

The Netherlands Antilles after six years of adjustments efforts with the IMF: A critical evaluation

*Speech by Dr. E.D. Tromp at the Annual Gala Diner of DHL.
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In 1995 the Minister of Finance of the Netherlands Antilles obtained a commitment from the Netherlands for budgetary assistance in the context of an IMF- supported program. That commitment was widely credited as the beginning of a new era or a breakthrough in Dutch – Antillean relations. It created a much-needed platform from which to negotiate objectively.

With this commitment, the Netherlands Antilles embarked on an adjustment program designed to restore confidence in the government and, hence, obtain the necessary financing for the budget. The adjustment strategy entailed a three-pronged approach:

1. financial soundness;
2. structural reform / sustainable economic growth, and
3. social policy.

After six years of adjustment efforts based on this commitment, what is the truly enduring lesson we have learned? Though it may be too early to provide a definitive answer, it is certainly not too early to ask the question.

During the past five years, we have made considerable progress in restructuring the public finances and implementing structural reform. The government bureaucracy has been reduced, wage costs have been brought under control, and the civil servants pension scheme has been partially reformed. These measures have reduced personnel costs substantially.

Expenditures have been reduced further by health care reforms and the improvement of cost efficiency in the government apparatus. Finally, the government has begun regularizing arrears and intergovernmental claims.

On the revenue side, a shift from direct to indirect taxes was initiated with the introduction of the turnover tax, the base of which has been broadened gradually. Tax assessment and collection have been improved, while arrears have been reduced. Furthermore, user fees for government services are applied more broadly. In addition, public sector financial administration and reporting has been enhanced.

In the field of structural reform, various measures have been implemented to foster competition and to create a business climate conducive to more investments. Labor legislation has been modernized, and the product market is being made much more competitive. Progress also has been made in the capital market: disclosures have improved, and the level of the rate of interest has declined. The privatization process also has started. All of this has been done with the objective of improving our business climate and, hence, restoring economic growth.

The second prong of the structural adjustment process, the development and implementation of a long-term investment program, is being undertaken in close cooperation with the World Bank. During a workshop a few months ago, the various islands presented their medium-term development plans, which will be consolidated into a long-term growth strategy for the Netherlands Antilles.

The above discussion serves to illustrate that a broad-based and unprecedented adjustment process has been set in motion. Unfortunately, ladies and gentlemen, I have to note that despite the progress achieved so far in the budgetary field, no financial assistance has been secured to make progress in the two other areas. As you may recall, the government of the Netherlands Antilles embarked on the adjustment process with the firm commitment that a substantial amount of financing would be forthcoming to finance the budget and revitalize the declining social-economic situation to cushion the adjustment costs.

Unfortunately this commitment so far has been limited to financing the first prong of the program. A full and complete honoring of this commitment would have guaranteed the implementation of the other two areas of this adjustment program.

Ladies and gentlemen, a careful analysis indicates that this partial fulfillment of the commitment is largely because both the Netherlands and the Netherlands Antilles act as interlocutors in the negotiations with the IMF, leading at times to confusion and indecision. The following examples are illustrative of this point.

- In a letter dated February 23, 2001, the IMF stated: "While budgetary and financial discipline is essential to build confidence it is not likely by itself to be sufficient to generate an economic recovery. Rapid and unwavering progress in other areas is equally needed and feasible. These include ... initiating public investment projects with Dutch financial assistance, ..."
- This recommendation was further elaborated on during the IMF's visit to the Netherlands Antilles in March. The IMF stated that: "to stimulate the economy, especially on the island of Curacao, it would be useful to implement a few well-targeted investment projects to create up to five hundred jobs during the second half of the year. For efficiency, these projects should be handled outside the existing administrative procedures and medium term investment programs. A small private sector-led foundation could be established to implement the projects. They should be selected to twin with existing private sector projects and to help boost the export potential of the economy." Despite this recommendation, the foundation has not been established nor has Dutch financial assistance been forthcoming.
- The World Bank in its preliminary report identified a number of projects that could be earmarked as projects to jump-start the economy and, hence, should qualify for official assistance. This proposal has not been implemented either.
- In a recent seminar organized in Curacao, the World Bank began a process to come up with recommendations for channeling Dutch development funds. The Dutch government is funding this process. In the meantime, however, another track is being followed. The Dutch government has called for a committee to advise the government about the setting up and channeling of development funds in the wake of the growth strategy being devised by the World Bank. It is not difficult to imagine the political consequences of this proposal. Therefore, it is recommended that this matter be revisited to determine which track should be followed.
- Ladies and gentlemen, the KABNA nostalgia dies slowly, and it certainly lingers in the principal ministries of Dutch power, notably in the BZK.

The question now is whether we should continue with this IMF- supported program in light of this less-than-full compliance by the Netherlands; or whether the preoccupation with the election campaign on both sides of the Atlantic will, in fact, dilute the political cohesion that made the commitment of budgetary support possible.

Continuation with the Fund-supported program is desirable and even inevitable. If we are to regain the confidence of the investors, then the IMF seal of approval is indispensable. But the terms under which we will continue will determine the success of our adjustment efforts. Our sudden epiphany may make us no longer wish to separate Holland from the IMF/WB axis, nor construct a partnership with IMF/WB to gain Holland finances, nor create a union with Holland to gain the IMF seal of approval for our program—all of which we have been actively pursuing.

If we are to continue on this adjustment path, the enduring lesson is that the objectives of the adjustment process remain clear. All parties must conduct themselves in keeping with the objectives of the program, even under difficult circumstances. Restructuring of the pension scheme is necessary, yet it should not be done at the expense of legal security of civil servants. The ALM problem has to be addressed to avoid undesirable consequences for the budget. Yet it should not be used to pursue other noneconomic objectives.

The way the different islands are being played out against each other is not conducive to a harmonious environment to discuss future constitutional arrangements. The public health care system and educational system need change - yet they should not be used as pressure to gain adjustments in other fields of the budget.

Are there any relevant lessons to be drawn here? For example, the recent initiative to create a committee to come up with suggestions for channeling Dutch development funds runs the risk of "fuzzifying" procedurally what needs to remain clear. The World Bank under the coordinating leadership of the Antillean Minister of Economic Affairs has already initiated a process for coming up with suggestions for channeling Dutch development funds. Yet the recently announced Dutch proposal calls for the creation of a committee in which Holland and an Antillean counterpart will deliberate regarding possible arrangements. Unlike the already existing consultative approach taken by the Minister of Economic Affairs under the auspices of the World Bank, the Dutch proposal does not allow for this participatory approach.

Ladies and gentlemen, the truly important lesson is much more prosaic. The IMF approach is an "all or nothing approach." It does not reward partial success. The necessary financing is obtained only after establishing the basis for an agreement with the Fund. The actual disbursement of the funds is based on progress in the implementation of the program. No impartial third party resolves differences between the adjusting country and the Fund. We have to move forward with an iron triad of Holland, IMF, and the Antilles. We cannot and should not split ourselves into blocs with competing objectives in which traditional differences could be exploited.

Engaging the IMF has to be pursued by the Netherlands Antilles and Holland on the basis of a long-term strategy to restore economic growth in the Netherlands Antilles, not for the sake of quick tactical benefits.

Looking ahead, the adjustment process will be constrained by our economic growth. Because of the various speeds that the different areas have been dealt with, a certain degree of adjustment fatigue has beset the nation. To continue making progress in the budgetary field, for example, we must address the burden being placed on the economy by our national debt. We also have to move forward with our growth strategy to lay the foundation for sustainable growth and, hence, create jobs. And finally, the social dimension of this program must be put at the forefront of the national agenda.

I, therefore, would like to propose the following adjustment strategy. The current debt-to-GDP ratio of the Netherlands Antilles is approximately 75%, which represents an annual interest expenditure of almost Naf. 230 million. This debt service is the result of past policy mistakes. In its 1986 report on the Netherlands Antilles, the World Bank stated that because of the large Antillean investment abroad, namely, in the United States, in the amount of Naf. 3.2 billion, the government of the Netherlands Antilles should finance its deficit domestically to encourage the repatriation of those funds. The Netherlands, following this advice, conditioned budgetary assistance to the Netherlands Antilles on the issuance of domestic government bonds. This was the beginning of the domestic debt explosion, the consequences of which are now placing an undue burden on the adjustment process.

Therefore, I call for a refinancing of the outstanding domestic debt at concessionary terms, that is, the terms under which current development funds are being extended to the Netherlands Antilles. To avoid this refinancing being used to encourage the misallocation of budgetary funds, it has to be coupled with a legal requirement that the budget of the general government be balanced. Thus the current discussion of extending the possibilities of capital market access to the other islands should be discontinued. The additional room created by the reduction in interest expense should be earmarked to improve the productive capacity of our economy and pursue the above-mentioned social policy. Since restoration in economic growth will imply budget surpluses, and hence, reduction of the domestic debt, the Dutch financial commitment to the Netherlands Antilles will decline over time. The Netherlands Antilles should use the surplus to create a revolving fund, hence reducing its reliance on Dutch development assistance. This plan is consistent with the stated Dutch policy of self-reliance.

Ladies and gentlemen, I recently made a proposal counter to the proposal I am making right now. This development in my thinking has been triggered by the recurrent annual discussion of the underutilization of the available funds at the end of the year and the never-ending discussion of future re-orientation of Dutch development aid assistance. With this proposal, the consequent political friction will be relegated to a historical footnote. This proposal will lead to a much more mature discussion among the various partners of the Kingdom, promote local institution building, and a sense of ownership.

As I have stated already, both the European and Caribbean part of the Kingdom are at the moment preoccupied with the election campaign. As a consequence, this proposal may be ill-timed. But I think that by putting it forward now, it may serve as a useful guide to determine the agenda for future discussions between the two partners of the Kingdom after the elections.

In concluding, ladies and gentlemen, what can be said of six years of adjustment efforts without a viable IMF program or the generous budgetary assistance of the Dutch? Does this mean that not enough has been done? The answer is clearly negative as illustrated above. The next logical question then is whether we should continue to work toward achieving a Fund-supported program. And again, ladies and gentlemen, I think I made it abundantly clear that if we want to enhance our attractiveness for investors, then an IMF program is necessary. However, these efforts to reach an agreement with the Fund should be guided by the following:

1. The program should not be too ambitious. An adjustment program cannot and should not be too long either in its preparation or in its implementation. Too much will then be demanded of a nation. Results, however limited, should be quickly visible to maintain broad social support.
2. A further postponement of the budgetary assistance from the Netherlands will erode the credibility of the Antillean leaders, Holland, and the International Monetary Fund. To be effective, our leaders have to remain credible. Lack of credibility leads to lack of confidence in the resumption of economic growth of the country in the foreseeable future. People are willing to make sacrifices, but not for six years as evidenced by the growing migration. This migration, or should I say brain-drain, will make the necessary adjustment much more difficult to realize and is detrimental to the development potential of the country. Migration disrupts society and will lead to an accelerated erosion of our most important assets: confidence and the human capital.

3. And finally, ladies and gentlemen, the objectives of the much-needed adjustment program should remain clear. Economic arguments should not be used to achieve political objectives or vice versa.

I thank you for your attention and wish you a Merry Christmas and a Happy New Year.