ANNUAL REPORT 2006

Bank van de Nederlandse Antillen

1 REPORT OF THE PRESIDENT

1.1 General review

Despite the firm growth in private sector expenditures, the economy of the Netherlands Antilles grew at the same pace in 2006 as in 2005. In both years, the expansion in real Gross Domestic Product was estimated at 1.5%. Both investment and consumption contributed to the growth in private expenditures. Private investment growth remained strong, backed by the expansion in business loans and mortgages. The growth in private consumption was attributable to more consumer credit, increased employment, and the further reduction of the income tax. The expansion in private spending was dampened by a decline in net foreign demand because the growth in imports -- stemming from strong private demand and high fuel prices -- exceeded the growth in exports. In addition, the growth in government spending slowed considerably as a result of a decline in consumption and a slower growth in investment.

The economic recovery that started in 2001 was finally translated into an improvement of the labor market, reflected by a decline in the weighted average unemployment rate of the Netherlands Antilles from 16.2% in 2005 to 13.2% in 2006. The decline in Curacao's unemployment rate in particular contributed to this improvement. The inflation rate declined to 2.9% in 2006, after peaking at 3.8% in 2005. The deceleration in inflation was accounted for mainly by the moderation in global oil prices, contributing also to the lower inflation of our principal trading partners.

An analysis of the economic growth by sector shows that the construction, wholesale & retail trade, and financial services sectors were the primary contributors to the economic expansion in 2006. The increase in construction activities stemmed particularly from tourism-related investment projects. The strong performance of the wholesale & retail trade sector was caused by higher domestic spending and more activities in the free zone and tourism industry. The financial sector continued to perform well, accounted for by both the domestic and international financial services industry. The domestic banking industry recorded a further expansion in assets -- largely due to the increase in the loan portfolio -- and profitably. However, the increase in nonperforming loans serves as a reminder that there is no substitute for prudence in credit extension. Capitalization strengthened, but earnings came somewhat under pressure, as a result of increased competition among local banks. Activities in the international financial and business services sector improved somewhat after 2005's decline. The near term outlook for the sector looks brighter because the number of tax information exchange agreements and tax treaties under negotiation as well as concluded is increasing. These agreements and treaties are expected to create new business for the sector since the introduction of the adjusted new fiscal framework (NFR) in 2002.

Tourism activities grew moderately, reflected also by the expansion in the hotels & restaurants sector. The growth was attributable entirely to stay-over tourism because the number of cruise tourists remained unchanged. Curacao contributed primarily to the overall growth in tourism, followed by Bonaire, reflected by an expansion in the number of stay-over and cruise tourists on both islands. St. Maarten seems to have reached its limit for the number of stay-over tourists it can accommodate as it did not show any growth in 2006. However, the expansion of the number of available rooms is expected to support an increase in stay-over tourism in 2007. Moreover, the number of cruise tourists visiting St. Maarten declined.

Both the transport, storage, & communication sector and the manufacturing sector recorded a growth again after a decline in the two previous years. In line with the growth in stay-over tourism, total passenger traffic at the airports expanded. This development was helped also by the arrival of new carriers, now filling completely the void left by the closure of the national airline, DCA, in October 2004. In addition, the amount of freight handled and the number of ship calls in the harbors increased, except in Bonaire.

The improvement in the manufacturing sector was backed by more activities in the oil and ship repair industries. The operational costs of the Isla refinery increased due mainly to maintenance projects. The high international oil prices and the global shortage in refining capacity prompted the island government of Curacao to start negotiations with the current lessee, the Venezuelan oil company PDVSA, and a third interested party on the privatization of the refinery. Given the considerable investments required to modernize the refinery's plants to meet international product and environmental standards, it is imperative in the selection of a third party that we be guided by a party with access to capital, technology, and crude supply. The current international environment together with the increasing interest in the exploration of carbon hydrates in our waters should strengthen our hands in the negotiations with PDVSA and an eventual third party. However, to make progress in the field of exploration, it is essential for the parliament to enact the necessary legislation to provide the legal framework within which eventual exploration will take place.

The ship repair industry recorded an expansion in the number of man-hours sold. Despite the continued growth in repair jobs and a well-filled order portfolio, the financial position of the industry's main company, the government-owned Curacao Dry Dock Company, deteriorated further. The shortage of working capital, obsolete equipment, and various outstanding claims require a substantial capital injection to secure the company's long-term viability. Therefore, we should step up the efforts to privatize the dry dock company as soon as possible.

The balance of payments improved for the sixth consecutive year in 2006, reflected by an increase in net international reserves compared to 2005. The improvement was the result of large capital inflows related to the external financing of the private sector and development aid, offsetting the deterioration of the current account. Nevertheless, the import coverage dropped from 2.4 to 2.3 months because merchandise imports increased more rapidly than official reserves, i.e., the reserves with the Bank.

The current account deficit deteriorated significantly in 2006, due mainly to the worsening of the trade balance. Merchandise imports outpaced exports, the result of high international oil prices, stronger growth in domestic spending, higher re-exports by free- zone companies, and the growth in tourism. The growth in merchandise exports stemmed primarily from increased earnings from bunkering due to the higher average oil prices, the gain in free zone re-exports, and more ship repair activities. In addition, the current transfers balance deteriorated considerably as a result of much lower dividend tax transfers by the Dutch tax authorities related to the tax arrangement for the Kingdom (BRK) in contrast to the windfall in 2005. The worsening of the trade and current transfers balances was mitigated by an improvement of the services and income balances. The improvement of the services balance was attributable to the favorable development in tourism, an increase in construction services provided to nonresidents, and more payments received for maintenance work at the refinery. The improvement of the income balance can be explained by an increase in dividend and interest income from abroad, the latter related to the higher international interest rates.

Because the higher deficit on the current account was financed externally, the private sector's net foreign indebtedness increased, indicating a decline in net foreign wealth. The increased indebtedness was due to the deterioration of the loans and credits balance and the portfolio investment balance, offset partially by an improvement in the direct investment balance. The deterioration of the loans and credits balance was mainly the result of a decline in resident companies' bank balances abroad, related to, among other things, a takeover in the financial sector. Moreover, the portfolio investment balance worsened largely due to the repatriation of funds invested in foreign securities by a local institutional investor. These funds were used to finance a foreign participation and acquisition, explaining part of the improvement of the direct investment balance. The latter improved also because of the purchase by a local bank of a local insurance company from its foreign parent.

The government finances deteriorated in 2006, associated mainly with significantly smaller receipts related to the BRK compared to the windfall in 2005. Together with fewer dividend remittances from public companies, the smaller BRK receipts resulted in a substantial decline in revenues. In contrast, tax revenues increased as a result of higher indirect taxes in line with stronger domestic spending. Expenditures decreased also, accounted for entirely by the decline in current expenditures. Lower transfers by the central government to other government levels and lower expenditures for wages and salaries by the island government of Curacao were the main contributors to this decline. The lower expenses on wages and salaries were caused by fewer contributions paid by the island government to the government pension fund, APNA, compared to a make-up of arrears financed with the BRK windfall in 2005. In contrast, capital expenditures increased due to the financing of a golf course for a major hotel project by the island government of Curacao.

Because revenues declined more than expenditures, the general government's[1] cash deficit increased, contributing to a further accumulation of debt to 85% of GDP in 2006. Clearly, a debt ratio of this size is unsustainable. The accompanying interest burden is absorbing an increasing part of tax revenues, reducing the government's spending autonomy. Moreover, without clear prospects for a structural reduction of the debt ratio, investors became increasingly reluctant to finance the government, aggravating the fiscal situation.

The strong growth in the monetary aggregates continued in 2006, accounted for by domestic as well as foreign factors. The expansion in net domestic assets was due to the expansionary impact of the private sector caused by sustained strong credit growth. All loan components on both the Leeward and Windward islands contributed to the growth, reflecting firm consumer and investment spending. In contrast, net credit to the government dropped due to the contractionary impact of both the central government and the island government of Curacao, occurring mainly as a result of the reduction by the commercial banks of their government securities portfolio. The reduction in government securities freed funds for expanding credit to the private sector. The expansion in net foreign assets resulted from the surplus on the balance of payments and the annual revaluation of the gold stock.

Following 2005, the Bank continued tightening its monetary policy during the first quarter of 2006 by raising the reserve requirement percentage two times reaching 13.0% as of March 16. These raises were warranted by the strong growth in private sector credit, the declining trend in official reserves, and shortfalls in mopping up bank liquidity through the auctioning of certificates of deposit (CDs). As of the second quarter, the Bank did not actively deploy its monetary policy instruments in light of an adequate level of official reserves and import coverage, a slight deceleration in private credit growth, and successful CD auctions. Furthermore, the Bank increased the pledging rate four times during 2006 reaching 5.5% as of June 30. These increases were a reaction to the further rise in US interest rates, given its impact on the local money and capital market.

[1] The central government and the island government of Curacao combined.

1.2 Policy considerations

The preparations for the new constitutional status of the islands of the Netherlands Antilles within the Kingdom of the Netherlands dominated the political agenda in 2006. The three small islands, Bonaire, St. Eustatius, and Saba, which chose to become extraordinary municipalities of the Netherlands, made considerable progress, reaching a political agreement with the Dutch government in October 2006. On the other hand, the two larger islands, Curacao and St. Maarten, which chose to become autonomous countries within the Kingdom, booked much less progress. Intra- and inter-island political dissension hampered the start of effective negotiations for months. When finally an agreement was reached in November 2006, the Island Council of Curacao could not reach a majority to ratify the agreement causing a change in the ruling coalition. The members that voted against it believed that it would not provide the desired degree of autonomy for the future of Curacao.

Since the agreements include major debt relief and support for social-economic development to provide a sound starting position for the islands in the new constitutional arrangement, uncertainty rose as a result of Curacao's refusal. The financial institutions became more cautious in financing the government, reflected by shortfalls in subscriptions on bond issues, a preference for shorter maturities, and rising yields. In this context, the Bank wants to emphasize again that for a lasting improvement of our public finances a major debt relief is indispensable. With the rising debt level and interest burden, the budgetary room to make policy is diminishing, reflected by an erosion of public services, such as education, health care, safety, infrastructure, and support for the poor. Put differently: the authorities' autonomy to design and implement desired policy programs is undermined by a lack of funds, aggravated by the dependency on the willingness of the financial institutions to continue to refinance maturing debt and finance the budget deficit. A swift and comprehensive solution of the debt problem will go a long way toward regaining this autonomy, and the Dutch government offers such a solution.

The political parties of Curacao that were against the agreement with the Dutch government formed a new government and established a commission to draw up an alternative for the agreement. After careful analysis of the recommendations of the commission, presented at the end of March 2007, it must be concluded that they are not a feasible alternative to the Dutch proposal. The commission's debt solution leans heavily on assumptions regarding privatization, refinancing at more favorable terms, and responsibility for part of the debt. Privatization takes time while the ultimate cash pay out to redeem part of the debt depends on the outcome of the negotiations and is, therefore, uncertain. Refinancing part of the debt at more favorable terms with a US Treasury zero coupon bond as collateral will not generate the envisaged interest savings, because the US interest rate level is much higher and, hence, the interest rate differential between local and US government securities has become much smaller than some years ago when this proposal would have been feasible. Finally, the commission advised to ignore the debt of the central government after its dismantlement. This recommendation will have far reaching consequences for the government pension fund, APNA, and the social security bank, SVB, in addition to undermining confidence in the government. In short, the commission's recommendations will not contribute to a swift and comprehensive solution of the debt problem and, hence, will not create the sound public finances necessary for a successful start of the new constitutional status.

In the meantime, the preparations for a new constitutional structure continued without Curacao. In February 2007, the other islands and the central government concluded a transition agreement with the Dutch government that included the date the new constitutional status will become effective (December 15, 2008), steps to be taken to fully prepare for the new status, and details regarding support for the social-economic initiatives and debt relief. The Dutch government will start with a phased debt takeover from the entities as soon as the supervision on the budgetary process is in place. In addition, extra support has been made available to address some urgent issues in the fields of poverty alleviation and health care. However, in working out the details on supervision, the islands have found that the Dutch proposal undermines the democratic process in the budget cycle. In this respect, the Bank calls upon the parties involved to arrive swiftly at a mutually acceptable solution so that the crucial takeover of the debt can go into effect. Prospects are that Curacao will join this process as soon as the new government that took office after the April 2007 elections approves the agreement of November 2006.

The Bank's monetary policy stance remained neutral during the first half of 2007. The adequate level of official reserves, moderate first-quarter private sector credit growth, and generally successful CD auctions did not warrant a change in the reserve requirement percentage, leaving it at 13.0%. In addition, the Bank's pledging rate remained at 5.5% as US interest rates remained stable. The likely start of the debt takeover by the Dutch government in the second half of 2007 will result in large inflows of euros, posing a major challenge for the Bank's monetary policy. Although a further strengthening of reserves is welcome, our economy can only partially absorb such a flood of liquidity. Therefore, the Bank is revising the investment rule for institutional investors, allowing for more investments abroad.

The economic prospects for 2007 look favorable. Various current and soon-to-be-started projects, particularly in the tourism sector, will contribute to a further growth in investments. Through timely training of job seekers, we can maximize the benefits for our economy of the extra employment created by these projects, further reducing the unemployment rate. The structural solution of the debt problem creates prospects for lasting sound public finances, generating more budgetary room for better education, crime reduction, strengthening of our infrastructure, neighborhood improvement, and the reduction of poverty. The realization of these policy objectives will be expedited by the social-economic initiatives designed for each island with Dutch support, aimed at creating a climate conducive to durable economic growth. The number and complexity of issues that must be addressed to fulfill the new constitutional structure may be overwhelming, but by working decisively according to an ambitious but realistic agenda, our decision makers together with their Dutch counterparts, should make considerable progress in meeting the target date of December 15, 2008, to enter a new prosperous future for each island.

E.D. Tromp
President

2 INTERNATIONAL ECONOMIC DEVELOPMENTS

Real GDP growth in the US economy was 3.3% in 2006, relatively similar to that in 2005 (see Table 1). Despite a slowdown in the housing market, economic activities in the United States were supported by strong consumption, continued employment growth, and low long-term interest rates. Growth in consumer spending was sustained by favorable financial conditions and robust labor income growth, outperforming the dampening effect of slow increases in housing wealth. Despite improvements in the trade balance, the US current account deficit remained large and steady at 6.5% of GDP during 2006. The labor market continued to improve as job losses in manufacturing and residential construction were more than offset by gains in other sectors. As a result, the unemployment rate dropped to 4.5% in 2006, close to a five-year low. Lower energy prices somewhat dampened the inflationary pressures, leading to a deceleration in consumer prices (3.2%) during 2006. In spite of a slowdown in consumer prices, inflation risk remained a concern. Therefore, the Federal Reserve did not lower the Fed funds rate further and has kept it steady at 5.25 percent since June 2006.

Table 1 Selected economic indicators of main trading partners (% change)

	United States			Netherlands			Venezuela		
	2004	**2005**	**2006**	**2004**	**2005**	**2006**	**2004**	**2005**	**2006**
Real GDP	3.9	3.2	3.3	2.0	1.5	2.9	18.3	10.3	10.3
Consumer prices (%)	2.7	3.4	3.2	1.2	1.7	1.1	21.7	16.0	13.7
Unemployment rate (%)	5.4	4.9	4.5	6.5	6.5	5.5	10.9	8.9	8.4

Source: US Bureau of Economic Analysis, US Bureau of Labor Statistics, Dutch Central Bureau of Statistics, Banco Central de Venezuela, and Instituto Nacional de Estadistica Venezuela.

In the Netherlands, real GDP growth strengthened by 2.9% in 2006, almost twice the increase in 2005. Exports, household consumption, and private investment were the driving forces of the economic growth. Higher exports were led mainly by re-exports of goods to the EU countries, largely to Germany and Belgium. In addition, more private investment was sustained by both residential and nonresidential investments, the latter being supported especially by a growth in equipment and computers. Increases in private domestic demand and foreign demand resulted in more activities in all sectors, but mostly in the commercial services, financial & business services, and construction sectors. For the first time in six years, the Dutch government realized a budget surplus, lowering the debt-to-GDP ratio by 4 percentage points to 48.7% in 2006. The reduction in national debt was related to the sale of government shares and a rise in central government tax revenues, the latter the result of more economic activities. The reduction in consumption-related taxes and government services and slowing energy prices kept the inflation rate in check at 1.1%, the lowest level since 1989. Throughout 2006, more jobs were created, leading to a decline in unemployment in all age categories, and a lowering of the general jobless rate to 5.5%.

Overall, the Venezuelan economy continued to expand at a robust pace of 10.3% in 2006, backed by the buoyancy in trade (19.9%), construction (32.1%), manufacturing (10.4%), and financial services (39.2%). Domestic demand continued to expand at a relatively rapid pace, spurred by high fiscal spending amid a windfall in revenue from oil sales. The government used its record revenues from the oil boost for increasing outlays on health, food, and education programs. These social programs fueled consumer spending, causing prices to rise because domestic production could not keep up. Moreover, a mix of price and currency controls accompanied by soaring spending drove up prices and exacerbated the food shortages. As a result, Venezuela has the highest pace of consumer price increases in Latin America. The growing oil income allowed the government to fund labor cooperatives and work-training programs, which created more public sector jobs. Consequently, Venezuela's jobless rate (8.4%) fell to its lowest since January 1999. The increasing oil prices widened Venezuela's current account surplus further by 6.4% to $27.2 billion in 2006.

3 GENERAL ECONOMIC DEVELOPMENTS IN THE NETHERLANDS ANTILLES

3.1 Introduction

Since the economic rebound in 2001, the economy of the Netherlands Antilles has not been growing by more than 1.5% per year. Again in 2006, the Netherlands Antillean economy remained steady, with GDP expanding at an annual rate of 1.5%. This stable growth was backed by more domestic economic activities mainly in the private sector (see Table 2). In contrast, the deficit in net exports had a dampening impact on GDP growth, as imports grew at a much faster pace than exports. The retreat of oil prices on international markets limited the inflationary pressures, resulting in a lower inflation rate of 2.9% in 2006. Notwithstanding the relatively subdued economic growth, the labor market improved, as the unemployment rate fell to 13.2%[2] in 2006, its lowest since 2000.

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

	2004	2005	2006
Domestic expenditures, of which:	1.2	4.8	4.0
Private sector	0.4	3.6	3.8
- Investment	0.2	2.4	2.5
- Consumption	0.2	1.2	1.3
Government	0.7	1.3	0.2
- Investment	-0.9	1.4	0.7
- Consumption	1.7	-0.1	-0.5
Changes in inventory	-0.1	0.1	0.0
Foreign net expenditures, of which:	0.0	-3.4	-2.5
Export of goods and services	6.0	1.2	3.4
Import of goods and services	6.0	4.6	5.8
GDP by expenditures	1.1	1.5	1.5
Net primary income	-0.3	0.4	0.5
Gross national income	1.0	1.9	2.1
Net current transfers from abroad	0.1	0.8	-2.0
Gross national disposable income	1.1	2.7	0.1

Source: BNA estimates.
[a] Expenditure categories data are weighted contributors to GDP growth.

Among the domestic expenditure components, growth in private demand and public investment contributed to the GDP growth in 2006. The rise in private consumption can be explained by the following factors: (1) more personal credit; (2) a rise in personal disposable income, due to a further reduction in the income tax; and (3) income growth from employment. Moreover, private investment growth continued to strengthen by 2.5% in 2006. Much of this good performance was backed by the expansion in mortgages and business loans. Conversely, net foreign demand contracted as higher import demand offset

[2] BNA estimate

export growth. Strong consumption and investment accompanied by high fuel costs increased both the prices and volumes of imports. The robust import growth was mostly due to gains in imports by the wholesale & retail, tourism, and construction sectors. Also, world oil prices continued to have an impact on the import bill, albeit to a somewhat lesser extent in 2006 than in 2005.

Throughout 2006, gross national income growth of the Netherlands Antilles remained relatively steady as net primary income from abroad showed only a slight increase. This slight gain, nonetheless, was outpaced by an expansion in total consumption and investment, leading to a contraction in national savings. This contraction resulted from a decrease in private savings as well as public savings. During 2006, higher private consumption was accompanied by a growth in both private and public investment. These higher levels of consumption and investment were sustained primarily through credit extension and foreign financing.

3.2 Domestic production

The economy of the Netherlands Antilles maintained its moderate performance during 2006, sustained by an expansion in the private as well as the public sector. At the sectoral level, the construction, wholesale & retail trade, and financial services sectors contributed primarily to the overall economic growth in 2006 (see Table 3). In addition, increased spending in the public sector was incurred by more outlays on wages & salaries. The construction sector continued to expand, benefiting particularly from tourism-related investment projects. Besides the surge in investment activity, the value of completed construction projects for residential as well as nonresidential purposes strengthened during 2006.

The real value-added growth in the wholesale & retail trade sector (2.0%) was caused by more activities in the free zone, tourism industry, and higher domestic spending. In contrast to the good performance in the free-zone, the number of free-zone visitors shrank, mostly in the Jamaican and the Dominican markets. The output in the financial services sector grew further, driven by both domestic and international financial services in terms of value added, but at a slower pace than in 2005.

In terms of real value added, activities in the hotels & restaurants sector expanded in 2006, owing to a 1.8% growth in stay-over visitor arrivals accounted for by the European, North American, and South American markets. The rise in the number of visitors from the European market may be connected to the marked depreciation of the US$ against the euro. The number of tourists from Europe rose by 4.9% in 2006, constituting 30.0% of total stay-over travelers. Moreover, the increase in visitors from the South American market was backed by the arrival of new carriers, which led to an increase in airlift. After a strong performance in 2005, cruise ship arrivals remained unchanged in 2006. Cruise tourism improved in both Curaçao and Bonaire, but was offset by the adverse results in St. Maarten.

An analysis by islands shows that stay-over tourism grew in Curaçao and Bonaire, while St. Maarten remained unchanged in 2006. Curaçao's main tourist markets, i.e., North America and Europe, contributed to the 5.5% increase in the island's stay-over tourism. By contrast, St. Maarten's stay-over tourism remained about the same after 2005's decline. After a weak performance in 2005, stay-over arrivals in Bonaire improved by 1.6%, which was accounted for by all markets, except the European. See Table 9 in the appendix for more details.

Table 3 GDP by sector (real percentage changes)

Sector	2004	2005	2006
Agriculture, fishery, & mining	2.7	1.7	2.6
Manufacturing	-2.5	-0.6	1.8
Electricity, gas, & water	0.8	0.2	0.3
Construction	2.5	4.5	5.1
Wholesale & retail trade	3.4	0.7	2.0
Restaurants & hotels	3.1	-0.6	1.7
Transport, storage, & communication	-2.1	-0.4	0.1
Financial intermediation	2.7	5.9	2.2
Real estate, renting, & business activities	0.5	-0.4	1.0
Private households	-3.1	-1.3	0.0
Total private sector	1.0	1.2	1.5
Public sector	0.0	3.6	1.6
GDP	1.1	1.5	1.5

Source: BNA estimates

During 2006, total value added in the manufacturing sector grew by 1.8%, backed by more activities in the oil and ship repair sectors. Both total operational costs of the "Isla" refinery and the number of man-hours sold in Curaçao's ship repair industry were up.

After several years of downturn, the transport, storage, & communication sector exhibited a slight growth in 2006, with gains in cargo movements across ports and air transportation. The expansion in the number of ships piloted into the harbors contributed also to the positive performance of the ports. The arrival of new carriers was able to fill the void left behind with the closure of the national airline, DCA, in October 2004. Furthermore, airport-related activities were up, stemming from a rise in total passenger traffic in the Netherlands Antilles. This outcome was in line with the favorable results in stay-over tourism and the air transportation sector.

3.3 Labor market

In spite of a modest GDP growth, the labor market conditions in the Netherlands Antilles posted a positive picture. The reduction in the number of unemployed was accompanied by a rise in the number of employed, resulting in a lower unemployment rate of 13.2%[3] in 2006 (see Table 4). The key explanation for the improvement of the labor market may be that the persons who migrated from the Netherlands in 2005 found employment in 2006. Moreover, the expansion in construction activities might have created more job opportunities in the construction sector. Labor productivity in Curaçao[4] turned around from a 2.0% growth in 2005 to a 7.3% drop in 2006 because of a decline in output produced per hour.

[3] BNA estimate.

[4] BNA estimate; AKO ("Labor force survey") 2006, Central Bureau of Statistics. Curaçao makes up about 70% of total employment of the Netherlands Antilles.

Table 4 Labor market developments in the Netherlands Antilles (number of persons)

	2002	2003	2004	2005	2006
Employed	70,629	74,245	74,777	76,212	80,120
Unemployed	12,114	13,439	13,282	14,748	12,214
Labor force	82,743	87,684	88,059	90,960	92,334
Total population	173,519	177,291	179,938	186,040	190,894
Participation rate	47.7%	49.5%	48.9%	48.9%	48.4%
Unemployment rate	14.6%	15.3%	15.1%	16.2%	13.2%

Source: Central Bureau of Statistics and BNA estimate

In 2006, the decline in Curaçao's unemployment rate to 14.7%[5] was the main reason for the lower jobless rate in the Netherlands Antilles. The lower unemployment in Curaçao was reflected also by a fall in the youth unemployment rate from 44.0% in 2005 to 37.6% in 2006. Despite an increase in the number of unemployed, Bonaire's jobless rate fell from 8.9% in 2004 to 7.8% in 2006. This improvement occurred because the number of employed grew at a faster pace than the number of unemployed, resulting in a larger labor force. The drop in the number of unemployed in Curaçao occurred largely among the male population. In 2006, the number of unemployed females in Curaçao declined by 6.4%, while the males' number shrank by 33.6%. In contrast, the number of unemployed females in Bonaire rose by 9.1%, whereas the males' number fell by 1.0% during the period 2004-2006.

In spite of a drop in the number of unemployed, the unemployment rate in the Netherlands Antilles continued in the double-digits, remaining a cause for concern. For the last two decades, the Netherlands Antilles has been suffering from a double-digit unemployment rate.

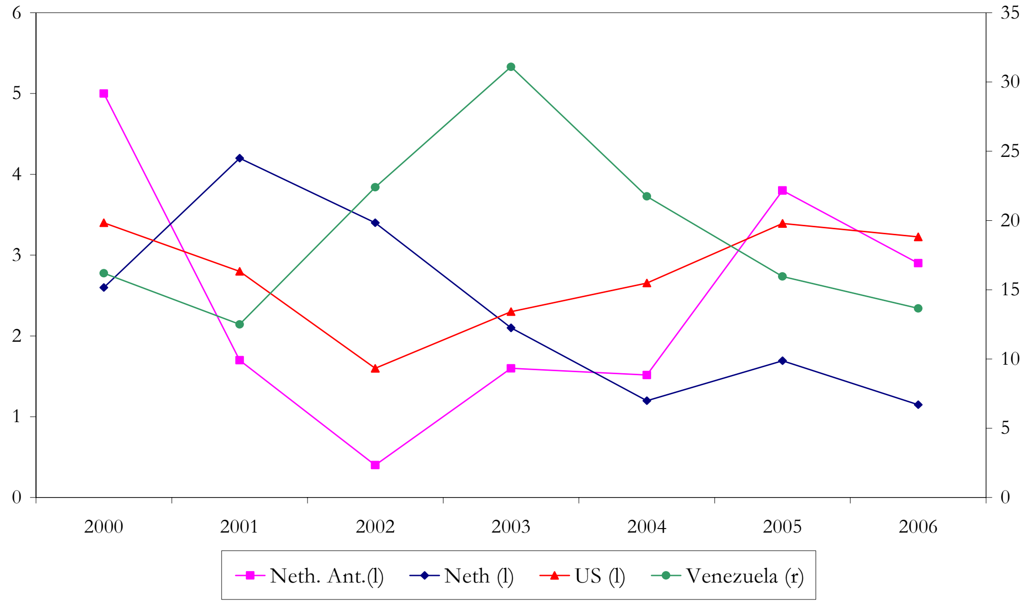
3.4 Inflation

With regard to price developments, consumer price inflation remained relatively benign in 2006 as global energy prices moderated. The annual inflation rate in the Netherlands Antilles eased somewhat from 3.8% in 2005 to 2.9% in 2006. Also, the lower inflation of our principal trading partners, the United States, the Netherlands, and Venezuela, contributed to the downward inflationary pressures. The main contributors to the lower inflation were the components "housing", "housekeeping & furnishings", and "transport & communication", due largely to a slowdown in energy prices and a decline in household costs. The changes in international oil prices were not reflected in domestic energy prices; gasoline and utility prices have remained unchanged since June 2005.[6] Meanwhile, the inflation trend was driven to a large extent by the categories "food" (7.2%), "beverages & tobacco" (3.7%), and "other" (2.0%). An analysis by islands shows that Curaçao registered the highest annual inflation (3.1%), followed by St. Maarten (2.3%), and Bonaire (1.3%). See Table 10 in the appendix for a detailed overview.

[5] AKO ("Labor force survey") 2006, Central Bureau of Statistics.

[6] Gasoline and utility prices in Curacao are set by the island government.

Graph 1 Developments in consumer prices (annual percentage change)



3.5 Public finances

3.5.1 Cash overview and financing

A revenue windfall in 2005 is the main explanation for the significant decline in revenues in 2006, forcing a reduction in public spending. Nevertheless, the deficit of the general government[7] on a cash basis deteriorated by NAf.35.1 million to NAf.189.6 million in 2006 because the drop in revenues outpaced the decline in expenditures (see Table 5). Government consumption increased as a result of higher wages and salaries, contributing partly to the GDP growth in 2006.

The primary balance (fiscal balance excluding interest costs) deteriorated also but remained positive indicating that the deficit was entirely the result of a high interest burden stemming from the unsustainable level of government debt.

[7] The general government is defined as the central government and the island government of Curacao.

Table 5 Selected key variables of the general government (in millions NAf.)

	2002	2003	2004	2005	2006
Revenues	1,250.4	1,346.7	1,349.1	1,616.2	1,485.6
% of GDP	23.8%	24.8%	24.2%	27.7%	24.4%
Tax revenues	1,124.7	1,140.2	1,204.9	1,251.8	1,284.1
Nontax revenues	84.2	129.9	107.9	151.5	110.71
Grants	39.1	64.5	35.3	212.8	89.8
Expenditures	1,467.3	1,589.5	1,690.2	1,770.7	1,675.2
% of GDP	27.9%	29.3%	30.3%	30.3%	26.9%
Current expenditures	1,416.1	1,505.4	1,625.5	1,749.6	1,635.6
Capital expenditures	51.2	84.1	64.7	21.1	39.6
Balance	-216.9	-242.8	-341.0	-154.5	-189.6
% of GDP	-4.1%	-4.5%	-6.1%	-2.6%	-3.1%
Primary balance	28.5	9.2	-84.2	130.0	93.8
% of GDP	0.5%	0.2%	-1.5%	2.2%	1.5%

A breakdown of general government revenues reveals that the drop in revenues was caused entirely by a drop in nontax and other revenues (NAf.162.9 million) in 2006. This drop was attributable mainly to a windfall in the transfers of dividend tax by the Dutch tax authorities to the central government related to the tax arrangement for the Kingdom of the Netherlands (BRK)[8] in 2005 that did not occur in 2006. These transfers amounted to NAf.194.9 million in 2005, compared to NAf.73.5 million in 2006. In addition, dividend remittances by government-owned companies declined.

A review by level of government shows that tax revenues of the central government, i.e., mostly indirect taxes, increased while those of the island government of Curaçao, relying more on taxes on income and profits, dropped. Higher domestic spending resulted in both higher sales tax revenues and import duties for the central government. The drop in tax revenues of the island government of Curaçao can be attributed to lower proceeds from profit and income taxes, due mainly to lower profit tax receipts from the international financial and business services sector.

A review of general government expenditures reveals that the drop in total expenditures was attributable entirely to current expenditures (NAf.114.0 million). A breakdown by level of government shows that the drop in current expenditures was accounted for by both levels of government. The drop in current expenditures of the central government was related to lower transfers to other government levels while the drop at the island government of Curaçao was caused by lower expenditures for wages and salaries due to fewer contributions paid to the government pension fund, APNA[9].

Contrary to the drop in current expenditures, capital expenditures of the island government of Curaçao increased due to an increase in net lending. As part of an agreement, the island government of Curaçao made financial resources available to finance the construction of a golf course for a major hotel project. Capital expenditures of the central government dropped by NAf.9.8 million in 2006 as the increase in investments was offset by decreases in net lending and capital transfers.

8 According to this arrangement, the withholding tax collected on dividends paid by Dutch companies to their parents in the Netherlands Antilles is transferred entirely to the Netherlands Antillean government.

9 In 2005, the island government used part of the windfall in revenues to reduce its arrears with APNA.

Similar to 2005, the cash deficit of the general government was financed entirely nonmonetarily in 2006. A breakdown by level of government reveals that the central government financed its cash deficit through increased holdings of government securities with the public. A contraction in government debt portfolios combined with higher deposit balances resulted in a monetary contraction through the commercial banks in 2006. The monetary financing through the central bank was due mainly to an expansion of the government securities portfolio.

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

	Central government		Curaçao government	
	2005	2006	2005	2006
Monetary financing	-15.6	-67.4	-20.0	-25.3
Central bank	13.4	16.3	-45.6	58.5
Commercial banks	-31.0	-85.2	25.6	-83.8
Coins and notes	2.0	1.5	0.0	0.0
Nonmonetary financing	94.7	155.4	95.4	126.9
Government securities with the public	93.1	180.9	56.1	140.7
Other	1.6	-25.5	39.3	-13.8
Cash balance	-79.1	-88.0	-75.4	-101.6

The island government of Curaçao financed its cash deficit in 2006 also through increased holdings of debt securities by the public. The monetary contraction resulted from the reduction of the government debt portfolios at the commercial banks. The monetary financing through the central bank was attributable mainly to a decline in deposits related to the drawdown of a time deposit created with the 2005 BRK windfall.

3.5.2 Public sector debt

The total consolidated public debt of the Netherlands Antilles expanded considerably in 2006 by NAf.320.2 million to NAf.5.2 billion, corresponding with 85.4% of GDP. The accumulation of debt was the result of an increase of NAf.224.0 million in the total consolidated domestic debt and an increase of NAf.96.2 million in the outstanding foreign debt. See Table 12 in the appendix for a detailed overview.

Further analysis reveals that net borrowing on the capital market by both the central government (NAf.88.3 million) and the island government of Curaçao (NAf.64.0 million) contributed mostly to the higher domestic debt. In addition, the debt of both the island government of Curaçao (NAf.38.6 million) and the central government (NAf.8.7 million) to the government pension fund (APNA) increased. The increase in debt of the other islands (NAf.22.2 million) was also due mostly to the accumulation of arrears with the government pension fund.

The increase in the foreign debt in 2006 was attributable mainly to the depreciation of the US dollar, to which the Netherlands Antilles guilder is pegged, against the euro. This depreciation caused a rise in the guilder-equivalent of the euro-denominated debt of approximately NAf.70 million.

3.6 Balance of payments developments

3.6.1 Introduction

In 2006, net foreign demand, i.e., net exports of goods and services, dampened the economic growth because the rise in the import of goods and services offset the increase in exports. The drop in net foreign demand combined with a worsening of the current transfers balance resulted in a current account deficit of NAf.483.1 million. Compared to 2005, the current account deficit rose by NAf.298.8 million in 2006. In line with the developments on the current account, the combined capital and financial account worsened. Due to strong net capital inflows, foreign exchange reserves increased, but by a smaller amount than in 2005 (see Table 7).

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

	2003	2004	2005	2006
Current account	4.5	-155.4	-184.3	-483.1
Capital transfers	46.1	142.2	171.1	179.6
Acquisition of nonproduced nonfinancial assets	0.8	0.0	0.0	0.0
External financing of the government	-26.7	4.6	-17.3	12.8
External financing of the private sector	56.5	10.2	45.5	317.0
- Direct investment *)	20.5	33.7	31.4	-16.0
- Loans and credits *)	29.4	-21.8	56.8	220.0
- Portfolio investments *)	6.6	-1.7	-42.7	113.2
Change in net foreign assets of banking system*)	-89.0	-66.1	-132.7	-84.3
- with commercial banks	-135.6	9.9	-63.9	-10.4
- with central bank	46.6	-76.1	-68.8	-73.8
Statistical discrepancies	7.8	64.6	117.8	58.0

*) a minus sign implies an increase in net foreign wealth

3.6.2 Current account

In 2006, the deficit on the trade balance widened by NAf.268.5 million compared to 2005 as merchandise import growth outpaced the rise in exports. In addition, high international oil prices fueled the increase in the import bill. The growth in merchandise imports was related to increased domestic spending, favorable developments in the tourism industry, and higher re-exports by the free-zone companies. Analysis by islands reveals that the growth in merchandise imports on the Windward Islands was due mainly to increased private consumption and construction activities in the tourism and transportation sectors. On the Leeward Islands, wholesale and retail sector imports posted a significant growth in 2006, led by higher domestic spending and an increase in tourism-related activities. A rise in imports by the free-zone companies to meet foreign and domestic demand also contributed to the growth in merchandise imports. Furthermore, the higher imports were related to the ongoing construction activities in the tourism sector and investments in the manufacturing industry, notably the refinery, and the transportation sector.

Merchandise exports in 2006 rose mainly as a result of increased earnings from bunkering activities due to higher average oil prices. Moreover, as mentioned, higher foreign demand led to a gain in re-exports by the free-zone companies in Curaçao, although at a slower pace than in 2005. In addition, foreign exchange receipts from ship repair activities rose, reflecting increased activities at the local ship repair company in 2006.

The deterioration of the trade balance was offset partially by an improvement in the services balance of NAf.128.5 million. This improvement was largely related to a rise in foreign exchange revenues from tourism on the island of Curaçao. In 2006, Curaçao's stay-over tourism performed particularly well, resulting in a NAf.52.8 million increase in stay-over tourism revenues compared to 2005. In addition, foreign exchange receipts from cruise tourism increased by NAf.8.4 million. On Bonaire, the foreign exchange revenues from cruise and stay-over tourism increased by NAf.3.3 million and NAf.3.9 million respectively. In contrast, tourism earnings declined slightly on the Windward Islands reflected by a drop in stay-over tourism receipts (NAf.5.7 million) and cruise tourism receipts (NAf.6.0 million).

In addition, earnings from construction services increased during 2006 mainly as a result of a rise in the construction of properties in St. Maarten owned by nonresidents. These construction activities were performed by local contractors. Furthermore, the refining fee paid by PDVSA for its operations in Curaçao increased mainly due to maintenance work that took place at the refinery during 2006.

These developments resulted in a decline of NAf.140.0 million in net exports of goods and services. Besides the drop in net exports of goods and services, the worsening of the current account balance was also related to a significant decline in net current transfers from abroad. This decline was due mainly to a large transfer of dividend tax by the Dutch tax service[10] in 2005, which did not occur to the same extent in 2006. As a consequence, the current transfers balance deteriorated by NAf.184.8 million in 2006.

In contrast, the income balance improved by NAf.25.9 million, largely due to dividend income received by a domestic bank from its subsidiary in Aruba. Furthermore, interest income earned by local banks on their foreign deposits increased in 2006 owing to the higher interest rates abroad. Overall, the current account deficit increased by NAf.298.8 million to NAf.483.1 million in 2006. See Table 13 in the appendix for a detailed overview.

3.6.3 Financing of the current account balance

Due to the higher current account deficit, the net foreign wealth of the private sector declined considerably by NAf.317.0 million during 2006. The change in the financing of the private sector was related to a deterioration of the loans and credits balance and the portfolio investment balance, offset partially by an improvement in the net direct investment balance.

The loans and credits balance worsened by NAf.220.0 million due mainly to a decline in the balances of resident companies' bank accounts abroad. This development was related to, among other things, the financing of the take-over of an international bank previously a subsidiary of a Dutch company, by a local institutional investor. In addition, foreign assets were repatriated to fund an international credit institution in the Netherlands Antilles. The worsening of the loans and credits balance was mitigated by the repayment of loans abroad by private companies. Furthermore, trade credits extended abroad grew in 2006, stemming from an increase in merchandise exports. As the trade credits extended offset the trade credits received from abroad, net trade credits extended increased.

Net portfolio investments declined by NAf.113.2 million largely due to the repatriation of funds invested in foreign bonds and notes by a local institutional investor. These funds were used mainly to finance the direct investment in a company abroad and the aforementioned

[10] This transfer was related to the tax arrangement for the Kingdom of the Netherlands Antilles (BRK).

acquisition of an international bank, explaining part of the improvement in the net direct investment balance by NAf.16.0 million.

The improvement in the net direct investment balance was also linked to the purchase by a local bank of a local insurance company that was previously foreign-owned. However, an increase in claims of foreign direct investors in the Netherlands Antilles partially offset the improvement in the net direct investment balance. The increase in claims was related to, among other things, investments in the oil terminal on the island of St. Eustatius and construction activities in the tourism sectors of Curaçao and St. Maarten. Capital transfers increased by NAf.8.5 million during 2006 due to an increase in development aid funds received from the Netherlands.

As a result of the high capital inflow during 2006, net foreign assets (i.e., international reserves) increased by NAf.84.3 million compared to 2005, reflecting a surplus on the balance of payments. See Table 14 in the appendix for more details.

3.7 Monetary developments

3.7.1 Monetary policy

During the first quarter of 2006, the Bank's monetary policy was directed mainly towards curbing the excessive increase in private credit extension[11], which was exerting increasing pressure on the official reserves. To achieve this, the Bank increased the reserve requirement percentage[12] on two occasions, from 12.25% to 12.75% in January and to 13.0% in March. As of the second quarter of 2006, monetary developments did not warrant a further tightening of policy. As a result, the reserve requirement percentage remained unchanged for the rest of the year.

The reserve requirement instrument is complemented with bi-weekly auctions of Certificates of Deposit (CDs) for the local commercial banks to mop up excess liquidity in the domestic money market. In contrast to the reserve requirement, this instrument is more market-oriented, as participation in the auctions is voluntary and at competitive terms. This instrument was implemented more actively during the first half of 2006. As a result, the amount of outstanding CDs doubled from NAf.22.0 million at the end of 2005 to NAf.45.0 million at the end of June 2006. Similar to the increases in the reserve requirement percentage, the higher amounts of CDs offered by the Bank were to curb the excessive credit extension to the private sector. During the second half of the year, the Bank aimed mainly at rolling over the maturing CDs. At the end of 2006, the amount of outstanding CDs reached NAf.48.6 million.

The Bank's official interest rate, i.e., the pledging rate, was raised on four occasions during 2006. In the months of February, March, May, and June, this rate was increased each time by 25 basis points, finally reaching 5.50% as of the end of June. These increases can be explained as follows. Since the yield on CDs auctioned by the Bank must be competitive with alternative investments abroad, the Bank had to offer higher rates on its CDs following the increase in foreign interest rates. To avoid interest arbitrage, the Bank had to ensure that the increases in its CD rates were accompanied by increases in the pledging rate.

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[11] Credit extension is considered excessive when its growth rate is increasingly above that of the projected nominal growth in GDP.

[12] Under the reserve requirement policy, the commercial banks are obliged to maintain a certain percentage of their domestic deposits in a blocked account at the Bank. This percentage is determined on a two-month basis.

3.7.2 Net accumulation of wealth and the money supply

Despite a decline in private net savings, related to the solid growth in private spending, private sector money holdings increased by NAf.491.7 million in 2006, NAf.68.2 million more than in 2005 (see Tables 15A and 15B in the appendix). The increase in money holdings in 2006 stemmed from significant increases in domestic bank credit, external financing, and capital transfers from abroad, mitigated by the financing provided by the private sector to the government.

3.7.3 Factors affecting the money supply

The money supply increased by 10.0% in 2006, slightly more than the 9.4% growth in 2005. Domestic as well as foreign factors contributed to the expansion in 2006. Net domestic assets expanded by 10.5%, due to an increase of 17.6% in net credit extension to the private sector. Net credit extended to the government sector dropped by 8.4%. Net credit to the private sector increased primarily due to an increase in commercial bank loans extended (13.1%) as private consumption and investment continued to expand. The expansion in private loans was the result of increases in all loan components on both island groups. Worth mentioning is that the largest increase came from business loans extended on the Leeward Islands.

Contrary to the expansion in private credit extension, net credit extended to the governments dropped during 2006. In 2005, a negligible increase of 0.1% was recorded. The 2006 result was accounted for by a drop in net credit extended to both the central government (9.9%) and the island government of Curaçao (5.7%). The drop in net credit extended to the central government resulted mainly from a decrease in central government securities in the commercial banks' portfolios, offsetting the increase of these securities in the Bank's portfolio. The decline in credit extended to the island government of Curaçao came also from a decrease of securities in the commercial banks' portfolios. This decrease even offset the drop in deposit balances, the result mainly of a time deposit withdrawal at the Bank (NAf.50.0 million).[13]

Net foreign assets expanded by 8.9%, a deceleration compared to the increase of 11.4% in 2005. The expansion in 2006 resulted from increases in both the commercial banks' net foreign assets position (12.0%) and the Bank's official reserves (2.1%). See Table 16 in the appendix for a detailed overview.

3.7.4 Developments in domestic interest rates

The increases in the Bank's official rate, i.e., the pledging rate, and the maximum 1-month CD rate were related to the increases in international rates. The CD rates had to increase to remain competitive with alternative investment instruments, while the pledging rate had to be raised to avoid interest arbitrage.

The average rate on passbook savings remained unchanged at 2.8% for the third consecutive year, while the average rate on 12-month time deposits recorded only a marginal increase of 0.1 percentage point to 4.2% during 2006. The average mortgage rate dropped further by 0.1 percentage point to 8.5% and the average rate on time loans fell by 0.2 percentage point to 10.6% in 2006. In contrast to the average borrowing rates, the average lending rates

[13] This time deposit was related to the windfall from the dividend tax transfer from the Netherlands in April 2005.

continued a decreasing trend, indicating the increased competition between the domestic commercial banks.

Both the average effective yield of 5 year government bonds and 1 month treasury bills increased during 2006 compared to 2005. This development was in line with the trend of increasing reticence with local investors, forcing the government to increase the attractiveness of its securities by offering a higher return. See Table 17 in the appendix for more details.

3.8 Developments in the commercial banking sector

3.8.1 Balance sheet and income statement

Total assets of the domestic commercial banks expanded by 8.8% during 2006, a deceleration compared to the growth of 33.0% in 2005.[13] The increase in assets in 2006 was attributable primarily to the expansion of the loan portfolio (11.6%) and the increase in interest-bearing cash (24.1%). Noteworthy is the decline in investments (26.9%) related partly to the sale of government bonds by a local bank to finance its investment in unconsolidated subsidiaries, the balance sheet item of which increased by NAf.170.7 million.

The aggregate income statement illustrates also a slower growth in income and expenses in 2006 compared to 2005.[14] Because operational income (3.7%) grew faster than operational expenses (2.0%), supported by higher extraordinary revenues, aggregate net income after taxes of the domestic commercial banks increased further by 11.4% to NAf.194.2 million.

3.8.2 Macroprudential indicators

The general performance of the commercial banking sector is analyzed by means of the macroprudential indicators. The capital adequacy, as measured by the ratio of total capital against total assets, increased significantly in 2006. This ratio improved as a result of the increased capitalization and general provisions, surpassing the growth in total assets.

The ratio of nonperforming loans-to-total loans increased during 2006, revealing a worsening in the quality of the asset base. This is also revealed by the decrease in the provisions for loan losses-to-nonperforming loans ratio. Both these developments can be explained by the increase in nonperforming loans, which exceeded the growth in both total loans and provisions for loan losses.

All three earnings-related indicators reveal a deterioration in 2006 compared to 2005. This deterioration can be explained by the fact that for all ratios assets grew faster than the income component, which may be the result of stiffer competition in the local banking sector. The ratio of total loans against total deposits rose during 2006. This development reveals a decrease in liquidity in the domestic banking sector.

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[14] Related to the acquisition by a domestic commercial bank of a foreign subsidiary in 2005.

Table 8 Macroprudential indicators (in %, end of period)

	2003	2004	2005	2006
Capital adequacy				
Total capital/ total assets	7.2	7.9	7.9	9.3
Asset quality				
Nonperforming loans/ total loans	5.9	3.6	2.6	3.6
Provisions for loan losses/ non-performing loans	61.1	92.7	106.0	87.3
Earnings				
Gross earnings-assets yield	7.4	7.3	7.5	7.1
Net interest margin	4.7	4.9	5.1	4.5
Return-on-assets	1.5	1.7	2.3	2.2
Liquidity				
Total loans/ total deposits	66.3	64.9	61.9	64.2

APPENDIX

Table 9 Developments in stay-over tourism per island (% change)[a]

	Curaçao				St. Maarten				Bonaire			
	2005		2006		2005		2006		2005		2006	
North America, of which:	6.9	(0.5)	8.4	(0.6)	-0.5	(-0.2)	-1.7	(-0.6)	-4.6	(-0.2)	6.7	(0.2)
-U.S.A.	5.0	(0.3)	4.7	(0.3)	-1.7	(0.6)	-0.3	(-0.1)	-4.7	(-0.2)	5.6	(0.2)
Europe, of which:	5.8	(0.7)	9.8	(1.3)	-2.7	(-0.3)	3.5	(0.4)	7.5	(0.3)	-6.2	(-0.2)
-The Netherlands	5.5	(0.6)	9.5	(1.1)	-0.7	(0.0)	2.6	(0.1)	6.0	(0.2)	-6.9	(-0.2)
South & Central America, of which:	-5.6	(-0.3)	-2.7	(-0.1)	-4.4	(-0.1)	26.4	(0.4)	-10.9	(0.0)	15.2	(0.1)
-Venezuela	-12.3	(-0.4)	-11.6	(-0.3)	-18.7	(-0.1)	-8.0	(0.0)	-0.1	(0.0)	0.6	(0.0)
-Other	5.0	(0.1)	9.3	(0.2)	-0.9	(0.0)	16.4	(0.2)	---	---	---	---
Caribbean, of which:	-16.8	(-0.7)	-0.4	(0.0)	-10.0	(-0.5)	-3.4	(-0.2)	-18.9	(-0.1)	22.9	(0.1)
-Aruba	-18.3	(-0.3)	19.0	(0.3)	---	---	---	---	-25.0	(-0.1)	28.4	(0.1)
-Dominican Republic	-27.9	(-0.2)	-27.4	(-0.1)	-40.9	(-0.2)	-6.9	(0.0)	---	---	---	---
-Other	-12.1	(-0.3)	-5.3	(-0.1)	-5.0	(-0.2)	-3.1	(-0.1)	---	---	---	---
Total	-0.6	(-0.2)	5.5	(1.7)	-1.5	(-0.9)	0.0	(0.0)	-1.0	(-0.1)	1.6	(0.1)

Source: Curaçao Tourist Board, St. Maarten Tourist Bureau, and Tourism Corporation Bonaire.

[a] Weighted growth rates between brackets.

Table 10 Netherlands Antilles consumer prices (annual percentage change)

	2003	2004	2005	2006
Food	2.1	4.4	7.2	7.2
Beverages & tobacco	-0.5	-0.4	2.6	3.7
Clothing & footwear	0.2	-0.2	-0.6	0.1
Housing	4.2	1.8	5.2	2.6
Housekeeping & furnishings	2.1	0.5	5.3	2.4
Health	0.7	0.9	1.3	0.7
Transport & communication	-1.0	0.8	2.7	2.3
Recreation & education	0.1	0.2	0.3	0.4
Other	0.7	0.6	1.4	2.0
General inflation rate	1.6	1.5	3.8	2.9

Source: Central Bureau of Statistics

Table 11 Budgetary overview (in millions NAf.)

	2003	2004	2005	2006
General government				
Revenues	1,346.7	1,349.1	1,616.2	1,485.6
Tax revenues, of which:	1,140.2	1,204.9	1,251.8	1,284.1
Taxes on income and profits	555.8	578.3	598.2	582.4
Taxes on goods and services	427.8	458.9	479.1	502.0
Taxes on international trade and transactions	119.5	127.0	130.7	143.9
Nontax and other revenues	206.5	144.2	364.4	201.5
Expenditures	1,589.5	1,690.2	1,770.7	1,675.2
Current, of which:	1,505.4	1,625.5	1,749.6	1,635.6
Wages and salaries	535.2	554.9	678.9	561.0
Goods and services	368.5	436.5	433.2	416.3
Transfers	267.9	332.9	310.9	330.4
Interest payments	251.9	256.8	284.5	283.4
Capital	84.1	64.7	21.1	39.6
Budget balance	-242.8	-341.0	-154.5	-189.6
Central government				
Revenues	671.6	692.3	912.6	822.6
Tax revenues, of which:	535.5	577.2	607.4	649.3
Taxes on goods and services	391.0	420.7	440.6	461.4
Taxes on international trade and transactions	119.5	127.0	130.7	143.9
Nontax and other revenues	136.1	115.1	305.2	173.3
Expenditures	834.4	898.4	991.7	910.6
Current, of which:	777.1	868.1	979.7	908.4
Wages and salaries	251.3	292.9	282.7	295.5
Goods and services	104.6	107.2	123.5	117.7
Transfers	278.6	324.3	427.9	348.2
Interest payments	133.7	142.0	145.6	147.0
Capital	57.3	30.3	12.0	2.2
Budget balance	-162.8	-206.1	-79.1	-88.0
Island government of Curaçao				
Revenues	833.0	818.7	982.3	842.5
Tax revenues, of which:	604.7	627.7	644.4	634.8
Taxes on income and profits	555.8	578.3	598.2	582.4
Taxes on goods and services	36.8	38.2	38.5	40.6
Nontax and other revenues	228.3	190.9	337.9	207.7
Expenditures	913.0	953.6	1,057.6	944.1
Current, of which:	886.2	919.2	1,048.5	906.6
Wages and salaries	283.9	262.0	396.2	265.5
Goods and services	263.9	329.3	309.7	298.6
Transfers	147.2	170.4	161.6	161.7
Interest payments	118.2	114.8	138.9	136.4
Capital	26.8	34.4	9.1	37.4
Budget balance	-80.0	-134.9	-75.4	-101.6

Table 12 Total outstanding consolidated public debt (in millions NAf.)

	2003	2004	2005	2006
Domestic consolidated debt, of which:	3,605.9	3,984.8	4,145.0	4,369.0
Central government, of which:	1,925.3	2,074.6	2,233.5	2,323.5
Long-term securities	1,586.1	1,700.0	1,771.6	1,897.0
Short-term securities	44.7	104.9	94.4	57.3
APNA	149.7	118.4	209.0	217.6
SVB	26.2	6.5	13.9	8.4
Curaçao, of which:	2,002.0	2,199.3	2,076.5	2,199.8
Long-term securities	586.8	733.3	737.4	802.1
Short-term securities	86.2	144.5	202.6	201.9
APNA	807.8	827.2	758.4	797.0
SVB	0.0	0.0	0.0	0.0
Central government	362.3	365.2	253.9	262.6
Other islands	307.2	350.7	312.6	334.8
Foreign debt	806.7	802.1	725.8	822.0
Total debt (consolidated)	4,412.6	4,786.9	4,870.8	5,191.0
(% of GDP)	81.3%	85.8%	83.4%	85.4%

Table 13 Detailed overview of balance of payments (in millions NAf.)

	2003	2004	2005	2006
Trade balance	-1,866.3	-2,122.7	-2,353.7	-2,622.2
-Exports	768.5	1,363.8	1,721.6	2,014.0
-Imports	-2,634.9	-3,486.5	-4,075.3	-4,636.2
Services balance	1,670.0	1,899.1	1,986.2	2,114.7
Receipts, of which:	3,028.0	3,228.8	3,309.2	3,473.4
-Travel	1,530.7	1,676.1	1,771.2	1,828.0
-Transportation	234.0	246.5	223.2	222.6
-Other services, of which:	1,263.2	1,306.2	1,314.8	1,422.8
- Int. fin. & bus. services sector	410.1	434.8	397.0	405.2
Expenses, of which:	1,358.0	1,329.7	1,323.1	1,358.6
-Travel	552.6	502.3	471.4	504.0
-Transportation	123.6	150.0	168.4	166.0
-Other services, of which:	681.8	677.4	683.4	688.6
- Int. fin. & bus. services sector	157.5	150.2	136.3	148.6
Income balance [a]	-12.6	-29.7	-13.1	12.8
Current transfers balance [b]	213.4	97.9	196.4	11.6
Current account balance	**4.5**	**-155.4**	**-184.3**	**-483.1**
Capital & financial account balance [c]	**-12.2**	**90.8**	**66.5**	**425.9**
Net errors & omissions	**7.8**	**64.6**	**117.8**	**58.0**

Due to rounding, figures may not add up.
[a] Labor and investment income.
[b] Public and private transfers.
[c] A minus sign implies on improvement in the foreign financial position.

Table 14 Breakdown of net changes in the financial account (in millions NAf.)

	2003	2004	2005	2006
Direct investment	20.5	33.7	31.8	-16.1
- Abroad [a]	0.9	-39.6	-117.0	-101.0
- In the Netherlands Antilles [b]	19.6	73.3	148.8	84.9
Portfolio investment [a]	6.6	-1.7	-42.7	113.2
Other investment, of which:	-45.5	84.2	130.8	374.8
- Assets [a]	-1.0	23.6	133.8	378.5
- Liabilities [b]	-44.5	60.6	-3.0	-3.7
Net lending/borrowing, of which:	48.2	-101.4	-91.4	-141.9
- Assets [a]	-66.8	-57.3	-101.6	-74.0
- Liabilities [b]	115.0	-44.1	10.2	-67.9
Reserves [c]	-89.0	-66.1	-132.7	-84.3
Total assets [a]	-149.3	-141.1	-260.2	232.4
Total liabilities [b]	90.1	89.8	156.0	13.3
Balance	-59.2	-51.3	-104.2	245.7

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

Table 15A Net accumulation of wealth (in millions NAf.)

2006	Domestic sectors Private	 Government	 Banking	External sector
Nonfinancial transactions	-305.1	-178.0		483.1
Government net lending	11.6	-11.6		
Government domestic non-bank financing	-229.0	229.0		
External financing of the government		12.8		-12.8
External financing of the private sector	317.0			-317.0
-Direct investment (equity)	-16.1			16.1
-Loans and credits	220.0			-220.0
-Portfolio, incl. debt	113.2			-113.2
Capital transfers & acquisitions	179.6			-179.6
Change in net foreign assets of the central bank			-73.7	73.7
Change in net foreign assets of commercial banks			-10.5	10.5
Change in domestic bank credit	608.0	-52.2	-555.8	
Change in broad money	-491.7		491.7	
Other items, net/errors & omissions	-90.3		148.3	-58.0

Table 15B Net accumulation of wealth (in millions NAf.)

	Domestic sectors			External sector
2005	**Private**	**Government**	**Banking**	
Nonfinancial transactions	-25.0	-159.3		184.3
Government net lending	-4.8	4.8		
Government domestic non-bank financing	-171.2	171.2		
External financing of the government		-17.3		17.3
External financing of the private sector	45.5			-45.5
-Direct investment (equity)	31.4			-31.4
-Loans and credits	56.8			-56.8
-Portfolio, incl. debt	-42.7			42.7
Capital transfers & acquisitions	171.1			-171.1
Change in net foreign assets of the central bank			-68.8	68.8
Change in net foreign assets of commercial banks			-63.7	63.9
Change in domestic bank credit	390.6	0.6	-391.2	
Change in broad money	-423.5		423.5	
Other items, net/errors & omissions	17.6		100.2	-117.8

Table 16 Monetary survey (in millions NAf.)

	2003	2004	2005	2006
Money supply (M2)	4,092.9	4,509.9	4,933.4	5,425.1
Money (M1)	1,501.4	1,790.5	1,947.3	2,152.2
Coins & notes with the public	232.9	231.3	239.9	263.7
Total demand deposits, of which:	1,292.4	1,365.3	1,544.1	1,712.4
- Netherlands Antillean guilders	989.3	1,050.7	1,188.0	1,246.7
- Foreign currency	303.1	314.6	356.1	465.7
Near money	2,567.6	2,913.3	3,149.4	3,449.0
Time deposits	1,501.4	1,790.5	1,947.3	2,152.2
Savings	1,066.2	1,122.8	1,202.1	1,296.8
Factors affecting the money supply				
Net domestic assets	2,772.5	3,048.3	3,305.5	3,652.7
General government	470.1	621.3	621.9	569.7
- Central government	272.4	363.9	397.9	358.5
- Island governments	197.7	257.4	224.0	211.2
Private sector	2,834.4	3,059.7	3,450.3	4,058.3
Net foreign assets	1,320.4	1,461.6	1,627.9	1,772.4
Central bank	904.5	1,015.3	1,117.9	1,251.9
Commercial banks	415.9	446.3	510.0	520.5
Memorandum items				
Government loans by commercial banks	489.5	620.1	603.4	456.5
- Central government	282.3	331.4	306.2	245.4
- Island governments	207.2	288.7	297.2	211.1
Private sector loans - Leeward Islands	1,981.4	2,129.5	2,367.4	2,610.4
- Mortgages	778.1	778.2	812.4	816.5
- Consumer loans	541.5	626.6	713.6	808.9
- Business loans	661.8	724.7	841.4	985.0
Private sector loans - Windward Islands	755.0	828.5	995.4	1,191.8
- Mortgages	373.1	306.0	362.0	426.1
- Consumer loans	145.4	195.6	243.2	300.4
- Business loans	236.5	326.9	390.2	465.3

Table 17 Developments in domestic interest rates (in %)

	2003	2004	2005	2006
Central bank				
- Pledging rate	2.25	2.75	4.50	5.50
- Maximum CD rate (1 month)	1.25	2.64	4.36	5.33
Commercial bank borrowing rates				
- Passbook savings	3.4	2.8	2.8	2.8
- Time deposit (12 months)	4.9	4.1	4.1	4.2
Commercial bank lending rates				
- Mortgages	9.5	8.9	8.6	8.5
- Time loans	12.5	12.0	10.8	10.6
Government securities				
- Government bonds (5-year effective yield)	6.9	6.8	6.3	7.5
- Treasury bills (1 month)	3.0	3.7	4.5	4.9

Table 18 Aggregate balance sheet for domestic commercial banks (in millions NAf.)

	2003	2004	2005	2006
Assets				
Non-interest bearing cash	430.6	440.0	475.7	548.6
Interest-bearing cash	1,431.3	1,590.6	1,836.7	2,278.5
Investments	611.3	744.0	1,675.8	1,225.1
Loans	3,697.2	4,049.2	5,140.0	5,736.6
Investments in unconsolidated subsidiaries and affiliates	13.5	12.2	11.4	182.1
Fixed assets	169.6	190.7	218.3	233.7
Other assets	147.0	162.6	200.9	195.1
Total assets	6,500.4	7,189.2	9,558.7	10,399.7
Liabilities				
Demand deposits	1,839.2	2,061.8	2,790.3	3,181.8
Savings deposits	2,326.2	2,467.1	3,094.2	3,294.1
Time deposits	1,485.3	1,810.8	2,555.7	2,620.0
Total deposits	5,650.7	6,339.6	8,440.3	9,095.9
Borrowings	125.4	30.4	34.2	31.5
Other liabilities	243.7	238.4	316.7	345.2
Total liabilities	6,019.8	6,608.5	8,791.1	9,472.7
Minority interest	6.4	6.4	7.0	7.9
Subordinated debentures	9.4	7.5	5.5	3.6
General provisions	140.1	144.4	141.8	187.5
Capital & reserves	324.7	422.5	613.2	728.0
Total capital	480.6	580.8	767.6	927.0
Total liabilities and capital	6,500.4	7,189.2	9,558.7	10,399.7

Table 19 Aggregate income statement for domestic commercial banks (accumulated, in millions NAf.)

	2003	2004	2005	2006
Interest income	427.2	457.8	608.1	674.3
Interest expenses	161.3	156.8	200.9	248.4
Net interest income	265.9	301.0	407.2	425.9
Other income	161.9	174.9	253.2	258.8
Total operational income	427.8	475.9	660.4	684.7
Salaries & other employee expenses	194.4	215.9	238.9	252.1
Occupancy expenses	51.9	57.3	68.1	71.4
Other operating expenses	58.8	50.1	106.6	96.0
Net addition to general provisions	34.7	35.5	40.3	43.5
Total operational expenses	339.9	358.8	453.9	463.0
Net operating income	87.9	117.1	206.5	221.7
Net extraordinary items	0.6	7.4	3.6	9.7
Applicable profit taxes	22.6	30.8	35.7	37.2
Net income after taxes	65.9	93.6	174.4	194.2

* Cumulative quarterly figures.

4 DOMESTIC FINANCIAL MARKET DEVELOPMENTS

4.1 Introduction

In the beginning of 2006, the capital market was fairly liquid. Banks had sufficient funds to invest in local government paper as well as other instruments, such as loans. The fixed income market was limited to government bonds and some private issues in the tourism sector.

The local capital market geared up for interest rate increases since the Federal Reserve was expected to raise its base interest rate. Normally, in such a situation, local investors would sell their securities because rising interest rates would erode the value of their securities since price and yield are inversely related. However, this did not happen during the first months of 2006 because of rumors in the market that the Netherlands would be prepared to take over most of the Antillean government debt, which would lead to even lower yields. As a result, investors held on to their securities. Consequently, the first two quarters of 2006 closed with very little activity in the securities market, except for the regular bi-monthly tender of treasury bills and a few secondary market dealings.

As noted, market participants did not offer securities for sale. Moreover, this also indicated that alternative local investment opportunities remained scarce. Liquidity in the market diminished as interest rates overseas increased, even though institutional investors are required to maintain a certain percentage of their portfolio in local investments.

During the first quarter of 2006, the Bank increased its government securities portfolio by NAf. 10.0 million for subsequent sale in the local market to maintain activity in the secondary market. However, the offers quickly finished, and the Bank made no further attempts to increase its portfolio of government paper. The lack of supply pushed securities prices up, which resulted in declining yields.

During 2006, the central government issued 5 new loans totaling a nominal amount of NAf.256.3 million. The island government of Curacao issued 3 new loans totaling a nominal amount of NAf.104.6 million. These issues had interest rates ranging from 5.75% for a 4-year loan to 7.875% for a 10-year loan.

In the money market, the interest rates on certificates of deposit (CDs) and time deposits (TDs) increased in the same proportion as the US Fed Funds rate.

4.2 Financial instruments and the money market

Certificates of deposit (CDs) issued by the Bank are among the few tradable nongovernmental instruments available in the local money market. CDs are a monetary tool used by the Bank to control the liquidity in the local money market through bi-monthly auctions according to a set schedule. Commercial banks did not trade in CDs but preferred to use uncollateralized interbank instruments.

As indicated in Table 20, the average monthly balance of outstanding CDs decreased throughout 2006 by NAf.45.5 million compared to 2005. In the first quarter of 2006, subscriptions were low or nil. In 2005, the CD rates offered by the Bank were not competitive enough to stimulate the swapping of US dollar funds for Antillean guilder-denominated instruments. This situation continued during the first months of 2006. Furthermore, the increasing interest rates in the United States prompted the banks to leave their funds overseas. However, towards the end of the first quarter, the Bank made CDs more attractive by increasing the margin vis-à-vis libid. The decline in outstanding CDs in 2006 was related to the decline in bank liquidity, reducing the amount of CDs offered by the Bank to mop up excess liquidity in the market.

The average monthly balance of the non-interest-bearing reserve requirement increased by NAf.79.0 million (17.4%) in 2006. The base amount on which the reserve requirement is calculated equals the commercial banks' domestic debt excluding interbank and long-term deposits. In addition to a higher base amount, the increase was due also to increases in the reserve requirement percentage set by the Bank from 12.25% at the end of 2005 to 12.75% on January 16, 2006, and to 13.00% on March 16, 2006.

The average outstanding demand deposits of the commercial banks decreased by NAf.34.3 million (58.1%) in 2006, indicating the decrease in liquidity referred to above.

Table 20 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.)

	2004	2005	2006	Change 2005-2006
Certificates of deposit	95.3	85.8	40.3	-53.0%
Non-interest-bearing reserve requirement	379.9	455.2	534.2	17.4%
Demand deposits	53.0	59.0	24.7	-58.1%
Total	528.2	600.0	599.2	-0.1%

Government issues of securities in the money market consisted of treasury bills with maturities of 1, 3, 6, and 12 months. During 2006, treasury bills continued to be auctioned twice a month. Financial market information is provided to market participants on a monthly basis to enhance market transparency. The financial market information provides data, such as the prices of securities, the local yield curve, the net debt position of both governments, and the maturity schedule. Market transparency is intended to promote activity in the secondary market.

Activities in the secondary market continued at a slow pace during 2006 because market participants perceived the possibility of an interest rate increase. The US short-term rate was increasing, prompting investors to hold on to their higher yielding bonds, which limited activities in the secondary market.

Treasury bills were traded mainly in the primary market and not in the secondary market. Perhaps because of the primary market that trades about every two weeks, market participants were satisfied with the frequency and yields of the short-term paper offered.

At the end of the first half of 2006, the yield on a 1-month treasury bill was 5.25%, the 3-month bill was 5.00%, while the 1-year treasury bill was at 6.15%. At the end of 2006, yields had risen: the 1-month treasury bill was trading at 5.50%, the 3-month treasury bill at 5.75%, and the 1-year treasury bill at 6.25%. Table 21 provides information on the size and the activity in the market for local treasury bills.

Table 21 Treasury bill issuance, outstanding balances, and average maturity as of December 31 (in millions NAf.)

	2004	2005	2006	Change 2005-2006
Issuance	**509.6**	**543.0**	**367.5**	**-32.3%**
Central government	307.0	248.8	74.2	-70.2%
Island government of Curaçao	202.6	294.3	293.3	-0.3%
Outstanding amount	**249.4**	**297.0**	**259.2**	**-12.7%**
Central government	104.9	94.4	57.3	-39.3%
Island government of Curaçao	144.5	202.6	201.9	-0.4%
Average maturity (months)	**3.7**	**5.0**	**5.6**	**12.0%**
Central government	4.1	4.8	5.3	10.4%
Island government of Curaçao	3.4	5.1	5.7	11.8%

4.3 The market for government securities

As in previous years, the demand for government bonds remained high in the local market in 2006. Despite the increases in US interest rates during 2006, local investors continued to prefer local bonds. This trend persisted throughout the year, reflecting the lack of other local investment opportunities with comparable risk and return and foreign investment restrictions for institutional investors. This occurred despite the high interest rates offered in the foreign markets. Towards the end of 2006, the demand for funds by both levels of government increased, which provoked higher interest rates in the local market.

During the second half of 2006, the island government of Curaçao started having liquidity problems. In a meeting with the local commercial banks and institutional investors, the Commissioner of Finance presented the financial outlook and solutions for resolving the liquidity crisis, which included eventually a balanced budget. However, toward the end of the year, the liquidity problems became worse, partly because the local capital market had become less liquid. The island government was forced to redeem part of its maturing bonds, and the supply of funds was offered mainly for the short term with higher than usual interest rates.

Gross general government debt issuance continued to decline to NAf.749.0 million in 2006, compared to NAf.821.6 million in 2005 and NAf.1,029.6 million during 2004. Treasury bills accounted for NAf.367.5 million of gross general government debt issuance in 2006, of which NAf.74.2 million was issued by the central government and NAf.293.3 million by the island government of Curaçao. In 2005, the central government issued NAf.248.8 million, and NAf.294.3 million was issued by the island government of Curaçao.

Both governments issued more bonds in 2006 than in 2005. The island government of Curacao issued NAf.55.9 million and the central government NAf.47.0 million more. Both governments tried to convert their short term loans into longer term loans, with no real success because the investors perceived longer maturities with higher risk and, hence, interest rates. The fact that both governments issued more in bonds in 2006 explains part of the declining yield.

The central government issued five new public loans during 2006: a 4-year bond with a coupon of 5.75% and a 10-year bond with a coupon of 7.00% in January, a 10-year bond with a coupon of 7.50% in May, an 8-year bond with a coupon of 7.50% in September, and a 7-year bond with a coupon of 7.375% in November. The last issue remained open till the end of the year.

The island government of Curaçao had three public issues in 2006: an 11-year bond with a coupon of 7.875% in June, a 10-year bond with a coupon of 7.50% in November, and a 3-year bond with a coupon of 7.25% in December. The last two issues remained open until the end of the year.

Graph 2 shows that net borrowing (excluding debt conversion) was higher in 2006 than in 2005, but lower than in the years 2002 - 2004.

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

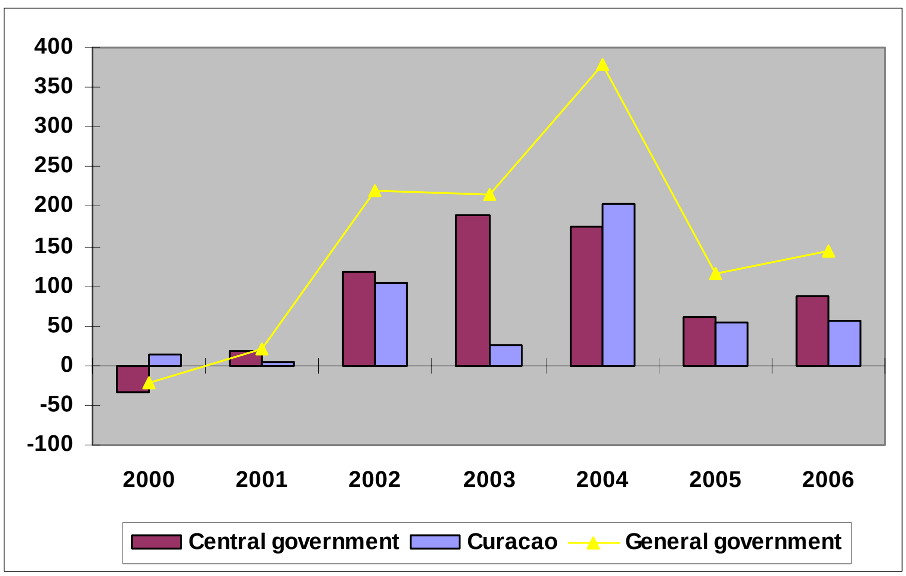


Table 22 indicates that net borrowing by the central government was concentrated in public issues in 2006, which increased 22.4%. Private placements declined due to two maturities that were refinanced with public issuances. The issuance of treasury bills decreased by 39.3%.

Table 22 Outstanding negotiable loans of the central government (in millions NAf.)

	2004	2005	2006	Change 2005-2006
Total, of which:	1,804.9	1,866.0	1,954.2	4.7%
Private placement	153.9	154.1	67.7	-56.1%
Public issues	889.2	966.8	1,182.9	22.4%
Treasury bills	104.9	94.4	57.3	-39.3%
Debt conversions	656.7	650.7	646.4	-0.7%
Net borrowing	174.2	61.1	88.3	44.8%

The island government of Curaçao noted an increase of 2.6% in its net borrowing in 2006 compared to 2005 (see Table 23). The public issues increased by 19.9%, mainly because the government was trying to convert its short-term loans to longer maturities. However, outstanding treasury bills decreased by only 0.4%.

Table 23 Outstanding negotiable loans of the island government of Curaçao (in millions NAf.)

	2004	2005	2006	Change 2005-2006
Total, of which:	1,287.8	1,342.4	1,398.3	4.2%
Private placement	122.3	122.3	64.7	-47.1%
Public issues	611.1	615.1	737.4	19.9%
Treasury bills	144.5	202.6	201.9	-0.4%
6.5% annuity	409.9	402.4	394.4	-2.0%
Net borrowing	197.8	54.6	55.9	2.6%

The maturity schedule in Table 24 indicates that 10% of the outstanding loans will mature within 1 year. The peak in maturities of central government loans lies in the 1-5 years bracket (62%). Maturities of the island government of Curaçao are more evenly spread over the brackets exceeding one year.

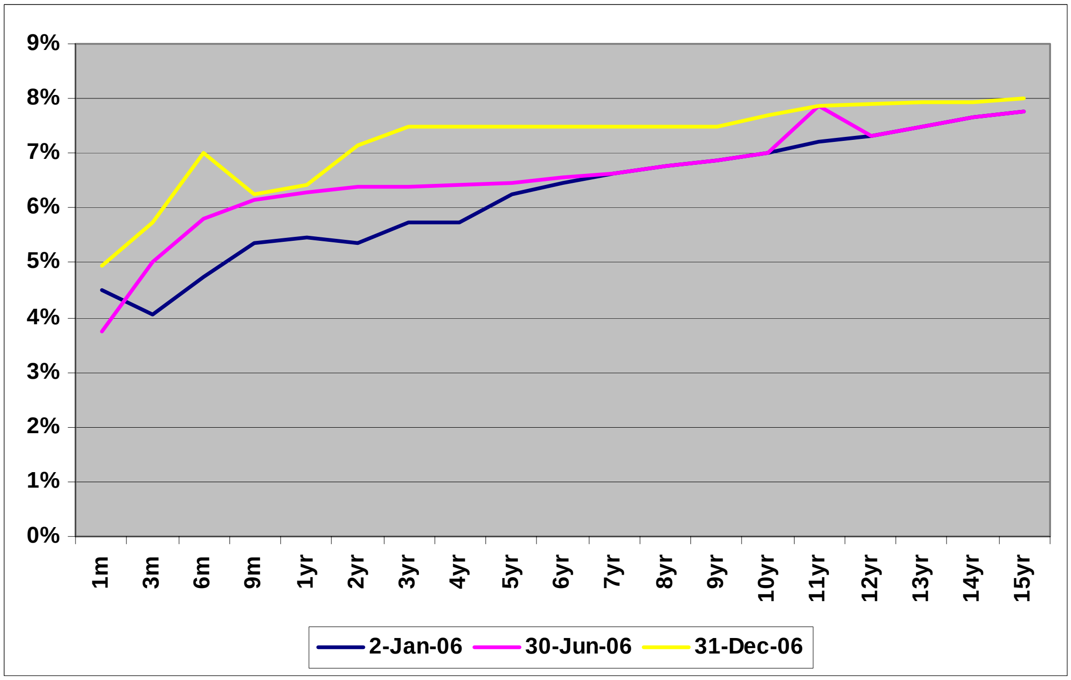
Table 24 Maturity schedule of negotiable government securities excluding treasury bills as per December 31, 2006 (% share)

	0-1 year	1-5 years	5-10 years	Over 10 years
Central government	9%	62%	23%	6%
Island government of Curaçao	11%	20%	36%	33%
Total	10%	46%	28%	16%

4.4 Domestic yield curve developments

The local yield curve reflected an increasing trend during 2006. This development was the result of various factors. First, interest rates in the United States increased, pushing up the rates on the local CD market. Second, the capital market became less liquid because funds were transferred to the more attractive US capital market. Third, the liquidity situation of both levels of government became very tight during the second half of 2006, pushing local interest rates even higher. Towards the end of 2006, local interest rates hit a 5-year high with treasury bills being accepted by the island government of Curacao for 7% with a 12-month term.

Graph 3 Local yield curve changes during 2006



5 INSTITUTIONAL INVESTORS

5.1 Introduction

June through November of each year is the period when most tropical cyclones form in the Atlantic basin. Of the 21 storm names selected for 2006, fortunately 12 remained unused, indicating an unusually slow season with no hurricanes striking the mainland of the United States of America and the Caribbean region. As a result, catastrophe damages were minimal compared to 2005. Although the necessity to recover amounts from the reinsurers, therefore, was also limited, the importance of having adequate reinsurance in place still stands. Worth mentioning in this respect is the expectation that international reinsurers will start operations in the Brazilian market in 2007, by far the largest insurance market in Latin America. This liberalized market might provide possibilities for increased capacity regarding reinsurance and retrocession business in the near future.

The Netherlands finalized the revision process of their pension legislation and the 'Pensioenwet' went into effect in December 2006. This legislation will serve as a basis for future adjustments to our National Ordinance on Corporate Pension Funds (P.B. 1985, nr. 44). European research indicates that the introduction of the International Financial Reporting Standards (IFRS) contributes to a level playing field among the European companies. Although transparency and comparability have increased, apparently some possibility for subjectivity still exists, diminishing somewhat the improvement in comparability. With a rapidly aging population, diminishing investment results, fewer possibilities to increase the pension premium of employees, limited indexation for pensioners, and the introduction of the IFRS accounting principles, the choice between a Defined Benefit pension plan and a Defined Contribution plan needs careful consideration. In the Netherlands Antilles, a combination of plans also is being provided by various pension funds and insurance companies.

As part of a globalized world, international and regional developments influence financial and other activities of entities operating in different jurisdictions. In June 2006, the Central Bank of Aruba announced that in view of changing market conditions and to improve its monitoring and its supervising capabilities, it would revise its policy for insurance companies that operate through branch offices or agencies in or from Aruba. Depending on the size of the parent company, the branch office doing business in Aruba might have to be transformed into a limited liability company in accordance with Aruban company laws. The new policy rules went into effect as of January 2007 and apply to Netherlands Antillean entities doing business through a branch office in the Aruban jurisdiction.

Despite the expected delay until 2009 in the implementation of the Solvency II requirements in the European Union, the analysis of catastrophe and other losses leads to a growing understanding by insurance companies that risk and capital management concepts should be a crucial part of their strategic policy. The Solvency II risk-based approach may trigger consolidation through mergers and acquisitions, resulting in fewer and larger companies in the market, thus benefiting from economies of scale.

While the effects of hurricanes can lead to the destabilization of an economy, the effects of fire incidents destroying commercial property, as experienced in Curaçao at the end of 2006, should not be underestimated. As in the case of natural catastrophes, the purchase of property insurance including business interruption coverage is a means to recover and thus limit one's financial loss. On the other hand, reinsurance bought by the primary carrier serves as a buffer to mitigate the negative results on the company's equity due to incurred claims. Also the adjustment of underwriting policies may limit future disbursements.

The Bank is a member of various international organizations dealing with the supervision of financial and nonfinancial institutions. One of these organizations is the Offshore Group of Insurance Supervisors (OGIS). In October 2006, a representative of the Bank was elected Secretary General of this international organization.

The insurance companies servicing the Antillean and the international market reported positive after-tax results in 2005. The life and the non-life companies operating in both markets complied on an aggregate basis with the solvency requirements. Also the pension industry performed well in 2005, reflected by an improvement in its equity position.

5.2 The institutional investors' sector

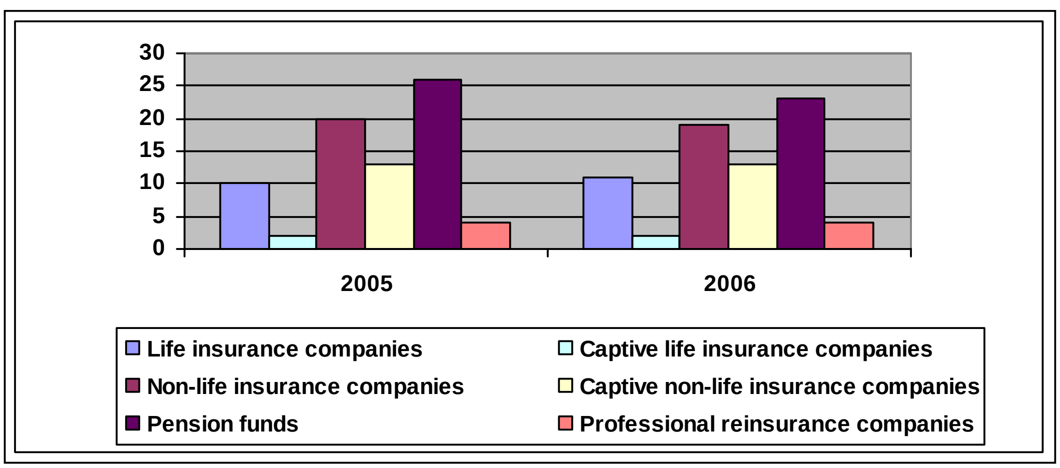
The number of institutional investors operating in the Netherlands Antilles in 2006 was 71 (2005: 74): 11 life insurance companies (2005: 10), 19 non-life insurance companies (2005: 20), 18 funeral service insurers and, 23 pension funds (2005: 26). In 2006, one life insurance company was licensed, while one non-life insurance company discontinued with its operations. Of the 26 pension funds registered at the Bank in 2005, 3 were in the process of liquidation in 2006.

The number of insurance companies servicing the international market was 19 at the end of both 2005, and 2006: 2 were involved in the life insurance business, 13 in the non-life business, and 4 were professional reinsurers.

Of 109 insurance intermediaries that applied for registration with the Bank, 63 have been registered. Of the remaining 46, 32 are still being processed, and 14 applications were rejected.

Graph 4 does not include the number of 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)



5.3 Life insurance industry

5.3.1 Balance sheet

According to Table 25, total assets of the local life insurance sector increased by NAf.213.1 million (13.5%) in 2005 compared to 2004. Of the total assets in 2005, 81.7% was related to investments and 10.4% to current assets. The increase in total liabilities in 2005 was mainly the result of an increase of NAf.107.6 million (8.2%) in technical provisions.

The equity position of the local life insurance companies, consisting of capital, surplus, and subordinated instruments, increased by NAf.23.7 million (16.3%) in 2005. This increase was due to the profit of NAf.8.4 million in 2005 (see Table 26), surplus contributions, and other changes that affected the surplus account positively.

In 2005, the solvency requirement of the local life insurance sector amounted to NAf.53.7 million, while the equity available to cover the solvency requirement amounted to NAf.154.5 million. Based on these figures, the sector had a solvency surplus excess of NAf.100.8 million.

Table 25 Consolidated balance sheet of the life insurance sector (in millions NAf.)

	2003		2004		2005	
	Local	**Int'l**	**Local**	**Int'l**	**Local**	**Int'l**
ASSETS						
Intangibles	0.1	-	0.1	-	-	
Total investments	1,254.2	96.3	1,340.7	115.3	1,462.3	121.3
Current assets	181.3	63.2	155.0	50.5	186.9	49.4
Other assets	6.0	-	23.3	-	26.9	-
From separate accounts statement	79.1	-	57.5	-	113.6	-
Total admissible assets	1,520.7	159.5	1,576.6	165.8	1,789.7	170.7
EQUITY, PROVISIONS, AND LIABILITIES						
Capital	57.4	7.7	62.8	7.7	62.8	8.1
Surplus	89.2	36.1	82.2	47.1	105.5	54.0
Subordinated instruments	0.1	-	0.1	-	0.5	-
Technical provisions	1,197.5	91.2	1,318.2	81.5	1,425.8	90.9
Current liabilities	77.3	21.8	46.3	25.1	57.1	16.1
Other liabilities	10.1	2.7	6.8	4.4	5.4	1.6
Contingent liabilities	10.0	-	2.7	-	19.0	-
From separate accounts statement	79.1	-	57.5	-	113.6	-
Total equity, provisions, and liabilities	1,520.7	159.5	1,576.6	165.8	1,789.7	170.7

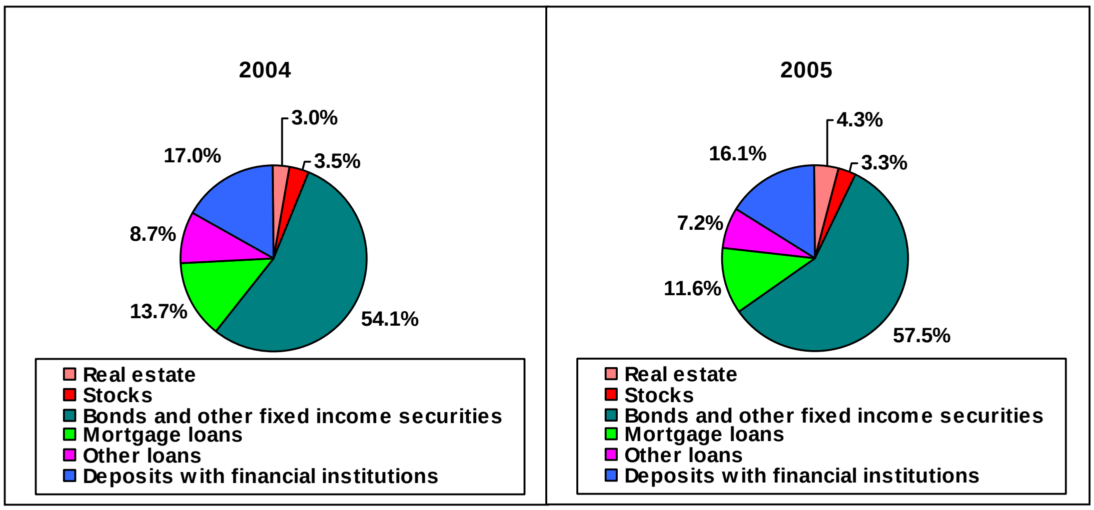
The total assets of the international life insurance companies (captive insurance companies and professional reinsurers) increased slightly by NAf.4.9 million (3.0%), reaching NAf.170.7 million at the end of 2005. The equity position increased by NAf.7.3 million (13.3%) to NAf.62.1 million, mainly due to the profit of NAf.15.9 million made in 2005 (see Table 26).

The solvency requirement of the international life insurance sector amounted to NAf.3.7 million in 2005. The equity available to cover the solvency requirement amounted to NAf.62.1 million, resulting in a solvency surplus excess of NAf.58.4 million.

5.3.2 Investments

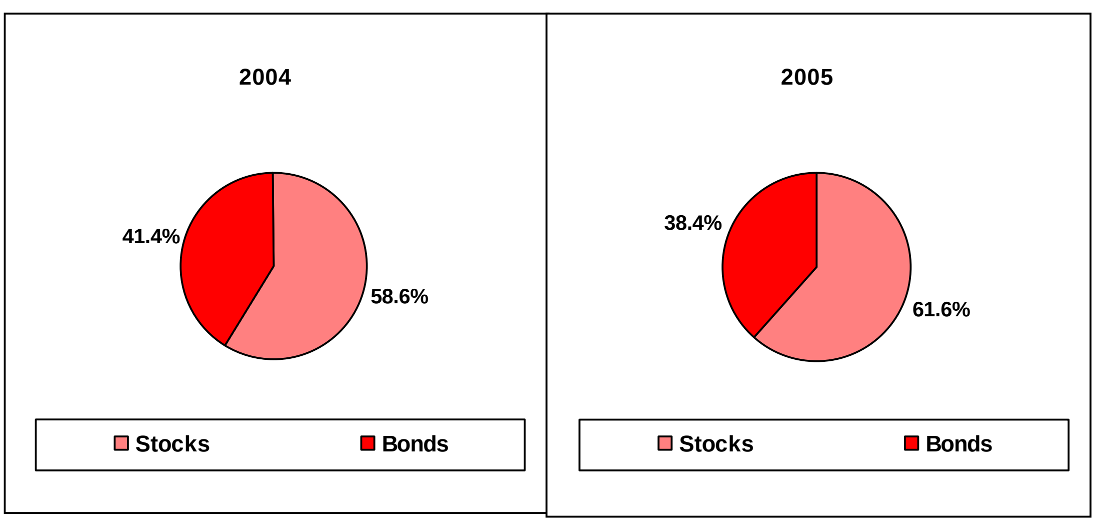
Total investments of the local life insurance sector increased by NAf.121.6 million (9.1%) in 2005, mainly due to an increase of investments in real estate and bonds. The composition of the consolidated 2004 and 2005 investment portfolios of the local life insurance companies is presented in graph 5. This graph indicates that the proportion of investments in real estate and bonds increased by, respectively, 1.3 and 3.4 percentage points in 2005 compared to 2004. These increases were at the expense of the other investment instruments.

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



The composition of the consolidated 2004 and 2005 investment portfolio of the international life insurance companies is presented in graph 6. This investment portfolio is not as diversified as that of the local life insurance companies, consisting only of stocks and bonds. The total investment portfolio increased by NAf.6.0 million (5.2%) in 2005 compared to 2004. From the graph, it can be deduced that the proportion of stocks increased by 3.0 percentage points to 61.6% at the expense of the investment in bonds.

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



5.3.3 Profit and loss statement

The operating results of the life insurance industry are presented in Table 26. Net premium income of the local life insurance sector increased by NAf.4.5 million (2.4%). The net operational result before corporate taxes and before net results from separate accounts increased by NAf.5.9 million (368.8%) in 2005 compared to 2004, but, in contrast, significantly decreased by NAf.18.6 million (92.1%) compared to 2003. The sector recorded a net profit of NAf.8.4 million in 2005, almost the same as in 2004.

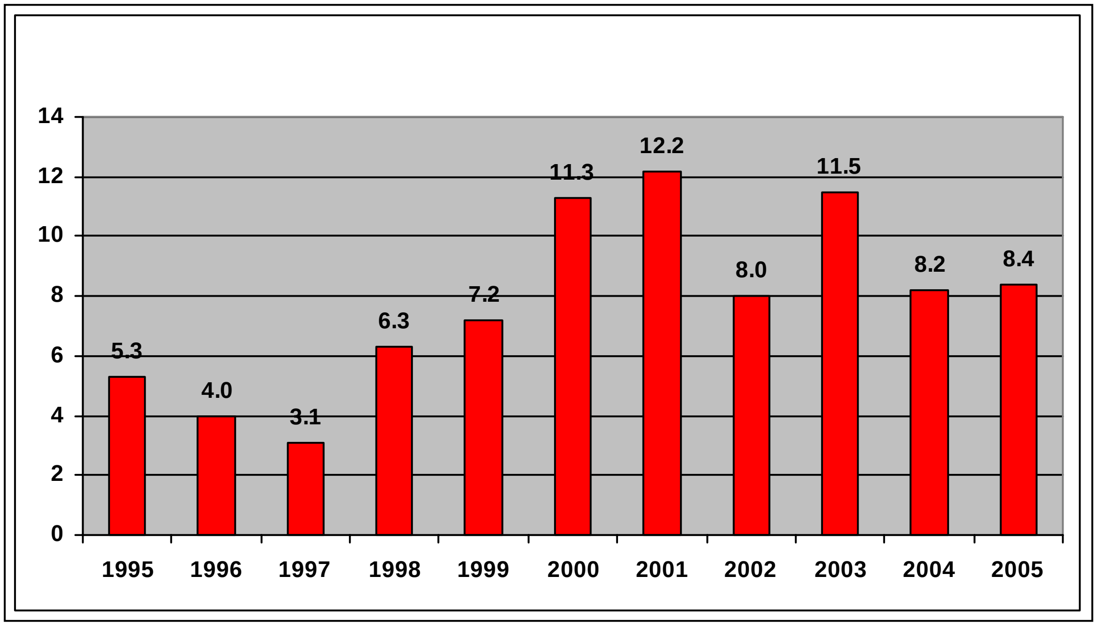
Table 26 Consolidated profit and loss statement of the life insurance sector (in millions NAf.)

	2003		2004		2005	
	Local	**Int'l**	**Local**	**Int'l**	**Local**	**Int'l**
INCOME						
Total net premium income	194.3	18.6	189.7	35.5	194.2	42.0
Net investment income and realized capital gains and losses	81.2	9.2	97.1	5.0	95.5	5.3
Net other operational income	5.9	0.9	5.8	1.8	2.1	2.1
Total operational income	281.4	28.7	292.6	42.3	291.8	49.4
EXPENSES						
Net benefits incurred	88.9	4.9	84.0	49.0	97.9	21.8
Changes in net technical provisions	99.2	24.3	123.9	-11.9	109.3	6.8
Net operational exp. incurred	51.1	1.9	61.3	2.6	59.7	3.5
Net other operational exp. incurred	5.1	1.2	6.9	1.7	2.5	0.7
Other changes affecting net results	0.2	-0.3	-0.4	-0.2	-	-
Profit sharing to policyholders	12.4	0.6	14.0	-	13.3	4.6
Total operational expenditures	256.9	32.6	289.7	41.2	282.7	37.4
Extraordinary results	-4.3	-0.9	-1.3	-0.4	-1.6	0.6
Net operational result before corp. taxes and before net results from separate accounts	20.2	-4.8	1.6	0.7	7.5	12.6
Corporate taxes	4.3	0.2	4.7	0.1	-5.4	0.2
Net operational result after corp. taxes and before net results from separate accounts	15.9	-5.0	-3.1	0.6	12.9	12.4
Net result from separate accounts	-5.2	-	10.3	-	1.6	-
Net operational result	10.7	-5.0	7.2	0.6	14.5	12.4
Net unrealized gains or losses	0.8	6.7	1.0	8.6	-6.1	3.5
Net profit or loss	11.5	1.7	8.2	9.2	8.4	15.9

The premium income of the international life insurance industry increased from NAf.35.5 million in 2004 to NAf.42.0 million in 2005. The net benefits incurred decreased from NAf.49.0 million to NAf.21.8 million, but the changes in net technical provisions increased by NAf.18.7 million in 2005. The international life insurance industry experienced a net profit of NAf.15.9 million in 2005, an increase of NAf.6.7 million compared to 2004.

Graph 7 presents an overview of the consolidated net profit or loss of the local life insurance companies during the period 1995 - 2005. In 2004, net results decreased mainly due to a slight decrease in net premium income and a higher amount added to the technical provisions. Noteworthy is that net results of the sector fluctuated between NAf.8.0 million and NAf.12.2 million during the period 2000 - 2005.

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



5.4 The non-life insurance industry

5.4.1 Balance sheet

Table 27 reveals that the 2005 balance sheet total of the non-life insurance companies operating in the domestic market reached NAf.447.6 million, an increase of NAf.6.4 million (1.5%) compared to 2004. Investments increased by NAf.34.9 million (14.1%), but current assets decreased by NAf.31.0 (17.1%).

Due to the short-term nature of the risks insured by the non-life insurance business in comparison to the life insurance business, a smaller percentage of total assets was invested, 63.2% in 2005 compared to 81.7% in the life insurance business. On the other hand, current assets comprised 33.5% of total assets in 2005 compared to 10.4% in the life insurance business.

The technical provisions of the local non-life insurance sector decreased by NAf.10.0 million, reaching NAf.176.2 million in 2005. The equity position increased by NAf.21.1 million (70.8%), mainly due to the retained profit reported by the sector in 2005.

The solvency requirement of the local non-life insurance sector amounted to NAf.45.3 million, and the equity available to cover the solvency requirement amounted to NAf.137.2

million in 2005. From these figures, it follows that the sector had a solvency surplus excess of NAf.91.9 million in 2005.

The non-life insurance companies servicing the international market (captive insurance companies and professional reinsurers) reported total assets of NAf.3.2 billion in 2005 compared to NAf.3.0 billion in 2004. While this sector experienced an average yearly growth of NAf.300.0 million in total assets for the past 4 years, the growth in 2005 was limited to NAf.160.3 million. The increase in 2005 was attributed to a NAf.210.4 million (7.4%) increase in investments, while current assets decreased by NAf.50.1 million (25.3%). On the liabilities side, the largest increase -- NAf.44.7 million (2.5%) -- was noted in the technical provisions. Furthermore, other provisions and liabilities increased from NAf.1.8 million to NAf.40.8 million. Equity increased by NAf.88.4 million, mainly because a higher amount of the net profit was retained with the companies.

The solvency requirement of the international non-life insurance sector amounted to NAf.125.0 million, while the equity available to cover the solvency requirement amounted to NAf.1.3 billion in 2005. From these figures, it can be concluded that the sector had a solvency surplus excess of NAf.1.2 billion in 2005.

Table 27 Consolidated balance sheet of the non-life insurance industry (in millions NAf.)

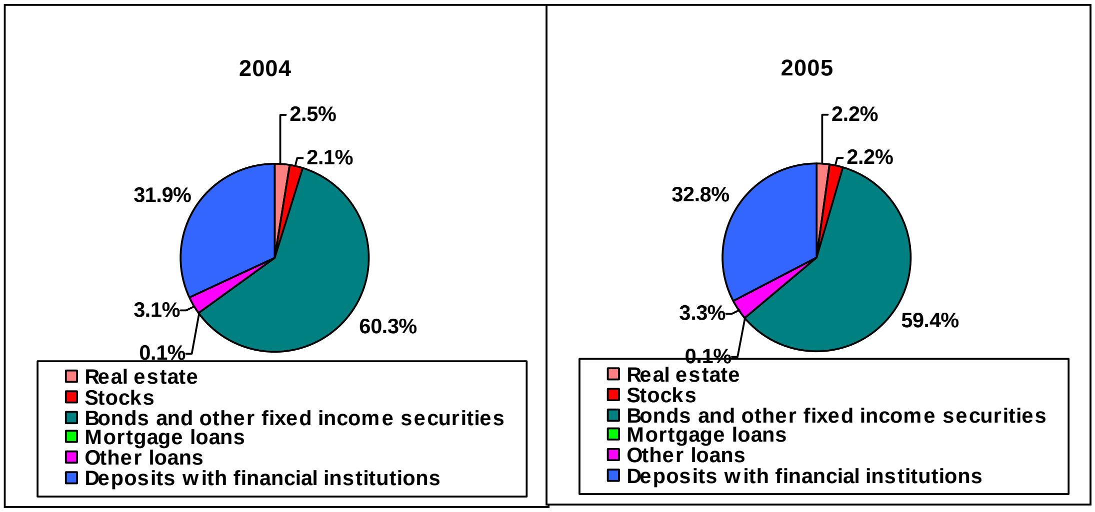
	2003		2004		2005	
	Local	**Int'l**	**Local***	**Int'l**	**Local**	**Int'l**
ASSETS						
Intangibles	-	-	1.0	-	3.5	-
Total investments	234.3	2,398.8	248.0	2,846.2	282.9	3,056.6
Current assets	197.3	316.6	181.1	198.1	150.1	148.0
Other assets	7.2	0.1	11.1	0.1	11.1	0.1
Total admissible assets	438.8	2,715.5	441.2	3.044.4	447.6	3,204.7
EQUITY, PROVISIONS, AND LIABILITIES						
Capital	75.2	171.7	75.1	312.0	75.1	313.2
Surplus	30.2	827.5	29.8	888.2	50.9	975.4
Subordinated instruments	1.0	-	1.0	-	17.7	-
Technical provisions	187.5	1,612.7	186.2	1,781.0	176.2	1,825.7
Other provisions & liabilities	8.1	12.1	16.9	1.8	12.4	40.8
Current liabilities	136.8	91.5	132.1	61.4	115.1	49.6
Contingent liabilities	-	-	0.1	-	0.2	-
Total equity, provisions, and liabilities	438.8	2,715.5	441.2	3.044.4	447.6	3,204.7

* Due to adjustments by some companies, the 2004 figures of the local non-life insurance industry have changed.

5.4.2 Investments

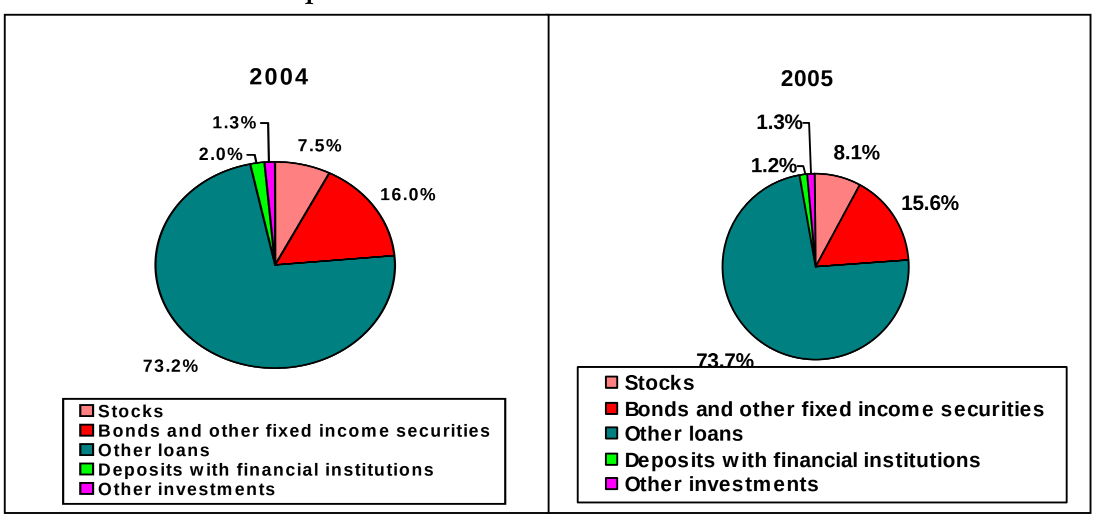
The composition of the investment portfolio of the local non-life insurance companies is presented in graph 8. As was the case in previous years, only some minor portfolio changes took place in 2005 compared to 2004. Bonds decreased from 60.3% of total investments in 2004 to 59.4% in 2005, while deposits with financial institutions increased from 31.9% of total investments to 32.8%. The changes in other instruments were less than 0.5 percentage point.

Graph 8 Composition of the investment portfolio of the local non-life insurance companies



The composition of the investment portfolio of the international non-life insurance companies is illustrated in graph 9. Similar to the local non-life insurance companies, only some minor portfolio changes took place. The graph indicates that, similar to previous years, the largest share of total investments consisted of other loans. Most of these other loans comprised loans and other interest-bearing receivables due from affiliates.

Graph 9 Composition of the investment portfolio of the international non-life insurance companies



5.4.3 Profit and loss statement

Table 28 shows that net earned premium of the local non-life insurance industry increased by NAf.7.5 million (3.5%) in 2005, compared to an increase of NAf.12.7 million (6.4%) in 2004. The net claims incurred during 2005 increased slightly by NAf.2.4 million (2.2%), while an increase of NAf.13.2 million (14.0%) was noted in 2004. The underwriting expenses and changes in various provisions decreased by NAf.16.8 million (16.5%) in 2005. The local non-life insurance sector experienced an underwriting result of NAf.18.8 million in 2005, an improvement compared to the negative underwriting result of NAf.4.8 million reported in 2004. Net investment income decreased slightly by NAf.1.7 million to NAf.15.8 million in

2005. The industry realized a net profit of NAf.24.2 million in 2005, an improvement of NAf.20.6 million compared to 2004.

Table 28 Consolidated profit and loss statement of the non-life insurance industry (in millions NAf.)

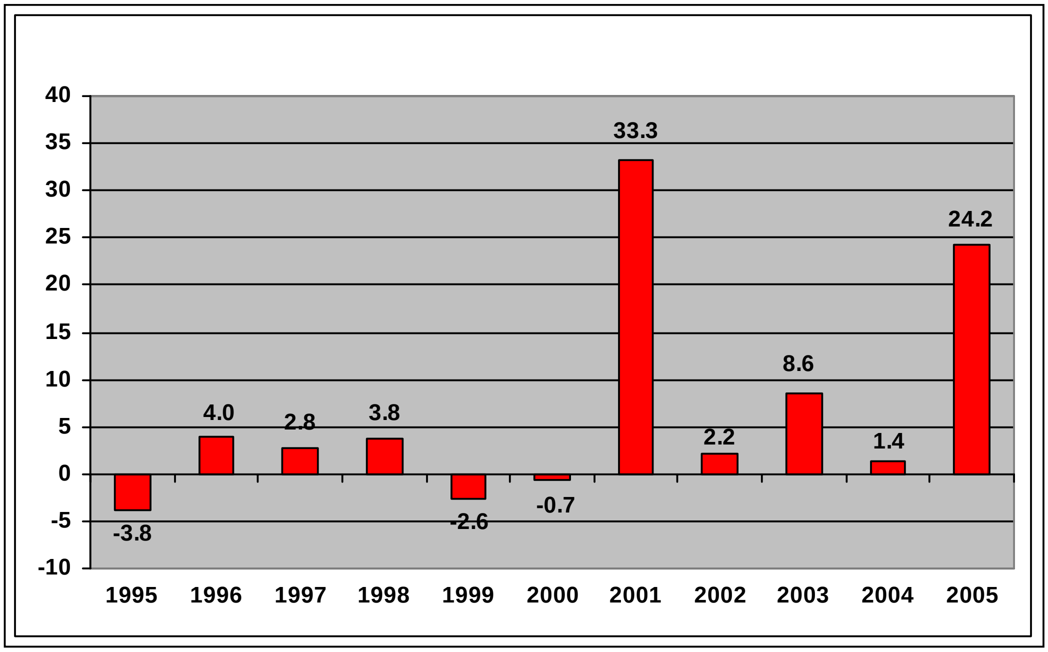
	2003		2004		2005	
	Local	**Int'l**	**Local***	**Int'l**	**Local**	**Int'l**
INCOME						
Total net earned premium	199.1	558.8	211.8	807.4	219.3	699.1
Net other underwriting income	0.2	2.3	0.7	2.9	0.7	0.6
Total operational income	199.3	561.1	212.5	810.3	220.0	699.7
EXPENSES						
Net claims incurred	94.0	460.8	107.2	420.5	109.6	358.1
Claim adjustment expenses	5.1	1.1	4.8	0.9	4.7	1.2
Changes in various provisions	1.1	150.2	2.2	147.8	-6.9	105.4
Underwriting expenses incurred	90.9	55.6	99.5	48.3	91.8	61.9
Net other operational expend.	0.9	2.9	3.6	2.6	2.0	3.4
Total operational expend.	192.0	670.6	217.3	620.1	201.2	530.0
Underwriting result	7.3	-109.5	-4.8	190.2	18.8	169.7
Net investment income	15.9	99.9	17.5	123.8	15.8	137.3
Other results	-4.3	32.5	-5.9	27.1	-1.9	-11.7
Extraordinary results	-4.6	-7.0	-2.9	-2.7	-	5.4
Net result before corp. taxes	14.3	15.9	3.9	338.4	32.7	300.7
Corporate taxes incurred	5.7	11.3	0.3	26.4	8.5	20.5
Net unrealized gains or losses	-	27.8	-	20.1	-	17.4
Net profit or loss	8.6	32.4	3.6	332.1	24.2	297.6

* Due to adjustments by some companies, the 2004 figures of the local non-life insurance industry have changed.

While the internationally operating non-life insurance companies reported a significant increase in net earned premium of NAf.248.6 million in 2004, this figure decreased by NAf.108.3 million in 2005. In addition to the decrease in net earned premium, total operational expenditures decreased by NAf.90.1 million in 2005. This decrease resulted from a decline in net claims incurred (NAf.62.4 million) and a decline in changes in various provisions (NAf.42.4 million). Despite the decrease in the operational expenditures, the sector's underwriting result deteriorated by NAf.20.5 million to NAf.169.7 million in 2005. The industry experienced a further increase in net investment income by NAf.13.5 million in 2005. The high underwriting result together with the net investment income was a major contributor to the net profit of NAf.297.6 million in 2005.

Graph 10 presents an overview of the consolidated net results after taxes of the local non-life insurance companies from 1995 to 2005. This graph depicts that the sector reported low net results during most of the years, except for 2001 and 2005. The large positive net result in 2001 was mainly due to the relatively high net investment income earned in that year while the net result in 2005 was mainly attributable to lower operational expenditures.

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



5.5 Overview of developments in the pension industry

5.5.1 Introduction

Awareness of the need for an adequate pension after retirement has grown in recent years. A decade ago, approximately only one third of the employed Antillean population had a second pillar pension plan.[15] The Bank recently conducted a survey to determine the number of persons with a second pillar pension plan as of the end of 2005. All pension funds plus group pension contracts with life insurance companies comprised approximately 30,900 active participants and 11,500 pensioners. An active participant in this respect is an employee participating in a pension scheme.

To make citizens aware of the importance of properly providing for their retirement, various seminars on pension issues were organized in the past two years. These seminars emphasized that the current state pension, AOV, despite the recent increase, is not enough to meet the financial needs after retirement. Pension service providers have aggressively started marketing their pension products to fill this gap.

As of January 2007, the government decided to increase the AOV pension from a maximum of NAf.554 to NAf.654 per month. In addition, pensioners meeting certain criteria are eligible for an additional NAf.100 per month. The general increase will be financed by an increase in the premium from 10% to 11.5%. The special increase of NAf.100 per month will be financed directly from the government budget.

In addition, discussions are continuing on how to finance the AOV pension in the long run. The aging of the Antillean population makes the financing of this social benefit more costly. One solution brought forward was to increase the current retirement age from 60 to 62 and eventually even to 65.

[15] A collective pension plan in addition to the state pension (AOV).

An internal committee of the Bank is working on a draft of a new law to amend the national ordinance governing the supervision of corporate pension funds. The intention is for this ordinance to provide for the supervision of second pillar pension arrangements and not only corporate pension funds as is currently the case. The new ordinance will be more in line with current market developments and international requirements with respect to pension plan supervision.

The number of active (corporate) pension funds in the Netherlands Antilles subject to supervision by the Bank as per year end 2006 was 26. This number does not include the number of pension funds in the process of liquidation. Pension funds in liquidation remain subject to supervision by the Bank.

5.5.2 Balance sheet

The equity position of the pension funds continued to improve in 2005, increasing by 33.6% compared to 2004. The ratio of investment-to-provision for pension obligations also improved, from 100.2% in 2004 to 102.1% in 2005. A further increase of this ratio would strengthen the financial position of the pension funds to the benefit of the participants. The Bank considers a ratio of 105% on a gross basis as a minimum. The latter depends also on the specific circumstances of each fund, whereby the average age of the participants in the fund and the financial strength of the sponsor play an important role.

The total assets of the pension funds increased by 4.4% in 2005 compared to 2004. The current assets and current liabilities represented 8.8% and 2.3%, respectively, of total assets.

Table 29 Consolidated balance sheet of the pension industry (in millions NAf.)

	2003*	2004*	2005
Assets			
Total investments	4,741.0	4,923.6	5,139.5
Current assets	284.8	470.9	499.1
Other assets	85.2	17.8	12.4
Total	**5,111.0**	**5,412.3**	**5,651.0**
Equity, provisions, and liabilities			
Equity	305.5	364.5	486.8
Provisions for pension obligations	4,672.2	4,915.0	5,032.3
Current liabilities	133.3	132.8	131.9
Total	**5,111.0**	**5,412.3**	**5,651.0**

*) Draft figures were replaced by audited figures. Some 2003 and 2004 figures have been regrouped for comparison purposes.

5.5.3 Profit and loss statement

The net investment income and capital gains and losses declined for two consecutive years. Nevertheless, the 2005 amount still exceeded the minimum required amount equal to 4% of the provisions for pension obligations. Therefore, the pension funds maintained an adequate net investment performance. The addition to the provisions for pension obligations in 2005 was less than the amount in 2004. In addition, due to the release of assigned surplus, the pension funds sector reported a strong increase in other income (232%). As a result, the 2005 operational result increased by 154.5% compared to 2004.

The 2005 operational result represented 4.8% of the provision for pension obligations and 4.3% of total assets, which is above the rate of 4% generally used by most of the local pension funds to discount the (future) pension obligations. The operational expenses incurred by the sector represented 0.5% of the provisions for pension obligations and 15.5% of the pension contributions.

Table 30 Consolidated profit and loss statement of the pension industry (in millions NAf.)

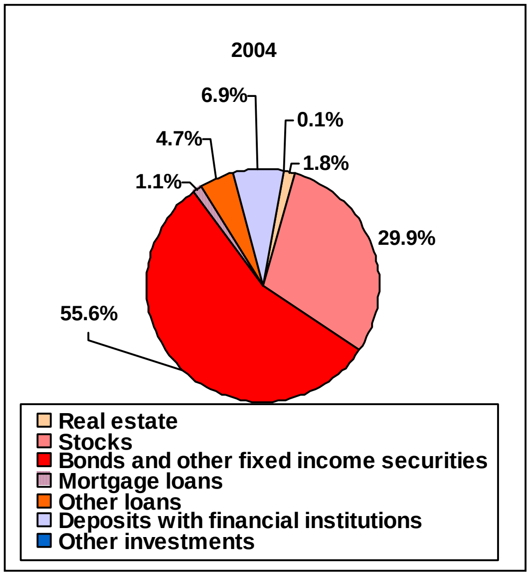
	2003*	2004*	2005
Income			
Contributions	154.5	158.7	163.6
Net investment income and capital gains and losses	427.3	355.6	323.5
Other income	10.4	46.3	153.6
Total income	**592.2**	**560.6**	**640.7**
Expenses			
Pension benefits incurred	173.2	185.4	188.4
Change in net technical provisions	197.1	249.5	168.9
Operational expenses incurred	20.8	23.3	25.3
Other expenses incurred	8.4	7.2	7.0
Total expenses	**399.5**	**465.4**	**389.6**
Extraordinary results	-	-	-8.8
Net profit or loss	**192.7**	**95.2**	**242.3**

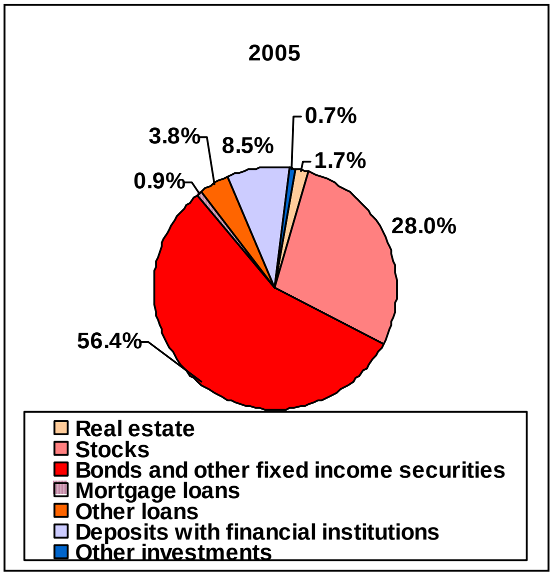
*) Draft figures were replaced by audited figures. Some 2003 and 2004 figures have been regrouped for comparison purposes.

5.5.4 Investments

The composition of the investment portfolio of the pension funds is presented in graph 11. At the end of 2005, bonds and other fixed income securities accounted for 56% of total investments (2004: 56%); stocks accounted for 28% (2004: 30%).

Graph 11 Composition of the investment portfolio of the pension industry





6 POLICIES AND ACTIVITIES OF THE BANK

This chapter provides an overview of important developments in policies and activities of the Bank in 2006 related to its supervision of the financial sector.

6.1 Supervision of investment institutions and administrators

The Bank started its supervision of investment institutions and administrators in 2002. During 2006, the number of institutions under supervision decreased slightly to 25. Special attention was given to assessing compliance with the policy document on the combating of money laundering and terrorism financing issued in 2005. In addition, department staff gave a presentation on the supervision of investment institutions and administrators in St. Maarten, complemented by regular onsite visits of a number of institutions under supervision.

6.2 Supervision of trust service providers

The trust sector has been subject to the supervision by the Bank since 2004. The number of companies and individuals providing trust services in or from the Netherlands Antilles with a license or exemption of the Bank stabilized at 127 in 2006. The Bank focused on the assessment of the completed Trust Service Providers' Supervisory Questionnaires issued in 2005. Furthermore, the Bank issued a guideline on the combating of money laundering and terrorism financing for the trust sector in 2006. In addition, department staff gave a presentation on the supervision of trust service providers in St. Maarten, complemented by regular onsite visits of a number of institutions under supervision.

6.3 Supervision of bank and credit institutions

At the beginning of 2006, the Bank finalized its examinations of the savings and credit funds; 8 funds were examined. In addition, the Bank conducted quick scans at all small credit unions and one local bank. Moreover, the Bank conducted regular examinations at 7 banks and 2 large credit unions.

The Bank's custodial care of one credit union was ended in 2006 because the circumstances that led to this measure were no longer evident. On the other hand, custodial care by the Bank of another credit union became effective in July, while the licenses of two credit unions were revoked. Furthermore, in September, the Bank began custodial care of an international bank. In October, the license of this bank was revoked, and the Court of First Instance confirmed the Bank's request to institute the emergency measure.

The Bank received 4 requests for an exemption to start local credit extension activities with own means and one request for a license to start activities of an international credit institution. The Bank also received some requests to start money transfer activities in the Netherlands Antilles. However, the evaluation of these requests will be postponed until the revision of the supervisory policy on money transfer has been finalized.

In March, the Bank introduced the Statement of Regulatory Compliance for all credit institutions with foreign banking operations. According to this statement, the institutions have to report to what extent their foreign branches and subsidiaries comply with the rules and regulations in their jurisdiction. If the foreign branch does not comply with all the rules and regulations, an explanation of the reasons and steps to remedy the deficiency must be provided.

Furthermore, as of the second half of 2006, persons or institutions applying for an exemption to start local credit extension activities with own means must file a Source of Funds Declaration with the Bank. In this declaration, they have to indicate the origin or source of their means to extend credit.

Finally, the Bank extended charging supervisory costs to credit unions, savings and credit funds, and individual consumer credit providers ("bon") in 2006.

6.4 Supervision of pension funds and insurance companies

In 2006, the Bank continued working on the revision of the National Ordinance on Company Pension Funds. A first draft of the legislation was discussed with the sector in July.

Regarding the supervision of insurance companies, the Bank issued the guideline Disclosure of Consolidated Financial Highlights of Insurance Companies in March 2006. This guideline stipulates publication by the insurance companies of the balance sheet and profit and loss statement together with a summary of the notes to the audited financial statements.

Furthermore, the Bank continued the investigation of funeral insurers begun in 2005. The objective of the investigation was to assess the companies' business conduct and financial situation. Most of the investigated companies showed room for improvement in their financial administration. Because of the limited powers in the current national decree on the supervision of funeral insurers, the Bank requested the government to expand its supervisory instruments for funeral insurers. As a result, in September 2006, the Minister of Finance approved the introduction of a supervision fee for these companies.

6.5 Integrity aspects of financial sector supervision

During 2006, the Bank continued to adjust and refine the rules and regulations on financial sector integrity. These efforts resulted in the issuance in February 2006 of the new Personal Questionnaire and Policy Rule on Integrity Testing and the revised Policy Rule for Sound Business Operations in the Event of Incidents and Integrity-sensitive Positions. The latter now contains a more detailed listing of 'other cases' with respect to handling incidents. A new regulation regarding the maximum allowed number of (co-)policy positions per person was also issued. The purpose of this regulation is to prevent conflicting interests, such as financial interests and/or controlling interests in several institutions, when combining a number of policy positions in the financial sector.

To improve the processing of applications for integrity testing, the Bank further modified its internal procedures. Instead of a "temporary approval", the applicant now receives an official ruling within two months as stipulated by law. However, if certain antecedents become evident within the scope of continuing integrity testing, the Bank may withdraw the permission. Furthermore, following a change in the screening procedure abroad, the Bank introduced a Declaration of No-Objection to be signed together with the questionnaire. By signing this declaration, the applicant indicates no objection to the Bank obtaining information on eventual antecedents from local and/or foreign bodies relevant to the integrity testing.

6.6 IT aspects of financial sector supervision

In 2006, the Bank conducted a quick scan at all the commercial banks participating in the Netherlands Antilles Clearing System (NACS). In addition, the first step for the introduction of IT governance at the financial institutions was made with the decision to revise the Policy memorandum on IT Examinations and to develop a Financial Institution IT Survey. Furthermore, the Bank issued a letter to all the financial institutions informing them of its intention to issue provisions to the credit institutions in the Netherlands Antilles to implement at least two-factor authentication for financial transactions through the internet no later than June 30, 2007. Finally, steps also were taken for the introduction of the first specific IT procedure: E-Banking Provisions and Guidelines.

6.7 International financial sector policy developments

The Netherlands Antilles, as a member of FATF, endorsed the 40 revised recommendations of 2003. During 2006, both the National Committee on Money Laundering and Terrorist Financing (CIWG) and the Bank worked continuously to implement the new requirements, including the Interpretation Notes and Best Practice Guidance to the Recommendations.

In early 2006, the National Committee on Money Laundering and Terrorist Financing (CWIG) submitted legislation on the reporting of unusual transactions (MOT) and identification in conducting financial services (LIF) to the government that will make the Netherlands Antilles compliant with the new obligations of the FATF 2003 revised recommendations. The scope of the framework for anti-money laundering and combating of terrorism financing will be broadened substantially once the draft laws have been enacted.

Furthermore, the Bank issued Provisions and Guidelines on the Detection and Deterrence of Money Laundering and Terrorist Financing for Company Service Providers. A seminar has been organized by the Bank for the company service providers to inform them of the obligations of these new provisions and guidelines. The Bank also issued clarifications on previously released provisions and guidelines for the various sectors of the financial industry to become effective in 2007.

Finally, staff members of the Bank were actively involved in FATF and CFATF activities in 2006. For the first time, the Bank provided an examiner for the mutual evaluation of a FATF country, namely Ireland. The report on the examination was presented at the FATF plenary meeting in South Africa.

6.8 Conferences and seminars

On February 7-8, 2006, the Bank and IBM organized a seminar on security awareness. A large number of employees of financial institutions participated.

From May 22-24, 2006, the Bank in cooperation with Centro de Estudios Monetarios Latinoamericanos (CEMLA) organized a conference on electronic payment systems. Representatives of various Caribbean islands, Latin American countries, and also Saudi Arabia participated. During the conference, experiences and views were exchanged on legislation and procedures to regulate payments in each country.

Finally, in September, at the request of one credit union, the Bank supported a seminar for members of statutory bodies of that credit union. The objective of the seminar was to explain and clarify financial topics to persons with a limited or no financial background.

7 FOREIGN EXCHANGE REGULATIONS AND LICENSE FEE

7.1 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.

As of October 1, 2005, the Bank eased the rules concerning the distribution between local and foreign investment for insurance companies and pension funds. Before that date, a minimum of 60% of reserves and debt were to be invested locally[16], implying that a maximum of 40% of reserves and debt could be invested abroad. Beginning October 1, 2005, for every amount invested in qualifying local investments, an equal amount may be invested abroad, implying that a maximum of 50% of reserves and debt could be invested abroad. As of April 1, 2006, a further easing came into effect, allowing deviations from the minimum local investment requirement but at a levy.

[16] For the amount of reserves and debt exceeding NAf.20 million.

7.2 Foreign exchange licenses

Compared to 2005, the number of foreign exchange licenses issued by the Bank in 2006 decreased by 92 (6%) to 1,428 (see Table 31). This decrease can be attributed primarily to the drop in the number of foreign exchange exemptions granted to international financial and business companies (64). In contrast, the total capital amount related to the licenses granted increased substantially by NAf.601.4 million (417%) to NAf.745.6 million. This increase can be explained primarily by the licenses granted for borrowing abroad related to hotel projects in St. Maarten (Baby Beach and Cupecoy), the telecommunication sector in St. Maarten, the harbor expansion in St. Maarten, and hotel projects in Curaçao (Santa Barbara and Riffort). Also noteworthy are the decreases in licenses for participation by nonresidents in local companies and portfolio investments abroad, the latter partly the result of the participation by local investors in the financing of the various projects mentioned above.

Table 31 Overview of foreign exchange licenses issued (in millions NAf.)

	2005		2006	
Description	**Number**	**Amount**	**Number**	**Amount**
Establishment company by nonresident	196	24.6	177	9.0
Transfer to own account abroad	32	6.8	23	9.8
Portfolio investment abroad	31	78.5	27	55.0
Borrowing abroad	46	32.0	40	663.4
Lending abroad	8	2.3	9	3.4
Request for foreign bank account	5	-	10	-
Request for local nonresident account	10	-	12	-
Granting guarantee abroad	6	-	1	-
Exemption int. fin. & bus. serv. companies	1,185	-	1,121	-
Other	1	-	8	5.0
Total	1,520	144.2	1,428	745.6

7.3 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 the re-investment of funds abroad, the re-exports of the free-zone companies, payments in Aruban florins, and payments by the central government.

Table 32 provides an overview of the license fees collected monthly from 2004 through 2006. From the total license fees collected in the Netherlands Antilles in 2006, NAf.35,164.3 thousand (59%) was generated on Curaçao, NAf.22,239.1 thousand (38%) on St. Maarten, and NAf.964.5 thousand (2%) on Bonaire. The remaining NAf.785.6 thousand (1%) of license fees was paid through the Bank.

Table 32 License fees collected from 2004 through 2006 (in thousands NAf.)

	2004	2005	2006*
January	3,883.7	3,936.3	4,493.8
February	3,788.3	3,855.8	4,272.0
March	4,524.9	4,534.8	5,165.8
April	3,820.4	4,211.4	4,235.1
May	3,831.8	4,228.8	4,815.9
June	3,956.7	4,306.1	5,097.5
July	3,877.8	4,505.2	4,611.5
August	3,920.5	4,282.0	4,749.7
September	3,625.0	4,228.5	5,312.9
October	3,645.6	3,825.0	4,911.8
November	4,301.0	4,436.2	4,988.4
December	5,311.9	5,318.9	6,499.0
Total	48,487.6	51,669.0	59,153.5

*Preliminary

8 FINANCIAL STATEMENTS FOR THE YEAR 2006

Table 33 Balance Sheet as of December 31, 2006 (before profit distribution)

	2005	2006
ASSETS		
Gold	305,452,117	365,805,528
Receivables and securities in foreign currency	822,208,263	1,319,337,825
Advances to the central government	18,496,965	12,801,491
Government bonds	186,321,470	217,490,594
Other long-term receivables	28,064,909	29,745,966
Fixed assets	99,119,969	91,937,842
Other current assets	17,796,691	34,006,752
Total Assets	1,477,460,384	2,071,125,998
LIABILITIES & EQUITY		
LIABILITIES		
Bank notes in circulation	284,100,143	310,951,560
Residents' current accounts		
- in guilders	657,393,123	666,611,750
- in foreign currency	8,022,870	12,084,756
Residents' time deposits		
- in guilders	174,000,000	219,900,000
Nonresidents' current accounts		
- in guilders	5,826,073	497,232
- in foreign currency	-	421,594,549
Money in custody	838,277	856,734
Other current liabilities	14,927,779	25,299,434
Total Liabilities	1,145,108,265	1,657,796,105
EQUITY		
Undistributed earnings	23,991,211	43,561,425
Specific reserves	248,360,908	309,768,558
Reserve fund	30,000,000	30,000,000
Capital	30,000,000	30,000,000
Total Equity	332,352,119	413,329,983
Total Liabilities & Equity	1,477,460,384	2,071,125,998

The 2005 and 2006 figures are extracted from the audited financial statements.

Table 34 Profit and Loss Account 2006

	2005	2006
INCOME		
Interest income	44,599,035	60,754,035
Interest expenses	-6,955,492	-12,227,164
Net interest income	37,643,543	48,526,871
Foreign exchange results	2,593,540	1,647,285
Miscellaneous income	4,877,699	13,878,871
Subtotal	45,114,782	64,053,027
License fee	51,317,965	59,481,232
Total income	96,432,747	123,534,259
EXPENSES		
Depreciation of fixed assets	5,353,377	4,979,612
Depreciation of printing costs for bank notes	1,000,891	1,026,400
Withdrawn bank notes	313,825	141,055
General expenses	32,373,443	40,025,767
Total expenses	39,041,536	46,172,834
Net income	57,391,211	77,361,425
Distribution of net income:		
Net income	57,391,211	77,361,425
Paid to the central government	-58,183,655	-57,791,211
Change in undistributed earnings	-792,444	19,570,214

The 2005 and 2006 figures are extracted from the audited financial statements.

8.1 Notes to the balance sheet as of December 31, 2006

8.1.1 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 specific reserves after approval by the Minister of Finance. Unrealized losses are deducted from the specific reserves. If these losses are greater than the reserves, the difference will be deducted from the result.

8.1.2 Receivables and securities in foreign currency

The receivables represent balances in current account, time deposits with foreign financial institutions, and securities. The increase in 2006 compared to 2005 is mainly the result of a deposit by a nonresident account holder (see also 8.1.11) and is deemed temporary.

The securities represent investment portfolios. These are valued at market price for securities available for sale and at their amortized cost for securities held to maturity. Unrealized gains from revaluations are added to the specific reserves after approval by the Minister of Finance. Unrealized losses are deducted from the specific reserves. If these losses are greater than the reserves, the difference will be deducted from the result.

8.1.3 Advances to the 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.

8.1.4 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 cost.

8.1.5 Other long-term receivables

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

8.1.6 Fixed assets

These assets, which also include the printing cost of bank notes and assets available for sale, 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.

8.1.7 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.

8.1.8 Bank notes in circulation

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

8.1.9 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.

8.1.10 Residents' time deposits

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

8.1.11 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. The increase in 2006 compared to 2005 is deemed largely temporary.

8.1.12 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 Ordinance on Money held in Consignation (P.B. 1886, no. 22).

8.1.13 Other current liabilities

This item includes accrued interest and accounts payable.

8.1.14 Undistributed earnings

This section discloses the accumulated earnings of the Bank for the current and previous years, less the amounts paid to the central government.

8.1.15 Specific 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 revaluation of securities are added to the specific reserves after approval by the Minister of Finance. Unrealized losses are deducted from the specific reserves. If these losses are greater than the reserves, the difference will be deducted from the result.

The 2006 revaluation resulted in a net increase in reserves of NAf.61.4 million.
The recorded unrealized gains on gold, foreign exchange, and investments were NAf.60.3 million, NAf.0.6 million, and NAf.0.4 million, respectively.

8.1.16 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).

8.1.17 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).

8.2 Notes to the profit and loss account 2006

8.2.1 Interest income

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

8.2.2 Foreign exchange results

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.

8.2.3 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.