

**"THE ROLE OF COMMERCIAL BANKS IN FINANCING GROWTH  
AND ECONOMIC DEVELOPMENT IN TRINIDAD AND TOBAGO  
AND THE CARIBBEAN: A PERSPECTIVE FROM THE ROYAL  
BANK OF TRINIDAD AND TOBAGO**

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DEVELOPMENT**

**The Role of Commercial Banks in Financing Growth and Economic  
Development in Trinidad and Tobago and the Caribbean: A perspective  
from The Royal bank of Trinidad and Tobago Limited**

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**1. INTRODUCTION**

Commercial banks are important financial intermediaries serving the general public in any society. In most cases, commercial banks hold more assets than any other financial institution. In some cases, even more than Central Banks. Apart from their many functions, commercial banks facilitate growth and development. Banks lend in many areas or sectors of the economy. Viewed from the real sector, they contribute to investments, employment creation, and by extension, the process of economic growth.

This paper seeks to analyze the role of a commercial banks - the Royal Bank of Trinidad and Tobago Company Limited in this development process. It seeks to answer the question, do banks contribute to growth in the domestic economy. Some commentators in the recent past argue that banks do not contribute to growth, but rather, simply introduce inefficiencies in the system on account of the high prices charged for financial services.

This paper, in joining the debate, argues that banks do contribute to growth. It uses the example of RBTT financial to show the involvement of the banking system in financing projects. These projects contribute to employment creation and economic development.

## 11. The Role and Dominance of Commercial Banks

Commercial banks are perhaps the most important financial intermediary serving the general public in any society. In most countries, commercial banks hold more assets than any other financial institution- about 40% of the aggregate resources of the financial sector. Commercial banks also represent a vital link in the transmission of government's economic policies (particularly monetary policy) to the rest of the economy. For example, when bank credit is scarce and expensive, spending in the economy tends to slow and unemployment usually increases. Fluctuations in the availability and cost of bank credit also have profound implications. If interest rates are very high, the cost of credit will be high and this could be inflationary. This is not surprising because bank deposits represent the most significant component of the money supply used by the public, and changes in money growth are highly correlated with changes in the prices of goods and services in the economy.

From the perspective of various groups in the country, access to bank credit and other bank service is absolutely essential. Financial intermediaries such as banks solve the problem of asymmetric risk. Depositors and borrowers are entirely different people and the risks are different. Banks solve problem of the asymmetry of information by the loan contract. Consumers, businesses and governments, look to commercial banks to supply credit in many different forms to meet their needs. Trinidad and Tobago boasts of a relatively modern and

sophisticated financial structure in terms of institutional mix and the range of instruments available. In Trinidad and Tobago, there are credit unions, non banks, development banks, mutual funds, and a stock exchange to name a few. However, notwithstanding the many institutions, commercial banks can be described as the behemoths of the financial system. They are by far the largest mobilizers of savings and providers of loanable funds. They now account for over 50% of the total assets of the financial system and far more than half of the financial savings of the domestic economy. In 2000, the assets of commercial banks reached an average of \$32,933 million (see Table 1).

**Table 1**

**Assets of the Banking System**

**1996-2000**

Institution	1996	1997	1998	1999	2000
Central Bank(\$TTM)	6,802.4	8,507.3	8,556.3	9,715.8	12,481
Commercial Banks(\$TTM)	22,959.9	27,193.9	26,473.5	28,929.7	32,933.1
Finance Co's (TT\$000)	2,212,478	2,385,974	4,011,980	4,935,632	4,791,498
Trust & Mortgage Co's(TT\$000)	4,452,334	5,577,801	4,889,853	6,631,875	9,157,253
Dev't Banks	984,839	1,009,418	1,102,867	1,120,485	1,349,007
Life Insurance	4945789	5232541	11090561	N/A	N/A

Source: Central Bank of Trinidad and Tobago.

With all these resources, commercial banks perform the role of financial intermediation. That is to say, they source funds or deposits from members of the public and they then onlend those funds or make those funds available to various individuals and institutions for financing productive activities, as well as for financing consumption. In performing this intermediation role, commercial banks assist in determining the degree of efficiency with which the entire economy functions.

The dominance of commercial banks in Trinidad and Tobago is a historical phenomenon. Commercial banks and insurance companies are the institutions that existed historically before the growth of other types of financial intermediaries in the last few years. Commercial banks came to Trinidad and Tobago in the 19<sup>th</sup> and in the 20th century, largely following trade and commerce – import and export activity – between Trinidad and Tobago and the northern countries, and they were able to finance that trade. In the last 50 years, commercial banks have moved in the direction of financing domestic activity. At present, there are six (6) commercial banks operating in the country with a total of approximately 128 branches. Banks employ in excess of 8,000 persons. The three largest banks account for two-thirds of the assets of the banking system.

The dominance of commercial banks is due in part to the geographic dispersion of banking offices and the easy availability of banking services to the population.

In Trinidad and Tobago, there is a branch for every 10,000 persons. Moreover, banks offer a wide and relatively sophisticated range of services, including loan facilities, deposit accounts, bills of collection, customer payments services, credit card services and 24- hour banking. Banks also have excellent international banking connections.

Deposits of commercial banks account for about 75% of commercial bank liabilities. Loans and investment constitute their asset portfolio. The former dominates their asset mix. Commercial bank lending include financing activity in the energy sector, in manufacturing, construction and services just to mention a few. In the last decade, however, many changes have occurred with respect to the role and functions of commercial banks. We shall return to this discussion later in the paper.

Commercial banks in Trinidad and Tobago are very safe, a haven for people's funds. The commercial banking system has been in existence for centuries. Banks developed out of institutions where their parent banks originally came from the United Kingdom, Canada and the USA. They have developed a certain set of practices, which serve to ensure that depositors' funds are completely safe and protected. They also serve to ensure that a depositor can get growth on their deposits with those institutions because the banks use those funds productively. That is, they lend them ensuring that at all times there is a return on that investment, and part of that return is passed on to the depositors in the

form of a rate of interest on the deposits which the banks hold. The above discussion highlights a historical role of commercial banks. This role is performed in many countries. It is not a new role but merely the minimum that we expect from commercial banks. In Trinidad and Tobago however, commercial banks perform many other functions and provide many services.

### **111. Industry Response to Global Trends**

During the 1960s, banks did three main things – they “borrowed money”, “transferred money”, and “lent money” through an array of simple vanilla type products. The term disintermediation did not exist. In the last decade, on account of liberalization, privatization and globalization, the role of banks in many countries has changed rapidly. The role of banks has also changed under the pressures from developments in technology (principally the use of computers and the electronic media) and government regulations. There is now greater competition between banks and non-banking institutions.

These non-bank thrift institutions, along with insurance companies, brokerage houses, and aggressive non-financial firms, are making it increasingly difficult to distinguish banks from other financial institutions. Historically, banks alone offered checking accounts and catered primarily to business (commercial) customers. That uniqueness, however, has gradually disappeared, and there is

now a frantic rush of non-bank financial-service providers to enter traditional banking markets.

The genesis of these changes began in Trinidad and Tobago in the late 1980s when the banking system introduced automated banking machines (ABM's) in 1986, Link ABM service in 1994 and LINX Debit Point of sale in 1996. This enabled more customers access to non-cash payment methods. Notwithstanding, the whole process received a fillip in 1993 when the authorities in Port-of Spain liberalized the financial system and floated the TT dollar. Simultaneously, the Financial Institutions Act (1993) was passed, which repealed the Banking Act (Chap.79: 01) and the Financial Institutions (Non-Banking) Act, 1979 (Chap.83: 01).

The Financial Institutions Act merged the activities of commercial banks and non-bank financial institutions and referred to them as Financial Institutions. These new pieces of legislation also allowed institutions to enter into areas, which was not their traditional business domain. At that time, the financial system began to demand a wider menu of instruments in which investors could place their excess funds. Additionally, there was need for new institutions to further develop the money and capital market. Under the Caricom Single Market and Economy initiative, there was also the need to harmonize laws and regulations. Against the above background, commercial banks have entered new areas, RBTT no exception.



#### IV. THE RBTT EXPERIENCE

With a modest foreign branch beginning in 1902, and transformation to a local Trinidad Bank in 1972, RBTT is now comprised of 31 companies, including 8 commercial banks, with over 75 branches and 150 automated banking machines, located throughout the English speaking Caribbean, Suriname, Aruba, and the Netherlands Antilles. RBTT is now the largest network of financial institutions in the region and as a result, there is a tremendous cross-border reach.

The Royal Bank of Trinidad and Tobago was the first local commercial bank to offer investors the opportunity to invest in a mutual fund. Previously, one firm, the Unit Trust Corporation, dominated the mutual fund industry. Today, RBTT financial offer investors the opportunity to invest in the Roytrin Mutual Income and Growth Fund, The Roytrin Mutual Money Market Fund or the Roytrin US Dollar Denominated Fund. In the last few years, the Group's proprietary mutual funds have performed creditably. The Roytrin Income and Growth Fund grew by 42% last year from TT\$199.89 million in 1999 to TT\$ 283.85 million in 2000.

The Capital return on unitholders' investments for 2000 improved significantly from negative 1.26% in 1999 to an impressive 8.38%. Unitholders also enjoyed a total income distribution of 9.41 cents per unit which represents an income yield of 5.22%, thus bringing their total return for 2000 to 13.6% compared with 5.8% a year earlier.

The Roytrin Mutual Money Market Fund continues along a phenomenal growth path, as total funds under management rose by an exceptional 159% from TT\$463 Million at December 31, 1999 to TT\$1.2 Billion at December 31, 2000. Unitholders enjoyed an effective annualized return of 10.56%. This return was competitively comparable to that yielded by subscribers to other money market funds in the domestic economy.

RBTT financial also offer specialized products in the area of insurance. These include deferred annuity plans, retirement plans and pension plans. These products are designed to allow an investor to manage assets while creating wealth and investments.

Additionally, dedicated commercial independent business units are providing high quality relationship management into target markets. The Royal Merchant Bank and Finance Company is, by any benchmark, the premier and leading Merchant Banking institution in the region. It has consistently executed mandates in various jurisdictions in the region in recent years. These jurisdictions include the Eastern Caribbean States, Barbados, Jamaica, Belize, The Netherlands Antilles and the Dominican Republic in addition to Trinidad and Tobago. It has successfully raised capital for diverse undertakings in these jurisdictions. The company has also been a pioneer in capital projects, hospitality, mining, manufacturing, communications, agriculture and distribution. The company has also pioneered capital market activities and securitized

products. This company has therefore been a major mobilizer of funds for the region and has contributed to the economic and social development of the region. At the end of January 2001, RBTT's cross border exposure was above US\$212 million. RBTT has financed the Grenada Stadium, provided financing for the government's of St Kitts, Belize, Barbados and Trinidad and Tobago, and has financed hotel construction in St Lucia.

RBTT Financial also has a subsidiary called RGM Limited. This company is a joint venture with insurance companies. It is a project financing capability for the execution of high quality commercial real estate projects and for the issue of real estate backed securities to the capital markets. Additionally, RBTT is involved with Development Finance Limited, BANCASSURANCE (CARIBBEAN) LIMITED and West Indies Stockbrokers Limited (WISE) just to mention a few.

Development Finance limited focuses its operations on the long- term segment of the market with concentration on the provision of corporate finance, risk capital and strategic management advisory services. BANCASSURANCE is a joint venture alliance with Guardian Holdings Limited which allows clients of the Group access to low-cost term insurance and investment linked products, and a full range of general insurance products from other associated companies. WISE became a subsidiary of the RBTT Group in 1999 and has contributed positively to the Groups bottom line ever since. On January 7, 2000, this company acquired Money Managers Limited, a stockbroking firm with considerable market

share in the domestic market, significantly enhancing its dominant position there. The operations of these two companies have been merged to achieve service quality, cost and operational efficiencies.

All of the above demonstrates that RBTT's vision is in sink with the need in Trinidad and Tobago for a more sophisticated technology oriented financial system. The vision is one where the investors in the country can have a wider choice of instruments from which to choose as well as various institutions in the country. Additionally, on account of globalization and liberalization, RBTT is fully aware that Trinidad and Tobago can be quite competitive indeed. On account of this competitiveness in the local economy, RBTT's presence in the region now stretches from Suriname in the south to Jamaica in the north, including the Netherlands Antilles. As we move forward, RBTT's challenge is to continue to build a strong and enduring regional brand, guided by a shared vision for efficiency, customer satisfaction and profitability. There can be no doubt therefore that commercial banks in general and RBTT in particular plays a critical role in Trinidad and Tobago's development and they will continue to do so.

## **V. BANKING DELIMITATIONS**

While commercial banks do make a valid contribution in Trinidad and Tobago, there is perhaps one area in which banks have not delivered. This is in the area of new small businesses and micro-firms. Generally, commercial banks have not

financed genuine entrepreneurship at these lower levels. New small businesses refer to people with a business idea, or a new line of activity. Such individuals usually have no collateral or very little. They generally have no track record in terms of management of business and as a result, banks tend not to lend to these entities. In contrast, Commercial banks favour larger, well-established ventures. Commercial banks, in assessing those particular businesses and the propositions which those large businesses bring before them, normally need collateral in the form of fixed and floating assets. Large companies have a track record. Banks know the managers of large companies. These companies would have several successful loans, which have performed prior to the particular application, and therefore commercial banks would naturally favour lending to those large businesses.

One possible way of encouraging the trickling down of wealth creation is to encourage greater employment in small and medium sized enterprises. This paper accepts the fact that Commercial banks in Trinidad and Tobago can do more for small businesses in the future. In this regard, venture capital could be a solution to this problem. There is an opportunity for commercial banks to create venture capital companies of their own, or to form alliances with other enterprises. This will go a long way in funding small business development in Trinidad and Tobago in the future. RBTT is currently working on the idea of venture capital financing.

## VI. CONCLUSION

This paper has shown that commercial banks are critical to the development process. By granting loans in areas such as agriculture, manufacturing, services, construction and the energy sector, banks contribute to the development of the country. By innovating and making new instruments available to investors, banks perform an intermediation function, but they also allow investors the opportunity to gather wealth based on their investment strategy. In the case of RBTT, the paper suggests that this organization is not only a Trinidad and Tobago bank, but also a regional bank. The recent mergers, acquisitions and alliances have propelled this institution as the premier Caribbean financial institution. One which in the final analysis, is concerned with "Caribbean Development."

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