



Dollarization as an option for the future monetary system of Curaçao and St. Maarten

Willemstad - According to the President of the Bank van de Nederlandse Antillen, Dr. Emsley Tromp, dolarization should be considered a possible alternative for the future monetary union between Curaçao and St. Maarten. Adopting the dollar has its advantages and disadvantages for the new countries of Curaçao and St. Maarten. However, given the islands' vulnerabilities in the present world economic order, the balance seems to favor dolarization.

In the new constitutional structure, the islands of Curaçao and St. Maarten agreed to form a monetary union with one central bank and share a common currency. However, the balance of payments vulnerability compels us to consider alternatives, one of which is dolarization. Already three of the five islands of the Netherlands Antilles, i.e., the BES islands have opted to introduce the US dollar as the legal tender once their new status takes effect. Is dolarization a better monetary system for Curaçao and St. Maarten? Arguments exist on both sides of the question. Adopting the US dollar as a legal tender for Curaçao and St. Maarten eliminates the risk of devaluation in a possible balance of payments crisis. The absence of this risk will promote trade and foreign investments. Also, dolarized economies could enjoy cheaper foreign borrowing and lower international transaction costs.

One of the disadvantages of dolarization is that the authorities will lose the ability to use the monetary policy to influence the economy. A second disadvantage is that the central bank loses its role as lender of last resort for its banking system. In addition, the central bank will lose its main sources of income, i.e., investment of the foreign exchange reserves and seignorage from issuing banknotes.

The first argument against dolarization can be counteracted by the fact that under the current exchange rate regime, we already have limited scope to pursue an independent monetary policy. Over time, it has shown that small open economies similar to ours rely on fiscal policies and structural measures to promote investments and growth. Regarding the lender of last resort, the introduction of a deposit insurance scheme will address this issue. Some of the funds of such a scheme can come from the current reserve requirements. As for the sources of income of the central bank, the largest share of the Bank's profit consists of license fees, which will continue to exist in a dolarized economy. Also, the Bank's profitability can be preserved by investing its capital and reserves (including gold) at a higher return because they are no longer required to maintain the peg.

In choosing the most suitable exchange rate regime for the future countries in the Kingdom, dolarization seems to be a viable option, given our vulnerabilities in the present world economic order.

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