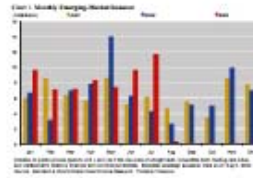




Emerging  
Markets  
Weekly



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## IS THE TRINIDAD & TOBAGO ECONOMY STARTING TO OVERHEAT?

Trinidad & Tobago is experiencing another wave of strong economic growth that has built up high expectations about the future. Its transformation into the regional financial centre and growing strategic integration into the global economy are likely to prove landmark events. But, as is typical, there are many storm clouds on the horizon. One such risk is that of overheating, which if not corrected, could lead to a hard landing for the economy.

The following are some signs that the Trinidad and Tobago economy might be approaching the overheating zone:

- **Strong pick up in inflationary pressures.** Headline inflation is running at around 7% on an annual basis, well outside the Central Bank's informal target range of 4%-5%. Even core inflation, which gives a better gauge of underlying inflationary pressures, has also jumped from 2% at the end of 2004 to 2.5% at end-February 2006. Looking ahead, the proposed hike in electricity rates will have a significant impact upon prices across the board. The Regulated Industries Commission (RIC) has proposed electricity rate hikes of 45% for residential customers and more than 50% for commercial users.
- **Substantial tightening in the labor market.** The official unemployment rate has steadily declined from its peak of 25% in the late 1980s to about 7% in 2005, the lowest level in four decades. Labor participation rates are at historical highs, especially as more women enter the job market. The demand for labor has grown across most industries and nearly all skill levels, suggesting that even higher wages and salaries are needed to attract and retain talent. The possibility of importing labor from CARICOM has been raised to ease shortages in the construction sector.
- **Expansionary fiscal policy.** The non-energy fiscal deficit (the overall balance less energy revenues) has been widening substantially due to higher government spending, and is the main culprit behind the liquidity overhang in the banking system. The 2005/2006 Budget envisages a non-energy deficit at an estimated 25% of non-energy GDP, more than twice the 12% of non-energy GDP in 2003.
- **Housing boom.** House prices have risen dramatically over the past few years. The boom was initially evident in the western peninsula but has since spread to other parts of the island. The sheer magnitude

of the house price boom has prompted the natural question of its sustainability and whether house prices are significantly overvalued. The longer house prices keep on rising the greater the chance of a disruptive adjustment in the housing market and on the balance sheets of more exposed banks and insurance companies.

Real GDP is likely to average 10% in 2006, reflecting a full year's production of Atlantic LNG Train IV and the M5000 mega methanol plant as well as strong momentum in the construction sector. Indeed, 2006 will represent Trinidad & Tobago's 13th consecutive year of economic growth but prospects over the next few years depend on the ability of the authorities to engineer a soft landing, that is, a slowing of growth to a more sustainable pace.

Fiscal policy has the key role to play in cooling down the economy. In the current circumstances of record oil prices, there is a compelling reason to keep public spending under tight control and within budget and to transfer additional revenues into the Revenue Stabilization Fund. The Central Bank is already attempting to tighten monetary conditions, and further tightening (even higher interest rates) is necessary to make sure that inflation slows at least in line with its informal target.

Translating good intentions into sound and decisive policy intentions now remains the challenge. And there is much at stake.

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## FINANCIAL & ECONOMIC INDICATORS

*As at 30 March 2006*

Exchange Rate/US\$	Closing Value	Previous Week
Yen	117.32	117.85
Euro	1.22	1.20
Jamaica	63.50	65.36
Guyana	200.40	200.40

Commodity Prices	Closing Value	Previous Week
Crude oil (US\$/bbl)	67.15	63.91
Natural Gas (US\$/mmbtu)	7.16	7.16
Gold (US\$/Troy Ounce)	588.65	549.80

### Eurobond Indices (Returns, % YTD as of 30-Mar-06)

Lehman Brothers Global Aggregate Index	0.13
JP Morgan EMBI+	-18.83
CMMB Eurobond Index	-0.17

Policy Interest Rates (%)	Closing Value	Previous Month
United States	4.75	4.50
Euro Zone	2.50	2.50
Japan	0.00	0.00
Brazil	16.50	16.50
Trinidad	6.75	6.50
Jamaica	12.60	12.60
Barbados	4.75	4.75

Market Interest Rates (%)	Closing Value	Previous Week
US 90-day T-Bill	4.50	4.55
US 10-Yr Treasury	4.86	4.74
3-month UK Libor	4.61	4.60
Japan 90-day T-Bill	0.18	0.18
Brazil 90-day T-Bill	15.73	15.80
TT 90-day T-Bill	5.43	5.12
Jamaica 90-day T-Bill	12.74	12.74
Barbados 90-day T- Bill	6.22	6.22

*Sources: Bloomberg, CMMB Research Centre, Central Bank of Trinidad and Tobago, Bank of Jamaica, Central Bank of Barbados, Bank of Guyana*

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