BOARD OF GOVERNORS
OF THE
FEDERAL RESERVE SYSTEM
WASHINGTON, D.C. 20551

May 20, 1974

CONFIDENTIAL (FR)

TO: Federal Open Market Committee

FROM: Arthur L. Broida

Enclosed for your information is a copy of a report by Governor Brimmer entitled "Visit to Trinidad and Tobago April 26-28, 1974."

BOARD OF GOVERNORS
OF THE
FEDERAL RESERVE SYSTEM

Office Correspondence

Date May 17, 1974

To Board of Governors

From Andrew F. Brimmer AFB

Subject: Visit to Trinidad and Tobago April 26-28, 1974.

On April 26-28, I visited Trinidad and Tobago, accompanied by Mr. Yves Maroni, of the Board staff.[1/] I called on the Central Bank, the Ministry of Finance and the local offices of Chase Manhattan Bank and First National City Bank--the two U.S. banks operating in the country. I also met with the managers of all of the banks in a group session at the Central Bank. At the end of my visit, I was invited by the Governor General of Trinidad and Tobago, Sir Ellis Clarke, a former Ambassador to the United States, to call at his residence where we had a long private conversation. I had also a private luncheon at the home of the Deputy Governor of the Central Bank, Mr. Leonard Williams, who was acting Governor in the absence of Governor Victor Bruce.[2/]

I was warmly received and I believe that my visit did much to strengthen the relations between the Federal Reserve System and the financial community of Trinidad and Tobago. I had been scheduled to make this visit a year ago, but had to cancel it at the last moment because of pressing business in Washington. By rescheduling the visit, I was able to show genuine interest in the country and its problems and to erase any bad feeling which might have been left by my earlier last minute cancellation.

1/ This report is largely based on his notes.
2/ Governor Bruce was out of the country during my visit.

Throughout the visit, I maintained close contacts with the U.S. Embassy and received strong support from Ambassador Lloyd I. Miller and his staff. The Economic officer of the Embassy, Mr. James C. Todd was especially helpful in arranging the schedule of appointments in cooperation with the Central Bank and in handling administrative details. At the start of the visit, I received a useful briefing from Ambassador Miller, Mr. Robert G. Rich, Deputy Chief of Mission, and Mr. Todd. Ambassador Miller accompanied me on my calls at the Central Bank and at the Ministry of Finance and later hosted a reception in my honor at his residence, at which I had a chance to meet a number of American businessmen operating in the country, in particular the representatives of oil companies with refining and offshore drilling facilities.

My conversations covered a wide variety of financial and economic subjects. They are summarized below under topical headings.

The "localization" of foreign banks

In 1967, the Prime Minister of Trinidad and Tobago laid down the policy that foreign banks must transform themselves into local banks within five years. This was understood to require local incorporation with--eventually--at least 51 per cent of the capital locally owned. Since then, Barclays Bank, the Royal Bank of Canada and the Bank of Nova Scotia have become locally incorporated and have begun to issue shares on the local market, and the Canadian Imperial Bank of Commerce is scheduled to follow their lead this year.

First National City Bank of New York has asked to be allowed to continue operating as a branch of the New York entity. In return, it has offered to bring in more capital to conduct its local banking activities than would be required from a locally incorporated institution, and to incorporate locally separate companies to conduct its congeneric activities, including a finance company, a leasing company, and a data processing company. These companies would be joint ventures with local capital and they would be in compliance with the localization policy. This proposal is still under consideration by the Trinidad and Tobago authorities. Chase Manhattan Bank, following the Citibank lead, has submitted an essentially similar proposal.

When I called on him, the Minister of Finance, Mr. G.M. Chambers, expressed satisfaction with the progress made so far in implementing the localization policy. But he did not specifically refer to the proposals made by the American banks. Mr. Williams, Deputy Governor of the Central Bank, told me that the authorities faced a difficult decision in this case. If the American banks' proposal is accepted, this is likely to be coupled with the establishment of special restrictions on their lending to place them on a basis comparable to that in effect for other banks. This is because applicable regulations relate the level of lending to the amount of a bank's capital--a relatively small amount for the banks which have complied with the localization policy, but a much larger one (the capital of the head office, to be precise) for those which continue to operate as branches of a worldwide concern. Last January, the Minister of Finance asked Parliament to amend the law to require the banks operating as branches of foreign banks to hold "ascribed capital" equal to not less than 5 per cent of their deposit liabilities, such "capital" to be brought in from abroad and to be invested in securities approved by the Central Bank.

The managers of both U.S. banks made it clear that the authorities would not permit the opening of any additional bank offices by foreign banks. Chase Manhattan was allowed to move one of its bank offices from its old location at the Hilton Hotel to the new Holiday Inn, but the Canadian Imperial Bank of Commerce was denied permission to open a bank office in the lobby of a new office building the construction of which it had financed. The site was awarded instead to the Government owned National Commercial Bank.

Competition Among Banks

Barclays Bank has been in the country the longest, has the largest number of banking offices, and the largest amount of deposits--about $200 million. The two American banks are relative newcomers and have been far more aggressive than the older established institutions. Mr. Ian Dasent, Manager of the Citibank branch, claimed that Barclays Bank earned only $1.5 million last year with its $200 million in deposits, but that he was able to earn $7 million on deposits of only $60 million.

He gave credit to the Bank of Nova Scotia for opening up the field of consumer credit which the two other Canadian banks and Barclays had ignored until then. He said that Barclays paid 2-1/2 per cent on savings deposits and refused to pay more because of the large volume of deposits on which a higher rate would apply. He noted that Barclays had an advantage in that it had offices in many areas where there was no other bank. With its low rate on savings deposits, Barclays was able to hold its lending rate down and thus put a squeeze on the other banks which had to pay increasingly higher rates last year to attract funds. Competition raised the rate paid by banks for new funds to levels which left little margin for profit. In the end, there was a gentlemen's agreement among the banks to pay no more than 9-1/2 per cent for funds.*

The Financial Situation

The growth of consumer credit was accompanied by a rapid rise in imports in 1972 and 1973. At the same time, there was a shift in the pattern of financing, as the local importers who, for many years, financed themselves in the United Kingdom, switched to local financing when interest rates in that country rose in the second half of 1972 and in 1973. The domestic credit expansion greatly reduced the excess reserves which the banks had long been accustomed to maintain, and put pressure on local interest rates. International reserves declined under the dual impact of rapidly rising imports and a reduced use of foreign financing for imports. Domestic prices also rose more rapidly.

Early in 1973, the Central Bank raised reserve requirements and introduced restrictions on consumer credit. But it was not until the Government raised relatively large loans abroad in the second half of 1973 that the

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* I was told informally that the idea of a ceiling originated with the Central Bank.

decline in reserves was halted. The rise in petroleum prices has since occurred, strengthening the external position of the country, which has a net export surplus in petroleum. Domestic prices, for their part, surged ahead more sharply, partly in response to worldwide price trends, especially as regards foodstuffs. Consumer prices, in particular, rose 23 per cent in 1973.

In many of my conversations, reference was made to the intensifying wage demands which organized labor has been putting forward. Recent contracts have been providing wage increases of 25-40 per cent over a three-year period. A special labor problem is emerging in the form of a drive to unionize bank workers. The recent inflationary upsurge has given the organizers of the bank unionization movement a strong argument to make headway among bank employees.

I wondered why the Trinidad and Tobago dollar remained tied to the pound when the greater part of the country's trade is with the United States. One answer I received was that the currency was overvalued and that the sterling link enabled it to float down against the dollar when sterling floated after June 1972. Another answer was that trade with the other communwealth Caribbean countries was growing and that these countries, with the exception of Jamaica, were also tied to sterling. Still another answer was that the sterling tie served the country well in veiw of the arrangements with the U.K. Treasury and the Bank of England, which provides some type of exchange rate guarantee.

International Financial Issues

During my call on the Minister of Finance, the Permanent Secretary of the Ministry, Mr. Frank Rampersad, expressed concern over the outcome of the C-20 discussions. He worried that the result might be the resurgence of the influence of the Group of Ten and the shelving of the proposals to improve the transfer of real resources to the developing countries, including the SDR-aid link proposal.

He also stated that the present system of floating exchange rates was disadvantageous to the developing countries for a number of reasons. One disadvantage was that the system was forcing importers to assume additional costs which intensified inflation. This apparently was a reference not only to the cost of hedging but also to the higher local currency cost of imports denominated in a currency against which the local currency is depreciating. Another disadvantage which Mr. Rampersad cited was that floating rates were accompanied by shortages which did not seem to be explainable by market conditions, but which appeared to occur because importers attempted to time their purchasing so as to benefit from the most favorable exchange rate possible.

Mr. Rampersad also expressed concern over the prospects for new activations of SDRs in a world in which the need for fresh additions to liquidity is diminished because balance of payments equilibrium can be achieved though floating. He agreed that a fixed rate system was a thing of the past, but he wondered whether appropriate guidelines for floating could be agreed upon.

Trinidad and Tobago will have a substantial increase in foreign exchange earnings as a result of the increase in petroleum prices. The Government has recently adopted the tax reference price system to calculate the taxes owed by the petroleum companies. The tax rate for petroleum companies has also been raised from 45 to 47.5 per cent and a throughput tax on refinery operations has been instituted. A number of oil wells, which were uneconomic at the lower price, have been reactivated. While the additional foreign exchange earnings will, in large part, be used to pay for imports--thereby eliminating the deficits of recent years--they are likely to allow also a substantial accumulation of reserves.

I gained the impression that, after the reserves have been rebuilt from what is now a rather low level, the authorities would make some contribution to alleviate the plight of the neighboring Caribbean countries which are entirely dependent on imports for their oil supplies. Indeed, after I left Trinidad, the representative of Trinidad and Tobago at the annual meeting of the Caribbean Development Bank announced that his country intended to set up a special trust fund within the Bank to help the poorer members of the Bank meet the local currency requirements which they must assume under Bank loans, and to assist them in overcoming the balance of payments difficulties stemming from the oil crisis. The amount to be provided was not specified, but was described as "substantial."

Development Policy

I sensed that there is no great interest in developing tourism in the country. The plane on which I traveled to Trinidad landed in Barbados--where most of the passengers got off. Only seven persons continued on to Trinidad, barely 40 minutes away. While we were on the ground in Barbados, several other planes arrived loaded with tourists--including a Boeing 747. By contrast, the airport at Port of Spain, Trinidad, was rather quiet.

This impression was confirmed when I visited the island of Tobago (on a Saturday) and saw some fine beaches and a number of tourist hotels, but few tourists. Further confirmation came in several of my conversations, which made it clear that investments to develop the infrastructure needed to stimulate the growth of a tourist industry were not being especially encouraged. Indeed, tourist income is thought to be rather an unreliable source of income, and the cancellations of airline flights because of the energy crisis were cited as evidence of this.

Not surprisingly, development interest centers around the country's offshore oil and natural gas resources. A few years ago, a plan was drawn up to liquefy the natural gas and to ship it to the United States where it was to be fed (after regassification) into the system supplying the City of Chicago. But this plan has now been shelved. Official policy is to use the gas locally and to develop a petrochemical industry. As a first step, the Government will construct a pipeline to bring the natural gas across Trinidad to a point on the west coast of the island where an industrial area is to be established. I heard some discussion as to whether this site was the best, but at any rate the Government has already reached agreement with W.R. Grace and Co. to establish a joint venture to build a liquid ammonia plant there.

Trinidad and Tobago welcomes additional foreign private investment, but is increasingly insisting on local participation in major projects. This does not necessarily mean that majority ownership must be in local hands, but where it does not, there is often a requirement that the foreign owners sell a controlling interest to local investors within a set period of time. Because there is not much locally owned private capital, the local investor frequently ends up being the Government.

As other petroleum producing countries, Trinidad and Tobago is attempting to increase its control over this natural resource. Bids were recently requested for oil concessions on the condition that the Government would retain a 35 per cent interest, and that this share would rise to 51 per cent, should petroleum production reach specified levels. The Government is also negotiating with the oil companies operating in the country to obtain a participation in their existing operations.

Concluding Comments

This visit gave me an opportunity not only to renew and broaden contacts with the financial community of another country but also to learn more about its problems, concerns, and attitudes, and their implications for American banks and businesses operating there. It was also useful in that I found much interest in hearing about conditions in the United States, and genuine appreciation for my responses to the frequent questions asked of me on this subject.

There is much to be said for undertaking visits of this kind to a larger number of countries, both large and small. The greater understanding which comes from personal contacts and the goodwill built up by showing interest in another country can be invaluable assets in a world in which interdependence is growing and the economic and financial problems requiring solution are becoming increasingly complex.

I hope that, as opportunities to travel abroad arise in the future, we will continue to take advantage of them, as we have in the past, to visit other countries so as to become better acquainted with their financial leaders and better informed about their points of view and about matters of interest to them.