



# CENTRALE BANK VAN CURACAO EN SINT MAARTEN

## Macroeconomic effects of the closure of the border of Sint Maarten due to the coronavirus (COVID-19)

### 1. Introduction

The government of Sint Maarten has implemented some precautionary measures in relation with the global outbreak of the coronavirus (COVID-19) for the country of Sint Maarten. One of these measures is the closure of the borders for commercial flights. Furthermore, the borders have also been closed for maritime traffic, with the exception of transport of oil products and freight.

The government of Sint Maarten has requested the Centrale Bank van Curaçao en Sint Maarten (CBCS) to calculate the economic impact that the worldwide outbreak of the coronavirus will have on the economy of Sint Maarten. Presently, the CBCS does not have all information in order to calculate the total impact of this pandemic on the economy due to some data deficiencies especially since hurricane Irma hit Sint Maarten. However, the CBCS has done a calculation of the impact that closure of the borders for commercial flights and cruise ships will have on the economy. Four impact scenarios were calculated based on the possible duration of these restrictions:

1. Period of 1 month;
2. Period of 2 months;
3. Period of 3 months;
4. Period of 6 months.

To assess the macroeconomic impact of this measure, the impact scenarios were compared to a baseline scenario. Furthermore, the impact scenarios are based on several assumptions. The key variables of interest in this case are the real GDP growth and the GDP components.

The coronavirus will have significant adverse effects on the global economy, our main trading partners, and Sint Maarten. The outbreak will result in increased health care costs and a significant decline in economic activities. The recovery from this economic shock depends on, among other things, the duration of the outbreak. In this note, the duration was not taken into consideration. International organizations such as the International Monetary Fund (IMF) have not yet updated their economic projections for the effects of this global pandemic. The CBCS will update and present a new outlook when these projections are available. Therefore, this note only estimates the effects that the closure of the borders of Sint Maarten to prevent an outbreak of the coronavirus will have on the economy of Sint Maarten.

The note is structured as follows. Section 2 describes the baseline scenario while the assumptions that were made in the impact scenarios are outlined in section 3. Section 4 presents the impact scenarios based on the assumption of a fast recovery after reopening of the borders. Meanwhile, section 5 discusses the impact scenarios in the case of a gradual recovery after reopening. Furthermore, the effects on employment are outlined in section 6. Finally, section 7 presents concluding remarks and some policy recommendations.

## **2. Baseline scenario**

In the baseline scenario, Sint Maarten's real GDP is projected to grow by 2.9% in 2020 driven by an increase in domestic demand. The outlook is predicated on the assumption that the number of cruise passenger arrivals will contract in 2020 for a variety of reasons including increased regional competition and fleet redeployment by major cruise lines. Private investments will increase as a result of, among other things, the start of the second phase of the reconstruction of the airport, the construction of a new 400+ room hotel in Philipsburg, and other ongoing smaller projects. Notwithstanding higher inflation, consumer spending will rise due to higher employment, among other things. Public investments also will increase due to the planned construction of a new hospital. Furthermore, public consumption is projected to rise.

In contrast, net foreign demand is projected to put a drag on real output growth because imports will increase at a faster pace than exports. The increase in exports will be driven mainly by the growth in tourism arrivals, particularly stay-over arrivals. In addition to the higher tourism demand, imports by the wholesale & retail trade sector will increase because of the higher domestic spending and more construction-related materials and services imported from abroad. Meanwhile, inflation is expected to increase to 2.5% in 2020, in line with the forecast rise in the US inflation rate, Sint Maarten's main trading partner.<sup>1</sup>

## **3. Assumptions impact scenarios**

The effects of the closure of the borders for commercial flights and cruise ships on Sint Maarten's GDP is calculated for the following impact scenarios:

1. Duration of closure is 1 month;
2. Duration of closure is 2 months;
3. Duration of closure is 3 months;
4. Duration of closure is 6 months.

Only the short-term effects were calculated, i.e., the effect on economic growth in 2020.

The impact scenarios are based on the following assumptions:

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<sup>1</sup> IMF World Economic Outlook, January 2020.

1. The closure of the borders has a negative effect on exports, in particular the foreign exchange earnings from tourism, transportation services and other services related to the tourism sector.
2. The closure of the borders has a negative effect on economic activities and employment, particularly in the sectors tourism, transport and other services related to tourism, and thereby indirectly also on domestic demand.
3. As a result of the negative effects on exports and domestic demand, the closure of the borders will also have a negative effect on the import of goods and services.
4. Exports will recover fast and develop consistent with the baseline following the reopening of the borders.

The following factors were not taken into account in the calculations:

1. The economic effects of a possible outbreak of the coronavirus in Sint Maarten (increased health care costs and negative spinoff on other economic activities).
2. Possible upward pressure on inflation as a result of a disruption of global supply chains due to the global outbreak of the coronavirus.
3. Change in inflation due to increased oil price volatility as a result of the global outbreak of the coronavirus.

#### **4. Effects in case of a fast recovery after reopening of the borders**

Table 1 shows the effects of a closure of the borders on the economy of Sint Maarten. In this case, it is assumed that after reopening of the borders, the economy will experience a fast recovery and reach the projected levels of the baseline scenario.

The closure of the borders will have an adverse impact on the economy of Sint Maarten. The magnitude depends on the duration of the closure. If these restrictions are set for 1 month, real GDP growth will slow down to 0.8%. This is 2.1 percentage points lower compared to the baseline scenario. However, a closure of longer than one month will result in a real GDP contraction ranging between 3.2% (2 months) and 15.0% (6 months). Hence, real GDP will deviate between 2.1 and 17.9 percentage points from the baseline scenario.

The adverse effect on real GDP is reflected by a more negative contribution of net foreign demand compared to the baseline scenario as a result of a decline in the export of goods & services, moderate by a decline in imports. While exports are projected to grow in the baseline scenario, this will not be the case in the impact scenarios. Exports will drop considerably as a result of lower foreign exchange earnings from the tourism and transportation sectors. Also, the earnings from the businesses that cater to the tourism sector will decline, particularly the renting, timeshare and wholesale & retail trade sectors. Imports also will turn around from a growth in the baseline scenario, to a contraction in the impact scenarios caused primarily by the drop in tourism activities (that have a high import content).

Meanwhile, domestic demand will increase at a slower pace compared to the baseline in case the closure of the borders lasts between 1 and 3 months. In particular, private consumption will be

affected as employment in the tourism-related sectors will drop. In addition, the other components of domestic demand will increase at a slower pace. In case the closure lasts 6 months, domestic demand will drop due to a decline in both private and public consumption, while private and public investments will increase at a slower pace compared to the baseline scenario.

**Table 1. Effect closure borders on the economy of Sint Maarten in 2020 – fast recovery**

	<b>Baseline scenario 2020</b>	<b>Scenario 1: closure 1 month</b>	<b>Scenario 2: closure 2 months</b>	<b>Scenario 3: closure 3 months</b>	<b>Scenario 4: closure 6 months</b>
<b>Domestic demand, of which</b>	<b>4.1%</b>	<b>3.7%</b>	<b>2.9%</b>	<b>1.7%</b>	<b>-0.4%</b>
Private sector	3.4%	3.0%	2.3%	1.4%	-0.3%
Investment	2.2%	2.2%	1.9%	1.5%	0.9%
Consumption	1.2%	0.8%	0.4%	-0.1%	-1.2%
Public sector	<b>0.7%</b>	<b>0.7%</b>	<b>0.6%</b>	<b>0.3%</b>	<b>-0.1%</b>
Investment	0.4%	0.4%	0.4%	0.3%	0.3%
Consumption	0.3%	0.3%	0.2%	0.0%	-0.4%
Changes in inventory	0.0%	0.0%	0.0%	0.0%	0.0%
<b>Net foreign demand, of which</b>	<b>-1.2%</b>	<b>-2.9%</b>	<b>-6.1%</b>	<b>-8.9%</b>	<b>-14.6%</b>
Export of goods and services	2.9%	-3.4%	-9.7%	-14.1%	-28.2%
Import of goods and services	4.1%	-0.5%	-3.6%	-5.2%	-13.6%
<b>GDP (real)</b>	<b>2.9%</b>	<b>0.8%</b>	<b>-3.2%</b>	<b>-7.2%</b>	<b>-15.0%</b>
<b>Inflation</b>	<b>2.5%</b>	<b>2.5%</b>	<b>2.5%</b>	<b>2.5%</b>	<b>2.5%</b>
<b>GDP in mln NAf. (nominal)</b>	<b>2,016.5</b>	<b>1,976.4</b>	<b>1,899.8</b>	<b>1,823.3</b>	<b>1,674.1</b>
<b>GDP in mln NAf. (real, prices of 2010)</b>	<b>1,613.6</b>	<b>1,580.6</b>	<b>1,517.9</b>	<b>1,455.2</b>	<b>1,332.9</b>

## 5. Effects of a gradual recovery after reopening of the borders

In this section, the impact scenarios are presented in case of a gradual recovery of the exports after reopening of the borders. In these scenarios it is assumed that in the first three months after the reopening of the borders, the exports will be 50% below the level of the baseline scenario. In the remainder of the year, the exports will be 25% below the level of the baseline scenario. The other assumptions remain the same as in the impact scenarios based on a fast recovery track.

Under a gradual recovery scenario, the adverse effect on the economy will be more pronounced than in the case of a fast recovery. Depending on the duration of the closure of the borders, the contraction

of real GDP will range between 5.7% (1 month) and 29.2% (6 months). Hence, real GDP growth will be between 8.6 (1 month) and 32.1 (6 months) percentage points below the baseline scenario.

**Table 2. Effect closure borders on the economy of Sint Maarten in 2020 – gradual recovery**

	Baseline scenario 2020	Scenario 1: closure 1 month	Scenario 2: closure 2 months	Scenario 3: closure 3 months	Scenario 4: closure 6 months
<b>Domestic demand, of which</b>	<b>4.1%</b>	<b>2.3%</b>	<b>1.1%</b>	<b>-0.3%</b>	<b>-2.6%</b>
Private sector	3.4%	2.0%	1.0%	-0.1%	-1.9%
Investment	2.2%	2.0%	1.5%	1.0%	0.4%
Consumption	1.2%	0.0%	-0.5%	-1.1%	-2.3%
Public sector	0.7%	0.3%	0.1%	-0.2%	-0.7%
Investment	0.4%	0.4%	0.3%	0.2%	0.2%
Consumption	0.3%	-0.1%	-0.2%	-0.4%	-0.9%
Changes in inventory	0.0%	0.0%	0.0%	0.0%	0.0%
<b>Net foreign demand, of which</b>	<b>-1.2%</b>	<b>-8.0%</b>	<b>-9.6%</b>	<b>-13.4%</b>	<b>-26.6%</b>
Export of goods and services	2.9%	-12.7%	-17.3%	-22.9%	-43.4%
Import of goods and services	4.1%	-4.7%	-7.7%	-9.5%	-16.8%
<b>GDP (real)</b>	<b>2.9%</b>	<b>-5.7%</b>	<b>-8.5%</b>	<b>-13.7%</b>	<b>-29.2%</b>
<b>Inflation</b>	<b>2.5%</b>	<b>2.5%</b>	<b>2.5%</b>	<b>2.5%</b>	<b>2.5%</b>
<b>GDP in mln NAf. (nominal)</b>	<b>2,016.5</b>	<b>1,852.0</b>	<b>1,798.4</b>	<b>1,698.9</b>	<b>1,402.4</b>
<b>GDP in mln NAf. (real, prices of 2010)</b>	<b>1,613.6</b>	<b>1,478.7</b>	<b>1,434.8</b>	<b>1,353.3</b>	<b>1,110.2</b>

## 6. Effect on employment

A projection of unemployment can be estimated based on correlation analysis. In times of economic contractions, unemployment will increase, ceteris paribus, while in times of economic growth, unemployment will decrease. Hence, in this assessment, the changes in structural unemployment in the traditional sense and demographics such as migration are not taken into account.

Table 3 shows the real GDP growth rate and the unemployment rate in the baseline scenario, the impact scenarios in case of a fast recovery after reopening, and the impact scenarios in case of a gradual recovery after reopening.

	Baseline scenario 2020	Scenario 1: closure 1 month	Scenario 2: closure 2 months	Scenario 3: closure 3 months	Scenario 4: closure 6 months
<b>Real GDP growth (%)</b>					
Fast recovery	2.9	0.8	-3.2	-7.2	-15.0
Gradual recovery	2.9	-5.7	-8.5	-13.7	-29.2
<b>Unemployment (%)</b>					
Fast recovery	4.0	5.6	8.6	11.6	17.4
Gradual recovery	4.0	10.4	12.5	16.4	28.1

## 7. Conclusion and policy recommendations

In this note, the effects of the closure of the borders of Sint Maarten for international commercial flights and cruise ships to prevent an outbreak of the coronavirus COVID-19, which is especially dangerous for elderly and people with other medical conditions, are presented. The closure of the borders will have a significant adverse effect on Sint Maarten's economy. An analysis of the GDP by expenditure shows that all components will be affected but the decline will be more pronounced in exports, imports, and private consumption. Furthermore, the magnitude of the adverse effect will depend on how fast the economy will recover after the borders are reopened. The real GDP contraction will be deeper in case of a gradual recovery combined with prolonged border restrictions. The analysis suggests an exponential worsening of Sint Maarten's economy, the longer the border restrictions are in place.

Sint Maarten experienced another severe external shock in 2017 with the passing of Hurricane Irma. The current projections indicate that the adverse effects of the global coronavirus outbreak will be even more severe. The main reason is that the hurricane reconstruction activities, driven primarily by the private sector, moderated Sint Maarten's economic contraction and pushed the country relatively quickly back on a recovery path.

Under these circumstances it is crucial that the major investment projects that were scheduled in 2020, i.e, the further reconstruction of the Princess Juliana International Airport and the construction of the new Sint Maarten Medical Center continue. Further delays or postponement of these investment projects will deepen the projected contraction. Furthermore, coordinated efforts should be taken by the private and public sectors to promote Sint Maarten as a safe tourist destination, once this crisis is over.

A deep economic contraction will worsen Sint Maarten's public finances. Following the hurricane in 2017, Sint Maarten was already allowed to deviate from the budgetary rules as stipulated by the Kingdom Law on Financial Supervision for Curaçao and Sint Maarten. With this new shock, the government of Sint Maarten should request the Dutch government and the CFT to prolong to allowed deviation from the rules.

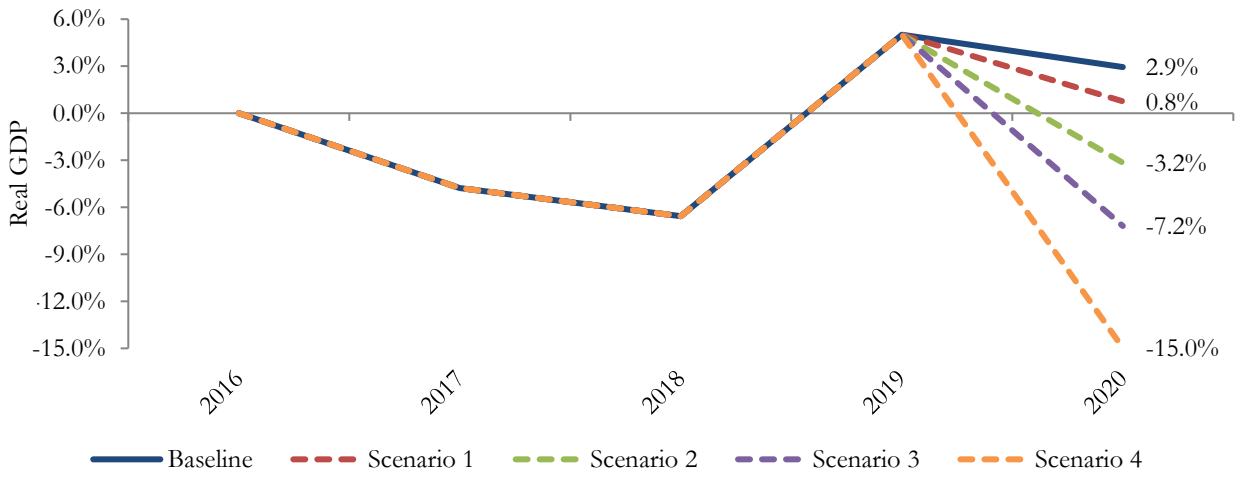
Financial support from the Netherlands will be crucial to alleviate the economic and social impact of this new shock and to achieve a fast recovery of the economy. Part of the funds that have been allocated to the Sint Maarten Recovery and Reconstruction Fund could be used for financial support for businesses that are severely affected by the border restrictions. Furthermore, the creation of a social safety net is essential to support those who will lose their job because of lower economic activities, particularly in the tourism sector.

**Centrale Bank van Curaçao en Sint Maarten**

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## Appendix

### Graph 1. Effect closure of borders on the economy of Sint Maarten in 2020 – fast recovery



### Graph 2. Effect closure of borders on the economy of Sint Maarten in 2020 – gradual recovery

