



QUARTERLY BULLETIN 2002-2

Bank van de Nederlandse Antillen

REPORT OF THE PRESIDENT

Developments in the second quarter of 2002 indicate that the recovery of the Netherlands Antillean economy did not gain more ground. Real Gross Domestic Product contracted by 0.5% on an annual basis, about the same as the 0.4% contraction in the previous quarter. Although the slowing global economic recovery was partly to blame, continuing uncertainty in the domestic economy contributed mainly to this mediocre performance. The long formation period after the January elections held back investment decisions of producers, while consumer confidence remained low as a result of uncertain job and income prospects. However, government spending expanded, mitigating the subdued private demand. Inflationary pressures continued to subside, due mainly to the reduction of the economic levy on cars as of January 1, 2002, and the lower inflation of our main trading partners.

In line with the sluggish development in the world economy, our export sector continued to perform weakly. The aftermath of the September 11 terrorist attacks on the United States and the threat of a war with Iraq continued to affect our major generator of foreign exchange, the tourism sector. The number of stay-over visitors declined further due to the development in St. Maarten, which depends heavily on the North American market. By contrast, Curacao's stay-over tourism continued to grow, supported by increased marketing efforts. The decline in stay-over tourism was set off partly by the growth in cruise tourism on both islands. In contrast, our second main generator of foreign exchange earnings, the international financial and business services sector, performed well. Both income received from services rendered and profit tax to the government increased. This improvement may be related to a growth in activities since the effectuation of the new tax arrangement for the Kingdom of the Netherlands (BRK) and the new fiscal regime (NFR) as of January 1, 2002.

Developments in the transportation sector remained mixed. Harbor activities increased, as Curacao's harbor recorded more ships and an increase in cargo handled. In addition, bunker sales of fuel rose but bunker sales of water fell. Bonaire's harbor also registered an increase in the number of ships, dominated by the ferry-connection with Curacao. The ship repair sector noted an expansion, reflected by an increase in the number of man-hours sold. Contrary to aforementioned developments, the activities in the air transportation industry declined, attributable to fewer passengers handled by Curacao's airport and a marked worsening in the regional operations of our national carrier Dutch Caribbean Airlines (formerly Air ALM). The decline in passengers at Curacao's airport was related mainly with the rerouting of a stopover to Bonaire by the Dutch carrier KLM on its Amsterdam-Lima flights, and the decline in passengers and freight transported by DCA. The latter can be explained primarily by the cancellation of cooperation agreements between Air ALM and other carriers, which have not been renewed yet by DCA. Because of the rerouting of KLM's flights, Bonaire's airport activities surged. Furthermore, oil transshipment and oil storage activities deteriorated. Also the refinery recorded a decline in activities, reflected by a drop in the number of barrels produced. Finally, free-zone activities in Curacao marked a mixed performance as re-exports decreased but the number of visits soared.

The sluggish economic development was accompanied by an improvement of our balance of payments. The current account deficit declined substantially owing to the improvements in the trade, services, and current transfers balances. The improvement in the trade balance was attributable to lower imports of general merchandise and oil products, due to weak private demand and lower oil

prices, respectively. The improvement in the services balance was accounted for mainly by the good performance of the international financial and business services sector, as tourism and transportation performed poorly. The growth in transfers from abroad by individuals continued in the second quarter of 2002, resulting in a marked improvement in the current transfers balance. The combined capital and financial account improved also, as a result of an increase in foreign assets and a decrease in foreign liabilities. The increase in assets was related primarily to more portfolio investments abroad and the increase in reserves, while the decrease in liabilities was caused mainly by a decline in outstanding trade credit received by local companies and fewer loans received from abroad.

The General Government registered an increase in its deficit on a cash basis in the second quarter of 2002. The widening of the deficit was attributable primarily to higher current expenditures. All expenditure categories contributed to the increase, of which interest payments and wages and salaries in particular. The higher interest payments were related to the increase in treasury bills issued through auctions coordinated by the Central Bank. Investors showed increased appetite for local government securities compared to the low-yielding alternatives abroad. This facilitated the government's access to domestic finance and, hence, budget spending. In the second quarter of 2001, the government was forced to reduce its cash expenditures as it was not able to rollover its maturing debt. The increase in wages and salaries was accounted for mainly by better compliance with payments to the civil servants pension fund. Enhanced revenues, primarily as a result of better tax performance, mitigated the higher expenditures. Wage and profit tax revenues rose particularly, due to special efforts of the tax authorities to improve compliance.

The Bank wants to re-iterate that the present abundance of domestic financing should not tempt the governments to delay their fiscal consolidation efforts, as the budget deficits are still high and the outstanding debt is rising rapidly. Therefore, the design and implementation of a credible program aimed at the further restructuring of the public finances must remain high on the political agenda.

The monetary aggregates showed a moderate expansion in the second quarter of 2002. The increase in net foreign assets resulting from the balance of payments surplus contributed mainly to this expansion, complemented by an increase in net domestic assets. The increase in the domestic sector was attributable entirely to the expansionary impact of the private sector due to a marked increase in loans. All loan categories recorded an expansion, which occurred entirely on the Leeward Islands. In contrast, the government sector exerted a contractionary impact. This development was due entirely to the island governments, resulting from a decline in securities of the Island Government of Curacao with the banking sector.

In light of our strong international reserves position, moderate credit growth, the excess liquidity in the banking sector, and low interest rates abroad, the Bank decided to further ease its monetary stance. This was effectuated through a further reduction of its official lending rate (i.e., the pledging rate) from 6.75% to 5.75% on June 1, followed by reductions to 5.0% on July 4, 4.0% on August 20, and 3.5% on November 4, 2002. These actions brought the Bank's official rate more in line with the declining trend in the rates in the domestic money and capital market. This trend was promoted partly by the Bank through the introduction of variable rate tenders of Certificates of Deposit and treasury bills since the beginning of the year.

The stagnation in the recovery of our economy calls for urgent actions by our policymakers to address the macroeconomic disequilibria and to promote economic growth. These actions should be translated in a credible government program based on the continuation of the three-pronged policy approach of fiscal consolidation, structural reform, and a growth strategy followed during the past few years. In this respect, the authorities should refrain from creating the impression that the liberalization of the product and labor markets will be partially reversed, as this may hamper the recovery process.

To underpin the authorities' commitment to such a program, periodic performance targets should be included to measure the program's progress. Full and timely implementation will strengthen investors' confidence and, hence, facilitate a sustainable recovery of our economy and the creation of much-needed jobs.

E.D. Tromp
President

REAL SECTOR AND INTERNATIONAL DEVELOPMENTS

General economic developments

In 2002's second quarter, the world economy was sluggish, as growth stalled in some European, Asian, and Latin American nations. In the United States, the corporate scandals, which began in mid-May, did more damage to the stock markets than the September 11 attacks, weakening the US dollar on a trade-weighted basis. The Dow Jones Euro Stoxx¹ -index, the Standard & Poor 500 index, and the Nikkei 225-index traded losses of, respectively, 14%, 11%, and 8% in the period of May 1 to July 3. During the second quarter of 2002, the world oil prices dropped, when measured against the same quarter in 2001. In line with the world economy, the economy of the Netherlands Antilles remained muted, as real GDP shrank in the months of April-June 2002. The second-quarter drop was accompanied by a weak labor market. Inflationary pressures continued to subside, as consumer prices withered in the second quarter of 2002.

National production and spending

Real GDP of the Netherlands Antilles contracted slightly by 0.5%² in the quarter ending June 2002, an improvement from the 3.3% drop in the corresponding period of 2001. The paltry improvement was helped by higher overseas demand, stemming from a surge in the harbor, mining, air transportation (transatlantic), and cruise tourism sectors. The financial sector deteriorated, however, as the number of registrations of the international financial companies shrank by 1.6%. Private demand dwindled, as a result of a lack of producer and consumer confidence, caused by the weak economy. Many producers continued to hold back their investments. Consumer confidence remained low, a result of uncertainties surrounding job and income prospects. Government consumption and investment rose by 11.8% and 35.7%, respectively. Annual inflation decelerated to 0.5% in the June quarter of 2002, due largely to a price drop in automobiles, owing to the phasing out of the economic levy.³

Inflation

Consumer prices in the Netherlands Antilles continued a downward trend in the second quarter of 2002. Annual inflation tapered to 0.5% from 3.2% during the period April-June 2001. The lower second-quarter inflation was related to: (1) cheaper automobile and car part prices, and (2) lower inflation of one of our major trading partners, the United States. In the June quarter of 2002, Curacao posted the lowest annual inflation of 0.4%, down from the 3.8% registered in the same period of 2001. Bonaire's and St. Maarten's annual inflation reached 0.8% and 1.1%, respectively, compared to 1.8% and 0.3% in the second quarter of 2001.

On a quarterly basis, Curacao's inflation drifted upwards by 1.5% in the second quarter of 2002, after a deflation of 1.6% in the first quarter of 2002. This price surge was driven mainly by

¹ (Stock)-index of the Euro-area

² Estimate by the BNA

³ The economic levy was lowered from 18% to 9% on January 1, 2002, as a result of the policy to phase out market protection

"housing" (3.1%) and "transport & communication" (3.0%), led by higher utility costs and gasoline prices. The higher gasoline price outbalanced the price drops in automobiles and car parts. During this period, domestic gasoline prices rose, attributable to the price adjustment mechanism policy ("correctiefactor systeem") of the oil distribution company "Curoil." In contrast, the deflation in the category "clothing & footwear" (1.2%) was linked to price reductions in apparel.

Table 1
Inflation rates in the second quarter of 2002 (% changes)

	Curacao	Bonaire	St. Maarten
Food	0.4	0.3	0.5
Beverages & tobacco	0.1	-0.2	-0.2
Clothing & footwear	-1.2	0.0	-0.2
Housing	3.1	0.1	0.3
Housekeeping & furnishings	0.5	-0.8	-0.4
Health	0.4	0.1	0.0
Transport & communication	3.0	-0.6	-0.2
Recreation & education	0.2	0.0	0.0
Other	0.4	0.1	0.2
General inflation rate	1.5	-0.1	0.1

Bonaire posted a deflation of 0.1% in the second quarter of 2002, following the first quarter's deflation of 0.8%. Price decreases in the sectors "housekeeping & furnishings" (0.8%), "transport & communication" (0.6%), and "beverages & tobacco" (0.2%) were responsible for the second-quarter deflation. The fall in "housekeeping" & furnishings" was due to lower household expenses. Lower-priced automobiles and car parts resulted in a deflation in "transport & communication." In contrast to Curacao, this price drop offset the price hike in gasoline in Bonaire. A decline in the beverages component caused the deflation in the item "beverages & tobacco." Meanwhile, costlier fresh produce led to the price gain in the "food" item (0.3%).

Consumer prices in St. Maarten accelerated by 0.1% in the June quarter of 2002, up from 0.6% deflation in the preceding quarter. The largest price surge was in the category "food" (0.5%), aided by price gains in fresh produce and outdoor dining. This increase was followed by "housing" (0.3%), a consequence of higher electricity costs. By contrast, "housekeeping & furnishings" showed the largest price decline of 0.4%, stemming from lower home furnishings costs.

Labor market

According to the Fourth Population and Housing Census Netherlands Antilles 2001, the jobless rate in the Netherlands Antilles tapered to 14.6% in 2001 from 15.3% in 1992. This drop was the result of a fall in the labor force, caused by the vast migration, largely from the island of Curacao. Analysis by island shows that the unemployment rate rose on all islands, except Curacao, during the period 1992-2001. The unemployment rate in Curacao fell from 16.9% in 1992 to 15.8% in 2001 (table 2). In contrast, the participation rate increased by 0.2 percentage point to 43.3%, because more women participated in the labor market.

Bonaire's jobless rate worsened to 9.1% in 2001 from 8.3% in 1992 (table 2). The unemployment discrepancies between males and females shrank, as the jobless rate of males was up, while that of

females dropped. Similar to Curacao, more women in the labor market accounted for the higher participation rate in Bonaire (49.6%).

Table 2
Labor force, participation rate, and unemployment rate on the Leeward Islands

	Curacao		Bonaire	
	1992	2001	1992	2001
Employed	51,642	47,686	4,430	4,865
Unemployed	10,534	8,973	402	486
Labor force	62,176	56,659	4,832	5,351
Total population	144,097	130,627	10,187	10,791
Participation rate (%)	43.1	43.3	47.4	49.6
Unemployment rate (%)	16.9	15.8	8.3	9.1

Source: Fourth Population and Housing Census Netherlands Antilles 2001, CBS

St. Maarten's unemployment rate remained almost unchanged at 12.8% in 2001 (table 3). Similar to Curacao, the total population and the labor force in St. Maarten decreased during the period 1992-2001. In contrast to the Leeward Islands, the participation rate in St. Maarten shrank by 1.9 percentage points to 58.1% in 2001.

Table 3
Labor force, participation rate, and unemployment rate on the Windward Islands

	St. Maarten		St. Eustatius		Saba	
	1992	2001	1992	2001	1992	2001
Employed	16,911	15,495	817	1,038	524	598
Unemployed	2,425	2,282	50	96	23	39
Labor force	19,336	17,777	867	1,134	547	637
Total population	32,221	30,594	1,839	2,292	1,130	1,349
Participation rate (%)	60.0	58.1	48.4	49.5	48.4	47.2
Unemployment rate (%)	12.5	12.8	4.2	8.5	4.2	6.1

Source: Fourth Population and Housing Census Netherlands Antilles 2001, CBS

Through the period 1992-2001, the labor force in St. Eustatius and Saba grew by 30.8% and 16.5%, respectively (table 3). The larger labor force was related mainly to the creation of more jobs. Nevertheless, the jobless rate in St. Eustatius and Saba jumped to 8.5% and 6.1%, respectively, in 2001. St. Eustatius' labor participation rate rose to 49.5%, while Saba's drifted down to 47.2%.

In the second quarter of 2002, the number of people collecting welfare payments in Curacao continued to decline, while the number of cancellations continued to increase, primarily because of migration.

Table 4
Development in welfare payments in
Curacao

	2001-II	2002-II
Number of requests	172	42
Number of cancellations	306	328

Source: Dienst Werk en Inkomen.

Developments by sector

Mining

In the second quarter of 2002, Bonaire's salt industry offered a mixed picture. Salt exports sagged by 7.8%, compared to the tumble of 54.8% in the period April-June of 2001. Conversely, salt production swelled by 23.7%, down from 32.3% in the second quarter of 2001.

Industry

Through the months April-June 2002, activities in the oil refinery "Isla" took a downturn, as oil refining withered by 17.7%, a deterioration compared to the growth of 4.4% in the corresponding period of 2001. This discouraging performance was accompanied by a fall of 0.3% in total operational costs, following 2001's second quarter gain of 1.5%. Declines in contract payments (16.9%) and other expenses (17.2%) mainly accounted for the lower total operational costs. Payroll expenses, however, were up by 12.5%, a result of adaptation in salaries and benefits.

In Curacao, the ship repair sector offered mixed results in the three months ending June 2002. The number of man-hours sold jumped by 22.7%, an improvement from the 10.8% drop in the second quarter of 2001. On the other hand, the number of ships repaired shrank by 15.0%, contrasting with the advance of 15.0% in the April-June period of 2001. During the second quarter of 2002, fewer ships came in for repairs, but the amount of work expanded. In addition, ship repair earnings rose by 5.9%.

Construction

Second-quarter developments in Curacao's construction sector were mixed in 2002. During this period, the number of finished projects declined by 13.3%, due to fewer residential developments. The value of construction permits, however, rose by 30.2%, owing to more nonresidential projects. Similar to Curacao, the total value of completed construction projects in Bonaire swelled by 12.2%, measured against a tumble of 23.8% in the second quarter of 2001.

Utilities

In 2002's second quarter, utility production in the Netherlands Antilles expanded. Water production rose by 1.5%, as opposed to a decrease of 2.6% in 2001's second quarter. An analysis by islands indicates that the higher water output was led by advances in Curacao (1.7%) and St. Maarten (1.3%). Bonaire, on the other hand, recorded a drop of 1.4%, in comparison to the 1.9% fall in the second quarter of 2001.

Alongside the higher output of water, electricity production in the Netherlands Antilles expanded by 2.8%, up from the 4.5% slide in the months April-June 2001. A breakdown by island indicates that the gain was due to accelerations of 10.4 and 7.2 percentage points to 10.7% and 1.0%, respectively, for the Windward Islands and Curacao. Similar to the development in water output, Bonaire's electricity production declined by 6.3%, down from the fall of 2.5% in the second quarter in 2001.

Trade

Curacao's free zone sector performed poorly through the months of April-June 2002. The free zone re-exports deteriorated by 16.2%, compared to a jump of 41.6% in the same quarter of 2001. The number of free zone visitors soared by 26.6%, up from the slide of 0.4% in the second quarter of 2001. This upbeat second-quarter outcome was largely the result of more visitors from the main markets, including Jamaica, the Dominican Republic, and Trinidad.

Tourism

Tourism figures for the second quarter of 2002 revealed that the number of stay-over visitors in the Netherlands Antilles fell by 8.0%, compared to a 0.6% fall in the second quarter of 2001. In contrast, the number of cruise tourists expanded by 9.5%, up from 2.4% in 2001's second quarter. As a result of these developments, proceeds from tourism declined by 3.3% in the second quarter of 2002.

St. Maarten's tourism industry offered mixed developments in the June quarter of 2002. Stay-over arrivals worsened by 11.7%, in comparison to a decline of 2.2% in the second quarter of 2001. The number of visitors declined in all markets, but the main markets--North America (6.5%) and Europe (16.8%)--were largely responsible for the lower stay-over tourism. The cruise tourism business, however, expanded by 6.6%, down from the second quarter's 10.5% in 2001. Evidently, St. Maarten's tourism sector still is suffering from the aftermath of the September 11 attacks.

Table 5
Developments in stay-over tourism in Curacao and St. Maarten (% change)

	Curacao		St. Maarten	
	2001-II	2002-II	2001-II	2002-II
North America,	6.5	6.6	5.5	-6.5
of which:				
-U.S.A.	9.9	8.7	8.3	-6.7
-Canada	12.7	-9.5	-19.1	-4.8
Europe,	16.2	-4.5	-16.4	-16.8
of which:				
-Germany	-15.6	6.1	-	-
-The Netherlands	14.1	-4.3	-2.3	-10.8
-France	-	-	-18.8	-15.5
South & Central America,	-6.4	-1.5	-14.5	-49.7
of which:				

-Argentina	4.8	-2.8	-41.4	-86.3
-Brazil	64.0	-6.1	41.3	-46.7
-Colombia	29.3	17.5	-	-
-Venezuela	-11.5	-9.4	-7.4	-50.3
Caribbean, of which:	-0.1	23.2	1.5	-5.2
-Dominican Republic	15.9	20.3	4.2	-27.9
-Haiti	-6.3	14.2	6.6	-30.4
-Jamaica	-21.7	95.5	-	-
-Trinidad & Tobago	6.3	15.0	20.1	7.6
-Aruba	-1.7	18.3	-	-
Rest of the world	-19.3	-11.0	-1.6	-16.8
Total	3.4	3.1	-2.2	-11.7

In 2002's second quarter, Curacao's tourism industry registered a growth of 3.1% in the number of stay-over visitors, down slightly from the 3.4% in the same period of 2001. The growth in the second quarter of 2002 stemmed from gains in the North American (6.6%) and the Caribbean markets (23.2%). Meanwhile, the European market showed a decline of 4.5%, due largely to fewer visitors from its main market, the Netherlands. The political turmoil in Venezuela was responsible for fewer Venezuelan arrivals, leading to a fall in the South American market (1.5%). Despite the favorable stay-over tourism figures, the hotel occupancy rate shrank by 0.3 percentage point to 52%. The lower hotel occupancy rate was attributable to: (1) the increase in the number of hotel rooms; and (2) stay-over visitors shifting from the larger hotels to other commercial accommodation providers. Cruise tourism arrivals were up by 18.8%, an improvement from the slide of 18.9% through the months of April-June 2001.

Transportation

Developments in Curacao's airport were unfavorable in the period ending June 2002. Total passenger traffic dwindled by 14.7%, due mostly to a decline in the flow of transit passengers (45.2%). The marked drop in the flow of transit passengers may be related to the rerouting of the stopover on KLM's Amsterdam-Quito flight from Curacao to Bonaire in June. The number of passenger departures, however, rose by 1.1%, compared to a fall of 1.2% in the period April-June 2001. In the second quarter of 2002, the number of commercial landings decreased by 6.3%, compared to a fall of 6.0% in the same period of 2001.

More activities were reported at Bonaire's airport in the second quarter of 2002. The flow of transit passengers doubled, causing Bonaire's total passenger traffic to surge by 7.4%. This outcome was linked to the rerouting of the daily KLM flight between Amsterdam and Quito from Curacao to Bonaire. By contrast, passenger arrivals and departures drifted down by 9.6% and 7.4%, respectively.

Curacao's air transportation sector held up poorly in the June quarter of 2002. The national airline "Air ALM" has officially changed its company name to "Dutch Caribbean Airlines." The number of passengers transported by the "Dutch Caribbean Airlines" weakened by 32.7%,⁴ following a drop of

⁴ Excluding transatlantic figures

4.1% in the same period of 2001. Additionally, cargo shipments worsened by 37.9%, as opposed to the 0.3% increase in 2001's second quarter. These declines were caused by the cancellation of the agreements between "Air ALM" and other carriers in the fourth quarter of 2001. In contrast, the number of passengers on the transatlantic flights by the "Dutch Caribbean Airlines" soared by 78.4% in the second quarter of 2002.

Through the June quarter of 2002, oil transshipment in the Netherlands Antilles shrank by 39.7%, caused by a drop in transshipment activities on all islands. Furthermore, oil storage activities weakened by 58.3%, measured against the second-quarter growth of 8.0% in 2001.

The performance in Curacao's harbor industry was buoyant in the second quarter of 2002. The number of ships that entered the harbor increased by 14.8%, compared to a gain of 3.6% in the corresponding period of 2001. The 2002 second-quarter increase was due largely to more than a three-fold surge in the number of other vessels, a result of more inter-island ferry transfers between Bonaire and Curacao. Conversely, the number of tanker ships slipped by 16.6%, related to a fall in oil transshipment. In spite of fewer cargo vessels (6.9%), total cargo movements increased by 11.6%, after a rise of 7.0% in 2001's second quarter. This acceleration was the result of more transshipment (57.7%) and local activities (7.3%). Second-quarter bunker sales of fuel in Curacao were up by 5.2%, while bunker sales of water tumbled by 23.9% in 2002.

Through the months April-June 2002, activities in Bonaire's harbor sector expanded, as the number of ships piloted into the harbor swelled by 41.9 %, an improvement from the reduction of 20.4% in the same quarter of 2001. Similar to Curacao, this gain was linked mostly to more inter-island ferry transfers of "the Chogogo" between Bonaire and Curacao.

International economic developments

The United States

In the June quarter of 2002, the US economy advanced by 2.1%, up from the 0.1% decline in the same period of 2001. The main contributors to the second-quarter growth were higher consumer spending (3.1%), residential investment (3.1%), and government spending (4.0%), largely on defense. Spending on national defense mounted by \$34.3 billion, as the government's war on terrorism continued. This increased spending raised the budget deficit. The corporate scandals that escalated in mid-May led the Dow Jones index to decline by about 18%. These scandals have weakened the US dollar, when measured against the currencies of its major trading partners (except Mexico), since February. The second-quarter growth was restrained by a deteriorating trade deficit. In spite of the weaker US dollar, exports narrowed (2.8%) and imports expanded (3.5%), worsening the current account deficit by 31.0% to \$130 billion. The threat of a July strike by dockworkers on the West Coast may have added to the second-quarter import growth.

Table 6
Selected indicators of various countries (% change)

	United States		Netherlands		Venezuela		Japan	
	01-II	02-II	01-II	02-II	01-II	02-II	01-II	02-II
Real GDP	-0.1	2.1	1.6	0.1	2.6	-9.9	0.6	-0.6
Cons. prices (%)	3.2	1.1	4.5	3.4	12.5	19.6	-0.8	-0.7
Unempl.rate (%)	4.6	5.9	2.1	2.5	*13.3	*16.2	4.9	5.4
Current account balance	-99	-130	-138	-872	1.7	1.7	792	1,507

(bln \$/mln ¥/bln \$/bln I)

Source: Bloomberg/Central Bureau of Statistics

* June 2001/June 2002

Despite increases in the cost of medical care, insurance premiums, and tobacco, inflation remained subdued at 1.1% in the second quarter of 2002, compared to 3.2% inflation in the same quarter of 2001. To buoy sales, automakers, major US carriers, and clothing retailers used major discounts. The job market remained weak as the unemployment rate jumped to 5.9%. Since the recession in March 2001, businesses prefer to extend the workweek instead of hiring more full-time workers. The longer work week combined with the new technology the companies purchased a decade ago, helped the second-quarter productivity to quicken by 4.8%. Meanwhile, unit labor costs fell by 2.2%, down from the surge of 3.6% in the April-June quarter of 2001. Based on low inflation expectations, the Federal Reserve left the federal funds rate unchanged for the third time this year at 1.75% in May.

European Union

The Euro-zone's economy expanded by 0.6%, owing to increases in the financial & business services (0.4%), other services (0.3%), and trade, transport, & communication services (0.2%) sectors. However, the industrial and construction sectors reduced production by 0.2% and 0.1%, respectively. An analysis by components of final demand reveals a deceleration in private consumption growth to 0.3% from 1.6% in the second quarter of 2001. Moreover, gross fixed capital formation declined by 2.9%, in comparison to the 2.5% fall in the second quarter of 2001. The current account deficit of the Euro-zone improved to Euro 1.8 billion, compared to Euro 9.9 billion in the June quarter of 2001. The jobless rate in the Euro-zone rose to a two-year high of 8.4% in the second quarter of 2002, after a steady decline since the third quarter of 2000. Two large companies, Fiat and Siemens, eliminated more than 250,000 jobs this year, due to the drop in sales. Inflation in the 12 nations sharing the Euro fell in the second quarter of 2002, due mainly to lower oil prices. The value of the euro appreciated against the US dollar, as the latter currency was dragged down by falling stocks and corporate accounting scandals.

Real GDP of the Netherlands grew marginally by 0.1% in the second quarter of 2002, down from 1.6% in the second quarter of 2001. An analysis by sector shows that the manufacturing sector decreased, while commercial services, such as trade, tourism, and transportation showed no growth. The second-quarter growth in 2002 was driven by household and government consumption, which grew by 1.1% and 3.0%, respectively. Meanwhile, investment and exports fell by 3.3% and 2.2%, respectively. Investment dwindled, as telecommunication service companies cut back on their investment programs because of faltering demand. The decrease in exports was mainly the result of a fall in re-exports. Along with exports, imports dropped by 3.5%. However, the decrease in

imports was outweighed by the decline of exports, causing the current account deficit to deteriorate by Euro 734 million.

In the quarter ending June 2002, the jobless rate in the Netherlands rose to 2.5% from 2.1% in the same period of 2001. With the economic slowdown, companies had to trim their workforce to reduce costs. Second-quarter inflation in the Netherlands remained high at 3.4%, compared to the Euro-nations' inflation (1.8%). Euro inflation decelerated when compared to the 3.0% inflation in the April-June period of 2001.

Caribbean States

September 11 has affected the tourism industry in most of the Caribbean states. The tourism-oriented Caribbean economies experienced a serious collapse, causing the small-scale hotel businesses to go bankrupt. Jamaica, the Virgin Islands, and Cuba are struggling to recover from the global shocks triggered by the attacks. After the collapse of the Soviet Union, tourism and remittances from Cuban-Americans became Cuba's main foreign exchange earners instead of sugar exports. Both have dropped substantially after the attacks on the United States. Cuba used to barter its sugar with its former allies at preferential rates in return for oil and other essentials. Since October 2000, Venezuela has been supplying one-third of Cuba's oil imports on credit with 2% interest, after Mexico refused to include Cuba in the San Jose Pact.⁵ Cuba produces approximately 31,000 barrels of crude oil a day, not enough to cover its needs. To finance the country's basic imports, tourism receipts have to increase. This may explain President Castro's efforts to allow former U.S. president Jimmy Carter to speak freely on television during his visit in Cuba.

The World Bank published a report on June 11, 2002, which estimated the economic and social costs of crime, drug-trafficking, prostitution, and Aids/HIV in the Caribbean region. The results showed the huge impact these issues have on the fragile Caribbean economies. Jamaica and the Bahamas recorded a loss of approximately \$70 million in tourism revenues as a result of the fear of crime. Premature deaths due to the Aids/HIV virus were calculated at a loss in production capacity of 0.01% to 0.37% of GDP to the Caribbean countries in 2000.

Latin America

South America's largest economy was sluggish, as Brazil's real GDP decelerated to 1.0% in the April-June quarter of 2002 from 2.1% in the second quarter of 2001. Weak consumer spending, a result of high interest rates and a declining currency, was responsible for the economic slowdown. Moreover, higher borrowing costs limited the companies' access to credit. Concerns over inflation caused the central bank to leave the overnight rate unchanged at 18.5% in June 2002.

The prospect that a leftist candidate will win the October presidential election in Brazil has caused the stock and bond markets to plunge and the real to depreciate since March 2002. The high interest rates accompanied by the real's weakness raised the country's debt burden. To avoid an economic and government collapse similar to Argentina's, Brazil borrowed \$10 billion from the International Monetary Fund in June. Despite the depreciation of the real and costlier fuel prices, the second-

⁵ Under the San Jose Pact, the two major crude exporters of Latin America - Mexico and Venezuela - provide some (specific) Central American and Caribbean countries with 120,000 barrels a day under preferential conditions

quarter inflation remained almost unchanged at 7.4% in 2002. In June, fuel prices rose as the government raised the wholesale charges for the state-controlled fuel. Many companies have not been able to pass on the higher costs of imported goods to consumers because of the weak consumer demand. Although the 9-month power rationing ended in March, many companies continued to cut jobs, causing Brazil's jobless rate to swell to 7.5% in the June quarter of 2002. Exports rose by 5.7%, while imports dropped by 6.0%, narrowing the current account deficit by 38.8% to \$1,294 million. The slumping currency and a strike in the customs agency since April boosted the trade surplus.

Argentina's frail economy worsened in the second quarter of 2002. The bank deposit limits imposed by the government in the fourth quarter of 2001 have deepened the recession. The deposit restrictions and rising inflation have led everyone to hoard dollars, thereby driving down the peso even further. Since the government abandoned the peg of the peso to the dollar in January 2002, the currency has lost about 70% of its value, pushing the inflation to around 28%. To maintain the solvency of the faltering banking system, the government has printed more than \$7 billion in pesos. The unemployment rate has risen as high as 20%, and 54% of the population is living below the poverty line. The government is still trying to reach an agreement with the IMF over Argentina's obligations to the Fund itself.

Real GDP in Venezuela dropped by 9.9% in the second quarter 2002, down from an increase of 2.6% in the second quarter of 2001. Production shrank as a result of devaluation, a cutback in oil production, and a plunge in sales in the aftermath of the failed coup. Consumer and producer confidence remained fragile, a consequence of the uncertainties surrounding the coup in April, undermining sales. Along with the slump in sales, the unemployment rate jumped to 16.2% in June 2002, up from 13.3% in June 2001. The increase in unemployment was remarkable, as the government imposed a freeze on layoffs for the period May to July 2002. Second-quarter oil production was reduced in compliance with the quota imposed by OPEC. In spite of the OPEC quota, the country's output still exceeded its mandatory limit of 2.5 million barrels a day. The Bolivar has depreciated 31% in 2002, after the central bank abandoned the crawling peg regime in February. The Bolivar depreciated, due to capital flight, lack of investment, and weak balance of payments. Inflation jumped to 19.6% in the second quarter of 2002, a result of the devaluation and an increase in the telephone rates.

Government spending rose by 1.5% in the first five months of 2002. The sagging economy curbed tax revenues, which raised the government deficit. A "new economic team" was chosen to formulate a plan to reduce the fiscal deficit and the lack of confidence in the economy. Meanwhile, former U.S. President Jimmy Carter was unsuccessful in gathering President Chavez and the opposition leaders at the negotiation table.

Japan

The world's second-largest economy, Japan, was glum in the second quarter of 2002. Through the months April-June of 2002, Japan's real GDP contracted by 0.6%, reflected by decreases in capital spending (15.5%), residential investment (2.7%), and public investment (2.3%). Deflation and soaring unemployment continued to plague the economy. The trend of continuing price declines cut into profits, lowered home values, and made it harder for banks to eliminate nonperforming loans. Koizumi's government has not been able to reform the financial system, as many

nonperforming loans still have not been written off. The government also is burdened by a growing national debt. As a result, business and consumer confidence remained weak. To lure consumers, many Japanese companies continued to keep their prices low, reducing their corporate profits (16.8%). Consumer prices remained almost unchanged at -0.7% in the June quarter of 2002, forcing many companies to slash their spending on factories and new equipment. With the sagging sales, companies had to cut costs to boost profits by eliminating jobs and lowering wages.

Japan's second quarter jobless rate rose by 0.5 percentage point to 5.4% in 2002. Many large employers spent billions of yens on incentives for workers to quit. The manufacturing industry as well as the construction sector has cut back on employment. The construction companies were the worst hit by Japan's economic downturn. Many companies relied on government contracts to stay in business, but the government lowered spending on public works, causing many companies to go bankrupt. In contrast, some export businesses fared well, as they benefited from higher overseas demand. Japan's current account surplus soared by 90.3% to ¥1,507.2 billion, as Japanese import demand sagged by 5.1%, and exports swelled by 7.1%.

PUBLIC FINANCE

General developments in the public sector

During the second quarter of 2002, the General Government registered a deficit on a cash basis of NAF.46.3 million, compared to NAF.38.2 million in the second quarter of 2001. The significant increase in expenditures of NAF.52.9 million (18.0%) contributed to the widening of the deficit, mitigated by a NAF.44.8 million (17.5%) rise in revenues.

The increase in revenues was attributable to both tax and nontax revenues, while capital revenues and grants declined. Tax revenues increased by NAF.41.8 million (17.4%) with all tax categories, except taxes on property, contributing. Taxes on income and profits and taxes on goods and services increased by NAF.32.3 million (33.3%) and NAF.9.7 million (10.0%), respectively. In addition, taxes on international trade and transactions and other taxes increased by NAF.4.4 million (14.4%) and NAF.1.4 million (116.7%), respectively. These increases were mitigated only by a drop of NAF.6.0 million (44.8%) in taxes on property. Nontax revenues increased by NAF.4.2 million (29.5%). Finally, no capital revenues were registered in the second quarter of 2002, while grants dropped by NAF.1.0 million (66.7%).

The surge in expenditures was attributable to increases in both current expenditures and capital expenditures. All categories contributed to the NAF.47.0 million (16.3%) increase in current expenditures. The largest increases were registered in interest payments and in wages and salaries -- NAF.18.0 million (39.0%) and NAF.10.9 million (11.0%), respectively. Outlays for goods and services increased by NAF.8.8 million (13.2%), subsidies by NAF.8.7 million (62.5%), and transfers by NAF.0.7 million (1.1%).

Table 7
Operations of the General Government (in millions NAF.)

	2001-II	2002-II	Change	
REVENUES	256.0	300.7	44.8	17.5%
Tax revenues	239.9	281.7	41.8	17.4%
Nontax revenues	14.3	18.5	4.2	29.5%
Capital revenues	0.2	0.0	-0.2	-89.3%
Grants	1.5	0.5	-1.0	-66.7%
EXPENDITURES	294.1	347.0	52.9	18.0%
Current expenditures	288.5	335.5	47.0	16.3%
Capital expenditures	5.6	11.5	5.9	105.1%
BALANCE	-38.2	-46.3	-8.1	21.3%
% of GDP	-3.5%	-4.2%		

Operations of the Central Government

The Central Government registered a cash deficit of NAF.4.4 million in the second quarter of 2002, a deterioration of NAF.1.7 million compared to the second quarter of 2001. The deterioration of the cash balance was attributable to the increase of NAF.17.3 million (12.1%) in expenditures, offset partly by a NAF.15.6 million (11.1%) increase in revenues.

Both tax revenues and nontax revenues contributed to the increase in total revenues in the second quarter of 2002. Tax revenues showed the largest increase, NAf.13.3 million (10.5%), compared to the second quarter of 2001. Nontax revenues increased by NAf.3.3 million (28.4%). By contrast, grants fell by NAf.1.0 million (66.7%), while no capital revenues were registered.

To a large extent, the increase in tax revenues can be ascribed to increases of NAf.6.9 million (530.8%) in gambling and other licenses, NAf.4.5 million (14.8%) in import duties, and NAf.2.1 million (7.3%) in excises. A NAf.5.9 million transfer to the government as part of a settlement with the Bureau of Telecommunication and Post of license fees for the year 2001 contributed primarily to the increase in gambling and other licenses. An increase of NAf.1.4 million (116.7%) in stamp taxes contributed further to the upsurge in tax revenues.

Contrarily, turnover tax revenues dropped by NAf.1.1 million (1.8%) attributable to decreases of NAf.0.4 million (0.8%) in Curacao and Bonaire and NAf.0.7 million (5.9%) on the Windward Islands.

Compared to the second quarter of 2001, all nontax revenue categories increased in the second quarter of 2002. Entrepreneurial and property income increased by NAf.2.3 million (34.8%), due to more transfers to the government of license fee collected by the Central Bank (NAf.2.0 million). In addition, proceeds from fees, charges, and sales increased by NAf.0.8 million (16.7%).

Table 8
Operations of the Central Government (in millions NAf.)

	2001-II	2002-II	Change	
REVENUES	140.0	155.6	15.6	11.1%
Tax revenues,	126.9	140.2	13.3	10.5%
of which:				
-Excises	28.7	30.8	2.1	7.3%
-Import duties	30.4	34.9	4.5	14.8%
-Property transfer tax	3.2	3.2	0.0	0.0%
-Turnover tax,	61.4	60.3	-1.1	-1.8%
of which:				
Curacao and Bonaire	49.5	49.1	-0.4	-0.8%
St. Maarten, Saba, & St. Eustatius	11.9	11.2	-0.7	-5.9%
-Gambling licenses and other	1.3	8.2	6.9	530.8%
-Stamp duties	1.2	2.6	1.4	116.7%
Nontax revenues,	11.6	14.9	3.3	28.4%
of which:				
-Entrepreneurial and				
property income	6.6	8.9	2.3	34.8%
-Fees, charges, and sales	4.8	5.6	0.8	16.7%
-Other nontax revenues	0.2	0.4	0.2	100.0%
Capital revenues	0.0	0.0	0.0	-
Grants	1.5	0.5	-1.0	-66.7%
EXPENDITURES	142.7	160.0	17.3	12.1%
Current expenditures,	139.2	152.0	12.8	9.2%
of which:				

-Wages and salaries	53.9	46.6	-7.3	-13.5%
Wages	44.3	46.7	2.4	5.4%
Social security contributions	2.2	2.2	0.0	0.0%
Pension premiums	7.4	-2.3	-9.7	-131.1%
-Goods and services	22.3	24.6	2.3	10.3%
-Interest payments	12.3	19.1	6.8	55.3%
-Subsidies to public corp.	0.0	9.2	9.2	-
-Transfers	50.7	52.5	1.8	3.6%
Other levels of government	37.5	41.3	3.8	10.1%
Households	8.9	7.4	-1.5	-16.9%
Nonprofit institutions and abroad	4.3	3.8	-0.5	-11.6%
Capital expenditures, of which:	3.5	8.0	4.5	128.6%
-Investments	3.5	4.1	0.6	17.1%
-Net lending	0.0	3.9	3.9	-
BALANCE	-2.7	-4.4	-1.7	63.0%

Total expenditures increased by NAF.17.3 million (12.1%) in the second quarter of 2002, compared to the second quarter of 2001. This increase was the result of increases of NAF.12.8 million (9.2%) in current expenditures and NAF.4.5 million (128.6%) in capital expenditures.

The increase in current expenditures was caused, among other things, by NAF.9.2 million in subsidies to public companies and an increase of NAF.6.8 million (55.3%) in interest payments. The subsidies were related to a payment for the layoff of personnel at Air ALM and liquidity support for Winair, both government-owned airlines.

The increase in interest payments can be explained by an increase of NAF.3.6 million in interest paid on government bonds and NAF.2.9 million more interest paid on treasury bills. This development is due to increased interest by investors in government debt paper as a result of the lifting of the ceiling on commercial banks' credit to the government as of March 1, 2002, and the attractive return compared to investments abroad. Furthermore, interest payments to non-residents increased by NAF.0.3 million.

Outlays for goods and services and transfer payments increased by NAF.2.3 million (10.3%) and NAF.1.8 million (3.6%), respectively. The increase in transfers was due to NAF.3.8 million (10.1%) more transfers by the Central Government to the island governments in relation to revenue-sharing agreements, mitigated by NAF.1.5 million (16.9%) less transferred to households due to the phasing-out of severance payments to laid-off personnel, and NAF.0.5 million (11.6%) less paid to nonprofit institutions.

By contrast, outlays for wages and salaries dropped by NAF.7.3 million (13.5%), the result of a NAF.9.7 million drop in pension contributions to the civil servants pension fund APNA. Contrary to the second quarter of 2001, no contributions were made by the Central Government in the second quarter of 2002. The drop in pension contributions was mitigated by a NAF.2.4 million (5.4%) increase in wages, attributable mainly to increases in medical expenses (NAF.1.1 million) and the wage component (NAF.0.9 million).

Table 9**Changes in the outstanding balances of the Central Government (in millions NAf.)**

	2001-II	2002-II
FISCAL BALANCE	-2.7	-4.4
MONETARY FINANCING,	14.2	3.5
of which:		
Central Bank	3.9	-10.1
Commercial banks	9.8	13.3
Coins and notes	0.5	0.3
NONMONETARY FINANCING,	-11.5	0.9
of which:		
Government securities with the public	-8.0	19.5
Other	-3.5	-18.6

Capital expenditures increased by NAf.4.5 million (128.6%), attributable to NAf.0.6 million more investment outlays and the provision of a NAf.4.0 million loan to the island government of Sint Maarten to fund projects to revitalize the economy.

The Central Government financed its cash deficit in the second quarter of 2002 both monetarily and nonmonetarily. The monetary financing was the result of an increase in net claims by the commercial banks (NAf.13.3 million), mainly as a result of the net purchase of government securities. This expansionary impact was mitigated by a monetary contraction at the Central Bank due to the net sale of government securities and an increase in deposits. The government managed to raise additional non-monetary funds as outstanding government securities with the public increased by NAf.19.5 million.

Operations of the Island Government of Curacao

The Island Government of Curacao registered a cash deficit of NAf.41.9 million in the second quarter of 2002, a deterioration of NAf.6.4 million compared to the second quarter of 2001. This development was the result of an increase of NAf.39.8 million (22.3%) in expenditures that exceeded an increase of NAf.33.3 million (23.3%) in revenues.

The surge in expenditures was caused by increases of NAf.38.4 million (21.7%) in current expenditures and NAf.1.4 million (66.4%) in capital expenditures. In current expenditures, wages and salaries increased by NAf.18.2 million (40.2%), caused almost entirely by pension contributions to the civil servants pension fund APNA. Contrary to the second quarter of 2001, when no contributions were made, NAf.16.2 million was disbursed in the second quarter of 2002. Furthermore, the wage component increased by NAf.2.0 million (4.4%).

Interest payments increased by NAf.11.2 million (33.1%) because of the elimination of arrears in annuity payments to APNA. The interest component of these annuities amounted to NAf.9.7 million.

Purchases of goods and services increased by NAf.6.5 million (14.6%) while an increase of NAf.3.0 million (7.7%) occurred in transfers. The increase in transfers can be attributed almost entirely to NAf.7.4 million (40.0%) more transfers to nonprofit institutions and abroad. Transfers to other

levels of government increased marginally by NAf.0.5 million, while transfers to households fell by NAf.4.9 million (28.5%), reflecting the diminishing severance payments to laid-off personnel. Finally, subsidies to public companies fell marginally by NAf.0.5 million (3.8%).

Table 10
Operations of the Island Government of Curacao (in millions NAf.)

	2001-II	2002-II	Change	
REVENUES	143.3	176.6	33.3	23.3%
Tax revenues,	113.0	141.5	28.5	25.2%
of which:				
-Taxes on income and profits,	97.3	129.6	32.3	33.2%
of which:				
Profit tax	22.7	36.5	13.8	60.7%
Income tax	-7.0	-4.7	2.4	-33.5%
Wage tax	81.6	97.8	16.2	19.8%
-Taxes on property,	9.7	4.1	-5.6	-57.7%
of which:				
Land tax	7.1	2.9	-4.1	-58.6%
Occupancy tax	2.7	1.2	-1.5	-55.5%
-Taxes on goods and services,				
of which:	6.0	7.8	1.8	30.5%
Motor vehicle taxes	3.5	6.4	2.9	82.5%
Nontax revenues,	2.7	3.6	0.9	33.8%
of which:				
-Entrepreneurial and property income	0.0	0.2	0.2	-
-Fees, charges, and sales	2.1	2.8	0.7	32.0%
-Other nontax revenues	0.5	0.6	0.1	17.2%
Capital revenues	0.2	0.0	-0.2	-
Grants	27.3	31.5	4.2	15.2%
EXPENDITURES	178.7	218.5	39.8	22.3%
Current expenditures,	176.6	215.0	38.4	21.7%
of which:				
-Wages and salaries	45.2	63.3	18.2	40.2%
Wages	45.2	47.2	2.0	4.4%
Pension premiums	0.0	16.2	16.2	-
-Goods and services	44.4	50.9	6.5	14.6%
-Interest payments	34.0	45.3	11.2	33.1%
-Subsidies to public companies	13.9	13.3	-0.5	-3.8%
-Transfers	39.1	42.1	3.0	7.7%
To other levels of government	3.4	4.0	0.5	15.5%
Households	17.2	12.3	-4.9	-28.5%
Nonprofit institutions	18.5	25.9	7.4	40.0%
Capital expenditures,	2.1	3.5	1.4	66.4%
of which:				
-Investments	2.1	3.5	1.4	66.4%
BALANCE	-35.5	-41.9	-6.4	18.2%

The increase in revenues was the result of increases in tax revenues, grants, and nontax revenues of NAf.28.5 million (25.2%), NAf.4.2 million (15.2%), and NAf.0.9 million (33.8%), respectively. In contrast, capital revenues dropped by NAf.0.2 million.

The surge in tax revenues was caused mainly by an increase of NAf.32.3 million (33.2%) in taxes on income and profits, fueled by increases in the wage tax and the profit tax of NAf.16.2 million (19.8%) and NAf.13.8 million (60.7%), respectively. The increases in the wage tax and the profit tax were due to special actions of the tax authorities to improve compliance. Furthermore, there were fewer net refunds in income taxes (NAf.2.4 million) in the second quarter of 2002 compared to the second quarter of 2001. In addition, the collection of the motor vehicle tax increased by NAf.2.9 million (82.5%). These increases were mitigated by less revenue collected from the land tax and the occupancy tax by NAf.4.1 million (58.6%) and NAf.1.5 million (55.5%), respectively.

The increase in nontax revenues was caused by increases in fees, charges, and sales of NAf.0.7 million (32.0%), in entrepreneurial and property income (NAf.0.1 million), and in other nontax revenues (NAf.0.1 million).

Table 11
Changes in the outstanding balances of the Island Government of Curacao
(in millions NAf.)

	2001-II	2002-II
FISCAL BALANCE	-35.5	-41.9
MONETARY FINANCING,	36.1	-14.8
of which:		
Central Bank	-0.3	-13.2
Commercial banks	36.4	-1.6
NONMONETARY FINANCING,	-0.6	56.7
of which:		
Government securities with the public	-9.4	42.3
Other	8.8	14.4

The Island Government of Curacao financed its cash deficit entirely nonmonetarily in the second quarter of 2002 (see table 11). The funds raised nonmonetarily were attributable mainly to the net purchase of government securities by the public (NAf.42.3 million). In contrast, the monetary contraction through the Central Bank was mainly the result of the net sale of government securities.

The total outstanding debt of the Netherlands Antilles

The total outstanding debt of the Netherlands Antilles increased by NAf.142.5 million (4.2%) during the second quarter of 2002, the result of increases of NAf.74.5 million (2.6%) in the domestic debt and NAf.67.9 million (13.0%) in the foreign debt. The total debt as a percentage of GDP amounted to 79.6% at the end of the second quarter of 2002.

The domestic debt of the Central Government increased by NAf.37.6 million (3.1%) during the second quarter of 2002. This increase was attributable to increases in securities in the hands of the public (NAf.19.5 million) and with the commercial banks (NAf.17.6 million), and higher arrears

with the social security bank SVB (NAf.8.0 million) and the civil servants pension fund APNA (NAf.2.4 million). A drop in securities in the Central Bank's portfolio (NAf.6.0 million), in outstanding debt to other government levels (NAf.0.3 million) and in other debt (NAf.3.7 million) mitigated these increases.

The domestic debt of the Island Government of Curacao increased by NAf.31.1 million (2.0%) in the second quarter of 2002 due mainly to increases in securities with the public and commercial banks of NAf.42.3 million and NAf.4.5 million, respectively. Furthermore, arrears accumulated with SVB (NAf.4.1 million), APNA (NAf.0.7 million), and other creditors (NAf.1.1 million). These increases in debt were mitigated mainly by a net sale of securities by the Central Bank (NAf.20.2 million) and a drop in commercial bank credit (NAf.1.4 million).

The domestic debt of the other island governments (i.e., Bonaire, St. Maarten, St. Eustatius, and Saba) rose by NAf.6.3 million, due to increased arrears with the civil servants pension fund (APNA) and the social security bank (SVB).

Table 12
Total outstanding consolidated public debt¹⁾ (in millions NAf.)

	2002-I	2002-II	Change	
Domestic consolidated debt,	2,865.4	2,939.9	74.5	2.6%
of which:				
-Central Government	1,213.2	1,250.8	37.6	3.1%
-Curacao	1,538.0	1,569.1	31.1	2.0%
-Bonaire	68.1	69.5	1.4	2.1%
-St. Maarten	47.6	52.0	4.4	9.2%
-St. Eustatius	2.6	2.7	0.2	7.1%
-Saba	4.2	4.4	0.2	5.2%
Foreign debt	520.5	588.4	67.9	13.0%
Total debt (consolidated)	3,385.9	3,528.4	142.5	4.2%
(% of GDP)	76.7%	79.6%		

¹⁾ Consolidated for the debts between the Central Government and the island governments.

The foreign debt increased by NAf.67.9 million (13.0%), in line with the appreciation of the Euro, the dominant currency in the official foreign debt, vis-a-vis the Antillean guilder in the second quarter of 2002.

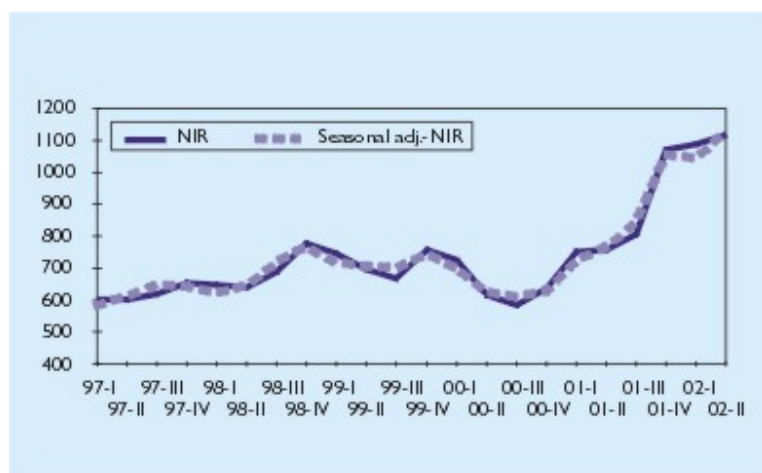
DEVELOPMENTS IN THE EXTERNAL SECTOR

General overview

At the end of the second quarter of 2002, net international reserves reached NAf. 1,116.9 million, an increase of NAf.28.4 million compared to the first quarter (graph 1). This increase resulted from a NAf. 41.6 million increase in international reserves at the Central Bank, which was partly mitigated by a NAf.13.2 decline in international reserves at the commercial banks.

Graph 1

Developments in the net international reserves (in millions NAf.)



In the second quarter of 2002, a decrease of NAf.153.6 million in the current account deficit to NAf.46.3 million was recorded. The improvement in the current account also was reflected in the financial account because the latter records how international transactions are financed. The financial account improved by NAf.143.7 million to NAf.3.8 million as a result of an increase in assets and a decrease in liabilities.

Table 13

Balance of payments summary¹⁾ (in millions NAf.)

	2001-II	2002-II	Diff.
Current account	-199.9	-46.3	153.6
Capital account	9.6	19.1	9.5
Financial account,	147.5	3.8	-143.7
of which:			
-Change in reserves ²⁾	-4.6	-28.4	-23.8
Statistical discrepancies	42.8	23.4	-19.4
Memorandum item			
Change in reserves ²⁾	-4.6	-28.4	-23.8
-with commercial banks	-23.3	13.2	36.5
-with Central Bank	18.7	-41.6	-60.3

1) Transaction basis

2) -Sign denotes an increase in reserves (excluding gold)

The current account

The deficit in the current account of the balance of payments decreased by NAf.153.6 million to NAf.46.3 million in the second quarter of 2002, compared to the same quarter of 2001. As illustrated in table 14, the improvement in the current account was the result of improved trade, current transfers, and services balances by NAf.63.4 million, NAf.57.2 million, and NAf.38.0 million, respectively. In contrast, the income balance deteriorated by NAf.5.0 million.

Table 14
A breakdown of the current account¹⁾ (in millions NAf.)

	2001-II	2002-II	Diff.
Trade balance	-575.8	-512.4	63.4
-Exports	277.0	247.5	-29.5
-Imports	852.8	759.9	-92.9
Services balance	362.7	400.7	38.0
Receipts, of which:	699.8	730.7	30.9
-Travel	324.6	312.8	-11.8
-Transportation	75.9	78.6	2.7
-Other services, of which:	299.3	339.3	40.0
Int. fin. & bus. services sector	131.8	174.2	42.4
Expenses, of which:	337.1	330.0	-7.1
-Travel	118.2	114.4	-3.8
-Transportation	36.1	39.0	2.9
-Other services, of which:	182.8	176.6	-6.2
Int. fin. & bus. services sector	45.2	57.5	12.3
Income balance ²⁾	7.5	2.5	-5.0
Current transfers balance, of which:	5.7	62.9	57.2
Profit taxes	11.0	21.9	10.9
Balance	-199.9	-46.3	153.6

¹⁾ Transaction basis

²⁾ Labor and investment income

The trade balance

The trade balance improved considerably by NAf.63.4 million in the second quarter of 2002, compared to the same quarter of 2001. This improvement was related to a NAf.92.9 million drop in imports, compensated partly by a NAf.29.5 million drop in exports (table 15). General merchandise and oil products were the categories that contributed to the drop in imports. Most of the drop in exports was due to a decline in goods procured in ports, mainly as a result of lower prices of bunker fuel.

A breakdown by island reveals that the trade balance of Curacao improved relatively more than that of Bonaire and the Windward Islands. A closer look reveals that the NAf.55.8 million improvement was generated mostly by a marked decrease in general merchandise imports (NAf.59.5 million). This

decrease was caused by fewer imports for construction projects in the second quarter of 2002, compared to the same quarter in 2001. In 2001, projects such as the upgrading project (IRUP) and the utility plant (BOO) at the oil refinery in Curacao, investments in the utility company Aqualectra, the US Air Force base, the new office building of the Central Bank, and the Kura Hulanda Hotel led to high imports. The decrease in imports was diminished partly by a decline in exports, caused mainly by fewer exports of goods procured in ports.

Table 15
A breakdown of the trade balance¹⁾ (in millions NAf.)

	2001-II		2002-II		Diff.	
	Export	Import	Export	Import	Export	Import
Bonaire	3.6	17.7	4.3	17.2	0.7	-0.5
-General merchandise	3.5	17.0	4.3	13.4	0.8	-3.6
-Oil products -	0.3	-	0.2	-	-	0.1
-Goods for processing	0.1	0.4	-	3.6	-0.1	3.2
-Repair on goods	-	-	-	-	-	-
-Goods procured in ports (bunker)	-	-	-	-	-	-
Curacao	180.6	620.9	169.5	554.0	-11.1	-66.9
-General merchandise,	131.7	528.9	129.7	469.4	-2.0	-59.5
of which: freezone	106.7	161.2	63.1	142.6	-43.6	-18.6
-Oil products	-	68.1	-	62.4	-	-5.7
-Goods for processing	2.9	21.2	2.5	16.6	-0.4	-4.6
-Repair on goods	15.6	-	14.8	2.5	-0.8	2.5
-Goods procured in ports (bunker)	30.4	2.7	22.5	3.1	-7.9	0.4
Windward Islands	92.8	214.2	73.7	188.7	-19.1	-25.5
-General merchandise	23.6	143.2	24.7	136.6	1.1	-6.6
-Oil products	3.4	70.9	4.1	52.1	0.7	-18.8
-Goods for processing	0.1	0.1	-	-	-0.1	-0.1
-Repair on goods	-	-	-	-	-	-
-Goods procured in ports (bunker)	65.7	-	44.9	-	-20.8	-
Netherlands Antilles	277.0	852.8	247.5	759.9	-29.5	-92.9
-General merchandise,	158.8	689.1	158.7	619.4	-0.1	-69.7
of which: freezone	106.7	161.2	63.1	142.6	-43.6	-18.6
-Oil products	3.4	139.3	4.1	114.7	0.7	-24.6
-Goods for processing	3.1	21.7	2.5	20.2	-0.6	-1.5
-Repair on goods	15.6	-	14.8	2.5	-0.8	2.5
-Goods procured in ports (bunker)	96.1	2.7	67.4	3.1	-28.7	0.4

¹⁾ Transaction basis

The trade balance of the Windward Islands improved by NAf. 6.4 million because of declines in oil imports (NAf.18.8 million) due to lower prices, and general merchandise imports (NAf.6.6 million). This development was outweighed partly by the NAf.20.8 million drop in exports of goods procured in ports, the result of lower oil prices and a decrease in oil transshipment activities.

The trade balance of Bonaire improved by NAf.1.2 million. The main developments contributing to this improvement were a NAf.3.6 million drop in general merchandise imports, mitigated by a NAf.3.2 million increase in imports of oil-related goods for processing. In addition, exports of

general merchandise increased by NAf.0.8 million.

The services balance

The surplus on the services balance increased by NAf.38.0 million in the second quarter of 2002 compared to the same quarter of 2001. This increase was due entirely to the developments in other services. The item "other services" developed favorably because of increased earnings from the international financial and business services sector and decreased expenses on construction projects. Earnings from the refining fee declined. Furthermore, the travel balance deteriorated by NAf.8.0 million, while the surplus on the transportation balance decreased only slightly by NAf.0.2 million.

Tourism

Foreign exchange receipts from the tourism sector declined by NAf.11.8 million (3.6%) in the second quarter of 2002 compared to the same quarter of 2001. This decline was caused entirely by the poor performance of the tourism sector on the Windward Islands and Bonaire. As can be seen in table 16, the increases in foreign exchange earnings from stay-over and cruise tourism on Curazao compensated in part for the decline on the Windward Islands and Bonaire. Tourism expenses decreased by NAf.3.8 million.

Table 16
Foreign exchange earnings from tourism per island¹⁾ (in millions NAf.)

	2001-II	2002-II	Diff.	%
Bonaire ²⁾	26.3	25.4	-0.9	-3.4
-Stay-over	25.9	25.0	-0.9	-3.5
-Cruise	0.4	0.4	0.0	0.0
Curazao	78.9	86.4	7.5	9.5
-Stay-over	72.3	79.5	7.2	10.0
-Cruise	6.6	6.9	0.3	4.5
Windward Islands	219.4	201.0	-18.4	-8.4
-Stay-over	176.8	156.2	-20.6	-11.7
-Cruise	42.6	44.8	2.2	5.2
Netherlands Antilles	324.6	312.8	-11.8	-3.6
-Stay-over	275.0	260.7	-14.3	-5.2
-Cruise	49.6	52.1	2.5	5.0

¹⁾ Transaction basis

²⁾ Bonaire's tourism earnings were estimated by the Bank using immigration data because the data on the number of tourists were not available due to the introduction of a new data-processing system.

The tourism sector on the Windward Islands depends heavily on the US market, which was affected by a slowdown of the economy and the aftermath of the September 11 attacks. Consequently, tourism earnings from the United States declined. However, the decrease in foreign exchange receipts from tourism was not only caused by the American market. The European market also generated less foreign exchange for the Windward Islands. The South American market performed especially poorly, reflecting the problems of countries such as Venezuela, Brazil, and Argentina. These developments resulted in a NAf.20.6 million (11.7 %) decrease in stay-over tourism earnings.

In contrast, cruise tourism performed slightly better compared to the second quarter of 2001, reflected by a NAf.2.2 million (5.2%) increase in earnings.

Unlike the Windward Islands, the tourism sector in Curacao performed well in the first quarter of 2002, compared to the same quarter of 2001. The foreign exchange receipts from stay-over tourism increased by 10.0%, reflecting the positive development in all markets, particularly the South-American market. Revenues from cruise tourism increased by 4.5%.

Transportation

Net earnings from the transportation sector decreased by NAf.0.2 million in the second quarter of 2002 compared to the same period of 2001. This decrease was the result of a NAf.2.9 million increase in expenses, which outweighed the NAf.2.7 million increase in earnings. Earnings from passenger air transport increased but were outweighed by the decrease in earnings from the other categories of transportation services.

Other services

Net earnings from other services increased by NAf.46.2 million in the second quarter of 2002 compared to the same quarter of 2001. This increase can be attributed to the improved performance of the international financial and business services sector. Net operational earnings increased by NAf.30.1 million, attributable to a NAf.42.4 million improvement in operational income, which was partly diminished by a NAf.12.3 million increase in operational expenses. Profit taxes paid by the sector to the government⁶ increased by NAf.10.9 million.

Furthermore, the expenses on construction services decreased. This NAf.22.0 million decrease was related to several large construction projects in 2001, which were finished before the second quarter of 2002. A decrease in the refining fee of the oil refinery (NAf.11.8 million), related to lower oil prices, partly diminished the effects of developments in the construction and international financial and business services sectors.

The income balance

The surplus on the income balance decreased by NAf.5.0 million to NAf.2.5 million in the second quarter of 2002 compared to the second quarter of 2001. The main cause of this decline was the increase in interest payments on investments. This was enhanced by a NAf.1.4 million drop in net labor income.

The current transfers balance

The surplus on the current transfers balance improved by NAf.57.2 million to a NAf.62.9 million surplus in the second quarter of 2002 compared to the same period of 2001. This improvement can be ascribed to the marked rise in transfers from abroad, particularly a NAf.67.5 million increase in current transfers by individuals to Antillean residents. This development also was recorded in the fourth quarter of 2001 and the first quarter of 2002. In addition, profit taxes paid by the

⁶ Recorded in the current transfers account

international financial and business services sector to the government increased by NAf.10.9 million. On the other hand, transfers by individuals to nonresidents increased by NAf.21.4 million.

Table 17
Breakdown of the current transfers (in millions NAf.)¹⁾

	2001-I		2002-II		Diff.	
	Debit	Credit	Debit	Credit	Debit	Credit
General	16.3	3.0	28.4	2.0	12.1	-1.0
Government						
-Profit taxes	11.0	0.0	21.9	0.0	10.9	0.0
-Other gov't	5.3	3.0	6.5	2.0	1.2	-1.0
transfers						
Other	62.7	70.3	128.2	91.7	65.5	21.4
sectors						
-Workers'	7.7	6.7	1.1	8.9	-6.6	2.2
remittances						
-Other	55.0	63.6	127.1	82.8	72.1	19.2
transfers,						
of which:						
Family	40.3	30.1	107.8	51.5	67.5	21.4
transfers						
Balance	79.0	73.3	156.6	93.7	77.6	20.4

¹⁾ Transaction basis

The capital and financial account

The combined capital and financial account improved by NAf.134.2 million to NAf.22.9 million in the second quarter of 2002 compared to the second quarter of 2001. This result was due to the NAf.143.7 million improvement in the financial account.

The capital account

The surplus on the capital account increased by NAf.9.5 million to NAf.19.1 million in the second quarter of 2002, compared to the same quarter in 2001. This improvement was related to the increase in funds received for development aid.

The financial account

Compared to the second quarter of 2001, the financial account improved by NAf.143.7 million in the second quarter of 2002. Table 18 indicates that this improvement can be attributed to an increase of NAf.70.2 million in foreign assets, enhanced by a decrease of NAf.73.5 million in foreign liabilities.

The increase in assets was related primarily to more portfolio investments abroad and the rise in reserves assets. Portfolio investments increased due to the net increase in investment in bonds and

debentures abroad by pension funds and investment companies. In addition, other investments abroad also increased.

Foreign liabilities decreased primarily as a result of the decline in trade credit liabilities. Less trade credit was received and more trade credit repaid by companies in the Netherlands Antilles. In addition, fewer loans were received during the second quarter of 2002 compared to the same quarter in 2001. The foreign loans received in the second quarter of 2001 were extended primarily to telecommunication companies.

Table 18
Breakdown of the financial account¹⁾ (net flows, in millions NAf.)

	2001-II	2002-II	Diff.
Direct investment	-22.2	-18.0	4.2
-Abroad ²⁾	0.0	-0.2	0.2
-In the Netherlands Antilles ³⁾	-22.2	-18.2	4.0
Portfolio investment ²⁾	-8.7	-33.9	-25.2
Other investment	183.0	84.1	-98.9
-Assets ²⁾	19.6	-3.5	-23.1
-Liabilities, of which: ³⁾	163.4	87.6	-75.8
Trade credit	92.1	36.6	-55.5
Loans	14.3	-7.1	-21.4
Other	57.0	58.1	1.1
Reserves ⁴⁾	-4.6	-28.4	-23.8
Balance	-147.5	3.8	-143.7
Memorandum items Financial account broken down in:			
-Assets ²⁾	6.2	-64.0	-70.2
-Liabilities ³⁾	141.3	67.8	-73.5

¹⁾ Transaction basis

²⁾ A -sign means an increase in assets

³⁾ A -sign means an decrease in liabilities

⁴⁾ A -sign means an increase in reserve assets

MONETARY DEVELOPMENTS

Introduction

During the second quarter of 2002, the money supply (M2) in the Netherlands Antilles increased by 1.3% (NAf.46.4 million), a deceleration compared to the 1.7% (NAf.52.1 million) increase during the same quarter of 2001. The increase in 2002 was due to increases in both components of the money supply: the money component (M1) and the near-money component, which increased by 1.2% (NAf.17.0 million) and 1.4% (NAf.29.4 million), respectively. In the second quarter of 2001, both components also increased, by 0.9% (NAf.10.4 million) and 2.2% (NAf.41.7 million), respectively.

The increase in the demand for liquid assets during the April-June period of 2002 was due to increases in net domestic assets of 0.7% (NAf.18.0 million) and in net foreign assets of 2.7% (NAf.28.4 million). During the second quarter of 2001, both these components also increased, by 2.0% (NAf.47.4 million) and 0.7% (NAf.4.7 million), respectively. The increase in net domestic assets was due to an increase of 2.1% (NAf.55.9 million) in net domestic credit to the private sector, which offset decreases in net domestic credit to the governments and miscellaneous factors of 4.8% (NAf.10.9 million) and 5.8% (NAf.27.0 million), respectively. The increase in net private credit extension was mainly the result of an increase of 2.7% (NAf.69.2 million) in loans. Of this increase, 4.1% (NAf.75.8 million) was recorded on the Leeward Islands, offsetting the decrease of 1.0% (NAf.6.6 million) recorded on the Windward Islands.

Monetary policy

The increase in net foreign assets continued during the first half of 2002. In addition, net private credit extension grew moderately. The combination of these developments led to a further increase in the liquidity position of the banking sector, triggering a decreasing trend in interest rates. In light of these developments, the Bank decreased its pledging rate ("beleningsrente") by 100 basispoints to 5.75%⁷, as of June 1, 2002. The pledging rate is the interest percentage against which commercial banks can borrow from the Bank under the condition of sufficient collateral.

Money supply

During the second quarter of 2002, the money supply increased by 1.3% (NAf.46.4 million), compared to a 1.7% (NAf.52.1 million) increase during the same quarter of 2001. The increase in 2002 was the result of increases in both the money component and the near-money component by 1.2% (NAf.17.0 million) and 1.4% (NAf.29.4 million), respectively. During the second quarter of 2001, these components showed a corresponding development, increasing by 0.9% (NAf.10.4 million) and 2.2% (NAf.41.7 million), respectively.

⁷ On January 1, 2002, the pledging rate was lowered by 25 basispoints to 6.75%. On July 4 and August 20, the pledging rate was reduced further to 5.00% and 4.00%, respectively

Table 19
Quarterly changes in the components of the money supply (in millions NAf. and percentages)

	2001-II		2002-II	
Coins & notes with the public	5.5	(2.9%)	-3.2	(-1.5%)
Total demand deposits, of which :	4.9	(0.5%)	20.2	(1.8%)
-Netherlands Antillean guilders	22.2	(2.9%)	22.9	(2.5%)
-Foreign currency	-17.3	(-7.9%)	-2.7	(-1.2%)
Money (M1)	10.4	(0.9%)	17.0	(1.2%)
Time deposits	21.8	(3.1%)	-3.8	(-0.5%)
Savings	19.9	(1.7%)	33.2	(2.5%)
Near money	41.7	(2.2%)	29.4	(1.4%)
Money supply (M2)	52.1	(1.7%)	46.4	(1.3%)

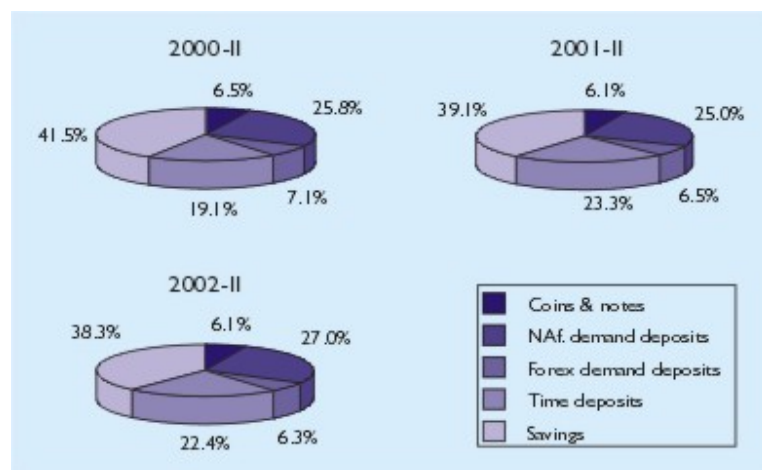
The increase in the money component of the money supply during the April-June period of 2002 was the result of an increase of 1.8% (NAf.20.2 million) in private-sector demand deposits, which offset a decrease of 1.5% (NAf.3.2 million) in coins and notes with the public. During the second quarter of 2001, private sector demand deposits also recorded an increase, although of a smaller magnitude, of 0.5% (NAf.4.9 million). However, coins and notes with the public showed a turnaround compared to the second quarter of 2001, when an increase of 2.9% (NAf.5.5 million) was recorded. The increase in private-sector demand deposits was due to a 2.5% (NAf.22.9 million) increase in demand deposits denominated in local currency, which exceeded the decrease of 1.2% (NAf.2.7 million) in demand deposits denominated in foreign exchange. During the second quarter of 2001, demand deposits denominated in local currency recorded a comparable increase of 2.9% (NAf.22.2 million). However, the decrease in deposits denominated in foreign exchange of 7.9% (NAf.17.3 million) was much larger compared to the second quarter of 2002.

The increase in the near-money component of the money supply during the second quarter of 2002 was the result of an increase of 2.5% (NAf.33.2 million) in savings, offsetting the decrease of 0.5% (NAf.3.8 million) in time deposits. During the second quarter of 2001, both time deposits and savings increased by 3.1% (NAf.21.8 million) and 1.7% (NAf.19.9 million), respectively.

On an annual basis, the increase in the money supply at the end of June 2002 amounted to 12.6% (NAf.394.0 million). This increase was the result of increases in both the money component and the near-money component of 17.5% (NAf.206.7 million) and 9.6% (NAf.187.3 million), respectively. The increase in the money component was the result of increases in coins and notes with the public and demand deposits by 11.3% (NAf.21.8 million) and 18.7% (NAf.184.9 million), respectively. The increase in demand deposits was attributable to increases in both demand deposits denominated in local currency and in foreign exchange of 21.1% (NAf.166.3 million) and 9.2% (NAf.18.6 million), respectively. The increase in the near-money component was due to increases in time deposits and savings of 8.1% (NAf.59.2 million) and 10.5% (NAf.128.1 million), respectively.

Graph 2 shows the shares of the different components of the money supply at the end of the second quarter of 2002, 2001, and 2000. Comparing 2002 with 2001, demand deposits denominated in Netherlands Antillean guilders and time deposits increased at the expense of demand deposits denominated in foreign currency and savings. Coins and notes with the public remained unchanged.

Graph 2
Composition of the money supply (in %)



Factors affecting the demand for liquid assets

During the April-June period of 2002, the total demand for liquid assets increased by 1.3% (NAf.46.4 million), slightly less than the increase of 1.7% (NAf.52.1 million) during the second quarter of 2001. The development in 2002 was due to increases in both net domestic assets and net foreign assets of 0.7% (NAf.18.0 million) and 2.7% (NAf.28.4 million), respectively (table 20).

Table 20
Quarterly changes in the demand for liquid assets by sector (in millions NAf. and percentages)

	2001-II		2002-II	
General government, of which:	60.8	(70.3%)	-10.9	(-4.8%)
-Central government	22.3	(-53.0%)	1.9	(2.3%)
-Island governments	38.5	(29.9%)	-12.8	(-8.7%)
Private sector	8.2	(0.3%)	55.9	(2.1%)
Miscellaneous	-21.6	(5.9%)	-27.0	(5.8%)
Net domestic assets	47.4	(2.0%)	18.0	(0.7%)
Net foreign assets	4.7	(0.7%)	28.4	(2.7%)
Total liquid assets	52.1	(1.7%)	46.4	(1.3%)

The increase in net domestic assets during the second quarter of 2002 was due entirely to an increase of 2.1% (NAf.55.9 million) in net credit extension to the private sector. This increase

exceeded the decrease in net domestic assets of the governments and the decrease due to miscellaneous factors⁸ of 4.8% (NAf.10.9 million) and 5.8% (NAf.27.0 million), respectively. During the same period of 2001, the increase in net credit extension to the private sector amounted to 0.3% (NAf.8.2 million), while net credit extension to the governments reflected a substantial increase of 70.3% (NAf.60.8 million). These increases offset a decrease of 5.9% (NAf.21.6 million) due to miscellaneous factors.

The increase of 2.1% (NAf.55.9 million) in net domestic credit to the private sector was induced mainly by a substantial increase of 2.7% (NAf.69.1 million) in private sector loans. During the second quarter of 2001, net credit extension to the private sector amounted to 0.3% (NAf.8.2 million), primarily the result of a 13.3% (NAf.5.4 million) increase in amounts receivable.

The turnaround in net domestic credit extension to the general government from an increase of 70.3% (NAf.60.8 million) during the April-June period of 2001, to a decrease of 4.8% (NAf.10.9 million) in the same period in 2002, was due to an 8.7% (NAf.12.8 million) decrease in net credit extension to the island governments. This decrease offset the 2.3% (NAf.1.9 million) increase in net credit extension to the central government. During the same quarter of 2001, net credit extension to both the island governments and the central government increased by 29.9% (NAf.38.5 million) and 53.0% (NAf.22.3 million), respectively. The decrease in net credit extension to the island governments during the second quarter of 2002 was mainly the result of the decline in securities of the Island Government of Curacao in the central bank's portfolio because of the sale to the public.

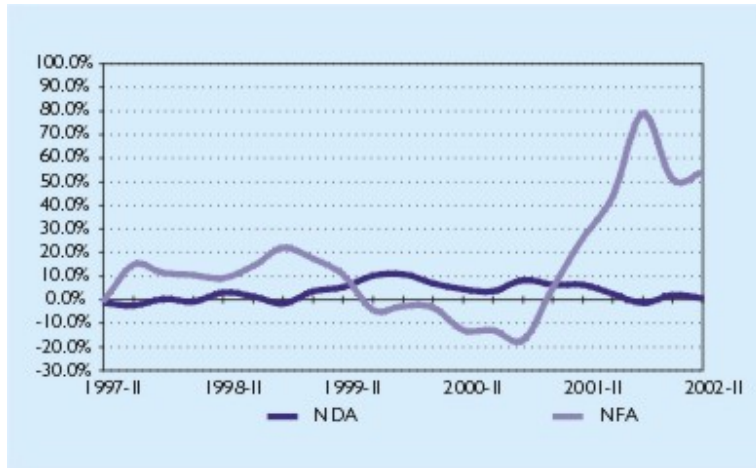
The decrease in net domestic assets due to miscellaneous factors of 5.8% (NAf.27.0 million) during the second quarter of 2002 was due mainly to increased miscellaneous liabilities at commercial banks. During the second quarter of 2001, an identical development was recorded with a decrease of 5.9% (NAf.21.6 million).

Net foreign assets increased by 2.7% (NAf.28.4 million) during the second quarter of 2002, larger than the 0.7% (NAf.4.7 million) increase recorded in the same quarter in 2001. The increase in 2002 was related mainly to increased foreign exchange reserves at the central bank.

On an annual basis, the demand for liquid assets increased by 12.6% (NAf.394.0 million) at the end of June 2002. This increase was due mostly to a substantial increase of 54.1% (NAf.378.1 million) in net foreign assets. NAf.233.3 million (40.5%) of this increase was related to the central bank, while the increase at the commercial banks amounted to NAf.144.8 million (118.7%). The increase in net domestic assets on an annual basis was much smaller, 0.7% (NAf.15.9 million). At the end of June 2001, the increase in net foreign assets on an annual basis amounted to 26.1% (NAf.144.6 million) and the increase in net domestic assets was 6.2% (NAf.143.2 million). These developments are illustrated in graph 3.

⁸ Miscellaneous factors comprise the net balance of the nonfinancial assets (e.g., buildings and inventory) and liabilities (e.g., capital and reserves) of the banking sector.

Graph 3
Developments in net foreign assets and net domestic assets



Domestic credit extension by commercial banks

Domestic credit extension by commercial banks increased by 3.2% (NAf.89.8 million) during the April-June period of 2002, substantially larger than the 0.9% (NAf.24.0 million) increase during the same period of 2001. The increase in the second quarter of 2002 was mainly the result of a 2.7% (NAf.69.1 million) increase in loans to the private sector. All three loan components recorded an increase: mortgages by 2.7% (NAf.28.9 million), consumer loans by 0.1% (NAf.0.9 million), and business loans by 4.3% (NAf.39.4 million). The increase in business loans was related primarily to time loans extended and increased current account overdrafts, the latter of which are generally short-term.

Credit extension to the governments increased by 8.8% (NAf.20.7 million) during the second quarter of 2002, compared to a 12.6% (NAf.29.1 million) increase during the same quarter of 2001. The increase in government credit extension in 2002 was due to increases at the central government and the Island Government of Curacao of 15.5% (NAf.17.6 million) and 2.6% (NAf.3.1 million), respectively. The expansion in credit extension to the governments can be related to both the lifting of the limit on domestic credit to the governments in the Monetary Cash Reserve Arrangement (as per March 1, 2002) and the increased liquidity position of the banking sector.

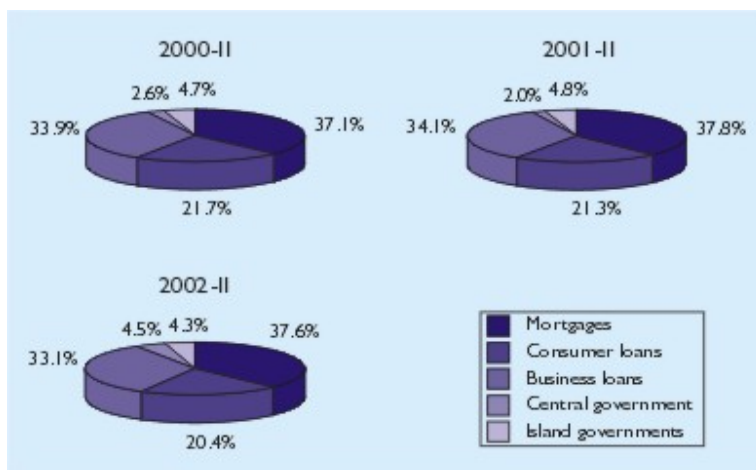
Table 21**Private sector loans and government loans at commercial banks as per end of period (in millions NAf. and percentage changes)**

	2001-II		2002-II	
Private sector loans, of which:	2,600.3	(0.1%)	2,627.7	(2.7%)
-Mortgages	1,054.4	(1.9%)	1,083.8	(2.7%)
-Consumer loans	595.2	(-0.2%)	588.9	(0.1%)
-Business loans	950.8	(-1.6%)	955.1	(4.3%)
Government loans, of which:	188.2	(12.6%)	255.3	(8.8%)
-Central Government	54.7	(24.6%)	131.0	(15.5%)
-Island Government of Curacao	133.5	(8.1%)	124.3	(2.6%)
Total	2,788.5	(0.9%)	2,883.0	(3.2%)

On an annual basis, credit extension by commercial banks increased by 3.4% (NAf.94.5 million) at the end of June 2002, the result of increases in both private sector loans and government loans of 1.1% (NAf.27.4 million) and 35.7% (NAf.67.1 million), respectively. In contrast to the change on a quarterly basis, the government sector recorded the largest increase on an annual basis.

Graph 4 reveals the development in the shares of private and government loans in the commercial banks' lending portfolio. The graph shows that the share of central government loans increased by 2.5 percentage points at the expense of all other loan components. Mortgages declined by 0.2 percentage point, consumer loans by 0.9 percentage point, business loans by 1.0 percentage point and loans to the Island Government of Curacao by 0.5 percentage point.

Graph 4
Developments in commercial banks' lending portfolio



Developments by island group

The developments in private sector lending by island group indicate that the increase during the April-June period of 2002 was due to an increase of 4.1% (NAf.75.8 million) on the Leeward Islands, which offset the decrease of 1.0% (NAf.6.6 million) on the Windward Islands. During the same quarter of 2001, a comparable development took place, when the Leeward Islands experienced an increase of 0.3% (NAf.6.8 million), while the Windward Islands recorded a decrease of 0.6% (NAf.3.9 million).

The increase on the Leeward Islands during the second quarter of 2002 was the result of increases in all loan categories: mortgages, consumer loans and business loans increased by 1.5% (NAf.10.7 million), 4.2% (NAf. 19.5 million), and 6.8% (NAf.45.6 million), respectively. Worth mentioning is the substantial increase in business loans, due mainly to time loans extended to business enterprises and other institutions and increased current account overdrafts of business enterprises. During the second quarter of 2001, all three loan categories also increased but at a much lower rate: mortgages by 0.7% (NAf.5.1 million), consumer loans by 0.3% (NAf.1.3 million), and business loans by 0.1% (NAf.0.4 million).

Table 22

Private sector loans at commercial banks on the Leeward Islands as per end of period (in millions NAf. and percentage changes)

	2001-II		2002-II	
Private sector loans,	1,954.1	(0.3%)	1,944.3	(4.1%)
of which:				
-Mortgages	747.1	(0.7%)	747.2	(1.5%)
-Consumer loans	484.7	(0.3%)	485.0	(4.2%)
-Business loans	722.2	(0.1%)	712.0	(6.8%)

Contrary to the increase on a quarterly basis, private credit extension on the Leeward Islands recorded a decrease of 0.5% (NAf.9.8 million) on an annual basis. This decrease was due entirely to a decrease of 1.4% (NAf.10.2 million) in business loans, which exceeded the slight increases in mortgages and consumer loans of NAf.0.1 million and NAf.0.3 million, respectively.

Table 23

Private sector loans at commercial banks on the Windward Islands as per end of period (in millions NAf. and percentages changes)

	2001-II		2002-II	
Private sector loans,	646.3	(-0.6%)	683.5	(-1.0%)
of which:				
-Mortgages	307.2	(5.1%)	336.6	(5.7%)
-Consumer loans	110.5	(-2.2%)	103.8	(-15.2%)
-Business loans	228.6	(-6.7%)	243.1	(-2.5%)

On the Windward Islands, private credit extension decreased by 1.0% (NAf.6.6 million) in the second quarter of 2002, a development identical with the second quarter of 2001 when a decrease of 0.6% (NAf.3.9 million) was recorded. The decrease during the second quarter of 2002 was the result of decreases in both consumer loans and business loans of 15.2% (NAf.18.6 million) and 2.5%

(NAf.6.2 million), respectively. These decreases offset the 5.7% (NAf.18.2 million) increase in mortgages. The explanation of the decrease during the second quarter of 2001 was similar: consumer loans and business loans decreased by 2.2% (NAf.2.5 million) and 6.7% (NAf.16.3 million), respectively, while mortgages increased by 5.1% (NAf.14.9 million).

Contrary to the decrease on a quarterly basis, private sector credit on the Windward Islands increased by 5.8% (NAf.37.2 million) on an annual basis. This increase was the result of increases in mortgages and business loans of 9.6% (NAf.29.4 million) and 6.3% (NAf.14.5 million), respectively. These increases offset a 6.0% (NAf.6.7 million) decrease in consumer loans.

Developments in domestic interest rates

In table 24 an overview is presented of the various interest rates in the Netherlands Antilles at the end of June 2001 and June 2002. The Central Bank's pledging rate decreased by 125 basis points to bring it more in line with the declining interest rates in the money and capital market. This development is related to the overliquidity in the banking sector and the low interest rates in the United States. The marginal lending rate⁹ decreased by 50 basis points. The latter decrease is related to the decrease in the pledging rate, since the marginal lending rate is equal to the pledging rate plus 100 basis points, as per January 1, 2002.

Table 24
Developments in domestic interest rates

	2001-II	2002-II
Central Bank		
-Pledging rate	7.00%	5.75%
-Marginal lending rate	7.25%	6.75%
Commercial banks' borrowing rates		
-Passbook savings	3.7%	3.6%
-12-month time deposit	4.9%	6.4%
Commercial banks' lending rates		
-Mortgages	10.0%	9.8%
-Current account overdraft	10.3%	10.1%
Government bonds		
5 yr., effective yield	9.0%	8.7%

Commercial banks' average interest rate on passbook savings decreased slightly by 0.1 percentage point to 3.6% in the second quarter of 2002 compared to the second quarter of 2001. The average interest rate on time deposits increased markedly by 1.5 percentage points.

Commercial banks' lending rates decreased slightly. The average interest rate on mortgages and current account overdrafts both decreased by 0.2 percentage point, attributable to the overliquidity in the banking sector.

Finally, the average yield on domestic government bonds decreased by 0.3 percentage point. This decrease is partly the result of the introduction of auctions of government treasury paper through

⁹ Charged on Central Bank borrowing exceeding NAf. 20 million

variable rate tenders, which improved the functioning of market forces. The introduction of these auctions was part of the monetary policy changes as per January 1, 2002. The downward trend in bond yields can be attributed further to the excess liquidity in the banking sector, the lifting of the ceiling on commercial banks' domestic credit extension to the government as of March 1, 2002, and the low interest rates in the United States.

DEVELOPMENTS IN THE FINANCIAL SECTOR

Introduction

In the second quarter of 2002, the Bank examined three commercial banks operating domestically and two money remitters. Furthermore, the Bank licensed a credit union established in St. Maarten named Christian Kingdom Cooperative and revoked the licenses of Banque Artesia Curacao N.V. and Banco de Venezuela N.V. to operate as international credit institutions in the Netherlands Antilles.

Developments in the domestic banking sector

Following the NAf.206.0 million (3.5%) contraction in total assets of the domestic banking sector of the Netherlands Antilles during the first quarter of 2002, total assets increased by NAf.122.6 million (2.1%) to NAf.5,890.2 million during the second quarter of 2002.

Interest-bearing cash grew by NAf.20.0 million (1.4%) to NAf.1,476.3 million as a result of the increase of NAf.43.4 million in interbank funds held at foreign banks and an increase of NAf.45.3 million in time deposits held at the Bank van de Nederlandse Antillen. However, time deposits held at foreign banks decreased by NAf.105.0 million, reducing the overall increase in interest-bearing cash.

The increase of NAf.81.7 million (2.5%) in the loan portfolio of the banks operating domestically also contributed to the increase in total assets. This increase was manifested first in the growth in time loans granted to both resident (NAf.30.3 million) and nonresident business enterprises (NAf.18.5 million). Second, time loans granted to local individuals and mortgages granted to local business enterprises increased by NAf.17.7 million and NAf.21.3 million, respectively.

On the liabilities side, total deposits increased by NAf.70.9 million (1.5%) to NAf.4,894.8 million. This increase resulted from a growth in demand deposits placed by local individuals (NAf.23.8 million), local business enterprises (NAf.13.1 million), foreign unconsolidated subsidiaries and affiliates (NAf.5.5 million), and other local banks (NAf.9.1 million). Savings deposits also contributed to the increase, growing by NAf.32.1 million (1.6%). This growth was reflected in the increase in savings deposits and time deposits held by local individuals of NAf.18.1 million and NAf.14.0 million, respectively.

In addition, borrowings by foreign unconsolidated subsidiaries and affiliates increased by NAf.32.7 million, while borrowings by all other foreign banks decreased by NAf.22.0 million. Other liabilities also increased due mainly to increases in the accounts "items in suspense" by NAf.12.1 million, "tax payable" by NAf.8.7 million, and "all other liabilities" by NAf.6.6 million.

Table 25
Aggregate balance sheet of commercial banks operating in the domestic banking sector of the Netherlands Antilles at quarter-end (in millions NAf.)

	2001-IV		2002- I		2002-II	
	NAf.	%	NAf.	%	NAf.	%
ASSETS						
Non-int.-bearing cash	457.4	7.7	328.8	5.7	329.7	5.6
Interest-bearing cash	1,494.9	25.0	1,456.3	25.2	1,476.3	25.1
Investments	261.9	4.4	334.9	5.8	344.1	5.8
Loans	3,417.8	57.2	3,310.9	57.4	3,392.6	57.6
Investm. unconsol. sub.	19.5	0.3	12.9	0.3	15.6	0.3
Fixed assets	162.7	2.7	163.8	2.8	171.4	2.9
Other assets	159.4	2.7	160.0	2.8	160.5	2.7
Total assets	5,973.6	100.0	5,767.6	100.0	5,890.2	100.0
LIABILITIES						
Demand deposits	1,606.9	26.9	1,597.4	27.7	1,646.2	27.9
Savings deposits	2,176.7	36.4	2,045.1	35.5	2,077.2	35.3
Time deposits	1,276.5	21.4	1,181.4	20.5	1,171.4	19.9
Total deposits	5,060.1	84.7	4,823.9	83.7	4,894.8	83.1
Borrowings	158.8	2.7	195.4	3.4	210.0	3.6
Other liabilities	266.3	4.5	258.7	4.5	288.7	4.9
Total liabilities	5,485.2	91.9	5,278.0	91.6	5,393.5	91.6
Minority interest	5.3	0.1	5.5	0.1	5.7	0.1
Subordinated debentures	6.2	0.1	6.4	0.1	7.7	0.1
General provisions	134.3	2.2	140.2	2.3	147.9	2.5
Capital & reserves	342.6	5.7	337.5	5.9	335.4	5.7
Total capital	488.4	8.1	489.6	8.4	496.7	8.4
Total liabilities and capital	5,973.6	100.0	5,767.6	100.0	5,890.2	100.0

Following the strengthening of the capitalization of the domestic banking sector by NAf.1.2 million in the first quarter of 2002, it improved further by NAf.7.0 million to NAf.496.7 million in the second quarter of 2002. However, compared to the end of the first quarter of 2002, the capital-to-assets ratio of the domestic banking sector of the Netherlands Antilles remained at 8.4%, above the international minimum capital standard of 8%.

The banks operating in the domestic banking sector of the Netherlands Antilles recorded a net operating income of NAf.34.4 million over the first half of 2002, a decrease of NAf.17.8 million (34.1%) compared to the net operating income of NAf.52.2 million recorded over the first half of 2001. Net interest income declined by NAf.7.8 million (5.5%) to NAf.134.9 million, while total operational expenses increased by NAf.16.5 million (10.7%). The latter was due primarily to increases in salaries and other employee expenses of NAf.8.3 million (9.6%) and other operating

expenses of NAf.5.4 million (16.9%).

Table 26
Aggregate income statement of commercial banks operating in the domestic banking sector of the Netherlands Antilles at quarter-end (in millions NAf.)

	2001-II	2002-II
Interest income	233.3	221.6
Interest expenses	(90.7)	(86.8)
Net interest income	142.6	34.8
Other income	64.1	70.6
Total operational income	206.7	205.4
Salaries & other employee expenses	(86.2)	(94.5)
Occupancy expenses	(24.5)	(26.7)
Other operating expenses	(31.9)	(37.3)
Net addition to general provisions	(11.9)	(12.5)
Total operational expenses	(154.5)	(171.0)
Net operating income	52.2	34.4
Net extraordinary items	0.3	0.8
Applicable profit taxes	(12.3)	(11.5)
Net income after taxes	40.2	23.7

The micro prudential indicators in table 27 provide a further indication of the performance of the commercial banks operating in the domestic banking sector of the Netherlands Antilles.

The indicators on the adequacy of the capitalization of the domestic banking sector reflect a total capital-to-total assets ratio of 8.5% and tier-1 capital-to-total assets ratio of 5.8% at the end of the second quarter of 2002, above international capital standards. Those standards require a total capital-to-risk-weighted assets ratio of at least 8% and a minimum tier-1 capital-to-risk-weighted assets ratio of 4%. The aforementioned ratios dropped slightly compared to the end of the first quarter of 2002, in line with the slight decrease in the capitalization of the domestic banking sector during the second quarter of 2002. Total capital is defined as the sum of equity capital, general provisions, and subordinated debentures qualifying as secondary capital.

The ratios reflecting the nonperformance of the loan portfolio of the domestic banks indicate that the overall quality of the loan portfolio at the end of the second quarter of 2002 changed little compared to the previous quarter. However, compared to the fourth quarter of 2001, especially the nonperforming loans-to-total capital ratio deteriorated as a consequence of an increase in nonperforming loans during the first two quarters of 2002. Compared to the fourth quarter of 2001, provisions for loan losses as a percentage of nonperforming loans declined during the first two quarters of 2002, indicating that the build-up of necessary provisions lagged behind their

nonperforming loans portfolio.

Table 27
Microprudential indicators of commercial banks operating in the domestic banking sector of the Netherlands Antilles at quarter-end

	2001-IV	2002-I	2002-II
	%	%	%
CAPITAL ADEQUACY			
Total capital/total assets	8.2	8.6	8.5
Tier 1 capital/total assets	5.8	6.0	5.8
Tier 2 capital/total assets	2.3	2.5	2.6
Tier 3 capital/total assets	0.1	0.1	0.1
ASSET QUALITY			
Nonperforming loans/total loans	6.0	7.1	7.1
Nonperforming loans/total capital	43.4	48.4	47.6
Provisions for loan losses/ nonperforming loans	60.8	56.6	57.7
EARNINGS¹⁾			
Gross earning assets yield	8.5	8.5	8.4
Break-even yield	3.0	3.2	3.3
Net interest margin	5.1	5.3	5.1
Return on assets	0.7	1.3	1.2
LIQUIDITY			
Total loans/total deposits	68.7	69.5	70.3
Liquidity surplus (in millions NAf.)	85.5	69.3	82.7

¹⁾These ratios are annualized.

The annualized earnings ratios indicate that the domestic banking sector will realize an acceptable return on assets of 1.2% during the year 2002.

The liquidity ratios indicate that at the end of the second quarter of 2002, the Netherlands Antilles banking sector was sufficiently liquid to meet its short-term obligations and to invest in earning assets.

Developments in the international banking sector

Total assets of the international banking sector increased by NAf.571.4 million (0.8%) to NAf.68.8 billion in the second quarter of 2002. Investments and loans increased by NAf.248.4 million (3.2%) and NAf.877.5 million (2.2%), respectively, whereas cash & banks decreased by NAf.747.3 million (6.2%).

On the liabilities side, savings and time deposits increased by NAf.498.5 million (4.3%) and borrowed funds increased by NAf.1,709.3 (4.1%). In contrast, demand deposits decreased by NAf.1,086.0 (17.7%) and other liabilities by NAf.516.2 million (31.9%).

Table 28
Aggregate balance sheet of commercial banks operating in the international banking sector of the Netherlands Antilles at quarter-end (in millions NAf.)

	2002-I		2002-II	
	NAf.	%	NAf.	%
ASSETS				
Cash & banks	12,139.5	17.8	11,392.2	16.6
Investments	7,736.3	11.4	7,984.7	11.6
Loans	39,501.4	58.0	40,378.9	58.7
Fixed & other assets	8,816.0	12.8	9,008.9	13.1
Total assets	68,193.2	100.0	68,764.6	100.0
LIABILITIES				
Demand deposits	6,145.2	9.0	5,059.2	7.4
Savings & time deposits	11,699.4	17.2	12,197.9	17.7
Borrowed funds	41,856.9	61.3	43,566.2	63.4
Other liabilities	1,618.6	2.4	1,102.4	1.6
Total liabilities	61,320.1	89.9	61,925.7	90.1
Capital	6,873.1	10.1	6,838.9	9.9
Total liabilities & capital	68,193.2	100.0	68,764.6	100.0

The total capital-to-total assets ratio of the international banking sector decreased marginally from 10.1% at the end of the first quarter of 2002 to 9.9% at the end of the second quarter.

The banks operating in the international banking sector of the Netherlands Antilles recorded a net operating income of NAf.18.8 million over the first half of 2002, considerably lower compared to the net operating income of NAf.276.2 million recorded over the first half of 2001. Net additions to general provisions doubled in the first half of 2002 compared to the first half of 2001. Furthermore, net extraordinary losses of NAf.42.6 million combined with the poor operational performance of NAf.18.8 million resulted in a net loss of NAf.32.4 million over the first half of 2002 compared to the net profit of NAf.272.3 million recorded over the first half of 2001.

Table 29
Aggregate income statement of commercial banks operating
in the international banking sector of the Netherlands
Antilles at quarter-end (in millions NAf.)

	2001-II	2002-II
	NAf.	NAf.
Interest income	1,465.3	1,059.9
Interest expenses	(1,459.9)	(1,028.4)
Net interest income	5.4	31.5
Other income	<u>541.3</u>	<u>403.3</u>
Total operational income	546.7	434.8
Salaries & other employee expenses	(46.6)	(49.5)
Occupancy expenses	(7.7)	(18.1)
Other operating expenses	(80.0)	(76.3)
Net addition to general provisions	(136.2)	(272.1)
Total operational expenses	(270.5)	(416.0)
Net operating income	276.2	18.8
Net extraordinary items	5.2	(42.6)
Applicable profit taxes	(9.1)	(8.6)
Net income after taxes	272.3	(32.4)