



## New Year CHALLENGES

*As* a New Year dawns it is helpful not only to be reminded of the achievements of the past year but perhaps more importantly to ponder on the challenges, which undoubtedly lie ahead. This applies no less to businesspersons and policy makers as it does to people in general. The importance of pondering the challenges ahead as far as the economy is concerned, is in order to implement appropriate action. Such action must (i) benefit from lessons learned from the previous year and (ii) help mitigate the worst effects of adverse shocks to the economy and society in the coming year.

Few will argue with the view that based on well-established criteria the Trinidad and Tobago economy performed well during the last twelve months. In 2007, output grew at an estimated 5.5 percent and the unemployment rate fell to approximately 6.0 percent. Net international reserves, excluding the Heritage and Stabilisation Fund, rose to US\$6.2 billion at the end of September 2007 or over nine (9) months of import cover. The country's external debt ratio fell further to approximately 5.6 percent and even the inflation rate was lower. In short, during the course of the year energy prices rose and so did government revenues and expenditures, employment, wages and salaries and in most cases profits as well. Even the international agencies, including the International Monetary Fund (IMF), were high in praise of this country's achievements.

This buoyancy was partly sustained on account of a 24 percent rise in fiscal injections in 2007, which translated, into a higher non-oil deficit of some 15.5 percent, according to the Central Bank. This means an even greater dependence on energy revenues. The reality is that there are penalties of an overheating economy, which can sometimes be severe. The size of the fiscal injection meant bottlenecks of various kinds including high consumer prices and traffic jams.

In the course of the year as well, the country witnessed a number of fatal road accidents, which now stands at 195 or just below the total of 210 recorded in 2006. The number of homicides remains high. According to one newspaper, the total at the time of writing is 353 and threatens to surpass the 2006 total of 371.

The international economy presented its own challenges with the global drive for bio-fuels, increasing food consumption in rapidly developing countries such as China and India and adverse weather conditions colluding to put strong upward pressure on global food prices.

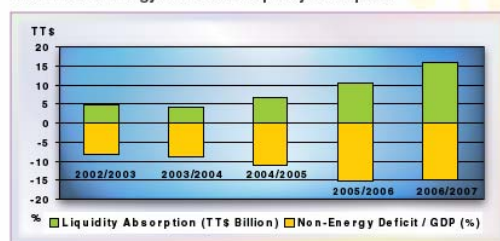
The ruling PNM Government was returned to power in general elections under the first-past-the-post system of parliamentary democracy. Elections were held on November 5th, following the presentation of the national budget less than three months earlier on August 20th, 2007.

Let us now consider what might be some of the main challenges, which face this country in the year ahead. To begin with, rising price levels will continue to be a cause for concern. While the average inflation rate for 2007 of just about 8.0 percent may still be lower than the 8.3 percent of 2006 it is far above the rate of 2.0 percent for the USA, this country's major trading partner. The challenge is to recognise the infrastructural and other constraints (human and physical) of a small developing economy and to ensure that while the supply constraints are being addressed high expenditures do not overwhelm capacity as is happening at present. Doing otherwise results in wastage, which is manifested in significant expenditures without the requisite returns. We concur fully with the statement of the Central Bank in its October, 2007 Monetary Policy Report that "...this may be an appropriate time to review and re-phase spending commitments in order to reduce the public sector's contribution to demand pressures and inflation."

Food prices are of particular concern to lower income groups and those on fixed incomes. However, there is little to indicate that there will be any fall in prices of imported food in the short or medium run. Indeed, the days of “cheap food” may very well be over. In this context, the challenge is to remove domestic and regional constraints to increased supply as soon as possible while at the same time giving targeted support to the most vulnerable in the society. Additionally, promotion of healthy eating habits can also address prices from the demand side. Put another way, it may well be possible to eat healthier or differently for less. The fact that this country has one of the highest obesity rates in the Caribbean is a clear sign of both the problem and its solution.

Any measure to reduce the price of food however, should not be seen as a substitute for prudent fiscal policy and greater savings generation in the context of huge oil windfalls. As is evident in Chart 1, the Central Bank seems to have borne the brunt of the burden of price reduction, through various forms of liquidity absorption including through increasing sales of foreign exchange. This cannot continue without some adverse consequences. Fiscal policy must play its part in keeping prices under control in the coming year.

Chart 1: Non-Energy Deficit and Liquidity Absorption



During 2007, the US dollar, to which the TT dollar is effectively pegged, has dropped to record lows against the major international currencies. As the US dollar continues to weaken, imported inflation is projected to increase. Thus, imports from Europe, England and Canada are all likely to become more expensive and Government's target inflation rate of 5 percent in 2008 will be difficult to achieve.

The falling value of the US dollar makes this country's exports more competitive on the international market, as this country's goods and services become cheaper. This change in relative prices should help to spur expansion in (i) domestic production for export and (ii) the production of domestic substitutes for higher cost imports. This is the challenge for the private sector as well as for the Government.

The recent Ryder Scott Audit of Trinidad and Tobago's natural gas reserves indicated that the country's reserves are dwindling and that an appropriate tax regime can be helpful in discovering new sources of supply. One of the challenges for the new administration in this area is to negotiate an incentives regime, which will encourage companies to explore for gas and oil especially in deeper water, while at the same time ensuring that the country gets its fair share of any new find. Clearly, the country's energy contract negotiators must be up to first world standards. Another challenge stemming from the Audit is the establishment of a platform for aggressive business expansion in selected clusters.

The truth is that the success of governmental initiatives largely depends on a truly professional public sector, which in turn demands decisive action in public sector reform. A fresh start should be made. There is no doubt that the economy will continue to do well in 2008 but major challenges loom. In the context of a New Year and a new administration, this is a good time to rethink priorities, strategies and opportunities.

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