

THE FINANCIAL SECTOR IN THE CARIBBEAN: CONTEMPORARY ISSUES

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SCOPE OF DISCUSSION

- To concentrate on the contemporary issues in:
- Banking
- Insurance
- Securities market
- Credit unions
- SME Financing Institutions and Venture Capital Financing

FINANCIAL STRUCTURE

- Trinidad and Tobago has a diversified financial structure which accounts for 9.5% of GDP.
- But Commercial Banks dominate the financial system, accounting for more than half the total assets of the financial system. Moreover, two commercial banks accounted for 52.5% of the total deposits in 2008.
- There has been a blurring of the boundaries between institutions (the concept of plain vanilla no longer exist)
- Large conglomerates became prominent
- Financial Institutions from Trinidad now operate in CARICOM Markets and Central America offering new and innovative investment products.

Table 1: Number of Existing Financial Institutions, 2001-2008

	2001	2002	2003	2004	2005	2006	2007	2008
Commercial Banks	6	6	6	6	6	6	6	6
Finance Companies and Merchant Banks	9	10	10	12	12	11	10	10
Trust and Mortgage Finance Co's	5	5	5	6	6	7	7	7
Dev't Banks	1	1	1	1	1	1	1	1
Credit Unions	122	122	125	126	129	129	131	130
Insurance Companies	57	56	51	51	51	51	51	51
Thrift Institutions	3	3	3	3	3	3	3	3
NIB	1	1	1	1	1	1	1	1
Stock Exchange	1	1	1	1	1	1	1	1
Unit Trust Corporation	1	1	1	1	1	1	1	1
Home Mortgage Bank	1	1	1	1	1	1	1	1
Private Pension Funds	212	215	248	256	256	256	256	256

THE COMMERCIAL BANKING SECTOR

- During the period 2000-2008, bank deposits increased annually by 23% on average, consistent with the strong growth in the economy witnessed during the period. In fact, most of the banking indicators (soundness indicators) showed marked improvements
- Capital adequacy ratios grew in excess of 18%, well above the 8% minimum regulatory requirement; non-performing loans remained low, around 1% in 2008; and profitability ratios have been high by international standards
- Systemic excess liquidity
- There is the concern for quite some that banks have consistently funded two popular sectors- Consumers and Distribution. There has always been the question as to “banks relevance “ in financing the development and expansion of top contributors to GDP
- There has been limited bank credit expansion to Agriculture or SMEs

COMMERCIAL BANKS

- Bank Spreads are consistently high. But Ramkissoon (May 2009) argues that spreads are high because investment and lending is risky business. He further argues that the rates are determined by the risk free rate which is usually comparative. In any case, high reserve requirements represent costs which are reflected in deposit rates.

INSURANCE

- During the last decade, insurance company business such as life insurance and general insurance blossomed on account of strong growth in the economy which encouraged the growth of product lines such as mortgage insurance and motor insurance
- Gross premiums increased by 11% in 2003 - 2008
- However, due to competition, and driven by the profit motive, the life insurance sector entered the short-term deposit products market. This created asset/liability maturity mismatch
- Life insurance investment portfolio returns have been declining since 2003 and pre-tax profits have declined on average since 2006
- Two companies exhibited an inability to meet statutory fund obligations
- Increased risks also by bank and insurance company linkages and Conglomeration- Two companies had to be bailed out by the Government
- Interestingly enough, Central bank survey last year showed that a vast number of citizens are still uninsured.

CREDIT UNIONS

- Credit Union sector now control over \$8 billion in assets of the financial sector
- Credit unions are also significant investors in financial markets
- The growth in assets and the business model of some large credit unions has led to some insolvency
- There is now a move by the Central Bank to regulate credit Unions. This has been met with tremendous protest by members in the movement

THE SECURITIES MARKET

- Maturities in the securities market has been narrow; characterized by some issues at the short and long maturities, but with few intermediate maturity instruments
- Secondary market activity remains low; Construction of yield curves difficult
- Major securities in issue in the region are bonds, equity securities, debt and credit derivatives, collective investment vehicles, stock options (ESOP)

THE SECURITIES MARKET (CON'T)

- Trinidad, Jamaica and Barbados are the main focus when it comes to raising debt and equity capital
- Collective Investment Vehicles are now the prominent vehicle for raising capital in both Trinidad and Tobago and Jamaica. In Trinidad and Tobago, funds under management in CIVs are almost the same level as bank deposits. (40% of GDP)
- In the equities market, there has been increased market capitalization, cross listings accommodation, the introduction of electronic trading and modern settlement systems has been introduced.
- Nevertheless, the market continue to offer only a limited range of products. The markets are also characterized by low liquidity and low turnover.

VENTURE CAPITAL FINANCING

- Venture Capital Financing is offered by a number of companies, such as DFL and NEDCO
- While these entities show prospect, there is much room for improvement
- SME financing through use of equity and bonds has tremendous scope
- But it needs to be carefully developed. Indeed, NEDCO and DFL must now undergo major changes to their structure and operations

Securities market Impediments

- Large no. of family-owned business, where there is little or no effective division of ownership and control
- Low level of investor education
- Inefficiencies in trading systems
- Inadequate regulation
- Interlocking directors
- Limited market making function and weak development of institutional investors to drive the market.

Strategies to Develop the Market

- Measures to boost investor preference for stocks, bonds, venture capital and other securities market instruments are needed
- Government – Fiscal Incentives
- Pension Funds and Insurance Companies need greater latitude to invest in securities
- There must be harmonization of:
 - » Listing of securities and restrictions in shareholding
 - » Trading and settlement cycle

- » Currency and settlement cycle
- » Central Clearing
- » Withholding tax
- » Certification of all market actors across cross-border
- » Regionalization of ownership
- » Takeover code
- » Dispute resolution
- » The Companies Act

- There is an urgent need to expand the range of financial products
- On the supply side, privatization of State-owned Enterprises should be actively pursued.

The International Financial Crisis:

- The International financial crisis has negatively affected the financial system
- In the banking sector, at the end of June 2009, there has been a reported decline in loans, an increase in non-performing loans and an increase in loan provisioning
- Banks have increased their prudential lending limits
- The CLICO affair seriously affected confidence in the financial sector, but the Central Bank has been able to restore some measure of confidence

Financial Crisis (Con't)

- The Financial crisis exposed structural and institutional vulnerabilities. These include:
 - Conglomerates with intra-group exposure
 - Lack of updated legislation
 - High levels of concentration in banking and insurance

ISSUES FOR THE FUTURE

- Regulation and Supervision – We take too long to pass necessary laws. By the time the laws are passed, the goal post changes.
- Do we possess the expertise to regulate the financial sector. Is there a human resource constraint
- What would be the total cost of the CLICO bailout to the country? Could it have been avoided?
- Has the banking or the insurance players considered the confidence issues ? Are the relevant Associations doing anything about it?