wealth has enabled it to achieve one of the higher standards of living in the region. Nevertheless, income inequality and poverty rates are only at about regional averages, and social and ethnic tensions remain high.

Trinidad and Tobago and the Caribbean: Selected Indicators

	GDP (billions of US$)	Population (million)	GDP per capita (thousands of US$)	Income Inequality (GINI index)	HDI 1/ (Ranking)	Illiteracy (Percent)	Life Expectancy (Years)	Poverty (Percent)
		(2003)		(Most Recent)	(2005)	(2001)	(2000–05)	(Most Recent)
Caribbean 2/	51.8	23.6	5.4	0.38	78	10	69	28
Highest 3/	16.5	8.8	16.7	0.65	30	49	77	66
Lowest 3/	0.3	0.04	0.5	0.10	153	1	50	12
Trinidad and Tobago	10.5	1.3	7.8	0.40	57	2	71	21

Sources: IMF and World Bank estimates.
1/ Human development index.
2/ Averages for Caribbean except GDP and population, which are totals.
3/ Highest and lowest for each category.

Energy in the Economy, 2004 1/
(In percent of GDP)



Source: Fund staff estimates.
1/ For countries other than Trinidad and Tobago, estimated based on earlier years and 2004 oil prices.

2. **The political balance is delicate**. In recent years, political affiliation has largely split along ethnic lines. The current government, formed by the People's National Movement party, took office in early 2003 after three successive elections in as many years. The government does not have the qualified parliamentary majority required for many important decisions, significantly complicating the task of policy-making. The next elections are not due until 2007 but may be called earlier—the political environment is already charged in anticipation.

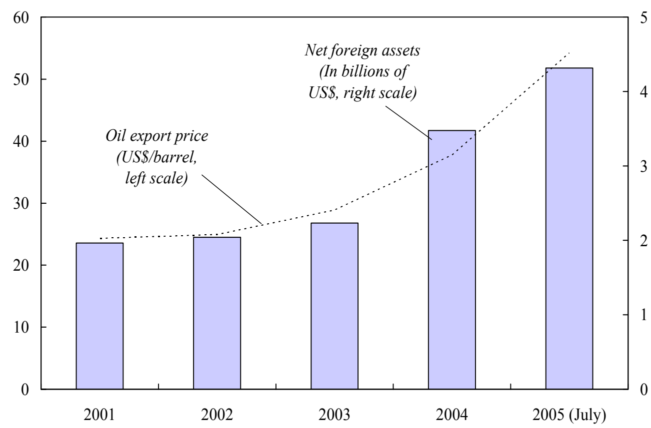
3. **Earlier Article IV consultations have emphasized fiscal and financial sector issues, which the authorities are addressing in large part**. In fiscal areas, the authorities are proceeding with tax reform and establishing a permanent oil fund. There has, however, been little progress in reforming fiscal management policies and practices. As regards the financial sector, the authorities are implementing their ongoing reform program embodied in the 2004 White Paper. With Fund and Bank assistance, and in conjunction with the current annual consultations, an assessment of the financial sector was also carried out during 2005.

II. Recent Economic Developments

4. **Macroeconomic performance and financial developments are being driven by a highly favorable external environment**. Surging oil prices have strengthened the external current account balance, fueled the expansion of domestic absorption, and contributed to high levels of liquidity in the financial system. There are tentative signs that the economy is producing at, or near, capacity and inflationary pressures are emerging.

5. **The balance of payments is in large surplus**. Exports rose by US$1.2 billion (10 percent of GDP) in 2004, significantly outpacing import growth and lifting the current account surplus to 14½ percent of GDP from 9 percent of GDP in 2003. While some of the higher current account receipts were offset by private capital outflows, the overall balance of payments surplus still doubled to US$0.7 billion (6 percent of GDP). With oil prices rising further, these trends are accelerating in 2005—the foreign assets of both the commercial banks and the central bank have continued to rise rapidly this year.

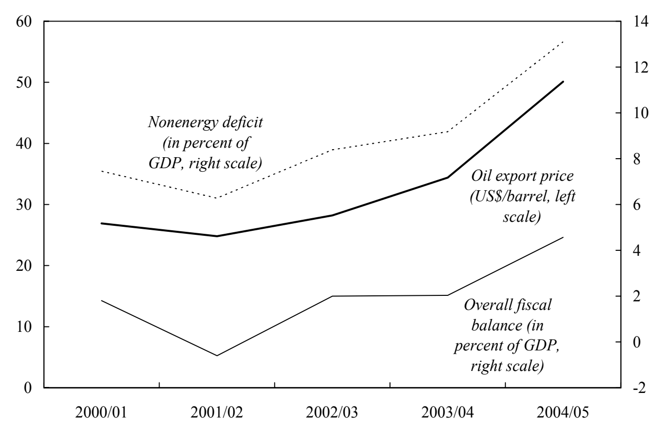
Oil Price and Foreign Assets 1/



Sources: Trinidad and Tobago authorities; and Fund staff estimates.
1/ Banking system.

6. **In recent years, the nonenergy fiscal deficit has widened substantially due to higher expenditures, although the overall balance remains in surplus**. An already expansionary budget for FY 2004/05 was supplemented by a mid-year amendment that implied a deterioration of the central government's nonenergy deficit (the overall deficit, excluding energy revenues) by 4½ percent of GDP in a single year.[1] While budgetary execution was initially running behind schedule, the authorities' preliminary estimates indicate a sharp pick-up in spending

Oil Price and Fiscal Balances



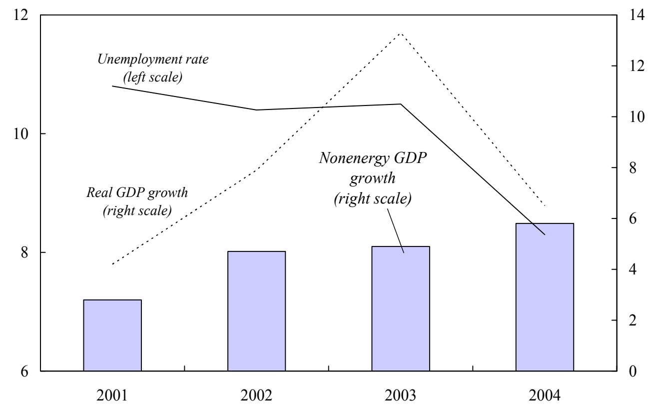
Sources: Trinidad and Tobago authorities; and Fund staff estimates.

[1] The definition used by staff of energy revenues includes, in addition to direct revenues from extraction, also receipts from downstream energy enterprises.

during the last few months of the fiscal year that ended in September 2005. Nevertheless, as the increase in energy revenues outpaced the expansion of the nonenergy deficit, the overall surplus is estimated to have increased in FY 2004/05, to about 3¼ percent of GDP from 2 percent the previous year.

7. **The economy is growing robustly on the back of the strong balance of payments and the expansionary fiscal stance**. Real GDP grew by 6½ percent during 2004. While this is lower than the outturn of 13 percent growth during 2003, the latter was driven primarily by the coming on stream of some large energy projects. The nonenergy sector has remained vigorous, growing by just under 6 percent on the back of a surge in government spending financed by the oil bonanza. The latter has also led to a boom in construction. The unemployment rate fell to single digits and ended 2004 at 7¾ percent, the lowest in about four decades.

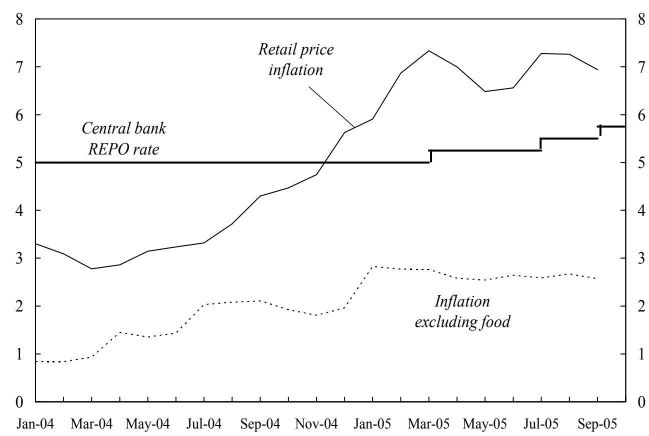
Real GDP Growth and Unemployment
(In percent)



Sources: Trinidad and Tobago authorities; and Fund staff estimates.

8. **Monetary conditions have largely been accommodative, although signs of accelerating inflation have led to a recent shift toward tightening**. The monetization of energy receipts by the government to finance the nonenergy deficit is the major source of liquidity injection into the financial system. The monetary impact of these injections was amplified in 2004 by changes in commercial banks' reserve requirements.[2] As a result, monetary conditions were easy throughout 2004 and early this year. This ample liquidity, coupled with the structural segmentation of the foreign exchange market, has helped soften pressures for an appreciation of the currency—at end-September, the exchange rate stood at TT$6.25 per U.S. dollar, little changed from the average level of about TT$6.30 per U.S. dollar that has prevailed for the past several years. Signs of inflation pressures have, however, recently emerged—headline inflation has crept up to 7 percent for the 12-month period ending in September 2005, up from 2¾ percent a year and a half ago. In response, the Central Bank of Trinidad and Tobago (CBTT) has raised the benchmark repo

Inflation and Interest Rate
(In percent)



Sources: Trinidad and Tobago authorities; and Fund staff estimates.

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[2] Commercial banks' reserve requirements are being reduced gradually to level the playing field between them and other financial institutions. Thus far, the rates have been reduced twice since late 2003. In both cases, the central bank mopped up the direct portion of the liquidity impact through open market operations.

rate on three occasions this year, each time by 25 basis points. However, following the successive rounds of tightening in the United States, the differential vis-à-vis U.S. interest rates remains narrower than at the start of the year and the real interest rate is negative.

9. **Consumers are being shielded from rising international oil prices**. Electricity, water and petroleum products, whose prices are administratively fixed, account for nearly 10 percent of the retail price index basket. There have been no substantive increases in administrative prices for petroleum products since 2003, leaving local gasoline prices currently at about two-thirds of the level in neighboring Caribbean countries. Electricity prices have also been unchanged for several years. Direct budgetary subsidies for petroleum products and electricity amounted to nearly 2 percent of GDP during FY 2004/05.

10. **Financial markets have generally been buoyant in reflection of the ample liquidity, and credit ratings are up**. Insurance, pension funds, finance companies, and mutual funds—belonging to a few regionally active conglomerates—have all experienced rapid asset accumulation, with mutual fund investments reaching roughly two-thirds of bank assets and stock market capitalization approaching 140 percent of GDP in 2004. The financial system as a whole increased credit to the private sector by 18 percent in 2004, a leap compared with single-digit annual growth since 2001. The banking soundness indicators generally improved in 2004, as the capital adequacy ratio increased to 22.7 percent and return on assets reached 3.7 percent. The overall stock market index climbed by 55 percent during 2004 and by a further 15 percent through May 2005 before falling back to the end-2004 level. In August 2005, Standard and Poor's raised the sovereign foreign currency debt rating to A-, providing a boost also to the credit worthiness of local companies.

11. **The budget for FY 2005/06 submitted to parliament on September 28, 2005 envisages a significant further expansion of the nonenergy deficit, to be financed by higher energy revenues**. The authorities reoriented the tax system to generate greater collections from the energy sector while sharply reducing income tax rates and expanding allowances for the nonenergy sector. As a result, several hundred thousand taxpayers have been removed from the tax net. The authorities also introduced numerous other changes to both direct and indirect taxes. Altogether, nonenergy revenue receipts are expected to decline by some 3¾ percent of GDP during FY 2005/06. At the same time, expenditures are budgeted to increase by a further 2 percentage points of GDP, relative to the estimated outturn for FY 2004/05, including on account of a number of one-off items. Cumulatively, this implies a doubling of the central government's nonenergy deficit over two years—from 9¼ percent of GDP in FY2003/04 to 18¼ percent of GDP now projected for FY 2005/06. Just over half of this deterioration, or 5¼ percentage points of GDP, is on account of higher non-interest expenditures, mostly under the "current" heading (Tables 1 and 2). A large overall surplus is nevertheless still projected for FY 2005/06 on account of increased energy revenues.

III. Outlook for 2005–06 and the Medium Term

12. **In the short run, Trinidad and Tobago's outlook remains favorable, owing to high oil prices and expanding energy production**. In the baseline scenario, overall real GDP growth is expected to pick up modestly, to 6¾ percent in 2005, and accelerate to over 10 percent in 2006 before stabilizing at around 3 percent over the medium term. The spike is

mostly due to the expected coming-on-stream in late 2005 of a new liquefied natural gas (LNG) facility. As regards the nonenergy sector, despite some moderation, growth is projected to be higher during 2005–06 than the recent average. Buoyant demand from the expanding government sector should, in particular, provide a further boost to overall activity, offsetting some weakening of agriculture. Emerging capacity constraints imply, nevertheless, that some of this demand will inevitably manifest itself in higher prices. Core inflation is, therefore, projected to pick up further in 2005–06. The impact on headline inflation of the expansionary fiscal stance should, however, be less pronounced, if food prices, responsible for most of the recent increase in overall inflation, stabilize as expected. All in all, consumer price inflation for 2006 is projected at 8 percent, up sharply from the range of 3–4 percent during 2001–03, prior to the oil-price induced boom.

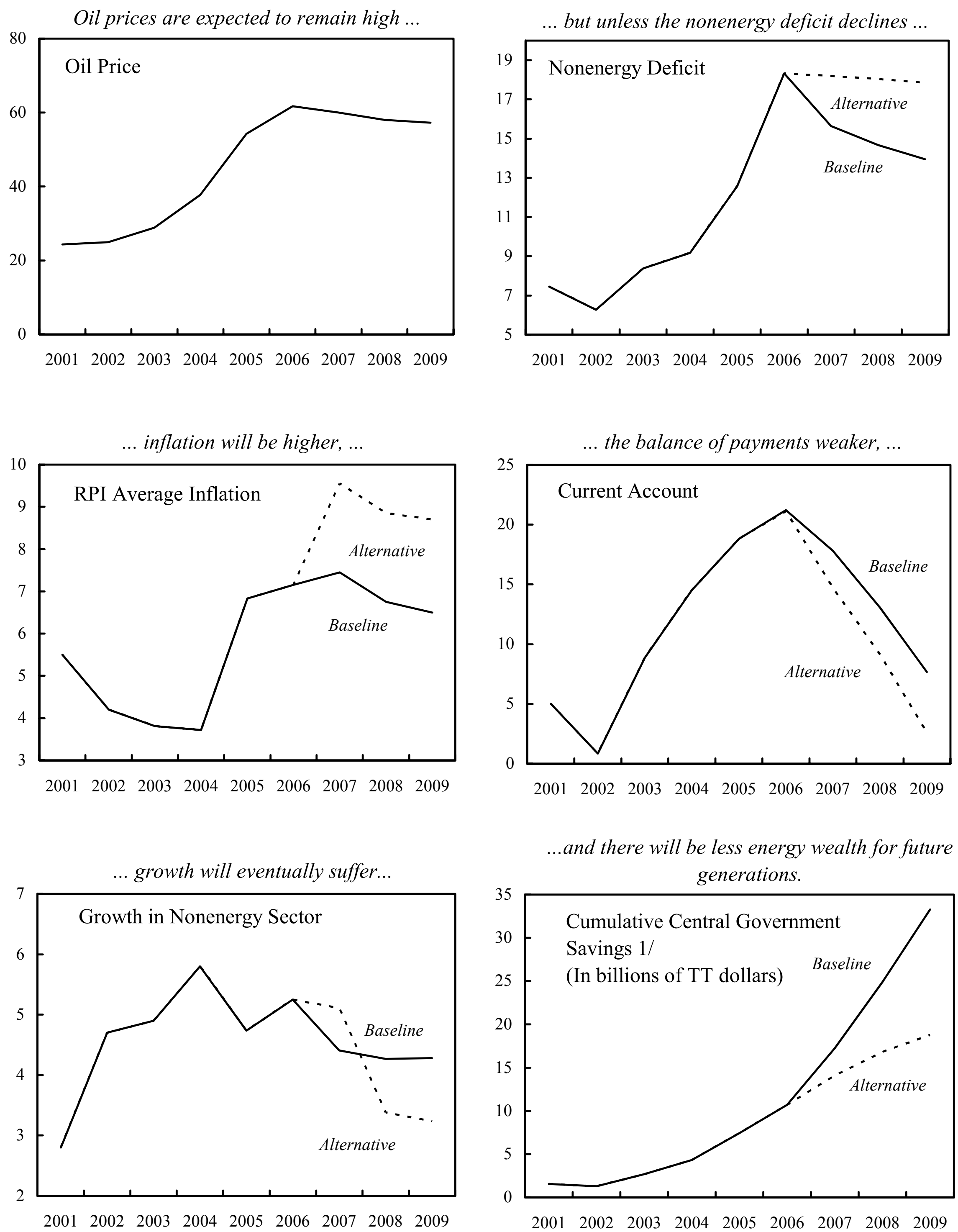
13. **Current staff baseline projections envisage high energy receipts and robust growth also into the medium term**. Under currently projected extraction rates for natural resources and expected WEO oil prices, the current account surplus will remain very large, albeit on a declining trend over the medium term. Annual growth of the nonenergy sector is projected to stabilize at about 4–4½ percent over the medium term, broadly in line with the average outturn during 2001–04. Overall GDP growth would be slightly lower as growth in the energy sector decelerates after the completion of the LNG plant. The nonenergy deficit should gradually improve beyond FY 2005/06 if, as the authorities currently envisage, one-off items from this year's budget are not replaced and the nonenergy tax base is expanded and compliance improved (see paragraph 31). This would then enable inflation to gradually trend downwards, albeit remaining above that of recent years throughout the medium term.

14. **The macroeconomic environment is likely to be less benign if large nonenergy deficits persist**. An illustrative scenario considers the impact of overall expenditures remaining broadly at budgeted FY 2005/06 levels in relation to GDP (implying an increase in non-interest expenditures as interest costs are forecast to decline with continuing overall fiscal surpluses) (Table 7 and Figure 1). In this scenario, the fiscal stance would aggravate pressures for a real exchange rate appreciation (Box 1). While in the short run, output could be somewhat higher than under the baseline, the demand pressures could lead to entrenched high inflation, crowd out the private sector, and ultimately have a detrimental impact on growth prospects over the longer term. The build-up of windfall savings would be less than in the baseline, also implying, with unchanged energy reserves between the two scenarios, that there would be less wealth from energy resources available for the future.

IV. Report on the Discussions

15. **The discussions focused on the policy implications of sustained high oil prices**. In the current environment, the specific challenges relate to: (i) striking an appropriate balance on the use of energy resources between the short-run and the longer term; (ii) managing aggregate demand to avoid overheating the economy in the short run; and (iii) pursuing policies to avoid Dutch disease and create an environment for sustainable private sector-led growth over the long term.

Figure 1. Trinidad and Tobago: Alternative Medium-Term Macroeconomic Outlook



Source: Fund staff estimates.

1/ Cumulative central government overall balance.

Box 1. Oil Prices and the Real Exchange Rate

A permanent increase in oil prices could exert significant upward pressures on the long-term real exchange rate of the Trinidad and Tobago dollar. The precise magnitudes remain very uncertain; depending, inter alia, on the response of private capital flows and other Trinidad and Tobago-specific parameters, including relative preferences between imports and domestically produced goods. However, two simple conceptual frameworks, using parameters obtained from cross-country studies, are suggestive of sizeable pressures emerging.

The first approach draws on the outcome of an extensive study undertaken by the Fund's Research Department.[1] The cross-country study has identified four variables (net foreign assets, relative per capita income, relative manufacturing output, and commodity prices) as core factors behind the movements of the real exchange rates of 39 countries between 1980 and 2003. According to the long-term relationship identified by the study, an improvement in the terms of trade by 10 percent raises the equilibrium real exchange rate by about 5 percent, after controlling for the effects of other variables. Relative to mid-2004, current WEO projections imply an improvement in Trinidad and Tobago's terms of trade by nearly 30 percent over the medium term.

The second approach considers the extent of real exchange rate realignment required to offset current account imbalances caused by a large swing in the terms of trade.[2] Standard assumptions about capacity constraints, labor mobility and income elasticity of consumption imply that for every 1 percent increase in permanent income, consumption of traded goods would need to rise by about 2 percent in Trinidad and Tobago in order to balance supply and demand in goods and labor markets. Depending on the elasticity of substitution between traded and nontraded goods, the adjustment in relative prices necessary to bring about such an adjustment may be of a broadly similar magnitude. A simple calibration suggests that the long-term purchasing power of the population of Trinidad and Tobago may have risen by some 10 percent due to the recent rise in trend oil prices, implying that if high oil prices persist, the real exchange rate may need to move by as much as 20 percent over the medium term.

1/ Equilibrium Real Exchange Rates: Estimates for Industrial Countries and Emerging Markets (mimeo, June 2005).

2/ Obstfeld, Maurice and Kenneth Rogoff, "Perspectives on OECD Capital Market Integration: Implications for U.S. Current Account Adjustment," in Federal Reserve Bank of Kansas City, *Global Economic Integration: Opportunities and Challenges*, March 2000, pp.169–208.

A. Fiscal Policy and the Management of Energy Wealth

16. **The government has a long-term development program to use energy resources to bring the country to "developed-economy status" by 2020**. This requires investments in human and physical capital to create room for the nonenergy economy to grow, which in turn should eventually reduce the budget's dependence on the energy sector. The authorities see the 2005/06 budget as part of this long-term strategy—it gives priority to the issues of security and safety, education, health care, and housing and poverty reduction. Accordingly, the expenditures growing most are transfers and subsidies to households, which include the costs of the free tertiary education that is now being made available to all. Until the recent oil boom, central government primary expenditures in Trinidad and Tobago have remained below that of the rest of the Caribbean in relation to GDP but the FY 2005/06 budget would bring them up to about the regional average. Notably, however, Trinidad and Tobago also undertakes a significant amount of expenditures, in particular capital expenditures, through off-budget entities.

17. **While recognizing the need to invest in the economy, the mission cautioned the authorities about the risks posed by the scale and scope of the fiscal expansion**. A nonenergy deficit of the size projected in the FY 2005/06 budget raised questions about long-term sustainability (Box 2). More immediately, it risked further exacerbating inflationary pressures, added to concerns about the impact on the real economy of a real exchange rate appreciation, and complicated the task of monetary management. Furthermore, weak institutions could limit the potential to undertake expenditures effectively—for example, Trinidad and Tobago's score in Transparency International's Corruption Perception Index has recently deteriorated. As regards the tax cuts, while they helped distribute the energy wealth to the population, Fund technical assistance missions had strongly emphasized the need to phase in rate reductions only very gradually, especially given that data unavailability had precluded assessments of their likely revenue impacts.

18. **The mission suggested that Trinidad and Tobago could benefit in several ways from saving a larger portion of the current high energy receipts**. The finite nature of energy resources suggested that a smaller and steady improvement of the nonenergy balance now was preferable to any sudden and very large adjustment down the line, as distant as that prospect may currently appear to be. Saving more of the energy wealth could also be beneficial from a growth perspective—the increased demand for nontradables coming from the fiscal expansion would, in the context of capacity constraints, adversely impact competitiveness. Furthermore, cross-country studies, including those focusing on the Caribbean, consistently suggested that decreasing the "government burden" on the economy (typically measured by government consumption in relation to GDP) could boost economic growth.[3]

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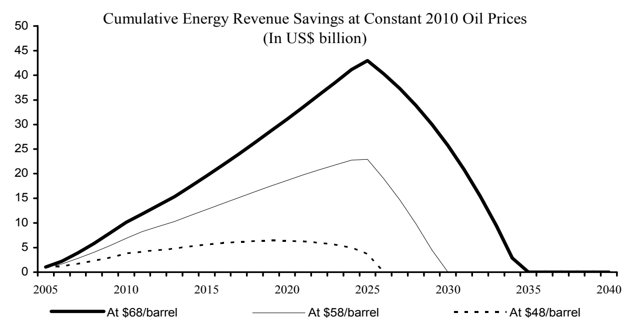
[3] See for example: World Bank, 2005, *Time to Choose: Caribbean Development in the 21st Century*.

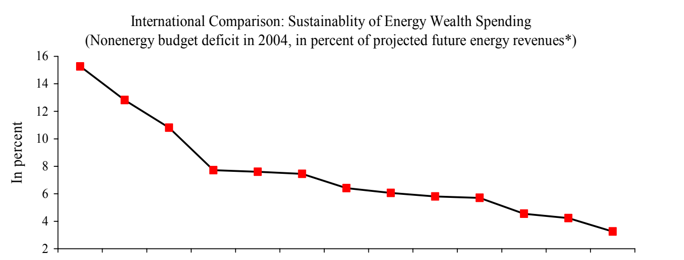
Box 2. Long-Term Sustainability

For countries using exhaustible resources to finance expenditures, a natural question that arises is "how long is the existing fiscal position tenable?" The answer depends crucially on the size of natural resources in the ground, prices that these resources can be expected to command over the long term, and the extent to which expenditures contribute to expanding the nonenergy economy, and thereby, the nonenergy revenue base, over the long term. The first two factors are subject to frequent and sizeable revisions in both directions and the latter is not always clearly measurable.

Nevertheless, a simple saving-dissaving model can provide useful insights into the question. The model considers when accumulated savings from fiscal surpluses would run out for a given nonenergy deficit in relation to nonenergy GDP (which is assumed to grow at a fixed rate). Such an analysis for Trinidad and Tobago suggests that the current fiscal stance is not consistent with long-term sustainability as defined in this model. Specifically, if the nonenergy deficit remained as in the staff's baseline medium-term scenario, accumulated savings would run out by 2030 (see chart below). This is under assumptions of oil prices as in the WEO through 2009 and constant at US$58 per barrel in real terms thereafter and taking into account the recent changes to the energy tax regime, which has significantly increased the government's share of energy wealth. A US$10 increase in oil prices over and above the baseline would extend the year of depletion to about 2035. Conversely, a US$10 decrease, relative to the baseline, would bring the date considerably forward. All three scenarios are based on optimistic assumptions that all currently estimated reserves (proven, possible and probable) are fully extracted, that the average real rate of return on savings is 3½ percent, and that the expected yield from energy revenue assumed in the FY 2005/06 budget is sustained. Looked at in a slightly different way, under these same optimistic assumptions, a nonenergy deficit of no more than about 13½ percent of current GDP can be financed indefinitely from the energy wealth compared to the currently projected nonenergy deficit of 18¼ percent of GDP for FY 2005/06.



How does the sustainability of the fiscal position of Trinidad and Tobago compare to other energy-rich economies? In 2004, Trinidad and Tobago's use of energy resources to finance the deficit was not far out of line with other similarly resource-rich countries (see chart below). In the absence of any changes in the other countries, the recent increase in Trinidad and Tobago's nonenergy deficit would, however, place it among the more intensive users of its natural resources.



Source: Various country reports of the Fund; BP statistical review of world energy 2004; and Fund staff estimates.
*Assuming a long-term real oil price of US$50/barrel, a 12 percent discount rate, and no changes in reserves and energy tax regimes.

19. **Reducing vulnerabilities also argued for larger fiscal savings**. There remained, in particular, a risk that energy export earnings may decrease substantially—oil price volatility has been very high in the past. Expenditures, on the other hand, were very difficult to rein in once increased. In this regard, the large spending programs and the dramatic widening of the nonenergy deficit exposed Trinidad and Tobago very much to the risks of sudden falls in energy prices. In this connection, the mission wondered, for example, about the continued rationale for large and expanding public employment programs in the midst of a tight labor market.

20. **The authorities noted the need to use the energy revenues more expeditiously to put in place the necessary infrastructure for growth**. They indicated that public investments, including in the areas of health and education, were vital to increasing productivity in the nonenergy sector. The budget execution system was, however, antiquated, having inherited a variety of institutional drawbacks, including impediments to attracting and retaining qualified staff, and overly rigid rules for evaluation, tender, and procurement. They noted that in an effort to ease these severe bottlenecks in expenditure administration, agencies outside the central government apparatus were being set up to manage government infrastructure initiatives. These agencies, 15 of which were identified in the budget statement for FY 2005/06, would take on some of the design, procurement and management functions that had hitherto been carried out by government ministries but would outsource the actual execution and operation of specific projects.

21. **The mission suggested that it may be more useful to reform and restructure the existing government apparatus than to set up new entities**. It would also be important to ensure that the entities that are set up conduct their operations with full transparency and accountability. In this regard, a fiscal Report on Observance of Standards and Codes (ROSC) could, in addition to documenting the strengths and weaknesses of expenditure administration, also suggest useful ways to strengthen budgetary management processes and ensure adequate accountability. The authorities confirmed their interest, in principle, in preparing a ROSC in due course.

22. **Some increase in expenditures notwithstanding, the authorities also reiterated their intent to maintain fiscal prudence by continuing to save a large portion of the energy windfall**. They pointed to larger amounts having been put aside in the interim revenue stabilization fund than had been budgeted for in FY 2004/05. They also emphasized the lessons from the late 1970s when a financial crisis had followed an oil bonanza. In this regard, they stressed the progress that was being made this time around toward establishing a permanent fund to manage long-term savings from energy revenues. They saw this fund, the Heritage and Stabilization Fund (HSF), serving three main purposes: (i) helping sustain public expenditure during cyclical downturns in oil prices; (ii) providing for savings to draw on following the eventual depletion of energy reserves; and, (iii) undertaking strategic and tactical investments for the diversification and transformation of the economy. Sixty percent of energy revenues arising from above a reference oil price would be deposited into the HSF's Financial Investment Portfolio (FIP) and the remainder into its Strategic Investment Portfolio (SIP). The FIP would be tapped when oil prices fell below a threshold whereas expenditures from the SIP would operate independently of the oil price.

23. **The mission welcomed the steps being taken toward establishing the HSF and suggested its strengthening in a number of respects**. Ideally, the fund should receive all energy revenues and finance the nonenergy deficit. The calculation of the medium-term reference oil price that would trigger deposits into the fund also warranted clarification. Finally, expenditures should not be undertaken directly from the fund—such investments are best handled through the budget's public sector investment program rather than through a separate mechanism that shields some expenditures from the normal competitive parliamentary budgetary process. Also, as the returns on domestic investments are likely to be highly correlated with domestic economic growth, and hence revenues, such investments would risk exposing both the budget and the accumulated savings to the same vulnerabilities.

24. **The authorities explained that there were both constraints and objectives impacting on the chosen features of the HSF**. There were constitutional limitations to all energy-related revenues first going directly into the fund. As regards the motivation for the SIP, the authorities underscored the need to safeguard the funding of strategic investments from the year-to-year vicissitudes in international energy prices and noted that opportunities for such investments might unexpectedly turn up in the midst of a budget year. They emphasized that the investments would ultimately still be subject to parliamentary oversight even if outside of the normal budgetary process. As regards the threshold oil prices, they indicated that a clear exposition of the mechanism for their calculation, including the reference world market prices, would be included in the final legislation.

B. Monetary and Exchange Rate Policies

25. **The challenges for monetary and exchange rate policy are also framed by the expected continued strength of the balance of payments position**. The discussions focused on the central bank's objectives and operational instruments for managing the liquidity arising from the expansionary fiscal position; and how to address the inevitable pressures for a real appreciation coming from the large terms of trade improvement.

26. **The authorities stated that the central bank's key objective has been internal and external price stability**. Liquidity is viewed by the authorities as an intermediate target and the Central Bank's repo rate is used to signal the direction of monetary policy. With the transmission mechanism operating through interest rates, open market operations should, in principle, be undertaken to vary the quantity of liquidity only at the margin. In practice, the CBTT carries out large volumes of open market operations and effectively also determines the nominal exchange rate, which has remained virtually unchanged vis-à-vis the U.S. dollar since 1999.[4] Notwithstanding the stability of the exchange rate, the mission acknowledged that there was some scope for monetary policy affecting liquidity owing to the variable interest rate margin (see paragraph 8) and a home-currency bias.

27. **The mission noted the signs of emerging capacity constraints, including the step increase in nonfood inflation and the tight labor market (Box 3)**. The authorities considered recent price developments as less indicative of emerging inflationary pressures

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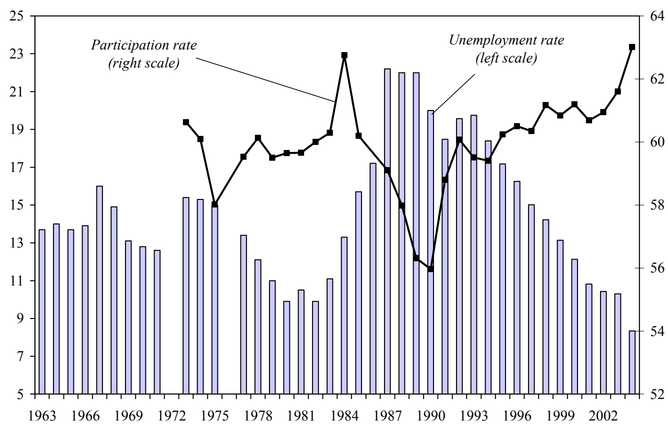
[4] The exchange rate is classified by the Fund as a de facto peg.

Box 3. Labor Market Developments

Unemployment has recently fallen to an all-time low and labor participation rates are at historical highs. The official unemployment rate, which uses a wide definition to include discouraged workers, has steadily declined from its peak in the late 1980s of 22 percent to an average of 8.3 percent in 2004. The labor participation rate, which was as low as 56 percent in 1990, is now at a historical high of 63 percent. The latter is mostly due to the sharp increase in the participation rate for women.

Unemployment and Labor Participation Rates



Source: Trinidad and Tobago authorities.

The current economic boom has led to increased demand for labor across most industries and all skill levels, although financially the educated appear to have benefited disproportionately. Unemployment rates have fallen for both sexes and all age groups. The unemployment rate for those with some tertiary education was always low but the rates for those with lower education has also recently fallen. In terms of industries, employment has increased in all sectors except agriculture. The declining agricultural employment is due, in large part, to the closure of the state-owned sugar company Caroni in 2003, which led to the separation of 9,000 employees or 1½ percent of the current labor force. Available data on income suggest that the labor market remains particularly tight for skilled categories—average monthly income for agricultural and elementary workers has not kept pace with inflation.

Employment and Wages

	2001	2002	2003	2004	Percent Change 2001–04
Unemployment rates (in percent)					
Both sexes	10.8	10.4	10.3	8.3	-2.5
Males	8.6	7.8	8.3	6.4	-2.2
Females	14.4	14.5	13.8	11.2	-3.2
Primary education	10.7	10.9	11.7	8.5	-2.2
Secondary education	12.0	11.3	10.9	9.1	-2.9
Some college	2.3	2.4	2.9	2.3	0.0
Employment by industry (in thousands)					
Total	514	525	535	562	9.4
Oil and gas	15	17	16	19	20.0
Other manufacturing (excl. sugar and oil)	53	56	55	59	11.4
Construction	71	69	73	84	17.6
Agriculture (incl. sugar)	40	36	31	26	-35.4
Others, incl. services	334	347	360	375	12.2
Average monthly income (in USD)					
Officials, professionals and technicians	644	725	774	823	27.8
Clerks and service workers	344	377	423	416	21.1
Machine operators and crafts	351	385	419	426	21.1
Agricultural and elementary	244	253	286	268	10.0
Unit labor costs (index 2000=100)					
Manufacturing (excl. petrochemicals)	90.3	86.6	86.0	85.6	-5.2
Oil and gas	106.6	114.2	114.4	136.7	28.3

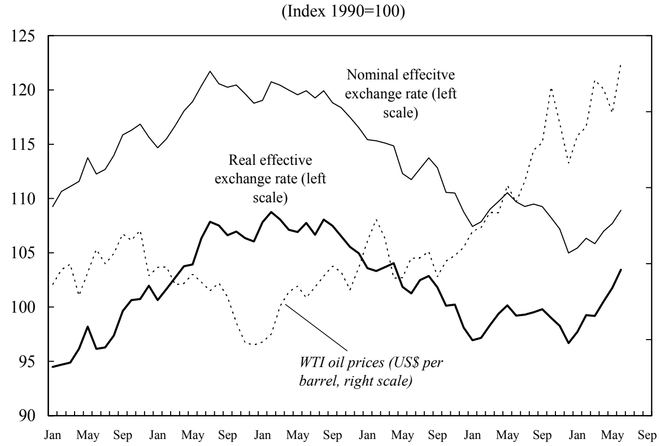
Sources: Trinidad and Tobago authorities; and Fund staff estimates.

than did the mission. They emphasized the role of food prices in the recent increases in headline inflation. Wage increases, especially at the lower end of the skill spectrum, were also still relatively muted. The authorities, nevertheless, noted their recent moves to increase interest rates and indicated that the central bank would continue to ensure that liquidity did not fan inflation further.

28. **The mission noted the pressures for a real appreciation, and pointed to the limits to monetary policy successfully addressing these pressures under the present exchange rate policy**. Ideally, the current account surplus would be sterilized through fiscal savings. In the absence of a sufficient fiscal effort, however, a real appreciation may be unavoidable. Notwithstanding the earlier slackness in the labor market, dollar wages for skilled labor had already increased significantly during 2001–04 and the current tight market presaged further wage pressures. With an open capital account, the central bank's scope to influence interest rates beyond a certain point was, however, necessarily limited by the current exchange rate regime. Under these circumstances, the choice was whether real appreciation occurred through inflation or by other means. Pointing to the adverse impact on poor household incomes of inflation, the mission recommended instead nominal exchange rate flexibility. Given the unchanged exchange rate in recent years and the complex structural features of the foreign exchange market, moves toward greater flexibility would, however, have to be carefully designed and implemented so as not to be destabilizing. At the same time, the monetary framework would need to be geared more toward explicitly targeting inflation.

29. **The authorities considered the current level of the real exchange rate to be appropriate and pointed to safety valves that would ameliorate pressures for appreciation**. They explained that the business community did not appear to view the current level of the exchange rate as detrimental to competitiveness. Available data for 2001–04 showed that real wage growth still lagged real nonenergy GDP growth and unit labor costs in manufacturing were continuing to decline, albeit at a slower rate than before (see Box 3). As regards capacity constraints, the private sector was expanding production into the larger region and skilled labor could be imported. Together with the capital outflows, these would mitigate some of the pressures from the balance of payments and the fiscal expansion (see Box 1). The mission, for its part, noted that the real exchange rate was, despite the recent appreciation, below its level a few years earlier, and hence still broadly competitive, and concurred that going forward, greater regional integration could indeed help boost competitiveness.

Effective Real and Nominal Exchange Rates
(Index 1990=100)



Source: IMF, Information Notice System.

C. Structural Issues

30. **The authorities view structural reforms as complementing the government's efforts to create space for the private sector to grow, in particular in the nonenergy sector**. The current focus is on tax and financial sector reform. In this vein, the authorities are also seeking to improve the business climate. The discussions touched on these areas, as well as on utility prices, privatization, and labor market policies.

31. **Trinidad and Tobago is in the process of implementing a comprehensive tax reform**. As regards the energy sector, reflecting its changing nature and increasing complexity, a decision has been made to distinguish between the regime governing gas and oil. The new regimes contain some provisions that will apply retroactively. The authorities are considering plans for taxation of the nonenergy sector that go beyond the measures introduced with the new budget. These latter measures, to be phased in over several years entail broadening the tax base and reducing the complexity of the system with an aim to increasing its efficiency and predictability. The budget speech for FY 2005/06 announced that consistent with Fund technical assistance advice, a Tax Policy Unit was being established in the Ministry of Finance with a mandate for the continuous reform of the tax regime.

32. **Financial sector reforms seek to consolidate and strengthen Trinidad and Tobago's role as a regional financial center**. The mission noted the FSAP's finding that while banks appeared well-capitalized and profitable, the nonbanking sector was more vulnerable, including on account of regional exposure. The financial system as a whole was also significantly exposed to the risks of a reversal in energy prices, particularly when accompanied by a decline in real estate and equity prices, and a significant increase in interest rates. Given the pre-eminence of conglomerates in the financial system, introducing a framework for consolidated supervision appeared urgent. Also, given the regional exposure of Trinidadian financial entities, cross-border activities should be carefully monitored.

33. **While agreeing with the thrust of the FSAP recommendations, the authorities emphasized capacity constraints and the need to prioritize measures**. They were pleased that the FSAP had broadly endorsed their existing reform program. Pointing to the very heavy reform agenda, the authorities indicated, however, that prioritization and sequencing of reforms will have to be undertaken carefully and noted that this will inevitably require time. They also noted the requirement for large amounts of technical assistance, which the mission offered its support in helping to coordinate.

34. **The authorities emphasized their efforts to create and strengthen a pro-business culture, including through their interventions in the labor market**. A paper prepared under the aegis of the Enabling Environment Committee—the Prime Minister's Standing Committee on Business Development, has produced a comprehensive list of impediments to business formation, growth and development. The authorities also pointed to some specific sectors, such as filming, printing and packaging, and food processing that had been identified as having potential and possibly meriting governmental support. As regards the labor market, the authorities noted that the budgetary public employment work programs had a strong training component and were administered in a manner that encouraged entrepreneurship. Reported labor shortages by the business community did not constitute a valid justification

for discontinuing the programs as, in addition to enhancing skill levels, they provided a social safety net for the more vulnerable members of society.

35. **The mission encouraged the authorities to consider reinvigorating privatization and adjusting utility prices to spur private sector development**. It noted a marked increase in the number of statutory bodies and public enterprises at the same time as the privatization program appeared to have petered out. The authorities emphasized that the new bodies being set up did not represent an expansion of the state into the private sphere. Rather, it was an attempt to bring private sector expertise to bear on the problem of government inefficiencies. As regards public utilities, noting the business community's complaints about inefficiencies, the mission suggested that tariff adjustments to cover the currently large financial losses could also help improve service provision. The authorities indicated that the petition for the increase in electricity tariffs was currently being reviewed and that for water would follow shortly.

V. Staff Appraisal

36. **Trinidad and Tobago is in an enviable position in many respects, but one that also comes with several challenges**. The increase in oil prices provides an opportunity to secure sustainable high living standards and improvements in social indicators. Maximizing the gains from the energy windfall requires, however, a careful balancing between meeting the demands of the moment and the needs of the future. It also calls for vigilance in safeguarding against vulnerabilities and a prudent mix of fiscal, monetary, and structural policies that help ensure that the public sector is getting value for its money, and that private sector competitiveness is maintained and enhanced.

37. **While mindful of the potential long-term benefits of increasing investment and reducing taxes, the relatively sudden and very large expansion of the nonenergy deficit gives pause for concern**. Fundamentally, there is a question about whether there exists the institutional capacity in the short run to absorb the increase in government expenditures, particularly current expenditures, in the most effective manner. There are also inflationary pressures emerging and the risks of Dutch disease. Finally, with the public sector so increasingly dependent on energy revenues, an unanticipated downward swing in energy prices could exact significant economic costs.

38. **Accordingly, increasing the share of energy revenues that is put aside for the future could provide several benefits**. It will go some way toward securing the sustainability of public finances and help guard against the risks of an unexpected worsening of the terms of trade. It could also shield the economy from the adverse consequences of a pro-cyclical fiscal stance, in terms of high inflation, loss of competitiveness, and a "boom bust" pattern of economic growth. Finally, by spacing expenditures over time, it would help ensure that the marginal rates of return on public spending remain high.

39. **A permanent and well-designed oil fund is one way to ensure that these benefits are realized**. The authorities are committed to establishing such a fund and the staff supports the ultimate objectives that lie behind the HSF. The HSF should, however, not be used for extra-budgetary spending. As a general rule, all public expenditures should compete for the same scarce resources within the standard budget process.

40. **A public expenditure review and a fiscal ROSC could be useful inputs to policy-making**. The recent sharp increases in expenditures have underscored the potential benefits of carrying out a comprehensive public expenditure review with external assistance, in line with previous staff recommendations. Inter alia, there are now numerous social programs on the budget that, in at least some cases, appear to have multiple objectives. A review could help increase the efficiency of public resources, including by suggesting ways to better target and focus public interventions. The staff welcomes the authorities' intentions to ensure that there remain adequate checks and balances, such as monitoring and reporting requirements, for the new expenditure executing agencies. In this regard, it reiterates the potential benefits of preparing a fiscal ROSC.

41. **Exchange rate policy will require a reconsideration in the face of the strong external inflows and widening nonenergy fiscal deficits**. In the absence of sufficient fiscal tightening, the change in fundamentals represented by a possibly permanent ratcheting upwards of oil prices is likely to require a real exchange rate adjustment. Increased flexibility of the exchange rate will enable the authorities to better manage the pressures for a real appreciation without stoking inflation.

42. **The staff welcomes the authorities' efforts to reform the financial sector**. Trinidad and Tobago has embarked on a program that, upon completion, will further secure its position as the financial center of the Caribbean. The scope of the reform program is ambitious and the staff concurs that it will take some time to fully implement. The authorities are encouraged to remain steadfast in implementing the reform agenda, a critical element of which is appropriately to strengthen supervision. The international community, for its part, will have to play its part in providing the necessary technical assistance.

43. **Structural reforms to support the growth of the private sector will have to remain an integral element of the agenda**. In this regard, the staff welcomes the efforts to reform taxation of the nonenergy sector, which is a key consideration for investors. Against the background of sharply rising expenditures, it reiterates, however, the importance of taking a more gradual approach to tax reform—especially given the uncertain revenue and distributional impacts and the need to assure predictability about future tax levels for investors. More generally, to enhance growth, the authorities are encouraged to focus their efforts on improving the overall business environment rather than seeking to pick winners and losers, as the state might not be in the best position to choose among competing industries. The government can, however, help create the necessary space for private enterprises by strengthening service provision, including by public utilities, and by reinvigorating its privatization program.

44. **The staff recommends that the next Article IV consultation be held on the standard 12-month cycle**.

Table 1. Trinidad and Tobago: Selected Economic and Financial Indicators

	2001	2002	2003	2004	Projections 2005	2006	2007	2008	2009
	(Annual percentage changes, unless otherwise indicated)								
Output and prices									
Real GDP	4.2	7.9	13.3	6.5	6.7	10.4	4.9	3.0	2.9
Energy	5.6	13.5	31.3	7.9	9.8	17.9	5.5	1.3	1.1
Nonenergy	2.8	4.7	4.9	5.8	4.7	5.3	4.4	4.3	4.3
GDP deflator	2.7	-5.7	5.6	7.5	12.4	8.2	5.9	5.2	5.3
Consumer prices									
End-of-period	3.6	4.3	3.0	5.6	6.5	8.0	7.0	6.5	6.5
Average	5.5	4.2	3.8	3.7	6.8	7.2	7.5	6.8	6.5
Unemployment rate (average, in percent)	10.8	10.4	10.3	8.3	...	...	...	...	...
	(In percent of GDP, unless otherwise indicated)								
Nonfinancial public finances 1/									
Overall budget balance	1.8	-0.6	2.0	2.0	3.2	2.7	5.0	5.2	5.0
Budgetary revenue	27.4	24.3	26.7	27.5	31.3	32.7	32.4	31.8	31.1
Of which : energy revenue	9.2	5.7	10.3	11.2	15.8	21.0	20.7	19.8	19.0
Budgetary expenditure	25.6	24.9	24.8	25.4	28.1	30.0	27.4	26.6	26.1
Of which : noninterest expenditure	21.3	20.9	20.8	22.3	25.2	27.5	25.8	25.7	25.7
Overall NFPS balance	-0.5	-3.9	1.9	2.1	1.3	3.7	5.5	4.8	3.6
Public sector debt 2/	55.0	58.4	54.7	49.1	41.3	31.8	23.2	18.0	15.4
External sector									
Current account balance	5.0	0.8	8.9	14.5	18.8	21.2	17.8	13.1	7.7
Of which									
Exports	48.5	43.1	48.2	52.0	64.5	67.5	59.0	50.5	44.5
Imports	40.4	40.5	36.2	39.7	45.5	46.1	40.5	36.8	36.3
External public sector debt	18.8	17.0	14.4	11.0	9.0	6.6	5.9	5.2	3.7
Gross official reserves (in US$ million)	1,876	1,924	2,258	2,993	3,893	4,993	5,743	6,443	7,093
In months of imports of goods	6.3	6.3	6.9	7.3	7.0	7.4	8.7	9.9	10.2
In percent of M3	56.5	56.5	65.7	73.7	79.9	86.1	89.4	92.5	94.0
Real effective exchange rate (1990 = 100) 3/	105.0	107.1	101.9	98.6	100.9	...	...	...	...
	(Percentage changes in relation to beginning-of-period M3)								
Banking system									
Net foreign assets	9.1	2.5	5.7	36.4	23.2	22.6	12.9	10.8	9.3
Net domestic assets	3.5	0.2	-3.7	-17.6	-3.3	-3.2	-1.8	-2.5	-0.9
Broad money (M3)	12.6	2.7	2.0	18.8	19.9	19.4	11.1	8.4	8.4
Memorandum items:									
Nominal GDP (in billions of TT$)	55.0	56.5	67.8	77.6	93.0	111.0	123.3	133.6	144.9
Exchange rate (TT$/US$)	6.2	6.2	6.3	6.3	...	...	...	...	...
Oil export price (US$/barrel)	24.3	25.0	28.9	37.8	54.2	61.8	60.0	58.0	57.3
Central government nonenergy deficit (in percent of GDP) 1/ 4/	7.5	6.3	8.4	9.2	12.6	18.3	15.6	14.7	13.9

Sources: Trinidad and Tobago authorities; and Fund staff estimates and projections.

1/ The data refers to fiscal years 2000/2001–2008/09.
2/ Refers to gross debt. The baseline projections assume a significant increase in government deposits at the CBTT, and accordingly lower net debt.
3/ For 2005, average up to July.
4/ Defined as expenditure minus nonenergy revenue of the central government.

Table 2. Trinidad and Tobago: Summary of Central Government Operations

	2000/01	2001/02	2002/03	2003/04	Est. 2004/05	Proj 2005/06
	(In millions of Trinidad and Tobago dollars)					
Revenue	14,825	13,620	17,366	20,628	27,915	34,795
Energy	4,996	3,185	6,717	8,422	14,100	22,401
Nonenergy	9,830	10,435	10,649	12,206	13,815	12,394
Expenditure	13,861	13,957	16,094	19,100	25,020	31,941
Current	13,079	13,214	15,096	17,499	22,287	28,456
Wages and salaries	4,284	4,225	4,548	4,849	5,446	6,521
Goods and services	1,768	1,742	2,038	2,375	3,365	4,512
Interest payments	2,330	2,260	2,592	2,364	2,594	2,625
Transfer and subsidies	4,697	4,988	5,918	7,911	10,883	14,799
Capital expenditure and net lending	782	743	998	1,601	2,734	3,485
Overall balance	**965**	**-337**	**1,272**	**1,528**	**2,895**	**2,853**
Total financing	**-965**	**337**	**-1,272**	**-1,528**	**-2,895**	**-2,853**
Foreign financing	-2	-194	12	-357	-1121	-827
Domestic financing	-963	531	-1,284	-1,171	-1,774	-2,026
	(In percent of GDP)					
Revenue	27.4	24.3	26.7	27.5	31.3	32.7
Energy	9.2	5.7	10.3	11.2	15.8	21.0
Nonenergy	18.2	18.6	16.4	16.2	15.5	11.6
Expenditure	25.6	24.9	24.8	25.4	28.1	30.0
Current	24.2	23.5	23.2	23.3	25.0	26.7
Wages and salaries	7.9	7.5	7.0	6.5	6.1	6.1
Goods and services	3.3	3.1	3.1	3.2	3.8	4.2
Interest payments	4.3	4.0	4.0	3.1	2.9	2.5
Transfers and subsidies	8.7	8.9	9.1	10.5	12.2	13.9
Capital expenditure and net lending	1.4	1.3	1.5	2.1	3.1	3.3
Overall balance	**1.8**	**-0.6**	**2.0**	**2.0**	**3.2**	**2.7**
Total financing	**-1.8**	**0.6**	**-2.0**	**-2.0**	**-3.2**	**-2.7**
Memorandum items:						
Primary balance	6.1	3.4	6.0	5.2	6.2	5.1
Overall nonenergy balance	-7.5	-6.3	-8.4	-9.2	-12.6	-18.3
(In percent of nonenergy GDP)	-10.3	-8.5	-12.7	-14.5	-20.5	-31.5
Expenditure (in percent of nonenergy GDP)	35.5	33.7	37.6	40.2	45.7	51.5
Oil price (U.S. dollar per barrel)	26.9	24.8	28.2	34.4	50.1	59.9

Sources: Trinidad and Tobago authorities; and Fund staff estimates and projections.

Table 3. Trinidad and Tobago: Consolidated Nonfinancial Public Sector
(In percent of GDP)

	2000/01	2001/02	2002/03	2003/04	Est. 2004/05	Proj. 2005/06
I. Nonfinancial Public Sector						
Current balance	4.6	-1.3	4.0	5.0	7.0	8.3
Capital revenue and transfers	2.3	1.6	2.0	3.3	3.5	3.5
Capital expenditure and net lending	7.4	4.1	4.1	6.2	9.2	8.0
Overall balance	**-0.5**	**-3.9**	**1.9**	**2.1**	**1.3**	**3.7**
Public sector debt 1/ 2/	**55.0**	**58.4**	**54.7**	**49.1**	**41.3**	**31.8**
II. Central Government						
Current balance	3.2	0.7	3.5	4.2	6.3	6.0
Current revenue	27.4	24.2	26.7	27.5	31.3	32.7
Current expenditure	24.2	23.5	23.2	23.3	25.0	26.7
Capital expenditure and net lending	1.4	1.3	1.5	2.1	3.1	3.3
Overall balance	**1.8**	**-0.6**	**2.0**	**2.0**	**3.2**	**2.7**
Central government debt 1/ 2/	**37.4**	**37.2**	**33.0**	**28.0**	**23.2**	**17.5**
III. Statutory Bodies 3/						
Current balance	-0.5	-0.9	-1.0	-1.4	-2.0	-2.4
Current revenue	3.9	3.6	3.6	3.2	2.5	2.2
Current expenditure	4.3	4.5	4.6	4.6	4.5	4.6
Capital revenue and transfers	0.7	0.6	0.7	0.6	1.0	1.8
Capital expenditure and net lending	1.3	0.5	0.3	0.3	0.4	0.3
Overall balance	**-1.1**	**-0.8**	**-0.6**	**-1.1**	**-1.4**	**-0.9**
IV. Public Enterprises 4/						
Current balance	1.9	-1.1	1.5	2.2	2.7	4.8
Current revenue	39.4	30.4	35.4	32.5	35.9	38.8
Current expenditure	37.6	31.5	33.9	30.3	33.2	34.1
Capital revenue and transfers	1.6	1.0	1.4	2.7	2.6	1.7
Capital expenditure and net lending	4.6	2.3	2.3	3.8	5.8	4.5
Overall balance	**-1.2**	**-2.4**	**0.6**	**1.1**	**-0.5**	**2.0**
Memorandum item:						
Nominal GDP (in TT$ million, FY)	54,098	56,121	64,940	75,125	89,157	106,531

Sources: Trinidad and Tobago authorities; and Fund staff estimates and projections.

1/ Refers to gross debt. The baseline projections assume a significant increase in government deposits at the CBTT, and accordingly lower net debt.

2/ Includes BOLT and leases.

3/ Includes Public Transport Company, Electricity Company, Water Authority, Airport Authority and Port Authority.

4/ Includes CARONI, MTS, NFM, NFM, NHSL, NPMC, NQCL, NGC, PETROTRIN, PLIPDECO, SWMCOL, TIDCO, TANTEAK, TRINGEN, TTST, and UDECOTT. Data for National Housing Authority was not available.

Table 4. Trinidad and Tobago: Summary Accounts of the Central Bank

	2001	2002	2003	2004	Proj. 2005
	(In millions of Trinidad and Tobago dollars)				
Net foreign assets	12,140	12,517	14,315	18,929	24,876
Net international reserves	11,631	11,978	13,834	18,487	24,434
Other foreign assets, net	509	539	481	442	442
Net domestic assets	-6,326	-6,932	-8,433	-13,144	-18,495
Net credit to public sector	-5,874	-6,336	-8,000	-12,718	-18,068
Central government	-6,113	-6,502	-8,156	-12,871	-18,222
Rest of public sector	239	167	156	154	154
Of which: public enterprises	0	0	0	0	0
Net claims on financial insitutions	380	380	380	380	380
Other items (net)	-832	-976	-813	-806	-806
Reserve money	5,814	5,585	5,882	5,785	6,381
Currency in circulation	1,843	2,005	2,295	2,554	3,062
Deposits of commercial banks	3,466	3,072	2,955	2,783	2,781
Deposits of nonbank financial institutions	505	509	632	449	538
	(Changes in percent of beginning-of-period reserve money)				
Net international reserves	56.3	6.5	32.2	78.5	102.8
Net domestic assets	-43.8	-10.4	-26.9	-80.1	-92.5
Of which					
Net credit to central government	-40.0	-6.7	-29.6	-80.2	-92.5
Reserve money	12.5	-3.9	5.3	-1.6	10.3
Memorandum item:					
Blocked account of government 1/	-2,334	-2,677	-3,100	-6,105	-10,222

Source: Central Bank of Trinidad and Tobago.

1/ Proceeds of treasury bills and treasury notes used for open market operations.

Table 5. Trinidad and Tobago: Monetary Survey

	2001	2002	2003	2004	Proj. 2005
	(In millions of Trinidad and Tobago dollars)				
Net foreign assets	**12,341**	**12,856**	**14,065**	**21,901**	**27,848**
Net domestic assets	8,237	8,279	7,486	3,691	2,836
Net credit to public sector	-3,261	-2,825	-4,925	-10,243	-12,056
Central government	-3,427	-3,797	-5,041	-10,115	-14,436
Rest of the public sector	166	972	116	-129	2,380
Of which					
Statutory bodies and public utilities	696	1,300	219	-46	-46
Public enterprises	560	786	-354	-395	-395
Credit to private sector	14,045	14,691	15,234	19,147	20,562
Other items (net)	-2,547	-3,587	-2,823	-5,213	-5,670
Liabilities to private sector (M3)	**20,578**	**21,135**	**21,551**	**25,592**	**30,684**
Currency in circulation	1,373	1,502	1,709	1,957	2,347
Demand deposits	4,238	5,393	5,595	6,866	8,232
Time deposits	5,318	4,222	3,410	3,858	4,625
Savings deposits	8,309	8,685	9,701	11,111	13,322
Fund-raising instruments 1/	1,340	1,333	1,136	1,800	2,159
	(Changes in percent of beginning-of-period M3)				
Net foreign assets	**9.1**	**2.5**	**5.7**	**36.4**	**23.2**
Net domestic assets	**3.5**	**0.2**	**-3.7**	**-17.6**	**-3.3**
Net credit to public sector	-7.2	2.1	-9.9	-24.7	-7.1
Of which : central government	-7.4	-1.8	-5.9	-23.5	-16.9
Credit to private sector	-10.1	3.1	2.6	18.2	5.5
Other items (net)	20.8	-5.1	3.6	-11.1	-1.8
Liabilities to private sector (M3)	**12.6**	**2.7**	**2.0**	**18.8**	**19.9**
Memorandum items:					
Credit to private sector (12-month increase)	5.0	4.6	3.7	25.7	7.4
M3 velocity	2.7	2.7	3.1	3.0	3.0

Source: Central Bank of Trinidad and Tobago.

1/ Include investment note certificates, secured commercial paper, and other asset-backed instruments.

Table 6. Trinidad and Tobago: Summary Balance of Payments

	2001	2002	2003	2004	Proj. 2005
	(In millions of U.S. dollars)				
Current account balance	**445**	**76**	**961**	**1,788**	**2,775**
Trade balance	718	238	1,293	1,509	2,802
Exports	4,304	3,920	5,205	6,403	9,519
Petroleum crude and refined	1,735	1,768	2,386	1,643	3,263
Gas	828	459	951	1,978	2,747
Petrochemicals	823	647	907	1,522	1,889
Other	918	1,046	962	1,260	1,619
Imports	3,586	3,682	3,912	4,894	6,717
Fuel imports	926	1,019	1,064	1,181	1,873
Capital	1,267	1,276	1,257	1,796	2,507
Other	1,393	1,388	1,591	1,917	2,336
Services and transfers (net)	-273	-161	-333	279	-27
Nonfactor services (net)	233	264	314	671	539
Factor income (net)	-539	-480	-705	-446	-628
Current transfers (net)	33	55	59	54	61
Capital and financial account (net) 1/	**25**	**-28**	**-627**	**-1,053**	**-1,875**
Official, medium and long-term (net)	-52	-51	-74	-230	-17
Disbursements	26	18	16	25	69
Amortizations	-78	-68	-90	-255	-86
Direct Investment (net)	777	684	583	973	1,705
Commercial banks (net)	199	-22	94	-524	0
Other private sector capital (net) 1/	-899	-639	-1,230	-1,272	-3,563
Of which: net errors and omissions	-342	-424	-121	-214	0
Overall balance	**470**	**49**	**334**	**735**	**900**
Change in gross official reserves (increase -)	-470	-49	-334	-735	-900
	(In percent of GDP, unless otherwise specified)				
Memorandum items:					
Current account	5.0	0.8	8.9	14.5	18.8
Exports of goods	48.5	43.1	48.2	52.0	64.5
Imports of goods	40.4	40.5	36.2	39.7	45.5
Gross international reserves (millions of US$, end of period)	1,876	1,924	2,258	2,993	3,893
Oil prices (WEO, spot crude)	24.3	25.0	28.9	37.8	54.2
GDP (millions of US$)	8,872	9,112	10,755	12,315	14,764

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

1/ Includes net errors and omissions.

Table 7. Trinidad and Tobago: Illustrative Medium-Term Scenarios

		Projections				
	2004	2005	2006	2007	2008	2009
Macroeconomic parameters						
Oil prices (U.S. dollars per barrel)	37.8	54.2	61.8	60.0	58.0	57.3
			I. Baseline Scenario			
			(Annual percentage changes)			
Real sector						
Real GDP	6.5	6.7	10.4	4.9	3.0	2.9
Energy	7.9	9.8	17.9	5.5	1.3	1.1
Nonenergy	5.8	4.7	5.3	4.4	4.3	4.3
Average CPI	3.7	6.8	7.2	7.5	6.8	6.5
GDP deflator	7.5	12.4	8.2	5.9	5.2	5.3
			(In percent of GDP, unless otherwise indicated)			
Nominal GDP (billions of TT dollars)	77.6	93.0	111.0	123.3	133.6	144.9
Central government 1/						
Government revenue	27.5	31.3	32.7	32.4	31.8	31.1
Government expenditure	25.4	28.1	30.0	27.4	26.6	26.1
Of which: noninterest expenditure	22.3	25.2	27.5	25.8	25.7	25.7
Government budgetary balance	2.0	3.2	2.7	5.0	5.2	5.0
Of which: nonenergy	-9.2	-12.6	-18.3	-15.6	-14.7	-13.9
Government and government-guaranteed debt 2/	49.1	41.3	31.8	23.2	18.0	15.4
External sector						
Current account balance	14.5	18.8	21.2	17.8	13.1	7.7
NIR of the central bank (in US$ million)	2,993	3,893	4,993	5,743	6,443	7,093
			II. High Expenditure Scenario			
			(Annual percentage changes)			
Real sector						
Real GDP	6.5	6.7	10.4	5.3	2.5	2.3
Energy	7.9	9.8	17.9	5.5	1.3	1.1
Nonenergy	5.8	4.7	5.3	5.1	3.4	3.2
Average CPI	3.7	6.8	7.2	9.6	8.9	8.7
GDP deflator	7.5	12.4	8.2	7.7	6.4	6.7
			(In percent of GDP, unless otherwise indicated)			
Nominal GDP (billions of TT dollars)	77.6	93.0	111.0	125.9	137.3	149.9
Central government 1/						
Government revenue	27.5	31.3	32.7	32.3	31.5	30.8
Government expenditure	25.4	28.1	30.0	30.0	30.0	30.0
Of which: noninterest expenditure	22.3	25.2	27.5	28.3	28.9	29.2
Government budgetary balance	2.0	3.2	2.7	2.3	1.5	0.8
Of which: nonenergy	-9.2	-12.6	-18.3	-18.2	-18.0	-17.8
Government and government-guaranteed debt 2/	49.0	41.3	31.8	25.4	21.6	19.0
External sector						
Current account balance	14.5	18.8	21.2	14.7	9.1	2.6
NIR of the central bank (in US$ million)	2,993	3,882	4,932	5,632	6,273	6,831

Sources: Trinidad and Tobago authorities; and Fund staff estimates and projections.

1/ Fiscal data refers to fiscal years ending September 30.

2/ Refers to gross debt. The baseline projections assume a significant increase in government deposits at the CBTT, and accordingly lower net debt.

Table 8. Trinidad and Tobago: Indicators of External and Financial Vulnerability

(In percent of GDP, unless otherwise indicated)

	2001	2002	2003	2004	Proj. 2005
External indicators					
Exports (percent change, 12-month basis in US$)	0.3	-8.9	32.8	23.0	48.7
Imports (percent change, 12-month basis in US$)	8.0	2.7	6.2	25.1	37.2
Terms of trade (percent change, 12-month basis)	-5.7	0.6	7.5	4.4	3.2
Current account balance	5.0	0.8	8.9	14.5	18.8
Capital and financial account balance	0.3	-0.3	-5.8	-8.6	-12.7
Gross official reserves (in US$ millions)	1,876	1,924	2,258	2,993	3,893
Official reserves in months of imports of goods	6.3	6.3	6.9	7.3	7.0
Ratio of reserves to broad money	56.5	56.5	65.7	73.7	79.9
Ratio of total public sector external debt to exports of goods and services	38.0	40.7	30.9	21.8	14.5
Ratio of public sector external interest payments to exports of goods and services	2.5	2.8	2.0	1.8	1.0
Public sector debt service to exports of goods and services	4.1	4.3	3.6	5.3	1.9
REER appreciation CPI-based (percent change)	7.6	2.0	-4.8	-3.2	...
Foreign currency debt rating, (Standard & Poor's, end of period) 1/	BBB-	BBB-	BBB	BBB+	A-
Financial indicators 2/					
90-day treasury bill, average discount rate 3/ 4/	8.3	4.8	4.8	4.8	4.9
90-day treasury bill, real rate 5/	2.7	0.6	1.0	1.0	...
Nonperforming loans (in percent of total loans)	3.4	3.6	2.8	3.1	...
Risk-based capital asset ratio	19.8	20.6	20.3	22.7	...
Ratio of after-tax profits to equity capital	17.2	20.0	16.9	27.5	...
Provisions (in percent of total loans)	2.7	3.2	3.7	2.4	...
Return on average assets	2.5	3.0	2.1	3.7	...
FX deposits (in percent of total deposits)	28.0	30.1	23.0	33.8	31.3
FX deposits (in percent of gross international reserves)	42.3	45.5	30.2	43.8	36.6

Sources: Central Bank of Trinidad and Tobago; Standard and Poor's; Trinidad and Tobago Stock Exchange; and Fund staff estimates and projections.

1/ Long-term foreign currency rating upgraded in June 2004.
2/ Include commercial banks only.
3/ As at end-August.
4/ Weighted average discount rate.
5/ Adjusted for inflation.

Table 9. Trinidad and Tobago: Public Sector Debt Sustainability Framework, 2000–10

(In percent of GDP, unless otherwise indicated)

		Actual					Projections						
		2000	2001	2002	2003	2004	2005	2006	2007	2008	2009	2010	Debt-stabilizing primary balance 10/
1	**Baseline: public sector debt 1/**	54.4	55.0	58.4	54.7	49.1	**41.3**	**31.8**	**23.2**	**18.0**	**15.4**	**14.1**	**-0.9**
	Of which : foreign-currency denominated	25.5	22.4	23.0	15.5	13.6	11.3	8.5	7.4	6.6	4.7	4.2	
2	Change in public sector debt	-0.1	0.6	3.4	-3.8	-5.5	-7.9	-9.4	-8.6	-5.2	-2.6	-1.4	
3	Identified debt-creating flows (4+7+12)	-8.2	-6.7	-1.3	-9.9	-9.4	-11.0	-9.4	-8.6	-7.1	-6.4	-6.0	
4	Primary deficit	-6.3	-6.1	-3.4	-6.0	-5.2	-6.2	-5.2	-6.7	-6.0	-5.4	-5.0	
5	Revenue and grants	25.6	27.4	24.3	26.7	27.5	31.3	32.7	32.4	31.8	31.1	30.7	
6	Primary (noninterest) expenditure	19.4	21.3	20.8	20.8	22.3	25.2	27.5	25.8	25.7	25.7	25.7	
7	Automatic debt dynamics 2/	-1.9	-0.6	2.1	-3.9	-4.3	-4.8	-4.3	-2.0	-1.0	-1.0	-1.0	
8	Contribution from interest rate/growth differential 3/	-1.9	-0.6	2.0	-3.9	-4.3	-4.8	-4.3	-2.0	-1.0	-1.0	-1.0	
9	*Of which:* contribution from real interest rate	1.7	3.5	6.3	2.1	-0.5	-2.1	-1.0	-0.3	-0.3	-0.6	-0.5	
10	*Of which:* contribution from real GDP growth	-3.6	-4.0	-4.2	-6.1	-3.8	-2.8	-3.3	-1.7	-0.7	-0.5	-0.5	
11	Contribution from exchange rate depreciation 4/	0.0	0.0	0.0	0.0	0.0	...	...	...	...	...	...	
12	Other identified debt-creating flows	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	
13	Privatization receipts (negative)	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	
14	Recognition of implicit or contingent liabilities	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	
15	Other (specify, e.g., bank recapitalization)	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	
16	Residual, including asset changes (2–3) 5/	8.0	7.3	4.8	6.1	3.9	3.1	0.0	0.0	1.9	3.9	4.6	
	Public sector debt-to-revenue ratio 1/	212.2	200.7	240.8	204.4	178.9	131.8	97.4	71.5	56.7	49.6	45.7	
	Gross financing need 6/	4.0	2.9	2.7	2.6	0.5	0.7	-0.1	-2.7	-2.9	-3.0	-2.9	
	In billions of U.S. dollars	0.3	0.3	0.2	0.3	0.1	0.1	0.0	-0.5	-0.6	-0.7	-0.7	
	Scenario with key variables at their historical averages 7/						**41.3**	**35.4**	**29.8**	**26.2**	**24.4**	**23.3**	**-0.4**
	Scenario with no policy change (constant primary balance) in 2005–10						**41.3**	**30.8**	**22.8**	**17.5**	**14.2**	**11.8**	**-0.7**
	Key macroeconomic and fiscal assumptions underlying baseline												
	Real GDP growth (in percent) 8/	7.7	8.2	8.0	12.0	8.0	6.7	9.5	6.1	3.4	2.9	3.2	
	Average nominal interest rate on public debt (in percent) 9/	10.8	8.7	7.6	7.9	6.7	7.0	7.1	5.8	4.1	2.1	1.9	
	Average real interest rate (nominal rate minus change in GDP deflator, in percent)	4.1	7.1	11.5	4.6	-0.4	-4.2	-2.0	-0.5	-1.3	-3.2	-3.4	
	Nominal appreciation (increase in U.S. dollar value of local currency, in percent)	0.0	0.1	-0.2	0.0	0.0	...	...	...	...	...	...	
	Inflation rate (GDP deflator, in percent)	6.7	1.6	-3.9	3.3	7.1	11.3	9.1	6.3	5.4	5.3	5.3	
	Growth of real primary spending (deflated by GDP deflator, in percent)	4.8	18.9	5.6	11.8	15.7	20.4	19.8	-0.7	3.4	2.9	3.2	
	Primary deficit	-6.3	-6.1	-3.4	-6.0	-5.2	-6.2	-5.2	-6.7	-6.0	-5.4	-5.0	

1/ Indicate coverage of public sector, e.g., general government or nonfinancial public sector. Also whether net or gross debt is used.

2/ Derived as $[(r - \pi(1+g) - g + \alpha\varepsilon(1+r)]/(1+g+\pi+g\pi))$ times previous period debt ratio, with r = interest rate; π = growth rate of GDP deflator; g = real GDP growth rate; α = share of foreign-currency denominated debt; and ε = nominal exchange rate depreciation (measured by increase in local currency value of U.S. dollar).

3/ The real interest rate contribution is derived from the denominator in footnote 2/ as $r - \pi(1+g)$ and the real growth contribution as -g.

4/ The exchange rate contribution is derived from the numerator in footnote 2/ as $\alpha\varepsilon(1+r)$.

5/ For projections, this line includes exchange rate changes.

6/ Defined as public sector deficit, plus amortization of medium and long-term public sector debt, plus short-term debt at end of previous period.

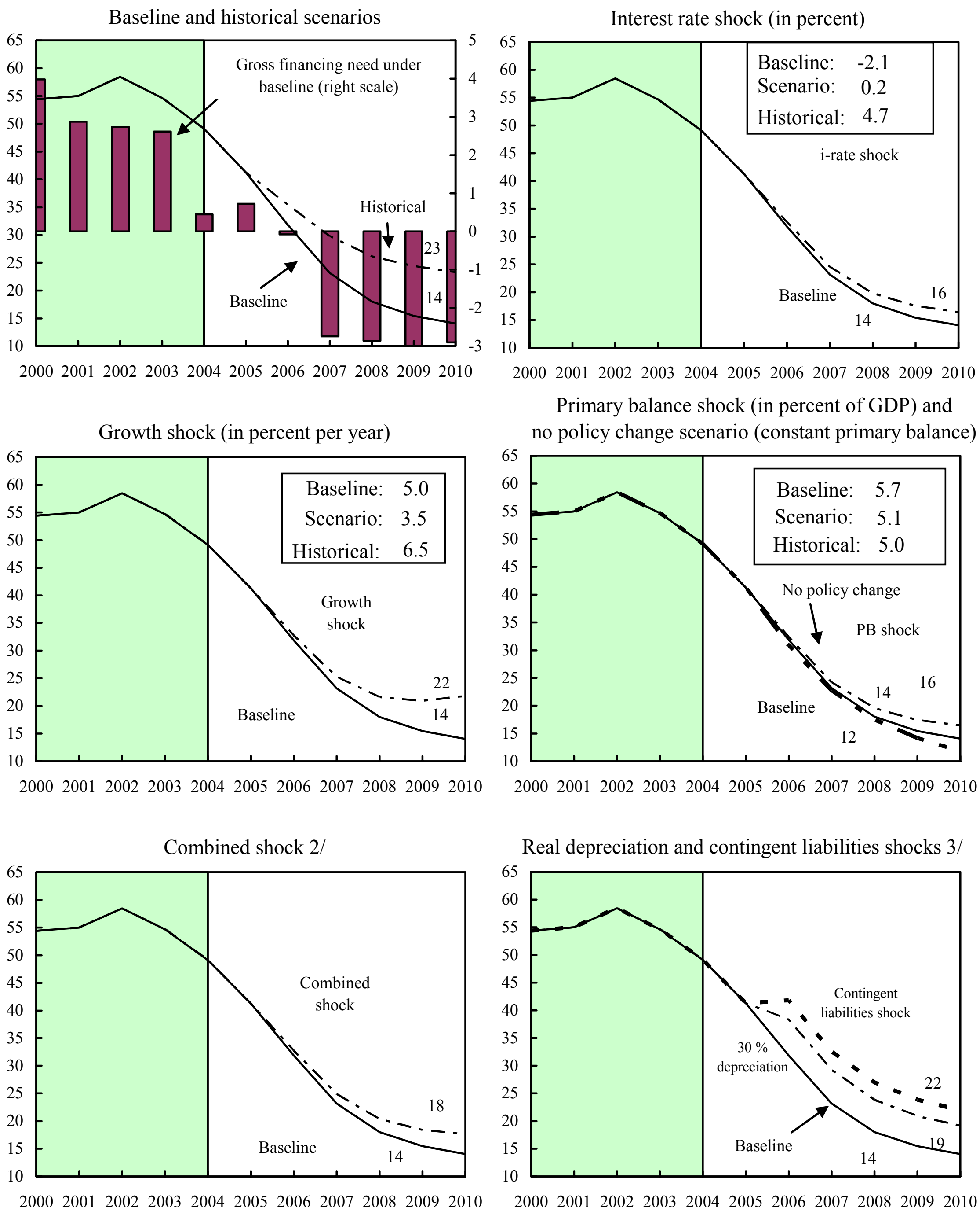
7/ The key variables include real GDP growth; real interest rate; and primary balance in percent of GDP.

8/ On a fiscal year basis (Table 10 is based on calendar years).

9/ Derived as nominal interest expenditure divided by previous period debt stock.

10/ Assumes that key variables (real GDP growth, real interest rate, and other identified debt-creating flows) remain at the level of the last projection year.

Figure 2. Trinidad and Tobago: Public Debt Sustainability: Bound Tests 1/
(Public debt in percent of GDP)



Sources: International Monetary Fund, Country desk data, and staff estimates.

1/ Shaded areas represent actual data. Individual shocks are permanent one-half standard deviation shocks. Figures in the boxes represent average projections for the respective variables in the baseline and scenario being presented. Ten-year historical average for the variable is also shown.

2/ Permanent 1/4 standard deviation shocks applied to real interest rate, growth rate, and primary balance.

3/ One-time real depreciation of 30 percent and 10 percent of GDP shock to contingent liabilities occur in 2006, with real depreciation defined as nominal depreciation (measured by percentage fall in dollar value of local currency) minus domestic inflation (based on GDP deflator).

Table 10. Trinidad and Tobago: External Debt Sustainability Framework, 2000–10
(In percent of GDP, unless otherwise indicated)

		Actual					Projections						
		2000	2001	2002	2003	2004	2005	2006	2007	2008	2009	2010	Debt-stabilizing noninterest current account 6/
1	**Baseline: external debt**	20.5	18.5	17.5	14.9	11.3	**9.3**	**6.9**	**6.1**	**5.4**	**3.9**	**3.4**	**-2.9**
2	Change in external debt	-2.7	-2.1	-0.9	-2.7	-3.6	-2.0	-2.5	-0.8	-0.6	-1.6	-0.4	
3	Identified external debt-creating flows (4+8+9)	-12.9	-11.9	-5.2	-4.7	-7.4	-15.4	-23.0	-20.6	-13.8	-11.0	-6.2	
4	Current account deficit, excluding interest payments	-8.0	-6.4	-2.3	-10.0	-15.6	-19.5	-21.8	-18.3	-13.5	-8.0	-3.6	
5	Deficit in balance of goods and services	-13.9	-10.7	-5.5	-14.9	-17.7	-22.6	-24.8	-21.3	-15.9	-10.0	-5.3	
6	Exports	59.2	55.3	50.1	54.0	59.6	71.3	73.8	64.7	55.9	49.7	45.4	
7	Imports	45.3	44.6	44.6	39.1	41.9	48.7	49.0	43.4	40.0	39.6	40.1	
8	Net nondebt creating capital inflows (negative)	-2.4	-5.3	-4.1	6.9	8.9	4.0	-1.0	-2.5	-0.6	-3.2	-2.9	
9	Automatic debt dynamics 1/	-2.5	-0.2	1.2	-1.6	-0.8	0.1	-0.2	0.1	0.2	0.2	0.2	
10	Contribution from nominal interest rate	1.3	1.4	1.4	1.1	1.1	0.7	0.6	0.4	0.4	0.3	0.3	
11	Contribution from real GDP growth	-1.4	-0.8	-1.4	-2.0	-0.8	-0.6	-0.8	-0.3	-0.2	-0.1	-0.1	
12	Contribution from price and exchange rate changes 2/	-2.4	-0.8	1.2	-0.8	-1.0	...	...	...	...	...	...	
13	Residual, incl. change in gross foreign assets (2–3) 3/	10.2	9.8	4.3	2.0	3.9	13.4	20.6	19.8	13.2	9.4	5.8	
	External debt-to-exports ratio (in percent)	34.7	33.4	35.0	27.6	19.0	13.1	9.3	9.4	9.7	7.8	7.5	
	Gross external financing need (in billions of U.S. dollars) 4/	-0.2	-0.3	0.1	-0.7	-1.4	-2.6	-3.4	-3.3	-2.6	-1.4	-0.7	
	in percent of GDP	-1.9	-2.9	1.2	-6.9	-11.5	-17.3	-19.3	-17.0	-12.4	-6.1	-2.7	
	Scenario with key variables at their historical averages 5/						**9.3**	**24.1**	**37.8**	**43.7**	**45.3**	**42.9**	**-4.8**
	Key macroeconomic assumptions underlying baseline												
	Real GDP growth (in percent)	7.3	4.2	7.9	13.3	6.5	6.7	10.4	4.9	3.0	2.9	3.3	
	GDP deflator in U.S. dollars (change in percent)	11.6	3.9	-5.9	4.5	7.1	12.4	8.2	5.9	5.2	5.3	5.3	
	Nominal external interest rate (in percent)	6.8	7.2	7.9	7.4	8.2	7.9	7.5	7.1	6.9	6.9	9.1	
	Growth of exports (U.S. dollar terms, in percent)	41.7	1.3	-7.1	27.9	25.9	43.5	23.5	-2.5	-6.4	-3.7	-0.6	
	Growth of imports (U.S. dollar terms, in percent)	22.6	6.7	2.5	4.1	22.1	39.4	20.2	-1.6	-0.1	7.4	10.0	
	Current account balance, excluding interest payments	8.0	6.4	2.3	10.0	15.6	19.5	21.8	18.3	13.5	8.0	3.6	
	Net nondebt creating capital inflows	2.4	5.3	4.1	-6.9	-8.9	-4.0	1.0	2.5	0.6	3.2	2.9	

1/ Derived as $[r - g - \rho(1+g) + \varepsilon\alpha(1+r)]/(1+g+\rho+g\rho)$ times previous period debt stock, with r = nominal effective interest rate on external debt; ρ = change in domestic GDP deflator in US dollar terms, g = real GDP growth rate, ε = nominal appreciation (increase in dollar value of domestic currency), and α = share of domestic-currency denominated debt in total external debt.

2/ The contribution from price and exchange rate changes is defined as $[-\rho(1+g) + \varepsilon\alpha(1+r)]/(1+g+\rho+g\rho)$ times previous period debt stock. ρ increases with an appreciating domestic currency ($\varepsilon > 0$) and rising inflation (based on GDP deflator).

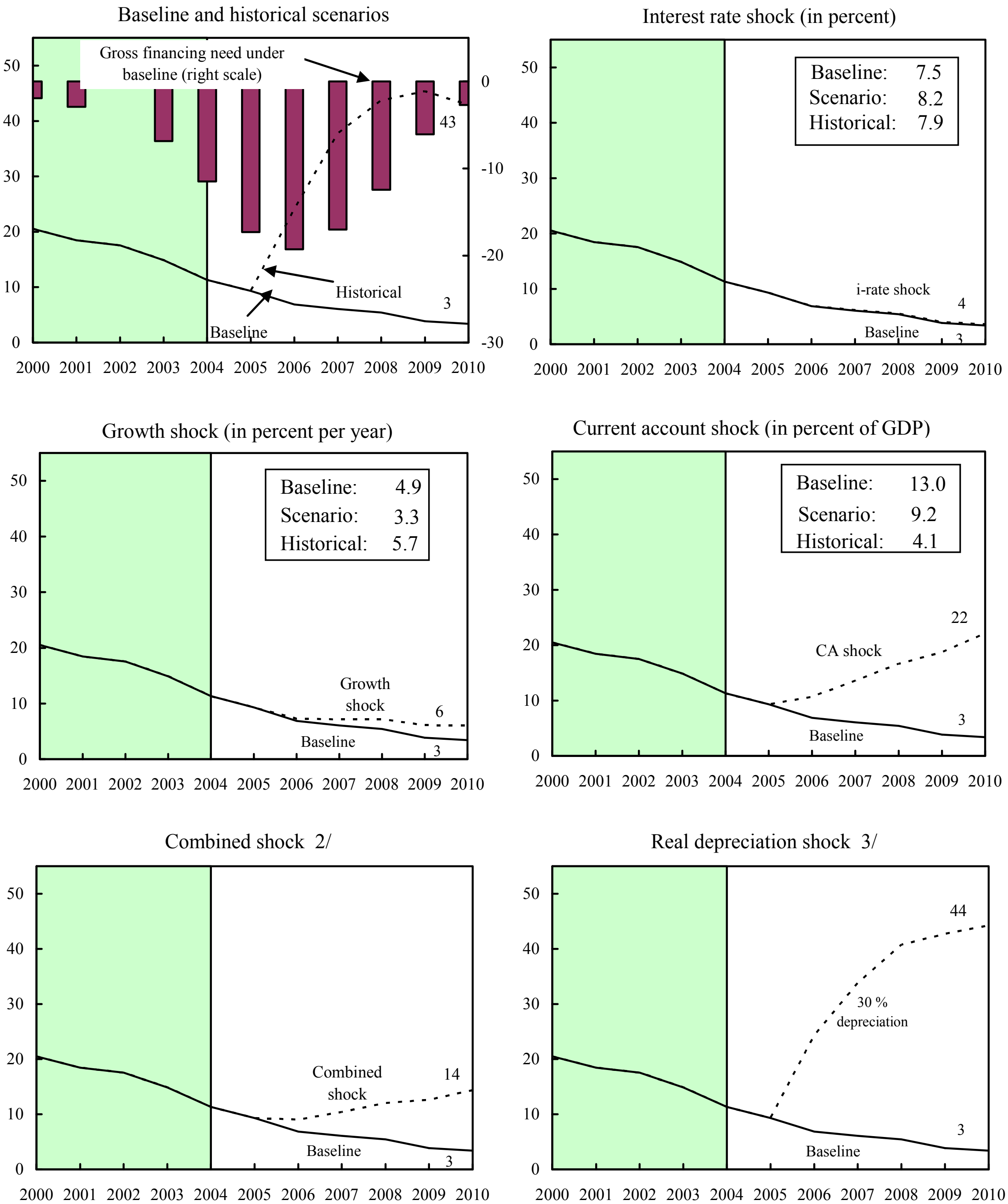
3/ For projection, line includes the impact of price and exchange rate changes.

4/ Defined as current account deficit, plus amortization on medium- and long-term debt, plus short-term debt at end of previous period.

5/ The key variables include real GDP growth; nominal interest rate; dollar deflator growth; and both noninterest current account and nondebt inflows in percent of GDP.

6/ Long-run, constant balance that stabilizes the debt ratio assuming that key variables (real GDP growth, nominal interest rate, dollar deflator growth, and non-debt inflows in percent of GDP) remain at their levels of the last projection year.

Figure 3. Trinidad and Tobago: External Debt Sustainability: Bound Tests 1/
(External debt in percent of GDP)



Sources: International Monetary Fund, Country desk data, and staff estimates.

1/ Shaded areas represent actual data. Individual shocks are permanent one-half standard deviation shocks. Figures in the boxes represent average projections for the respective variables in the baseline and scenario being presented. Ten-year historical average for the variable is also shown.

2/ Permanent 1/4 standard deviation shocks applied to real interest rate, growth rate, and current account balance.

3/ One-time real depreciation of 30 percent occurs in 2006.

TRINIDAD AND TOBAGO—FUND RELATIONS
(As of August 31, 2005)

I. Membership Status: Joined: September 9, 1963; Article VIII.

II. General Resources Account:

	SDR Million	Percent of Quota
Quota	335.60	100.00
Fund holdings of currency	247.20	73.66
Reserve position in Fund	88.41	26.34

III. SDR Department:

	SDR Million	Allocation
Net cumulative allocation	46.23	100.00
Holdings	2.44	4.85

IV. Outstanding Purchases and Loans: None

V. Latest Financial Arrangements:

Type	Approval Date	Expiration Date	Amount Approved (SDR Million)	Amount Drawn (SDR Million)
Stand-by	04/20/90	03/31/91	85.00	85.00
Stand-by	01/13/89	02/28/90	99.00	99.00

VI. Projected Obligations to Fund: (SDR Million; based on existing use of resources and present holdings of SDRs):

	Forthcoming				
	2005	2006	2007	2008	2009
Charges/Interest	0.30	1.19	1.19	1.19	1.19
Total	0.30	1.19	1.19	1.19	1.19

VII. Exchange Arrangements:

Trinidad and Tobago dollar has been within ±1 percent band around TT$6.3 against the U.S. dollar in the past year. Accordingly, it is classified as a conventional peg.

VIII. Last Article IV Consultation and Recent Contacts:

The 2004 Article IV consultation was completed by the Executive Board on October 22, 2004; the documents were IMF Country Report Nos. 05/4 (Staff Report) and 05/6 (Selected Issues). Trinidad and Tobago participated in the Financial Sector Assessment Program in early 2005. In this connection, the two Fund/World Bank missions visited Port-of-Spain in February and May, 2005.

IX. Technical Assistance:

- **MFD/LEG**: Assistance with the drafting of a new Insurance Act, and amendments to the Financial Institutions Act (ongoing)
- **STA**: National Accounts Assessment Mission in August-September 2005
- **FAD**: A follow-up tax policy mission in April 2005, focusing on personal and corporate income taxes.
- **FAD**: A tax policy mission in November 2004 on the VAT and other main indirect taxes.
- **CARTAC**: Training in bank supervision techniques, in September 2004.
- **STA**: GDDS Metadata Development Mission in May-June 2004.
- **MFD**: Follow up missions on strengthening financial system supervision: insurance and pensions in 2004.
- **MFD**: A series of missions on strengthening financial system supervision: insurance and pensions in 2003.
- **FAD**: A pension reform technical assistance mission visited Port-of-Spain in April 2002.
- **MAE**: A monetary policy advisor to the central bank was in place from April 2001 to March 2003.
- **STA**: In January 2000, a multi-topic technical assistance mission prepared a comprehensive program for the improvement of major statistical series.
- **FAD**: In December 1999, a technical assistance mission advised the Ministry of Finance on restructuring energy taxation.
- **MAE**: From February 1, 1999 to July 31, 2001, a Caribbean regional central bank advisor was assigned with residence in Port-of-Spain.
- **MAE**: In 1998 and 1999, there were three visits each by two experts providing assistance in the area of monetary policy and developing central bank research capacity.
- **MAE**: In November 1997, a technical assistance mission assisted the central bank in defining its technical assistance needs in the area of research.

TRINIDAD AND TOBAGO—RELATIONS WITH THE WORLD BANK

(As of June 10, 2005)

The World Bank's last Country Assistance Strategy for Trinidad and Tobago was discussed at the Board in 1999. The CAS was conceived as a first step within a 10-year framework and was approved for the period up to 2002. The program articulated a 10-year development agenda for the country, focusing on: (i) facilitating private sector led employment generation and entrepreneurship in labor-intensive agriculture and export services sectors by (a) streamlining investment approval process; (b) removing labor market rigidities; (c) reforming the agricultural sector; and (d) encouraging the services sector; (ii) increasing human capital through investment in education, health and social programs, notably by improving (a) healthcare facilities; and (b) targeting and efficiency of social programs; (iii) improving the delivery of public services to support private sector-led economic diversification; and (iv) ensuring environmental sustainability of growth.

The current World Bank program includes two ongoing projects with total commitment of US$30.8 million (a Postal Service Reform project in the amount of US$10.8 million and an HIV/AIDS Prevention and Control Project in the amount of US$20 million), of which US$22.0 million is undisbursed.

I. PROJECTS

Postal Service Reform: The Postal Service Reform project (US$10.8 million) assists the Government in the privatization of the Postal Service, with the objective of reducing public sector losses while improving the quality and efficiency of the postal service.

HIV/AIDS Prevention and Control Project: The project (US$ 20.0 million) was approved in June 2003 and is funded under the Multi-Country APL for the Caribbean Region, with the following objectives: (i) curbing the spread of HIV/AIDS epidemic; (ii) reducing the morbidity and mortality attributed to HIV/AIDS; (iii) improving the quality of life for persons living with HIV/AIDS; and (iv) developing a sustainable organizational and institutional framework for managing the HIV/AIDS epidemic over the longer term.

II. ECONOMIC AND SECTOR WORK

A Financial Sector Assessment Program by the World Bank and the IMF is ongoing.

Trinidad and Tobago also benefits from World Bank regional studies, such as the recently-completed report "A Time to Choose—Caribbean Development in the 21st Century."

III. Statement of World Bank Loans

(In millions of U.S. dollars)

Operation	Original Principal	Available	Disbursed
HIV/AIDS prevention and control	20.0	19.0	1.0
Postal service reform	10.8	3.0	7.8
	30.8	**22.0**	**8.8**

Disbursements and Debt Service
(Fiscal year ending June 30)

	Actual							Projections	
	1999	2000	2001	2002	2003	2004		2005	2006
Total disbursements	9.8	14.8	12.3	9.6	12.7	3.8		2.3	8.4
Repayments	7.7	8.8	9.7	10.2	12.2	15.5		16.7	16.4
Net disbursements	2.1	5.9	2.5	-0.6	0.4	-11.7		-14.4	-8.0
Interest and fees	5.5	6.9	7.1	6.7	5.9	5.1		3.7	3.1

Loans Summary in U.S. dollars as of June 10, 2005

Total disbursed (IBRD):	265,752,928
Of which has been repaid:	178,012,001
Total now held by IBRD:	63,394,624
Total undisbursed:	22,068,251

Trinidad and Tobago—Relations with the Inter-American Development Bank
(As of June 17, 2005)

In November 2004, the IDB Board approved the new Country Strategy with Trinidad and Tobago. This document reflects the extensive process of dialogue with all major stakeholders in the country, and the agreements with Government on three principal and inter-dependent areas of strategic focus. These three areas are: (i) promoting private sector development to achieve economic diversification; (ii) promoting public sector modernization to improve efficiency and effectiveness; and (iii) promoting social development through improved public services.

In each area, criteria have been established to guide conceptualization and design of operations, and also to guide program dialogue to define new operational priorities consistent with the strategy. The strategy recognizes the particular characteristics of Tobago, and pays attention to considering, as a crosscutting feature of IDB programs, gender issues. The strategy allows for flexibility to expand this program in line with possible Bank lending directly to the private sector and/or to support new operations in the out-years stemming from the public sector reform "road map" exercise that is now underway. An integral of the strategy is to focus on timely completion of projects and programs currently in execution, and achievement of their development objectives.

As of June 17, 2005, the IDB has an active public sector lending portfolio of seven loans with a total value of US$409 million, of which US$191 million (47 percent) has been disbursed. In addition to loans for the public sector, the IDB lends directly to the private sector and provides grant resources through technical cooperations. MIF, an IDB institution providing grant resources for private sector development, has four operations in execution for an amount of US$2.8 million, of which US$0.8 million (29 %) has been disbursed.

Following is a brief description of the Bank's public sector loans in execution by strategic area.

Promoting private sector development to achieve economic diversification

The IDB is in the process of preparing a Private Sector Development Strategy, which will complement the efforts of the ongoing Business Climate Initiative. The Initiative calls for: (i) a Diagnostic Assessment to identify a prioritized list of issues to improve the business climate; (ii) agreement on a Business Climate Action Plan, the implementation of which the Bank would support with an array of operational instruments; and (iii) agreement on a system to monitor and evaluate the effectiveness of the Action Plan's implementation.

In March 2003, the IDB approved a loan of US$5.0 million for a Trade Sector Support Program. The operation was developed under a new sector facility and its main objective is to improve the international trade performance of Trinidad and Tobago. That goal will be met by strengthening the country's technical and institutional capacity to formulate and implement trade policy, to participate effectively in trade negotiations, to implement trade agreements, and to increase and diversify exports.

In 1996, the IDB approved US$120.0 million in lending for the National Highway Program. The program aims to improve and sustain road services provided by the main national road network, reduce road transportation costs, and provide incentives for the development of small contractors and microenterprises.

Promoting public sector modernization to improve efficiency

In December 2003, the IDB approved a loan of US$5 million for a Public Sector Reform Initiation Facility. This facility is aimed at the development and initial implementation of a long-term strategy to modernize the public sector. The plan or "road map", which will result from the project through a consensus-building approach, should be ready by December 2006. It will include actions to improve the composition of public spending by optimizing the size, management, structure, organization, functioning, human resources, legal framework, accountability, and service delivery mechanisms of the Government.

In 1995, the IDB approved a US$8.0 million reimbursable technical cooperation project to assist the Government of Trinidad and Tobago in implementing the Agriculture Sector Reform Program. This technical cooperation project is expected to assist agribusiness in the identification of opportunities, and to strengthen the long-term institutional capacity of the Ministry of Agriculture.

Promoting social development through improved public services

In 2002, the IDB approved funding in the amount of US$32.0 million to support the National Settlements Program-Stage Two. The general objective is to establish a more equitable, transparent and sustainable system of affordable housing, and more specifically to improve housing conditions for low-income groups. The program includes support for squatter upgrading, family subsidies and institutional capacity building.

In 1999, the IDB approved financing in the amount of US$l05.0 million for a Secondary Education Program. This program's objectives are aimed at providing equitable, high quality secondary education; updating educational content and teaching methodologies; and developing a more efficient management of resources at the central and local levels.

In 1996, the IDB approved a US$134.0 million loan for a Health Sector Reform Program in order to strengthen the policy-making, planning and management capacity of the Ministry of Health. The program is financing activities aimed at separating health services from financing and regulatory responsibilities, shifting public expenditures, redirecting private expenditures to priority areas and finding cost effective solutions; establishing new administrative and employment structures that encourage accountability, increased autonomy, improved productivity and efficiency; reducing preventable morbidity and mortality through lifestyle changes and social interventions; and financial sustainability of the service delivery system.

TRINIDAD AND TOBAGO—STATISTICAL ISSUES

Trinidad and Tobago produces a wide range of economic and financial statistics that are largely based on sound methodological principles, and data provision is adequate for surveillance purposes. The national internet website where many of these statistics are reported can be accessed through links in the IMF's Data Standards Bulletin Board. On September 30, 2004 Trinidad and Tobago started participating in the IMF's General Data Dissemination System and hopes to subscribe to the Special Data Dissemination Standard in the near future. However, institutional arrangements need to be strengthened to facilitate improved compilation and reporting as well as collaboration among the central bank, the central statistical office, and the ministry of finance, planning, and development, and to avoid duplication of data production efforts and some inconsistencies across sectoral databases.

Real sector

The Central Statistical Office (CSO) makes good use of available source data to produce annual national accounts. In applying the recommendations of STA technical assistance (2000), the CSO has revised the real GDP series by rebasing it from 1985 to 2000, improved the methodology for calculating production at each sector level, and switched from valuation at factor cost to market prices. This particularly involved the inclusion of the large gas sector which came on stream in 2000; and changing the estimation techniques in the telecommunications sector (by using the number of call units as opposed to the number of callers) and the financial sector (by constructing individual extrapolators for each sub-industry and then aggregating them up). The central statistical office does not currently produce quarterly GDP estimates. Although the central bank currently constructs quarterly indicators of real GDP, eventually the central statistical office should assume exclusive responsibility for compiling quarterly national accounts. A recent STA mission on national accounts in September 2005 found that institutional weaknesses at the CSO remain; although there is no serious shortage of staff that could affect the production of the statistics, a reallocation would improve efficiency. The mission encouraged the CSO to start compiling quarterly GDP estimates. Work is well advanced in compiling a supply and use table that should improve the accuracy of the estimates.

The retail price index has been rebased from 1985 to January 2003 reflecting the 1997/98 Household Budgetary Survey, and correcting the aggregation formula. The CSO should ensure that a similar methodology is used to revamp the producer price index.

Fiscal accounts

Data on central government operations and debt are compiled separately by the Ministry of Finance, Planning, and Development (MFPD) and the central bank, and show significant differences. The authorities should work to reconcile on a regular basis these two sets of data. Transfers to the revenue stabilization fund are recorded as an expenditure item, but should be recorded as a financial flow below the line. Data on the nonbank financing are derived as a residual owing to the absence of data collection. The national classification system for government transactions and debt of the central government seems to be sufficiently detailed for use in compiling data according to *GFSM 1986* methodology, although no data have been submitted for use in the *GFSY*. Also, there is no evidence of significant migration to the use of *GFSM 2001*, which should be initiated.

Data on selected public enterprises and statutory bodies are being compiled by the investment division, the domestic debt division, and the budget division of the MFPD. The data from these divisions have to be reconciled, particularly on the transfers for debt servicing, transfers for government capital projects, guaranteed debt, and letters of comfort. The capital expenditure on behalf of government should be classified as capital expenditure instead of other goods and services.

Monetary accounts

The major recommendations of the IMF in monetary and financial statistics have been implemented by the authorities, leading to a substantial improvement in the analytical usefulness of the monetary statistics. There are, however, some areas for improvement. The monthly monetary account for other depository corporations (ODCs) currently covers only financial institutions that are licensed by the central bank under the 1993 Financial Institutions Act. Nonlicensed ODCs only report voluntarily on a quarterly basis. No data are reported by credit unions and the Post Office Savings Bank. The lack of these data have prevented the compilation of a more comprehensive Depository Corporation Survey. Currently only a few commercial banks are involved in limited transactions in options and swaps. If the use of these instruments becomes more significant, the central bank should initiate reporting of data on them in the monetary statistics. The authorities should also consider developing systems for reporting balance sheet accounts for the mutual funds, with a view to compiling a more comprehensive financial survey in the future.

Balance of payments

The balance of payments data conform to many of the standards of the *BPM5*. The Private Sector Capital Flows and Investor Perception survey needs to be improved on the quantity and quality of responses, and estimating market value shares. There are sizable differences between some items of the external public debt compiled by the central bank and the ministry of finance, planning, and development. The central bank should expand its current debt reporting system to include comprehensive coverage of external loans and debt of the entire public sector, as well as publicly nonguaranteed debt.

Trinidad and Tobago: Table of Common Indicators Required for Surveillance
As of October 13, 2005

	Date of latest observation	Date received	Frequency of Data[6]	Frequency of Reporting[6]	Frequency of publication[6]
Exchange Rates	September 2005	September 2005	D	D	M
International Reserve Assets and Reserve Liabilities of the Monetary Authorities[1]	July 2005	October 2005	M	M	M
Reserve/Base Money	July2005	September 2005	M	M	M
Broad Money	July 2005	October 2005	M	M	M
Central Bank Balance Sheet	July 2005	October 2005	M	M	M
Consolidated Balance Sheet of the Banking System	July 2005	October 2005	M	M	M
Interest Rates[2]	September 2005	October 2005	M	M	M
Consumer Price Index	August 2005	October 2005	M	M	M
Revenue, Expenditure, Balance and Composition of Financing[3] – General Government[4]	May 2005	July 2005	A	A	NA
Revenue, Expenditure, Balance and Composition of Financing[3]– Central Government	September 2005	October 2005	M	M	A
Stocks of Central Government and Central Government-Guaranteed Debt[5]	September 2005	October 2005	A	A	A
External Current Account Balance	December 2004	September 2005	A	A	A
Exports and Imports of Goods and Services	December 2004	September 2005	A	A	A
GDP/GNP	2004	July 2005	A	A	A
Gross External Debt	December 2004	July 2005	M	M	M

[1] Includes reserve assets pledged or otherwise encumbered as well as net derivative positions.
[2] Both market-based and officially-determined, including discount rates, money market rates, rates on treasury bills, notes and bonds.
[3] Foreign, domestic bank, and domestic nonbank financing.
[4] The general government consists of the central government (budgetary funds, extra budgetary funds, and social security funds) and state and local governments.
[5] Including currency and maturity composition.
[6] Daily (D), Weekly (W), Monthly (M), Quarterly (Q), Annually (A); Irregular (I); Not Available (NA)

INTERNATIONAL MONETARY FUND
Public Information Notice
EXTERNAL RELATIONS DEPARTMENT

Public Information Notice (PIN) No. 05/159
FOR IMMEDIATE RELEASE
November 30, 2005

International Monetary Fund
700 19th Street, NW
Washington, D. C. 20431 USA

IMF Executive Board Concludes 2005 Article IV Consultation with Trinidad and Tobago

On November 11, 2005, the Executive Board of the International Monetary Fund (IMF) concluded the Article IV consultation with Trinidad and Tobago.[1]

Background

Trinidad and Tobago's economy, which is endowed with large energy reserves, is experiencing a strong energy sector-based expansion. The energy sector already accounts for about 40 percent of GDP, over 80 percent of exports, and approximately half of government revenues. However, its contribution to employment is less than 5 percent. Within the Caribbean, Trinidad and Tobago has become a major financial center and a source of capital for regional entities. Trinidad and Tobago is one of the larger Caribbean nations in terms of GDP and population. Its energy wealth has enabled it to achieve one of the highest standards of living in the region. Nevertheless, income inequality and poverty rates are only at about regional averages.

Macroeconomic performance and financial developments are currently being driven by a highly favorable external environment. Surging oil prices have strengthened the external current account balance, financed an expansion of aggregate demand, and contributed to high levels of liquidity in the financial system. There are tentative signs that the economy is producing at, or near, capacity and inflationary pressures are emerging.

The economy is growing robustly and unemployment has fallen to historical lows. Real GDP grew by 6½ percent during 2004. While this is lower than the outturn of 13 percent growth during 2003, the latter was driven primarily by the coming on stream of some large energy projects. The nonenergy sector has remained vigorous, growing by just under 6 percent during

[1] Under Article IV of the IMF's Articles of Agreement, the IMF holds bilateral discussions with members, usually every year. A staff team visits the country, collects economic and financial information, and discusses with officials the country's economic developments and policies. On return to headquarters, the staff prepares a report, which forms the basis for discussion by the Executive Board. At the conclusion of the discussion, the Managing Director, as Chairman of the Board, summarizes the views of Executive Directors, and this summary is transmitted to the country's authorities.

2004 on the back of a surge in government spending financed by the oil bonanza. The latter has also led to a boom in construction. Under the official definition of unemployment, which includes some discouraged workers, the average unemployment rate stood at 8¼ percent in 2004, the lowest in decades.

The balance of payments is in large surplus, driven by exports, which rose by US$1.2 billion (10 percent of GDP) in 2004, significantly outpacing import growth and lifting the current account surplus to 14½ percent of GDP from 9 percent of GDP in 2003. While some of the higher current account receipts were offset by private capital outflows, the overall balance of payments surplus still doubled to US$0.7 billion (6 percent of GDP). With oil prices rising further, these trends are accelerating in 2005—the foreign assets of both the commercial banks and the central bank have continued to rise rapidly this year.

There has been a substantial widening of the nonenergy fiscal deficit (the overall deficit, excluding energy revenues) although the overall budget balance remains in surplus on account of buoyant energy revenues. The budget for FY 2005/06 envisages a significant further expansion of the nonenergy deficit, due to a reduction in nonenergy revenues (from lower income tax rates, and other changes to both direct and indirect taxes), as well as a further increase in non-interest expenditures. High energy prices as well as some recent changes to the energy tax regime should, however, lead to increased receipts from the oil and gas sector.

Monetary conditions have largely been accommodative, although signs of accelerating inflation have led to a recent shift toward tightening. The monetization of energy receipts by the government to finance the nonenergy deficit is the major source of liquidity injection into the financial system. Despite a sustained freeze of public utility tariffs and gasoline prices, headline inflation has crept up to 7 percent for the 12-month period ending in September 2005, up from 2¾ percent a year and a half ago. A significant part of this reflects movements in volatile food prices. Nevertheless, core inflation is also up and the Central Bank of Trinidad and Tobago (CBTT) has raised the benchmark repo rate on three occasions this year, each time by 25 basis points.

Financial markets have generally been buoyant in reflection of the ample liquidity. Insurance, pension funds, finance companies and mutual funds have all experienced rapid expansion, with mutual fund investments reaching roughly two-thirds of bank assets and stock market capitalization approaching 140 percent of GDP in 2004. The financial system as a whole increased credit to the private sector by 18 percent in 2004, a leap compared with single-digit annual growth since 2001. Banking soundness indicators generally improved in 2004.

Executive Board Assessment

Executive Directors noted the currently highly favorable external environment for Trinidad and Tobago and the benefits that were accruing from surging energy export prices and track record of strong economic policies. Economic growth was robust, unemployment was at historical lows, and government finances, as well as the balance of payments, were registering large surpluses. Financial markets had generally remained buoyant and credit ratings were up. Directors remarked that the current circumstances, where high energy prices were driving macroeconomic developments, provided a unique opportunity for Trinidad and Tobago to make significant progress toward securing sustainable high living standards for its population.

Directors noted that maximizing the gains from the energy windfall required a prudent mix of fiscal, monetary, and structural policies. Such policies should ensure that the public sector was getting value for its money and private sector competitiveness was maintained and enhanced. Directors considered that a careful balancing of priorities and policies was called for.

While mindful of the potential long-term benefits of reducing tax rates and increasing capital spending, Directors expressed some apprehensions about the recent significant expansion of the nonenergy fiscal deficit, i.e., the deficit excluding energy revenues. They noted that the plans for current spending needed to be assessed against institutional limitations and the economy's capacity to absorb the higher levels of expenditures. There were, in particular, emerging concerns about inflation and the risks of Dutch disease down the road. Directors also indicated that the expanding nonenergy deficit rendered the public finances vulnerable to sudden downward swings in energy prices.

Against this background, Directors called on the authorities to consider increasing the share of energy revenues that is saved. Noting the limited energy reserves, Directors underscored the importance of ensuring long-term sustainability of public finances. They also emphasized the benefits greater savings would provide in terms of helping shield the economy from the adverse consequences of a pro-cyclical fiscal stance, in terms of high inflation, loss of competitiveness, and a "boom bust" pattern of economic growth.

Directors praised the authorities' efforts to simplify the nonenergy tax regime to increase its efficiency and predictability. They indicated a preference, however, for a more gradual approach to the reforms, given their uncertain revenue and distributional impacts in the context of a widening nonenergy deficit, and the need to assure predictability about future tax levels for investors. Directors welcomed the intention to establish a Tax Policy Unit in the Ministry of Finance with a mandate for continuous reform of the tax regime.

Directors underscored the role of institutions in ensuring that the benefits from the current high oil prices were realized. In this regard, they welcomed the authorities' intentions to establish a permanent energy fund. Noting the importance of designing the fund well from the outset, Directors advised the authorities to avoid using the fund for extra budgetary spending and urged them to channel all public spending to compete for scarce resources within the standard budgetary process in parliament.

Directors welcomed the authorities' assurances that there would be adequate checks and balances on the special new agencies that were being set up to expedite expenditure execution. However, most Directors encouraged the authorities to consider reforming and restructuring the existing government apparatus, rather than setting up new entities. In any case, Directors suggested that a comprehensive public expenditure review (PER), carried out with external assistance, and a fiscal Report on Standards and Codes (ROSC) prepared with assistance from the Fund, could be useful inputs to policy-making at this time. They noted the potential benefits of these studies—the PER in helping identify ways to better target and focus public interventions; and the ROSC in helping strengthen budgetary management processes and accountability.

Looking forward, and given the strong external inflows and widening nonenergy fiscal deficits, most Directors advised a reconsideration of exchange rate policy to achieve greater exchange rate flexibility. Directors noted the pressures for a real appreciation and pointed to the limits to monetary policy alone successfully addressing these pressures in an environment of improving terms of trade and expanding fiscal nonenergy deficits, although increased investments abroad by the private sector would mitigate to a certain extent the appreciation pressures stemming from the strengthened current account position. They considered that in the absence of sufficient fiscal tightening or changes in private sector behavior, the choice was whether real appreciation occurred through inflation, which would have an adverse impact on poor households, or by other means.

Directors encouraged the authorities to take advantage of the current favorable economic environment to press ahead with structural reforms to support private sector led growth. In this regard, continued progress on utility prices, privatization, and labor market reforms will be critical. Directors praised the authorities' efforts to reform the financial sector. They welcomed the FSAP findings, urged the authorities to undertake the necessary legal reforms, and agreed that the Fund would help coordinate the necessary technical assistance following from the FSAP recommendations. Directors called on other technical assistance providers to extend support to the authorities' reform program. They concurred that the authorities' financial sector reform program, upon its successful completion, should help further secure Trinidad's position as the financial center of the Caribbean.

Public Information Notices (PINs) form part of the IMF's efforts to promote transparency of the IMF's views and analysis of economic developments and policies. With the consent of the country (or countries) concerned, PINs are issued after Executive Board discussions of Article IV consultations with member countries, of its surveillance of developments at the regional level, of post-program monitoring, and of ex post assessments of member countries with longer-term program engagements. PINs are also issued after Executive Board discussions of general policy matters, unless otherwise decided by the Executive Board in a particular case. The staff report for the Article IV consultation with Trinidad and Tobago may be made available at a later stage if the authorities consent

Trinidad and Tobago: Selected Economic Indicators

	2000	2001	2002	2003	2004
(Annual percentage changes)					
Output and prices					
Real GDP	7.3	4.2	7.9	13.3	6.5
Energy GDP	12.4	5.6	13.5	31.3	7.9
Unemployment rate (percent of labor force)	12.2	10.8	10.4	10.3	8.3
Consumer prices (end of period)	5.6	3.6	4.3	3.0	5.6
Money and credit 1/					
Net foreign assets	19.5	9.1	2.5	5.7	36.4
Net domestic assets	-13.6	3.5	0.2	-3.7	-17.6
Public sector credit (net)	-17.6	-7.2	2.1	-9.9	-24,7
Private sector credit	7.8	3.7	3.1	2.6	18,2
Broad money (M3)	5.9	12.6	2.7	2.0	18.8
(In percent of GDP, unless otherwise indicated)					
Public finances 2/					
Budgetary revenue	25.6	27.4	24.3	26.7	27.5
Budgetary expenditure	24.5	25.6	24.9	24.8	25.4
Overall budget balance	1.1	1.8	-0.6	2.0	2.0
Overall nonenergy budget balance	-6.6	-7.5	-6.3	-8.4	-9.2
Overall nonfinancial public sector balance	0.3	-0.5	-3.9	1.9	2.1
Public sector debt	55.1	55.0	58.4	54.7	49.1
External sector					
External public debt	20.5	18.5	17.5	14.9	11.3
Current account balance	6.6	5.0	0.8	8.9	14.5
Of which: exports	52.4	48.5	43.1	48.2	52.0
Of which: imports	40.6	40.4	40.5	36.2	39.7
Gross official reserves (millions of US$)	1,406	1,876	1,924	2,258	2,993
Terms of trade (percentage change, end of period)	20.7	-5.7	0.6	7.5	4.4
Memorandum item:					
Nominal GDP (in billions of TT$)	51.4	55.0	56.5	67.8	77.6

Sources: Trinidad and Tobago authorities; and IMF staff estimates.

1/ Changes in percent of beginning-of-period broad money.
2/ Fiscal year October–September. Data refer to fiscal years 1999/2000–2003/04.

Statement by Eduardo Loyo and Executive Director for Trinidad and Tobago and Charles de Silva, Senior Advisor to Executive Director November 11, 2005

High oil prices and increasing energy sector output have continued to provide the stimulus for expansion of the economy of Trinidad and Tobago, which marked eleven consecutive years of strong growth in 2004. More recent performance has been equally robust with forthcoming data expected to show growth in the first half of the year remaining in the region of the 6.5 percent seen in 2004.

Trinidad and Tobago's economic strategy has focused on escaping the historical narrow dependence on oil extraction through diversification of its energy sector. This has involved the intensive development of natural gas resources and the establishment of a large-scale petrochemical and other gas-based industries, a process which was deepened in 2004 with the start-up of two new petrochemical plants. This expansion in capacity helped to fuel a robust energy sector growth rate of 7.9 percent notwithstanding the fact that crude oil production fell significantly during the period. Non-energy sector growth also strengthened appreciably in 2004, though much of this dynamism derived from developments in the energy sector.

Although inflationary pressures were relatively subdued earlier in the year, a sharp pick-up took place in the fourth quarter of 2004 and has been sustained into the current year, pushing the 12-month headline rate to 6.9 percent by September. The acceleration is being fueled largely by food prices, which in September registered a 12-month increase of 23 percent compared with an increase of 2.6 percent in core (non-food) inflation. Rising import prices have also been an important factor in both food and non-food inflation.

The resurgence in inflation and the accompanying rise in inflationary expectations have prompted a shift in the central bank's monetary policy away from the accommodative stance in place since mid-2002. The bank increased its policy interest rate on three occasions in 2005, from 5 percent to 5.75 percent, triggering a rise of similar magnitude in commercial banks' prime lending rates and inducing increases in money market rates as well as in long-term interest rates. In explaining the policy shift, the bank also signaled concern about growing demand pressures in the foreign exchange market and the narrowing of interest rate differentials with the United States, which could increase incentives for capital outflows.

The robust growth of the economy has had a positive impact on the labor market, with the unemployment rate averaging 8.4 percent in 2004, down from 10.5 percent the previous year, while more recent data show the rate declining further to 8 percent in June. Heightened non-oil sector activity, particularly in the construction sector as the government accelerates its housing program, and the continuation of construction projects in the energy sector seem set to drive unemployment even further down in the months ahead.

With regard to capacity constraints, the authorities acknowledge that there has been a visible tightening of labor market conditions, which they see as a key source of vulnerability for the economy. In response, the government has been attempting to address labor constraints in various sectors of the economy through the importation of skilled personnel, including medical personnel to address shortages in the health sector. At the same time, firms in the construction sector have been importing skilled labor from the Caribbean area and other sources to meet existing shortfalls.

On the external front, booming energy prices and increases in export volumes in 2004 enabled Trinidad and Tobago to double the balance of payments surplus of the previous year. However, the capital account continued to reflect a deficit, partly as a result of the domestic capital market's expanding role as a regional supplier of funds. Reflecting the economy's growing strength, two major international credit rating agencies announced upgrades of Trinidad and Tobago's external debt ratings, from BBB+ to A- in the case of Standard and Poor's, and from Baa2 to Baa3 in the case of Moody's.

The Trinidad and Tobago authorities broadly share the staff's assessment of the outlook for the economy and of the challenges that lie ahead. While prospects for growth appear bright over the medium term, the authorities are mindful of the growing risks to macroeconomic stability and longer-term sustainability as the economy approaches the limits of its capacity. With signs of an inflationary takeoff already present in the economy, the authorities view containment of this trend as a key short-term priority and avoidance of Dutch disease risks as a critical medium-term challenge. On this latter score, they consider the threat of Dutch disease to be less severe than during the energy boom of the 1970s given the structural changes the economy has undergone since then.

Monetary policy remains firmly committed to maintaining domestic price stability, which the authorities acknowledge is shaping to be an increasingly demanding challenge in the context of continuing strong liquidity growth. The central bank intends to remain vigilant and to act decisively to mitigate inflationary pressures. The exchange rate will be managed to provide support to the goals of monetary policy and to respond flexibly to developments in the real economy. At the same time, the central bank, in conjunction with the Fund, is continuing to look closely at ways of addressing structural peculiarities in the foreign exchange market, including its highly oligopolistic nature, to enable it to function more effectively.

Notwithstanding the challenges ahead, the authorities are determined to capitalize on the opportunity offered by the present circumstances to raise the long-term growth potential of the economy, by scaling up the level of investment in human capital and in social and economic infrastructure. Education has emerged as a key focus of the 2005/06 budget, highlights of which included the introduction of free tuition for nationals enrolled at public tertiary institutions and plans for an ambitious program to construct three new campuses for the University of Trinidad and Tobago. The UTT was recently established to ensure an output of industry-ready graduates with specialized skills and to strengthen the focus on research and development activities that are relevant to the needs of the country and industry related. Whereas these expenditures would increase the non-energy deficit, especially in the short term owing to construction outlays, the improvement in the quality of the labor force is expected over time to contribute towards a more sustained development of the non-energy sector.

With the aim of accelerating infrastructural development in line with its long-term vision and increasing the rate of implementation of its investment program, the government proposes to outsource project management responsibilities for identified projects to fifteen special-purpose state entities. This approach will enable the government to address the challenges of skill shortages and cumbersome bureaucratic procedures that have traditionally constrained implementation of the PSIP, but is not intended as a permanent mechanism. The authorities have stressed their commitment to the highest standards of good governance, transparency, and accountability in the operations of these entities.

Our authorities fully share the view that raising the level of fiscal savings, as recommended by staff, is an important element of macroeconomic policy, and of the strategy to protect the budget from the volatility of oil prices and to share the benefits of the oil and gas patrimony equitably across generations. With this in mind, the government has reconceptualized its planned revenue stabilization fund as the Heritage and Stabilization Fund and has substantially increased the size of its contributions pending formal establishment of the Fund through enactment of legislation currently being prepared with the assistance of an international consultant. While in the 2005 Budget the government had undertaken to transfer TT$1.4 billion to the Interim Revenue Stabilization Fund, it in fact transferred TT$2,593 million compared to TT$1,263.2 million in 2004. This brought the balance in the Fund to TT$5439.0 million, equivalent to about US$907 million. For fiscal 2006 government has budgeted to deposit a further TT$1,862.8 million to the Fund.

Over the longer haul structural reforms of the non-energy tax regime are expected to impact positively on the productivity of the tax base and ultimately help to attenuate the expansionary effects of the non-energy deficit. As a first step, the government has moved to simplify the direct tax regime by the removal of most special purpose allowances and has identified as potential targets for reform some aspects of the indirect tax system that are inhibiting its performance, including the level of excise tax rates, the extent of zero rating under the VAT system, and the level of VAT refunds. The government is also actively considering recommendations to expand the tax base through the introduction of a comprehensive capital gains tax and a complete overhaul of the present property tax system. In addition, the 2005-06 budget announced the establishment, in the Ministry of Finance, of a Tax Policy Unit with a mandate that includes the continuous assessment of the tax regime in Trinidad and Tobago.

In the financial system, the authorities are in the process of implementing an ambitious and far-reaching program of institutional strengthening in line with the government's 2004 White Paper. A major focus of the reforms is the strengthening of financial sector legislation, improving regulation and supervision, and the development of a framework of cross-border supervision of financial conglomerates. The recently concluded FSAP has identified a challenging agenda which the authorities are committed to implementing as expeditiously as resources allow, and in this regard they have sought technical assistance from the Fund. Nevertheless, given resource and capacity constraints the authorities have stressed the need for prioritization and sequencing of reforms, in keeping with their own assessment of what may be feasible within given timeframes.

In closing, our authorities thank Management and staff of the Fund for their excellent support for Trinidad and Tobago and for the productive policy dialogue held in the course of the recent Article IV mission.