

Financial Stability Report 2015



CENTRAL BANK OF
TRINIDAD & TOBAGO

Safeguarding Financial Stability in the New Normal

Central Bank Conference Facilities, June 8 2016

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Presentation flow

1

- Performance and Potential Vulnerabilities in the Domestic Financial System

2

- De-risking: FATCA and AML/CFT Issues

3

- Institutional Reforms: Insurance Legislation and the National Payments System

4

- Key Messages



1

- **Performance and Potential Vulnerabilities in the Domestic Financial System**

2

- **De-risking: FATCA and AML/CFT Issues**

3

- **Institutional Reforms: Insurance Legislation and the National Payments System**

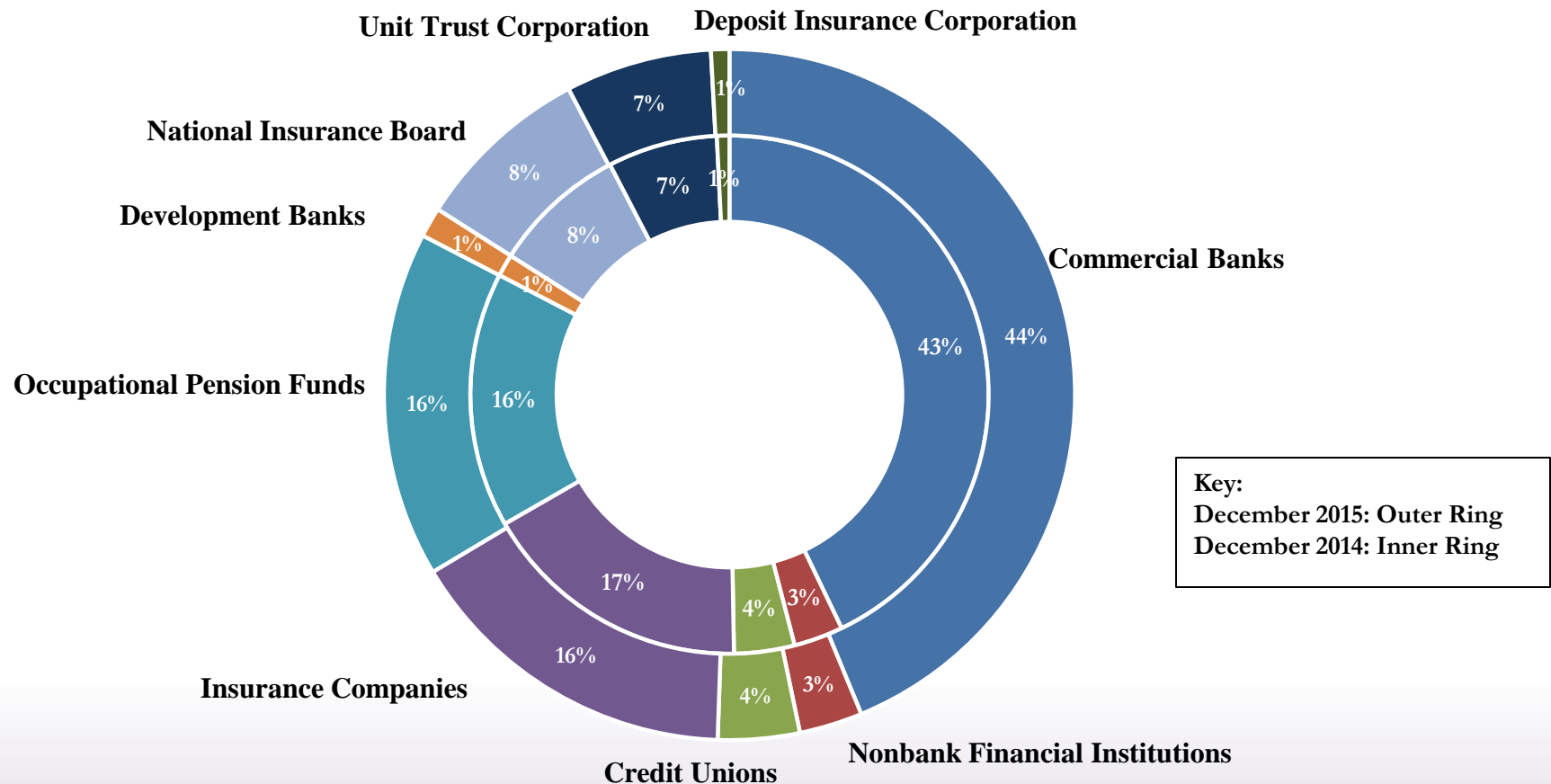
4

- **Key Messages**

1A THE DOMESTIC FINANCIAL SYSTEM

Players in the Domestic Financial Sector

Composition of Assets in the
Financial Sector, 2014 - 2015



Banking System Performance

Banking System: Financial Soundness Indicators, 2011 -2015

	Dec-11	Dec-12	Dec-13	Dec-14	Dec-15
Capital adequacy					
Regulatory capital to risk-weighted assets	26.0	25.7	25.0	24.6	24.1
Regulatory capital-to-total assets	13.5	13.3	13.3	12.5	12.6
Net Open position in foreign exchange-to-capital	10.4	10.7	13.9	6.6	9.3
Banking sector asset composition					
Sectoral distribution of loans-to-total loans					
Households	41.5	43.1	45.0	44.2	44.0
Financial sector	17.3	16.1	13.5	15.1	13.1
Oil and gas sector	2.6	2.9	2.9	2.8	2.6
Construction	10.7	9.1	8.0	9.8	9.5
Foreign currency loans-to-total loans	17.8	18.8	16.9	16.6	15.2
Banking sector asset quality					
Nonperforming loans-to-gross loans	6.2	5.5	4.3	4.4	3.7
Total provisions-to-impaired loans	36.7	49.9	49.9	53.0	54.3
Banking sector earnings and profitability					
Return on assets	2.8	3.0	2.5	2.1	2.9
Return on equity	17.5	18.3	15.8	13.5	18.1
Interest margin-to-gross income	61.0	60.6	58.9	56.3	57.6
Non-Interest income-to-gross income	39.0	39.4	41.1	43.7	42.4
Banking sector liquidity					
Liquid assets-to-total assets	26.7	24.7	26.8	25.0	23.1
Liquid assets-to-total short-term liabilities	37.3	33.1	35.7	32.5	30.6

Source: Central Bank of Trinidad and Tobago.

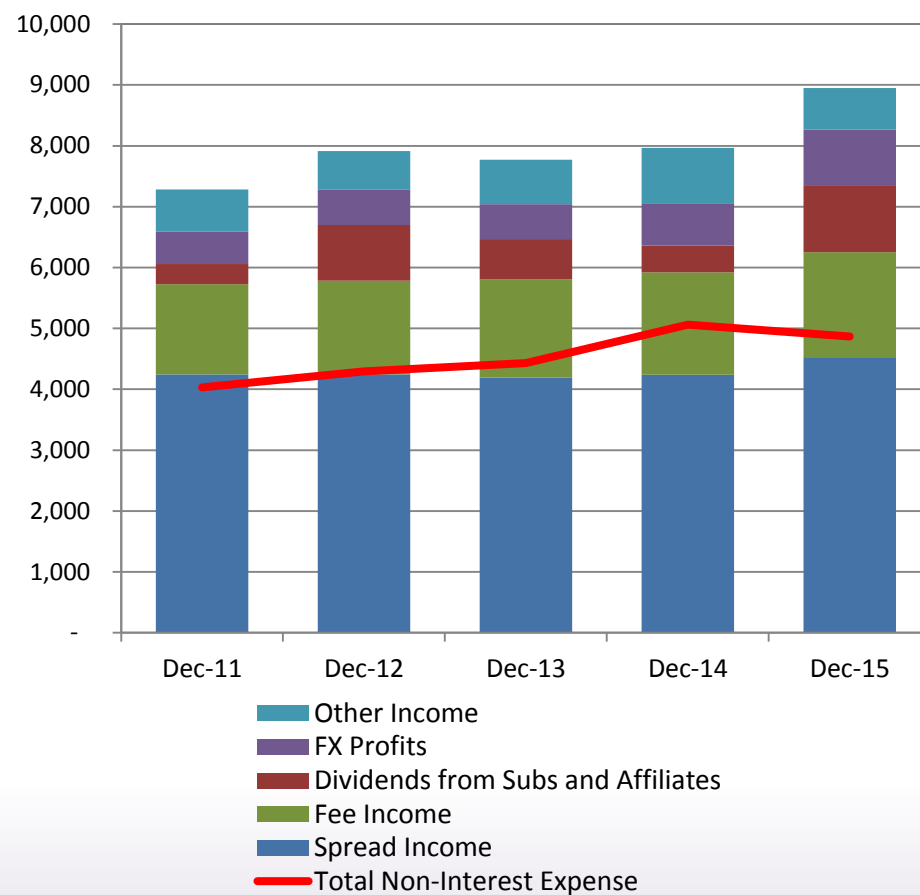
Note: The banking system refers to commercial banks and non-bank financial institutions (NFIs) collectively. All figures are weighted by assets. End of Period except for Banking Sector Earnings and Profitability.

Banking System Performance

Banking System: Non-Performing Loans to Gross Loans (per cent)



Banking System: Contribution to Profit and Expense by Source (TT\$ Millions)



Source: Central Bank of Trinidad and Tobago.

Insurance Sector Performance

Life Insurance Companies: Financial Soundness Indicators (Per cent)

	Dec-11	Dec-12	Dec-13	Dec-14	Dec-15
Capital Adequacy					
Capital to total assets	22.1	22.0	21.2	21.3	20.7
Earnings and Profitability					
Expense ratio = expense (incl. commissions) / net premium	38.6	37.8	35.1	33.6	33.1
Investment yield = Investment income to investment assets	5.7	5.4	5.1	4.8	4.5
Return on Equity (ROE) = Pre-tax profits to shareholders funds	10.3	14.1	15.1	10.6	11.2
Liquidity					
Liquid assets to current liabilities	33.5	33.6	32.6	34.2	37.7

Note: Figures exclude data from CLICO and British American Insurance Company (Trinidad) Limited.

Source: Central Bank of Trinidad and Tobago.

Non-Life Insurance Companies: Financial Soundness Indicators (Per cent)

	Dec-11	Dec-12	Dec-13	Dec-14	Dec-15
Reinsurance and Actuarial Issues					
Risk Retention Ratio = Net premiums written/total gross premiums	44.4	42.6	43.0	42.5	43.0
Earnings and Profitability					
Combined Ratio	100.2	97.1	96.4	95.7	101.0
Investment income/net premium	8.8	8.2	10.3	5.8	5.8
Return on Equity (ROE) = Pre-tax profits to shareholders funds	15.5	17.5	20.0	14.2	10.0
Return on assets (ROA)	6.4	7.6	8.9	6.4	4.7
Liquidity					
Liquid assets to current liabilities	42.9	56.5	60.5	61.2	58.8

Note: Figures exclude data from CLICO and British American Insurance Company (Trinidad) Limited.

Source: Central Bank of Trinidad and Tobago.

1B POTENTIAL VULNERABILITIES

Global Risks

Key Global Financial Stability Risks

High

Medium

Low

GLOBAL RISKS TO FINANCIAL STABILITY

Lower commodity prices.

Geopolitical tensions.

Lower growth in China.

ADVANCED ECONOMIES

EMERGING ECONOMIES

LATIN AMERICA AND THE CARIBBEAN

Low growth and deflation.

Capital flow reversals.

Widening macroeconomic imbalances.

Source: Central Bank of Trinidad and Tobago.

Domestic Risks

Summary Heat Map – Key Risks to Financial Stability in Trinidad and Tobago

Key Risks	Probability	Impact		
Risk 1: Persistent low energy prices				
Risk 2: Household Financial Stress and a Correction in House Prices				
Risk 3: A Spike in Long-Term US Interest Rates				
Risk 4: Sovereign Debt Restructuring in the Caribbean				
Low	Moderate	Elevated	High	Very High

Source: Central Bank of Trinidad and Tobago.



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2A THE DE-RISKING CHALLENGE

“De-risking”

- The practice of financial institutions exiting relationships with and closing the accounts of clients perceived to be “high risk.”

Drivers of De-Risking

- Regulatory and legal concerns
- Rising fines and penalties
- Profitability
- Reputational risk
- Perception that region is high risk for ML/TF

The De-risking Challenge

Regional Impact

- Bahamas, Jamaica, Cayman Islands & TCI – Money Service Businesses
- Barbados – IBC transactions including Wire Transfers
- Belize – commercial banking transactions
- Guyana & Haiti – Commercial banking transactions
- Eastern Caribbean – IBC transactions, local charities and MSBs

Trinidad and Tobago

- Some private members' clubs and money remitters have been impacted.



Next Steps

- Strengthen AML/CFT regimes to comply with FATF standards.
- Ensure compliance with FATCA and other international standards taxation.
- Policymakers and regional regulators to explore collaborative implementation of Know Your Customer (KYC) registries.
- High level advocacy groups in the Caribbean (CGBS, CFATF, CAIR, Global Forum) are meeting with relevant authorities to represent the region's interest.

2B ANTI MONEY LAUNDERING (AML) AND COMBATTING THE FINANCING OF TERRORISM (CFT)

What is a Mutual Evaluation?

- Assessment of a country's AML/CFT regime against Financial Action Task Force (FATF) Standards
 - Assesses technical Compliance & effectiveness
 - Involves knowing the country's risk (National Risk Assessment)

Why do we care?

- Protect the financial system from abuse
- Identify vulnerabilities
- Set national policy direction
- Could result in 'de-risking' or 'blacklisting'

Findings

- Relatively sound AML/CFT regime
- 'Enhanced Follow-up' Status
- Strengthen AML/CFT Regime in areas like:
 - Private members' clubs
 - Terrorism financing and sanctions
 - Proliferation financing
 - Beneficial ownership information
 - Convictions
 - Confiscation

AML/CFT Priorities

- National AML/CFT Committee to develop an action plan to address identified gaps in the Mutual Evaluation Report:
 - ✓ T&T to complete the National Risk Assessment
 - ✓ Amend/enact legislation to treat with:
 - Private members' clubs, terrorism financing, proliferation financing (weapons of mass destruction), credit unions, beneficial ownership, non-profit organizations, etc.
- Revise AML/CFT Guidelines to provide better sector-specific risk based guidance.
- Enhance AML/CFT related data and statistics.

2C FOREIGN ACCOUNT TAX COMPLIANCE ACT (FATCA)

What is FATCA?

- A United States (U.S.) tax law which became effective on July 1st 2014 .
- Designed and enacted to combat offshore tax evasion by U.S. persons with accounts and/or investments with both foreign financial and non- financial entities.
- Places a requirement on foreign financial institutions (FFIs) to identify and report to the U.S. Internal Revenue Service (IRS), on the accounts of its U.S. clients.
 - ✓ Foreign financial assets with an aggregate value of more than the reporting threshold (at least US\$50,000) must be reported to the IRS.

Who does FATCA Impact and How?

FATCA will impact:

- Every financial institution in Trinidad and Tobago, either directly in the conduct of their core business or indirectly through relationships with other financial institutions.
- U.S. persons holding accounts with financial institutions to declare and provide necessary information to financial institutions.

Non-compliance with FATCA:

- Financial institutions and U.S. persons will be subject to a withholding tax of 30%, applied on all U.S. sourced income (such as interest or dividends) and U.S. sourced capital gains paid to it by U.S. financial institutions.
- May carry significant implications for local financial institutions in relation to correspondent banking as well as affect Trinidad and Tobago's diplomatic relations with the U.S.

Legislating and Implementing FATCA

- Inter Governmental Agreements (IGAs) between the U.S. and other countries developed to assist in FATCA implementation.
- In Trinidad and Tobago, a Bill drafted to legislate FATCA/“Model 1” IGAs requirements and amend other relevant laws.
- Financial institutions to develop procedures to determine origin/citizenship of clients, modify and/or implement IT systems to facilitate FATCA reporting requirements and train staff.
- The Ministry of Finance will be the Competent Authority with the Board of Inland Revenue (BIR) as its agent responsible for FATCA reporting.

FATCA: Next Steps



Signing of the IGA (Ministry of Finance)

Enactment of FATCA implementing legislation

Transmission of data to the IRS by the deadline of September 30, 2016

Raise public awareness on the pending implementation of FATCA



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3A INSURANCE LEGISLATIVE REFORM

Existing Insurance Legislation

- The **Insurance Act (IA) 1980** is fundamentally unchanged from the 1966 Act and does *not*:
 - ✓ *Require* insurance companies to hold capital commensurate with their risk profile;
 - ✓ Reflect minimum, international corporate governance requirements;
 - ✓ Treat with consolidated supervision; and
 - ✓ Address the oversight of financial groups
- The **reform process began in 2001** and resulted in the formulation and laying of three Insurance Bills in Parliament in 2011, 2013 and 2015.
- Specific **amendments to the IA were enacted in 2009** to treat with sharing of information, sufficiency of assets in the Statutory Fund, access to the premises of an insurance company, and strengthening of enforcement powers of the Central Bank.

Key Provisions of the Insurance Bill, 2015

- The Insurance Bill 2015 provides for a **new regulatory framework** for insurance companies and the regulation of privately administered pension plans.
- Will significantly enhance **prudential regulation and financial soundness** of insurers by:
 - ✓ Increasing **minimum capital** requirements;
 - ✓ Introducing **risk based capital**;
 - ✓ Introducing a consistent, minimum **basis for the valuation of liabilities**;
 - ✓ Introducing a **stress testing** regime (Financial Condition Report); and
 - ✓ Introducing more prudent **limits for credit exposures** to connected parties.

Key Provisions of the Insurance Bill, 2015 (cont'd)

Enhance corporate governance by requiring:

- ✓ Mandatory **audit committees** of the Board;
- ✓ Appointment of **independent directors**;
- ✓ The board and senior management to attest to the adequacy of **internal controls**; and
- ✓ Approval of **interlocking directorships** outside of financial group.

Key Provisions of the Insurance Bill, 2015 (cont'd)

Enhance **supervision of insurance groups** by:

- ✓ Providing for supervision of insurers that are part of a conglomerate on a **consolidated basis**;
- ✓ Allowing the Central Bank to access **information from unregulated, non-financial entities** within a group;
- ✓ Instituting **cross-border supervision** of insurance subsidiaries and branches; and
- ✓ Allowing the Central Bank to require the establishment of a **Financial Holding Company (FHC)**.

Status of the Insurance Legislative Reform

1

The reform process began in 2001 prior to the transfer of regulation and supervision of the insurance industry to Central Bank in May 2004

2

Fast track amendments were made to the current legislation in February 2009

3

A Joint Select Committee (JSC) appointed by Parliament in 2013, reviewed the Bill and the Bill was revised to include several of their recommendations

4

The Bill is on the short-term legislative agenda of the Government

3B THE NATIONAL PAYMENTS SYSTEM



...the heart of the financial system....

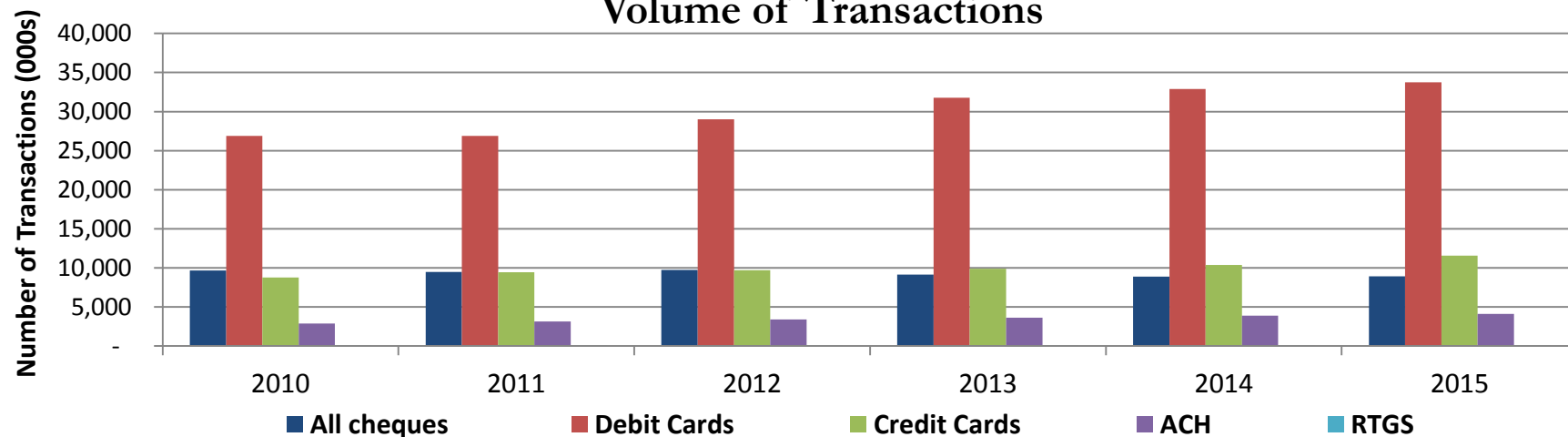
Payments System Reforms

Major Reform of Payments System: 2002 -2010

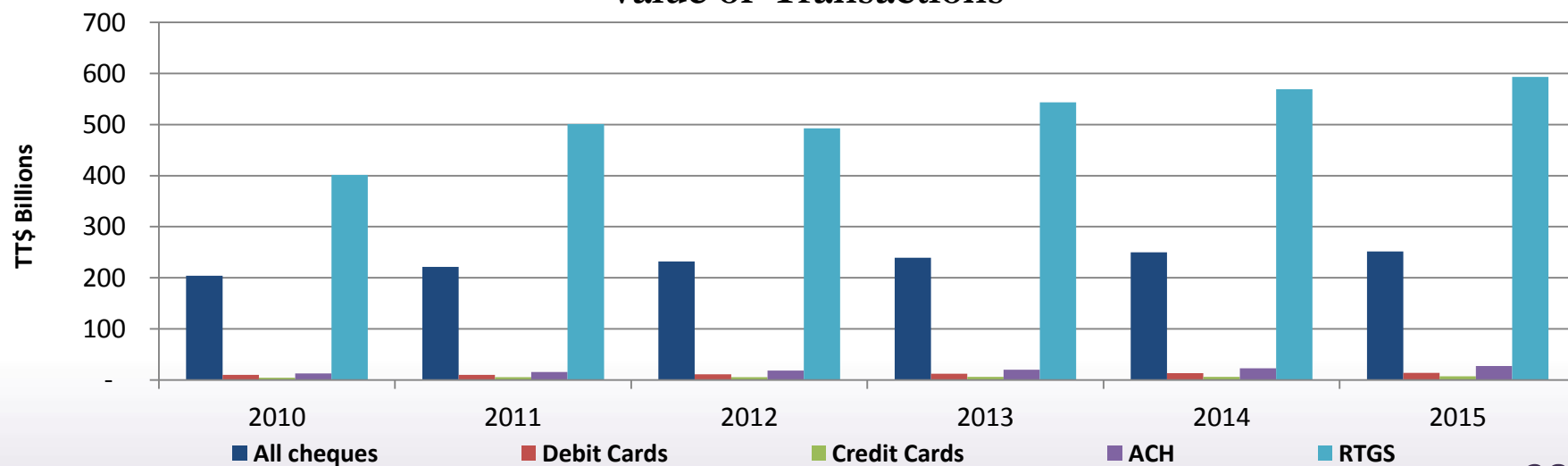
- Enhancement of the **infrastructure** with the introduction of electronic securities and payments, clearance and settlements:
 - ✓ Real Time Gross Settlement System (RTGS) – 2004;
 - ✓ Government Securities Settlement System (GSS) – 2004;
 - ✓ Automated Clearing House (ACH) – 2006.
- Strengthening of the **legislative framework** to enable supervision and oversight of the domestic payments system.
- The institutionalization of the **Payments System Oversight Function** at the Central Bank of Trinidad and Tobago.
- Establishment of a **Payment System Council** (2002).

Payments System Transactions

Volume of Transactions



Value of Transactions



Payments System in the Modern World

- **Rapid Pace of Innovation in Technology Globally**
 - ✓ Emergence of new Payments Products;
 - ✓ Novel processing methods; and
 - ✓ New players such as non-banks
- **Greater demands of new International Best Practice Standards**
 - ✓ 24 Principles for Financial Market Infrastructures (PFMIs)
- **E- Government Agenda**
 - ✓ E-payment initiatives for the public
- **Business and Consumer demands for more efficient payment services**
 - ✓ Straight through processing of electronic payments
 - ✓ Faster, reliable and transparent services
 - ✓ Effective reconciliation of transactions
 - Timely and complete data for businesses

An Example: Government's E-Payment Initiative

The Central Bank has also worked with Government to improve efficiency through the use of electronic payments.

Legislative reform

- ✓ Amendments to the Exchequer and Audit Act (approved by Parliament in 2014) and pursuant regulations (presented in 2015).

Critical work still to be done

Operationalization of Government e-payments

- ✓ Payments (salaries and vendor payments)
- ✓ Receipts (taxes and fees)



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4. KEY MESSAGES

- Overall the **financial sector in Trinidad and Tobago is sound and resilient.**
- By most metrics, financial institutions remain **well capitalized, liquid and profitable with relatively low incidence of non-performing loans.**
- Nonetheless, the **current economic environment and short-term outlook pose risks for credit quality**; care must be taken to avoid undue asset concentration.
- The high degree of inter-connectedness of financial institutions and conglomerates across the region demands **close collaboration among regional regulators.**

KEY MESSAGES (CONT'D)

- Practical steps need to be put in place to further **advance compliance with FATCA and AML/CFT standards** in the context of our global financial interactions.
- The **legislative reforms for the insurance sector** should be completed urgently.
- Concerted and coordinated efforts should be made to **bolster the security and efficiency of the payments system**, including completing steps for Government electronic transactions.



Thank you for your attention