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Bank van de Nederlandse Antillen

REPORT OF THE PRESIDENT

1.1 General review

In 2002, the world economy recovered slightly from the downturn in 2001, despite a further decline in stock markets and increasing tensions in the Middle East. Economic performance varied widely by region. While the United States and some Asian countries registered moderate growth, most European economies weakened. In Latin America, the crisis in Argentina spilled over to neighboring Brazil and Uruguay, and the political turmoil in Venezuela deepened. The Caribbean region continued to suffer from the effects of the September 11, 2001, events on the tourism sector.

In line with the slight improvement in the world economy, the economy of the Netherlands Antilles registered marginal growth of 0.3% in real Gross Domestic Product in 2002. The increase in economic activity was attributable entirely to the improved export performance, as domestic demand declined. Producer and consumer spending deteriorated. Producers held back on investment decisions because of the uncertainties surrounding the IMF's approval of a program to address the financial-economic crisis at the end of 2001, the long period taken to form a government after the January elections, and the subsequent slow progress in the design of a program by the new government. In addition, the completion of various large investment projects in the tourism sector and at the refinery contributed to the decline in private investment. Consumer spending slowed due to the continuing net migration and uncertain job and income prospects. The decline in private spending was mitigated by an increase in government consumption supported by the ample availability of domestic financing. In contrast, public investment declined.

The unemployment rate decreased marginally to 14.2% in 2002, but is considered still high compared to international standards. Employment grew faster than unemployment, perhaps because of the grace period granted to illegal immigrants. In addition, the inflation rate tempered further from 1.7% in 2001 to 0.4% in 2002. This deceleration reflected the lower inflation of our main trading partners, the United States and the Netherlands, cheaper automobile prices resulting from the phasing-out of the economic levy, and lower airfares.

The improvement in our export performance was supported primarily by the international financial and business services sector. Activities increased significantly, reflected by strong growth in operational receipts. This favorable performance was mainly the result of the effectuation of the new tax arrangement for the Kingdom of the Netherlands (BRK) on January 1, 2002, ending a period of uncertainty in the sector. At the same time, some adjustments in the new fiscal regime (NFR) became effective. The NFR eliminated, among other things, the distinction between onshore and offshore activities in the Netherlands Antilles, a distinction that came be associated with harmful tax practices by the OECD and the European Union. With the effectuation of the new BRK and the NFR, our reputation as an international financial center and our competitive position in negotiating new tax treaties and the development of new financial products will be enhanced. Negotiations on tax treaties with Venezuela, Mexico, Spain, Italy, and the United States have started or will begin soon. An additional benefit of the new BRK is an increase in tax revenues -- the 8.3% withholding tax on dividends from the Netherlands to the Netherlands Antilles collected by the Dutch tax office will be transferred entirely to the Antillean government.

The tourism sector improved its performance in 2002, although developments varied by island. Curacao's tourism sector continued to perform well, as reflected by an expansion in both stay-over and cruise tourism. St. Maarten, which has the largest share in the Antillean tourism sector, did not recover fully from the aftermath of the September 11 attacks. This result was reflected by a decline in the number of stay-over visitors, although at a slower rate than in 2001. In contrast, the number of cruise visitors increased markedly. Moreover, Bonaire's tourism registered a recovery in both stay-over and cruise visitors. Combined, these developments resulted in a marginal decline in stay-over tourism, a strong increase in cruise tourism, and a moderate improvement in tourism-related foreign-exchange income earned in the Netherlands Antilles.

The transportation sector showed mixed developments in 2002, resulting in a decline in the generation of foreign exchange revenues. The transition of the former national carrier, Air ALM, into a new company, Dutch Caribbean Airline (DCA), was completed in the second half of 2002. DCA operates with a considerably smaller staff than Air ALM and started with a much healthier balance sheet. The combined activities of Air ALM and DCA indicated strong growth in 2002 in the number of passengers on the transatlantic route to Amsterdam, but a further decline in the number of passengers and the amount of cargo on the regional connections. DCA expects to close 2002 with a small profit. Together with an expansion of its fleet, the company has become attractive for a strategic partnership with a foreign carrier, which will secure its long-term viability. The ultimate objective is to privatize this government-owned company. The Bank welcomes the progress made in the overhaul of the national carrier, because of its importance for our tourism sector and, hence, the generation of foreign exchange.

Airport activities recorded divergent developments in 2002, with Curacao showing a decline and Bonaire an expansion in total passengers handled. This mixed result was attributable primarily to the shift in transit passengers due to the rerouting of the intermediate stops on some of KLM's flights between Amsterdam and Latin America from Curacao and Aruba to Bonaire. Excluding transit passengers, both airports recorded an increase in passenger arrivals and departures in line with the growth in stay-over tourism. Furthermore, the harbor industry performed well. Curacao's harbor recorded increases in ship calls, cargo handled, and bunker activities. Bonaire's harbor also noted an expansion in the number of ship calls. However, the rise in ship calls in both harbors was attributable entirely to the inter-island ferry connection between the islands. If the ferry connection is excluded, the number of ship calls declined on both islands, due to a decline in the number of tankers and freighters. The decline in tankers was related to the drop in oil storage and oil transshipment activities. Moreover, Curacao's ship repair sector performed poorly, as reflected by a decline in both the number of man-hours sold and ships repaired.

The oil refinery experienced a difficult year in 2002, as reflected by a marked drop in the number of barrels refined and an almost halving of the refining margin. The refinery had to cope with several plant shutdowns for repairs and maintenance. In addition, the political turmoil in Venezuela forced the refinery to discontinue operations in December because it ran out of storage capacity for refined products. This problem was related to the general strike in Venezuela that included the state oil company PDVSA, which leases the refinery from the Curacao government. As a result, the refined products could not be exported. Despite the short-term uncertainties related to the situation in Venezuela, the long-term viability of the refinery is enhanced by the progress on two major investment projects: (1) the Isla Refinery Upgrading Program (IRUP), completed in 2002, and (2) a new utility plant using the build-own-operate concept, which will be in full operation by the end of the second quarter of 2003. These projects will strengthen the refinery's competitiveness, improve its reliability, enhance its safety, and reduce its environmental impact.

Finally, the free zone sector in Curacao registered mixed developments. On the one hand, re-exports declined, due partly to the instability in Venezuela. On the other hand, the number of visits by shopping tourists increased significantly. In particular, visits by Jamaicans increased, supported by regular flights by Air Jamaica beginning in the fourth quarter of 2001.

The balance of payments again recorded a surplus in 2002, albeit considerably less than the unprecedented surplus in 2001. As a result, our international reserves position improved further, and our official reserves reached the international benchmark of three months of import coverage for the first time since 1988. Both the current account and the financial account contributed to the improvement in 2002. The capital account deteriorated, due to less development aid and fewer migrants' transfers received.

The improvement in the current account was the result of improvements in the trade, services, and current transfers balances. The trade deficit declined because of a drop in imports related to, among other things, fewer construction activities and lower average oil prices. The increase in the surplus on the services balance was due mainly to the good performance of the international financial and business services sector and the increase in receipts from tourism. The higher surplus in the current transfers balance resulted from a strong increase in transfers from abroad by individuals. These improvements were offset partly by a deterioration in the income balance, caused mainly by lower interest income on investments due to the decline in interest rates in the United States.

The improvement in the financial account was caused by a substantial decrease in the growth in foreign liabilities. This decrease was related to extraordinary developments in 2001, including the exceptional foreign borrowing by the domestic banking sector. In addition, the decline in imports implied that Antillean companies received less supplier credit on imports.

In the field of public finances, the general government recorded a substantial deterioration in its balance on a cash basis from a small surplus in 2001 to a considerable deficit in 2002. This deterioration was attributable entirely to the rise in expenditures as revenues declined moderately. In general, the higher expenditures were facilitated by the substantially improved access to domestic finance by the government in 2002, compared to 2001. The improved access was related to the attractive yield on local government securities vis-a-vis alternatives abroad. This situation contrasted sharply with 2001, when the government had to cope with net redemption of maturing debt for most of the year. As a result of the abundant availability of domestic finance in 2002, the government was able to meet its spending requirements according to the budget and reduce arrears.

The growth in expenditures was largely in current expenditures, as capital expenditures remained about the same. All current expenditure categories except transfers recorded growth. The increases in personnel costs and interest payments were most pronounced. The increase in personnel costs was due primarily to the strong improvement in the payment of regular contributions to the civil servants pension fund and the reduction of arrears in retained social premiums and wage taxes of government employees. In addition, the termination of the wage freeze caused a rise in wages and salaries. Interest payments increased because of the higher domestic debt, increased short-term financing, the formalization of arrears, and the payment of interest due on Dutch development loans for both 2001 and 2002. The decline in transfers was due mainly to the phasing-out of severance payments to laid-off civil servants. The drop in revenues was attributable primarily to nontax revenues because no dividends were received from government-owned companies, and the central bank transferred fewer earnings. Tax revenues remained about the same in 2002.

The high deficit contributed to the further accumulation of government debt in 2002, reaching more than 80% of GDP. Clearly, our debt situation needs urgent correction. The Bank welcomes the government's initiative to establish a committee to come up with recommendations for curbing further debt accumulation and suggestions for debt relief. It should be underscored, however, that realizing a sustainable debt position is inextricably linked to a lasting fiscal consolidation.

The money supply expanded significantly in 2002, attributable to both the domestic and external sectors. The expansionary impact of the external sector was caused by the further improvement in our balance of payments. The domestic money creation resulted mainly from the considerable increase in net credit extension to the government sector. This increase occurred because of the lifting of the limit on commercial banks' credit extension to the government as per March 1, 2002, and the attractive yield on domestic government securities compared to foreign investments. In addition, credit extension to the private sector gained some strength in line with the marginal recovery of the economy.

During 2002, the Bank further adjusted its monetary policy in light of the significant increase in our international reserves and the continuing decline in interest rates in the United States. One of the most important changes in the Bank's monetary policy was the introduction of bi-weekly auctions of Certificates of Deposit (CDs). As of January 1, 2002, banks can determine freely how many CDs they want to buy and at what rate. Furthermore, the reserve requirement percentage was reduced by 2.5 percentage points to 9% and is set for three months instead of one. However, the reserve requirement became entirely non-interest-bearing. In addition, the Bank reduced its pledging rate in five steps from 7.0% to 3.5%, bringing its official rates more in line with the declining trend in interest rates in the domestic money and capital market. This trend was related to the decline in international interest rates. Finally, as noted, the Bank lifted the ceiling on domestic credit extension by the commercial banks to the government on March 1, 2002, implying the inactivation of the monetary cash reserve arrangement. This decision was made because of the high level of foreign exchange reserves.

The slight economic recovery had a positive impact on the performance of the domestic banking sector. The sector's profitability improved. Nonperforming loan ratios decreased, indicating an improvement in asset quality. In addition, loan loss provisioning was strengthened further. The sector's capitalization remained above international standards, while its liquidity surplus remained high. Furthermore, activities in the international banking sector continued to grow at a healthy rate as measured in total assets. However, profits remained under pressure due to increased provisions and extraordinary losses. Nevertheless, the capitalization of the international banks remained well above international standards.

The Bank continued its efforts to enhance supervision of the institutional investors operating in the Netherlands Antilles. A new policy rule on integrity testing became effective June 2002. Furthermore, the Bank will adopt the Principles on the Minimum Requirements for the Supervision of Reinsures established by the International Association of Insurance Supervisors (IAIS) in

October 2002. On January 1, 2003, the National Ordinance on the Supervision of Investment Institutions and Administrators took effect, expanding the Bank's supervisory tasks with these institutions. Also the reporting of institutional investors was improved with the introduction of the Annual Reports Automated Statements (ARAS) in April 2002.

The Netherlands Antilles continued its efforts against money-laundering activities in line with international developments. Based on the recommendations of the Financial Action Task Force (FATF), it took actions to prevent terrorists or terrorist organizations from using the Antillean financial system. In addition, the IMF's assessment of our supervisory and legal infrastructure will be finalized in 2003. These efforts are aimed at strengthening the Netherlands Antilles as an internationally reputed financial center.

1.2 Policy considerations

The recovery of the Antillean economy is still fragile. Further strengthening of the economy is dependent on domestic and external factors. The world economic outlook for 2003 is surrounded by uncertainties related mainly to the development of the war in Iraq. Although those uncertainties are unlikely to wane anytime soon, world economic growth is expected to exceed that of 2002, which may contribute positively to our economic recovery.

On the domestic front, the economies of the Leeward and the Windward Islands registered diverging developments. While the main Windward island, St. Maarten, has not fully recovered from the post-September 11, 2001, decline in tourism, the largest economy of the Leeward Islands, Curacao, continued to grow. The resilience of Curacao's economy underscores the benefits of past structural reforms. The liberalization of labor and work permit legislation has boosted the labor-intensive tourism sector. In addition, progress in trade reform, further streamlining of the bureaucracy, and some reduction in red tape helped to attract more foreign investment.

Developments in public finances remained worrisome largely because of the lack of a credible program to address our fiscal ills. Doubts surrounding the budgetary projections for 2002 and the financial winding-up of the transition of Air ALM into Dutch Caribbean Airline resulted in a stand off in the fiscal area. In addition, most of 2002 was characterized by a lack of new policy initiatives due to the long time taken to form a new central government after the January elections and to design and agree on a government program.

In the absence of a fiscal consolidation program, fiscal discipline weakened, resulting in a significant deterioration of the general government's cash deficit to NAf.217 million in 2002. The 2003 budget indicates a further worsening of the deficit to NAf.314 million. As a consequence, government debt is rising rapidly. At the end of 2002, the debt-to-GDP ratio reached 80%, and it is expected to grow further by the end of 2003 with the formalization of funds deficits of the Social Security Bank. Clearly, this huge debt burden is unsustainable for our small open economy that is prone to external shocks.

The Bank welcomes the initiative of the government to establish a debt committee to address this issue. As noted, dealing with this issue is tantamount to achieving a sound macro-economic environment: that is, we have to (1) initiate new efforts to attain balanced budgets, and (2) design a growth strategy.

A first step on the path to balanced budgets is to substantially reduce the 2003 deficit. Areas that qualify for attaining this objective include health care reform, tax reform, pension reform, privatization, and improved control of extra-budgetary units.

Despite valuable recommendations by several committees and experts, little progress has been made in the reform of our health care system. Health care is one of the few areas that has escaped austerity measures, although its costs comprise about 11% of GDP, high by international standards. Therefore, the authorities should commit themselves to design and implement a credible package of health care measures without delay. These measures should include stringent cost controls for health care providers, limits on free health care, phasing-out the open-ended nature of health care payments through a general budgeting framework, and reducing diseconomies of scale and inefficiencies.

Two issues must be addressed with respect to tax reform: tax administration and the tax system. Streamlining and consolidating the tax assessment and collection apparatus must be finalized swiftly, while the restructured apparatus must be staffed adequately to guarantee efficient and effective tax collection. In addition, the comprehensive tax reform measures should be finalized as planned. These measures are aimed at lowering direct taxes with offsetting base-broadening measures and increasing indirect taxes as well as eliminating the cascading features of the current turnover tax. In the short-term, revenue neutrality must be ensured to avoid undermining the public finances.

Pension reform should remain high on the political agenda. Its importance is underscored by the recent court ruling forbidding the inclusion of the AOV franchise in the maximum benefit of current participants and the deteriorated funding ratio of the civil servants pension fund, APNA. In addition to dealing with the challenges of an aging population, reform measures should include a higher retirement age, higher premiums, and benefits based on the average wage instead of the final wage to guarantee adequate benefits to retired government employees in the future.

Privatization is another area of slow progress. The privatization process must be significantly accelerated, and the proceeds should be devoted exclusively to debt reduction. If outright privatization is not feasible in the short run, strategic partnerships and management contracts are valuable alternatives. This approach has been followed for the airport of Curacao and the postal services, both to become effective in 2003. Moreover, the authorities should accelerate the passing of legislation establishing an independent regulatory agency to regulate the privatization of monopolies.

A final area needing reform is government departments and agencies that have been transformed into more independent extra-budgetary units. These units reportedly have recorded significant expenditure increases, affecting the government budget directly through higher transfers or indirectly through higher costs for services provided. A mechanism must be put in place to reverse these developments and prevent a recurrence of this trend.

During the last six years, the central government and the island government of Curacao have made considerable progress toward restructuring the public finances. In contrast, the island governments of St. Maarten, Bonaire, St. Eustatius, and Saba have made little effort to restructure their public finances. As a result, deficits and arrears accumulated causing increasing liquidity constraints and, hence, recurring calls on the central government for financial support. These island governments also must embark on a major restructuring of their public finances similar to the measures taken by the central government and the island government of Curacao. The Bank welcomes the protocols agreed upon between the central government and the island governments of St. Maarten and Bonaire in November. These protocols tightly link financial support to the implementation of measures directed at a structural reduction of the budget deficits. Moreover, a similar protocol soon will be agreed upon with the island government of Saba.

The second prong for achieving sustainable public finances is the implementation of a debt-relief strategy. This strategy should focus on reducing the interest burden, which is projected to absorb almost 25% of total tax revenues in 2003. Such a high interest burden increasingly crowds out funds for important policy areas such as education, reducing crime, alleviating poverty, and improving infrastructure.

The need for further fiscal consolidation will be supported by an appropriately tight monetary policy. The significant increase in commercial banks' credit extension to the government was the main cause of monetary expansion in 2002. If left unchecked, this development ultimately will erode our international reserves position. Therefore, the Bank increased the reserve requirement percentage from 9.0% to 9.5% on January 16, and to 10.0% on April 16, 2003. The Bank advocates that commercial banks' credit extension be directed more towards the private sector, particularly foreign exchange-generating activities, which will contribute to a strengthening of the economic recovery. Furthermore, the Bank introduced some refinements in its auctions of certificates of deposit (CDs) to increase their attractiveness to the commercial banks, effective January 15, 2003.

The adjustment efforts of the last six years seem to have laid a foundation for re-establishing economic growth. However, to increase actual and potential economic growth, the structural changes that have been implemented together with fiscal consolidation must be continued and deepened to improve the economy's attractiveness for new productivity-increasing investment and to reverse the unsustainable government debt dynamics. Therefore, the Bank views with concern the discussion to roll back the important structural reforms made in the labor field. To adjust to an ever-changing global environment, our small open economy must have proper functioning markets with price and wage developments that enhance our competitive position. Undesirable side-effects should be corrected, but such actions must not interfere with the proper functioning of the market. Past reforms must not be reversed, but should be deepened to unleash the country's long-term growth potential.

To create a climate in which the nascent economic recovery can gain strength, the authorities must accelerate their efforts toward the further structural adjustment of our economy. These efforts should result in the full and timely implementation of a comprehensive and credible program focused on fiscal consolidation, structural reform, the promotion of growth, and the alleviation of poverty. This approach will promote the creation of much-needed jobs and a broad-based improvement in living standards.

E.D. Tromp
President

REAL SECTOR AND INTERNATIONAL DEVELOPMENTS

2.1 General economic developments

The world economy performed relatively well in 2002 despite a turbulent stock market, a recession in some South American nations, and the crisis in the Middle East. The United States and some Asian countries registered a growth, while some major European nations experienced a decline. The collapse of Argentina's economy in late 2001 had a negative impact on neighboring countries. In addition, the political turmoil in Venezuela contributed to the economic decline in South America.

In line with the global economic situation, the economy of the Netherlands Antilles showed a slight improvement in 2002, as real GDP drifted up by 0.3%.[1] This marginal growth was mainly the result of an enhancement in exports and government spending. The private sector continued to restructure as a consequence of weak domestic demand. The lower demand was partly the result of uncertainties in job opportunities and migration. The slight economic upturn was accompanied by a tame inflation and a beleaguered labor market. According to estimates[2] by the Bank, the unemployment rate remained high at 14.2% in 2002, a slight deceleration compared to the 14.5% in 2001. Consumer prices continued to subside in 2002 as annual inflation tapered to 0.4%.

2.1.1 National production and spending

Real GDP of the Netherlands Antilles was up slightly by 0.3% in 2002, following a decline in 2001. The 2002 economic growth came from an increase in foreign demand, supported by the cruise tourism sector, harbor activities and sea transportation, the financial sector, and telecommunication activity. Net exports improved, led by higher exports (0.3%) and a decline in imports (3.2%). In comparison with 2001, there were no major investments in 2002. Weak demand and a lack of producer confidence constrained investment, leading to a decline of 6.5%. Private consumption dropped by 2.2%, led by low consumer confidence as a result of doubts surrounding job and income prospects. In contrast, government consumption rose by approximately NAf.154.2 million, while public investment contracted by NAf.9.9 million. Overall, domestic demand shrank by 2.7%.

2.1.2 Inflation

Consumer prices continued to decelerate, as annual inflation in the Netherlands Antilles abated to 0.4% in 2002 from 1.7% in 2001. The price deceleration was due to (1) lower inflation of our major trading partners, the United States and the Netherlands; (2) a drop in the price of automobiles, owing to the phasing out of the economic levy; (3) cheaper airfares; and (4) special discounts on some goods.

An analysis by island indicates that St. Maarten had the highest inflation in 2002, followed by Curacao, while Bonaire showed a deflation. Consumer prices in Curacao remained subdued at 0.4% in 2002, down from the 1.8% inflation in 2001. The lower 2002 inflation stemmed from a fall in the

[1] All changes in real terms.

[2] Estimate for the Netherlands Antilles based on Arbeids Krachten Onderzoek (labor market survey) level by the CBS.

category "transport & communication" (-2.9%), supported by a price decline in vehicles and lower airfares. The phasing out of the economic levy on automobiles was mainly responsible for the lower car prices. Moreover, a deflation of 1.9% in "clothing & footwear" was caused by a price slide in clothing. The highest inflation came from "food" (3.7%), fueled mostly by costlier fresh produce. This increase was followed by "housing" (2.1%), up because of pricier utilities.

Table 2.1
Inflation rates for Curacao, Bonaire, and St. Maarten in 2001 and 2002 (% changes)

	Curacao		**Bonaire**		**St. Maarten**	
	2001	**2002**	**2001**	**2002**	**2001**	**2002**
Food	3.4	3.7	1.4	1.6	2.2	4.0
Beverages & tobacco	2.3	-0.4	-1.8	-1.4	-0.4	2.1
Clothing & footwear	-1.2	-1.9	0.0	0.0	0.1	-0.4
Housing	2.9	2.1	1.6	1.3	1.0	0.6
Housekeeping & furnishings	0.8	-1.2	-1.2	-2.0	1.4	0.8
Health	6.9	1.8	0.5	0.9	0.1	-0.1
Transport & communication	1.1	-2.9	3.2	-3.5	0.7	-2.8
Recreation & education	-0.5	-0.7	-0.1	0.0	1.3	1.4
Other	1.2	1.2	0.9	0.5	0.7	1.9
General inflation rate	1.8	0.4	1.2	-0.3	1.0	0.5

In 2002, St. Maarten's inflation decelerated to 0.5%, following a gain of 1.0% in 2001. The largest price surge took place in the category "food" (4.0%), as outdoor dining, meat & fish products, and fresh produce became more expensive. A price gain in "beverages" contributed to the inflation of 2.1% in "beverages & tobacco." Deflation occurred in the category "transport & communication" (2.8%), due to a price drop in airfares. Furthermore, the "clothing & footwear" category also registered a deflation of 0.4%.

During 2002, Bonaire's inflation tapered to -0.3% from 1.2% in 2001. Price declines in the categories "transport & communication" (-3.5%), "housekeeping & furnishings" (-2.0%), and "beverages & tobacco" (-1.4%) were responsible for the 2002 deflation. Similar to Curacao, lower-priced automobiles and airfares resulted in a deflation in "transport & communication." The drop in "housekeeping & furnishings" was attributed to a price cut in household expenses. As in Curacao, the highest price hike was in "food" (1.6%), driven by costlier fresh produce. The next largest price gain was in "housing" (1.3%), a result of higher-priced propane gas.

2.1.3 Labor market

The population in the Netherlands Antilles shrank by 2.2%[3] in 2002. Migration continued, but at a slower pace. At the same time, the flow of immigrants from regional countries to Curaзao persisted,

[3] Estimate by the BNA based on Census 2001.

due to the "grace period"[4] granted to people with an illegal status. The AKO[5] results showed an increase in the demand for labor. The estimated net employment in the Netherlands Antilles is predicted to have increased by 2.7% in 2002. The estimated unemployment rate in the Netherlands Antilles decelerated slightly from 14.5% in 2001 to 14.2% in 2002. The surge in the demand for employment may have been created by, among other things, the BOO project.

Beginning in August 2000, the Department of Labor no longer needed to approve the laying-off of individuals for the island of Curacao. This change had an impact on the labor market and other macroeconomic developments. A survey in the tourism sector suggests that the change in the law contributed lowering costs in the hotel sector, especially in times of low occupancy rates.

Table 2.2
Labor market in the Netherlands Antilles

	2001	**2002**
Population	173,151	169,356
Labor force	81,199	83,142
Unemployed	11,743	11,834
Unemployment rate (%)	14.5%	14.2%
Employed	69,456	71,308

Source: Bank van de Nederlandse Antillen estimates and A(rbeids) K(rachten) O(nderzoek) by the Central Bureau of Statistics

Compared to 2001, the number of people collecting welfare payments as well as welfare cancellations in Curacao shrank in 2002. The number of people collecting welfare declined for the following reasons: (1) some of the welfare recipients found employment; (2) some became eligible for the old age pension; and (3) it became more difficult to obtain welfare, as each application gets thoroughly scrutinized. In comparison to 2001, the number of cancellations dropped in 2002 because of the crackdown on ineligible welfare collectors in 2001.

[4] In 2001, the government of Curacao granted a grace period to illegal immigrants who entered the country before August 2001 to apply for a residence permit and/or work permit. This will allow these immigrants to reside and/or work for 2 years as long as they meet the following conditions: (a) employment, (b) no criminal record, and (c) certified birth certificate. The aim of this government policy was to obtain an indication of the number of illegal workers in Curacao.

[5] Arbeids Krachten Onderzoek (labor market survey) by the CBS.

Table 2.3
Development in welfare payments in Curacao

	2001	2002
Number of requests	574	232
Number of cancellations	1,255	1,088

Source: Dienst Werk en Inkomen.

2.2 Developments by sector

2.2.1 Mining

Through the year 2002, activities in Bonaire's salt industry declined. Salt exports fell by 7.0%, compared to the tumble of 35.8% in 2001. Production shrank by 3.6%, down from the jump of 34.9% a year ago.

2.2.2 Industry

Results of the "Isla" refinery in Curacao were gloomy in 2002, as oil refining contracted by 16.7%, after a surge of 5.4% in 2001. Oil refining was down, because of various plant shutdowns and the general strike in Venezuela in the fourth quarter. Due to the strike, the refinery could no longer export its refined products. At a certain moment, the refinery ran out of storage capacity and had to shut down the plants.

During 2002, Curacao's ship repair industry fell into a slump. The number of man-hours sold sagged by 10.6%, a deterioration compared to the growth of 32.6% in 2001. In addition, the number of ships repaired plunged by 21.4%, contrasting with the advance of 3.4% in 2001. In line with these poor developments, total earnings from ship repair dwindled by 19.7% to NAf.56.0 million in 2002.

2.2.3 Utilities

Utility production rose in the Netherlands Antilles, reflected by a gain in water and electricity production in 2002. Water production expanded in the last three quarters of 2002, leading to a higher output of 1.9%, up from a 1.7% decline in 2001. Increases in water production were reported on all three islands: Curacao (2.1%), Bonaire (4.4%), and St. Maarten (0.6%).

Electricity output grew by 2.5%, contrasting with the fall of 2.8% in 2001. This development is in line with the economic recovery. A breakdown by island shows that advances in Curacao (1.3%) and the Windward Islands (7.8%) led to the higher electricity production in 2002. Conversely, Bonaire recorded a decline of 4.0%, down from the decrease of 2.7% in 2001.

2.2.4 Trade

Developments in Curacao's free zone were mixed in the year 2002. The free zone re-exports decreased, as foreign exchange receipts shrank by 16.3% in 2002. The number of free zone visitors soared by 31.9%, measured against the gain of 4.4% in 2001. This buoyant result was due to increases in the principal markets, such as Jamaica, the Dominican Republic, Trinidad, and other

Caribbean islands. The inclusion of Air Jamaica flights to Curacao at the end of 2001 accounted for the more than two-fold increase in Jamaican visitors to the free zone.

2.2.5 Tourism

Tourism activity posted a mixed picture in the Netherlands Antilles in 2002, as stay-over arrivals shrank, while cruise tourism improved. Stay-over tourism fell by 1.0%, compared to a drop of 2.5% in 2001. Cruise tourism grew by 17.2%, in comparison to a decline of 0.9% in 2001. Both Curacao and Bonaire registered a growth in stay-over arrivals, while St. Maarten showed a decline. Total proceeds from tourism strengthened by 2.0% to NAf.1.3 billion in 2002.

Table 2.4
Developments in stay-over tourism per island (% change)

	Curacao		**St. Maarten**	
	2001	**2002**	**2001**	**2002**
North America, of which:	6.0	17.6	0.8	-1.2
-U.S.A.	7.1	20.5	2.7	-0.5
-Canada	-6.7	-21.8	-11.9	-6.5
Europe, of which:	11.8	-3.8	-20.0	-10.6
-The Netherlands	8.9	-2.3	-2.2	-9.8
-France	-	-	-22.3	-10.5
-Germany	-6.1	-5.0	-	-
-Other Europe	33.1	-10.2	-19.2	-11.2
South & Central America, of which:	2.8	0.4	-17.6	-46.1
-Venezuela	-6.3	-7.6	-25.3	-33.0
-Brazil	121.8	-41.0	-3.1	-33.5
-Other S&C America	15.7	17.5	-15.3	-51.9
Caribbean, of which:	-0.9	28.8	1.3	5.4
-Aruba	-11.2	21.6	-	-
-Santo Domingo	7.2	22.4	8.4	-26.0
-Other Caribbean	2.7	35.6	0.1	11.0
Rest of the World	56.3	-3.4	-8.1	-4.0
Total	7.0	6.5	-6.9	-5.4

In 2002, St. Maarten's tourism industry offered mixed results. Stay-over tourism remained in a slump, as arrivals dwindled by 5.4%, following a drop of 6.9% in 2001. Clearly, St. Maarten's tourism industry has not fully recovered from the aftermath of the September 11 attacks in 2001. The second half of 2002's advance in stay-over visitors was outweighed by the downturn in the first half of the year. Arrivals were down in almost all markets, except for the Caribbean (5.4%). Decreases occurred in the North American (1.2%), the European (10.6%), and the South American (46.1%) markets. Moreover, the hotel occupancy rate worsened by 20.0 percentage points to 32.0%. Cruise ship arrivals, however, increased by 21.6%, an improvement from the 0.1% slide in 2001.

In contrast to St. Maarten, Curacao's tourism sector performed stronger in 2002 than in 2001. Stay-over tourism expanded by 6.5%, compared to the gain of 7.0% in 2001. This expansion was caused mainly by the growth in the number of visitors from the United States (20.5%) and other Caribbean islands (28.8%). More arrivals from the other Caribbean islands may be related to the Air Jamaica flights that started at the end of 2001. Meanwhile, the contraction in the European market can be explained by the rerouting of some KLM flights from Curacao to Bonaire since the summer of 2002. In spite of the encouraging stay-over tourism figures, the hotel occupancy rate abated by 9 percentage points to 57%. The lower hotel occupancy rate stemmed from (1) an increase in the number of available hotel rooms; and (2) stay-over passengers shifting from the larger hotels to other commercial accommodation. In addition to the upbeat stay-over tourism, cruise passenger arrivals mounted by 6.2%, after a decrease of 2.4% in 2001.

During 2002, Bonaire's tourism registered an improvement of 4.1% in stay-over visitors, as opposed to a drop of 1.7% in 2001. This encouraging development was the result of a marked increase in the number of passengers from the island's main market: the Netherlands, owing to the rerouting of the stopover on KLM flights between Amsterdam and Latin America from Curacao and Aruba to Bonaire in June 2002. Cruise ship visitors grew by 4.1%, in contrast to a decline of 6.8% in 2001.

2.2.6 Transportation

Fewer activities were reported at Curacao's airport in 2002. The flow of transit passengers plunged by 42.1%, resulting in a fall in total passenger traffic by 9.7%. This poor performance was related to the rerouting of the stopover on the daily KLM flights between Amsterdam and Quito from Curacao to Bonaire in June. By contrast, passenger arrivals and departures were up by 4.6% and 5.1%, respectively, related to the good tourism performance. The number of commercial landings shrank by 9.8%, following a decline of 4.1% in 2001.

Unlike Curacao, activities at Bonaire's airport were favorable during the year 2002, as total passenger traffic swelled by 34.6%, aided mostly by more than a three-fold gain in the flow of transit passengers. This buoyant picture stemmed from the rerouting of the stopover on the KLM's Amsterdam-Quito flight from Curacao and the Amsterdam-Lima flight from Aruba to Bonaire. Moreover, the number of passenger arrivals and departures grew by 2.3% and 3.6%, respectively, in line with the growth in stay-over tourism. Alongside the positive total passenger traffic, the number of commercial landings rose by 16.9%, in contrast with last year's 10.5% decrease.

In 2002, Curacao's air transportation industry posted a mixed picture. The number of passengers on the transatlantic flight by the national carrier "Dutch Caribbean Airlines" (DCA) soared by 47.0%. Conversely, the number of passengers transported on the regional connections of DCA sagged by

19.0%, down from the 15.7% slide in 2001. Moreover, cargo shipments withered by 7.9%, following a drop of 13.9% in 2001. DCA is the successor of "Air ALM", which ceased its operations in the second quarter of 2002.

In 2002, oil transshipment in the Netherlands Antilles dropped by 24.5%, due largely to a decrease in activities in Bonaire (69.9%). Beside the dismal oil transshipment performance, oil storage in all three islands contracted by 42.6% in 2002.

Curacao's harbor industry posted a positive picture in 2002. The number of ships arriving into the harbor was up by 6.0%, after an advance of 8.2% in 2001. This growth stemmed from a marked increase in the category "other vessels" (92.4%), led by more inter-island ferry transfers between Bonaire and Curacao. Fewer tanker ships were reported, connected to the drop in oil transshipment. Despite fewer cargo ships, total cargo movements rose by 2.2%, because of more local and transshipment activities. Moreover, bunker sales of fuel and water expanded by 0.1% and 6.0%, respectively, in 2002.

Results of Bonaire's harbor sector were encouraging, as the number of vessels that entered the harbor swelled by 20.4% in 2002, compared to the rise of 6.9% in 2001. As in Curacao, this buoyant outcome was due to more inter-island ferry transfers between Bonaire and Curacao.

2.3 International economic developments

2.3.1 The United States

In 2002, the US economy grew by 2.4%, up from 0.3% in 2001. The 2002 growth was supported by consumer spending (4.5%) and government spending (6.2%), the latter largely from national defense (11.9%). In spite of worries about a possible war with Iraq, the turbulent stock market, and a higher jobless rate (5.8%), consumer spending was up. The contributors to the higher consumer spending were low interest rates, zero percent financing offers, rising home values, and extra cash left from a surge of home mortgage refinancing.

The labor market has been weak since the recession in March 2001. The corporate scandals, the stock market slide, and the threat of war in Iraq made companies reduce costs and delay hiring. To expand output, some companies preferred to raise flexible working hours rather than hiring new employees. As a result, productivity enhanced by 4.8%, while unit labor costs declined by 1.8%. The improved productivity and deep discounts in stores across the country kept inflation in check (1.6%) despite higher health care expenses, insurance premiums, and rising energy costs. The Venezuelan strike and the threat of war with Iraq pushed up the oil costs in the fourth quarter.

The corporate scandals that escalated in mid-May 2002 affected the stock market and weakened the US dollar against the currencies of its major trading partners. In November 2002, the Federal Reserve had its first rate cut for the year and its 12th since January 2001. The half percentage point reduction pushed the federal funds rate down to a 40-year low of 1.25 percent, hoping that it will stimulate the still-weak economy.

Table 2.5
Economic indicators of selected countries (% change)

	United States		Netherlands		Venezuela		Japan	
	2001	**2002**	**2001**	**2002**	**2001**	**2002**	**2001**	**2002**
Real GDP	0.3	2.4	1.3	0.3	2.7	-9.0	0.5	0.3
Cons. prices (%)	2.6	1.6	4.2	3.3	12.4	24.2	-0.9	-0.7
Unempl.rate (%)	4.9	5.8	2.4	2.5	13.7	15.5	5.1	5.4
Curr. acc. balance	-98	-126	2,255	2,364	1,129	2,161	1,101	1,417

(bln $/mln Ђ/mln $/bln Ґ)
Source: Bloomberg

For 2002, the US trade deficit widened by 14.9% to $435.2 billion, caused by the weak global economy, which led to a fall in exports (1.3%) for the second consecutive year. Rising imports (3.8%) and less demand abroad for US goods (-1.3%) broadened the current account deficit.

2.3.2 European Union

Real GDP growth in the euro zone decelerated to 0.8% in 2002, compared to 1.5% in 2001. The decline in investments contributed to the deceleration, but was offset partly by the surge in government and private consumption. The growth was concentrated in financial services & business activities, trade, transport & communication services, and other services sector.

Economic growth in the Netherlands decelerated to 0.3% in 2002, down from 1.3% in 2001. This performance was below the euro-zone average of 0.8%. Similar to 2001, government, education, and health care were the fastest growing sectors, followed by the chemical and food industries. Production dropped in manufacturing and trade. Exports were down, the first time in twenty years, as exporters experienced the effects of a delay in the economic recovery. Investment declined, as the private business sector reduced investment spending. Moreover, total portfolio investment of the pension funds and insurance companies in the Netherlands fell by 6.0% in 2002, as a result of the huge losses in the stock market. Both household and government spending grew in 2002.

Consumer prices[6] in the euro zone declined to an estimated 2.2% in 2002, in comparison to 2.4% in 2001. Germany (1.3%) and Belgium (1.6%) registered the lowest inflation rates, while inflation in the Netherlands was one of the highest in the euro zone. Inflation in the Netherlands was 3.3% in 2002, substantially lower than the 4.2% in 2001.

Unemployment in the euro zone increased to 8.4% in 2002, up from 8.0% in 2001. Unemployment in the Netherlands remained far below the euro-zone average. In the year 2002, 2.5% of the labor force was unemployed, compared to 2.4% in 2001. The slight increase in the unemployment rate eased the tension in the labor market. The results provided from a comparative study of Eurostat

[6] Harmonized price index.

indicated that 72.8% of women in the Netherlands work part-time,[7] the highest percentage in Europe.

2.3.3 The Caribbean region

According to ECLAC,[8] the Latin American and Caribbean countries performed poorly in 2002. The decline in economic activity was estimated at 0.5%, equivalent to a fall in per capita gross domestic product below 1997 levels. South American economies, particularly Argentina, Uruguay, and Venezuela, were the main contributors to the disappointing output. Moreover, the lack of dynamism was widespread throughout this region.

In 2002, the Caribbean tourism industry struggled to recover from the aftermath of the September 11th event. In the cruise liner industry, two companies -- American Classic Voyages and Renaissance Cruises -- went bankrupt. The companies that survived changed their itineraries closer to home.

Since 1973, Caricom has gradually eliminated all tariffs on intraregional trade and is working on common customs legislation. The next step will be the completion of a Single Market and Economy (CMSE). The CMSE, which is to be finalized in 2004 - 2005, is expected to promote competitiveness, higher levels of employment, more investment, trade expansion, and a stronger position in international trade negotiations. Moreover, the Caribbean Court of Justice (CCJ) will be operational in mid-2003. CCJ will be the institution of CMSE that has the authority to apply and amend the customs treaty.

2.3.4 Latin America[9]

In 2002, real GDP growth of Brazil -- South America's largest economy -- remained similar to 2001 at 1.5%. The 2002 growth leant on the export-oriented sectors, owing to the depreciation of the currency. Economic activity was restrained partly by the higher interest rates, putting a damper on investment and consumer spending. The overnight interest rate was raised to 25% in December 2002 to curtail inflation (12.0%), fueled largely by higher oil prices. Brazil's jobless rate was 11.6% in 2002.

After Argentina's $141 billion public debt default in December 2001, the recession deepened in 2002, as bank deposits were frozen and the peso devalued. Real GDP of Argentina contracted by 12.0% in 2002, compared to a decline of 4.4% in 2001. Consumer prices climbed by 41.0% after the peso lost about 70 percent of its value in January 2002. This currency plunge cut the purchasing power of the population and pushed more than half of the Argentines under the poverty line. About 20.0% of the Argentines were unemployed in 2002.

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[7] Fewer than 30 hours per week

[8] Economic Commission for Latin America and the Caribbean

[9] Estimate Latin American Monitor

After defaulting on loans from foreign investors in 2001, Argentina failed to secure a loan package from the International Monetary Fund (IMF) after 10 months of negotiations. As a result, the government defaulted on a \$680 million payment to the Inter-American Development Bank and an \$830.7 million payment to the World Bank in late 2002.

Real GDP of Venezuela contracted by 9.0% in 2002, a deterioration from the gain of 2.7% in 2001. Despite the high oil prices, the economy headed downwards, as internal disputes paralyzed production. The main declines occurred in the second and fourth quarters of 2002. The Venezuelan economy was hit by a general strike in December, reflecting the depth of the political polarization in the country. The strike curtailed oil exports to 500,000 barrels a day, down from 3 million barrels per day. Food shortages, reduction in domestic airline traffic by 60%, and a plunge in foreign investment of 66% was the result of the political impasse in Venezuela.

In February, monetary policy was changed to a floating exchange rate system. As a result, the Bolivar had depreciated by 83% at the end of 2002, compared to 2001. Consequently, consumer prices jumped to 24.2% in 2002 from 12.4% in 2001. In June 2002, the unemployment rate increased to 15.5%, compared to 13.7% in June 2001.

2.3.5 Japan

Japan's economic growth decelerated to 0.3% in 2002, down slightly from 0.5% in 2001. Stronger demand from abroad for Japanese goods was offset partly by a fall in domestic demand (0.4%), led by private demand. Net exports drifted up by 0.3%, as exports and imports rose by 6.6% and 1.4%, respectively. A higher demand from other Asian countries propped up 2002 exports. Amid falling wages and job cuts, household spending by salaried workers drifted down by 0.2% in 2002. Household income of salaried workers fell by 1.1%, and the jobless rate hit a record high of 5.4%. Continued deflation (0.7%) eroded corporate earnings and assets, forcing many companies to reform by slashing jobs, cutting capacity, and moving operations to China and elsewhere in Asia. The 2002 fall in consumer prices stemmed from a decline in housing rent, and lower clothing and household appliance prices.

PUBLIC SECTOR

3.1 Cash overview and financing

3.1.1 Introduction

The year 2002 was characterized by a loosening of fiscal policy. The implementation of fiscal reforms halted because no agreement had been reached with the IMF on a new financial-economic program by the end of 2001. Government expenditures increased, facilitated by the availability of domestic finance as domestic government securities became more attractive compared to lower-yielding foreign alternatives.

The general government[10] ended up with a deficit on a cash basis of NAf.216.9 million in 2002, compared to a small cash surplus of NAf.3.8 million in 2001. The primary surplus, i.e., the cash balance excluding interest payments, deteriorated significantly from 4.1% of GDP in 2001 to 0.6% of GDP in 2002. A marked increase of NAf.197.9 million in expenditures and a drop of NAf.22.8 million in revenues contributed to this development.

The increase in total expenditures was caused almost entirely by an increase of NAf.196.6 million in current expenditures. All current expenditure categories except transfers recorded an increase. Outlays for wages and salaries increased markedly by NAf.125.2 million due to, among other things, more pension contributions paid. Because government operations were not hampered by liquidity constraints, no net arrears were built up with the civil servants pension fund (APNA) in 2002. In addition, interest payments increased by NAf.56.9 million as a consequence of the rising stock of government debt. Furthermore, outlays for goods and services and for subsidies increased by NAf.29.0 million and NAf.19.0 million, respectively. These increases were offset partly by a drop of NAf.33.6 million in transfers. Finally, capital expenditures increased by NAf.1.4 million in 2002.

The drop of NAf.22.8 million in revenues in 2002 was almost entirely the result of a drop of NAf.25.3 million in nontax revenues. Grants dropped slightly by NAf.0.6 million. These decreases were mitigated by increases in tax revenues and capital revenues of NAf.1.3 million and NAf.1.8 million, respectively.

Table 3.1
Overview of cash operations of the general government 2000 - 2002 (in millions NAf.)

	2000	2001	2002
Total revenue	1,261.3	1,266.1	1,243.3
-Tax revenues	1,095.4	1,144.6	1,145.9
-Nontax revenues	117.6	109.4	84.1
-Capital revenues	1.4	0.6	2.4
-Grants	46.9	11.5	10.9

[10] The central government and island government of Cura3ao combined.

Total expenditures	1,362.4	1,262.2	1,460.2
-Current expenditures	1,296.6	1,212.6	1,409.1
-Capital expenditures	65.8	49.7	51.1
Balance	-101.1	3.8	-216.9

The drop in nontax revenues was mainly the result of less entrepreneurial and property income transferred to the government in 2002. Tax revenues registered a mixed development. Increases in taxes on goods and services (NAf.13.8 million), taxes on international trade and transactions (NAf.5.0 million), and other taxes (NAf.0.5 million), were largely mitigated by declines in taxes on income and profits (NAf.10.7 million) and on property (NAf.7.3 million).

Table 3.2
Selected key budgetary figures of the general government 2000 - 2002 (cash basis, % of GDP)

	2000	2001	2002
Revenues	26.4	26.7	26.1
Tax revenues	23.0	24.2	24.0
Expenditures	28.6	26.7	30.6
Wages and salaries	11.5	8.5	11.1
Interest payments	3.3	4.0	5.1
Investments	0.6	0.7	0.5
Balance	-2.1	0.1	-4.5
Primary balance[1)]	1.2	4.1	0.6
Tax burden[2)]	21.9	21.9	21.7
Collective burden[3)]	26.9	26.8	26.9

[1)] Balance excluding interest payments
[2)] Excluding taxes from the international financial and business sector.
[3)] Tax burden plus social premiums (AOV/AWW/AVBZ) collected by SVB and BZV.

The cash balance as a percentage of GDP deteriorated from a small surplus of 0.1% in 2001 to a substantial deficit of 4.5% in 2002. Revenues as a percentage of GDP dropped slightly by 0.6 percentage point to 26.1%, but the increase in expenditures by 3.9 percentage points to 30.6% of GDP in 2002 contributed in particular to the deterioration of the cash balance. Tax revenues as a percentage of GDP declined by 0.2 percentage point to 24.0%. The tax burden decreased by 0.2 percentage point to 21.7% of GDP, but the collective burden increased by 0.1 percentage point to 26.9% of GDP. The ratio of government investments to GDP dropped to 0.5% in 2002.

The government had no problems raising funds on the domestic capital market in 2002. Net borrowing amounted to NAf.221.0 million, considerably more than the NAf.21.7 million in 2001.

3.1.2 Central government

The cash deficit of the central government widened by NAf.88.5 million to NAf.127.1 million in 2002, compared to 2001. This development was the result of an increase of NAf.96.2 million in expenditures that outweighed an increase of NAf.7.7 million in revenues.

The increase in expenditures can be ascribed to increases in current and capital expenditures of NAf.87.6 and NAf.8.6 million, respectively. The current expenditure categories that contributed to the increase were wages and salaries (NAf.52.5 million), interest payments (NAf.28.8 million), subsidies (NAf.13.3 million), and goods and services (NAf.3.6 million). In contrast, transfers dropped by NAf.10.6 million.

The increase in wages and salaries was accounted for by increases of NAf.41.6 million in pension contributions and NAf.11.2 million in wages. More medical expenses and allowances of NAf.5.0 million and NAf.6.2 million, respectively, contributed to the increase in the wage component. The increase in pension contributions occurred because the central government paid part of its arrears in addition to the regular contributions in 2002.

The increase in interest payments resulted from increases in the domestic and foreign components of NAf.15.6 million and NAf.13.2 million, respectively. The increase in the domestic component was related to the higher domestic debt, the formalization of arrears, and increased short-term financing. The payment of interest on Dutch development loans due for both 2001 and 2002 caused the increase in the foreign component.

Furthermore, the increase in subsidies in 2002 can be explained by financial support provided to Air ALM (NAf.15.4 million), the predecessor of the current national carrier DCA, and the carrier of the Windward Islands Winair (NAf.2.2 million).

The drop in transfers was the result of lower transfers to households (NAf.10.7 million) related to the phasing-out of severance payments to laid-off civil servants (NAf.10.0 million).

Capital expenditures increased by NAf.8.6 million, reflecting increases of NAf.15.7 million in net lending and NAf.3.7 million in capital transfers, mitigated by a drop of NAf.10.8 million in investments. The increase in net lending was attributable to loans extended by the central government to Sint Maarten (NAf.14.0 million) and Bonaire (NAf.4.0 million) in connection with liquidity support.

The increase in revenues in 2002 was accounted for mostly by NAf.21.3 million higher tax revenues. The latter can be attributed primarily to the increases of NAf.12.5 million in taxes on goods and services, NAf.5.0 million in taxes on international trade and transactions, and NAf.3.3 million in taxes on property. The increase in taxes on goods and services can be explained by increases of NAf.8.0 million in sales & turnover tax revenues and NAf.5.1 million in gambling and other licenses. The more buoyant sales & turnover tax revenues were caused entirely by the NAf.8.4 million increase in revenues on the Leeward Islands. The increase in gambling and other licenses was due to the settlement of 2001 license fees due by the Telecommunication and Postal Services Bureau (NAf.5.9 million), which were transferred in addition to the 2002 license fees. Furthermore, the increase in taxes on international trade and transactions was entirely the result of more import duties collected (NAf.5.3 million), related to the gradual economic recovery. Finally, the higher property taxes resulted from increases of NAf.2.0 million in inheritance and gift taxes and NAf.1.3 million in property transfer tax.

The NAf.13.1 million drop in nontax revenues can be explained mainly by the NAf.12.4 million drop in entrepreneurial and property income, because the central bank transferred less earnings (NAf.11.8 million) in 2002.

Table 3.3
Overview of cash operations of the central government 2000 - 2002 (in millions NAf.)

	2000	2001	2002
Revenues	658.3	608.8	616.5
- Tax revenues	519.0	512.3	533.6
Taxes on property	17.0	14.5	17.8
Taxes on goods and services, of which:	363.5	369.9	382.4
Excises	115.1	116.4	115.8
Sales and turnover tax	231.8	242.3	250.3
Gambling and other licenses	16.6	11.2	16.3
Taxes on international trade and transactions, of which:	128.1	122.7	127.7
Import duties	126.5	121.7	127.0
Other taxes	10.4	5.2	5.7
-Nontax revenues, of which:	92.3	85.0	71.9
Entrepreneurial and property income	55.6	63.8	51.4
Fees, charges, and sales	34.7	20.1	19.1
-Grants	46.9	11.5	10.9
Expenditures	729.6	647.4	743.6
-Current	674.2	616.6	704.2
Wages and salaries	248.6	199.9	252.4
Goods and services	96.1	82.6	86.2
Interest payments	77.2	94.8	123.6
Subsidies	10.8	4.3	17.6

Transfers	241.5	235.0	224.4
-Capital	55.4	30.8	39.4
Investment	16.3	21.0	10.2
Capital transfers	35.5	8.1	11.8
Net lending	3.6	1.7	17.4
Balance	-71.2	-38.6	-127.1

The central government's cash deficit was financed mainly monetarily in 2002 (see table 3.4). The monetary financing occurred largely through the commercial banks (NAf.162.4 million) due to the purchase of government securities. The negative monetary financing through the central bank resulted, however, from a reduction in central government securities in portfolio. Government securities with the public declined also, by NAf.16.0 million.

Table 3.4
Financing of the cash deficit of the central government (in millions NAf.)

	2000	2001	2002
Cash balance	-71.2	-38.6	-127.1
Monetary financing	6.8	36.8	121.0
-Central bank	6.7	49.6	-41.8
-Coins & notes	1.2	0.9	0.4
-Commercial banks	-1.1	-13.8	162.4
Nonmonetary financing	64.4	1.8	6.1
-Government securities with the public	-13.9	-30.2	-16.0
-Other	78.3	32.0	22.1

3.1.3 Island Government of Curaзao

The operations of the island government of Curacao resulted in a deficit on a cash basis of NAf.89.8 million in 2002, a turnaround compared to the NAf.42.5 million surplus in 2001. An increase of NAf.104.8 million in expenditures and a drop of NAf.27.5 million in revenues contributed to this development. The increase in expenditures was attributable entirely to NAf.112.0 million more in current expenditures; capital expenditures dropped by NAf.7.1 million. In current expenditures, wages and salaries showed the biggest increase (NAf.72.7 million), followed by the increases in interest payments (NAf.28.1 million), outlays for goods and services (NAf.25.4 million), and subsidies to public companies (NAf.5.7 million). These increases were mitigated by a NAf.20.0 million drop in transfers.

The increase in wages and salaries can be broken down into increases of NAf.29.9 million in gross wages and NAf.42.8 million in pension contributions. The increase in gross wages occurred mainly because the government paid arrears in retained employees' pension premiums, social security premiums, and wage taxes. In addition, the termination of the wage freeze led to a general raise. The increase in pension contributions resulted from improved compliance with the monthly payments to the civil servants pension fund. Overall, the increased expenditures on wages and salaries and goods and services can be ascribed to a substantial reduction in payment arrears, because no liquidity constraints were encountered in 2002.

The increase in interest payments was due mainly to higher domestic interest payments related to an increase in outstanding government securities and a shift into shorter maturities (one year and less).

The drop in transfer payments was attributable to nonprofit institutions and households. Transfers to nonprofit institutions declined (NAf.11.5 million) due to the settlement of a claim of the island receiver on the former national carrier ALM in 2001 that did not recur in 2002. The drop in transfers to households (NAf.10.4 million) resulted from the phasing out of severance payments to laid-off civil servants.

Finally, the drop in capital expenditures was attributable to a drop of NAf.8.0 million in capital transfers. The latter was related to the settlement of a claim in connection with a hotel project in 2001.

Table 3.5
Overview of cash operations of the island government of Curacao 2000 - 2002 (in millions NAf.)

	2000	**2001**	**2002**
Revenues	758.4	775.9	748.4
-Tax revenues	576.4	632.3	612.3
Taxes on income and profits	512.0	578.8	568.1
Profit tax	165.4	196.3	187.2
Wage tax	335.6	389.8	393.3
Income tax	11.0	-7.3	-12.4
Taxes on property	28.6	25.4	14.8
Land tax	21.2	17.8	10.9
Occupancy tax	7.4	7.6	3.9
Taxes on goods and services	35.8	28.1	29.4
-Nontax revenue, of which:	25.3	24.4	12.2
Entrepreneurial and property income	2.8	7.8	0.2
Fees, charges, and sales	13.7	11.4	9.4
-Capital revenue	1.3	0.6	2.3
-Grants	155.4	118.6	121.6
Expenditures	788.3	733.4	838.2
-Current	777.8	714.5	826.5
Wages and salaries	297.8	203.1	275.8

Goods and services	219.3	192.6	218.0
Interest payments	82.5	93.7	121.8
Subsidies	51.1	53.2	58.9
Transfers	127.0	172.0	152.0
-Capital, of which:	10.5	18.9	11.8
Investment	10.5	10.9	11.7
Balance	-29.9	42.5	-89.8

The NAf.27.5 million drop in revenues in 2002 was caused by decreases of NAf.20.0 million in tax revenues and NAf.12.2 million in nontax revenues. These decreases were mitigated by increases in capital revenues and grants of NAf.1.7 million and NAf.3.0 million, respectively.

Taxes on income and profits and taxes on property dropped by NAf.10.7 million and NAf.10.6 million, respectively. In contrast, taxes on goods and services increased by NAf.1.3 million.

The drop in taxes on income and profits can be ascribed to decreases of NAf.9.1 million in the profit tax and NAf.5.1 million in the income tax. The latter was due to even higher rebates in 2002 than in 2001. These decreases were mitigated by an increase of NAf.3.5 million in the wage tax. The decline in taxes on property was the result of decreases in the land tax and occupancy tax of NAf.6.9 million and NAf.3.7 million, respectively. The decrease in the land tax occurred because no assessments were made in 2002 due to administrative problems. The decline in the occupancy tax is related to its abolishment as of January 1, 2002.

The modest increase in taxes on goods and services was caused by an increase of NAf.3.1 million in motor vehicle taxes, mitigated mainly by a NAf.1.7 million drop in fees for licenses.

The lower nontax revenues was the result of decreases in entrepreneurial and property income, fees, charges, and sales, and other nontax revenues of NAf.7.6 million, NAf.2.0 million, and NAf.2.6 million, respectively. Entrepreneurial and property income fell because no dividends were received from government-owned companies in 2002. The drop in fees, charges, and sales was related to a backlog in the assessment of land lease. Finally, grants increased by NAf.3.0 million in 2002 as more income was received from the central government related to revenue sharing.

The island government of Curaзao financed its cash deficit primarily nonmonetarily in 2002 because of an increase in outstanding government securities with the public by NAf.89.6 million. The monetary financing occurred through the commercial banks (NAf.42.0 million) due to an increase in island government securities in portfolio (NAf.64.7 million). A decline in island government securities in portfolio (NAf.44.5 million) contributed to a monetary contraction (NAf.23.0 million) through the central bank.

Table 3.6
Financing of the cash deficit of the island government of Curacao (in millions NAf.)

	2000	2001	2002
Cash balance	-29.9	42.5	-89.8
Monetary financing	14.1	18.5	19.0
-Central bank	55.9	-3.9	-23.0
-Commercial banks	-41.8	22.4	42.0
Nonmonetary financing	15.8	-61.0	70.8
-Government securities with the public	-11.1	-12.0	89.6
-Other	26.9	-49.0	-18.8

3.2 Public sector debt

3.2.1 Introduction

The total consolidated public debt of the Netherlands Antilles increased by NAf.353.2 million (10.1%) to NAf.3.842 billion in 2002, or 80.6% of GDP. Increases in both the domestic component and the foreign component of NAf.228.6 million (7.9%) and NAf.124.5 million (21.0%), respectively, contributed to this development.

Table 3.7
Public sector debt (in millions NAf.; end of year)

	2000	2001	2002
Domestic debt[1)]	2,723.5	2,895.1	3,123.7
Foreign debt	619.4	593.6	718.1
Total debt	3,343.0	3,488.6	3,841.8
% of GDP	70.1%	73.7%	80.6%

[1)] Consolidated.

3.2.2 Public sector domestic debt

The increase in the domestic debt of the Netherlands Antilles in 2002 was attributable to all governments. The NAf.136.2 million (10.0%) increase in the debt of the central government can be ascribed to increases in government securities in the commercial banks' portfolios of NAf.159.9 million and in arrears to the Social Security Bank (SVB) of NAf.31.0 million. These increases were mitigated by drops in government securities in the central bank's portfolio (NAf.26.5 million), in securities with the public (NAf.16.0 million), in arrears at the civil servants pension fund APNA

(NAf.6.9 million), and in other debt (NAf.5.3 million). Noteworthy is that total outstanding central government securities rose by NAf.117.4 million.

The total domestic debt of the island government of Curacao increased by NAf.141.8 million (7.7%) in 2002, caused mainly by increases in island government securities with the public, commercial bank debt, and the debt to the central government[11] of NAf.89.7 million, NAf.59.2 million[12], and NAf.64.0 million, respectively. These increases were mitigated by drops in government securities with the central bank and in arrears to other creditors of NAf.44.5 million and NAf.34.7 million, respectively.

Table 3.8
Composition of public sector domestic debt (in millions NAf., end of year)

	2000	2001	2002
Central government, of which:	1203.4	1366.2	1502.4
Central bank	70.7	125.5	99.0
Commercial banks	74.0	67.5	227.4
Government securities with the public	849.0	818.8	802.8
Social Security Bank (SVB), arrears	68.0	86.2	117.2
Civil servants pension fund (APNA), arrears	69.5	167.0	160.1
Other	72.2	101.2	95.9
Island government of Curaзao, of which:	1830.3	1851.9	1993.7
Central bank	70.8	89.0	44.5
Commercial banks	101.1	122.7	181.9
Government securities with the public	348.6	336.5	426.2
Civil servants pension fund (APNA), arrears	758.6	806.4	814.5
Central government	390.1	334.6	398.6
Arrears to other creditors	161.1	162.7	128.0
Other island governments, of which:	242.7	220.7	274.6
Civil servants pension fund (APNA), arrears	74.2	18.8	28.3
Central government	168.5	201.9	246.3

[11] Related to, among other things, arrears in the payment of health insurance premiums for family members of civil servants and the final settlement of claims and debts with the central government.

[12] NAf.64.7 million of which was in island government securities.

Total consolidated domestic debt	2723.5	2895.1	3123.7

Finally, the total identified debt of the other island territories amounted to NAf.274.6 million in 2002, of which NAf.145.0 million can be ascribed to Sint Maarten, NAf.107.9 million to Bonaire, NAf.14.1 million to Saba, and NAf.7.6 million to Sint Eustatius. Arrears to the civil servants pension fund APNA increased by NAf.9.5 million, while the debt to the central government increased by NAf.44.4 million in 2002. The latter was related to budget support, and increasing arrears in the payment of health insurance premiums for family members of civil servants, debt service payments, and other claims of the central government.

3.2.3 Public sector foreign debt

The increase in the foreign debt in 2002 can be ascribed mainly to the 19.0% depreciation of the US dollar, to which the Netherlands Antilles guilder is pegged, against the Euro. This depreciation caused a rise in the guilder-equivalent of the Euro-denominated debt of approximately NAf.90 million. Furthermore, the Dutch government provided NAf.40 million additional financial support in the form of a concessional loan to alleviate the impact of the September 11 events on the Netherlands Antillean economy.

THE EXTERNAL SECTOR

4.1 General overview

The external reserves position of the Netherlands Antilles improved by NAf.135.2 million in 2002. This improvement was considerably smaller than the NAf.415.1 million increase recorded in 2001.

The increase in reserves in 2002 was attributable primarily to the improvement in the current account of the balance of payments. The trade deficit improved as a result of declining imports. In addition, the services balance improved because of a moderate recovery in foreign exchange earnings from tourism and the good performance of the international financial and business services sector. These improvements were enhanced by a considerable increase in transfers to individuals from abroad.

The capital and financial account improved primarily as a result of the increase in our reserve assets. Overall, the NAf.135.2 million balance of payments surplus resulted in an international reserves position of NAf.1,186.7 million, including gold, at the end of 2002 (graph 4.1).

Graph 4.1
Developments in net international reserves (in millions NAf.)

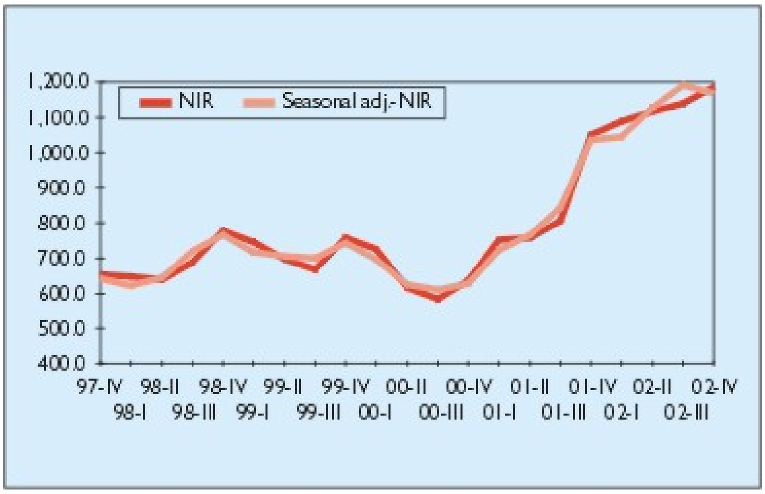


Table 4.1
Balance of payments summary[№)] (in millions NAf.)

	2001	2002	Diff.
Current account	-388.7	-90.3	298.4
Capital account	66.5	49.7	-16.8
Financial account, of which:	214.5	-32.4	-246.9
-Change in reservesI)	-415.1	-135.2	279.9
Statistical discrepancies	107.7	73.0	-34.7
Memorandum item			
Change in reservesI)	-415.1	-135.2	279.9
-with commercial banks	-342.8	53.1	395.9
-with central bank	-72.3	-188.3	-116.0

1) Transaction basis.
2) -Sign denotes an increase in reserves (excluding gold).

4.2 The current account

The current account of the balance of payments reached a deficit of NAf.90.3 million in 2002, a NAf.298.4 million improvement compared to 2001. This improvement was the result of developments in the current transfers, trade, and services balances, which improved by NAf.180.1 million, NAf.99.5 million, and NAf.56.9 million, respectively (table 4.2). In contrast, the income balance deteriorated by NAf.38.1 million in 2002.

Table 4.2
A breakdown of the current account[1)] (in millions NAf.)

	2001	2002	Diff.
Trade balance	-2,062.3	-1,962.8	99.5
-Exports	1,140.6	1,030.0	-110.6
-Imports	3,202.9	2,992.8	-210.1
Services balance	1,609.1	1,666.0	56.9
Receipts, of which:	2,958.4	3,096.5	8.1
-Travel	1,341.5	1,368.3	26.8
-Transportation	316.1	304.6	-11.5
-Other services, of which:	1,300.8	1,423.6	122.8
Int. fin. & bus. services sector	549.2	731.3	182.1
Expenses, of which:	1,349.3	1,430.5	1.2
-Travel	465.8	553.4	87.6

-Transportation	160.3	154.5	-5.8
-Other services, of which:	723.2	722.6	-0.6
Int. fin. & bus. services sector	194.9	202.4	7.5
Income balance[2)]	29.5	-8.6	-38.1
Current transfers balance,[3)] of which:	35.0	215.1	180.1
Profit taxes	87.3	83.7	-3.6
Balance	-388.7	-90.3	298.4

1) Transaction basis.
2) Labor and investment income.
3) Public and private transfers.

4.2.1 The trade balance

The improved trade balance for the year 2002 was the result of a NAf.210.1 million decline in imports that surpassed the NAf. 110.6 million decline in exports. Imports declined due to lower imports of general merchandise, oil products, and goods for processing. The decline in general merchandise imports can be explained, among other things, by fewer construction activities. Furthermore, the lower average oil prices in 2002 contributed to the decline in imports of oil products.

The decrease in exports was due mainly to goods procured in ports, related also to the lower oil prices. Furthermore, all other categories of exports, except goods for processing, contributed to the overall drop in exports.

A breakdown by island reveals that the trade balances of Curaзao and Bonaire improved considerably by NAf.103.6 million and NAf.15.2 million, respectively. In contrast, the trade balance of the Windward Islands deteriorated by NAf.19.3 million.

Table 4.3
A breakdown of the trade balance[№)] (in millions NAf.)

	2001		2002		Diff.	
	Export	Import	Export	Import	Export	Import
Bonaire	16.7	73.6	22.4	64.1	5.7	-9.5
-General merchandise	5.7	70.7	13.5	56.3	-2.2	-14.4
-Oil products	-	1.1	-	0.6	-	-0.5
-Goods for processing	1.0	1.8	8.9	7.3	7.9	5.5
-Repair on goods	-	-	-	-	-	-
-Goods procured in ports (bunker)	-	-	-	-	-	-

Curacao	796.1	2,336.3	714.2	2,150.7	-81.9	-185.5
-General merchandise,	577.1	2,012.1	553.3	1,849.5	-23.8	-162.6
of which: free zone	472.3	585.7	395.3	496.6	-77.0	-89.1
-Oil products	-	248.6	-	247.7	-	-0.9
-Goods for processing	16.4	62.9	18.6	37.7	2.2	-25.2
-Repair on goods	69.7	-	56.0	2.5	-13.7	2.5
-Goods procured in ports (bunker)	132.9	12.6	86.3	13.3	-46.6	0.7
Windward Islands	327.8	793.0	293.4	778.0	-34.4	-15.1
-General merchandise	78.3	539.5	94.1	566.8	15.8	27.3
-Oil products	21.3	252.9	12.9	211.1	-8.4	-41.8
-Goods for processing	0.1	0.6	-	-	-0.1	-0.6
-Repair on goods	-	-	-	-	-	-
-Goods procured in ports (bunker)	228.1	0.1	186.4	0.1	-41.7	-
Netherlands Antilles	1,140.6	3.202.9	1,030.0	2,992.8	-110.6	-210.1
-General merchandise,	671.1	2,622.3	660.9	2,472.6	-10.2	-149.7
of which: free zone	472.3	585.7	395.3	496.6	-77.0	-89.1
-Oil products	21.3	502.6	12.9	459.4	-8.4	-43.2
-Goods for processing	17.5	65.3	27.5	45.0	10.0	-20.3
-Repair on goods	69.7	-	56.0	2.5	-13.7	2.5
-Goods procured in ports (bunker)	361.0	12.7	272.7	13.4	-88.3	0.7

1) Transaction basis.

The improvement in the trade balance of Curacao was mainly the result of a drop in general merchandise imports. This drop was caused mainly by a decline in free zone imports and fewer construction-related imports compared to 2001. Furthermore, the import of goods for processing declined. The decline in exports was caused by the free zone, bunker, and repair on goods. The latter was due to the decline in activities in the ship repair sector.

The trade balance of Bonaire improved mostly because imports of general merchandise decreased. In contrast, exports of goods for processing grew because of an incidental sale of oil waste products.

The trade balance of the Windward Islands deteriorated due to declining exports. This decline was attributable mainly to a decrease in exports of goods procured in ports related to bunkering. In addition, imports of general merchandise increased, which can be related to the gradually recovering tourism industry after the event of September 11, 2001.

4.2.2 The services balance

The surplus on the services balance increased by NAf.56.9 million in 2002 compared to 2001. This improvement was caused mainly by the good performance of the international financial and business services sector.

4.2.2.1 Tourism

Foreign exchange receipts from the tourism sector increased by NAf.26.8 million (2.0%) in 2002 compared to 2001, mainly as a result of the increases in foreign exchange earnings from stay-over tourism on Curaзao and cruise tourism on the Windward Islands. As can be seen in table 4.4, these increases were mitigated mainly by the poor performance of stay-over tourism on the Windward Islands, which has not yet recovered fully from the impact of the September 11, 2001, event. Furthermore, increased cash withdrawals of foreign exchange and increased credit card payments abroad explain the NAf.87.6 million higher expenses on tourism in 2002.

Table 4.4
Foreign exchange earnings from tourism per island№) (in millions NAf.)

	2001	2002	Diff.	%
Bonaire2)	115.2	112.7	-2.5	-2.2
-Stay-over	109.8	106.8	-3.0	-2.7
-Cruise	5.4	5.9	0.5	9.3
Curaзao	360.6	386.0	25.4	7.0
-Stay-over	320.5	344.5	24.0	7.5
-Cruise	40.1	41.5	1.4	3.5
Windward Islands	865.7	869.6	3.9	0.5
-Stay-over	676.7	640.5	-36.2	-5.3
-Cruise	189.0	229.1	40.1	21.2
Netherlands Antilles	1,341.5	1,368.3	26.8	2.0
-Stay-over	1,107.0	1,091.8	-15.2	-1.4
-Cruise	234.5	276.5	42.0	17.9

1) Transaction basis
2) Bonaire's tourism earnings were estimated by the Bank because the data on the number of tourists were not available.

4.2.2.2 Transportation

Net earnings in the transportation sector decreased by NAf.5.7 million in 2002, compared to 2001. This decrease was the result of a decline in earnings of NAf.11.5 million, offset partly by a decrease in expenses of NAf.5.8 million. Although earnings from passenger air transport increased, these earnings were outweighed by the decrease in earnings from sea transport and air freight. Expenses on travel by air decreased, partly as a result of lower air fares after the September 11 event.

4.2.2.3 Other services

Net earnings from other services increased by NAf.123.4 million in 2002 compared to 2001. This improvement can be attributed to the good performance of the international financial and business services sector. Activities increased because the uncertainties surrounding the new tax arrangement for the Kingdom of the Netherlands (BRK) and the new fiscal regime (NFR) ended with the effectuation of these arrangements on January 1, 2002.

Net operational earnings of the international financial and business services sector increased by NAf.174.6 million, attributable entirely to the NAf.182.1 million improvement in operational income. In contrast, profit taxes paid by the sector[13] to the government decreased slightly by NAf.3.6 million.

The increased net earnings from this sector were mitigated by a decrease in the refining fee of the oil refinery, related to lower oil prices.

4.2.3 The income balance

The NAf.29.5 million surplus on the income balance in 2001 turned around in a NAf.8.6 million deficit in 2002. The main cause of this deterioration was the drop in net interest income on investments, due to the decrease in interest rates in the United States. This drop was enhanced by a decrease in net labor income from abroad.

4.2.4 The current transfers balance

The surplus on the current transfers balance improved by NAf.180.1 million to NAf.215.1 million in 2002 compared to 2001. This development can be ascribed entirely to the strong increase in transfers from abroad by individuals to Antillean residents. Most of these personal transfers originated in the Netherlands. This development began in the fourth quarter of 2001. The increase in incoming transfers was offset partly by higher workers' remittances and family transfers abroad by Antillean residents.

Table 4.5
Breakdown of the current transfers (in millions NAf.)[1)]

	2001		**2002**		**Diff.**	
	Debit	**Credit**	**Debit**	**Credit**	**Debit**	**Credit**
General government	106.2	17.2	125.0	16.3	18.8	-0.9
-Profit taxes	87.3	0.0	83.7	0.0	-3.6	0.0
-Other government transfers	18.9	17.2	41.3	16.3	22.4	-0.9

[13] Recorded in the current transfers account.

Other sectors	285.8	339.8	508.3	401.9	222.5	62.1
-Workers' remittances	21.8	21.0	35.6	36.2	13.8	15.2
-Other current transfers, of which:	264.0	318.8	472.7	365.7	208.7	46.9
-Family transfers	141.6	143.9	396.4	199.1	254.8	55.2
Balance	392.0	357.0	633.3	418.2	241.3	61.2

1) Transaction basis

4.3 The capital and financial account

The combined capital and financial account improved by NAf.230.1 million in 2002, compared to 2001, the result of an improvement in the financial account, as the capital account deteriorated.

4.3.1 The capital account

The surplus on the capital account decreased by NAf.16.8 million to NAf.49.7 million in 2002. This development was due to, among other things, decreases in funds received for development aid and in migrants' transfers from abroad.

4.3.2 The financial account

Table 4.6 indicates that the improvement of the financial account can be attributed to a decrease in foreign liabilities of NAf. 339.1 million, offset partly by a decrease in foreign assets of NAf.92.2 million.

The decrease in liabilities was mainly the result of a decline in other investment liabilities. One of the reasons these investment liabilities declined was a drop in loans received by the Netherlands Antilles from abroad. Extraordinary developments in 2001 contributed to this outcome. First, a commercial bank contracted a large loan from abroad. Second, the locally operating RBTT Bank purchased part of the international ABN-AMRO operations. Therefore, other investment liabilities, under which these transactions were recorded in 2001, registered a substantial decrease in 2002. In addition, credit received on imports increased less in 2002 than in 2001.

Foreign assets increased less in 2002 than in 2001, also related to the developments in 2001. First, the exceptional foreign borrowing by a commercial bank was invested in foreign assets. Second, the integration of the international operations of ABN-AMRO into the local RBTT Bank operations resulted also in an increase in foreign assets.

The smaller increase in reserve assets was offset partly by an increase in other investment assets abroad. This increase can be explained by fewer funds repatriated from abroad, on the one hand, and more funds invested abroad by pension funds and other investment companies, on the other hand. In addition, Antillean companies extended more trade credit on exports.

Table 4.6
Breakdown of the financial account[1] (net flows, in millions NAf.)

	2001	2002	Diff.
Direct investment	-2.4	-29.5	-27.1
-Abroad[2]	-0.8	-1.9	-1.1
-In the Netherlands Antilles[3]	-1.6	-27.6	-26.0
Portfolio investment[2]	-47.4	-67.1	-19.7
-Abroad[2]	-47.0	-68.7	-21.7
-In the Netherlands Antilles[3]	-0.4	1.6	2.0
Other investment	679.4	199.4	-480.0
-Assets[2]	138.4	-26.5	-164.9
-Liabilities[3]	541.0	225.9	-315.1
Reserves[4]	-415.1	-135.2	279.9
Balance	214.5	-32.4	-246.9
Memorandum item			
Financial account broken down in			
-Assets[2]	-324.5	-232.3	92.2
-Liabilities[3]	539.0	199.9	-339.1

1) Transaction basis.
2) A -sign means an increase in assets.
3) A -sign means a decrease in liabilities.
4) A -sign means an increase in reserve assets.

MONETARY DEVELOPMENTS

5.1 Introduction

During 2002, international reserves continued to increase. The increase of NAf.135.2 million (13.4%) during 2002 did not match that recorded in 2001, but was still considerable. In the third quarter of 2002, official reserves reached the targeted level of three months of goods imports, the first time since 1988. The increase in international reserves and, hence, net foreign assets was caused by several factors. The most important factor was a rise in capital inflows due to the repatriation of funds and foreign borrowing. The repatriation of funds was triggered by decreasing international interest rates and returns on investment compared to local alternatives. The increased foreign borrowing also resulted from the lower international interest rates compared to local bank rates.

Net private credit extension increased moderately, specifically during the first half of 2002. This development was caused by the still marginal recovery of economic activity and the competition from low international interest rates.

In contrast, net credit extension to the governments increased substantially in 2002, mainly as a result of the net increase in government securities at the commercial banks. This increase was influenced by the low return on foreign investments, in combination with the Bank's lifting of the limit on credit extension to the governments as per March 1, 2002.

As a result of these developments, the excess liquidity in the banking sector continued. In combination with the introduction of auctions of government securities on January 1, 2002, domestic interest rates started a downward trend. This trend was noticeable particularly for treasury bills.

5.1.1 Monetary policy changes in 2002

As of January 1, 2002, the Bank further adjusted its monetary policy. This decision was taken in light of the significant increase in international reserves in the Netherlands Antilles and the continuing decline in interest rates in the United States.

One of the most important changes in the Bank's monetary policy was the introduction of bi-weekly auctions of Certificates of Deposit (CDs). As of January 1, 2002, the banks can determine freely how many CDs they want to buy and at what rate. Furthermore, the reserve requirement percentage was reduced by 2.5 percentage points to 9% and is set for three months instead of one. However, the reserve requirement became entirely non-interest-bearing.

In addition, during 2002, the Bank reduced its pledging rate from 7.0% to 3.5% in five steps. These reductions brought the Bank's official rates more in line with the declining trend in interest rates in the domestic money and capital market. This trend was related to the decline in international interest rates.

Finally, the Bank lifted the ceiling on domestic credit extension by the commercial banks to the governments on March 1, 2002, implying the inactivation of the monetary cash reserve arrangement. This decision also was made in light of the high level of foreign exchange reserves.

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

5.2.1 Money supply

The money supply increased substantially by NAf.395.9 million (11.7%) during 2002, slightly less then the increase of NAf.425.9 million (14.4%) recorded in 2001. Both the money component and the near-money component increased in 2002, by NAf.187.5 million (14.3%) and NAf.208.4 million (10.1%), respectively. During 2001, a similar development was recorded with increases of NAf.154.2 million (13.3%) and NAf.271.7 million (15.1%), respectively.

Table 5.1 shows that the increase in the money component of the money supply in 2002 was due to increases in all three components. Coins and notes with the public increased by NAf.17.0 million (7.8%), compared to an increase of NAf.29.3 million (15.5%) in 2001. The largest increase, NAf.153.5 million (17.7%), occurred in demand deposits denominated in Netherlands Antillean guilders, considerably more than the increase of NAf.99.8 million (13.0%) in 2001. Demand deposits denominated in foreign currency increased also in 2002, by NAf. 17.0 million (7.5%), though less than the increase of NAf. 25.1 million (12.5%) during 2001. The higher increase in demand deposits was accounted for by the acceleration in private sector credit extension and the persisting excess liquidity in the banking sector.

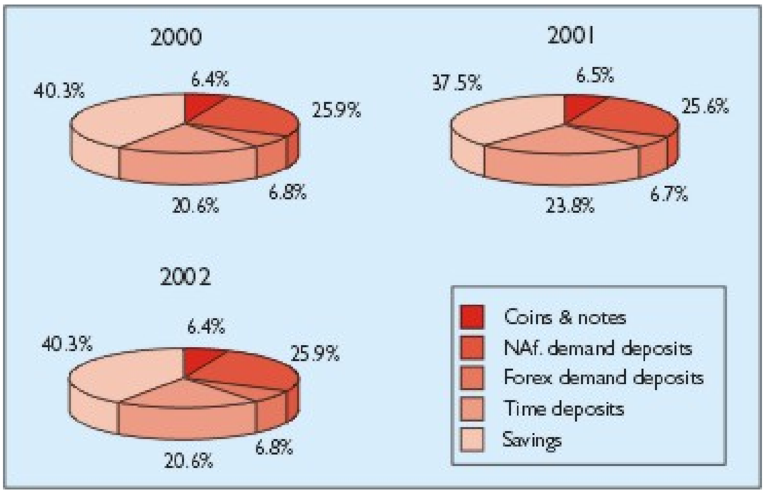
Table 5.1
Developments in the money supply and its components (in millions NAf. and percentage changes)

	2001		2002	
Coins & notes with the public	218.2	(15.5%)	235.2	(7.8%)
Total demand deposits, of which :	1,091.5	(12.9%)	1,262.0	(17.0%)
-Neth. Antillean guilders	866.1	(13.0%)	1,019.6	(17.7%)
-Foreign currency	225.4	(12.5%)	242.4	(7.5%)
Money (M1)	1,309.7	(13.3%)	1,497.2	(14.3%)
Time deposits	804.3	(32.4%)	881.4	(9.6%)
Savings	1,266.9	(6.3%)	1,398.2	(10.4%)
Near money	2,071.2	(15.1%)	2,279.6	(10.1%)
Money supply (M2)	3,380.9	(14.4%)	3,776.8	(11.7%)

The near-money component of the money supply grew by NAf.208.4 million (10.1%) in 2002, a deceleration compared to the increase of NAf.271.7 million (15.1%) in 2001. Both time deposits and savings increased, by NAf.77.1 million (9.6%) and NAf.131.3 million (10.4%), respectively. During 2001, the largest increase was recorded in time deposits -- NAf.197.0 million (32.4%)[14] -- surpassing the increase in savings of NAf.74.7 million (6.3%).

Worth mentioning is that during the final months of 2002, time deposits and savings denominated in Netherlands Antillean guilders increased at the expense of foreign exchange-denominated time deposits and savings. This development is related to the decreases in US interest rates, which put downward pressure on local interest rates on US$-denominated time deposits and savings. As a result, account holders were inclined to shift balances from US$-denominated deposits to higher yielding local currency-denominated deposits.

5.1 Developments in the composition of the money supply



Graph 5.1 reveals that the share of the money component in the money supply increased slightly at the expense of the near-money component. The increase in the share of the money component by 0.3 percentage point to 39.1% was the result of increases of 0.3 percentage point and 0.1 percentage point, respectively, in the shares of demand deposits denominated in local currency and foreign currency. These increases offset the decrease of 0.1 percentage point in the share of coins and notes with the public. The share of the near-money component decreased by 0.4 percentage point reaching 60.9%. This decrease was the result of a decrease of 3.2 percentage points to 20.6% in the share of time deposits, which offset the increase of 2.8 percentage points to 40.3% in the share of savings.

[14] NAf.74.2 million of this increase was due to a transitory adjustment with one bank.

5.2.2 Factors affecting the demand for liquid assets

In 2002, the total demand for liquid assets increased by NAf.395.9 million (11.7%), less than the decrease of NAf.425.9 million (14.4%) recorded during 2001. Both net domestic assets and net foreign assets increased in 2002, by NAf. 260.7 million (11.0%) and NAf.135.2 million (13.4%), respectively. The increase in net domestic assets was a turnaround compared to the decrease of NAf.9.6 million (0.4%) in 2001. The increase in net foreign assets was a deceleration compared to the substantial increase of NAf.435.5 million (75.7%) recorded in 2001.

The increase in net domestic assets in 2002 was a result of increases of NAf.195.6 million (125.4%) and NAf.91.0 million (3.4%) in net credit extension to the governments and the private sector, respectively. These increases offset the drop of NAf.25.9 million (5.4%) in net domestic assets due to miscellaneous factors. In 2001, net domestic assets decreased by NAf.91.3 million (0.4%). This decrease was the result of a drop in net domestic assets due to miscellaneous factors, which exceeded the increases in net credit extension to the governments and the private sector of NAf.67.6 million (76.5%) and NAf.14.1 million (0.5%), respectively.

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

	2001		2002	
General government, of which:	156.0	(76.5%)	351.6	(125.4%)
-Central government	8.5	(123.4%)	189.5	(2,129.4%)
-Island governments	147.5	(18.2%)	162.1	(9.9%)
Private sector	2,691.5	(0.5%)	2,782.5	(3.4%)
Miscellaneous	-477.7	(-23.6%)	-503.6	(-5.4%)
Net domestic assets	2,369.8	(-0.4%)	2,630.5	(11.0%)
Net foreign assets	1,011.1	(75.7%)	1,146.3	(13.4%)
Total liquid assets	3,380.9	(14.4%)	3,776.8	(11.7%)

The government sector was responsible for the largest increase in the demand for liquid assets in 2002. Both government levels recorded an increase: the central government for an amount of NAf.181.0 million (2,129.4%) and the island governments for NAf.14.6 million (9.9%). The increase at the central government level was especially substantial compared to the increase of NAf.44.9 million (123.4%) in 2001. Net credit extension to the island governments decelerated compared to the increase of NAf.22.7 million (18.2%) in 2001. The increase in net credit extension to the governments in 2002 was mainly the result of increases of NAf.159.9 million and NAf.64.7 million in securities of the central government and the island government of Curaзao in the commercial banks' portfolios, respectively. The NAf. 26.5 million increase in government securities at the commercial banks offset the decrease of NAf. 44.5 million in these securities in the central bank's portfolio. The increase in government securities at the commercial banks was mainly the result of two factors. First, lower interest rates and return on investment abroad, particularly in the United States, resulted in a shift from foreign investments to local investments. Second, the limit on commercial banks' domestic credit extension to the governments was lifted as of March 1, 2002.

Net domestic private credit extension increased by NAf.91.0 million (3.4%) in 2002, an acceleration in comparison with the increase of NAf.14.1 million (0.5%) recorded during 2001. The increase in 2002 was the result of an increase in loans of NAf.101.3 million (4.0%), which exceeded decreases in amounts receivable, and securities and participations of NAf.5.0 million (6.4%) and NAf. 5.3 million (16.0%), respectively.

Net domestic assets resulting from miscellaneous factors, which comprise the net balance of the nonfinancial assets and liabilities of the banking sector, decreased by NAf.25.9 million (5.4%) during 2002. This decrease was mainly the result of an increase in miscellaneous liabilities of the commercial banks due, among other things, to increased loans provisions. During 2001, the drop in net domestic assets resulting from miscellaneous factors amounted to NAf.91.3 million (23.6%).

Net foreign assets increased by NAf.135.2 million (13.4%) in 2002, a substantial deceleration compared to the increase of NAf.435.5 million (75.7%) in 2001. The increase in 2002 was due to an increase of NAf.188.3 million (27.8%) recorded at the central bank, which exceeded the decrease of NAf.53.1 million (15.9%) recorded at the commercial banks. As in 2001, the main factors influencing the increase in net foreign assets were the repatriation of funds and foreign borrowing due to the lower international interest rates and return on investments. During 2001, the increase in net foreign assets was related mainly to large investment projects.

5.3 Domestic credit extension by commercial banks

5.3.1 General developments

In 2002, total domestic loans at commercial banks increased by NAf.320.3 million (11.6%) reaching NAf.3,091.0 million. This was a turnaround compared to 2001, when a decrease of NAf.16.4 million (0.6%) was recorded. The increase in 2002 was the result of an increase in domestic loans to both the government sector and the private sector.

The increase in government loans at commercial banks in 2002 was due particularly to an increase in central government paper of NAf.159.9 million (236.9%), reaching NAf.227.4 million. In addition, loans extended to the island government of Cura3ao increased by NAf. 59.1 million (48.2%) to NAf.181.8 million. During 2001, loans extended to the central government recorded the opposite development with a decrease of NAf.6.5 million (8.7%) to NAf.67.5 million. On the other hand, loans extended to the island government of Cura3ao increased by NAf.21.6 million (21.3%), reaching NAf.122.7 million.

Domestic lending by commercial banks to the private sector expanded by NAf.101.3 million (3.9%) to NAf.2,681.8 million in 2002. This was a turnaround compared to 2001, when a decrease of

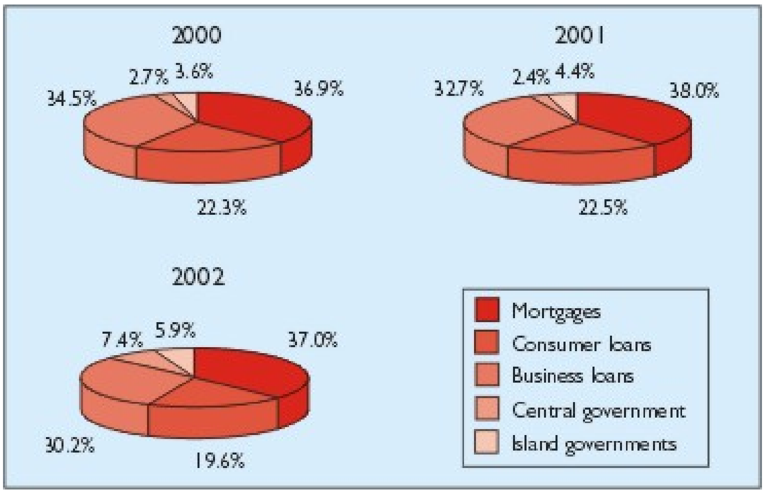
NAf.31.5 million (1.2%) was recorded. The increase in 2002 was due to increases in mortgages and business loans of NAf.82.3 million (7.8%) and NAf.26.9 million (3.0%), respectively. These increases offset the decrease in consumer loans of NAf.8.0 million (1.3%). During 2001, business loans dropped by NAf.55.9 million (5.8%), offsetting the increases in mortgages and consumer loans of NAf.24.1 million (2.3%) and NAf.0.3 million (0.0%), respectively.

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

	2001		2002	
Private sector loans, of which:	2,580.5	(-1.2%)	2,681.8	(3.9%)
-Mortgages	1,052.0	(2.3%)	1,134.3	(7.8%)
-Consumer loans	622.6	(0.0%)	614.7	(-1.3%)
-Business loans	905.9	(-5.8%)	932.8	(3.0%)
Government loans, of which:	190.2	(8.6%)	409.2	(115.1%)
-Central government	67.5	(-8.7%)	227.4	(236.9%)
-Island government of Curacao	122.7	(21.3%)	181.8	(48.2%)
Total	2,770.7	(-0.6%)	3,091.0	(11.6%)

Graph 5.2 reveals that the share of government loans in the domestic banks' loan portfolio increased by 6.5 percentage points to 13.3%. Both the shares of the central government and the island government of Curaзao increased, by 5.0 percentage points to 7.4% and 1.5 percentage points to 5.9%, respectively. The increase in the share of government loans was at the expense of all three private loan components: mortgages decreased by 1.0 percentage point to 37.0%, consumer loans decreased by 2.9 percentage points to 19.6%, and business loans decreased by 2.5 percentage points to 30.2%.

Graph 5.2
Developments in the domestic lending portfolio of commercial banks



5.3.2 Developments by island group

In 2002, commercial banks' private sector lending increased on both the Leeward Islands and the Windward Islands, by NAf.82.4 million (4.3%) and NAf.18.9 million (2.8%), respectively. During 2001, private loans declined by NAf.26.6 million (2.3%) on the Leeward Islands, offsetting the increase of NAf.13.5 million (2.0%) on the Windward Islands.

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

	2001		2002	
Private sector loans,	1,905.9	(-2.3%)	1,988.3	(4.3%)
of which:				
-Mortgages	740.3	(-0.3%)	790.7	(6.8%)
-Consumer loans	479.4	(-2.3%)	505.8	(5.5%)
-Business loans	686.2	(-4.4%)	691.9	(0.8%)

In 2002, all three loan components expanded on the Leeward Islands: mortgages by NAf.50.4 million (6.8%), consumer loans by NAf.26.4 million (5.5%), and business loans by NAf.5.7 million (0.8%). This development was a turnaround compared to 2001 when all three loan components declined: mortgages by NAf.2.3 million (0.3%), consumer loans by NAf.11.2 million (2.3%), and business loans by NAf.31.5 million (4.4%), respectively. The turnaround in private sector loans growth may indicate that the economy of the Leeward Islands is starting to recover.

The increase in private sector loans recorded on the Windward Islands in 2002 was due to increases in mortgages and business loans of NAf.31.9 million (10.2%) and NAf.21.2 million (9.7%), respectively, exceeding the drop in consumer loans of NAf.34.3 million (24.0%). The year 2001 also recorded an increase in loans extended. Mortgages and consumer loans increased by NAf.26.4 million (9.2%) and NAf.11.5 million (8.7%), respectively, offsetting the NAf.24.4 million (10.0%) decrease in business loans.

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

	2001		2002	
Private sector loans,	674.6	(2.0%)	693.5	(2.8%)
of which:				
-Mortgages	311.7	(9.2%)	343.6	(10.2%)
-Consumer loans	143.2	(8.7%)	108.9	(-24.0%)
-Business loans	219.7	(-10.0%)	240.9	(9.7%)

5.4 Developments in domestic interest rates

Table 5.6 reveals the developments in domestic interest rates as per end of period. During 2002, the Bank decreased its official rate -- the pledging rate -- in five steps from 7.00% at the end of 2001 to 3.50% at the end of 2002. These decreases were induced by a combination of developments, both local and international. One factor was the continuous increase in international reserves. In the third quarter, the official reserves -- the international reserves at the central bank (excluding gold) -- reached the internationally accepted benchmark of three months of goods imports. The resulting liquidity increase in the domestic banking sector warranted a decline in the official rate. In addition, local money and capital market rates started to decline in line with the drop in international interest rates. The marginal lending rate, the rate charged to commercial banks for borrowing in excess of NAf.20.0 million at the central bank, also dropped during 2002 because as of September 1, 2001, the marginal lending rate is equal to the pledging rate with a markup of 100 basis points.

Commercial banks' borrowing rates showed diverging developments during 2002. On the one hand, the average rate offered on passbook savings decreased by 0.1 percentage point to 3.6%. On the other hand, the average rate on 12-month time deposits increased by 0.4 percentage point to 5.5%. The latter development may be related to a trend which started in 2001. As per September 16, 2000, long-term deposits are excluded from the calculation of a commercial bank's reserve requirement. This adaptation in the central bank's monetary policy promoted increased competition among banks for those deposits. The decrease in savings rates could be related to the excess liquidity in the local banking sector.

During 2002, commercial banks' lending rates decreased. Interest rates for mortgages decreased by 0.6 percentage point to 9.4%, mainly the result of increased competition in the banking sector. This increased competition is the result of several factors, such as the excess liquidity in the local banking sector, stimulating competition for borrowers by offering lower rates. In addition, competition from abroad increased because of the decline in international interest rates. The average interest rate charged on current account overdrafts also dropped, by 0.3 percentage point to 10.2%. This drop also could be related to the excess liquidity.

Table 5.6
Developments in domestic interest rates (end of period)

	2001	**2002**	**Change (%-points)**
Central bank			
-Pledging rate	7.00%	3.50%	(-3.50)
-Marginal lending rate	7.75%	4.50%	(-3.25)
Commercial banks' borrowing rates			
-Passbook savings	3.7%	3.6%	(-0.1)
-12-month time deposit (NAf. 10,000)	5.1%	5.5%	(0.4)
Commercial banks' lending rates			
-Mortgages	10.0%	9.4%	(-0.6)
-Current account overdrafts	10.5%	10.2%	(-0.3)
Government bonds			
5 yr, effective yield	9.00%	7.25%	(-1.75)

Finally, government bond yields dropped markedly during 2002, from 9.00% to 7.25%, due to the sharp increase in demand by local investors for domestic government securities. This development can be attributed to three factors: (1) the decline in interest rates and returns on investment in the international financial markets compared to higher yielding local alternatives, (2) the lifting of the ceiling on commercial banks' credit extension to the government on March 1, 2002, and (3) the introduction of auctions of treasury paper by the Bank as of January 1, 2002.

DOMESTIC FINANCIAL MARKET DEVELOPMENTS

6.1 Introduction

Monetary and financial conditions underwent rapid changes in 2002. Contrary to 2001, the general government was able to finance its budget deficit and to refinance maturing loans, while at the same time the interest rates on government securities dropped drastically. The increased demand for government paper led to the largest annual net borrowing amount (NAf.221 million) since reporting started in 1992.

In the money market, the demand for certificates of deposit (CDs) issued by the Bank increased substantially as a result of a change in the Bank's monetary policy. In this new policy, CDs are auctioned in bi-weekly tenders with the interest rate determined by the market. As the interest rate offered increased from 0.375% in December 2001 to 2.5% in January 2002 and 3.5% in April 2002, commercial banks sold US dollars to the Bank to finance their CD purchases. These sales resulted in a concentration of international reserves with the Bank, which contributed to reaching the target level of three months of merchandise imports for the first time since 1988.

6.2 Financial instruments and the money market

In the Netherlands Antillean money market, CDs issued by the Bank are the only tradable nongovernment instrument available. In 2002, the maturity of the CDs was changed from 3 months to 4 weeks because the 3-month maturity was considered too long for cash-management purposes. By reducing the maturity and increasing the frequency of the auctions, the commercial banks have more flexibility in managing their liquidity. Commercial banks sometimes trade CDs, but they seem to prefer uncollateralized interbank loans over the sale and repurchase of CDs. The changes in the CD market have eliminated large imbalances in the local money market, even though the overdraft facility offered by the Bank was used occasionally by some banks.

As can be seen in table 6.1, the average monthly balance of CDs outstanding increased by NAf.79.5 million (69.7%) in 2002. This result was attributable to the substantial increase in the rate offered on CDs from 0.375% in December 2001 to 3.5% in April 2002. Because the Bank lowered its pledging rate in several steps from 7% to 3.5% during 2002, the maximum CD rate offered was effectively capped at 2.5%.[15]

[15] The interest rate offered on CDs is capped by the Bank at its pledging rate minus 1 percentage point. Because the Bank reduced its pledging rate further to 3% in January 2003, the cap on the CD rate was reduced to 2%. In March 2003, market expectations on future domestic interest rate developments have lowered the interest rate demanded on new 12-week CD issues to 1.85%.

Table 6.1
Average monthly balances of certificates of deposit, non-interest-bearing reserve requirement and demand deposits of commercial banks with the central bank (in millions NAf.)

	2000	2001	2002	% change 01-02
Certificates of deposit	103.2	114.1	193.6	69.7%
Non-interest-bearing reserve requirement	145.4	148.5	277.0	86.5%
Demand deposits	-52.0	20.3	45.3	123.2%
Total	196.6	282.9	515.9	82.4%

The average monthly balance of the non-interest-bearing reserve requirement increased by NAf.126.5 million (86.5%), because the Bank broadened the base over which the reserve requirement is calculated.[16] In addition, the base itself increased, in line with money growth in 2002. The increase of NAf.25.0 million (123.2%) in commercial bank demand deposits with the Bank (i.e., the free reserves) resulted from the inflow of foreign funds due to a balance of payments surplus and the sale of foreign currency to the Bank.

Government securities in the money market comprise treasury bills with 1-, 3-, 6-, and 12-month maturities. As of January 2002, these treasury bills are auctioned twice a month, and auction results are disseminated among market participants. In addition, more information on market prices, gross and net issuance, and total outstanding debt is provided to market participants to increase the transparency of the government debt market. Increased transparency and low interest rates in the United States have led to a significant increase in the demand for local short-term securities. In addition, as the issue dates and maturities of treasury bills became more standardized, a secondary market for these securities developed. Activity on this secondary market remained limited, however, as investors' demand was met mainly by increased primary market supply. Table 6.2 provides information on the size of and the activity on the market for local treasury bills.

Table 6.2
Treasury bills issuance, outstanding balances, and average maturity as per December 31, 2002 (in millions NAf. and months)

	2001	2002	% change 01-02
Issuance	550.0	674.1	22.6
-Central government	258.5	361.2	39.7
-Island government of Curacao	291.5	312.9	7.3
Outstanding amount	58.6	248.3	323.7

[16] The base equals the commercial banks' domestic debt excluding interbank and long-term deposits.

-Central government	26.4	136.6	417.4
-Island government of Curacao	32.2	111.7	246.9
Average maturity (months)	1.23	3.77	206.5
-Central government	1.17	2.80	139.3
-Island government of Curacao	1.27	4.97	291.3

6.3 The market for government bonds

Unlike the previous two years, 2002 was characterized by a large increase in investors' demand for local government bonds. Local investors increased their holdings of government paper, as interest rates abroad became less attractive. Another factor explaining the increased demand was the decision of the Bank to lift the limit on commercial bank lending to the governments as per March 1, 2002. As a result, commercial banks built up a sizeable portfolio of government debt. As demand for government bonds picked up, the Bank was able to sell a significant part of its portfolio in the secondary market, which unlike the market in bills, became rather active in 2002.

Gross general government debt issuance totaled NAf.958.7 million during 2002, NAf.674.1 million (70%) of which was related to treasury bills with maturities of less than one year. Total bond issuance in 2002 reached NAf.284.7 million (30%), compared to NAf.217.9 million (28%) in 2001. The central government issued three new public issues, a 10-year bond yielding 9.875% in March, a 3-year bond yielding 7.6% in August, and a 9-year bond yielding 8.125% in December. In addition, some private placements were re-opened. The island government of Curaзao issued two new public issues in 2002: a 6-year bond yielding 9% in April, and a 5-year bond yielding 7.6% and 7.1% in September and October, respectively. Issuance increased for both levels of government and for both bills and bonds, which led to net borrowings of NAf.117.4 million and NAf.103.6 million for the central government and the island government of Curaзao, respectively. As can be seen in graph 6.1, net borrowing in 2002 was the highest ever recorded.

Graph 6.1 Annual net borrowings (in millions NAf.)

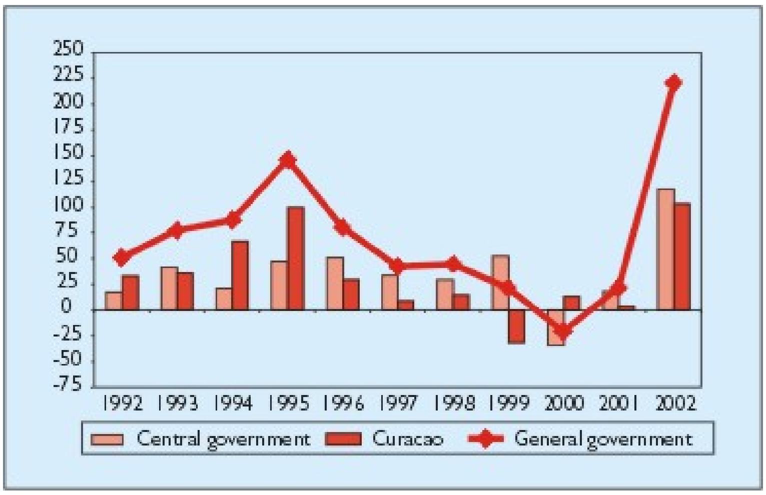


Table 6.3 shows that net borrowing by the central government was concentrated in treasury bills and public issues. Contrary to 2001, private placements were of less importance. As demand for government securities was high, bond tenders were oversubscribed, which enabled the government to reduce its borrowing costs. Private placements declined in 2002, as the central government used the proceeds of a transfer from the Dutch government (NAf 24.5 million) to partially repay a loan to the Bank in February 2002. As mentioned, the increase in treasury bills resulted from low foreign interest rates, changes in the sale of these securities, and the removal of the limit on commercial bank lending to the governments. The outstanding amount of debt conversions dropped slightly in 2002, in line with the predetermined redemption schedules of these loans.

Table 6.3
Outstanding negotiable loans of the central government (in millions NAf.)

	2000	2001	2002	Difference 02-01
Total, of which:	964.5	982.6	1,100.0	11.9%
Private placement	174.5	210.5	180.7	-14.2%
Public issues	432.0	411.7	451.9	9.8%
Treasury bills	16.6	26.4	136.6	417.4%
Debt conversions	341.3	334.0	330.8	-1.0%
Net borrowing	-34.2	18.1	117.4	548.6%

The island government of Curacao registered net borrowings of NAf.103.6 million in 2002, compared to NAf.3.6 million in 2001. As can be seen in table 6.4, net borrowing resulted from a large increase in public issues and treasury bills outstanding, the demand for which increased for the same reasons as with the central government. Furthermore, the island government of Curacao experienced a drop in private placements, which, like the central government, was caused by a NAf.15.5 million repayment on a loan from the Bank with funds transferred by the Dutch government. In addition, two private placements were refinanced with new public issues in 2002. The outstanding amount of debt conversions and the 6.5% 30-year annuity dropped according to their predetermined redemption schedules.

Table 6.4
Outstanding negotiable loans of the island government of Curacao (in millions NAf.)

	2000	2001	2002	Difference 00-01
Total, of which:	956.3	959.9	1,063.5	10.8%
Private placement	132.8	177.3	133.8	-24.5%
Public issues	264.2	259.8	333.7	28.4%
Treasury bills	57.1	32.2	111.7	246.9%
Debt conversions	66.4	60.7	60.6	-0.2%

6.5%-annuity	435.8	429.9	423.7	-1.4%
Net borrowing	13.4	3.6	103.6	2,877.8%

The developments in 2002 contributed to a large increase in the amount of negotiable loans outstanding. The maturity schedule of the general government's domestic debt in table 6.5 indicates that 23.7% of the total negotiable loans outstanding, excluding treasury bills, will mature in the next two years, while 31.2% have a maturity between 3 and 5 years. Compared to 2001, the average maturity of government bonds dropped by 0.4 year, although more bonds were placed in the 6-10 year bracket. The long average maturity of loans of the island government of Curacao is a result of the 30-year annuity.

The average yield on outstanding government bonds dropped marginally in 2002, as only 10% of the outstanding bonds were refinanced. In addition, yields on government bonds were very high in the first quarter of 2002, which compelled the governments to place relatively expensive bonds (10-year at 9.875% and 6-year at 9%) to refinance some large maturing bonds. As a consequence, the governments have not yet fully benefited from the drop in domestic long-term interest rates. The average yield on outstanding debt of the island government of Curacao is affected by the large share of the 6.5% annuity in its total debt.

Table 6.5
Maturity schedule of negotiable government securities excluding treasury bills as per December 31, 2002 (in percentages of total)

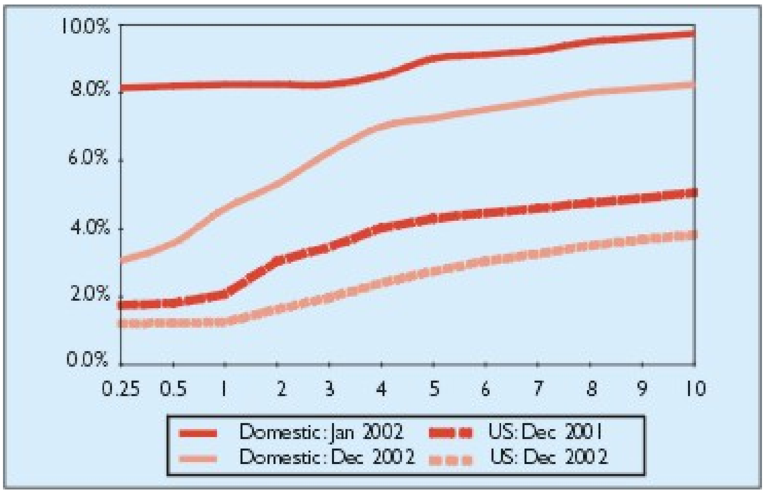
	0-2 years	3-5 years	6-10 years	over 10 years	Average yield	Average maturity
Central government	19.2	39.1	41.7	-	8.60	4.9 yr
Island government of Curacao	28.4	23.3	13.2	35.1	`	13.0 yr
General government	23.7	31.2	27.6	17.4	8.14	8.9 yr

When issuing new bonds, a trade-off has to be made between the security offered by longer maturities and the interest savings, resulting from the steep yield curve, offered by shorter maturities. Domestic interest rates dropped drastically in 2002, especially for short-term maturities. In January 2002, at the time of the first treasury bill auctions, short-term interest rates were above 8%. In December 2002, they dropped to slightly over 3% for the 3-month maturity. Long-term interest rates started to drop only in the second half of the year and by a much smaller amount. As a result, the domestic yield curve changed from relatively flat to extremely steep, with interest rates on 10-year government bonds more than 500 basis points above the rate on 3-month treasury bills.

The decline in local interest rates was caused by both domestic and international factors. Domestically, the decision of the Bank to lift the limit on commercial bank lending to the government led to a sharp increase in commercial banks' demand for government paper. The further decline in already low international interest rates induced institutional investors to shift their asset allocation towards more domestic, higher-yielding investments, thereby increasing the demand for local government paper. At the end of 2002, local investors seemed more concerned about getting an attractive return than they worried about the risks of an excessive build-up of government debt.

Interest rates on US Treasuries dropped, as the Federal Reserve eased its monetary policy in an effort to stimulate the economy in 2002. Yields for longer-dated maturities also declined, as economic data pointed towards a weaker economy, which may lead to a longer period of low interest rates. Yields on 3-month treasury bills declined by 53 basis points, while the yield on 10-year Treasuries dropped by 123 basis points, flattening the curve by 70 basis points.

Graph 6.2
Domestic and US government yield curve developments



As a result of the developments in the local and US yield curves, the spread between a 3-month domestic and US treasury bill declined by 456 basis points to 186 basis points at the end of 2002. For longer-dated maturities, the spread tightening was less pronounced: the 10-year spread dropped by 27 basis points to 443 basis points. With the prospect of prolonged low interest rates in the United States, the spread for longer-dated maturities is expected to decline further in 2003.

THE FINANCIAL SECTOR

7.1 General developments in the financial sector

In 2002, the Bank conducted on-site examinations at 10 institutions: 5 full-scope examinations and one follow-up examination at domestically operating commercial banks, 2 full-scope examinations at specialized credit institutions, and 2 examinations at money remitters. The Bank also performed quick-scans at 33 internationally operating commercial banks to assess in particular their compliance with anti-money-laundering regulations and their adherence to minimum substance requirements.

The Bank issued a license to Christian Kingdom Cooperative to operate as a credit union in St. Maarten. In addition, the Bank revoked the license of Integra Bank N.V., an internationally operating commercial bank, because the institution was no longer compliant with prudential supervisory requirements. The Bank also revoked the license of the internationally operating commercial banks Banque Artesia Curacao N.V., Banco de Venezuela N.V., and ING Bank (Netherlands Antilles) N.V., and the thrift and savings fund Stichting E. Moreno Brandao & Zonen N.V., because they went into voluntary liquidation.

The operations of the internationally operating commercial banks CBA Compagnie Bancaire des Antilles N.V., The Caribbean American Bank N.V., and BanUnion N.V. were continued under their new statutory names CBG Compagnie Bancaire Geneve (Curacao) N.V., Bancaribe Curacao Bank N.V., and BANESCO N.V., respectively.

As a result of the restructuring of the operations of the RBTT group in the Netherlands Antilles, the operations of the internationally operating RBTT Bank Antilles International N.V. were taken over on October 1, 2002 by the internationally operating RBTT Bank St. Maarten International N.V. and continued under the new name RBTT Bank International N.V. On November 1, 2002, the operations of the domestically operating commercial bank RBTT Bank St. Maarten N.V. were taken over by the domestically operating commercial bank RBTT Bank Antilles N.V. and continued under the new name RBTT Bank N.V.. Consequently, the Bank revoked the licenses of RBTT Bank Antilles International N.V. and RBTT Bank St. Maarten N.V.

As a result of the take-over of the Caribbean operations of Barclays Bank PLC by the new entity FirstCaribbean International Bank Limited in Barbados, the operations of the former domestic branch office of Barclays PLC in St. Maarten were continued as a branch office of FirstCaribbean International Bank (Cayman) Limited, a subsidiary of FirstCaribbean International Bank Limited.

On December 5, 2002, at the request of the Bank, the Court of First Instance placed Girobank N.V. under the emergency measure following the revocation of its license by the Bank.

As a result of the licensing, revocation of licenses and restructuring of activities, the number of internationally operating commercial banks and domestically operating commercial banks in the Netherlands Antilles was at 41 and 11, respectively, at the end of 2002.

7.2 Domestic banking

7.2.1 General activities of commercial banks operating in the domestic banking sector

Following the increase of NAf.676.6 million (12.8%) in 2001, total assets of the domestic banking sector grew by only NAf.226.0 million (3.8%) to NAf.6,199.6 million in 2002. Investments more than doubled, mainly as a result of increases in short-term and long-term government debentures. Short-term and long-term debentures of the island government of Curacao increased by NAf.56.5 million and NAf.189.9 million, respectively, while those of the central government increased by NAf.38.6 million and NAf.30.1 million, respectively. This development can be attributed to low foreign interest rates, the apparent lack of sufficient sound projects in the domestic private sector, and the lifting of the ceiling on government loans as of March 1, 2002. Furthermore, the credit portfolio of the commercial banks grew moderately by NAf.83.1 million (2.4%) to NAf.3,500.9 million.

The increased activities of the commercial banks operating domestically were funded primarily by increases in deposits of NAf.188.6 million (3.7%) and borrowings of NAf.24.3 million (15.3%) in 2002.

TABLE 7.1
Balance sheet of commercial banks operating in the domestic banking sector at year-end (in millions NAf.)

	2000		2001		2002	
	NAf.	%	NAf.	%	NAf.	%
ASSETS						
Non-int.-bearing cash	314.4	5.9	457.4	7.7	395.6	6.4
Interest-bearing cash	953.9	18.0	1,494.9	25.0	1,371.5	22.1
Investments	264.1	5.0	261.9	4.4	582.8	9.4
Loans	3,449.4	65.1	3,417.8	57.2	3,500.9	56.5
Inv. unconsol. subs	30.9	0.6	19.5	0.3	12.2	0.2
Fixed assets	164.2	3.1	162.7	2.7	170.0	2.7
Other assets	120.1	2.3	159.4	2.7	166.6	2.7
Total assets	5,297.0	100.0	5,973.6	100.0	6,199.6	100.0
LIABILITIES						
Demand deposits	1,421.7	26.8	1,606.9	26.9	1,798.0	29.0
Savings deposits	1,873.6	35.4	2,176.7	36.4	2,148.7	34.7
Time deposits	1,108.1	20.9	1,276.5	21.4	1,302.0	21.0
Total deposits	4,403.4	83.1	5,060.1	84.7	5,248.7	84.7
Borrowings	250.3	4.7	158.8	2.7	183.1	2.9
Other liabilities	228.4	4.3	266.3	4.5	274.6	4.4
Total liabilities	4,882.1	92.1	5,485.2	91.9	5,706.4	92.0

Minority interest	5.6	0.1	5.3	0.1	6.6	0.1
Subordinated debent.	5.1	0.1	6.2	0.1	9.7	0.2
General provisions	119.4	2.3	134.3	2.2	161.7	2.6
Capital & reserves	284.8	5.4	342.6	5.7	315.2	5.1
Total capital	414.9	7.9	488.4	8.1	493.2	8.0
Total liabilities and capital	5,297.0	100.0	5,973.6	100.0	6,199.6	100.0

7.2.1.1 Capital

Total capital increased by 1.0% to NAf.493.2 million in 2002, while total assets recorded an increase of 3.8%. Since capital increased at a slower rate than total assets, the capital-to-assets ratio deteriorated slightly from 8.2% to the internationally accepted minimum of 8.0%.

7.2.1.2 Net income

Total operational income of the domestic banking sector increased by NAf.27.0 million to NAf.404.7 million in 2002, offsetting partly the increase in total operational expenses of NAf.30.9 million. These developments resulted in a net operational income of NAf.65.8 million, NAf.3.9 million less than in 2001. However, net income after taxes increased by NAf.19.4 million (72.9%) to NAf.46.0 million in 2002. This improvement was caused by an extraordinary income of NAf.3.2 million in 2002, compared to the significant extraordinary loss of NAf.25.6 million in 2001.

TABLE 7.2
Income statement of commercial banks operating in the domestic banking sector (in millions NAf.)

	2000	**2001**	**2002**
Interest income	447.8	415.2	421.1
Interest expenses	(159.1)	(156.4)	(154.3)
Net interest income	288.7	258.8	266.8
Other income	126.7	118.9	137.9
Total operational income	415.4	377.7	404.7
Salaries & other employee expenses	(170.1)	(161.0)	(186.9)
Occupancy expenses	(53.7)	(48.2)	(52.6)
Other operating expenses	(73.7)	(59.7)	(70.4)
Net addition to general provisions	(30.9)	(39.1)	(29.0)
Total operational expenses	(328.4)	(308.0)	(338.9)
Net operating income	87.0	69.7	65.8
Net extraordinary items	1.5	(25.6)	3.2
Applicable profit taxes	(20.1)	(17.5)	(23.0)
Net income after taxes	68.4	26.6	46.0

7.2.1.3 Liquidity

The liquidity of the domestic banking sector in 2002 increased further compared to 2001 (see table 7.3). Due to the apparent lack of sufficient sound local projects, many banks were in a situation of excess liquidity. All liquidity ratios reflected an increase during 2002. The overall liquidity of the commercial banks is considered sound.

TABLE 7.3
Liquidity ratio at year-end (in percentages)

	2000	2001	2002
Non-interest-bearing cash and short-term treasury paper to:			
-total deposits	9.0	9.6	11.0
-total liabilities	8.1	8.9	10.1
Non-interest & interest-bearing cash and short-term treasury paper to:			
-total deposits	30.7	36.0	37.1
-total liabilities	27.7	33.5	34.2

The aggregate macro prudential indicators in table 7.4 provide an indication of the performance of the commercial banks.

The indicators of capital adequacy of the domestic banking sector reflected a total capital-to-total assets ratio and a tier 1 capital-to-total assets ratio of 8.2% and 5.3%, respectively, in 2002, above international capital standards. According to these standards a total capital-to-risk-weighted assets ratio of at least 8% and a minimum tier 1 capital-to-total assets ratio of 4% is required. Furthermore, table 7.4 reflects a decrease in the tier 1 capital-to-total assets ratio and an increase in the tier 2 capital-to-total assets ratio, which resulted from the transfer of capital and reserves to general provisions.

The decrease in the nonperforming loans ratios by 0.1 and 3.5 percentage points in 2002 compared to 2001 indicates a slight improvement in asset quality, which can be related to the modest economic recovery. Furthermore, the loan loss provision as a percentage of nonperforming loans increased, indicating that the provisioning for loans in 2002 was still not adequate.

The earnings indicators reflect that the profitability of the domestic banking sector remained at an acceptable level. The return-on-assets ratio increased from 0.7% in 2001 to 1.1% in 2002, above the benchmark of 0.5%. Moreover, the break-even yield declined from 3.0 in 2001 to 2.8% in 2002, allowing the domestic banking institutions to realize a higher net income. However, the gross-earning assets yield decreased from 8.5% in 2001 to 7.6% in 2002, indicating that the banks' assets were less productively employed.

TABLE 7.4
Macro prudential indicators of commercial banks operating in the domestic banking sector of the Netherlands Antilles at year-end (in percentages)

	2000	2001	2002
CAPITAL ADEQUACY[1)]			
Total capital/total assets	8.9	8.2	8.2
Tier 1 capital/total assets	8.3	5.8	5.3
Tier 2 capital/total assets	2.5	2.3	2.7
Tier 3 capital/total assets	0.1	0.1	0.2
ASSET QUALITY			
Nonperforming loans/total loans	4.6	6.0	5.9
Nonperforming loans/total capital	24.0	43.4	39.9
Provisions loan losses/nonperforming loans	70.4	60.8	73.6
EARNINGS			
Gross earning assets yield	9.4	8.5	7.6
Break-even yield	3.3	3.0	2.8
Net interest margin	6.1	5.1	4.8
Return on assets	1.6	0.7	1.1
LIQUIDITY			
Total loans/total deposits	79.1	68.7	67.6
Liquidity surplus (in millions NAf.)	25.7	85.5	85.1

1) Excluding branches of foreign banks.

The loans-to-deposits ratio indicates that the banks used only 67.6% of their deposit base to fund their credit extension activities and maintained the remainder of their deposit base as liquid assets in 2002. Consequently, the liquidity surplus remained almost unchanged at NAf.85.1 million.

7.2.2 Domestic activities of commercial banks operating in the domestic banking sector

Total domestic assets of the domestic banking sector increased by NAf.500.6 million (13.8%) in 2002 compared to NAf.162.9 million (4.7%) in 2001 (table 7.5). The increases in interest-bearing cash and investments of NAf.283.3 million (86.5%) and NAf.223.8 million (114.5%), respectively, accounted primarily for the growth in total domestic assets. The increase in interest-bearing cash was partly the result of the introduction of Certificates of Deposit (CDs) auctions by the central bank in which the banks determine the interest rate. Furthermore, the increase in investments was due to the net purchase of government securities.

A comparison of tables 7.1 and 7.5 reflects that total domestic credit extension comprised 77.0% of total credit extension by the domestic banking sector while residents held 72.0% of total deposits in 2002.

TABLE 7.5
Domestic activities of commercial banks operating in the domestic banking sector at year-end (in millions NAf.)

	2000		2001		2002	
	NAf.	%	NAf.	%	NAf.	%
ASSETS						
Non-int.-bearing cash	79.3	2.3	198.6	5.5	111.7	2.7
Interest-bearing cash	320.1	9.3	327.7	9.1	611.0	14.8
Investments	198.5	5.8	195.5	5.4	419.3	10.2
Loans	2,615.8	75.8	2,607.0	72.1	2,695.5	65.5
Investm. unconsol. subs.	6.3	0.2	13.2	0.4	12.0	0.3
Fixed assets	141.7	4.1	140.9	3.9	148.0	3.6
Other assets	90.1	2.5	131.8	3.6	117.8	2.9
Total assets	3,451.8	100.0	3,614.7	100.0	4,115.3	100.0
LIABILITIES						
Demand deposits	1,048.6	33.9	1,179.6	33.2	1,373.2	34.5
Savings deposits	1,270.6	41.0	1,356.5	38.1	1,497.2	37.7
Time deposits	601.8	19.4	801.9	22.6	908.9	22.9
Total deposits	2,921.0	94.3	3,338.0	93.9	3,779.3	95.1
Borrowings	8.1	0.3	8.4	0.2	7.2	0.2
Other liabilities	166.2	5.4	209.8	5.9	189.1	4.7
Total liabilities	3,095.3	100.0	3,556.2	100.0	3,975.6	100.0

Table 7.6 indicates that lending to the government through direct credit extension decreased by NAf.12.6 million in 2002 compared to 2001. In contrast, lending to the private sector increased by NAf.101.1 million (3.9%) in 2002, resulting from increases in business loans and mortgages of NAf.18.8 million (2.1%) and NAf.90.4 million (8.6%), respectively.

TABLE 7.6
Domestic lending to the government and the private sector at year-end (in millions NAf.)

	2000	2001	2002
Government [1)]	0.2	26.3	13.7
Private sector:	2,615.6	2,580.7	2,681.8
Consumer loans	626.0	622.8	614.7
Business loans	961.7	905.9	924.7
Mortgages	1,027.9	1,052.1	1,142.5
Total	2,615.8	2,607.0	2,695.5

[1)] Excluding government securities

Table 7.7 illustrates the distribution of the domestic deposit base between the public sector and the private sector. The private sector maintains by far the largest share of the domestic deposit base of approximately 97%.

TABLE 7.7
Holders of deposits at year-end (in millions NAf and %)

	2000		2001		2002	
	NAf.	%	NAf.	%	NAf.	%
Deposit holders:						
- Government	81.8	2.8	91.3	2.7	107.6	2.8
-Private sector	2,839.2	97.2	3,246.7	97.3	3,671.7	97.2
Total deposits	2,921.0	100.0	3,338.0	100.0	3,779.3	100.0

Table 7.8 indicates a further growth by 13.1% in the domestic deposits of the private sector in 2002. This growth was accounted for by a 13.7% increase in guilder deposits and a 10.3% increase in foreign currency deposits.

TABLE 7.8
Change in domestic private sector deposits by currency (in millions NAf. and %)

	2000		**2001**		**2002**	
	NAf.	%	NAf.	%	NAf.	%
N.A. guilders	92.8	4.1	299.3	12.6	366.1	13.7
Foreign currency	(3.9)	(0.8)	108.2	23.3	58.8	10.3
Total	88.9	3.2	407.5	14.4	424.9	13.1

7.2.3 Foreign activities of commercial banks operating in the domestic banking sector

Total foreign assets of commercial banks operating in the domestic banking sector contracted by NAf 274.6 million (11.6%) to NAf 2,084.3 million in 2002, mitigating the increase of NAf 500.6

million in total domestic assets. This contraction resulted mainly from a decline in interest-bearing cash of NAf 406.8 million (34.8%). The decline in interest-bearing cash can be explained by the decrease in foreign interest rates, which made higher yielding local alternatives more attractive. Foreign assets accounted for 33.6% of the total assets of the domestic banking sector in 2002.

In addition, total foreign liabilities decreased by NAf.65.7 million (3.7%) to NAf.1,730.8 million. The decrease in total foreign liabilities resulted from the decrease in foreign deposits, more than offseting the increases in foreign borrowings and other foreign liabilities.

TABLE 7.9
Foreign activities of commercial banks operating in the domestic banking sector at year-end (in millions NAf.)

	2000		2001		2002	
	NAf.	%	NAf.	%	NAf.	%
ASSETS						
Non-int.-bearing cash	235.1	12.7	258.8	11.1	283.9	13.6
Interest-bearing cash	633.8	34.3	1,167.3	50.6	760.5	36.5
Investments	65.6	3.6	66.4	2.8	163.5	7.8
Loans	833.6	45.2	810.8	33.1	805.4	38.7
Investm. unconsol. sub.	24.6	1.3	6.3	0.3	0.2	0.0
Fixed assets	22.5	1.2	21.8	0.9	22.0	1.1
Other assets	30.0	1.7	27.5	1.2	48.8	2.3
Total assets	1,845.2	100.0	2,358.9	100.0	2,084.3	100.0
LIABILITIES						
Demand deposits	373.1	20.9	437.3	18.1	424.8	24.5
Savings deposits	603.0	33.7	820.3	32.7	651.5	37.7
Time deposits	506.3	28.3	474.6	19.9	393.1	22.7
Total deposits	1,482.4	82.9	1,732.2	70.7	1,469.4	84.9
Borrowings	242.2	13.6	7.8	26.6	175.9	10.2
Other liabilities	62.2	3.5	56.5	2.7	85.5	4.9
Total liabilities	1,786.8	100.0	1,796.5	100.0	1,730.8	100.0

7.3 Secondary financial institutions

In 2002, the number of secondary institutions operating in the Netherlands Antillean financial sector remained unchanged at 36. These institutions include credit unions, specialized credit institutions, savings banks and thrift foundations. The individuals holding a dispensation to extend credit coupons ('bonnen') for short-term consumer credit to households numbered 8 by the end of 2002.

7.4 International banking

Total assets of the international banking sector of the Netherlands Antilles increased by NAf.7.7 billion (11.3%) to NAf.75.8 billion in 2002 compared to an increase of NAf.6.2 billion (10.0%) recorded in 2001. The increase in total assets in 2002 was attributable primarily to loans to unconsolidated affiliates (NAf.4.1 billion) and investments in unconsolidated subsidiaries (NAf.3.2 billion).

On the liability side, borrowings accounted for NAf.7.1 billion (17.4%) to the funding of the increase in total assets.

Finally, total capital reflected a capitalization of 8.7%, well above the international accepted capital-to-risk-weighted assets ratio of 8%.

TABLE 7.10
Balance sheet of commercial banks operating in the international banking sector at year-end (in billions NAf.)

	2000		2001		2002	
	NAf.	%	NAf.	%	NAf.	%
ASSETS						
Non-int.-bearing cash	1.8	2.9	2.0	2.9	0.9	1.2
Interest-bearing cash	9.6	15.5	13.1	19.2	13.2	17.4
Investments	4.3	6.9	4.5	6.6	4.2	5.5
Loans	33.8	54.5	38.1	56.0	42.2	55.7
Inv. unconsol. subs.	0.2	0.3	2.1	3.1	5.3	7.0
Fixed assets	0.1	0.1	0.1	0.1	0.1	0.1
Other assets	12.1	19.8	8.2	12.0	9.9	13.1
Total assets	61.9	100.0	68.1	100.0	75.8	100.0
LIABILITIES						
Demand deposits	4.8	7.7	6.4	9.4	7.6	10.0
Savings deposits	0.2	0.3	0.2	0.3	0.4	0.5
Time deposits	15.2	24.5	13.0	19.1	12.3	16.2
Total deposits	20.2	32.5	19.6	28.8	20.3	26.7
Borrowings	35.0	56.5	40.7	59.8	47.8	63.1
Other liabilities	1.0	1.7	1.1	1.6	1.1	1.5
Total liabilities	56.2	90.7	61.4	90.2	69.2	91.3
Minority interest	0.1	0.2	0.9	1.3	2.0	2.6
Subordinated debentures	0.0	0.0	0.0	0.0	0.0	0.0
General provisions	0.3	0.5	0.2	0.3	0.2	0.3
Capital & reserves	5.3	8.6	5.6	8.2	4.4	5.8
Total capital	5.7	9.3	6.7	9.8	6.6	8.7
Total liabilities and capital	61.9	100.0	68.1	100.0	75.8	100.0

Total operational income of the international banking sector contracted by NAf.111 million (10.0%) to NAf.1,002 million in 2002. This contraction resulted from a decrease in other income of NAf.246 million (22.8%), which offset the increase of NAf.135 million in net interest income. Furthermore, total operational expenses decreased less than total operational income, resulting in a decline of NAf.58 million (14.7%) to NAf.337 million in net operating income compared to 2001. Together with a NAf.49 million increase in extraordinary losses, net income after taxes declined by NAf.103 million (27.3%) to NAf.274 million in 2002.

TABLE 7.11
Income statement of commercial banks operating in the international banking sector (in millions NAf.)

	2000	2001	2002
Interest income	3,327	2,672	2,300
Interest expenses	(3,288)	(2,637)	(2,130)
Net interest income	39	35	170
Other income	1,155	1,078	832
Total operational income	1,194	1,113	1,002
Salaries & other employee expenses	(93)	(112)	(100)
Occupancy expenses	(36)	(26)	(18)
Other operating expenses	(231)	(205)	(166)
Net addition to general provisions	(179)	(375)	(381)
Total operational expenses	(539)	(718)	(665)
Net operating income	655	395	337
Net extraordinary items	15	(6)	(55)
Applicable profit taxes	(26)	(12)	(8)
Net income after taxes	644	377	274

INSTITUTIONAL INVESTORS

8.1 Introduction

A critical task for the insurance sector is to get a better grip on risk management. Not only the management and analysis of transaction or product level risks should be emphasized, but also other areas of their business. At the core of risk management is governance.

In today's environment of increased management and board accountability, the establishment of effective corporate governance guidelines becomes very important. In addition to guidelines for two-tier boards, the Bank has also developed guidelines for one-tier boards. The one-tier guidelines will be introduced to the sector before the end of 2003. The Bank's guidelines must be followed by all institutions incorporated in the Netherlands Antilles and subject to supervision by the Bank.

Financial reporting of business enterprises is important to all stakeholders. Employees, creditors, board of directors, government, shareholders, and clients all are interested in the real value of businesses and need reliable information to make proper decisions. Needless to say, financial reports should be transparent and reliable.

In this globalizing world where financial institutions diversify their activities across national borders and sectoral boundaries, harmonized accounting standards are in the interest of all stakeholders, including supervisors. Information presented in financial reports prepared by business enterprises should not only be reliable and timely but also in a usable form. Greater comparability of financial information has become crucial for investors worldwide. The date set for the International Accounting Standards (IAS) to become effective in Europe is 2005. Realizing that the IAS requires their attention, institutions in the United States are facing the potential implications of, among other things, the proposed model for insurance contracts under the IAS.

The International Association of Insurance Supervisors (IAIS) located in Basle, with a membership of over 100 insurance supervisors from around the world, has been meeting with the International Accounting Standards Board (IASB) to discuss the work of the Board in relation to the proposed amendments to IAS 39 and 32. Discussions are being conducted to determine how the IAIS can best contribute to that work.

In addition, the IAIS adopted the Principles on the Minimum Requirements for the Supervision of Reinsurers in its last annual meeting in October 2002, a significant step towards harmonizing supervisory practices for the global reinsurance industry. The underlying premise for the new principles is that all reinsurers must be supervised and that a global approach to the supervision of reinsurance will be anchored in the home jurisdiction. The principles identify elements of a supervisory framework common for primary insurers and reinsurers, such as licensing, fit and proper testing, on-site inspection, and those elements that need to be adapted to reflect the reinsurer's unique risks.

The past few years have been difficult for the insurance industry. The consequences of the September 11, 2001, event are still being felt through increased reinsurance premiums or a decrease in insurance issued because of its higher cost. The record losses from the attack on the World Trade Center eroded insurance companies' net results. Although the insurance companies in the

Netherlands Antilles were not affected directly by the attack, the indirect affects still are being felt; the reinsurance market has hardened, and reinsurance premiums have risen between 30% and 40%.

The sharp decline in investment returns in the international stock exchanges affected the portfolio performance of the institutional investors industry worldwide. As part of that worldwide industry, the Netherlands Antillean institutions were not spared. Investment portfolio losses were either reported in the profit and loss statement as realized or brought directly against the surplus as unrealized losses. The Bank has regularly been discussing strategies to deal with this situation with management and investment managers of supervised institutions. There is, however, little recovery expected in investment markets, at least in the short-term. The war in Iraq, potential terrorist strikes, and other occurrences make realistic predictions about the securities market difficult.

To mitigate the effects of these negative developments, many companies have been intensifying their underwriting guidelines and asset-liability management programs. To survive, insurance companies must ensure that their underwriting becomes profitable again. In addition, they should follow a strict investment policy of steady returns with particular emphasis on matching the timing of investments with the anticipated payment of liabilities.

The availability of financial data of the institutions is very important in every supervisory system. These data must provide a clear picture of the policy carried out and the overall financial position. The Annual Reports Automated Statements (ARAS) version 2.7 was formally introduced to the sector in April 2002. In its continued effort to make the annual reporting system more effective and efficient, the Bank soon will introduce version 2.8, which includes more user-friendly features and more comprehensive financial disclosure.

In addition, the Bank developed a new data retention system to process the information provided by the new reporting system. This project will allow the supervisor to dispose of important market information for a period of five years. The system will include an early warning system and enables the Bank, among other things, to analyze the performance of a single company, compare its performance with other companies, and generate reports. Another feature of the system is the agenda function, which will enable the Bank to closely monitor imposed deadlines. The system will become operational in 2003.

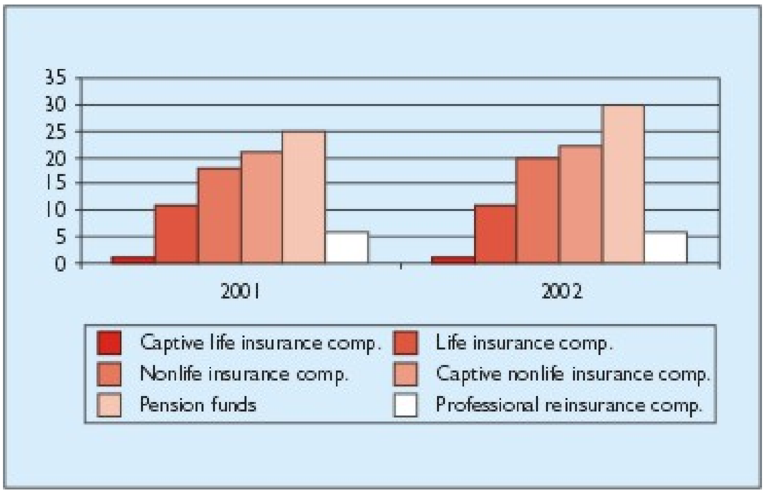
8.2 The institutional investors sector

The number of institutional investors operating in the Netherlands Antilles was 85 at the end of 2002, 3 more than in 2001. This increase was due to the formation of 3 new companies: 2 nonlife insurance companies and a captive insurer. In addition, the process of registering funeral service insurers with a minimum of 200 insureds proceeded in 2002.

Of the 85 institutions, 11 were life insurance companies, 3 of them locally incorporated. The number of nonlife insurance companies increased to 20, 13 of them locally incorporated.

The number of insurance companies servicing the international markets was 29 at the end of 2002, an increase of one compared with 2001. Of these companies, one is in the life insurance business, 22 in nonlife insurance, and 6 are professional reinsurers. Most of the internationally operating insurance companies have European parents, and more than 50 percent of the companies originate in the Netherlands.

GRAPH 8.1
Composition of the institutional investors sector (number of companies)



The number of pension funds was 30 at the end of 2002. Five of them are in the process of liquidation and another 5 officially registered with the Bank during 2002. In most cases, the risks associated with the pension obligations of the liquidated pension funds were transferred to an insurance company.

8.3 Overview of developments in the insurance industry

8.3.1 General

As a result of the financial and economic difficulties in the Netherlands Antilles in 2001, many Antillean residents immigated to Holland. The effects of this shrinking population affected the insurance industry. It appeared also that buying insurance no longer was a priority with the public, due to a decline in disposable income. For example, it is estimated that the number of uninsured motorists has increased considerably.

The results reported by the nonlife insurance industry in recent years show that net premiums written increased up to financial year 2000. However, premiums written decreased by 5.7% in the financial year 2001. In addition to the financial economic difficulties, the increase of 24.6% in ceded premiums also led to a decrease in net written premiums in 2001. The increase in ceded premiums can be attributed mainly to the notable increase in reinsurance costs in 2001 as a consequence of the tragic events of September 11, 2001.

Nevertheless, the nonlife sector showed a favorable consolidated net result after taxes in 2001, with a reported profit of NAf.33.7 million. This result was a significant improvement compared to the net losses of NAf.0.7 million in 2000 and NAf.2.6 million in 1999. The downward trend in net results, noticed since 1999, appeared to halt in 2001. Both premium income and claims incurred decreased in 2001 compared to 2000. Despite the decrease in premium income, the industry reported a positive underwriting result of NAf.11.0 million in 2001 after two years with a negative result. In addition, the industry reported increased investment income in 2001, which led to an overall positive net result for the sector.

Premium income of the local life industry increased in 1999 and 2000. However, similar to the nonlife insurance industry, the life insurance industry experienced a decrease in premium income. Premium income in 2001 decreased by NAf.17.3 million (5.4%), indicating a decrease in the demand for life insurance products. Despite this development, the life insurance industry in the Netherlands Antilles remained profitable in 2001 reflected by an increase of NAf.5.5 million (48.7%) in the net result after corporate taxes.

8.3.2 Life insurance industry

8.3.2.1 Balance sheet

According to table 8.1, total assets of the local life insurance industry increased by 3.0% in 2001, compared with a 9.0% growth in 2000. Of the total assets in 2001, 66.7% was related to investments and 20.4% to current assets. Total liabilities increased mainly as a result of a NAf.21.7 million (2.6%) increase in technical provisions.

TABLE 8.1
Consolidated balance sheet of life insurance companies (in millions NAf.)

	1999		2000		2001	
	Local	Int'l	Local	Int'l	Local	Int'l
ASSETS						
Intangibles	-	-	-	-	-	-
Total investments	798.4	31.6	852.3	30.3	864.8	34.0
Current assets	211.8	6.4	253.3	18.8	264.0	17.8
Other assets	14.7	-	10.3	-	10.5	-
From separate accounts statement	130.7	-	143.5	-	157.4	-
Total admissible assets	1,155.6	38.0	1,259.4	49.1	1,296.7	51.8

EQUITY, PROVISIONS, AND LIABILITIES						
Capital	12.5	7.1	12.8	7.1	10.7	7.1
Surplus	84.9	20.7	89.4	20.7	99.0	21.9
Subord. instruments	-	-	-	-	-	-
Technical provisions	751.5	6.6	825.8	15.7	847.5	17.8
Other provisions & liabilities	9.2	0.9	10.2	1.2	9.8	1.3
Current liabilities	157.1	2.7	168.9	4.4	163.6	3.7
Contingent liabilities	9.7	-	8.8	-	8.8	-
From separate accounts statement	130.7	-	143.5	-	157.4	-
Total equity, provisions, and liabilities	1,155.6	38.0	1,259.4	49.1	1,296.8	51.8

The equity position of the local life insurance companies, consisting of capital, surplus, and subordinated instruments, increased by NAf.7.5 million (7.3%) in 2001. This increase can be attributed to an increase of NAf.9.6 million (10.7%) in the consolidated surplus account. The equity position of the local life insurance companies represents more than three times the amount needed to meet the 4% solvency requirement, which is equivalent to NAf.33.0 in 2001.

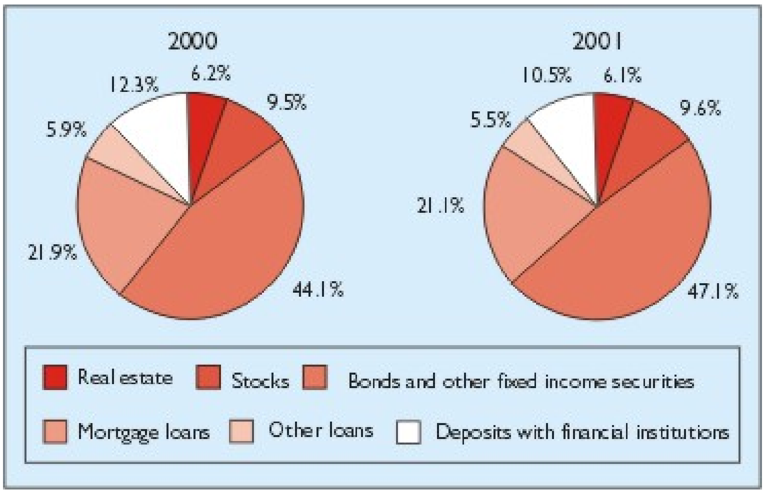
Total assets of the international life insurance companies increased by NAf.2.7 million (5.5%), reaching NAf.51.8 million at the end of 2001. The equity position experienced a slight increase to the amount of NAf.29.0 million at the end of 2001, well above the legally required solvency margin of NAf.0.6 million.

8.3.2.2 Investments

Total investments of the local life insurance industry increased by NAf.12.5 million (1.5%) in 2001, mainly due to the increase in bonds. Investment in real estate remained about the same as in 2000.

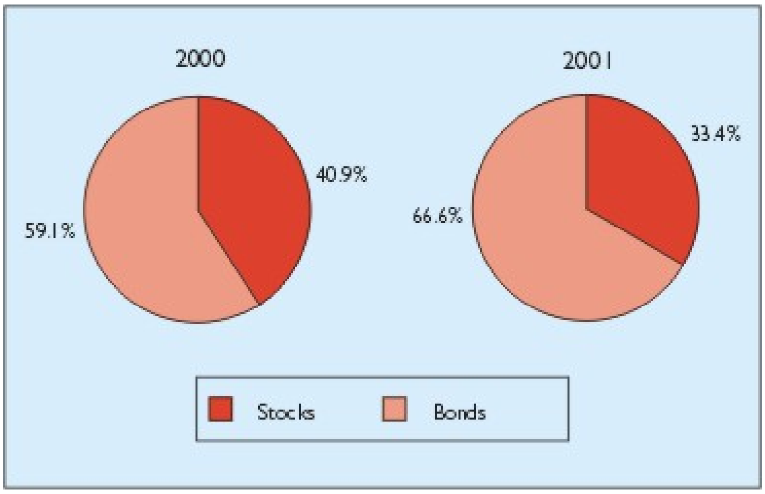
The composition of the consolidated investment portfolio of the local life insurance companies is presented in graph 8.2. This graph indicates that the shares of bonds and stocks increased by, respectively, 3.0 and 0.1 percentage points in 2001 compared to 2000. These increases were at the expense of the shares of deposits with financial institutions, mortgage loans, and other loans, which declined by 1.8, 0.8 and 0.4 percentage points, respectively.

GRAPH 8.2
Composition of the investment portfolio of local life insurance companies



The total investment portfolio of the international life insurance companies increased by NAf.3.7 million (12.2%) in 2001 compared to 2000, due primarily to an increase in bonds. In addition, it can be deduced from graph 8.3 that the share of bonds increased from 59.1% to 66.6%, while the share of stocks decreased from 40.9% to 33.4%.

GRAPH 8.3 Composition of the investment portfolio of international life insurance companies



8.3.2.3 Profit and loss statement

The operating results of the local life insurance industry are presented in table 8.2. The net result before corporate taxes increased by NAf.3.3 million (19.4%) in 2001, compared with the NAf.4.6

million (37.1%) increase in 2000. The net result after taxes increased by NAf.5.5 million to NAf.16.8 million in 2001 (48.6%).

TABLE 8.2
Consolidated profit and loss statement of life insurance companies (in millions NAf.)

	1999		2000		2001	
	Local	**Int'l**	**Local**	**Int'l**	**Local**	**Int'l**
INCOME						
Total net premium income	123.6	5.5	148.9	8.9	140.9	7.3
Net investm. income allocated to technical provisions	50.6	-	60.6	-	24.5	-
Net other operational income	0.4	-	0.4	1.1	0.4	1.5
Total operational income	174.6	5.5	209.9	10.0	165.8	8.8
EXPENSES						
Net benefits incurred	49.5	3.9	54.3	-	63.2	-
Change in net techn. prov.	73.3	-	94.5	7.5	80.4	5.4
Policyholders' dividends	9.3	0.5	10.2	0.5	9.8	0.5
Insurance expenses and non-corporate taxes	28.4	0.9	31.1	0.3	26.7	0.3
Commission and other acquisition costs	11.0	-	11.7	0.7	12.3	0.6
Net other operational expend.	0.9	-	2.6	0.3	0.1	0.1
Total operational expend.	172.4	5.3	204.4	9.3	192.5	6.9
Net operational result	2.2	0.2	5.5	0.7	-26.7	1.9
Net investment income allocated to surplus	9.2	1.4	9.4	2.3	46.8	2.2
Other income and expenses	-1.0	1.6	-	-0.6	-	-0.7
Net result from separate accounts	2.0	-	2.0	-	-	-
Extraordinary results	-	-1.2	0.1	0.7	0.2	0.3
Net result before corp. taxes	12.4	2.0	17.0	3.1	20.3	3.7
Corporate taxes incurred	5.2	-	5.7	-	3.5	-
Net result after corp. taxes	7.2	2.0	11.3	3.1	16.8	3.7

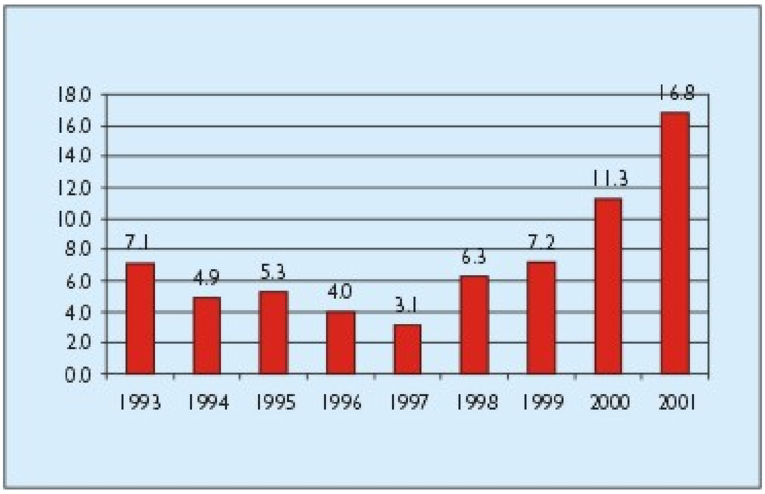
Premium income decreased by NAf.8.0 million (5.4%) in 2001, compared to 2000. Of the total premium income, 65.4% was related to individual life and 34.6% to group life business. Premium income for both individual life and group life decreased during 2001. The remarkable increase in net investment income of NAf.37.4 million (397.9%) to NAf.46.8 million was mainly responsible for the positive result in 2001.

The net operational result reflected a decrease of NAf.32.2 million to a loss of NAf.26.7 million in 2001. This decrease occurred because the decrease of NAf.44.1 million (21.0%) in total operational income exceeded the decrease of NAf.11.9 million (5.8%) in total operational expenditures. Total operational expenditures decreased mainly due to a decrease of NAf.14.1 million (14.9%) in the change in technical provisions, while the decrease of total operational income can be attributed primarily to the decrease of NAf.36.1 million (59.6%) in net investment income allocated to technical provisions.

Net premium income in the international life insurance industry showed a decrease from NAf.8.9 million in 2000 to NAf.7.3 million in 2001. Nevertheless, the net operational result increased by NAf.1.2 million to NAf.1.9 million in 2001, due primarily to a NAf.2.1 million lower change in net technical provisions.

As a result of positive investment returns, the life insurance industry servicing the international market ended up with a net result after corporate taxes of NAf.3.7 million in 2001, NAf.0.6 million (19.4%) more than in 2000.

GRAPH 8.4
Net results after corporate taxes of the local life insurance sector (in millions NAf.)



8.3.3 The nonlife insurance industry

8.3.3.1 Balance sheet

The balance sheet total of the nonlife insurance companies operating in the domestic market decreased by NAf.99.1 million (27.7%) to NAf.258.7 million at the end of 2001, compared to 2000. This decrease contrasted with 2000, when total assets increased by 17.9%, compared to 1999.

Current assets decreased by NAf.96.2 million (45.5%) and total investments by NAf.1.8 million (1.3%) in 2001.

Due to the short-term nature of the nonlife business in comparison with the life business, a smaller percentage of total assets is invested, namely, 54.0% in 2001. In 2000, 39.5% of total assets was invested. Consequently, a larger portion of total assets (44.6% in 2001) relates to current assets, compared to 20.4% in the life business.

On the liability side, the decrease in the balance sheet total in 2001 was reflected mainly by a NAf.88.9 million (71.2%) decrease in current liabilities.

The equity position of the local nonlife insurance industry decreased by NAf.7.9 million (10.1%) totaling NAf.70.7 million at the end of 2001. In 2000, an increase of 4.9% was recorded, compared to 1999. Despite the decrease in capitalization in 2001, the figure was well above the 15% margin (NAf.33.5 million) required by law to cover the industry's solvency margin.

TABLE 8.3
Consolidated balance sheet of the nonlife insurance industry (in millions NAf.)

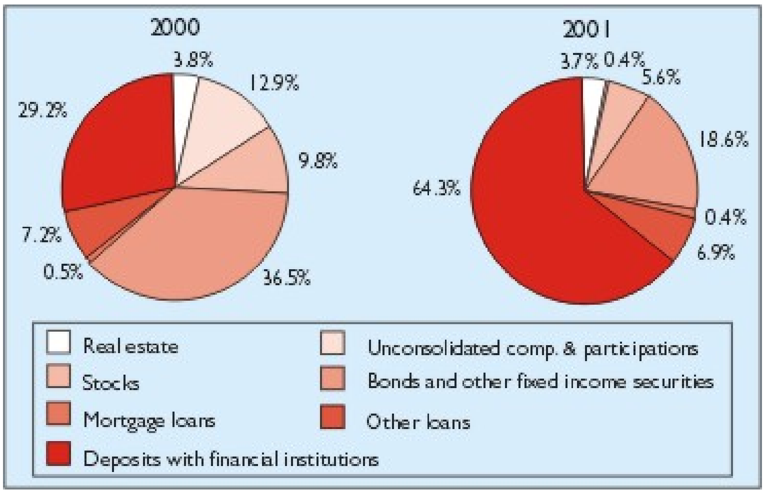
	1999		2000		2001	
	Local	**Int'l**	**Local**	**Int'l**	**Local**	**Int'l**
ASSETS						
Intangibles	0.2	-	0.1	-	-	-
Total investments	129.5	2,030.8	141.5	1,642.8	139.7	1,914.0
Current assets	168.5	113.9	211.5	133.7	115.3	114.3
Other assets	5.4	0.1	4.7	0.1	3.7	-
Total admissible assets	303.6	2,144.8	357.8	1,776.6	258.7	2,028.3
EQUITY, PROVISIONS, AND LIABILITIES						
Capital	37.1	113.7	41.9	115.5	29.2	146.1
Surplus	35.7	1,012.1	36.6	536.9	40.3	617.0
Subord. instruments	2.1	-	0.1	-	1.2	-
Technical provisions	145.4	920.4	150.3	1,059.4	146.2	1,200.5
Other provisions & liabilities	2.6	7.3	4.0	7.6	5.8	7.2
Current liabilities	80.7	91.3	124.9	57.2	36.0	57.5
Contingent liabilities	-	-	-	-	-	-
Total equity, provisions, and liabilities	303.6	2,144.8	357.8	1,776.6	258.7	2,028.3

The balance sheet total of the nonlife insurance companies servicing the international markets reflects an increase of NAf.251.6 million (14.2%), totaling over NAf.2 billion at the end of 2001. This increase in total assets was caused mainly by a NAf.271.2 million (16.5%) increase in investments. On the liability side, the largest increases were noted in the surplus account and technical provisions -- NAf.80.1 million (14.9%) and NAf. 141.1 million (13.3%), respectively. The industry disposed of NAf.763.1 million in equity at the end of 2001. As a result, the consolidated solvency position of the internationally operating nonlife insurance companies exceeded significantly the required solvency margin of NAf.69.2 million.

8.3.3.2 Investments

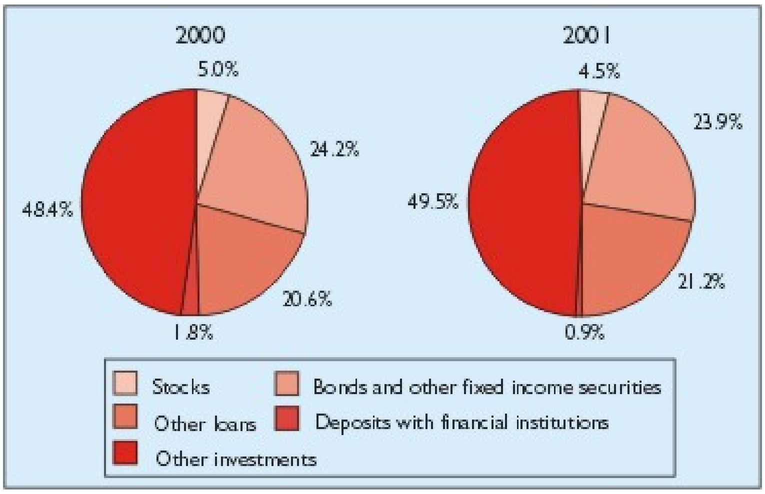
The composition of the investment portfolio of the local nonlife insurance companies is presented in graph 8.5. This graph indicates that the share of deposits with financial institutions in total investments increased from 29.2% in 2000 to 64.3% in 2001, reflecting a shift into liquidity. The increased share of deposits was largely at the expense of the shares of bonds, unconsolidated companies and participations, and stocks, which declined by 17.9, 12.5, and 4.2 percentage points, respectively.

GRAPH 8.5
Composition of the investment portfolio of the local nonlife insurance companies



The composition of the investment portfolio of the international nonlife insurance companies is illustrated in graph 8.6. No substantial changes were seen in 2001, compared to 2000. The graph indicates that the shares of other investments and other loans increased by 1.1 and 0.6 percentage points, respectively. These increases were at the expense of the shares of deposits with financial institutions, stocks, and bonds by 0.9, 0.5, and 0.3 percentage points, respectively.

GRAPH 8.6
Composition of the investment portfolio of the international nonlife insurance companies



8.3.3.3 Profit and loss statement

The net earned premiums of the local nonlife insurance industry decreased by NAf.4.9 million (2.9%) in 2001, compared to an increase of NAf.0.8 million (0.5%) in 2000. The net claims incurred during 2001 decreased by NAf.16.2 million (17.3%), while an increase of NAf.0.9 million (1.0%) was noted in 2000. The year 2001 closed with an underwriting profit of NAf.11.0 million, compared to underwriting losses of NAf.0.5 million in 2000 and NAf.2.4 million in 1999. Net investment income increased by NAf.19.8 million to NAf.27.4 million in 2001, compared to 2000. As a result of corporate taxes incurred, the industry ended up with a net profit of NAf.33.7 million in 2001, a turnaround compared to the losses in 1999 and 2000.

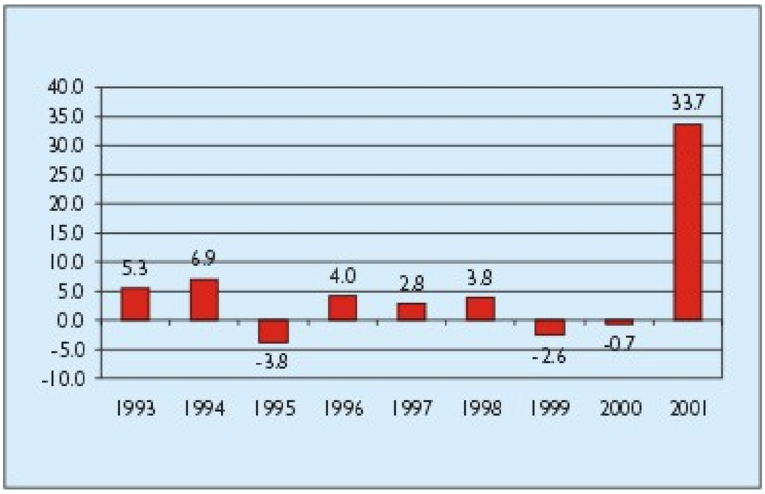
The total net earned premiums of the internationally operating nonlife insurance companies increased by NAf.175.0 million (39.3%) in 2001, compared to an increase of NAf.84.1 million (23.3%) in 2000. The net claims incurred increased by NAf.117.2 million (58.5%) in 2001. The underwriting result increased to NAf.158.8 million, NAf. 14.1 million (9.7%) more than in 2000.

The industry experienced a NAf.40.5 million (37.8%) decline to NAf.66.7 million in investment income in 2001. Due partly to this lower investment income, the sector ended with a net result after corporate taxes of NAf.168.4 million in 2001, NAf.60.9 million (26.6%) less than in 2000.

TABLE 8.4
Consolidated profit and loss statement of the nonlife insurance industry (in millions NAf.)

	1999		2000		2001	
	Local	**Int'l**	**Local**	**Int'l**	**Local**	**Int'l**
INCOME						
Total net earned premiums	168.4	361.5	169.2	445.6	164.3	620.6
Net underwriting income	0.1	2.4	5.4	0.2	6.0	0.6
Total operational income	168.5	363.9	174.6	445.8	170.3	621.2
EXPENSES						
Net claims incurred	92.8	240.4	93.7	200.2	77.5	317.4
Change in various provisions	1.2	-	1.4	65.8	1.4	81.9
Claim adjustment expenses	7.6	0.7	1.7	0.7	5.0	0.5
Net other underwr. expend.	59.3	23.3	68.9	32.4	71.3	59.8
Net other operational expend.	10.0	0.7	9.4	2.0	4.1	2.8
Total operational expend.	170.9	265.1	175.1	301.1	159.3	462.4
Underwriting results	-2.4	98.8	-0.5	144.7	11.0	158.8
Net investment income	9.0	123.5	7.6	107.2	27.4	66.7
Other results	-1.9	3.4	-0.3	-20.0	-1.5	-55.9
Extraordinary results	0.1	-0.4	-	1.1	0.3	1.7
Net result before corp. taxes	4.8	225.3	6.8	233.0	37.2	171.3
Corporate taxes incurred	7.4	2.1	7.5	3.7	3.5	2.9
Net result after corp. taxes	-2.6	223.2	-0.7	229.3	33.7	168.4

GRAPH 8.7 Net results after corporate taxes of the local nonlife insurance sector (in millions NAf.)



8.4 Overview of developments in the pension industry

Total assets of the pension industry increased by 1.1 % in 2000 compared to 1999. Investments accounted for 76.9% of the industry's total assets, of which bonds accounted for 42.5% of total assets. The equity position of the pension industry improved by 34.8% in 1999 compared to 1998, while a decrease of 21.4 % was noted in 2000 compared to 1999.

During the period 1998-2000, the average amount in premium contributions received by the pension funds equaled NAf. 165.3 million, while the average amount in benefits paid amounted to NAf.139.8 million. On an annual basis, premium contributions decreased by NAf. 49.3 million (26.6%) in 1999, but increased by NAf. 37.9 million (27.7%) in 2000.

TABLE 8.5
Consolidated balance sheet of the pension industry (in millions NAf.)

	1998	1999	2000
ADMISSIBLE ASSESTS			
Investments, of which:			
-Real estate	68.6	76.9	91.2
-Participations	6.4	17.2	22.7
-Stocks	962.3	1,121.2	1,023.2
-Bonds and other fixed income sec.	1,844.1	1,820.5	1,834.5
-Participations in investment pools	-	-	-
-Mortgage loans	73.0	77.5	88.8
-Other loans	89.5	121.7	141.2
-Deposits with financial institutions	44.1	82.2	112.8

-Other investments	5.6	6.4	7.5
Current assets	407.4	406.9	407.0
Other assets	457.4	542.4	591.6
Total	3,958.4	4,272.9	4,320.5
EQUITY, PROVISIONS, AND LIABILITIES			
Equity, of which:			
-Foundation capital			
-Surplus	382.7	516.0	405.7
Technical provisions, of which:			
-Provisions for pension obligations	3,486.7	3,685.5	3,888.7
-Other technical provisions	-14.0	16.1	10.9
Other provisions and liabilities	1.4	1.4	6.8
Current liabilities	101.6	53.9	8.4
Contingent liabilities			
Total	3,958.4	4,272.9	4,320.5

Total expenses of the pension industry decreased by NAf.24.6 million (6.3%) in 2000 compared to 1999. The benefit payments and additions to the technical provisions accounted for 92.6% of expenses in 2000. Contrary to the previous years, the sector experienced a loss of NAf.68.3 million in 2000, attributable mainly to unrealized capital losses.

TABLE 8.6
Consolidated profit and loss statement of the pension industry (in millions NAf.)

	1998	**1999**	**2000**
INCOME			
Contributions	185.5	136.2	174.1
Transferred pension obligations received	-	-	-
Net investment income earned and net realized capital gains and losses	256.9	276.5	319.1
Benefits received from reinsurer	0.3	0.5	0.6
Profit sharing from reinsurer	2.1	2.7	3.1
Other income	13.1	5.3	3.4
Total income	457.9	421.2	500.3
EXPENSES			
Pension benefits incurred	140.2	134.5	144.6

Change in net technical provisions	185.1	222.4	195.3
Pension obligations transferred	0.8	0.7	1.1
Reinsurance premiums incurred	14.7	12.0	9.9
Operational expenses incurred	11.9	13.3	13.3
Other expenses incurred	12.0	8.7	2.8
Total expenses	364.7	391.6	367.0
Extraordinary result	-	-	-4.7
Net operational result before gains or losses	93.2	29.6	128.6
Net unrealized gains or losses, of which:			
Invested assets	-	-	-
Non-invested assets	-	1.2	0.1
Foreign exchange	77.0	127.6	-197.0
Net profit or loss	170.2	158.4	-68.3

8.5 Investment institutions and administrators

To promote the soundness and stability of the financial sector in the Netherlands Antilles and to continue to pursue high standards and integrity, legislation was drafted for the supervision of investment institutions and administrators. The National Ordinance on the Supervision of Investment Institutions and Administrators (N.G 2002, no. 137) took effect on January 1, 2003. The objectives of this new ordinance are threefold: (1) to ensure that the interests of the investors are protected, (2) to promote the adequate functioning of the financial markets, and (3) to maintain the reputation of the Netherlands Antilles as a respectable international financial center.

The supervision of investment institutions is focused on the adequacy of the investment institutions' infrastructure. This adequacy is revealed by the conduct of business, the institution's equity capital, and the competence and integrity of the persons who (co-)determine the institution's policy, based on applicable rules and regulations, as well as the provision of information to (prospective) investors.

Moreover, the Bank's supervision of administrators is focused on the adequacy of the infrastructure of the administrator, as revealed by the conduct of business, the competence and integrity of the persons who (co-)determine the administrator's policy, and the administrator's compliance with rules and regulations.

The Bank also issued Directives on the Supervision of Investment Institutions and Administrators. The new ordinance, together with the directives, provides the basis for the supervision of investment institutions offering participating interests in or from the Netherlands Antilles, and administrators that provide administrative services to investment institutions in or from the

Netherlands Antilles. Furthermore, the Bank recently issued Policy Guidelines on Exemption Regulation for both investment institutions and administrators. These policy guidelines outline the basis on which the Bank may grant an exemption to investment institution or administrator.

In addition, three other national decrees governing the appointment of a representative organization, supervision costs, and fines were drafted and are pending enactment.

POLICIES AND ACTIVITIES OF THE BANK

9.1 Training and seminars

The Bank's staff attended various courses, seminars, and conferences in 2002 as part of the Bank's continuing education policy to keep its personnel abreast of the latest developments in their fields of expertise.

Staff in the department of Supervision on Institutional Investors attended, among other things, the annual meeting of the International Association of Insurance Supervisors (IAIS), a seminar on risk-based capital of the IAIS, a congress of the International Actuarial Association, a pension workshop organized by the IMF and World Bank, and the annual meeting of the Offshore Group of Insurance Supervisors. Furthermore, staff in the Statistical Information and Reporting Department attended a meeting of the Irving Fisher Committee on Central Bank Statistics of the International Statistical Institute and participated in a seminar organized by the IMF to evaluate the 2001 and prepare the 2002 Coordinated Portfolio Investment Survey. The Netherlands Antilles participates in the survey, held among companies operating in the domestic and international financial sector. Staff in the Banking Supervision Department attended seminars on risk management & internal control and risk focus supervision, both hosted by the Association of Supervisors of Banks of the Americas (ASBA), and a seminar on international accounting and auditing for banks organized by the Financial Stability Institute. Moreover, Research Department staff participated in workshops on economic modeling organized by the World Bank and the Center of Monetary Studies for Latin America and the Caribbean, and in a seminar on inflation targeting hosted by the central bank of Guatemala.

During 2002, the Bank continued to support "The Financial Institute", an institution geared towards educating employees in the local financial sector. The Bank helped organize seminars and examinations, participated in by the Bank's staff. Seminars were held on document security, compliance, and derivatives.

9.2 Developments in supervision of institutional investors

To enhance the integrity of the financial sector, the Bank introduced a new Policy Rule on Integrity Testing, effective June 2002. This new integrity and fitness testing of supervised institutions' policymakers will take place every two years.

Reinsurers operating in or from the Netherlands Antilles are subject to supervision by the Bank by virtue of the Special Insurance License Decree (N.G. 1992, nr. 50). As a member of the IAIS, the Bank will adopt the principles laid down in the IAIS guidelines, and where necessary will adjust its present supervisory guidelines to be in line with the international developments and requirements. Also the Financial Stability Forum (FSF) has endorsed the introduction of principles for reinsurance supervision, calling for improved transparency in reinsurance markets and enhanced disclosure of reinsurers' activities.

Furthermore, the committee working on the introduction of the Motor Insurance Guarantee Fund was reactivated. The committee is working on changes concerning the motor liability insurance legislation and the infrastructure needed to make the fund operational. A centralized registration system will be introduced to facilitate law enforcement. The aim of this registration system is to prevent uninsured vehicles from participating in traffic.

The aim of supervision is to ensure a solvent insurance and pension industry in the interest of the policyholders and other beneficiaries. The Bank's supervision concentrates mainly on the financial aspects of an institution. However, developments, both local and international, are forcing supervisors towards a supervisory regime that concentrates also on the nonfinancial aspects of an institution, for example, its dealings with policyholders and claimants, so-called market conduct. The four key market conduct areas the Bank initially will be concentrating on are sales and advertising, underwriting, rating, and claims. Examination procedures for this purpose have been drafted by the Bank.

In September 2000, the Bank issued the policy paper 'Guidelines for the Detection and Deterrence of Money Laundering for Life Insurance Companies'. In March 2003, the Bank started money-laundering visitations to the premises of life insurance companies. The purpose of the visitations is to review the company's procedures to prevent and deter money laundering. The findings of a visitation will be documented in a visitation report, which will be shared with the company.

Finally, in December 2002, Parliament approved legislation for the licensing and supervision of investment institutions and administrators. With this legislation, the Netherlands Antilles complies with the international standards.

9.3 International financial sector developments

In October 2001, the FATF adopted 8 special recommendations on the financing of terrorism to complement the 40 recommendations of 1996. The Netherlands Antilles endorsed these 8 special recommendations and worked out the details for their implementation during 2002. Furthermore, the Netherlands Antilles drafted legislation to be able to ratify the 1999 UN Convention on Terrorism Financing.

The Central Bank issued several letters to the financial institutions under its supervision instructing them to scrutinize all accounts for a possible relationship with terrorists or terrorist organizations. Any funds suspected of being related to terrorism had to be frozen immediately, according to the Ministerial Decrees on the freezing of assets. The Central Bank also instructed financial institutions how to handle wire transfers to comply with special recommendation VII of the FATF.

The tasks of the Committee on Money Laundering have been expanded to include the combating of terrorism financing in 2002. This new mandate is based on a Ministerial Decree of August 2002, which includes also the new composition of the committee.

At the Bank' request, the IMF visited the Netherlands Antilles to assess our supervisory and legal infrastructure. This was done in the framework of the Offshore Financial Center Program (OFCP) of the IMF. This assessment will be finalized in 2003.

9.4 Monetary policy

The reserve requirement is the main monetary policy instrument of the Central Bank. This instrument is aimed at controlling the liquidity in the banking system and, hence, the potential for credit extension. Under the reserve requirement, commercial banks are required to deposit a fixed percentage of their domestic liabilities at the Central Bank. Until January 1, 2002, this percentage was determined monthly on the basis of developments in the free reserves of commercial banks, the official reserves, and domestic credit extension. Part of the reserve requirement could be held in Certificates of Deposit (CDs), while the remainder was non-interest-bearing. In addition to the reserve requirement, the Central Bank has several other instruments for conducting monetary policy. The monetary cash reserve arrangement, effective until March 1, 2002, limited commercial bank lending by imposing a maximum allowed penalty-free credit growth. Furthermore, commercial banks are not allowed to have a negative net foreign assets position to prevent them from accumulating foreign debt. The Bank uses CDs and Repos to support the other instruments.

As of January 1, 2002, the Bank further adjusted its monetary policy, aimed at promoting market forces in the conduct of its policy. This decision was taken in light of the significant increase in international reserves in the Netherlands Antilles and the continuing decline in interest rates in the United States.

One of the most important changes in the Bank's monetary policy was that commercial banks are no longer compelled to buy Certificates of Deposit (CDs) to comply with the reserve requirement. As of January 1, 2002, the banks can determine freely how much CDs they want to buy. The interest rate on CDs will no longer be set by the Bank, but will be determined by the market participants in bi-weekly tenders. However, the CD rate is bound to a maximum, equal to the Bank's pledging rate minus 100 basis points. Furthermore, the reserve requirement percentage was reduced by 2.5 percentage points to 9% and is set for three months, but the reserve requirement will be entirely non-interest-bearing. In addition, the Bank will initiate open-market operations through buying or selling government securities whenever monetary developments warrant.

Moreover, the Bank reduced its pledging rate, i.e., its official lending rate, in five steps during 2002: by 0.25 percentage point to 6.75% on January 1, by 1.0 percentage point to 5.75% on June 1, by 0.75 percentage point to 5.0% on July 4, by 1.0 percentage point to 4.0% on August 20, and by 0.5 percentage point to 3.5% on November 4. On January 13, 2003, the pledging rate was reduced further by 0.5 percentage point to 3.0%. As a result, the rates linked to the pledging rate decreased also. The marginal lending rate -- a mark-up on the pledging rate of 100 basis points applicable on commercial banks' borrowing exceeding NAf.20 million-- declined to 4.0%, while the maximum CD rate fell to 2.0%. These reductions brought the Bank's official rates more in line with the declining trend in the rates in the domestic money and capital market.

These measures were complemented by the lifting of the ceiling on domestic credit extension to the governments as of March 1, 2002, implying the inactivation of the monetary cash reserve arrangement. This decision was made in light of the high level of foreign exchange reserves.

On January 15, 2003, the Bank introduced some refinements in its CD auctions to increase the attractiveness of subscribing for commercial banks. The refinements included CD maturities of 12, 26, and 52 weeks, in addition to the maturity of 4 weeks. Furthermore, the banks can subscribe at interest multiples of 0.01% instead of 0.25%.

Finally, the Bank increased the reserve requirement from 9.0% to 9.5% on January 16 and to 10.0% on April 16, 2003. This decision was taken because commercial banks' credit growth, particularly credit to the government, is increasingly deviating from the targeted growth rate. If left unchecked, this development will ultimately erode our foreign exchange reserves position.

FOREIGN EXCHANGE REGULATIONS AND LICENSE FEE

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

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

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

1. to promote the Netherlands Antilles as an international financial center; for this reason, the Ordinance contains special provisions for companies engaged in international financial and business transactions;
2. to gather 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.

In 2002, the number of foreign exchange licenses issued by the Bank was 1,508, a decline of 268 (15%) compared to 2001. This decline can be attributed primarily to the drop in the number of foreign exchange exemptions granted to international financial and business companies (327). In contrast, the total capital flow related to the licenses granted increased by NAf.227.7 million (87%) to NAf.490.0 million. This increase is explained particularly by the licenses granted to the utility company IUH in Curacao for participation by the American utility company Mirant (NAf.72 million) and the financing of a multi-annual investment and loan refinancing program by a consortium of foreign and local financial institutions (NAf.205 million). In table 10.1, the participation is included under the item "Other" and the foreign financing under "Borrowing abroad".

Table 10.1
Overview of foreign exchange licenses issued (in millions NAf.)

Description	2001 Number	2001 Amount	2002 Number	2002 Amount
Establishm. comp. by nonresident	55	0.9	73	0.9
Transfer to own account abroad	15	13.7	9	1.2
Portfolio investment abroad	8	5.5	6	9.8
Borrowing abroad	149	228.9	201	402.9
BOO-project	1	12.7	-	-
Lending abroad	8	0.6	8	2.2
Request for foreign bank account	3	-	-	-
Request for local nonresident account	12	-	8	-
Request for intercomp. account abroad	-	-	2	-
Granting guarantee abroad	4	-	2	-
Exemption int. fin. & bus. companies	1,521	-	1,194	-
Other	-	-	5	73.0
Total	1,776	262.3	1,508	490.0

Starting January 1, 1996, a license fee was introduced whereby the foreign exchange banks have to pay a fee to the Central Bank on their international transactions. This license fee replaced the foreign exchange tax, 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 the re-investment of funds abroad and the re-exports of the free-zone companies.

Table 10.2 provides an overview of the license fees collected monthly during 2000 through 2002. From the total amount of license fees generated in the Netherlands Antilles in 2002, NAf.27,089.8 thousand (67%) was generated on Curacao, NAf.12,379.8 thousand (31%) on St. Maarten, and NAf.567.5 thousand (2%) on Bonaire. The remaining NAf.137.7 thousand in license fees was paid through the Central Bank.

Table 10.2
License fees collected, 2000 through 2002 (in thousands NAf.)

	2000	2001	2002*
January	3,096.2	3,369.2	3,103.1
February	3,170.8	2,924.4	2,698.2
March	3,255.3	3,439.1	3,070.9
April	2,827.0	2,777.4	3,072.9
May	3,560.4	3,074.9	3,568.6

June	3,168.6	3,182.4	3,260.5
July	3,112.5	2,998.2	3,510.7
August	3,001.3	3,261.8	3,294.0
September	3,083.6	2,559.7	3,266.3
October	2,955.5	3,038.6	3,637.1
November	3,139.3	2,958.2	3,337.3
December	3,394.0	3,186.5	4,355.2
Total	37,764.5	36,770.4	40,174.8

*Preliminary

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Table11.1
Balance Sheet as of December 31, 2002

ASSETS	**2001**	**2002**
Gold	138,858,059	138,858,059
Receivables and securities in foreign currency	543,009,930	719,106,460
Advance account Central Government	29,203,216	29,203,216
Government bonds	185,257,337	114,316,609
Other long-term receivables	13,744,237	23,607,648
Fixed assets	94,498,754	102,625,692
Other current assets	18,741,797	20,406,215
TOTAL ASSETS	1,023,313,330	1,148,123,899

LIABILITIES	**2001**	**2002**
Bank notes in circulation	256,938,031	284,760,076
Residents' current accounts		
- in guilders	430,954,098	425,420,723
- in foreign currency	44,864,385	41,390,513
Residents' time deposits		
- in guilders	113,800,000	219,500,000
Nonresidents' current accounts		
- in guilders	789,927	2,240,000
- in foreign currency	-	-
Money in custody	892,827	981,113
Other current liabilities	19,084,760	16,001,321
Undistributed earnings	14,621,219	16,392,024
Special reserves	81,438,129	81,438,129
Reserve fund	30,000,000	30,000,000
Reserve for hedged positions	-70,046	-
Capital	30,000,000	30,000,000
TOTAL LIABILITIES	1,023,313,330	1,148,123,899

The 2002 figures are preliminary and unaudited. The 2001 figures are derived from the audited 2001 financial statements.

Table 11.2
Profit and Loss Account 2002

	2001	**2002**
<u>INCOME</u>		
Interest income	35,079,508	33,271,264
Foreign exchange earnings	1,015,041	1,190,839
Miscellaneous earnings	4,438,692	3,973,335
Subtotal	40,533,241	38,435,438
License fee	36,827,624	40,099,046
TOTAL INCOME	77,360,865	78,534,484
<u>EXPENSES</u>		
Interest expenses	3,852,125	5,643,278
Depreciation of fixed assets	2,185,759	4,196,980
Depreciation of printing costs bank notes	435,866	383,397
General expenses	22,524,728	26,069,938
TOTAL EXPENSES	28,998,478	36,293,593
OPERATING PROFIT	48,362,387	42,240,891
Extraordinary income/loss	-1,342,769	-172,086
<u>NET INCOME</u>	47,019,618	42,068,805
<u>Distribution of net income</u>		
Net income	47,019,618	42,068,805
Paid to the central government	52,099,000	40,298,000
Change in undistributed earnings	-5,079,382	1,770,805

The 2002 figures are preliminary and unaudited. The 2001 figures are derived from the audited 2001 financial statements.

11.1 Notes to the balance sheet as of December 31, 2002

11.1.1 Gold

The gold bars 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%. The gold is revalued every three years. Changes resulting from revaluations are debited or credited to the special reserves after approval from the Minister of Finance. The last revaluation was ultimo 2000.

11.1.2 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 mid-rate prevailing at the balance date.

11.1.3 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.

11.1.4 Government bonds

Government bonds reflect the Bank's portfolio of bonds issued by the central government and the island government of Cura3ao. The Bank holds this portfolio mainly for monetary purposes. The bonds are valued at their purchase price or lower nominal value.

11.1.5 Other long-term receivables

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

11.1.6 Fixed assets

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

The increase in fixed assets reflects, among other things, the finalization of the construction of the Bank's new premises in Scharloo in 2002.

11.1.7 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.

11.1.8 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.

11.1.9 Residents' current accounts

These include the balances in current account of domestic banks, central and island government 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 mid-rates prevailing at year end.

11.1.10 Residents' time deposits

These include the balances in time deposits of domestic banks and government institutions. The balances are interest-bearing.

11.1.11 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 mid-rates prevailing at year end.

11.1.12 Money in custody

This amount represents the 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 Consignation (P.B. 1886, no. 22).

11.1.13 Other current liabilities

This balance includes accrued interest and accounts payable.

11.1.14 Undistributed earnings

Under this heading appears the accumulated earnings of the bank for the current and previous years, less the amounts paid to the central government.

11.1.15 Special reserves

This reserve was formed originally due to the revaluation of the gold stock in the years 1971 and 1973. The profits made by the sale of numismatic coins during 1990 also were added to the balance of this account. As of 1994, the Bank revalues its gold every 3 years. Due to the 2000 revaluation, the reserve decreased with NAf.40,9 million. The next revaluation will be in 2003.

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.

11.1.16 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).

11.1.17 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).

11.2 Notes to the profit and loss account 2002

11.2.1 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.

11.2.2 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 on Foreign Exchange Tax 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.