24TH January, 2011

MEDIA BRIEF

What the International Agencies are saying about Trinidad and Tobago - REPORTS ON TRINIDAD AND TOBAGO

IMF ARTICLE IV CONSULTATIONS

FINANCIAL SECTOR ASSESSMENT AND

STANDARD AND POOR'S RATINGS REVIEW

Over the past month or so, Trinidad and Tobago has been subjected the most intense and rigorous scrutiny since the onset of the financial crisis in 2008.

During the period October 27th to November 8th, 2010 an International Monetary Fund (IMF) Mission visited Port of Spain and simultaneously conducted both the annual Article IV Consultation with Trinidad and Tobago as well as a Financial Sector Assessment. Prior to this the last Article IV Consultation took place in 2008 and the last FSAP was in 2005.

The Article IV Consultation involved extensive discussions relating to the medium and long term growth prospects of Trinidad and Tobago, issues of fiscal and monetary policy and developments with respect to balance of payments, external debt and exchange rate. These discussions formed the basis for the identification of potential vulnerabilities, the development of medium-term projections for key economic variables and the evaluation of the policy programme being pursued by Government and the formulation of policy recommendations for the consideration of Government policy makers.

The Consultation was not limited to macroeconomic policies, but included discussions on social sector policies, labour market developments, trade, the industrial relations climate and the political situation as these areas also significantly affect the macroeconomic performance of the Trinidad and Tobago economy.

The IMF held discussions with a wide **range of stakeholders** above and beyond Government Ministries and Agencies. The Article IV Consultations provided for in depth discussions between the IMF Mission and officials of the Central Bank of Trinidad and Tobago as well as with **representative private sector agencies such as the North, South and American Chambers of Commerce, the Trinidad and Tobago Manufacturers' Associations and the Bankers Association of Trinidad and Tobago and a selection of the major banking institutions in Trinidad and Tobago. Meetings were also scheduled with various non-governmental bodies, the Labour Unions, the National Insurance Board (NIS), and the Leader of the Opposition.**

In addition, in light of recent world financial market developments, the Fund delegation also held discussions with specific institutions including the Trinidad and Tobago Securities Exchange Commission, the Regulated Industries Commission, CL Financial Limited and Petroleum sector companies, such as British Gas, Petroleum Company of Trinidad and Tobago and BP T&T. A number of well known economists were also selected by the Mission to provided independent insights into the issues facing Trinidad and Tobago.

POLICY DISCUSSIONS

Given the prevailing macroeconomic conditions arising from the recent crisis, policy discussions focused on the following main issues:

a. Balancing expanded fiscal support for economic recovery with managing increasing public debt,
b. Declining energy revenue trends,
c. Nurturing a monetary environment conducive to supporting a non-energy sector recovery,
d. Restructuring Government's bailout liabilities whilst containing the fiscal costs and maintaining financial sector stability, and
e. Diversifying the economy towards reducing its reliance on energy

Key Aspects of IMF Appraisal

According to the IMF's appraisal, Trinidad and Tobago's economic performance was summarized as follows-:

Trinidad and Tobago has been hard hit by the global economic crisis;

The economic recovery is expected to begin in 2011;

The immediate priority is to support economic activity;

Over the medium term, economic policy needs to focus on ensuring that public debt remains sustainable as well as rebuilding buffers;

The current accommodative monetary stance is broadly appropriate;

The real effective exchange rate is broadly in line with fundamentals;

The banking system has shown resilience in the face of the economic crisis and the challenges with CL Financial; and

The Government needs to improve the statistical infrastructure.

IMF Recommendations

The IMF recommended that the following-;

implementation of the budget be accelerated, with particular emphasis being given to capital spending;

Establish a credible medium term framework aiming for an overall balance by 2012/2013;

Consider further reductions in the policy rate if economic conditions warrant;

Implement FSAP recommendations relating to the restructuring of CLICO liabilities, strengthening capital requirements for banks and improving legislation for insurance companies;

The main strategy to bring the debt-to-GDP on a downward trend was based on the following measures:

Partially reversing the recent large increase in transfers without withdrawing support to the most vulnerable,

Containing expenditures on goods and services, while maintaining a high level of investment to support diversification,

Strengthening non-energy revenues, through improving the efficiency of the VAT, and

The IMF informed the Trinidad and Tobago authorities that the next Article IV consultation is expected to be held on the standard 12-month cycle in 2011.

FINANCIAL SECTOR ASSESSMENT

In addition to the Article IV, the IMF also conducted the first ever Financial Stability Module review of Trinidad and Tobago under the **Financial Sector Assessment Programme (FSAP).**

The Report of the Mission noted the resilience of the banking and insurance sectors in the face of the global financial crisis and details the progress made in financial sector regulation for banks and insurance companies since the FSAP was conducted in 2005. It also lays out a set of recommendations for further enhancing the domestic regulatory and supervisory environment.

A. Banking System

The Report acknowledges that the authorities have taken major steps to strengthen the regulation and supervision for banks through:

(i) the passage of the Financial institutions Act (FIA), 2008 which provides for consolidated supervision and information sharing between the Central Bank and other authorities (both domestic and foreign) involved in financial sector supervision;

(ii) the mandatory application by all licenses, both on an individual and consolidated basis, of capital adequacy requirements as well as limits on large exposures and connected-party lending;

(iii) the issuance of new or updated guidelines on corporate governance, impaired assets and consolidated prudential reporting; and

(iv) the strengthening of the framework for Anti-money laundering and Counter Terrorism Financing (AML/CFT) with the establishment of the Financial Intelligence Unit (FIU) under the FIU Act of 2009 and the renewal of the Financial Obligations Regulations (FOR) in 2010

Despite the recent progress, bank regulation and oversight need to be strengthened in the following areas:

(a) **Capacity building** by way of additional specialists to assess banking risks related to Information Technology (IT), the market and AML/CFT as well as to validate internal bank models.

(b) **Changes to the 1994 prudential regulations** by (i) extending risk coverage beyond credit and market risks to include operational risks; (ii) reviewing the risk weighting of exposures to sovereigns in light of the standards in Basel 1 and 11 and (iii) endowing the Central Bank with the power to deduct connected exposures from a bank's capital.

(c) **Giving consideration to the implementation of Pillars 2 and 3 of Basel 11** which are associated with the supervisory review of banks' capital needs and the disclosure of individual bank information.

B. Insurance Sector

The FSAP report also noted the considerable progress made with the strengthening of the regulatory framework for the insurance sector since the conclusion of the FSAP Mission in 2005. Some noteworthy areas of progress include:

(1) The issuance of guidelines by the Central Bank to cover corporate governance, prudent lending and claims handling. These guidelines seek to address deficiencies in the current Insurance Act which virtually dates back to 1966 and which does not reflect best practices in legislation for financial institutions,

The drafting of a new Insurance Act, following extensive consultations with the insurance industry, which reflects a risk-based approach to insurance regulation and supervision. A key element of the proposed legislation is the requirement for insurers to adopt a risk-based capital regime which, when implemented, would correct a crucial deficiency in the current system and be more effective in protecting policyholders. **In this regard, and to give full effect to the new legislation, Government intends to introduce critical reforms to strengthen investment requirements, corporate governance and financial reporting.**

(2) **Insurance supervision** has been strengthened with a **more "hands-on" approach to supervision** being taken by the Central Bank after it took over the regulation of the sector at the end of 2004. Insurance companies are now subject to on-site inspection and have each been assigned a "relationship officer" who coordinates supervisory activity.

(3) **Important changes in financial reporting have been introduced and insurers are now required to file returns on a quarterly basis**. Prior to this, reports were filed on an annual basis. **New standards for reporting policy-holder liabilities have been developed** and "test runs" for the valuation of policy-holder liabilities have been conducted in parallel for the past three years using the Caribbean Policy Premium Method which is ready for adoption. **The adoption of this new actuarial valuation methodology,** once the new legislation is passed, is consistent with international best practices.

The Article IV Report and the Financial Stability Assessment Report of the Fund Mission, and the policy recommendations emanating there from were considered by the IMF Board of Directors on Friday January 21st, 2010. A Copy of the Comments of the Board is attached for ease of reference.

STANDARD AND POORS RATINGS REVIEW

In addition to the Article IV Mission by the IMF, Standard and Poor's Rating Services conducted its annual rating exercise during the period December 01 – 03, 2010.

The review was prepared on the basis of a comprehensive review of the performance of the Trinidad and Tobago economy with particular emphasis on macroeconomic, political and social developments, Government's finances and the country's domestic and external debt position.

In November 2010, in addition to taking into account factors affect a sovereign government's willingness and ability to service its debt on time and in full, Standard and Poor's fine tuned its calibration of factors employed in sovereign analysis to allow the agency to incorporate information derived from the 2008-2009 global recession with particular emphasis on the impact of financial sector difficulties on government's fiscal profiles.

In its Press Statement on January 14, 2011, **Standard & Poor's Ratings Services affirmed Trinidad and Tobago's long-term foreign currency rating at 'A' which reflects the prime signal to investors. The ratings on the long-term local currency, short-term foreign currency and short-term local currency were also affirmed at 'A+', 'A-1 and 'A-1' respectively.**

The ratings in the debt categories reflect **improved economic growth prospects in 2011; a stable external and fiscal profile** resulting from several years of buoyant energy prices as well as significant off-budget and contingent liabilities.

Standard and **Poor's acknowledged that Trinidad & Tobago's external and fiscal flexibility allows fiscal leeway to deal with the fallout of the global economic crisis and the bankruptcy of the country's largest financial conglomerate, the CL Financial Group (CLFG).**

However, the agency projects a widening of the net general government debt to approximately 28% in 2011 from 15% in 2010; given the latest plan to bail out investors at CLFG's Life Insurance Company, Colonial Life Insurance Co. (CLICO).

The following major rating factors that were identified by Standard and Poors:

- **Improved economic growth prospects estimated at 2.5 percent; a lower government deficit of 2.6 percent and a current account surplus of 13 percent of GDP in 2011;**

- **Solid external and fiscal positions continue to support Trinidad and Tobago's policy flexibility which will**

enhance the government's external liquidity position; and

- Although **Government's plan to bail out investors at Colonial Life Insurance Co. (CLICO) will increase the net general government debt, the debt burden will remain below the 36 percent median for 'A' rated sovereigns.**

Standard & Poor's also **affirmed Trinidad and Tobago's stable outlook which balances the risks of the challenges to address the intervention of the CLFG bankruptcy without eroding the fiscal balance sheet**.

Standard & Poor's noted that improvements in the ratings were constrained by the following factors:

- The contingent liability arising from continued losses in public sector enterprises, specifically the Water and Sewerage authority (WASA) which is expected to report an operating loss of approximately 0.8 percent in 2010 and possibly unfavorable future country ratings; and

- Fiscal deterioration as well as further slippages in the restructuring of government-owned entities that could lead to lower future ratings.

The agency stated further that improvements in transparency, governance and regulation of the financial industry and among public-sector enterprises in particular, could induce the agency to raise its ratings in the medium term.

Ratings Affirmed

Foreign Currency	A/Stable/A-1
Local Currency	A+/Stable/A-1
Transfer & Convertibility Assessment	AA
Senior Unsecured	A
Senior Unsecured	A+