ANNUAL REPORT 2003

Bank van de Nederlandse Antillen

REPORT OF THE PRESIDENT

1.1 General review

The recovery of the Netherlands Antillean economy continued in 2003 amidst an improving world economic climate. Economic growth, measured by real Gross Domestic Product, is estimated at 1.4% compared to 0.4% in 2002. The increase in economic activity was fueled primarily by the expansion in net exports, supported by higher private and government consumption. The growth in private consumption was related to an improvement in disposable income stemming from an increase in private transfers from abroad and the reinstatement of the vacation allowance for civil servants. An expansionary fiscal policy reflected by, among other things, higher personnel expenses – due to the payment of vacation allowance and the improved adherence with the contributions to the government pension fund – and more outlays for goods and services, contributed to the increase in government consumption. Nevertheless, domestic expenditure developed weakly due to a further decline in investment. Private investors put investment decisions on hold because of growing uncertainty surrounding the sustainability of the recovery. This uncertainty was fueled by the failure of the new government, which took office in July 2003, to present its program and the overhasty reversion of past reforms in the labor and product markets.

The economic recovery has not yet translated in an improvement of the labor market, reflected by an increase in the unemployment rate from 14.6% in 2002 to 15.3% in 2003. Unemployment rose because the increase in employment could not keep up with the expansion of the labor force. The latter resulted from an increase in the number of migrants to the islands and the impact of the legalization of illegal aliens during 2002. Furthermore, inflation accelerated to 1.9% in 2003, up from 0.4% in 2002. The higher inflation rate can be explained mainly by an increase in utility prices due to a rise in world oil prices, the impact of the appreciation of the euro on prices of imports from Europe, and the higher inflation rates of our trading partners the United States and Venezuela.

The improvement in our export performance in 2003 was attributable primarily to the tourism, transportation, and oil sectors. Tourism registered a further expansion, particularly in the number of stay-over visitors. This expansion can be explained by the further recovery of the North American market from the impact of the terrorist attacks in September 2001, the quick ending of the war in Iraq, and the decision of American tourists to stay closer to home. In addition, the European market grew markedly as a result of the appreciation of the euro against the US dollar and a capacity increase on the mid-Atlantic route at lower airfares. The Latin-American market suffered from the introduction of visa for Colombians, more rigid visa procedures for Dominicans, and the political and economic crisis in Venezuela. Compared to St. Maarten and Bonaire, Curacao noted a marginal growth because the deterioration in the Latin-American and Caribbean markets largely offset the expansion in the North-American and European markets. Cruise tourism improved also due to the expansion in St. Maarten and Bonaire. Curacao, however, registered a decline in the number of cruise tourists.

The performance of the transportation sector was favorable in 2003. The Antillean carrier, Dutch Caribbean Airline (DCA), registered a substantial growth in both the number of passengers and the amount of freight transported. Regional activities in particular contributed to the growth, primarily because of the expansion of its fleet. Nevertheless, the increase in activities has not translated in an improvement of the airline's financial position. Especially, the liquidity position is weak because suppliers demand cash payments after the large arrears built up by its predecessor, Air ALM. As a result, arrears are accumulating in the remittance of wage tax and social premiums withheld. The airline's owner, the island government of Curacao, is prepared to forgive NAf 10 million of these arrears on top of a capital injection of NAf 15 million. Although this financial support may be justifiable with respect to the company's economic importance, the government must avoid that it will develop in a recurrent event. Therefore, the support should be provided under strict conditions that guarantee a lasting improvement in the company's financial condition and, hence, secures its long-term viability.

In line with the growth in stay-over tourism, activities on the airports expanded. Noteworthy is the shift in transit passengers from Curacao to Bonaire, which boosted the number of passengers handled by Bonaire's airport at the expense of the growth at Curacao's airport. This shift is attributable to the rerouting of the intermediate stops on KLM's flights between Amsterdam and Latin America from Curacao and Aruba to Bonaire since the summer of 2002. Furthermore, the harbor industry showed mixed developments. The harbor of Curacao reported a decline in the number of ship calls, especially tankers. However, the amount of freight handled increased marginally, owing to more transshipment. In contrast, Bonaire's harbor registered a marked increase in the number of ship calls, which occurred particularly in tankers. The development in tanker calls was related to a general strike in Venezuela, including state oil company PDVSA which leases the refinery from the Curacao government, at the end of 2002. Because the refined products could no longer be exported, they were transshipped primarily to Bonaire's oil terminal. As a result, oil storage and transshipment activities expanded considerably. Moreover, the difficulties in Curacao's ship repair sector continued, reflected by a decline in the number of man-hours sold.

The oil refinery did not fully recover from the impact of the temporary shutdown at the end of 2002, as the number of barrels produced declined in 2003. Nevertheless, the refinery's contribution to the economy improved as measured by the refining fee. Noteworthy is that a new utility plant using the build-own-operate concept came into full operation around mid-year, strengthening the refinery's competitiveness and reliability and, hence, its long-term viability. A major challenge remains the environmental impact of the refinery's operations. Tourism development and public health considerations require investments to reduce this impact but may not endanger the economic viability of the refinery. Therefore, the refinery's operator together with the government should work out feasible solutions aimed at reaching a durable equilibrium between these adverse interests.

The international financial and business services sector recorded a decline in activities as measured by receipts for services rendered. The elimination of the distinction between onshore and offshore activities in the Netherlands, effectuated with the introduction of the new fiscal framework (NFR), ended the low tax regime for offshore activities. This disadvantage would be more than compensated by the improved competitive position of the Netherlands Antilles in negotiating new tax treaties, supported also by the new tax arrangement for the Kingdom of the Netherlands (BRK). Although negotiations have started with, among others, Venezuela and the United States, progress is slow, affecting the creation of new business in the sector. However, the new BRK resulted in higher tax revenues for the government because the withholding tax on dividends form the Netherlands to the Netherlands Antilles collected by the Dutch tax office is transferred entirely to the Antillean government.

Finally, the free zone sector in Curacao showed mixed developments in 2003, reflected by an increase in re-exports and a decline in the number of visitors. The lower number of visitors was related, among other things, to the tightening of visa procedures for visitors from Colombia and the Dominican Republic, and the political and economic instability in Haiti. Overall, the sector's activities continued to grow, which resulted in an expansion of its facilities to accommodate new businesses.

The balance of payments improved for the third consecutive year in 2003, although the surplus continued to decline. As a result, our international reserves increased further but official reserves declined, contributing to a deterioration of the import coverage to 2.7 months. Official reserves declined because the commercial banks purchased foreign exchange at the Bank to invest abroad, among other things, in light of the rising stock markets.

The improvement in the current account was attributable to improvements in the trade, services, and current transfers balances. The trade balance recorded a lower deficit because the increase in exports, due particularly to bunker sales, exceeded the increase in imports. Imports were higher as a result of more oil imports related to the rise in world oil prices. The surplus on the services balance improved primarily due to the favorable development in tourism. Moreover, the higher surplus on the current transfers balance resulted from the transfer of dividend tax by the Netherlands related to the new BRK and a higher net inflow of transfers by individuals. In contrast, the income balance recorded a further deterioration which can be explained mainly by more interest payments abroad.

The capital and financial account improved also, because of a higher increase in foreign assets than in foreign liabilities. Apart from the increase in reserves, foreign assets grew as a result of more trade credit extended by Antillean exporters and higher balances on foreign accounts related, among other things, to maturing investments. The latter was reflected by a decline in assets on the portfolio investment account. Foreign liabilities increased largely due to more trade credit received by Antillean importers and an increase in loans taken up abroad, among other things, to finance the reconstruction of Curacao's airport.

The public finances deteriorated further in 2003, reflected by an increase in both the cash deficit and the debt of the general government. The deterioration of the deficit was attributable entirely to the rise in expenditures, more than offsetting the higher revenues. Like 2002, higher government spending was facilitated by the ample availability of finance on the local capital market because domestic government securities continued to offer more attractive yields compared to alternatives abroad. However, in the second half of 2003, growing uncertainty surrounding the authorities' commitment to address the deterioration of the public finances caused investors' interest in government securities to wane and yields to rise again as higher risk premiums were demanded.

The expansionary budgetary policy was reflected by an increase in all expenditure categories except net lending. Most pronounced were the increases in the outlays on goods and services, domestic interest payments, and capital transfers. The higher interest payments can be explained by the rapid accumulation of debt, while the increase in capital transfers was due to the settlement of guarantees extended to the former government-owned airline, Air ALM. The increase in revenues was accounted for entirely by the rise in non-tax revenues as a result of the transfer of dividend tax by the Dutch government, dividend remittances by government-owned companies, and the settlement of claims and debts with the public housing foundation, FKP.

The financing of the cash deficit, the formalization of accumulated funds deficits of the social security bank, SVB, and the appreciation of the euro contributed to the further accumulation of government debt in 2003, reaching 90% of GDP. To address this unsustainable debt position, the government established a debt commission ("Commissie Schuldenproblematiek") which presented its report in July 2003. Its recommendations included, among other things, fiscal consolidation, the strengthening of budget discipline, and refinancing of the outstanding debt at lower interest rates. Although the government adopted the commission's recommendations, no action was taken, aggravating the short-term fiscal outlook. Therefore, to prevent a deepening of the financial-economic disequilibria in our economy, bold and convincing steps by the authorities in line with the recommendations of the debt commission are urgently needed.

The monetary aggregates expanded further in 2003, albeit at a slightly slower pace than in 2002. Both the domestic and external sectors contributed to 2003's expansion. The domestic expansion was attributable primarily to the government sector, particularly the central government. The central government's expansionary impact resulted from an increase in debt securities as well as the withdrawal of deposits, while the expansionary impact of the island governments was due entirely to the withdrawal of deposits. In addition, credit extension to the private sector grew moderately in line with the economic recovery.

In line with the further decline in international interest rates and, hence, its impact on domestic money and capital market rates, the Bank reduced its official lending rate (i.e., the pledging rate) further in three steps during 2003 from 3.5% on January 1 to 2.25% on June 30. In addition, effective January 15, 2003, the Bank introduced some refinements in its auctions of certificates of deposit (CDs) to increase their attractiveness to commercial banks. These refinements included more maturities and subscription at smaller interest multiples. Finally, the Bank increased the reserve requirement percentage from 9.0% to 9.5% on January 16, and to 10.0% on April 16, 2003. These steps were considered necessary to curb the strong growth in commercial banks' credit extension to the government given its potential negative impact on our foreign exchange reserves.

The further recovery of the economy improved the performance of the domestic banking sector, reflected by a stronger growth in assets and a higher profitability. However, asset quality deteriorated slightly, indicated by an increase in the nonperforming loan ratios, but loan loss provisioning was adequate. Moreover, the sector's capitalization remained above international standards. Contrary to the domestic banking sector, the international banking sector incurred a decline in activities as measured in total assets. Nevertheless, the sector's profitability improved substantially due to less provisioning. In addition, the capitalization of the international banks remained well above the international standards.

The Bank continued its efforts to enhance its supervision of the financial sector in the Netherlands Antilles to keep up with the international supervisory developments and, hence, remain an internationally reputed financial center. On January 1, 2003, the Bank's supervisory tasks were expanded with the supervision on investment institutions and administrators. During 2003, several directives and guidelines were issued detailing specific supervisory issues regarding these companies. In addition, on September 1, 2003, the updated supervisory regulation on general and specific provisions for loan losses of credit institutions became effective. Furthermore, the supervision on the insurance sector was expanded with insurance intermediaries when the National Ordinance on Insurance Intermediaries took effect on January 1, 2004. On the same date, the Bank became entrusted with the supervision of trust service providers previously executed by a separate supervisory body.

The Netherlands Antilles continued its efforts against money-laundering activities in line with international developments. The Netherlands Antilles endorsed the revised version of the 40 recommendations on money laundering and terrorist financing of the Financial Action Task Force (FATF). These recommendations must be applied also to lawyers, public notaries, accountants, real estate companies, and dealers in precious metals and stones. Furthermore, in June 2003, the Bank issued new, more comprehensive provisions and guidelines on the detection and deterrence of money laundering and terrorist financing for credit institutions, insurance companies, and money transfer companies.

1.2 Policy considerations

Although the recovery of the Antillean economy is slowly gaining strength, its fundamentals are still weak. Economic growth in 2002 and 2003 was largely fueled by domestic consumption, while investment declined. Therefore, efforts should be made to promote investment growth, which is crucial for a durable economic recovery. These efforts will be facilitated by the expected strengthening of world economic growth in 2004, which will have a positive impact on our exports.

The year 2003 can be considered a year of lost opportunities for the Netherlands Antilles. The change of government, frequent tensions between the coalition partners, the lack of a government program, and the reversal of structural reforms all contributed to a climate of increasing uncertainty and eroding confidence. The policy prescription for a lasting recovery of our economy is well known but the authorities failed to come up with a credible program to address the large and growing macro-economic and social disequilibria. Such a program should focus on fiscal consolidation, structural reform, growth promotion, and poverty alleviation.

Developments in public finances remained worrisome, reflected by high deficits and the rapid accumulation of debt. Although the general government's operational deficit of NAf 200 million in 2004 remains within the target of the debt commission, its financing requirement is estimated at more than NAf 500 million. The high financing requirement is the result of shortfalls, accumulated arrears, and outstanding claims that must be settled. Clearly, an amount of this size cannot be financed fully on the local capital market, especially since investors are showing less appetite for domestic government securities. Therefore, a credible program to address our fiscal ills together with external support is urgently needed to improve the fiscal outlook.

If we are to deal in an effective way with the growing social demands, fiscal consolidation should be structured along the recommendations of the debt commission, implying a balanced budget within a period of five years and budget surpluses thereafter to reduce the outstanding debt. The deficits should be eliminated with a combination of own efforts and external support. The own efforts should include a freeze of primary expenditures complemented with expenditure reduction according to a predefined path with intermediate targets. Areas eligible for budgetary savings are, among other things, health care, transfers to government departments and agencies that have become more independent, subsidies, and general operational expenses. The savings in subsidies and transfers should be realized primarily through improved control mechanisms.

The austerity measures must be supported by strict adherence to all laws, rules, and policy decisions regarding the government budget in order to restore fiscal discipline. In addition, fiscal discipline should be strengthened through the legal anchoring of budgetary targets for, among other things, real primary expenditures, the budget balance, and the debt ratio. A special monitoring mechanism should be designed to monitor the adherence to the rules and targets and to advice on corrective actions.

It is important to note that fiscal consolidation is the responsibility of all governments, including the island governments of St. Maarten, Bonaire, St. Eustatius, and Saba. These island governments are plagued frequently by financial crises and approach the central government for support, resulting in protocols in which financial support is linked to the implementation of measures directed at a structural reduction of the budget deficits. However, once the initial financial support has been received, the agreed upon measures are implemented with large delays or not at all. Therefore, the execution of the protocols in a full and timely manner should be promoted by including them in the special monitoring mechanism to guarantee a lasting improvement of the public finances of the smaller islands.

Furthermore, progress in tax reform has been slow and should be speeded-up significantly. On the one hand, tax administration must be strengthened by streamlining and consolidating tax assessment and collection, and adequate staffing. On the other hand, the much-debated reform of the tax system should be finalized without further delay. This reform includes a major simplification, lower direct taxes with a broadening of the tax base, more emphasis on indirect taxes, and elimination of the cascading features of the turnover tax.

A final area of the public finances that warrants more attention is pension reform, including the public pension (AOV) as well as the civil servants' pension. The objective of the reform should be to guarantee an adequate pension at reasonable costs for employers and employees. Clearly, the recent initiative to increase the AOV-pension through a significant rise of the maximum income subject to premium levy does not meet this objective as it increases wage costs and reduces net income in the higher income brackets considerably. Therefore, in light of the challenges of an aging population, the fiscal disequilibria, and adequate funding of the pension systems, the Bank advocates a more broad-based reform. This reform should include increases in the retirement age, premiums, and the contribution period, while benefits based on the average wage instead of the final wage should be considered.

In the area of structural reform, unfortunately, the authorities have backtracked in several areas. The prior approval of individual dismissals by the Department of Labor has been reinstated, the privatization process has been frozen, legislation has been drafted that will tighten market protection, and discussions has started on the partial reversal of the liberalization of shop opening hours. Instead of reversing past reforms, the authorities should deepen them to improve the functioning of labor and product markets. Well-functioning markets promote a better match between demand and supply and more competitive prices, contributing positively to the strengthening of our investment climate. This is necessary to support a consistent and credible policy directed toward sustainable economic growth.

The structural reforms should be supported by a growth strategy to identify and implement projects that will boost economic activity and employment. For the development of this strategy we can rely on several recent studies of reputed institutions, including the World Bank and the OECD. The OECD included the Netherlands Antilles in its Caribbean Rim Investment Initiative, a program aimed at promoting economic growth through the creation of an attractive investment climate.

The fourth and final pillar of the structural adjustment program is poverty alleviation. The recent agreement with the Dutch government on assistance from the World Bank and the United Nations Development Program to design and implement a poverty reduction program fails to recognize the urgency of the growing social demands. The social realities of the Netherlands Antilles serve to indicate that no adjustment policies can be successful without addressing the growing social demands of the public. Therefore, any design and implementation of a policy directed toward poverty alleviation should be immediate and without delay. This can be achieved by using existing infrastructure such as the "Reda Soshal," "Wegenfonds Curacao," FKP, and "Monumentenzorg."

The Bank's monetary policy will be accommodative to the need for structural adjustment. The objectives of this policy include striving at a level of official reserves corresponding with three months of merchandise imports, minimizing monetary financing of the government deficits, and promoting commercial banks' credit extension towards private sector foreign exchange-generating activities. To enhance the effectiveness of the reserve requirement, the period for which the reserve requirement percentage is fixed has been reduced from three to two months as of January 16, 2004. Moreover, in light of the persistent decline in official reserves in the beginning of 2004, the Bank increased the reserve requirement percentage from 10.0% to 10.25% on March 16, 2004.

The medium-term and long-term economic prospects for the Netherlands Antilles will depend crucially on how well we deal with the financial-economic and social problems facing us. Bold leadership is required to balance the government budget, stabilize and subsequently reduce the debt-to-GDP ratio, restore confidence, promote investments in key growth sectors, and alleviate poverty. The realization of these objectives should be addressed simultaneously in a comprehensive and well-balanced adjustment program with clear intermediate targets to measure its progress. The consistent, full and timely implementation of this program will facilitate external support and, hence, lay a foundation for sustainable economic growth. It is only through growth that real progress can be made in creating durable jobs, reducing poverty, and improving our welfare.

E.D. Tromp
President

2. INTERNATIONAL ECONOMIC DEVELOPMENTS

Real GDP in the United States rose by 3.1% in 2003, strengthened by business investment, residential fixed investment, and consumer spending. Higher capital investment was related to improved business confidence, boosted by a combination of strong household spending and rising corporate profits. Meanwhile, the rise in demand for housing was fueled by favorable mortgage rates. In addition, low interest rates accompanied by higher wages led to an increase in consumer spending. Productivity growth of 4.2% raised both business profits and workers' compensation. Strong competition forced businesses to reduce costs by letting their existing employees work harder instead of hiring new full-time workers. As a result, job creation remained subdued, as the jobless rate lingered at 5.7% in 2003. Inflation was up by 0.7 percentage point to 2.3%, fueled by higher utility costs and health care expenses. Against the backdrop of a sluggish job market amid subdued inflationary expectations, the Federal Reserve reduced the Fed funds rate by 0.25 percentage point to a 45-year low of 1 percent in June 2003.

Table 1 Selected indicators of various countries (% change)

	United States			Netherlands			Venezuela		
	2001	**2002**	**2003**	**2001**	**2002**	**2003**	**2001**	**2002**	**2003**
Real GDP	0.5	2.2	3.1	1.2	0.2	-0.8	2.8	-8.9	-9.2
Consumer prices (%)	2.8	1.6	2.3	4.5	3.4	2.1	12.5	22.4	31.1
Unemployment rate (%)	4.9	6.0	5.7	3.4	4.1	5.3	16.4	15.7	17.0*

Source: US Bureau of Economic Analysis, US Bureau of Labor Statistics, Dutch Central Bureau of Statistics, Dutch Central Planning Bureau, *Latin America Monitor (forecast), and Banco Central de Venezuela

In 2003, the Dutch economy shrank by 0.8%, contrasting with a growth of 0.2% in 2002. The factors behind the economic decline were consumer spending and private nonresidential investment. Consumers cut back on spending (1.1%), as their real disposable income fell because of higher pension contributions and health insurance premiums. Conversely, government consumption dampened somewhat the economic contraction in 2003. Public health care spending was up but partly outweighed by a fall in public investment. Production activities decreased in the manufacturing, construction, and mining sectors. The economic slowdown was accompanied by a higher jobless rate (5.3%) and lower inflation (2.1%). The 2003 inflation rate was the lowest since 1998.

Political developments in Venezuela accounted for the further GDP decline in 2003. Real GDP worsened by 9.2% as both the oil and non-oil sectors shrank by 10.7% and 8.0%, respectively. Activities in the non-oil sector fared badly, particularly in the construction sector, shrinking by 37.4% in 2003. Foreign currency restriction impeded the import of raw materials, thereby lowering production of local businesses. These developments had a detrimental impact on the labor market, as the unemployment rate reached 17.0% in 2003. Despite strict currency and price controls, inflation topped 31.1%.

3. GENERAL ECONOMIC DEVELOPMENTS IN THE NETHERLANDS ANTILLES

3.1 Introduction

In line with the growth of the world economy, the economy of the Netherlands Antilles continued its recovery; real GDP is estimated to have risen by 1.4% in 2003. This improvement occurred despite adversities, such as the economic situation in Venezuela and the introduction of visas for Colombian visitors. The economic growth was based mostly on strong net foreign demand. These developments were accompanied by a higher inflation rate of 1.9% fueled mainly by higher utility costs due to the increase in world oil prices.

Table 2 GDP growth by expenditures[1] (real percentage changes)

	2001	2002	2003
Domestic expenditures, of which:	4.0	-1.2	-0.2
Private sector	5.1	-0.5	-0.5
- Investment	4.8	-1.1	-0.9
- Consumption	0.3	0.6	0.4
Government	-1.1	-0.7	0.3
- Investment	-0.1	-1.0	-0.1
- Consumption	-1.0	0.4	0.5
Changes in inventory	0.1	-0.3	-0.1
Foreign net expenditures, of which:	-4.0	1.9	1.7
Export of goods and services	-1.2	-2.9	1.6
Import of goods and services	2.7	-4.8	-0.2
GDP by expenditures	0.2	0.4	1.4
Net primary income	-0.1	-0.8	-0.3
Gross national income	0.0	-0.5	1.1
Net current transfers from abroad	-0.9	3.4	0.1
Gross national disposable income	-0.8	2.9	1.2

BNA estimate

Foreign demand expanded for both goods and services, particularly in bunker sales of fuel and tourism. Higher oil prices and increased demand contributed to the buoyant performance in bunker sales. In addition, tourism improved, stemming from a stronger focus on marketing, the recovery of the US economy, cheaper airfares, more airlift, and the weaker US dollar vis-à-vis the euro. Although domestic demand showed no real growth, it was still a recovery from the decline in 2002. This recovery was largely the result of a resurgence of government spending, a result of an increase in outlays on both wages & salaries and goods & services. Despite more economic activities, consumer spending posted only a slight growth because of a deceleration in real disposable income growth accompanied by higher savings. This slower growth in real disposable income can be explained largely by a deceleration in private transfers received from abroad. The weak labor market developments also may have had a dampening effect on consumer demand. In contrast, the uncer-

[1] Domestic and foreign expenditure are contributors to growth.

tain economic and political climate continued to deter enterprises from investing; private investment remained subdued in 2003.

3.2 Domestic production

The favorable economic developments in 2003 were due to a rise in private sector production activities (1.2%)[2] and expansionary public sector spending (0.3%).[2] The major contributing sectors to the private production growth were wholesale & retail trade, restaurants & hotels, financial, and business services.

Encouraging developments continued in the tourism industry, enhancing the total value added in the wholesale & retail trade sector (2.5%) and in the restaurants & hotels sector (3.8%) (table 3). In 2003, stay-over tourism in the Netherlands Antilles went up by 9.6%, in contrast to a drop of 1.0% in 2002. The 2003 growth was led by more stay-over tourist arrivals from the North American and European markets. The number of European visitors expanded due to lower airfares, more airlift, and the depreciation of the US dollar against the euro. In contrast, cruise passenger arrivals decelerated from 17.7% in 2002 to 5.5% in 2003. This deceleration was caused solely by the island of Curacao. Changes in the cruise ships' home base and Curacao's geographic location were two factors that caused a fall in the number of cruise tourists. Many ships started to dock closer to the United States, which caused many itineraries to shift to the Northern Caribbean.

An analysis by islands shows that stay-over tourism rose on all islands in 2003. In Curacao, the buoyant North American and European markets offset the fall in the South American and the Caribbean markets, resulting in a moderate 1.6% expansion. The economic situation in Venezuela affected visitor arrivals from that country. Furthermore, the introduction of a visa for Colombians and stricter visa procedures for Dominicans had a negative impact on the number of travelers. Bonaire's stay-over tourism sector continued to strengthen-- tourist arrivals grew by 23.0% in 2003. This growth was due primarily to the marked increase in the number of Dutch visitors (61.5%), linked to the rerouting of the intermediate stops on KLM's flights between Amsterdam and Latin America from Curacao and Aruba to Bonaire beginning summer 2002. Stay-over tourism in St. Maarten rose by 12.3% in 2003, encouraged mainly by the North American market. See table 8 in the appendix for a detailed overview.

[2] Weighted sectoral contribution to GDP growth

Table 3 GDP by sector (real percentage changes)

Sector	2001	2002	2003
Agriculture, fishery & mining	-0.4	-5.3	5.9
Manufacturing	-0.1	2.0	0.0
Electricity, gas & water	-0.4	2.4	1.5
Construction	13.3	-10.2	-5.2
Wholesale & retail trade	3.2	0.5	2.5
Restaurants & hotels	2.5	3.0	3.8
Transport, storage & communication	-2.1	-1.1	1.6
Financial intermediation	3.0	3.8	1.9
Real estate, renting & business activities	-2.2	-0.5	1.2
Private households	-1.9	-0.1	-0.2
Total private sector	1.4	0.2	1.4
Public sector	-7.3	1.3	1.7
GDP	0.2	0.4	1.4

BNA estimate

Through 2003, the total added value in the transportation sector recorded a growth of 1.6% as the positive developments at the airports and in air transportation outweighed the decline in the harbor sector. In line with the positive results in the tourism sector, the number of passengers and amount of cargo transported by "Dutch Caribbean Airlines" rose in 2003. In addition, total passenger traffic at the airports and commercial landings posted an increase.

Oil transshipment as well as storage in the Netherlands Antilles improved, due largely to the island of Bonaire. This improvement was related to the temporary shutdown of the refinery in December 2002 due to a general strike in Venezuela. As a result, the refined oil could not be exported. In contrast, the harbor sector performed poorly as the number of ships piloted into the harbor contracted by 14.2%, the result of fewer ships in all categories. In spite of fewer cargo ships, total cargo movements expanded marginally by 0.6% because of more transshipment activities.

In 2003, the total value added in the manufacturing sector showed no growth in spite of positive developments in the oil sector, related solely to the bunkering of fuel. This increase was the result of more bunker sales accompanied by higher oil prices. Conversely, fewer activities were reported in Curacao's ship repair and oil refinery as the number of man-hours sold and oil refining shrank. The latter decrease can be attributed to the aftermath of the temporary shutdown of the refinery.

The 2003 GDP growth was dampened by a contraction in the construction sector where added value shrank by 5.2%. The business environment remained uncertain, postponing major investment decisions. As a result, construction activity dropped for the second consecutive year because many of the major projects were completed or were in their final phase.

3.3. Labor market[3]

The economic recovery in the Netherlands Antilles has not yet resulted in a fall in the unemployment rate, which worsened from 14.6% in 2002 to 15.3% in 2003. Analysis by islands shows that both St. Maarten and Bonaire contributed to the higher jobless rate. St. Maarten's and Bonaire's unemployment rate rose by, respectively, 4.7 and 0.8 percentage points to 17.5% and 12.4% in 2003. Meanwhile, Curacao's unemployment rate dropped slightly from 15.6% in 2002 to 15.1% in 2003. In 2003, the labor force in the Netherlands Antilles expanded by 6,264 persons, as both the number of unemployed and employed increased. Overall, labor productivity may have dropped, because more labor hours were devoted to the production of goods and services.

In 2003, the total population in the Netherlands Antilles rose, owing largely to the situation in Curacao. Migration from the island continued, but at a much slower pace, causing it to be surpassed by the number of migrants to the island. Moreover, illegal migrants attaining legal status during 2002 had an impact on the population growth.

Noteworthy is that the government reintroduced a permit for individual dismissal in 2003, which had been abolished on the island of Curacao three years before. This decision was taken in response to pressure from local workers and labor unions.

Table 4 Labor force, participation rate, and unemployment rate in the Netherlands Antilles

	2001	2002	2003
Employed	69,267	70,366	75,076
Unemployed	11,791	12,023	13,577
Labor force	81,058	82,389	88,653
Total population	172,926	171,835	179,422
Participation rate	46.9%	47.9%	49.4%
Unemployment rate	14.5%	14.6%	15.3%

BNA estimates

3.4 Inflation

The annual inflation rate of the Netherlands Antilles accelerated from 0.4% in 2002 to 1.9% in 2003. The higher inflation was influenced mostly by the following factors: (1) higher world oil prices; (2) the depreciation of the US dollar and, hence, the Netherlands Antillean guilder; (3) higher inflation of our main trading partner, the United States; and (4) the developments in Venezuela.

A breakdown of the inflation rate by major subcategories shows that the higher 2003 inflation was attributable primarily to the categories "housing" and "food". Housing expenses were up by 5.4% because of higher utility costs. Food prices rose by 2.1%, fueled by the stronger euro and an inflation of 31.1%[4] in Venezuela. Analysis by islands reveals that Curacao had the highest annual inflation (2.0%), followed by St. Maarten (1.5%), and Bonaire (0.8%). See table 9 in the appendix for a detailed overview.

[3] AKO ("Labor force survey") 2003, Central Bureau of Statistics
[4] Banco Central de Venezuela

Graph 1 Developments in consumer prices (annual percentage change)

3.5 Public finances

3.5.1 Cash overview and financing

The budget deficit of the general government deteriorated by NAf.25.9 million in 2003 compared to the outcome in 2002. This deterioration was the result of an 8.8% increase in expenditures offsetting an 8.3% increase in revenues. The resulting cash deficit of the general government reached NAf.242.8 million at the end of 2003 corresponding with 5.0% of GDP (see table 5).

The expansionary budgetary policy was reflected in both higher current (NAf.96.3 million) and capital (NAf.33.0 million) expenditures. All expenditure categories contributed to the increased spending except net lending. The higher government consumption accounted for part of the economic growth in 2003. The increase in revenues was fueled entirely by higher nontax revenues of NAf.109.1 million. The remittances of dividend tax by the Dutch tax authorities[5] and dividends by government-owned enterprises explain mainly the increase in nontax revenues. See table 10 in the appendix for a detailed overview.

Noteworthy is that the primary balance, i.e., the balance excluding interest payments, still showed a surplus in 2003, reflecting the high interest burden of the government. Interest payments amounted to NAf.251.9 million in 2003, corresponding with 22% of tax revenues and 16% of total expenditures.

Table 5 Selected key variables of the general government 2001 – 2003 (cash basis, % of GDP)

	2001		2002		2003	
	NAf.	% GDP	NAf.	% GDP	NAf.	% GDP
Revenues	1,266.1	27.1	1,243.4	26.4	1,346.7	27.6
Tax revenues	1,144.6	24.5	1,145.9	24.3	1,140.2	23.4
Nontax revenues	121.5	2.6	97.5	2.1	206.5	4.2
Expenditures	1,262.3	27.0	1,460.3	30.9	1,589.5	32.6
Current expenditures	1,212.6	25.9	1,409.1	29.9	1,505.4	30.9
Capital expenditures	49.7	1.1	51.2	1.1	84.1	1.7
Balance	3.8	0.1	-216.9	-4.6	-242.8	-5.0
Primary balance	192.3	4.1	28.5	0.6	9.1	0.2
Collective burden[1)]	1,274.2	27.2	1,277.9	27.1	1,296.7	26.6

[1)] Tax burden plus social premiums (AOV/AWW/AVBZ) collected by SVB and BZV.

[5] In the new tax arrangement for the Kingdom of the Netherlands (BRK), the tax proceeds on dividend transfers from the Netherlands to the Netherlands Antilles will be remitted entirely to the government of the Netherlands Antilles.

A review by level of government shows that the deterioration in the outcome of the central government operations contributed to the overall deterioration of the budget deficit because the outcome of the island government of Curaçao improved. The central government's deficit widened by NAf.35.7 million to NAf.162.8 million because the increase in expenditures (NAf.90.8 million) outweighed the increase in revenues (NAf.55.1 million).

Central government expenditures expanded by 12.2% due almost entirely to higher current expenditures. All expenditure categories contributed to the rise in current expenditures except subsidies to public companies –the result of fewer subsidies to government-owned airlines– and personnel costs. Transfers to other levels of government accounted for 83% of the expansion in current expenditures due to the transfer of 75% of the dividend tax received from the Dutch government to the island government of Curaçao, and contributions in the deficits of funds of the social security bank, SVB, and the fund that covers medical expenses of retired government employees, FZOG. The higher interest payments were caused by the further accumulation of debt.

Capital expenditures grew by 45.4%, resulting from the increase in capital transfers related to the settlement of guarantees extended to the former government-owned airline, Air ALM. This increase was mitigated by a decline in net lending because, contrary to 2002, no loans were extended to the island governments for liquidity support.

A breakdown of revenues by categories shows that the overall increase was caused almost entirely by an increase in grants (NAf.53.6 million) related to the transfer of dividend tax by the Dutch government. Central government tax revenues increased only marginally by 0.4% because the higher proceeds from sales tax and excises –due mainly to the growth in domestic consumption– were offset almost entirely by fewer import duties and license fees. The decline in import duties may be explained by the phasing-out of economic levies on imported goods, while the drop in license fees was related to a transitory settlement with the Bureau of Telecommunications and Post in 2002.

Compared to 2002, the cash deficit of the island government of Curaçao improved by NAf.9.8 million to NAf.80.0 million in 2003. This improvement was the result of an increase in revenues (NAf.84.5 million) that outweighed expenditure growth (NAf.74.7 million). Tax revenues increased by NAf.26.2 million due primarily to the profit tax in connection with the partial transfer by the central government of the dividend tax received from the Netherlands. Noteworthy also is the higher collection of the motor vehicle tax, related to the improved administration of this tax. Furthermore, nontax revenues rose by NAf.58.4 million because of dividend remittances by government-owned companies and the settlement of claims and debts with the public housing foundation, FKP.

The government of Curacao's expansionary fiscal policy was reflected primarily in higher current expenditures (NAf.59.7 million). Increased outlays on goods and services, personnel costs, and subsidies contributed mainly to the higher current spending. The increase in personnel costs can be attributed to improved compliance with the pension contributions to the civil service pension fund. The increase in subsidies, together with the increase in capital expenditures, also was related to the settlement with FKP.

Table 6 Financing of the cash balances (in millions NAf.)

	Central government		Curaçao government	
	2002	**2003**	**2002**	**2003**
Monetary financing	121.0	71.0	20.0	31.2
Central bank	-41.8	10.1	-23.0	-28.4
Commercial banks	162.4	59.3	43.0	59.6
Coins and notes	0.4	1.6	-	-
Nonmonetary financing	6.1	91.8	69.8	48.8
Government securities with the public	-16.0	116.6	89.6	30.2
Other	22.1	-24.8	-19.8	18.6
Cash balance	-127.1	-162.8	-89.8	-80.0

About 42% of the general government's cash deficit was financed monetarily in 2003, contributing largely to the domestic monetary expansion (see table 6). Analysis by level of government shows that the central government's cash deficit was financed 44% monetarily in 2003. The monetary financing occurred mainly through the commercial banks as a result of the purchase of government securities. The funds raised nonmonetarily through the purchase of government securities by the public were used partly to reduce other nonmonetary debt, including arrears with the social security bank, SVB.

The island government of Curaçao financed its cash deficit mainly nonmonetarily (61%) in 2003. The purchase of government securities by the public contributed primarily to the nonmonetary financing. The monetary financing occurred entirely through the commercial banks due to an increase in island government securities in portfolio and the withdrawal of deposits. The monetary contraction through the central bank resulted from a decline in island government securities in portfolio.

3.5.2 Public sector debt

The total consolidated public debt of the Netherlands Antilles expanded considerably by NAf.519.4 million (13.5%) in 2003 to NAf.4.361 billion or 89.6% of GDP. Contributing to this expansion were increases in both the domestic component and the foreign component of NAf.431.1 million (13.8%) and NAf.88.3 million (12.3%), respectively. The increase in the domestic component resulted from the financing of the cash deficit and the formalization of accumulated funds deficits of the social security bank, SVB. See table 11 in the appendix for further details.

An analysis by level of government reveals that the accumulation of domestic debt was caused almost entirely by the central government debt (NAf.423.0 million). The debt of the other islands increased by NAf.32.6 due to the accumulation of arrears with the civil servants pension fund, APNA, and the central government. In contrast, the domestic debt of the island government of Curaçao dropped by NAf.42.7 million. The increase in the domestic debt of the central government was caused by a NAf.622.7 million increase in long-term debt securities, NAf.338 million of which was related to the formalization of funds deficits and arrears at the SVB. Because of the latter, outstanding arrears at the SVB declined. In addition, long-term debt securities increased to finance the net redemption of short-term debt securities. Noteworthy is the conversion of the debt on the advance account at the central bank in a bond in February 2003 (NAf.29.2 million). The advance account was replaced by a overdraft facility, which was nil at the end of 2003.

The drop in the domestic debt of the island government of Curaçao was reflected in all debt categories except long-term debt securities, which rose by NAf.58.7 million. Like the central government, the island government financed the net redemption of short-term debt securities with long-term debt securities. The largest decline occurred in the debt to the central government (NAf.36.6 million).

The increase in the foreign debt in 2003 was attributable mainly to the 20% appreciation of the euro against the Netherlands Antillean guilder. This appreciation caused a rise in the guilder-equivalent of the euro-denominated debt of approximately NAf.111 million. In addition, the shift in interest payments due to the Netherlands at the end of 2003 to 2004 contributed to the increase in the foreign debt. The largest decrease occurred in the short-term debt to the Dutch government (NAf.31.9 million) because the accumulated arrears in the Antillean contribution to the coast guard were waived.

3.6 Balance of payments developments

3.6.1 Introduction

In 2003, net export of goods and services, i.e., net foreign demand, increased compared to 2002. This rise was related mainly to higher earnings from bunker sales, tourism, and oil refining, contributing partly to the growth of the economy in 2003. The increase in the net export of goods and services combined with the continued growth in net current transfers from abroad led to a turnaround in the current account deficit. In line with the developments on the current account, the capital and financial account balance improved. Foreign exchange reserves increased although at a lower rate than in 2002.

Table 7 Balance of payments summary (in millions NAf.)

	2001	2002	2003
Current account	-377.4	-105.0	11.4
Capital account	66.6	49.6	46.8
Financial account, of which:	239.5	-35.4	-141.3
Change in reserves 1)	-415.1	-122.0	-88.0
Statistical discrepancies	71.3	90.9	83.1
Memorandum items			
Change in reserves 1)	-415.1	-122.0	-88.0
with commercial banks	-342.8	53.2	-135.8
with central bank	-72.3	-175.2	47.8

Due to rounding figures may not add up
1) A minus sign implies an increase.

3.6.2 Current account

Export of goods and services increased by NAf.321.8 million in 2003 compared to 2002, mainly as a result of increased earnings from bunkering activities. The positive development in bunker sales can be explained by both higher oil prices and increased foreign demand. Concomitantly, foreign exchange earnings from the tourist industry expanded as both stay-over and cruise tourism increased. Furthermore, refinery income increased despite the economic and political instability in Venezuela.

A breakdown by island reveals that the increased earnings from bunker activities were attributed mainly to the Windward Islands, while Curaçao showed a moderate growth. On Curaçao, however, freezone exports were a major contributor to the growth in export goods. Foreign exchange earnings from the tourist industry increased on all islands, but were highest on the Windward Islands where tourism earnings increased by 10% compared to 2002.

Following increased export activity, the import of goods and services rose by NAf.216.8 million. The growth in imports can be ascribed largely to higher oil imports and increased tourist expenditures by residents abroad. The rise in oil imports was due to both higher prices and increased demand.

Contrary to the growth in bunker sales, the import of oil products decreased on Curaçao. This decrease was due mainly to a decline in domestic demand, related mostly to a drop in demand from the utility sector. In addition, imports of the free zone declined because inventories were reduced to provide for the higher exports. The overall increase in the import of goods and services was related mainly to increased imports of goods and oil products on the Windward Islands. The increased oil imports were due largely to higher oil prices and increased demand, while the rise in the import of goods can be explained partly by the growth in tourism.

In 2003, the deficit in the trade and services balance improved by NAf.105.1 million because the export growth in goods and services offset the import growth. In line with the developments in the trade and services balance, the current transfers balance recorded a higher surplus in 2003. This higher surplus can be explained by the transfer of dividend tax by the Netherlands related to the new Tax Arrangement for the Kingdom of the Netherlands (BRK) and the higher net inflow of transfers by individuals. Consequently, the current account balance recorded a surplus of NAf.11.4 million in 2003. See table 12 in the appendix for further details.

3.6.3 Capital and financial account

In line with developments in the current account, the capital and financial account balance improved in 2003. The financial account improved as a result of an increase of NAf.151.5 million in total foreign assets, mitigated by an increase of NAf.45.5 million in total foreign liabilities. Despite the improvement in the financial account, the growth of our foreign exchange reserves decelerated, reaching 2.7 months of import coverage at the end of 2003.

The increase in foreign assets occurred mainly in the categories 'other investment' and 'net lending and borrowing'. Foreign assets on the 'other investment' account improved by NAf.92.5 million, related mostly to the increase in the balances on bank accounts held by resident companies abroad. These foreign account balances increased in part due to the maturing of funds invested abroad. The assets on the 'net lending and borrowing' account were up by NAf.163.8 million, caused primarily by higher trade credit extended. These increases in foreign assets were mitigated by the decline in assets on the 'portfolio investment' account, stemming, among other things, from the maturing of invested funds that were partly repatriated. Due to the uncertain international economic and political developments in 2003 and the low rates of return, most companies did not reinvest the maturing funds in foreign equity or debt securities.

The expansion in foreign liabilities in 2003 originated largely from an increase in liabilities in the category 'net lending and borrowing' (NAf.262.7 million), which includes trade credit and foreign loans received. This increase was due mostly to trade credit received as companies used additional credit to finance their higher imports. In addition, more loans were received to finance, among other things, the construction activities at the Curaçao airport. The growth in foreign liabilities in the 'net lending and borrowing' account was offset partly by a decrease in foreign liabilities related to direct investments in the Netherlands Antilles (NAf.158.3 million) as various companies made more payments to their parent companies abroad to settle their outstanding debt. See table 13 in the appendix for further details.

3.7 Monetary developments

3.7.1 Monetary policy and money supply

Adaptations in the Bank's monetary policy during 2003 were concentrated in the first half of the year. Two particular developments are worth mentioning: (1) the increase in international reserves and (2) the growth in credit extended to the governments by the commercial banks. The increase in reserves was attributable to, among other things, the repatriation of funds by local investors due to decreasing international interest rates, especially US interest rates, during the January-June period of 2003. This repatriation resulted in further liquidity growth in the domestic banking sector, which exercised a downward pressure on domestic interest rates. In line with the decline in both international and domestic interest rates, the Bank lowered its pledging rate – the interest percentage against which commercial banks can borrow from the Bank under the condition of sufficient collateral – three times during the first half of 2003, reaching 2.25% as of June 30.

Credit extension by the commercial banks to the government sector continued to exceed the targeted growth stipulated by the Bank during the first six months of 2003. To reverse this trend, the Bank raised the reserve requirement percentage on January 16 and April 16 by 0.5 percentage points, respectively, reaching 10.0%.

During the second half of 2003, monetary developments did not warrant any particular adaptations in the Bank's monetary policy. International reserves dropped, both at the central bank and at the commercial banks, while the growth in credit extended by the commercial banks to the government sector halted.

During 2003, the money supply (M2) in the Netherlands Antilles rose by 8.4% (NAf.316.2 million). Together with a real growth in domestic production of 1.3% and the inflation rate of 1.9%, this rise implied a drop of 5.2% in the velocity of money. The latter was reflected particularly by the rise in both time deposits and savings in combination with the decrease in coins and notes with the public. Table 14 in the appendix presents further details.

3.7.2 Factors affecting the money supply

The increase in the money supply during 2003 was the result of an expansion in both of its components: net domestic assets and net foreign assets grew by NAf.217.1 million and NAf.99.1 million, respectively. The rise in net domestic assets resulted from increases in net credit extended to both the government sector, concentrated mainly in the January-June period of the year, and the private sector of NAf.116.8 million and NAf.51.9 million, respectively. Although total private credit extension rose, it did not occur in the productive loan categories. This is revealed by, among others things, the drop in business loans on both island groups and in mortgages on the Leeward Islands, respectively. The drop in business loans reflects reigning uncertainties regarding future economic perspectives.

Net foreign assets expanded due to an increase of NAf.135.8 million in the net foreign position of the commercial banks, which offset the drop of NAf.36.7 million in net foreign assets at the Bank. These opposite developments are explained partly by commercial banks' purchase of foreign exchange from the Bank. This shift took place particularly during the second half of 2003 as commercial banks wanted to increase their foreign portfolios in light of the rising stock markets and less appetite for local government securities. Contrary to the first half of 2003, the commercial banks were reluctant to increase their investments in government securities during the second half of 2003. This reluctance was partly a reaction to the perceived lack of diligence by the governments in tackling the high budget deficit and domestic debt positions. In addition, the increase in foreign investment was influenced further by the lack of domestic the private investment opportunities, dampening the private sector's demand for credit.

3.7.3 Domestic credit extension by commercial banks

During 2003, domestic credit extended by the commercial banks increased by NAf.134.1 million. Credit extended to both the government sector and the private sector rose by NAf.79.3 million and NAf.54.6 million, respectively. The rise in credit extended to the governments was the result of an increase in securities of both the central government and the island government of Curaçao and took place mainly during the first six months of the year.

Loans extended to the private sector grew moderately by 2.0%, attributable entirely to the increase of NAf.61.5 million on the Windward Islands. This increase offset the drop of NAf.6.9 million in loans extended on the Leeward Islands. The increase on the Windward Islands was not reflected in all three loan components: while consumer loans and mortgages rose, by NAf.36.5 million and NAf.29.5 million, respectively, business loans dropped by NAf.4.4 million. The drop on the Leeward Islands was due to decreases in business loans and mortgages of NAf.30.1 million and NAf.12.6 million, respectively, exceeding the rise of NAf.35.7 million in consumer loans.

The increase in consumer loans on both island groups is in line with the increase in consumer spending, while the drop in business loans corresponds with the decline in private investment. This development reflects mainly the reigning uncertainties experienced by the business sector regarding future economic perspectives. Finally, contrary to the drop on the Leeward Islands, the rise in mortgages on the Windward Islands did not coincide with the contracting activity recorded in the construction sector. The explanation for this contradiction may be increases in existing mortgages for purposes other than construction activity.

3.7.4 Developments in domestic interest rates

In line with the downward trend in both international and domestic interest rates, the central bank's pledging rate and, consequently, the marginal lending rate[6] were lowered three times during 2003. All

[6] The marginal lending rate is equal to the pledging rate plus 100 basis points applicable on commercial banks' borrowing exceeding NAf.20 million.

three reductions in the pledging rate took place during the first six months of the year: on January 13th from 3.5% to 3.0%, on May 19th to 2.5%, and on June 30th to 2.25%. Monetary developments during the second half of 2003 did not warrant any further changes in these rates.

The average interest rate offered by commercial banks on both savings and time deposits continued to decline in 2003 to 3.4% and 4.9%, respectively. This trend is related to the excess liquidity in the domestic banking sector, reducing the need for commercial banks to compete for funding through higher interest rates.

The downward trend in the average rate on mortgages halted at 9.5% following four years of decline. The average rate on current account overdrafts increased to 10.7%.

The average yield on domestic government bonds continued its downward trend, reaching 6.9% at the end of 2003. The drop in this rate was related mainly to developments in both the international and the domestic financial markets. On the one hand, the return on international investments has been declining due to lower international interest rates, especially in the United States. On the other hand, domestic investment opportunities through private sector demand for credit were muted. Consequently, local investors shifted to higher yielding domestic government bonds and treasury bills to realize a better return on investment. The resulting increase in demand exercised a downward pressure on the average interest returns of these securities. This trend halted during the second half of 2003 because of a lack of effort by the government to address the unsustainable deficit and debt position. See table 15 in the appendix for further details.

APPENDIX

Table 8 Developments in stay-over tourism per island (% change)

	Curaçao		St. Maarten		Bonaire	
	2002	2003	2002	2003	2002	2003
North America, of which:	17.6	6.5	-1.2	16.9	-1.4	-1.8
-U.S.A.	20.5	2.3	-0.5	15.8	0.5	-3.0
Europe, of which:	-3.8	29.8	-10.6	1.3	11.2	65.3
-The Netherlands	-2.3	37.5	-9.8	40.6	8.0	61.5
South & Central America, of which:	0.4	-27.5	-46.1	-13.5	-21.5	2.2
-Venezuela	-7.6	-17.4	-33.0	-27.9	-37.9	-3.4
-Other S&C America	17.5	-40.7	-51.9	-7.9	---	---
Caribbean, of which:	28.8	-6.5	5.4	19.6	75.0	21.5
-Aruba	21.6	4.8	---	---	81.5	38.9
-Dominican Republic	22.4	-18.7	-26.0	31.2	---	---
-Other Caribbean	35.6	-7.8	11.0	18.2	---	---
Total	6.5	1.6	-5.4	12.3	3.6	23.0

Table 9 Netherlands Antilles consumer prices (annualized percentage change)

	2001	2002	2003
Food	3.1	3.6	2.1
Beverages & tobacco	1.7	-0.1	-0.5
Clothing & footwear	0.9	-1.6	0.2
Housing	2.6	1.9	5.4
Housekeeping & furnishings	0.8	-1.0	2.1
Health	5.7	1.5	0.7
Transport & communication	1.2	-2.9	-1.1
Recreation & education	-0.2	-0.4	0.1
Other	1.1	1.2	0.7
General inflation rate	1.7	0.4	1.9

Table 10 Budgetary overview (in millions NAf.)

	2001	2002	2003
General government			
Revenues	1,266.1	1,243.4	1,346.7
Tax revenues, of which:	1,144.6	1,145.9	1,140.2
Taxes on income and profits	578.8	568.1	555.8
Taxes on goods and services	398.0	411.8	427.8
Taxes on international trade and transactions	122.7	127.7	119.5
Nontax revenues	121.5	97.5	206.5
Expenditures	1,262.2	1,460.3	1,589.5
Current, of which:	1,212.5	1,409.1	1,505.4
Wages and salaries	403.0	528.2	535.2
Goods and services	275.2	304.2	368.5
Transfers and subsidies	345.9	331.3	349.7
Interest payments	188.5	245.4	251.9
Capital	49.7	51.2	84.1
Budget balance	3.9	-216.9	-242.8
Central government			
Revenues	608.8	616.5	671.6
Tax revenues, of which:	512.3	533.6	535.5
Taxes on goods and services	369.9	382.4	391.0
Taxes on international trade and transactions	122.7	127.7	119.5
Nontax revenues	96.5	82.9	136.1
Expenditures	647.4	743.6	834.4
Current, of which:	616.6	704.2	777.1
Wages and salaries	199.9	252.4	251.3
Goods and services	82.6	86.2	104.6
Transfers and subsidies	239.3	242.0	287.5
Interest payments	94.8	123.6	133.7
Capital	30.8	39.4	57.3
Budget balance	-38.6	-127.1	-162.8
Island government of Curaçao			
Revenues	775.9	748.5	833.0
Tax revenues, of which:	632.3	612.3	638.5
Taxes on income and profits	578.8	568.1	589.6
Taxes on goods and services	28.1	29.4	36.8
Nontax revenues	143.6	136.2	194.5
Expenditures	733.4	838.2	913.0
Current, of which:	714.5	826.5	886.2
Wages and salaries	203.1	275.8	283.9
Goods and services	192.6	218.0	263.9
Transfers and subsidies	225.2	210.9	220.1
Interest payments	93.7	121.8	118.2
Capital	18.9	11.8	26.8
Budget balance	42.5	-89.8	-80.0

Table 11 Total outstanding consolidated public debt (in millions NAf.)

	2001	2002	2003
Domestic consolidated debt[1]),	2,895.8	3,123.7	3,554.8
of which:			
-Central government, of which:	1,366.9	1,502.3	1,925.3
Long-term securities	956.2	963.4	1,586.1
Short-term securities	26.4	136.6	44.7
APNA	167.0	160.1	149.7
SVB	86.2	117.4	26.2
-Curaçao, of which:	1,852.0	1,993.7	1,951.0
Long-term securities	497.7	528.1	586.8
Short-term securities	32.2	111.7	86.2
APNA	806.4	814.5	807.8
Central government	334.6	398.6	362.3
-Other islands	220.7	274.6	307.2
Foreign debt	593.6	718.0	806.3
Total debt (consolidated)	3,489.3	3,841.7	4,361.1
(% of GDP)	74.5%	81.4%	89.6%

[1]) Consolidated for debts between the central government and the island governments.

Table 12 Detailed overview balance of payments (in millions NAf.)

	2001	2002	2003
Trade balance	-1,994.5	-1,838.0	-1,796.7
-Exports	1,142.4	1,030.3	1,212.8
-Imports	3,136.9	2,868.3	3,009.5
Services balance	1,580.1	1,537.0	1,600.8
Receipts, of which:	2,952.6	2,914.5	3,053.8
-Travel	1,344.0	1,380.1	1,513.5
-Transportation	317.0	303.4	247.7
-Other services, of which:	1,219.7	1,231.0	1,292.6
- Int. fin & bus. services sector	491.1	484.0	411.0
Expenses, of which:	1,372.5	1,377.4	1,453.0
-Travel	479.6	498.9	576.4
-Transportation	196.3	181.4	140.1
-Other services, of which:	696.6	697.1	736.4
- Int. fin & bus. services sector	154.2	157.2	157.6
Income balance[1)]	35.5	1.3	-12.4
Current transfers balance[2)]	1.4	194.7	219.6
Current account balance	**-377.4**	**-105.0**	**11.4**
Capital & financial account balance	**306.1**	**14.1**	**-94.5**
Capital balance	66.6	49.6	46.8
Financial balance	239.5	-35.4	-141.3
Net errors & omissions	**71.3**	**90.9**	**83.1**

Due to rounding, figures may not add up.

1) Labor and investment income.

2) Public and private transfers.

Table 13 Breakdown of net changes in the financial account (in millions NAf.)

	2001	2002	2003
Direct investment	-9.3	12.1	-142.6
- Abroad [1]	-0.8	-1.9	1.7
- In the Netherlands Antilles [2]	-8.5	14.0	-144.3
Portfolio investment [1]	-56.8	-67.1	7.3
Other investment, of which:	349.8	287.3	128.7
- Assets [1]	57.5	62.2	-30.3
- Liabilities [2]	292.3	225.1	159.0
Net lending/borrowing, of which:	370.9	-145.8	-46.9
- Assets [1]	78.2	-19.4	-183.2
- Liabilities [2]	292.7	-126.4	136.3
Reserves [3]	-415.1	-122.0	-88.0
Total assets [1]	-336.7	-149.8	-301.3
Total liabilities [2]	576.2	114.4	159.9
Balance	239.5	-35.4	-141.4

Due to rounding, figures may not add up.
[1] A minus sign implies an increase in assets.
[2] A minus sign means a decrease in liabilities.
[3] A minus sign means an increase in reserves.

Table 14 Monetary survey (in millions NAf.)

	2001	2002	2003
Money supply (M2)	3,380.9	3,776.7	4,092.9
Money (M1)	1,309.7	1,497.2	1,525.3
Coins & notes with the public	218.2	235.2	232.9
Total demand deposits, of which:	1,091.5	1,262.0	1,291.9
- Netherlands Antillean guilders	866.1	1,019.6	989.3
- Foreign currency	225.4	242.4	303.1
Near money	2,071.2	2,279.5	2,567.6
Time deposits	1,209.7	1,324.0	1,501.4
Savings	861.5	955.5	1,066.2
Factors affecting the money supply			
Net domestic assets	2,369.8	2,643.6	2,860.7
General government	156.1	351.6	468.4
- Central government	8.5	189.4	270.8
- Island governments	147.6	162.2	197.6
Private sector	2,691.5	2,782.5	2,834.4
Net foreign assets	1,011.1	1,133.1	1,232.2
Central bank	677.9	853.0	816.3
Commercial banks	333.2	280.1	415.9
Memorandum items			
Government loans by commercial banks	198.2	410.2	489.5
- Central government	67.5	227.4	282.3
- Island governments	130.7	182.8	207.2
Private sector loans - Leeward Islands	1,905.9	1,988.3	1,981.4
- Mortgages	740.3	790.7	778.1
- Consumer loans	479.4	505.8	541.5
- Business loans	686.2	691.9	661.8
Private sector loans - Windward Islands	674.6	693.5	755.0
- Mortgages	311.7	343.6	373.1
- Consumer loans	143.2	108.9	145.4
- Business loans	219.7	240.9	236.5

Table 15 Developments in domestic interest rates (% at year-end)

	2001	2002	2003
Central bank			
- Pledging rate	7.00	3.50	2.25
- Marginal lending rate	7.25	4.50	3.25
Commercial banks borrowing rates			
- Passbook savings	3.7	3.6	3.4
- 12-month time deposit	6.3	5.5	4.9
Commercial banks lending rates			
- Mortgages	10.0	9.4	9.5
- Current account overdraft	10.5	10.2	10.7
Government bonds			
5 year (effective yield)	9.0	7.3	6.9

4 DOMESTIC FINANCIAL MARKET DEVELOPMENTS

4.1 Introduction

The monetary and financial conditions that shaped developments in the domestic financial market in 2002 prevailed until mid-2003. The first half of 2003 sustained a continued demand for government paper as a result of a net capital inflow because investors were capitalizing on the relatively high interest rates in the local market as compared to the low interest rates offered in the international US dollar money market. However, the high demand for government paper contributed to an interest rate decline in the local market. The governments' net borrowing through the issuance of debt paper amounted eventually to NAf.557.3 million in 2003, compared to NAf.221.0 million in 2002. This increase was due mainly to a debt conversion[7] by the central government of NAf.341.6 million.

The second half of 2003 was marked by a noticeable change: while the demand for government paper remained high, the interest rate in the local market started to increase again. Investors began to demand a higher yield for their investments because of increasing uncertainties surrounding the government's commitment to addressing the unsustainable deficit and debt position.

In the money market, the interest rates on certificates of deposit (CDs) issued by the Bank declined from 2.5% to 1.25% in line with the lower US interest rates.

4.2 Financial instruments and the money market

In 2003, certificates of deposit (CDs) issued by the Bank were the only tradable nongovernmental instruments available. CDs continued to trade bi-monthly according to a set schedule. Commercial banks seemed to prefer uncollateralized inter-bank loans over the sale and repurchase of CDs. As indicated in table 16 the average monthly balance of outstanding CDs decreased by NAf.48.9 million (25.3%) in 2003. This decrease was due mainly to interest rate declines -- from 2.50% to 2.00% in January, to 1.50% in May, and to 1.25% in June 2003. Moreover, monetary conditions led to a reduction in the amounts auctioned. The CD rate decrease was related to the decline in the domestic market interest rates, which triggered a reduction of the Bank's pledging rate. The maximum CD-rate lies 100 basis points below the pledging rate, while the latter was reduced in three steps from 3.50% to 2.25%.

[7] Accumulated funds deficits and arrears at the social security bank, SVB, were converted into a bond.

Table 16 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.)

	2001	2002	2003	Change 2002-2003
Certificates of deposit	114.1	193.6	144.7	-25.3%
Non-interest-bearing reserve requirement	148.5	277.0	336.6	21.5%
Demand deposits	20.3	45.3	42.5	-6.2%
Total	282.9	515.9	523.8	1.5%

The average monthly balance of the non-interest-bearing reserve requirement increased by NAf.59.6 million (21.5%) because the Bank increased the reserve requirement percentage in two steps from 9% to 10% during 2003. In addition, the base on which the reserve requirement is calculated increased, in line with the money growth in 2003. The base equals the commercial banks' domestic debt excluding inter-bank and long-term deposits.

Government securities in the money market consisted of treasury bills with maturities of 1, 3, 6, and 12 months. During 2003, treasury bills were auctioned twice a month. In an effort to enhance market transparency, financial market information is provided to market participants on a monthly basis. The financial market information provides data such as the prices of securities, the local yield curve, debt of both governments, and the maturity schedule. The enhancement of market transparency eventually will promote more activity in the secondary market.

Activities in the secondary bond market increased considerably during the first half of 2003. As interest rates decreased and, consequently, bond prices increased, many investors used the opportunity to swap and/or invest in either longer or shorter-term securities or took their profit. However, during the second half of the year when interest rates started to move upward, the secondary market saw less trading.

Treasury bills were traded mainly in the primary market, perhaps because the primary market trades about every 2 weeks. Table 17 provides information on the size and the activity in the market for local treasury bills.

Table 17 Treasury bills issuance, outstanding balances, and average maturity as per December 31 (in millions NAf. and months)

	2001	2002	2003	Change 2002-2003
Issuance	**550.0**	**674.1**	**514.0**	**-22.4%**
Central government	258.5	361.2	213.4	-40.9%
Island government of Curacao	291.5	312.9	300.6	-3.9%
Outstanding amount	**58.6**	**248.3**	**130.8**	**-45.1%**
Central government	26.4	136.6	44.6	-67.4%
Island government of Curacao	32.2	111.7	86.2	-22.8%
Average maturity (months)	**1.2**	**3.9**	**2.3**	**-39.7%**
Central government	1.2	2.8	1.8	-35.7%
Island government of Curacao	1.3	5.0	2.8	-43.7%

4.3 The market for government bonds

During 2003, the demand for local government bonds continued to increase, especially during the first half of the year. As a consequence of the high demand, domestic interest rates declined. The less attractive interest rates abroad was the main reason for investors to invest their funds locally, increasing their holdings of government paper considerably. Another contributing factor was that as of March 1, 2002, commercial banks were no longer restricted by the Bank in financing the government. To promote the secondary market of government securities, the Bank sold a substantial part of its local portfolio in the secondary bond market which, unlike the secondary market in treasury bills, was fairly active during 2003.

Gross general government debt issuance totaled NAf.1,383.9 billion during 2003; NAf.514.0 million was related to treasury bills, NAf.528.3 million to bond issuance, and NAf.341.6 million to a debt conversion. The central government issued four new public loans during 2003: a 4-year bond yielding 6.875% in January, a 10-year bond yielding 8% and a 5-year bond yielding 6.5% in June, and a 10-year bond yielding 7.25% in November. In addition, a 5-year private placement at 6.0% was issued in August. The island government of Curaçao also had four public issues but no private placements during 2003. A 6-year bond yielding 7.25% was issued in April, a 10-year bond yielding 7.875% in May, a 7-year bond yielding 7.0% in July, and a 4-year bond yielding 5.50% in September.

Bond issuance increased while treasury bill issuance decreased at both levels of government. This development was mainly the result of the institutional investors' targeting of the higher yields on longer-term issues. The general government's net borrowing excluding debt conversion amounted to NAf.215.7 million in 2003. Including debt conversion, the net amount borrowed was the highest ever recorded at NAf.557.3 million, as can be seen in graph 2.

Graph 2 General government annual net borrowing incl. debt conversion (in millions NAf.)

Table 18 shows that the net borrowing by the central government, excluding debt conversions, was concentrated in public issues, which increased by 59.3%. Private placements increased as well, but to a lesser extent (11.1%). On the other hand, the issuance of treasury bills declined due to less demand for these instruments on the financial market because investors preferred higher interest rates on their investments. During the first half of 2003, the demand for government securities was high, resulting in oversubscription of bond tenders, which enabled the government to reduce its borrowing costs. That situation changed during the second half of the year when interest rates started to climb back to their previous levels. Finally, debt conversions more than doubled in 2003 (101.1%).

Table 18 Outstanding negotiable loans of the central government (in millions NAf.)

	2001	2002	2003	Change 2002-2003
Total, of which:	982.6	1,100.0	1,630.7	48.3%
Private placement	210.5	180.7	200.8	11.1%
Public issues	411.7	451.9	719.9	59.3%
Treasury bills	26.4	136.6	44.6	-67.4%
Debt conversions	334.0	330.8	665.2	101.1%
Net borrowing	18.1	117.4	530.8	352.1%

The island government of Curaçao registered a 74.4% decline in its net borrowing in 2003, compared to 2002. As can be seen in table 19, the net borrowing in 2003 resulted from the increase in public issues (25.9%). Outstanding treasury bills declined because investors preferred to invest in bonds that carry a higher yield. Furthermore, the island government of Curaçao experienced a drop in private placements, which were rolled-over by the public issues. The outstanding amount of debt conversions and the 6.5% 30-year annuity dropped according to their predetermined redemption schedules.

Table 19 Outstanding negotiable loans of the island government of Curaçao (in millions NAf.)

	2001	2002	2003	Change 2002-2003
Total, of which:	959.9	1,063.5	1,089.9	2.5%
Private placement	177.3	133.8	106.6	-20.3%
Public issues	259.8	333.7	420.2	25.9%
Treasury bills	32.2	111.7	86.1	-22.9%
Debt conversions	60.7	60.6	60.0	-1.0%
6.5%-annuity	429.9	423.7	417.0	-1.6%
Net borrowing	3.6	103.6	26.5	-74.4%

The maturity schedule in table 20 indicates that 21.4% of the outstanding loans will mature within the next 2 years, while 54.5% is within the maturity bracket of 3 to 10 years. The high maturity rate of the island government of Curacao in the bracket "over 10 years" is due to the 6.5% 30-year annuity loan maturing in December 2028.

Table 20 Maturity schedule of negotiable government securities excluding treasury bills as of December 31, 2003 (in percentages of total)

	0-2 years	3-10 years	over 10 years	Average yield
Central government	19.2	74.1	6.7	8.1%
Island government of Curaçao	23.6	34.8	41.5	7.5%
General government	21.4	54.5	24.1	7.8%

4.4 US government yield curve developments

Interest rates on US Treasuries dropped as the Federal Reserve continued easing its monetary policy to stimulate the economy in 2003. During the first quarter of the year, bond yields followed largely the progress in the Iraq conflict. After April, the dominant theme was the general condition of the US economy.

In November 2003, the 2-year note fell from 2.10% to 1.77%, while the 10-year note fell 27 basis points to 4.13%. In the final days of the year, the yields drifted somewhat higher as a result of profit taking, shifting the 2-year note back to 1.84% and the 10-year note to 4.26%.

4.5 Domestic yield curve developments

When issuing new bonds, a trade off has to be made between the security offered for investors with longer maturities and the interest savings for the government, resulting from the steep yield curve, offered by shorter maturities. Even though the domestic interest rates increased at the second half of the year, the yield curve reflects the overall drop in the previous years, especially at the longer end of the curve. The short-term interest rates increased more than the long-term interest rates[8] because the island government of Curaçao experienced acute liquidity difficulties towards the end of the year. This situation was reflected in a significant increase in the short-term yield curve making it steeper at the short end, while maintaining a flatter line on the long end of the curve.

Graph 3 Local yield curve development

[8] During the first half of the year, the yield on a 1-month treasury bill stood at 1.93%, on a 3-month bill at 2.49%, and on the 1-year treasury bill at 4.50%. At the end of the year, the situation changed in that the 1-month treasury bill was trading at 3.00%, the 3-month at 4.00%, and the 1-year at 5.35%.

5 THE FINANCIAL SECTOR

5.1 General developments in the financial sector

During 2003, the Bank conducted on-site full-scope examinations at 13 institutions: 7 internationally operating commercial banks, 3 domestically operating commercial banks, and 2 credit unions. In addition, the Bank conducted an on-site follow-up examination at one domestically operating commercial bank.

Furthermore, the Bank revoked the license of the specialized credit institution Servisio di Pago di Korsow N.V., the credit union Kooperativa di Spar i Krédito San Dominico, and the internationally operating commercial bank Banco Continental Overseas N.V.

In addition, the operations of the internationally operating commercial banks CBG Compagnie Bancaire Genève (Curaçao) N.V, Middenbank Curaçao N.V., and Banco de Venezuela S.A.I.C.A. (Curaçao branch) were continued, respectively, under the new statutory names SG Private Banking (Curaçao) N.V., ING Middenbank Curaçao N.V., and Banco de Venezuela, S.A. Banco Universal (Curaçao branch).

Following the withdrawal of the license of the internationally operating commercial bank Integra Bank N.V. on February 21, 2002, the Court of First Instance of the Common Court of Justice of the Netherlands Antilles and Aruba pronounced the bankruptcy of the institution on September 26, 2003.

At the end of 2003, the number of internationally operating commercial banks in the Netherlands Antilles was 40, and the number of domestically operating commercial banks was 11.

As of September 1, 2003, an updated version of Supervisory Regulation V concerning General and Specific Provisions for Loan Losses of Credit Institutions became effective, replacing the original version issued in June 1995.

5.2 Domestic banking

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

Total assets of the domestic banking sector grew by NAf.298.3 million (4.8%) in 2003 to NAf.6,497.9 million. The growth resulted primarily from an increase in the loan portfolio, followed by increases in interest-bearing cash, non-interest-bearing cash, and investments.

The loan portfolio increased by NAf.196.6 million (5.6%), due mainly to the increase in loans extended to both local and foreign business enterprises by NAf.51.5 million and NAf.68.5 million, respectively. Time loans extended to both local and foreign individuals contributed also to the total increase by, respectively, NAf.35.1 million and NAf.25.5 million. In addition, loans to local agencies and institutions of the government increased by NAf.24.2 million, and loans extended to other local institutions increased by NAf.20.9 million. Moreover, mortgage loans to local individuals, foreign individuals, and foreign business enterprises increased by NAf.18.1 million, NAf.18.6 million, and NAf.17.5 million, respectively. In contrast, current account overdrafts of local business enterprises decreased by NAf.70.1 million, mitigating the total increase in loan activities.

Table 21 Balance sheet of commercial banks operating in the domestic banking sector at year-end (in millions NAf.)

	2001		2002		2003	
	NAf.	%	NAf.	%	NAf.	%
ASSETS						
Non-int.-bearing cash	457.4	7.7	395.6	6.4	431.5	6.6
Interest-bearing cash	1,494.9	25.0	1,371.5	22.1	1,431.1	22.0
Investments	261.9	4.4	582.8	9.4	609.9	9.4
Loans	3,417.8	57.2	3,500.9	56.5	3,697.5	56.9
Investm. unconsol. sub.	19.5	0.3	12.2	0.2	13.5	0.2
Fixed assets	162.7	2.7	170.0	2.7	169.6	2.6
Other assets	159.4	2.7	166.6	2.7	144.8	2.2
Total assets	5,973.5	100.0	6,199.6	100.0	6,497.9	100.0
LIABILITIES						
Demand deposits	1,606.9	26.9	1,798.0	29.0	1,839.4	28.3
Savings deposits	2,176.7	36.4	2,148.7	34.7	2,334.7	35.9
Time deposits	1,276.5	21.4	1,302.0	21.0	1,473.7	22.7
Total deposits	5,060.1	84.7	5,248.7	84.7	5,647.8	86.9
Borrowings	158.8	2.7	183.1	2.9	125.4	1.9
Other liabilities	266.3	4.5	274.6	4.4	244.4	3.8
Total liabilities	5,485.1	91.9	5,706.4	92.0	6,017.6	92.6
Minority interest	5.3	0.1	6.6	0.1	6.4	0.1
Subordinated debentures	6.2	0.1	9.7	0.2	9.4	0.1
General provisions	134.3	2.2	161.7	2.6	140.3	2.2
Capital & reserves	342.6	5.7	315.2	5.1	324.2	5.0
Total capital	488.4	8.1	493.2	8.0	480.3	7.4
Total liabilities & capital	5,973.5	100.0	6,199.6	100.0	6,497.9	100.0

Interest-bearing cash increased by NAf.59.6 million due to an increase of NAf.225.4 million in time deposits held by foreign banks. In contrast, time deposits held at the central bank (i.e., certificates of deposit) and foreign subsidiaries and affiliates decreased by NAf.96.8 million and NAf.68.8 million, respectively.

In addition, the NAf.35.9 million increase in non-interest-bearing cash was the result of the growth in cash and demand balances held at the central bank and foreign subsidiaries and affiliates by

NAf.51.5 million and NAf.46.5 million, respectively. Cash and demand balances due from other banks decreased by NAf.58.2 million, mitigating the overall increase in non-interest-bearing cash.

Investments contributed NAf.27.1 million to the increase in total assets as a result of the increases in short-term debentures of the central government (NAf.39.8 million) and the island government of Curaçao (NAf.6.9 million). On the other hand, short-term debentures of foreign governments decreased by NAf.22.9 million. Finally, other assets decreased by NAf.21.7 million, slightly offsetting the increases in the aforementioned assets categories.

The increased activities of the commercial banks operating domestically were funded by an increase in deposits of NAf.399.1 million (7.6%). Time deposits increased by NAf.171.7 million because of higher placements by local financial institutions (NAf.155.3 million) and foreign business enterprises (NAf.51.3 million). These increases were mitigated by a drop in time deposits held by local subsidiaries and affiliates, and by other local banks of NAf.10.3 million and NAf.23.6 million, respectively.

Savings rose by NAf.186.0 million due to net deposits by local and foreign individuals of NAf.120.8 million and NAf.59.5 million, respectively. Furthermore, the growth in demand deposits (NAf.41.4 million) was attributable to net deposits by local and foreign business enterprises of NAf.71.0 million and NAf.72.5 million, respectively. These increases were offset partly by the decline in demand deposits of local and foreign financial institutions by NAf.51.0 million and NAf.21.8 million, respectively, and by foreign subsidiaries and affiliates (NAf.31.9 million).

In addition, borrowings dropped by NAf.57.5 million due to fewer funds borrowed from foreign subsidiaries and affiliates (NAf.40.4 million) and from other foreign banks (NAf.21.2 million).

Capital

Total capitalization of the domestic banking sector decreased by NAf.12.9 million (2.6%) to NAf.480.3 million at the end of 2003. This decline was the result of a depletion of general provisions.

Net income

Total operational income of the domestic banking sector increased further by NAf.22.8 million to NAf.428.0 million in 2003, almost entirely the result of "other income" (NAf.21.8 million). Total operational expenses declined by NAf.5.6 million, resulting from the reduction in "other operating expenses" of NAf.12.6 million, offset partly by an increase in "salaries and other employee expenses of NAf.8.0 million. Net operating income and net income after taxes increased by NAf.28.7 million and NAf.26.5 million to NAf.95.3 million and NAf.73.3 million, respectively.

Table 22 Income statement of commercial banks operating in the domestic banking sector (in millions NAf.)

	2001	2002	2003
Interest income	415.2	418.7	427.2
Interest expenses	156.4	(153.8)	(161.3)
Net interest income	258.8	264.9	265.9
Other income	118.9	140.3	162.1
Total operational income	377.7	405.2	428.0
Salaries & other employee expenses	(161.0)	(186.4)	(194.4)
Occupancy expenses	(48.2)	(52.4)	(51.9)
Other operating expenses	(59.7)	(70.9)	(58.3)
Net addition to general provisions	(39.1)	(28.9)	(28.1)
Total operational expenses	(308.0)	(338.6)	(332.7)
Net operating income	69.7	66.6	95.3
Net extraordinary items	(25.6)	3.2	0.6
Applicable profit taxes	(17.5)	(23.0)	(22.6)
Net income after taxes	26.6	46.8	73.3

Liquidity

The liquidity of the domestic banking sector increased further in 2003 (see table 23). Due to the apparent lack of sufficient sound local projects, many banks were faced with excess liquidity. All liquidity ratios reflected an increase during 2003. The overall liquidity of the commercial banks is considered sound.

Table 23 Liquidity ratio at year-end (in percentages)

	2001	2002	2003
Non-interest-bearing cash and short-term treasury paper to:			
total deposits	9.6	11.0	12.1
total liabilities	8.9	10.1	11.2
Non-interest & interest-bearing cash and short-term treasury paper to:			
total deposits	36.0	37.1	39.4
total liabilities	33.5	34.2	36.2
Total loans-to-total deposits	60.4	66.7	65.5

The aggregate macroprudential indicators in table 24 provide an indication of the performance of the commercial banks.

The indicators of capital adequacy of the domestic banking sector reflect a total capital-to-total assets ratio and a tier 1 capital-to-total assets ratio of, respectively, 7.7% and 5.3% in 2003. According to international standards, a total capital-to-risk-weighted assets ratio of at least 8% and a minimum tier 1 capital-to-risk-weighted assets ratio of 4% is required. The risk-weighted ratio of 8.4% is above the international standard.

The increase in the nonperforming loans ratios by 0.2 and 2.3 percentage points in 2003, compared to 2002, indicates a slight deterioration in asset quality. However, the loan loss provision as a percentage of the nonperforming loans decreased, which indicates that the banks reached an adequate provisioning level for loans in 2003.

Table 24 Macroprudential indicators of commercial banks operating in the domestic banking sector of the Netherlands Antilles at year-end (in percentages)

	2001	2002	2003
CAPITAL ADEQUACY[1]			
Total capital/total assets	8.2	8.2	7.7
Tier 1 capital/total assets	5.8	5.3	5.3
Tier 2 capital/total assets	2.3	2.7	2.2
Tier 3 capital/total assets	0.1	0.2	0.2
ASSET QUALITY			
Nonperforming loans/total loans	6.0	5.9	6.1
Nonperforming loans/total capital	43.4	39.9	42.2
Provisions for loan losses/non-performing loans	60.8	73.6	61.1
EARNINGS			
Gross earning assets yield	8.5	7.6	7.5
Break-even yield	3.0	2.8	2.8
Net interest margin	5.1	4.8	4.7
Return-on-assets	0.7	1.1	1.5
LIQUIDITY			
Total loans/total deposits	68.7	67.6	63.7
Liquidity surplus (in millions NAf.)	85.5	85.1	103.4

1 Excluding branches of foreign banks.

The earnings indicators reflect that the profitability of the domestic banking sector remained at an acceptable level. The return-on-assets ratio increased from 1.1% in 2002 to 1.5% in 2003 and is well above the benchmark of 0.5%. In contrast, the gross earning assets yield of the banks operating domestically decreased slightly from 7.6% in 2002 to 7.5% in 2003, indicating that their assets were slightly less productively employed. The break-even yield remained stable at 2.8% allowing the domestic banking institutions to realize an acceptable net income.

The loans-to-deposits ratio reveals that the banks used only 63.7% of their deposit base to fund their credit extension activities and maintained the remainder as liquid assets. Consequently, the liquidity surplus increased by NAf.18.3 million to NAf.103.4 million.

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

Total domestic assets of the domestic banking sector increased by NAf.92.0 million (2.2%) in 2003 (table 25). The increase in loans and investments by NAf.51.5 million (1.9%) and NAf.102.7 million (24.5%), respectively, contributed primarily to the growth in total domestic assets. These increases were offset partly by the decline in interest-bearing cash by NAf.125.8 million (20.6%). The higher investments were caused mainly by the net purchase of local government securities while the decline in interest-bearing cash was due partly to fewer certificates of deposit (CDs) auctioned by the central bank.

A comparison of tables 21 and 25 reflects that domestic credit extension comprised 74.3% of total credit extension by the domestic banking sector while residents held 71.1% of total deposits in 2003.

Table 25 Domestic activities of commercial banks operating in the domestic banking sector at year-end (in millions NAf.)

	2001		2002		2003	
	NAf.	%	NAf.	%	NAf.	%
ASSETS						
Non-int.-bearing cash	198.6	5.5	111.7	2.7	168.6	4.0
Interest-bearing cash	327.7	9.1	611.0	14.8	485.2	11.5
Investments	195.5	5.4	419.3	10.2	522.0	12.4
Loans	2,607.0	72.1	2,695.5	65.5	2,747.0	65.3
Investm. unconsol. sub.	13.2	0.4	12.0	0.3	13.3	0.4
Fixed assets	140.9	3.9	148.0	3.6	148.0	3.5
Other assets	131.8	3.6	117.8	2.9	123.2	2.9
Total assets	3,614.7	100.0	4,115.3	100.0	4,207.3	100.0
LIABILITIES						
Demand deposits	1,179.6	33.2	1,373.2	34.5	1,359.0	32.2
Savings deposits	1,356.5	38.1	1,497.2	37.7	1,630.0	38.6
Time deposits	801.9	22.6	908.9	22.9	1,032.1	24.4
Total deposits	3,338.0	93.9	3,779.3	95.1	4,021.1	95.2
Borrowings	8.4	0.2	7.2	0.2	11.2	0.3
Other liabilities	209.8	5.9	189.1	4.7	192.1	4.5
Total liabilities	3,556.2	100.0	3,975.6	100.0	4,224.4	100.0

Table 26 indicates that lending to the government through direct credit extension decreased by NAf.5.5 million in 2003 compared to 2002. In contrast, lending to the private sector increased by 2.1%, resulting from a growth in consumer loans and mortgages of 11.9% and 1.6%, respectively.

Table 26 Domestic lending to the government and the private sector at year-end (in millions NAf.)

	2001	2002	2003
Government [1]	26.3	13.7	8.2
Private sector:	2,580.7	2,681.8	2,738.8
Consumer loans	622.8	614.7	687.6
Business loans	905.9	932.8	898.3
Mortgages	1,052.1	1134.3	1,152.9
Total	2,607.0	2,695.5	2,747.0

[1] Excluding government securities

Table 27 illustrates the distribution of the domestic deposit base between the public sector and the private sector. The private sector continued to maintain by far the largest share of the domestic deposit base in 2003 (98.5%).

Table 27 Holders of deposits at year-end (in millions and %)

	2001		2002		2003	
	NAf.	%	NAf.	%	NAf.	%
Deposit holders						
Government	91.3	2.7	107.6	2.8	60.0	1.5
Private sector	3,246.7	97.3	3,671.7	97.2	3,961.0	98.5
Total deposits	3,338.0	100.0	3,779.3	100.0	4,021.0	100.0

Table 28 illustrates a further growth by 7.9% in the domestic deposits of the private sector in 2003. Deposits denominated in foreign currencies grew by 10.4% while guilder deposits increased by 7.4%.

Table 28 Change in domestic private sector deposits by currency (in millions NAf.)

	2001		2002		2003	
	NAf.	%	NAf.	%	NAf.	%
N.A. guilders	299.3	12.6	366.1	13.7	223.7	7.4
Foreign currencies	108.2	23.3	58.8	10.3	65.7	10.4
Total	407.5	14.4	424.9	13.1	289.4	7.9

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

Total foreign assets of commercial banks operating in the domestic banking sector increased by NAf.206.3 million (9.9%) to NAf.2,290.6 million in 2003 (table 29). This expansion resulted mainly from increases of NAf.185.4 million (24.4%) in interest-bearing cash and of NAf.145.1 million (18.0%) in loans. Foreign assets accounted for 35.3% of the total assets of the domestic banking sector in 2003.

In addition, total foreign liabilities increased by NAf.62.5 million (3.6%) to NAf.1,793.2 million, due to the NAf.157.3 million (10.7%) rise in foreign deposits. The rise in deposits was mitigated by decreases in foreign borrowings (NAf.61.7 million) and other liabilities (NAf.33.2 million). Only 30% of the increase in foreign assets was funded by foreign liabilities.

Table 29 Foreign activities of commercial banks operating in the domestic banking sector at year-end (in millions NAf.)

	2001		2002		2003	
	NAf.	%	NAf.	%	NAf.	%
ASSETS						
Non-int.-bearing cash	258.8	11.1	283.9	13.6	262.9	11.5
Interest-bearing cash	1,167.3	50.6	760.5	36.5	945.9	41.3
Investments	66.4	2.8	163.5	7.8	87.9	3.8
Loans	810.8	33.1	805.4	38.7	950.5	41.5
Investm. unconsol. sub.	6.3	0.3	0.2	0.0	0.2	0.1
Fixed assets	21.8	0.9	22.0	1.1	21.6	0.9
Other assets	27.5	1.2	48.8	2.3	21.6	0.9
Total assets	2,358.9	100.0	2,084.3	100.0	2,290.6	100.0
LIABILITIES						
Demand deposits	437.3	18.1	424.8	24.5	480.4	26.8
Savings deposits	820.3	32.7	651.5	37.7	704.7	39.3
Time deposits	474.6	19.9	393.1	22.7	441.6	24.6
Total deposits	1,732.1	70.7	1,469.4	84.9	1,626.7	90.7
Borrowings	7.8	26.6	175.9	10.2	114.2	6.4
Other liabilities	56.5	2.7	85.5	4.9	52.3	2.9
Total liabilities	1,796.5	100.0	1,730.8	100.0	1,793.2	100.0

5.3 Secondary financial institutions

In 2003, 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 2003.

5.4 International banking

Total assets of the international banking sector of the Netherlands Antilles decreased by NAf.4.1 billion (5.4%) to NAf.71.7 billion in 2003 compared to the increase of NAf.7.7 billion (11.3%) recorded in 2002. The NAf.10.8 billion (25.6%) decline in the loan portfolio accounted primarily for the decrease in total assets. This decline was mitigated mainly by an increase of NAf.6.5 billion (49.2%) in interest-bearing cash.

On the liabilities side, the decrease by NAf.11.8 billion (24.7%) in borrowings more than offset the NAf.7.9 billion (38.9%) increase in total deposits.

Finally, total capital reflected a capitalization corresponding with 9.0% of total assets, well above the international capital-to-risk weighted assets ratio of 8%.

Table 30 Balance sheet of commercial banks operating in the international banking sector at year-end (in billions NAf.)

	2001		2002		2003	
	NAf.	%	NAf.	%	NAf.	%
ASSETS						
Non-int.-bearing cash	2.0	2.9	0.9	1.2	3.3	4.6
Interest-bearing cash	13.1	19.2	13.2	17.4	19.7	27.5
Investments	4.5	6.6	4.2	5.5	5.8	8.1
Loans	38.1	56.0	42.2	55.7	31.4	43.7
Investm. unconsol. sub.	2.1	3.1	5.3	7.0	2.2	3.1
Fixed assets	0.1	0.1	0.1	0.1	0.1	0.1
Other assets	8.2	12.0	9.9	13.1	9.2	12.8
Total assets	68.1	100.0	75.8	100.0	71.7	100.0
LIABILITIES						
Demand deposits	6.4	9.4	7.6	10.0	11.1	15.4
Savings deposits	0.2	0.3	0.4	0.5	0.8	1.1
Time deposits	13.0	19.1	12.3	16.2	16.3	22.8
Total deposits	19.6	28.8	20.3	26.7	28.2	39.3
Borrowings	40.7	59.8	47.8	63.1	36.0	50.1
Other liabilities	1.1	1.6	1.1	1.5	1.1	1.6
Total liabilities	61.4	90.2	69.2	91.3	65.3	91.0
Minority interest	0.9	1.3	2.0	2.6	1.1	1.6
Subordinated debentures	0.0	0.0	0.0	0.0	0.0	0.0
General provisions	0.2	0.3	0.2	0.3	0.2	0.3
Capital & reserves	5.6	8.2	4.4	5.8	5.1	7.1
Total capital	6.7	9.8	6.6	8.7	6.4	9.0
Total liabilities & capital	68.1	100.0	75.8	100.0	71.7	100.0

Total operational income of the international banking sector increased by NAf.70.0 million (7.0%) to NAf.1.1 billion in 2003, owing to a NAf.102 million improvement in other income. Operating expenses decreased by NAf.187 million (28.1%) due to fewer additions to general provisions (NAf.281 million). As a result, net income after taxes improved considerably by NAf.255 million (93.1%) to NAf.529 million in 2003.

Table 31 Aggregate income statement of commercial banks operating in the international banking sector of the Netherlands Antilles at quarter-end (in millions NAf.)

	2001	**2002**	**2003**
Interest income	2,672	2,300	2,063
Interest expenses	(2,637)	(2,130)	(1,925)
Net interest income	35	170	138
Other income	1,078	832	934
Total operational income	1,113	1,002	1,072
Salaries & other employee expenses	(112)	(100)	(130)
Occupancy expenses	(26)	(18)	(33)
Other operating expenses	(205)	(166)	(215)
Net addition to general provisions	(375)	(381)	(100)
Total operational expenses	(718)	(665)	(478)
Net operating income	395	337	594
Net extraordinary items	(6)	(55)	(47)
Applicable profit taxes	(12)	(8)	(18)
Net income after taxes	377	274	529

6 INSTITUTIONAL INVESTORS

6.1 Introduction

In today's environment of lower investment results, on the one hand, and increased premium rates following the events of September 11, on the other, insurance companies operating worldwide are forced to come up with cost-reducing measures on a structural basis. In the past, insurance companies adopted tighter underwriting guidelines to limit insurance risks, but they are now facing mitigating sales due to the higher cost of insurance and increased competition in the market.

The developments in the market undoubtedly will result in changes in the distribution channels and in the products offered to consumers. For example, life insurance policies with guaranteed pay-out rates will be reduced while nonlife insurers might offer coverage only for a limited period of time to be able to adjust their commitments. Furthermore, international and regional developments in financial holding companies, including mergers and acquisitions of banking, insurance and securities services, may provide a competitive edge for companies within the group based on larger economies of scale.

Property catastrophe capacity remains more than adequate to satisfy most reinsurance buyers. Expanded use of catastrophe modeling has resulted in more efficient pricing of catastrophe exposures with faster turnaround time for reinsurance underwriters. Models are transforming catastrophe reinsurance into a commodity with little variation in pricing among reinsurers. Catastrophe rates should continue to improve, allowing most insurance companies to reduce their overall catastrophe reinsurance costs without increasing net exposure.

The insurance sector is susceptible to various risks of which money laundering and terrorist financing are of increasing concern. Against the background of the World Trade Center tragedy, major reinsurers maintain standard terrorism exclusion clauses in most reinsurance contracts. At the same time, some reinsurers are offering specific terrorism coverage for a variety of risk classes. Although capacity in this area remains limited, selective terrorism reinsurance is evolving into a special line of business. Until a secondary market for this risk develops, the reinsurers offering terrorism coverage will continue to be highly selective in allocating aggregates.

The issue of combating money laundering and terrorist financing is being dealt with by the Financial Action Task Force (FATF). The vulnerability of the insurance sector to money laundering was one of the five topics chosen at the annual FATF typologies exercise in 2003. The Bank has installed an anti-money laundering working group that is responsible for amending existing guidelines where necessary and developing new ones. In 2003, the Bank initiated anti-money-laundering visitations at the premises of the life insurance companies subject to its supervision. These visitations are used to verify the companies' compliance with the 'Guidelines for the Detection and Deterrence of Money Laundering for Insurance Companies', issued by the Bank. Visitation reports of the Bank's findings were drafted and shared with the respective companies. The main findings were that the indicators included in the guidelines needed additional clarification while some companies expressed the need for additional training and seminars on the subject of anti-money laundering.

The Bank is a member of the International Association of Insurance Supervisors (IAIS) in Basle, an organization participated by over 100 insurance supervisors from around the world. In recognition of the need to ensure the protection of policyholders and financial sector stability, the IAIS developed Insurance Core Principles and Insurance Core Principles Methodology to provide the international financial community with benchmarks to assess the effectiveness of insurance supervisory regimes. The IAIS, through its various committees, regularly issues guidance notes and papers for its members.

The Bank was assessed on its observance of the IAIS Core Principles. The assessment was conducted in the context of the Module II Offshore Financial Center Assessment performed by an IMF Monetary and Exchange Affairs Department mission in January and April of 2002. Assessed were the legal and regulatory framework, as well as the policies and practices of the Bank as the supervisory authority. The assessment resulted in a recently published report. The report concluded that the Bank was observant or broadly observant of 16 of the 17 principles. On one principle relating to market conduct supervision, the Bank was rated materially nonobservant. The major reason for this rating was the absence of supervision of insurance intermediaries. In the meantime, the national ordinance that provides for this supervision was accepted by Parliament and went into effect on January 1, 2004. The IAIS recently has expanded the number of principles from 17 to 23. The Bank also will seek to comply with the new principles and is upgrading and revising its supervisory and monitoring systems accordingly.

With the enactment of the National Ordinance on Insurance Intermediaries (N.G. 2003, nr. 113), the Bank was entrusted with the supervision of insurance intermediaries. This ordinance provides the Bank with an effective tool to set rules prior to entering into an insurance contract between an insurance company and a potential policyholder. Pursuant to this new legislation, engaging in the insurance brokerage business in the Netherlands Antilles is prohibited unless the insurance intermediary is listed in the register maintained by the Bank. The register is subdivided into a life and a nonlife section; registration in both sections is allowed. To be listed in the register, the insurance intermediary must comply with the legal requirements regarding professional competence, integrity, financial soundness, professional liability insurance, and physical presence in the Netherlands Antilles.

The internal committee of the Bank responsible for amending the national ordinance governing the supervision of corporate pension funds is progressing in its work. In amending this ordinance, international developments and guidelines issued by international supervisory authorities will be taken into account.

Very important in every supervisory system is the availability of the financial data of the institutions supervised. These data must provide a clear picture of the policy carried out and the overall financial position of the institutions. The Bank developed the Annual Reports Automated Statements (ARAS) to serve this goal.

The new data retention system developed by the Bank to process the information provided by the ARAS reporting system currently is being fed with information on the industry. This system will provide important market information for a period of five years. The system also includes 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.

6.2 The institutional investors sector

For the year 2003, the number of institutional investors operating in the Netherlands Antilles was 72: 10 life insurance companies, 18 nonlife insurance companies, and 24 pension funds. In addition, the process of registering funeral service insurers with a minimum of 200 insured is still ongoing.

The number of insurance companies servicing the international markets was 20 at the end of 2003. Of these companies, one is involved in the life insurance business, 15 in the nonlife business, and 4 are professional reinsurers. Most of the internationally operating insurance companies have European parents.

The overview in graph 4 does not include the 11 companies and pension funds in the process of liquidation. However, these institutions remain subject to supervision by the Bank.

Graph 4 Composition of the institutional investors' sector (number of companies)

6.3 Overview of developments in the insurance industry

6.3.1 General

The results reported by the local nonlife insurance industry in recent years show that net premiums written increased up to financial year 2000. After a 2.3% decrease in 2001, net premiums written went up again by 14.3% in 2002. This improvement was the result of an increase of 18.3% in direct written premiums.

The consolidated net result after taxes of the nonlife sector amounted to NAf.2.2 million in 2002, a significant decrease (93.5%) compared to the consolidated net profit of NAf.33.3 million in 2001. Both net claims incurred and other underwriting expenses increased in 2002, by 16.3% and 26.9%, respectively, leading to a lower underwriting result of NAf.2.7 million. Net investment income also decreased significantly (53.5%), contributing further to the deterioration in the net result reported in 2002.

Total premium income of the local life insurance industry increased by 21.3% in 2002 compared to 2001. This improvement corresponds with the development in the local nonlife insurance industry, indicating an increase in the local demand for insurance products. Despite the higher premium income, the consolidated net result after taxes of the local life insurance industry decreased by 36.9% to the amount of NAf.7.7 million in 2002, caused mainly by higher extraordinary losses.

6.3.2 Life insurance industry

6.3.2.1 Balance sheet

According to table 32, total assets of the local life insurance industry increased by 8.3% in 2002, compared with a 5.5% growth in 2001. The increase in total assets in 2002 can be attributed mainly to an increase of NAf.159.9 million (17.7%) in invested assets. Of the total assets in 2002, 74.0%

was related to investments and 18.8% to current assets. Total liabilities increased mainly as a result of a NAf.213.4 million (24.4%) increase in technical provisions.

Table 32 Consolidated balance sheet of life insurance companies (in millions NAf.)

	2000		2001		2002	
	Local	Int'l	Local	Int'l	Local	Int'l
ASSETS						
Intangibles	-	-	-	-	0.1	-
Total investments	852.3	30.3	904.5	34.1	1,064.4	29.1
Current assets	253.3	18.8	251.1	17.8	270.3	38.7
Other assets	10.3	-	10.3	-	5.4	-
From separate accounts statement	143.5	-	162.5	-	98.0	-
Total admissible assets	1,259.4	49.1	1,328.4	51.9	1,438.2	67.8
EQUITY, PROVISIONS, & LIABILITIES						
Capital	12.8	7.1	10.8	7.1	57.4	7.1
Surplus	89.4	20.7	94.9	21.9	66.7	27.7
Subordinated instruments	-	-	-	-	5.5	
Technical provisions	825.8	15.7	875.4	17.9	1,088.8	25.5
Other provisions & liabilities	10.2	1.2	8.8	1.3	6.5	1.6
Current liabilities	168.9	4.4	165.9	3.7	106.5	5.9
Contingent liabilities	8.8	-	10.1	-	8.8	-
From separate accounts statement	143.5	-	162.5	-	98.0	-
Total equity, provisions, & liabilities	1,259.4	49.1	1,328.4	51.9	1,438.2	67.8

The equity position of the local life insurance companies, consisting of capital, surplus, and subordinated instruments, increased by NAf.23.9 million (22.6%) in 2002. This increase can be attributed to an increase of NAf.46.6 million in capital. The 2002 equity position of the local life insurance companies represents about three and a half times the amount needed to meet the 4% solvency requirement, which is equivalent to NAf.35.9 million in 2002.

Total assets of the international life insurance companies increased by NAf.15.9 million (30.6%), reaching NAf.67.8 million at the end of 2002. This increase can be attributed to an increase of NAf.20.9 million in current assets. The 2002 equity position increased by 20.0% to NAf.34.8 million, well above the legally required solvency margin of NAf.0.7 million.

6.3.2.2 Investments

As indicated in the previous paragraph, total investments of the local life insurance industry increased by NAf.159.9 million (17.7%) in 2002. This increase was due mainly to the increase in bonds. The composition of the consolidated 2001 and 2002 investment portfolio of the local life insurance companies is presented in graph 5. This graph indicates that the shares of bonds, mortgage loans, and real estate increased by, respectively, 4.1, 0.5, and 0.1 percentage points in 2002 compared to 2001. These increases were at the expense of the shares of deposits with financial institutions and stocks, which declined by 2.1 and 2.6 percentage points, respectively.

Graph 5 Composition of the investment portfolio of local life insurance companies

The composition of the consolidated investment portfolios of the international life insurance companies in 2001 and 2002 is presented in graph 6. The total investment portfolios of the international life insurance companies decreased by NAf.5.0 million (14.7%) in 2002 compared to 2001, due primarily to a decrease in the share of stocks. From the graph it can be deduced that the share of bonds increased by 2.2 percentage points to 68.7%, at the expense of the share of stocks.

Graph 6 Composition of the investment portfolio of international life insurance companies

6.3.2.3 Profit and loss statement

The operating results of the local life insurance industry are presented in table 33. The net result before corporate taxes decreased by NAf.2.3 million (14.1%) in 2002, compared with the NAf.0.7 million (4.1%) decrease in 2001. The net result after taxes decreased by NAf.4.5 million (36.9%) to NAf.7.7 million in 2002, due to higher corporate taxes incurred.

Premium income increased by NAf.30.8 million (21.4%) in 2002, compared to 2001. Of the total premium income, 67.2% was related to individual life and 32.8% to group life business.

The net operational loss amounted to NAf.27.6 million in 2002, slightly higher (NAf.0.6 million) than in 2001. This deterioration was attributable to an increase of NAf.38.8 million in operational expenditures, which exceeded the increase of NAf.38.2 million in operational income. The increase in operational expenditures was caused mainly by an increase in net benefits incurred in the amount of NAf.27.7 million (41.2%).

Table 33 Consolidated profit and loss statement of life insurance companies (in millions NAf.)

	2000		2001		2002	
	Local	Int'l	Local	Int'l	Local	Int'l
INCOME						
Total net premium income	148.9	8.9	143.6	7.3	174.4	9.7
Net investm. income allocated to technical provisions	60.8	-	26.4	1.5	27.9	0
Net other operational income	0.4	1.1	0.3	1.5	8.2	2.2
Total operational income	209.9	10.0	170.3	10.3	208.5	11.9
EXPENSES						
Net benefits incurred	54.3	-	67.2	2.6	94.9	5.0
Change in net techn. prov.	94.5	7.5	78.6	2.7	74.3	7.5
Policyholders' dividends	10.2	0.5	10.7	0.5	12.5	-0.6
Insurance expenses and non-corporate taxes	31.1	0.3	25.5	0.4	28.7	0.4
Commission and other acquisition costs	11.7	0.7	14.9	0.6	14.5	0.8
Net other operational expend.	2.6	0.3	0.4	0.2	11.2	0.2
Total operational expend.	204.4	9.3	197.3	7.0	236.1	13.3
Net operational result	5.5	0.7	-27.0	3.3	-27.6	-1.4
Net investment income allocated to surplus	9.4	2.3	43.6	0.8	52.6	2.9
Other income and expenses	[illegible]	-0.6	[illegible]	-0.2	[illegible]	0
Net result from separate accounts	2.0	-	0	-	2.4	-
Extraordinary results	0.1	0.7	-0.5	0.4	-8.5	-1.8
Net result before corp. taxes	17.0	3.1	16.3	4.3	14.0	-0.3
Corporate taxes incurred	5.7	-	4.1	-	6.3	-
Net result after corp. taxes	11.3	3.1	12.2	4.3	7.7	-0.3

Net premium income in the international life insurance industry showed an increase from NAf.7.3 million in 2001 to NAf.9.7 million in 2002. Nevertheless, the net operational result turned around from a NAf.3.3 million surplus to a NAf.1.4 million loss, due primarily to a NAf.4.8 million higher change in net technical provisions.

As a result of a relatively high extraordinary loss, the life insurance industry servicing the international market ended up with a net loss after corporate taxes of NAf.0.3 million in 2002. This represents a deterioration of NAf.4.6 million compared to 2001.

Graph 7 presents an overview of the consolidated net results after taxes of the local life insurance companies during 1993-2002. This graph depicts declining net results until 1997. Thereafter, net results started to rise again but declined in 2002.

Graph 7 Net results after corporate taxes of the local life insurance sector (in millions NAf.)

6.3.3 The nonlife insurance industry

6.3.3.1 Balance sheet

The balance sheet total of the nonlife insurance companies operating in the domestic market increased by NAf.196.9 million (75.6%) to NAf.457.2 million at the end of 2002, compared to 2001. This increase contrasted with 2001, when a decrease of 27.3% in total assets was noted. Total investments increased by NAf.72.8 million (52.1%), and current assets more than doubled by NAf.124.1 million (106.2%) in 2002.

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 46.5% in 2002. This percentage is a decrease compared to 2001, in which 53.6% of total assets was invested. Consequently, a larger portion of total assets (52.7% in 2002) relates to current assets, compared to 18.8% in the life business.

On the liability side, the increase in the balance sheet total in 2002 was reflected mainly by a NAf.131.2 million (352.5%) increase in current liabilities, compared to 2001. The equity position of the local nonlife insurance industry increased by NAf.21.4 million (30.0%) totaling NAf.92.7 million at the end of 2002. In 2001, a decrease of 9.2% was recorded. The equity position at the end of 2002 was well above the 15% solvency margin (NAf.34.8 million) required by law.

The balance sheet total of the nonlife insurance companies servicing the international market reflects an increase of NAf.232.8 million (11.5%) to approximately NAf.2.3 billion at the end of 2002, compared to 2001. This increase was caused mainly by a NAf.166.2 million (8.7%) increase in investments. On the liabilities side, the largest increase of NAf.169.3 million (14.1%) was noted in the technical provisions. The industry disposed of an amount of NAf.813.1 million in equity at the end of 2002. As a result, the consolidated solvency position of the internationally operating nonlife insurance companies exceeded significantly the required solvency margin of NAf.93.7 million.

Table 34 Consolidated balance sheet of the nonlife insurance industry (in millions NAf.)

	2000		2001		2002	
	Local	Int'l	Local	Int'l	Local	Int'l
ASSETS						
Intangibles	0.1	-	-	-		
Total investments	141.5	1,642.8	139.7	1,914.0	212.4	2,080.2
Current assets	211.5	133.7	116.9	117.1	241.0	183.6
Other assets	4.7	0.1	3.8	0.1	3.8	0.1
Total admissible assets	357.8	1,776.6	260.4	2,031.2	457.2	2,263.9
EQUITY, PROVISIONS, & LIABILITIES						
Capital	41.9	115.5	29.2	146.8	68.7	143.9
Surplus	36.6	536.9	41.0	618.5	23.0	669.2
Subordinated instruments	0.1	-	1.2	-	1.0	-
Technical provisions	150.3	1,059.4	145.5	1,203.4	178.3	1,372.7
Other provisions & liabilities	4.0	7.6	6.3	7.2	17.8	15.4
Current liabilities	124.9	57.2	37.2	55.3	168.4	62.7
Contingent liabilities	-	-	-			
Total equity, provisions, & liabilities	357.8	1,776.6	260.4	2,031.2	457.2	2,263.9

6.3.3.2 Investments

The composition of the investment portfolio of the local nonlife insurance companies is presented in graph 8. This graph indicates that the share of bonds and other fixed income securities increased from 18.6% in 2001 to 37.4% in 2002, reflecting a shift to long-term investments. The higher share of bonds and other fixed income securities was primarily at the expense of the share of deposits with financial institutions, which decreased from 64.3% to 52.3%.

Graph 8 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 9. No substantial changes occurred in 2002 compared to 2001. The graph indicates that, contrary to 2001, international nonlife insurance companies participated in investment pools in 2002 (3.1%). This increase was largely at the expense of the share of bonds and other fixed income securities, which declined by 4.2 percentage points to 18.8%.

Graph 9 Composition of the investment portfolio of the international nonlife insurance companies

6.3.3.3 *Profit and loss statement*

Net earned premium of the local nonlife insurance industry increased by NAf.24.2 million (14.2%) in 2002, compared to an increase of only NAf.1.4 million (0.8%) in 2001. The net claims incurred during 2002 increased by NAf.12.7 million (16.3%), while a decrease of NAf.16.0 million (17.1%) was noted in 2001. The year 2002 was closed with an underwriting profit of NAf.2.7 million, compared to NAf.12.5 million in 2001. Net investment income decreased by NAf.14.7 million to NAf.12.7 million in 2002, compared to 2001. The negative other results deteriorated further from NAf.3.3 million in 2001 to NAf.7.8 million in 2002. The industry ended up with a net profit of NAf.2.2 million in 2002, a substantial decline compared to 2001.

Table 35 Consolidated profit and loss statement of the nonlife insurance industry (in millions NAf.)

	2000		2001		2002	
	Local	Int'l	Local	Int'l	Local	Int'l
INCOME						
Total net earned premium	169.2	445.6	170.6	624.4	194.8	613.6
Net other underwriting income	5.4	0.2	-	0.6	0.2	0.8
Total operational income	174.6	445.8	170.6	625.0	195.0	614.4
EXPENSES						
Net claims incurred	93.7	200.2	77.7	316.2	90.4	376.0
Change in various provisions	1.4	65.8	0.3	82.0	1.4	61.5
Claim adjustment expenses	1.7	0.7	4.5	2.3	5.0	0.4
Net other underwr. expend.	68.9	32.4	71.2	63.5	90.4	68.7
Net other operational expend.	9.4	2.0	4.4	2.0	5.1	1.8
Total operational expend.	175.1	301.1	158.1	466.0	192.3	508.4
Underwriting results	-0.5	144.7	12.5	159.0	2.7	106.0
Net investment income	7.6	107.2	27.4	73.2	12.7	66.7
Other results	-0.3	-20.0	-3.3	-59.5	-7.8	-8.5
Extraordinary results	-	1.1	0.2	1.8	-0.1	-5.6
Net result before corp. taxes	6.8	233.0	36.8	174.5	7.5	158.6
Corporate taxes incurred	7.5	3.7	3.5	2.9	5.3	2.9
Net result after corp. taxes	-0.7	229.3	33.3	171.6	2.2	155.7

The total net earned premium of the internationally operating nonlife insurance companies decreased by NAf.10.8 million (1.7%) in 2002, compared to an increase of NAf.178.8 million (40.1%) in 2001. The net claims incurred increased by NAf.59.8 million (18.9%) in 2002. These developments contributed largely to the decline in the underwriting result by NAf. 53.0 million (33.3%) to NAf.106.0 million.

The industry experienced a NAf.6.5 million (9.0%) decline to NAf.66.7 million in investment income in 2002. Due to the substantially lower negative other results (NAf. 51.0 million), the decline in the sector's net result after corporate taxes remained limited to NAf.15.9 million (9.1%).

Graph 10 presents an overview of the consolidated net results after taxes of the local nonlife insurance companies during 1994 - 2002.

Graph 10 Net results after corporate taxes of the local nonlife insurance sector (in millions NAf.)

6.4 Overview of developments in the pension industry

Total assets of the pension industry increased by NAf.186.6 million (4.3 %) to NAf.4.5 billion at the end of 2001, compared to 2000. Investments accounted for 82.0% of the industry's total assets; bonds accounted for 45.0% of total assets. The equity position of the pension industry decreased by 28.2% in 2001 compared to 2000, which showed a decrease of 22.1% compared to 1999.

During the period 1999-2001, the average amount in premium contributions received by the pension funds equaled NAf.144.4 million, while the average amount in benefits paid amounted to NAf.141.2 million. Premium contributions increased by NAf.37.9 million (27.8%) in 2000, but decreased by NAf.51.3 million (29.4%) in 2001. Investment income decreased by NAf.95.2 million (29.9%) in 2001 compared to an increase of NAf.42.4 million (15.3%) in 2000.

Total expenses of the pension industry decreased by NAf.4.1 million (1.1%) in 2001 compared to 2000. The benefit payments and additions to the technical provisions accounted for 86.3% of expenses in 2001. The sector continued to experience losses. In 2001, the reported loss amounted to NAf.130.8 million, almost double the amount of 2000. This deterioration can be attributed mainly to the decline in income.

Table 36 Consolidated balance sheet of the pension industry (in millions NAf.)

	1999	2000	2001
Admissible assets			
Investments, of which:			
- Real estate	76.9	91.2	83.4
- Participations	17.2	22.7	318.9
- Stocks	1,121.2	1,027.3	675.8
- Bonds and other fixed income securities	1,820.5	1,830.5	2,019.8
- Mortgage loans	77.5	88.8	102.0
- Other loans	121.7	141.2	185.1
- Deposits with financial institutions	82.2	112.8	143.6
- Other investments	6.4	7.6	163.9
Current assets	406.9	405.2	396.7
Other assets	542.4	592.9	417.6
Total	4,272.9	4,320.2	4,506.8
Equity, provisions, & liabilities			
Equity:			
- Surplus	516.0	400.2	287.2
Technical provisions, of which:			
- Provisions for pension obligations	3,685.5	3,889.3	4,161.3
- Other technical provisions	16.1	15.6	6.0
Other provisions & liabilities	1.4	7.1	21.0
Current liabilities	53.9	8.0	31.3
Total	4,272.9	4,320.2	4,506.8

Table 37 Consolidated profit and loss statement of the pension industry (in millions NAf.)

	1999	2000	2001
Income			
Contributions	136.2	174.1	122.8
Transferred pension obligations received			5.4
Net investment income earned and net realized capital gains and losses	276.5	318.8	223.6
Benefits received from reinsurers	0.5	0.7	
Profit sharing from reinsurers	2.7	3.1	0.2
Other income	5.3	3.5	5.7
Total income	421.2	500.2	357.7
Expenses			
Pension benefits incurred	134.5	144.6	144.4
Change in net technical provisions	222.4	194.6	168.6
Pension obligations transferred	0.7	1.7	1.9
Reinsurance premiums incurred	12.0	9.9	5.8
Operational expenses incurred	13.3	13.2	14.5
Other expenses incurred	8.7	2.8	27.5
Total expenses	391.6	366.8	362.7
Extraordinary results	-	-4.7	-7.7
Net operational results before gains or losses	29.6	128.7	-12.7
Net unrealized gains or losses for:			
Invested assets	-	-	-0.2
Noninvested assets	1.2	-	-4.2
Foreign exchange	127.6	-197.4	-113.7
Net profit or loss	158.4	-68.7	-130.8

6.5 The investment institutions, administrators and trust service providers sector

The National Ordinance on the Supervision of Investment Institutions and Administrators (N.G. 2002, nr. 137), hereafter referred to as "NOSIIA", came into effect on January 1, 2003. The objectives of the NOSIIA 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.

In January 2003, the Bank issued its Directives on the Supervision of Investment Institutions and Administrators. In addition, in July 2003, the Bank issued Policy Guidelines on Exemption Regulation for Administrators and Policy Guidelines on Exemption Regulation for Investment Institutions, which outline the basis on which the Bank may grant an exemption to an investment institution or administrator. The latter document was revised in September 2003. Furthermore, the Bank issued Policy Guidelines for Foreign Investment Institutions and Policy Guidelines for Foreign Administrators, which contain the requirements for foreign investment institutions and administrators operating in the Netherlands Antilles.

On June 30 and December 18, 2003, respectively, the National Decree on Supervisory Fees to be charged to Investment Institutions and Administrators and the National Decree on Fines to be imposed on Investment Institutions and Administrators were issued by the government.

The Bank also has drafted other policy guidelines for investment institutions and administrators. The subjects addressed in these guidelines include anti-money-laundering and terrorist financing, administrative organization of investment institutions, safeguards to be held by (semi-) open-ended investment institutions, large investors, and the outsourcing of tasks. In addition, reporting guidelines for investment institutions and administrators were drafted. The sector was given the opportunity to comment on the policy guidelines and reporting guidelines.

The Bank's supervision of investment institutions is focused on the adequacy of the infrastructure of the investment institutions, as revealed by the conduct of business, the institution's equity capital, the competence and integrity of the persons that (co-) determine the institution's policy, and on the provision of information to (prospective) investors. On the other hand, 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 that (co-)determine the administrator's policy, and the administrator's compliance with rules and regulations.

During 2003, 69 local investment institutions requested exemptions, all of which were granted by the Bank. Exemptions also were granted to 3 foreign investment institutions, 5 local administrators, and 3 foreign administrators. Twenty local investment institutions and 12 local administrators applied for a license, some of which are still being processed.

The Bank recently has been entrusted with the supervision of trust service providers in the Netherlands Antilles. This supervision is exercised by virtue of the National Ordinance on the Supervision of Trust Service Providers (N.G. 2003, nr. 114), hereafter referred to as "NOST", which was enacted on December 31, 2003. With the enactment of this national ordinance, the National Ordinance on the Supervision of Fiduciary Business (N.G. 2001, nr. 81) was revoked. Pursuant to the NOST, trust services may only be provided by (i) trust offices granted a license by the Bank (and the natural and/or legal persons listed on the annex to such license), and (ii) persons granted a dispensation by the Bank. Pursuant to the transitional provision contained in article 27, paragraph 2 of the NOST, 119 temporary licenses were issued to trust service providers in the Netherlands Antilles.

7 POLICIES AND ACTIVITIES OF THE BANK

7.1 Training and seminars

The Bank's staff attended a variety of courses, seminars, and conferences in 2003 as part of the Bank's continuing education policy and to enable its personnel to keep abreast of the latest developments in their fields of expertise.

Staff in the department of Supervision on Institutional Investors attended, among other things, a working meeting of the Caribbean Association of Insurance Regulators, the Caribbean Regional Insurance Supervision Seminar sponsored by the Office of the Superintendent of Financial Institutions in Canada (OSFI) and the Caribbean Regional Technical Assistance Center (CARTAC), and several locally organized seminars and workshops on pensions. In addition, staff in the Investment Institutions & Trust Supervision department attended the annual conference of the International Institute for Securities Market Development hosted by the US Securities and Exchange Commission, and a workshop on the regulation of trust service providers organized by the British Virgin Islands Financial Services Commission. Furthermore, staff in the Statistical Information and Reporting department participated in a seminar organized by the IMF to evaluate the 2002 and prepare the 2003 Coordinated Portfolio Investment Survey. The Netherlands Antilles also participates in the survey, which is held among companies operating in the domestic and international financial sector. Staff in the Banking Supervision department attended, among other things, a seminar on risk management & internal control and a course on bank analysis and examination both organized by the Federal Reserve System; seminars and workshops on risk-focused supervision & problem bank resolution, international accounting & auditing for banks, and corporate governance & operational risk management, all hosted by the Financial Stability Institute; a workshop on consolidated supervision of banks organized by CARTAC; and several seminars on the new Basle Capital Accord. Moreover, Research Department staff participated in the annual conference of the Financial Management Association, the annual central banking seminar of the Federal Reserve Bank of New York, and a course on monetary policy in developing countries hosted by Study Center Gerzensee.

During 2003, the Bank continued to support "The Financial Institute", an institution geared towards educating employees in the local financial sector. The Bank helped organize workshops and examinations, also participated in by the Bank's staff. The topics of workshops included credit extension, compliance, and liability insurance & reinsurance.

Apart from "The Financial Institute", the Bank organized also various seminars and workshops in cooperation with local consultancy firms. Topics included the implementation of International Financial Reporting Standards, pensions, and pension funds. In addition, the Bank hosted the biannual seminar for legal advisors of Caribbean central banks. The main theme of this seminar was integrity and its supervision.

7.2 International financial sector developments

In June 2003, the Financial Action Task Force (FATF) finalized the revision of its 40 recommendations on money laundering and terrorist financing. The Netherlands Antilles, as a member of the FATF, endorsed these forty revised recommendations and is now preparing to implement the new obligations. This preparation entails a substantial effort because all the measures against money laundering and terrorist financing must be applied also to lawyers, public notaries, accountants, real estate companies, and dealers in precious metals and stones. The National Committee on Money Laundering and Terrorist Financing (CIWG) started with a consulting round to find out how these measures can be implemented in the most effective way considering the new obligations and the practical experiences of the specific sectors. The objective is to introduce the new measures by the end of 2004.

Furthermore, the Bank issued its new Provisions and Guidelines on the Detection and Deterrence of Money Laundering and Terrorist Financing in June 2003. These provisions and guidelines were issued separately for credit institutions, insurance companies, and money transfer companies. They are very comprehensive and cover most new developments in the areas of money laundering and terrorist financing. The Bank organized workshops to familiarize the financial institutions with their new obligations.

Finally, in December 2003, Parliament approved legislation bringing the supervision of the trust service providers under the responsibility of the central bank in accordance with the recommendations of the IMF.

7.3 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 16, 2004, this percentage was for a three-month period9 on the basis of developments in the free reserves of commercial banks, the official reserves, and domestic credit extension. The reserve requirement is 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, inactivated from March 1, 2002, limits 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 net foreign debt. The Bank uses bi-weekly auctions of Certificates of Deposit (CDs) and initiates open-market operations through buying or selling government securities to support the other instruments. The interest rate on CDs is determined by the market participants but is bound to a maximum, equal to the Bank's pledging rate minus 100 basis points.

During 2003, the Bank made various adjustments to its monetary policy related to the further decline in interest rates in the United States, the strong expansion in credit to the government, and the promotion of market forces in the conduct of its policy.

Following a reduction in five steps from 7.0% to 3.5% in 2002, the Bank reduced its pledging rate, i.e., its official borrowing rate, again in three steps during 2003: by 0.5 percentage point to 3.0% on January 13, by another 0.5 percentage point to 2.5% on May 19, and by 0.25 percentage point to 2.25% on June 30. 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'

[9] From January 16, 2004, the reserve requirement percentage is set for a two-month period to increase this instrument's flexibility.

borrowing exceeding NAf.20 million-- declined to 3.25%, while the maximum CD rate fell to 1.25%. 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 caused by the decline in US interest rates.

Furthermore, on January 15, 2003, the Bank introduced some refinements in its CD-auctions to increase their attractiveness to commercial banks. The refinements included CD maturities of 12, 26 and 52 weeks, in addition to the 4-week maturity. Moreover, 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, to contain the excessive growth in credit extension to the government by the commercial banks and, hence, its potential negative impact on our foreign exchange reserves.

7.4 175-year anniversary

On February 6, 2003, the Bank celebrated its 175th anniversary with a week of various festivities for its personnel and guests. One of the highlights was a lecture by the president of the European Central Bank, Dr. Willem Duisenberg, on credible fiscal policy, followed by a panel discussion with the presidents of the central banks of the Netherlands, Aruba, and the Netherlands Antilles. The anniversary was commemorated also by special issues of stamps and coins and a book with articles on central banking written by the Bank's staff.

8 FOREIGN EXCHANGE REGULATIONS AND LICENSE FEE

8.1 Introduction

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 normally are 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.

8.2 Foreign exchange licenses

In 2003, the number of foreign exchange licenses issued by the Bank declined by 91 (6%) to 1,417 compared to 2002 (see table 38). This decline can be attributed primarily to the drop in the number of foreign exchange exemptions granted to international financial and business companies (117). In addition, the total capital flow related to the licenses granted decreased by NAf.236.5 million (48%) to NAf.253.5 million. This decrease is explained by the licenses granted in 2002 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 38, the participation is included under the item “Other” and the foreign financing under “Borrowing abroad.” Noteworthy further are that nonresidents established more companies in the Netherlands Antilles and that residents transferred more funds to their own accounts abroad.

Table 38 Overview of foreign exchange licenses issued (in millions NAf.)

Description	2002		2003	
	Number	Amount	Number	Amount
Establishment company by nonresident	73	0.9	106	15.9
Transfer to own account abroad	9	1.2	9	6.8
Portfolio investment abroad	6	9.8	10	10.4
Borrowing abroad	201	402.9	176	215.4
Lending abroad	8	2.2	11	3.4
Request for foreign bank account	-	-	4	1.6
Request for local nonresident account	8	-	23	-
Request for intercompany account abroad	2	-	-	-
Granting guarantee abroad	2	-	-	-
Exemption int. fin. & bus. companies	1,194	-	1,077	-
Other	5	73.0	1	-
Total	1,508	490.0	1,417	253.5

8.3 License fee

Starting January 1, 1996, a fee was introduced for the license to operate as a foreign exchange bank. This license fee is assessed on the international transactions of foreign exchange banks and 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 39 provides an overview of the license fees collected monthly from 2001 through 2003. From the total amount of license fees collected in the Netherlands Antilles in 2003, NAf.27,956.7 thousand (65%) was generated on Curacao, NAf.14,264.4 thousand (33%) on St. Maarten, and NAf.515.2 thousand (1%) on Bonaire. The remaining NAf.164.8 thousand (1%) of license fees was paid through the Bank.

Table 39 License fees collected from 2001 through 2003 (in thousands NAf.)

	2001	2002	2003*
January	3,369.2	3,103.1	3,775.6
February	2,924.4	2,698.2	2,976.2
March	3,439.1	3,070.9	3,596.8
April	2,777.4	3,072.9	3,183.6
May	3,074.9	3,568.6	3,204.8
June	3,182.4	3,260.5	3,676.4
July	2,998.2	3,510.7	3,998.4
August	3,261.8	3,294.0	3,485.5
September	2,559.7	3,266.3	3,681.5
October	3,038.6	3,637.1	3,434.6
November	2,958.2	3,337.3	3,427.5
December	3,186.5	4,355.2	4,460.2
Total	36,770.4	40,174.8	42,901.1

*Preliminary

9 FINANCIAL STATEMENTS FOR 2003

Table 40 Balance Sheet as of December 31, 2003

	2002	**2003**
ASSETS		
Gold	215,898,246	237,045,638
Receivables and securities in foreign currency	721,096,834	670,750,885
Advance account central government	29,203,216	-
Government bonds	114,749,879	110,587,021
Other long-term receivables	23,607,648	23,320,911
Fixed assets	102,625,692	99,908,905
Other current assets	20,266,822	23,093,455
Total assets	1,227,448,337	1,164,706,815
LIABILITIES		
Bank notes in circulation	284,760,076	275,939,166
Residents' current accounts		
- in guilders	425,420,723	491,466,877
- in foreign currency	41,390,513	43,222,357
Residents' time deposits		
- in guilders	219,500,000	77,700,000
Nonresidents' current accounts		
- in guilders	2,240,000	552,634
Money in custody	981,113	981,113
Other current liabilities	16,428,434	17,266,962
Undistributed earnings	16,127,740	17,346,044
Special reserves	160,599,738	180,231,662
Reserve fund	30,000,000	30,000,000
Capital	30,000,000	30,000,000
Total liabilities	1,227,448,337	1,164,706,815

The 2002 en 2003 figures are preliminary and unaudited.

Table 41 Profit and Loss Account 2003

	2002	2003
INCOME		
Interest income	32,602,485	28,750,083
Foreign exchange earnings	1,013,367	1,118,732
Miscellaneous earnings	3,973,335	5,003,142
Subtotal	37,589,187	34,871,957
License fee	40,099,046	42,841,063
Total income	77,688,233	77,713,020
EXPENSES		
Interest expenses	5,643,278	2,680,778
Depreciation of fixed assets	4,196,980	5,119,766
Depreciation of printing costs bank notes	383,397	350,323
General expenses	26,378,497	25,460,383
Total expenses	36,602,152	33,611,250
Operating profit	41,086,081	44,101,770
Extraordinary income/loss	-172,086	-
Net income	40,913,995	44,101,770
Distribution of net income:		
Net income	40,913,995	44,101,770
Paid to the central government	-40,298,000	-42,883,466
Change in undistributed earnings	615,995	1,218,304

The 2002 and 2003 figures are preliminary and unaudited.

9.1 Notes to the balance sheet as of December 31, 2003

9.1.1 Gold

Gold is valued at the average market price in the three years preceding the date of valuation. Gold is revalued every year. Unrealized gains from revaluations are added to the special reserves after approval by the Minister of Finance. Unrealized losses are deducted from the special reserves. If these losses are greater than the reserves, the difference will be deducted from the result.

9.1.2 Receivables and securities in foreign currency

The receivables represent balances in current account and time deposits with foreign financial institutions. The securities represent investment portfolios. These are valued at market price. Unrealized gains from revaluations are added to the special reserves after approval by the Minister of Finance. Unrealized losses are deducted from the special reserves. If these losses are greater than the reserves, the difference will be deducted from the result.

9.1.3 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. The advance account is not interest-bearing. As per ultimo 2003 there was no amount outstanding.

9.1.4 Government bonds

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

9.1.5 Other long-term receivables

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

9.1.6 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.

9.1.7 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.

9.1.8 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.

9.1.9 Residents' current accounts

These include the balances in current accounts 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.

9.1.10 Residents' time deposits

These include the balances in time deposits (i.e., certificates of deposit) of domestic banks and government institutions. The balances are interest-bearing.

9.1.11 Nonresidents' current accounts

This amount represents the balances in current accounts 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.

9.1.12 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).

9.1.13 Other current liabilities

This balance includes accrued interest and accounts payable.

9.1.14 Undistributed earnings

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

9.1.15 Special reserves

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.

Unrealized gains from revaluations are added to the special reserves after approval by the Minister of Finance. Unrealized losses are deducted from the special reserves. If these losses are greater than the reserves, the difference will be deducted from the result.

The 2003 revaluation resulted in a net increase in reserves of NAf.19.6 million. Gold and foreign exchange recorded unrealized gains of NAf.21.1 million and NAf.0.1 million, respectively, while investments recorded an unrealized loss of NAf.1.6 million.

9.1.16 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).

9.1.17 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).

9.2 Notes to the profit and loss account 2003

9.2.1 Interest income

Interest income is generated mainly from government bonds, gold investments, and securities in foreign currency.

9.2.2 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.

9.2.3 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 1% 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.