

## **ANNUAL REPORT 2007**

**Bank van de Nederlandse Antillen**

## 1. REPORT OF THE PRESIDENT

### 1.1 General review

The economic situation in the Netherlands Antillean economy deteriorated in 1997 for the second consecutive year, as real GDP contracted by approximately 2%. Domestic demand declined as the export sector showed signs of recovery. The decline in domestic demand resulted from the decline in both consumption and investment. Private consumption fell because of the reduced purchasing power resulting from the fiscal measures in the structural adjustment program. The latter also contributed to the fall in government consumption, which was further compounded by financial constraints on the domestic capital market. Private investment declined as a result of the decline in consumption and uncertainties regarding the government's fiscal consolidation efforts and the start of large projects in the utility and tourist sectors. The decline in private investment was mitigated by an increase in government investment. The contraction of economic activities contributed to an increase in the unemployment rate. The decline in domestic demand and, hence, imports, combined with the slight improvement in the performance of the export sector, resulted in an increase in the international reserves position.

The economic downturn was accompanied by a deceleration in the inflation rate. The main domestic factor contributing to this development was the fading effect of the government's revenue-enhancing measures, including the increase in indirect taxes, social premiums, and the implementation of various user fees. Foreign factors contributing to the decline in inflation were the moderate inflation rates in our main trading partners and the appreciation of the Netherlands Antillean guilder vis-à-vis the non-dollar currency areas.

Our main export industry, tourism, performed well in 1997. This positive performance was mainly the result of developments in St. Maarten -- progress made in the reconstruction of the tourist infrastructure after the hurricane disaster in September 1995, and intensification of marketing efforts. Tourist activities in Curacao remained sluggish, reflected by a further decline in the number of stay-over visitors. In contrast, cruise tourism in Curacao grew significantly, contributing to an overall increase in foreign exchange income earned. The situation in Bonaire was similar. Stay-over tourism declined, while cruise tourism expanded markedly. The expansion in cruise tourism contributed to a slight increase in foreign exchange income generated. Developments in Curacao and Bonaire can be explained partly by a deterioration in their competitiveness versus other Caribbean destinations, aggravated by the appreciation of the Netherlands Antillean guilder vis-à-vis the European currencies. The prospects for 1998 are moderately positive. The rebuilding of the tourist infrastructure in St. Maarten is still to be completed as the large hotels are still closed. In Curacao, several projects in progress will enhance tourism activities. These projects include the reconstruction of a large hotel under the management of a well-known international chain and the construction of a pier for mega cruise ships. The prospects for recovery of Bonaire's tourist sector have improved with the support from Dutch development funds for an intensification of Bonaire's marketing efforts. The Bank wishes to underscore the importance of the tourist sector as one of the main generators of foreign exchange. Its sustained recovery should greatly facilitate the adjustment process the government has embarked upon. The authorities should, therefore, give their full support to viable initiatives that strengthen this important economic pillar.

The oil refinery continued to perform well in 1997, reflected by an expansion in the number of barrels refined. Efforts to reduce the operating costs started to pay off in 1997, as the refinery realized its first profit since the Venezuelan oil company PDVSA started its operations on the island of Curacao in 1985. This result and upcoming large investments should enhance the refinery's long-term viability. In the beginning of 1999, the construction of a power plant is expected to start according to the "build, own and operate" principle. In addition, investments will be made to upgrade the refinery aimed at further improving its cost efficiency and reducing the negative effects of the refinery's operations on the environment. These investments are a welcome stimulus for the economy.

Developments in the transportation sector were mixed in 1997. After a strong increase in 1996, the national carrier *Air ALM* recorded a modest growth in the number of passengers, and the amount of cargo transported declined. The deterioration in performance can be attributed to a substantial slippage in the restructuring of the company into a profitable business. As a result, the company's liquidity problems increased, and a substantial capital injection is needed now to safeguard the company's long-term viability. Given the weak public finances, the government can ill afford to subsidize the national carrier. Consequently, the necessary funds should be raised on the capital market. However, to gain investors' confidence, a credible business plan should be presented with prospects for a profitable operation in the coming years.

Activities in the harbor also recorded mixed developments, reflected by an increase in the number of ships piloted and a decline in the amount of cargo handled. The increase in the number of ships piloted can be attributed to the buoyant development in cruise tourism and the sharp increase in the number of tankers resulting from the strong expansion in oil transshipment activities. The decline in the amount of cargo handled resulted from the decision of the European Union to restrict the import of rice and sugar from Overseas Countries and Territories and the overall decline in imports related to the economic recession. Furthermore, bunker activities deteriorated slightly. Activities in the ship repair sector decreased in 1997, as measured by the number of man-hours sold. Nevertheless, the amount of foreign exchange income generated increased and the operations remained profitable. With the negotiations for the privatization of the dry-dock company well advanced, it is expected that activities in 1998 should be positively influenced.

The international financial and business services sector recorded a further decline in activities in 1997 after peaking in 1995. Both profit tax transfers to the government and receipts to cover operational expenditures declined. These declines can be explained partly by changes in the tax arrangements with the Netherlands, which affected the competitive position of the Netherlands Antilles vis-à-vis other jurisdictions. The Bank welcomes the founding of the Captive Insurance Association of Curacao, whose objective is to promote the establishment of captive insurance companies in Curacao. The swift passage of the pending laws to enhance our competitive position in this field is in order. The passage of the long overdue stock exchange legislation and the private foundation has become imperative. The passage of the new fiscal regime legislation is also called for.

Activities in the construction sector continued to decline in line with the economic downturn. Furthermore, free zone activities maintained their trend of the past few years, reflected by an increase in re-export and a decline in the number of visitors. The growth in free zone re-exports is expected to accelerate further with the recent opening of a free zone at the airport of Curacao, which is in line with the objective to develop Curacao as a major regional transportation center.

On the fiscal front, we were confronted with the challenge of reconciling growth and employment with the objective of meeting fiscal targets. Policy slippages, reduced availability of financing from non-bank domestic sources, increased interest spreads on borrowing and the consequent build up of arrears have weakened near-term growth prospects considerably. While the deficit of the government improved substantially on a cash basis, it reached unsustainable proportions on a commitment basis. Part of the improvement was attributable to the implementation of fiscal consolidation measures included in the structural adjustment program, but the main reason for the lower deficit was the deferment of expenditures forced by increasing financing constraints on the domestic capital market. The latter was reflected by, among other things, a sharp increase in arrears at the civil servants pension fund APNA, postponement of the governments' contribution to the Sinking Fund and a partial shift to 1998 of the capital injection in the national carrier ALM and the relief payments to St. Maarten in connection with the hurricane damage. Further measures are needed to resume the path of adjustment.

The budget deficit on a cash basis remained within the target set in the structural adjustment program. Government revenues declined due to a marked decline in nontax revenues resulting from shortfalls in the transfer of dividends from government enterprises and fees and charges collected for services provided. Tax revenues increased owing to the introduction of a turnover tax on the Windward Islands, a pay-as-you-file system for profit tax, and the full-year impact of the sales tax on the Leeward Islands. However, the overall increase in taxes turned out to be much lower than projected due to shortfalls in the receipts from import duties and taxes on income and profits in connection with the economic recession. To ensure a lasting reduction of the government deficits, the structural elements of the fiscal consolidation package, such as the implementation of the core-task analysis and the privatization program, should be accelerated. Such an approach will gradually reduce the diversion of scarce resources from productive investments and, hence, enhance the prospects for a sustained economic recovery.

The decline in imports related to the decline in domestic demand, combined with a slight improvement in our export performance owing mainly to tourism, resulted in a substantial reduction of the deficit on the current account of the balance of payments in 1997. In contrast, the surplus on the capital account decreased primarily because of the exceptional surplus of the private sector in 1996, the result of transitory factors. However, the improvement of the current account deficit more than offset the deterioration of the capital account surplus, resulting in an increase in our foreign exchange reserves. This increase was only marginally below the December 1997 target of reserves accumulation in the structural adjustment program. Despite its improvement, however, the deficit on the current account is unsustainable. To ensure a lasting improvement in our balance of payments and, hence, international reserves, efforts should be made to strengthen our export sector. The recommendations of the Interamerican Development Bank provide a good starting point.

The increase in net international reserves was the main factor that contributed to the expansion of the money supply in 1997. The domestic sector recorded a marginal expansionary impact due to miscellaneous factors. Both the private sector and the government sector exerted a contractionary impact. The contractionary impact of the government sector was accounted for by the nonmonetary financing of the deficits of the island governments. The contractionary impact of the private sector resulted from a decline in commercial banks' credit extension in connection with the tightening of monetary policy and the weak demand for credit related to the economic recession and uncertainties surrounding the government finances. The tightening of monetary policy in 1997 was reflected by

the introduction of intermediate quarterly targets for credit extension to the private sector and a progressive penalty system in the monetary cash reserve arrangement. As a result, credit to the private sector remained well within its growth target of 3.5% of the October 1996 base amount, and the ceiling on net credit to the government was not exceeded. In addition, the Bank increased the reserve requirement from 2% to 3% in August 1997. This decision was taken because of the persistent overliquidity in the banking system, a potential source of excess credit extension. The Bank's monetary stance resulted in adherence to the monetary targets set in the structural adjustment program corrected for net government credit since the government did not make any contributions to the sinking fund. In the period ahead, monetary policy will remain appropriately tight.

## **1.2 Policy considerations**

The economic situation in the Netherlands Antilles during 1997 developed against the background of a world economic situation characterized by expanding economies in industrial countries, Latin America, many countries in Eastern Europe, and significant parts of Africa. On the other hand, Japan and its Asian trading partners encountered significant difficulties.

The economic situation in the Netherlands Antilles continued its downward path. The policy shortcomings and their ramifications seem to have contributed to a worsening of the fiscal situation. Against the background of growing fiscal deficits and dwindling foreign exchange reserves, the government of the Netherlands Antilles embarked on a comprehensive structural adjustment program. With assistance from the IMF, quarterly quantitative and policy benchmarks were established for fiscal and monetary performance in 1997. These benchmarks should contribute to a balanced budget and adequate foreign exchange reserves by the year 2000. The successful implementation of the program would be supported by a precautionary line of credit by the Dutch Central Bank, refinancing of the principal payments on Dutch development loans, and a contribution to the social program accompanying the adjustment process.

Despite the introduction of a package of fiscal measures, the program went off track in the first quarter of the program year. The faltering of the program can be attributed largely to internal factors, including delays in the implementation of structural reforms, weaknesses in tax administration and enforcement, and overly optimistic projection of nontax revenues. In addition, the lack of appropriate expenditure monitoring and control mechanisms allowed expenditure overruns, particularly at the Central Government level. Nevertheless, the government deficit on a cash basis remained within the program target. This meeting of the target was realized, however, through deferring expenditures to 1998 and a substantial build-up of arrears due to financing constraints.

The political and economic panorama that has unfolded over the last few months understandably has puzzled and preoccupied market participants. The involvement of a social dimension in the restructuring efforts should not mask the need for corrective fiscal measures. Economic growth is required for sustained social development. Sound macroeconomic policies are necessary to encourage productive investment essential for sustainable growth. Adjusted for the carry-over of expenditures from 1997 and newly identified shortfalls, the approved budgets of the Central Government and the Island Government of Curaçao resulted in a combined deficit of over NAf.400 million (10% of GDP) in 1998. A deficit of this size cannot be financed fully from nonbank domestic sources, as clearly demonstrated by the difficulties experienced in financing a far smaller deficit in 1997. Such a deficit will result in an unsustainable debt-to-GDP ratio. Given a nominal GDP growth of 4% an-

nually, the current domestic debt-to-GDP ratio of 54% will increase to 70% in a period of five years if no additional measures are taken.

Credible corrective measures are urgently needed to restore the fiscal situation. In a no-policy-change scenario, the fiscal situation is likely to deteriorate. The road to fiscal consolidation remains long and difficult. But only with a sense of realism in economic policy-making will we be able to grow out of our fiscal problems. A major step forward is the adoption of a structural adjustment program with a set of forceful, far-reaching structural reforms to strengthen the fiscal situation and provide the necessary incentives to reinvigorate the economy. Continued domestic policy efforts are key to sustained recovery. Without these programs, the costs to the general public would be much higher.

Fiscal crises are not a new phenomenon, and they will occur again in the future. A key task for policymakers is to put fiscal consolidation at the forefront of the national agenda and to address in a comprehensive way the downside risks in the budgets. On the revenue side, steps should be taken to reverse the precipitous decline in direct tax collections and to improve the buoyancy of indirect tax revenues by broadening the tax base and eliminating loopholes. Consolidation of assessment and collection responsibilities under one administration would have a significant positive impact on tax enforcement. On the expenditure side, the civil service wage policy should remain tight, and efforts should be made to reduce expenditures further through efficiency gains. To ensure a lasting reduction in government expenditures, these efforts should be complemented by an intensification of the implementation of the core-task analysis and the privatization program through a specified action plan. As the needed policies are implemented, confidence should recover, gradually paving the way to a rebound in growth.

Actions on the fiscal front will be complemented by an appropriate tight monetary policy. Up to June 1998, the maximum allowed credit growth to the private sector in the monetary cash reserve arrangement has been set at 2% over the amount outstanding at the end of September 1997. The ceiling on net domestic credit to the government has been maintained on the amount outstanding on October 31, 1996, to minimize monetization of the deficits. In addition, the Bank increased its reserve requirement from 3% to 4% in April 1998 to sterilize the excess reserves in the banking system and, hence, the risk of excessive credit extension. Monetary policy for the remainder of the year will be structured against the background of the fiscal program being pursued and developments in the external position.

Tight fiscal and monetary policies will create a solid foundation for restoring private sector confidence and mobilizing investments that could underpin a durable resumption of economic growth. To accelerate this process, a growth-promoting policy by the authorities is warranted. This policy should be set up along the lines of the Interamerican Development Bank report, "Policies and Strategies for Sustainable Growth in the Netherlands Antilles." The Bank's recommendations include labor market policies aimed at ensuring high employment through competitive and flexible wages and removing other rigidities in this area, tax reform, refocusing of public expenditures on core tasks, and measures directed at enhancing the overall business climate. To underpin the authorities' commitment to implement the recommendations, a clear plan with specific actions and an associated timetable should be developed. Such an approach will be critical to a successful reinvigoration of our economy and, hence, the much-needed creation of jobs to address the unacceptably high un-

employment rate of approximately 15%. To prevent a further increase in the unemployment rate it is estimated that 700 new jobs should be created annually.

The current structural imbalances in our economy pose an enormous challenge for policymakers. Countering the crisis is a considerable challenge that needs to be met by getting the structural adjustment process back on track and, hence, creating the necessary conditions for a renewal of economic growth and the strengthening of our foreign exchange reserves. Only through a viable and comprehensive adjustment program with clear objectives will we be able to overcome the financial-economic crisis and increase employment and living standards in the near future. The interrelationships between social and economic issues should be recognized during the adjustment period. The best social policy is a policy aimed at creating durable employment through sustainable growth.

## **2 DEVELOPMENTS IN THE REAL SECTOR**

### **2.1 General economic developments**

For two consecutive years, the performance of the Netherlands Antillean economy has been characterized by a contraction in production and high inflation. The overall weak economic performance was the net result of declining domestic demand, on the one hand, and improved performance of the external sector, on the other. Despite the intensification of protection policies from Europe vis-à-vis the Netherlands Antilles, namely, the introduction of the quota on agricultural products from the Overseas Countries and Territories (O.C.T.), the overall performance of the external sector improved. This improvement contributed positively to the balance-of-payments outcome. The positive development in the external sector, however, did not outbalance the decline in domestic spending. Furthermore, instability in producer confidence resulted in a decline in the volume of investment contributing to the 1.8% contraction in the GDP.

The high inflation of 3.1% in 1997 was the result of the higher indirect taxes implemented as part of the adjustment program. Inflationary pressure combined with the negative effects of producer confidence characterized developments in 1997. Lower real investment, as a result of producer confidence and less turnover, as a result of the reduction in domestic spending, led to a contraction in production. Consequently, employment opportunities declined, and the unemployment rate increased from 14.1% in 1996 to 14.9% in 1997.

#### ***2.1.1 National production and aggregate demand***

National production, as measured by the GDP, contracted by 1.8% in 1997. This decline was due to weak performances in practically all sectors, excluding the tourism, oil industry, and financial sectors. Total aggregate demand declined in 1997, as real consumption and investment were sluggish. The reduction in private consumption was the result of less disposable income due to reduced purchasing power and higher unemployment. The decline in the volume of private investments is attributable to less domestic activity and increasing uncertainty related to the unsustainable high budget deficit. Furthermore, the continuation of a tight monetary policy under the Monetary Cash Reserve of the Central Bank limited the financing sources for private investment. The increase in the volume of government investment was not sufficient to counteract the negative growth in the private investment. The lower private consumption and the reduction in government consumption, combined with sluggish private investments, resulted in the decline in overall aggregate demand in 1997.

### 2.1.2 Inflation

The annualized rate of inflation in the Netherlands Antilles, as measured by the consumer price index (CPI), decelerated from 3.4% in 1996 to 3.1% in 1997. The declining trend in the general price index can be attributed to the fading away of the effect of the 'sales tax' on the Leeward Islands combined with favorable import prices due to the strong U.S. dollar in the international market.

Mentioned effect is noticeable when comparing 1997 inflation rates with those in 1996 and analyzing the developments by island. Curaçao's, inflation rate in 1997 was 3.1% compared with 3.6% in 1996; Bonaire's was 2.3% in 1997 compared with 2.7% in 1996. Despite these downward trends, Curaçao still had a relatively high inflation rate of 3.1%. Together with St. Maarten, it has the highest rate of inflation in the Netherlands Antilles (table 1). Contrary to the developments in the Leeward Islands, prices accelerated in St. Maarten, where inflation rose from 2.3% in 1996 to 3.1% in 1997. This trend is explained largely by the effects of the introduction of the turnover tax in St. Maarten in the beginning of 1997.

**Table 2.1**  
**Inflation rates for Curaçao, Bonaire, and St. Maarten**  
**1996, and 1997 (% changes)**

	Curaçao		Bonaire		St. Maarten	
	1996	1997	1996	1997	1996	1997
Food	5.1	2.3	4.5	1.7	4.9	3.0
Beverage & tobacco	4.0	3.7	0.1	2.8	4.0	1.3
Clothing & footwear	-2.7	0.7	0.1	0.0	0.3	0.4
Housing	6.0	3.9	1.9	2.4	2.5	3.6
Housekeeping & furnishings	1.1	2.1	3.1	1.5	1.4	1.7
Health	1.5	3.3	5.7	3.8	1.4	0.1
Transport & communication	5.4	4.1	3.6	4.2	2.1	5.4
Recreation & education	0.7	2.5	0.9	1.9	0.6	2.5
Other	2.5	4.6	3.1	3.3	2.0	2.9
General inflation rate	3.6	3.1	2.7	2.3	2.3	3.1

A breakdown of the rate of inflation by item reveals a remarkable increase in the items "other" and "transport and communication" by 4.3% and 4.2%, respectively (table 2). The category "clothing and footwear" shows a relative low inflation rate of 0.6%.



**Table 2.2**  
**Inflation rates in the Netherlands Antilles in the years 1993 - 1997 (% changes)**

	1993	1994	1995	1996	1997
Food	3.0	2.8	5.3	5.0	2.4
Beverage & tobacco	3.1	1.5	2.5	3.8	3.4
Clothing & footwear	-0.3	-0.7	-3.2	-2.2	0.6
Housing	0.9	-0.5	3.3	5.3	3.8
Housekeeping & furnishing	1.8	5.3	3.7	1.3	2.0
Health	3.3	5.0	1.9	1.8	2.9
Transport & communication	3.2	1.9	2.4	4.9	4.2
Recreation & education	1.8	1.2	1.8	0.7	2.5
Other	2.0	3.9	2.3	2.5	4.3
General inflation rate	1.9	1.9	2.8	3.4	3.1

A breakdown of the rate of inflation by island shows similarity between islands: a substantial increase in the category "transport and communication" and a low inflation rate in the category "clothing and footwear" on all the islands (table 1). In Curaçao, the rates of inflation in the categories "other"<sup>1</sup> and "housing" were, respectively, 4.6% and 3.9%. The increase in the category "housing" can be attributed mainly to the increase in the energy prices. The item "clothing and footwear" increased marginally by 0.7%. In Bonaire, the highest price increases in 1997 were recorded in the items "transport and communication" and "health" by, respectively, 4.2% and 3.8%, the result of higher dentist fees and an increase in the prices of vehicles. In St. Maarten, the highest inflation rate in 1997 was measured in the category "transport and communication" (5.4%) as a result of the introduction of the turnover tax. The "health" sector and the category "clothing and footwear" showed relatively low inflation rates of 0.1% and 0.4%, respectively.

<sup>1</sup> Increase in insurance premia

### **2.1.3 Labor market**

In 1997, the developments in the Netherlands Antillean labor market deteriorated further as the estimated unemployment rate increased to 14.9%<sup>1</sup> in 1997 compared to 14.1% in 1996. This increase is the result of weak labor demand, resulting from the decline in economic activity, as compared to the increasing supply of labor. Furthermore, the labor market has been facing structural problems for years because of a qualitative discrepancy between demand and supply of labor. This discrepancy is the result of an increasing number of dropouts with a low educational level, contrasted with a growing demand for skilled labor especially in the financial sector.

In line with the decline in economic activities, the demand for labor was weak on all islands of the Netherlands Antilles in 1997. In Bonaire, reduced employment is a consequence of the weak economic activities. This development can be attributed mainly to the European Committee's decision regarding the quota on imports from O.C.T. into Europe. The rice industry in Bonaire especially was severely affected by this measure, causing a decline in the demand for labor. Bonaire's unemployment rate is estimated to have increased from 6.1% in 1996 to 7.5%<sup>2</sup> in 1997.

In Curaçao,<sup>2</sup> the unemployment rate rose from 14.0% in 1996 to 15.3% in 1997 (table 3), the highest level of unemployment recorded since 1990. The demand for labor was affected by the unfavorable developments in production as employment declined by 718 persons. The same trend in the labor market developments is underscored by the data<sup>3</sup> on requests for dismissal, which increased by 2% to 731 persons in 1997 compared to 717 persons in 1996. Similar to 1996, dismissals were concentrated in the construction sector and in the trade, hotel, and restaurant sector.

<sup>1</sup> *Estimate of the Bank van de Nederlandse Antillen*

<sup>3</sup> *The Central Bureau of Statistics conducted a labor force survey (AKO) in 1997*

<sup>4</sup> *Department of Labor and Social Affairs*

**Table 2.3**  
**Labor market**

	Curaçao		St. Maarten	
	1996	1997	1995 <sup>1)</sup>	1997
Total population	151611	152035	34861	36229
Labor force	66216	66380	20905	22827
Unemployed	9252	10134	2408	3931
Unemployment rate	14.0%	15.3%	11.5%	17.2%

<sup>1)</sup> *Ako February, 1995*

Source: Central Bureau of Statistics

In St. Maarten, the 1997 labor force survey (AKO) indicated a substantial increase in the unemployment rate to 17.2% compared to 11.5% (table 3) in the pre-hurricane period (February 1995).

## 2.2 Sectoral developments

### 2.2.1 Mining

The performance in the salt industry improved in 1997 compared to 1996: production expanded by 14.4% compared with a drop of 21.5% in 1996. Due to limited capacity in the industry and unfavorable weather conditions, salt exports declined further in 1997, by 9.3%, a worsening compared to the decline of 7.3% in 1996.

### 2.2.2 Industry

The performance in the oil sector was satisfactory in 1997, as its main activity in Curaçao, oil refining, went up by 15.6% relative to a decline of 1.3% in 1996. This improvement can be explained largely by increased labor productivity and favorable price developments in the international markets.

Furthermore, the related activities, i.e., oil storage and transshipment, also were buoyant, recording increases of 58.3% and 23.2%, respectively. The sharp increase in oil storage in 1997 must be seen in light of the low level in 1996, when a drop of 63.9% was recorded.

In line with developments in Curaçao, oil-related activities in Bonaire were favorable, reflected by expansions of 67.0% and 87.8% in oil storage and transshipment, respectively. This positive performance must be seen against the background of weak performance in 1996, when negative growth rates of 23.7% and 22.8%, respectively, were recorded.

In the ship repair sector, production activities, as measured by man-hours sold, declined in 1997 by 19% after an increase of 64.4% in 1996. The decline is the result of reduced foreign demand. Foreign exchange income from ship repair increased in 1997 by 18.8% which may indicate prefinancing of forthcoming activities.

### ***2.2.3 Utilities***

The overall performance in the utility sector in the Netherlands Antilles improved, as water and electricity production increased by 1.5% and 2.4%, respectively. Growth in electricity production implies an acceleration compared to the growth of 1.9% in 1996.

A breakdown by island reveals that a drop in water production occurred in St. Maarten, where a decrease of 1.6% was recorded. This represents a turnaround compared to 1996, when St. Maarten recorded a growth rate of 2.8%. In contrast to the downturn in St. Maarten, Bonaire's water production grew by 6.3% in 1997, which can be ascribed to a general annual growth. After a decline of 0.6% in 1995, followed by zero growth in 1996, water production in Curaçao grew by 1.8% in 1997. This growth in both Curaçao's and Bonaire's water production outbalanced the negative growth rate of St. Maarten, resulting in the overall expansion in total water production.

In addition to the increase in the Antillean water production, electricity production also grew. Analysis by island shows that electricity production in St. Maarten and Bonaire was up by 13.0% and 5.2%, respectively. Compared with 1996, this means a deceleration of 3.1 percentage points for Bonaire and an acceleration of 16.7 percentage points for St. Maarten. Curaçao's electricity production decreased by 0.5% in 1997, after growing by 2.9% in 1996.

### ***2.2.4 Construction***

According to the Bank's Business Cycle survey and in line with overall economic performance, activities in the construction sector declined in 1997 compared to 1996. In Bonaire, the value of completed construction projects declined by 10.7% in 1997 compared to 16.9% in 1996. Construction activities in Curaçao declined by 7.6%, in 1997 as indicated by the value of total licenses granted in 1996. The decline is particularly noticeable, in the nonresidential projects.

### ***2.2.5 Trade***

Free zone re-exports increased in 1997 by 41.2% compared with 4.3% in 1996. In 1997, the number of visitors declined, partly as a result of a slight change in the marketing strategy in this sector. Next to the policy of attracting visitors to the free zone, salespersons of companies in the free zone are

traveling abroad and offering their products to customers. Because of this strategy, a visible decline was seen in the number of visitors to the free zone. Other factors that affected the number of free zone visitors are the difficult economic situation and devaluation of the currencies of some of the countries from which free zone visitors originate (table 2.4).

**Table 2.4**  
**Rates of free zone related economies**

	Real GDP (%)	Annual inflation <sup>1)</sup> (%)	Exchange rate <sup>2)</sup> 1996	Exchange rate <sup>2)</sup> Dec. 1997
<b>Island</b>				
Jamaica	1	10	34.0J\$	34.8J\$
Dominican Republic	6	6.2	13.8Ps	14.6Ps
Trinidad & Tobago	4	3.1	6.14TT\$	6.2TT\$
Venezuela	4.7	39.4	474 Bol	500 Bol

<sup>1)</sup> End period

<sup>2)</sup> End of period for 1 US \$

Source: Latin American monitor Caribbean, Andean Group

Business activities in the trade sector worsened in 1997 when compared to 1996, according to the Business Cycle survey. The same trend was reported in a survey conducted by the Chamber of Commerce for the island of Curaçao. According to this survey, the largest decline in turnover was recorded, among other things, in the trade sector. The decline in activities is due mainly to the reduced domestic spending in the trade sector.

### **2.2.6 Tourism**

The tourism sector developed positively in 1997, as the number of stay-over and cruise tourists increased by 9.9% and 33.1%, respectively. Further analysis reveals a turnaround for stay-over tourism, when compared to the negative growth rates of 12.2% and 13.4%, respectively in 1995 and 1996. Foreign exchange income recorded a growth of 12.9% in 1997 compared to the decline of 2% in 1996. A breakdown by island shows that the largest growth in stay-over tourism was recorded on the island of St. Maarten, where the number of stay-over visitors expanded by 21.2% in 1997, following a decline of 21.1% in 1996 (table 5). In Bonaire and in Curaçao, stay-over tourism declined by 4.1% and 4.3%, respectively, in 1997.

**Table 2.5**  
**Developments in stay-over tourism (% growth)**

	Curaçao		Bonaire		St. Maarten	
	1996	1997	1996	1997	1996	1997
North America, of which:	-10.1	-5.6	7.2	-0.5	-29.0	32.6
-U.S.A.	-8.6	-3.0	5.1	1.6	-26.2	29.6
-Canada	-25.1	-35.2	63.4	-38.3	-48.6	61.2
Europe, of which:	-6.9	-6.1	13.8	-4.7	-9.4	9.7
-The Netherlands	-0.8	-7.3	21.1	-7.1	-5.3	24.6
-France	n.a.	n.a.	-48.3	2.3	-6.5	7.1
-Germany	-23.8	-7.5	-7.6	10.6	n.a.	n.a.
-Other	-34.9	7.3	11.0	-3.7	-23.1	13.2
South & Central America, of which:	-5.2	0.4	3.1	-8.3	-41.5	32.3
-Venezuela	-13.3	6.3	-6.0	-8.4	-5.9	67.4
-Brazil	12.8	-23.7	30.5	-15.7	-60.0	89.1
Caribbean, of which:	-3.4	-2.8	13.7	-14.0	7.1	3.2
-Aruba	-2.0	5.0	16.0	-14.5	n.a.	n.a.
-Santo Domingo	-14.1	-2.3	-30.7	-14.5	5.9	-0.2
Rest of World	27.7	-9.2	25.7	-27.7	3.5	7.6
Total	-4.2	-4.3	9.5	-4.1	-21.1	21.2

In St. Maarten, cruise as well as stay-over tourism expanded significantly. Stay-over arrivals turned around sharply, from a drop of 21.1% in 1996 to an increase of 21.2% in 1997. The drop in 1996 was related to the effects of the 1995 hurricanes, whereas the increase in 1997 was due mainly to the effects of the intensification of marketing efforts to promote this sector. A breakdown by markets reveals that the growth is attributable to the growth in the North American market (32.6%), the European market (9.7%), and especially in the Dutch market (24.6%). Cruise tourism in St. Maarten continued to expand, rising by 34.8% in 1997, compared to an increase of 16.5% in 1996.

In Curaçao, performance in the tourism industry was mixed in 1997: the number of stay-over tourists declined, and the number of cruise tourists grew. Competitive prices of new destinations affected stay-over tourism; it declined further by 4.3% in 1997, compared with a decline of 4.2% in 1996. Similar to 1996, the decline was mainly in the largest markets: the Netherlands (7.3%) and USA (3.0%). Cruise tourism grew by 24.1% in 1997, a significant increase when compared to the 0.8% increase in 1996.

In Bonaire, the number of total visitors declined by 4.1% in 1997 compared with a growth of 9.5% in 1996. The setback in stay-over tourism in 1997 was due mainly to competitive prices of new destinations, the postponements of "Avensa" flights (Venezuela), and the appreciation of the NAf. vis-à-vis the Dutch guilder. Moreover, the number of tourists staying less than 24 hours in Bonaire, as a share of the total number of visitors, dropped by 14.1%. The number of visitors from the Netherlands, South America, Aruba, and Canada declined by respectively, 7.1%, 8.3%, 14.5%, and 38.3%. Contrary to these negative developments, performance in the German market improved, as the number of visitors from this destination increased by 10.6% compared to -7.6% in 1996. Cruise tourism in Bonaire increased by 76.2% in 1997 compared with the increase of 8.1% in 1996.

### ***2.2.7 Transport and telecommunication***

The performance of the air transport was mixed. On the one hand, the number of passengers transported by the local airline, ALM, increased by 3.3% compared to 13.7% in 1996; on the other hand, freight declined by 23.6% in 1997 after growing 7.8% in 1996. The decline in freight can be explained partly, by the deceleration in growth in the number of passengers, particularly the free zone visitors. In Curaçao, the flow of transit passengers continued to expand; a growth of 10.4% was registered in 1997, compared to the increase of 6.4% in 1996.

Harbor activities also were mixed; the number of ships piloted into the harbor increased, while, the freight handled declined. An analysis by islands shows that the number of ships piloted into the harbor of Curaçao increased by 8.7%, and freight handling declined by 22.4% in 1997. In Bonaire, the number of ships piloted into the harbor increased by 13.2% in 1997 compared to the decline of 14.2% in 1996. A breakdown by type of vessel reveals that on both islands, the increase in the number of ships piloted into the harbor was the result of an increase in cruise ships and tankers. The decline in freight handled was the result of (1) the introduction of the quota on agricultural products from the O.C.T., which has limited the re-exports and freight handling in the harbor, and, (2) the lower imports of goods resulting from the depressed economy.

In the telecommunication sector, the Business cycle survey reports an overall increase in business activities in 1997 compared to 1996.

## **3 PUBLIC SECTOR AND DEVELOPMENT AID**

### **3.1 Major developments in the public sector**

Fiscal policy in 1997 must be seen against the background of continuing implementation of the structural adjustment program (SAP). In 1997 an agreement was reached with the IMF on performance targets and policy benchmarks within the SAP, among other things included in the "Memorandum of Economic Policies." The aim of the structural adjustment program is, among other things to correct the macroeconomic imbalances faced by the economy of the Netherlands Antilles. These imbalances are reflected in higher fiscal deficits and declining economic activities.

To curb domestic demand, new taxes were levied and credit extension to government was frozen. To complement the sales tax already in place in Curaçao and Bonaire as of July 1, 1996, a turnover

tax (BBO<sup>1</sup>) was introduced in the Windward Islands on January 1, 1997. On January 1, 1997, a self-assessment system for profit tax from enterprises was introduced. Together with other revenue-enhancing measures, these measures curtailed domestic demand, which in turn, slowed down economic growth. In 1997 import duties were lowered by 1 percentage point as of January 1997.

Despite the efforts made within the SAP, the government still runs a budget deficit and has a high public sector debt-ratio of close to 70% of GDP. Some improvement was noticeable in the deficit of the General Government<sup>2</sup>; it dropped from 3.6% of GDP in 1996 to 1.3% of GDP in 1997. This development was possible only because of postponement of certain obligations, because financing was extremely difficult in 1997. The reduction in the cash deficit must be interpreted cautiously, however, because it implies financing of expenditures by accumulation of arrears.

Economic activity continued to be weak, a development that impacted tax revenue growth. This weak economic activity occurred in part because of not simultaneously executing the second and third phases of the structural adjustment program, which are designed to reduce expenditures and to create incentives to revitalize the economy.

<sup>1</sup> The turnover tax became effective with an overall rate of 3% except for basic necessities, which are charged at a rate of 1%.

<sup>2</sup> General Government is defined here as the consolidation of the accounts of the Central Government and the Island Government of Curaçao.

## **3.2 Budgetary Overview**

### **3.2.1 General Government**

The budget balance (including foreign amortization) on a cash basis of the General Government improved from NAf.155.4 million in 1996 to NAf.55.1 million in 1997. This deficit, as a ratio of GDP, narrowed from 3.6% in 1996 to 1.3% in 1997 (table 3.1). This improvement in the budget deficit was possible mainly because of postponement of current obligations to, among other things, the civil servant pension fund (APNA). This deferment explains in part the large increase of NAf.172.8 million in domestic debt in 1997. Further analysis of the deficit reveals that the primary balance<sup>3</sup> improved from a deficit of 0.7% of GDP in 1996 to a surplus of 2.1% of GDP in 1997 (table 3.1.), but this development also must be seen against the background of an accumulation of payment arrears.

Total revenues of the General Government decreased by NAf.11.2 million (i.e., 0.3% of GDP), largely as a result of a NAf.46.4 million drop in nontax revenues and a NAf.34.7 million increase in tax revenues. The growth in tax revenues can be ascribed mainly to a NAf.111.2 million increase in taxes on goods and services. The introduced sales- and turnover tax contributed with NAf.85.9 to mentioned increase in the taxes on goods and services. In contrast, taxes on international trade and transactions dropped by NAf.40.4 million. This drop was partly because of the 1% reduction in import duties and the reduction in purchasing power that affected aggregate demand and imports.

Total expenditures dropped by NAf.111.5 million (7.7%) in 1997 when compared to 1996. This development is the result of a drop of NAf.93.1 million (6.8%) in current expenditures and a drop of

NAf.18.4 million (24.9%) in capital expenditures. The major category of the current expenditures that caused this lower spending level was wages and salaries. Wages and salaries dropped by NAf.104.2 million in 1997 when compared to 1996 mostly because of noncompliance with obligations to the civil servant pension fund (APNA) in the amount of NAf.78.1 million. When adjusted for these arrears, wages and salaries payments remained practically unchanged from 1996 to 1997. A drop of 8.6% (NAf.8.4 million) was measured in subsidies to public companies.

<sup>3</sup> *The primary balance is defined as the budget balance, excluding interest payments. The primary balance gives an indication of the deficit situation in the public sector in the absence of public debt. This concept is employed to better assess the impact of fiscal measures being implemented.*

**Table 3.1**  
**Budgetary overview of the General Government, 1995 - 1997 <sup>D</sup>**

	(in millions NAf.)			in % of GDP		
	1995	1996	1997	1995	1996	1997
<b>Revenues</b>	1235.2	1283.6	1272.4	29.6	30.0	29.4
-Tax revenues,	1016.8	1084.8	1119.5	24.3	25.4	25.9
of which:						
Taxes on income and profits	647.3	659.7	617.2	15.5	15.4	14.3
Taxes on property	31.5	34.4	41.0	0.8	0.8	0.9
Taxes on goods and services	148.9	219.9	331.1	3.6	5.1	7.7
Excises	115.3	138.3	148.6	2.8	3.2	3.4
Sales tax	0.0	41.8	127.7	0.0	1.0	3.0
Taxes on int. trade & trans.	182.9	162.2	121.8	4.4	3.8	2.8
-Nontax revenues	209.7	191.2	144.8	5.0	4.5	3.3
-Capital revenues	0.2	0.9	0.4	0.0	0.0	0.0
-Grants	8.5	6.7	7.7	0.2	0.2	0.2
<b>Expenditures</b>	1400.9	1439.0	1327.5	33.5	33.7	30.7
-Current expenditures	1353.6	1365.2	1272.1	32.4	32.0	29.4
Wages and salaries	693.2	702.2	598.0	16.6	16.4	13.8
Goods and services	325.8	297.0	300.9	7.8	7.0	7.0
Subsidies	77.2	97.8	89.4	1.8	2.3	2.1
Transfers	136.0	141.1	135.7	3.3	3.3	3.1
Interest payments	121.4	127.1	148.1	2.9	3.0	3.4
-Capital expenditures, of which:	47.3	73.8	55.4	1.1	1.7	1.3



Investments	53.6	41.9	48.7	1.3	1.0	1.1
Capital transfers	7.5	12.5	9.4	0.2	0.3	0.2
Net lending	-13.8	19.4	-2.7	-0.3	0.5	-0.1
Foreign amortiza- tion	37.6	0.0	0.0	0.9	0.0	0.0
Balance incl. amortization	-203.3	-155.4	-55.1	-4.9	-3.6	-1.3
Primary balance	-44.3	-28.3	93.0	-1.1	-0.7	2.1

<sup>1)</sup> The budget figures for 1995 are not totally comparable to the figures presented here for 1996 and 1997. In conformity with the structural adjustment program, the government now is reporting its revenues and expenditures on a "cash basis." The financial data for 1995 are from government accounts set up on an accrual basis.

Despite efforts<sup>4</sup> to cut expenditures on goods and services, a slight increase of NAf.3.9 million (1.3%) was registered in 1997 when compared to 1996. Total expenditures dropped by 2.6% of GDP to 30.7% of GDP in 1997.

<sup>4</sup> The Central Government intended to cut spending on goods and services by 35%

### **3.2.2 Budgetary overview of the Central Government**

The budget deficit (including amortization) on a cash basis of the Central Government improved by NAf.48.1 million to NAf.33.3 million in 1997. This improvement is the net result of a growth in revenues of NAf.44.3 million and a slight decrease in expenditures of NAf.3.8 million.

**Table 3.2**

#### **Budgetary overview of the Central Government, 1995 - 1997 (in millions NAf.)**

	<b>1995</b>	<b>1996</b>	<b>1997</b>
Tax revenues	321.8	372.7	441.3
Nontax revenues	146.8	118.6	93.5
Capital revenues	0.2	0.2	0.0
Grants	8.5	6.7	7.7
Total revenues	477.3	498.2	542.5
Current expenditures	522.4	530.0	535.9
Capital expenditures	19.7	49.6	39.9
Total expenditures	542.1	579.6	575.8
Balance incl. amortization	-77.5	-81.4	-33.3
Primary balance	-16.7	26.3	11.7

The increase in revenues of the Central Government to the amount of NAf.44.3 million can be ascribed to a rise of NAf.68.6 million in tax revenues, mitigated partly by a NAf.25.1 million drop in non-tax revenues. The major category in tax revenues that contributed to the increase in tax income was taxes on goods and services, which rose by NAf.100.3 million. A major contributor to this increase was the sales tax (BBO<sup>5</sup>) introduced on January 1, 1997, on the Windward Islands (St. Maarten, Saba, and St. Eustatius), which generated NAf.31.9 million. Together with the sales tax (ABB) already in effect in Curaçao and Bonaire since July 1, 1996, total income from the sales tax amounted to NAf.127.7 million in 1997. This substantial increase in tax revenues was mitigated partly by the lower import duties. Import duties fell by NAf.32.1 million in 1997 (table 3.3.). This development can be attributed to the lowering of the tariff by 1% on the one hand, and tax measures that have affected disposable income, on the other hand. Related to this development, household spending dropped.

Nontax revenues registered a drop of NAf.25.1 million in 1997. Of the different categories, entrepreneurial and property income fell the most by 27% (NAf.15.6 million).

<sup>5</sup>. *Turnover tax*

**Table 3.3**  
**Developments in the revenues of the Central Government (in millions NAf.)**

	1995	1996	1997
Total revenues	477.3	498.2	542.5
Tax revenues	321.8	372.7	441.3
Taxes on property	15.6	15.0	23.9
Inheritance and gift tax	7.1	2.1	4.8
Property transfer tax	8.5	12.9	19.1
Taxes on goods & services.	117.1	186.9	287.2
(excises)	115.3	138.3	148.6
Licenses	1.8	6.8	10.9
Sales tax	0.0	41.8	127.7
Taxes on int. trade & trans.	182.9	162.2	121.8
import duties	147.9	150.5	118.4
foreign exchange tax	32.1	9.2	0.1
Other taxes	6.2	8.6	8.4
Non-tax revenues	146.8	118.6	93.5
Entrepreneurial & property income.	84.4	57.7	42.1
Fees, charges, and sales	54.5	39.9	38.3
Other non-tax revenues	7.9	21.0	13.1
Capital revenues	0.2	0.2	0.0

Grants	8.5	6.7	7.7
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Total expenditures of the Central Government fell slightly in 1997. There were 0.7% (NAf.3.8 million) less expenditure outlays, the result of 19.6% less capital outlays (NAf.9.7 million) and an increase by 1.1% (NAf.5.9 million) in current expenditures in 1997 compared to 1996.

Higher current expenditures in 1997 were largely accounted for by increased outlays in the following two categories: interest payments (NAf.20.5 million) and goods and services (NAf.2.7 million). The categories wages and salaries dropped by NAf.11.2 million, subsidies to public companies fell by NAf.2.8 million, while transfers fell by NAf.3.3 million in 1997. Further analysis of the various components of the category 'wages and salaries' reveals that the drop of NAf.13.7 million in the government wage in 1997 was mainly because of the one-time settlement of retroactive payments based on equal pay for males and females in 1996. Furthermore, the Central Government accumulated arrears to the civil servant pension fund to the amount of NAf.14.1 million in 1997. The higher interest payment is the result of the rising indebtedness of the government (refer to section 3.5). Among other things, the Central Government paid NAf.4.2 million in interest on the loan to the civil servant pension fund APNA and the social security bank SVB because of the settlement of the debt of the Islands of Saba, St. Eustatius, and St. Maarten to mentioned institutions in 1996.

The NAf.9.7 million drop in capital expenditures can be ascribed largely to a decline of NAf.15.2 in net lending and a NAf.3.1 decrease in transfers to St. Maarten in connection with reconstruction activities following the hurricanes. These drops were mitigated partially by the higher investments in the amount of NAf.8.6 million. The lower net lending is the result of payments (NAf.10.0 million) received from Antelecom in anticipation of a bond issue by this company, amortization paid by OBNA in the amount of NAf.1.0 million, and NAf.5.2 less paid in 1997 on capital transfers to the airline company ALM.

**Table 3.4**  
**Developments in the expenditures of the Central Government (in millions NAf.)**

	1995	1996	1997
Total expenditures	542.1	579.6	575.8
Current expenditures	522.4	530.0	535.9
Wages and salaries	305.5	301.8	290.6
Wages	216.6	238.9	225.2
Soc. Security (SVB)	6.8	8.7	9.3
Pension premiums	82.1	54.2	56.1
Goods and services	93.3	89.9	92.6
Interest payments	48.1	54.4	74.9
Domestic	41.3	48.6	60.5
Abroad	6.8	5.8	14.4
Subsidies to public comp.	1.5	8.3	5.5

Transfers	74.0	75.6	72.3
Other levels of govt.	50.3	49.6	44.1
Households	8.5	8.8	7.2
Nonprofit institutions, abroad	15.2	17.2	21.0
Capital expenditures	19.7	49.6	39.9
Investments	20.7	26.1	34.7
Capital transfers	0.0	12.5	9.4
Net lending	-1.0	11.0	-4.2
Balance	-64.8	-81.4	-33.3
Foreign amortization	12.7	0.0	0.0
Balance incl. amortization	-77.5	-81.4	-33.3

### ***3.2.3 Budgetary overview of the Island Government of Curaçao***

The budget deficit on a cash basis of the Island Government of Curaçao (including amortization<sup>6</sup>) improved from NAf.74.0 million in 1996 to NAf.21.8 million in 1997. This decline in the cash balance by NAf.52.2 million in 1997 is to a great extent the result of NAf.103.8 million less current expenditures. This drop in expenditures was offset partly by a drawback of NAf.60.3 million in total revenues. The reduction in the cash deficit implies, however, the forced financing of the government deficit by accumulation of arrears to creditors, especially the civil servants pension fund (APNA).

The drop in total revenues reflects both lower tax and nontax revenues as well as fewer grants received. Tax revenues dropped by 4.8% (NAf.33.9 million), which to a large extent is attributable to a drop in wage taxes in 1997 in the amount of NAf.22.8 million when compared to 1996. In 1996, the wage taxes increased, in part because the Island Government of Curaçao and the Central Government settled the outstanding court-mandated wage payments related to the elimination of discrepancies in salaries based on gender. For 1997 these payments did not occur.

<sup>6</sup> *There were no foreign amortization in 1996 and 1997*

***Table 3.5  
Budgetary overview of the Island Government of  
Curaçao, 1995 - 1997 (in millions NAf.)***

	1995	1996	1997
Tax revenues	695.0	712.1	678.2
Nontax revenues	62.9	72.6	51.3
Capital revenues	0.0	0.7	0.4
Grants	28.9	23.5	18.7
Total revenues	786.8	808.9	748.6
Current expenditures	860.1	858.7	754.9

Capital expenditures	27.6	24.2	15.5
Total expenditures	887.7	882.9	770.4
Balance incl. amortization	-125.8	-74.0	-21.8
Primary balance	-27.6	-1.3	51.4

Revenue from profit taxes dropped by 1.9% (NAf.5.4 million) in 1997 when compared to 1996. This drop in the profit tax proceeds can be explained, among other factors, by a downturn in the business cycle and lower-than-expected profit tax receipts from Antelecom. The latter must be seen against the background of competition from international callback services. Profit taxes from the offshore sector seem to have stabilized. However, despite new efforts to improve direct tax revenues through the introduction in 1997 of the pay-as-you-file self-assessment system for the profit tax, total taxes generated from the business sector fell.

Nontax revenues dropped by NAf.21.3 million, attributable to a drop in entrepreneurial and property income by NAf.5.7 million, decreases in fees, charges, and sales in the amount of NAf.8.7 million, and a drop of NAf.6.9 million in other nontax revenues.

**Table 3.6**  
**Development in revenues of the Island Government of Curaçao**  
**(in millions NAf.)**

	1995	1996	1997
Total revenues	786.8	808.9	748.6
Tax revenues	695.0	712.1	678.2
-Taxes on income and profits	647.3	659.7	617.2
Profit tax	299.5	277.3	271.9
Wage tax	308.3	339.0	316.2
Income tax	39.5	43.4	29.1
-Taxes on property	15.9	19.4	17.1
Land tax	13.4	15.7	9.9
Occupancy tax	2.5	3.7	7.2
-Taxes on goods and services	31.8	33.0	43.9
Motor vehicle taxes	21.2	18.4	23.6
Licenses	8.4	11.6	16.3
Hotel room tax	2.2	3.0	4.0
-Other taxes	0.0	0.0	0.0
Nontax revenues	62.9	72.6	51.3
-Entrepreneurial & property income	40.8	24.0	18.3
-Fees, charges, and sales	17.5	28.9	20.2
-Other nontax revenues	4.6	19.7	12.8
Capital revenues	0.0	0.7	0.4

Grants	28.9	23.5	18.7
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Total expenditures recorded a substantial drop of NAf.112.5 million in 1997, as current expenditures dropped by NAf.103.8 million, and capital expenditures decreased by NAf.8.7 million. The overall wage bill of the Island Government of Curaçao dropped in 1997 by NAf.93.0 million compared to 1996. Wages dropped by NAf.23.2 million in 1997 mainly because of one-time payments paid in 1996 for the elimination of salary discrepancies based on marital status. Also, NAf.69.8 million less were paid for pension premiums in 1997 compared to 1996. In 1997 the Island Government of Curaçao accumulated further arrears in premiums to the civil servant pension fund (APNA) in the amount of NAf.64.0 by paying only premium obligations for half a year. Expenditures on goods and services remained practically unchanged.

**Table 3.7**  
**Developments in the expenditures of the Island Government of Curaçao (in millions NAf.)**

	1995	1996	1997
Total expenditures	887.7	882.9	770.4
Current expenditures	860.1	858.7	754.9
Wages and salaries	387.7	400.4	307.4
Wages	286.0	308.0	284.8
Pension premiums	92.7	92.4	22.6
Goods and services	232.5	207.1	208.3
Subsidies	75.7	89.5	83.9
Public companies	75.7	89.5	83.9
Transfers	90.9	89.0	82.1
To other levels of govt.	16.3	18.0	14.4
Households	46.2	40.8	38.8
Nonprofit institutions	28.4	30.2	28.9
Interest payments	73.3	72.7	73.2
Domestic	60.5	60.8	72.7
Abroad	12.8	11.9	0.5
Capital expenditures	27.6	24.2	15.5
Investments	32.9	15.8	14.0
Capital transfers	7.5	0.0	0.0
Net lending	-12.8	8.4	1.5
Balance	-100.9	-74.0	-21.8
Foreign amortiza-	24.9	0.0	0.0

tion			
Balance incl. amortization	-125.8	-74.0	-21.8

Subsidies decreased by NAf.5.6 million in 1997, and transfers also dropped by NAf.6.9 million. Investment expenditures dropped by NAf.1.8 million in 1997, while net lending fell sharply by NAf.6.9 million. These drops resulted in a drop in capital expenditures of NAf.8.7 million in 1997 compared with the level in 1996.

### 3.3 Financing the deficit of the Governments

The deficits of both the Island Government of Curaçao and of the Central Government were financed almost entirely nonmonetarily in 1997. This must be seen against the background of the tightening of monetary policy. Since March 1995, a ceiling has been put on the level of net domestic credit to the governments. This policy was continued in 1997 whereby outstanding credit extended by commercial banks to the governments was frozen at the amount outstanding at the end of October 1996. Therefore, both governments had to rely on nonmonetary sources to finance their budget deficits.

**Table 3.8**  
**Financing of the budget balance of the Governments (in millions NAf.)**

	Central Government			Curaçao		
	1995	1996	1997	1995	1996	1997
Budget Balance	77.5	81.4	33.3	125.8	74.0	21.8
Monetary financing	-8.4	-13.6	2.7	-60.6	-11.0	-9.8
Central Bank	-1.5	3.7	6.0	1.9	11.2	-3.5
Commercial banks	-8.8	-18.8	-3.3	-36.6	51.1	-6.3
Giro Curaçao	1.9	1.5	0.0	-25.9	-73.3	0.0
Coins and Notes	0.0	0.0	0.0	0.0	0.0	0.0
Nonmonetary financing	85.9	95.0	30.6	186.4	85.0	31.6
Loans with the public	156.1	78.7	27.9	92.5	88.4	24.3
Advance by Curaçao	0.0	23.6	-23.6	0.0	0.0	0.0
Other	-70.2	-7.3	26.3	93.9	-3.4	7.3

Both the Central Government and the Island Government of Curaçao financed their deficits predominantly through the issuance of securities with the public.

### 3.4 Public sector debt and guarantees

An analysis of the debt situation of the Netherlands Antilles revealed that the budget problem is essentially one of high and increasing domestic debt<sup>7</sup>. A centralized monitoring and a mandatory publication of the debt figures should enhance transparency in both the debt situation and its development.

Some of the recommendations of the van Lennep Committee were included in the "Memorandum of Economic Policies" concluded in 1997 with the IMF. The aim of the Structural Adjustment Program (SAP) is to secure lasting improvements in the public finances, restore confidence in the government, and realize the foreign exchange reserves target of three months of imports.

Because of the problems encountered during the execution of the budget in 1997, execution of the Structural Adjustment Program, as contained in the Memorandum of Economic policies, encountered a considerable delay.

As shown in table 3.9, the total debt of the Netherlands Antilles increased by NAf.81.3 million in 1997, the result of an increase of NAf.172.8 million in the domestic debt and a drop of NAf.91.5 million in the foreign debt. In 1997 only marginal changes occurred in the total outstanding foreign debt of the Netherlands Antilles, denominated in Dutch guilders, when compared with the development in the debt in previous years. When considering the foreign debt in Antillean guilders, however, a drop of 13.8% was registered, reflecting the appreciation of the Antillean guilder against the Dutch guilder in 1997 compared to 1996.

<sup>7</sup> The debt-committee headed by the late Mr. Van Lennep presented its report that addresses the debt problem of the Netherlands Antilles and Aruba, January 1996.

**Table 3.9**  
**Total public debt <sup>1)</sup> and guarantees (in millions NAf.)**

	1995	1996	1997	% changes	
				1996	1997
Domestic debt	2049.9	2170.2	2343.0	5.9	8.0
Foreign debt	724.1	662.5	571.0	-8.5	-13.8
Total debt	2774.0	2832.7	2914.0	2.1	2.9
(% of GDP)	66.4	66.3	67.3		
Guarantees	391.7	385.6	352.3	-1.6	-8.6
Total debt & guarantees	3165.7	3218.3	3266.3	1.7	1.5
(% of GDP)	75.8	75.3	75.5		

<sup>1)</sup> This is defined as the total outstanding securities, debt on the advance account at the Central Bank, overdraft at the commercial banks, debt at the Giro, arrears to creditors, APNA, and SVB.



Total estimated outstanding guarantees dropped by NAf.33.3 million due to redemption of loans and the appreciation of the Antillean guilder against major European currencies in which the guarantees were denominated.

Table 3.10 gives an overview of the composition of the domestic debt. Major factors that contributed to the rise in domestic debt were increased government securities with the public in the amount of NAf.52.3 million and increased payment arrears in connection with the contribution to the civil servant pension fund (APNA).

**Table 3.10**  
**Composition of public sector domestic debt (end of year, in millions NAf.)**

<b>Public Sector Domestic Debt</b>	<b>1995</b>	<b>1996</b>	<b>1997</b>
<b>Central Government</b>			
Central Bank	53.9	52.5	65.0
-advance account	16.7	17.2	29.8
-securities	37.2	35.3	35.2
Commercial bank credit	0.0	0.0	0.0
Commercial bank securities	88.0	83.0	88.9
Government securities with the public	478.6	610.2	638.2
Social Security Bank (SVB)	64.9	78.1	83.6
Civil servants pension fund (APNA)	6.1	22.0	36.1
Other government levels	n.a	25.0	25.7
Arrears	0.0	12.2	21.0
Other debt	30.8	27.4	23.8
<b>Total</b>	<b>722.3</b>	<b>909.0</b>	<b>976.6</b>
<b>Curaçao</b>			
Central Bank	30.0	0.0	0.0
Commercial bank credit	0.0	0.0	0.0
Commercial bank securities	104.2	158.5	142.8
Giro Curaçao	73.3	0.0	0.0
Government securities with public	252.6	345.9	370.2
Social Security Bank (SVB)	10.0	9.2	21.1
Civil servants pension fund (APNA), of which:	499.2	527.3	623.7
-arrears	147.7	146.0	210.0
-zero-coupon bond	351.5	381.3	413.7
Arrears to other creditors	249.0	179.2	154.7

Total	1218.3	1220.1	1312.5
<b>Other Islands</b>			
Social Security Bank (SVB)	51.8	24.1	30.0
Civil servants pension fund (APNA)	57.5	42.0	49.6
Total	109.3	66.1	79.6
TOTAL (consolidated)	2049.9	2170.2	2343.0
% of GDP	49.1	50.8	54.1

### 3.5 Development aid

Development aid assistance to the Netherlands Antilles, which originates from the Dutch Government, reached a total of Hfl.234.3 million (grants) in 1997. Concessional loans can be granted in the case of projects by government entities like utility companies. Of mentioned Hfl.234.3 million that was received Hfl.190.2 million (81.2%) can be categorized as official development assistance.

The use of these funds, mostly for government project and, as administrated by the Department of Finance of the Central Government, is summarized in table 3.11.

**Table 3.11**  
**Expenditures on governmental projects (in millions NAf.)**

	1995	1996	1997
<b>Governmental projects</b>			
Central Government	12.8	15.9	28.1
Curaçao	52.8	46.2	42.0
Bonaire	8.6	1.6	1.1
St. Maarten	5.7	45.1	33.9
St. Eustatius	2.4	1.5	1.1
Saba	2.3	2.1	5.9
General	0.2	0.0	3.8
Total	84.8	112.4	115.9

*Source: Department of Finance, Central Government*

With regard to aid from the European Community, the government currently is deliberating with the authorities for the VIII European Development Fund (EDF), which will involve ECU.37.0 million. The agreement for this VIII EDF for the period 1995 to 2000 has still not been finalized.

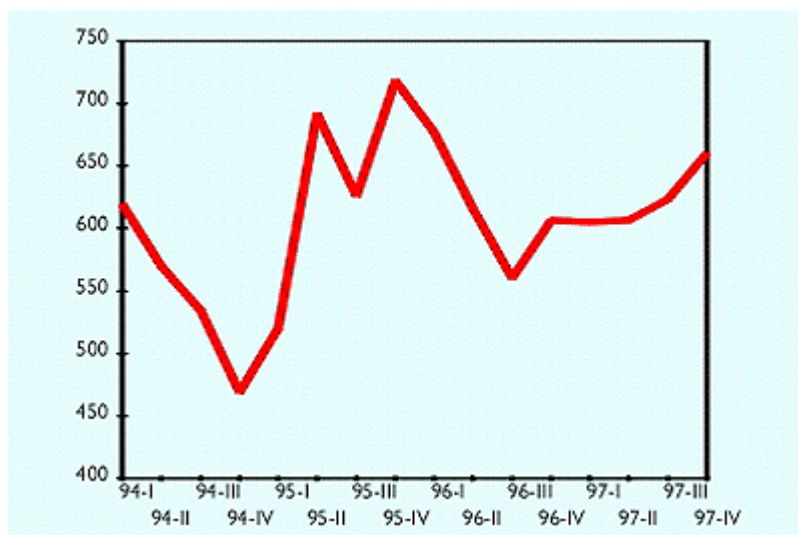
## 4. THE EXTERNAL SECTOR

### 4.1 Introduction

Developments in the external sector were influenced both by the restrictive measures taken by the government to resolve deficit problems and by the tight monetary policy of the Bank. Both of these factors had a contractionary impact on the spending capacity of consumers, which dropped by 3.5% in real terms. As a consequence, the demand for imports was weak, thereby improving the trade balance. Furthermore, developments in the external sector in 1997 were influenced to a great extent by improved performance in the tourist sector. The balance of payments showed a surplus of NAF.53.6 million (1.3% of GDP) in 1997 compared to a deficit of NAF.92.2 in 1996.

Net international reserves increased to NAF.660.2 million in 1997, the result of a NAF.44.5 million expansion in the official reserves and an increase of NAF.9.1 million in the foreign exchange reserves held at the commercial banks. (graph 4.1)

**Graph 4.1**  
**Developments in the net international reserves (in millions NAF)**



As shown in table 4.1, the significant improvement in the current account explains almost entirely the increase in the net international reserves. As a percentage of the GDP, the deficit in the current account dropped by 5 percentage points to 5% in 1997.

**Table 4.1**  
**Balance of payments summary <sup>1)</sup> (in millions NAf.)**

	1995	1996	1997	Diff. 97-96
Current account	-29.9	-422.5	-207.9	214.6
Capital account	134.7	325.6	271.7	-53.9
Statistical discrepancies	3.4	4.7	-10.2	-14.9
Balance of payments	108.2	-92.2	53.6	145.8
Change in reserves <sup>2)</sup>	-108.2	92.2	-53.6	-145.8
-with commercial banks	-12.4	14.0	-9.1	-23.1
-with Central Bank	-95.8	78.2	-44.5	-122.7
Memorandum items				
Official reserves (excl. gold)				
-in millions NAf.	416.5	338.3	382.8	44.5
-in months of merch. im- ports	2.1	1.7	1.8	0.1
Total reserves (excl. gold)				
-in millions NAf.	509.3	417.1	470.7	53.6
-in months of merch. im- ports	2.4	1.9	2.3	0.4

<sup>1)</sup>Cash basis

<sup>2)</sup>Sign denotes an increase in reserves (excluding gold)

## 4.2 The current account

The current account of the balance of payments improved by NAf.214.6 million to a deficit of NAf.207.9 million. As illustrated in table 4.2, the improvement in the current account was the result of

- a substantial drop in the level of imported goods, as a result of, among other things, the deficit-reducing measures taken by the government;
- higher earnings of approximately NAf.135 million from the tourism and transportation sectors.

**Table 4.2**  
**A breakdown of the current account <sup>1)</sup> (in millions NAf.) <sup>2)</sup>**

	1995	1996	1997	Diff. 97-96
Trade balance	-2168.3	-2217.9	-2016.1	201.8
-Exports	377.1	403.0	480.2	77.2
-Imports	2545.4	2620.9	2496.3	-124.6
Services balance	2214.3	1788.3	1820.1	31.8
-Receipts, of which:	3282.9	2912.5	2880.2	-32.3
-Transportation	557.5	609.6	612.7	3.1
-Travel	1004.5	984.0	1115.5	131.5
-Int. fin. & bus. services sector	800.3	712.9	671.6	-41.3
-Expenditures	1068.6	1124.2	1060.1	-64.1
-Travel	397.2	455.9	455.3	-0.6
-Int. fin. & bus. services sector	200.1	244.9	208.8	-36.1
Income balance <sup>3)</sup>	31.0	113.4	87.1	-26.3
-Receipts	208.7	241.8	182.3	-59.5
-Expenditures	177.7	128.4	95.2	-33.2
Unrequited transfers <sup>4)</sup>	-106.9	-106.3	-98.9	7.4
-Receipts	150.0	171.1	204.3	33.2
-Expenditures	256.9	277.4	303.2	25.8
Current account balance	-29.9	-422.5	-207.9	214.6

<sup>1)</sup> Cash basis

<sup>2)</sup> The 1995 services balance includes approximately NAf.300 million received from indemnity payments related to the hurricane damages.

<sup>3)</sup> Income : investment and labor income.

<sup>4)</sup> Unrequited transfers: private remittances (excl. labor income and life insurance).

#### **4.2.1 The trade balance**

The trade balance improved by NAf.201.8 million in 1997, compared to 1996. This improvement of the merchandise balance was attributable to lower non-oil-related imports (6.2%) and considerable growth in exports (19.2%). An analysis of non-oil-related imports by island reveals that the improvement in the merchandise balance was concentrated primarily in Curaçao and on the Windward Islands. Curaçao's merchandise balance improved by NAf.111.6 million as a result of higher exports and lower imports, while the Windward Islands recorded an improvement of NAf.77.0 million in their trade account, due primarily to lower imports.

Non-oil-related imports decreased overall by just NAf.4.5 million on Curaçao. However, if adjusted for imports for free zone-related activities, the decline amounts to NAf.98.5 million. This decline is

related primarily to the drop in domestic spending, as evidenced by the drop in imports by the wholesale and retail sectors (excluding the free-zone companies) of approximately NAf.104 million. The decline in imports on Curaçao was balanced by substantial higher exports of NAf.114.6 million (36.7%). The growth in exports was related almost entirely to the re-exporting activities of some of the main free zone companies. In contrast, the rice- and sugar-exporting industries stopped their operations, following the European Council's decisions concerning the agreement with overseas countries (LGO).

The NAf.13.2 million improvement in Bonaire's trade deficit was primarily the result of lower imports. The decline of NAf.18.5 million in imports was related to weak domestic demand resulting from the various income-reducing measures introduced by the Central Government in 1997. The drop in the merchandise exports of NAf.5.5 million was due mainly to lower exports of salt in 1997.

The Windward Islands recorded a substantial improvement in their trade balance in 1997, as compared to 1996, due mainly to lower imports. As expected, the turnover-tax introduced on January 1, had a contractionary impact on the domestic spending capacity on the Windward Islands. The reduction in non-oil-related imports of approximately NAf.116.1 million on the Windward Islands, was the highest of any of the Netherlands Antilles.

Table 4.3 gives a breakdown of imports by main sectors for 1995 through 1997.

**Table 4.3**  
**Non-oil merchandise imports by main sector <sup>1)</sup> (in millions NAf.)**

	<b>1995</b>	<b>1996</b>	<b>1997</b>	<b>Diff. 97 -96</b>
Manufacturing	123.5	127.9	119.6	-8.3
Utilities	67.7	104.8	59.5	-45.3
Construction	35.6	42.7	33.3	-9.4
Wholesale & Retail (excl. Freezone)	1113.5	1092.2	988.1	-104.1
Transp. & Telecomm.	69.4	94.5	87.9	-6.6
Community, Social Ser- vices	36.7	51.7	54.5	2.8
Other	483.6	445.5	383.5	-62.0
Free zone-related im- ports	272.5	271.0	364.9	93.9
Total non-oil merchan- dise imports	2202.5	2230.3	2091.3	-139.0

<sup>1)</sup>Cash basis

## 4.2.2 The services balance

Developments in the service balance were characterized by a reticent domestic and foreign demand. Consequently, the surplus in the services balance increased by NAf.31.3 million in 1997. This increase was largely the result of a significant drop of NAf.64.1 million in payments for foreign services, due to weak domestic demand. This development, however, was mitigated partly by the weak performance of the foreign exchange-generating services sectors, which declined by NAf.32.3 million. The only sector that recorded an improvement was the tourist sector. Foreign exchange earnings from the international financial and business services sector dropped for the second consecutive year, although less than initially anticipated.

As shown in table 4.4, the composition of earnings from the services sector has remained the same in recent years. The tourist sector and the international financial and business services sector remain the main contributors to our foreign exchange reserves.

**Table 4.4**  
**Composition of earnings from the services sector (in percentages)**

	1993	1994	1995	1996	1997
Tourism	40	41	31	34	39
Int.fin. & bus. services sector	27	23	24	24	23
Other services, of which :	67	64	55	56	62
-Transportation	33	36	45	44	38
-Refining fee	16	16	17	21	21
-Telecommunication	11	10	8	9	7
Total earnings of services sector	2	1	2	1	1
	100	100	100	100	100

### 4.2.2.1 Tourism

The tourist sector, as projected, performed far better in 1997 than in 1996. As can be seen in table 4.5, the foreign exchange receipts from the tourism sector in the Netherlands Antilles as a whole increased by 11.8%.

**Table 4.5**  
**Foreign exchange revenues from tourism per island<sup>1)</sup> (in millions NAf.)**

	1994	1995	1996	1997
Bonaire	58.0	66.1	75.8	79.1
Curaçao	333.9	314.0	332.0	358.9
Windward Islands	751.5	624.4	576.2	677.5
Netherlands Antilles	1143.4	1004.5	984.0	1115.5
Percentage growth	4.9%	-12.1%	-2.0%	11.8%

<sup>1)</sup>Cash basis

An analysis by island shows that the foreign exchange generated from the tourism industry on the *Windward Islands* increased by 15% (NAf.101.3 million) in 1997. Underlying this development is the buoyant performance in the number of stay-over visitors, which expanded by 21%. Furthermore, cruise tourism also increased significantly in 1997.

The strong development in tourism activities on the Windward Islands was supported by positive developments on the Leeward Islands. The foreign exchange earnings on Bonaire continued their upward trend, as foreign exchange revenues from tourism activities increased by NAf.3.3 million (4.2%). This performance was reflected primarily in the 76% growth in cruise tourism. In addition, Curaçao recorded a good performance following a disappointing year: foreign exchange revenues rose by NAf.26.9 million (7.5%) in 1997, despite the 4.3% drop in the number of stay-over tourists. As was the case on Bonaire, cruise tourism showed a significant growth on Curaçao of approximately 24% in 1997 compared to 1996.

While tourism receipts increased, expenses by residents abroad remained fairly stable, considering the marginal decline by NAf.0.6 million compared to 1996. Concomitant with this development, expenditures on passenger's fares to foreign carriers also increased by 9% in 1997.

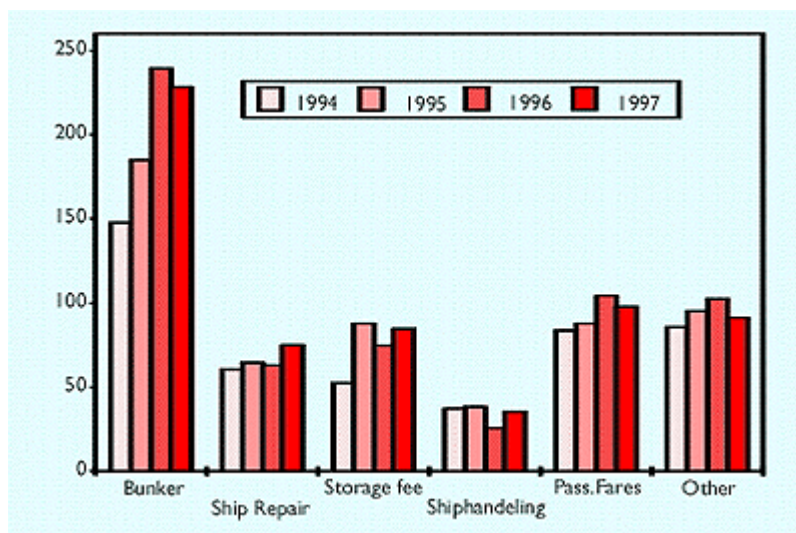
#### 4.2.2.2 Transportation

The transportation sector recorded a fair performance (graph 4.2). Foreign exchange earnings from transportation activities increased slightly by NAf.3.1 million in 1997 compared to 1996. The receipts from the ship repair industry and storage activities recorded a combined NAf.22.1 million increase. These developments were offset, however, by a drop of NAf.11.1 million (4.5%) and NAf.6.4 million (6.1%) in bunker activities and passenger fares, respectively.

Overall payments for transportation services received from abroad decreased by NAf.13.2 million in 1997, despite a NAf.3.3 million increase in the expenses on passenger fares to foreign carriers.

#### **Graph 4.2**

***Developments in foreign exchange generation in the transportation sector by branch of industry (in millions NAf.)***



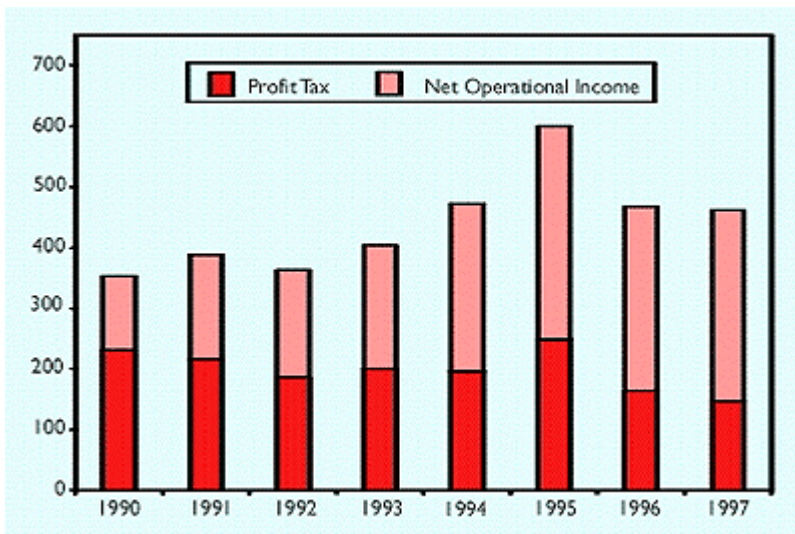


#### 4.2.2.3 *The international financial and business services sector*

Foreign exchange earnings from the international financial and business services sector recorded a net drop of NAf.5.2 million in 1997, compared to 1996. This drop can be explained largely by a deterioration of NAf.41.3 million in foreign exchange earnings from this sector. This decline can be broken down into a drop of NAf.17.1 million in profit tax receipts, and a decline of NAf.24.2 million in operational income. Foreign exchange outflow in this sector dropped considerably in 1997 by NAf.36.1 million, partly mitigating the net foreign exchange loss. Despite this net loss, the international financial and business services sector remains the second largest contributor to our foreign exchange-generating capacity.

#### **Graph 4.3**

***Development in the international financial and business services sector (in millions NAf.)***



#### 4.2.2.4 *The refining industry*

Compared to 1996, foreign exchange earnings from the refining industry decreased by nearly NAf.62 million (23%) in 1997. The reason for this significant decline can be attributed to the refinery policy. The main objective of the refinery management is to increase the competitive position of the refinery through improved efficiency in its production process. Because approximately 75% of foreign exchange receipts from the refinery company Petroleos de Venezuela cover operational costs of the refinery, this efficiency operation implies less foreign exchange revenue for the Netherlands Antilles.

#### 4.2.2.5 The 'other services' sector

'Other services' including telecommunication services, also showed a significant weakness in 1997. Telecommunication services experienced a substantial drop of NAF.17.6 million in foreign exchange revenues generated in 1997 compared to 1996. Developments in telecommunications activities worldwide and competition from abroad partly explain the drop in foreign exchange receipts.

#### 4.2.3 The income balance

The income account of the balance of payments recorded a surplus of NAF. 87.1 million in 1997, a drop of NAF.26.3 million compared to 1996. This decline can be ascribed to both the net investment income and the net labor income. As table 4.6 reveals, the decrease in the investment income balance was the result of a substantial decline in receipts from investments abroad, mitigating the drop in return on investments transferred to nonresidents.

**Table 4.6**  
**Breakdown of the income account <sup>1)</sup> (in millions NAF.)**

	1995	1996	1997	Diff. 97 - 96.
Investment income	25.4	100.3	88.1	-12.2
-Direct investment income	-80.6	-26.4	-32.8	-6.4
Received	4.1	23.2	10.2	-13.0
Paid	84.7	49.6	43.0	-6.6
-Other investment income	106.0	126.7	120.9	-5.8
Received	193.1	195.3	161.9	-33.4
Paid	87.1	68.6	41.0	-27.6
-Labor income	5.6	13.1	-1.0	-14.1
Received	11.5	23.3	10.2	-13.1
Paid	5.9	10.2	11.2	1.0
Balance	31.0	113.4	87.1	-26.3

<sup>1)</sup>Cash Basis

The drop in investment income receipts was the result of a decline in interest income and dividends received of approximately NAF.38 million by insurance companies and pension funds. On the other hand, interest payments by resident companies to their parent companies decreased by almost NAF. 30 million, thus mitigating the negative impact of lower return on foreign investments.

The drop in the labor income balance was the result of lower receipts. In the beginning of 1996, many foreign workers were contracted for the reconstruction process on the Windward Islands and were paid with foreign funds.

### 4.3 The capital account

The surplus in the capital account of the balance of payments fell by NAf.54.2 million to NAf.271.7 million in 1997, compared to 1996. This development can be attributed entirely to a deterioration in the private capital balance.

#### 4.3.1 The private capital balance

Table 4.7 shows that the deterioration of NAf.61.5 million in the private capital balance was the result of the drop in net borrowing activities, mainly by the commercial banks from abroad (NAf.84.4 million). Overall, commercial banks and private sector borrowing taken together, the net loan balance fell by NAf.54.4 million in 1997. Contrary to this development, net portfolio balance improved by NAf.72.4 million as a result of a substantial increase in the repatriation of short-term investments by institutional investors. A specific development in the financial market in 1997, which influenced the repatriation of funds, was that the government pension fund encountered liquidity problems due to the sustained arrears by the Central Government. Consequently, the fund had to liquidate some of its foreign funds to cover operational expenses.

#### 4.3.2 The official capital balance

The official capital balance increased by NAf.7.3 million, primarily as the result of more receipts of Dutch aid. The foreign amortization payment due for 1997 to the Dutch Government also was deferred, because of the liquidity shortage the governments were facing in 1997.

**Table 4.7**  
**Major components of the capital account <sup>D</sup> (Net flows in millions NAf.)**

	1995	1996	1997	Diff.
Private capital	65.3	214.9	153.4	-61.5
of which:				
-direct investm.(real estate)	-0.9	12.1	25.1	13.0
-portfolio investm.(sec.)	-30.3	-54.7	17.7	72.4
-loans (net)	-43.3	13.1	43.1	30.0
-comm. banks borrowings	-10.4	82.0	-2.4	-84.4
-other private capital	150.2	162.4	69.9	-92.5
Official capital	69.4	111.0	118.3	7.3
of which:				
-loans & grants	73.8	114.3	125.6	11.3
-other gov. capital	-4.4	-3.3	-7.3	-4.0
Balance	134.7	325.9	271.7	-54.2

<sup>1)</sup> *Cash basis*

## **5 MONETARY DEVELOPMENTS**

### **5.1 Introduction**

During 1997 monetary policy in the Netherlands Antilles was conducted against the background of the structural adjustment program (SAP) aimed at re-establishing internal and external equilibrium in the medium term. The SAP stipulated binding performance criteria for both fiscal and monetary policy. The criteria for monetary policy entailed, among other things, a maximum allowed growth in net domestic assets (NDA) and a minimum required growth in net international reserves. The main instrument of monetary policy for the Bank is the monetary cash reserve arrangement, which includes a progressive penalty system aimed primarily at limiting excessive credit extension to the private sector.

For net domestic credit to the private sector, a penalty-free growth rate of 3.5% was set for the October 31, 1996, to December 31, 1997, period. The target for net domestic credit by commercial banks to the General Government was set at the October 31, 1996, level, implying a zero growth for 1997. As agreed in the SAP, the establishment, of a sinking fund at the Central Bank, in which both the Central Government and the Island Government of Curaçao would deposit a total of NAf.40 million during 1997, would have meant (combined with the zero-growth provision) a drop in NDC to the General Government of NAf.40 million.

Domestic credit extension to the private sector contracted slightly during 1997, mainly as a result of the weak domestic demand due to the less favorable economic conditions. As neither government managed to raise the funds to be deposited in the sinking fund, NDC to the General Government dropped by only NAf.3.1 million instead of the targeted NAf.40 million. The combined effect of these developments was that the net domestic assets of the banking system remained well below their maximum allowed value.

In an effort to reduce the excess liquidity in the banking system, the Bank increased the reserve requirement for the commercial banks from 2% to 3% in August 1997. This is to reduce the risk of excessive credit extension.

For 1998 the Bank will maintain the October 1996 balance as the limit for net domestic credit to the General Government. The Bank will continue to monitor domestic credit extension to the private sector very closely during 1998 to keep its growth in line with economic growth.

## 5.2 Developments in the money supply and in the money-creating process

### 5.2.1 Money supply

During 1997, the money supply increased by 2.6% (NAf.64.7 million) compared to a decrease of 2.5% (NAf.65.6 million) during 1996. This development was primarily the result of the marked turnaround in the growth rate of the money component of the money supply.

As shown in table 5.1, the money component of the money supply increased by 2.3% (NAf.23.8 million) in 1997, compared to a 7.5% (NAf.83.4 million) contraction in 1996. This development can be attributed to turnarounds in both the growth rate of demand deposits in local currency and the growth rate of demand deposits in foreign currency.

The former changed from a 5.3% (NAf.38.1 million) contraction to a 3.1% (NAf.20.7 million) expansion and the latter from a 16.0% (NAf.30.3 million) contraction to a 7.1% (NAf.11.2 million) expansion. Coins and Notes with the public contracted by 4.3% (NAf.8.2 million) during 1997 compared to a 7.2% (NAf.14.9 million) contraction during 1996. On an annual basis the amount of coins and notes with the public has been falling for eight consecutive quarters. This development reflects the increasing use of debit cards and other electronic and computer-linked instruments in our payments system.

**Table 5.1**  
**Developments in the money supply and its components (in millions NAf. and percentage changes)**

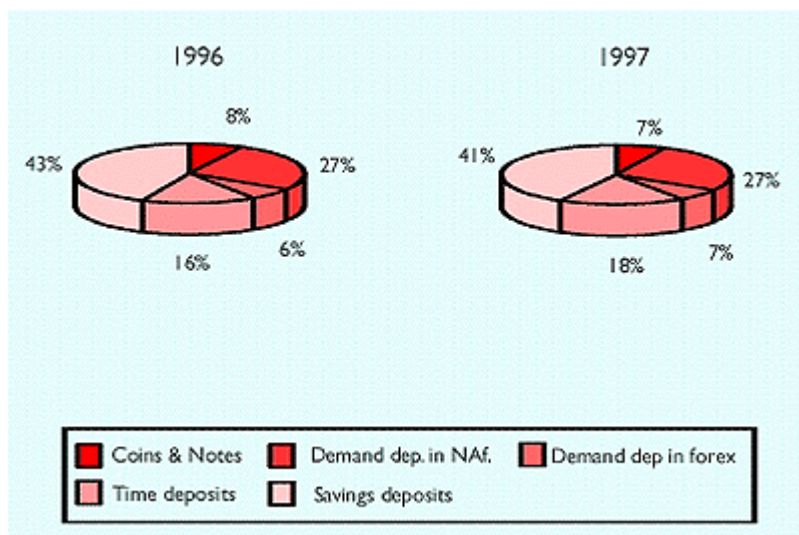
	1996		1997	
Coins & notes with the public	191.6	(-7.2%)	183.4	(-4.3%)
Demand deposits in:				
-Neth. Ant. guilders	674.1	(-5.3%)	694.8	(3.1%)
-Foreign currency	158.7	(-16.0%)	169.9	(7.1%)
Money (M1)	1,024.3	(-7.5%)	1,048.1	(2.3%)
Time deposits	410.0	(14.5%)	463.1	(13.0%)
Savings	1,098.5	(-3.0%)	1,086.3	(-1.1%)
Near money	1,508.5	(1.2%)	1,549.4	(2.7%)
Money supply (M2)	2,532.8	(-2.5%)	2,597.5	(2.6%)

The near-money component of the money supply recorded a 2.7% (NAf.40.9 million) increase during 1997, compared to a 1.2% (NAf.17.8 million) increase in 1996. This acceleration in the growth of the near-money component of the money supply can be explained by the development in savings deposits, which contracted by 1.1% (NAf.12.2 million), a slower pace compared to the 3.0%

(NAf.34.2 million) contraction in 1996. During the two years ending December 1997, the level of savings dropped by NAf.46.4 million. This marked decrease during that two-year period is the combined result of the slowdown in economic activities in the Netherlands Antilles, the rise in the cost of living on the Netherlands Antilles since the introduction of a sales tax on July 1, 1996, and the continuing efforts of the tax office to speed up the collection of tax arrears. Time deposits grew by 13.0% (NAf.53.1 million), a 1.5 percentage point deceleration compared to 1996.

Graph 5.1 reveals an increase by 2 percentage points to 18% in the share of time deposits in the composition of the money supply. This increase was mainly at the expense of the share of savings deposits, which dropped by 2 percentage points to 41%. The increase in the share of time deposits, which are held by institutions, may be a reflection of the reticent attitude of firms towards other investments due to uncertainties related to, among other things, the public finances.

**Graph 5.1**  
***Developments in the composition of the money supply***



### ***5.2.2 Factors affecting the demand for liquid assets***

During 1997, the growth in the demand for liquid assets expanded by 2.6% (NAf.64.7 million) a turnaround compared to the 2.5% (NAf.69.9 million) contraction in 1996. This development was induced entirely by the marked turnaround in the growth rate of our net foreign assets from a 26.9% (NAf.193.4 million) contraction to a 10.6% (NAf.55.8 million) expansion. The increase in our net foreign assets during 1997 is almost entirely the net result of a surplus of NAf.271.7 million in the capital account of the balance of payments on the one hand, and a deficit of NAf.207.9 million in the current account of the balance of payments on the other. The impact of domestic factors on the demand for liquid assets decelerated from a 6.6% (NAf.123.5 million) expansion in 1996 to a 0.4% (NAf.9.0 million) expansion in 1997. This drop in the growth rate can be attributed mainly to the turnaround in credit extension to the private sector from a 6.8% (NAf.145.4 million) expansion during 1996 to a 0.6% (NAf.12.7 million) contraction during 1997. Latter development, especially if seen against a background of a permissible growth rate for credit extension to the private sector of

3.5% for 1997, reflects the reticent attitude of economic agents towards borrowing mainly due to our weak economy and uncertainties surrounding the government finances.

Net domestic credit to the General Government contracted by 1.8% (NAf.3.0 million) during 1997 compared to a 14.0% (NAf.26.8 million) contraction during 1996. The contractionary impact during 1997 was the net result of a contraction by NAf.5.8 million in the demand for liquid assets by the island governments on the one hand and an increase by NAf.2.8 million in the demand for liquid assets by the Central Government on the other. Net domestic credit to the General Government was targeted to drop by NAf.40 million during 1997, primarily as a result of the creation of a sinking fund at the Central Bank of which the proceeds would be used for the financing of early retirement of civil servants. As neither government succeeded in depositing any funds in the sinking fund, the targeted level for NDC to the General Government as per end December 1997 was exceeded by NAf.37.0 million.

The increase in the demand for liquid assets by the Central Government during 1997 resulted from the increase in the net liabilities of the Central Government at the Central Bank by NAf.6.1 million on the one hand, and the decrease in the net liabilities of the Central Government at the commercial banks by NAf.3.3 million on the other. The amount of Central Government paper held in portfolio by the commercial banks increased from NAf.83.0 million at the end of 1996 to NAf.88.9 million at the end of 1997.

The contraction in the demand for liquid assets by the island governments resulted from an increase by NAf.3.5 million in their net deposits at the Central Bank on the one hand and a rise by NAf.0.7 million in their net liabilities at the commercial banks. The amount of government paper issued by the Island Government of Curaçao decreased from NAf.158.5 million at the end of December 1996 to NAf.142.8 million at the end of 1997. This 9.6% contraction reflects among other things the reluctance of commercial banks to refinance these financial titles based on uncertainties related to the finances of the Island Government of Curaçao.

**Table 5.2**  
**Developments in the demand for liquid assets by sector (in millions NAf. and percentage changes)**

	1996		1997	
Central Government	72.5	(-13.6%)	75.3	(3.9%)
Island governments	91.7	(-14.4%)	85.9	(-6.3%)
Private sector	2,275.7	(6.8%)	2,263.0	(-0.6%)
Miscellaneous	-431.7	(-1.1%)	-407.0	(-5.7%)
Domestic sector	2,008.2	(6.6%)	2,017.2	(0.4%)
Net foreign assets	524.6	(-26.9%)	580.4	(10.6%)
Total liquid assets	2,532.8	(-2.5%)	2,597.5	(2.6%)

### 5.3 Domestic credit extensions by commercial banks

During 1997 domestic lending to the private sector by the commercial banks<sup>1</sup> expanded by 0.1% (NAf.2.4 million) compared to a 7.3% (NAf.149.8 million) expansion during 1996 (see table 5.3). This development can be explained primarily by the drop of 9.7 percentage points to 4.0% (NAf.13.8 million) in the growth rate of mortgages. Consumer loans contracted by 5.8% (NAf.29.7 million) during 1997, a marked turnaround compared to the 4.5% (NAf.21.9 million) expansion during 1996. Business loans contracted by 0.4% (NAf.3.4 million) compared to a 2.6% (NAf.20.6 million) expansion during 1996.

<sup>1</sup> *I.e. domestic credit as reported in the previous paragraph excluding the items securities and participations by the commercial banks and amount receivables.*

**Table 5.3**  
**Domestic loans at commercial banks**  
**(per end of period in millions NAf.)**

	1996		1997	
Private sector loans,	2,196.2	(7.3%)	2,198.6	(0.1%)
of which:				
-Mortgages	890.2	(13.7%)	925.7	(4.0%)
-Consumer loans	507.7	(4.5%)	478.1	(-5.8%)
-Business loans	798.2	(2.6%)	794.8	(-0.4%)

A breakdown of commercial bank's private sector lending by island group reveals that the 7.2 percentage points drop in the growth rate of total lending during 1997 resulted from marked decreases in the growth rate of lending on both the Leeward and the Windward Islands.

**Table 5.4**  
**Domestic loans at commercial banks on the Leeward Islands (per end of period in millions NAf.)**

	1996		1997	
Private sector loans,	1,662.1	(4.9%)	1,670.9	(0.5%)
of which:				
-Mortgages	622.4	(9.7%)	644.2	(3.5%)
-Consumer loans	386.5	(1.7%)	366.1	(-5.3%)
-Business loans	653.1	(2.5%)	660.6	(1.2%)

Table 5.4 reveals a growth rate of 0.5% (NAf.8.8 million) for total lending to the private sector on the Leeward Islands during 1997 compared to a growth rate of 4.9% (NAf.77.5 million) in 1996. This deceleration can be ascribed primarily to the turnaround in consumer loans from a 1.7% expansion during 1996 to a 5.3% contraction during 1997, a development in line with a contracting economy. Further, the growth in mortgages and business loans decelerated by 6.2 percentage points to



3.5% and by 1.3 percentage points to 1.2%, respectively, during 1997. The drop in the growth rate of mortgages reflects the marked contraction (17.2%) in the value of licenses granted for residential projects on Curaçao during 1997.

On the Windward Islands, the outstanding loans to the private sector contracted by 1.2% (NAf.6.4 million), compared to a 15.7% (NAf.72.3 million) expansion in 1996. Turnarounds in the growth rate of both consumer loans and business loans and a marked deceleration in the growth rate of mortgages caused this development. The comparison between 1996 and 1997, however, must be seen in light of the substantial increases especially in mortgages and consumer loans during 1996 related to the reconstruction activities on St. Maarten, a consequence of damages caused by two major hurricanes in September 1995.

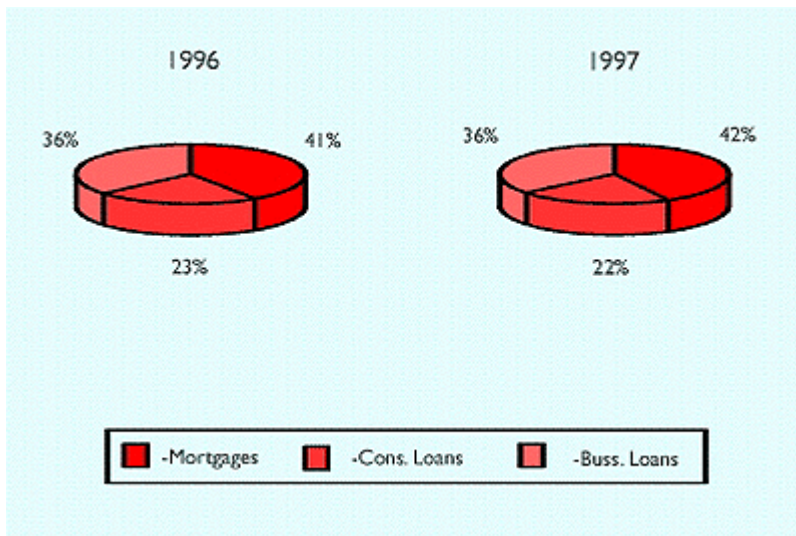
**Table 5.5**  
**Domestic loans at commercial banks on the Windward Islands (per end of period in millions NAf.)**

	1996		1997	
Private sector loans,	531.1	(15.7%)	527.7	(-1.2%)
of which:				
-Mortgages	267.8	(24.4%)	281.6	(5.1%)
-Consumer loans	121.2	(14.4%)	112.0	(-7.6%)
-Business loans	145.1	(3.2%)	134.1	(-7.5%)

### **5.3.1 Developments in the lending portfolio of commercial banks**

Graph 5.2 reveals an increase of 1 percentage point to 42% in the share of mortgages at the expense of the share of consumer loans. The decrease in the share of consumer loans reflects the reticent attitude of consumers due to the sagging economy and the reluctance of commercial banks to extend loans to consumers.

**Graph 5.2**  
**Developments in the lending portfolio of commercial banks**



## 6 DOMESTIC FINANCIAL MARKET DEVELOPMENT

### 6.1 Introduction

In 1997 the general government had increasing difficulty financing its deficit. As a result of this constraint and the crowding-out effects of private investments, the interest rates on government securities were gradually raised, which resulted in an upward shift of the yield curve. The banking sector reacted to this development by gradually reviewing its overall interest rate structure.

In December the Parliament of the Netherlands Antilles approved legislation to deduct interest income generated from investment in local government securities and savings from the calculation of the taxable income for individuals and business entities. With this, the government intended to make its securities more attractive to the general public and the financial sector.

In August the Bank further tightened its policy stance by increasing the reserve requirement rate to 3% of the adjusted domestic debt, thereby mopping up an additional NAf.20 million to NAf.63.6 million from the money market. The policy must be seen against the background of the agreements with the IMF under the structural adjustment program (SAP) to mitigate the potential negative effects of domestic liquidity overhang on the balance of payments. As a result of this policy change, the reserve deposits at the Central Bank averaged NAf. 50.3 million during 1997.

The liquidity in the banking sector, as measured by the demand deposits of commercial banks at the Central Bank, averaged NAf. 59.9 million<sup>1</sup>.

<sup>1</sup> For the purpose of calculating the liquidity ratio of commercial banks, the reserve deposits were included in the liquidity of banks as of August, due to the amendment in the reserve requirement rate (table 6.1)

## 6.2 Financial instruments and the money markets

During 1997 the average monthly amount of CDs outstanding was NAf.5.9 million, substantially less than the 1996 average. The reaction of the banks on the CD-instrument was weak because banks chose to increase their operating cash balances instead of participating in the CD facility.

In July of 1997 the Bank introduced a new interest scheme for certificates of deposit (C.D.s) to make the CD-facility more attractive to commercial banks. The interest rates of the BNA C.D.s were linked up to the US dollar target fed fund rate. The new interest mechanism provides local commercial banks with investment opportunities of one, three, and six months. The new yield structure of the offered CD facilities has now been fixed<sup>2</sup>.

The objective of this policy was to offer local banks investment opportunities with returns tied to US money market yields. Given that the Antillean guilder is pegged to the US dollar, the linkage of local short-term returns of investable funds to the US market supports the foreign exchange policy objective of the Bank.

<sup>2</sup> *One-month CD: target FED-funds rate minus 175 basis points*  
*Three-month CD: target FED-funds rate minus 150 basis points*  
*Six month CD: target FED-funds rate minus 100 basis points*

**Table 6.1**  
**Outstanding balances of certificates of deposits, and commercial bank reserve requirement at the Central Bank in 1997 ( In millions NAf.)**

	Certificates of deposit	Reserve requirement at the BNA	Demand of bank deposits at the BNA
January	-	39.8	65.5
February	-	40.4	58.5
March	9	40.1	57.4
April	6	40.4	69.0
May	8	42.7	54.7
June	13	42.3	49.4
July	13	42.6	44.7
August	5	63.3	55.9
September	2	62.8	56.1
October	8	62.5	62.6
November	6	62.8	49.3
December	1	63.6	96.0
Total average	5.9	50.3	59.9

### 6.3 The market for government bonds

Demand for government securities<sup>3</sup> declined by 34.6% during 1997 when compared to 1996 net government borrowings (refer to table 6.2). Subsequent to the extraordinary gross borrowing of the general government during 1996 of NAf. 194.6 million, investor confidence declined, as investors, amongst others, became increasingly skeptical about the government's ability to reduce its deficits by means of expenditure reductions. As per year-end 1997, gross general government bond issuance amounted to NAf.151.4 million, of which NAf.99.1 million were to refinance maturing securities. This implies that the net borrowing amounted to NAf.52.3 million during 1997. Investor preference for Central Government paper became more pronounced as 72.9% of the net borrowing was for the Central Government.

During 1997 the Central Government's net borrowing amounted to NAf.38.1 million (table 6.2). This borrowing was particularly concentrated with private placements, which grew by NAf.28.5 million. Furthermore, public issues of Central Government securities increased by NAf 20.7 million to NAf.401.0 million.

The Central Government has been confronted by liquidity problems due to increases in its budget deficit. The liquidity deficit was financed partly by the accumulation of arrears with APNA and through postponement of payment of the revenue-sharing agreements with the Island Government of Curaçao. Investor reluctance to finance increasing deficits, combined with limited opportunities to increase revenues, leaves the Central Government with few options but to reduce its budget deficit in the coming years to limit a liquidity crisis.

In the primary market, the Central Government issued benchmark 10-year bonds and reopened existing longer term bond issues with the objective of promoting secondary market liquidity and achieving a more efficient maturity structure for government debt.

<sup>3</sup> *Excluding APNA debt conversions*

**Table 6.2**  
**Domestic capital market borrowing by**  
**the Central Government (outstanding**  
**amounts, in millions NAf. per year end)**

	1995	1996	1997
Central Government			
Private placement	86.3	115.3	143.8
Public issues	359.0	380.3	401.0
Treasury bills	72.5	72.9	61.8
Subtotal	517.8	568.5	606.6
Debt conversions	86.0	160.0	155.8
Total	656.7	728.5	762.4
Net capital market borrowing <sup>1)</sup>	47.2	50.7	38.1

<sup>1)</sup> *Excluding issuance and redemptions of debt conversions.*

The reduced demand for government securities aggravated the increased deficit problems of the Island territory of Curaçao that led Curaçao to continue accumulating arrears with APNA. Curaçao's inability to finance its increased liquidity shortage in the money and capital markets, combined with the arrears with APNA, leaves Curaçao with few alternatives but to concentrate on further reducing its expenditures.

**Table 6.3**  
**Domestic capital market borrowing by the Island Government of Curaçao (outstanding amounts, in millions NAf. per year end)**

	1995	1996	1997
CURAÇAO			
Private placement	144.1	178.1	189.2
Public issues	205.8	221.0	219.1
Treasury bills	37.0	17.1	22.1
Subtotal	386.9	416.2	430.4
Debt conversion		88.2	82.5
Zero coupon bonds	351.7	381.3	413.7
Total	738.6	885.7	926.6
Net capital market borrowing <sup>1)</sup>	99.2	29.3	14.2

<sup>1)</sup> *Excluding issuance and redemptions of debt conversions.*

Curaçao's debt<sup>4</sup> increased by NAf. 40.9 million during 1997. This increase in net borrowing by Curaçao conceals the fact that some NAf. 64 million was incurred of arrears to APNA to finance its budget deficit.

Table 6.4 reveals that of the total government bonds issued in the local financial market<sup>5</sup> during 1997, 28.7% had a maturity of up to two years. Securities ranging from two to five years comprised 34.6% of the issues, while 36.7% had maturities of over five years. The share of outstanding longer-term securities dropped from 42.9% in 1996 to 36.7% in 1997.

<sup>4</sup> *Including APNA zero-coupons*

<sup>5</sup> *Excluding APNA debt conversions*

**Table 6.4**  
**Maturity structure of total outstanding**  
**government securities in 1997 <sup>1)</sup>**

	0-2 years	2-5 years	over 5 years	Total
Netherlands Antilles	22.0%	39.1%	38.9%	100.0%
Island Gov- ernment of Curaçao	38.6%	27.8%	33.6%	100.0%
Total	28.7%	34.6%	36.7%	100.0%

<sup>1)</sup> Excluding APNA zero-coupon bond but including estimated wage equalization and indexation bonds.

However, if the maturing zero-coupon bond is included in the loans of the island government of Curacao, the Curaçao loans maturing within two years grow from 38.6% to 66.0%. This zero-coupon bond will mature in September 1998 at a value of NAf.436.2 million. Thus the zero-coupon bond accounts for a major part of the outstanding loans of the public sector.

Table 6.5 shows the distribution of domestic government bonds outstanding excluding the Curaçao zero-coupon bond. Individual investors increased their holdings by 8.2% points to 18.5% of bonds outstanding. This increase can be attributed to the higher yields on government bonds relative to alternative interest-bearing instruments, and the governments', issuing of wage equalization and indexation bonds to civil servants.

The trend witnessed in 1996 of institutional investors diversifying their portfolios by purchasing fewer general government securities and participating more actively in the mortgage and real estate market, continued in 1997. After two years of bond market share increases, the share of general government bonds held by institutional investors decreased by 7.1% points to 67.8%. Institutional investors are sceptical about the governments' willingness to reduce expenditures and hence reduce the budget deficits.

Commercial banks' portfolio of government bonds declined from 14.8% to 13.7% during 1997. This decline of 1.1% points was less pronounced than the decline of 3.9% points during 1996 as the commercial banks purchased (short-dated) bonds from their clients while not renewing some maturing treasury bills. As stated in the Bank's 1996 annual report, commercial bank holdings of the mentioned securities are not expected to increase as long as the present monetary policy stance (MCR <sup>6)</sup> limits net lending to the public sector to a specific fixed ceiling.

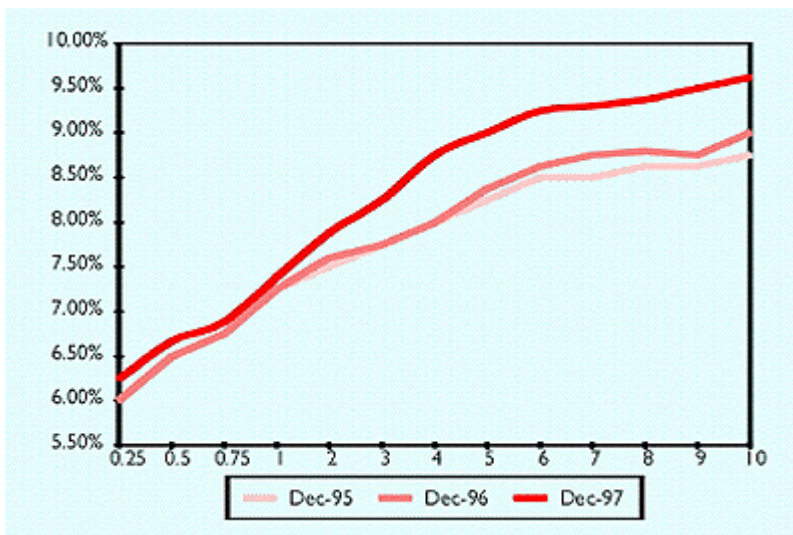
<sup>6</sup> Monetary Cash Reserve

**Table 6.5**  
**Holding of government securities, 1994 - 1997 (in %)**

	1994	1995	1996	1997
Institutional investors	64.0	71.4	74.9	67.8
Commercial banks	22.8	18.7	14.8	13.7
General public	13.2	9.9	10.3	18.5

Even though U.S. government notes and bond yields declined between 23 and 72 basis points during 1997, domestic government interest rates increased between 12.5 and 62.5 basis points in 1997. Domestic money market yields increased by 12.5 to 25 basis points as the U.S. Federal Reserve increased its Fed funds target rate on March 31, 1997, by 25 basis points to 5.50% after not having altered this target rate during 1996. The US yield-curve flattened, i.e., money market yields increased while longer term yields declined; in contrast the domestic yield-curve steepened.

**Graph 6.1**  
**Yield curve for domestic government securities**



The basis for the domestic yield-curve steepening was that longer term domestic bond yields increased by 37.5 to 62.5 basis points while short-term yields increased by only 12.5 to 25 basis points. The steepening of the domestic yield curve indicates that despite the fact that alternate US dollar-fixed income investment yields are declining, investors in Netherlands Antillean government securities are demanding higher yields to compensate for the perceived increase in risk of holding Netherlands Antillean government papers.

## 7. INTERNATIONAL AND REGIONAL DEVELOPMENTS

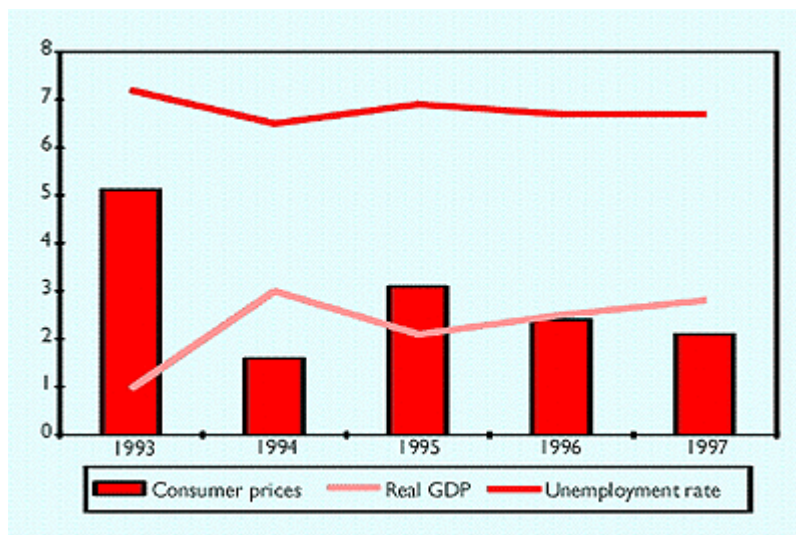
### 7.1 Introduction

International stock markets plummeted in October of 1997 as the Asian area was hit by a financial crisis. The economies of the United States and the United Kingdom showed unexpected strong growth, while optimism about the Japanese recovery is gathering momentum.

Noteworthy developments concerning EMU include the growing determination of European Union governments to start EMU on time with widespread participation, and the British decision not to join the first wave. The GDP of the 15 nations of the EU expanded by 0.6% in the fourth quarter of 1997, after slowing down to 0.7% in the third quarter. The fourth quarter deceleration of growth was due to the stagnation of most of the components of demand, with only consumption contributing to the GDP growth. The economy of the European Union recorded a growth of 2.6% for the entire year of 1997.

The overall growth for the industrial world remained favorable with real GDP expanding 2.8% in 1997 compared to a 2.5% growth rate in 1996. This growth can be attributed to the strong growth of the United States and the United Kingdom. The growth is expected to continue in 1998, but at a slower pace of 2.5%. Inflation remained stable at around 2.2% during 1997, ending the year at 2.1%. Spare capacity was large in much of the area, in particular in continental Europe and Japan. In continental Europe, consumer prices were very low at around 1.5%, and they are not expected to increase much in 1998. Japan's inflation rate remained around 0.5% during 1997. However, both the US and the UK economies face considerable inflationary uncertainty as demand pressures are expected to ignite inflation.

**Graph 7.1**  
**Selected OECD Major Seven economic key figures (% changes)**



The unemployment rate also remained at around 6.6%-6.7% during 1997, ending the year 6.7%.



Although a moderation of world growth is likely to occur at some point in 1998, it is expected that the current expansions can be sustained possibly into the next decade.

## **7.2 Economic performance in the Netherlands**

### ***7.2.1 Introduction***

The GDP of the Netherlands expanded in 1996 according to the revised national accounts. This growth is expected to continue at this pace until 1998. Furthermore, a tightening of the monetary policy in 1998 is expected to prevent the Dutch economy from overheating. Consequently, a tight monetary policy will trigger a gradual slowdown in business activity. The GDP growth rates are expected to be higher in 1998 than in 1997 because of the negative impact of the swine fever epidemic on the Dutch output in 1997. With strong economic fundamentals such as contained inflation, dropping unemployment rates, and expansion in economic activities, the Netherlands have no problem qualifying for participation in the EMU scheduled to commence on January 1, 1999.

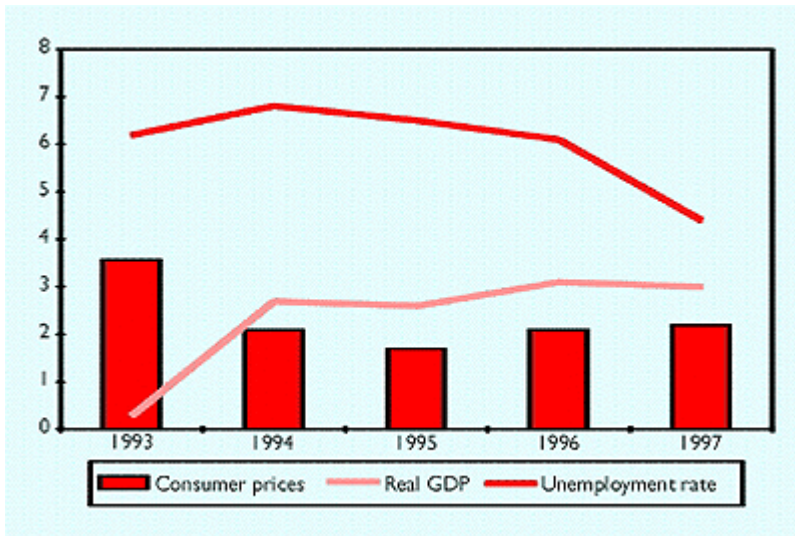
### ***7.2.2 Developments in 1997***

The Dutch economy expanded by 3.0% in 1997 compared to a growth rate of 3.1% in 1996. The economic growth picked up particularly in the fourth quarter due to strong consumer spending as a result of favorable consumer confidence. The Dutch economy expanded 1.0% in the fourth quarter of 1997 compared to the previous quarter. The growth recorded in consumer spending is the largest growth in the last six years. Investment also expanded during 1997 mainly in residential areas, for business construction, and in the machinery sector. The 1997 annual growth is comparable to the 1996 economic expansion, despite the outbreak of the swine fever that influenced the growth negatively during 1997. The Dutch economy has now expanded for almost 20 consecutive quarters, excluding a fall in the first quarter of 1995.

Contrary to the stable economic growth of the Dutch economy, industrial production decelerated from 4.9% in 1996 to 2.7% in 1997. This slowdown in production growth can be attributed to worsened business confidence during the last months of 1997, which made producers less optimistic about output expansion. However, in December of 1997, industrial sales surged by 13%, indicating that production will be picking up during the first months of 1998.

The Dutch unemployment rate fell to a five-year record low in the last quarter of 1997, because the economy continued to open new job opportunities at a near-record pace. The unemployment rate dropped from 6.1% in 1996 to 4.4% in 1997.

**Graph 7.2**  
**Selected economic key figures of the Netherlands (% changes)**



Many economists expected that the record low unemployment rate would induce employees and unions to push for higher wages. However, the Dutch economy continued to boost productivity and create jobs while keeping inflation low, thereby reducing the need for higher wage demand. Also the practice of limiting wage demand in exchange for job creation, shorter workweeks, and other employees benefits kept inflation under control. Consumer prices remained almost constant increasing only slightly from 2.1% in 1996 to 2.2% in 1997.

Dutch producer prices declined more than expected in the month of December of 1997 as oil prices declined, allaying inflation concern even though 1997 was the most expensive year for producers. Producer prices more than doubled from 1.2% in 1996 to 2.9% in 1997. This growth was due primarily to the increase in export prices, especially in base metal and metal product industry.

### 7.3 Economic performance in the United States

#### 7.3.1 Introduction

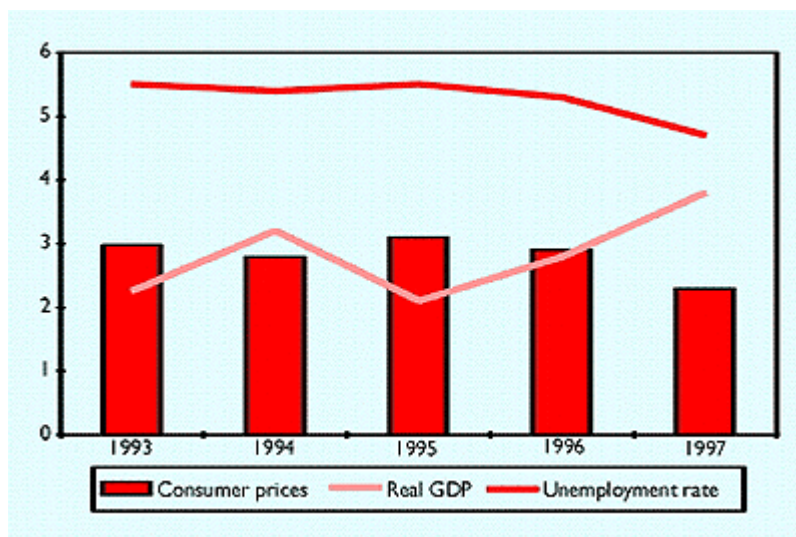
The US economy grew at an above average-trend for three consecutive quarters in 1997, slowing down to a more sustainable pace in the fourth quarter of 1997. Given that the unemployment rate is falling, the continued strong growth is expected to provoke the Federal Reserve Bank to tighten monetary policy action in the future. Higher interest rates, coupled with a strong dollar and a weakening of some exports markets, resulted in a GDP growth rate of 3.8% in 1997. GDP growth is expected to slow down to 2.4% in 1998 and to 2% in 1999. Furthermore, growth is expected to average about 2.4% during the period 2000- 2001.

### 7.3.2 Developments in 1997

As noted, the US is experiencing a strong growth during the first three quarters of 1997, the US economic growth slowed down in the fourth quarter of 1997. This slowdown occurred because the Asian financial crisis, began to impact the US economy. Corporate profits dropped for the first time in more than a year. The slowdown in the fourth quarter of 1997 contributed to an average year-end growth of GDP of 3.8%, lower than previously anticipated. Despite this development, GDP growth was the strongest in nine years, due mainly to consumer spending and higher spending on housing.

Concomitant with the growth of the US economy, the unemployment rate continued its decreasing trend in 1997, dropping from an average of 5.1% in the first half of 1997 to an average 4.7% in the second half of 1997. On an annual basis, the unemployment rate dropped from 5.3% at the end of 1996 to 4.7% at the end of 1997. Due to the low unemployment rate, labor costs rose to their highest level in five years during the fourth quarter of 1997, which could indicate that inflation will start rising in 1998.

**Graph 7.3**  
**Selected economic key figures of the United States (% changes)**



Contrary to expectation and despite the substantial economic expansion in 1997, the inflation rate was lower during 1997 with a year-ending rate of 2.3% compared to a rate of 2.9% at the end of 1996. This decrease in the inflation rate can be attributed to decreasing energy prices, transportation tariffs, and foods cost, which dropped especially in December of 1997.

Producer prices also showed a declining trend in 1997, with a deceleration in prices more substantial than with consumer prices. Producer prices decelerated from 2.7% at the end of 1996 to 0.4% at the end of 1997. This deceleration can be attributed to lower energy prices, on the one hand and to a weaker demand for oil from the Asian countries, on the other. The effects of the plunge in the Asian currencies also resulted in lower prices paid by the businesses sector for imported goods from this region.

## 7.4 Economic performance in Venezuela

### 7.4.1 Introduction

The Venezuelan economy recorded a growth of 4.3% in 1997 ending a long period of poor economic performance. A turnaround again is expected, however, in 1998 due to restrained consumption. In real terms, the external sector is expected to remain healthy as the expansion of oil exports will outbalance the growth in non-oil imports. The oil sector is expected to continue growing, while the same outlook is seen for the non-oil sector. Currency adjustments in 1999 will boost nontraditional exports and dampen imports. As faster progress is expected on privatization and the oil sector continues to attract large investments, growth should rebound in 1999.

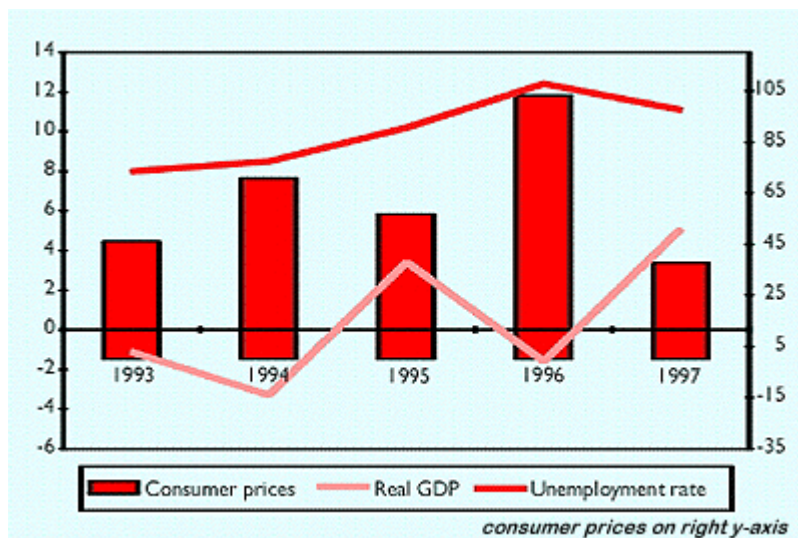
### 7.4.2 Developments in 1997

The Venezuelan economy performed strongly in 1997 bringing the GDP growth rate to an estimated 4.3%, following three consecutive years of poor performance. This strong growth can be attributed to the government's laudable reform policies on foreign investments in the oil industry, which led to higher investments. In 1997 a third sale of concessions of marginal oil fields attracted bids worth US\$ 1.5 billion. The expansion of the Venezuelan GDP can be attributed mainly to the growth in both the oil and the non-oil sectors.

Average inflation for 1997 was 50%, with the year-end rate at 37.6%. Despite the high inflation, this development can be considered a substantial deceleration in inflation from the 103% at the end of 1996. The deceleration in the annual inflation rate can be attributed to a combined effect of monetary restraint primarily aimed at strengthening the bolivar, on the one hand, and subdued domestic demand, on the other. Tighter fiscal and monetary measures have been proposed to further dampen monetary growth. A monthly inflation rate of around 1.9% is needed according to the monetary authorities to meet the official year-end target of 25% for 1998.

#### **Graph 7.4**

#### ***Selected economic key figures of Venezuela (% changes)***



Concomitant with the strong economic growth of the Venezuelan economy in 1997, the unemployment rate fell from 12.4% in 1996 to an estimated 11.1% in 1997. The economic growth resulted in 500,000 new jobs during the second semester of 1997. The job creation initiated as the economy started to expand fueled by the expansion of the oil industry. The number of workers employed in the unregulated and untaxed business sectors also decreased in 1997. Venezuela has a workforce of approximately 9.5 billion.

Venezuelan ended 1997 with international reserves totaling \$17.38 billion. Venezuela generates most of its international reserves from oil sales in the international market. The country's international reserves have more than doubled since falling as low as \$8.67 billion in October 1995.

## **8 THE FINANCIAL SECTOR<sup>1</sup>**

### **8.1 Developments in the financial sector**

In 1997 the number of commercial banks operating in the domestic banking sector of the Netherlands Antilles remained unchanged at 15. In the international banking sector, one new bank was admitted and three banks went into voluntary liquidation. At the end of 1997, there were 39 banks operating in that sector. Furthermore, Indosuez Antilles N.V. changed its name to SNS Bank International N.V. due to a change of shareholders.

The Bank continued its examination of credit institutions during 1997. Seventeen credit institutions were examined including both domestic and international banks, specialized credit institutions, and credit unions. During those examinations, the Bank also assessed the implementation of money-laundering deterrence and detection procedures by the credit institutions.

Furthermore, the Bank started to give special attention to the "Year 2000" problem. In September 1997, the Bank issued a "Year 2000" questionnaire to all credit institutions to assess their preparedness for the year 2000. In addition, a "Year 2000" quick scan has been added to the Bank's regular examination procedures.

In the area of legislation, the National Ordinance on the Reporting of Unusual Transactions ("MOT") and the National Ordinance on the Identification of Customers when Rendering Financial Services ("LIF"), which were enacted in November 1996, became effective in October and November 1997, respectively. An independent entity, "het Meldpunt", which falls directly under the competence of the Minister of Finance, is charged with the execution of the National Ordinance on the Reporting of Unusual Transactions.

In the context of the supervision of the credit unions, the Bank revised the manual for these credit institutions and submitted the revised manual in draft to the representative organization for comment.

<sup>1</sup> Please note that the figures used in this chapter are classified for prudential supervisory purposes which is a different classification from the one used for monetary purposes in chapter 5

## 8.2 Domestic banking

### **8.2.1 General activities of commercial banks operating in the domestic banking sector**

Following a contraction in 1995, total assets of the commercial banks operating in the domestic banking sector reflected a growth for the second consecutive year, increasing by NAf.174.4 million (4.2%) to NAf.4,361.9 millions during 1997 (see table 8.1). This increase was accounted for largely by the growth in non-interest-bearing cash and in the loan portfolio. Non-interest-bearing cash increased in 1997 following a decrease in 1996, and the loan portfolio expanded compared to 1996. Furthermore, investments in unconsolidated subsidiaries and affiliates decreased by NAf.13.6 million to NAf.13.4 million in 1997. Fixed assets and other assets increased by NAf.17 and NAf.10.5 million, respectively.

**TABLE 8.1**  
**Balance sheet of commercial banks operating in the domestic banking sector at year-end (in millions NAf.)**

	1995		1996		1997	
	NAf.	%	NAf.	%	NAf.	%
<b>ASSETS</b>						
Non-int.-bearing cash	347.1	8.5	301.6	7.2	385.2	8.8
Interest-bearing cash	716.5	17.6	583.8	13.9	557.3	12.8
Investments	246.2	6.1	313.3	7.5	314.4	7.2
Loans	2,518.4	61.9	2,738.1	65.4	2,840.4	65.1
Inv. unconsol. subs.	23.4	0.6	27.0	0.6	13.4	0.3
Fixed assets	135.6	3.3	145.7	3.5	162.7	3.8
Other assets	80.6	2.0	78.0	1.9	88.5	2.0
<b>Total Assets</b>	<b>4,067.8</b>	<b>100.0</b>	<b>4,187.5</b>	<b>100.0</b>	<b>4,361.9</b>	<b>100.0</b>
<b>LIABILITIES</b>						
Demand deposits	1,141.4	28.1	1,159.0	27.7	1,207.4	27.7
Savings deposits	1,620.4	39.8	1,606.7	38.3	1,615.7	37.0
Time deposits	721.7	17.7	748.2	17.9	824.7	18.9
<b>Total deposits</b>	<b>3,483.5</b>	<b>85.6</b>	<b>3,513.9</b>	<b>83.9</b>	<b>3,647.8</b>	<b>83.6</b>
Borrowings	84.4	2.1	131.4	3.1	150.1	3.4
Other liabilities	179.0	4.4	181.8	4.3	194.7	4.5
<b>Total Liabili-</b>	<b>3,746.9</b>	<b>92.1</b>	<b>3,827.1</b>	<b>91.3</b>	<b>3,992.6</b>	<b>91.5</b>

ties

Minority interest	4.4	0.2	4.8	0.1	5.3	0.1
Subordinated debent.	12.8	0.3	11.1	0.3	9.1	0.2
General provisions	103.1	2.5	85.9	2.1	113.2	2.6
Capital & reserves	200.6	4.9	258.6	6.2	241.7	5.6
Total Capital	320.9	7.9	360.4	8.7	369.3	8.5
Total Liabilities and Capital	4,067.8	100.0	4,187.5	100.0	4,361.9	100.0

The operations of the local banks continued to be funded mainly through deposits, which comprised 83.6% of total funding sources. Compared to the end of 1996, a slight shift occurred between the share of savings and time deposits in the total deposit base. Savings deposits decreased slightly, while time deposits increased slightly as a percentage of total deposits.

In 1997 the increase in total assets outpaced the increase in capital. Consequently, the total-capital-to-total assets ratio of the domestic banking sector decreased slightly by 0.2 percentage point to 8.5%. Notwithstanding this decrease, the domestic banking sector reflected a higher solvency surplus at the end of 1997 as compared to the end of 1996 because the increase in total actual capital outpaced the increase in total required capital.

The net income of the domestic banking sector decreased by NAf.39 million, (61.4%) to NAf.24.5 million in 1997. The substantial decrease of net income can be attributed mainly to an increase in employees' salaries and benefits and additions to the provisions for losses.

The overall liquidity surplus of commercial banks operating in the domestic banking sector improved by NAf.144.7 million to NAf.175.2 million in 1997 (table 8.2). This improvement was due to a sharp increase in total actual liquidity, which was attributed mainly to the effects of the monetary cash reserve arrangement and the reserve requirement currently in effect.

**Table 8.2**  
**Liquidity at year-end (in millions NAf.)**

	1995	1996	1997
Total actual liquidity	1,076.7	891.5	1,019.5
Total required liquidity	909.3	861.0	844.3
Liquidity Surplus/(Deficit)	167.4	30.5	175.2

## **8.2.2 Domestic activities of commercial banks operating in the domestic banking sector**

Total domestic assets of commercial banks operating in the domestic banking sector increased further by NAf.75.1 million, (2.6%) to NAf.3,011.4 million (table 8.3) in 1997. This increase was reflected mainly in the increase in both non-interest- and interest-bearing cash. Contrary to the 7.9% increase in 1996, credit extension to residents of the Netherlands Antilles remained considerably moderate, growing only by 0.9 % in 1997. This growth is fully in line with the prevailing monetary cash reserve arrangement.

On the liability side, savings deposits continued to be the largest domestic funding source.

A comparison of table 8.1 and table 8.3 reveals that the domestic assets of the commercial banks accounted for 69% of their total assets. Compared to 1996, the percentage of local borrowers in the total loan portfolio declined slightly from 79.5% in 1996 to 77.4% in 1997. Furthermore, approximately 72% of all deposits with the commercial banks stemmed from residents.

**Table 8.3**  
**Domestic activities of commercial banks**  
**operating in the domestic banking sector**  
**at year-end (in millions NAf.)**

	1995		1996		1997	
	NAf.	%	NAf.	%	NAf.	%
<b>ASSETS</b>						
Non-int.-bearing cash	206.0	7.5	150.7	5.1	193.1	6.4
Interest-bearing cash	86.5	3.2	121.9	4.3	144.3	4.8
Investments	218.8	8.0	274.5	9.3	260.9	8.7
Loans	2,020.4	73.82	1,801.74	74.22	1,998.73	73.0
Inv. unconsol. subs.	21.0	0.8	22.0	0.8	9.8	0.3
Fixed assets	122.3	4.5	132.8	4.5	140.9	4.7
Other assets	61.1	2.2	54.3	1.8	62.6	2.1
<b>Total Assets</b>	<b>2,736.1</b>	<b>100.02</b>	<b>2,936.3</b>	<b>100.03</b>	<b>3,011.4</b>	<b>100.0</b>
<b>LIABILITIES</b>						
Demand deposits	874.6	33.4	905.3	33.6	935.9	33.9
Savings deposits	1,178.2	45.11	1,209.74	44.81	1,193.04	43.2
Time deposits	419.4	16.1	444.9	16.5	483.7	17.5
<b>Total deposits</b>	<b>2,472.2</b>	<b>94.62</b>	<b>2,559.94</b>	<b>94.92</b>	<b>2,612.6</b>	<b>94.6</b>
Borrowings	1.7	0.1	2.8	0.1	1.6	0.1
Other liabilities	137.5	5.3	134.8	5.0	146.3	5.3



Total Liabilities 2,611.4100.02,697.5100.02,760.5100.0

The private sector continued to be the main borrower of the local commercial banks (see tables 8.1 and 8.4).

Table 8.4 reflects that in 1997 lending to the public sector decreased, while the growth of domestic credit extension to the private sector remained moderate. The growth in consumer and business loans reflected in 1996 did not continue in 1997, whereas mortgages to the residents of the Netherlands Antilles increased slightly by 4.0% in 1997.

**Table 8.4**  
**Domestic lending to the public and private sector at year-end (in millions NAf.)**

	1995	1996	1997
Government	5.2	4.0	1.3
Private Sector:	2,015.2	2,176.1	2,198.5
-Consumer loans	454.6	490.7	483.1
-Business loans	779.2	795.2	789.7
-Mortgages	781.0	890.2	925.7
Total	2,020.4	2,180.1	2,199.8

Table 8.5 indicates that the private sector continued to be the main deposit holder of the local commercial banks. Compared to 1996, funding of total assets through deposits by the private sector remained unchanged at 58% at year end 1997 (see tables 8.1 and 8.5).

**Table 8.5**  
 **Holders of deposits at year-end (in millions NAf. and %)**

	1995		1996		1997	
	NAf.	%	NAf.	%	NAf.	%
Deposit holders:						
-Government	109.3	4.4	130.5	5.1	95.7	3.77
-Private sector	2,362.995.62	95.62	2,429.594.92	54.92	2,516.9	96.37

The growth of deposits by the private sector denominated in the Netherlands Antillean guilder decelerated slightly in 1997 (table 8.6), amounting to NAf.118.2 million in 1997. Private deposits denominated in foreign currencies continued to decelerate, possibly the result of the license fee, especially on commercial banks operating in Sint Maarten.

**Table 8.6**  
**Growth of domestic private sector deposits by currency (in millions NAf.)**

	1995		1996		1997	
	NAf.	%	NAf.	%	NAf.	%
N.A. guilders	69.2	41.5	96.2	144.4	118.2	135.2
Foreign currencies	97.7	58.5	(29.6)	(44.4)	(30.8)	(35.2)
Total	166.9	100.0	66.6	100.0	87.4	100.0
Growth						

### **8.2.3 International business of commercial banks operating in the domestic banking sector**

Following a contraction in 1996, total foreign assets of commercial banks operating in the domestic banking sector increased by NAf.99.2 million (7.9%) to NAf.1,350.5 million in 1997 (table 8.7). The increase was mainly caused by an increase in non-interest-bearing cash and loans. Interest-bearing cash decreased further by 10.6% to NAf. 413.0 million. Similarly to the domestic business, the foreign business of commercial banks was funded mainly by savings deposits.

**Table 8.7**  
**Foreign activities of commercial banks operating in the domestic banking sector at year-end (in millions NAf.)**

	1995		1996		1997	
	NAf.	%	NAf.	%	NAf.	%
<b>ASSETS</b>						
Non-int-bearing cash	141.0	10.6	151.0	12.1	192.1	14.2
Interest-bearing cash	629.9	47.2	461.9	36.9	413.0	30.6
Investments	27.4	2.1	38.8	3.1	53.5	4.0
Loans	498.0	37.4	558.0	44.6	640.6	47.4
Inv. unconsol. subs.	2.4	0.2	5.0	0.4	3.6	0.3
Fixed assets	13.4	1.0	12.9	1.0	21.8	1.6
Other assets	19.5	1.5	23.7	1.9	25.9	1.9
Total Assets	1,331.6	100.0	1,251.3	100.0	1,350.5	100.0
<b>LIABILITIES</b>						
Demand deposits	266.9	23.6	253.7	22.5	271.5	22.0
Savings deposits	442.2	38.9	397.0	35.1	422.7	34.3

Time deposits	302.3	26.6	303.3	26.9	341.0	27.7
Total deposits	1,011.4	89.1	954.0	84.5	1,035.2	84.0
Borrowings	82.8	7.3	128.5	11.4	148.5	12.1
Other liabilities	41.5	3.6	47.0	4.1	48.4	3.9
Total Liabilities	1,135.7	100.0	1,129.5	100.0	1,232.1	100.0

### 8.3 Secondary financial institutions

At the end of 1997, 36 licensed secondary institutions were operating in the Netherlands Antillean financial sector. Those institutions included credit unions, specialized credit institutions, savings banks, and thrift foundations. By the end of 1996, 19 individuals held a dispensation to extend credit coupons ('bon') for short-term consumer credit to households. However, in 1997 the Bank decided to postpone the granting of dispensations until further notice. Consequently, the number of individuals with a dispensation to extend credit coupons ('bon') for short-term consumer credits remained unchanged at 19.

### 8.4 International banking

Total assets of the international banking sector of the Netherlands Antilles grew by NAf.5.6 billion in 1997. Loans increased by NAf.4.1 billion, representing the largest item in the increase in total assets. Another factor contributing to the increase in total assets was interest-bearing cash, which increased by NAf.2.7 billion in 1997.

The increase in total assets of the international banking sector was financed primarily through borrowings and time deposits.

In 1997 net income amounted to NAf.385.4 million. Contrary to 1996, the international banks earned slightly more interest income during 1997. However, the growth in loans did not generate enough income to offset the decline in other income and fees.

**Table 8.8 <sup>1)</sup>**  
**Balance sheet of commercial banks operating in the international banking sector at year-end (in billions NAf.)**

	1995		1996		1997	
	NAf.	%	NAf.	%	NAf.	%
<b>ASSETS</b>						
Non-int.-bearing cash	1.1	2.4	1.5	3.0	1.1	2.0
Interest-bearing cash	7.9	16.7	7.8	15.4	10.5	18.6
Investments	6.4	13.6	7.2	14.2	5.9	10.5
Loans	29.0	61.3	31.7	62.5	35.8	63.5
Inv. unconsol. subs.	0.6	1.3	0.3	0.7	0.3	0.6
Fixed assets	0.1	0.2	0.1	0.2	0.1	0.1
Other assets	2.1	4.5	2.1	4.0	2.6	4.7
<b>Total Assets</b>	<b>47.2</b>	<b>100.0</b>	<b>50.7</b>	<b>100.0</b>	<b>56.3</b>	<b>100.0</b>
<b>LIABILITIES</b>						
Demand deposits	3.3	7.0	4.0	7.9	3.1	5.6
Savings deposits	0.1	0.3	0.1	0.2	0.1	0.2
Time deposits	13.7	29.1	14.7	28.9	18.3	32.4
Total deposits	17.1	36.4	18.8	37.0	21.5	38.2
Borrowings	8.1	17.1	25.5	50.2	28.6	50.8
Other liabilities	2.0	4.3	2.6	5.3	2.5	4.5
<b>Total Liabilities</b>	<b>27.2</b>	<b>57.8</b>	<b>46.9</b>	<b>92.5</b>	<b>52.6</b>	<b>93.5</b>
Minority interest	0.1	0.2	0.1	0.2	0.1	0.2
Subordinated debent.	16.8	35.5	0.2	0.4	0.1	0.1
General provisions	0.6	1.3	0.5	1.0	0.2	0.3
Capital & reserves	2.5	5.2	3.0	5.9	3.3	5.9
<b>Total capital</b>	<b>20.0</b>	<b>42.2</b>	<b>3.8</b>	<b>7.5</b>	<b>3.7</b>	<b>6.5</b>
<b>Total Liabilities and Capital</b>	<b>47.2</b>	<b>100.0</b>	<b>50.7</b>	<b>100.0</b>	<b>56.3</b>	<b>100.0</b>

<sup>1)</sup> Figures for 1995 and 1996 have been adjusted.

## 9. INSTITUTIONAL INVESTORS

### 9.1 Introduction/regulatory developments

Traditionally the institutional investors markets in the Netherlands Antilles have shown a rather conservative development. However, things have changed the last five years, resulting in a more dynamic environment. Consequently, changes in the legal infrastructure supporting these markets are inevitable.

Some delay was encountered in concluding the revised draft legislation regulating the insurance brokers in the Netherlands Antilles. However, the draft legislation has been concluded now and will be submitted to government for enactment in 1998. Once in force, this piece of legislation will strengthen the position of the insurance broker and will allow insurance brokerage services to be rendered by registered insurance brokers only. This will extend the protection of the policyholder to the pre-contractual stage.

In addition, the introduction of the compulsory health insurance scheme encountered some delay also. Government requested a committee, on which the different players involved in the execution of the scheme are represented, to formulate solutions for the existing problems. The committee expects to conclude the scheme in 1998.

Furthermore, the work on a motor insurance guarantee fund has been progressing well. Based on the recommendations by the Motor Insurance Guarantee Fund Committee, Government instituted the 'Inter-island Working Group for the Introduction of the Motor Insurance Guarantee Fund' to carry out the recommendations of the former committee. The different island territories, the Central Government and the insurance industry are represented on the working group. The contribution of the island territories is of utmost importance since the needed physical infrastructure is legally their responsibility.

In November 1997, the Pension Committee submitted its recommendations to government in a document entitled "On our way to a pension policy for the Netherlands Antilles". The document includes two options to solve the pension issue:

- make it mandatory for the employer and the employee to introduce a pension arrangement
- leave the introduction of a pension arrangement to the discretion of the employer and the employee. However at the same time granting the Minister of Labor and Social Affairs the authority to expand the scope of existing pension arrangements to other corporations lacking such an arrangement or to institute, in consultation with the social partners, a new pension arrangement for those (group of) corporations.

The Committee also emphasized the urgency of reforming the funding of the basic old age pension, the AOV. The aging population in the Netherlands Antilles causes this problem. In principal, government accepted the recommendations of the Pension Committee. Government requested the Pension Committee to inform the social partners and the institutions carrying out pension arrangements extensively, in order to gain social acceptance and support. Furthermore, this will formally give them an opportunity to influence the decision making process.

Accurate and timely reporting by the institutional investors still remains a problem, especially the reporting by the pension funds. The originated backlog still is not eliminated and consequently their consolidated figures cannot be included in this report. The Bank is in the process of preparing an automated reporting system for the institutional investors, which should enable both timely and accurate reporting as well as the elimination of the existing backlog. In order to reduce costs and increase the reliability of the data, the Bank has to come to an understanding with the external auditor and the actuary with respect to principles, norms and standards that ought to be taken into consideration while carrying out their respective duties. A shift in emphasis from purely financial aspects of supervision to operational and organizational aspects further emphasizes this need. Therefore, the norms, principles and standards will be represented in the new automated reporting system.

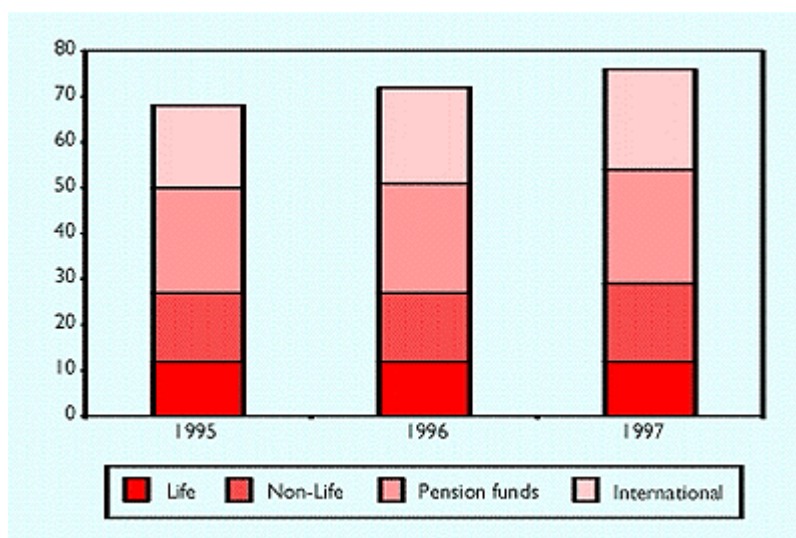
## 9.2 The institutional investors' sector

The number of insurance institutions operating in the institutional investors sector increased by four during 1997 (See graph 9.1). There are still 12 life insurance companies operating in the Netherlands Antilles of which nine are branches and three are locally incorporated. The number of non-life insurance companies increased by two to reach 17, of which nine are incorporated in the Netherlands Antillean jurisdiction, while the others are branches of foreign organizations.

The number of insurance companies domiciled in the Netherlands Antilles serving the international insurance market remained 21. These companies originate from various parts of the world, including several countries in the region, the United States, Canada, India and notably the Netherlands.

The number of pension funds increased from 24 to 26. One of these two new pension funds is domiciled in the Netherlands Antilles, but its participants consist of expatriates residing outside our jurisdiction.

**Graph 9.1**  
**Composition of the institutional investors sector**



Considering the excellent infrastructure provided by the Netherlands Antilles, the incorporation of captives has been at a rather slow pace the last five to ten years. The reason for this was a 'low profile approach' with respect to marketing the Netherlands Antilles as a captive domicile. Captive managers and management companies have undertaken several initiatives and recently formed an association. This association will increase the efforts to market the Netherlands Antilles in general, and the island of Curaçao in particular, in the international insurance markets.

### **9.3 Overview of developments in the insurance industry**

#### ***9.3.1 General***

The number of natural disasters decreased considerably in 1997 compared to 1996. Economic losses in 1997 totaled US\$ 30 billion worldwide, substantially less than US\$ 60 billion recorded in 1996. Most of the disasters occurred in regions with a low insurance density. The reinsurance market will reimburse approximately 15% of the losses; consequently the premiums in reinsurance market are expected to remain stable.

There is a trend noticeable to higher retentions by individual insurance companies. This, combined with the largely available capacity and increased competition due to the deregulation of insurance markets in Europe and Japan, will keep reinsurance premiums low in the short term. However, further decline in the reinsurance prices will jeopardize the required rates of return for the reinsurance companies, indicating that market forces might push-up the level of reinsurance premiums in the long run.

Insurance premiums soared in St. Maarten in 1996, after hurricane Luis struck the island in September 1995. The Government of the island of St. Maarten started negotiating with the insurance industry in an effort to agree on more affordable property and casualty premiums for its citizens.

There is an increase in the number of risks being underwritten by insurance companies that do not possess a license. By law, an insurance company needs a license in order to underwrite insurance in the Netherlands Antilles. The Bank periodically publishes a list of companies licensed to underwrite insurance in the Netherlands Antilles. Policyholders are advised to adhere to one of these companies when engaging in insurance services.

#### ***9.3.2 Life insurance industry***

##### *9.3.2.1 Balance sheet*

According to table 9.1, total assets of the local life insurance industry increased from NAf.803.4 million in 1995, to NAf.898.0 by the end of 1996. This increase of NAf.94.6 million (11.8%) is only slightly less than the 12.2% growth in 1995. The increase can be attributed mainly to the NAf.56.1 million (84.5%) and NAf.22.1 million (3.7%) growth in the separate accounts statement<sup>1</sup> and total investments, respectively.

Total liabilities increased mainly as a result of an increase by NAF.51.3 million (9.8%) in technical provisions and mentioned increase in the separate account statement. Furthermore, total liabilities increased by NAF.6.2 million due to subordinated instruments. This increase represents subordinated debentures provided by the parent companies of locally incorporated life insurance companies. On the other hand, other provisions showed a marked decline of NAF.47.6 million (73.2%), as a result of a reduction in future claims, due to the surrender of policies.

The equity position of the local life insurance companies, consisting of capital, surplus and subordinated instruments, improved by NAF.15.6 million (40.1%). This is the result of an increase of NAF.3.6 million in capital (34.6%), of NAF.5.8 million in surplus (20.4%) and mentioned increase in subordinated instruments. As a result, the equity position represented 9.3% of last year's technical and other provisions, well above the solvency requirement of 4%.

<sup>1</sup> *The separate account statement represents the assets and liabilities in the investment policies sold by the life insurance companies*



**Table 9.1**  
**Consolidated balance sheet of life insurance companies (in millions NAf.)**

	1994		1995		1996	
	Local	Int'l	Local	Int'l	Local	Int'l
<b>ASSETS</b>						
Intangibles	0.5	-	0.4	-	-	-
Total investments	534.9	22.3	604.2	27.0	626.3	29.2
Current assets	111.7	6.3	117.0	5.2	133.6	7.7
Other assets	13.4	-	15.4	-	15.6	-
From separate accounts						
statement	55.5	-	66.4	-	122.5	-
Total admissible assets	716.0	28.6	803.4	32.2	898.0	36.9
<b>LIABILITIES</b>						
Capital	10.7	5.8	10.4	5.9	14.0	4.1
Surplus	18.5	12.6	28.5	17.2	34.3	22.7
Subord. instruments	-	-	-	-	6.2	-
Technical provisions	467.4	5.1	521.2	6.6	572.5	4.8
Other provisions and liabilities	65.0	1.1	65.0	1.2	17.4	1.2
Current liabilities	98.9	4.0	111.9	1.3	123.6	3.8
Contingent liabilities	-	-	-	-	7.5	0.3
From separate accounts						
statement	55.5	-	66.4	-	122.5	-
Total equity, provisions, and liabilities	716.0	28.6	803.4	32.2	898.0	36.9

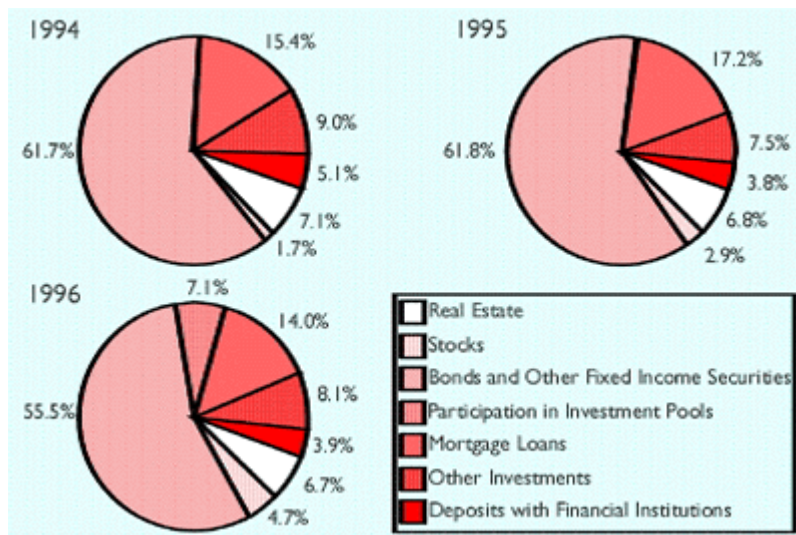
Total assets of the international life insurance companies increased by NAf.4.7 million (14.6%), reaching NAf.36.9 million at the end of 1996. This is mainly the result of increases in current assets and investments by NAf.2.5 million (48.1%) and NAf.2.2 million (8.1%), respectively. The equity position improved by NAf.3.7 million (16.1%), totaling NAf.26.8 million by the end of 1996, well above the legally required solvency margin. Furthermore, the technical provisions, declined by NAf.1.8 million (27.3%). This is related to the NAf.2.5 million (192.3%) increase in current liabilities, indicating the recognition of claims to be paid.

### 9.3.2.2 Investments

As mentioned above, total investments increased by NAf.22.1 million (3.7%). This growth can be broken down in the several components of the total investment portfolio. The composition of the consolidated investment portfolio of the local life insurance companies is shown in graph 9.2. This graph reveals that 'Bonds and other fixed income securities' have dropped considerably in relative importance. This is partly the result of a shift of funds from this category to 'Participation in investment pools'. While the former declined by NAf.15.6 million (4.2%), the latter increased by NAf.44.0 million to reach 7.1% of total investments in 1996. Furthermore, investments in stocks increased for the third year in a row. After a NAf.12.2 million (69.7%) increase in this category in 1996, it accounts for 4.7% of total investments, compared to 2.9% in 1995.

**Graph 9.2**

**Composition of the investment portfolio of local life insurance companies**



### 9.3.2.3 Profit and loss statement

The operating results of the life insurance industry are represented in table 9.2. Net results after taxes of the local life insurance industry declined by NAf. 1.3 million (30.2%), mainly as a result of an increase in the tax burden. The fundamentals however, remain strong, as can be derived from total operational income. Total operational income showed an improvement of NAf.14.8 million (11.0%), totaling NAf.149.6 million in 1996. Responsible for this result is a continued increase in both premium income and investment income. In 1996, both increased by NAf.12.7 million (12.9%) and NAf.2.0 million (5.6%), respectively.

In contrast to this favorable development, there was an increase in total operational expenditures by NAf.13.0 million (10.2%). This can be attributed to the increase in net benefits incurred by NAf.5.4 million (15.7%) and the change in technical provisions by NAf.6.0 million (11.0%). Net operational results showed an improvement of NAf.2.6 million (33.3%), totaling NAf.9.4 million in 1996. This

improvement was partially offset by increases in both other income and expenses and corporate taxes incurred leading to mentioned decline in net result after corporate taxes of NAf.1.3 million.

**Table 9.2**  
**Consolidated profit and loss statement of life insurance companies (in millions NAf.)**

	1994		1995		1996	
	Local	Int'l	Local	Int'l	Local	Int'l
<b>INCOME</b>						
Total net earned premium	96.0	4.9	98.7	6.4	111.4	6.2
Net investm. income allocated to technical provisions	34.2	-	36.0	-	38.0	0.9
Net other operational income	0.1	-	0.1	-	0.2	-
Total operational income	130.3	4.9	134.8	6.4	149.6	7.1
<b>EXPENSES</b>						
Net benefits incurred	30.8	0.3	34.3	0.4	39.7	1.4
Change in net techn. prov.	61.1	-	54.6	1.4	60.6	-
Policyholders' dividends	7.7	1.1	7.7	1.8	7.3	1.5
Insurance expenses and non-corporate taxes	13.3	0.4	15.5	0.4	16.7	-
Commission and other acquisition costs	15.1	0.2	13.9	0.6	14.9	-
Net other operational expend.	0.8	0.1	1.0	0.1	1.0	0.9
Total operational expend.	128.8	2.1	127.0	4.7	140.0	3.8
Net operational results	1.5	2.8	7.8	1.7	9.4	3.3
Net investm. income allocated to surplus	7.6	3.0	7.3	3.6	9.1	2.6

Other income and expenses	(2.1)	-	(5.7)	-	(8.1)	(1.2)
Net results from separate accounts	(1.0)	-	(2.5)	-	(2.0)	-
Extraordinary results	-	(0.4)	(0.1)	(0.6)	(0.1)	(0.8)
Net results before corp. taxes	6.0	5.4	6.8	4.7	8.3	3.9
Corporate taxes incurred	1.6	-	2.5	-	5.3	-
Net results after corp. taxes	4.4	5.4	4.3	4.7	3.0	3.9

Total net earned premium in the international life insurance industry decreased by NAF.0.2 million (3.1%), totaling NAF.6.2 million over 1996. On the other hand, operational income increased by NAF.0.7 million (10.9%), due to the increase in investment income. Net operational results almost doubled with an improvement of NAF.1.6 million (94.1%), the result mainly of a reduction in operational expenditures. This decline can be explained by the fact that no change in technical provisions was needed, while the insurance expenses and noncorporate taxes were negligible. Net results after corporate taxes are NAF.0.8 million (17.0%) less than in 1995, the result of a decline in investment income and an increase in other income and expenses. Net results after taxes for the internationally operating life insurance companies have been declining for the third year in a row now.

### **9.3.3 The non-life insurance industry**

#### *9.3.3.1 Balance sheet*

The balance sheet total of the local non-life insurance companies operating in the domestic market increased by NAF.46.5 million (11.8%), totaling NAF.442.1 million at the end of 1996. Current assets increased by NAF.34.9 million (11.0%) and are mainly responsible for this growth in total assets. Furthermore, there was an increase by NAF.12.4 million (17.2%) in total investments, while other assets showed an increase also.

On the liability-side, the growth in the balance sheet total was mainly reflected in an increase in current liabilities by NAF.54.2 million (27.9%). This increase can be attributed mainly to a corresponding decrease by NAF.30.7 million (20.1%) in technical provisions, which indicates that a large amount of claims have been acknowledged but not yet paid out. This, in turn, is related to the hurricane damage on St. Maarten.

In addition, the local non-life insurance industry improved its equity position by NAF.13.1 million (35.8%). The major part of this increase (NAF.9.4 million) was the result of subordinated loans provided by parent companies of locally operating non-life insurance companies. As a result, the indus-

try's solvency margin amounted to 39.6% of net (after reinsurance) premium income in 1995. This is well above the 15% margin required by law.

**Table 9.3**  
**Consolidated balance sheet of the non-life insurance industry (in millions NAf.)**

	1994		1995		1996	
	Local	Int'l	Local	Int'l	Local	Int'l
<b>ASSETS</b>						
Intangibles	-	-	0.4	-	--	
Total investments	83.7	675.9	72.3	802.1	84.7	1,110.9
Current assets	156.8	100.5	316.3	120.8	351.2	120.9
Other assets	9.1	1.0	6.6	0.6	6.2	0.1
Total admissible assets	249.6	777.4	395.6	923.5	442.1	1,231.9
<b>LIABILITIES</b>						
Capital	34.0	128.6	34.2	133.2	34.0	129.7
Surplus	17.1	252.4	12.1	375.9	16.0	514.3
Subordin. instruments	0.3	-	0.3	-	9.7	-
Technical provisions	108.8	363.4	152.9	389.0	132.2	562.9
Other prov. and liabilities	1.0	8.5	1.4	10.0	1.5	0.2
Current liabilities	88.2	24.5	194.5	12.0	248.7	24.8
Contingent liabilities	0.2	-	0.2	3.4	-	-
Total equity, provisions, and liabilities	249.6	777.4	395.6	923.5	442.1	1,231.9

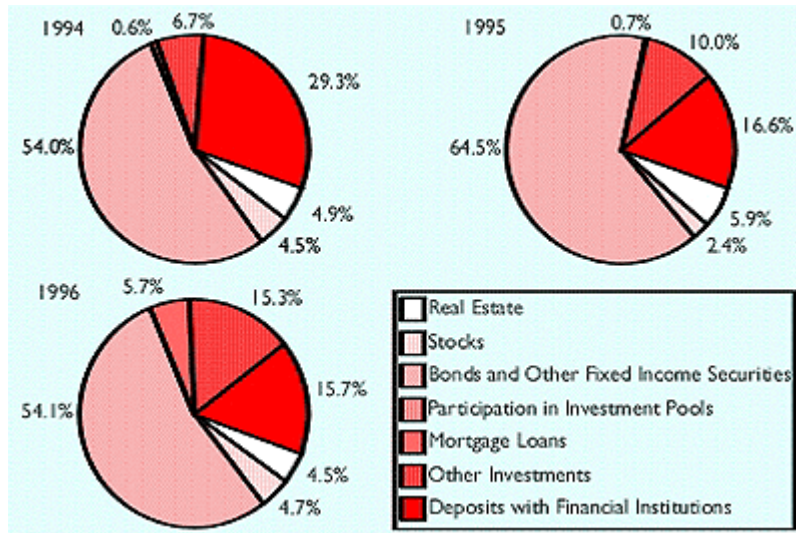
The balance sheet total of the insurance companies operating in the international markets showed a significant increase by NAf.308.4 million (38.4%), totaling NAf.1.2 billion at the end of 1996. This can be explained by the inclusion of two new insurance companies in 1996, compared to the 1995 figures. The increase in total assets can be entirely attributed to the growth in investments, as the other categories did not change significantly. On the liability-side, the technical provisions increased by NAf.173.9 million (44.7%), while current liabilities increased by NAf.12.8 million (106.7%) in 1996. In addition, the equity position was further strengthened by an increase of NAf.134.9 million (26.5%), reaching NAf.644.0 million in 1996. This increase is completely attributable to an increase in surplus, as capital dropped slightly. As a result, the consolidated solvency position of the internationally operating insurance companies exceeds the legal requirements by a significant margin.

### 9.3.3.2 Investments

The composition of the investment portfolio of the local non-life insurance companies is presented in graph 9.3. This graph indicates that 1995 was a rather exceptional year, since 'Bonds and other fixed income securities' comprised nearly two-thirds of total investments. A closer look at the data shows that the absolute investments in this category are almost constant over this three-year period, but that the relative importance fluctuated with the magnitude of total investments. Total investments were low in 1995, when deposits with financial institutions had to be used to pay out claims

related to the hurricane damage. Furthermore, this graph shows that in 1996, the local non-life insurance companies did not place as much funds with financial institutions as they used to, but instead used other investment opportunities. In addition, the growth in relative importance of investments in mortgage loans is compelling.

**Graph 9.3**  
**Composition of the investment portfolio of the local non-life insurance companies**



### 9.3.3.3 Profit and loss statement

The local non-life insurance industry recovered remarkably well from the losses caused by hurricane Luis. Net earned premium increased by NAF.13.8 million (9.3%) in 1996. This is the combined result of a sharp increase in the premium level and a drop in the number of premium payments. In turn, this indicates that the high premium level forces part of the policyholders to be not insured. Net claims incurred decreased by NAF.5.8 million (6.0%) but still are far above the 1994 level. As a consequence total operational expenditures are also above their normal levels. These effects of the hurricane damage are likely to phase out in 1997.

The increase in premium income resulted in a significant improvement in net underwriting results by NAF.14.9 million to reach a loss of NAF.0.5 million. Further improvement depends on the ability of the industry to control its operational expenditures. The improvement in net underwriting income, together with a slight increase in investment income and other results, lead to a NAF.16.9 million improvement in net results before corporate taxes. Since the local insurance companies had to pay taxes in 1996 -as opposed to 1995- the net result after corporate taxes improved by NAF.11.0 million.

**Table 9.4**  
**Consolidated profit and loss statement of the non-life insurance industry (in millions NAf.)**

	1994		1995		1996	
	Local	Int'l	Local	Int'l	Local	Int'l
<b>INCOME</b>						
Total net earned premium	130.8	135.2	148.2	169.8	162.0	207.7
Net underwriting income	1.3	2.5	0.1	1.6	0.1	0.7
Total operational Income	132.1	137.7	148.3	171.4	162.1	208.4
<b>EXPENSES</b>						
Net claims incurred	70.0	77.0	97.0	88.4	91.2	120.0
Change in various provisions	2.5	-	2.7	-	1.0	-
Claim adjustment expenses	3.2	0.3	2.4	0.4	6.9	-
Net other underwr. expend.	34.1	6.3	37.4	8.2	36.1	10.7
Net other operational expend.	18.0	4.3	24.2	1.6	27.4	3.4
Total operational expend.	127.8	87.9	163.7	98.6	162.6	133.8
Underwriting results	4.3	49.8	(15.4)	72.8	(0.5)	74.6
Net investment income	6.1	21.3	7.4	58.2	7.7	74.9
Other results	1.1	(9.0)	(0.2)	(10.8)	1.5	(14.7)
Extraordinary results	-	(0.1)	(0.1)	(0.1)	(0.1)	(7.8)
Net results before corp. taxes	11.5	62.0	(8.3)	120.1	8.6	127.0
Corporate taxes incurred	2.8	1.0	(2.5)	1.8	3.4	2.2
Net results after corp. taxes	8.7	61.0	(5.8)	118.3	5.2	124.8

Total net earned premium of the internationally oriented non-life insurance companies increased by NAF.37.9 million (22.1%) a substantial growth, taking into account the weak performance in the international insurance markets. This growth in income was partially offset by an increase in the net claims incurred by NAF.31.6 million (35.7%). The overall improvement in underwriting result amounted to NAF.1.8 million (2.5%).

Net results before and after corporate taxes continued to improve by NAF.6.9 million (5.7%) and NAF.6.5 million (5.5%), respectively. The difference can be explained by the increase in the tax burden of the international non-life insurance companies. The growth in net results after corporate taxes has slowed down considerably from 93.9% to 5.5%. This can be explained by the relative sharp increase in operational expenditures, in general, and in net claims occurred, in particular.

## **10 POLICIES AND ACTIVITIES OF THE CENTRAL GOVERNMENT**

### **10.1 Introduction**

This chapter summarizes the main policies and activities of the Bank during 1997.

### **10.2 Training and seminars**

From May 26 - 30, 1997, the Bank hosted a course under the auspices of the Center of Monetary Studies in Latin America (CEMLA) on banking supervision. Lecturers were from the CEMLA, Banco de Mexico, Bank of England, The Federal Deposit Insurance Corporation (USA), and The Federal Reserve Bank (USA). Participants were from different Caribbean islands. During this five-day course, among other things, the following topics were covered:

- The role of central banking in banking supervision
- Off-site supervision and bank rating systems
- Prudential regulatory and supervisory standards
- Banking supervision legislation
- Risk assessment and risk audit
- Risk management in derivatives markets
- Anti-money-laundering techniques
- Problem bank resolution and emergency measures
- Analyses of the financial conditions of banks
- Deposit insurance and safety nets

During 1997 the Bank organized two courses on professional writing in the Dutch Language for its staff and personnel -- a basic course and an advanced course on effective reporting and formulation. The purpose of these courses was to make the Bank's employees, on all levels, more familiar with modern Dutch grammar and spelling and hence improve the quality of internal reporting and external correspondence. Special attention was given to the current writing style of the different types of texts that Bank employees must write in their line of work. Both courses were provided by the Language Teachers Institute.



Staff members of the Central Bank also participated intensively in the activities of the Caribbean Financial Action Task Force (CFATF) during 1997. The CFATF is a regional organization for the prevention and combating of money laundering. The Netherlands Antilles participated in the Plenary and Council Meetings of the CFATF. The Netherlands Antilles also is a member of the Steering Committee of this organization. In 1997 the CFATF organized two money-laundering typologies meetings to discuss new developments and trends. A staff member of the Bank was invited to be one of the examiners for the mutual evaluation of the Bahamas. Officials of the Bank also attended the meetings of the Financial Action Task Force (FATF) with the Secretariat in Paris.

### **10.3 Monetary Policy measures**

During 1997 monetary policy in the Netherlands Antilles was conducted against the background of a structural adjustment program (SAP) aimed at re-establishing internal and external equilibrium in the medium term. The SAP stipulated binding performance criteria for both fiscal and monetary policy. The criteria for monetary policy entailed, among other things, a maximum allowed growth in net domestic assets (NDA) and a minimum required growth in net international reserves. The main instrument of monetary policy for the Bank is the monetary cash reserve arrangement (MCR), which entails among other things, a progressive penalty system aimed primarily at limiting excessive credit extension to the private sector. The rationale behind the MCR is that restricting domestic credit to the private sector controls private sector expenditures, which is favorable for the balance of payments.

For net domestic credit to the private sector, a penalty-free growth rate of 3.5% was set for the period October 31, 1996, to December 31, 1997.

Another instrument for monetary policy is the Reserve Requirement (RR). The rationale behind this measure, which was introduced in August 1993, is that limiting the free reserves of the commercial banks, enables the Bank to limit their potential for credit extension. This is achieved by requiring the banks to deposit a fixed percentage of their domestic debt, interest free, at the Central Bank. Since October 1994, the RR was fixed to 2% of the adjusted domestic debt. In August 1997, in an effort to prevent a build up of excess liquidity in the banking system, the Bank raised its RR from 2% to 3%.

The target for net domestic credit of commercial banks to the General Government was set at the October 31, 1996, level, implying a zero growth for 1997.

## **11 FOREIGN EXCHANGE REGULATIONS AND LICENSE FEE**

The foreign exchange regulations in the Netherlands Antilles are based on the National Ordinance Foreign Exchange System of 1981. According to that Ordinance, current transactions are in principle free, while capital transactions require a foreign exchange license.

Although capital transactions are bound to a license, over time several foreign exchange notifications have been issued that liberalized certain capital transactions. The Bank applies a liberal licensing system with respect to capital transactions: licenses are normally granted upon request.

The main purpose of the foreign exchange regulations as embodied in the Foreign Exchange Ordinance of 1981 are:

1. to promote the Netherlands Antilles as an internationally recognized financial center; for this reason, the Ordinance contains special provisions for companies engaged in international financial and business transactions;
2. to obtain the necessary information and data essential for compiling the balance of payments;
3. to support the monetary and economic policy efforts of the monetary authorities, whereby the maintenance and safeguarding of the monetary reserves, and thus exchange rate stability, are considered of primary importance; and
4. to prevent the use of Antillean Guilders as a means of payment in the international payment system.

The general foreign exchange policy is vested with the government of the Netherlands Antilles. The Bank is charged with executing the foreign exchange regulations and managing the available foreign exchange reserves for account and risk of the government. Therefore, the Bank is empowered to grant licenses and exemptions by virtue of the Foreign Exchange Ordinance of 1981.

Table 11.1 compares the total amounts invested by residents abroad during the financial years 1995, 1996, and 1997 based on foreign exchange licenses granted.

**Table 11.1**  
**Investments abroad by residents 1995**  
**through 1997 (in millions NAf.)**

	1995	1996	1997
January	2.2	1.3	0.0
February	0.4	0.0	17.9
March	0.5	0.0	0.0
April	0.0	0.9	2.0
May	1.0	0.0	1.8
June	0.0	0.0	0.0
July	0.0	2.0	0.4
August	0.0	0.0	0.1
September	3.5	0.9	0.9
October	0.0	1.6	0.6
November	0.0	0.0	1.3
December	0.2	3.6	0.3
Total	7.8	10.3	25.3

*Note:*

*In the figures, investments made by natural persons in amounts less than NAf.100,000.00 annually have not been included because no license is required for these amounts. Some institutional investors are not included because they have a general license to make investments abroad within certain limits.*

Starting January 1, 1996, the foreign exchange banks are responsible for paying a license fee to the Central Bank on international transactions. This license fee replaced the foreign exchange tax which was in force until December 1995. The license fee is calculated on the basis of the payments made by residents to nonresidents, with the exception of those payments related to re-investment of funds abroad and the re-exports of the "Free-Zone" companies.

**Table 11.2**  
**License fees collected during 1996 and 1997 (in thousand NAf.)**

	<b>1996</b>	<b>1997</b>
January	3,643.3	3,007.4
February	2,791.4	2,546.8
March	3,199.4	2,633.3
April	2,901.8	2,927.0
May	3,201.3	2,619.0
June	3,185.3	2,678.0
July	3,142.9	2,951.4
August	2,943.2	2,692.1
September	2,611.5	2,604.4
October	3,127.5	2,805.6
November	2,602.7	2,524.1
December	2,966.4	3,212.5
Total	36,316.7	33,201.4

Table 11.2 gives an overview of the license fees collected monthly during 1996 and 1997.

From the total amount of license fees generated in the Netherlands Antilles, NAf.21,691.9 thousand was generated on the island of Curaçao, NAf.10,653.2 thousand on St. Maarten, and NAf.660.2 thousand on Bonaire. The remaining NAf.196.1 thousand of license fees was paid through the Central Bank.

## 12 FINANCIAL STATEMENTS FOR 1997

**Table 12.1**  
**Balance Sheet as of December 31, 1997**

	1996	1997
<b>ASSETS</b>		
Gold and gold receivables	189,480,885	188,954,171
Receivables and securities in foreign currency	361,248,863	409,555,098
Advance account Central Govern- ment	16,970,501	29,593,971
Government bonds	35,320,000	35,175,000
Other long-term receivables	9,438,238	10,925,228
Fixed assets	14,924,159	18,576,987
Printing costs banknotes	790,399	298,210
Other current assets	13,561,364	13,621,286
<b>TOTAL ASSETS</b>	<b>641,734,409</b>	<b>706,699,951</b>
	<b>1996</b>	<b>1997</b>
<b>LIABILITIES</b>		
Banknotes in circulation	245,977,515	238,958,980
Residents' current accounts		
- in guilders	153,480,390	218,658,564
- in foreign currency	12,128,491	23,246,599
Residents' time deposits		
- in guilders	6,770,400	5,391,967
- in foreign currency	715,800	716,000
Nonresidents' current accounts		
- in guilders	18,735,795	15,097,366
Money in consignment	758,628	786,893
Other current liabilities	12,814,294	14,634,470
Undistributed earnings	7,470,660	6,853,390
Special reserves	122,882,436	122,355,722
Reserve fund	30,000,000	30,000,000
Capital	30,000,000	30,000,000
<b>TOTAL LIABILITIES</b>	<b>641,734,409</b>	<b>706,699,951</b>

**Table 12.2**  
**Profit and Loss Account 1997**

	1996	1997
<b>INCOME</b>		
Interest income	29,844,809	25,522,367
Foreign exchange earnings	1,226,845	1,085,032
Micellaneous earnings	1,984,761	1,479,553
	33,056,415	28,086,952
License fee	36,748,406	33,369,293
<b>TOTAL INCOME</b>	<b>69,804,821</b>	<b>61,456,245</b>
<b>EXPENSES</b>		
Interest expenses	994,764	543,011
Depreciation of fixed assets	2,299,723	2,495,107
Depreciation of printing costs bank notes	499,199	499,349
General expenses	19,089,062	19,736,048
<b>TOTAL EXPENSES</b>	<b>22,891,248</b>	<b>23,273,515</b>
<b>NET INCOME</b>	<b>46,913,573</b>	<b>38,182,730</b>
<b>Distribution of net income</b>		
Net income	46,913,573	38,182,730
Paid to the Central Government	45,000,000	38,800,000
Change in undistributed earnings	1,913,573	-617,270

## 12.1 Notes to the balance sheet as of December 31, 1997

### 12.1.1 Gold and gold receivables

This category includes gold bars, as well as the Bank's share in the remaining gold stocks of the Goldfund of the Netherlands Antilles and Aruba. This fund was instituted with the separation of Aruba to divide the available gold between the two respective central banks.

Gold and gold receivables are valued at the average of the lowest London market price in the three years preceding the date of valuation, less a margin of 30%. Gold and gold receivables are revalued every three years. Changes resulting from revaluations are debited or credited to the special reserves after approval from the Minister of Finance. On December 31, 1997, a revaluation resulted in a downward adjustment of NAf.526,714, which was debited to the special reserves.

### ***12.1.2 Receivables and securities in foreign currency***

The receivables and securities represent balances in current accounts, time deposits, and investment portfolios, including accrued interest maintained in foreign currency with foreign financial institutions. Valuation in guilders is made at the official midrate prevailing at the balance date.

### ***12.1.3 Advance account Central Government***

In conformity with paragraph 1 of Article 15 of the National Ordinance constituting the Central Bank Charter (P.B. 1985, no. 183), this advance is at all times bound to a maximum of 10% of the revenues of the Central Government during the previous fiscal year. This advance account is not interest-bearing.

### ***12.1.4 Government bonds***

In 1989, an agreement was signed with the Minister of Finance whereby the old advance account of the Central Government of the Netherlands Antilles was converted into bonds. The bonds are valued at their purchase price or lower nominal value.

### ***12.1.5 Other long-term receivables***

These loans are valued at their nominal value, less a provision for possible losses.

### ***12.1.6 Fixed assets***

These assets are valued at cost after deduction of accumulated depreciations, computed on the basis of the expected useful life of the assets following the straight-line method.

In 1990, a piece of land was purchased for the construction of the new office building. This asset is valued at cost.

### ***12.1.7 Printing costs of bank notes***

This amount represents the printing costs of bank notes, after deducting accumulated depreciation, computed on the basis of expected useful life of the bank notes following the straight-line method.

### ***12.1.8 Other current assets***

This item includes, among other things, license fee receivables, accrued interest, prepaid expenses, coins and currency held as petty cash, and other short-term receivables. These assets are valued at their nominal value.

### ***12.1.9 Bank notes in circulation***

This balance represents the nominal value of the bank notes issued by the Bank that are in circulation at year end.

### ***12.1.10 Residents' current accounts***

These include the balances in current account of domestic banks, Islands Collectors, and other government institutions within the Netherlands Antilles. Most of the balances are denominated in guilders. Foreign currency balances are translated into guilders at the Bank's official midrates prevailing at year end.

### ***12.1.11 Residents' time deposits***

These include the balances in time deposits of domestic banks and government institutions. The balances are interest-bearing. Foreign currency balances are translated into guilders at the Bank's official midrates prevailing at year end.

### ***12.1.12 Nonresidents' current accounts***

This amount represents the balances in current account of foreign banks and/or foreign government institutions. Foreign currency balances are converted into guilders at the Bank's official midrates prevailing at year end.

### ***12.1.13 Money in consignment***

This amount represents nominal value of the Bank's liability on account of money received in custody from third parties in conformity with the National Ordinance on Money held in Consignment (P.B. 1886, no. 33).

### ***12.1.14 Other current liabilities***

This balance includes accrued interest and accounts payable.

### ***12.1.15 Undistributed earnings***

Under this heading appears the accumulated earnings of the bank for the current and previous years, less the amounts paid to the country's treasury. After official approval of the figures for 1997 and an official decision concerning the distribution of the net income, this balance will be allocated accordingly.

### ***12.1.16 Special reserves***

This reserve was formed originally by a reserve created by revaluation of gold stock in the years 1971, 1973, 1994, and 1997. The profits made by the selling of numismatic coins during 1990 also were added to the balance of this account.

Article 5 of the National Ordinance constituting the Central Bank Charter (P.B. 1985, no. 183) stipulates that the Bank can form these reserves with the consent of the Minister of Finance.

#### ***12.1.17 Reserve fund***

The National Ordinance constituting the Central Bank Charter (P.B. 1985, no. 183) introduced a Reserve Fund of NAF.30,000,000 (Article 4).

#### ***12.1.18 Capital***

The enactment in 1986 of the National Ordinance constituting the Central Bank Charter (P.B. 1985, no. 183) also introduced a Capital of NAF.30,000,000 (Article 3).

### **12.2 Notes to the the profit and loss account 1997**

#### ***12.2.1 Foreign exchange earnings***

These earnings result from the margin between the buying and selling rates applied by the Bank when trading in foreign currencies and from the differences in exchange rates arising from conversions and translations.

#### ***12.2.2 License fee***

As of January 1, 1996, the Bank charges the foreign exchange banks a monthly license fee, based on amendments to article 12 of the National Ordinance constituting the Central Bank Charter (P.B. 1985, no. 183). The National Ordinance Foreign Exchange Fee was revoked as of that same date. The license fee is calculated as a percentage of the gross outflow of money due to transfers from residents to nonresidents and foreign currency cash transactions, as stipulated by a National Decree holding general orders.