

I. THE ECONOMIC ENVIRONMENT

(1) MAJOR FEATURES OF THE ECONOMY

1. Trinidad and Tobago is a resource-based economy. The economy derives most of its income from oil and oil-based products and petrochemicals, although its dependence on this single commodity has declined as industrial diversification has been pursued in the last few decades. Proven oil reserves are estimated at 534 million barrels, about 12 years' supply at current production rates. Trinidad and Tobago also has significant deposits of natural gas (proven reserves are enough to last 55 years), on which it has based its petrochemicals industry. In addition to primary energy products, related industrial activities include oil refining, gas processing and the production of ammonia, urea, methanol, iron and steel. Total GDP in 1997 was roughly US\$5.8 billion (Table I.1).

Table I.1
Major features of the Trinidad and Tobago economy, 1996 and 1997

	1996	1997 ^a
Area: 5,130 square kilometres		
Population (thousands)	1,264.0	1,271.0
Population growth rate (%)	0.3	0.6
Labour force (thousands)	530.4	541.0
Unemployment	16.3	15.0
GDP at current prices (US\$ million)	5,653.4	5,843.4
GDP per capita (US\$)	4,472.6	4,597.5
Share in GDP (%)		
Agriculture	3.0	2.8
Industry	36.3	35.6
Petroleum sector	28.1	26.6
Manufacturing	8.2	9.0
Services	60.0	61.1
Construction	7.8	8.4
Distribution, hotel	16.1	17.0
Government	9.1	8.3
Financial services	11.3	11.5
Other services	15.7	15.9
Other	0.7	0.5
Merchandise exports f.o.b. (US\$ million)	2,506.0	2,427.0
Merchandise imports c.i.f. (US\$ million)	2,159.0	3,038.0
Merchandise exports to GDP (%)	44.3	41.5
Merchandise imports to GDP (%)	38.2	52.0
Non-factor services (US\$ million)	245.0	213.0
Exports of goods and non-factor services GDP (%)	52.6	49.4
Imports of goods and non-factor services GDP (%)	42.2	56.3

a Estimates.

Note: All figures are based on current market prices, unless otherwise stated.

Source: IMF, *International Financial Statistics*, (various issues).

2. Trinidad and Tobago imports some 75% of its domestic food requirements. Agriculture employs 9.6% of the labour force but contributes 2.3% to GDP. The main crops are sugar, coffee, cocoa and, more recently, citrus fruit. Manufacturing, despite attempts at diversification, continues to

depend heavily on petroleum-related industries, and employs around 8% of the labour force. The service sector is the major contributor to GDP and employment, the public sector being the dominant employer. However, as many state enterprises have been privatized, employment in the public sector has fallen from 30% of the labour force in 1987 to 25% in 1997.

3. After a period of fast economic growth between 1973 and 1982, triggered by the increase in oil prices, the economy of Trinidad and Tobago experienced a decade of contracting output and falling per capita income. In 1988, as a response to economic contraction, high unemployment, and the loss of foreign exchange reserves, Trinidad and Tobago introduced a programme of structural reform and liberalization, aimed particularly at restoring its external balance. The programme provided for the relaxation of price controls, improvement in financial intermediation, and a reduction of the public sector deficit, particularly through expenditure-cutting measures.

4. Structural reform has been strengthened during the 1990s: import duties have been reduced, and the role of the private sector in economic activity has been enhanced. However, due to the importance of the oil sector, there remains a large participation of the State in the economy: it is estimated that government consumption and investment represent between one fourth and one third of GDP. As a member of CARICOM, Trinidad and Tobago adopted in 1993 the Common External Tariff's (CET) four-phased schedule of rate reductions aimed at lowering the maximum rate for industrial goods from 35% to 20% by 1998.

5. The economy grew at an average annual rate of 1.7% between 1989 and 1997; population growth averaged 1.2% a year, implying annual average growth in per capita income of 0.5% for the period. Two distinct sub-periods can be identified: the first one of low or negative growth (1989-1993), and a subsequent sub-period (1994-97) with growth rates above 3%. The second sub-period coincides with an increase in the degree of openness of the economy, as evidenced by the implementation of the CET's four-phased tariff reduction programme, the removal of capital controls, the floating of the exchange rate, and the privatization or liquidation of public enterprises. GDP growth was 3.2% in 1997, and is expected to accelerate in 1998, reflecting the effects of massive investment in the oil/gas sector. The recent decline in oil demand and prices may temper, however, initial forecasts. By the end of 1997 unemployment had fallen from its peak levels but remained high at 13.5%.

6. Apart from oil and natural gas, Trinidad and Tobago has large deposits of asphalt, andesite, argillite, chromium, clay, copper, fluorspar, graphite, gypsum, iron, limestone, sand, and porcellanite. Among these, clay is the most abundant and extensively utilized. It also has one of the largest natural sources of asphalt in the world. There is a large variety of agricultural crops, exports of which are concentrated mainly in sugar, cocoa and, until recently, coffee. The main exports of processed products are beverages and preparations of cereals. Tourism is not as important as in other Caribbean islands (282,000 arrivals in 1995, and 3,874 hotel rooms), but the Government plans to enhance its contribution to economic activity. There are two major airports - the Piarco Airport in Trinidad and the Crown Point Airport in Tobago - which are owned and managed by the government-controlled Airport Authority of Trinidad and Tobago. The major sea ports are Port of Spain and Point Lisas, in Trinidad, and Scarborough in Tobago. The supply of water is adequate and electricity is mostly generated from domestically-produced natural gas. Constraints to growth have arisen in the past from a dependence on the oil sector, labour market rigidities and excessive government intervention in the economy. High unemployment is partly due to the capital-intensive character of some of the main production and export activities, especially oil/gas and mining which are encouraged by investment incentives.

7. One of Trinidad and Tobago's recent concerns is the effectiveness of monetary policy, since the extensive use of unremunerated high reserve requirements for banks is proving inadequate to prevent credit expansion. Open-market operations have been increasingly used to complement the effectiveness of reserve management. The strong inflow of foreign exchange as a consequence of oil-related investments is partly behind the increase in the money supply. Another factor is the enhancement of financial intermediation which has led to circumvention of legal reserve requirements and thereby to a higher money multiplier. The surge in private consumption spending, estimated at about 20% in 1997, is largely explained by credit expansion.

8. Imports and exports of goods and services together amount to over 100% of GDP, over 20% of which are exports of fuels. Foreign exchange receipts rely heavily on the oil/natural gas sector, with investment in that sector being the major force behind the strong capital account surplus (US\$837 million) posted in 1997. The concentration of exports in the oil/natural gas sector places Trinidad and Tobago in a vulnerable position to external shocks. Reliance on a single market, the United States, for almost half of its merchandise exports adds to this vulnerability. Attempts to diversify have resulted in a substantial increase in trade with other CARICOM countries which now absorb almost a quarter of total exports.

(2) RECENT ECONOMIC PERFORMANCE

(i) GDP and employment

9. Economic performance can be divided into three phases: the oil boom, lasting roughly from 1973 to 1982; a period of severe recession from 1982 to 1993 when per capita income fell to pre-1973 levels; and a period of growth since 1994, during which stabilization policies and an increased openness of the economy have succeeded in attracting foreign investment, particularly in the energy sector.

10. During the oil boom the economy grew by 5.5% a year, boosted by an improvement in the terms of trade. Nominal per capita income rose from US\$4,200 to US\$6,200; savings and investment averaged 30% of GDP. Meanwhile, industrial policy based on protection against imports focused on shifting manufacturing output towards products with higher value added. With the collapse in oil prices after 1982, the economy suffered over the next decade an almost uninterrupted decline in output. Per capita income fell by an average 5% per annum, returning to its 1973 level. Gross fixed capital formation fell from an average 22.6% in 1983-86 to 15.2% in 1987-93, having a negative effect on labour productivity and labour demand. Unemployment rose from 10% in 1982 to 22% in 1989. Output decline continued in 1992 and 1993.

11. Since 1994, the economy has recorded positive growth (Table I.2). In 1994 and 1995, export growth and private investment fuelled the expanding economy whereas in 1996, as direct and indirect taxes were cut, consumption overtook investment as the main impetus to growth. The decline in investment stopped in the early 1990s, and its share in GDP is estimated to have reached 21.8% in 1997. Gross national savings, however, have been declining since 1995, reflecting a sharp increase in consumer spending (estimated at over 19% in 1997) and an increase (until 1996) in net factor payments. The savings/GDP ratio, which stood at over 20% between 1994 and 1996, fell to slightly under 10% in 1997, well below the investment /GDP ratio. The large investment/savings gap posted in 1997 (the counterpart of which was a large current account deficit) was financed by external savings - mainly by foreign direct investment in the fuel sector.

Table I.2
Economic performance, 1992-97
(Per cent)

	1992	1993	1994	1995	1996	1997 ^a
Percentage change (based on 1985 prices)						
Real GDP at market prices	-1.6	-1.5	3.6	3.8	3.5	3.2
Private consumption	-2.2	2.3	-11.6	5.4	13.0	19.4
Government consumption	-2.7	-8.9	5.1	-0.6	-2.9	-8.2
Gross national investment	-24.8	3.0	44.7	-13.9	11.5	0.0
Exports of goods and non-factor services	13.2	-4.4	16.9	15.2	-6.9	3.9
Imports of goods and non-factor services	4.1	3.9	-9.6	16.9	13.4	50.6
Unemployment (annual average rate)	19.6	19.8	18.4	17.2	16.3	15.0
Consumer price index (1990=100)	6.5	10.8	8.8	5.2	3.4	3.7
Percentage of GDP						
Government finance						
Government revenue	26.3	27.6	25.8	27.0	28.1	27.1
Government expenditure	29.1	27.3	26.1	26.8	26.4	25.3
Government surplus/deficit(-)	-2.8	0.2	-0.3	0.2	1.7	1.8
Government domestic debt	21.7	21.9	19.0	20.0	18.6	22.3
Public external debt	40.7	45.8	41.6	35.9	33.2	26.1
Memorandum:						
Gross National Investment/GDP	13.8	14.3	20.2	16.0	17.2	21.8
Gross National Savings/GDP	14.4	12.0	24.8	21.0	18.4	9.6

a Estimates.

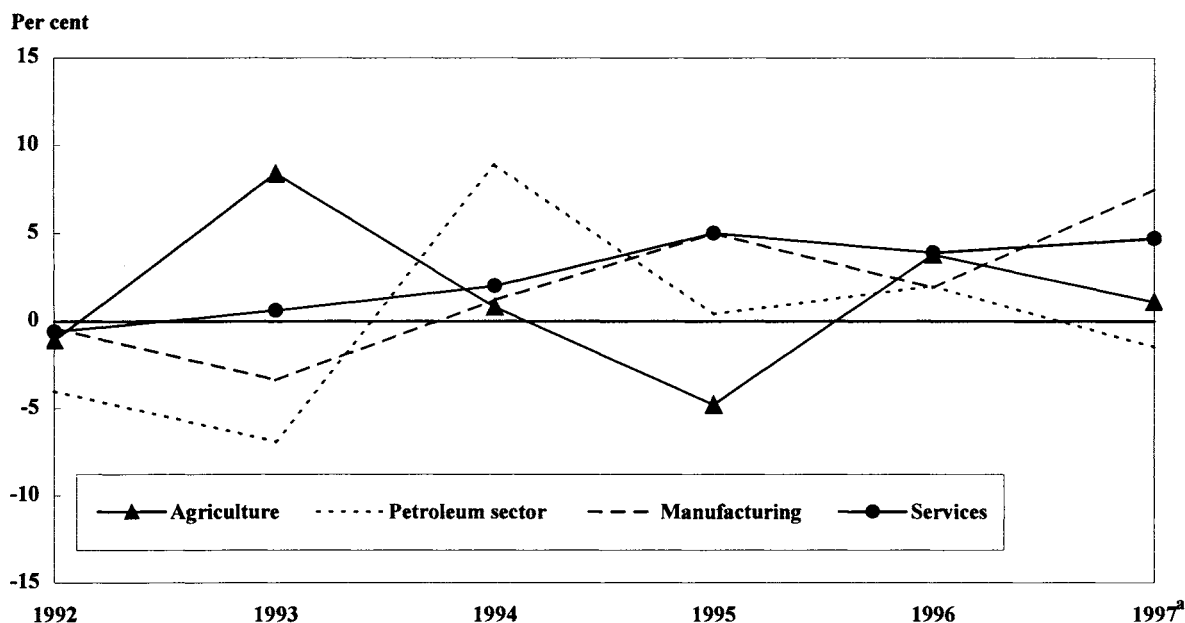
Source: IMF, International Financial Statistics (various issues).

12. While unemployment has been a persistent challenge for the Government, in the last few years, the more labour-intensive segments of the economy have outperformed the petroleum sector. By the fourth quarter of 1997, unemployment had fallen to 13.5%, the lowest level in 13 years.¹ This rate remains high, however, and is not likely to fall significantly in the near future because growth is expected to be concentrated mainly in the capital-intensive oil/natural gas sector.

13. The non-petroleum sector has performed in a more stable fashion, having achieved a fairly steady average annual growth rate of around 3.8% between 1994-97. The petroleum sector increased at an average annual rate of 2.4% in the same period, but annual growth rates were subject to large fluctuations (Chart I.1). In the non-petroleum sector the fastest growing activities were hotels, distribution, and construction. In the petroleum sector the most dynamic area was the production of petrochemicals.

¹ The average unemployment rate for the year was 15 %.

Chart I.1
GDP growth rates, by sector, 1992-97



^a Estimates.

Source: IMF, *International Financial Statistics* (various issues).

14. Tight fiscal and monetary policies, especially tight management of bank reserve requirements and other policies aimed at curtailing credit expansion, have proved ineffective in stopping a sharp increase in consumer spending, which accounted for some 75% of GDP in 1997. Imported goods, particularly motor vehicles and other consumer durable goods, account for a considerable part of this spending. The expansion in private consumption observed in 1997 has lowered the private savings GDP ratio to an estimated 2%. Spending on imported goods and services in the 1995-97 period grew at a faster rate than that on domestically produced goods; in 1997 alone, it is estimated to have increased by over 50% compared to the previous year. The real effective appreciation of the Trinidad and Tobago dollar observed in 1997 may have contributed to an expenditure-switching effect, leading to a greater increase in consumption of imported goods over domestically produced goods. This, together with lower export prices, resulted in a negative contribution of net exports to GDP growth of around 7%, reversing the trend of the previous year.

15. Although unemployment has increased throughout most of the 1990s, and productivity growth has been weak at best, real wages have risen.² Real wage increases are the result of skilled labour shortages, particularly in the oil refining sector³, strong union bargaining power, and wage indexation.

² As an example, real wages for all industries increased by 7 % in the first nine months of 1995, and by 5.1 % in the first nine months of 1996. Central Bank of Trinidad and Tobago (1997a), p. 9.

³ Real wages in the oil refining sector increased by 43.2% in the first nine months of 1995, and by 12.3% in the first nine months of 1996.

(ii) Prices

16. The rate of inflation has been falling since 1993, from an annual average of 13.1% to 3.7% in 1997, mainly as the result of the positive effect of trade liberalization measures, including tariff reductions, exchange rate stability, and the removal of the value-added tax (VAT) for certain food items. These positive effects have partly countered the inflationary pressure stemming from high wage increases.

17. Monetary and fiscal policies have also helped to keep inflation under control. The restrictive fiscal policy applied by the Government since the beginning of the 1990s has led to several years of central government surpluses. The current increase in consumption added to the relative ineffectiveness of monetary policy in curtailing credit growth could pose a future inflationary threat. However, tariff reductions under Phase IV of the CET (Chapter III(2)(iii)) could have a welcome effect in tempering inflationary pressures.

18. Since 1993, most price controls have been eliminated. Only the prices of sugar, pharmaceuticals and school books continue to be regulated. Maximum retail prices for drugs distinguish between imported and locally manufactured products (Chapter III (4) (vi)).

(iii) Monetary policy

19. The Central Bank of Trinidad and Tobago, established in 1964 by the Central Bank Act (since amended), is in charge of monetary policy and acts as lender of last resort to the Government. The Bank must report to and act under the authority of the Ministry of Finance, although this authority is seldom exercised.⁴ The Government is currently considering enhancing the Central Bank's independence. The main policy instrument for monetary control has been the use of high legal reserve requirements for commercial banks in order to sterilize the inflow of foreign currency associated with foreign direct investment. In addition, until the late 1980s, restrictions on consumer credit and a ban on borrowing by foreign corporations were applied. Local banks were not allowed to open foreign currency accounts for residents. Moreover, the Central Bank encouraged banks to lend to selected sectors at preferential rates; credit ceilings were placed on loans to state-owned enterprises. Beginning in the late 1980s, the Central Bank started to move away from selective intervention in credit markets while strengthening its prudential powers.⁵

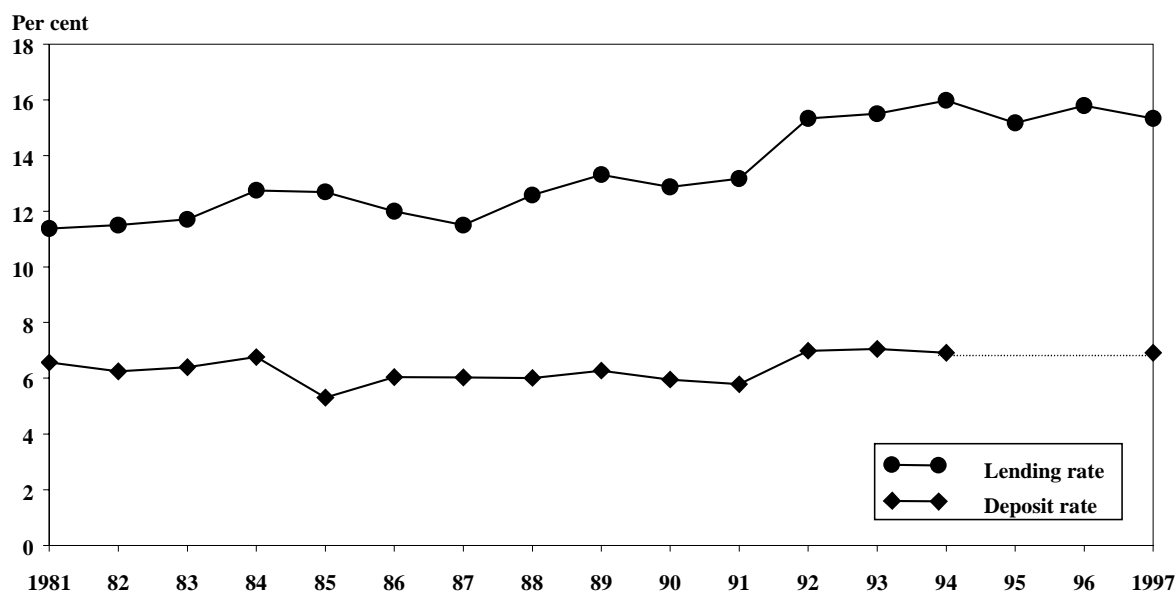
20. After the floating of the Trinidad and Tobago dollar and the removal of capital controls in 1993, monetary policy focused on exchange rate stability and low inflation. By early 1994, all selective credit controls and guidelines had been abolished. Open-market operations were launched in September 1996, an initiative aimed at reducing reliance on reserve requirements. Since the transition away from monetary controls, interest rates have become positive in real terms after many years of negative real rates of return on savings (which may help to explain Trinidad and Tobago's low savings rate) (Chart I.2).⁶

⁴ The Minister of Finance's authority to give the Central Bank a written directive in respect of monetary and fiscal policy has been exercised only once since 1964.

⁵ Clarke and Leon, 1996.

⁶ The spread between deposit and lending rates has been traditionally very high in Trinidad and Tobago (Chart I.2), as the market for loans is basically local and the costs of operating high reserve requirements is passed on to the customer. In 1997, the spread between loan rates and time deposits shrank somewhat, due to a reduction in the former and an increase in the latter. The existence of high spreads may be due to inefficiencies in the banking system.

Chart I.2
Deposit and lending rates, 1981-97



Note: 1995 and 1996 data for lending rates are not available.

Source: IMF, *International Financial Statistics* (various issues).

21. In an attempt to keep credit expansion under control, monetary policy was tightened further in 1997. The rate of unremunerated reserve requirements for banks was increased from 21% to 24% in the fourth quarter (it had been reduced by 2 percentage points at the beginning of the year), while the rate for non-banks was raised from 6% to 9%.⁷ The increase in reserve requirements was accompanied by open-market operations withdrawing TT\$100 million (US\$16.1 million) out of the financial system.

22. Although monetary policy was tightened in 1997, broad money M3 continued to expand at a rate exceeding 15%, well above the rate of inflation; liabilities to the private sector increased by 23%. Domestic credit continued to be the main source of money creation, despite tight reserve requirements, with credit extended to the private sector expanding by over 30%. There was also a steep increase in domestic financing of the Central Government. The accumulation of net external assets was another important source of money creation. To contain the expansion of the money supply, the Central Bank resorted heavily to open-market operations, increasing substantially (by over 70%) Treasury Bill holdings by the private sector and pushing up yields.⁸ Due to negative real

⁷The Central Bank estimates that the increase in reserve requirements for banks and non-banks amounted to withdrawing TT\$484 million (US\$77 million) from the system. Central Bank of Trinidad and Tobago (1997b).

⁸The average yield for Treasury Bills issued for open-market operations in the fourth quarter of 1997 was 10.84%, while the yield for those issued for the purpose of refinancing maturing treasury debt was 10.69%; both yields are above those observed in the second and third quarters of 1997. Despite the fourth quarter increase, however, annual Treasury Bill yields in 1997, at 9.8% on a weighted-average basis for both types of issues, were below average yields in 1996 which stood at 10.45%.

returns, banks have tended not to keep excess reserves.⁹ Interest rates remained high in real terms, but loan rates fell in the second half of the year while time deposit rates increased slightly.¹⁰

(iv) Exchange rate policy

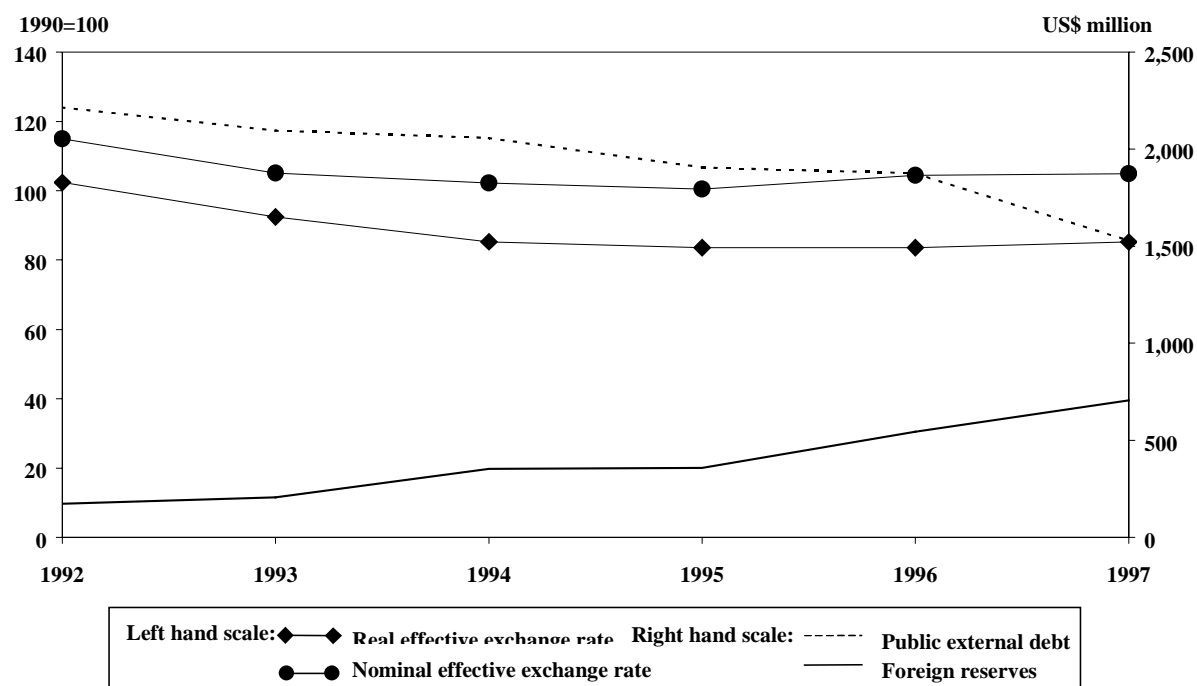
23. Until 1993, Trinidad and Tobago maintained a fixed exchange rate regime. In 1976, the Trinidad and Tobago dollar was pegged to the U.S. dollar at the rate of TT\$2.40 to US\$1. A system of exchange controls was in place, including the allocation of foreign exchange by the Central Bank. The exchange rate remained unchanged until the mid-1980s, leading to a real appreciation of the Trinidad and Tobago dollar. In 1985, the Trinidad and Tobago dollar was devalued (to TT\$3.60 per US\$1) and again in 1988 (to TT\$4.25 for US\$1). From 1988, the foreign exchange regime was gradually liberalized: net earners of foreign exchange were exempted from the allocation process starting in 1989, and the Government eliminated most restrictions on import payments by the end of 1990. From mid-1992, non-residents were allowed to open foreign currency accounts with local banks.

24. On 13 April 1993 the Trinidad and Tobago dollar went on to a managed float and was devalued by 26%. Following passage of the Central Bank Amendment Act of 1993, remaining exchange controls were removed and foreign investors were no longer required to obtain approval to repatriate capital, interest, dividends or capital gains. Capital account transactions were liberalized and Trinidad and Tobago accepted the obligations of the IMF's Article VIII, 2, 3 and 4 on 13 December 1993. In an attempt to curtail the "dollarization" of the economy, the Government imposed a 10% tax on interest earned on foreign currency accounts held locally by individuals. Foreign exchange transactions are conducted through authorized dealers, requiring a licence; foreign exchange dealers may be commercial banks or *bureaux de change*.

25. A goal of the Central Bank is to achieve nominal exchange rate stability. This goal has been largely achieved: between 1994 and 1997, nominal exchange rate fluctuations were generally less than 2% (Chart I.3). Due to the fact that inflation has remained subdued, movements in the real exchange rate have been moderate in that period. One of the Central Bank's key concerns has been to convince the main earners of foreign exchange to keep the market supplied on a regular basis. Insufficient supply of foreign exchange has led in the past to a trend towards depreciation of the Trinidad and Tobago dollar, with the Central Bank intervening to stabilize the exchange rate. In 1997, this situation changed because strong capital inflows led to an increase in the availability of foreign exchange. This resulted in a real effective appreciation of the Trinidad and Tobago dollar of around 2%.

⁹The average balances with the Central Bank/deposits ratio for commercial banks was 17.6 %, below the 21% statutory cash reserve requirement applicable in most of 1997. This included special deposits in the Central Bank, which are remunerated at 4%.

¹⁰Median loan rates were 15% in the second half of 1997, half a percentage point below rates in 1996 and three quarters of a percentage point higher than on the first half of 1997. The median rate for time deposits ended the year at 6.75%, compared to 6.44% in 1996.

Chart I.3**Selected indicators of external performance, 1992-97**

Source: IMF, *International Financial Statistics* (various issues).

(v) Public finances

26. During the oil boom, revenue from oil taxes provided the Government with the capacity to intervene on a large scale. Much of these revenues were used to subsidize public enterprises. After the fall in oil prices in the early 1980s, the Government tried to maintain expenditure levels despite reduced revenues. As a result, the public sector went into deficit, which was financed by the accumulation of external debt. With a further drop in oil prices in 1986 and the exhaustion of foreign exchange reserves by 1987, a strict regime of import licensing (Negative Import List) and foreign exchange controls was put into effect. As a part of the structural adjustment programme launched in 1988, the Government introduced a series of austerity measures intended to control expenditures and reduce the budget deficit: cost-of-living allowances for public servants were suspended, salaries reduced by 10%, government subsidies and transfers were cut, and the direct tax structure was modified. In 1992, the pace of structural adjustment was intensified with the revamping of taxation of the oil and natural gas sector to encourage exploration, and large scale divestment of public enterprises (Box I.1).

27. As a part of the programme of structural adjustment, a value-added tax was introduced in 1990 and, as a result, the revenue base has broadened. Customs duties were reduced in 1991, when the Common External Tariff was introduced; they were reduced further in 1993, 1995, 1997, and 1998. Since 1993, revenue collection has been much improved and, in the last few years, the maximum corporate and income tax rates have been lowered progressively. In 1996, the corporate tax rate was reduced from 38% to 35%, the same as the top marginal tax rate on individuals. The threshold for commercial suppliers subject to VAT was increased from TT\$100,000 to TT\$150,000 and the number of zero-rated foods was increased. Between 1993 and 1997 (except in 1994), the

Central Government balance has been in surplus.¹¹ Central Government revenue during the 1994-97 period remained stable at around 27% of GDP, of which 23 percentage points stem from non-oil revenue; expenditure averaged 26% of GDP in the same period. Income tax and VAT receipts accounted for over 50% of revenue. Customs duties accounted for 5.2% of revenue in 1996, increasing to 6.2% in 1997 following a rise in imports (section(3)(ii)).

Box I.1: Privatization

By the late 1980s, state-owned enterprises accounted for one fifth of GDP in Trinidad and Tobago. In May 1987, the Government appointed a team to review the performance and assess the viability and future prospects of public enterprises and make recommendations for their restructuring and reform. In 1990, 49% of the telephone company, Telco, was sold. As of 1 January 1992, the Government's portfolio of investments included shareholding in 87 enterprises with a value of TT\$6.5 billion. Of these 37 were wholly owned, 17 majority-owned, 2 minority-owned and 17 indirectly owned. In addition, the government held investments in the four statutory public utilities supplying water, power, transport and port facilities. State enterprises have been important contributors to the economy, accounting for 23.3% of GDP, 30.3% of capital investment, 9.8% of employment and 56.3% of foreign exchange earnings in 1992. Of the 87 entities in the Government's portfolio in 1992, 61 were slated for divestment or liquidation, 7 for restructuring and 19 were to be retained. As explained below, this goal has not been attained yet.

In 1993 the Government outlined the role of state enterprises, limiting state participation to areas of strategic importance such as oil and natural gas and to enterprises providing social services. The Divestment Secretariat, a unit of the Ministry of Finance but located in the Central Bank, was established in 1993 as the executing body for the government divestment programme. In the period 1992-97, the Divestment Secretariat was engaged in 36 assignments, including the national carrier BWIA International (51%), Fertilizers of Trinidad, Trinidad and Tobago Urea Company, Trinidad and Tobago Methanol Company, Iron and Steel Company, National Flour Mills (49%), Power Generation Company of Trinidad and Tobago (49%), Point Lisas Industrial Port Development Corporation (49%). Other companies partly or wholly privatized between 1993 and 1996 include Trinidad and Tobago Packaging and Printing, Trinidad and Tobago Fruit Processors, Airline Caterers, Trinidad and Tobago Cement, National Poultry, Trinidad and Tobago Mortgage and Finance Company, Maritime Life, National Fishers, National Television and Broadcasting, Reinsurance Company of Trinidad and Tobago, Shipping Corporation of Trinidad and Tobago, and Telecommunication Services of Trinidad and Tobago, among others. Much of the privatization has been effected by sales to foreign interests. As of 1 January 1998, the Government still had direct equity holdings in 36 enterprises, including the Petroleum Company of Trinidad and Tobago (Petrotrin), the National Gas Company of Trinidad and Tobago and Caroni. Petrotrin and Caroni, both of which ran heavy losses in 1997, remained completely in Government hands.

28. Public external debt declined between 1993 and 1997, from 45.8% of GDP to 26.1%. External debt service fell accordingly, from 30.8% of exports of goods and services in 1993 to 15.8% in 1997.

¹¹The overall public sector balance was in surplus between 1993 and 1996. In 1997, it registered a small deficit due to the losses incurred by Petrotrin and Caroni.

(3) EXTERNAL PERFORMANCE**(i) Balance of payments**

29. Until 1997, Trinidad and Tobago normally had a trade surplus, primarily from fuel exports. Imports have, however, been expanding much faster than exports during the 1990s, and in 1997 a trade deficit of US\$610 million was posted due to a strong increase in imported consumption and capital goods.¹² The capital-intensive nature of the oil sector has created an increasingly strong dependence on imported capital goods. Imports of goods represented 52% of GDP in 1997, heavily outweighing exports (41.5%) (Table I.3). Imports of merchandise expanded by 41% in 1997, while exports declined by 3%, mainly due to lower oil prices. Between 1993 and 1997, imports have more than doubled, while exports have increased by around 50%. Fed by the investment and consumption spending sprees and by the recent real appreciation of the Trinidad and Tobago dollar, import growth is expected to continue outpacing export growth, and a trade deficit, albeit smaller than in 1997, is forecast for 1998.

30. Traditionally, the balance of non-factor services posts a small surplus, primarily from travel and transportation. The traditional deficit in investment income reflects remittances of profits and dividends by oil companies and interest payments abroad. In 1997, the deficit declined, partly reflecting a reduction in interest payments on the external debt, and partly lower profit repatriation by oil companies.

31. The current account, in surplus for most of the 1990s, recorded a deficit of US\$708 million (12.1% of GDP) in 1997. The deficit is expected to be slightly lower in 1998. The structure of Trinidad and Tobago's capital account is dominated by direct investment flows. Private capital inflows which hovered between US\$200-US\$300 million a year during 1992-96, increased to US\$814 million in 1997. The total stock of foreign direct investment is estimated at nearly US\$4 billion or 75% of GDP.¹³ An additional US\$1 billion, related to gas exploration, is expected to flow into the country before the end of the decade. The capital account has registered a surplus since 1996, peaking at US\$619 million in 1997, leading to a substantial accumulation of net foreign exchange reserves, which stood at the equivalent to over four months of imports at end-1997.

(ii) Evolution, composition and direction of trade

32. Total merchandise exports in 1997 amounted to US\$2.4 billion, 3% below 1996 levels. The share of energy products (in value terms) is still high, but declining (from close to 93% in 1980 to 52.6% by 1996) (Table AI.1). For the same period, crude oil declined from 40% of total exports to 17.9%. Meanwhile, processed energy products have increased in importance. Manufactured goods, representing only 5% of exports in 1980, grew to 38.7% in 1996, led by petrochemicals, which account for two thirds of the total (Trinidad and Tobago is the second largest exporter of ammonia), and iron and steel, which account for a quarter. Export-to-production ratios of cement and steel, industries privatized some years ago, have improved significantly. Exports of chemicals more than doubled between 1985 and 1996.

¹²Imports of capital goods more than doubled in 1997, from US\$652 million to US\$1.4 billion, as a direct consequence of the investment boom in the oil sector.

¹³UNCTAD, (1997).

Table I.3
Balance of payments, 1992-97
(US\$ million)

	1992	1993	1994	1995	1996	1997 ^a
Merchandise trade balance	422.0	163.0	598.0	592.0	347.0	-611.0
Exports f.o.b.	1,622.0	1,662.0	1,972.0	2,477.0	2,506.0	2,427.0
Imports c.i.f.	1,200.0	1,499.0	1,374.0	1,885.0	2,159.0	3,038.0
Services, net	-355.0	-264.0	-370.0	-306.0	-270.0	-103
Non-factor services	89.0	61.0	43.0	159.0	245.0	213
Factor services	-444.0	-325.0	-413.0	-465.0	-515.0	-316.0
Current transfers, net	-16.0	-7.0	-6.0	-16.0	-7.0	5.0
Current account balance	91.0	-108.0	221.0	270.0	69.0	-708.0
Capital account, net	-139.0	89.0	-34.0	-36.0	36.0	619.0
Memorandum items:						
Current account balance/GDP (%)	1.7	-2.4.0	4.5	5.1	1.2	-12.2
Direct investment, net	177.9	379.2	516.2	298.9	356.3	979.7
Net official reserves	-83.0	74.0	262.0	296.0	510.0	688.0
Public external debt	2,214.90	2,096.0	2,058.0	1,905.0	1,876.0	1,527.0
Public external debt/GDP (%)	40.7	45.8	41.6	35.9	33.2	26.1
Debt service ratio (% of exports)	29.8	30.8	26.3	17.6	13.2	16.6
Exchange rate (TT\$/US\$)	4.3	5.4	5.9	6.0	6.0	6.3
Nominal effective exchange rate (Index; 1990=100)	115.0	105.1	102.2	100.5	104.4	104.9
Real effective exchange rate (Index; 1990=100)	102.4	92.4	85.3	83.6	83.6	85.2
Terms of trade (percentage change)	-6.9	-5.5	9.3	7.0	2.5	7.9
Trade balance/GDP	8.0	3.6	12.1	11.2	6.1	-10.5
Exports/GDP	34.4	36.3	39.9	46.7	44.3	41.8
Non-oil exports/GDP	18.3	19.4	24.6	26.1	22.9	24.0
Imports/GDP	26.4	32.7	27.8	35.5	38.1	52.3

a Estimates.

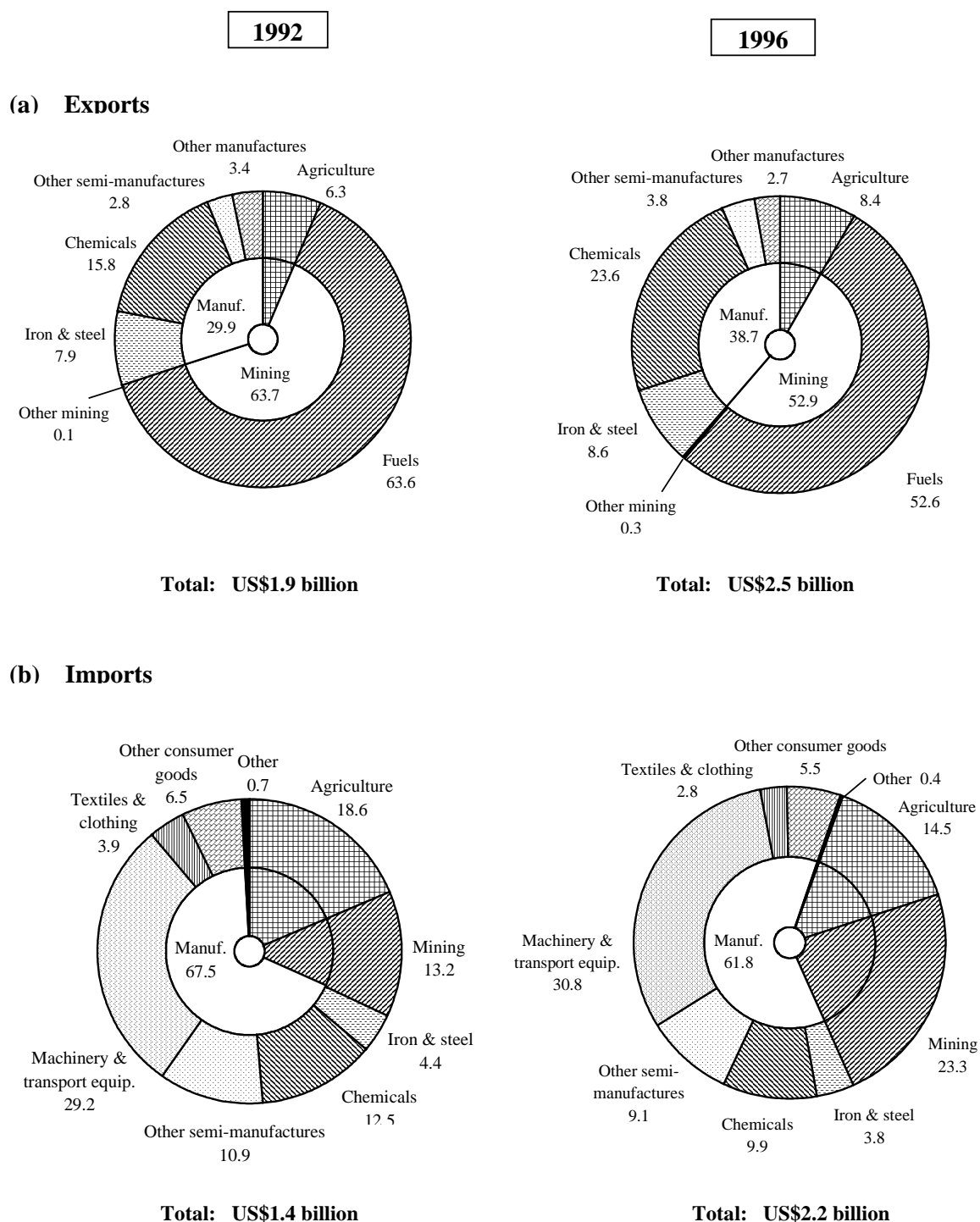
Source: IMF, *International Financial Statistics*, (various issues).

33. Imports (c.i.f.) were US\$3 billion in 1997, some 41% higher in value terms than in 1996. Import growth in 1997 was triggered by an increase in foreign direct investment and, to a lesser extent, by the real appreciation of the Trinidad and Tobago dollar. Imports of consumer and capital goods progressed rapidly in 1997 imports of motor cars were particularly dynamic. Almost two thirds of imports are manufactures, especially machinery and equipment (one third of the total). Trinidad and Tobago is also a large importer of agricultural goods and of fuels (for refining purposes) (Chart I.4 and Table AI.2).

34. Trinidad and Tobago's most important trading partner is the United States, accounting for 48.3% of exports and 38.1% of imports in 1996 (Chart I.5 and Table AI.3) CARICOM, especially Jamaica, is also an important market, absorbing almost a quarter of Trinidad and Tobago's exports, but supplying less than 4% of its imports. The European Union accounts for 10% of total exports and supplies 17.2% of imports.

Chart I.4**Product composition of merchandise trade, 1992 and 1996**

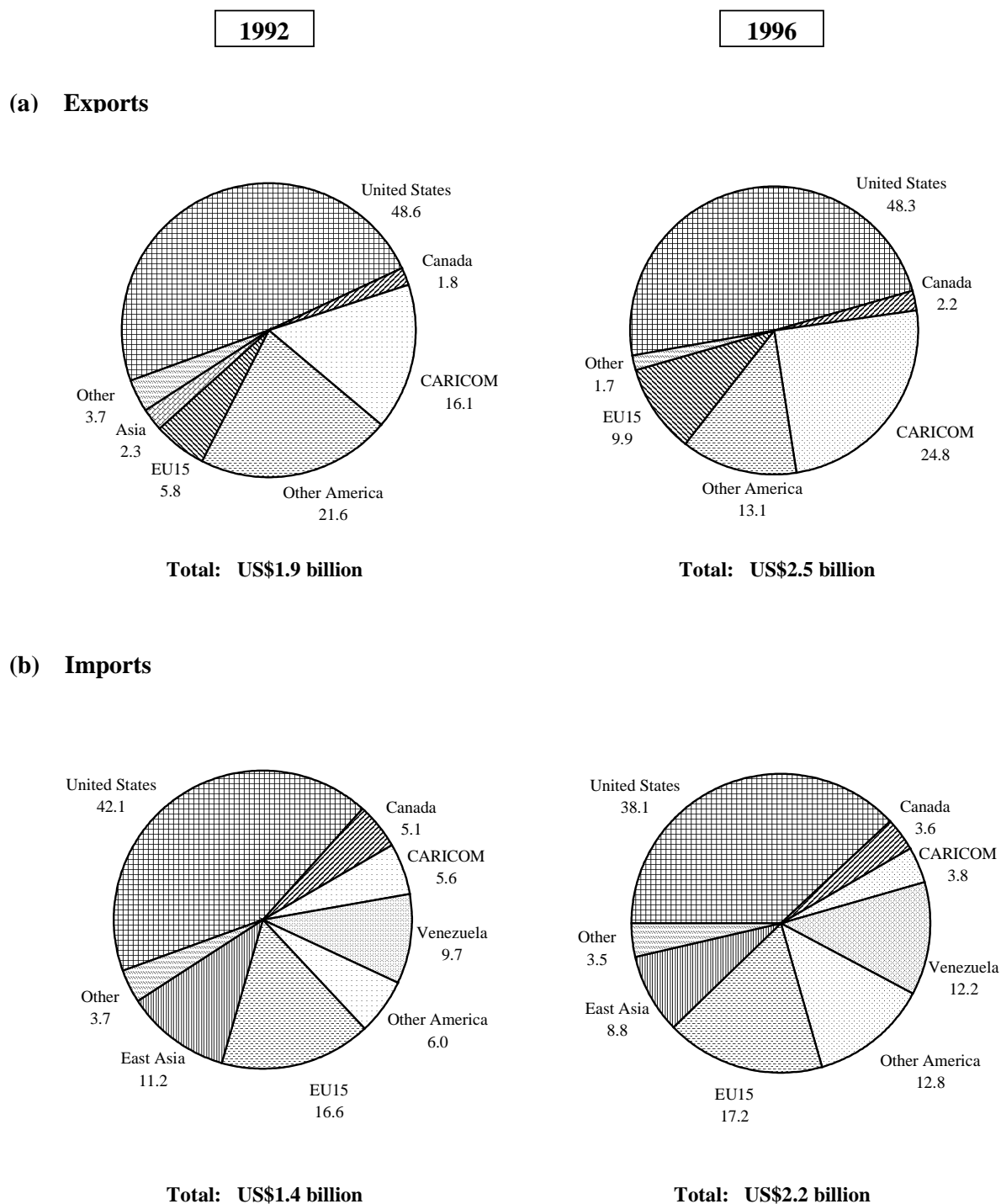
Per cent



Source: UNSD, Comtrade database (SITC Rev.1).

Chart I.5
Merchandise trade by main origin and destination, 1992 and 1996

Per cent



Source: UNSD, Comtrade database (SITC Rev.3).

35. Trinidad and Tobago has a trade surplus with CARICOM. The surplus was about TT\$3 billion in 1996, 16% higher than in 1995; imports were TT\$493.7 million, exports totalled TT\$3.5 billion. Figures for the first half of 1997 showed a surplus of TT\$1.7 billion. The main CARICOM trading partner is Jamaica, which absorbs almost 37% of Trinidad and Tobago's exports to CARICOM partners and supplies around 23% of its imports. Other important trading partners in CARICOM are Barbados and Guyana.

(4) ECONOMIC OUTLOOK

36. Lower oil prices should temper GDP growth, limiting it to 3-4% in 1998 and 1999. Lower growth will have an impact on consumption and imports, and will probably contribute to a reduction in the current account deficit in both 1998 and 1999; however, lower oil prices will mean lower export earnings, so the final effect on the trade and current account balances remains uncertain. If the effect on imports is larger, this will translate into lower demand for credit, which should enhance monetary policy effectiveness. The implementation of Phase IV of the CET will contribute to controlling inflation. Lower oil prices will affect oil-sector revenues and hence public finances, which are likely to post a deficit in 1998. Despite important investment inflows, unemployment is expected to remain high.