CENTRAL BANK OF
TRINIDAD & TOBAGO

Monetary Policy Report

April 2006

Volume VI Number 1

MONETARY POLICY REPORT

APRIL 2006

VOLUME VI NUMBER 1

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

MONETARY POLICY REPORT

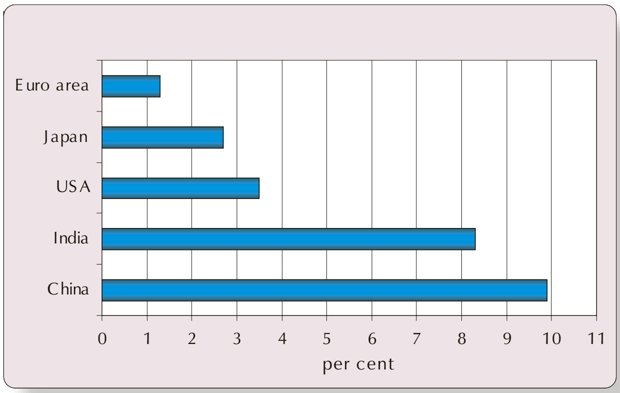
APRIL 2006

1. Overview

The International Setting

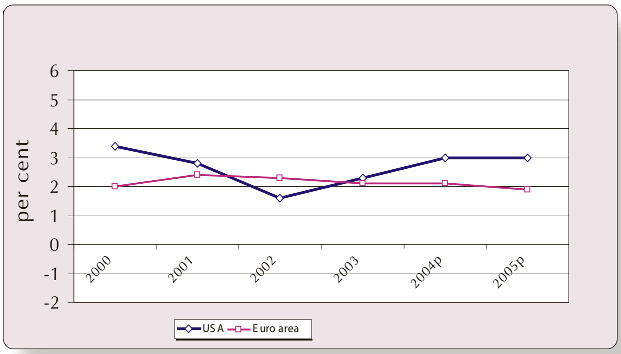
Despite soaring energy prices, **the global economy** achieved a real growth rate of 4.8 percent in 2005 compared with 5.3 percent the previous year. Among industrial countries, while the US remained the main engine of growth, economic expansion in Japan strengthened and there were signs of a recovery in the Euro area. Among emerging markets and developing countries, economic growth was particularly buoyant in China and India (Chart 1). Latin America and the Caribbean continued to record strong economic growth (4.3 per cent) compared with 5.6 per cent in 2004. This performance was boosted by strong global demand for commodities, in partcular, fuels, metals and agricultural products.

Chart 1
Selected Global Growth Rates, 2005



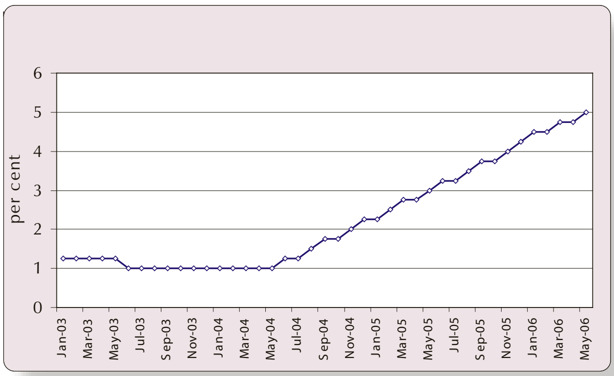
In several industrialized countries, **headline inflation** was boosted somewhat by soaring energy prices. In general, core inflation remained subdued in 2005 as the pass-through of the higher energy prices to the rest of the economy remained contained. In the US, headline inflation ticked up to 3.4 per cent (compared with 2.7 per cent in 2004) and core inflation remained under 2 per cent (Chart 2).

Chart 2
Selected Inflation Rates



The global economic growth momentum has remained strong in 2006, with core inflation rates still well under control. Headline inflation in the US stood at 3.5 per cent (year on year) in April 2006 with core inflation at 2.3 per cent. In the Euro area, headline inflation at 2.4 per cent is a bit outside the target zone (below 2 percent) but core inflation at 1.6 per cent in April 2006 was well in check.

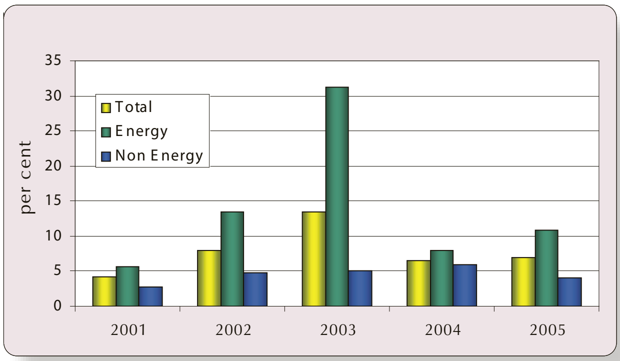
Chart 3
Federal Funds Rate



The gradual withdrawal of monetary accommodation that began in mid-2004 in the US continued in the first five months of 2006. Through monthly increases of twenty-five basis points, **the Federal funds rate has**

been raised from 1.00 per cent to 5.00 per cent as at May 2006 (Chart 3). Other short-term interest rates in the US have responded correspondingly but long-term rates have lagged causing the yield curve to flatten.

Chart 4
Growth in Real GDP



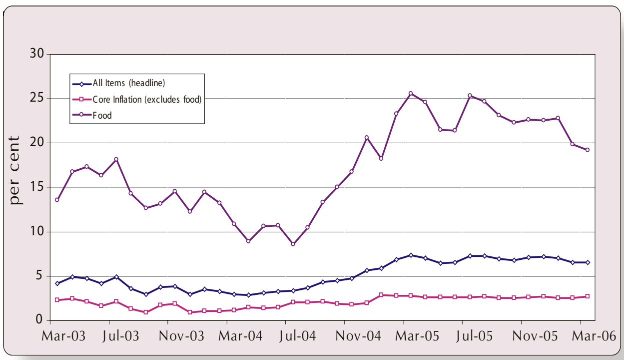
Review of the Domestic Economy

The Domestic Economy

In 2005, **the Trinidad and Tobago economy continued to register strong economic growth**, led by rapid expansion in the energy sector (10.9 percent) (Chart 4). Non-energy sector growth was estimated at 4 percent with construction and manufacturing making the main sector contributions . Growth in the non-energy sector was stimulated by a strong increase in government expenditure and by buoyant consumption spending. During the year, there were clear signs that burgeoning domestic demand was leading to capacity constraints in some sectors and contributing to inflationary pressures. Rising consumer prices are being accompanied by a rapid increase in real estate values.

In 2006, partial indicators point to even faster economic growth, reflecting, in part, the full-year impact of large energy sector investments. With energy sector prices showing remarkable buoyancy, the outlook is for higher government expenditure adding to the growth momentum in the non-energy sector. In these circumstances, containing inflationary pressures remains a major challenge.

Chart 5
Retail Prices Index
(year-on-year changes)



Inflation

After three years of increases averaging about 3.5 per cent, **headline inflation rose to 5.6 per cent in 2004 and to 7.2 per cent in 2005.** The main driver of inflation was the movement in food prices which rose from an average of 10.3 per cent in 2001-2003, to 20.6 per cent in 2004 and 22.6 per cent in 2005. **Core inflation**, which excludes the impact of food prices, went from 2 per cent in 2004 to 2.7 per cent in 2005 (Chart 5).

Chart 6
Non-Energy Fiscal Deficit

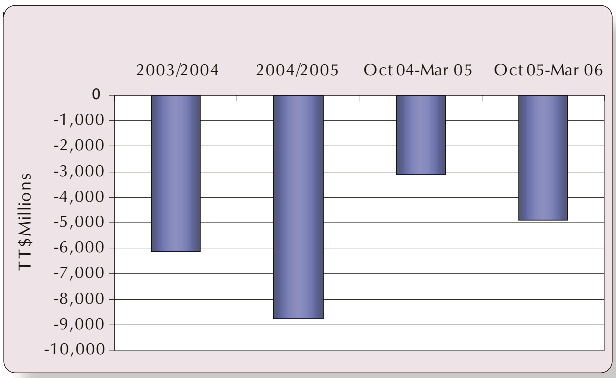
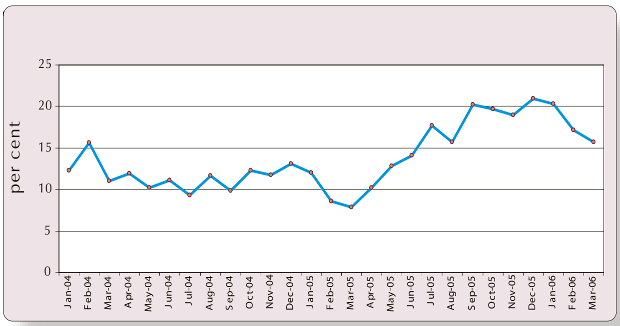


Chart 7
Private Sector Credit by the Consolidated Financial System
(year-on-year changes)



Over the last several years, the increase in **food prices** in Trinidad and Tobago has been much higher than in the rest of the Caribbean and may have to do with declining food production in the agricultural sector and the presence of an oligopolistic distribution regime. The sharp rise in food prices in 2005 was clearly influenced by floods in the last quarter of 2004, which severely impacted domestic food production at a time when buoyant economic conditions and excess liquidity were boosting domestic demand.

Increasing demand in the context of declining excess capacity also contributed to the rise in core inflation. In the non-food basket, the largest price increases were for **pharmaceuticals, recreation** and **leisure** and **rents**.

As noted above, along with the rise in consumer prices, the economy has seen a sharp rise in **construction costs** and in **real estate prices** over the past few years. While a reliable series is not yet available, studies suggest that construction costs could have increased by as much as 40 percent, between 2003 and 2005.

A major factor underpinning the rising inflationary pressures has been the increase in **government spending** and its impact on the **non-energy fiscal deficit** (Chart 6). With government spending increasing from the equivalent of 24.9 percent of GDP in 2003/2004 to 27 per cent of GDP in 2004/2005, the non-energy fiscal deficit rose from 7.7 per cent to 9.7 per cent of GDP over the period. The evolution of the central government finances in the first six months of fiscal year 2005/2006 suggests that the non-energy fiscal deficit has continued to increase sharply. The monetization of energy receipts to finance this growing deficit is a major source of liquidity injection and of inflationary pressures.

To compound the impact of government expenditure, bank credit to the private sector has also been increasing rapidly. Thus, the 12-month rate of expansion in private sector credit from the consolidated financial system accelerated from 13.1 per cent in December 2004 to 21 per cent in December 2005. Reflecting the impact

Chart 8
Monetary Policy Response

Monetary Policy Actions

March 2005:	'Repo' rate increased to 5.25 per cent.
June 2005:	'Repo' rate increased to 5.50 per cent.
Sept. 2005:	'Repo' rate increased to 5.75 per cent. Special Deposit rate de-linked from 'Repo' rate. Special Deposit rate reduced to 2.50 per cent.
Nov. 2005:	'Repo' rate increased to 6.0 per cent.
Dec. 2005:	Commercial banks deposited TT$1 billion in interest bearing account at the Central Bank for a minimum of one year. Special Deposit rate reduced to zero.
Jan. 2006:	'Repo' rate increased to 6.25 per cent.
Feb. 2006:	'Repo' rate increased to 6.50 per cent.
Mar. 2006:	'Repo' rate increased to 6.75 per cent.

of the recent interest rate hikes, the rate of private sector credit expansion slowed to 15.7 per cent by March 2006 (Chart 7).

The Monetary Policy Response

Against the background of rising inflationary pressures and an upward climb in US interest rates, the Central Bank began to raise its policy interest rate (the Repo rate) and tighten liquidity in early 2005 (Chart 8). The Repo rate was raised on four occasions in 2005 and three times in the first quarter of 2006, each time by twenty-five (25) basis points. These adjustments brought the Repo rate from 5.00 per cent as at February 2005 to 6.75 per cent as at March 2006. In response to the rise in the Repo rate, the prime lending rates of the commercial banks were adjusted from 8.75 per cent to 10.50 per cent. However, in the presence of excess liquidity, this rise in the quoted prime lending rates (which serves as a base rate) has not been fully transmitted throughout the structure of interest rates in the financial sector. In many cases, banks with ample loanable funds have priced consumer loans below the prime lending rate.

Chronic excess liquidity posed a major challenge for monetary policy particularly during the second half of 2005. With the acceleration of government expenditure in the fourth quarter of fiscal year 2004/2005, there began a substantial rise in excess liquidity in the financial system. **Commercial banks' holdings of special deposits** at the Central Bank – one measure of excess liquidity – which averaged $300 million in January 2005, almost doubled by October 2005 and reached $2 billion by mid-December (Chart 9).

With the build-up in liquidity limiting the pass-through of increases in the Repo rate to short-term interest rates, and as regular open market operations were not sufficient to deal with this huge liquidity overhang, the Bank employed a number of liquidity reducing measures to improve the effectiveness of monetary policy. **On December 28, 2005, the Central Bank requested commercial banks to deposit TT$1 billion in an interest-bearing account for a minimum period of one**

Chart 9
Excess Liquidity: Special Deposits and Excess Reserves

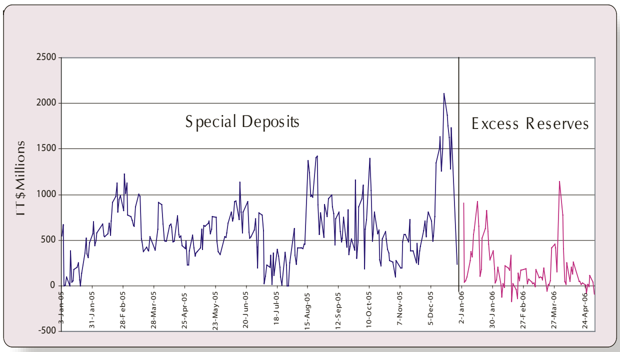


Chart 10
Yield Curve on Government Securities

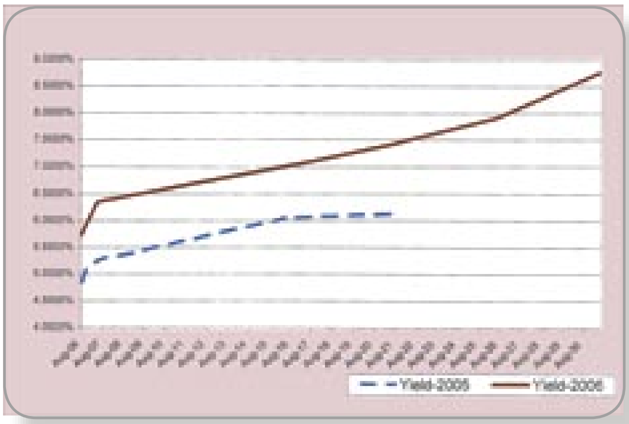
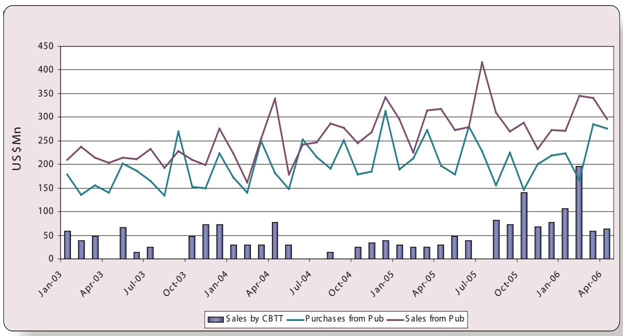


Chart 11
Commercial Banks' Sales and Purchases of Foreign Currency



year. In addition, the rate paid on special deposits held by commercial banks at the Central Bank was reduced from 3.50 per cent to 2.50 per cent in September and then to zero with effect from December 28, 2005. This latter measure was aimed at discouraging the use of the special account and stimulating activity in the inter-bank market.

The Central Bank has continued to absorb liquidity through open market operations. Since late 2005, with a view to providing more options for liquidity management, the Bank has increased its sales of 6-month and 12-month securities (and some two-year securities as well) as distinct from the more customary 3-month bills. It should also be noted that since the second half of 2005, substantial liquidity absorption has occurred through Central Bank sales of foreign exchange to commercial banks.

Inter-bank rates hovered in a range of 4 - 5 per cent for most of 2005. Following the special measures to absorb liquidity towards the end of the year, inter-bank rates rose to almost 6 per cent at the end of April 2006. Government treasury bill rates followed a similar path rising from 4.81 per cent in 2005 to 5.68 per cent by the end of April 2006.

Increases in long-term interest rates exceeded those at the shorter end of the spectrum resulting in a steeper yield curve (Chart 10). This may be due to investors' views as to long-term inflation prospects as well as the sizeable financing requirements of the quasi-government sector. The yield on a 25-year government guaranteed bond was 8.75 per cent in March 2006. By comparison, a bond of a similar tenor yielded 8.00 percent when it was issued in December 2005. Similarly, a 15-year bond was issued at a yield of 7.20 per cent in October 2005 compared with 6.40 per cent for the same maturity in June 2005.

Rising interest rates have also contributed to the sluggish performance of the local stock market. After an average increase of 26.5 per cent over the period 2002 and 2003 and a jump of 54.8 per cent in 2004 the composite stock market index has fallen by 10.8 per cent since December 2004. The slowdown appeared

Chart 12
Comparative 90-Day Treasury Bill Rates: Trinidad and Tobago and United States

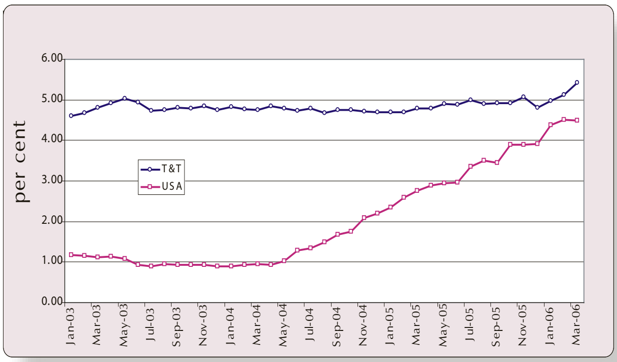
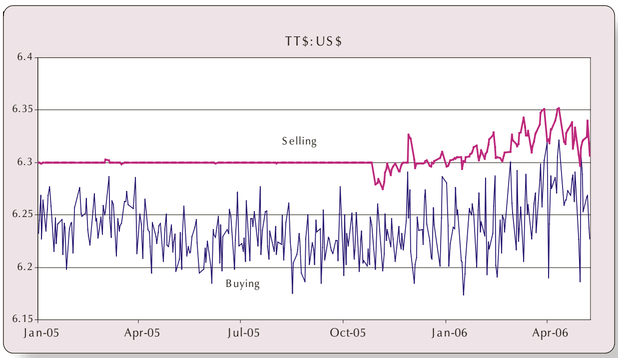


Chart 13
Weighted Average Exchange Rate



to be linked to a widely expected market correction as well as the rebalancing of portfolios to meet prudential requirements.

In 2006, the stock market continued to decline with the composite index falling by 10.2 per cent during the first quarter.

The Foreign Exchange Market

With the rapid increase in economic growth, the narrowing of the differential between short-term TT and US dollar interest rates and the accompanying boom in consumption and construction activity, foreign exchange demand increased significantly in 2005 (Chart 12). In addition to the sharp increase in import payments, there has been a sustained rise in capital outflows attributable to:

(i) portfolio diversification, encouraged by the reduction in the spread between local and foreign interest rates and the continued downturn in the stock market;

(ii) the high level of foreign acquisitions and foreign currency bond placements by external borrowers;

(iii) capital flight related to socio-political uncertainties; and

(iv) high foreign exchange requirements for public sector infrastructural projects.

To help meet the rising foreign exchange demand, the Central Bank increased sales to the market by 73.8 per cent to US$695 million while enhancing exchange rate flexibility (Chart 11).

During the year, in order to improve market conditions, the Central Bank agreed on a schedule for bi-weekly foreign exchange sales to the market. Additional sales were also committed as demand conditions warranted. While this arrangement generally improved the functioning of the market, there were still occasional periods of tightness in the system, mainly as a result of fluctuations in the banks' short positions.

Pressures in the foreign exchange market continued in 2006. In the period January – April, Central Bank foreign exchange sales amounted to US$438 million, compared with US$110 million in the corresponding period of 2005. The weighted average selling rate for the US dollar fluctuated between 6.2999 and 6.3404 between October 2005 and April 2006 (Chart 13).

Short-Term Prospects

After a particularly strong first three months of 2006, there were signs of some slowdown in economic activity in the US in the second quarter. This, combined with continued evidence that core inflation remains contained, is being cited as possible justification for the Federal Reserve to bring the current phase of monetary tightening to an end. In the Eurozone, even as the economy is gaining strength, discussions focus on tightening monetary policy before inflation becomes a more serious threat.

In Trinidad and Tobago, economic growth is projected to remain robust with real GDP growth currently projected to reach 10 per cent in 2006. Against this background, the Central Bank will continue to face two main challenges in the short term: containing inflation and efficiently managing the foreign exchange market.

Fiscal policy constitutes a key ingredient to meeting the inflation challenge. Notwithstanding the shortfall in actual relative to budgeted expenditure, the increase in the net fiscal injection has been a main factor in the build-up of inflationary pressures. Buoyant private consumption spending, financed by bank borrowing, has also contributed to rising inflation.

In the second half of 2006, there is likely to be upward pressure on the price level from continued increases in the prices of a range of construction materials.

Chart 14

Short-term Outlook

- **Prospects for 2006**
  - Expanding energy sector output
  - Increased construction activity
  - Robust energy prices
  - Low unemployment levels
- **Challenges**
  - Containing inflation
  - Dampening consumer credit
- **Required Policy Responses**
  - Fiscal Restraint
  - Tightening Monetary Policy
  - Wage Containment

Some increase in import prices is also likely as the energy price shock works its way through prices in Trinidad and Tobago's major import markets.

Given these influences, a moderation in government spending is a pre-requisite for effective inflation control. At the same time, the Central Bank will need to intensify efforts to reduce excess liquidity and contain bank credit expansion. Accordingly, tight monetary conditions and continued increases in interest rates could be expected for the next several months.

So far, interest rates on consumer lending have lagged behind adjustments in the prime lending rate. The Central Bank will discuss with the commercial banks measures to dampen consumer credit expansion while giving priority to credit for productive purposes.

The containment of wage increases in line with productivity gains would also facilitate inflation control. In this context, the level of the upcoming public sector wage settlement could well set the standard for private sector settlements over the next year or so.

Given the evolution of inflation so far and assuming that the non-energy fiscal deficit could be contained to between 14 - 15 per cent of GDP (compared with 17.5 per cent in the budget), the Central Bank projects inflation for the year as a whole at between 6.0 - 6.5 per cent, down from last year's figure of 7.2 per cent. Even this outcome would be outside of the Bank's target range of 4 - 5 per cent.

Fiscal containment along with tight monetary policies could also facilitate the orderly management of the foreign exchange market. In this context, while there is some likelihood that the step increases in the US policy interest rate could end soon, interest rate policy in Trinidad and Tobago will need to take into account the objective of inflation control as well as the need to re-establish an appropriate spread between TT and US interest rates in order to discourage capital outflows. The Bank will continue to provide support to the foreign exchange market as required to maintain orderly conditions.

Chart 15
Growth in Real GDP by Selected Sub-Sectors

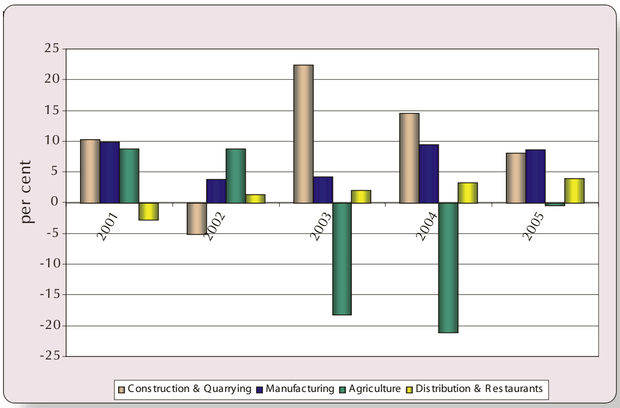


Table 1
Unemployment Rates – 1988-2005
/Per Cent/

	March	June	September	December
1988	22.7	21.4	21.6	22.4
1989	22.5	22.3	22.4	20.8
1990	20.1	20.3	20.6	19.2
1991	20.4	17.6	18.5	17.4
1992	19.8	20.6	18.7	19.2
1993	21.1	19.5	19.0	19.4
1994	19.7	18.1	17.9	17.9
1995	18.1	16.5	17.8	16.3
1996	17.1	15.1	16.9	15.9
1997	17.2	14.5	14.9	13.5
1998	14.6	13.4	13.8	15.1
1999	14.1	11.7	13.6	13.2
2000	12.5	..	12.1	11.9
2001	10.7	10.8	10.1	11.7
2002	10.3	10.1	10.6	10.6
2003	11.0	10.2	10.5	10.2
2004	10.2	7.8	7.7	7.8
2005	9.0	8.0	8.2	6.7

Source: Central Statistical Office.

2. Recent Economic Developments

Real GDP

According to the Central Statistical Office, the economy expanded by 7 per cent in 2005, driven by the heightened activity in the energy sector (10.9 per cent) and moderate expansion of the non-energy sector (4 per cent). The strong performance of the energy sector reflected not only soaring energy prices but also increased production capacity as two petrochemical plants (liquefied natural gas and methanol) came on stream in the last quarter of the year. In addition, oil production received a large boost from a recently discovered oil field, reversing a decade-old downward trend.

The strong growth in construction (8.1 per cent) and manufacturing (8.6 per cent) were the main contributors to growth in the non-energy sector. Construction activity benefited largely from government spending on infrastructural development and the erection of office and residential buildings. Other sectors that recorded growth were electricity and water (5.3 per cent), transport, storage and communication (6.4 per cent) and distribution (3.9 per cent). However, output in the agriculture sector declined by 0.5 per cent, although this was substantially lower than the previous year's contraction of 21.1 per cent (Chart 15).

Chart 16
Trends in Labour Force and Unemployment

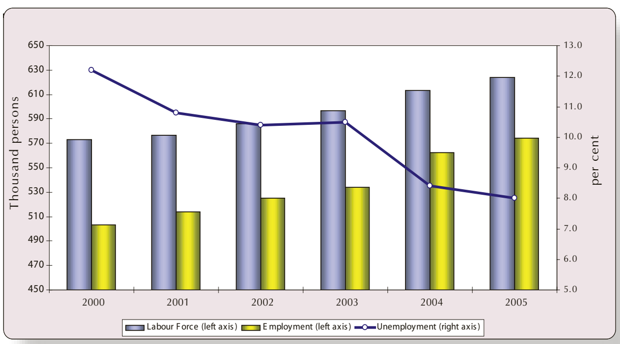


Chart 17
Changes in Employment: Selected Sectors

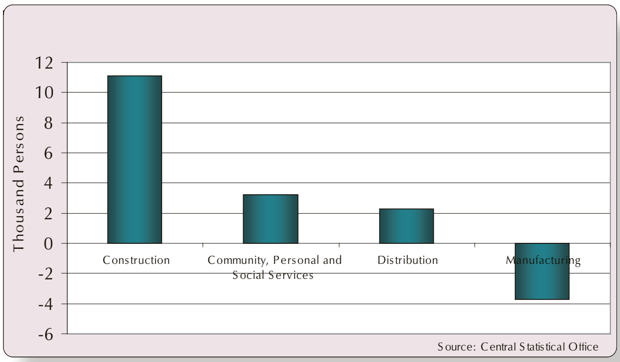
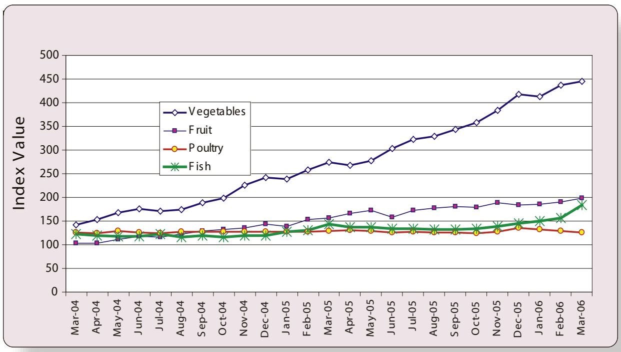


Chart 18
Prices Movements in Selected Food Categories



Employment

Robust economic activity in 2005 led to further employment gains and in some sectors, particularly construction and distribution, shortages of both skilled and unskilled labour were reported. Although 10,200 persons joined the labour force in 2005, 11,600 jobs were created, which brought the unemployment rate down to an average of 8 per cent from 8.4 per cent in the previous year. The participation rate rose to 63.7 per cent, from 60.9 per cent in 2002 as more persons sought employment given more buoyant economic conditions (Chart 16).

The construction sector generated the largest number of jobs (11,100), as a result of government spending on housing and infrastructural works and private sector investment in real estate (Chart 17). Other sectors that registered employment gains were community, social and personal services (3,200 jobs) and distribution (2,300 jobs). However, the manufacturing sector lost 3,200 jobs as a result of technological improvements. Employment in the agriculture sector also fell as 1,000 workers lost jobs.

Prices

Index of Retail Prices

Among the challenges facing the Monetary Authority in 2005 and into 2006, was a steady build-up in inflationary pressures. Headline inflation averaged 6.9 per cent in 2005, significantly higher than in 2004 (3.7 per cent). The food price component exerted the greatest influence on the Index rising by 22.9 per cent (Chart 18). This reflected structural rigidities in the agriculture sector with respect to the production of fruits and vegetables. A severe rainy season also curtailed the supply of agricultural produce. Core inflation, which excludes the volatile food component, measured 2.7 per cent higher than the 1.6 per cent increase recorded in 2004. Increases in the cost of educational (5.8 per cent) and health (4.1 per cent) services contributed to the rise in core inflation. The hotels, cafes and restaurant component of the index also increased parallel with rising food prices. Other notable

Table 2
Index of Retail Prices (January 2003=100)

	ALL ITEMS			CORE		FOOD		
Date	Index	Mthly %	Y-o-Y %	Index	Y-o-Y %	Index	Mthly %	Y-o-Y %
Jan-05	109.40	0.46	5.91	103.69	2.83	135.40	-0.44	18.25
Feb-05	110.50	1.01	6.87	103.70	2.77	141.50	4.51	23.26
Mar-05	111.20	0.63	7.34	103.80	2.76	144.90	2.40	25.56
Apr-05	111.60	0.36	7.00	104.27	2.58	145.00	0.07	24.57
May-05	111.70	0.09	6.48	104.19	2.59	145.90	0.62	21.48
Jun-05	112.10	0.36	6.56	104.26	2.64	147.80	1.30	21.45
Jul-05	113.50	1.25	7.28	105.09	2.59	151.80	2.71	25.35
Aug-05	113.80	0.26	7.26	105.20	2.67	153.00	0.79	24.69
Sep-05	114.10	0.26	6.94	105.14	2.57	154.90	1.24	23.13
Oct-05	114.80	0.61	6.79	105.67	2.57	156.40	0.97	22.28
Nov-05	115.70	0.78	7.03	105.62	2.65	161.60	3.32	22.61
Dec-05	116.70	0.86	7.16	105.72	2.69	166.70	3.16	22.57
Jan-06	117.10	0.34	7.04	106.30	2.52	166.3	-0.24	22.82
Feb-06	117.70	0.51	6.52	106.31	2.52	169.6	1.98	19.86
Mar-06	118.50	0.68	6.56	106.58	2.68	172.8	1.89	19.25
Apr-06	119.30	0.68	6.90	107.49	3.09	173.10	0.17	19.38

Chart 19
Index of Retail Prices of Building Materials

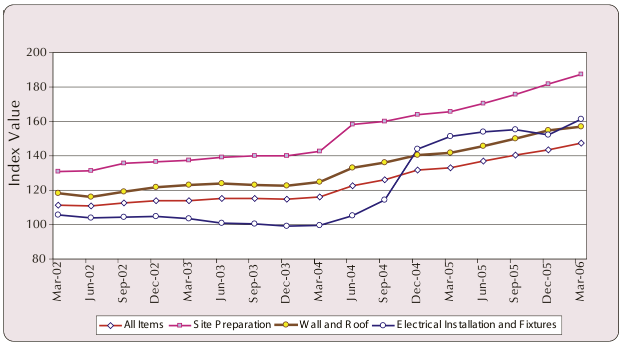
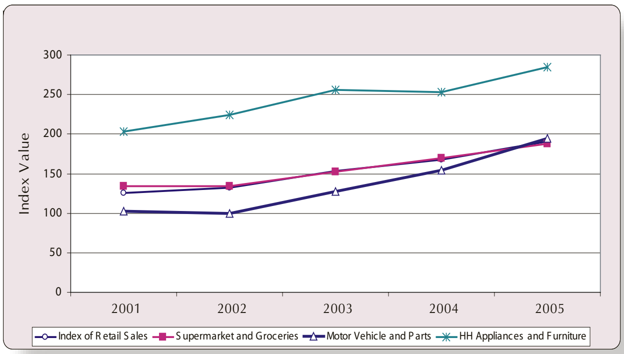


Chart 20
Index of Retail Sales



increases were in recreation and culture (7.7 per cent) and rent (5.7 per cent) components of the Index.

In the twelve months to April 2006, headline inflation measured 6.90 per cent, roughly the same increase as a year earlier. While there was a modest slowdown in food prices, core inflation rose to 3.09 per cent from 2.58 per cent a year earlier, on account of increases in the cost of home ownership, rent as well as health services.

Index of Retail Prices of Building Materials

In the absence of official statistics on real estate prices, the Index of Retail Prices of Building Materials, which covers the prices of building materials and building services, provides a useful indicator for monitoring movements in house prices. This Index increased sharply by an average of 11.57 per cent in 2005 compared with increases of 8.14 per cent and 2.31 per cent in 2004 and 2003, respectively (Chart 19). The main components of the Index, the cost of building materials for site preparation, walls and roof and electrical installation and fixtures rose by 11 per cent, 10.9 per cent and 32.4 per cent, respectively. The rapid increase in construction activity led to shortages of these items during the year. These shortages have been partly met by increased imports.

Chart 21
Credit Card Loans Outstanding
(year on year changes)

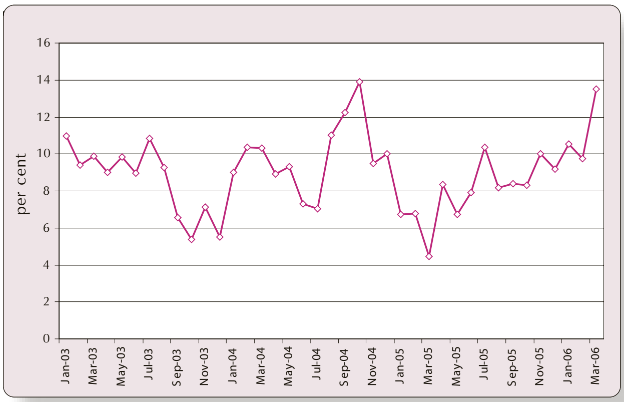


Chart 22
Crude Oil Prices (WTI)

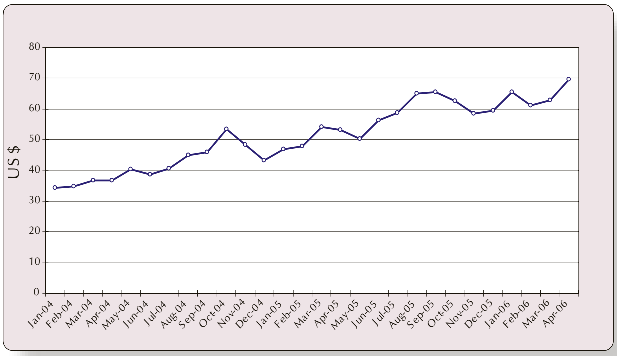
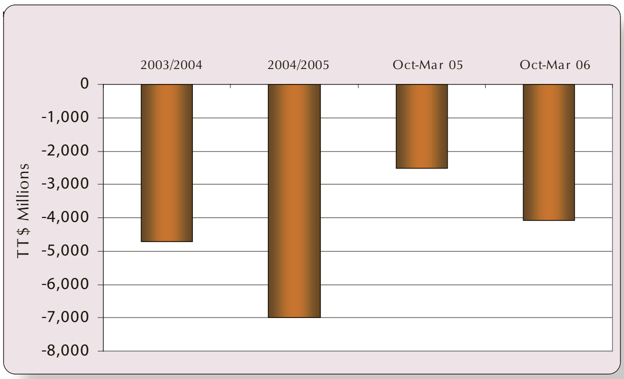


Chart 23
Net Domestic Budget Deficit



Increased disposable income in the hands of consumers has contributed to the growth in private consumption expenditure. Consumer spending has therefore remained strong in line with more buoyant economic activity in the domestic economy. Although data on quarterly consumption expenditure are not readily available, the movement of the index of retail sales gives some indication of the trend in some key areas of consumer expenditure. In 2005, retail sales increased by 14.4 per cent indicating higher sales of durable goods in the domestic economy (Chart 20). Among the major components of the index that displayed significant increases were sales of motor vehicles and parts, which increased by 31.1 per cent in 2005 compared with 18.3 per cent and 15.4 per cent in 2003 and 2004 respectively. Sales of clothing (30 per cent), household appliances and furniture (17 per cent) and dry goods (17.9 per cent) also registered sizeable increases. From a financing perspective, credit card loan balances outstanding have also displayed strong growth increasing on a year-on-year basis to December 2005 and March 2006 by 9.2 per cent and 13.5 per cent, respectively (Chart 21).

Fiscal Developments

For the first six months of the fiscal year 2005/2006, the central government posted a surplus of $3,308.7 million. Revenue was higher than projected at $16,754.1 million on account of larger tax receipts both from individuals and companies and a 26 per cent increase in oil prices (Chart 22). The higher receipts also reflected the changes to the oil and gas tax regime announced in the 2006 budget. Total expenditure to the end of March reached $13,445.4 million, somewhat short of projections, but higher than the amount ($10,211.8 million) expended to March 2005. Spending on the capital programme was lower than projected and reflected administrative delays.

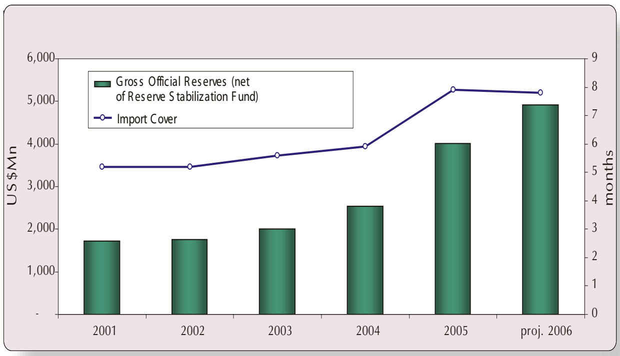
As government continued to increase expenditure on upgrading the country's economic and social infrastructure, the non-oil fiscal defict widened to $4,911.3 million, for the first six months (October 2005-March 2006) of the fiscal year. This figure was 56 per

Table 3
Summary of Government's Fiscal Operations
/$million/

	October 2004 - March 2005	October 2005 - March 2006		
	Actual	Actual	Budgeted	Variance
Total Revenue	12,656.6	16,754.1	15,558.2	1,195.9
Current	12,651.9	16,753.0	15,547.6	1,205.4
of which Oil Revenue	5,576.9	8,220.0	8,704.8	-484.8
Non-Oil Revenue	7,075.0	8,533.0	6,842.8	1,690.2
Capital	4.7	1.1	10.6	(9.5)
Total Expenditure	10,211.8	13,445.4	17,605.4	-4,160.0
Current	9,532.4	11,984.8	15,092.0	-3,107.2
Capital	679.4	1,460.6	2,513.4	-1,052.8
Overall Balance	2,444.8	3,308.7	(2,047.2)	5,355.9
Financing	-2,444.8	-3,308.7	2,047.2	-5,355.9
External (net)	-1,108.6	-122.6	-59.1	-63.5
Disbursements	155.6	185.6	220.0	-34.4
Repayments	-1,264.2	-308.2	-279.1	-29.1
Domestic (net)	-1,336.2	-3,186.1	2,106.3	-5,292.4
Memo items				
Non-Oil Fiscal Deficit	(3,132.1)	(4,911.3)		
Outstanding VAT Refunds	4,459.0	3,495.8		
Average Realised Oil Price (WTI)	US$48.96	US$61.63		

Source: Ministry of Finance.

Chart 24
Gross Official Reserves and Import Cover



cent higher than the deficit ($3,132.1 million) posted in the corresponding period of the previous fiscal year. The increase in this deficit has been a major contributor to the increase in liquidity in the domestic financial system (Chart 23).

External Accounts

Higher energy prices and increased export volumes resulted in a current account surplus of US $2,672.3 million. Total exports rose by 38 per cent on account of a 48 per cent increase in the value of shipments of mineral fuels and lubricants. Merchandise imports increased by 26.4 per cent to US$6,186 million, as both energy and non-energy imports recorded strong growth. In spite of heavy direct investment inflows of US$940 million, there was a deficit of US$306.4 million (or 2.1 per cent of GDP) on the capital account. Outflows linked to regional bond issues amounted to US$240.5 million. The balance of payments surplus amounted to US$1,893 million, (13.2 per cent of GDP) in 2005, more than double the previous year's surplus.

Gross official reserves totalled US$4.9 billion. Net of the Revenue Stabilisation Fund, gross official reserves amounted to US$4.0 billion, equivalent to 7.9 months of import cover (Chart 24).

3. Financial Sector Developments

Money and Credit

The buoyancy in the economy was reflected in the strong growth in the monetary aggregates. Narrow money (M-1A) defined as currency in active circulation and demand deposits increased by 30.8 per cent in the twelve months to March 2006, as the two components expanded by 17.6 per cent and 34.5 per cent, respectively. Broad money, M-2 (defined as M-1A plus time and savings deposits) increased by 29.9 per cent partly reflecting the growth in time deposits (67.6 per cent) (Chart 25). The sharp increase in time deposits was due mainly to intra-group transfers from non-bank affiliates to commercial

Table 4
Trinidad and Tobago: Summary Balance of Payments
/$million/

	2003	2004	2005e
Current Account Balance	**984.7**	**1,647.1**	**2,672.3**
Trade Balance	1,293.2	1,508.7	2,647.7
Exports	5,204.9	6,402.9	8,834.0
Energy	4,377.5	5,143.0	7,592.0
Non-energy	827.4	1,259.9	1,242
Imports	3,911.7	4,894.2	6,186.0
Energy	1,374.3	2,977.0	3,845.0
Non-energy	2,537.4	1,917.2	2,341.0
Services (Net)	313.8	479.5	526.5
Income (net)	- 680.9	- 397.3	- 554.4
Current Transfers (Net)	58.6	56.2	52.5
Capital and Financial Account*	-650.5	- 912.1	- 779.3
Overall Balance	334.2	735.0	1,893.0
Gross Official Reserves	2,258.0	2,993.0	4,781.4
Gross Official Reserves (Net of RSF)	2,094.5	2,539.1	3,906.1
Import Cover (Net of RSF)	5.9	5.9	7.8

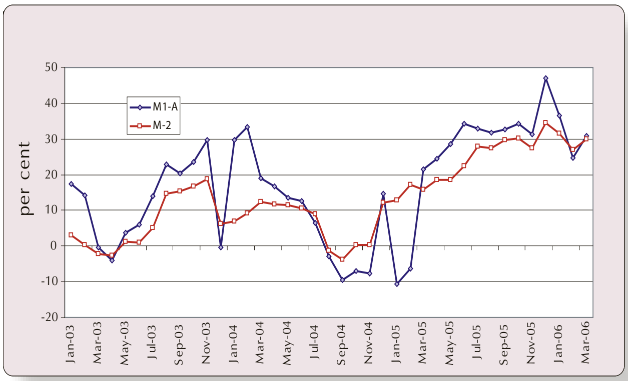
Source: Central Bank of Trinidad and Tobago.
e – estimate.
* - Includes errors and omissions.

Table 5
Commercial Banks Distribution of Loans by Interest Rate Bands
/$million/

Rate Bands	Value (TT$000s)	Distribution (per cent)	Cumulative Distribution (per cent)
2003			
0 % - 5 %	1,040,392	8.8	8.8
5 % - 7 %	1,850,303	15.7	24.6
7 % - 8 %	720,620	6.1	30.7
8 % - 9 %	1,279,112	10.9	41.6
9 % - 10 %	1,779,507	15.1	56.7
10 % - 12 %	2,338,529	19.9	76.6
Over 12 %	2,757,664	23.4	100.0
Total	11,766,127	100.0	
2004			
0 % - 5 %	1,420,927	9.1	9.1
5 % - 7 %	3,051,336	19.6	28.7
7 % - 8 %	1,352,881	8.7	37.4
8 % - 9 %	3,865,359	24.8	62.2
9 % - 10 %	1,690,535	10.8	73.0
10 % - 12 %	2,134,681	13.7	86.7
Over 12 %	2,069,949	13.3	100.0
Total	15,585,668	100.0	
2005			
0 % - 5 %	2,393,207	10.9	10.9
5 % - 7 %	3,608,305	16.5	27.4
7 % - 8 %	2,899,504	13.2	40.7
8 % - 9 %	3,693,480	16.9	57.5
9 % - 10 %	3,674,888	16.8	74.3
10 % - 12 %	3,168,305	14.5	88.8
Over 12 %	2,450,528	11.2	100.0
Total	21,888,217	100.0	

Source: Central Bank of Trinidad and Tobago.
The shaded areas represent the distribution of loans below the prime lending rate.

Chart 25
Monetary Aggregates
(year on year changes)



banks. Consequently, quasi money (time and savings deposits) showed strong growth. Foreign currency deposits expanded by 6.2 per cent on a year-on-year basis to March 2006. These deposits comprised 25.9 per cent of total deposits, slightly lower than the ratio recorded a year earlier.

Since the last edition of the Monetary Policy Report, the 'Repo' rate was increased on four occasions in 2005 and in each month of the first quarter of 2006. Correspondingly, commercial banks' prime lending rate has increased in equal steps of 25 basis points each from 9.50 per cent in October to 10.50 per cent by the end of March (Chart 27). The weighted average lending rate also rose to 9.49 per cent at the end of March 2006 from 9.09 per cent at the end of December 2004. The weighted average deposit rate stood at 2.42 per cent from 1.86 per cent in December 2004.

Chart 26
Credit to Businesses and Consumers by the Consolidated Financial System

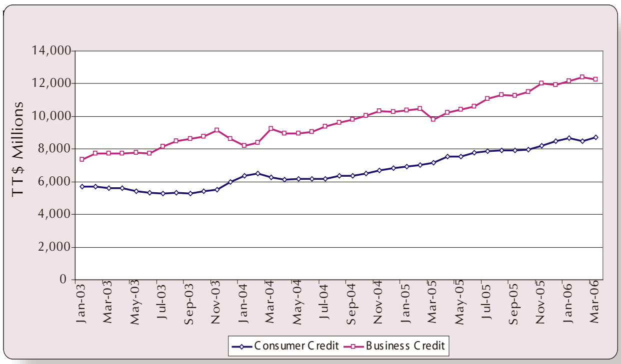


Chart 27
Selected Interest Rates

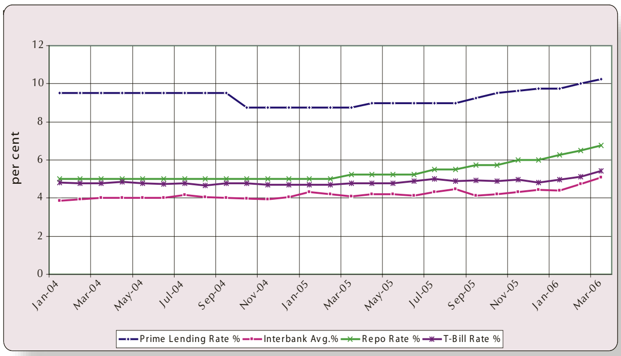
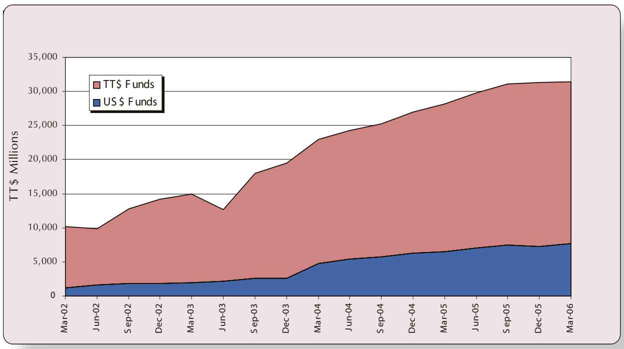


Chart 28
Mutual Funds by Currency Denomination



Consequently, the spread between lending and deposit rates narrowed to 7.07 per cent in March 2006 from 7.23 per cent in December 2004.

Commercial bank credit to the private sector expanded by 28.4 per cent in the twelve months to March 2006, almost double the growth (14.7 per cent) a year earlier. Consumer credit grew by 21.6 per cent, while loans to business firms jumped to 24.7 per cent from 6.1 per cent in March 2005. In 2005, almost 60 per cent of loans were contracted at rates below the prime lending rate. Credit to the private sector by the consolidated financial system increased by 15.7 per cent in the twelve months to March 2006, slower than the growth of 21 per cent recorded in December 2005 (Chart 26).

Mutual Funds

The rate of growth of mutual funds slowed to 16 per cent in 2005 compared with an average annual expansion of 44.2 per cent over the previous five years. This fall-off mirrored the recent weak performance of the stock market. Money market funds increased by 17.9 per cent to $25 billion, outperforming income and growth funds which grew by 8.9 per cent, substantially below the increase of 56.3 per cent seen in 2004. Net incremental investments totalled TT$3.9 billion, of which 79.5 per cent was invested in TT-dollar denominated funds (Chart 28). Returns on money market instruments ranged between 4.83 per cent and 7.16 per cent, while returns on some of the income and growth funds were negative.

During the first quarter of 2006, funds under management remained relatively unchanged from the previous quarter. Money market funds grew by 2.95 per cent while the income and growth funds recorded a decline of 8.63 per cent. Returns on the money market funds were relatively unchanged from a year ago at 5.74 per cent, while the TT-dollar income and growth segment posted a return of -14.77 per cent.

Chart 29
Primary Bond Market Activity 2005

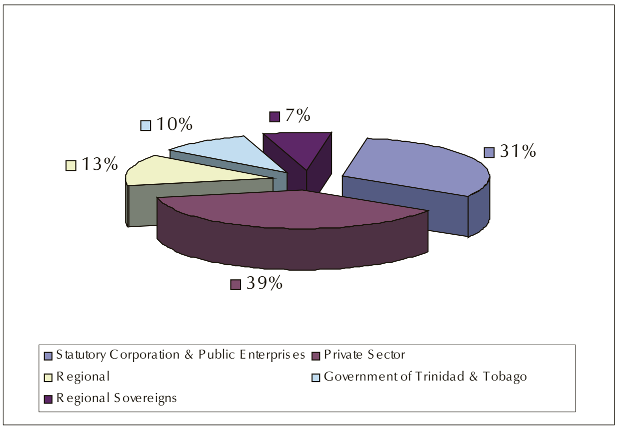


Chart 30
Primary Bond Market Activity 2003 - 2005

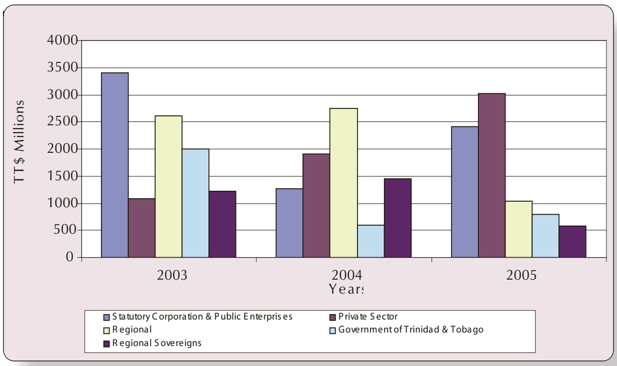
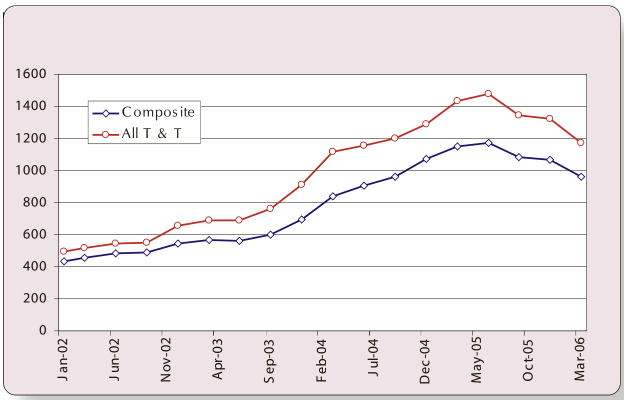


Chart 31
Trinidad and Tobago Stock Price Indices



Bond Market

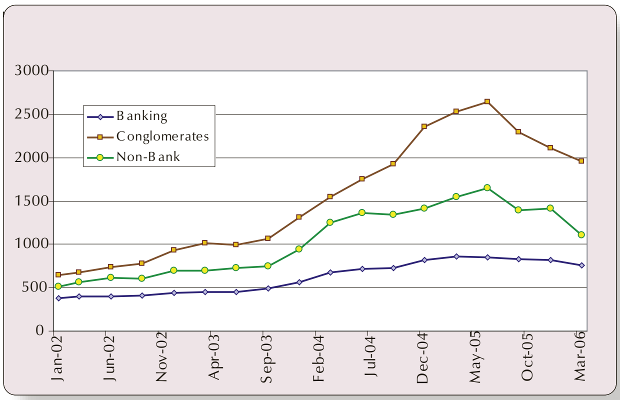
In 2005, there were 37 placements on the primary bond market with a face value of TT$7.8 billion. Of these, 11 were foreign currency issues, accounting for 29.7 per cent of total activity while the remaining 26 were TT-dollar placements valued at over TT$4.9 billion. On the regional front, there was only 1 placement by a sovereign (the Government of Aruba) in the amount of US$93 million (with a tenor of 10 years and fixed interest rate of 6.4 per cent) and 4 private sector issues valued at US$165.2 million (Chart 30). The latter placements carried 10 and 12 year-maturities with both fixed and floating rates. The public sector issued 8 bonds (3 by the central government and 5 by statutory corporations) (Chart 29). These issues were conducted using the automated auction system. The tenors on these bonds ranged between 10 and 25 years with interest rates ranging between 6.00 and 7.75 per cent.

During the first quarter of 2006, available data indicated that there were 2 issues by the public sector. The Urban Development Corporation of Trinidad and Tobago (UDeCOTT) raised TT$192 million at a rate of 7.00 per cent, while the Housing Development Corporation (HDC) issued the first tranche of a $1.4 billion bond in two parts, raising $136 million in December 2005 and $464 million in January 2006. The tenor of the HDC bond was 25 years and the coupon rate was 7.75 percent. At the initial auction in December, the yield was 8.00 per cent which rose to 8.75 per cent when the remaining $464 million was raised.

Stock Market

In the first five months of 2005, the Composite Stock Price Index (CPI, 1983=100) and the All Trinidad and Tobago Index (ATI, 1999=100), increased by 13.1 per cent and 20.6 per cent, respectively (Chart 31). However, in the second half of the year, the market declined sharply and all the gains achieved were wiped out by year's end. The CPI closed the year at 1,067.4, 0.7 per cent lower than in the previous year. This represented a reversal of the bull run in 2004 when growth of 54.8 per cent was registered. Market capitalization fell by 0.1 per cent and the volume of shares traded also decreased by 33.1 per cent from 312.5 million, one year earlier. All the sub-indices with the exception of the Manufacturing I,

Chart 32
Trinidad and Tobago Stock Price Indices: Selected Sub-Sectors



Manufacturing II and Trading closed the year at lower levels. Of these three, the Trading sub-index recorded the largest gain of 38.2 per cent with Manufacturing I and II increasing by 6.2 per cent and 21.1 per cent, respectively (Chart 32).

During the first three months of 2006, the market continued to be bearish, with the CPI and ATI falling by 10.2 per cent and 11.5 per cent, respectively. The number of shares traded amounted to 41.1 million with a value of $715.1 million, while market capitalization was $97.1 billion. By comparison, the volume of shares traded in the first quarter of 2005 totalled 54.4 million valued at $1,026.7 million while market capitalization was $139.3 billion.

The Real Estate Mortgage Market

The real estate mortgage market continued to experience steady growth in the final quarter of 2005. The value of mortgage loans outstanding on the books of deposit taking institutions (commercial banks and trust and mortgage companies) increased from $5,000 million in December 2004 to $5,818.2 million at the end of March 2006, an expansion of 16.4 percent (Chart 33). Since mid-2005, real estate mortgage rates of commercial banks have trended upward following increases in the Central Bank's Repo rate. Available data indicate that the mortgage rates of the commercial banks increased from 9.38 per cent in September 2005 to 10.38 per cent as at the end of March 2006, an increase of 100 basis points (Chart 34).

Chart 33
Deposit-taking Institutions: Mortgage Loans Outstanding

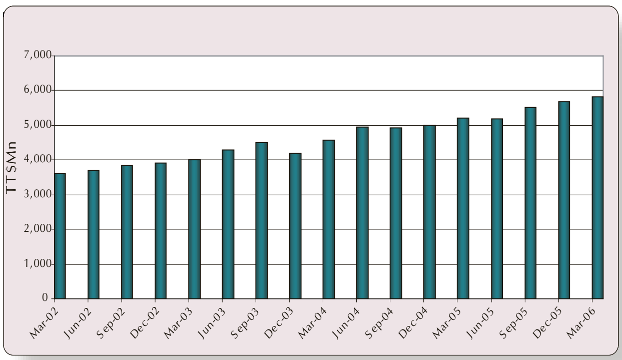
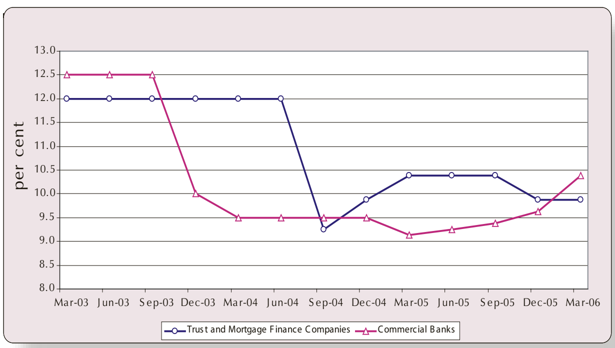


Chart 34
Commercial Banks and Trust Companies Real Estate Mortgage Loan Rates



Appendices:

Media Releases on the 'Repo' Rate from November 2005 to April 2006

1 **Media Release dated November 25, 2005 -**
Central Bank Raises 'Repo' Rate to 6.0 Per cent

2 **Media Release dated December 22, 2005 -**
Central Bank Maintains 'Repo' Rate at 6.0 Per cent but Introduces Special Measures to Reduce Excess Liquidity

3 **Media Release dated January 20, 2006 -**
Central Bank Raises 'Repo' Rate to 6.25 Per cent

4 **Media Release dated February 24, 2006 -**
Central Bank Raises 'Repo' Rate to 6.50 Per cent

5 **Media Release dated March 28, 2006 -**
Central Bank Raises 'Repo' Rate by 25 Basis Points to 6.75 Per cent

6 **Media Release dated April 28, 2006 -**
Central Bank Maintains 'Repo' Rate at 6.75 Per cent

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Media Release

CENTRAL BANK RAISES 'REPO' RATE TO 6.0 PER CENT

Inflation data released by the Central Statistical Office for the month of October indicate that headline inflation, which measured 6.8 per cent year-on-year to October, has remained outside of the Central Bank's target range. Food prices, which continue to provide the main impetus for headline inflation, rose by 22 per cent in the twelve months to October. Core inflation, however, remained steady at 2.6 per cent year-on-year to October.

The net domestic fiscal deficit continues to add to liquidity in the financial system. The liquidity overhang has contributed to both a strong growth in private sector credit and demand pressures in the foreign exchange market. Private sector credit grew on a year-on-year basis to September by 20.3 per cent, with consumer credit increasing by 24 per cent. Business credit, however, has been growing at a much slower pace (15.1 per cent) than consumer credit.

The gradual increases in the Feds Funds rate have contributed to a narrowing of the differential between the 90-day TT and US treasury bill rates. This differential, which stood at 2.35 per cent at the start of 2005, has narrowed to just 1.02 per cent at the end of October.

Against the background of persistent inflationary pressures, the sharp narrowing in the differential between short-term TT and US dollar rates, and a persistent liquidity overhang, the Central Bank has decided to raise its 'Repo' rate to 6.0 per cent with effect from November 25, 2005.

The Bank will continue to keep monetary conditions under close review.

The next 'Repo' rate announcement is scheduled for December 21, 2005.

November 25, 2005.

- END -

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Media Release

CENTRAL BANK MAINTAINS 'REPO' RATE AT 6.0 PER CENT BUT INTRODUCES SPECIAL MEASURES TO REDUCE EXCESS LIQUIDITY

The latest data released by the Central Statistical Office indicate that headline inflation, measured by the 12-month increase in the index of retail prices, rose to 7.03 per cent in November compared with 6.94 per cent in October. The increase was led by food prices, which rose by 22.6 per cent in the twelve months to November. In November alone, food prices rose by 3.3 per cent, the second highest monthly increase for the year so far. Core inflation, which excludes food, at 2.65 per cent (year-on-year) is up noticeably from a year earlier (1.81 per cent).

The high levels of liquidity, arising in part from increased public sector spending, is a major contributor to the current inflationary environment. The receipt of foreign loans to finance domestic expenditures has boosted the already elevated levels of liquidity. This has contributed to an exceptionally high level of special deposits held at the Central Bank.

Changes in the 'Repo' rate are therefore not being effectively transmitted to the general level of interest rates because of the existence of excess liquidity. With banks awash with cash, the growth in bank credit to the private sector has also remained relatively high. Credit to the private sector in the twelve months to October 2005 grew by 19.7 per cent, with consumer credit and loans to businesses growing by 22 per cent and 14.5 per cent, respectively.

The difficulties at the ports and the impact of recent floods on agricultural production seem to be adding to inflationary expectations. This, coupled with the current level of inflation, could trigger wage pressures and further complicate inflation control.

- 2 -

In light of these developments, the Central Bank has decided to introduce additional measures geared towards managing liquidity and improving the efficiency of monetary policy. The specific measures being introduced are as follows:

- The rate paid on special deposits held by commercial banks at the Central Bank which was lowered from **3.50 per cent** to **2.50 per cent** as at September 1, 2005, has been further reduced to **zero per cent** with effect from **Wednesday December 28, 2005**.

- Commercial banks will be required to place in aggregate **TT$1.0 billion** in an interest-bearing deposit account at the Central Bank for **a minimum period of one year**.

The Bank will maintain the 'Repo' rate at its current level of 6.0 per cent and will continue to keep monetary conditions under close review.

The next 'Repo' rate announcement is scheduled for **January 20, 2006**.

December 22, 2005.

- End -

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Media Release

CENTRAL BANK RAISES 'REPO' RATE TO 6.25 PER CENT

Inflation data released by the Central Statistical Office indicate that headline inflation rose to 7.2 per cent in the twelve months to December 2005 compared to 7.0 per cent in November 2005 and 5.6 per cent one year earlier. Food prices continued to drive headline inflation rising by 22.6 per cent in the twelve months to December. The prices of vegetables and fruits, which rose by 72.9 per cent and 27 per cent, respectively over the year, continued to provide the main impetus for the increase in food prices. Core inflation held steady at 2.7 per cent.

Last month, the Bank moved to tighten liquidity by withdrawing TT$1 billion dollars from the system. Since then, the Bank has stepped up sales of open market bills of longer term maturity (one and two years). These measures have sharply reduced excess liquidity and created a more favourable environment for the transmission of interest rate signals.

Meanwhile, the continuing increase in US interest rates has reduced the differential between TT and US short term rates to 80 basis points, the lowest spread to date.

Against this background and in light of persistent inflationary pressures, the Bank has decided to raise its overnight 'Repo' rate by 25 basis points to 6.25 per cent with effect from January 20, 2006. The rate was last changed in November 2005.

The Bank will continue to keep monetary conditions under close review.

The next 'Repo' rate announcement is scheduled for **February 24, 2006**.

January 20, 2006.

- End -

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Media Release

CENTRAL BANK RAISES 'REPO' RATE TO 6.50 PER CENT

Recent inflation data released by the Central Statistical office point to persistent inflationary pressures with headline inflation increasing by 7.04 per cent year-on-year to January 2006. Food prices, which rose by 22.8 per cent on a year-on-year basis to January, continued to provide the main impetus for the rise in headline inflation. Core inflation, which excludes the impact of food prices, declined to 2.5 per cent in January 2006 (year-on-year) from 2.8 per cent one year earlier.

Financial conditions in January were little changed from the second half of 2005. Bank credit expanded at a rapid pace and the high level of the net domestic fiscal deficit continued to propel the growth in liquidity in the financial system. In December 2005, the Central Bank required commercial banks to deposit TT$1 billion in an interest-bearing account, which had the effect of dampening liquidity conditions. The Bank continued to engage in active open market operations and, since the beginning of 2006, absorbed some TT$ 1.9 billion in liquidity through foreign exchange sales.

In 2005, private sector credit expanded by 21 per cent with consumer credit growing faster (by 24 per cent) than credit to businesses (16 per cent).

With the continued increase in the Fed Funds rate to 4.5 per cent in January 2006, the differential between TT and US short-term interest rates has narrowed sharply to 55 basis points from 198 basis points in February 2005. This narrowing of the differential has contributed to a strong demand for foreign exchange.

Against the background of persistent inflationary pressures and a sharp fall in the spread between TT and US dollar short-term interest rates, the Central Bank has decided to increase the 'Repo' rate by 25 basis points to **6.50** per cent from **6.25** per cent with effect from February 24, 2006.

The Bank will continue to keep monetary conditions under close review.

The next 'Repo' rate announcement is scheduled for **March 24, 2006**.

February 24, 2006

- End -

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Media Release

CENTRAL BANK RAISES 'REPO' RATE BY 25 BASIS POINTS TO 6.75 PER CENT

The Central Bank has decided to increase the 'Repo' rate by 25 basis points from 6.5 per cent to 6.75 per cent with effect from March 28, 2006. This decision comes against the background of persistent inflationary pressures, the continued sharp growth in private sector credit and the narrowing of the differential between TT and US dollar short-term interest rates as US rates continue their upward climb.

The latest available data on prices released by the Central Statistical Office indicate that headline inflation measured 6.5 per cent year-on-year to February 2006, down from 7.04 per cent in January, but still outside of the Bank's target range of 4–5 per cent. Core inflation held steady at 2.5 per cent.

The Bank has intensified its efforts at absorbing liquidity, including through the use of longer term debt instruments. As a result, treasury bill yields have increased 50 basis points since the start of the year. The strong bank credit growth has persisted notwithstanding the steady rise in commercial banks' prime lending rates. In the 12 months to January 2006, private sector credit increased by 20.3 per cent from 12.0 per cent one year ago, with consumer credit (25.1 per cent) leading overall credit expansion.

The recent increase in the Fed Funds rate to 4.50 per cent has caused the spread between US and TT short-term rates to narrow to 61 basis points compared with 198 basis points at the end of February 2005. A larger spread normally translates into higher borrowing costs locally and encourages firms to borrow abroad rather than locally to fund their acquisition of foreign assets.

The Bank will continue to keep monetary conditions under close review.

The next 'Repo' rate announcement is scheduled for **April 28, 2006**.

March 28, 2006.

- End -

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Media Release

CENTRAL BANK MAINTAINS 'REPO' RATE AT 6.75 PER CENT

Recent data on inflation released by the Central Statistical Office indicate that headline inflation measured 6.6 per cent on a year-on-year basis, slightly up from the 6.5 per cent reported for February but still outside of the Bank's target range of 4-5 per cent. Food prices continue to be the main driver of inflation registering an increase of 19.3 percent year-on-year. In this category, fruits and vegetables and fish have posted significant price increases. Core inflation nudged up to 2.7 per cent (year-on-year) from 2.5 per cent on account of increases in medical services (8.8 per cent) and other fuels (1.5 per cent).

There are as yet no clear signs of any substantial easing in inflationary pressures. The non-energy fiscal deficit continues to increase.

Private sector credit on a year-to-year basis to February 2006 grew by 18.5 per cent with consumer credit rising by 20.4 per cent. While overall credit growth may be slowing consumer credit continues to expand strongly.

The Bank has maintained its policy of absorbing liquidity through the issue of short and medium-term instruments. As a result of a steady rise in domestic treasury bill rates the differential between TT and US short-term rates widened slightly to 104 basis points in April 2006 from just under 1 per cent at the end of March.

The Central Bank considers that monetary policy needs to remain tight to address inflation pressures. In the coming weeks the Bank will discuss with commercial banks further measures to absorb liquidity and dampen consumer credit.

Against this backdrop the Bank has decided to maintain the 'Repo' rate at 6.75 percent.

The next 'Repo' rate announcement is scheduled for **May 26, 2006**.

April 28, 2006.

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