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CENTRAL BANK OF
TRINIDAD & TOBAGO

# Monetary Policy Report

December 2014

Volume XIV   Number 2

# MONETARY POLICY REPORT

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## VOLUME XIV   NUMBER 2

The Central Bank of Trinidad and Tobago conducts monetary policy geared towards the promotion of low inflation and a stable foreign exchange market that is conducive to sustained growth in output and employment. This Report provides an account of how monetary policy actions support this objective, in light of recent economic developments.

# Table of Contents

# MONETARY POLICY REPORT

## December 2014

## PART I – Overview and Outlook

### Overview

The Central Bank of Trinidad and Tobago in the third quarter of 2014 began to position its monetary policy to address the potential impact of challenges arising domestically and internationally. With the non-energy sector on a sustainable growth path, as evidenced by 14 consecutive quarters of growth by the third quarter of 2014, the Bank's monetary policy deliberations evolved to consider the potential threats of a pick-up in inflationary pressures and the possible disruptive effects arising from narrow interest rate differentials on TT and US Treasury securities (**Table Ib**). As a result, the Bank made successive increases to its Repo rate, at its September and November 2014 Monetary Policy Committee meetings, after holding the rate at a record low for nearly two years.

Overall energy sector output remained constrained thus far in 2014 due to dismal performance over the first six months of the year. However, preliminary estimates for the third quarter point to a year-on-year rebound in energy sector output. After a series of shutdowns and stoppages which resulted in a sharp decline in energy sector production in the first half of 2014, the exploration and production and petrochemical sub-sectors recovered in the third quarter of 2014. This pick-up was able to mitigate some of the earlier declines witnessed in the sector.

Further, several non-energy indicators pointed to a robust level of domestic activity in the local economy. In the third quarter of 2014, the non-energy sector grew for the 14th consecutive quarter, led by advances in the distribution and finance sectors. The Central Bank of Trinidad and Tobago's September 2014 Business Confidence Survey (BCS), reported that the corporate sector is cautiously optimistic about the near- to medium-term prospects. According to latest data from the Central Statistical Office, the unemployment rate fell to a record low at the end of 2013. Further, the September 2014 BCS showed that the vast majority of businesses intend to retain or hire more workers over the next 12 months. Furthermore, private sector credit continued to strengthen into 2014, as the recovery in business lending consolidated as the year progressed. Concomitantly, consumer and real estate mortgage lending also remained relatively buoyant.

After a relatively sedate first six months of 2014, inflationary pressures picked up in the subsequent four months. The up-tick in inflation, however, was driven primarily by food prices. Core inflation, a more accurate measure of underlying inflation, decelerated from the first half of the year. Nevertheless, given high levels of consumer spending as evidenced by strong growth in consumer lending and a rapid increase in the sales of new motor vehicles, core inflationary pressures are expected to build over the medium-term. Further, the robust levels of Government spending budgeted in fiscal year 2014/15 may also contribute to inflation. In general, the potential threat from rising price levels was one of the main factors influencing the Bank's decision to increase the Repo rate in September and November 2014.

High liquidity levels in the financial system continued to be a source of concern for the Central Bank. As such, the Bank utilized several policy tools to contain the accumulation of excess liquidity in the system. In 2014, the Bank expanded its net open market operations of Treasury securities, facilitated the issue of a liquidity-sterilization Treasury bond in June 2014 and rolled over commercial banks' special fixed deposits which matured during the year thus far. The Bank continued to provide additional support to the foreign exchange market through increased sales of foreign exchange to authorised dealers. This in turn, resulted in an indirect removal of liquidity from the financial system.

Internationally, there was the familiar theme of uncertainty. The United States (US) shrugged off a dismal first quarter performance, rebounding strongly in the second and third quarters of 2014. Further, by the end of the third quarter of 2014, the US unemployment rate fell to the lowest level since September 2008. Given the robustness in the US economy, yields on longer-term US Treasury securities began to climb as investors anticipated the end of 'quantitative easing' (QE) by the end of October 2014, and an increase in the Federal Reserve's (Fed) policy rate by mid-2015. However, the news of deteriorating conditions in the Eurozone, and China's slowdown in the third quarter of 2014, overshadowed the positive development in the US. Disappointing economic news arising from Europe and China, mixed with geopolitical tensions in several parts of the world and the threat of the Ebola virus, dampened market sentiments. During October 2014, the VIX index spiked, the CDX high-yield and emerging market spread indices widened while the benchmark 10-year US Treasury yield plummeted.

In response to the increase in volatility, policy makers in the US and UK sought to calm markets. The Bank of England's Governor hinted that policy rate increases could be pushed beyond spring 2015 if economic conditions in the Eurozone remain weak. Moreover, a number of Fed Governors stated that monetary policy will remain supportive, indicating that a slowdown in the global economy could impact the US economic recovery. By the end of October 2014, market tensions eased and Treasury yields rebounded from the inter-month low as the Fed ended its QE programme. Higher US Treasury yields have implications for TT-US yield differentials. Narrow TT-US yield differentials have been of some concern to the Central Bank and was another key factor influencing the decision to increase its policy rate from September 2014.

Growth in the Eurozone and Japan has been relatively slow and somewhat anaemic. In order to avoid deflation, the European Central Bank (ECB) has taken aggressive steps by reducing interest rates, providing financing facilities for banks and engaging in asset purchasing programmes **(Table Ia)**. In its bid to revive credit markets, the ECB reduced its bank deposit rate into negative territory in June 2014 – making it the first major central bank to implement such a measure. Additionally, further rate cuts were made in September 2014. On the other side of the globe, the Japanese economy contracted in the second and third quarters of 2014 as the sales tax increase which was introduced in April 2014 served to dampen personal consumption. While the Bank of Japan announced an increase in its money supply expansion in October 2014, the third arrow of Prime Minister Shinzo Abe's "Abenomics" – structural reform – is yet to hit its target.

Emerging markets – recently considered the drivers of growth in the global economy – are now experiencing slower growth rates. China's attempts to rebalance its economy towards one led more by internal demand rather than by investment and trade, have resulted in some cooling in the world's second-largest economy. In the third quarter of 2014, China's real GDP growth slowed to the lowest level in five years, while inflation was below target. Meanwhile, Brazil and India have struggled because of the spill-over effects of capital outflows and depreciating currencies arising out of the Fed's QE tapering. After halting its monetary tightening cycle in early 2014, the Brazilian Central Bank (BCB) took markets by surprise with another rate increase in October 2014. The BCB is now faced with the two negative impacts of declining growth and inflationary pressures. In India, the Reserve Bank held its policy rate unchanged as the economy was poised to achieve its "loose" inflation target by January 2015. Following a dismal first quarter, India's real GDP gained momentum in the second quarter of 2014.

Closer to home, the English-speaking Caribbean continued to experience muted growth rates. As a result, regional central banks maintained an accommodative monetary policy stance during the first 10 months of 2014. A prolonged period of sluggish economic activity in the Caribbean region may have negative repercussions for Trinidad and Tobago's non-energy sector exports to the region.

## Outlook

The market turbulence experienced in mid-October 2014 suggests that despite the increased communication in the form of forward guidance by central banks, economic agents remain largely uncertain about the future path of the global economy. Several factors have contributed to the uncertainty facing the world economy; these include geopolitical tensions in Eastern Europe and the Middle East, economic stagnation in the Eurozone and Japan, cooling growth in China and the potential economic effects of the Ebola virus. Another dimension of ambiguity relates to the timing of monetary tightening in the US. In its Federal Open Market Committee meeting in October 2014, the Fed upgraded its assessment of the economy, but maintained that short-term rates will remain near zero for a “considerable time”. While many are of the view that the Fed remains on track to increase policy rates by mid-2015, some analysts question whether the US – and by extension the world economy – can stand firmly without the support of accommodative US monetary policy.

In 2014 thus far, the IMF has consistently lowered its forecast for global growth in 2014 and 2015, though marginally for the latter year. In its October 2014 World Economic Outlook, the IMF revised global growth downwards to 3.3 per cent in 2014, and 3.8 per cent in 2015 from its April 2014 projections of 3.6 per cent and 3.9 per cent, respectively. The downgrade was largely due to the flagging economies of the Eurozone, Japan and Russia.

On the domestic front, following growth of approximately 2.0 per cent in 2013, it was generally expected that the economy would have further strengthened in 2014. Though performance in the non-energy sector was sufficiently robust, overall economic prospects for the year as a whole have been tempered by low energy production over the first six months of 2014. Looking further ahead, improved production in the third quarter of 2014, and the coming on stream of new production from Repsol and Incremental Production Service Contract (IPSC) operators auger well for growth prospects in 2015. Meanwhile, growth in the non-energy sector is expected to continue in 2015. On-going public sector projects such as the Point Fortin Highway, the Energy Port at Galeota, the Children's Hospital and Multi-Training Facility in Couva and new projects like the Dry Dock Facility at Sullivan Island are expected to contribute positively to the non-energy sector in the medium-term. The private sector has also undertaken significant investment. In addition to the cinemas and malls being developed, construction on the Massy/ Mitsubishi Dimethyl-ether project is expected to begin in early 2015. Also, results from the September 2014 BCS indicated that 50 per cent of large businesses expected to undertake capital investments in the coming year and 55 per cent of all businesses expected improvements in the local economy.

With improving growth prospects and as the economy gains momentum there is also the possibility of higher inflation in 2015. Relatively tight labour market conditions, robust personal consumption and high levels of Government spending, when combined with an already liquid financial system, can create an environment conducive for a rapid build-up of inflation. In its September 2014 Monetary Policy Announcement, the Bank highlighted inflation and rising US interest rates as two of the major challenges that the domestic economy may confront in 2015. In October, another potential risk has emerged in the form of falling oil prices. A combination of waning global demand and rising US oil inventories has seen oil prices drop by around 25 per cent from June to October 2014. An extended decline in oil prices has the potential to result in a fall in other energy prices, specifically LNG and natural gas. As a result, it is worth monitoring LNG shipments to destination markets where natural gas is indexed to crude oil prices, as well as the volume of cargo that is sold on contract or spot markets. Low energy prices not only impact the energy sector, but may also present challenges for the non-energy sector, with implications for Government's revenues, public debt levels, foreign reserves accumulation and private consumption.

In the medium-term, given the threat of higher inflation and rising US interest rates, the Central Bank positioned its monetary policy to confront these challenges. However, given the dynamic economic environment and the new risks stemming from lower energy prices and dimming global prospects, the Bank will continue to closely monitor both domestic and international developments in order to undertake any necessary course of action to ensure stable prices and balanced growth. Additionally, the Bank will continue to utilize available tools to address the large liquidity overhang in the financial system.

**Table Ia**
**Key Central Bank Policy Rates**
**(Per Cent Per Annum)**

| | Current Rate | Last Change | Amount of Change |
|---|---|---|---|
| United States | 0 to 0.25 | Dec-08 | -0.75 |
| Euro Area | 0.05 | Sep-14 | -0.10 |
| United Kingdom | 0.50 | Mar-09 | -0.50 |
| Japan | 0 to 0.10 | Oct-10 | 0 to -0.10 |
| China | 5.60 | Nov-14 | -0.40 |
| India | 8.00 | Jan-14 | +0.25 |
| Brazil | 11.25 | Oct-14 | +0.25 |

Source: Bloomberg.

## Table Ib
## Summary Economic Indicators for 2013-2014

| | Jan-Sep 2013 | Jan-Sep 2014 |
|---|---|---|
| **REAL SECTOR ACTIVITY** | | |
| **Energy Sector** | | |
| Total Depth Drilled (metres) | 88,226 | 83,671 |
| Crude Oil Production (b/d) | 81,155 | 80,692 |
| Crude Oil Exports (bbls) | 9,460 | 8,782 |
| Refinery Throughput (b/d) | 132,113 | 103,554 |
| Natural Gas Production (mmcf/d) | 4,163 | 4,109 |
| Natural Gas Utilization (mmcf/d) | 3,865 | 3,821 |
| LNG Production (cubic metres) | 24,763 | 24,093 |
| Fertilizer Production (000 tonnes) | 3,819 | 4,052 |
| Fertilizer Exports (000 tonnes) | 3,532 | 3,710 |
| Methanol Production (000 tonnes) | 4,105 | 4,169 |
| ECPI (Jan 2007 = 100) | 139 | 143 |
| **Non-Energy** | | |
| Local Sales of Cement (000 tonnes) | 474,675 | 512,023 |
| Motor Vehicle Sales | 12,233 | 13,764 |
| Daily Job Vacancy Advertisements | 795 | 1,027 |
| **Prices** | | |
| *Year-on-Year Per Cent Change* | | |
| Producer Prices | 1.8 | 2.1 |
| Headline Inflation* | 2.7 | 9.0 |
| Food Inflation* | 3.7 | 18.2 |
| Core Inflation* | 1.9 | 1.4 |
| **Monetary**** | | |
| *Year-on-Year Per Cent Change* | | |
| Private Sector Credit | 3.2 | 6.7 |
| Consumer Lending | 5.7 | 8.4 |
| Business Lending | -3.7 | 3.8 |
| Real Estate Mortgages | 14.2 | 11.5 |
| M-1A | 29.8 | 10.6 |
| M-2 | 13.2 | 7.3 |
| Average Commercial Banks' Excess Reserves ($ million) | 8,272.9 | 6,059.4 |
| TT 91-day Treasury Bill Rate (per cent) | 0.14 | 0.11 |
| **Financial Stability**** | | |
| Non-Performing Loans (per cent) | 4.6 | 4.3 |
| Capital Adequacy Ratio (per cent) | 24.1 | 23.4 |
| **Capital Market** | | |
| Composite Price Index (1983 = 100)* | 1,179.0 | 1,146.0 |
| Volume of Shares Traded (million)*** | 85.3 | 78.7 |
| Mutual Funds under management ($ billion) | 40.1 | 41.4 |
| **External** | | |
| *US$ Million* | | |
| Sales of Foreign Exchange to Public *** | 5,651.1 | 5,863.2 |
| Purchases of Foreign Exchange from Public *** | 4,694.3 | 4,571.7 |
| CBTT Sales to Authorized Dealers *** | 1,115.0 | 1,440.0 |
| Net Official Reserves* | 9,360.6 | 11,106.8 |

Sources: Central Bank of Trinidad and Tobago, Central Statistical Office of Trinidad and Tobago and Ministry of Energy and Energy Affairs.

* As at October.
** As at September.
*** For the period January-October.

# PART II – International and Regional Monetary Policy Developments

## Introduction

The global recovery remains uneven and vulnerable to setbacks. Despite a weak first half, global activity is projected to improve slightly in the coming months, supported by the US and the UK. Prospects in the Eurozone, Japan and a number of emerging markets have deteriorated somewhat over the recent past and could provide a drag on the global economy. The recent divergence in monetary policy among advanced economies, as well as heightened speculation about the timing and extent of US monetary policy normalization, has spurred volatility in global financial markets and created disruptive capital outflows for emerging markets. For a select few of the larger emerging market nations, this has resulted in weaker currencies and strong price pressures prompting central banks to take measures to curb inflation. On the other hand, some Latin American central banks have targeted policies to support growth as waning global demand softened prices of their main export commodities.

## International

The Federal Reserve (Fed) opted to end its five-year, $4.5 trillion "quantitative easing" (QE) programme in October 2014, as the US recovery substantially outpaced those of the other advanced economies. Following a drop in the first quarter, the US economy rebounded strongly, expanding by 4.2 per cent and 3.9 per cent on an annualized basis, in the second and third quarters of 2014, respectively. The US unemployment rate fell to 5.9 per cent in September 2014 – the lowest post-crisis level. At its Federal Open Market Committee meeting at the end of October 2014, the Fed upgraded its assessment of the US economy, but maintained its commitment to keep interest rates low for a "considerable time," as expected lower inflation and a weak world economy could undermine the pace of US expansion.

During January to October 2014, financial markets in the US exhibited significant levels of volatility as investors were confronted with mixed economic signals. On the heels of disappointing economic data from Europe, Japan and to some extent China, in mid-October 2014 the VIX index rose above 25.0 points for the first time since June 2012. Additionally, the Markit's CDX North America Investment Grade Index on five-year corporate bonds experienced a spike in October 2014, indicating a widening credit spread. With markets reacting to the prospects of slower global growth, the yield on the 10-year US Treasury note fell below 2.0 per cent for the first time since May 2013. By the end of the October 2014 however, the US 10-year yield increased to 2.35 per cent following positive US data and the end of the Fed's QE programme.

Economic performance in the UK has been among the strongest in advanced economies. On a year-on-year basis, the UK economy grew by 3.0 per cent in the third quarter of 2014. On the other hand, the unemployment rate fell to 6.0 per cent in August 2014 from a high of 7.2 per cent at the end of 2013. Inflation remained below the Bank of England's (BoE) 2.0 per cent target in the first nine months of 2014. In its Monetary Policy Committee meeting in September 2014, the BoE kept its policy rate steady at 0.5 per cent and maintained its asset purchase programme at £375 billion (US$630 billion).

The stalled recovery in the Eurozone and the impending threat of deflation has prompted the European Central Bank (ECB) to further ease monetary policy. As a result, the ECB cut its policy rates in June and September, taking the benchmark rate on its main refinancing operations to 0.05 per cent in September from 0.25 per cent at the start of the year. The ECB was also the first major central bank to implement negative interest rates, cutting the rate on its deposit facility to -0.10 per cent in June and -0.20 per cent in September 2014. The ECB also expanded its balance sheet, making approximately €700 billion (US$889 billion) available to banks in the form of financing operations and asset purchases. The ECB expects that these measures will enhance the functioning of the monetary policy transmission, support the provision of credit to the broad economy and raise inflation to 2.0

per cent over the medium-term. In October 2014, the Eurozone remained dangerously close to deflation, with inflation measuring just 0.4 per cent on a year-on-year basis.

The Japanese economy is now in its fourth recession since 2008, as a result of unexpected adverse effects from the April 2014 sales tax hike. Following the sales tax increase, growth declined by 1.8 per cent and 0.4 per cent (quarter-on-quarter) in the second and third quarters of 2014, respectively. The slump occurred despite the Bank of Japan's (BoJ) efforts to bolster the faltering economy by accelerating its quantitative and qualitative monetary easing (QQME) policies aimed at achieving a 2.0 per cent inflation goal by 2015. In October 2014, the BoJ announced that it will increase the pace of its purchases of Japanese Government Bonds in an attempt to increase the money supply by an annual level of 80 trillion yen (US$730 billion) from the originally targeted level of 60 trillion to 70 trillion yen (US$670 billion).

### *Emerging Economies*

Following the former Fed Governor's April 2013 speech, which first hinted at the unwinding of the Fed's QE programme, emerging markets began to experience the effects of international portfolio rebalancing that diverted capital away from these economies. This development placed pressures on emerging market currencies which resulted in inflation and created balance of payment imbalances. To limit the impact of further capital flow volatility arising out of monetary policies in the advanced economies, the BRICS countries of Brazil, Russia, India, China and South Africa constituted a Development Bank and established the Contingency Reserve Arrangement (CRA) in July 2014. The CRA will have resources of US$100 billion, with contributions from China (US$41 billion), Brazil, Russia and India (US$18 billion each) and South Africa (US$5 billion). According to this arrangement, members can draw from the fund when foreign exchange reserves fall below a critical level or are depleted.

In China, economic growth fell to a five-year low of 7.3 per cent year-on-year by the third quarter of 2014, prompting concerns of a more protracted slowdown. As a counteractive measure, the People's Bank of China (PBOC) lowered its benchmark interest rate for the first time since July 2012, reducing the rate by 0.4 percentage points to 5.6 per cent. The bold monetary policy step follows other modest measures to increase lending that have had a limited impact on growth. In November 2014, the Bank also reduced the 14-day Repo rate for the third time in as many months, and in September second-home buyers were permitted a 30.0 per cent discount on mortgage rates, in a bid to avert a deeper slide in the housing market. Furthermore, PBOC and Chinese regulators have also reduced down payment levels to 30.0 per cent from previous levels of between 60.0 to 70.0 per cent. Importantly, in its latest outlook, Moody's Investors Service has warned that a steep housing downturn in China could derail the global recovery.

The Indian economy grew faster than expected in the second quarter of 2014, recording the highest growth rate since the fourth quarter of 2011. Meanwhile, India's inflation rate (year-on-year) slowed to 6.5 per cent in September, from 7.8 per cent in the previous month. With inflation set to hit the 8.0 per cent target by January 2015, the Reserve Bank of India (RBI) has kept its policy rate firmly at 8.0 per cent since the start of the 2014 but has introduced measures to improve liquidity. As a result, the statutory liquidity ratio (SLR) of scheduled commercial banks was reduced by 50 basis points to 22.5 per cent. While the Indian rupee has been relatively stable over the past year, in October 2014 it was down by 14.0 per cent when compared to levels in April 2013.

Following a pause in a 12-month (April 2013 to March 2014) monetary tightening cycle, the Central Bank of Brazil took markets by surprise in October 2014, by increasing its key policy rate, the SELIC, by 25 basis points to 11.25 per cent. The rate increase came on the heels of the re-election of President Dilma Rousseff for a second term. Despite a struggling economy, the BCB indicated that the intensification of price pressures was the major challenge facing the country. In September 2014, headline inflation rose to 6.75 per cent (year-on-year), above the BCB's target band (4.5 per cent + 2.0 per cent). A weakening currency was the major cause of higher price levels as the Brazilian Real depreciated by over 10 per cent in the 12 months leading up to October 2014. On the other hand, and in order to further support economic growth by encouraging lending, the BCB reduced its reserve requirements on term deposits to 60.0 per cent.

The Central Bank of Russia (CBR) has aggressively increased its policy rate to combat higher inflation levels and the negative impacts on its currency as a result of geopolitical tensions. In October 2014, the CBR increased its key interest rate by 150 basis points to 9.5 per cent. This represented the fourth rate increase for this year and compares with a policy rate of 5.5 per cent at the start of 2014. With the Rouble losing 30 per cent of its value in the 10 months leading up to October, year-on-year headline inflation accelerated to 8.0 per cent in September 2014, when compared to approximately 6.0 per cent at the beginning of the year. Facing higher inflationary pressures, the South African Reserve Bank also increased its policy rate by 75 basis points to 5.75 per cent in the first 10 months of 2014.

## Regional

Monetary policy in the Caribbean region remained accommodative to support economic activity **(Table IIa)**. While the majority of the regional central banks did not adjust their policy rates, there was selected intervention in the foreign exchange markets in order to ensure currency stability. In a similar stance, monetary policy in Latin American countries remained accommodative as economies grappled with poor macroeconomic fundamentals, declining reserves and depreciating currencies. Meanwhile, the end of the Fed's quantitative easing programme and timing of its increase in interest rates have highlighted concerns that there may be potential changes in the currency flows to select Latin American economies.

Growth in Suriname and Guyana though still stronger than the rest of the region, is expected to slow as gold and agricultural commodity prices soften. To date, Jamaica has successfully negotiated the requirements of the

International Monetary Fund's (IMF) Extended Fund Facility (EFF), obtaining approval for the fifth successive drawdown in September 2014. With economic conditions slowly recovering thus far in 2014, Jamaica successfully accessed the international capital markets, issuing its largest US-dollar bond in the country's history. Over the recent past, Barbados has experienced challenging economic conditions, including limited fiscal space and a tight external account position. Facing severe budget constraints, the Barbadian Government scaled back on expenditure which led to a reduction in the number of public servants. As a result, unemployment rose and the Barbadian economy stagnated in the second quarter of 2014.

Facing slower output, the central banks of Mexico, Peru and Chile embarked on policy rate reductions over the first 10 months of 2014. Copper exporters such as Chile and Peru continue to experience the negative effects of lower demand and prices of their shipments to China. In a bid to defend its currency, the Central Bank of Argentina sold US$407 million to the public in August and September 2014. In addition, commercial banks were ordered to reduce their US dollar holdings and signed an US$800 million foreign-exchange swap agreement with the Chinese Central Bank. Meanwhile Venezuela continues to struggle with macroeconomic challenges of stagnant growth, consumer price inflation and a lack of investment. The country's level of reserves has deteriorated, signalling a decline in the ability of the Venezuelan Government to service its external debt.

**Table IIa**
**Key Central Bank Policy Rates in the Region**
**(Per Cent Per Annum)**

| | Current Rate | Last Change | Amount of Change |
|---|---|---|---|
| Trinidad and Tobago[1] | 3.25 | Dec. 01 | 0.25 |
| Barbados[2] | 7.00 | Jun. 09 | -1.00 |
| Jamaica[3] | 5.75 | Feb. 13 | -0.50 |
| Guyana[4] | 5.00 | Mar. 13 | -0.25 |

Sources: Central Banks of Trinidad and Tobago, Guyana, Barbados and Bloomberg.

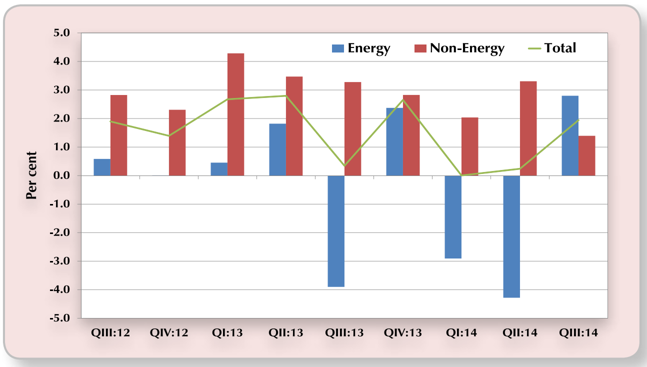
1 Repo rate as at December 2014.
2 Bank rate as at July 2014.
3 30-day CD Rate as at July 2014.
4 Bank rate as at August 2014.

# PART III – Domestic Economic Conditions

## a) Gross Domestic Product

During the first nine months of 2014, overall economic activity in the domestic economy has been mired by production stoppages in the energy sector. Robust performances in the non-energy sector, however, have buttressed the economy, counteracting the sharp decline in the energy sector over the first half of the year. Additionally, the energy sector rallied in the third quarter of 2014 and this helped ease some of the earlier declines within the sector. Provisional estimates from the Central Bank's Quarterly Real Gross Domestic Product (QGDP) Index suggest that on a year-on-year basis, the domestic economy grew by 0.7 per cent over the first three quarters of 2014, as growth of 1.9 per cent in the third quarter buoyed relatively flat growth conditions over the first half of the year (Chart IIIa).

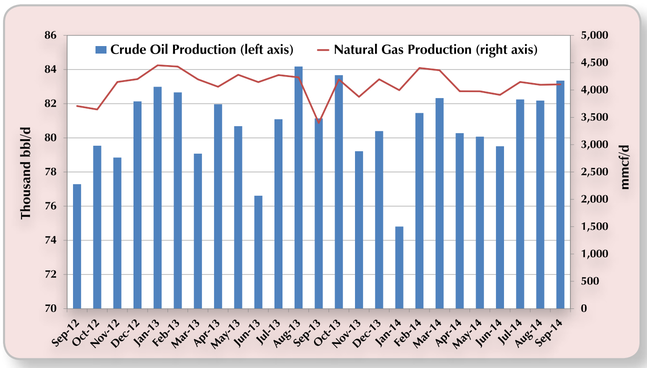
**Chart IIIa**
**Trinidad and Tobago - Real GDP Growth**
(Year-on-Year Per Cent Change)




Source: Central Bank of Trinidad and Tobago.

For the first nine months of 2014, the energy sector declined on account of downtime by the country's two largest natural gas producers over the majority of this period (Chart IIIb). On a year-on-year basis, the energy sector contracted by 1.5 per cent over January to September 2014. Growth in the third quarter amounting to 2.8 per cent cushioned the economy from declines of 2.9 per cent and 4.3 per cent in the first and second quarters of 2014, respectively. The exploration and production sub-sector contracted 1.3 per cent over the first three quarters of 2014 because of depressed natural gas activity. Increased natural gas output of 3.6 per cent (year-on-year) in the third quarter was unable to reverse the declines from earlier in the year. The refining sub-sector declined an average of 4.2 per cent over the January to September 2014 period on account of maintenance work at Atlantic LNG and lower refinery throughput at Petrotrin. However, preliminary estimates for the third quarter showed initial signs of recovery with a 5.4 per cent increase in LNG output. Petrochemical output increased by an average of 3.7 per cent during the first nine months of 2014.

**Chart IIIb**
**Crude Oil and Natural Gas Production**




Source: Ministry of Energy and Energy Affairs.

The non-energy sector remained buoyant, expanding for the 14th consecutive quarter to September 2014. Average growth of 2.2 per cent (year-on-year) over the first three quarters of 2014 was attributed to robust activity in the construction, distribution and finance sub-sectors. The distribution sub-sector increased by an average 2.9 per cent over the period, mainly reflecting increases in the local sales of new motor vehicles (12.5 per cent). Further, buoyant activity in the commercial bank sub-industry fuelled growth in the finance, insurance and real estate sector which increased by 3.2 per cent. Likewise, the construction sector posted growth of 3.1 per cent over the nine-month period, despite a decline of 2.0 per cent in the third quarter of 2014 which weighed on strong growth in the previous six months.

The manufacturing sector trended upwards to 1.2 per cent over the first nine months of the year, as higher production of cement and other construction-related products boosted the chemicals and non-metallic sub-industry. Untapped potential within the sector continued to be high, as manufacturing companies utilized just below two thirds of their existing capacity **(Table IIIa)**. The capacity utilization rate for firms in the chemicals and non-metallic minerals sub-industry however, increased from 63.4 per cent to 72.7 per cent during the second quarter of 2014. Additionally, the agriculture sector grew by an average of 3.1 per cent over the nine month period.

**Table IIIa**
**Capacity Utilization Rate**
**Manufacturing Sector**
**(Per Cent)**

| | 2012 | | | | 2013 | | | | 2014 | |
|---|---|---|---|---|---|---|---|---|---|---|
| | Mar | Jun | Sep | Dec | Mar | Jun | Sep | Dec | Mar | Jun |
| Manufacturing | 63.7 | 65.4 | 65.1 | 64.5 | 62.3 | 67.3 | 65.5 | 62.4 | 62.5 | 63.2 |
| Food, Drink & Tobacco | 70.1 | 72.3 | 69.1 | 71.0 | 67.7 | 74.5 | 72.5 | 61.5 | 63.4 | 61.5 |
| Chemicals and Non-Metallic Minerals | 50.5 | 51.2 | 62.6 | 63.3 | 60.6 | 64.4 | 60.0 | 67.5 | 63.4 | 72.7 |
| Assembly-Type and Related Industries | 57.0 | 61.1 | 54.9 | 50.8 | 55.8 | 54.0 | 56.8 | 54.2 | 57.0 | 48.8 |

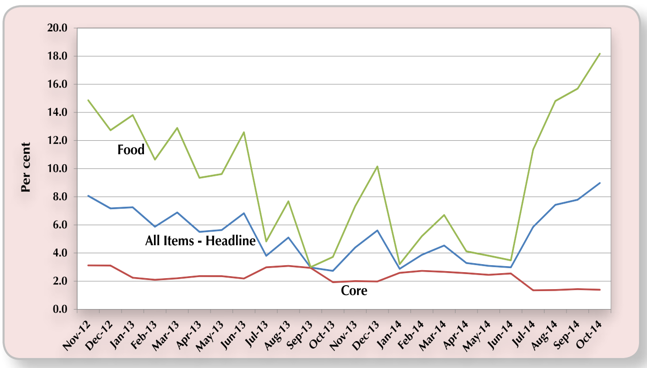
Source: Central Bank of Trinidad and Tobago.

The business community remained optimistic, but guardedly so, in their outlook for the economy of Trinidad and Tobago over the next six to 12 months. This was according to the results of the September 2014 Business Confidence Index (BCI) which increased to +37 in the third quarter of 2014 from +32 in the second quarter of 2014. The survey indicated that over the coming year, 55 per cent of the respondents anticipated improvements in the local economy, while 65 per cent expected their financial outlook to improve over the next 12 months. Approximately one half of the business community expressed confidence with respect to an improving global economy and the majority of firms (93 per cent) expected to maintain or increase their workforce over the next 12 months. Sector indices showed that firms producing wood and related products were the most confident (with a BCI Index value of +69) about the prospects for the economy followed by the Finance, Insurance and Real Estate sector (+53) and the Hotels and Guest Houses sector (+42). Businesses in Central Trinidad and in Tobago remained the most confident about the business and economic outlook in the short term. For the second consecutive quarter, the business respondents indicated that the economic environment, a shortage of skilled workers and increased competition from local firms were the main constraints to local business activity.

## b) Prices

After a period of subdued price increases during the first half of this year, headline inflation gained momentum during the third quarter. By October 2014, headline inflation rose on a year-on-year basis to 9.0 per cent after averaging 3.4 per cent during the first six months. This change is explained primarily by an increase in food prices since core inflation generally slowed over the third quarter of 2014 (Chart IIIc).

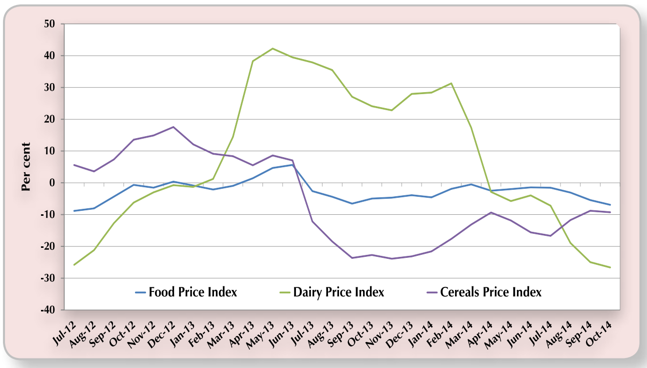
**Chart IIIc**
**Index of Retail Prices**
**(Year-on-Year Per Cent Change)**




Source: Central Statistical Office of Trinidad and Tobago.

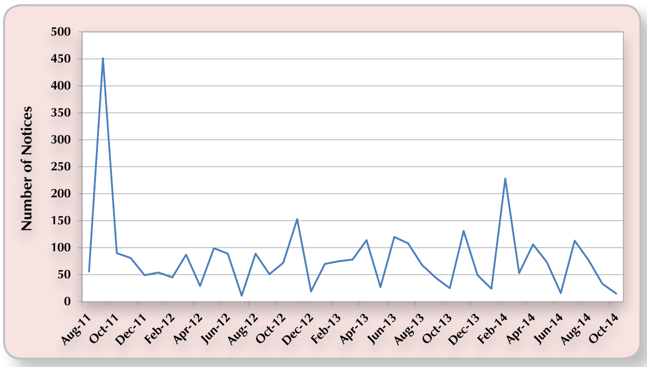
During the first 10 months of 2014, core inflation has been relatively well-contained. Despite a slight increase during the first few months, core inflation exhibited a general downward trend towards the latter part of 2014. On a year-on-year basis, core inflation decelerated to 1.4 per cent in October from a 10-month high of 2.7 per cent in February 2014. One of the major drivers of this slowdown was the recreation and culture sub-index,

**Chart IIId**
**FAO Food Price Index**
**(Year-on-Year Per Cent Change)**



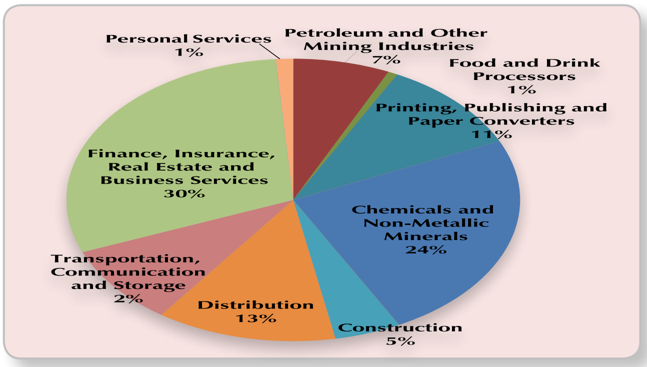

Source: Food and Agriculture Organization.

**Chart IIIe**
**Retrenchment Notices Registered**




Source: Ministry of Labour and Small and Micro Enterprise Development.

**Chart IIIf**
**Retrenchment Notices Registered By Sector**
**January - October 2014**
**As a Proportion of Total Notices Filed**




Source: Ministry of Labour and Small and Micro Enterprise Development.

which experienced a decline of 2.5 per cent by October. Other notable categories recording slower increases in the price level in October were the transport and health sub-indices.

In contrast to core inflation, food inflation accelerated sharply since July 2014. During the 12 months to October 2014, food inflation rose to 18.2 per cent after averaging 4.4 per cent over the first six months of 2014. Vegetable prices, historically one of the most volatile components in the food sub-index, rose by 17.3 per cent in October 2014. There were also faster price increases for fruit and food products not elsewhere classified as at October 2014. Early indicators suggest this rise in domestic food inflation was the result of domestic shocks and not necessarily international food prices. In fact, the Food and Agriculture Organization's (FAO) Food Price Index declined by 6.9 per cent (year-on-year) in October; this was due to sharp price contractions within the sub-indices of dairy (26.6 per cent) and cereals (9.3 per cent) **(Chart IIId)**. On the domestic front, evidence suggests that the cessation of planting at Caroni Green negatively impacted the supply of vegetables in the third quarter, placing upward price pressures on this sub-category.

## c) Labour Market

In the absence of official labour market statistics for 2014, retrenchment notices (an indicator of job separation), along with sentiments from the business community suggests some stability in the labour market. Retrenchment notices increased by a mere 1.2 per cent in the first 10 months of 2014 compared with the corresponding period a year earlier **(Chart IIIe and Chart IIIf)**. Further, the Central Bank of Trinidad and Tobago's September 2014 Business Confidence Index indicated that 93.0 per cent of businesses surveyed expect to maintain or increase their workforce over the next 12 months. Approximately 60 per cent of miscellaneous manufacturing and personal services companies intend to hire additional staff over the coming year. Furthermore, roughly 54.0 per cent of energy and energy-related businesses surveyed stated that they intend to increase their workforce over the next 12 months.

Latest information from the Central Statistical Office (CSO) indicated that the annual unemployment rate fell to 3.7 per cent in 2013 (a historic low) from 4.9 per cent in 2012. The number of persons with jobs increased by 2.0 per cent to 626,300 persons, while the number of unemployed persons declined by 25.3 per cent to 23,900 persons. Consistent with economic developments, significant job growth occurred in Services (4,000 persons), Construction (3,875 persons), Transport, Storage and Communication (3,050 persons) and Wholesale and Retail Trade, Restaurants and Hotels (2,425 persons). In contrast, job losses were concentrated in the Manufacturing (150 persons) and Agriculture (925 persons) sectors.

## d) Fiscal Operations

Preliminary estimates of Central Government's operations during fiscal year 2013/2014 pointed to a more favourable outturn than initially anticipated. According to the revised estimates, the fiscal accounts registered a deficit of $4,876.6 million (2.7 per cent of GDP) during October 2013 to September 2014 **(Table IIIb)**. This was much lower when compared to original budget estimates of $6,357.1 million and was primarily due to significantly higher collections from the non-energy sector. For the fiscal year 2014/2015, a deficit of $4,313.3 million or 2.3 per cent of GDP is budgeted. The Government plans to finance the budgeted deficit by borrowing 86.6 per cent externally and 13.4 per cent domestically.

While the 2014/2015 budget is expansionary and is designed to support sustained economic growth, the fiscal stimulus is lower relative to previous budgets. The non-energy fiscal balance is anticipated to fall from 19.5 per cent in fiscal year 2013/2014 to 17.9 per cent of GDP in 2014/2015. Nevertheless, the implementation of various infrastructure projects under the capital programme is estimated to cost $8.2 billion in fiscal year 2014/2015, which could provide a fillip to growth. Some of the major projects targeted for this fiscal year include the Energy Port at Galeota, the Children's Hospital and Multi-Training Facility in Couva, as well as the National Oncology Centre.

## Table IIIb
## Summary of Central Government Fiscal Operations
**(TT$ Million)**

| | 2010/2011 | 2011/2012 | 2012/2013[r] | 2013/2014[re] | 2014/2015[b] |
|---|---|---|---|---|---|
| **Revenue** | **47,500.6** | **49,277.9** | **52,760.1** | **59,911.7** | **60,351.2** |
| Energy | 27,340.9 | 26,625.8 | 26,603.6 | 29,966.0 | 29,024.5 |
| Non-Energy | 20,159.7 | 22,652.1 | 26,156.6 | 29,945.7 | 31,326.7 |
| **Expenditure** | **48,602.5** | **51,474.8** | **57,668.5** | **64,788.3** | **64,664.5** |
| Current | 41,649.9 | 44,487.1 | 49,228.7 | 55,658.2 | 56,502.5 |
| Wages and salaries | 7,179.7 | 7,282.3 | 9,171.5 | 9,113.9 | 9,260.8 |
| Goods and services | 6,504.3 | 7,061.6 | 7,180.1 | 9,034.2 | 9,915.8 |
| Interest payments | 2,866.4 | 2,937.1 | 2,808.7 | 2,984.3 | 3,006.6 |
| Transfers and subsidies | 25,099.5 | 27,206.1 | 30,068.4 | 34,525.8 | 34,319.3 |
| Capital expenditure and net lending | 6,952.6 | 6,987.7 | 8,439.8 | 9,130.1 | 8,162.0 |
| **Overall Non-Energy Balance** | **-28,442.8** | **-28,866.1** | **-31,512.0** | **-34,842.6** | **-33,337.8** |
| **Overall Balance** | **-1,101.9** | **-2,196.9** | **-4,908.4** | **-4,876.6** | **-4,313.3** |
| Total Financing (net) | 1,101.9 | 2,196.9 | 4,908.4 | 4,876.6 | 4,313.3 |
| Net Foreign Financing | 545.2 | 1,054.1 | -155.1 | 3,267.7 | 3,735.8 |
| Net Domestic Financing | 556.6 | 1,142.8 | 5,063.5 | 1,608.9 | 577.5 |
| *Of which: Transfers to Heritage and Stabilization Fund* | *2,890.0* | *1,332.1* | *271.7* | *0.0* | *0.0* |
| *(In Per Cent of Fiscal Year GDP)* | | | | | |
| **Revenue** | **31.5** | **31.3** | **30.8** | **33.5** | **32.3** |
| Energy | 18.1 | 16.9 | 15.5 | 16.8 | 15.5 |
| Non-Energy | 13.4 | 14.4 | 15.3 | 16.7 | 16.8 |
| **Expenditure** | **32.2** | **32.7** | **33.7** | **36.2** | **34.6** |
| Current | 27.6 | 28.2 | 28.8 | 31.1 | 30.3 |
| Wages and salaries | 4.8 | 4.6 | 5.4 | 5.1 | 5.0 |
| Goods and services | 4.3 | 4.5 | 4.2 | 5.1 | 5.3 |
| Interest payments | 1.9 | 1.9 | 1.6 | 1.7 | 1.6 |
| Transfers and subsidies | 16.6 | 17.3 | 17.6 | 19.3 | 18.4 |
| Capital expenditure and net lending | 4.6 | 4.4 | 4.9 | 5.1 | 4.4 |
| **Overall Non-Energy Balance** | **-18.9** | **-18.3** | **-18.4** | **-19.5** | **-17.9** |
| **Overall Balance** | **-0.7** | **-1.4** | **-2.9** | **-2.7** | **-2.3** |
| Total Financing (net) | 0.7 | 1.4 | 2.9 | 2.7 | 2.3 |
| Net Foreign Financing | 0.4 | 0.7 | -0.1 | 1.8 | 2.0 |
| Net Domestic Financing | 0.4 | 0.7 | 3.0 | 0.9 | 0.3 |
| *Of which: Transfers to Heritage and Stabilization Fund* | *1.9* | *0.8* | *0.2* | *0.0* | *0.0* |
| **Memorandum Items** | | | | | |
| Nominal GDP (in TT$ Million, FY) | 150,868.4 | 157,646.1 | 171,217.6 | 178,783.6 | 186,656.8 |

Sources: Ministry of Finance and the Economy and Central Bank of Trinidad and Tobago.

r Revised.
re Revised Estimates.
b Budgeted data based on an oil price of US$80 per barrel and natural gas price of US$2.75.

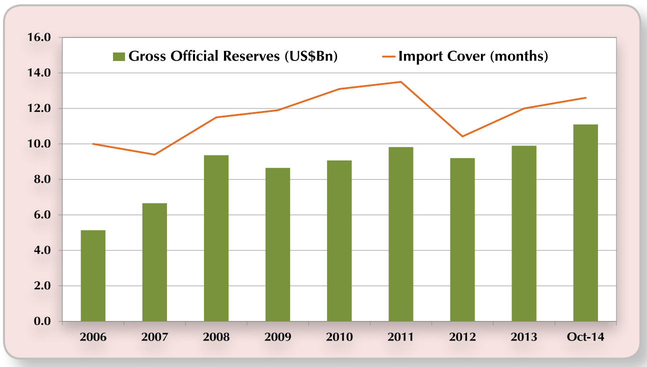
The 2014/15 National Budget has implications for monetary policy. Firstly, the increase in the number of fiscal incentives outlined in the budget (including increases in the Public Assistance Grant, the Disability Grant, the personal allowance for individuals aged 60 and over, the Senior Citizens Pension and the creation of the Baby Fund), as well as the planned capital projects may place upward pressure on demand and prices. Secondly, although the net domestic budgeted deficit is lower than the previous year, the additional Government spending can add to an already liquid financial system. With respect to debt levels, preliminary projections indicate that total public sector debt as a per cent of GDP will rise to 43.8 per cent in fiscal year 2014/2015 (the corresponding figure for fiscal year 2013/2014 was 42.4 per cent), while the external debt is expected to increase to 10.0 per cent of GDP from 7.3 per cent of GDP one year earlier.

## e) External Accounts

*(Data in this section are in US dollars unless otherwise stated)*

During the first six months of 2014, the balance of payments registered an overall surplus of $318.2 million, an improvement from the $195 million surplus recorded in the corresponding period in 2013. At the end of June, gross official reserves stood at $10,305.2 million, representing 11.8 months of import cover. The current account, however, posted a smaller surplus of $151.8 million when compared with the same period one year earlier. The smaller current account surplus reflected a lower merchandise trade balance arising mainly from decreased natural gas and crude oil production levels and higher net outflows of investment income. On the other hand, the capital and financial account recorded a surplus of $166.4 million compared with a deficit of $770.4 million in the first half of 2013. Net foreign direct investment increased slightly to $397.1 million, partly due to higher reinvestments by energy companies. Meanwhile, portfolio investment recorded a net outflow of $93.1 million, due to increased purchases of foreign long-term debt securities by the financial sector.

**Chart IIIg**
**Trinidad and Tobago Official Gross Reserves**




Source: Central Bank of Trinidad and Tobago.

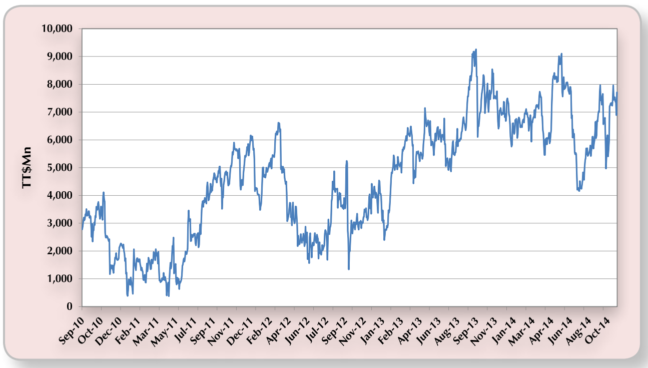
The latest information based on the change in international reserves suggests that the external accounts registered an overall surplus of $1,119.8 million in the period January to October 2014. This was much higher than the surplus ($159.9 million) in the corresponding period in the previous year and was mainly due to the sale of an asset to a non-resident. The level of gross official reserves rose to US$11,106.8 million or 12.6 months of prospective imports of goods and non-factor services as at October 2014 **(Chart IIIg)**.

# PART IV - Monetary and Financial Sector Developments

## Monetary Developments

Since the May 2014 Monetary Policy Report publication, the Central Bank's monetary policy stance has been largely supportive of the domestic economy. By September 2014 however, evidence suggested that conditions for sustained growth were well entrenched in Trinidad and Tobago. By September 2014, the non-energy sector had recorded 14 consecutive quarters of growth. Business lending has recovered in 2014 to date, while the economic performance of the US, a key trading partner, improved significantly. On the other hand, as growth prospects improved, potential threats have also emerged. Inflation has picked up due to food prices, while strong consumer demand as evidenced by sharp increases in new motor vehicles sales and consumer loans, coupled with robust Government spending expected in the new fiscal year, may place upward pressures on core inflation. In addition, if the US economy strengthens as expected, the Fed has hinted that it is willing to increase its policy rate in 2015. Against this backdrop, the Bank felt that it was appropriate to begin to withdraw from its ultra-accommodative monetary policy stance. Therefore, the Bank increased the Repo rate by 25 basis points to 3.00 per cent in September 2014 and further increased the rate by 25 basis points to 3.25 per cent following its November 2014 Monetary Policy Committee Meeting.

**Chart IVa**
**Commercial Banks: Excess Reserves**




Source: Central Bank of Trinidad and Tobago.

These increases in the Repo rate signal the end of an era of record low interest rates. As at October 2014 however, there was little change in domestic money market interest rates and the median commercial bank prime lending rate remained at 7.5 per cent. The prevalence of high liquidity levels kept money markets inactive and by so doing, weakened the policy rate pass-through effect. Commercial banks' excess reserves held at the Central Bank averaged roughly \$6.7 billion daily over the first 10 months of 2014, compared with \$6.0 billion in the corresponding period of 2013 **(Chart IVa)**. Over the period January to October 2014, net domestic fiscal injections added $9.3 billion into the system, while the maturity of two Central Government bonds previously issued for liquidity absorption purposes, also returned approximately $1.5 billion into the system **(Table IVa)**.

## Table IVa
## Fiscal Injections and Liquidity Absorption
**(TT$ Million)**

| | 2010 | 2011 | 2012 | 2013 | Jan-Oct-13 | Jan-Oct-14 |
|---|---|---|---|---|---|---|
| Fiscal Injections | 12,301.9 | 14,002.6 | 14,938.2 | 10,364.6 | 8,815.1 | 9,292.7 |
| | **Liquidity Absorption Measures** | | | | | |
| Open Market Operations (OMOs) | 156.9 | -656.8 | 260.1 | -260.1 | -260.1 | -2,300.0 |
| CBTT Sale of Foreign Exchange | 9,767.5 | 9,353.1 | 11,366.4 | 8,367.0 | 7,096.4 | 9,104.4 |
| Central Gov't Treasury Bond Issues | 0.0 | 0.0 | 0.0 | 1,559.3 | 1,559.3 | 1,000.0 |
| Commercial Banks' Fixed Deposits | 1,000.0 | 0.0 | 1,500.0 | 0.0 | 0.0 | 0.0 |

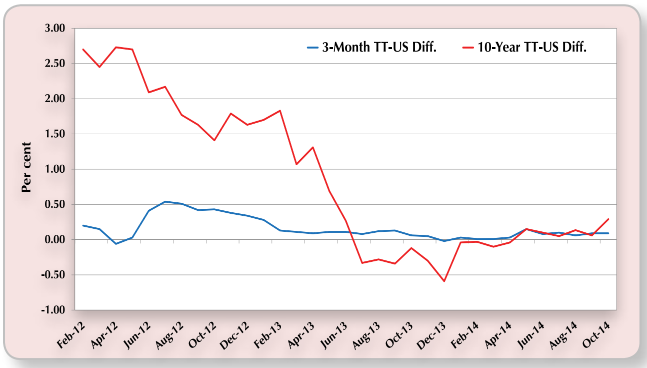
Source: Central Bank of Trinidad and Tobago.

A negative sign means that there was a net issue of OMOs resulting in a withdrawal of liquidity and a positive sign means a net redemption of OMOs that injects liquidity.

In order to effectively manage liquidity levels, the Bank utilized several tools at its disposal. Given the increased limits under the Treasury Bills and Notes Acts, over the period January to October 2014 the Central Bank withdrew $2.3 billion via net open market operations. In addition, the Central Bank rolled over three commercial banks' fixed deposits totalling $4.5 billion and facilitated the issue of a $1 billion, 2.20 per cent coupon, seven-year, liquidity sterilization Treasury bond in June 2014. Additionally, on October 9th 2014, the Bank conducted open market operations amounting to approximately $7.5 billion in order to sterilize the liquidity-creating impact of a one-off purchase of foreign exchange from a private institution. Further, Central Bank sales of foreign exchange to authorized dealers indirectly removed $9.1 billion from the system over the review period – roughly 28 per cent higher than in the same period one year ago.

The discount rate on the TT three-month Treasury bill stood at 0.12 per cent in October 2014, slightly lower than the 0.14 per cent in May. With the rate on the corresponding US security also inching down, the

### Chart IVb
### 3-Month and 10-Year TT-US Differentials

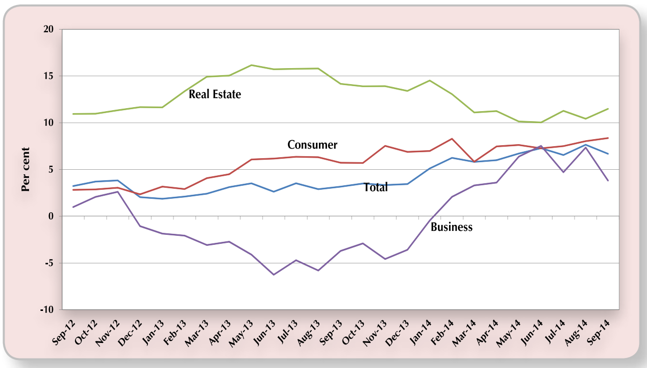



Source: Central Bank of Trinidad and Tobago.

differential between TT and US three-month Treasuries measured 10 basis points in October, compared with 11 basis points in May 2014. However, while short-term US rates have been relatively steady, longer term rates were somewhat volatile as international investors made spasmodic reactions to new information. The yield on the benchmark 10-year US Treasury bond began the year at around 3.0 per cent, but fell to 2.35 per cent by the end of October 2014 as weak economic data from Europe threatened the global recovery. With TT yields relatively stable **(Box 1)**, the decline in the US yields helped the differential on 10-year Treasuries rebound into positive territory by October from depressed levels at the end of December 2013 **(Chart IVb)**.

Commercial banks continued to lower lending rates in a bid to maintain loan demand. Banks' weighted average lending rate declined steadily from 8.51 per cent in December 2013 to 8.03 per cent by September 2014. With deposits rates steady at 0.55 per cent over the first nine months of 2014, the spread between the weighted average lending and deposit rates narrowed by 48 basis points from December 2013 to 7.48 per cent in September 2014.

### Chart IVc
### Consolidated Financial System: Private Sector Credit
**(Year-on-Year Per Cent Change)**




Source: Central Bank of Trinidad and Tobago.

Low interest rates, high liquidity and the cautiously optimistic sentiment of the business community have supported the expansion in private sector lending **(Chart IVc)**. For the first nine months of 2014, the year-on-year growth of credit to the private sector averaged 6.5 per cent monthly, up from 2.8 per cent in the corresponding period in 2013. Commercial banks drove the increase in overall lending, with bank credit averaging 7.0 per cent over the period, compared with 4.6 per cent over the comparable period in 2013. In addition, on a year-on-year basis credit extended by non-bank financial institutions expanded in seven of the nine months of 2014.

The recovery in business lending which emerged in the first quarter of 2014 strengthened as the year progressed. Over the nine months leading up September 2014, the year-on-year increase in business lending averaged 4.3 per cent (on a monthly basis) compared to an average decline of 3.8 per cent over the same period in 2013.

For the quarter ended September 2014, the sectoral decomposition of commercial banks' loans to businesses indicated that the recovery in business lending was strengthened by an expansion in lending to the distribution sector (21.5 per cent). Further, loans to the finance, insurance and real estate sector also accelerated (4.4 per cent) during the period. On the other hand, there were declines to the construction (10.3 per cent), manufacturing (9.1 per cent) and other services (1.6 per cent) sectors.

Consumer loans continued to accelerate into the third quarter of 2014. The expansion in consumer loans averaged 7.5 per cent over the period January to September 2014, up from an average of 5.0 per cent over the equivalent period in 2013. A disaggregation of consumer credit for the third quarter of 2014 showed strong growth of loans for the purchase of motor vehicles (20.6 per cent) and credit card purchases (9.0 per cent). Housing-related loans maintained their upward trend with expansions in loans for bridging finance (14.6 per cent) and home improvement/ renovation (11.3 per cent).

While there has been some slowdown in the expansion of real estate mortgage loans, growth in the nine-month period to September 2014 remained in double digit territory. Consistent with the upward trend in house prices over the past five years, the size of mortgage loans has also increased to match the rise in house prices.

## Financial Sector Developments

### *Foreign Exchange Market*

Over the first 10 months of 2014, intermittent periods of tightness in the foreign exchange market were met by Central Bank interventions **(Table IVb)**. Sales of foreign currency by authorized dealers (to the public) during the first 10 months of 2014 amounted to US$5,863.2 million, 3.8 per cent higher relative to the amount sold over the same period in 2013. However, as a result of lower conversions from the energy sector, purchases of foreign currency from the public (except from the Central Bank) totaled US$4,571.8 million. This was 2.6 per cent lower than purchases over the first 10 months of 2013.

The system's net sale position of US$1,291.4 million in the first 10 months of 2014 was approximately 35.0 per cent higher than the net sales gap of US$956.7 million in the corresponding period of 2013. In order to fill this gap and support the market, the Central Bank sold US$1,440 million to authorized dealers. As a result, the weighted average selling rate appreciated to TT$6.3620 to US$ 1.00 dollar at the end of October, declining from the rate (TT$6.4593 = US$1.00) recorded at the end of December 2013.

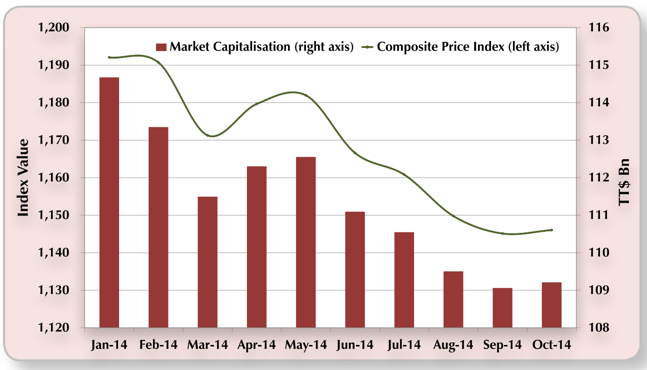
**Table IVb**
**Authorized Dealers: Foreign Exchange Market Activity**
**(US$ Million)**

| Date | Purchases from Public | Sales to Public | Net Sales | Purchases from CBTT |
|---|---|---|---|---|
| 2009 | 3,808.2 | 5,637.2 | 1,828.9 | 1,899.1 |
| 2010 | 4,043.3 | 5,536.0 | 1,492.7 | 1,550.0 |
| 2011 | 4,755.5 | 6,186.8 | 1,431.4 | 1,475.0 |
| 2012 | 4,859.1 | 6,713.7 | 1,854.6 | 1,785.0 |
| 2013 | 5,802.2 | 7,076.4 | 1,274.2 | 1,315.0 |
| | | | | |
| Jan-Oct 2013 | 4,694.3 | 5,651.1 | 956.7 | 1,115.0 |
| Jan-Oct 2014 | 4,571.8 | 5,863.2 | 1,291.4 | 1,440.0 |
| **Y-o-Y Per Cent Change** | **-2.6** | **3.8** | **35.0** | **29.1** |

Source: Central Bank of Trinidad and Tobago.

## *Capital Markets*

**Chart IVd**
**Trinidad and Tobago Composite Price Index**
**(10 months ending October 2014)**




Source: Trinidad and Tobago Stock Exchange.

Over the period January to October 2014, the local stock market posted its first 10-month decline since 2009 (Chart IVd). On a year-to-date basis, the Composite Price Index (CPI) and the All Trinidad and Tobago Index (ATI) were down 3.3 per cent and 1.6 per cent, respectively. The cross-listed stocks continued to underperform due to the sluggish performance of the regional economies. The Cross Listed Index fell by 12.6 per cent in the first 10 months of 2014. However, the Manufacturing II sub-index was the worst performing sub-sector, due to a 9.4 per cent price decline in Trinidad Cement Limited's share price. Market capitalization stood at $109.1 billion as at the end of October 2014.

Over the period January to September 2014, activity on the domestic primary bond market was generally on par with the corresponding period a year earlier. During the first nine months of 2014, four bond issues were raised totaling approximately $4.2 billion. This is in contrast with six primary issues which raised just under $4.0 billion in the corresponding period in 2013. The Central Government and state enterprises were the main borrowers on the market **(Table IVc)**. In addition to the liquidity sterilization Treasury bond in June 2014, the Central Government also issued a $1.5 billion, 12-year, 2.8 per cent coupon bond for budgetary support in September 2014. The only private sector issue was for strategic business acquisitions and developments.

**Table IVc**
**Primary Bond Market**
**January – September 2014[p]**

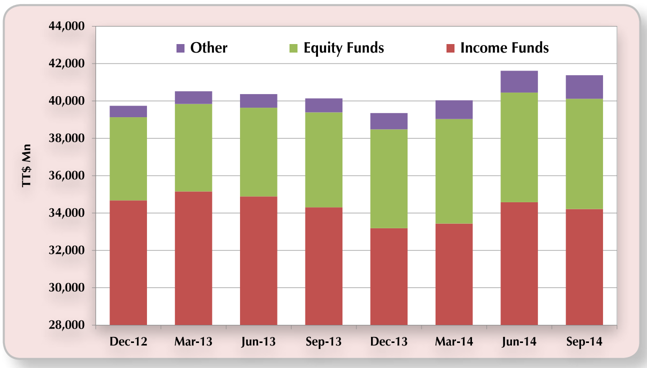
| | Borrower | Face Value ($Mn) | Period To Maturity | Coupon Rate Per Annum | Placement Type |
|---|---|---|---|---|---|
| June | Central Government of Trinidad and Tobago | 1,000.00 | 7 years | Fixed Rate 2.2% | Public |
| July | Massy Holdings Limited | 600 | 15 years | Fixed Rate 4.0% | Public |
| | | 600 | 10 years | Fixed Rate 5.25% | Public |
| August | First Citizens Bank | 400 | 7 years | Fixed Rate 3.1% | Private |
| | | 100 | 10 years | Fixed Rate 3.25% | Private |
| September[p] | Central Government of Trinidad and Tobago | 1,451.84 | 12 years | Fixed Rate 2.8% | Auction |

Source: Central Bank of Trinidad and Tobago.

p Provisional.

When compared to the previous year, trading activity on the Trinidad and Tobago Stock Exchange's (TTSE) secondary Central Government bond market was significantly lower over the period January to September 2014. In the first nine months of 2014, bonds with a total value of $455 million were traded. This was much lower than the value ($1.4 billion) traded over the corresponding period last year. With the exception of a few short to medium-term tenors, yields on Treasury securities generally trended upwards in the nine months of 2014. The benchmark 10-year TT Treasury bond yield rose to 2.71 per cent in September, up from approximately 2.50 per cent at the end of 2013.

## Chart IVe
## Mutual Funds Under Management by Type




Source: Central Bank of Trinidad and Tobago.

Following a weak performance in 2013, the mutual fund industry expanded modestly over the first nine months of 2014. Aggregate mutual funds under management stood at $41.4 billion in September 2014 (Chart IVe), representing an increase of 5.1 per cent from year end 2013. This was higher than the 1.0 per cent growth in the corresponding period last year. Over the period January to September 2014, the industry attracted net sales of roughly $1.3 billion compared with $306 million in the same period one year ago. Contributing to the stronger growth of the mutual fund industry was the increase in equity funds under management which rose by 11.5 per cent in the first nine months of 2014 (compared with growth of 14.0 per cent in the same period of 2013). Income funds recovered by 3.0 per cent after a contraction of about 1.0 per cent one year ago. In terms of currency profile, both foreign currency and TT dollar-denominated funds improved in the first nine months of 2014. On a year-to-date basis, foreign currency-denominated funds expanded by 4.8 per cent in September 2014 compared with a fall of 4.9 per cent in the same period in 2013. The TT dollar-denominated funds grew by 5.1 per cent over the nine-month period, compared with a smaller increase of 2.6 per cent in the comparable period of 2013.

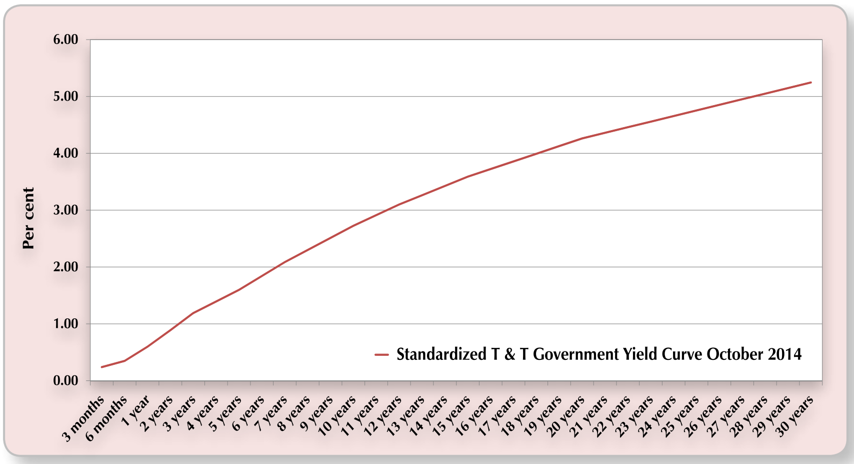
## BOX 1

### The Development of the Standardized TT Treasury Yield Curve

A Treasury yield curve displays the relationship between yields on Government debt and their maturities. It is an important metric in any bond market since government debt is often regarded as default free. As a result, the Treasury yield curve can serve as a benchmark for pricing of all other debt instruments. The local Government bond market in Trinidad and Tobago has been deficient of a standardized Treasury Yield curve since the development of the market. On recognizing the importance of the development of this standardized benchmark, the Central Bank of Trinidad and Tobago, in collaboration with various stakeholders in the financial sector embarked on the task of creating this important standardized metric.

The partnership between the CBTT and other market players resulted in the creation of the Standardized TT Treasury Yield Curve. The new curve is expected to be a benchmark for more uniform and efficient pricing of Central Government bonds issued on the primary bond market and traded on the TTSE Secondary Government bond market. Further, the curve will provide users with the ability to determine other State Enterprise and Private bond market prices and yields. The TT Treasury Yield Curve is expected to become the standardized metric by which stakeholders in the financial sector will use for a variety of capital market functions. The Central Bank will transition towards the Standardized TT Treasury Yield Curve for reporting and publication purposes by the first quarter of 2015.

Chart 1: Standardized Trinidad and Tobago Central Government Yield Curve




Source: Central Bank of Trinidad and Tobago.

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