

## Ewart S Williams: Opportunities available for business growth in Trinidad and Tobago

Address by Mr Ewart S Williams, Governor of the Central Bank of Trinidad and Tobago, at the Employers' Consultative Association Conference, Port-of-Spain, 21 January 2010.

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I would like to commend the Employers' Consultative Association (ECA) for staging this conference that brings together the employer community to exchange ideas on how best they could build and sustain their competitiveness in today's highly volatile environment. This discussion is most timely since the economy is now at an important inflexion point, at which we need to devise new strategies to maintain our growth momentum and living standards, over the medium term.

It is worth noting that we are essentially a private sector economy and that **real economic growth on a sustainable basis could only be generated by the private sector**. I would go further to add that while the energy sector has brought us to where we are, given its future prospects, **it is going to be the non-energy private sector**, to take us the rest of the journey.

The private sector now faces several challenges but a whole host of opportunities.

As you know, the economy registered very rapid growth in the period 2001–2007, when real GDP increased at an annual rate of 7.6 per cent. While growth in the period was driven by the expansion of the energy sector, reflecting in the main, the establishment of liquid gas and other petro-chemical facilities, the non-energy sector also expanded briskly – at a rate of 5.4 per cent per year.

What was interesting though was that the major growth drivers in the non-energy sector were construction, banking and real estate, and distribution (wholesale and retail). Manufacturing did reasonably well but on the basis of domestic demand, with the data **suggesting that there was a leveling-off of non-energy exports**.

I should note, ladies and gentlemen, that the behaviour of the economy in this period of surging oil and gas prices was not atypical for a resource-based economy and in fact, it was consistent with a thesis called "Dutch disease". In line with this "thesis", the buoyant energy sector spawned a boom in government revenues and expenditures, high inflation and wage increases, a loss of competitiveness of the non-energy export sector and increased investment in non-tradable, such as, real estate and retail establishments (stores, and restaurants and so on).

With this pattern of development **there was only limited diversification of the non-energy sector**. In principle, this scenario could continue for a while, once the oil and gas industries continue to provide increasing amounts of foreign exchange to finance increasing imports of food, for the construction sector (which is heavily import-intensive) and for the retail industries.

Since mid-2008 our economy has gone into a downturn similar to that of so many developed and developing economies all over the world. The indicators suggest that there has been a reduction in private consumption as well as in business investment. Activity is now being sustained, even more than previously, by government expenditures. Clearly, this is not sustainable. While some of the current stagnation may be cyclical, there is no doubt that something fundamental has changed. Going forward, it's more than likely that fiscal policy will need to be more constrained to avoid an unacceptable public debt burden; and that the private sector will need to assume a greater role in driving the economy.

It is my view, ladies and gentlemen, that the uncertainties that surround our energy sector (including the maturing oil fields and the pressures to reduce global energy demand), combined with the impact of the international economic crisis, which has not yet fully run its course, make it very clear that we will have to find alternative growth sources to complement the energy sector, if we are to attain medium-term economic sustainability.

All private sector business activities (including small and micro business activity) benefit the economy in some way. They meet specific consumer needs and they provide employment and income. For medium-term sustainability, however, we need a diversification strategy that focuses on sectors that exploit our comparative advantage and which are efficient and globally competitive. For sustainability, we need to develop more of those activities that generate foreign exchange or that save on foreign exchange.

Against this background, our economy faces both immediate and longer-term challenges.

**The immediate challenge** is to spur a recovery in economic activity after a prolonged downturn. This afternoon the Central Bank will announce data for 2009, which suggest that real growth declined in the third quarter of 2009, making it the fourth consecutive quarter of GDP decline. The indicators suggest that private sector construction remains depressed; that private sector investment in the non-energy sector is at a low point and that the manufacturing sector is operating with significant spare capacity.

The stagnation in economic activity is reflected, in a tangible way in the absolute decline in bank credit outstanding. After increasing by 13.7 per cent year on-year in 2008, bank credit outstanding declined by 4 per cent in the year to November 2009. This is a significant reversal. The absence of credit demand is being reflected in record levels of excess liquidity and historically low savings rates.

Notwithstanding Government's expansionary fiscal stance, to facilitate an economic rebound in 2010, **there must be some resurgence in business activity**. And, this is not as far fetched as some would like to believe **as many of the pre-conditions for such a rebound already exist**. Let me cite a few:

- **Inflation** has come down sharply, to the lowest level in decades. This, together with the slack in labor markets, should result in **an easing of wage pressures**, which should help business recovery.
- **Oil and gas prices** have stabilized at higher prices than we expected a year ago. Oil prices, which were targeted **in the budget** at US\$55 per barrel are now hovering between US\$75–US\$80 per barrel. Gas prices, which were targeted in the budget at US\$2.75 per mmbtu are now in the region of \$5.00–\$6.00 per mmbtu.

These higher prices are important for several reasons.

- **First**, the record shows that strong oil and gas prices serve to bolster consumer and business confidence.
- **Second**, these higher prices should strengthen fiscal performance, compared with budget, reducing the projected budget deficit, thus supporting subdued inflation, low interest rates and a strong foreign reserve position. All these factors are conducive to an economic rebound.
- Banks' lending rates are the lowest they have been in years and banks have an abundance of funds for credit expansion. And with interest rates likely to remain low for some time, private construction and other projects, which were postponed for the last year, could now be taken up.
- Indications are that recovery in regional markets that rely on tourism and workers' remittances will lag behind that of Trinidad and Tobago. For a while, therefore, business activity will need to rely **even more than before**, on the domestic market.

However, the replenishment of inventories, after a year of de-stocking, should also provide for an increase in domestic demand.

But the immediate urgency of an economic rebound in 2010, ***should not blind us to the overriding longer term goal, which is the achievement of self-sustaining growth to maintain our living standards.*** To achieve this, a meaningful ***economic diversification*** should be our overwhelming policy objective.

As indicated in the Government's Vision 2020 strategy, diversification should be pursued through the creation of new businesses producing high-end goods and services that are globally competitive. This strategy imposes responsibilities on the state as well as on the private sector.

I am certain that over the past few years, both the state and the private sector have taken important steps towards setting the basis for economic diversification. However, as I saw somewhere, ***"an international crisis is a terrible thing to waste"***, the implication being that ***we should convert our current mis-fortunes into an opportunity to finally diversify the economy***, while some energy sector revenues are still forthcoming.

What are the primary obligations of the state in respect of economic diversification?

At the macro-economic level, Government's role is the provision of the public goods and services that are essential to the growth process. Thus, the focus should be on the improvement of our economic infrastructure – specifically roads, water, electricity, ports and so on. Government has indeed announced sizable investment programmes in these areas, starting this fiscal year. Government has also been paying great emphasis on education and training. ***Hopefully this emphasis would serve to create a culture that institutionalizes continuous learning*** and a "can do" attitude which is critical for an environment conducive to innovation.

The Government also has responsibility for maintaining an enabling environment. While there are several elements under this heading (including macro-economic stability), ***"business facilitation"*** is one that requires particular attention.

Based on data from the World Bank's study ***Doing Business 2010***, compared with other countries in Latin America and the Caribbean, Trinidad and Tobago fares rather poorly as regards ***the time required to set up a business*** (to get the necessary approvals and permits etc.), and as ***regards enforcing contracts***. Many of our competitors have overhauled business registration procedures with the use of online systems, for example. Many of our competitors have established efficient "one-stop" shops to reduce cumbersome bureaucracy. The greater use of the electronic payments methods, updated bankruptcy laws and more efficient property registration procedures would also help certainly reduce the cost of doing business.

The Government has made efforts at trade facilitation – specifically through the conclusion of several free trade agreements and double taxation treaties. However, from the data available, the expansion of trade under these agreements has been limited to date.

As for the private sector responsibilities, you business people know that creating and sustaining viable competitive industries, require an intensified focus on productivity enhancement. ***Increasing productivity has become even more important*** as China, India and other emerging market countries increase their presence in the world economy.

Our businesses need to make more efficient use of labor and capital through continuous job training, greater use of modern IT and ICT technology and ongoing innovation. And under innovation, I include more efficient processes and new products, as well as the development of new technology.

It is my view, ladies and gentlemen, that our current economic challenges present us with a golden opportunity ***for advancing an agenda of social partnerships*** among the Government, business and labour. The conventional approach to business development

requires that entrepreneurs read price and market signals, and invest in response to these signals.

More and more emerging market countries are supplementing this market model with **an industrial policy strategy** that involves close collaboration between government and business in selected industries, with the Government helping in research and development, training, market development and even joint in venture financing. In many cases, Government's assistance is time-bound to the early stages of business development **when the risks are greatest**. Many countries also stipulate that once these businesses are up and running they should be available for public participation.

There are many other initiatives that would certainly facilitate the needed diversification effort. I am referring, for example, to the broadening of the capital market to provide more risk capital; expanded financing arrangements, including venture capital for small business financing and greater exploitation of the advantages we possess for outsourcing (including through the International Financial Centre).

Many business sector leaders argue that **fiscal incentives** are the key to business expansion. I am not totally against fiscal incentives but I wonder whether their impact is not exaggerated. Many available fiscal incentives are not fully utilized and even those that are, have not provided the necessary impetus for business expansion and development.

I believe that there is a case for **targeted fiscal incentives** that are tied to **employment creation, new markets**, training, and research and development. I believe also that, in the final analysis, what will spur the diversification of the economy is a **tax system** with low rates that is simple, equitable and efficient.

I would like to end by reiterating that our medium term economic fortunes are in your hands. The country depends on you, as private sector entrepreneurs, to take risks and to innovate; to be more aggressive in seeking out investment opportunities; and to plan for the long-term. You must rise to this challenge if the business sector is to expand and if the economy is to enjoy sustained growth. I am confident that you have the capacity to do this because you have so demonstrated in the past.

I wish you a very productive and rewarding two-day conference.

Thank you.