ADDRESS BY
SENATOR THE HON. CONRAD ENILL
MINISTER IN THE MINISTRY OF FINANCE
TO THE CONFERENCE ON ACCOUNTING FOR THE PETRO DOLLAR
HOSTED BY THE UNIVERSITY OF THE WEST INDIES, ST. AUGUSTINE AND THE OILFIELD WORKERS TRADE UNION ON NOVEMBER 14 2005

Accounting for the Petro Dollar

Mr. Chairman, I wish to thank the Department of Economics, of The University of the West Indies, St. Augustine, and the Oilfield Workers Trade Union (OWTU) for organizing this conference on *Accounting for the Petro Dollar*. The conference and its theme is timely and well advised given that oil prices have been persistently edging higher since **2002** and so have gas prices. The combination of these factors Mr. Chairman, has been generating higher levels of public revenues and have been providing the fiscal space to allow for the scaling-up of socio-economic and public infrastructure expenditure in line with other budget priorities and consistent with a sustainable fiscal stance.

Mr. Chairman, as you are aware, the Government is committed to advancing and deepening the development and transformation process of this country to ensure the achievement of developed country status by 2020, if not before. We cannot miss this opportunity offered by the present favourable circumstances to raise the long-term growth potential of the economy. As you are aware, higher levels of investment in human capital and in social and economic infrastructure are critical for raising the productivity and long-term efficiency of the economy; but let me emphasise that in the drive to expand *growth-enhancing public investment*, in particular high priority infrastructure projects, *we are paying particular attention to the maintenance of fiscal sustainability*.

Mr. Chairman, our lessons from the past are now guiding us in a much better manner as to the level of additional public expenditure which is required within a medium-term framework so as *to ensure that our present macroeconomic viable conditions* – a competitive exchange rate, stable and low interest rates and reasonable price stability – *are not compromised*. The economy of Trinidad and Tobago grew by an average of **6.0 percent** per annum in the past decade – **1995-2004 -** and this is better than the performance of all emerging and developing countries as a group which grew by approximately **5.0 percent,** including those countries in the Western Hemisphere – which grew by approximately **3.0 percent**. During this period, inflation has been in the low single digits and the unemployment rate has fallen to below **10.0 percent**.

Mr. Chairman, these positive developments have been anchored in a solid policy framework – prudent fiscal, monetary and foreign reserve management, as well as strengthened financial sector supervision – and increased foreign investments equivalent to approximately **7.0 percent** of Gross Domestic Product per annum mostly in downstream gas-based industries. The recent upgrades in this country's investment grade rating by **two (2)** international rating agencies – Standard and Poor's and Moody's Investor Services - are reflective of these positive developments. These **two (2)** assessments have reaffirmed to the international financial community, including our major investors, that this country remains committed to sound macroeconomic and financial management, including saving a portion of our windfall oil and gas gains for use by future generations.

Mr. Chairman, Trinidad and Tobago can now be described as a gas-based economy. You are no doubt aware that our rebased national accounts with the year **2000** as the base year, captured the importance of the gas and gas-based sub-sector which emerged during the last decade. The rebasing reflected an economy which had become increasingly diversified and transformed during the last decade and our public expenditure profile represents a foundation on which private sector productivity and efficiency could flourish and prosper.

As a result Mr. Chairman, in the recent budget statement the Government announced its decision to establish a separate taxation regime for gas. Our gas industry, as indeed those of many other petroleum-producing countries, had emerged out of the exploration and development efforts of petroleum companies. The gas and oil businesses were inextricably linked. Accordingly, oil and gas revenues were not optimized. Technological developments in the petroleum and gas sectors have now enabled us to separate and identify revenues and expenditure stemming from both oil and gas production. At the same time markets for oil and gas are becoming distinct and separate. In fact, we are now seeing the emergence of a true world gas market similar to that for the oil market. It was these considerations which enabled the Government to establish separate tax regimes for oil and gas.

Mr. Chairman, the first phase of the reform of the energy taxation involved an amendment to the Finance Bill 2005 which was enacted in **July 2005**. As a result of those changes which essentially involved the closing of many loopholes and the clarification of certain measures, petroleum revenue would be enhanced – by **$1.0 billion** in **2006**.

Moreover Mr. Chairman, the new gas tax regime which is being put in place and which is centered on the concept of fair market value prices for gas will also generate additional revenue. In addition to a reformed regime for the energy sector, Mr. Chairman, the secular decline in oil production has been reversed with the new discoveries and production by BHP Billiton while gas production is expected to continue at a measured pace in the context of the commitment by the major gas producer, bpTT, to drill **one (1)** new well per year over the course of the next **three (3)** years. Other major gas producers are in the process of firming up plans for accelerating gas exploration and production.

Mr. Chairman, with energy sector output on the rise and separate tax regimes for oil and gas now balancing the economic and financial interests of both producers -- who are receiving an economical rate of return and Government – which is receiving a predictable and stable flow of public revenues, the recent and enduring increases in oil prices are generating substantial oil and gas revenues. *In **2006**, oil and gas revenues are estimated at **$19.4 billion** or almost **six (6)** times the comparable revenues in **2000** and **63.0 percent** greater than the **2005** comparator*.

Mr. Chairman, oil prices have continued to be buoyant, reflecting in the main, higher-than-expected oil demand growth in China and India – **two (2)** emerging market economies - and in the United States of America – an advanced economy; constrained supply conditions have been supporting the buoyant oil prices, in particular the geopolitical concerns about insecure reserves, refining and distribution industry bottlenecks in some major consuming markets.

Mr. Chairman, when we and other analysts review the prevailing oil market outlook, we detect one clear message - *there is a substantial imbalance between oil demand and oil supply* and indications are that demand growth would continue to exceed supply in the foreseeable future. Accordingly, we are now entering an era which would be characterized by much higher prices than in the past and in the opinion of a number of well-established analysts, those prices could remain centered on an average of **US$50.00** per barrel at least to the end of the decade.

Mr. Chairman, the distinguishing feature of the current energy situation which is generating substantial oil and gas revenue – **19.0 percent** of GDP in **2006** – when compared with the **two (2)** previous oil shocks of **1973/1974** and **1979/1980** is that *apart from the high oil and gas prices*, it is now mainly driven by **two (2)** factors:

First: by the large newly discovered reserves of oil and natural gas and by the expansion in the liquefied natural gas sub-sector; and

Second: by the establishment of separate tax regimes for oil and gas.

Mr. Chairman, the growth in revenues resulting from energy output expansion and from a reformed tax regime for the energy sector is helped by the high international energy prices prevailing for some time and which are expected to prevail over the medium-term. In the period **2002-2006** our oil and gas revenues have totaled approximately **$47.0 billion** which has covered approximately **41.2 percent** of our public expenditure during that period. However, whereas oil and gas revenue covered **20.2 percent** of public expenditure in **2002** it is now covering approximately **57.0 percent** of public expenditure. We expect that our reform of the non-energy tax regime – generally lower marginal rates of taxation – will generate increasing amounts of revenue to rebalance on a sustainable basis energy and non-energy sources of taxation.

But Mr. Chairman, the ramped-up expenditure is taking place in the context of a much more diversified economic structure as well as on a firmer foundation of energy output and prices. We do not envisage therefore, the emergence of the so-called *dutch disease*. Our widely diversified economy and our prudent macroeconomic management would avert the kind of disruptive effects which emerged during our previous **two (2)** booms. We all recall the pervasive decline in the un-competitiveness of our non-energy tradable sector and the increasing vulnerability of our economy to external economic shocks. Illustratively, the sharp drop in oil prices which began in **1981-1982.** You all recall that macroeconomic and structural adjustment programme was required to restore growth in the economy after years of secular decline. However, we have now had **eleven (11)** consecutive years of economic growth and significantly, productivity and efficiency are being driven by investment expenditures, in particular public expenditures.

Mr. Chairman, I refer here to those investment expenditures which are best undertaken by the public sector and which are essential for increasing levels of economic growth, in particular investment in human capital through expenditures on comprehensive education and training, accessible and quality health care, affordable housing and social and economic infrastructure.

Mr. Chairman, we have also scaled-up our expenditures in national security to address issues of crime and safety of our citizens and we have ensured that our development agenda is equitable and balanced through expenditures on our most vulnerable and disadvantaged groups as well as on Tobago to allow all our citizens to share in the fruits of our growth and development.

Accordingly Mr. Chairman, oil and gas revenues of approximately **$47.0 billion** in the period **2002-2006** *could not cover* these investment priorities. Let me provide you with some data in respect of the relationship between investment on selected expenditures and oil and gas revenues:

- state-of-the-art national security of **$10.3 billion** or **22.0 percent**;
- quality and free tertiary education of **$18.3 billion** or **39.0 percent**;
- quality and accessible health care of **$9.6 billion** or **20.0 percent**;
- affordable housing of **$1.4 billion** or **3.0 percent**;
- social protection of **$12.8 billion** or **27.0 percent**;
- social and economic infrastructure of **$10.7 billion** or **23.0 percent**;
- development of Tobago of **$5.0 billion** or **10.0 percent**; and
- the insulation of our citizens from the adverse effects of the rising prices of petroleum products of **$2.4 billion** or **5.0 percent**.

Mr. Chairman, oil and gas revenues were only able to cover **67.0 percent** of these priority expenditures, therefore domestic revenues have been playing key roles in this process. We are well aware that we are utilizing the opportunities posed by the current windfall in gas and oil revenues to advance the modernization of our economy and that we are deriving these windfall revenues from exhaustible resources – oil and gas. As you are aware, in resource-endowed economies policy makers are faced with **two (2)** major issues. The *first* – related to the finite nature of these resources – is how much oil revenue to spend on the present generation and how much to save for future generations. The *second* is how to adjust spending and cushion the domestic economy from the sharp and unpredictable variations in oil and gas prices and revenue. Moreover, in the context of our own situation, on-going strategic and tactical investments are required to achieve Vision 2020. Indeed, the recent purchase by the Petroleum Company of Trinidad and Tobago Limited and the National Gas Company of **30.0 percent** of the bpTT's former Teak, Samaan and Poui assets is a case in point.

Mr. Chairman, to accommodate these objectives we are now taking steps to establish the operational modalities of the Heritage and Stabilisation Fund. On enactment of the legislation, the Interim Revenue Stabilisation Fund would be retired and the funds in that account would be transferred to the Heritage and Stabilisation Fund. Of the approximately **$47.0 billion** in oil and gas revenues generated in the period **2002-2006** we would have saved **$6.2 billion** or **13.2 percent** by the end of the current fiscal year. The balance in the Fund would therefore be approximately **$7.2 billion**.

Finally Mr. Chairman, we are of the view that we have established the right long-term policy framework for managing our oil and gas revenues. While we intend to save our oil and gas surpluses in a manner which would benefit both current and future generations, we will always ensure that our expenditure remains appropriate, sustainable and prudent. We believe that we are within the critical threshold of where public expenditure should lie. At **$32.3 billion** in **2006** or **31.7 percent** of GDP public expenditure has risen by less than **5.0 percent** of GDP over the **four (4)** year period average - **2002-2005 –** of **26.8 percent** of GDP. Within this threshold we believe that the skillful management of our oil and gas resources - for which I have given an appropriate accounting this morning - would ensure the continuation of stable economic conditions, the fostering of sustainable growth and development and the generation of good quality jobs and a reasonable standard of living for all our citizens.

Mr. Chairman, relentlessly and unwaveringly we intend to establish as early as is practicable, Trinidad and Tobago as a modern industrial state.

Thank you Mr. Chairman.