Economic Alert iQ

First Citizens
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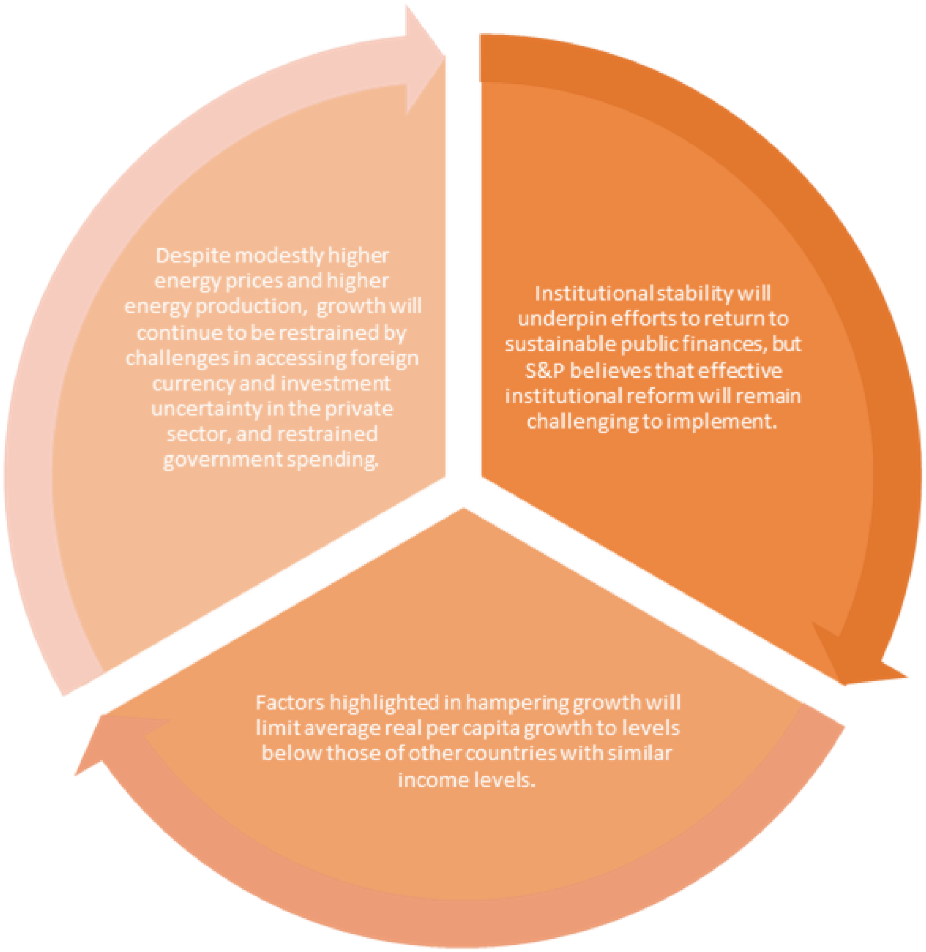
Economic Alert: S&P Affirms Trinidad and Tobago Ratings; Outlook Revised To Negative On Macroeconomic Risks And External Imbalances

- On 27th April 2018, S&P Global Ratings revised its outlook on the Republic of Trinidad and Tobago to *"Negative"* from *"Stable".* The rating agency affirmed its 'BBB+/A-2' long- and short-term foreign and local currency sovereign credit ratings on Trinidad and Tobago.
- S&P stated the "negative" outlook reflects the view that there is at least a one-in-three chance that S&P could lower the ratings over the next 12-to-24 months.
- It is expected that moderately higher energy prices and higher production levels would lead to a mild economic recovery and smaller current account deficit over this period.
- S&P believes there is uncertainty about whether this improvement will be sufficient to mitigate the impact that imbalances such as:
  1. Exchange rate pressure
  2. Restrictions on accessing foreign currency
  3. Negative yield differentials on short-term treasury securities relative to those of the U.S.
  4. Historical gas supply shortages

  These could lead to a faster depletion of the country's external assets, or a weakening of the effectiveness of monetary policy. Under this scenario, S&P could lower the rating.
- Another point of concern that could factor in a downgrade in the next two years would be the government's fiscal consolidation measures in shrinking the deficit.

- Finally, S&P could take a negative rating action should the government fail to implement key institutional reforms such that large revenue collection leakages and weaknesses in data provision persist into the foreseeable future.
- On the flip side, the rating agency cited that the outlook moving to stable would be based on a strong track record of growth in the energy sector, for instance due to higher-than-expected energy prices or production, shrinking current account deficits and larger capital inflows. Additionally, combined with a track record of successful fiscal consolidation, declining interest costs, and effective institutional reform, could lead S&P to revise the outlook to stable.

Institutional and Economic Profile: Growth in the energy sector will drive mild, if below-average economic recovery, while institutional reform will progress slowly.



Source: First Citizens Research & Analytics, Standard & Poor's

- S&P notes that following an estimated 7% contraction in real GDP over the past two years, largely due to the downturn in Trinidad and Tobago's large energy sector, the rating agency expects that the operation of new fields and modestly higher energy prices will steer the economy back to growth.
- It is forecasted that real GDP will increase by 1.6% and 2% in 2018 and 2019 respectively.
- S&P expects natural gas production to increase about 13% over the next two years, due to the start-up of new domestic gas production, with forecasted Henry Hub natural gas prices to remain stable at US$3 per mmBtu. This projection excludes the potential new cross-border field development with Venezuela.
- On the other hand, S&P doesn't expect crude oil production, which, together with oil exploration represents about 17% of the energy sector, to increase during the same period, due to natural decline and uncertainty surrounding new sources of production. WTI oil prices are expected to rise to US$55 per barrel in 2018 and stay stable thereafter.
- Despite some growth in the energy sector over the next two years, it is expected that Trinidad and Tobago's persistent current gas supply shortage, U.S. dollar shortage in the banking system, private sector investment uncertainty, and contractionary fiscal policies will contribute to subdued growth in the non-energy sector.
- S&P expressed confidence in the current administration stating that since taking office in late 2015, the government has progressively adjusted fiscal and monetary policies to the less favorable economic conditions.
- However, while the government is expected to advance policies that seek to achieve fiscal sustainability over the next two years, S&P believes the pace and effectiveness of the implementation of substantial institutional reform are uncertain.

Flexibility and Performance Profile: Sizable financial assets continue to buffer the country's weaker fiscal and external positions, although imbalances could pose further strain.

S&P views the solid, if declining, central bank reserves, and sizable government assets, including a sovereign wealth fund, will continue to limit fiscal and external financing risks

New revenue measures, spending restraint, and stronger energy performance will contribute to the improved fiscal deficit, although S&P expects that over half of this improvement will come from one-off revenue measures.

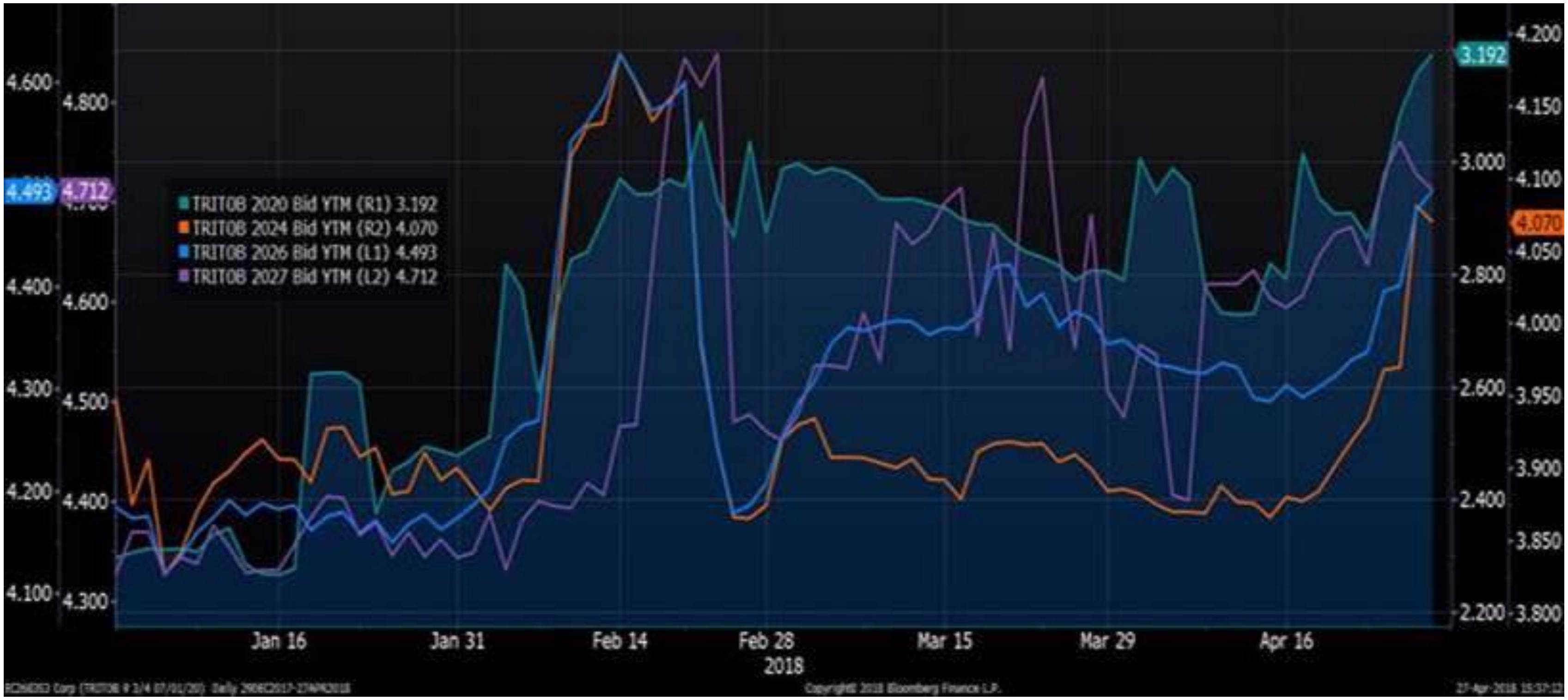
External imbalances will weaken the country's external asset position.

Source: First Citizens Research & Analytics, Standard & Poor's

- Despite some drawdowns, Trinidad and Tobago's sovereign wealth fund, the Heritage and Stabilization Fund (HSF), has accumulated value over the past decade, and it is expected along with other government financial assets and central bank reserves, will continue to provide the government with fiscal and external buffers.
- Although the government has used some of the funds to finance recent deficits, the fund continues to grow and now holds about 25% of GDP in financial assets.
- Although S&P forecasts moderate financial inflows over the next four years, including direct investment inflows in the downstream energy sector, the rating agency does not believe that these inflows will curb the decline in the central bank's reserves. In addition, large errors and omissions in current account reporting complicate the analysis of current account deficit financing. Errors and omissions have accounted for over 70% of the current account balance on average over the past five years for which S&P has data.
- The government's fiscal accounts will continue to rely heavily on the energy sector. It is expected that energy-related revenue will account for about one-third of the government's total revenues over the forecast horizon. Energy sector revenues fell by more than half in the 2015-2016 fiscal year due to the downturn in prices and production.
- Nevertheless, stronger energy-sector revenues, revenues from new fiscal measures, and one-off revenues will shrink the fiscal deficit over the next two years. S&P forecasts that the annual increase in net general government debt will average 1.9% of GDP from 2018-2020.
- Furthermore, it is believed that the government faces moderate contingent risks from its nonfinancial public enterprises, including Petroleum Co. of Trinidad and Tobago (Petrotrin). In total, public enterprise debt accounts for about 14% of GDP.
- Conclusively, S&P expects the banking sector to remain profitable, well-capitalized, and highly liquid. Credit quality has benefited from relatively stable employment levels, despite the economic downturn.

Selected Indicators	**2013**	**2014**	**2015**	**2016**	**2017f**	**2018f**	**2019f**	**2020f**
Real GDP growth (%)	1.0	(0.3)	1.5	(6.0)	(0.8)	1.6	2.0	2.0
Real Export Growth (%)	41.2	(24.2)	(16.2)	(31.0)	(0.8)	1.6	2.0	2.0
Unemployment Rate (%)	3.7	3.3	3.4	3.6	4.5	5.0	4.7	4.7
General government balance/GDP (%)	(5.9)	(2.5)	(1.7)	(5.4)	(7.9)	(4.0)	(3.3)	(3.8)
General government debt/GDP (%)	49.8	57.2	66.0	76.2	70.8	71.6	70.9	71.1
Net general government debt/GDP (%)	13.5	19.9	31.4	32.0	27.4	28.5	28.3	28.8
General government interest /revenues (%)	5.3	5.3	6.0	8.4	12.0	10.5	8.1	9.0
CPI growth (%)	5.2	5.7	4.7	3.1	1.9	3.2	3.7	3.3
Current account balance/GDP (%)	20.4	14.7	4.6	(11.7)	(6.0)	(4.9)	(3.7)	(2.1)
Current account balance/CARs (%)	27.9	23.7	8.7	(26.0)	(11.8)	(9.9)	(7.4)	(4.3)

Trinidad & Tobago Eurobonds Performance Year to Date (YTD)



Source: First Citizens Research & Analytics, Standard & Poor's, Bloomberg

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