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Ad hoc measures interfere with sound financial policy in the countries

WILLEMSTAD/PHILIPSBURG - Curaçao did not comply with the balanced budget rule as agreed upon in the dissolution accord of the Netherlands Antilles that included the debt relief for the entities. Preliminary data reported by the Curaçao government indicate that the country registered a cash deficit of NAf.169.3 million in 2011. The failure of the Curaçao government to implement crucial reforms to reduce health care spending was one of the major causes of this deficit. In addition, non-tax revenues remained subdued due to low dividend payouts by state-owned enterprises. Also, tax revenues were lower than expected.

Public sector figures indicate that Sint Maarten recorded a small cash surplus of NAf.1.1 million in 2011 as government revenues slightly surpassed expenditures. This positive outcome was largely ascribable to a rise in turnover tax proceeds as a result of the increase in the turnover tax rate in 2011. Revenues from other tax categories including wage tax, property tax, and excise on gasoline also rose. However, profit tax proceeds dropped in line with the slowdown in economic activities in Sint Maarten during 2011.

The governments of the Netherlands, the former Netherlands Antilles, and the island territories of Curaçao and Sint Maarten agreed in 2006 that the Dutch government would take over the debt of the entities of the Netherlands Antilles up to the level corresponding with an interest burden rule. Because of this, the governments of Curaçao and Sint Maarten could enter their new autonomous status with a sound financial position. After merely two years and one fully completed budgetary process, the Curaçao budget--contrary to the projected surplus--is not in balance. A large gap appears to exist between the projections presented in the approved budget and the budget's realization. The existence of such a gap points to a failing financial management system. This bottleneck must be corrected quickly to prevent the frequent introduction of unexpected compensating measures that will put a drag on economic growth. Moreover, little room exists for further tax increases given the 2011 tax-to-GDP ratio of Curaçao of 26%.

The debt relief will lead to sustainable budgets only if it is complemented with policies aimed at structurally healthy public finances and a solution for the many socioeconomic challenges. One of these challenges is the aging of the population, which is putting an upward pressure on public spending on health care and the old age pension system (AOV). This is particularly the case in Curaçao. The Social Security Bank of Curaçao has indicated that if structural measures are not taken soon, the AOV fund will be depleted by 2014.

Reforming the health care and old age pension systems will require some unpopular measures, including augmenting efficiency in the provision of health care services and increasing the retirement age. Over the years, several studies have been conducted on these subjects and numerous recommendations made to the governments. Regretfully, the much-needed reforms have not been implemented, thus aggravating the scope of the problems and their impact on the budget.

To maintain sustainable public finances and achieve macroeconomic stability, these important reforms cannot be delayed any longer in the anticipation of better times. Relying only on ad hoc measures, which could have undesirable effects, is not an option. Failing to act on all fronts ultimately will erode confidence and increase the risks to macroeconomic and financial stability. Ad hoc measures make structural or fiscal adjustments seem less urgent. In addition, monetary policy also may be constrained by this approach.