ANNUAL REPORT 2007

Bank van de Nederlandse Antillen

1. REPORT OF THE PRESIDENT

1.1 General review

The economy of the Netherlands Antilles recorded robust growth in 2007. Real Gross Domestic Product expanded by 3.7%, the highest rate since 1994. The acceleration in growth was attributable mainly to the strengthening of Curacao's economy[1] (3.5%); St. Maarten posted a growth of 4.5% and Bonaire 5.0%. The expansion in 2007 was induced entirely domestically with the private sector as the engine of growth. Both private investment and consumption increased strongly. Private investment growth was sustained by more domestic as well as foreign financing. The higher private consumption was supported by the growth in employment and consumer credit. Government spending grew only marginally. The expansion in domestic spending was mitigated by a decline in net foreign demand because imports grew much faster than exports. The high import growth resulted mainly from the strong private demand, but the appreciation of the euro vis-à-vis the Netherlands Antillean guilder and the further rise in international oil prices also contributed.

The jobs created through the economic expansion resulted in a further improvement of the labor market, reflected by a decline in the weighted average unemployment rate of the Netherlands Antilles from 13.2% in 2006 to 11.1% in 2007. The inflation rate remained stable at 2.8% in 2007, despite the rising global energy and food prices and the appreciation of the euro. Government controlled gasoline and utility prices prevented the increase in international energy prices from being fully reflected in domestic prices, while the lower inflation of our principal trading partner, the United States, also helped to keep price rises in check.

A review by sector reveals that all sectors contributed to 2007's expansion, but the most significant growth was seen in the construction, hotels & restaurants, transport, storage & communication, and real estate, renting & business services sectors. Construction activities recorded the highest growth due to various projects in the tourism industry and retail sector. The significant rise in stay-over tourism in Curacao and Bonaire contributed to the expansion in the hotels & restaurants sector. St. Maarten did not show any growth for the second consecutive year, which may indicate that the available accommodations have reached full capacity. However, the various hotel projects underway are expected to provide room for further growth in the number of stay-over visitors. Cruise tourism expanded also, though the expansion was less buoyant than for stay-over tourism. This expansion again was attributable to Curacao and Bonaire because St. Maarten did not post any growth.

Activities in the transport, storage & communication sector also showed favorable development. Airport activities expanded in line with the growth in the number of stay-over visitors. However, only Curacao noted an overall growth in passenger traffic. A decline in the number of transit passengers in Bonaire and St. Maarten caused a fall in the total number of passengers handled. The decline was most pronounced in Bonaire due to fewer stopovers by KLM on its flights to South America. The harbors in the Netherlands Antilles handled more ships and freight related to the high demand for imports, the growth in cruise tourism, and more oil storage and transshipment activities.

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[1] The share of Curacao in the economy of the Netherlands Antilles is approximately 70%.

The financial services sector continued to grow in 2007. Total assets of the domestic banking sector grew more rapidly than in 2006, but profitability declined somewhat as a result of declining interest rates related to intensified competition and developments in the international financial markets. The rapid growth in private sector credit extension seems to have been accompanied by more leniency towards lending standards, resulting in a deterioration in nonperforming loans. This development calls for increased provisioning and more prudence in credit extension. International financial and business services declined in terms of foreign exchange income generated, sustaining the trend that began with the adjustment of the new fiscal framework (NFR) in 2002, which eliminated the more favorable tax treatment of offshore companies vis-à-vis domestic companies. However, an increasing number of tax information exchange agreements are under negotiation or have been concluded, opening the door to start the negotiation of tax treaties. Once concluded, these treaties can create new business, which is expected to turn around the recent decline in activities.

Activities in the manufacturing sector grew moderately owing entirely to the oil sector. The Isla refinery in Curacao recorded increases in the amount of oil refined as well as in operational expenses. Negotiations with the current lessee, the Venezuelan oil company PDVSA, on the privatization of the refinery are still going on amidst increasing public pressure to reduce its burden on the environment and public health. The rapidly rising international oil prices and the global shortage in refining capacity put the island government in a strong negotiating position to demand considerable investments in modernization of the plants to meet international environmental and product standards. Without such investments, the long-term viability of the refinery cannot be guaranteed.

A similar situation exists in the ship repair industry. The government-owned Curacao Dry Dock Company, which recorded a decline in the number of man-hours sold in 2007, is also in need of substantial investments to secure its long-term viability. Thus, the Bank welcomes the government's intention to intensify its search for a strong foreign partner, which should lead to the company's privatization.

The balance of payments recorded its seventh consecutive surplus in 2007, reflected by a further accumulation of net international reserves. As in previous years, large capital inflows explained the surplus, offsetting the current account deficit. The average import coverage remained stable at 2.7 months because the official reserves and merchandise imports grew at par.

The current account deficit more than doubled in 2007 compared to 2006, due mainly to the widening of the trade deficit. The increase in the trade deficit resulted from higher imports while exports declined. Imports increased because of strong domestic demand, the expansion in tourism, higher international fuel prices, and the further appreciation of the euro vis-à-vis the Netherlands Antillean guilder. The decline in exports can be attributed to the free zone as a result of foreign currency restrictions in Venezuela and the aftermath of the fires in the last quarter of 2006 and the first quarter of 2007. The current transfers balance deteriorated also, due to a smaller amount of dividend tax transferred by the Netherlands related to the provisions in the tax arrangement for the Kingdom (BRK). The deterioration of the trade and current transfers balances were mitigated by an improvement of the services and income balances. The improvement of the services balance was accounted for primarily by the strong growth in tourism, construction services for nonresidents on St. Maarten, and increased activities at the refinery in Curacao and the oil terminal in St. Eustatius. The income balance improved as a result of higher interest income received on foreign bonds and other debt instruments.

The higher current account deficit was financed mainly by direct investment and net borrowing from abroad. Direct investment expanded primarily because of an increase in liabilities of domestic companies with their foreign affiliates and more real estate purchased by nonresidents. The increase in net borrowing from abroad was related mainly to the repatriation of funds abroad by local financial institutions, the net decline in domestic companies' foreign bank balances, and the net repayment of trade credit extended to foreign customers. In addition, development aid from the Netherlands increased. The increased foreign financing was mitigated by higher investments in equity securities abroad by the institutional investors.

The general government's[2] cash deficit improved slightly in 2007 compared to 2006, reaching 2.6% of GDP. The improvement was attributable entirely to higher revenues. Tax revenues in particular expanded to which all categories contributed. The strong economic performance explains the gain in tax revenues. In contrast, grants declined due to lower dividend tax transfers from the Netherlands. Expenditures increased also, but at a slower pace than revenues. Wages & salaries and interest payments contributed mainly to the increase in expenditures. The higher wages & salaries were related to indexation and performance evaluations while the interest burden rose as a result of the further accumulation of debt and higher average treasury bill yields. The high interest burden associated with the unsustainable debt ratio of 85% of GDP in 2007 absorbs a considerable share of the budgetary resources, which could have been put to much better use for improving education, crime prevention, strengthening the infrastructure, and poverty alleviation. The fact that the budget would have shown a surplus of 2.3% of GDP if interest payments were excluded serves as a clear example. The Bank welcomes the recent approval by parliament and the island council of Curacao of the draft Kingdom legislation on financial supervision of the budgetary process bringing the start of the debt relief by the Dutch government much closer.

The monetary aggregates continued to grow strongly in 2007, due to domestic as well as foreign factors. The increase in net foreign assets, related to the balance of payments surplus and the annual revaluation of the gold stock, contributed most to the expansion of the money supply. The increase in net domestic assets was fueled by continued strong private sector credit growth and the expansionary impact by the government. The growth in private sector loans occurred in all loan components and on the Leeward as well as the Windward islands. Both the central government and the island governments contributed to the increase in net government credit, due mainly to the expansion of the government securities portfolio of the banks.

After a relatively neutral monetary policy stance in the first half of 2007, the Bank tightened its policy slightly during the second half of the year to temper the strong growth in private sector credit extension. On July 17, the reserve requirement percentage was raised from 13.000% to 13.125% followed by another increase to 13.250% on November 16 to mop up sufficient liquidity when subscriptions by the banks on the auctions of certificates of deposit (CDs) fell short of the targeted amounts. In addition, the reserve requirement measure was adapted in two ways. First, effective October 16, 2007, an omission in the calculation of the reserve requirement was corrected. Second, the two-month period in which the reserve requirement percentage is fixed was considered too rigid and, therefore, was reduced to one month as of November 16, 2007, increasing the effectiveness of this instrument. Furthermore, the Bank changed its

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

lending rate, i.e., the pledging rate, on three occasions in a reaction to the changes in US interest rates and their impact on the local money and capital market. After an increase by 25 basis points to 5.75% on September 7, 2007, a declining trend started on September 21 by 50 basis points and on November 5 by 25 basis points reaching 5.00%. During the first half of 2008, the pledging rate was reduced further in five steps to 2.50% as of May 16.

1.2 Policy considerations

Economic growth in the Netherlands Antilles is expected to remain strong in 2008 and beyond, although some moderation is likely due to the slowdown of the world economy in the aftermath of the international financial crisis and the rising prices of fuel, raw material, and food. In 2008, the economy is estimated to grow at approximately 3% supported by ongoing investments in the construction and tourism sectors, further growth in tourism activities, and the implementation of the Social Economic Initiative. However, inflation is expected to increase rapidly to around 5% because the government is no longer able to absorb part of the continuing increase in international fuel prices and started to adjust domestic gasoline and utility prices. In combination with the rising food prices, the vulnerable groups in our society are hurt particularly, requiring targeted short-term government measures to mitigate the impact of the high prices and prevent an increase in poverty. In the longer run, we must reduce our dependency on oil by intensifying the exploration of alternative sources of energy, such as the sun, wind, and cooling with seawater. The progress made in this area in Bonaire and the pilot program in some hotels in Curacao could serve as examples.

The positive outlook for further growth is more than welcome in a period of structural change on the way towards a new constitutional status for the islands. Although the preparations for the constitutional change are taking much more time than initially envisaged, progress has been made in numerous areas. We must continue expeditiously on this road to our new destination, seizing the opportunities offered and overcoming the inevitable challenges posed.

In the area of public finances, the three smaller islands, Bonaire, Saba, and St. Eustatius, which opted for closer integration with the Netherlands, have fiscal supervision in place, are complying with their budgetary targets, and will see the start of the debt takeover by the Dutch government in the second half of 2008. The islands that are becoming a country in the new constitutional structure, Curacao and St. Maarten, together with the central government are expected to meet the conditions to be eligible for debt relief by the end of the year, creating firm prospects of balanced budgets in 2009 and beyond. However, a major challenge remains creating budgetary room for new policy in areas such as education, crime prevention, poverty alleviation, and infrastructure. Measures to achieve this objective should include tax reform, continued improvements in tax collection, improved governance of public enterprises, and rationalization of the civil service. In addition, in the medium term, pension and health care reform is getting more urgent due to the ageing population and, hence, the increasing strain on future budgets.

The elimination of the central government layer and the resulting new tasks for the future countries of Curacao and St. Maarten provide a unique opportunity to design an efficient and effective government apparatus. This exercise is currently taking place in cooperation with external consultants. The new apparatus can be staffed from the current pool of civil servants at the central and island levels. If civil servants do not meet the required skills, they should be properly trained. Civil servants who become redundant should be adequately compensated and trained for a job in the private sector where employment opportunities look bright.

The constitutional changes also pose major challenges in the area of monetary policy and financial sector supervision. In the new constellation, Curacao and St. Maarten have agreed to share a common central bank and currency, i.e., forming a monetary union. Since autonomous countries have their own policy responsibilities, a monetary union requires a high degree of policy coordination and harmony to ensure a balanced and effective monetary policy. In addition, a well functioning monetary union requires free movement of goods, services, capital, and labor between the countries. Therefore, strong political commitment is required to give up some of the newly won policy autonomy in the interest of a stable and effective monetary union. Furthermore, the central bank's independence should not be subject to discussion. The Bank should be managed by persons with a high degree of professional standing and integrity, irrespective of nationality or place of birth. With regard to the supervisory board of directors, the governments of the two countries could be allowed to nominate candidates according to a predetermined number for each country and provided that certain professional and integrity standards are met.

Another challenge is related to the debt relief. Once the Dutch government begins paying back the outstanding debt of the Netherlands Antilles to its creditors, the domestic economy will have to cope with a substantial increase in liquidity. If not sterilized adequately, this increased liquidity may endanger the stability of the financial system. The Bank's policy approach to resolve this problem is three-fold. First, a gradual schedule of debt relief payments should be agreed upon with the Dutch government, in line with the maturity schedule of outstanding government securities. Second, the investment rule for institutional investors will be eased, allowing them to invest more abroad and, hence, broadening their choice of investment instruments at a comparable risk-return profile. Third, any remaining excess liquidity will be mopped up through some tightening of the traditional monetary policy instruments, i.e., the reserve requirement and CD auctions, if necessary.

The economic prospects for 2008 and beyond look favorable, although international developments are likely to slow the pace of growth somewhat. To sustain this positive outlook, we must all work together expeditiously to finalize the preparations for our new constitutional future. To be successful also requires serious efforts to reconcile the prevailing differences among various groups in our society. In addition, we must continue with the implementation of our structural reform agenda, including the tax system, the labor market, and the reduction of red tape. These reforms are key in improving competitiveness, preserving investor confidence, becoming more resilient to shocks, and raising living standards. If we focus consistently on meeting these objectives, we can step into our new constitutional destiny with confidence.

E.D. Tromp
President

2. INTERNATIONAL ECONOMIC DEVELOPMENTS

During 2007, countries all over the world saw major volatility in financial markets, owing to uncertainty about the impact of the financial crisis in the United States on the world economy. In the summer of 2007, the default of loans in the US sub-prime mortgage market rippled through the structured credit market. The full impact of the credit crunch was felt in mid-August. To ease the financial market pressures, the US Federal Reserve cut the Fed funds rate three consecutive times to 4.25% in 2007. In addition, the major central banks attempted to ease the crisis by pumping more liquidity into the system. The financial market turmoil was deepening in the advanced economies, but so far it has not greatly affected the emerging markets and developing countries. Amid the recent financial market crisis and weakening of the US economy, the world economy slowed in 2007.

The housing slump and credit crunch had a negative impact on US domestic demand, contributing to a slowdown in the US economy with real GDP growth reaching 2.2% in 2007 compared to 2.9% in 2006. Slower domestic activities were driven mainly by private consumption and gross fixed investment, somewhat mitigated by an improvement in net exports. As a result, the current account deficit improved by 10.5% to $711 billion. US exports became more competitive because of the weaker US dollar resulting from the financial market crisis. In line with the weaker economy, the jobless rate rose from 4.5% in 2006 to 5.0% in 2007. So far, the higher energy prices have not had a widespread impact on the prices of goods and services. Higher labor productivity, among other things, kept US consumer prices in check at 2.9% in 2007.

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

	United States			Netherlands			Venezuela		
	2005	2006	2007	2005	2006	2007	2005	2006	2007
Real GDP	3.2	2.9	2.2	1.5	3.0	3.5	10.3	10.3	8.5
Consumer prices (%)	3.4	3.2	2.9	1.7	1.2	1.6	16.0	13.7	18.7
Unemployment rate (%)	4.9	4.5	5.0	6.5	5.5	4.5	8.9	8.4	6.2

Sources: 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.

As noted, the advanced economies were affected most by the financial market crisis originating in the United States. Hence, production in the Euro area slowed down from 2.8% in 2006 to 2.6% in 2007. In contrast, the Netherlands, the fifth-largest economy among the 15 nations that use the euro, showed an increase of 3.5% in 2007. So far, the sub-prime mortgage crisis has not had a major impact on the Dutch economy. Real GDP increase was sustained by gains in consumer spending, investments, and exports, the latter at a slower pace than in 2006. Higher consumer spending led to more activities in the retail & wholesale sector. Both residential and nonresidential fixed investments contributed to the expansion in the construction industry. In addition, the financial and nonfinancial business services sectors benefited from more economic activities. The strong economic performance was accompanied by a lower unemployment rate of 4.5%. In 2007, the Dutch inflation rate accelerated to 1.6%, fueled largely by stronger fuel and food prices.

The economy of our third main trading partner, Venezuela, remained robust, growing at 8.5% in 2007, albeit at a slower pace than in 2006. The economic expansion was backed by the non-oil sector, mainly by the construction, trade, communications, and the financial services sectors. The soaring oil revenues allowed the government to continue financing state projects. The hiring of more public servants, higher wages, and more social programs led to higher public spending. Lax fiscal policy accompanied by credit expansion contributed to a rapid rise in liquidity in the economy. This development boosted consumer demand, outstripping the supply of products, resulting in a shortage of goods. Since the government has enforced exchange and price controls and started nationalizing private companies, investments have declined. Fewer private investments caused shortages of produce, medicines, and construction supplies. As a result, Venezuela's inflation jumped to 18.7%, the highest in Latin America. Increased hiring in both the private and public sectors lowered the jobless rate to 6.2% in 2007. In contrast to 2006, the current account surplus decreased by 26.3% to $2.0 billion, owing mostly to a deceleration in oil exports, which make up about 90% of total export earnings.

3 GENERAL ECONOMIC DEVELOPMENTS IN THE NETHERLANDS ANTILLES

3.1 Introduction

The Netherlands Antillean economy expanded by 3.7% in 2007, the highest rate since 1994, up from 2.4%[3] in 2006. This buoyant growth was aided 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 of goods & services grew at a much faster rate than exports. Annual inflation remained steady at 2.8% in 2007, reflecting partly the slower world oil price increases throughout the year. In line with the favorable momentum in the economy, labor market conditions improved, leading to a lower unemployment rate of 11.1%[4] in 2007, the lowest since 1994.

Among the domestic expenditure components, the greatest impact on 2007 GDP growth came from private demand. Higher private consumption was reflected by the increase in personal credit and the favorable employment and income conditions. Moreover, private investment growth rose further by 6.9% in 2007, sustained by rising mortgages and business loans. Conversely, net foreign demand declined, with subdued exports outbalanced by stronger import demand. The continuous strong consumption and investment raised the volume of imports. The rapid expansion in import demand was due to more activities in the wholesale & retail, tourism, and construction sectors. The import bill was also affected by the appreciation of the euro and the rising global oil prices, the latter less vigorous than in 2006.

Throughout 2007, gross national income growth of the Netherlands Antilles rose, caused largely by more economic activities. The income growth, however, was offset by gains in total consumption and investment, resulting in a reduction in national savings. This contraction was led by a decrease in private savings outweighing the slight improvement in public dissavings. The higher levels of consumption and investment were funded through increased borrowing and foreign financing.

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[3] Revised GDP figure
[4] BNA estimate

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

	2005	2006	2007
Domestic expenditures, of which:	4.8	4.2	11.3
Private sector	3.6	3.8	10.9
- Investment	2.4	2.6	6.9
- Consumption	1.2	1.2	4.0
Government	1.3	0.4	0.3
- Investment	1.4	0.7	0.1
- Consumption	-0.1	-0.4	0.3
Changes in inventory	0.1	0.0	0.0
Foreign net expenditures, of which:	-3.4	-1.7	-7.6
Export of goods and services	1.2	4.4	0.5
Import of goods and services	4.6	6.1	8.1
GDP by expenditures	1.5	2.4	3.7
Net primary income	0.4	0.5	0.3
Gross national income	1.9	3.0	4.0
Net current transfers from abroad	0.8	-1.5	-1.3
Gross national disposable income	2.7	1.5	2.7

Source: BNA estimates.

[a] Expenditure categories data are weighted contributors to GDP growth.

3.2 Domestic production

The economy of the Netherlands Antilles recorded a robust expansion during 2007, supported largely by positive developments in the private sector. In 2007, all sectors reported a growth, but construction, hotels & restaurants, transportation, storage & communication, and real estate, renting & business services were mainly accountable for the overall economic expansion (see Table 3). Throughout 2007, fiscal policy loosened, leading to higher public spending, as outlays on wages & salaries and goods & services were up.

The construction sector continued as one of the main engines of growth, reflected also by an increase in mortgages. Construction investment activities expanded sharply, related to retail trade, hotels, and tourism-related investment projects.

The wholesale & retail trade sector recorded a real value added rise of 1.8% in 2007, somewhat less than in 2006. This slower growth was the result of fewer activities in the free zone. Nonetheless, the adverse results in the free zone were mitigated by more activities in the tourism industry and the resilience of domestic spending. In contrast to the free-zone performance, the number of free-zone visits posted a rapid increase. This increase may be due to the improved registration of free-zone visitors entering the compound.

Production in the financial services sector continued to expand in 2007, aided by both domestic and international financial services in terms of value added, albeit at a somewhat slower pace than in 2006. The performance of the domestic financial services sector moderated, as higher operational expenses mitigated the income growth.

The significant rise in the number of stay-over tourists in the Netherlands Antilles (10.2%) made a positive contribution to the hotels & restaurants sector. The growth in stay-over visitor arrivals was backed by the European, North American, and South American markets. The rise in the number of European visitors was related primarily to the marked appreciation of the euro against the US$. In particular, the number of Dutch tourists rose in 2007 (17.2%), representing 57% of total European travelers. Moreover, the number of Venezuelan visitors almost tripled, leading to a significant growth in South American visitor arrivals. The exchange controls in Venezuela accompanied by the vast divergence of the black market exchange rate of the Bolivar from the official peg might be the reasons for the large influx of Venezuelan tourists to the islands. This development started in the first quarter of 2007, but gradually became more noticeable throughout the year. In 2007, cruise ship visitor arrivals were up by 3.1%, reflecting growth in both Curaçao and Bonaire, whereas St. Maarten posted no growth.

An analysis by islands shows that the positive performance in stay-over tourism was driven mostly by Curaçao in 2007. The European and the South American markets were accountable for the 27.9% increase in the island's stay-over tourism. In addition, Bonaire's stay-over tourism improved significantly (16.9%), supported by a growth in all markets. By contrast, St. Maarten's stay-over tourism remained relatively unchanged in 2007. This muted performance was due to a contraction in the European and Caribbean markets, mitigating the growth in the North American and South American markets. See Table 9 in the appendix for more details.

Table 3 GDP by sector (real percentage changes)

Sector	2005	2006	2007
Agriculture, fishery, & mining	1.7	4.0	7.8
Manufacturing	-0.6	3.3	1.6
Electricity, gas, & water	0.2	0.3	3.0
Construction	4.5	6.4	11.1
Wholesale & retail trade	0.7	2.4	1.8
Restaurants & hotels	-0.6	1.8	6.8
Transport, storage, & communication	-0.4	0.6	2.7
Financial intermediation	5.9	2.8	1.8
Real estate, renting, & business activities	-0.4	4.1	3.7
Private households	-1.3	0.8	2.2
Total private sector	1.2	2.2	2.9
Public sector	3.6	2.9	3.5
GDP	1.5	2.4	3.7

Source: BNA estimates

Total value added in the manufacturing sector exhibited a growth of 1.6% in 2007, attributable solely to more activities in the oil sector. Total operational costs of the "Isla" refinery rose, but the number of man-hours sold in Curaçao's ship repair industry declined.

The development in the transport, storage, & communication sector was more favorable in 2007 than in 2006, with increases in cargo movements across the islands' ports and air transportation. The ports also benefited from more ships being piloted into the harbors.

Additionally, airport-related activities expanded, owing solely to the sharp gain in Curaçao's total passenger traffic. This outturn was reflected by the positive results in stay-over tourism and the air transportation sector.

3.3 Labor market

The situation in the labor market continued to improve in the Netherlands Antilles, reflected by a further decline in the number of unemployed. In line with the declining trend in unemployment was an increase in the number of employed, leading to a lower jobless rate of 11.1%[5] in 2007 (see Table 4), the lowest since 1994. The improved labor market may be propelled largely by the expanding construction, wholesale & retail trade, and hotels & restaurant sectors, which have created more job opportunities in the private sector. The growth in these sectors resulted in hiring more staff, as many companies in these sectors are relatively labor-intensive. Labor productivity in Curaçao[6] turned around from a 7.1% drop in 2006 to an increase of 2.7% in 2007 because of a rise in output produced per hour.

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

	2003	2004	2005	2006	2007
Employed	74,245	74,777	76,212	80,120	82,498
Unemployed	13,439	13,282	14,748	12,214	10,348
Labor force	87,684	88,059	90,960	92,334	92,846
Total population	177,291	179,938	185,817	190,894	196,638
Participation rate	49.5%	48.9%	49.0%	48.4%	47.4%
Unemployment rate	15.3%	15.1%	16.2%	13.2%	11.1%

Source: Central Bureau of Statistics and BNA estimate

The lower jobless rate in the Netherlands Antilles in 2007 was due mainly to a drop in Curaçao's unemployment rate to 11.9%.[7] The reduction in the number of unemployed in Curaçao occurred largely among the female population. The number of unemployed females shrank by 21.0%, while the number of unemployed males fell by 12.3%. Besides the decline in the number of unemployed females, the number of employed females grew at a faster pace than did the number of employed men. The lower unemployment in Curaçao was reflected also by a fall in the youth unemployment rate from 37.8% in 2006 to 24.2% in 2007.

St. Maarten's unemployment rate declined from 13.4% in 2005 to 10.6% in 2007, due to a fall in the number of unemployed. At the same time, the number of employed grew, outpacing the decline in the number of unemployed, resulting in a growth in the labor force. During the period 2005-2007, the number of unemployed males in St. Maarten dropped by 21.7%, whereas the females' number decreased by 5.9%.

3.4 Inflation

The annual inflation rate in the Netherlands Antilles remained unchanged at 2.8% in 2007 compared to 2006. The main contributors to the inflation in 2007 were the

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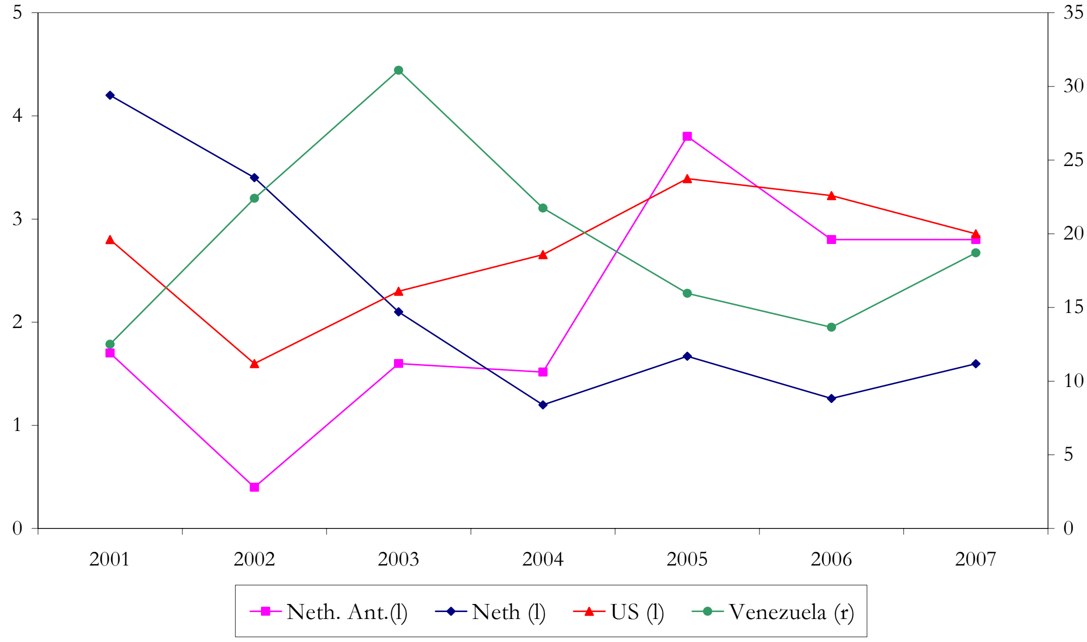
[5] BNA estimate.
[6] BNA estimate; AKO (Labor force survey) 2007, Central Bureau of Statistics. Curaçao makes up about 70% of total employment of the Netherlands Antilles.
[7] AKO (Labor force survey) 2007, Central Bureau of Statistics.

components "food" (7.9%), "housing" (2.6%), and "housekeeping & furnishings" (2.3%). These price increases were largely the result of rising global energy and food prices, and the appreciation of the euro. Consumers had to pay more for food in particular, showing marked price gains pushed up by the price surge in all the food items. Most notably, the prices of basic food products recorded a major increase. By contrast, the changes in international oil prices were only partly reflected in the domestic energy prices. Gasoline and utility prices remained unchanged since June 2005,[8] except for two price adjustments in the third and the fourth quarters of 2007. The higher inflationary pressures were mitigated by lower inflation in the categories "beverages & tobacco" and "transport & communication." Also, the lower inflation of one of our principal trading partners, the United States, may have contributed to the contained inflationary pressures. An analysis by islands reveals that Curaçao registered the highest annual inflation (3.0%), followed by St. Maarten (2.3%), and Bonaire (1.8%). See Table 10 in the appendix for a detailed overview.

Graph 1 Developments in consumer prices (annual percentage change)



3.5 Public finances

3.5.1 Cash overview and financing

A windfall in revenues caused an increase in public spending during 2007. As the increase in revenues outpaced the surge in government expenditures, the budget deficit of the general government[9] declined. The increased government consumption fueled by higher wages and salaries partly contributed to the GDP growth in 2007. The fiscal deficit on a cash basis improved by NAf.19.2 million in 2007 compared to 2006. The higher revenues were attributable mainly to a surge in tax revenues, related to the economic expansion. Nevertheless, the debt-to-GDP ratio increased slightly to 84.7% in 2007, which is high by international standards and shows that the financial situation of the public sector

[8] Gasoline and utility prices in Curacao are set by the island government.
[9] The general government constitutes both the central government and the island government of Curaçao.

remained a cause of major concern. See Tables 11 and 12 in the appendix for a detailed overview.

In addition to the smaller fiscal deficit, the primary balance (i.e., the fiscal balance excluding interest costs) improved also but much more significantly from 1.5% of GDP in 2006 to 2.4% in 2007 (see Table 5). This development illustrates clearly the heavy interest burden accompanying the high level of debt.

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

	2004	2005	2006	2007
Revenues	1,349.1	1,616.2	1,485.6	1,558.0
% of GDP	24.2%	27.7%	24.4%	23.8%
Tax revenues	1,204.9	1,251.8	1,284.1	1,403.1
Nontax revenues and grants	144.2	364.4	201.5	154.9
Expenditures	1,690.2	1,770.7	1,675.2	1,728.4
% of GDP	30.3%	30.3%	27.3%	26.4%
Current expenditures	1,625.5	1,749.6	1,635.6	1,706.4
Capital expenditures	64.7	21.1	39.6	22.0
Balance	-341.0	-154.5	-189.6	-170.4
% of GDP	-6.1%	-2.6%	-3.1%	-2.6%
Primary balance	-84.2	130.0	93.8	152.8
% of GDP	-1.5%	2.2%	1.5%	2.3%

A breakdown of general government revenues reveals that the increase in revenues was caused almost entirely by a surge in tax revenues (NAf.119.0 million) in 2007. The increase in tax revenues occurred in all categories. The drop in nontax revenues and grants was attributable mainly to fewer grants received in 2007. In 2007, 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)[10] amounted to NAf.14.3 million compared to NAf.73.5 million in 2006, causing the receipts from this source to drop by NAf.59.2 million.

A review by level of government shows that the increase in tax revenues of the central government occurred mostly in indirect taxes, while the increase of the island government of Curaçao came from taxes on income & profits and property. Higher domestic spending resulted in a growth in sales tax revenues, excises, and import duties for the central government. For the island government of Curaçao, the increase in profit and income tax revenues can be attributed to the improved business performance and higher employment. Property taxes increased as a result of the reduction of arrears in the collection of the land tax.

A review of general government expenditures reveals that the increase in current expenditures (NAf.70.8 million) contributed entirely to the rise in total expenditures, due primarily to the categories "wages and salaries" and "interest payments." In contrast, capital expenditures dropped by NAf.17.6 million. A breakdown by level of government shows that the increase in current expenditures was accounted for by both governments. The increase in current expenditures of the central government (NAf.9.1 million) was

[10] 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.

related to higher interest payments and outlays for wages and salaries. The increase for the island government of Curaçao (NAf.27.7 million) was caused by gains in outlays for goods & services, interest payments, and wages & salaries.

Capital expenditures of the island government of Curaçao dropped in 2007. In contrast to 2006, when financial resources were made available for the financing of a golf course of a hotel project, such expenditures did not occur in 2007. The increase in capital expenditures of the central government (NAf.12.2 million) in 2007 can be explained by the repayment of a loan by the island governments in 2006 related to the settlement by the central government of their arrears with the government pension fund, APNA. These repayments resulted in a negative amount for the component "net lending" in 2006, which did not occur in 2007.

The budget deficits of both government levels were financed primarily through the net issuance of debt securities in 2007, which was reflected by the monetary financing through the commercial banks and the increase in government securities with the public, i.e., mostly institutional investors (see Table 6). In contrast, the monetary contraction through the central bank was attributable to a decline in government securities in portfolio.

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

	Central government		Curaçao government	
	2006	**2007**	**2006**	**2007**
Monetary financing	-67.4	27.5	-25.3	50.1
Central bank	16.3	-46.0	58.5	-23.7
Commercial banks	-85.2	71.0	-83.7	73.8
Coins and notes	1.5	2.5	0.0	0.0
Nonmonetary financing	155.4	67.2	126.9	25.5
Government securities with the public	180.9	52.0	140.7	42.3
Other	-25.5	15.2	-13.8	-16.8
Cash balance	-88.0	-94.7	-101.6	-75.7

3.5.2 Public sector debt

In 2007, the total consolidated public debt of the Netherlands Antilles expanded by NAf.427.4 million (8.4%) to NAf.5.5 billion (84.7% of GDP). This higher debt was the result of gains in the consolidated domestic debt (NAf.349.0 million) and in the foreign debt (NAf.78.4 million). See Table 12 in the appendix for a detailed overview.

The increased domestic debt was due largely to net borrowing on the capital market by both the central government and the island government of Curaçao. The increase in central government securities (NAf.150.2 million) resulted from a rise in short-term paper (NAf.174.3 million) and a drop in long-term paper (NAf.24.1 million). In contrast, net borrowing by the island government of Curaçao (NAf.83.1 million) was the result of an increase in long-term paper (NAf.121.1 million) and a decrease in short-term paper (NAf.38.0 million).

In addition, the island government of Curaçao incurred further arrears with the government pension fund, APNA (NAf.82.8 million), and built up its debt with other creditors (NAf.56.3 million). Overall, the central government debt increased by NAf.157.4 million (6.8%), while that of the island government of Curacao expanded by

NAf.222.0 million (9.9%). Moreover, the debt of the other islands increased by NAf.8.6 million due to the debt accumulation with the central government.

The increase in the foreign debt in 2007 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.72 million.

3.6 Balance of payments developments

3.6.1 Introduction

In 2007, the current account deficit widened markedly by 127% to NAf.1,055.6 million. This development was due to a worsening of the trade balance and a drop in net current transfers from abroad. The trade balance deteriorated as a result of a sharp increase in merchandise imports accompanied by a drop in exports. In line with the developments on the current account, the capital and financial account deteriorated (See Table 7).

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

	2004	2005	2006	2007
Current account	-157.6	-189.4	-465.2	-1,055.6
Capital transfers	142.2	171.1	179.6	217.7
External financing of the government	4.6	-16.2	-8.5	5.8
External financing of the private sector	27.7	110.1	315.0	961.9
- Direct investment	-0.7	-42.1	-140.5	420.7
- Loans and credits	30.2	194.8	353.9	687.4
- Portfolio investments	-1.7	-42.7	101.6	-146.2
Change in net foreign assets of the banking system*)	-65.7	-132.7	-84.1	-277.4
- with central bank	10.2	-68.8	-73.8	-297.0
- with commercial banks	-75.9	-63.9	-10.5	19.6
Statistical discrepancies	48.9	57.2	63.5	147.5

*) a minus sign implies an increase

3.6.2 Current account

The trade balance deteriorated by NAf.630.2 million in 2007 compared to 2006 as merchandise imports rose (NAf. 597.6 million) while exports dropped (NAf.32.6 million). The substantial increase in merchandise imports was related to higher domestic spending and favorable developments in the tourism industry. Another factor that impacted the value of merchandise imports in the Netherlands Antilles during 2007 was the appreciation of the euro. Oil imports increased as well, due mainly to higher average fuel prices, albeit to a somewhat lesser extent than in 2006. On the Leeward Islands, imports by the retail and wholesale sectors rose sharply due to higher domestic consumption and increased tourism-related activities. Higher private investments in, among other things, hotels and other tourism-related industries, the retail sector, and the transportation industry also resulted in higher imports. However, merchandise import growth was partially offset by a drop in imports by the free-zone companies related to lower re-exports. On the Windward Islands, the increase in imports of non-oil products was attributable to higher private consumption. Furthermore, the ongoing construction activities in the tourism industry contributed to the import growth.

Merchandise exports dropped due largely to a decline in re-exports by the free-zone companies. This development can be ascribed to currency trading restrictions in Venezuela and the fire outbreaks that took place in the free zone in the last quarter of 2006 and the first quarter of 2007. The decline in exports was partially offset by an increase in earnings from bunker sales reflecting higher average fuel prices. Moreover, foreign exchange revenues from ship repair activities rose in 2007.

In contrast to the trade balance, the services balance improved in 2007 by NAf.115.0 million. This improvement was related almost entirely to a marked rise in tourism in Curaçao. Foreign exchange receipts from stay-over tourism on this island increased by NAf.89.5 million in 2007, while those from cruise tourism rose by NAf.4.4 million. The foreign exchange earnings from stay-over and cruise tourism on Bonaire rose by NAf.27.5 million and NAf.5.8 million, respectively. Moreover, on the Windward Islands, revenues from stay-over tourism increased by NAf.7.6 million and from cruise tourism by NAf.10.9 million.

Higher earnings from construction services also contributed to the improvement of the services balance. This increase was led by a rise in construction of properties on St. Maarten owned by nonresidents. Furthermore, increased activities at the refinery in Curaçao and the oil terminal in St. Eustatius resulted in a growth of the refining fee. The improvement of the services balance was partially offset by increased foreign exchange expenses on freight transportation, reflecting higher merchandise imports. Furthermore, the import of construction services rose, due to the ongoing construction activities in the tourism industry on Curaçao and St. Maarten. In addition, foreign exchange revenues from international financial and business services declined in 2007 owing to a decline in trust services provided to abroad. The developments on the trade and services balances resulted in a substantial decline of NAf.515.2 million in net exports of goods and services.

The income balance improved by NAf.20.2 million in 2007, due largely to higher interest income received on bonds and other debt instruments. Higher dividend payments by resident companies to their foreign affiliates partially mitigated this improvement. Meanwhile, the current transfers balance worsened by NAf.95.3 million because of a smaller amount of dividend tax transferred by the Netherlands in light of the tax arrangement for the Dutch Kingdom (the BRK arrangement). Overall, the current account recorded a deficit of NAf.1,055.6 million in 2007, representing a deterioration by NAf.590.4 million compared to 2006. See Table 13 in the appendix for an overview.

3.6.3 Financing of the current account balance

In line with the worsening current account, net foreign indebtedness of the private sector increased, indicating a drop in net foreign wealth. The increased indebtedness was related to a worsening of the loans and credits (NAf.687.4 million) and direct investment (NAf.420.7 million) balances. In contrast, the portfolio investment balance improved (NAf.146.2 million) due mainly to increased investments in equity securities abroad by institutional investors.

The worsening of the loans and credits balance was related, among other things, to the repatriation of funds abroad by local financial institutions. Furthermore, the balance of domestic companies' foreign bank accounts dropped in 2007, largely to finance part of their increased imports. A decline in the net trade credits balance contributed also to the worsening of the loans and credits balance. Net trade credits extended abroad declined, offsetting the drop in net trade credits received on imports. Net trade credits extended abroad declined because the growth in repayments exceeded the rise in trade credits extended to foreign customers. Net trade credits received on imports dropped because the increase in repayments outpaced the rise in new trade credit.

The direct investment balance deteriorated primarily because of an increase in liabilities of resident direct investment companies with their foreign affiliates. In addition, nonresidents purchased more real estate in the Netherlands Antilles in 2007.

Capital transfers grew by NAf.37.9 million in 2007, related to an increase in development aid funds received from the Netherlands. As a result of all international transactions during 2007, net foreign assets (i.e., reserves) increased by NAf.277.4 million compared to 2006, reflecting a surplus on the balance of payments. See Table 14 in the appendix for a detailed overview.

3.7 Monetary developments

3.7.1 Monetary policy

During 2007, the Bank's monetary policy was directed mainly towards curbing the excessive growth in private credit extension[11]. To maintain the external stability of the Netherlands Antillean Guilder (NAf.), via the fixed peg with the US$, the Bank aims to maintain a level of official reserves (excluding gold) that covers at least three months of goods imports. This goal is pursued by influencing bank liquidity in the domestic money market and, hence, the ability of the banks to extend credit. The Bank has two main instruments at its disposal to influence bank liquidity, namely, the reserve requirement[12] and the auctioning of certificates of deposit (CDs). In the first half of 2007, monetary conditions did not warrant the active use of the reserve requirement. It was not until July 16, 2007, that the Bank raised the reserve requirement percentage from 13.000% to 13.125%. This decision was taken due to the strong growth in credit extension to both the private sector and the government. Furthermore, the commercial banks had less appetite to invest in CDs. During the second half of 2007, a further tightening in the domestic money market was pursued through the auctioning of CDs. The reserve requirement percentage remained unchanged until November 16, 2007. A shortfall in subscriptions on CDs and strong private credit growth prompted the Bank to raise the reserve requirement percentage from 13.125% to 13.250%. Furthermore, the reserve requirement measure was adapted in two ways. First, effective October 16, 2007, an omission in the calculation of the reserve requirement was corrected by excluding deposits of unconsolidated subsidiaries and affiliates. Second, the two-month period in which the reserve requirement percentage is fixed was considered too rigid and, therefore, was reduced to one month as of November 16, 2007, increasing the effectiveness of this instrument.

The other monetary policy instrument of the Bank, the bi-weekly auction of CDs, is used to mop up excess liquidity in the domestic money market. In contrast to the reserve requirement, this instrument is more market-driven because participation in the auctions is voluntary. The use of this instrument was successful during the first half of 2007 with

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

[12] Via 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.

an average monthly outstanding amount of NAf.43 million. However, during the second half of 2007, the average outstanding amount dropped to NAf.28 million by November 2007 because the amounts offered were not fully subscribed. As of November, the focus changed from mainly rolling over maturing CDs to auctioning more CDs. This change proved successful as the amount of outstanding CDs increased to NAf.52.8 million at the end of 2007.

Due to the peg to the US$, the Bank's interest rate policy follows closely that of the Federal Reserve System of the United States and, hence, US market interest rates. After the development in international interest rates prompted the Bank to raise its lending rate, i.e., the pledging rate, on September 7, 2007, by 25 basis points to 5.75%, a declining trend started on September 21. On that date, the pledging rate was lowered by 50 basis points following a similar reduction by the Fed. On November 5, a second reduction was effectuated, by 25 basis points to 5.00%.

3.7.2 Net accumulation of wealth and the money supply

Money holdings of the private sector increased by NAf.658.3 million (12.1%) during 2007, an acceleration compared to the rise of NAf.491.7 million (10.0%) in 2006. The increase in domestic liquidity in 2007 stemmed from increases in domestic bank credit, external financing, and capital transfers from abroad, mitigated by the financing needed to cover the net current international transactions and the financing provided by the private sector to the government. See Tables 15A and 15B in the appendix for more details.

3.7.3 Factors affecting the money supply

The rise in the money supply in 2007 (12.1%) implied an acceleration compared to the increase (10.0%) in 2006. Contrary to 2006, it was the increase in net foreign assets that contributed most to the increase in the money supply in 2007. Net foreign assets expanded by 19.7% in 2007 compared to the increase of 8.9% in 2006. This expansion was largely the result of an increase in the Bank's official reserves (29.5%).

The increase in the domestic component of the money supply amounted to 8.5% in 2007 compared to 10.5% in 2006. The expansion in 2007 can be accounted for by increases in both net credit extended to the private sector (11.7%) and to the government sector (10.3%). Net credit to the private sector increased primarily due to an increase in commercial bank loans extended (13.1%), in line with more private sector activities. The expansion in private loans was the result of increases in all loan components on both island groups, with the exception of mortgages extended on the Windward Islands, which dropped 1.6% in 2007.

The increase in net credit extended to the governments resulted from increases at both the central government (10.2%) and the island governments (10.5%). Both increases resulted from the rise in government securities in the commercial banks' portfolios, offsetting the decline of these securities in the Bank's portfolio and higher government deposit balances. See Table 16 in the appendix for more details.

3.7.4 Developments in domestic interest rates

In line with the international interest rate developments, both the Bank's official rate, the pledging rate, and the maximum 1-month CD rate dropped during 2007, reaching 5.0% and 4.9%, respectively, at the end of the year.

Commercial bank borrowing rates showed diverse developments in 2007. The average rate on passbook savings dropped by 0.3 percentage point to 2.5%, while the average rate on 12-month time deposits increased by 0.2 percentage point to 4.4%. Lending rates continued their declining trend with the average mortgage rate dropping by 0.5 percentage point to 8.0% and the average rate on time loans by 1.1 percentage point to 9.5%. Increased competition between the domestic commercial banks and lower rates abroad may explain this trend.

Contrary to 2006, the average effective yield of 5-year government bonds dropped in 2007 by 0.3 percentage point to 7.2%. Conversely, the average rate of one-month treasury bills continued increasing, reaching 5.1% at the end of 2007. See Table 17 in the appendix for a detailed overview.

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 16.4% during 2007 compared to 8.9% in 2006. The largest contributors to the increase in 2007 were the loan portfolio (11.3%) non-interest-bearing cash (72.8%), investments (24.4%), and interest-bearing cash (13.5%). The increase in investments can be explained mainly by the expansion of the domestic government securities portfolio. See Table 18 in the appendix for more details.

In 2007, income of the domestic commercial banking sector grew at a slower pace (7.0%) than in 2006 (9.8%). This deceleration was attributable to the decline in "other income" (1.2%) because "net interest income" increased more rapidly (12.0%) compared to 2006 (4.6%). Operational expenses grew by 13.1% in 2007, much faster than in 2006 (1.6%), and outpacing the growth in operational income. As a result, net income after taxes dropped by 8.9% to NAf.161.6 million in 2007. See Table 19 in the appendix for more details.

3.8.2 Macroprudential indicators

The general performance of the domestic commercial banking sector is analyzed by means of the macroprudential indicators (see Table 8). The capital adequacy, as measured by the ratio of total capital against total assets, improved slightly to 8.8% in 2007 compared to 2006 as the increased capitalization and general provisions surpassed the growth in total assets.

The ratio of nonperforming loans-to-total loans increased further during 2007, revealing a worsening in the quality of the asset base. This development is also revealed by the decrease in the provisions for loan losses-to-non-performing loans ratio. Both these developments can be explained by the increase in non-performing loans, which exceeded the growth in both total loans and provisions for loan losses.

All three earnings-related indicators continued to deteriorate in 2007 because assets grew at a faster pace than income. Income growth may be under pressure as a result of stiffer competition in the local banking sector and the decline in international interest rates. The ratio of total loans to total deposits dropped during 2007. This development reveals an increase in liquidity in the domestic banking sector.

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

	2004	2005	2006	2007
Capital adequacy				
Total capital/ total assets	7.9	7.9	8.7	8.8
Asset quality				
Non-performing loans/ total loans	3.6	2.6	3.6	4.6
Provisions for loan losses/ non-performing loans	92.7	106.0	87.3	66.8
Earnings				
Gross earning-assets yield	7.3	7.5	7.1	6.9
Net interest margin	4.9	5.1	4.5	4.4
Return-on-assets	1.7	2.3	2.2	1.8
Liquidity				
Total loans/ total deposits	64.9	61.9	64.2	61.4

APPENDIX

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

	Curaçao				St. Maarten				Bonaire			
	2006		2007		2006		2007		2006		2007	
North America, of which:	8.4	(0.6)	-3.7	(-0.2)	-1.7	(-0.6)	3.4	(1.2)	6.7	(0.2)	19.4	(0.8)
-U.S.A.	4.7	(0.3)	-3.2	(-0.2)	-0.3	(-0.1)	3.2	(0.9)	5.6	(0.2)	19.8	(0.8)
Europe, of which:	9.8	(1.3)	16.5	(2.4)	3.5	(0.4)	-0.7	(-0.1)	-6.2	(-0.2)	11.4	(0.4)
-The Netherlands	9.5	(1.1)	17.8	(2.1)	2.6	(0.1)	6.6	(0.1)	-6.9	(-0.2)	23.1	(0.6)
South & Central America, of which:	-2.7	(-0.1)	113.2	(10.9)	26.4	(0.4)	10.3	(0.2)	15.2	(0.1)	25.6	(0.1)
-Venezuela	-11.6	(-0.3)	184.3	(13.3)	-8.0	(0.0)	79.5	(0.3)	0.6	(0.0)	54.6	(0.2)
-Other	9.3	(0.2)	15.8	(0.3)	16.4	(0.2)	-3.8	(0.0)	---	---	---	---
Caribbean, of which:	-0.4	(0.0)	20.8	(1.0)	-3.4	(-0.2)	-9.8	(-0.4)	22.9	(0.1)	21.2	(0.1)
-Aruba	19.0	(0.3)	13.8	(0.2)	---	---	---	---	28.4	(0.1)	21.9	(0.1)
-Dominican Republic	-27.4	(-0.1)	-4.0	(0.0)	-6.9	(0.0)	-8.9	(0.0)	---	---	---	---
-Other	-5.3	(-0.1)	31.5	(0.8)	-3.1	(-0.1)	-9.9	(-0.4)	---	---	---	---
Total	5.5	(1.7)	27.9	(9.9)	0.0	(0.0)	0.3	(0.2)	1.6	(0.1)	16.9	(1.6)

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)

	2004	2005	2006	2007
Food	4.4	7.2	7.1	7.9
Beverages & tobacco	-0.4	2.6	3.6	2.7
Clothing & footwear	-0.2	-0.6	0.1	0.8
Housing	1.8	5.2	2.6	2.6
Housekeeping & furnishings	0.5	5.3	2.4	2.3
Health	0.9	1.3	0.6	0.7
Transport & communication	0.8	2.7	2.3	1.9
Recreation & education	0.2	0.3	0.4	0.8
Other	0.6	1.4	2.0	1.6
General inflation rate	1.5	3.8	2.8	2.8

Source: Central Bureau of Statistics

Table 11 Budgetary overview (in millions NAf.)

	2004	2005	2006	2007
General government				
Revenues	1,349.1	1,616.2	1,485.6	1,558.0
Tax revenues, of which:	1,204.9	1,251.8	1,284.1	1,403.1
Taxes on income and profits	578.3	598.2	582.4	617.2
Taxes on goods and services	458.9	479.1	502.0	532.4
Taxes on international trade and transactions	127.0	130.7	143.9	166.1
Nontax and grants	144.2	364.4	201.5	154.9
Expenditures	1,690.2	1,770.7	1,675.2	1,728.4
Current, of which:	1,625.5	1,749.6	1,635.6	1,706.4
Wages and salaries	554.9	678.9	561.0	586.2
Goods and services	436.5	433.2	416.3	424.4
Subsidies	44.3	42.2	44.4	44.0
Transfers	332.9	310.9	330.4	328.6
Interest payments	256.8	284.5	283.4	323.2
Capital	64.7	21.1	39.6	22.0
Budget balance	-341.0	-154.5	-189.6	-170.4
Central government				
Revenues	692.3	912.6	822.6	837.2
Tax revenues, of which:	577.2	607.4	649.3	710.7
Taxes on goods and services	420.7	440.6	461.4	492.3
Taxes on international trade and transactions	127.0	130.7	143.9	166.1
Nontax and grants	115.1	305.2	173.3	126.5
Expenditures	898.4	991.7	910.6	931.9
Current, of which:	868.1	979.7	908.4	917.5
Wages and salaries	292.9	282.7	295.5	312.2
Goods and services	107.2	123.5	117.7	105.7
Transfers	324.3	427.9	348.2	324.3
Interest payments	142.0	145.6	147.0	175.3
Capital	30.3	12.0	2.2	14.4
Budget balance	-206.1	-79.1	-88.0	-94.7
Island government of Curaçao				
Revenues	818.7	982.3	842.5	866.3
Tax revenues, of which:	627.7	644.4	634.8	692.4
Taxes on income and profits	578.3	598.2	582.4	617.2
Taxes on goods and services	38.2	38.5	40.6	40.1
Nontax and grants	190.9	337.9	207.7	173.9
Expenditures	953.6	1,057.6	944.1	941.9
Current, of which:	919.2	1,048.5	906.6	934.3
Wages and salaries	262.0	396.2	265.5	274.0
Goods and services	329.3	309.7	298.6	318.7
Transfers	170.4	161.6	161.7	149.8
Interest payments	114.8	138.9	136.4	147.9
Capital	34.4	9.1	37.4	7.6
Budget balance	-134.9	-75.4	-101.6	-75.7

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

	2004	2005	2006	2007
Domestic consolidated debt, of which:	3,984.8	4,145.0	4,369.9	4,718.9
Central government, of which:	2,074.6	2,233.5	2,323.7	2,481.1
Long-term securities	1,700.0	1,771.6	1,897.0	1,872.9
Short-term securities	104.9	94.4	57.3	231.5
APNA	118.4	209.0	217.6	129.4
SVB	6.5	13.9	8.4	6.4
Curacao, of which:	2,262.1	2,123.1	2,239.3	2,461.3
Long-term securities	733.3	737.4	802.1	923.2
Short-term securities	144.5	202.6	201.9	163.8
APNA	827.2	758.4	797.0	860.8
SVB	0.0	0.0	0.0	0.0
Central government	428.0	300.5	301.4	321.0
Other islands	350.7	312.6	334.8	343.4
Foreign debt	727.2	655.5	742.3	820.8
Total debt (consolidated)	4,712.0	4,800.5	5,112.2	5,539.6
(% of GDP)	84.5%	82.2%	83.3%	84.7%

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

	2004	2005	2006	2007
Trade balance	-2,150.8	-2,402.5	-2,711.2	-3,341.4
-Exports	1,088.3	1,088.3	1,243.5	1,210.9
-Imports	-3,084.0	-3,490.9	-3,954.7	-4,552.2
Services balance	1,925.0	2,042.7	2,206.8	2,321.8
Receipts, of which:	3,222.3	3,356.5	3,564.2	3,758.5
-Travel	1,676.2	1,771.2	1,824.6	1,966.1
-Transportation	220.7	226.9	236.3	259.2
-Other services, of which:	1,325.4	1,358.4	1,503.4	1,533.2
- Int. fin. & bus. services sector	432.6	396.2	402.8	354.9
Expenses, of which:	1,297.3	1,313.8	1,357.4	1,436.8
-Travel	502.3	471.4	504.0	557.9
-Transportation	139.6	153.3	148.4	164.5
-Other services, of which:	655.4	689.1	705.0	714.3
- Int. fin. & bus. services sector	150.5	136.3	148.7	135.4
Income balance [a]	-29.7	-27.0	-1.8	18.4
Current transfers balance [b]	97.9	197.4	41.0	-54.3
Current account balance	**-157.6**	**-189.4**	**-465.2**	**-1,055.6**
Capital & financial account balance [c]	**108.8**	**132.2**	**401.9**	**908.0**
Net errors & omissions	**48.9**	**57.2**	**63.5**	**147.5**

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

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

	2004	2005	2006	2007
Direct investment	-0.7	-42.1	-140.5	420.7
- Abroad [a]	-39.6	-117.0	-101.3	5.8
- In the Netherlands Antilles [b]	38.9	74.9	-39.2	414.9
Portfolio investment [a]	-1.6	-42.7	101.6	-146.2
Other investment, of which:	136.3	243.6	547.1	450.9
- Assets [a]	49.1	173.0	417.4	414.6
- Liabilities [b]	87.2	70.6	129.7	36.3
Net lending/borrowing, of which:	-101.4	-64.9	-201.7	242.3
- Assets [a]	-57.3	-100.6	-71.6	351.0
- Liabilities [b]	-44.1	35.7	-130.1	-108.7
Reserves [c]	-65.7	-132.7	-84.1	-277.4
Total assets [a]	-115.1	-220.0	-262.0	347.8
Total liabilities [b]	82.0	181.2	-39.6	342.5
Balance	-33.1	-38.8	222.4	690.3

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.)

2007	Domestic sectors			External sector
	Private	Government	Banking	
Nonfinancial transactions	-885.2	-170.4		1,055.6
Government net lending	0.0	0.0		
Government domestic nonbank financing	-106.0	106.0		
External financing of the government		5.8		-5.8
External financing of the private sector	961.9			-961.9
-Direct investment (equity)	420.7			-420.7
-Loans and credits	687.4			-687.4
-Portfolio, incl. debt	-146.2			146.2
Capital transfers & acquisitions	217.7			-217.7
Change in net foreign assets of the central bank			-296.9	297.0
Change in net foreign assets of commercial banks			19.5	-19.6
Change in domestic bank credit	474.6	58.6	-533.2	
Change in broad money	-658.3		658.3	
Other items, net/errors & omissions	-4.8		152.3	-147.5

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

2006	Domestic sectors			External sector
	Private	Government	Banking	
Nonfinancial transactions	-287.2	-178.0		465.2
Government net lending	11.6	-11.6		
Government domestic nonbank financing	-250.3	250.3		
External financing of the government		-8.5		8.5
External financing of the private sector	315.0			-315.0
-Direct investment (equity)	-140.5			140.5
-Loans and credits	353.9			-353.9
-Portfolio, incl. debt	101.6			-101.6
Capital transfers & acquisition	179.6			-179.6
Change in net foreign assets of the central bank			-73.7	73.8
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	-84.8		148.3	-63.5

Table 16 Monetary survey (in millions NAf.)

	2004	2005	2006	2007
Money supply (M2)	4,509.9	4,933.4	5,425.1	6,083.4
Money (M1)	1,790.5	1,947.3	2,152.2	2,254.3
Coins & notes with the public	231.3	239.9	263.7	304.4
Total demand deposits, of which:	1,365.3	1,544.1	1,712.4	1,994.2
- Netherlands Antillean guilders	1,050.7	1,188.0	1,246.7	1,441.5
- Foreign currency	314.6	356.1	465.7	552.7
Near money	2,913.3	3,149.4	3,449.0	3,784.8
Time deposits	1,790.5	1,947.3	2,152.2	2,254.3
Savings	1,122.8	1,202.1	1,296.8	1,530.5
Factors affecting the money supply				
Net domestic assets	3,048.3	3,305.5	3,652.7	3,961.8
General government	621.3	621.9	569.7	628.3
- Central government	363.9	397.9	358.5	394.9
- Island governments	257.4	224.0	211.2	233.4
Private sector	3,059.7	3,450.3	4,058.3	4,532.9
Net foreign assets	1,461.6	1,627.9	1,772.4	2,121.6
Central bank	1,015.3	1,117.9	1,251.9	1,620.6
Commercial banks	446.3	510.0	520.5	501.0
Memorandum items				
Government loans by commercial banks	620.1	603.4	456.5	641.2
- Central government	331.4	306.2	245.4	368.3
- Island governments	288.7	297.2	211.1	272.9
Private sector loans - Leeward Islands	2,129.8	2,368.4	2,635.8	2,977.8
- Mortgages	778.5	813.4	818.4	966.4
- Consumer loans	626.6	713.6	808.9	902.3
- Business loans	724.7	841.4	1,008.5	1,109.2
Private sector loans - Windward Islands	838.7	1,002.0	1,201.4	1,307.3
- Mortgages	306.0	362.1	426.1	419.3
- Consumer loans	205.8	249.8	310.0	386.5
- Business loans	326.9	390.2	465.3	501.6

Table 17 Developments in domestic interest rates (in %)

	2004	2005	2006	2007
Central bank				
- Pledging rate	2.8	4.5	5.5	5.0
- Maximum CD rate (1 month)	2.6	4.4	5.3	4.9
Commercial bank borrowing rates				
- Passbook savings	2.8	2.8	2.8	2.5
- Time deposits (12 months)	4.1	4.1	4.2	4.4
Commercial bank lending rates				
- Mortgages	8.9	8.6	8.5	8.0
- Time loans	12.0	10.8	10.6	9.5
Government securities				
- Government bonds (5-year effective yield)	6.8	6.3	7.5	7.2
- Treasury bills (1 month)	3.7	4.5	4.9	5.1

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

	2004	2005	2006	2007
Assets				
Non-interest-bearing cash	440.0	475.7	548.6	948.0
Interest-bearing cash	1,590.6	1,836.7	2,278.5	2,585.8
Investments	744.0	1,675.8	1,225.1	1,524.0
Loans	4,049.2	5,151.5	5,736.6	6,386.5
Investments in unconsolidated subsidiaries and affiliates	12.2	11.2	182.2	150.3
Fixed assets	190.7	218.3	234.2	260.7
Other assets	162.6	188.4	205.2	257.7
Total assets	7,189.2	9,557.7	10,410.5	12,113.0
Liabilities				
Demand deposits	2,061.8	2,799.1	3,181.8	4,093.2
Savings deposits	2,467.1	3,094.3	3,294.1	3,557.1
Time deposits	1,810.8	2,555.7	2,620.0	2,895.3
Total deposits	6,339.6	8,449.0	9,095.9	10,545.6
Borrowings	30.4	25.2	31.5	71.1
Other liabilities	238.4	316.3	360.2	451.8
Total liabilities	6,608.5	8,790.6	9,487.7	11,068.4
Minority interest	6.4	7.0	7.9	8.4
Subordinated debentures	7.5	5.5	3.6	1.7
General provisions	144.4	159.2	187.5	203.3
Capital & reserves	422.5	595.3	723.8	831.2
Total capital	580.8	767.1	922.8	1,044.6
Total liabilities and capital	7,189.2	9,557.7	10,410.5	12,113.0

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

	2004	2005	2006	2007
Interest income	457.8	608.1	674.4	753.7
Interest expenses	156.8	200.9	248.4	276.4
Net interest income	301.0	407.2	426.0	477.3
Other income	174.9	215.5	257.9	254.8
Total operational income	475.9	622.8	683.9	732.1
Salaries & other employee expenses	215.9	238.8	252.4	275.6
Occupancy expenses	57.3	68.1	71.4	84.0
Other operating expenses	50.1	106.6	95.8	116.0
Net addition to general provisions	35.5	39.8	41.1	45.7
Total operational expenses	358.8	453.3	460.7	521.3
Net operating income	117.1	169.5	223.2	210.8
Net extraordinary items	7.4	25.9	9.7	0.5
Applicable profit taxes	30.8	36.6	55.5	49.7
Net income after taxes	93.6	158.7	177.4	161.6

4 DOMESTIC FINANCIAL MARKET DEVELOPMENTS

4.1 Introduction

The liquidity in the domestic financial market showed a positive correlation with conditions in the US financial market. Towards the end of 2007, US interest rates started to decline. The Fed funds target rate had remained constant during 2007 at 5.25% until the last quarter when it started its descent to 4.75% and closed the year at 4.50%. Local investors took full advantage of the opportunity to go long in the US dollar market and to lock in the interest rate difference. As a result, local liquidity contracted, especially with the smaller banks. The fixed income market was limited to government bonds and some private issues in the tourism and transportation sectors.

As it became apparent in the local market that the Netherlands would begin the debt relief as agreed in the “slotverklaring,” market participants became hesitant to offer their government securities in the secondary market, while alternative local investment opportunities remained scarce. These developments were the main reason why the year closed with limited activities in the secondary market.

In the first quarter of 2007, the Bank rolled over a treasury bill of the central government that was purchased in December 2006 in an effort to alleviate refinancing difficulties with a maturing loan. Later in the year, the central government paid off the treasury bill. During 2007, a total of NAf.55.1 million of government securities in the Bank’s portfolio matured. The portfolio contained securities issued by both the island government of Curacao and the central government. The Bank purchased a total of NAf.33.3 million in government securities to replace the maturing securities, resulting in a smaller portfolio at the end of 2007.

During 2007, the central government issued two new loans, compared to five in 2006, totaling NAf.149.4 million. The island government of Curacao issued five new loans totaling NAf.254.1 million. These issues had interest rates ranging from 7.00% for a 2-year loan to 8.00% for a 10-year loan.

In the money market, the interest rates on certificates of deposit (CDs) and time deposits (TDs) moved in the same direction 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 held according to a set schedule. Commercial banks did not trade in CDs in the secondary market but preferred to use uncollateralized interbank instruments.

As indicated in Table 20, the average monthly balance of outstanding CDs decreased throughout 2007 by NAf.3.2 million compared to 2006. In the first quarter of 2007, there were more subscriptions than CDs offered. Banks would rather invest in CDs than invest overseas in short-term instruments due to foreign exchange fees. In 2007, the CD rates offered by the Bank were between 4.60% and as high as 5.71% in August when international rates rose as a result of the credit crisis caused by the sub-prime problem in the United States.

During 2007, CD offerings were oversubscribed except on four occasions, perhaps because the rates offered were almost equal to the libid rates offered in the international money market. This marginal difference made local CDs not competitive enough to stimulate the swapping of US dollar funds for these Antillean guilder-denominated instruments. The decline in outstanding CDs in 2007 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.67.9 million (12.7%) in 2007 compared to 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 13.00% at the end of 2006 to 13.250% by the end of 2007. The average outstanding demand deposits of the commercial banks increased by NAf.5.7 million (23.1%) in 2007 compared to 2006.

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.)

	2005	**2006**	**2007**	**Change 2006-2007**
Certificates of deposit	85.8	40.3	37.1	-7.9%
Non-interest-bearing reserve requirement	455.2	534.2	602.1	12.7%
Demand deposits	59.0	24.7	30.4	23.1%
Total	600.0	599.2	669.6	11.7%

Government issues of securities in the money market consisted of treasury bills with maturities of 1, 3, 6, and 12 months. During 2007, 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, including 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 2007 because market participants perceived the possibility of an interest rate decline due to market indications that the Netherlands would start by taking over interest and principal payments on the existing government loans. In addition, due to this prospect, the governments were accepting only refinancing of maturing loans. Funds that could not be invested in local securities were then used to purchase short-term US paper that was yielding relatively high with the prospects of a yield decline towards the end of the year. Treasury bills were traded mainly in the primary market and hardly in the secondary market. Perhaps because the primary market 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 2007, the yield on a 1-month treasury bill was 5.50%, on a 3-month bill 7.12%, while the 1-year treasury bill yielded 7.22%. These yields were higher than in 2006. However, towards the end of 2007, yields started to decline: the 1-month treasury bill was trading at 5.10%, the 3-month treasury bill at 5.73%, but the 1-year treasury bill remained around 7.22%. Table 21 provides information on the size and activity in the market for local treasury bills.

The central government was unable to issue new loans during much of 2007 because the maximum coupon rate set in the budget conflicted with the reality of the market. The market was demanding higher rates, partly due to interest rate increases in the United States. As a result, much of their maturing loans were refinanced with treasury bills.

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

	2005	2006	2007	Change 2006-2007
Issuance	**543.0**	**367.5**	**709.0**	**92.9%**
Central government	248.8	74.2	447.6	503.2%
Island government of Curaçao	294.3	293.3	261.4	-10.9%
Outstanding amount	**297.0**	**259.2**	**395.0**	**52.4%**
Central government	94.4	57.3	231.1	303.3%
Island government of Curaçao	202.6	201.9	163.8	-18.9%
Average maturity (months)	**5.0**	**5.6**	**5.0**	**-10.7%**
Central government	4.8	5.3	3.8	-28.3%
Island government of Curaçao	5.1	5.7	6.6	15.8%

4.3 The market for government securities

As in previous years, the demand for government bonds remained high in the local market in 2007. Despite the increase in US interest rates during 2007, 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. Towards the end of 2007, the demand for funds by both levels of government increased, provoking higher interest rates in the local market. Both levels of the government needed extra liquidity because it became evident that the start of the debt relief from the Netherlands would take longer than initially foreseen.

Gross general government debt issuance increased to NAf.1.112.6 million, compared to NAf.749.9 million in 2006. Treasury bills accounted for NAf.709.0 million of gross general government debt issuance in 2007, NAf.447.6 million of which was issued by the central government and NAf.261.4 million by the island government of Curaçao. In 2006, the central government issued NAf.74.2 million, and NAf.293.3 million was issued by the island government of Curaçao.

Only the island government of Curacao issued more bonds (5 public issues) during 2007. A 2-year bond with a coupon of 7.0% and a 10-year bond with a coupon of 8.00% were issued in January. These were followed by a 5-year bond with a coupon of 7.375% in June, a 6-year bond with a coupon of 7.50% in April, and another 10-year bond in September with a coupon of 8.0%. The central government was not able to issue bonds until November: it then issued a 10-year bond with a coupon of 7.625% and a nominal value of NAf.129.7 million.

On a net basis, in 2007, the island government of Curacao issued NAf.74.6 million and the central government NAf.149.8 million in debt securities. The island government tried to convert its short-term loans into longer-term loans with no real success because investors associated longer maturities with higher risk and, hence, higher interest rates. Graph 2 shows that net borrowing (excluding debt conversion) was higher in 2007 than in the previous two years.

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

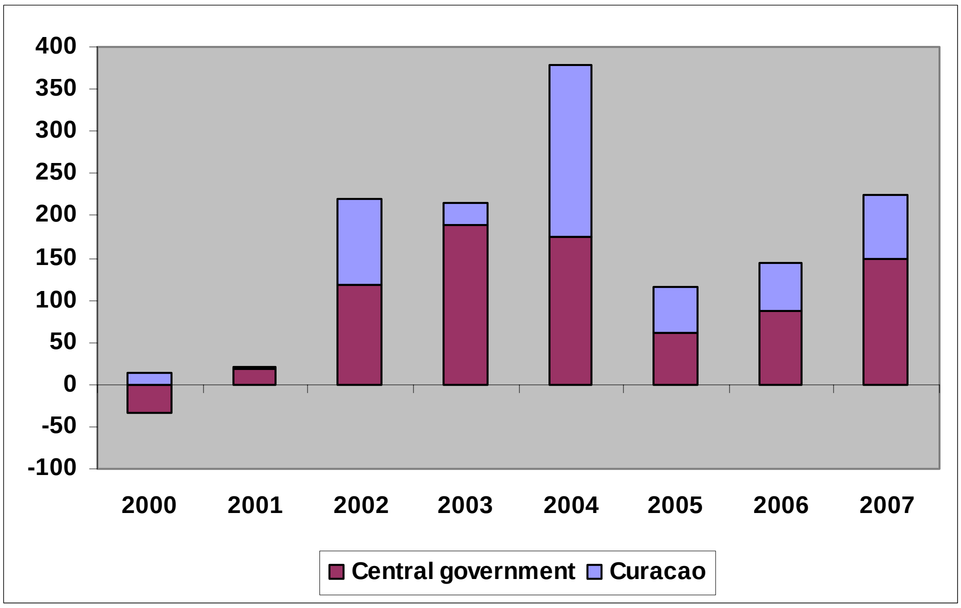


Table 22 indicates that in 2007, net borrowing by the central government was concentrated in treasury bills issues, which increased 303.0%. Private placements and public issues remained the same.

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

	2005	2006	2007	Change 2006-2007
Total, of which:	1,866.0	1,954.2	2,104.0	4.7%
Private placement	154.1	67.7	67.7	0.0%
Public issues	966.8	1,182.9	1,182.7	0.0%
Treasury bills	94.4	57.3	231.2	303.0%
Debt conversions	650.7	646.4	622.5	-0.4%
Net borrowing	61.1	88.3	149.8	70.0%

The island government of Curaçao noted an increase of 33.5% in its net borrowing in 2007 compared to 2006 (see Table 23). The public issues increased by 19.8%, mainly because the government was trying to convert its short-term loans to longer maturities. Outstanding treasury bills decreased by 18.9% in 2007.

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

	2005	2006	2007	Change 2006-2007
Total, of which:	1,342.4	1,398.3	1,472.9	5.3%
Private placement	122.3	64.7	40.0	-38.2%
Public issues	615.1	737.4	883.3	19.8%
Treasury bills	202.6	201.9	163.8	-18.9%
6.5% annuity	402.4	394.4	385.8	-2.2%
Net borrowing	54.6	55.9	74.6	33.5%

The maturity schedule in Table 24 indicates that 7% of the outstanding loans will mature within 1 year. The peak in maturities of central government loans lies in the 1-5 year bracket (54%). Maturities of the island government of Curaçao are concentrated over the brackets exceeding 5 years.

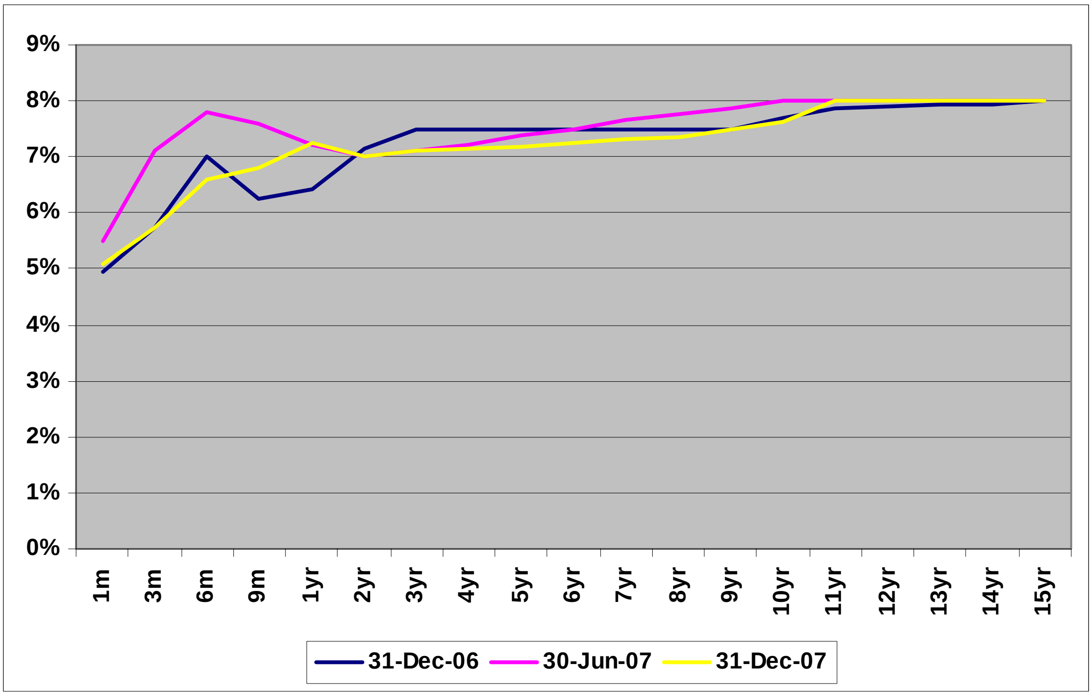
Table 24 Maturity schedule of negotiable government securities excluding treasury bills as per December 31, 2007 (% share)

	0-1 year	1-5 years	5-10 years	Over 10 years
Central government	8%	54%	25%	13%
Island government of Curaçao	6%	17%	31%	46%
Total	7%	39%	27%	27%

4.4 Domestic yield curve developments

The local yield curve shifted upward around mid-2007. This development was the result of various factors. First, interest rates in the United States increased until the fourth quarter, pushing up the rates on local securities to remain attractive. 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 first half of 2007, pushing up local interest rates even higher. Towards the end of 2007, local interest rates started to decline as a result of declining interest rates in the United States, while domestic liquidity increased.

Graph 3 Local yield curve changes during 2007



5 INSTITUTIONAL INVESTORS

5.1 Introduction

Increasing oil prices and the sub prime mortgage crisis were two important economic developments in 2007. The sub prime mortgage crisis is an ongoing economic problem manifesting itself through liquidity issues with banks and other financial institutions owing to foreclosures which accelerated in the United States in late 2006 and triggered a global financial crisis during 2007. The crisis began with the bursting of the US housing bubble and high default rates on "sub prime" and other adjustable rate mortgages made to higher-risk borrowers with lower income or poorer credit history than "prime" borrowers. Loan incentives and a long-term trend of rising housing prices encouraged borrowers to assume mortgages, believing they would be able to refinance at more favorable terms later. However, once housing prices started to drop in 2006 – 2007 in many parts of the United States, refinancing became more difficult. Defaults and foreclosure activity increased dramatically as interest rates rose. During 2007, nearly 1.3 million US housing properties were subject to foreclosure activity, an increase of 79% compared to 2006. As of December 2007, sub prime defaults were estimated at US$ 200 – 300 billion.

Central banks are primarily concerned with managing the rate of inflation and avoiding recessions. They are also "lenders of last resort" to ensure liquidity. In connection with the sub prime market crisis, the Bank conducted a survey of the insurers, re-insurers, and pension funds under its supervision. Preliminary results indicate that the sub prime market crisis did not greatly affect these institutions.

Globally the two greatest concerns identified by insurance companies are price competition and climate change. Price has always been the most important differentiator in the general insurance mass market, but the phenomenal success of web aggregators has enabled consumers to compare prices easily. As a result, product and service differentiation are two other ways for insurers to protect their margins and differentiate themselves from their competitors. At the same time, with margins under severe pressure, pricing more precisely for risk represents the principal strategy for insurance companies to protect their market share without eroding their profitability to an unacceptably low level. This trend is also visible in the Netherlands Antilles insurance market.

Mitigating climate change to acceptable levels will require large-scale political breakthroughs. Depending on how quickly the world starts to restrict emissions of carbon dioxide and other greenhouse gasses, a slower or faster introduction of alternative energy sources or carbon capture techniques will be needed. In many cases, the solutions envisaged require new technologies which may still be in an experimental phase. Commercial activities need financing and insurance cover, but decision making is hindered by a lack of understanding of the risks involved in these activities. Therefore, it might be easier to get financing and insurance cover for traditional energy production. The challenge and also the opportunity for (re)insurance companies seem to be the awareness that the insurance industry is entering a new era. Therefore, (re)insurance companies need to start expanding their knowledge base so they can offer financing and insurance cover on terms at least equal to new technologies.

Europe's regulators want to bring the Solvency II framework into effect in 2012 to improve the safety and soundness of the European Union's 5,000 insurers and reinsurers. The regime is modeled on the three-pillar structure of capital requirements (pillar 1), supervisory review (pillar 2), and market discipline (pillar 3) embodied in the Basel II bank capital adequacy rules, but adjusted for the more complex world of insurance. In terms of the minimum capital requirements for insurers to absorb losses from systemic shocks, the aim is to get firms to align their capital more accurately to the risks they face and, thereby, to reflect the diversification of risk around a group and its activities.

The International Accounting Standards Body (IASB) in London developed the international accounting rules known as the International Financial Reporting Standards or IFRS. Preliminary views on valuing the insurance policies that form the bulk of an insurer's liabilities indicate that under IFRS the insurance companies' financial results in some jurisdictions could be more volatile and susceptible to changes in estimates by global accounting rules. However, in other jurisdictions, they may become less volatile because fair value movements in assets should be recognized in the same period as fair value movements in related liabilities. The difficulties of agreeing on a standard for insurance contracts prompted the IASB to tackle the problem in two stages. Under phase 1, insurers in jurisdictions using IFRS since 2004 have valued their financial assets at fair value, or current market prices. In the interim they continue to account for their liabilities on a plethora of bases, generally historic cost, until phase 2 is completed with an agreed-upon single international standard for insurance contracts. The Bank is following these developments closely. If necessary, changes will be made to the Bank's ARAS Valuation Guidelines which are currently being drafted.

In 2007, the Bank developed the reporting format to be used by the insurance intermediaries registered with the Bank. This format was discussed with the representative organizations and will be introduced to the sector during 2008. This format will provide the Bank with, among other things, information on the fiduciary responsibilities of insurance intermediaries.

5.2 The institutional investors' sector

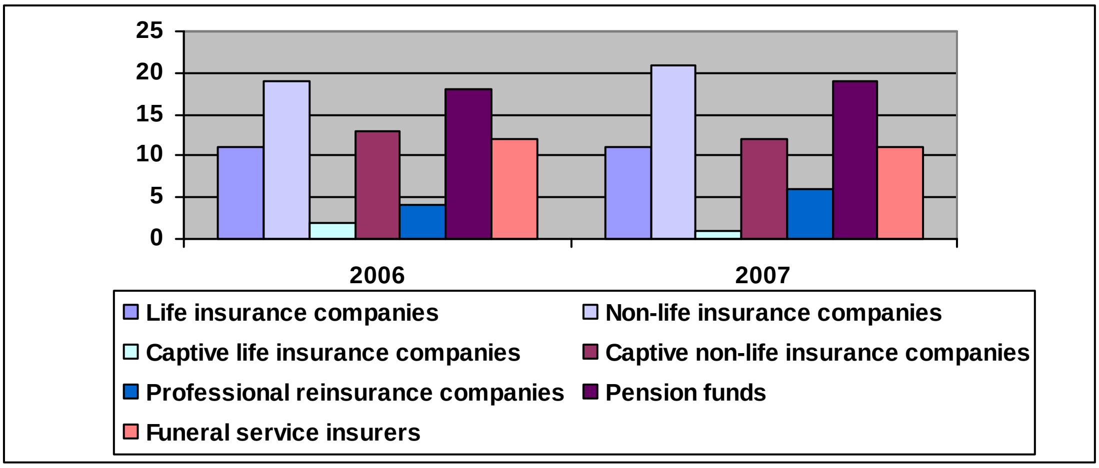
The number of institutional investors operating in the Netherlands Antilles in 2007 was 65 (2006: 63): 11 life insurance companies (2006: 11), 21 non-life insurance companies (2006: 19), 11 funeral service insurers (2006: 12), and 22 pension funds (2006: 21). In 2007, two non-life insurance companies were licensed. Of the 22 pension funds registered at the Bank in 2007, 3 were in the process of liquidation.

The number of insurance companies servicing the international market was 19 at the end of both 2006 and 2007: 1 was involved in the life insurance business, 12 in the non-life business, and 6 were professional reinsurers.

Of the 104 insurance intermediaries that applied for registration with the Bank, 67 have been registered. Of the remaining 37, 18 are still being processed, and 19 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.181.3 million (10.1%) in 2006 compared to 2005. Of the total assets in 2006, 80.5% was related to investments and 9.6% to current assets. The increase in total liabilities in 2006 was mainly the result of an increase of NAf.124.6 million (8.7%) in technical provisions.

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

	2004		2005		2006	
	Local	Int'l	Local	Int'l	Local	Int'l
ASSETS						
Intangibles	0.1	-	-	-	-	-
Total investments	1,340.7	115.3	1,462.3	121.3	1,587.5	148.1
Current assets	155.0	50.5	186.9	49.4	189.3	64.1
Other assets	23.3	-	26.9	-	36.5	-
From separate accounts statement	57.5	-	113.6	-	157.7	-
Total admissible assets	1,576.6	165.8	1,789.7	170.7	1,971.0	212.2
EQUITY, PROVISIONS, AND LIABILITIES						
Capital	62.8	7.7	62.8	8.1	77.9	8.1
Surplus	82.2	47.1	105.5	54.0	117.1	78.6
Subordinated instruments	0.1	-	0.5	-	0.6	-
Technical provisions	1,318.2	81.5	1,425.8	90.9	1,550.4	104.3
Current liabilities	46.3	25.1	57.1	16.1	46.9	21.5
Other liabilities	6.8	4.4	5.4	1.6	6.1	-0.3
Contingent liabilities	2.7	-	19.0	-	14.4	-
From separate accounts statement	57.5	-	113.6	-	157.6	-
Total equity, provisions, and liabilities	1,576.6	165.8	1,789.7	170.7	1,971.0	212.2

The equity position of the local life insurance companies, consisting of capital, surplus, and subordinated instruments, increased by NAf.26.8 million (15.9%) in 2006. This increase was due to the profit of NAf.9.8 million in 2006 (see Table 26) and other surplus contributions.

In 2006, the solvency requirement of the local life insurance sector amounted to NAf.57.1 million, while the equity available to cover the solvency requirement amounted to NAf.195.6 million. Based on these figures, the sector had a solvency surplus of NAf.138.5 million.

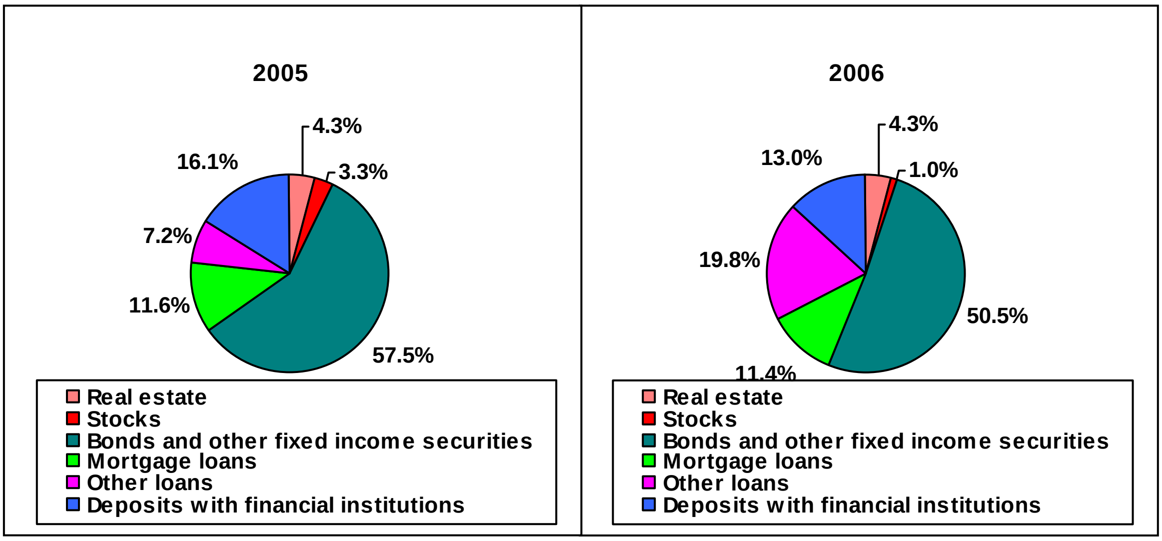
The total assets of the international life insurance companies (captive insurance companies and professional reinsurers) increased by NAf.41.5 million (24.3%), reaching NAf.212.2 million at the end of 2006. The equity position increased by NAf.24.6 million (39.6%) to NAf.86.7 million, due mainly to the profit of NAf.25.4 million made in 2006 (see Table 26).

The solvency requirement of the international life insurance sector amounted to NAf.3.8 million in 2006. The equity available to cover the solvency requirement was NAf.86.7 million, resulting in a solvency surplus of NAf.82.9 million.

5.3.2 Investments

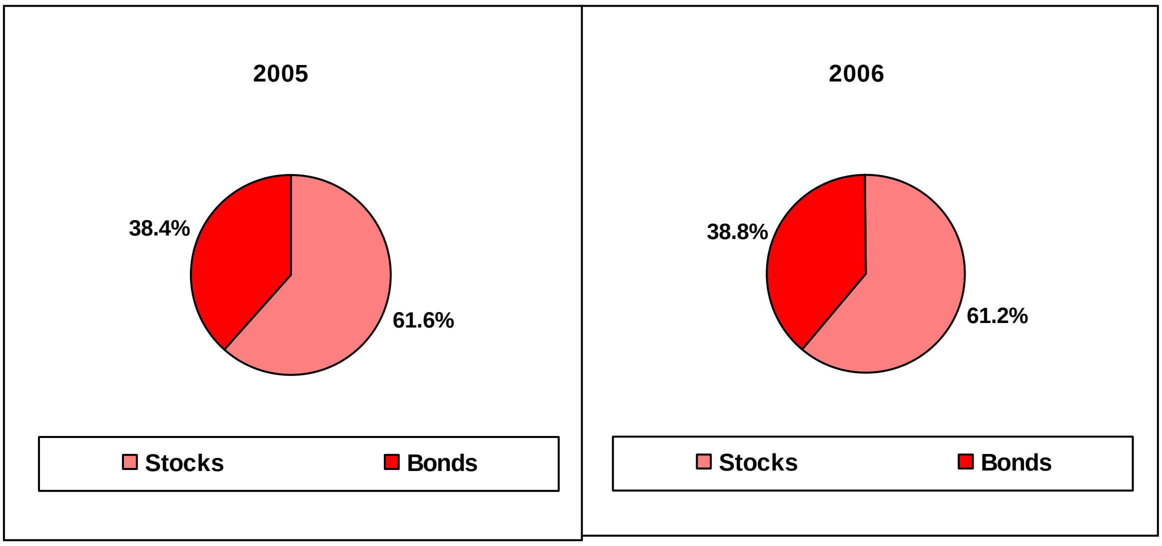
Total investments of the local life insurance sector increased by NAf.125.2 million (8.6%) in 2006, due mainly to an increase of investments in mortgages and other loans. The composition of the consolidated 2005 and 2006 investment portfolio of the local life insurance companies is presented in graph 5. This graph indicates that the proportion of investments in other loans increased by 12.6 percentage points, mainly at the expense of investments in bonds, which decreased from 2005 to 2006 by 7.0 percentage points.

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



The composition of the consolidated 2005 and 2006 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 from 2005 to 2006 by NAf.26.8 million (22.1%) while the composition remained about the same.

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. The net premium income of the local life insurance sector increased by NAf.2.5 million (1.3%). The net operational result before corporate taxes and before net results from separate accounts increased slightly by NAf.0.3 million (4.0%) in 2006 compared to 2005. The sector recorded a net profit of NAf.9.8 million in 2006, an increase of NAf.1.4 million (16.7%) over 2005.

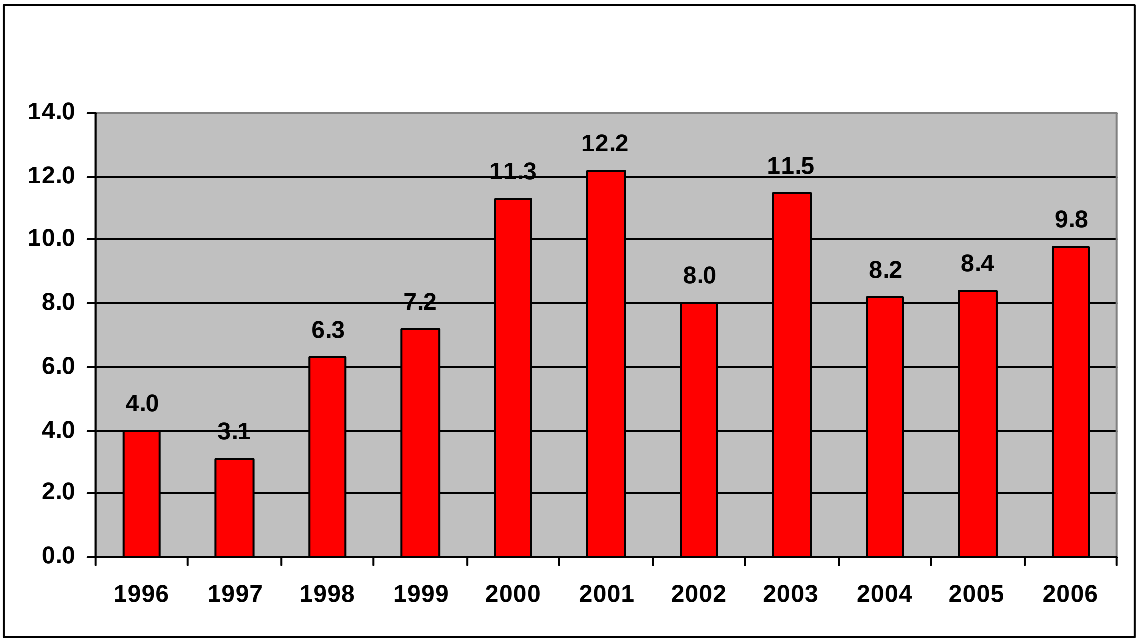
The premium income of the international life insurance industry increased by NAf.10.2 million to NAf.52.2 million in 2006 when compared to 2005. Net benefits incurred increased from NAf.21.8 million to NAf.26.4 million. Due to the substantial increase in the net unrealized gains or losses of NAf.9.7 million in 2006, the international life insurance industry ended up with a net profit of NAf.25.4 million in 2006.

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

	2004		2005		2006	
	Local	Int'l	Local	Int'l	Local	Int'l
INCOME						
Total net premium income	189.7	35.5	194.2	42.0	196.7	52.2
Net investment income and realized capital gains and losses	97.1	5.0	95.5	5.3	108.0	8.9
Net other operational income	5.8	1.8	2.1	2.1	2.3	2.2
Total operational income	292.6	42.3	291.8	49.4	307.0	63.3
EXPENSES						
Net benefits incurred	84.0	49.0	97.9	21.8	105.0	26.4
Changes in net technical provisions	123.9	-11.9	109.3	6.8	112.7	7.9
Net operational exp. incurred	61.3	2.6	59.7	3.5	63.5	5.2
Net other operational exp. incurred	6.9	1.7	2.5	0.7	0.9	1.4
Other changes affecting net results	-0.4	-0.2	-	-	1.0	-
Profit sharing to policyholders	14.0	-	13.3	4.6	14.5	9.9
Total operational expenditures	289.7	41.2	282.7	37.4	297.6	50.8
Extraordinary results	-1.3	-0.4	-1.6	0.6	-1.6	-0.3
Net operational result before corp. taxes and before net results from separate accounts	1.6	0.7	7.5	12.6	7.8	12.2
Corporate taxes	4.7	0.1	-5.4	0.2	-0.9	-
Net operational result after corp. taxes and before net results from separate accounts	-3.1	0.6	12.9	12.4	8.7	12.2
Net result from separate accounts	10.3	-	1.6	-	2.7	-
Net operational result	7.2	0.6	14.5	12.4	11.4	12.2
Net unrealized gains or losses	1.0	8.6	-6.1	3.5	-1.6	13.2
Net profit or loss	8.2	9.2	8.4	15.9	9.8	25.4

Graph 7 presents an overview of the consolidated net profits and losses of the local life insurance companies during the period 1996 - 2006. Average profitability amounted to NAf.8.2 million during this period, indicating that 2006 was an above average year.

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 2006 aggregated balance sheet total of the non-life insurance companies operating in the domestic market reached NAf.497.0 million, an increase of NAf.49.4 million (11.0%) compared to 2005. Investments increased by NAf.57.7 million (20.4%).

Due to the short-term nature of the risks insured by the non-life insurance business compared to the life insurance business, a smaller percentage of total assets was invested, 68.5% in 2006 compared to 80.5% in the life insurance business. On the other hand, current assets comprised 29.6% of total assets in 2006 compared to 9.6% in the life insurance business.

The technical provisions of the local non-life insurance sector increased by NAf.25.9 million, reaching NAf.202.1 million in 2006. The equity position increased by NAf.39.8 million (31.6%), due mainly to the retained profit reported by the sector in 2006.

The solvency requirement of the local non-life insurance sector in 2006 was NAf.46.2 million, and the equity available to cover the solvency requirement was NAf.165.8 million. Based on these figures, the sector had a solvency surplus of NAf.119.6 million in 2006.

The non-life insurance companies servicing the international market (captive insurance companies and professional reinsurers) reported total assets of NAf.3.6 billion in 2006, NAf.0.4 billion (12.5%) more than in 2005. This increase was attributed to a NAf.292.5 million (9.7%) increase in investments and an increase of NAf.129.6 million (87.6%) in current assets. On the liabilities side, the technical provisions increased by NAf.89.3

million (4.9%) compared to 2005. Equity increased by NAf.333.5 million, due mainly to the profit of NAf.314.7 million in 2006 (see Table 28).

The solvency requirement of the international non-life insurance sector amounted to NAf.90.6 million, while the equity available to cover the solvency requirement was NAf.1.6 billion in 2006. From these figures, it can be concluded that the sector had a solvency surplus of NAf.1.5 billion in 2006.

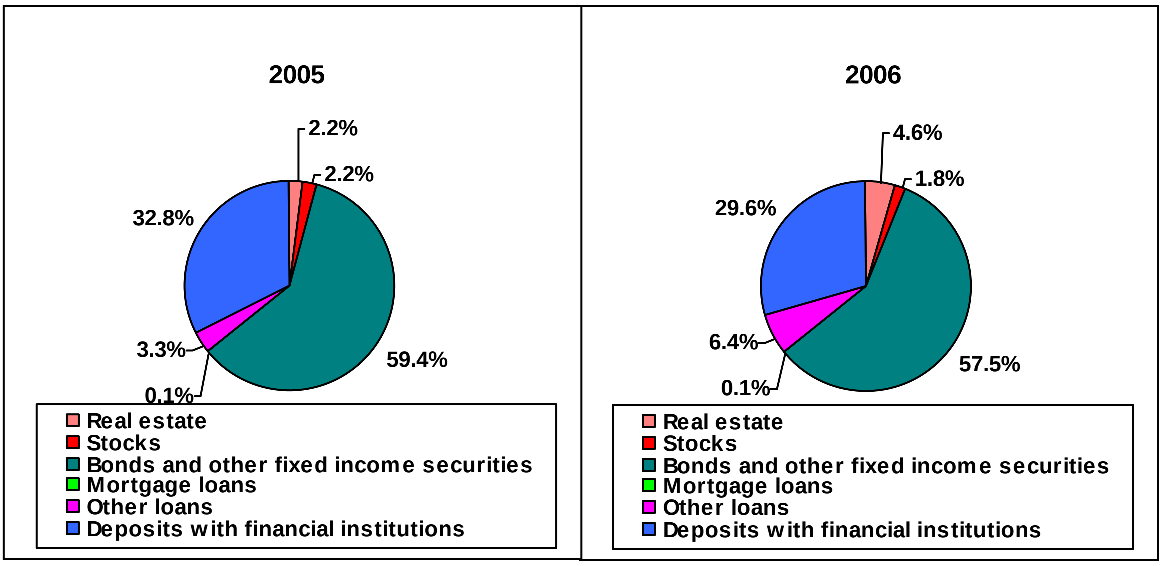
Table 27 Consolidated balance sheet of the non-life insurance industry (in millions NAf.)

	2004		2005		2006	
	Local	**Int'l**	**Local**	**Int'l**	**Local**	**Int'l**
ASSETS						
Intangibles	1.0	-	3.5	-	2.8	-
Total investments	248.0	2,846.2	282.9	3,056.6	340.6	3,349.1
Current assets	181.1	198.1	150.1	148.0	147.0	277.6
Other assets	11.1	0.1	11.1	0.1	6.6	0.1
Total admissible assets	441.2	3.044.4	447.6	3,204.7	497.0	3,626.8
EQUITY, PROVISIONS, AND LIABILITIES						
Capital	75.1	312.0	75.1	313.2	92.5	416.9
Surplus	29.8	888.2	50.9	975.4	73.3	1,205.2
Subordinated instruments	1.0	-	17.7	-	1.7	-
Technical provisions	186.2	1,781.0	176.2	1,825.7	202.1	1,915.0
Other provisions & liabilities	16.9	1.8	12.4	40.8	4.2	36.6
Current liabilities	132.1	61.4	115.1	49.6	123.1	53.1
Contingent liabilities	0.1	-	0.2	-	0.1	-
Total equity, provisions, and liabilities	441.2	3.044.4	447.6	3,204.7	497.0	3,626.8

5.4.2 Investments

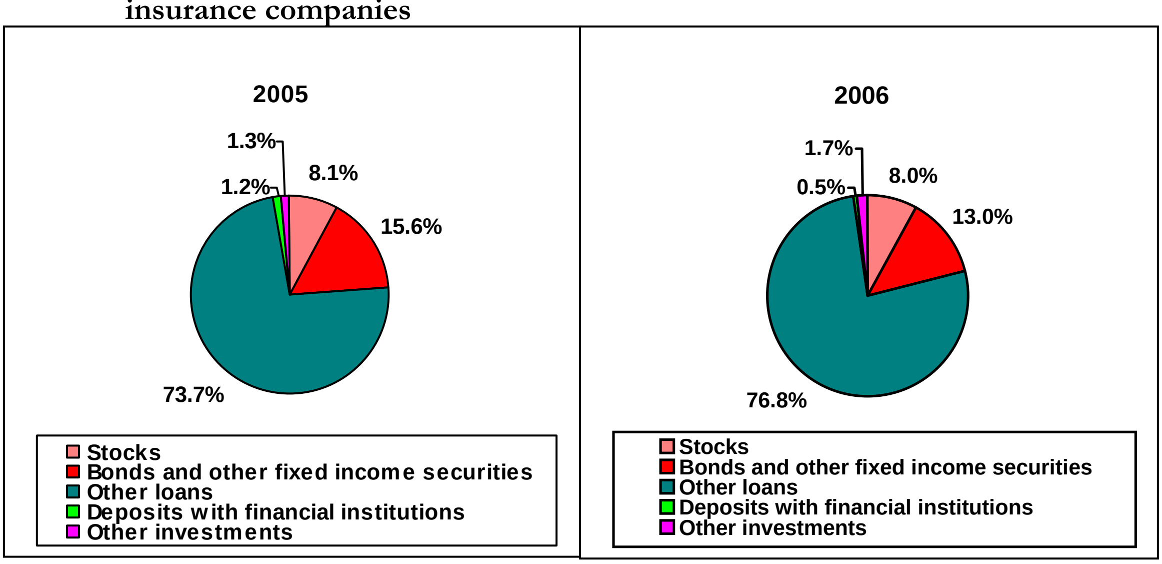
The composition of the investment portfolio of the local non-life insurance companies is presented in graph 8. As was the case in previous years, only some minor portfolio changes took place in 2006. The investments in bonds and deposits with financial institutions decreased by 1.9 and 3.2 percentage points, respectively, while investments in other loans and real estate increased by 3.1 and 2.4 percentage points, respectively, in 2006.

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 in 2006. The graph indicates that, similar to previous years, the largest share of total investments consisted of other loans. Most of these other loans were 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.20.0 million (9.1%) in 2006, compared to an increase of NAf.7.5 million (3.5%) in 2005. The net claims incurred during 2006 increased by NAf.7.7 million (7.0%), compared to an increase of NAf.2.4 million (2.2%) in 2005. The underwriting expenses and changes in various provisions increased by NAf.24.2 million (28.5%) in 2006. The local non-life insurance sector experienced an underwriting result of NAf.7.9 million in 2006, less than half of the underwriting result reported in 2005. Net investment income increased by NAf.3.6 million to NAf.19.4 million in 2006. The industry realized a net profit of NAf.16.6 million in 2006, a decrease of NAf.7.6 million compared to 2005.

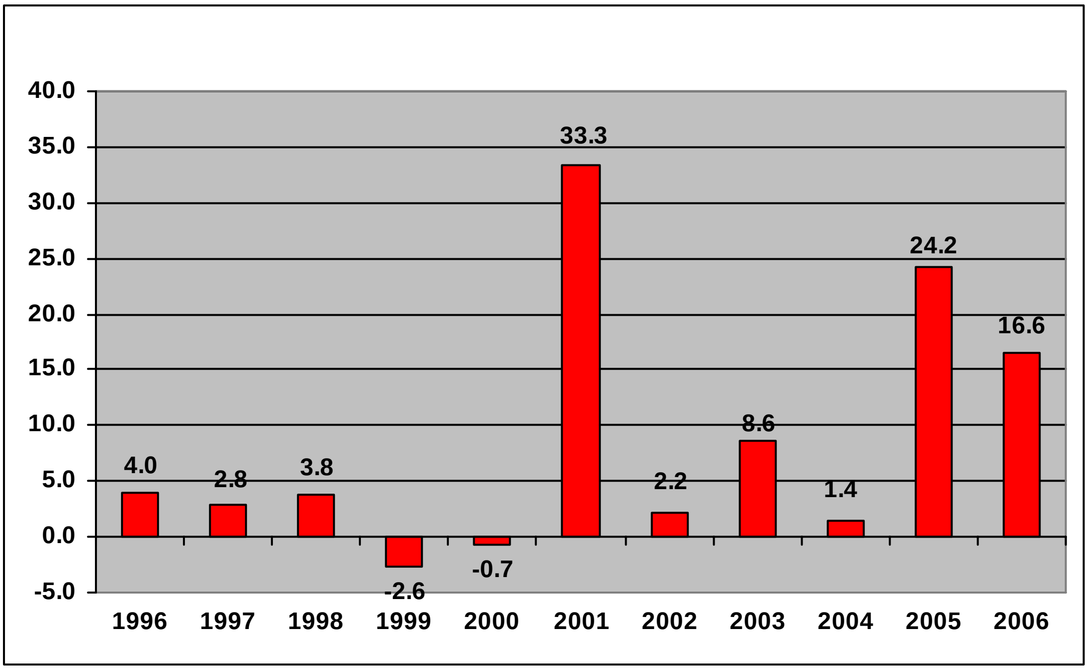
Table 28 Consolidated profit and loss statement of the non-life insurance industry (in millions NAf.)

	2004		2005		2006	
	Local	Int'l	Local	Int'l	Local	Int'l
INCOME						
Total net earned premium	211.8	807.4	219.3	699.1	239.3	641.1
Net other underwriting income	0.7	2.9	0.7	0.6	1.3	27.0
Total operational income	212.5	810.3	220.0	699.7	240.6	668.1
EXPENSES						
Net claims incurred	107.2	420.5	109.6	358.1	117.3	417.4
Claim adjustment expenses	4.8	0.9	4.7	1.2	5.8	0.4
Changes in various provisions	2.2	147.8	-6.9	105.4	1.4	73.7
Underwriting expenses incurred	99.5	48.3	91.8	61.9	107.7	27.5
Net other operational expend.	3.6	2.6	2.0	3.4	0.5	54.4
Total operational expenditures	217.3	620.1	201.2	530.0	232.7	573.4
Underwriting result	-4.8	190.2	18.8	169.7	7.9	94.7
Net investment income	17.5	123.8	15.8	137.3	19.4	178.5
Other results	-5.9	27.1	-1.9	-11.7	-1.8	8.1
Extraordinary results	-2.9	-2.7	-	5.4	3.1	2.6
Net result before corp. taxes	3.9	338.4	32.7	300.7	28.6	283.9
Corporate taxes incurred	0.3	26.4	8.5	20.5	11.7	8.4
Net unrealized gains or losses	-	20.1	-	17.4	-0.3	39.2
Net profit or loss	3.6	332.1	24.2	297.6	16.6	314.7

The international non-life insurance companies reported net earned premium income of NAf.641.1 million in 2006, a decrease of NAf.58.0 million compared to 2005. On the other hand, net other underwriting income increased by NAf.26.4 million. Total operational expenditures increased by NAf.43.4 million in 2006. Due to the decrease in the net earned premium income and the increase of the operational expenditures, the sector's underwriting result deteriorated by NAf.75.0 million to NAf.94.7 million in 2006. In contrast, the industry experienced a further increase in net investment income by NAf.41.2 million in 2006. Net unrealized gains or losses increased by NAf.21.8 million in 2006. Due to the increase in net investment income and unrealized gains, the industry realized an increase of NAf.17.1 million in net profit for 2006.

Graph 10 presents an overview of the consolidated net results after taxes of the local non-life insurance companies from 1996 to 2006. This graph depicts low net results during most of the years, except for 2001, 2005, and 2006. The large net result in 2001 was due mainly 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

As of January 1, 2007, the Pension Act ("Pensioenwet") went into effect in the Netherlands replacing the Pension and Savings Funds Act ("Pensioen- en spaarfondsenwet"). The Pension Act should bring more transparency and accountability and also includes restrictions on the transfer of pension rights. Current adjustments to our National Ordinance on Corporate Pension Funds (P.B. 1985, nr. 44) are based partially on the Dutch Pension Act. The latest development in the pension industry in the Netherlands is the introduction of the general pension institution ("Algemene Pensioeninstelling"), a new type of pension service provider not related to a specific type of employer or industrial sector and allowed to offer a variety of pension plans.

5.5.2 Balance sheet

The equity position of the pension funds continued to improve in 2006, increasing by 20.3% compared to 2005 (see Table 29). The ratio of investment-to-provision for pension obligations also improved, from 102.1% in 2005 to 102.5% in 2006. A further increase in 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 level of this ratio also depends on the specific circumstances of each fund, according to which 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 6.5% in 2006 compared to 2005. The current assets and current liabilities represented 9.3% and 2.2%, respectively, of total assets.

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

	2004*	2005*	2006
Assets			
Total investments	4,923.6	5,139.5	5,426.4
Current assets	470.9	499.1	561.5
Other assets	17.8	12.4	30.8
Total	**5,412.3**	**5,651.0**	**6,018.7**
Equity, provisions, and liabilities			
Equity	364.5	486.8	585.5
Provisions for pension obligations	4,915.0	5,032.3	5,292.4
Current liabilities	132.8	131.9	140.8
Total	**5,412.3**	**5,651.0**	**6,018.7**

*) Some 2004 and 2005 figures have been regrouped for comparison purposes.

5.5.3 Profit and loss statement

The net investment income and capital gains & losses increased by 32% from 2005 to 2006 (see Table 30). Moreover, the net investment income and capital gains & losses were twice the minimum required amount of 4% of the provisions for pension obligations. Therefore, the pension funds maintained an adequate net investment performance.

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

	2004*	2005*	2006
Income			
Contributions	158.7	163.6	186.0
Net investment income and capital gains & losses	355.6	323.5	428.1
Other income	46.3	153.6	44.1
Total income	**560.6**	**640.7**	**658.2**
Expenses			
Pension benefits incurred	185.4	188.4	196.0
Change in net technical provisions	249.5	168.9	288.9
Operational expenses incurred	23.3	25.3	24.0
Other expenses incurred	7.2	7.0	12.7
Total expenses	**465.4**	**389.6**	**521.6**
Extraordinary results	-	-8.8	-6.7
Net profit or loss	**95.2**	**242.3**	**129.9**

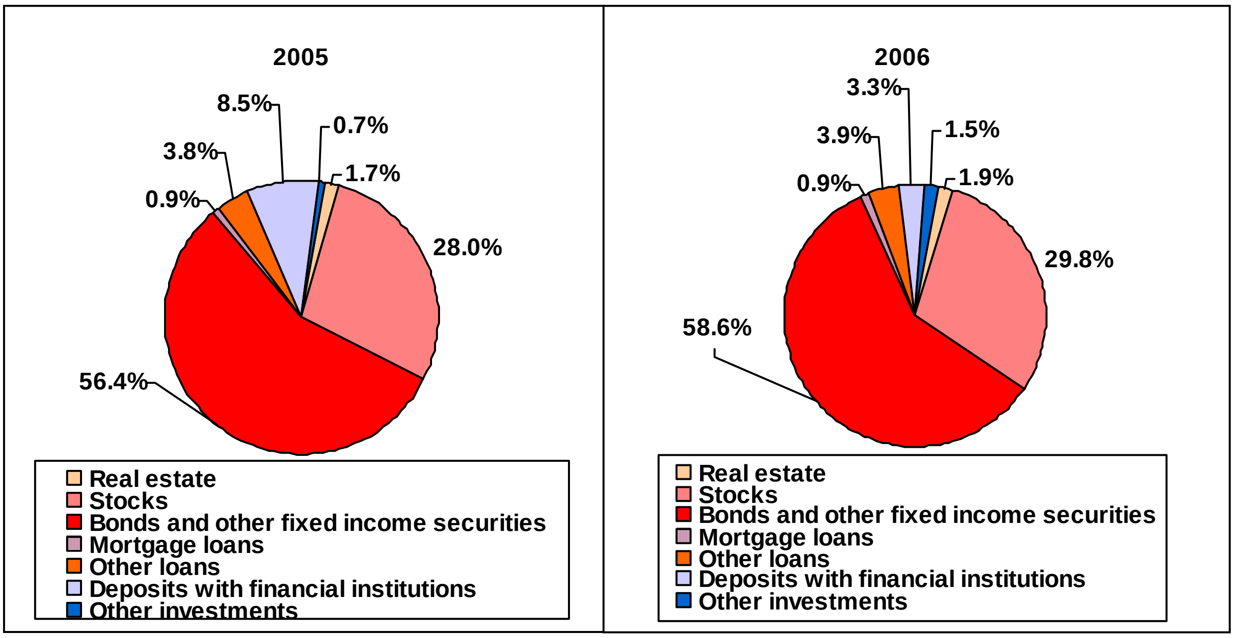
*) Some 2004 and 2005 figures have been regrouped for comparison purposes.

The 2006 operational result represented 2.5% of the provision for pension obligations and 2.2% of total assets, under the 4% rate generally used by most of the local pension funds to discount (future) obligations. This shortfall is caused mainly by an increase of 71% in the technical provisions in 2006. The operational expenses incurred by the sector represented 0.2% of the provisions for pension obligations and 12.9% of the pension contributions.

5.5.4 Investments

The composition of the investment portfolio of the pension funds is presented in graph 11. The largest change occurred in the deposits with financial institutions, which declined by 5.2 percentage points in 2006 compared to 2005.

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 2007 related to its supervision of the financial sector.

6.1 Supervision of investment institutions and administrators

Investment institutions and administrators have been subject to the Bank's supervision since the beginning of 2003. The number of supervised investment institutions and administrators remained unchanged during 2007 at 14 and 11, respectively. During 2007, the Bank conducted follow-up risk- based examinations at four investment institutions and administrators. During these examinations, the Bank focused particularly on assessing the institutions' compliance with the anti-money laundering and combating of terrorist financing guidelines that were issued in 2005. Significant improvement in this area was observed at the institutions visited.

The Bank continued to play an active and vital role in the regional developments regarding the regulation of investment institutions and administrators with the re-election of one of its staff members to chair the Offshore Group of Collective Investment Scheme Supervisors (an organization of regulators of various regional offshore jurisdictions).

6.2 Supervision of trust service providers

The Bank has been entrusted with the supervision of the trust sector since the beginning of 2004. In 2007, the number of licensed trust services providers increased by 3 to 86, while the number of trust service providers with dispensation increased by 7 to 51, for a total of 137 trust service providers per ultimo. Special attention was devoted in 2007 to the timely submission of the certified *Trust Service Providers' Supervisory Questionnaires* and the certified financial statements by the trust service providers. In addition, the Bank conducted 15 on-site risk based examinations at trust service providers, including St. Maarten. Special attention was given to the institutions' compliance with the anti-money laundering and combating of terrorist financing guidelines that were issued by the Bank for the trust sector in 2006.

6.3 Supervision of bank and credit institutions

In 2007, the Bank conducted on-site examinations at 18 supervised credit institutions, of which 2 were joint-examinations: one joint-examination with the Investment Institutions and Trust Supervision department and one with the Institutional Investors Supervision department.

The Banking Supervision department was intensely involved with the revision of the Chart of Accounts, a reporting tool for domestically and internationally operating credit institutions in the Netherlands Antilles. In addition, the department was involved with the revision of Supervisory Regulations I, II, and III. Furthermore, as part of its continuous efforts to deter and to combat money laundering and the financing of terrorism activities, revised provisions and guidelines for the banking sector were issued.

The working group involved with the implementation of a deposit insurance system for the Netherlands Antilles was re-activated in 2007.

The Bank received three license applications in 2007: one for the conduct of domestic banking activities, one for the conduct of international banking activities, and one for the conduct of money transfer activities. Furthermore, the Bank received five requests for a dispensation of the prohibition to undertake credit extension activities to the public: four requests for undertaking consumer credit extension activities and one for the conduct of "bonkrediet."

In 2007, the Bank finished the research of its legal framework to supervise money transfer companies. The research revealed that the current legal framework is not comprehensive enough to effectively and efficiently supervise money transfer companies and prevent their use for money laundering and terrorist financing purposes against the background of preserving the integrity of our financial sector. Consequently, the Bank decided to continue its policy of not issuing new licenses for the conduct of money transfer business pending the implementation of the necessary legal framework to adequately supervise money transfer companies.

6.4 Supervision of institutional investors and insurance intermediaries

Work on the revision of the National Ordinance on Company Pension Funds continued during 2007. Once finalized, this legislation will provide the Bank with more tools for better supervision of the pension fund industry.

Furthermore, reporting forms for insurance intermediaries were developed and discussed with the industry in 2007. Intermediaries will be required to submit quarterly reports on their outstanding balances with insurance companies and submit annual financial figures to the Bank.

6.5 Integrity aspects of financial sector supervision

After finalizing the update of the main rules and regulations on financial sector integrity in 2006, the Bank focused its efforts in 2007 on a further automation of its Integrity Database (" IFS Register"), promoting better compliance with the various integrity aspects of financial sector supervision.

The Bank subscribed officially to the World-Check Database for an automated regular screening of all its officially registered (co-)policymakers from institutions under the Bank's supervision, (candidate) holders of qualifying interests in these institutions, and other persons involved. Full compliance was achieved with the required FATF 'Customer Due Diligence' procedures for screening all subjects in the IFS Register against eventual money laundering, terrorist financing, and high risk political exposure.

The IFS Register now contains approximately 2,500 subjects. During 2007, 283 integrity tests were conducted with a positive result: 174 for the banking and credit institutions sector, 88 for the trust and investment sector, and 21 for the institutional investors sector. Of the 283 integrity tests, 188 persons had been registered and tested for the first time: 113 for the banking and credit institutions sector, 62 for the trust and investment sector, and 13 for the institutional investors sector.

Cases of doubt with respect to integrity were officially discussed and dealt with by the Integrity Commission of the Bank. Of these cases, 9 were reported internally and resulted in a negative test result or serious doubts. In accordance with the Policy Rule on Integrity Testing and in the opinion of the Bank, these persons formed an impediment to discharging the position of (co)policymaker, holding a qualifying interest, or obtaining a dispensation in pursuance of the Supervision Act.

As part of the integrity testing, the Bank systematically screens on antecedents through information requests, both on a national and international level, including to other regulatory authorities. At the same time, the Bank receives information requests as part of the integrity testing by its colleague supervisory authorities worldwide. In 2007, the Bank responded to 26 such information requests.

During 2007, the Bank registered 43 reported incidents eroding integrity: 9 were reported internally and 34 externally. The latter is pursuant to the Policy Rule for Sound Business Operations in the Event of Incidents and Integrity-sensitive Positions.

The Bank also regularly issues warning notices on its website, containing the names of entities operating in or from the Netherlands Antilles that are suspected of violating provisions of the Supervisions Act or other financial regulations, thereby affecting the integrity of the financial sector. During 2007, the Bank issued 3 warning notices.

6.6 IT aspects of financial sector supervision

In the first quarter of 2007, the Bank concluded its quick scan at the commercials banks with regard to their compliance with the Rules and Regulations governing the Netherlands Antilles Clearing System (NACS). This scan was also conducted at the Bank itself as an operator as well as a user of the NACS. The conclusion of this examination was that compliance with the rules and regulations was very weak and that almost all the institutions need to revise their procedures with respect to the system.

In 2007, regular IT-examinations were conducted at 4 commercial banks, 1 credit institution, and 2 insurance companies. Furthermore, a "penetration" test was executed on the Bank's network. The objective of this test was to determine whether the Bank had all the necessary security measures in place to secure its network against hackers. The result of the test was positive; the security measures implemented at the Bank were very tight.

In December 2007, the Bank issued its Provisions and Guidelines for Safe and Sound Electronic Banking. However, credit institutions were granted an extension for their implementation until July 31, 2008.

6.7 International financial sector policy developments

The Netherlands Antilles, as a member of FATF, endorsed the 40 revised recommendations of 2003. During 2007, both the National Committee on Money Laundering and Terrorist Financing (CIWG) and the Bank worked continuously to implement the new requirements, including the Interpretative Notes and Best Practice Guidance to the Recommendations. The Bank carries the presidency and the secretariat of the CIWG.

In early 2007, the CIWG submitted updated draft legislation on the reporting of unusual transactions (MOT) and identification in conducting financial services (LIF) to the government. This legislation 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. Their enactment will bring the AML/CFT framework of the Netherlands Antilles up to the international standards.

Furthermore, the Bank updated the Provisions and Guidelines on the Detection and Deterrence of Money Laundering and Terrorist Financing for all financial service providers in the Netherlands Antilles. The updates were published on the Bank's website.

Finally, staff members of the Bank were actively involved in FATF and CFATF activities in 2007.

6.8 Conferences and seminars

On October 22, 2007, the Bank organized a seminar on "multifactor authentication", related to the introduction of its Provisions and Guidelines for Safe and Sound Electronic Banking later that year. During the seminar, participants were informed about the risks associated with the use of "single factor authentication". In addition, the Bank gave a presentation on the provisions and guidelines and allowing the institutions to give their final comments on the document. Also some vendors from the United States, the Netherlands, and Venezuela were present to expose their products related to multifactor authentication to the seminar attendees.

Furthermore, the Bank began offering seminars in which the research done by its staff is presented to students and other interested parties in a non-technical manner. In 2007, 3 research papers were presented, the topics of which were "The Effect of Oil Price Shocks on the Price of Gasoline in Curacao," "Purchasing Power Parity Theory in a Fixed Exchange Rate System," and "The Shadow Economy in the Netherlands Antilles." These papers can be downloaded from the Bank's website (www.centralbank.an).

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 have 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 to:

1. 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. gather the necessary information and data essential for compiling the balance of payments;

3. 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. 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,[13] 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. The levy is determined per quarter and based on the average 3-month US-dollar Libid rate plus a surcharge. During 2007, the levy declined from 6.730% in the first quarter to 5.898% in the fourth quarter due to a decline in the US-dollar Libid rate and a reduction of the surcharge related to the improvement in reserve adequacy.

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

7.2 Foreign exchange licenses

Compared to 2006, the number of foreign exchange licenses issued by the Bank in 2007 increased by 136 (10%) to 1,564 (see Table 31). This increase can be attributed primarily to the higher number of foreign exchange exemptions granted to international financial and business companies (97), perhaps indicating that activities in this sector are recovering. In contrast, the total capital amount related to the licenses granted decreased by NAf.220.2 million (30%) to NAf.525.4 million. This decrease can be explained primarily by fewer licenses granted for borrowing abroad related to hotel projects compared to 2006, when the financing was concluded for large projects in St. Maarten (Baby Beach and Cupecoy) and Curaçao (Santa Barbara and Riffort). The licenses granted for major borrowing abroad in 2007 were mainly for investment projects in St. Maarten, including expansion of the harbor and yachting facilities, and capacity expansion of the utility company, GEBE. Also noteworthy is the decline in the number and value of licenses for portfolio investments abroad, which may be related to the drop in foreign interest rates and the turbulent securities markets, especially in the United States.

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

	2006		2007	
Description	**Number**	**Amount**	**Number**	**Amount**
Establishment company by nonresident	177	9.0	199	2.7
Transfer to own account abroad	23	9.8	15	5.6
Portfolio investment abroad	27	55.0	20	39.2
Borrowing abroad	40	663.4	47	464.0
Lending abroad	9	3.4	25	6.7
Request for foreign bank account	10	-	13	-
Request for local nonresident account	12	-	16	-
Granting guarantee abroad	1	-	5	-
Exemption int. fin. & bus. serv. companies	1,121	-	1,218	-
Other	8	5.0	6	7.2
Total	1,428	745.6	1,564	525.4

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 through 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 2005 through 2007. From the total license fees collected in the Netherlands Antilles in 2007, NAf.42,537.9 thousand (61%) was generated on Curaçao, NAf.25,840.3 thousand (37%) on St. Maarten, and NAf.1,364.0 thousand (2%) on Bonaire. The remaining NAf.368.3 thousand (0%) of license fees was paid through the Bank.

Table 32 License fees collected from 2005 through 2007 (in thousands NAf.)

	2005	2006	2007*
January	3,936.3	4,439.4	5,874.0
February	3,855.8	4,249.1	4,916.7
March	4,534.8	5,140.4	5,795.9
April	4,211.4	4,203.6	5,381.4
May	4,228.8	4,763.3	6,135.5
June	4,306.1	5,065.6	5,802.5
July	4,505.2	4,611.6	5,760.1
August	4,282.0	4,749.7	5,981.3
September	4,228.5	5,310.3	5,398.8
October	3,825.0	4,942.9	6,374.0
November	4,436.2	4,997.9	5,956.6
December	5,318.9	6,407.8	6,733.7
Total	51,669.0	58,881.6	70,110.5

*Preliminary

8 FINANCIAL STATEMENTS FOR THE YEAR 2007

Table 33 Balance sheet as of December 31, 2007 (before profit distribution)

	2006	2007
ASSETS		
Gold	365,805,528	437,627,742
Receivables and securities in foreign currency	1,319,337,825	1,860,108,543
Advances to the central government	12,801,491	-
Government bonds	217,490,594	170,491,708
Other long-term receivables	29,745,966	40,754,277
Fixed assets	91,937,842	87,144,726
Other current assets	34,006,752	22,405,010
Total Assets	2,071,125,998	2,618,532,006
LIABILITIES & EQUITY		
LIABILITIES		
Bank notes in circulation	310,951,560	366,532,033
Residents' current accounts		
- in guilders	666,611,750	758,096,432
- in foreign currency	12,084,756	13,731,672
Residents' time deposits		
- in guilders	219,900,000	295,000,000
Nonresidents' current accounts		
- in guilders	497,232	198,808,271
- in foreign currency	421,594,549	465,683,662
Money in custody	856,734	856,734
Other liabilities	25,299,434	26,982,600
Total Liabilities	1,657,796,015	2,125,691,404
EQUITY		
Undistributed earnings	43,561,425	50,051,250
Specific reserves	309,768,558	382,789,352
Reserve fund	30,000,000	30,000,000
Capital	30,000,000	30,000,000
Total Equity	413,329,983	492,840,602
Total Liabilities & Equity	2,071,125,998	2,618,532,006

The 2006 and 2007 figures are extracted from the audited financial statements.

Table 34 Profit and loss account 2007

	2006	2007
INCOME		
Interest income	60,754,035	90,653,667
Interest expenses	-12,227,164	-34,639,310
Net interest income	48,526,871	56,014,357
Foreign exchange earnings	1,647,285	2,130,480
Miscellaneous income	13,897,737	7,202,069
Subtotal	64,071,893	65,346,906
License fee	59,481,232	69,478,053
Total income	123,553,125	134,824,959
EXPENSES		
Depreciation of fixed assets	4,979,612	5,298,175
Depreciation of printing costs of bank notes	1,026,400	1,334,499
Withdrawn bank notes	141,055	43,700
General expenses	39,692,034	36,143,719
Total expenses	45,839,101	42,820,093
Net income	77,714,024	92,004,866
Distribution of net income:		
Net income	77,714,024	92,004,866
Paid to the central government	-58,143,811	-85,515,041
Change in undistributed earnings	19,570,213	6,489,825

The 2006 and 2007 figures are extracted from the audited financial statements.

8.1 Notes to the balance sheet as of December 31, 2007

8.1.1 Gold

Gold is revalued every year using an average market price. The average market price is calculated as the closing price on the end- of- year balance sheet for three consecutive years. 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 2007 is due partly to funds received from the Dutch Ministry of the Interior and Kingdom Relations related to the debt relief.

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 investment portfolios are added to the specific reserves. Unrealized losses are deducted from the specific reserves formed in previous years. If these unrealized losses are greater than the specific reserves, the difference will be deducted from the result. Realized gains and losses are immediately accounted for in the profit and loss account.

8.1.3 Advances to the central government

In conformity with paragraph 1 of Article 15 of the National Ordinance constituting the Central Bank Statute (P.B. 1985, no. 183), these advances are at all times bound to a maximum of 10% of the budgeted 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 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, accounts receivable, 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 accounts include the noninterest-bearing balances in current accounts of domestic banks, central and island government tax collectors, and other government institutions within the Netherlands Antilles. Most of the balances are denominated in guilders. Foreign currency balances are converted into guilders at the Bank's official mid-rates prevailing at year end.

8.1.10 Residents' time deposits

These deposits 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 balances are mostly interest- bearing.

8.1.12 Money in custody

This amount represents the nominal value of the Bank's liability for 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 liabilities

This item includes an early-retirement provision, accrued interest, and accounts payable.

8.1.14 Undistributed earnings

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

8.1.15 Specific reserves

Article 5 of the National Ordinance constituting the Central Bank Statute (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 2007 revaluation resulted in a net increase in reserves of NAf.73.0 million.

These unrealized gains on gold, foreign exchange, and investments were NAf.71.8 million, NAf.0.1 million, and NAf.1.1 million, respectively.

8.1.16 Reserve fund

The National Ordinance constituting the Central Bank Statute (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 Statute (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 2007

8.2.1 Interest income

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

8.2.2 Foreign exchange earnings

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

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 Statute (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.