MARLA DUKHARAN

ECONOMICS 102

There is no such thing as a free lunch.

#BeltAndRoadLoading

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“Countries only approach the International Monetary Fund when they run out of foreign exchange, and they can’t service their foreign debt. That, Madam Speaker, is Economics 101”
- The Honourable Colm Imbert, Minister of Finance, June 9th, 2021.

We often hear that ‘politics trumps economics’. So, when such statements uttered by career politicians seem illogical, if not untrue from an economics standpoint, I am left only to hope that they make some sense when viewed through that dynamic and mysterious lens of politics.

Trinidad and Tobago finds itself, perennially it seems, being misled by those responsible for leading - both by the current administration, and by the current opposition (especially when they were in power). At the risk of repeating myself, as much of what the Minister articulated on June 9th was addressed in an earlier piece, I draw heavily on that and other writing, in an attempt to present a clearer picture here, on some of his recent statements.

1. “Countries only approach the International Monetary Fund when they run out of foreign exchange, and they can’t service their foreign debt. That, Madam Speaker, is Economics 101”

Countries do not approach the IMF only when they ‘run out of foreign exchange’, which constitutes a Balance of Payments (BoP) crisis. On the contrary! The Minister then immediately contradicted himself by restating the well-known fact that T&T receives Technical Assistance from the IMF: “we interface with the IMF on a regular basis for technical assistance. In fact, we had a meeting just a month ago where we asked the IMF to assist us with a number of fiscal and monetary matters and that these are ongoing technical assistance programs at the IMF.” In addition to Technical Assistance opportunities, there are rapid financing mechanisms available from the IMF in emergency situations, unrelated to a BoP crisis.

2. “Whenever the IMF is approached for financial assistance...you have to commit to a structural adjustment program”

In the first place, access to the IMF’s Rapid Financing Instrument for example, does NOT require a commitment to an IMF supported reform program. The IMF does require, however, a certain level of transparency and accountability for (pandemic-related) fiscal spending, as the IMF has asked Governments to “keep the receipts.” Accessing any financing from the IMF comes with a certain level of transparency and scrutiny, which may make those with ‘cocoa in the sun’ uncomfortable.

Secondly, the term ‘Structural Adjustment’ is so 1980’s! This terminology was discontinued along with many of the reforms prescribed back then to ‘liberalize’ (developing) economies in debt / BoP crises. T&T is hemorrhaging over USD1 billion in foreign reserves annually (absent HSF drawdowns and USD borrowing), and will run out of USD by 2022, falling into a BoP crisis UNLESS there is reform. Seeking BoP support from the IMF (as opposed to Rapid Financing, which is emergency-driven) implies some commitment to reforms which we should want anyway, to mitigate the risk of repeating our mistakes. The Minister stated however, that “the country cannot afford” such reforms at this time. Classic short-termism.

Finally, reforms are not imposed by the IMF – arriving at an agreement involves a negotiation process based on the evidence, resulting in a bespoke reform agenda. For example, Jamaica agreed to depreciate its currency while Barbados did not. Barbados agreed to external and domestic debt restructure, while Jamaica only restructured its domestic debt - twice. Barbados and Jamaica agreed to address their public sector wage bill via retrenchment, but Grenada did not.

3. A June 16th 2021 article stated **"Finance Minister Colm Imbert says the Government opted to accept a TTD1.4 billion loan from China as it had fewer conditions attached to it as opposed to one from the Washington DC-based International Monetary Fund (IMF). Imbert observed that the rate of interest for the loan from China was 2% compared to 1.05% from the IMF."**

It is quite telling when a government opts to borrow from a more expensive lender, because their 'conditions' are deemed to be better. Better for whom? Taxpayers are ultimately liable for repayment of this and all sovereign obligations, and it is in the interest of the taxpayer - the ultimate borrower - that such financial obligations and the disbursement of the associated funds, is conducted in a transparent manner. Transparency does not appear to be a priority for this Government, as evidenced by the amendment to the Procurement Legislation which exempts such bilateral deals. The Government's aversion towards transparency in the first place, and to proactive reforms more broadly, is deeply troubling. This stated preference for less transparent, more costly bilateral deals is precisely the approach adopted by Venezuela, and the consequences are self-evident. As the Global Financial Crisis reminded us, lenders bear a level of responsibility for ensuring that the loans they grant are likely to be repaid comfortably by the borrower. Lending to a borrower who is already exhibiting signs of distress - compromised ability to repay debt as evidenced by a longstanding primary fiscal deficit, inability to honour VAT refunds, rising arrears on current obligations in LOCAL currency, let alone foreign currency, as in the case of T&T - is irresponsible at best, and could suggest a possible (hidden) agenda.

Granted, bilateral loans are usually some of the easiest to renegotiate in a default / BoP crisis scenario, but what happens when the borrower can't meet the lender's repayment requirements? Security for the loan is usually then realized. What security has this and previous Governments offered the Chinese for their loans? What state assets are encumbered or are likely to be used to repay loans that we are unable to honour in cash?

The Belt and Road initiative is at least a stated agenda, unlike similar (covert) missions of the global North in years gone by, and we are grateful to the Chinese Government for their generosity. But we must ask the questions: Are the details of these deals transparent? No. Are these deals in the best interest of our nation's socio-economic development in the long-term? Without the details, we can't be sure, but I would guess not (think white elephants and higher borrowing costs). Is this (rising) level of exposure to one (bilateral) lender healthy? Absolutely not. The Government of China's Belt and Road agenda may be pure, but with so much at stake, they are likely to be conflicted, and unlikely to have our nation's best interest at heart, over theirs, in any event. Again, see Venezuela. Financing a bankrupt Government if not failed state is irresponsible at best, and introduces doubt as to the true motives for such lending.

China's interests in Trinidad and Tobago:

YEAR	MONTH	CHINESE ENTITY	USD MILLIONS	TRANSACTION PARTY	SECTOR	SUBSECTOR
2008	January	Jiangsu International	$180	Construction Contract	Other	Education
2009	May	CNOOC, Sinopec	$320	Talisman Energy	Energy	Oil
2011	November	CIC	$850	GDF Suez	Energy	
2014	December	Power Construction Corp	$100	Construction Contract	Utilities	
2015	May	China Railway Construction	$230	Construction Contract	Health	
2018	January	China Railway Construction	$220	Construction Contract	Transport	Autos
2018	November	Beijing Construction Engineering	$100	Construction Contract	Other	Industry
2019	May	Shanghai Construction	$160	Construction Contract	Health	

Source: China Global Investment Tracker, The American Enterprise Institute and The Heritage Foundation.

Outstanding loans owed by T&T to China:

LOAN NAME	LOAN AMOUNT / CURRENCY	INTEREST EXPENSE 2021 BUDGET (TTD)	PRINCIPAL PAYMENTS 2021 BUDGET (TTD)
Couva Children's Hospital	USD270 million	17,500,000	66,000,000
National Academics for the Performing Arts	RMB812,000,000	9,600,000	68,500,000
Chinese Multi-purpose Vessels	USD34,200,000	3,100,000	
Total Foreign Loans Expenditure 2021 Budget		1,402,557,500	1,342,063,800

Source: 2020/2021 Estimates of expenditure; https://www.thedialogue.org/map_list/

With this backdrop, let's take a look at the fiscal numbers recently released by the Minister of Finance.

FISCAL DEFICIT

The fiscal deficit for FY2019/2020 was originally expected to be TTD5.3 billion, but the pandemic led to an actual deficit around TTD17 billion. This does NOT include arrears on VAT refunds and other items. To finance this deficit :

• US900 million was withdrawn from the HSF;

• We tapped into the domestic capital market under the Development Loans Act and utilised just over TTD1 billion of the TTD10 billion available;

• We sourced USD300 million from various multilateral agencies: USD20 million from the World Bank, USD130 million from the Inter-American Development Bank (IADB) and USD150 million from the Development Bank of Latin America (CAF); and

• We sourced a net USD250 million on the external capital market.

The deficit for FY2020/2021 was expected to decline from ~TTD17 billion, to TTD8.2 billion, based on the following projections:

• Total revenue - TTD41.364 billion
• Oil revenue - TTD9.265 billion
• Non-oil revenue - TTD31.193 billion
• Capital revenue - TTD0.905 billion
• Total expenditure (net of capital Repayments and sinking fund contribution) - TTD49.573 billion

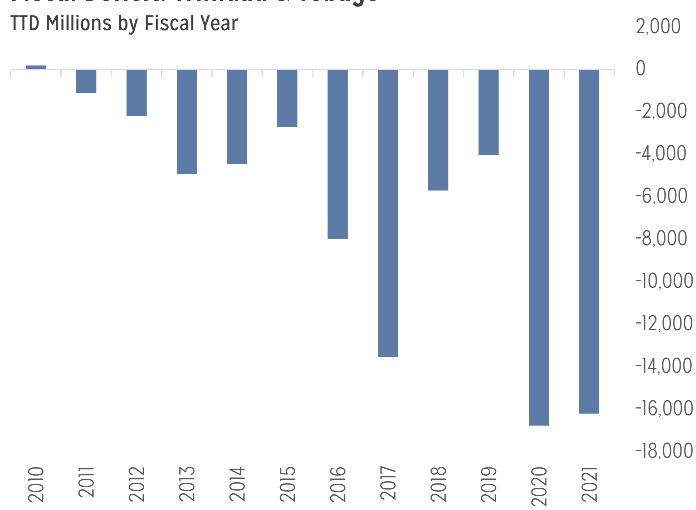
The Minister went on to say: "if you take that TTD3 billion more or less (expenditure increase), then the TTD5 billion (revenue shortage), we are looking at an unplanned event in the vicinity of TTD8 billion." This will cause the deficit to now reach about TTD16 billion.

It is important to note that the stated deficit number does NOT include VAT and other arrears, and there were TTD3 billion in outstanding VAT arrears in March 2021 according to Central Bank data. The true expected deficit, if arrears were honoured, would therefore reach roughly TTD19 billion (8+8+3) at least.

In the 10 fiscal years prior to the pandemic, the Government overspent what it earned in revenues by TTD46.4 billion, indicating that the pandemic did not create our fiscal imbalances, but it has exacerbated what was already an unsustainable situation.

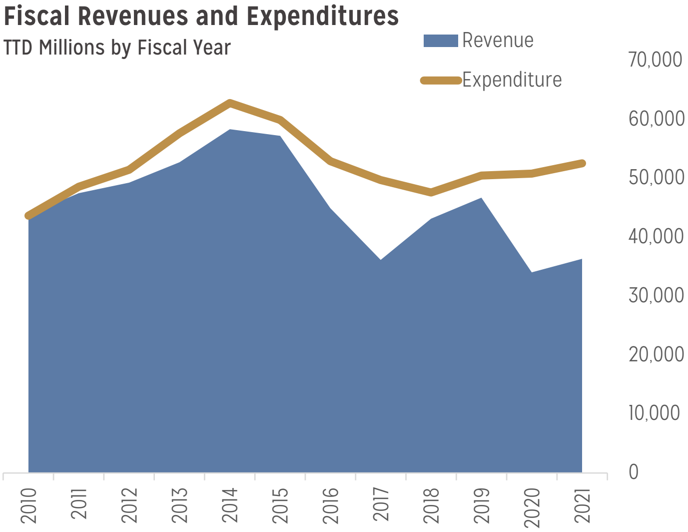
Fiscal Deficit: Trinidad & Tobago

TTD Millions by Fiscal Year



Source: Central Bank of Trinidad & Tobago,
IMF, Review of the Economy & Budget Statement, Min. of Finance, Marla Dukharan

Fiscal Revenues and Expenditures
TTD Millions by Fiscal Year

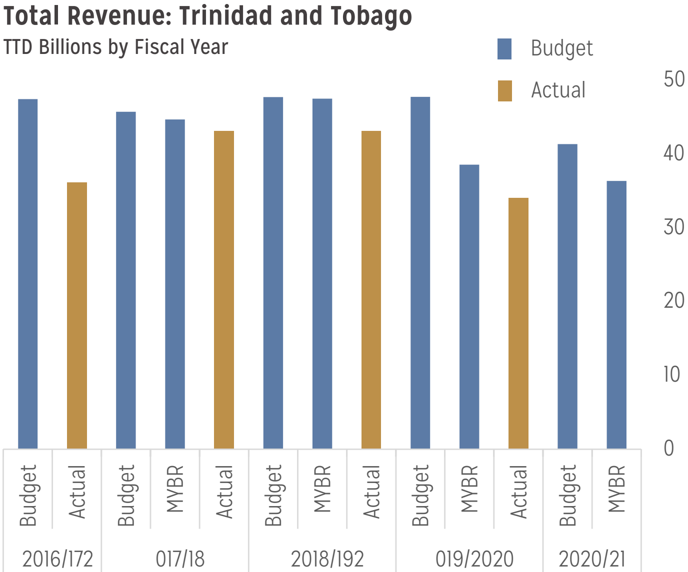


Source: Ministry of Finance of Trinidad and Tobago, Central Bank of Trinidad and Tobago, Marla Dukharan

OIL AND GAS PRICES, PRODUCTION AND REVENUES

For many years, actual fiscal revenue collected has fallen short of budgeted revenue. Perhaps this indicates a fundamental flaw in the revenue budgeting methodology (particularly for the oil and gas sector), which again, the pandemic didn't create, but has exacerbated.

Total Revenue: Trinidad and Tobago
TTD Billions by Fiscal Year

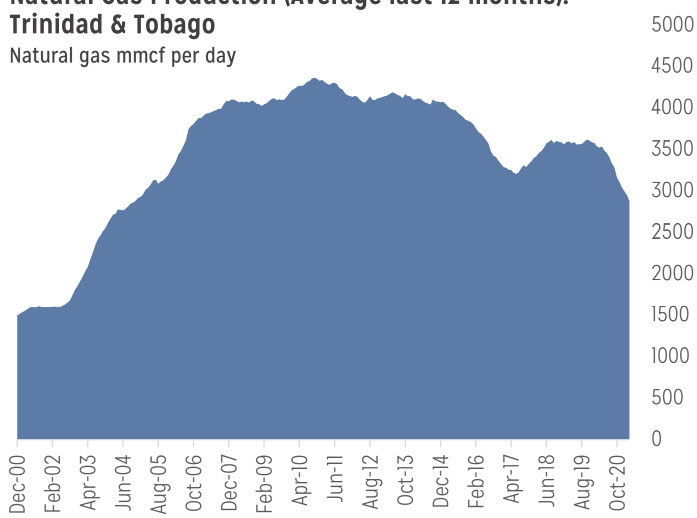


Source: Central Bank of Trinidad & Tobago, Review of the Economy & Budget Statement, Min. of Finance, Marla Dukharan

The Minister stated that Natural gas production is below forecast, natural gas prices are below forecast, oil prices are significantly above the forecast, but oil production is a bit below budget. Two-thirds of our (oil and gas) fiscal revenue, and sometimes more, comes from natural gas, and just 1/3 or less comes from oil. Lower prices and production of natural gas have affected revenues significantly.

Natural gas production over the last 12 months for which data is available, averaged 2,878 mmcf/d. This is on par with production levels in 2004.

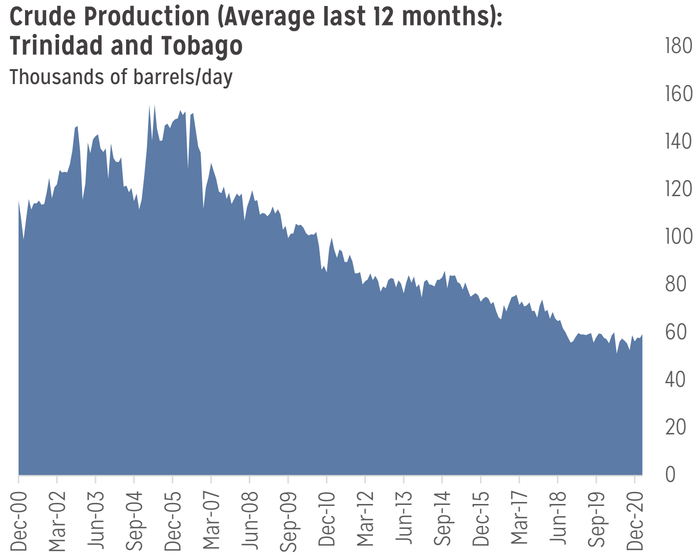
Natural Gas Production (Average last 12 months): Trinidad & Tobago
Natural gas mmcf per day



Source: Central Bank of Trinidad and Tobago, Marla Dukharan

Crude oil Production is only moving in one direction:

Crude Production (Average last 12 months): Trinidad and Tobago
Thousands of barrels/day



Source: Central Bank of Trinidad and Tobago, Marla Dukharan

The Minister disclosed the following points on Revenue:

• Average oil production for the period October 2020 to May 2021 was 57,889 barrels per day, which is below the projected production level. Weighted average price for this financial year from October 2020 to April 2021 is USD52.76/bbl - above the budgeted USD45/bbl.

• Budgeted income from oil companies' taxes on incomes and profits by the end of April 2021 was TTD1.3 billion, but came in at TTD900 million, so there is a shortfall of about TTD400 million.

• The budget anticipated that by the end of April we would have received TTD2.9 billion in royalties on oil and gas, however the actual receipts are TTD1.1 billion - a significant shortfall of TTD800 million.

• There was a reduction in terms of taxes on incomes and profits from oil companies, other corporations, withholding tax, business levy, and all affected by the situation in the energy sector, of some TTD500 million.

• Extraordinary revenue from oil and gas companies is short by some TTD230 million.

• The fiscal revenue outturn (from oil and gas) to April 2021 is a shortfall of approximately TTD2.5 billion.

NON-ENERGY REVENUE

• Revenue from non-energy companies was budgeted at about TTD3.1 billion and we have received TTD3.0 billion, so the shortfall is about TTD100 million.

• We budgeted to receive TTD3.5 billion in income from individuals by the end of April and we received TTD3.48 billion.

EXPENDITURE

The Minister highlighted the fact that WASA costs taxpayers in excess of TTD2 billion per annum, which likely falls under "Transfers and Subsidies". He stopped short of sharing what was being done to address this unsustainable situation.

He disclosed that we are likely to spend in total about USD15.7 million on the acquisition of vaccines for 85% of the population, or approximately 1.2 million persons.

FOREIGN EXCHANGE

The Minister repeatedly attempted to dispel the notion that there was any challenge regarding the nation's foreign exchange situation, but the evidence does not support his arguments:

• Between March 2015 and September 2020, the country lost USD9.796 billion in foreign exchange under the Errors and Omissions item of the Balance of Payments. This means that we are unable to account for how almost USD10 billion left our country in just five years. What a difference USD2 billion each year could have made!!

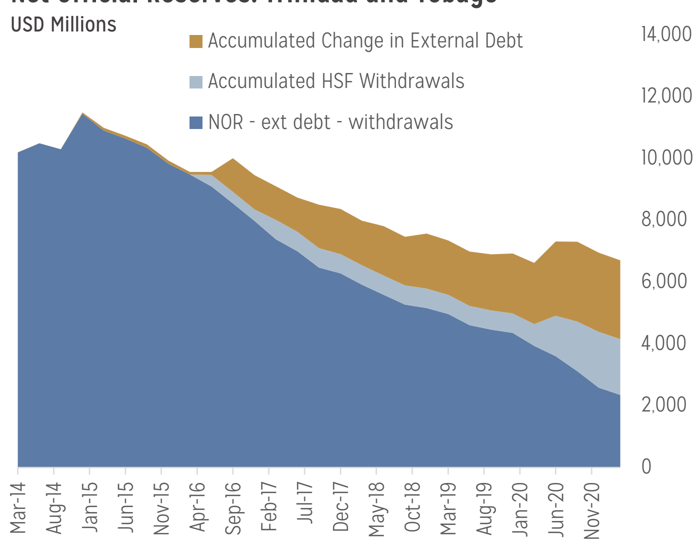
• Foreign exchange reserves reached USD6.675 billion at the end of May 2021, which is roughly the same as the December 2007 level.

• Despite USD562 million in net external debt being accumulated over the last 12 months and USD1.1 billion in HSF withdrawals, reserves declined 3.2% y/y in May 2021.

• Reserves since March 2014, before oil prices fell, to March 2021:

	USD MILLIONS
Reserves March 2014	10,203
Accumulated change in External Debt (Mar 2014 - Mar 2021)	2,548
Accumulated HSF withdraws (Mar 2014 - Dec 2020)	1,806
March 2021 total reserves	6,705
March 2021 reserves excluding debt and HSF withdraws	2,351

Net Official Reserves: Trinidad and Tobago



Source: Ministry of Finance of Trinidad and Tobago, Central Bank of Trinidad and Tobago, Marla Dukharan

Reserves are largely at the current level of USD6.7 billion because of external borrowing and HSF withdrawals. Were it not for these two FINITE sources of USD, we would now have around USD2.3 billion or 3 months of import cover, which is the precautionary benchmark. Falling below this benchmark signals rising risk of capital flight, and ultimately a BoP crisis.

The fact that T&T has been unable to organically grow its level of FX reserves over the years, tells us that there are serious structural problems in the economy. Uncompetitiveness and chronic fiscal deficits are the main drivers of declining reserves, but is anything being done to address these chronic challenges?

The Minister stated "...in 2021, our objective is to keep the economy moving, to stimulate economic activity, to continue to provide financial assistance to individuals and businesses, where necessary and appropriate and to keep as many people employed as is possible... With respect to borrowing, if we stop borrowing then we cannot finance the fiscal deficit, we cannot do the supplementation, we can't pay salaries, we can't finance education, and certainly we cannot finance health care and provide water and electricity to our citizens at current rates... We are certainly not going to make structural adjustments such as retrenchment, removal of subsidies and devaluation at this time, certainly not."

Also the Minister : "We are thus focusing on our medium-term fiscal responsibility approach to target the emergence of a primary fiscal balance in 2022 and a reduction in the fiscal deficit from 5.5% of GDP in 2021 to 2% of GDP in 2023."

It is indisputable that the T&T economy is facing chronic structural problems which the pandemic exacerbated on the one hand, but also 'excuses' on the other. The fact that we have hemorrhaged USD10 billion in 5 years in Errors and Omissions that we can't account for, the fact that the Government is unable or unwilling to honour TTD3 billion in VAT arrears such that the private sector is involuntarily financing the Government at 0% interest, the fact that our organic level of reserves is a mere USD2.85 billion or roughly three months of import cover, and the fact that the Minister missed the opportunity (when coming to the House to request additional funds and to announce additional borrowing, no less) to disclose his Government's plans to address these fundamental challenges, is extremely disturbing. Furthermore, the fact that the Opposition has consistently failed to raise these issues, suggest solutions, and/or insist on an action plan to address them, and instead resorts to making grossly misleading and irresponsible statements, points to a hopeless situation indeed.