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Central bank president recommends joint risk fund

WILLEMSTAD/PHILIPSBURG – The president of the Centrale Bank van Curaçao en Sint Maarten, Dr. Emsley Tromp, has called for the establishment of a joint fund among the Dutch Caribbean countries, once the authority to borrow is removed. "Curaçao and Sint Maarten are small open economies very susceptible to external shocks, including natural disasters," Dr. Tromp pointed out. "If they will have to finance capital investments through surpluses on the current account budget, creating extra fiscal buffers to mitigate the social and economic costs from external shocks will not be viable." The central bank president continued by adding that "to provide for that buffer, an insurance-type stabilization fund can be established for the Dutch Caribbean from which temporary funds can be obtained to mitigate the impact of such an external shock."

Since attaining the status of autonomous countries in the Dutch Kingdom, both Curaçao and Sint Maarten have seen their debt to GDP ratios increase rapidly. "Although these ratios are still relatively low compared to other countries in the region, Curaçao and Sint Maarten must be cautious lest their debt ratios again become unsustainable," Tromp warned. "In Curaçao, growth has been lackluster over the past several years. If the country's poor economic performance continues, servicing debt in the future might soon become a challenge.

"In the case of Sint Maarten, it can be concluded that the price of becoming an autonomous country was inheriting part of the public debt of the former Netherlands Antilles, as Sint Maarten was not allowed to borrow before October 10, 2010," Tromp continued. "Sint Maarten can now borrow to finance investments, but tax revenues have been rising only marginally. Hence, the question arises whether Sint Maarten will be able to cover its current expenditures while complying with its debt obligations in the future.

"Given the risks of unsustainable debt levels in the near future, the authority of the Curaçao and Sint Maarten governments to borrow should be reconsidered except in extraordinary situations. Thus, the current golden rule stating that the current account of the budget must be at least in equilibrium, should be expanded," Tromp said. "When the governments can no longer borrow, capital expenditures should be financed by surpluses on the current account of the budget. The overriding criterion to deviate from this rule would be in the case of a significant adverse external shock that negatively affects the economy by, for example, more than 5% of GDP," he pointed out.

"Instead of burdening future generations with unsustainable debt, the standing subscription rule can be used to provide the initial resources for the suggested stabilization fund. Each partner in the Dutch Kingdom, i.e., the Netherlands, Curaçao, Sint Maarten, and Aruba, should pay an annual fee to the fund," Tromp suggested. "The fund could invest its resources in assets liquid enough to convert easily into cash if one or more countries require funds. If the fund's resources are not sufficient when a shock occurs, the fund could borrow through the Dutch State Treasury Agency," Tromp outlined.

Tromp explained that the European Union is currently exploring the establishment of a European Stabilization Fund, while much closer to home in the Caribbean the Catastrophe Risk Insurance Facility already exists among many of the former British islands since 2007. "The main benefit of such a fund is that the impact of a negative external shock on the government budget will remain limited," he said.

"Given that the fund would have to assess the size of the shock and the budgetary needs of the country requesting financial support, the fund could also assume the role of the budget chamber for Curaçao, Sint Maarten, and Aruba when the current budget supervision authority, CFT, ceases to exist," Tromp continued. "This budget chamber would safeguard the integrity of the budgetary process and assess whether the countries are complying with their budget rule. To prevent free riding, a country requesting resources from the fund should have been in compliance with its annual obligations to the fund and have at least a balanced current budget. As a result, this fund would promote fiscal and debt sustainability for all the Dutch Caribbean countries as well as provide a cushion to mitigate the negative effects of external shocks," Dr. Tromp concluded.

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