Economic Alert iQ

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Moody's downgrades Trinidad and Tobago's issuer rating to Ba1 from Baa3 and changes outlook to stable from negative.

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Key Drivers

- Moody's downgraded Trinidad and Tobago's issuer rating to Ba1 (non-investment grade) from Baa3 and changed the outlook to stable from negative. The rating action was based on the following 3 key drivers:

    1. The authorities' policy response has been insufficient to effectively offset the impact of low energy prices on government revenues, as fiscal consolidation efforts have mostly relied on one-off revenue measures.
    2. A steady rise in debt ratios driven by large government deficits has eroded fiscal strength.
    3. Declining production from maturing oil and gas fields coupled with limited investment prospects, in the context of low energy prices, have materially undermined medium-term growth prospects. The stable outlook on the Ba1 rating incorporates moderate external risks as well as the benefits of the government's sizeable fiscal buffers in offsetting further downside risks and ample access to a relatively deep domestic financial market.

- Trinidad and Tobago's foreign-currency bond and deposits ceilings were lowered to Baa3/P-3 and Ba2/NP from Baa2/P-3 and Baa3/P-3, respectively. At the same time, the local-currency bond and deposits country ceilings were lowered to Baa2 from Baa1. Since the U.S. election, expectations of looser fiscal policy in the United States have contributed to a stronger dollar and higher U.S. Treasury interest rates, pushing up yields elsewhere as well.

Ratings Rationale

- Policy response to the energy price shock continues to be insufficient to contain elevated budgetary pressures.
- As a result of the decline in oil and gas prices, energy-related government revenues fell to only 1% of GDP in the 2016 fiscal year from 8% of GDP in the previous fiscal year, and current revenues declined 28% over 2015-16.
- Expenditures will continue to increase in 2017 due higher debt servicing costs and larger capital expenditures.
- Government strategies to raise current revenues have yielded very limited results, equivalent to 1% of GDP this fiscal year.
- Revenues from eliminated exemptions from the value added tax while lowering the overall rate to 12.5% from 15%, were lower than forecasted. According to Moody's changes to the property tax will yield modest results and will not be accounted for until 2018.
- Government has depended on dividends from National Gas Company (NGC) and asset sales to contain the fiscal deficit. While the government expects to earn TTD9.69 billion (6.4% of GDP) from one-off capital measures in 2017 fiscal year, Moody's believe TTD6 billion (4% of GDP) is a more likely outcome given significant implementation risks.
- Lack of timely macroeconomic data and weak policy execution capacity have limited the effectiveness of the policy response to the energy price decline. Government efforts have promoted only limited economic diversification, modestly decreasing the dependence of the economy in the energy sector.

Rising Debt Erodes Fiscal Strength

- Moody's expects the fiscal deficit will be close to 6% of GDP in this fiscal year (2016/17), once the anticipated 4% of GDP capital revenue estimate derived from asset sales and dividends from National Gas Company (NGC) is realized.
- Despite heavy reliance on asset sales to close the fiscal balance, debt to GDP exceeded 56% in 2016, rising from 42% in 2014, Moody's does not anticipate that the government will achieve a debt-stabilizing primary balance over the next 3 years and, consequently, Moody's expects the debt ratio to rise to almost 70% of GDP by 2019. This is substantially higher than the baseline scenario assumed when the rating was lowered to Baa3 from Baa2 one year ago.
- Without meaningful fiscal adjustment to reduce double-digit fiscal deficits excluding capital revenues, the government will likely continue to use resources from the Heritage Stabilization Fund (HSF). Even though its assets stand at around USD5.7 billion (24% of GDP), recurring withdrawals will continue to erode an important credit strength of the sovereign.

Declining oil and gas production coupled with limited investment prospect undermine medium-term growth potential

- Economic growth in Trinidad and Tobago has slowed as oil and gas fields mature and production levels decline.
- The economy contracted 2.3% in 2016 according to government figures and expected growth this year is in the range of 0% to 1.5%, with positive growth hinging on the timely completion of two gas projects scheduled to become operational in the second half of 2017.
- Beyond 2017, increased investment is required to reverse the declining trend in oil and gas production and lift production in the medium term.

Rationale for stable outlook

- The stable outlook captures the effect that sizeable fiscal buffers will have in offsetting any further downside risks.
- An aggressive rollback of financial regulation, which could spur excessive risk taking and increase the likelihood of future financial crises.
- Asset sale proceeds and dividends from the National Gas Company, as well as drawdowns from the Heritage Stabilization Fund (HSF) will help finance the government deficit, slowing the rate of debt increases.

- The outlook also reflects moderate external risks given very low external payments relative to foreign exchange reserves and modest current account deficits.
- Low gross borrowing requirements and access to a relatively deep domestic financial market buffer against international financial risks.

Factors that result in an upgrade

- Moody's would consider moving the outlook to positive if it is decided that fiscal consolidation will likely lead to lower fiscal deficits in 2018-19, and stabilize government debt ratios faster than currently anticipated.
- The emergence of a fiscal and economic policy response that proves effective in containing the deterioration in government debt metrics would be supportive of a rating upgrade.
- Higher GDP growth and a recovery in government revenues is expected to place upward pressure on the rating.

Factors that could lead to a downgrade

- Downward pressures on the rating would emerge if fiscal deficits and government debt ratios rise at a higher rate than currently expected.
- Depletion of fiscal buffers -- i.e., reduction in assets available for sale and assets held in the Heritage Stabilization Fund -- coupled with limited fiscal consolidation beyond 2018, would add negative pressure to the rating.
- The possibility that government support in the form of loan guarantees to Petrotrin that could be higher than currently assumed would also add downward pressure, as would a weakening balance of payments position.

Public Sector Debt Outstanding (In % of GDP)	***16-Sep***	***16-Dec***
Total Public Debt	81.40%	77.20%
Total Public Debt (excl. sterilized debt)	60.10%	56.60%
Central government domestic debt (excl. sterilized debt)	24.40%	23.40%
External Debt	14.50%	13.90%
Contingent Liabilities	21.20%	19.30%

Source: Central Bank Trinidad and Tobago

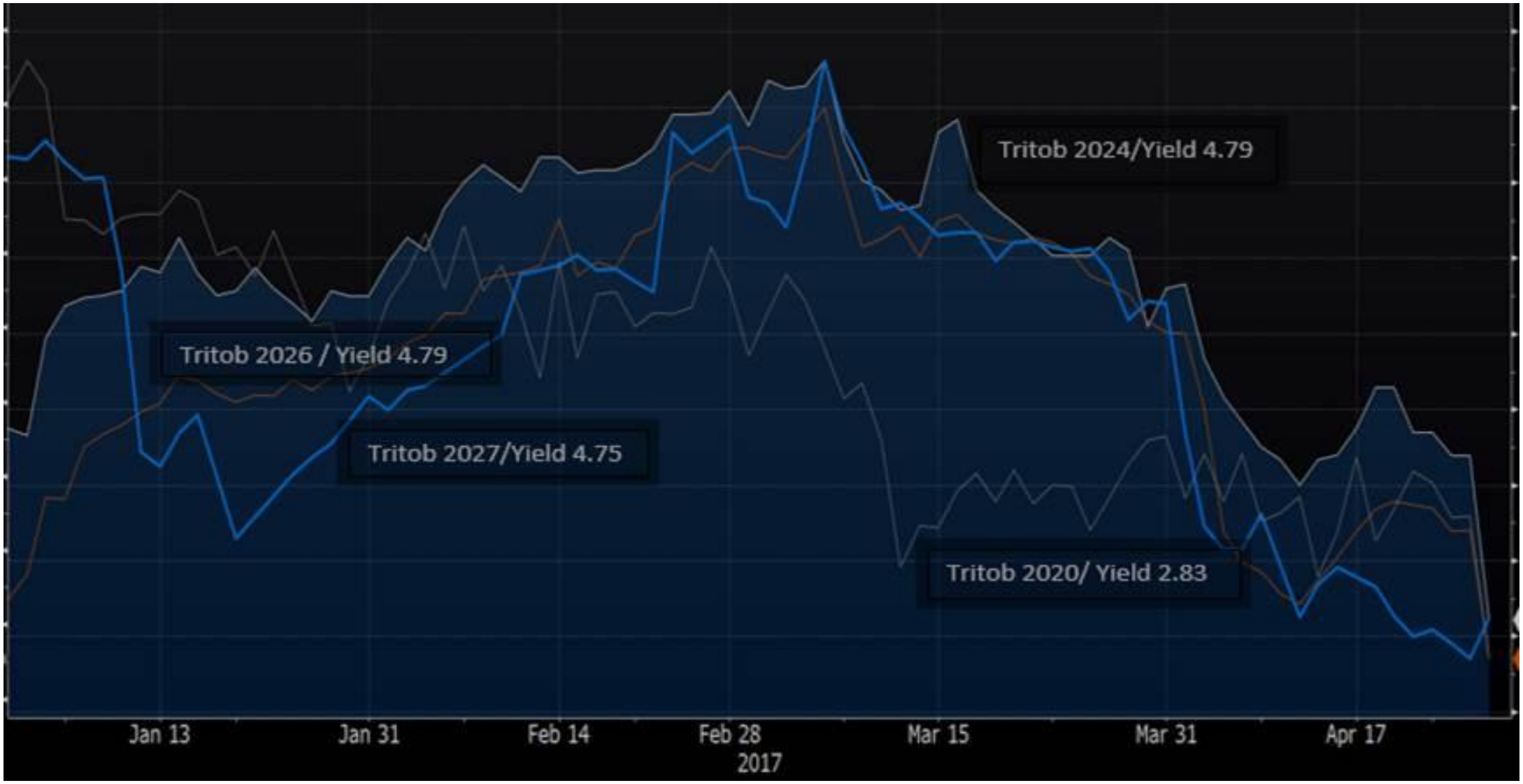
Selected Economic Indicators		Period
Quarterly Index of Real Economic Activity (YoY change)	-10.80%	(Q316)
Quarterly Index of Real Economic Activity - Energy (YoY change)	-18.30%	(Q316)
Quarterly Index of Real Economic Activity - Non- Energy (YoY change)	-6.70%	(Q316)
Index of Retail Sales (YoY change)	-6.20%	(Q316)
Headline Inflation Rate	3.10%	Dec-16
Unemployment Rate	4.40%	Q216
External Current account (% of GDP)	-5.20%	Jan-Jun 2016
Net Official Reserves (USD, millions)	9,105.40	Apr-17
Import Cover (In Months)	10.1	Apr-17

Source: Central Bank Trinidad and Tobago

Fiscal Operations (In TTD, millions)	FY 2015	FY 2016
Current Revenue	52,244.50	41,026.60
Energy Revenue	18,660.90	6,584.60
Non-Energy Revenue	33,583.60	34,442.00
Current Expenditure	52,322.90	47,526.20
Current Account Balance	(78.40)	(6,499.60)
Capital Revenue	4,989.20	3,915.20
Capital Expenditure	7,620.80	4,708.70
Overall Balance	(2,709.90)	(7,293.10)

Source: Central Bank Trinidad and Tobago

Government of Trinidad and Tobago Eurobond Performance Year to Date



Source: Bloomberg

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