

## Report of the President

The economic recession in the Netherlands Antilles continued in the fourth quarter of 1997, reflected by a decline in real Gross Domestic Product of approximately 2.0% on an annual basis. This decline was less than in the previous quarter, which may indicate that the economic downturn is bottoming out. The decline in economic activities in the fourth quarter was due to sluggish domestic demand as the overall export performance improved. Domestic demand was dominated by the decline in government spending due primarily to financing constraints. In contrast, private spending picked up. The inflation rate remained moderate in the fourth quarter compared to the third quarter of 1997. The annualized inflation rate continued to decline primarily because of the fading effect of the government's revenue-enhancing measures on prices.

The improvement in export performance was attributable mainly to the developments in tourism and merchandise exports. The overall performance of the tourist sector was favorable in the fourth quarter of 1997; all indicators of tourist activities recorded a growth. The developments by island differed. In St. Maarten, both the number of stay-over and cruise tourists and the amount of foreign exchange generated increased substantially, owing to the progress made in the island's recovery from the hurricane disaster. In Curaçao and Bonaire, the development in cruise tourism was buoyant, but the number of stay-over tourists continued to decline. The strong growth in the number of cruise tourists in Curaçao contributed to an increase in foreign exchange income generated. In Bonaire, however, foreign exchange revenues from tourism declined. The decline in the number of stay-over tourists can be attributed partly to the appreciation of the Netherlands Antillean guilder, through its peg to the US dollar, vis-à-vis the European currencies. Merchandise exports increased substantially, which can be attributed primarily to the favorable export performance of the free zone.

The oil refinery performed well during the fourth quarter of 1997, as reflected by a substantial increase in the amount of oil refined. The refinery's contribution to the economy increased also, owing to an increase in its operational costs related primarily to payments to local contractors for services rendered.

The transportation sector continued to perform weakly in the fourth quarter of 1997. The developments at the national carrier "ALM" were sluggish, as reflected by a marginal growth in the number of passengers and a further decline in the amount of freight transported. The Bank wants to underline the importance of finding a solution for the company's weak financial position. A solution is crucial for the further implementation of its business plan and, hence, its survival. Furthermore, the amount of foreign exchange generated in the ship repair sector and with oil storage and bunker activities declined. Harbor activities were mixed. In the harbors of Bonaire and Curacao, both the number and tonnage of ships piloted into the harbor grew substantially. This increase was attributable primarily to the near doubling of the number of cruise calls and the marked increase in the number of tankers related to the buoyant oil transshipment activities. In contrast, total cargo movements in the harbor of Curacao continued to decline. This decline can be explained by the sharp decline in bulk goods related to the measures of the European Union to restrict the import of rice and sugar from Overseas Countries and Territories. Container movements continued to increase after the downward development turned around in the third quarter of 1997.

The international financial and business services sector continued to perform weakly, reflected by a decline in both profit taxes paid to the government and income received from services rendered. This development can be related, among other things, to the competitive position of the Netherlands Antilles vis-à-vis other jurisdictions.

In line with the improved export performance and the weak development in merchandise import related to sluggish domestic demand, the deficit on the current account of the balance of payments recorded an improvement. In contrast, the surplus on the capital account declined, due mainly to less development aid received. Nevertheless, the capital account surplus more than compensated for the current account deficit, resulting in an increase in our foreign exchange reserves in the fourth quarter of 1997. This outcome was only marginally below the December target of reserves accumulation in the structural adjustment program.

The General Government recorded a surplus in the fourth quarter of 1997, compared to a deficit in the same quarter of 1996. This improvement was attributable entirely to a sharp decline in expenditures, which more than compensated for a decline in tax revenues. The latter decline was due primarily to a decrease in the collection of profit and income taxes in connection with the economic recession. The decline in expenditures was accounted for partly by an improvement in expenditure control. More important factors were the transitory settlement of the retroactive pay equality to the civil servants in the fourth quarter of 1996 and the forced deferral of payments due to financing constraints. This deferral resulted in increasing arrears at the government pension fund APNA, the sinking fund for early retirement, and in transfers to the national carrier "ALM" and the smaller islands. As a result, the budgetary outcome on a cash basis remained within the target of the structural adjustment program in the fourth quarter as well as for the entire year of 1997.

For 1998, the approved budgets of the Central Government and the Island Government of Curacao adjusted for the carryover of expenditures from 1997, and newly identified shortfalls result in a combined deficit of NAf 257 million. This is a substantial deterioration compared to the actual outcome of NAf 55 million in 1997. Obviously, a deficit of that extent cannot be financed and demands urgent corrective actions from the authorities. These actions should be comprehensive, have a clear short-term impact, and be durable. Steps should be taken to arrest the decline in direct tax collections, and the buoyancy of indirect tax receipts should be improved through a broadening of the tax base and the elimination of loopholes. Furthermore, the budgeted expenditures should be reviewed critically for the possibility of further cuts, and the personnel expenditure policy should remain tight. In addition to these short-term measures, the implementation of structural measures, such as the core-task analysis and the privatization program, should be intensified. Only with a viable package of short- and medium-term measures can the current crisis in our public finances be addressed. Such a package also will facilitate efforts to attract additional finances for a smoother adjustment process.

The monetary aggregates developed moderately in the fourth quarter of 1997. The expansion of the money supply was due primarily to the increase in net international reserves resulting from the surplus on our balance of payments. The domestic sector exerted a marginal expansionary impact dominated by miscellaneous factors. The increase in private sector credit was negligible, which can be attributed to the tight monetary policy and the sluggish demand for credit related to the economic recession. The government sector exerted a contractionary impact owing to an increase in deposits resulting from the budget surplus. As a result, the monetary aggregates remained within the targets set in the structural adjustment program, except for net government credit in the absence of contributions to the sinking fund. Given the high government deficit and uncertainties surrounding the new government's course regarding the structural adjustment program, the Bank further tightened its monetary stance in April 1998. The maximum allowed credit growth to the private sector in the monetary cash reserve arrangement of 2% over the outstanding amount at the end of September 1997 has been extended for the second quarter of 1998. The extension also included the current ceiling on net domestic credit to the government. In addition, the Bank increased the reserve requirement from 3% to 4% in light of the persistent overliquidity at the commercial banks, which is a potential source of excessive credit extension.

The uncertainties surrounding the formation of a new government hamper the much needed structural adjustment of our economy. One of the most important issues to be addressed by the new government is the imbalances in the public sector. Once a viable policy package is implemented, investors' confidence can be regained. Together with an improvement of our investment climate in line with the recommendations of the Interamerican Development Bank, we will be able to create a climate conducive to economic recovery and employment growth.

**E.D. Tromp**  
**President**