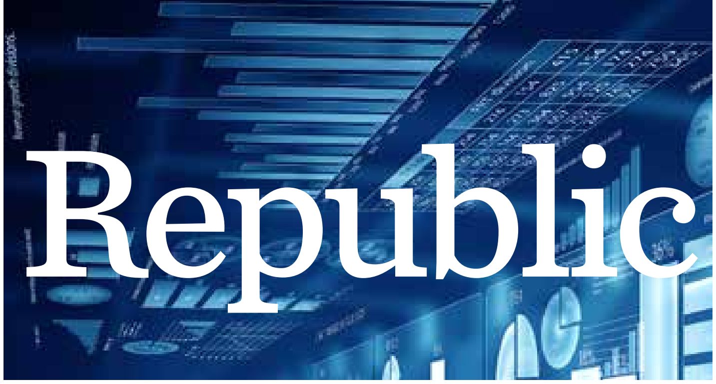

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Energy Sector Developments Generate Subdued Optimism

OVERVIEW

Against the backdrop of the ongoing travails of the domestic economy, the recent announcement by BPTT of two significant gas finds in its Savannah and Macadamia exploration wells is certainly welcomed news. While this development generated some optimism for the medium-term prospects for the economy, the current reality of the average citizen continues to be shaped by the weak performance of both the energy and non-energy sectors. Despite some improvement, conditions in the energy sector remain challenging, with continued gas shortages in the first quarter of 2017. In the non-energy sector, leading indicators suggest further declines in key industries during the period. Overall, Republic Bank estimates that economic activity contracted by 2 percent when compared to the last three months of 2016, while the unemployment rate rose to an estimated 4.2 percent. In this environment, the stock market has struggled to record consistent gains. After registering a two percent advance in the first three months of 2017, the Composite Price Index fell in April and May.

TRINIDAD AND TOBAGO KEY ECONOMIC INDICATORS

INDICATOR	2016	2016.1	2017.1 p/e
Real GDP (% change)	-2.3	-3.9	-2.0
Retail Prices(% change)	3.1	0.8	0.7
Unemployment Rate (%)	4.0	3.8	4.2
Fiscal Surplus/ Deficit ($M)	-8,986	-2,367.7	Deficit
Bank Deposits(% change)	4.25	2.5	Increase
Private Sector BankCredit (% change)	4.1	3.2	Decrease
Net ForeignReserves (US$M)	12,204	11,932.2	11,939.2
Exchange Rate(TT$/US$)	6.62/6.67	6.46/6.52	6.72/ 6.78
Stock Market Comp. Price Index	1,209.5	1,133.16	1,233.79
Oil Price (WTI) (US$ per barrel)	43.33	33.35	51.64
Gas Price (Henry Hub) (US$ per mmbtu)	2.51	2.00	3.01

Source:
Central Bank of Trinidad and Tobago, TTSE, EIA
p - Provisional data
e - Republic Bank Limited estimate

ENERGY SECTOR

As a result of weaker revenues, linked to continual gas shortages, Atlantic LNG moved to offer voluntary separation packages (VSEP) to its permanent employees, with the intention to reduce its staff complement by seven percent. The company indicated that severe gas shortages have resulted in facility utilisation rates of 70 percent during the last two years. In fact, with the fall in production, Trinidad and Tobago lost its position as the world's sixth largest exporter of liquefied natural gas to Algeria. Qatar remains the number one exporter, followed by Australia, Malaysia, Nigeria and Indonesia, in that order. Domestic natural gas production fell marginally, to average 3.3 billion cubic feet per day (bcf/d) during the first quarter of 2017, which is below the installed demand (4 bcf/d). The Henry Hub price of gas also fell by 3 cents to US$3.01 during the period. On the other hand, oil production rose by 3.2 percent to average 74,289 barrels per day, while the average West Texas Intermediate (WTI) price increased to US$51.64 from US$49.18 in the fourth quarter of 2016. In the downstream sector, production of ammonia and liquefied natural gas (LNG) fell by 5.2 percent and 0.4 percent, respectively, while methanol production increased by 1.7 percent. At the same time, traditional gauges of exploration activity recorded conflicting results, with depth drilled increasing by 32.4 percent and rig days falling marginally to 562. On the positive side, BPTT's Savannah and Macadamia finds are estimated to hold a total of 2 trillion cubic feet (tcf) of gas and are expected to provide a boost to domestic supplies within five years, after the production from Juniper and Angelin wanes.

NON-ENERGY SECTOR

With continued reports of retrenchment and the poor performances of specific leading indicators, conditions in the non-energy sector continue to be very challenging to say the least. In distribution, new motor vehicle sales (a gauge of sector activity) decreased by 26.6 percent in the first quarter of 2017, when compared to the fourth quarter of 2016 and by 25.5 percent year-on-year (y-o-y). Similarly, construction sector activity cooled during the period, as cement sales fell 5.7 percent from the levels recorded in the last three months of 2016 and by 16.6 percent y-o-y. In terms of job losses in the non-energy sector, some companies in the banking, telecommunications and other industries have taken action in the first half of 2017 to cut staff levels, or announced plans to so do in the near future. The government, in its efforts to streamline its expenditure has moved to restructure or wind up certain state enterprises, including Caroni Green Ltd and the Tourism Development Company.

FISCAL POLICY

According to the 2017 mid-year budget review, the government incurred a budget deficit estimated at $5.4 billion during the first six months of the fiscal year (October 2016-March 2017). The deficit was financed by a US$251 million (TT$1.7 billion) drawdown

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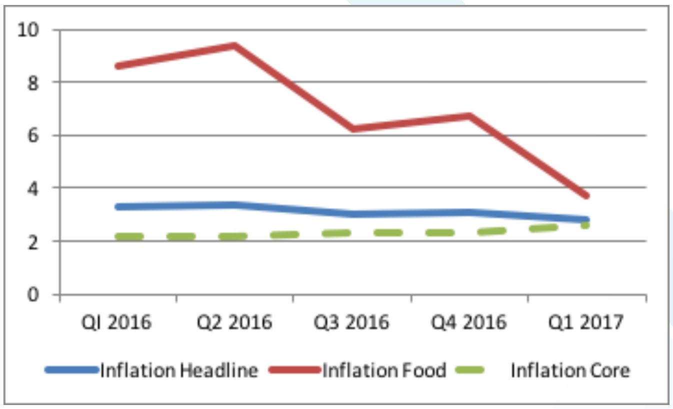
from the Heritage and Stabilisation Fund (HSF) made in March and by government borrowing, including a $1.5 billion, 6-month, 1.7 percent fixed rate bond, issued in March. During the first half of the fiscal year, government was unable to reach its expected revenue targets, as delays in the sale of public assets caused capital revenue to fall short of the $6.3 billion mid-term target. In addition, VAT collections were $699 million below initial projections.

MONETARY POLICY

In its May 2017 Monetary Policy Announcement, the Central Bank's Monetary Policy Committee (MPC) highlighted the need to facilitate growth in the domestic economy. Accordingly, the MPC decided to maintain the Repo rate at 4.75 percent. This action was supported by the fact that inflation remains at moderate levels, with the headline rate reaching 2.8 percent y-o-y and core inflation recorded at 2.6 percent in March (Figure 1). Nevertheless, with interest rates on the rise in the US, the MPC did acknowledge that the narrowing of interest spreads between Trinidad and Tobago and the US has implications for the domestic balance of payments. As such, the Central Bank of Trinidad and Tobago (CBTT) will continue to monitor international and domestic developments.

Figure 1: Inflation (%)

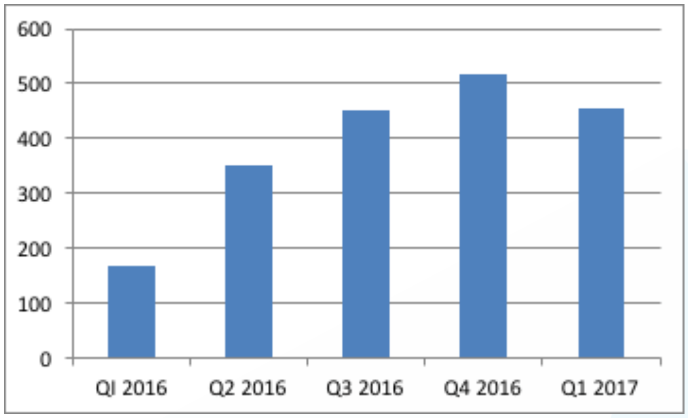


With the Repo rate unchanged, the commercial banks' average prime lending rate remained at 9.08 percent in March 2017, while the mortgage market reference rate (MMRR) stayed at 3 percent. However, the demand for credit continued to slow during the first quarter of 2017, as loans by the consolidated financial sector to businesses declined by 0.7 percent y-o-y in March. Reflective of weak credit demand, financial system liquidity remained fairly high during the first quarter of 2017. Commercial banks' excess reserves, which averaged $3.5 billion in the fourth quarter of 2016, rose above $4 billion in late March, before averaging $3.4 billion in April.

RESERVES

The US$251 million drawdown from the HSF would have provided a boost to the country's reserve position, but given the overall supply/demand dynamics, the market for foreign currency remains very tight. During the first three months of 2017, the net sale of foreign currency fell by 12 percent from the previous quarter to US$455 million, but was significantly above the US$168 million recorded during the same period in 2016 (Figure 2). In the same period, the country's currency depreciated by 1 cent against the US to average TT$6.78 per US$1. The level of foreign currency reserves represented by the net foreign position, remained stable, measuring US$12.2 billion, as it did in December 2016.

Figure 2: Net Sale of Foreign Currency



OUTLOOK

With the start-up of BPTT's Trinidad Onshore Compression project in the second quarter of 2017 and with production at the company's Juniper platform expected to begin late in the year, domestic gas production is expected to receive a boost in the second half of 2017. While this is expected to impact positively on the energy sector and the wider economy, it is not envisaged to completely resolve the supply shortages. In the non-energy sector, the recent resumption of work on the Point Fortin Highway extension project provides optimism that some momentum can be gained in public sector construction activity. Such impetus could be critical to the sector, with distribution expected to remain in the doldrums for the remainder of the year. Restoration work to address the damage inflicted by Tropical Storm Bret could also provide some thrust for the economy. However, the losses suffered in the agriculture sector as a result of flooding is likely to cause some acceleration in inflation. Overall, fragile growth is expected during the second half of 2017, although a flat performance will not be a surprise.

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Navigating the State of Flux

It is said that the only constant in life is change. If that is the case, then life has been pretty constant, because changes abound. After a tumultuous 12 months, book-ended with shock election results, the UK together with the European Union have begun the uncharted process of negotiating an economic separation. With both entities also facing seemingly incessant terrorist attacks, one gets the sense that they are being pushed to a tipping point. We just do not know what the tipping point leads to. In the Middle East, Qatar is in the third week of a blockade by neighbouring Gulf states and in the West, no one can say with even the slightest bit of certainty, how the Trump administration in the US will act or react to domestic and global issues. It is like everything is up in the air, and no one knows how things will eventually settle. What of regional states in all this? How are Caribbean countries to navigate this state of flux?

BARBADOS

The economy grew by an estimated 2 percent in the first quarter of 2017, down slightly from the 2.3 percent in the corresponding 2016 period. The 2016 tourism trend continued, with an 8.2 percent increase in arrivals registered for the first 4 months of 2017, as a strong increase in US and Canadian visitors more than offset declines from the UK and Germany. The industry may be losing its competitive edge however, as in 2016, Barbados slipped 12 places from 46th to 58th out of 141 countries in the World Economic Forum's Travel & Tourism Competitiveness Index. The construction sector expanded by an estimated 2 percent in the first quarter of 2017, due in part to various commercial projects such as the Sandals Royal. All other sectors made only modest contributions in the first quarter.

For the fiscal year April 2016 to March 2017, the deficit of 6.3 percent of GDP, though high, was an improvement over the 8.2 percent recorded in the previous year. As at March 2017, Gross Public Sector Debt stood at $9,111 million, equivalent to 98.5 percent of GDP. At that time international reserves stood at $705.4 million, having grown by $24.3 million during the quarter. By May 25th, international reserves grew a further $45 million to reach $750 million. On May 30th the Financial Statement and Budgetary Proposals for 2017/2018 were presented. The key revenue generating measures proposed were an increase in the National Social Responsibility Levy from 2 percent to 10 percent, and a 2 percent commission on foreign exchange transactions including wire transfers, credit card transactions and over the counter sales.

CUBA

Following a year of contraction and reduced oil supply, due largely to Venezuela's ongoing challenges, Cuba is pushing on with various counter-measures. The authorities are actively trying to explore zones that might produce oil, and have secured imports from other sources such as Russia. In late March, the government approved the construction of a new hotel and golf complex that will permit foreigners to purchase condominiums on the site. Cuba currently has just one 18-hole golf course as no new golf courses have been built since the Cuban revolution in 1959. Plans for the construction of 12 new golf courses on the island, therefore represent a notable turnaround in the state's attitude towards foreign tourism. In June, Swiss-based Kempinski Hotels SA inaugurated its Gran Hotel Manzana in the heart of Havana, billing it as Cuba's first true luxury hotel. More of such hotels are under construction in order to meet growing demand. Cuba's Tourism Minister Manuel Marrero said in May that more than 4.2 million tourists were expected this year, up from 4 million in 2016. He indicated the country was adding 2,000 hotel rooms a year to its stock of 65,000 hotel rooms and 21,000 homes renting to tourists. This optimism may be somewhat misplaced however, as on June 16th the US government adopted a tougher stance on Cuba, with President Trump announcing plans to tighten rules on Americans travelling to Cuba and to significantly restrict US companies from doing business with Cuban enterprises controlled by the military.

GRENADA

Grenada's economic growth of 3.9 percent in 2016 was driven largely by strong construction activity and a solid, tourism sector performance. After increasing by 5.1 percent in 2015, stay-over arrivals grew by a relatively modest 2.6 percent last year, as flat Canadian arrivals and declining numbers from Europe, were offset by a 10.7 percent jump in US arrivals. Early indications are that the moderating trend continued into 2017, with arrivals for January and February 0.8 percent lower than the same period in 2016. Nonetheless, the sector should receive a boost with the start of JetBlue airline's service from New York to the island in June.

In May, the International Monetary Fund (IMF) completed its sixth and final review of Grenada's performance under the Extended Credit Facility (ECF) arrangement. The IMF found that all targets to the end of March 2017 were met, and Grenadian authorities succeeded in restoring fiscal sustainability and strengthening the financial sector. A fiscal surplus equivalent to 2.4 percent of GDP was achieved in 2016 and there was a big turnaround in private sector credit, from a 3.8 percent contraction in 2015 to growth of 4.1 percent last year. This, along with a greater push to restructure public debt in recent months, saw Grenada's debt to GDP ratio decline to 83.4 percent at the end of 2016. Average inflation for 2016 rose to 1.7 percent and unemployment inched down, but still remained high at 28.6 percent. Commercial banks' prime lending rate remains at 6 percent.

GUYANA

Overall economic growth of 3.3 percent for 2016 was achieved largely due to the 45.5 percent growth in mining sector output, based on very strong gold production. Average inflation moved into positive territory, registering a modest 1 percent and unemployment was estimated to be about 8 percent at end-2016. Conditions remained positive in the first quarter of 2017, with the construction sector experiencing improved public sector project execution, but weak home construction. Gold output increased by 0.5 percent, with greater production from smaller miners offsetting an overall decline from the major producers. While rice production grew by over 50 percent, the sugar industry's woes continued, with the sector contracting by almost 34 percent in the first three months of this year. Notwithstanding the importance of the mining sector, the significance of the sugar industry was underlined on May 27th when Finance Minister Winston Jordan alluded that Guyana's 2017 growth projection figure may have to be revised due to 'developments' in the sugar sector. Commercial banks' prime lending rate remains at 13 percent.

In June the government of Guyana granted ExxonMobil approval to proceed with the development of Phase One of the Liza oilfield, located in the Stabroek Block. The US$4.4 billion project is expected to be finished by 2020, when it will begin producing around 120,000 barrels of oil per day.

SURINAME

With the intensification of multiple shocks from 2015, most of Suriname's economic indicators deteriorated significantly in 2016. The IMF estimates that Suriname's economy contracted by 9 percent in 2016, and its debt-to-GDP ratio increased to 68 percent. However, with the opening of the Newmont Merian gold mine in October, and a slight improvement in commodity prices in recent months, conditions have improved slightly thus far in 2017. Prices rose by just 0.5 percent in February compared to January, bringing annual consumer price inflation to 45.1 percent, down from 48.7 percent in January and 52.4 percent in December 2016. Owing partly to the mine's foreign currency earnings, the Suriname dollar has become more stable, with the early April rate of Sr$7.61: US$1, only moderately weaker than the end-of-2016 rate of Sr$7.4: US$1. Reflecting new borrowing, as well as some recovery in commodity prices, foreign reserves have also started to recover, registering US$399 million at the end of February, up from a December figure of US$381 million and a low of US$213 million in May 2016. Although the fiscal deficit narrowed in 2016 to 7.5 percent of GDP from 9.1 percent in 2015, government's finances remain under pressure, as various groups, such as teachers continue to press for pay increases. Many fiscal tightening measures recommended by the IMF have not been implemented and there are growing questions over the government's willingness to implement such a package, particularly in light of the other sources of finance received by Suriname over the last 12 months. Currently, payment of a second tranche of financing under the IMF stand-by agreement has been delayed.

REGION

In Jamaica, the first quarter of 2017 was flat, as growth in the manufacturing and finance industries was outweighed by decreases in the mining and quarrying industry, and the agriculture, forestry and fishing industry. The country's hotels and restaurants industry grew by 0.3 percent, reflecting increases in stopover arrivals (0.1 percent) and cruise passenger arrivals (3.2 percent). Total visitor expenditure increased by 3.7 percent to US$759.3 million. The buoyancy in tourism continued, as in mid-June Jamaica welcomed its millionth stopover visitor, two weeks earlier than projected. The sector reported earnings of over US$1.2 billion for the year thus far. After a largely positive performance in 2016, 2017 has been more difficult thus far, for the members of the Organisation of Eastern Caribbean States (OECS). Of the six countries for which data is available, only St. Lucia recorded an increase in stay over arrivals during the first quarter. During the period, St. Lucia was the only country in the group to record increased arrivals from all major markets.

OUTLOOK

Despite the lackluster start to 2017, tourist arrival numbers are likely to be solid for the rest of the year, led by strong growth in the US market. Despite continued low oil prices, global conditions may be somewhat less accommodating towards the end of the year, as some food commodity prices are on the rise, and there will be increasing upward pressure on interest rates, as the US raises its benchmark rate. With many regional states being largely single-engine economies, growth is expected to be moderate as opposed to spectacular. In this regard the tourism-based economies should fare better than the commodity exporters, although the gap between them will be narrower as the latter group slowly recovers from the annus horribilis that was 2016.

GLOBAL THREATS

Regional Opportunities

The phrase, "the world is changing", has become an all too familiar cliché. Nevertheless, it remains relevant in this period of uncertainty. As global events unfold, there is a sense that the world is changing rapidly and the level of unpredictability associated with these changes are quite frankly, leaving many of us perplexed.

Looking back, the 2008 International Financial Crisis (IFC) was considered to be a major world-changing event. Labelled as one of the largest financial shocks since the Second World War, to this day, the world is still languidly recovering from its after-effects. Global economic growth of 3 percent is considered to be recessionary and with growth averaging 3.3 percent during the seven years post-IFC period compared to 4.4 percent seven years pre-IFC, it is safe to say that we are not out of the woods yet. Turning our attention to the present day, the constant flow of new global threats may not equate to the IFC, but could create a high level of uncertainty and further impede global recovery. While some economic sages and financial experts are painting a dystopian future with regard to the myriad of global threats, this article will veer from pessimism to show the silver lining in every cloud from a Caribbean perspective. In short, every global threat provides an opportunity for the region.

The global oil market is changing and there are signs that the Organization of Petroleum Exporting Countries (OPEC) is losing its stranglehold on the global oil market. OPEC's decision to extend the production cut until March, 2018, is nothing more than a stopgap, as the resurgent US shale industry and output from other countries (excluded from the OPEC production cut) will continue to add to the current global oil inventory. However, while the supply has been the cynosure of the global oil market, not enough attention has been paid to global demand. With China transitioning from more energy and carbon intensive industries to a more low-carbon service-oriented economy, the global demand for oil has been declining. Moreover, this trend is likely to continue with an increasing number of countries making strides in renewable energy and other greening initiatives. So is this high supply-low demand the 'new normal' for the global oil market? If this is the case, then this low oil price environment would most likely persist longer than anticipated.

While this situation is a ray of sunshine for the tourism-dependent countries in the region (which are net-importers of oil), it does not bode well for energy producing countries like Suriname and Trinidad and Tobago. But, there is gold among the dross and these nations can use this as the perfect opportunity to focus on diversification. This situation can also encourage better prioritisation of public sector projects and discourage the misuse of government revenue derived from the energy sector. Put simply, wastage is a luxury that cannot be afforded at this juncture.

Protectionism and anti-globalisation are also generating some geopolitical headwinds. The 'Brexit' vote and US President, Donald Trump's 'America first' mantra are just the tip of the iceberg, as global terrorism threatens to add fuel to the anti-globalisation fire.

Despite the recent quelling of far-right parties in Europe and British Prime Minister, Theresa May now leaning towards a softer 'Brexit', tensions are still high following the recent terrorist attacks in the UK. But what are the implications for the Caribbean?

Protectionism translates into closed borders and this inevitably leads to less global trade. This is not the most favourable situation for a region that is just too small to grow independently from North-South and South-South trading (The North market represents developed countries whereas the South market refers to developing countries). There is also the possibility for less global aid for the region in light of the US President already proposing cuts to foreign aid for Africa, Latin America and the Caribbean. With spill-over effects from the ongoing migrant crisis in Europe and the current Venezuelan crisis, there have been reports that refugees are now seeking haven in the Caribbean. This would invariably create a financial burden for a region that is already characterised with low growth, high debt and wide fiscal deficits.

In the midst of these possible threats, the Caribbean could turn this adversity into an advantage. Instead of waiting to see the outcome of 'Brexit' and the possible adverse effects on trade, the region could proactively seek new trading partners. Finding the delicate balance in openness to trade, while improving our economic and political governance would help to boost growth and lower the probability for economic volatility. Less aid funding may seem unfavourable, but this could provide the right motivation for the Caribbean to improve its credit ratings. Some creditors are unwilling to lend to the region due to poor international credit ratings. This situation can be reversed if there are improvements in debt sustainability, fiscal management and data collection. The ominous global refugee crisis could also spur the region to protect its own house. As the local saying goes, "If your neighbour's house is on fire, it would be wise to throw water on yours". Heightened border security and proper vetting of foreigners are just a few measures we can take to protect our already porous borders. It may sound a bit farfetched but prevention is always better than a cure, so let us not wait for a catastrophic event to prompt us into action.

Global de-risking trends are also posing some challenges for the region. The decline in corresponding banking relationships (CBRs) could negatively impact countries like Jamaica, which is dependent on remittances (remittances contributed to 16 percent of GDP in 2015). International credit rating downgrades, restrictions in credit and limited access to foreign direct investment and international trade are just some of the other threats associated with de-risking. Nevertheless, the Caribbean can see this as an opportunity to improve its reputation with the rest of the globe by significantly enhancing its efforts to combat drug-trafficking, money laundering and other criminal activities which are creating many social ills for the region.

Currently, twelve (12) Caribbean countries have inter-Governmental Agreements with the US, with five (5) having officially signed and one (1) agreed in substance. Thirteen (13) territories have been labelled as compliant with the Organisation of Economic Co-operation and Development (OECD) Global Forum on Transparency and Exchange of Information for Tax Purposes, and seven (7) have already committed to the OECD's Common Reporting Standards (CRS). These are all positive steps, but more can be done through ongoing reforms specific to the banking sector, such as the adoption of a supervisory framework like Basel II. Continued enhancements to the Anti-Money Laundering and Combating the Financing of Terrorism (AML/CFT) framework, as well as improvements in governance would help reduce the incidence of de-risking in the region.

The evolving global oil market, protectionism, global terrorism and de-risking are just some of the major global threats that could provide downside risks for the region. Given the region's track record, it could be said that taking advantage of the opportunities identified above, would be a daunting or unrealistic task. This and other constructive counter-arguments should not be casually dismissed, as these could spur healthy debate, which is key to problem solving. Perspective is also important. Yes, the dangers are real, but we need to find the middle ground in avoiding the ostrich effect or any pessimism biases. Global threats must not deter us from seeking opportunities to remain resilient, creative and to adapt in this period of global uncertainty.