



QUARTERLY BULLETIN 2000-4

Bank van de Nederlandse Antillen

REPORT OF THE PRESIDENT

The Netherlands Antillean economy continued its downward trend in the fourth quarter of 2000, as reflected by a decline in real Gross Domestic Product of approximately 4.4% on an annual basis. The decline in economic activities can be explained mainly by poor domestic spending, as the export performance showed signs of improvement. Domestic spending remained poor because of the decline in real disposable income and the continuing migration. In addition, the delays in the implementation of the measures agreed upon with the IMF had a negative impact on business confidence and, hence, private investment. The improved export performance was due mainly to the growth in tourism in St. Maarten. Fourth quarter inflation in Curaçao and Bonaire remained moderate compared to the third quarter. The annualized inflation rate reached 5.8% in Curaçao and 3.9% in Bonaire, up from 0.4% and 3.5%, respectively, in 1999. The high inflation in 2000 can be attributed to the increase in the turnover tax rates, the rise in world oil prices, and higher inflation with our main trading partners.

The overall export performance improved in the fourth quarter of 2000. Our main export sector, tourism, showed favorable results, as foreign exchange revenues from both stay-over and cruise tourism increased. This was entirely the result of the developments on St. Maarten. The tourism sector in St. Maarten recovered significantly from the slump in the fourth quarter of 1999, when the passing of hurricane Lenny caused both cruise and stay-over tourism revenues to plummet. The increase in tourism revenues on the Windward Islands was mitigated by the sluggish developments in Curaçao and Bonaire. Fourth quarter stay-over tourism dropped on both islands, compared to the fourth quarter of 1999. Only cruise tourism in Bonaire improved, but its impact on total tourism revenues was only marginal.

The international financial and business services sector recorded an increase in foreign exchange income. This development was due partly to a rise in profit taxes transferred to the government. In addition, net operational income increased, as a result of both an increase in operational income and a decline in expenses for services rendered. The sector's prospects look brighter after the agreement on the tax arrangement for the Kingdom (BRK) with the Dutch government at the end of December 2000. This agreement ended a period of uncertainty, which was characterized by a marked decline in activities.

Furthermore, the oil refinery recorded an increase in production. In contrast, operational costs declined, due primarily to the lower payments to local contractors. This decline outweighed the increasing costs of the refinery's own fuel consumption in connection with the increased production and the sharp rise in world oil prices. In addition, the performance of the free zone in Curaçao improved, as the number of visitors increased.

The transportation sector performed well in the fourth quarter of 2000, compared to the fourth quarter of 1999. Almost all subsectors contributed to the improvement. The national carrier Air ALM recorded increases in both the number of passengers and the amount of freight transported. This is even excluding the transatlantic flights, which were introduced in December 2000 in cooperation with the Belgium company City Bird. The airport of Curaçao recorded an increase in total passenger movements due to a substantial increase in transit

passengers. The number of ships piloted into the harbors of Curaçao and Bonaire increased substantially in the fourth quarter of 2000. This increase was accompanied by increases in both transshipment and local cargo movements in Curaçao's harbor. Finally, activities in the ship repair sector improved as both the number of man-hours sold and ships repaired increased. Only bunker sales showed a decline in both water and fuel.

In line with the positive developments in our main export industries, the current account of the balance of payments improved significantly in the fourth quarter of 2000. Other factors that contributed to this improvement were the receipt of the final settlement of the division of assets and liabilities ("boedelscheiding") with Aruba and a decrease in expenditures on travel by Netherlands Antillean residents. This decrease in expenses can be attributed to the sluggish development in domestic demand. Contrary to the current account, the combined capital and investment account deteriorated, as a result of official capital transactions. Namely, the inflow of Dutch liquidity assistance in the fourth quarter of 2000 was considerably less than the inflow from Dutch foreign exchange assistance and foreign borrowing in the fourth quarter of 1999. The liquidity assistance came on top of that received in September in connection with the agreement with the IMF and was necessary to alleviate the shortage of domestic finance in the government sector. As the improvement of the current account more than offset the deterioration of the capital and investment account, our foreign exchange reserves increased.

The General Government's deficit on a cash basis deteriorated substantially in the fourth quarter of 2000, compared to the fourth quarter of 1999. The deterioration was attributable entirely to the increase in expenditures, related primarily to the reduction in arrears to the civil servants pension fund and private creditors with the liquidity support received from the Dutch government. In addition, higher subsidies to Air ALM, liquidity support from the central government to the smaller island governments, and the sharing of turnover tax revenues between the central government and the governments of the smaller islands contributed to the increase in expenditures. The rise in expenditures was mitigated partly by higher revenues, owing to a transfer from Aruba related to the final settlement of assets and liabilities with the Netherlands Antilles and more tax revenues. The increase in tax revenues was concentrated in the turnover tax and the wage tax. The higher turnover tax revenues can be explained by the fact that businesses had to get accustomed to the tariff increase of October 1999. The increase in wage tax revenues resulted from a special effort of the tax office with Dutch technical assistance to improve compliance. In contrast, revenues from excises, import duties, profit tax and income tax all declined, due to the continued economic downturn.

Although the deficit on a cash basis remained below the program target in 2000, a considerable shortfall has been projected for 2001. During its March 2001 visit, the IMF delegation estimated a deficit of NAf 225 million, compared to the targeted NAf 85 million. Factors that contributed to this shortfall were a weaker than expected economy, the ill-prepared decentralization of the tax apparatus, new spending initiatives, and partial and delayed implementation of the program measures. Given the continuing shortage of domestic financing, it is evident that the original target cannot be attained. Therefore, the authorities agreed with the IMF to reduce the deficit to the 2000 level of NAf 150 million. Measures to raise the necessary NAf 75 million include health care reforms, reduction of expenditures on goods and services, and a repetition of the effort of the tax office to improve tax collection with Dutch technical assistance.

The money supply increased markedly in the fourth quarter of 2000. The expansion was attributable to increases in both net foreign assets and net domestic assets of the banking sector. The increase in net foreign assets is explained by the surplus on the balance of payments. The domestic expansion resulted from an increase in credit to the private sector and a decline in capital and reserves of the Bank due to the revaluation of the gold reserves. In contrast, the government sector had a contractionary impact on the money supply, as its demand for liquid assets dropped in connection with the liquidity assistance received from the Dutch government. Without this exceptional factor, the monetary impact of the government sector would also have been expansionary. Although private sector credit growth has decelerated considerably in the fourth quarter of 2000, the pace of credit growth continued to exceed the nominal growth rate of the economy, thereby imposing a potential threat to our foreign exchange reserves position. In light of this development, the Bank increased the reserve requirement from 11% to 11.25% in November 2000, and to 11.5% in January 2001. This increase will tighten the liquidity position of the commercial banks, which should mitigate domestic money creation and thus support our foreign exchange reserve position. On the other hand, the Bank excluded interbank deposits from the reserve requirement as of February 16, 2001, to eliminate double counting and to promote the development of the interbank market.

The authorities started vigorously with the implementation of a comprehensive structural adjustment program, which has been agreed with the IMF on September 15, 2000. Based on the progress made, the IMF requested the Dutch government to provide additional liquidity assistance in November 2000, because of the shortfall in domestic financing. However, from December 2000 delays in the implementation started to accumulate. In March 2001, the authorities discussed a set of prior actions to get the program running again. In addition to the reduction of the deficit, these prior actions included the implementation of the measures that had been delayed. It is crucial that the authorities show their commitment to continue on the track of structural adjustment. Therefore, the prior actions should be met without delay to resume the adjustment program and to free the liquidity support from the Dutch government. Resumption of the program is also essential to release funds for the revitalization of our economy with the assistance of the World Bank and the FIAS. Only this two-tier approach will create a solid foundation for restoring confidence, sustainable economic recovery and, hence, the much-needed creation of jobs.

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President