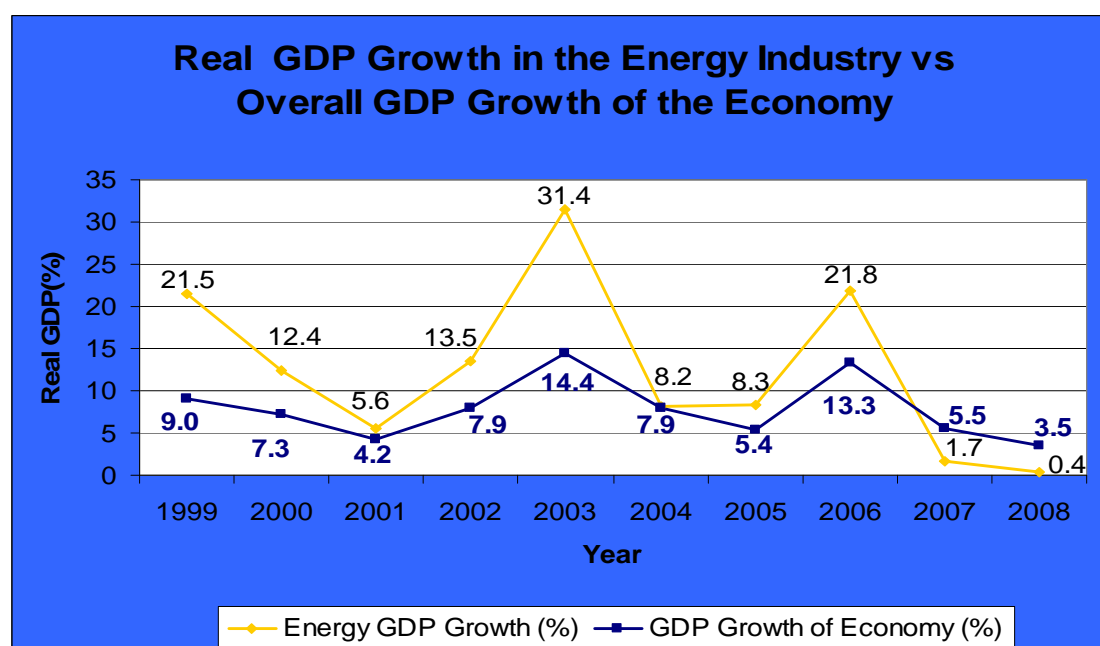


The Anatomy of a Recession

“A recession is when your neighbour loses his job. A depression is when you lose yours and recovery is when Jimmy Carter loses his.” Ronald Reagan during the 1980 US presidential campaign.

Declaring the start of a recession, even defining a recession, in the context of a small open economy that is subject to significant output and price volatility is probably more of an art than a science. It is noteworthy that in 2005, 2006 and 2007 there were isolated quarters of negative growth even though these were years of overall positive economic growth. What is critical in the context of the economic performance of Trinidad and Tobago is the performance of the energy sector and by extension, the expenditure profile of the Central Government. Fiscal policy has a strong signalling effect and bolsters consumer confidence through job creation and increased incomes. In short, when the Government spends, jobs are created, the consumer is confident and will increase spending and then the domestic private sector expands but the reverse is also painfully true. The beginning of the dismal economic performance that we now endure is rooted in the declining performance of the energy sector and was later exacerbated by declining non-energy exports. Therefore, the genesis of this downward spiral into lower economic growth and rising unemployment can be located at the end of 2007 when the growth of the energy sector fell well below its 10 year average, a new reality which continued into 2008.



Once these conditions of low growth in the energy sector persisted throughout 2007 and 2008, there was the increased likelihood of the eventual contraction of the local economy, all other things being equal. Does this mean that the recessionary conditions began at the end of 2007 in Trinidad and Tobago and therefore corrective policy action should have commenced in earnest since then? Awaiting the delayed publication of CSO GDP data or Central Bank GDP estimates before recognising and acting on the fundamentally changed condition of the broad economy creates a flawed environment for decision making.

Fast forward to 2009 and the Central Bank has declared that the local economy has contracted over the course of two consecutive quarters, the 4th quarter of 2008 (-1.1%) and the 1st quarter of 2009 (-3.3%). It is noteworthy that the degree of contraction increased from the 4th quarter of 2008 to the 1st quarter of 2009 and the expectation is that further contraction would have occurred in the 2nd quarter of 2009 as consumer and investor confidence waned and government spending remained restricted by insufficient revenues, all of which was exacerbated by the debacle of CL Financial, a holder of significant assets in the energy sector.

Consumer and investor confidence are eroded long before the recession is officially declared, since the effects of a slowing economy are experienced by a significant cross section of the economy and the negative sentiments of the environment become embedded. A popular definition of a recession, two consecutive quarters of real GDP contraction, specifies a particular period of economic contraction before a recession can be declared. Another well used definition is, a general slowdown in real economic activity over a prolonged period of time. This second definition, which is non-specific with respect to the timeframe of the slowdown, recognises that recessionary conditions can be present even though the economy is still experiencing positive but declining growth. In essence, there can be subdued growth in key sectors of the economy, even though other less significant sectors continue to enjoy robust growth rates. In the case of Trinidad & Tobago the energy sector is not a significant employer, therefore lower growth in this sector would not have exacerbated the unemployment situation. Hence, the economy was drifting into a period of economic contraction but unemployment was still falling !

In the context of the contemporary structure of the local economy, significantly lower real economic growth commencing in 2007 and continuing into 2008 was the first sign that the robust growth environment was cooling with little prospect of a “soft landing”. Ours was not an economy that was gradually returning to a long-term growth trend but was instead descending into a period of contraction. That would have been the opportune time for the policy makers to recognize the shift in the future growth prospects of the economy.

The definition of a recession as two consecutive quarters of negative real growth or real economic contraction inadequately fits our contemporary circumstances. A period of slowdown in *key sectors of the economy* as a modified definition of a recession would have served as a better trigger to inform decision making. The implication of such a modified definition is that Trinidad & Tobago would have recognized the emerging recessionary environment at the beginning of 2008 as opposed to 2009 !

This means that the country’s focus would have been on the real output growth of the key energy sector and less confidence would have been placed in the historically high global prices for oil and natural gas in mid 2008. Then, the fiscal budget for 2008/09 would have had a more realistic revenue estimate from the inception. It also implies that there would have been even less consumer tolerance of the rising inflation rate in anticipation of the rising unemployment that was soon to follow.

We must define our environment in a way that works for us, otherwise we continually run the risk of missing the key signals and operating “behind the curve”.