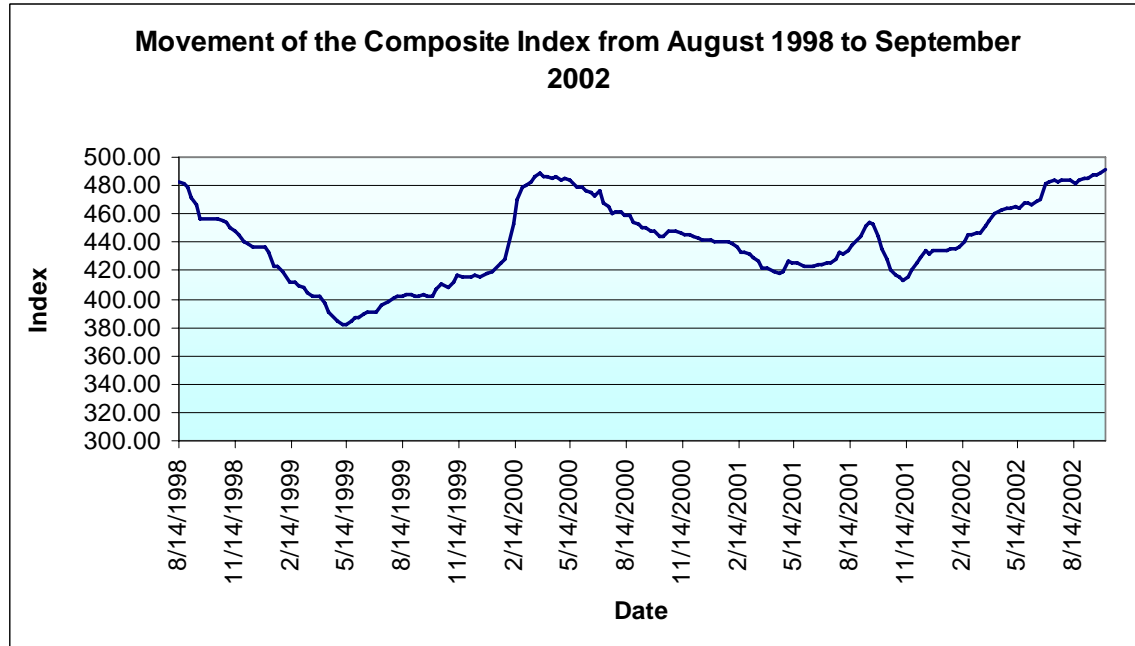


## Still a Way From Recovery

After almost a year of decline, the Stock Market made somewhat of a turnaround in the first week of May as the Indices started to move in a positive direction. The Composite Index went to as low as 914.35 on May 3 (25.79 per cent below its peak) while the All T&T Index moved to a low of 1,114.34 (29.13 per cent below its peak) on May 2. Was this a sign that the market is on its way to a full recovery? Firstly, let us look at a couple of the past market recovery periods.

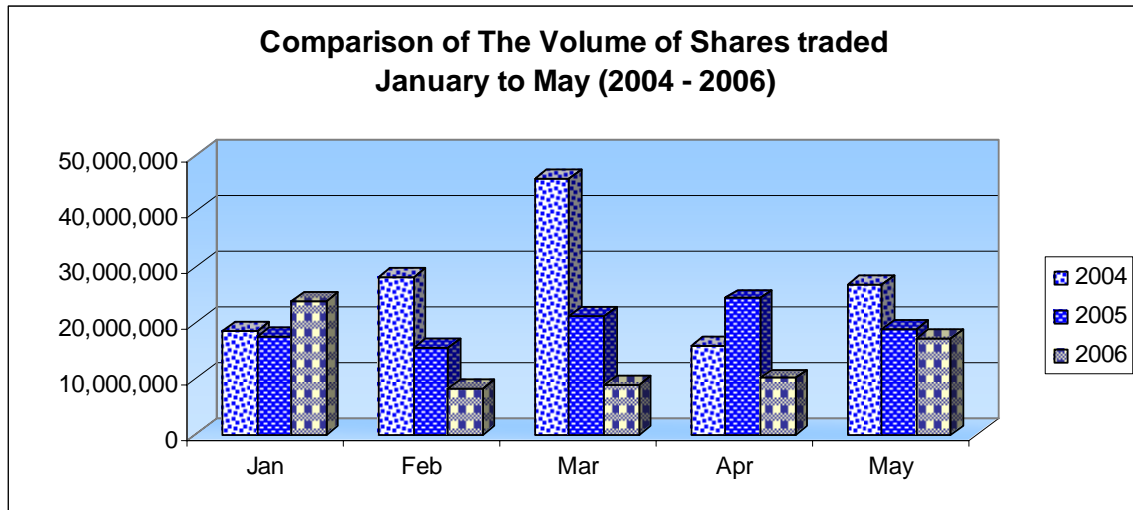
Figure 1



As Figure 1 shows, past recovery periods have averaged approximately 20 months. The last time the market declined in August 1998, it took approximately 19 months before it recovered. During that period, the market fell by 21 per cent in 9 months and then took 10 months before it fully recovered. The recovery was however short-lived as a couple of weeks later the market again began to fall again in part due to political instability. It then dropped approximately 14 per cent in 11 months before it turned around.

The advance however was soon nullified by the September 11 attacks in 2001 which sent the market sliding further down before heading back in a positive direction. The market then took approximately 10 months before it climbed to its previous high. This alone gives an indication of our market and the length of time it takes to recover. Though one would think that the buoyancy of our economy would help the market on a path to recovery, the stock market is still operating under conditions which are ailing its growth.

Figure 2



One of the main reasons is still the absence of institutional investors. As Figure 2 shows, in comparison to 2006, with the exception of January, the years 2004 and 2005 registered much better volumes of shares changing hands. In fact, in 2006 the total volume of shares traded for the January to May period was 30 per cent less than that of 2005 and 49 per cent less for the same period of 2004.

This is important because the presence of large buyers on the market foster healthy volumes which aid in sustaining or advancing the price of a share. Advances in prices and large volumes of shares traded are of course what drive the Indices into positive strides. The absence of these 'players' in the market therefore make volumes demanded comparatively weak. This in turn pressures shares that have large volumes on offer on the market thereby making growth in the Indices sluggish. In 2004, when volumes demanded were strong, the January to May period saw the Composite Index advance approximately 29 per cent while in 2005 it had advanced 13 per cent. Hence, it is evident that in a thin market the absence of strong volumes would slow the growth of the Indices.

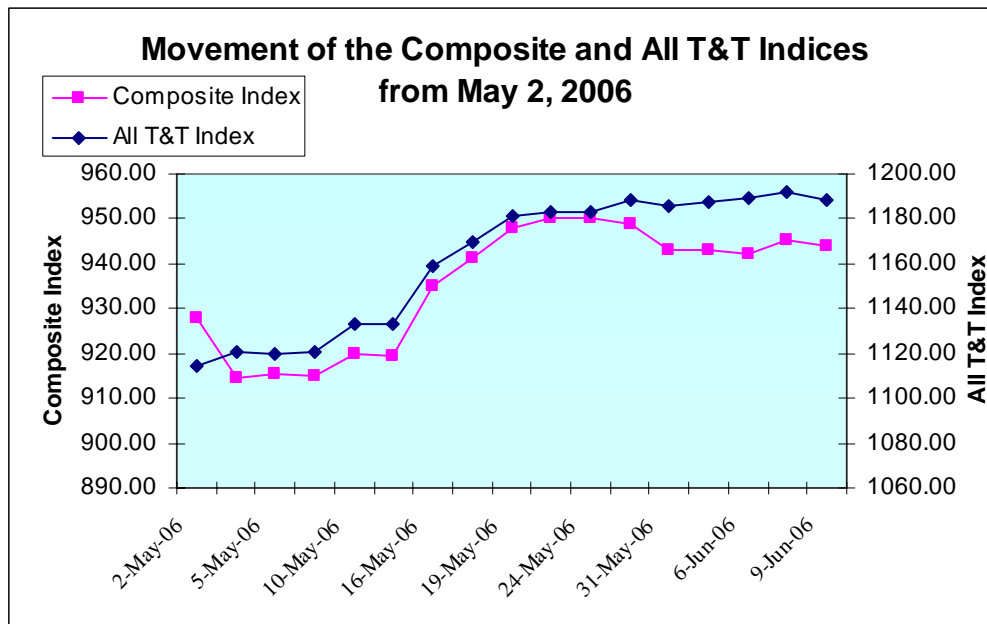
At this point in time, we are still faced also with the problem of capital flight. Evidence of this problem is found in the fact that the Central Bank increased sales to the market by 73.8 per cent this year in order to satisfy the demand for foreign dollars. In the Central Bank's Monetary Policy report dated April 2006, one of the reasons cited for the sustained rise in capital outflows was portfolio diversification encouraged by the reduction in the spread between local and foreign interest rates.

The reduction stems from the hiking of short term interest rates in the US. The Fed has been raising these rates in order to deal with economic ills such as inflation. Such hikes have resulted in the narrowing of the differential between the US and TT rate. Reduction in the US/TT interest rate differential is not to our Country's benefit as this would gear investors towards holding their liquid assets in US Dollars as the US currency is more stable than the TT Dollar.

Hence, in order to manage the differential (and also inflation) the Central Bank in turn responded by raising the repo rate. This rate has moved from 5.25 per cent in March 2005 to 7.00 per cent currently. The US short-term interest rate currently stands at approximately 5.00 per cent with the expectation that it would be raised to 5.25 per cent on June 29, 2006. It is hoped by maintaining the spread, investors would be more inclined to the Trinidad & Tobago market. Though perhaps, with the large outflows we have seen, it is probable that has not been enough to alleviate the problem.

This is an indication of how much extra money is leaving the country away from the Stock Market and other financial investments thereby subduing hopes of any speedy recovery. In addition, the crime situation among other socio-political instabilities in the country have also made investors skeptical about investing in the Trinidad & Tobago market.

Figure 3



It is also interesting to note that the Indices have not been on a steady climb since reaching their lows (See Figure 3). The Indices have in fact fluctuated since their respective lows with no clear sustained upward direction. In addition, though the advance/decline ratio progressively improved week on week to the end of May, the ratio of advances to declines lessened in the first two weeks of June hinting at the possibility that we may still see week on week declines in the Indices.

The good news is there are still opportunities existing in the market especially for investors with a medium to long term horizon. While the return of the institutional presence would help in the recovery of the market, there is also the need for investors to regain confidence in the TT market. Investors however have to condition themselves for this market in order to turn their short term fears into long term success. Too often, shares in this market advance in price based on momentum. We have seen this in the not

so distant past where investors rush the same share they have been worrying about in the previous few months.

In conclusion, given that previous periods of recovery has averaged approximately 20 months (from its peak), the problems still existing in the market and the fluctuation of the Indices, it is evident that there may still be some time before a full recovery.