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Kingdom of the Netherlands—Netherlands Antilles: 2001 Article IV Consultation Discussions—Staff Report; Public Information Notice on the Executive Board Discussion

Under Article IV of the IMF's Articles of Agreement, the IMF holds bilateral discussions with members, usually every year. In the context of the 2001 Article IV consultation with Kingdom of the Netherlands—Netherlands Antilles, the following documents have been released and are included in this package:

- the staff report for the 2001 Article IV consultation discussions, prepared by a staff team of the IMF, following discussions that ended on **March 12, 2001** with the officials of Kingdom of the Netherlands—Netherlands Antilles on economic developments and policies. **Based on information available at the time of these discussions, the staff report was completed on April 18, 2001.** The views expressed in the staff report are those of the staff team and do not necessarily reflect the views of the Executive Board of the IMF.
- a Public Information Notice (PIN), which summarizes the **views of the Executive Board as expressed during its May 7, 2001 discussion** of the staff report that concluded the Article IV consultation discussions.

The document listed below will be separately released:

- Kingdom of the Netherlands—Netherlands Antilles - Recent Developments, Selected Issues, and Statistical Appendix.

The policy of publication of staff reports and other documents by the IMF allows for the deletion of market-sensitive information.

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KINGDOM OF THE NETHERLANDS—NETHERLANDS ANTILLES

Staff Report for the 2001 Article IV Consultation Discussions

Prepared by the Staff Representatives for the 2001 Consultation
with the Kingdom of the Netherlands—Netherlands Antilles

Approved by Alessandro Leipold and Martin Fetherston

April 18, 2001

- The Article IV consultation discussions took place in Willemstad during February 28 – March 12. The mission comprised Messrs. Everaert (head), Bell, and Martijn (all EU1).

- The mission met with the Prime Minister, the President of the Central Bank, the Governor for the Kingdom of the Netherlands, the Deputy Prime Minister, the Ministers of Finance and Interior, Labor and Social Affairs, the State Secretary for Privatization, the Commissioners of Finance, Health, and Economic Affairs of the Island Government of Curaçao, and senior officials of the central bank, the administrations of the Central Government and Island Government of Curaçao, the civil servants' pension fund, the public health insurance institutions, the Privatization Foundation, and the statistics office. The mission also met with representatives of banks, institutional investors, labor unions, the private employers' federation, the tourism association, and the international financial sector.

- The acceptance of obligations of Article VIII, Sections, 2, 3, and 4, by the Kingdom of the Netherlands also applies to the Netherlands Antilles.

Contents

Executive Summary

Background: The past decade has witnessed a progressive weakening of the Antillean economy. Inadequate adjustment to declining offshore and oil refining inflows and high incidence of hurricanes in recent years have led to a prolonged recession, high unemployment, a tide of emigration, and a weakening of the financial system. The peg to the U.S. dollar has kept inflation low, but external competitiveness has suffered, and sizeable official capital inflows have become indispensable to support the budget and the balance of payments. Free labor mobility to the Netherlands limits effective use of wages and the exchange rate to facilitate adjustment. In late 1999, a renewed adjustment effort was initiated, centered on a drastic downsizing of the civil service and supported by significant structural reforms. As with past episodes, success has so far remained elusive, mainly because of lack of perseverance in implementing reforms. Budget deficits have continued to exceed available financing, and the pace of expenditure reduction and accrual of benefits from liberalizing trade and removing labor market rigidities have slowed.

Short-term policy issues: Halting the economic decline and restoring the prospects for job creation and growth are immediate policy concerns. There was broad agreement between the staff and the authorities that this would require imparting a renewed impetus to implementing a comprehensive adjustment program, comprising mutually reinforcing structural reforms, public investments, and sound budgetary policies. The authorities, while emphasizing that further fiscal adjustment would be contractionary, accepted that the budget deficit should not be allowed to rise above last year's level. To contain the deficit, they would seek to strengthen tax administration, curtail spending on goods and services, and reform health care. The staff noted that, since budget deficits would need to be financed by the Netherlands in the near term, it would be essential to provide such financing in line with progress in implementing the adjustment program to ensure proper balance between adjustment and financing. The staff also stressed the importance of reinvigorating structural reforms to restore confidence and attract investors. The staff agreed that monetary policy should continue to support the exchange rate peg and that supervision would need to be in a heightened state of alert to safeguard the soundness of the financial system.

Medium-term policy issues: Fiscal policy can support growth over the medium term in several ways. Achieving budget balance—as is the authorities' objective—would be beneficial, given the limited domestic financing capacity and population ageing. A comprehensive reform to simplify the tax system and tax cuts could improve the investment climate and resource allocation. To meet these objectives, it will be essential to expand expenditure savings associated with the ongoing downsizing of the government, contain quasi-fiscal risks, establish budget discipline in the broader public sector, and implement further pension and health care reforms. Steadfast progress in structural reforms will be important to boost the economy's long-term growth potential. In particular, reducing the administrative burden on the private sector, further improving labor market functioning, and raising efficiency of the financial sector and public enterprises will be crucial.

I. INTRODUCTION

1. The Netherlands Antilles consist of a federation of five Caribbean islands, with a population of about 200,000 inhabitants.[1] It is an autonomous but integral part of the Kingdom of the Netherlands and as such does not have a separate quota or other financial relationships with the Fund (Appendix I). Its own currency, the Netherlands Antillean guilder (NA f.), has been pegged to the U.S. dollar at a rate of NA f. 1.79 per US$1 since December 23, 1971. Traditionally based on financial offshore and oil refining inflows and tourism, the Antillean economy is undiversified and has suffered severely from the decline of these inflows during the past 15 years and from the high incidence of hurricanes in the 1990s. Policy adjustment has been hesitant, and the past decade has been marked by intermittent fiscal crises and attempts to adjust.

2. In concluding the last Article IV consultation discussions on June 7, 1999 (SM/99/106, 5/10/99), Executive Directors urged the authorities to take immediate deficit-reducing measures to avert an impending fiscal crisis. They commended the authorities for keeping monetary policy tight and viewed the exchange rate peg to the U.S. dollar as appropriate. To restore confidence and favorable growth prospects, they called on the authorities to persevere with fiscal adjustment, mainly by reducing the size of the civil service; prevent further accumulation of arrears; normalize financial relations with the Netherlands; and make rapid progress with structural reforms. In this context, promoting labor market flexibility and the sound development of the financial sector, and improving the efficiency of utilities were seen to be essential. Directors welcomed the authorities' commitment to combat money laundering and promote the development of the international financial sector.

3. In the event, partly owing to disputes within the governing coalition, fiscal measures were not implemented soon enough to avert a crisis, which prompted the Dutch authorities to provide emergency liquidity support in December 1999, after a new coalition had taken office. With staff assistance, adjustment efforts were reinvigorated in 2000. The authorities also sought the advice of the World Bank and Foreign Investment Advisory Services (FIAS) in designing structural reforms (Appendix II). The next central government elections are scheduled for January 2002. Policy making is already being affected by the electoral calendar.

4. Data provision to Fund staff on budgetary, monetary, and external developments has been adequate to follow the implementation of the authorities' program, but remaining data deficiencies complicate the assessment of economic conditions (Appendix III). In particular, data on real sector developments lack sufficient coverage and timeliness. The authorities have adopted the GDDS framework as a device to improve Antillean statistics.

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[1] The five islands are Curaçao and Bonaire (the Leeward Islands), and Saba, St. Eustatius, and the southern part of St. Maarten (the Windward Islands). In addition to a central government, each island has a separate autonomous government.

II. Background

5. **The economy of the Netherlands Antilles is undiversified and prone to external shocks, which on balance have been adverse during the past 15 years.** The boom of tourism was insufficient to compensate for the decline in the oil refining and offshore sectors (Box 1). The shock to the latter was particularly severe: tax revenues derived from the sector fell from about 15 percent of GDP in the mid-1980s to less than 2 percent of GDP in 2000. Moreover, in the second half of the 1990s, hurricanes caused a sharp drop in stayover tourism, which has not yet fully recovered. Consequently, during 1998–2000, real GDP and real per capita GDP fell by a cumulative 6¼ percent and 2¼ percent, respectively, and rising emigration dampened the underlying increase in unemployment (Figure 1, and Table 1). This growth performance is appreciably weaker than that of main trading partners and other Caribbean countries (Figure 2). The recession also caused nonperforming loans in the financial sector to rise from about 3 percent in 1997 to 4.7 percent in 2000 (Table 2).

6. **For three decades, the key monetary policy target has been the exchange rate peg to the U.S. dollar, which has kept inflation low, but external competitiveness has suffered.** In 1999, changes in the reserve requirement replaced quantitative controls as the preferred instrument of monetary policy, but ceilings on bank credit to the government nonetheless remained in place. Core inflation has been in line with that of the United States, even though indirect tax and energy price hikes boosted headline inflation to an estimated 4.7 percent in 2000 (Figure 3). The consumer-price-based real effective exchange rate has fluctuated without clear trend since the mid-1980s (Figure 4), but the decline in market share in regional tourism during the 1990s is evidence of flagging competitiveness.[2] Comparative regional studies indicate that high labor costs and utility prices are competitive disadvantages for investment in the Antilles, partly compensated by higher skills and a stable legal and political environment. Weak competitiveness has contributed to large and widening current account deficits, while official reserve cover has remained low, a pattern not atypical for the Caribbean (Figure 5, and Tables 3 and 4). Sizable official capital inflows from the Netherlands have become indispensable to support the budget and the balance of payments (Table 5).

7. **With Antillean citizens free to move to the Netherlands, migration plays a central role in the adjustment of the economy to shocks and the design of the policy response.** Since the Antilles offer limited scale economies and benefits, a large share of the Antillean population (about one third) has already moved to the Netherlands in search of higher wages or benefits. Adverse shocks and fiscal tightening alone will further induce emigration, as happened during 1998–2000, when more than 9 percent of the population of Curaçao left.[3] With most emigrants belonging to the younger age groups, the economy's potential and the sustainability of the health

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[2]Market share in regional tourism dropped from 7.4 percent in 1990 to 6.4 percent in 1998.

[3] Owing to a sharp rise in immigration to St. Maarten, overall population of the Netherlands Antilles is estimated to have declined by only 4 percent during this period.

care and pension systems are being adversely affected (Figure 6). Alternatively, budgetary transfers from the Netherlands could cushion the impact of adverse shocks, but risk creating bailout expectations or a dependence on such transfers without ensuring sustainable growth. Indeed, this risk seems to have been borne out during the past decade as increased financial assistance from the Netherlands was unable to stem the tide of emigration.[4] Thus, comprehensive domestic reform and policy adjustment appear to constitute the only viable policy option.

Box 1. Exogenous Shocks, 1986–2000

Being small and undiversified, the Antillean economy is susceptible to exogenous shocks and external developments. During the past 15 years, these shocks have been mostly adverse. Three such shocks can be easily identified:

- The Antillean financial offshore sector suffered a severe decline as the result of changes in tax legislation in other countries (see Box 3). Tax revenue obtained from this sector—a good proxy for its value added—fell from about 15 percent of GDP in the mid-1980s to less than 2 percent of GDP in 2000.
- Inflows from oil refining dropped from more than 7½ percent of GDP in the early 1990s to slightly more than 3 percent of GDP in 2000.
- Hurricanes severely lowered tourism revenues in 1995 and 1996, by a cumulative 5.7 percent of GDP.

Of course, not all developments were negative. Tourism boomed in the early 1990s, largely compensating for the declines in other sectors until the 1995–96 hurricanes. Still, a small counterfactual experiment illustrates what might have been without the impact of these adverse shocks. Assuming that real activity of the offshore and refining sectors had remained at their 1986 and 1993 levels, respectively, and that tourism had not been affected by hurricanes, real GDP today would have been higher by more than 16 percentage points. Moreover, the decline of the offshore sector represented an additional burden. Taxes paid by the sector, and thus by foreigners, needed to be shifted onto the domestic economy, and by implication onto other Antillean exports. But in these markets (tourism, ship repair, and trade), the Antillean economy was mostly a price-taker.

The Antillean economy is also very sensitive to developments in the Netherlands, because of free labor mobility to the Netherlands, and in Venezuela, which is one of its largest non-tourism trading partners. The booming Dutch economy during the 1990s made emigration a relatively attractive proposition, especially for skilled labor, thus leading to domestic shortages of such labor. By contrast, Venezuela's economy performed poorly during the 1990s: real GDP growth fluctuated between 10 percent and minus 7 percent and by 1999 the level of real GDP was not much different from that of 1992.

[4] Development assistance increased to about 5 percent of GDP by 1999 and commitments peaked at 7 percent of GDP in 2000, in the context of the most recent adjustment effort.

8. **The 1990s were marked by periodic, but unsustained attempts at fiscal adjustment and absence of structural reform.** Past fiscal adjustment efforts faltered on the inability to control the public wage bill and to sustain tax increases, and low commitment to reform (Box 2, Figure 7, and Table 6). By the mid-1990s fiscal deficits had risen to 4-5 percent of GDP, setting off adverse debt dynamics and eroding confidence. Since then, financing constraints have limited the size of the budget deficit. The deficit was financed largely by the civil servants' pension fund whose claims on the government doubled between 1994 and 2000 to reach almost 28 percent of GDP (more than 44 percent of its total assets). Arrears to the Dutch government were also tolerated.

9. **In late 1999, a renewed adjustment effort was initiated, centered on a reduction in the size of the civil service and supported by significant structural reforms.** [5] This effort was prompted by the conditioning of Dutch financial support on the sustained implementation of an adjustment program, designed with assistance from Fund staff. Bold fiscal and structural measures were required to reverse past policy slippage. The turnover tax rate was increased from 2 percent to 5 percent, the 1998 income tax relief package was reversed, 20 percent of civil servants were dismissed (though with high severance benefits), salary increases and vacation allowances were suspended. Labor market rigidities were tackled, inter alia by abolishing the individual dismissal permit, and allowing more flexible application of the workweek, with the tourist sector benefiting from a more liberal regime. Measures were taken to reduce the administrative burden on private business, liberalize trade, and promote privatization and electronic commerce.

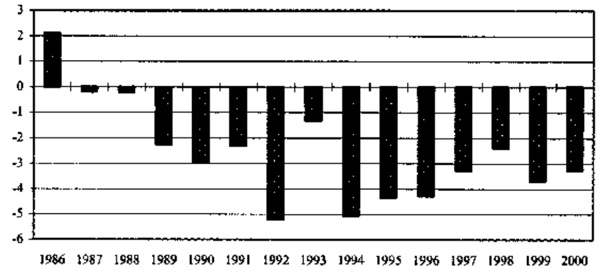
10. **Nonetheless, success remained elusive and confidence in the authorities' economic policies was not established.** Delays in pension and health care reforms and regularization of arrears and the disruption of tax administration caused by an ad hoc approach to layoffs of civil servants undermined the viability of the 2000 budget. Unsustainable expenditure compression limited the deficit to 3¼ percent of GDP, while further arrears to the pension fund and private suppliers accrued. Vested interests slowed the pace of structural reform and expenditure reduction and succeeded in forcing through new spending initiatives. Policy coordination problems between the dual layers of government and with the Netherlands delayed progress in implementing public investment programs, thus leaving the economy with little support.

[5] A detailed description of the adjustment effort since late 1999 is provided in the background paper.

Box 2. Fiscal Policy, 1986–2000

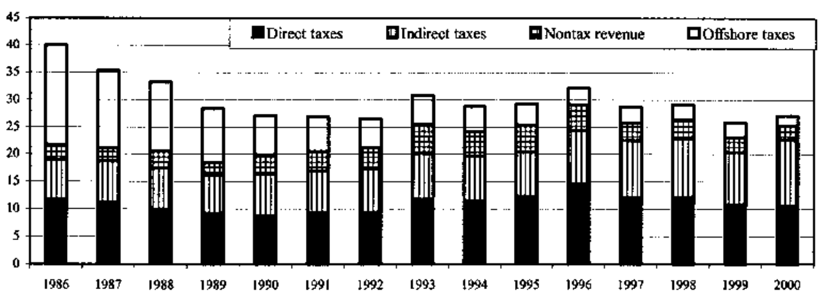
Except for the first of the past 15 years, the budget of the general government of the Netherlands Antilles has been in deficit in each year (Figure B1). A fall in offshore tax revenue led to a sudden and sharp decline in the revenue-to-GDP ratio between 1986 and 1992 (Figure B2) and adjustment on the expenditure side lagged behind, leading to a rapid expansion of the budget deficit. Following large salary increases in 1992, an attempt to stabilize in 1993 was not sustained, and expenditure drifted upward through 1996 when financing constraints began to be felt (Figure B3). Again, adjustment was short-lived, and yielded to an expansionary fiscal strategy in 1999 when direct and indirect taxes were cut. This approach failed to revive the economy and led to the accumulation of budgetary arrears as insufficient resources were available to finance the underlying widening of the deficit.

Figure B 1. General Government Balance
(in percent of GDP)



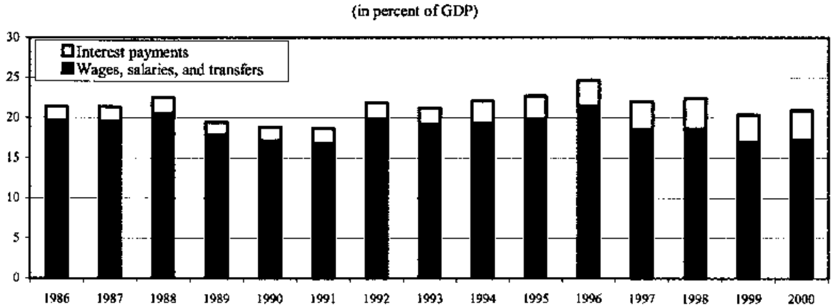
Source: Authorities

Figure B 2. Selected Components of Revenue
(in percent of GDP)



Source: Authorities

Figure B 3. Selected Components of Expenditure
(in percent of GDP)



Source: Authorities

The pattern of adjustment reflects a systematic underestimation of the size and duration of adverse shocks and overestimation of the size and duration of positive shocks. Thus the decline in offshore revenues in the mid-1980s did not lead to forceful adjustment on either side of the budget, while the expansion of the tourism sector in the early 1990s was quickly accompanied by increases in public sector wages and employment.

III. Policy Discussions

11. **The discussions focused on policies required to halt the economic decline and restore prospects for job creation and growth.** There was general agreement on the need to implement mutually reinforcing structural reforms, public investment programs, and sound budgetary policies. Monetary policy would continue to support the exchange rate peg and supervision would be intensified to safeguard the soundness of the financial system. The authorities accepted the need to contain the budget deficit to instill confidence, but felt that further near-term fiscal contraction would be counterproductive. They felt that a boost to public investment—financed from abroad—would be crucial to stimulate the economy. They noted that structural reforms would have to proceed gradually, in line with limited implementation capacity. The staff emphasized that front-loaded progress, especially in implementing the required fiscal adjustment measures, establishing financial discipline, and proceeding with already identified structural reforms would be essential to build a track record of sustained adjustment and restore confidence.

A. Short-Term Outlook and Policies

12. **The authorities attributed the recent recession mainly to the short-term contractionary effects of some of the adjustment measures and argued that, without economic stimulus, the economy would not recover.** Recent fiscal adjustment measures, emigration, and the uptick in headline inflation had dimmed economic prospects. Without stimulus, they argued, the economy, especially on Curaçao, would remain trapped in a downward drift. The staff concurred with the need for economic revival but emphasized that, given the structural nature of the problems facing the Antillean economy and the very high import content of domestic expenditures, fiscal demand stimulus would not promote growth. Instead, progress along three parallel tracks would be needed: sound budgetary policies to establish financial discipline and help restore confidence; investment projects to support employment in the short run, and raise the economy's potential in the long run; and structural reforms to strengthen competitiveness and raise export potential.

13. **On the basis of renewed adjustment, the staff projected that the economy would bottom out in 2001** (Table 7).[6] A continuing expansion of cruise tourism, the return of stayover tourism to normal levels, and an increase in investment were expected to stabilize economic prospects. The staff projected growth to remain moderate for some time, though with clear upside potential, proportional to the strength of an adjustment program and the related return of confidence. Consumer price inflation was expected to decline to very low rates, and prices of some essential products could even fall as the benefits of trade liberalization and the elimination of production monopolies are realized. Lack of progress in pursuing a comprehensive adjustment program constituted the most important downside risk.

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[6] All projections in figures and tables in this report covering 2001 onward are conditional on the implementation of a comprehensive adjustment program, and thus constitute a normative scenario.

14. **The staff noted that implementing a viable budget would be a prerequisite for an economic recovery.** The weaker-than-expected economy, the disruptive reorganization of tax collection, new spending initiatives, and partial and delayed implementation of measures to support the adopted budget implied that achieving the targeted general government deficit of 1.8 percent of GDP in 2001 was now well beyond reach. The staff projected that the deficit would reach 5 percent of GDP, an estimate that was not disputed by the authorities, though they were more optimistic about dividend receipts. Since such a deficit could not be financed, and the magnitude of the deviation from the original target would remove all credibility from the current adjustment effort, the staff urged the authorities to take immediate measures to put the budget deficit back on a declining path. Repeating last year's successful special effort in tax auditing and collection could boost revenues. On the expenditure side, there appeared to be room to scale back new spending initiatives, curtail health care and pension costs, preserve savings on the wage bill associated with unfilled vacancies, and reduce subsidies and transfers.

15. **The authorities accepted to hold the budget deficit to last year's level—3¼ percent of GDP.** Adjusted for a shift in timing of planned expenditure of ¾ of one percentage point of GDP from last year and a weaker economy, this deficit was in line with the original target and reflected a significant improvement in the primary balance. The authorities were not in a position to define specific measures at the time of the mission, but planned to focus on strengthening tax administration, keeping spending on goods and services to budgeted levels, and reform health care. They noted that pressing ahead with pension reforms at this stage would be risky, since legal action to reverse planned changes had been threatened and was likely to succeed. The authorities also saw little prospect for achieving further savings on the wage bill, since real salaries had already declined significantly and filling vacancies was necessary to ensure normal functioning of the government. They agreed that there was no room to finance the deficit domestically and indicated that they expected budget support from the Netherlands. The staff observed that, to maintain a proper balance between adjustment and financing, such support would need to be commensurate with progress in implementing a comprehensive adjustment program.

16. **Accelerating some externally-financed public investment projects would be desirable to help stabilize the economy**. While medium-term public investment programs, financed by the Netherlands, should be pursued, it was considered useful, in the immediate period ahead, to put some public infrastructure projects on a fast track. Such projects would alleviate infrastructure bottlenecks and be twinned with private sector investments geared at raising exports. The staff emphasized that care should be taken not to burden the budget with guarantees, equity participations, or subsidies of a recurrent nature, as had occurred in the past.

17. **To ensure stability, there was agreement that the current exchange rate peg to the U.S. dollar should be continued**. Even though the authorities recognized the need to boost competitiveness, they agreed that modifying the exchange rate peg or regime would not be an effective means. Such action could trigger a confidence crisis and would most likely not durably improve competitiveness because the possibility of emigrating to the Netherlands would keep wages high compared to the region. Instead, steadfast structural reforms to reduce non-wage costs and raise productivity were needed to strengthen competitiveness. Some decision makers and private agents suggested that dollarization could be a cure for high interest rates and

transaction costs. The staff pointed out that residents were already free to transact in dollars, and that interest rate differentials vis-à-vis the United States reflected country risk and the relative inefficiency of the domestic financial system, issues that dollarization would not resolve. Moreover, dollarization would require further fiscal adjustment to offset the loss of seigniorage and proceeds from the exchange license fee.[7]

18. **The staff observed that, until very recently, the tightening of monetary policy had not been effective in keeping official reserves from falling and that their level remained low** (Figure 8). The central bank responded that monetary policy had been overburdened. Increased overdrafts by private suppliers affected by budgetary arrears and lending to distressed borrowers had recently contributed to a very rapid credit expansion, out of line with declining economic activity, though bank intermediation of some large investment projects had also played a role (Table 8). The authorities further noted that the conduct of monetary policy was being hampered by the lack of competition in the banking system and the absence of secondary markets. They felt nonetheless that the steady increase in reserve requirements and the continuation of moral suasion and ceilings on credit to the government would succeed in maintaining official reserves at their current level and preserving confidence in the peg. If need be, they would be prepared to reactivate ceilings on bank credit to the private sector to achieve this objective. The staff, noting that some banks did not comply with the reserve requirements, argued for a substantial increase in penalty rates on borrowed reserves to ensure compliance. The mission also cautioned about the distortionary effects of reintroducing credit controls.

19. **Looking ahead, the authorities agreed that monetary conditions would need to remain tight, even if the budget deficit were brought under control.** The staff pointed out that possible large disbursements of financial assistance from the Netherlands in support of sustained adjustment would pose a challenge to monetary policy. The authorities agreed with the need to guard against an undue easing of liquidity conditions. However, they felt that to the extent that official inflows would substitute for domestic financing of the budget, their impact would be largely sterilized by the underlying private portfolio shift to investments abroad. In addition, the authorities would have the option of opening up additional possibilities to place funds abroad, e.g., by reducing the domestic investment requirement for institutional investors.

20. **The difficulties in financing the budget deficit and the recession appeared to threaten the soundness of the financial system.** Budgetary arrears to suppliers had given rise to distressed borrowing, and the margin of value of collateral underlying loans had almost completely been eroded. Credit unions had been particularly affected by loans turning bad. Overall, bank profitability and capital adequacy had been declining (Table 2). Some banks had been reducing exposure to poor credit risks, but others had taken the opportunity to expand market share. In addition, not all banks seemed to be using proper loan classification procedures, imparting an upward bias to observed capital adequacy. In response, the central bank—noting that its prudential requirements exceeded the Basel standards—had intensified supervision by

[7] Though estimates of seigniorage vary, proceeds from the exchange license fee alone amount to about ¾ percentage points of GDP.

increasing the frequency of on-site inspections and strengthening reporting. The central bank felt that reserves of the banking system were still adequate, but admitted that an economic turnaround would be essential to prevent trouble in the financial sector.

B. Medium-Term Fiscal Policy

21. **The authorities' aim to achieve budget balance over the medium term while allocating some of the expenditure savings from civil service reform to tax cuts seemed to be in jeopardy**. In the staff's view, given limited domestic financing capacity and demographic pressures, reaching budget balance in 2005, when severance payments ran out, remained essential. However, with the budget deficits in 2001 and beyond much higher than initially expected, even if all expenditure savings were allocated to deficit reduction, the staff estimated that the budget would not attain balance. Moreover, the freeze of civil servants' wages, especially for high-skilled employees, could not be sustained indefinitely, and the planned education reform was likely to involve additional outlays. To reconcile these demands, and allow for desirable tax cuts, the staff urged the authorities to phase out subsidies to public enterprises, reduce transfers, and further streamline the civil service by eliminating remaining overlap between levels of government, which should permit additional savings on spending on goods and services. The authorities agreed that further spending reductions would be necessary, which they expected to obtain mainly from further decentralization of government services.

22. **The staff argued that a budget-neutral comprehensive tax reform could significantly improve the investment climate and resource allocation.** The authorities recognized that currently both indirect and direct taxes were highly distortionary and excessively complex, placing a high burden on the private sector and tax administration. On indirect taxes, they proposed to remove the cascading feature of the current turnover tax system and simplify administration. They saw merit in the mission's recommendations to take a comprehensive approach to tax reform and to consider reducing the number of taxes and high marginal rates, broadening the tax base, phasing out the import surcharge and exchange license fee, and eliminating discretionary tax exemptions and holidays. The authorities felt that significant technical assistance would be required to implement such a package already in the context of the 2002 budget as suggested by the staff. Even then, a more phased approach might be preferable in view of the limited capacity of the public and tax administration.

23. **To realize the planned expenditure reduction and contain quasi-fiscal risks, budget discipline needed to be firmly established and extended to the broader public sector**. The staff pointed out that progress had been disappointing in this area. As an urgent step, the backlog of outstanding claims and debts among government entities had to be resolved and the Solidarity Fund made operational in its new form to allow the smaller islands to adopt viable budgets.[8] Oversight over newly autonomous public institutions—e.g., through performance contracts—had

[8] The Solidarity Fund is an existing redistribution mechanism within the Kingdom of the Netherlands designed to support the smaller islands. The nominal amount of transfers reallocated by this fund has not been revised since 1986.

to be established. Reporting and monitoring systems were to be expanded to cover these institutions, smaller islands, and public enterprises. Furthermore, as the authorities acknowledged, financial difficulties of several public enterprises, in particular the national airline and the water and electricity utility, required urgent attention. The mission also pointed out that the recurrent emergence of claims on public guarantees extended to hotel projects clearly demonstrated the drawbacks of the past policy of liberal extension of such guarantees.

24. **Implementation of plans to strengthen the civil servants' pension fund and to undertake health care reform would be crucial to ensure medium-term fiscal sustainability.** The authorities recognized that modifications to the pension contribution rate for fiscal purposes and frequent recourse to the pension fund to finance budget deficits—mainly through periodically regularized arrears—jeopardized the funded nature of the system. They agreed that these practices should be terminated and expected that planned privatization would be a decisive step. The staff suggested the desirability of other pension reforms, such as the phasing in of a higher retirement age for the basic old age pension, but the authorities were reluctant to commit to such changes. With respect to health care, the need for increased efficiency, budgetary savings, and containment of cost increases was generally accepted. The authorities agreed with the mission's suggestions to introduce budgeting for basic health care as well as incentives (e.g., co-payments) to curb demand, but details of the reforms remained to be elaborated.

C. Structural Reforms

25. **The staff strongly emphasized that, with free labor mobility to the Netherlands anchoring real wages, policies to reduce business costs and raise labor productivity were the only option to restore job and growth prospects.** The authorities, stressing that they lacked the capacity to design and implement structural reforms at the pace suggested by the staff, noted that they had recently called upon the World Bank and FIAS to strengthen capacity. Preliminary findings of these institutions had indicated that the administrative and regulatory burden was particularly onerous in the Netherlands Antilles, an observation echoed by the private sector.[9] To attract investors, it would be imperative to drastically ease this burden.

26. **The staff argued for further measures to improve the functioning of the labor market, building on progress made in 2000.** The authorities felt that the labor market had become quite flexible, and that continued public support for other components of the adjustment program required a pause in labor market reform. Nonetheless, they agreed with the staff that domestic skills shortages had to be remedied. In addition to the recent removal of obstacles to obtaining work permits by Dutch citizens, they would give priority to reducing the backlog in work permit applications by foreigners. The staff encouraged the authorities to involve social partners in a dialogue to address remaining labor market anomalies, in particular the high

[9] The World Bank discussed its findings with the authorities in March 2001, stressing the need for wide-ranging reforms and offering further assistance with public expenditure and tax reform, identification of priority investment projects, privatization, labor market reform, and improving domestic financial intermediation.

mandatory overtime pay, restrictive features of the severance pay legislation, and lack of pension plans in the private sector. Easing restrictions on shop opening hours and expanding the availability of child care facilities could also further improve the functioning of the labor market.

27. **The central bank continued to pursue avenues to raise the efficiency of the domestic financial sector.** The establishment of competition between banks and non-banks for government securities, mortgages, and consumer loans, and the liberalization of capital outflows on the deposit side, to address the dominance of the largest bank in retail banking, had had only limited success in lowering interest rate spreads and increasing the responsiveness of interest rates to economic conditions. The central bank would continue to promote entry of foreign banks and consolidation of the smaller domestic financial institutions. On liberalizing foreign borrowing by enterprises, the staff supported the central bank's cautious approach, given the current poor state of the budget and the economy. The staff suggested that the forthcoming competition law could provide a direct route to strengthening competition in the financial sector.

28. **Trade and product market liberalization had been initiated with the abolition of production monopolies and import quotas and the implementation of the first phase of the gradual elimination of economic levies.**[10] The mission stressed that to realize the benefits from liberalization it would be important to expedite plans to adopt a competition law. The staff also recommended further trade liberalization, e.g., by reducing the highest import tariffs and the number of tariff bands and beginning to phase out the import surcharge in the context of a possible overhaul of the tax system. The authorities noted that their trade regime was relatively liberal and indicated that the planned passage of a customs act and a new law to streamline import procedures would facilitate trade.[11]

29. **The mission observed that there was significant scope to improve the performance of public enterprises.** High prices of water, electricity, and telecommunications compared to the region constituted a major impediment to new investment. While the authorities had instructed public enterprises to raise efficiency by 10 percent, they had done so in the first instance to ensure dividend receipts. The mission encouraged the authorities to shift focus to lowering prices of services, and to complete the planned adoption of a regulatory framework for utilities as soon as possible. The staff supported the pursuit of privatization as an avenue to improve resource allocation, urging the authorities to ensure that the privatization foundation had full authority

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[10] Production monopolies, quotas, and economic levies protect 19 companies, directly employing 690 persons and producing several essential consumer goods, furniture, and construction materials.

[11] The Antillean trade regime consists of regular import tariffs, an import surcharge of 5 percent, and economic levies. Tariffs range from 0 to 95 percent, covering 40 bands. In 2000, the all-inclusive import-weighted average tariff amounted to 13.88 percent and budgetary revenues from trade taxes were 2.9 percent of GDP, compared to 6.7 percent of GDP on average for countries of the Eastern Caribbean Currency Union.

Box 3. International Financial Sector

The contribution of the offshore sector to the Antillean economy has declined substantially from its peak in the mid-1980s. At its highest, the offshore sector contributed directly more than 18 percent of GDP in tax revenues. Today, its contribution has dwindled to less than 2 percent of GDP. The decline in the sector is due to changes in the tax regime of industrialized countries. To give some examples, a major decline started in 1986, when the United States instituted a withholding tax on dividends paid to companies abroad, which previously went untaxed. In the mid-1990s, changes in Dutch legislation prevented the establishment of Dutch pension funds in the Antilles, made interest paid by a Dutch company to an Antillean counterpart under some circumstances nondeductible for tax purposes, and induced some large corporate finance companies to return to the Netherlands. In response to the Antilles' reduced attractiveness as a tax haven, the offshore sector has embarked on product differentiation. New services are being offered by the sector, especially to Central and Latin American customers, banking on the stable legal environment of the Netherlands Antilles.

The offshore sector remains important for the Antillean economy. It directly employs some 1,500 highly skilled experts and produces about 9 percent of GDP. Since the sector is by definition export oriented, it contributes in the same amount to the balance of payments. Together with indirect employment, the sector provides jobs for 5.5 percent of the labor force. Tentatively, income tax payments of persons employed in the sector are estimated to amount to about 1¼ percent of GDP. Assets managed by the sector total about US$28 billion.

Prospects for the sector, particularly as a source of budgetary revenue, have recently been affected by the increased scrutiny of offshore financial centers by the international community. In response, the Antillean authorities have clarified tax issues and taken measures to develop the international financial service sector (for details, see background paper):

- With respect to money laundering, the Financial Action Task Force (FATF) has made a favorable assessment. The FATF does not include the Netherlands Antilles on the list of 15 non-cooperative jurisdictions (published by the FATF in June 2000).

- In December 2000, the OECD removed the Netherlands Antilles from its list of 35 jurisdictions with harmful tax practices (established in June 2000 and on which 33 jurisdictions remain). The authorities committed to cooperate with the OECD to ensure transparency and equal treatment of onshore and offshore sectors by 2005.

- As a result of end-2000 approval by the U.S. Internal Revenue Service of relevant Antillean banking regulations, financial intermediaries located in the Netherlands Antilles can now apply for Qualified Intermediary status, exempting them from onerous withholding taxes.

- The Financial Stability Forum (FSF) expressed concern about the quality of financial supervision of offshore centers, and, in a report in May 2000, placed the Netherlands Antilles in the category of institutionally weakest jurisdictions. In response, the Antillean authorities have embarked on a self-assessment of their supervision of the offshore sector, with technical assistance from the Fund.

over the enterprises under its purview and that its sole purpose was privatization. However, the authorities thought that the current arrangements would suffice.

30. **Following a clarification of its tax treatment, prospects for the international financial service sector had become less uncertain.**[12] Ongoing action against money laundering and a commitment in late 2000 to adhere to international rules regarding harmful tax competition had yielded favorable assessments of the Netherlands Antilles in international fora (Box 3). As a result, upbeat sentiment had returned to the sector. With technical assistance from the Fund, the central bank is in the process of completing a self-assessment of supervision of the international financial sector, which is expected to be published later in 2001.

IV. STAFF APPRAISAL

31. **The past decade has witnessed a progressive weakening of the Antillean economy, and prospects for a recovery will depend on reinvigorating and sustaining adjustment.** Inadequate adjustment to adverse shocks to the offshore, oil refining, and tourism sectors has led to a prolonged recession, high unemployment, a tide of emigration, and pressure on the financial system. To the authorities' credit, policies implemented since late 1999 have laid the foundation for an economic recovery. Success has, however, remained elusive, mainly because adjustment policies have not been sustained. Budget deficits continue to exceed available financing, and the pace of expenditure reduction and structural reforms has slowed. As a result, confidence in the authorities' economic policies has yet to be established.

32. **The response now should consist of more vigorous reforms, well coordinated across governments and supported by building social consensus.** Such reforms should comprise three mutually reinforcing components. Further structural changes are needed to boost competitiveness, attract foreign investors, and raise the economy's export potential. Well-targeted public investments, financed from abroad, could help stabilize the economy in the short term, and support its medium-term development. Sound budgetary, monetary, and prudential policies are indispensable to instill confidence and ensure that structural reforms and public investments bear results. Reinvigorating adjustment now should lead to signs of economic recovery later in 2001, in turn creating job prospects and reducing the vulnerability of the banking system.

33. **As an early priority, budget deficits need to be brought under control and put on a declining path.** Although the originally adopted deficit target for 2001 will remain far beyond reach, plans to improve tax collection and curtail spending need to be implemented as soon as possible to prevent the budget deficit from rising above last year's level, which could well trigger a fiscal crisis. In the near term, deficits will continue to exceed available domestic financing, requiring donor support. Possible provision from the Netherlands of such support should be phased in line with the implementation of a comprehensive adjustment program. Over

[12] A more detailed discussion of the Antillean international financial service sector is provided in the background paper.

the medium term, additional efforts will be required to achieve budget balance, an appropriate objective in light of limited domestic financing capacity and population aging.

34. **Fiscal policy can support growth over the medium term by reforming the tax system and lowering the tax and administrative burden on the private sector.** Priority should be given to implementing a comprehensive tax reform to simplify the system in the context of the 2002 budget. In the first instance, such a reform should be budget neutral. Nonetheless, an eventual lowering of the overall tax burden would be desirable from the perspective of boosting the economy. The additional expenditure cuts needed to make lower taxes feasible could be obtained from a further reduction in the size of the public sector and strict enforcement of budget constraints on autonomous public sector institutions.

35. **The sustainability of the adjustment effort will depend crucially on the extension of budget discipline throughout the broader public sector, containment of quasi-fiscal risks, and successful pension and health care reforms.** Budget procedures need to be strengthened further through adoption of already drafted legislation to improve budgetary control. Efforts underway to settle the backlog of outstanding intergovernmental claims, debts, and arrears should be completed as soon as possible, and arrears to the pension fund, private suppliers, and the Netherlands should be regularized. Financial difficulties of public enterprises need to be resolved within available budgetary resources. Implementation of plans to privatize the public pension fund will be a welcome step toward safeguarding civil servants' pensions as it should prevent further misuse of the pension fund to finance budget deficits. Raising the retirement age for the basic old age pension would also contribute to fiscal sustainability. To secure continued provision of basic health care, public health care costs will need to be contained.

36. **The long-standing peg to the U.S. dollar has contributed to price stability and should be maintained.** Given the lack of effectiveness of the exchange rate as an adjustment tool in the Antillean reality, the much needed improvement in competitiveness of the economy will need to be brought about through structural reforms. The current monetary policy of targeting official reserves and tightening liquidity conditions to safeguard the exchange rate peg should be continued. Its efficacy needs to be improved by significantly increasing penalty rates for non-compliance with the reserve requirement. Whether or not fiscal adjustment proceeds as planned, the stance of monetary policy will need to remain tight.

37. **Stability in the financial sector will be essential for an economic recovery.** With the soundness of the banking system under threat from deteriorating loan performance and eroding collateral value, the central bank has correctly stepped up supervision. The intention to conduct more frequent on-site inspections and develop contingency plans to limit systemic effects of individual troubled financial institutions is welcome. In addition, reporting needs to be strengthened and the central bank should not hesitate to recall licenses of institutions that do not comply with prudential regulations. Looking ahead, further consolidation in the financial sector and capital account liberalization—implemented with caution, and once fiscal consolidation has taken hold—would permit a narrowing of interest rate spreads and a decline in real interest rates.

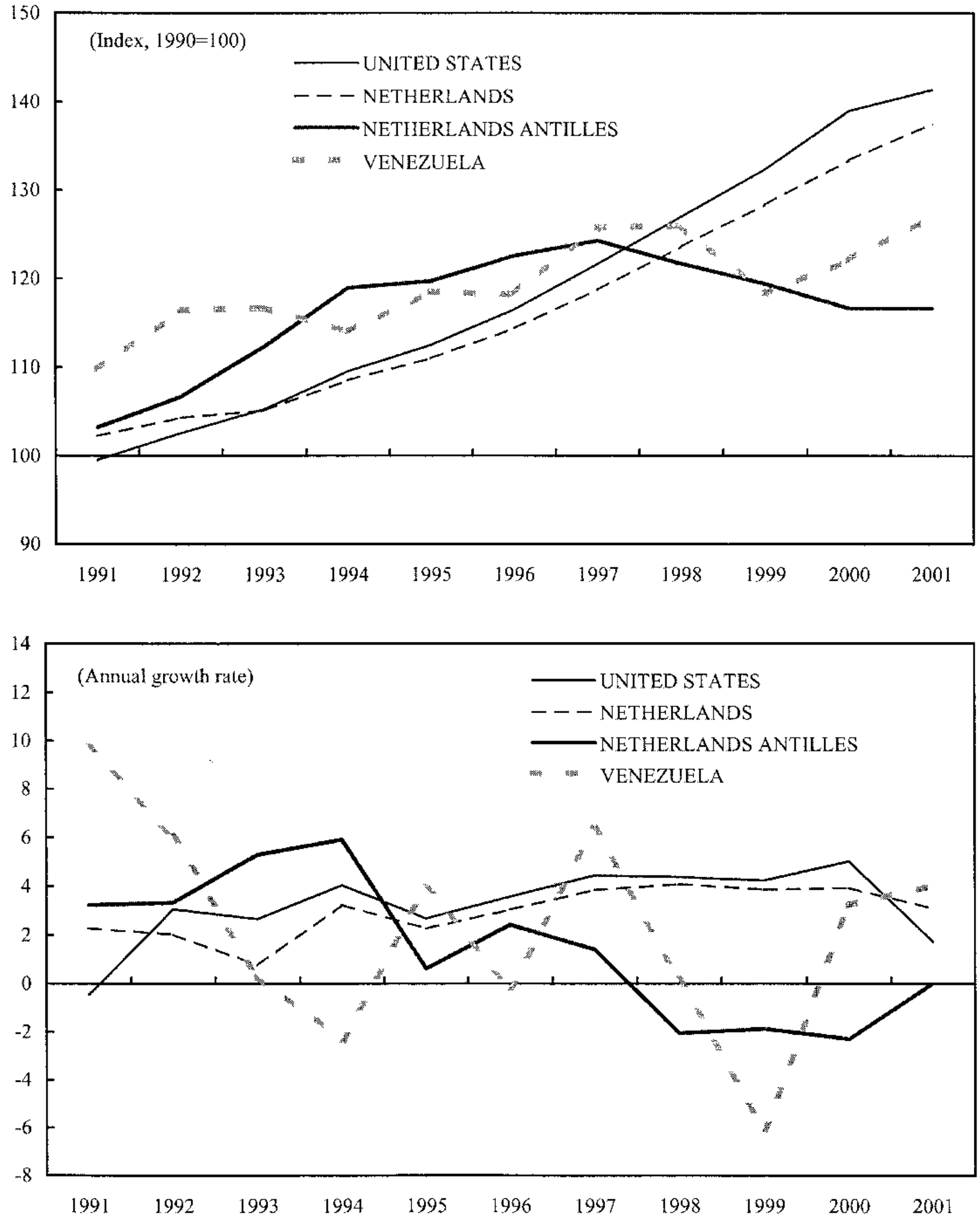
38. **Continuing progress with structural reforms is critical to improve the prospects for job creation and economic growth.** Drastically cutting the administrative and regulatory

burden will be essential to attract investors. In the labor market, domestic skills shortages and remaining rigidities need to be addressed. To reap the benefits from recent trade and product market liberalization and prospective privatization, adoption of a competition law and a regulatory framework needs to be expedited. Privatization would benefit from increasing the authority and autonomy of the recently established privatization foundation. Commendable efforts have been made to combat money laundering and adhere to international guidelines on tax competition. Supervision of the international financial sector needs further strengthening. In this context, the planned completion of a Fund assisted self-assessment is welcome.

39. **The assessment of economic developments and design of economic policies would be much facilitated by the improvement of the statistical database of the Antilles.** While core data on the budget are readily available and qualitatively sufficient, the scope of reporting on the public sector should be expanded to include the smaller islands' budgets, public enterprises, and extrabudgetary institutions and public foundations. An acceleration of the timeliness of reporting on the balance of payments and national accounts is also necessary. The commitment to adopt the GDDS as a framework to improve statistics is welcome.

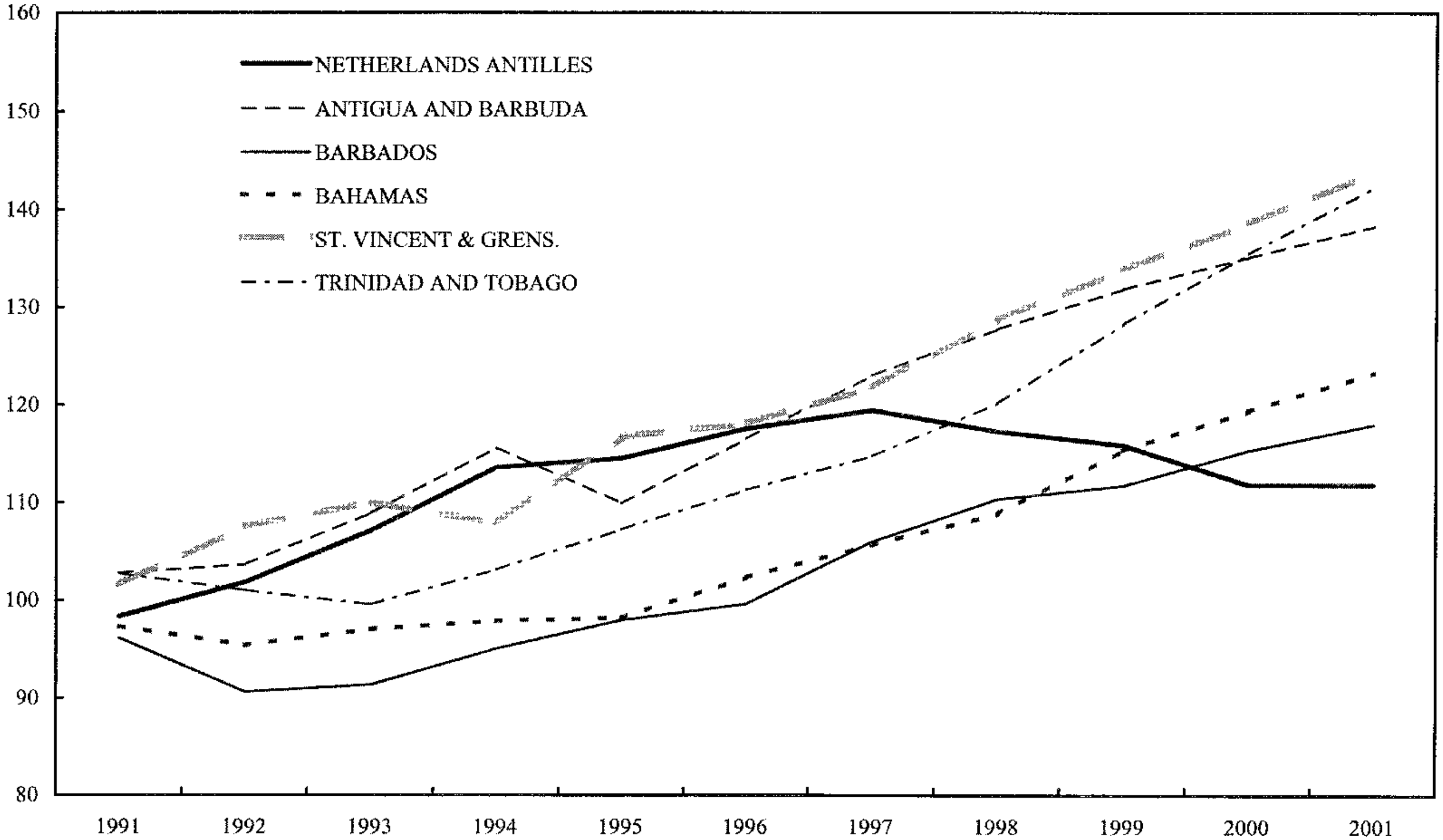
40. It is recommended that the **next Article IV consultation** discussions be held within 24 months.

Figure 1. Netherlands Antilles and Trading Partners: Real GDP 1/



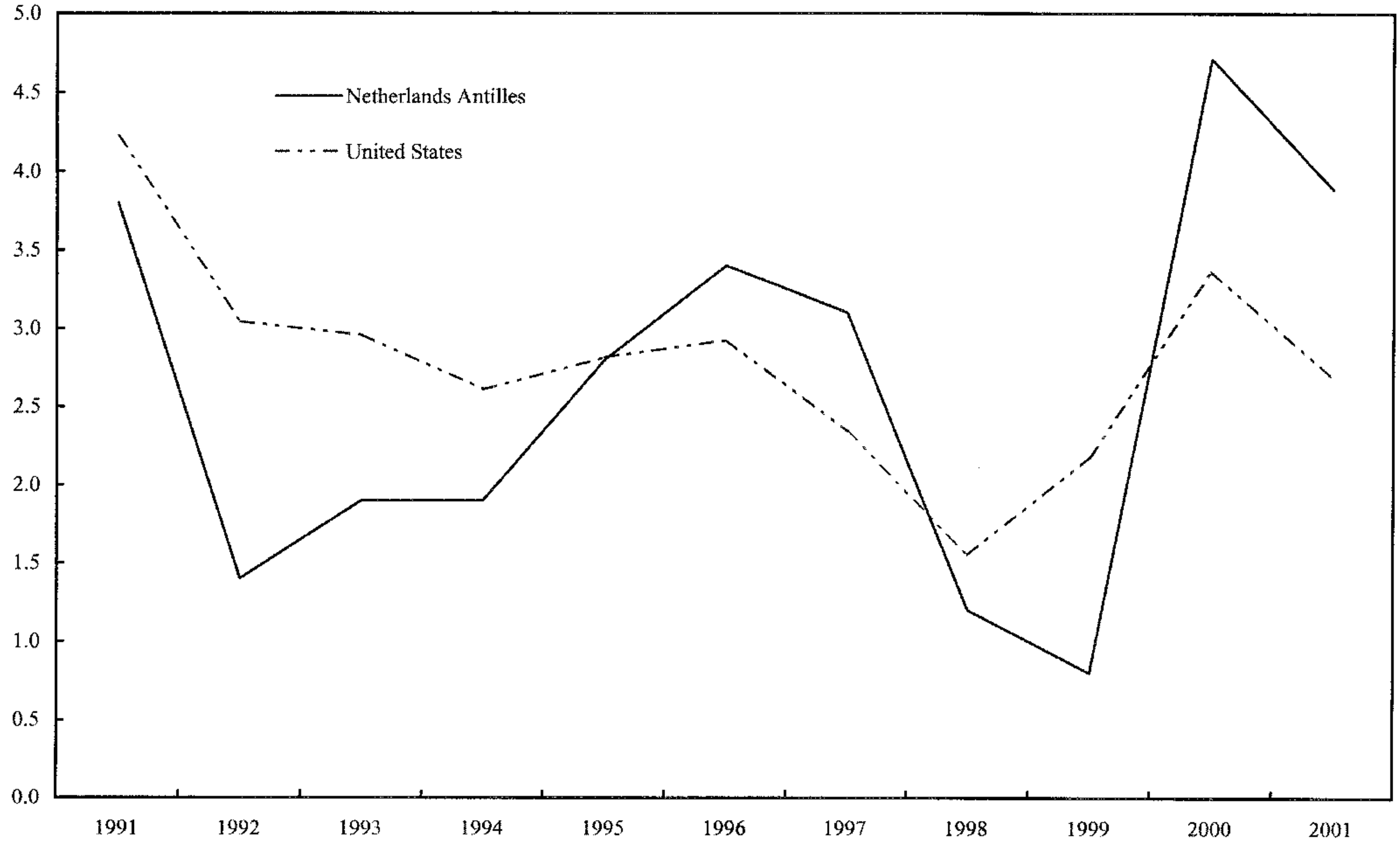
Source: IMF, WEO.
1/ Projections in 2001.

Figure 2. Netherlands Antilles and Selected Caribbean Countries: Real GDP 1/
(Index, 1990=100)



Source: IMF, WEO.
1/ Projections in 2001.

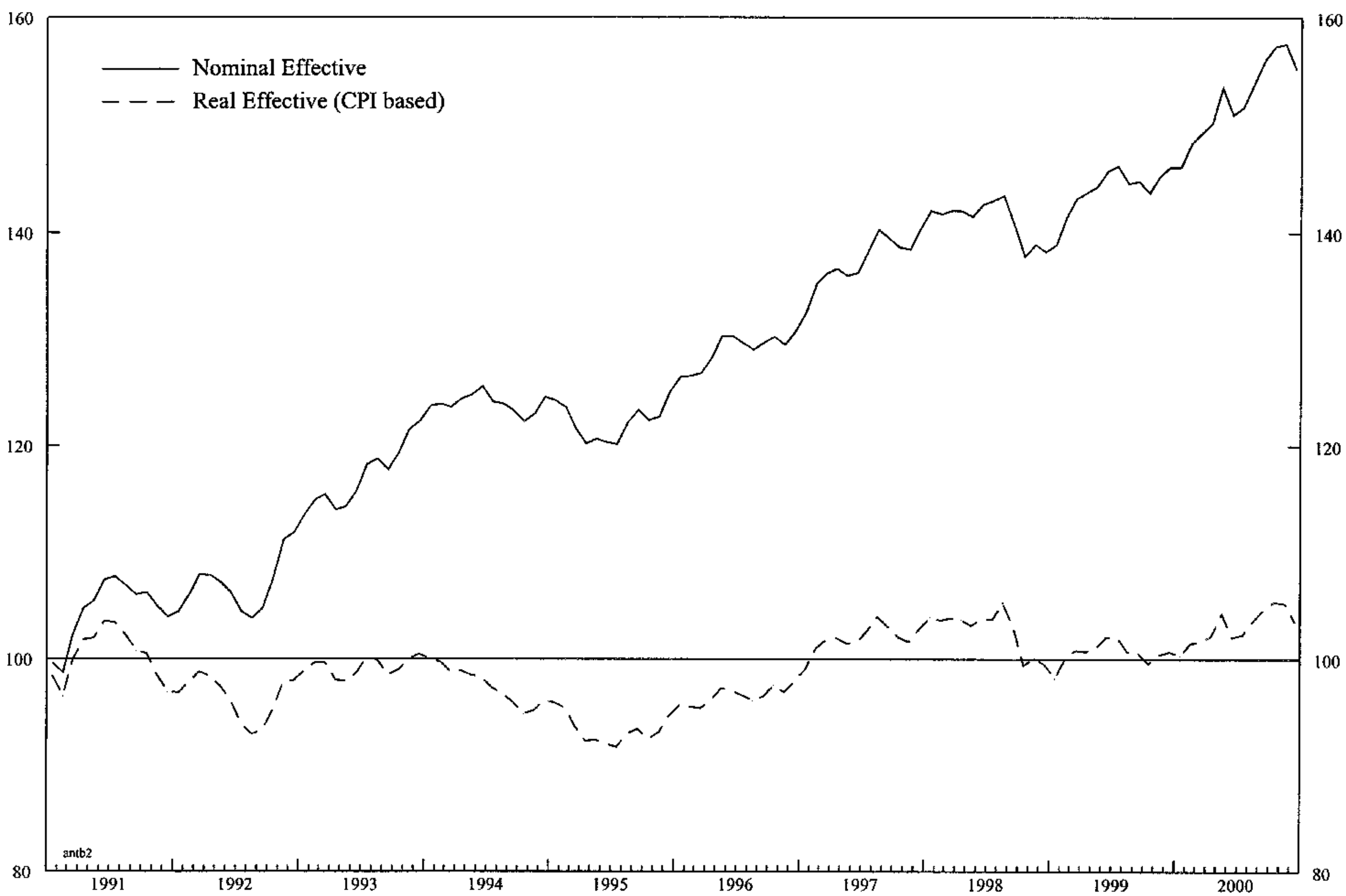
Figure 3. Netherlands Antilles: Consumer Price Inflation 1/



Sources: Data provided by the Antillean authorities; and IMF, WEO.
1/ Projections in 2001.

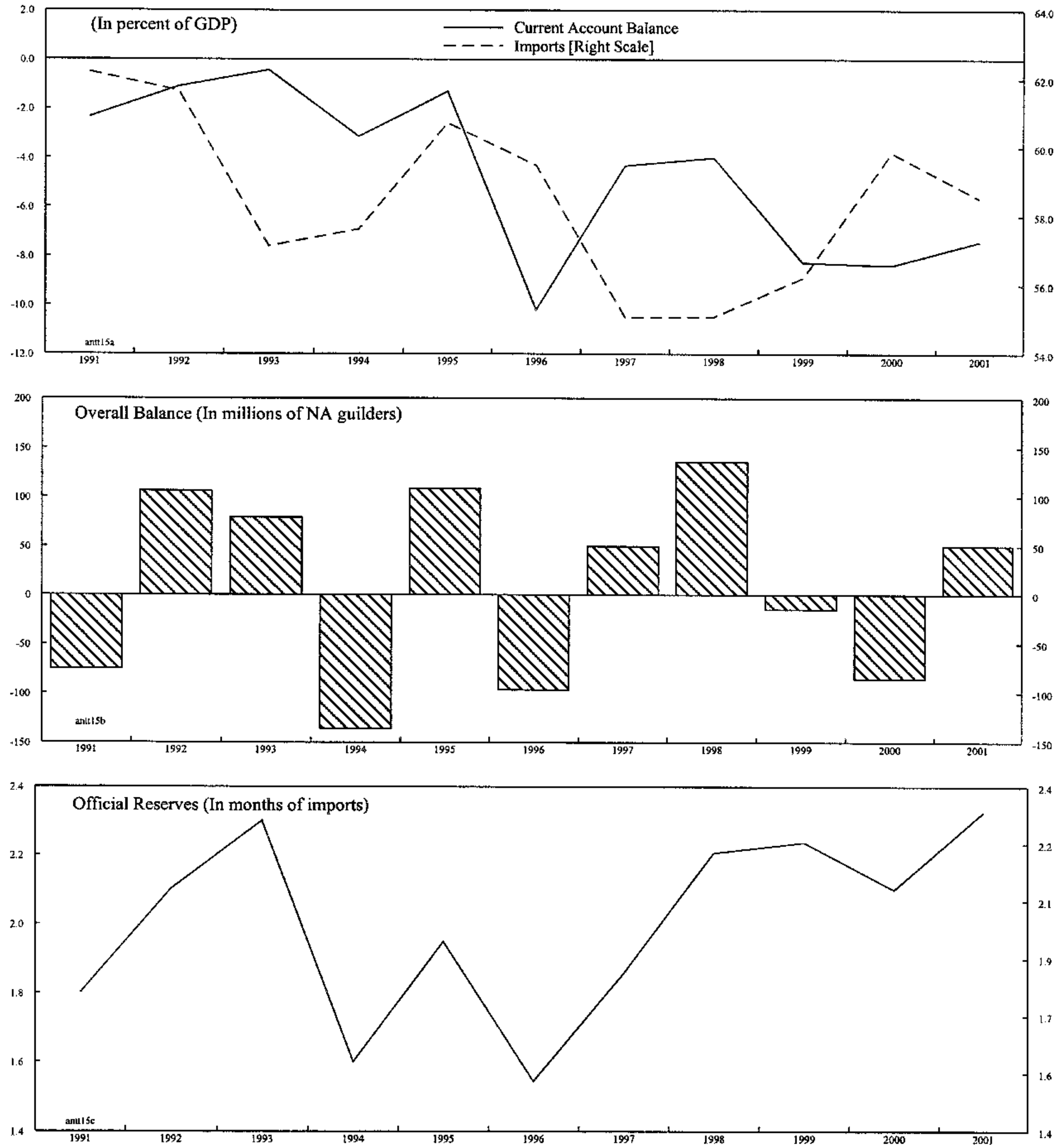
Figure 4. Netherlands Antilles: Effective Exchange Rates

(1990=100)



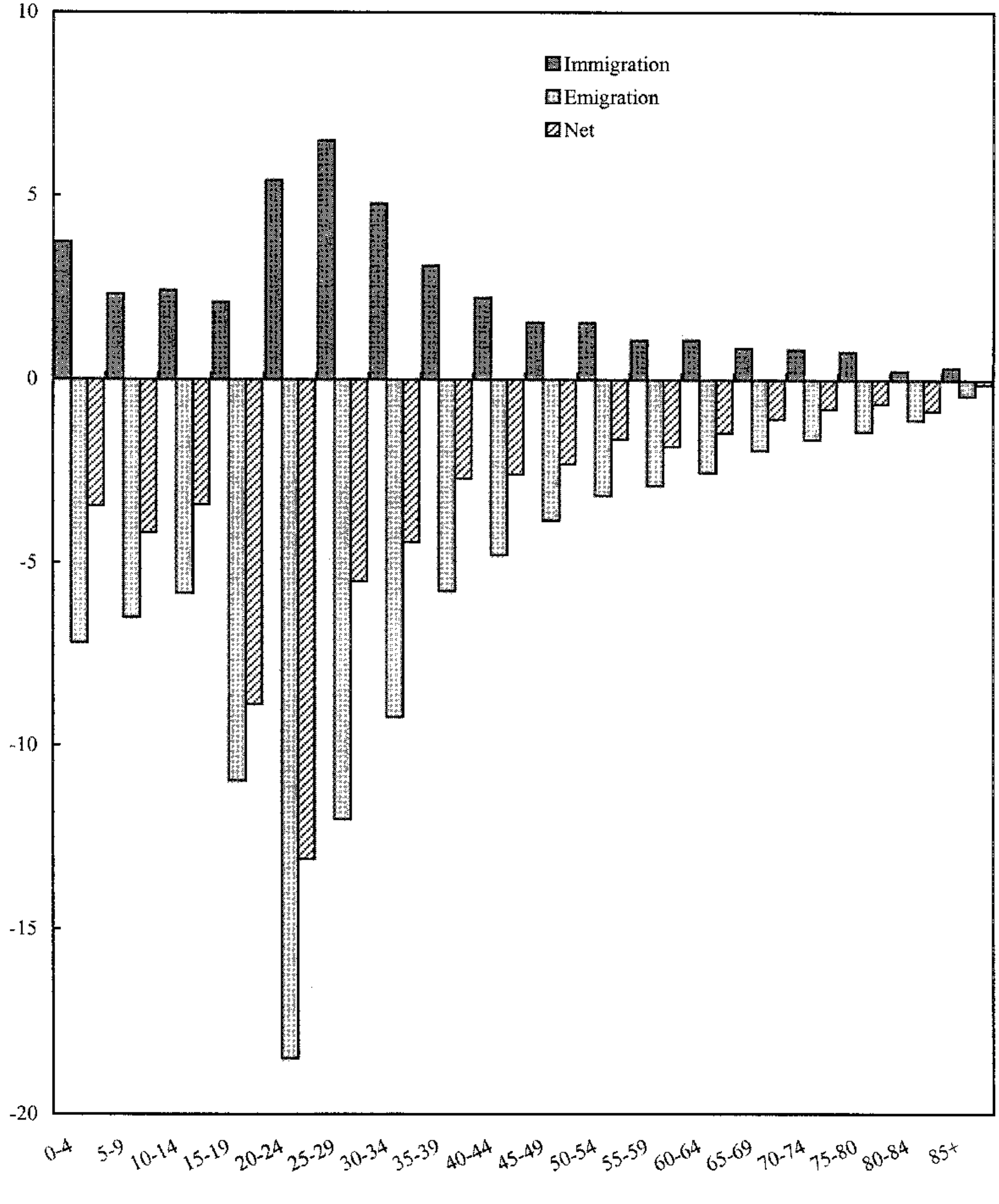
Source: IMF, International Financial Statistics.

Figure 5. Netherlands Antilles: External Sector Developments 1/



Source: Data provided by the Antillean authorities and Fund staff projections.
1/ Projections in 2001.

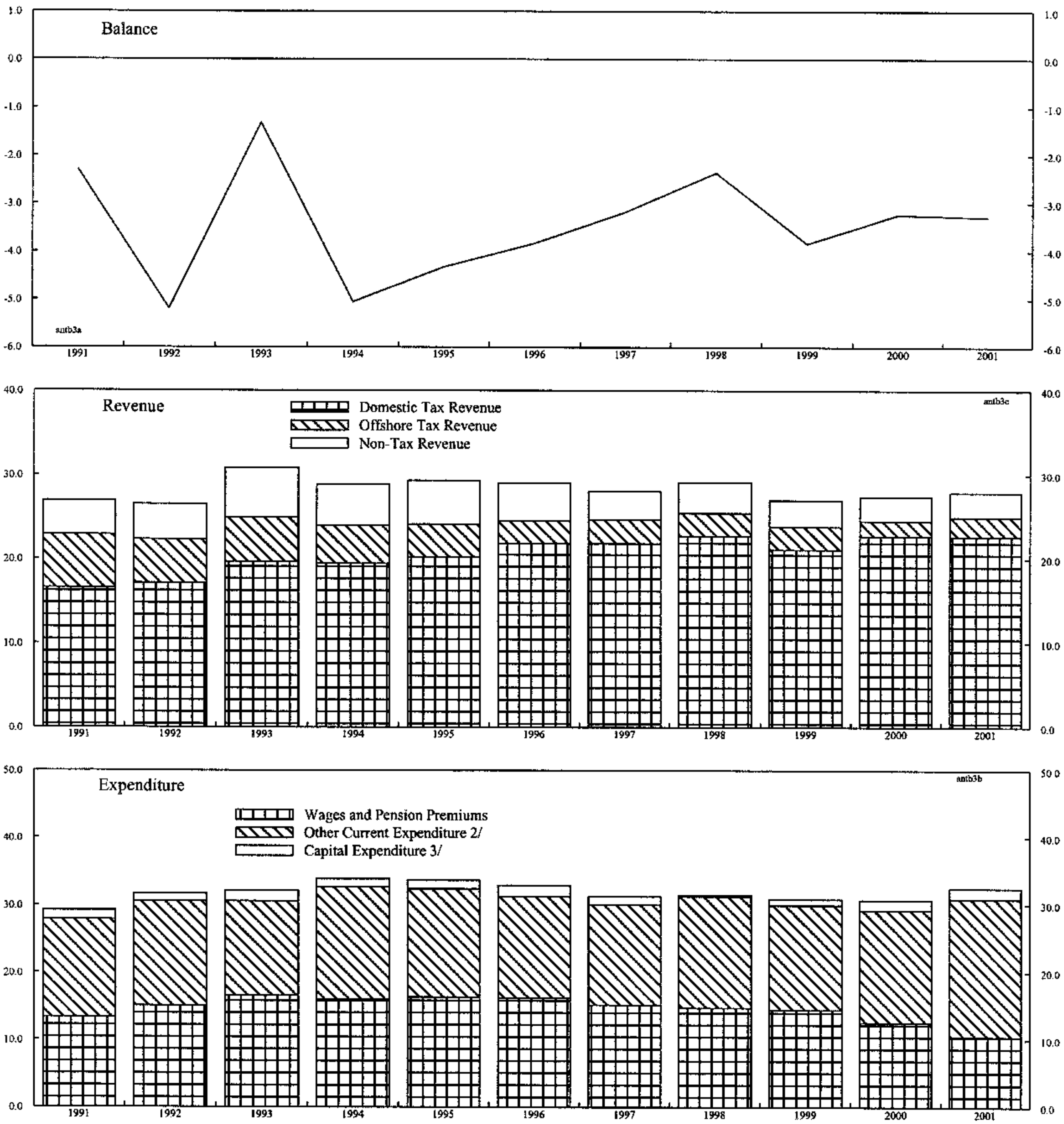
Figure 6. Netherlands Antilles: Age Profile of Migration in Curaçao and Bonaire, 1999
(In percent of age group)



Source: Data provided by the Antillean authorities.

Figure 7. Netherlands Antilles: Operations of the General Government 1/

(In percent of GDP)



Source: Data provided by the Antillean authorities and Fund staff projections.
1/ Projections in 2001.
2/ Including projected adjustment measures in 2001.
3/ Including projected contributions to a sinking fund in 2001.

Figure 8. Netherlands Antilles: Net Foreign Assets of the Central Bank 1/
(In millions of NA guilders)

Source: Data provided by the Antillean authorities.
1/ Data exclude government foreign exchange deposits arising from Dutch financial support. Last observation January 2001.

Table 1. Netherlands Antilles: Selected Economic and Financial Indicators, 1996–2001

	1996	1997	1998	1999 Est.	2000 Est.	2001 Proj.
Real economy (change in percent)						
Real GDP 1/	2.4	1.4	-2.1	-1.9	-2.3	0.0
Cruise Tourism	12.8	33.2	0.3	-24.3	43.5	...
Stayover Tourism	-12.7	9.9	3.6	-2.0	-4.2	...
Per capita real GDP	0.8	1.6	-0.3	-0.8	-1.2	...
CPI	3.4	3.1	1.2	0.8	4.7	3.9
Unemployment rate (in percent) 2/	14.0	15.3	16.7	16.5	14.0	...
Public finances (percent of GDP) 3/						
Central government balance	-2.2	-1.1	-0.6	-1.9	-2.7	-2.0
General government balance	-3.8	-3.2	-2.4	-3.8	-3.2	-3.3
Public debt	60.9	60.8	67.1	72.6	69.8	68.1
Money and credit (end of year, change in percent)						
Reserve Money	-19.7	15.6	11.3	-7.1	8.2	3.9
Domestic credit	5.1	-0.6	0.4	8.3	4.7	1.9
Private sector	6.8	-0.6	1.6	10.3	5.6	-1.3
Government	-13.4	-1.2	-17.0	-24.0	-15.6	100.5
M2	-2.5	2.6	3.7	7.1	2.2	3.9
Interest rates (percent)						
Deposit rate (passbook)	3.7	3.7	3.6	3.6	3.6	...
Government bond yield	8.3	8.7	8.6	8.8	8.8	...
Balance of payments (percent of GDP)						
Trade balance	-43.4	-38.0	-36.9	-39.3	-39.8	-39.8
Current account	-10.2	-4.3	-4.0	-8.3	-8.4	-7.4
Reserves (US$ millions) 4/	189.0	214.0	248.0	265.0	260.7	288.7
(in months of merchandise imports)	1.5	1.9	2.2	2.2	2.1	2.3
Fund position	The Netherlands Antilles is part of the Kingdom of the Netherlands and does not have a separate quota.					
Exchange rate	The Netherlands Antilles guilder is pegged to the U.S. dollar at NA f. 1.79 = US$1					
Nominal effective rate (1995=100)	105.52	112.39	115.51	117.83	124.76	...
Real effective rate (1995=100)	103.40	109.13	110.02	107.73	110.35	...

Sources: Data provided by the Antillean authorities; and Fund staff estimates.

1/ National account statistics are not available for years after 1997, nor are GDP-deflators. The real GDP figures are Fund staff estimates.

2/ For 1998-2000, Curaçao only.

3/ The 1996 deficit includes one-time retroactive payments equivalent to 0.8 percent and 2.3 percent of GDP for the central government and the general government, respectively.

4/ Total reserves of the central bank, excluding gold, end of period.

Table 2. Netherlands Antilles: Structure and Performance of the Banking System, 1996–2000

	1996	1997	1998	1999	2000
Number of licensed banks	14	14	14	11	11
Of which : Majority state owned	1	1	1	1	1
As a percentage of total assets	3.0	3.5	3.8	5.0	5.6
Majority foreign owned (number)	2	2	2	2	2
As a percentage of total assets	3.6	5.7	5.4	7.1	7.4
Number of branches of foreign banks	4	4	4	3	3
As a percentage of total assets	25.9	24.5	24.9	22.9	23.1
Number of Banks accounting for:					
25 percent of total assets	1	1	1	1	1
75 percent of total assets	4	4	4	4	4
	(In percent of GDP, unless stated otherwise)				
Total assets	81.9	80.8	87.8	93.3	98.1
Total credit	55.1	53.6	55.9	61.0	62.5
Private sector credit	49.6	48.5	51.1	56.5	58.6
Total deposits excluding interbank	54.7	54.9	59.0	63.1	63.8
Corporate sector credit (in percent of total credit) 1/ 2/	56.3	55.7	55.2	56.1	55.7
Credit to households (in percent of total credit) 1/ 2/	40.9	42.6	42.9	41.4	41.1
	(In percent of total assets)				
Foreign currency denominated					
Assets	33.1	31.7	32.4	32.2	34.7
Balance sheet liabilities	31.1	29.8	29.1	30.5	32.9
Contingent and off-balance sheet accounts	8.8	9.3	8.6	8.8	7.4
	(In percent)				
Risk-weighted capital/asset ratio	9.1	10.7	8.4	10.3	8.9
Central bank credit to banks (in percent of GDP)	0.0	0.0	0.3	1.4	1.3
Average pretax profit on total assets	7.9	6.8	3.9	1.4	1.5
Nonperforming loans (in percent of total loans)	3.1	3.4	4.3	4.1	4.7
Provision for loan losses (in percent of nonperforming loans)	110	122	68	83	76
Money (M2) (change in percent, end of period)	-2.5	2.6	3.7	7.1	2.2
Private sector credit (change in percent, end of period) 1/	6.8	-0.6	1.6	10.3	5.6
Average lending spread (lending-deposit rate) 3/	8.4	8.9	8.7	5.8	4.8

Source: Data provided by the Antillean authorities; and Fund staff estimates.

1/ Extended by commercial banks only.

2/ Corporate sector: business loans + other mortgages. Households: consumer loans + individual mortgages.

3/ Interest rate on working capital loans - time deposit rate. Interest rates for prime borrowers are usually about two percentage points less, but no consistent time series is available. From 12/1999 lending rate is current account overdrafts.

Table 3. Netherlands Antilles: Balance of Payments, 1996–2003
(In millions of NA guilders)

	1996	1997	1998	1999	2000 Est.	Normative scenario 2001	2002	2003
Current Account	-451.2	-196.5	-175.9	-362.6	-374.4	-339.1	-257.4	-251.7
Trade Balance	-1,918.3	-1,723.4	-1,615.9	-1,709.3	-1,774.1	-1,811.2	-1,787.6	-1,851.4
Exports	712.2	775.0	796.7	749.2	892.9	854.1	902.1	938.7
Imports	2,630.5	2,498.4	2,412.6	2,458.5	2,667.0	2,665.3	2,689.8	2,790.2
Services balance	1,325.9	1,470.2	1,429.5	1,338.6	1,317.2	1,344.4	1,407.1	1,474.0
Earnings	2,360.6	2,408.8	2,530.3	2,620.4	2,762.2	2,865.1	2,968.4	3,086.9
Expenses	1,034.6	938.5	1,100.8	1,281.8	1,445.1	1,520.7	1,561.3	1,612.9
Transportation	204.4	215.4	187.9	187.2	159.5	163.3	169.0	176.6
Earnings	312.8	312.0	317.9	302.9	266.5	273.0	282.7	295.4
Expenses	108.4	96.6	130.1	115.7	107.0	109.7	113.7	118.8
Tourism	528.1	661.9	801.3	678.0	714.4	824.8	885.3	940.4
Earnings	984.0	1,117.6	1,343.9	1,363.3	1,493.3	1,603.6	1,690.8	1,780.9
Expenses	455.9	455.7	542.6	685.3	778.9	778.9	805.5	840.5
Other services	593.4	592.9	440.3	473.4	443.2	356.3	352.8	357.1
Earnings	1,063.8	979.2	868.4	954.3	1,002.5	988.5	994.9	1,010.6
Expenses	470.3	386.3	428.1	480.8	559.2	632.1	642.1	653.5
Income balance	113.6	22.0	67.9	12.4	41.0	80.6	79.6	86.0
Earnings	241.9	180.2	261.7	180.9	216.4	256.0	265.8	278.7
Expenses	128.3	158.1	193.8	168.4	175.5	175.5	186.2	192.7
Current transfers balance	27.6	34.7	-57.4	-4.3	41.5	47.2	43.5	39.6
Incoming transfers	310.9	308.2	255.3	324.0	396.7	422.7	442.5	463.6
Transfered abroad	283.3	273.5	312.6	328.4	355.1	375.5	399.0	423.9
Capital & Financial Account	446.1	205.0	170.0	343.2	374.1	109.8	172.6	214.1
Capital Account	126.9	134.4	155.2	193.6	20.6	120.1	132.4	144.6
Capital transfers balance	126.9	134.4	155.2	193.6	20.6	120.1	132.4	144.6
Incoming transfers	128.3	137.6	163.1	196.3	24.0	123.7	136.1	148.5
of which: development aid	114.0	127.1	148.4	182.0	19.4	100.0	110.0	120.0
Transfered abroad	1.5	3.1	7.9	2.6	3.4	3.6	3.7	3.9
Financial Account	319.2	70.6	14.8	149.5	353.6	-10.4	40.2	69.5
Direct Investment balance	11.2	28.0	13.0	17.0	18.6	19.3	60.1	142.7
Incoming capital	24.3	34.7	27.5	26.8	33.2	34.5	75.9	159.2
Outgoing capital	13.1	6.7	14.5	9.8	14.6	15.2	15.8	16.5
Portfolio investment balance	-54.5	16.4	-35.3	-18.3	-79.6	-70.6	-73.6	-106.5
Incoming capital	354.8	431.5	497.5	487.1	643.7	680.5	709.8	710.6
Outgoing capital	409.2	415.1	532.8	505.4	723.3	751.1	783.4	817.1
Other investment balance	266.1	75.9	172.4	128.8	329.0	90.9	103.7	93.3
Incoming capital	580.5	418.8	453.0	590.0	1,057.9	1,047.3	1,101.2	1,133.7
Outgoing capital	314.4	342.9	280.6	461.3	728.9	956.4	997.5	1,040.4
Change in reserves (-=increase) 1/	96.4	-49.7	-135.3	14.7	85.6	-50.0	-50.0	-60.0
Net Errors & Omissions 2/	5.1	-8.5	5.8	19.4	0.3	229.3	84.8	37.7
Official Reserves	338.3	386.9	443.6	458.3	466.7	516.7	566.7	626.7
In months of merchandise imports	1.5	1.9	2.2	2.2	2.1	2.3	2.5	2.7
Memorandum items:								
Current account balance (in percent of GDP)	-10.2	-4.3	-4.0	-8.3	-8.4	-7.4	-5.5	-5.2
Current account +FDI balance (in percent of GDP)	-9.9	-3.7	-3.7	-8.0	-8.0	-7.0	-4.2	-2.3

Source: Data provided by the Antillean authorities; and Fund staff estimates and projections.

1/ Including commercial banks, excluding gold revaluation.

2/ In projections, this comprises the financing gap.

Table 4. Netherlands Antilles: A Regional Perspective (Average 1994–98 unless otherwise indicated)

(In percent)

	Nominal GDP per capita (US$ thousands) 1998	Real GDP (change)	CPI inflation	Current account (share of GDP)	Consolidated public sector balance (share of GDP)	Grant receipts (share of GDP) 1998	Official reserves (months of GNFS imports) 1998	Prime lending rates 1998	Tax revenue (share of GDP) 1998	Wages and salaries (share of GDP) 1998
Netherlands Antilles	11,823	1.9	2.5	-5.0	-3.7	3.5	1.9	13.9	25.4	14.7
Antigua and Barbuda	8,833	3.5	1.9	-11.2	-5.4	1.5	1.4	10-13.5	17.6	11.6
The Bahamas	14,450	2.4	1.4	-10.3	-1.4	0.0	1.8	6.8	16.5	9.3
Barbados	8,212	4.0	2.2	3.5	0.6	0.2	2.5	10.4	30.0	10.9
Belize	2,820	2.4	2.3	-3.3	-4.3	1.2	1.2	16.5	19.7	10.2
Dominica	3,100	2.6	1.4	-12.3	-1.4	3.0	2.1	9-10.5	23.8	14.7
Grenada	3,209	4.5	1.9	-9.5	-2.4	4.7	2.2	10.5	22.7	11.4
Jamaica	2,604	-0.5	23.5	-2.4	-4.2	0.3	2.2	30.4	26.3	12.5
St. Kitts and Nevis	6,935	5.2	4.1	-22.0	-3.8	1.4	2.7	9.5-13	21.8	14.8
St. Lucia	4,013	2.7	2.8	-9.9	1.4	1.0	2.0	9.5-10.5	23.7	10.9
St. Vincent and the Grenadines	2,745	3.2	2.4	-15.3	-0.3	4.8	2.1	10-12.5	24.6	12.8
Trinidad and Tobago	4,596	4.1	5.0	-2.0	0.4	0.1	2.7	17.5	22.0	9.2
Venezuela	4,132	1.6	61.3	4.0	-3.5	...	7.0	46.4	10.6	3.7
Memorandum item:										
Netherlands	25,060	3.3	2.2	6.0	-2.3	...	1.2	6.5	24.0	10.1

Source: Data provided by the Antillean authorities; IMF, IFS; and Fund staff calculations.

Table 5. Netherlands Antilles: Indicators of External and Financial Vulnerability
(In percent of GDP, unless otherwise indicated)

	1996	1997	1998	1999	2000
External indicators					
Exports (annual percent change, in US dollars)	-0.1	3.6	4.5	1.3	8.5
Imports (annual percent change, in US dollars)	3.8	-6.2	2.2	6.5	9.9
Current account balance	-10.2	-4.3	-4.0	-8.3	-8.4
Official reserves (in US dollars, millions)	401.5	395.4	409.2	417.8	415.3
Reserves (incl. domestic banks; in US dollars, millions)	443.2	437.7	495.4	474.4	427.3
Official reserves (incl. gold) in months of imports (goods and services)	2.4	2.5	2.5	2.4	2.2
Broad money (M2) to official reserves (ratio)	3.5	3.7	3.7	3.9	4.0
Central bank foreign liabilities (in US dollars, millions)	10.4	8.4	1.4	0.5	1.7
Foreign assets of the banking sector 1/	0.40	0.40	0.47	0.47	...
Foreign liabilities of the banking sector 1/	0.40	0.39	0.42	0.45	...
Foreign assets of offshore banking units 1/	28.1	31.4	36.4	32.8	...
Foreign liabilities of offshore banking units 1/	26.3	29.4	33.8	30.0	...
External public debt (in US dollars, millions)	372.8	321.6	343.5	294.6	293.0
Exchange rate (per U.S. dollar, period average)	1.79	1.79	1.79	1.79	1.79
Financial Market Indicators					
Public sector debt	60.9	60.8	67.1	72.6	69.8
Public sector debt incl. guarantees	...	67.4	73.7	78.2	...
Government bond yield 2/	8.3	8.7	8.6	8.8	8.8
Government bond yield (real) 2/	4.9	5.6	7.4	8.0	4.0
Spread of government bond yield with the U.S. 2/	1.81	2.32	3.34	3.11	2.70
Financial Sector Risk Indicators 3/					
Mortgage credit to total assets (in percent)	...	30.7	26.9	29.7	...
Risk based capital-asset ratio	9.1	10.7	8.4	10.3	8.9

Sources: Data provided by the authorities, and IMF, International Financial Statistics.

1/ In billions of U.S. dollars.

2/ For 2000: July.

3/ Domestic banking sector only.

Table 6. Netherlands Antilles: Operations of the General Government
(In percent of GDP)

	1996	1997	1998	1999	2000	Normative scenario 2001	2002	2003
Total revenue	29.0	28.0	29.1	27.0	27.5	27.9	27.5	27.4
Tax revenue	24.5	24.7	25.4	23.9	24.6	25.0	24.6	24.4
Taxes on income and profits	14.9	13.6	13.9	13.0	11.5	12.0	11.5	11.5
Taxes on property	0.8	0.9	0.8	0.9	1.0	1.0	0.8	0.7
Taxes on goods and services	5.0	7.3	7.6	6.5	9.0	8.9	9.1	9.1
Of which: Sales and turnover tax	0.9	2.8	3.2	2.4	5.2	5.2	5.4	5.4
Taxes on international transactions	3.7	2.7	3.0	3.3	2.9	3.0	2.9	2.9
Other taxes	0.2	0.2	0.2	0.2	0.2	0.2	0.2	0.2
Nontax revenue	4.3	3.2	3.5	2.9	2.6	2.6	2.7	2.7
Capital revenue	0.0	0.0	0.0	0.0	0.0	0.1	0.0	0.0
Grants 1/	0.2	0.2	0.2	0.2	0.2	0.3	0.3	0.3
Total expenditure	32.9	31.2	31.5	30.8	30.7	32.8	30.3	29.3
Current expenditure	31.2	30.0	31.2	29.9	29.2	30.8	29.2	28.1
Wages and salaries	16.2	15.1	14.7	14.4	12.6	10.5	10.2	10.0
Excl. pension premiums	12.6	11.4	11.6	11.8	10.2	8.1	7.9	7.7
Pension premiums 2/	3.6	3.7	3.1	2.6	2.5	2.4	2.3	2.2
Goods and services	6.7	6.6	7.1	7.2	6.8	7.5	6.9	6.7
Subsidies to enterprises	2.2	2.0	1.8	1.5	1.4	1.3	1.2	1.2
Transfers 1/ 3/	3.2	3.0	3.9	3.4	4.8	6.5	6.2	5.6
Interest payments	2.9	3.3	3.8	3.5	3.6	5.0	4.7	4.6
Capital expenditure	1.7	1.2	0.2	0.9	1.5	1.6	0.9	0.9
Investment	0.9	1.1	0.9	0.9	0.6	0.7	0.7	0.7
Capital transfers and net lending	0.7	0.1	-0.6	0.0	0.9	0.9	0.2	0.2
Contingency	...	...	...	...	...	0.3	0.1	0.1
Sinking fund	...	...	...	...	...	0.1	0.1	0.1
Balance before additional measures	-3.8	-3.2	-2.4	-3.8	-3.2	-5.0	-2.8	-1.9
Additional measures	...	...	...	...	...	-1.7	-1.2	-0.9
Balance after additional measures	-3.8	-3.2	-2.4	-3.8	-3.2	-3.3	-1.6	-1.0
Financing	3.8	3.2	2.4	3.8	3.2	3.3	1.6	1.0
Domestic	4.3	3.7	2.7	4.0	0.1	-2.8	0.4	0.8
Monetary financing	-0.5	-0.1	-0.5	1.2	0.5	0.0	0.0	0.0
Arrears APNA	0.3	2.0	0.4	2.0	0.4	-0.6	0.0	0.0
Other arrears	0.0	0.0	0.0	0.6	0.0	-0.4	0.0	0.0
Other domestic	4.5	1.9	2.7	0.1	-0.7	-1.8	0.4	0.8
Foreign	-0.1	0.0	0.0	0.0	0.8	-0.5	-0.7	-0.7
Amortization payments	-0.1	0.0	0.0	0.0	0.0	-0.7	-0.7	-0.7
Other foreign	0.0	0.0	0.0	0.0	0.8	0.2	0.0	0.0
Discrepancy/program financing	-0.3	-0.5	-0.3	-0.1	2.3	6.5	1.8	0.8
Memorandum Item:								
Primary balance	-1.0	0.1	1.4	-0.4	0.4	1.7	3.2	3.7
Debt/GDP ratio 4/	60.9	60.8	67.1	72.6	69.8	68.1	67.4	66.0

Sources: Data provided by the authorities; and Fund staff projections.

1/ Net of transfers between different levels of government.

2/ Pensions premiums due (including non-paid amounts).

3/ The sharp increase in 2000 and 2001 mainly reflects the severance payments to dismissed civil servants, which is also reflected in reduced wage and salary costs.

4/ Including amortization arrears on loans extended by the Netherlands.

Table 7. Netherlands Antilles: Medium-Term Macroeconomic Framework, 1996–2003

	1996	1997	1998	1999	2000 Est.	Normative scenario 2001	2002	2003
	(Percentage change)							
Real GDP growth	2.4	1.4	-2.1	-1.9	-2.3	0.0	1.0	2.0
GDP deflator	2.2	1.2	-1.4	1.1	5.0	2.2	1.3	1.5
CPI	3.4	3.1	1.2	0.8	4.7	3.9	2.5	2.5
Broad money	-2.5	2.6	3.7	7.1	2.2	3.9	4.2	5.0
Domestic credit	5.1	-0.6	0.4	8.3	4.7	1.9	2.8	3.4
Of which: Private sector	6.8	-0.6	1.6	10.3	5.6	-1.3	3.0	3.6
	(In percent of GDP)							
General government								
Total revenue	29.0	28.0	29.1	27.0	27.5	27.9	27.5	27.4
Of which: Tax revenue	24.5	24.7	25.4	23.9	24.6	25.0	24.6	24.4
Total expenditure	32.9	31.2	31.5	30.8	30.7	32.8	30.3	29.3
Of which: Wages	16.2	15.1	14.7	14.4	12.6	10.5	10.2	10.0
Of which: Interest	2.9	3.3	3.8	3.5	3.6	5.0	4.7	4.6
Of which: Investment	0.9	1.1	0.9	0.9	0.6	0.7	0.7	0.7
Overall balance before additional measures	-3.8	-3.2	-2.4	-3.8	-3.2	-5.0	-2.8	-1.9
Additional Measures	0.0	0.0	0.0	0.0	0.0	-1.7	-1.2	-0.9
Overall balance	-3.8	-3.2	-2.4	-3.8	-3.2	-3.3	-1.6	-1.0
Primary balance	-1.0	0.1	1.4	-0.4	0.4	1.7	3.2	3.7
Financing	3.8	3.2	2.4	3.8	3.2	3.3	1.6	1.0
Domestic	4.3	3.7	2.7	4.0	0.1	-2.8	0.4	0.8
Foreign	-0.1	0.0	0.0	0.0	0.8	-0.5	-0.7	-0.7
Discrepancy/program financing	-0.3	-0.5	-0.3	-0.1	2.3	6.5	1.8	0.8
Total government debt	60.9	60.8	67.1	72.6	69.8	68.1	67.4	66.0
Balance of payments								
Exports of goods and nonfactor services	69.5	70.2	76.0	77.6	82.0	81.6	83.0	83.4
Imports of goods and nonfactor services	82.9	75.8	80.2	86.1	92.3	91.9	91.2	91.2
Foreign balance	-13.4	-5.6	-4.3	-8.5	-10.3	-10.2	-8.2	-7.8
Current account	-10.2	-4.3	-4.0	-8.3	-8.4	-7.4	-5.5	-5.2
Private sector net savings	-6.4	-1.1	-1.6	-4.5	-5.2	-4.1	-3.9	-4.3

Sources: Data provided by the Antillean authorities; and Fund staff projections.

Table 8. Netherlands Antilles: Monetary Survey, 1996–2003

	1996 Dec	1997 Dec	1998 Dec	1999 Dec	2000 Dec	Normative scenario 2001 Dec	2002 Dec	2003 Dec
	(In millions of NA guilders, end of period)							
Net foreign assets 1/	524.6	584.6	714.1	693.9	575.6	625.6	675.6	735.6
of which NIR:	602.4	652.1	777.7	762.9	636.4	686.4	736.4	796.4
Net domestic assets 1/	2,012.1	2,017.4	1,984.5	2,197.4	2,379.4	2,445.7	2,525.4	2,624.2
Domestic credit	2,443.8	2,429.0	2,437.6	2,640.9	2,765.8	2,819.1	2,898.8	2,997.6
Government (net)	168.0	166.0	137.8	104.7	88.4	177.2	177.2	177.2
Private sector	2,275.8	2,263.0	2,299.8	2,536.2	2,677.4	2,641.9	2,721.6	2,820.4
Other items, net 1/	-431.7	-411.6	-453.1	-443.5	-386.4	-373.4	-373.4	-373.4
Money and quasi-money	2,536.7	2,602.0	2,698.6	2,891.3	2,955.0	3,071.3	3,201.0	3,359.8
Money	1,028.4	1,052.7	1,075.2	1,187.1	1,155.5	1,224.0	1,289.3	1,339.6
Quasi-money	1,508.3	1,549.3	1,623.4	1,704.2	1,799.5	1,847.3	1,911.7	2,020.2
	(Changes in percent from end of previous year)							
Net foreign assets	-26.9	11.4	22.2	-2.8	-17.0	8.7	8.0	8.9
Net domestic assets	6.8	0.3	-1.6	10.7	8.3	2.8	3.3	3.9
Domestic credit	5.1	-0.6	0.4	8.3	4.7	1.9	2.8	3.4
Government (net)	-13.4	-1.2	-17.0	-24.0	-15.6	100.5	0.0	0.0
Private sector	6.8	-0.6	1.6	10.3	5.6	-1.3	3.0	3.6
Money and quasi-money	-2.5	2.6	3.7	7.1	2.2	3.9	4.2	5.0
	(Changes in percent of beginning-of-period broad money)							
Net foreign assets	-7.4	2.4	5.0	-0.7	-4.1	1.7	1.6	1.9
Net domestic assets	4.9	0.2	-1.3	7.9	6.3	2.2	2.6	3.1
Domestic credit	4.6	-0.6	0.3	7.5	4.3	1.8	2.6	3.1
Government (net)	-1.0	-0.1	-1.1	-1.2	-0.6	3.0	0.0	0.0
Private sector	5.6	-0.5	1.4	8.8	4.9	-1.2	2.6	3.1
Money and quasi-money	-2.5	2.6	3.7	7.1	2.2	3.9	4.2	5.0

Sources: Bank van de Nederlandse Antillen; and Fund staff projections.

1/ Includes gold revaluations from NA f. 189.5 million in January 1996 to NA f. 179.8 in November 1998 and to NA f. 138.9 million in December 2000.

Kingdom of the Netherlands—Netherlands Antilles: Fund Relations

The Netherlands Antilles is part of the Kingdom of the Netherlands and does not have a separate quota, nor other financial relationships with the Fund. Since January 1, 1986, when Aruba split from the Netherlands Antilles, the Kingdom of the Netherlands consists of the Netherlands itself, the Netherlands Antilles, and Aruba. The Kingdom of the Netherlands is an original member of the Fund. On February 15, 1961, the Kingdom formally accepted the obligations of Article VIII, Sections 2, 3, and 4 of the Fund Agreement for all its territories. The initial par value of the Netherlands Antillean guilder—NA f. 1.88585 = US$1—was established with the Fund on December 18, 1946. The authorities communicated to the Fund a rate of NA f. 1.79 per US$1 to take effect as a central rate on December 23, 1971. Since then, the Netherlands Antillean guilder has been pegged to the U.S. dollar at this rate.

The Fund's Statistics Department provided technical assistance on balance of payments statistics and on money and banking statistics in October 1997 and December 1997, respectively. The Monetary and Exchange Affairs Department provided assistance on a self-assessment of supervision of the offshore financial sector in November 2000 and March 2001. The Fiscal Affairs Department assessed the pension system and the civil servants' pension fund in February 2001.

A Fund resident representative was present in Willemstad from October 1, 1996 to August 31, 1998. The costs of this position were borne by the Dutch authorities.

The Executive Board conducted the last Article IV consultation discussions for the Netherlands Antilles on June 7, 1999 (EBM/99/60) on the basis of staff report SM/99/106 (05/10/99) and Selected Issues and Statistical Appendix paper SM/99/113.

Kingdom of the Netherlands—Netherlands Antilles: World Bank Relations

The Netherlands Antilles is part of the Kingdom of the Netherlands and is not eligible for support from the World Bank Group. Nonetheless, at the request of the Antillean and Dutch authorities the World Bank Group provides technical assistance on an exceptional basis and paid for by the Netherlands.

In February 2000, an IFC team assessed the prospects of the national airline (ALM), advising the authorities on the relative merits of the options of privatizing ALM as a going concern and taking ALM through receivership.

In November 2000, FIAS (Foreign Investment Advisory Services) held an exploratory visit to identify the areas where further assistance needs are most pressing. A follow-up mission took place in February 2001 and a report with recommendations on eliminating red tape, simplifying business regulations, and providing investment incentives is expected to be ready by end-April 2001.

In December 2000, a World Bank mission made a broad assessment of the problems of the Netherlands Antilles and elaborated a broad reform agenda entitled "Elements of a Strategy for Economic Recovery and Sustainable Growth." Its findings as well as a follow-up program were discussed with the authorities in March 2001. The Bank stressed the need for infrastructure projects to help revive the economy and the prospects of the tourism sector for the near term. The Bank offered its services on a wide range of issues, including public expenditure and tax reform, identification of priority investment projects, privatization, labor market reform, and improving domestic financial intermediation.

Kingdom of the Netherlands—Netherlands Antilles: Statistical Issues

After significant progress from 1995 to mid-99, further improvements in statistics of the Netherlands Antilles, especially on the real sector, were delayed by a fiscal crisis and attendant budget cuts. In late 2000 progress resumed, but data problems continue to hamper effective assessment of economic conditions. Most data are published with considerable lags, and are often subject to measurement errors and large revisions. The frequency and timeliness of data availability of the core statistical indicators are shown in the attached table. A new quarterly publication of the Central Bureau of Statistics (CBS), initiated in 1996, has significantly improved the publicity of the research conducted by CBS. The central bank (BNA) continues to provide comprehensive reviews of the economy in its Annual Reports, Quarterly Bulletins, and through data disseminated on its website. The authorities have made a commitment to adopt the GDDS. In December 2000, both the CBS and BNA adopted data release calendars and signed a detailed protocol of cooperation on statistics. A plan has been drawn up to reduce overlap between agencies collecting and processing statistics.

Final **national accounts** are available until 1997, only at current prices, and only on the production and expenditure sides. Preliminary national accounts estimates from the production side are available through 1999. Since no deflators are calculated in the official data, it is difficult to assess real growth of the economy. Recently, the Central Bureau of Statistics (CBS) has begun to publish estimates of real GDP growth and projections for the current year on the basis of selected indicators of production and trade. The BNA conducts a quarterly business survey used for flash estimates of economic growth. Private sector **employment** figures—based on annual surveys of the labor market—are subject to large revisions, while for government employment several, inconsistent series are available.

The national **consumer price index** is generally adequate and published with a lag of two months by the CBS, while the separate consumer price indices for each of the three main islands are published by the BNA on its website with a longer lag. A consistent time series on **wages** is available in a timely manner only for minimum wages and wages in public enterprises, while economy-wide wage data are available for Curaçao only, but with a considerable time lag. Although data are available for the aggregate wage bill of the various levels of government, uncertainty surrounding the actual number of civil servants makes it very difficult to infer average wage developments.

Significant steps were taken by the central government and island government of Curaçao in 1996 and 1997 to improve expenditure monitoring and reporting of data on **public finances**. As a result, expenditures are now no longer only registered in the year that they were appropriated, but also in the year that they took place, and data on the cash budget execution is publicly available, with some lag. Following the departure of the Fund's resident representative in 1997, the lag with which the Island Government of Curaçao's monthly accounts become available steadily increased. Since September 2000, reporting has improved and the lag has been reduced to about 6 weeks. To obtain a fully consolidated picture of the public sector, the coverage of data reporting needs to be extended to the other islands and several autonomous public institutions. Disagreement between the various government bodies concerning their mutual financial obligations has led to inconsistent reporting. These issues are expected to be resolved during the first half of 2001.

Monetary and financial statistics are published in the BNA's Quarterly Bulletin with a lag of six months, but summary indicators are published on the central bank's website with a two-three month delay, and data in ***International Financial Statistics*** are timely and published 3 months after the reference period. A money and banking statistics mission from the Statistics Department visited the Netherlands Antilles in December 1997. Most of its recommendations have been implemented and have led to substantive improvements in data and reporting, starting with end-1998 data. Until the introduction of a new Chart of Accounts in 2000, the BNA used an interim method, as suggested by the technical assistance mission, to ensure that reporting is done on a gross rather than a net basis to avoid underestimation of money and credit. A broadening of the coverage of the monetary statistics to include non-bank deposit taking institutions (e.g., credit unions, savings institutions) has been initiated, but is not complete. The recommendations to exclude foreign currency deposits from the definition of narrow money (M1) and to limit the concept of international reserves to foreign exchange reserves of the BNA only have not been implemented. It should be noted, however, that sufficiently detailed information is published to allow the determination of these concepts.

The BNA collects **balance of payments** statistics primarily on the basis of exchange records, with supplementary information provided by foreign bank account holders, and an enterprise survey. All companies without a general exemption to obtain a license for their foreign exchange transactions, report these transactions monthly through their domestic banks to the central bank. Those companies that have obtained a general exemption for approval of their foreign exchange transactions submit data on transactions quarterly directly to the central bank. An October 1997 balance of payments statistics mission from the Statistics Department recommended the use of additional data sources, in particular from the direct investment survey and the Ministry of Finance (for data on grants and external debt). It was recommended that the Customs Office finalize the implementation of the Automated System for Customs Data, to improve the accuracy and timeliness of trade statistics and that a Balance of Payments Section be created within the BNA. Implementation of these recommendations was initiated in early 1999 with the appointment of a head for this section, and significant progress has been made since then. In late 2000, the balance of payments presentation was switched to coincide with the fifth edition of the manual, but some teething problems remain. In any case, the small size and undiversified nature of the economy impart considerably volatility to individual items, making it difficult to interpret the statistics. In addition, the diversified and ever-changing structure of the offshore sector makes an appropriate classification of in- and outflows problematic.

Kingdom of the Netherlands—Netherlands Antilles: Core Statistical Indicators as of End-March, 2001

	Exchange Rates 1/	International Reserves	Central Bank Balance Sheet	Reserve/ Base Money	Broad Money	Interest Rates	Consumer Price Index	Exports/ Imports	Current Account Balance	External Public Debt	Overall Government Balance/Debt Service 2/	GDP/GNP
Date of Latest Observation	3/31/01	2/28/01	2/28/01	2/28/01	1/31/01	1/31/01	1/01	2000Q3	2000Q3	01/01	01/01	1997
Date Received	3/31/01	3/15/01	3/15/01	3/15/01	3/15/01	3/15/01	3/01	2/15/01	2/15/01	3/15/01	3/15/01	12/2000
Frequency of Data	daily	weekly	monthly	monthly	monthly	monthly	monthly	quarterly	quarterly	quarterly	monthly	annual
Frequency of Reporting	daily	weekly	monthly	monthly	monthly	monthly	monthly	quarterly	quarterly	irregular	monthly	Annual
Source of Update	Bloomberg	BNA 3/	BNA	BNA	BNA	BNA	CBS 4/	BNA	BNA	BNA	Treasury	CBS
Mode of Reporting	electronic	mail	fax	fax	website	website	publication	electronic	electronic	mission	electronic/ mail	publication
Confidentiality	no	no	yes	no	no	no	no	no	no	no	no	no
Frequency of Publication	daily	weekly	n.a.	monthly	monthly	monthly	monthly	irregular	irregular	irregular	n.a.	annual

1/ Fixed exchange rate against the U.S. dollar since 1986; the Fund would be notified of a parity change.
2/ Including external.
3/ BNA = Bank van de Nederlandse Antillen (central bank).
4/ CBS = Central Bureau of Statistics.

Kingdom of the Netherlands—Netherlands Antilles: Selected Social Indicators

Area	
Size	800 sq. km.
Population per sq. km. (end 1998)	259
Population characteristics	
Total population (end 1998)	206,981
Population growth (in percent, 1998)	-1.0
Population age structure (in percent, 1998)	
0-14	26
15-60	63
60 and over	11
Life expectancy at birth (in years, 1986-91)	
Male	71.8
Female	77.7
Live birth rate (per thousand, 1998)	15
Crude death rate (per thousand, 1997)	6
Per capita income (1999)	US$12,120

Source: Central Bureau of Statistics.

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IMF Concludes Article IV Consultation Discussions with the Kingdom of the Netherlands—Netherlands Antilles

On May 7, 2001, the Executive Board of the International Monetary Fund (IMF) concluded the Article IV consultation discussions with the Kingdom of the Netherlands—Netherlands Antilles.[1]

Background

Traditionally based on financial offshore and oil refining inflows and tourism, the Antillean economy is relatively undiversified and has suffered from the decline of these inflows during the past 15 years and the high incidence of hurricanes in the 1990s. Adjustment to these shocks has been hampered by labor and product market rigidities, high administrative and tax burdens, and inefficiencies in public enterprises. Moreover, by the mid-1990s budget deficits increased to levels that could only be financed through arrears to the civil servants' pension fund and the Netherlands, leading to an erosion of investor confidence. Consequently, the economy has been in recession during 1998-2000, unemployment has risen sharply, and many people have emigrated. Even though headline inflation accelerated briefly in 2000 due to indirect tax and energy price increases, the peg to the U.S. dollar has kept underlying inflation low. Competitiveness has suffered and the balance of payments and the budget have been supported by sizable official capital inflows.

Fiscal adjustment undertaken since late 1999 has so far included the following measures: an increase in the turnover tax from 2 percent to 5 percent, the reversal of the 1998 tax relief package, the dismissal of some 20 percent of civil servants, and the suspension of vacation allowances and salary increases in the civil service. However, a weaker economy, high

[1] Under Article IV of the IMF's Articles of Agreement, the IMF holds bilateral discussions with members, usually every year. A staff team visits the country, collects economic and financial information, and discusses with officials the country's economic developments and policies. On return to headquarters, the staff prepares a report, which forms the basis for discussion by the Executive Board. At the conclusion of the discussion, the Managing Director, as Chairman of the Board, summarizes the views of Executive Directors, and this summary is transmitted to the country's authorities. This PIN summarizes the views of the Executive Board as expressed during the May 7, 2001 Executive Board discussion based on the staff report.

severance payments, delays in settling outstanding claims and arrears, and disruptions of tax administration, implied that the overall budget deficit in 2000 still exceeded available financing. With most of these problems also affecting this year's budget, the planned reduction in the deficit to less than 2 percent of GDP is not forthcoming. Instead, without additional measures it is likely to rise to 5 percent of GDP.

For the past three decades, the key monetary policy target has been the exchange rate peg to the U.S. dollar. In 1999, reserve requirements replaced quantitative controls as the preferred instrument of monetary policy, but ceilings on bank credit to the government nonetheless remained in place. Some banks are, however, not complying with the reserve requirement. In response to deteriorating loan performance, the central bank has intensified supervision over the financial system.

During the past year, several structural reforms have been implemented. A drastic streamlining of the public sector is nearing completion. Labor market rigidities have been tackled by the abolition of the dismissal permit and more flexible application of the work week. Import quotas and production monopolies have been abolished, and the market protection regime is being phased out. A framework for privatization and legislation supporting the development of electronic commerce have been adopted. With respect to the international financial sector, commitments have been made to adhere to international guidelines regarding harmful tax competition and a self-assessment of supervision of the sector has been initiated.

Executive Board Assessment

Executive Directors noted that the Netherlands Antilles' economic performance has weakened since the mid-1990s, reflecting declines in the offshore and oil refining sectors and hurricane damage. A prolonged recession, high unemployment, a pick-up in inflation, and a tide of emigration have ensued. Directors considered that a fuller and more sustained response to the exogenous shocks would have been appropriate. At the same time, they recognized that policymakers had to deal with the small size and undiversified nature of the Antillean economy, as well as with the possibility that residents had of emigrating to the Netherlands. Directors regarded a combination of structural reform, well-targeted public investments, and determined pursuit of macroeconomic stability as critical preconditions for sustained economic growth and job creation. They urged the authorities to reinvigorate adjustment efforts, building on progress made since late 1999.

Directors recognized the authorities' efforts to address the deteriorating fiscal situation. They generally considered that fiscal policy should avoid giving a contractionary impulse in the short term, but also underscored the need to prevent the budget deficit from rising above last year's level of 3.25 percent of GDP, by improving tax collection and reducing spending. Even with the deficit contained, considerable financial support from the Netherlands will still be required. Directors observed that, to be effective, such support should be phased in line with the implementation of the authorities' adjustment program.

Directors supported the authorities' medium-term objective of achieving budget balance, with public investment continuing to be largely financed by development assistance. Directors encouraged the authorities to simplify the tax system, starting in the 2002 budget, and to reconsider spending priorities so as to facilitate a reduction in the tax burden while redirecting spending to development purposes. They commended ongoing steps to reform the civil service. Directors observed that medium-term fiscal sustainability would require the extension of budget discipline throughout the broader public sector, settlement of all intergovernmental debt and arrears, and successful pension and health care reforms. Directors encouraged early implementation of plans to privatize the public pension fund.

Directors noted that the long-standing exchange rate peg to the U.S. dollar had kept inflation low. They supported the continuation of the peg at its current level and urged the authorities to improve competitiveness through structural reforms. With regard to the banking system, Directors noted that the lack of competition and absence of secondary markets hampered the conduct of monetary policy. They emphasized the need to ensure compliance with monetary policy requirements and welcomed the strengthened supervision of the domestic and international financial sectors, notably with regard to nonperforming loans and more frequent on-site inspections of the domestic financial sector. Directors welcomed the authorities' intention to complete a Fund-assisted self-assessment of supervision in the offshore financial sector in the near term. They praised the authorities' efforts to combat money laundering and encouraged continued focus on this issue.

Following the progress made so far, Directors emphasized the need to improve the functioning of the labor and product markets, including through more efficient provision of public services, and to continue to pursue trade liberalization. Directors highlighted the desirability of cutting the administrative and regulatory burdens on the private sector, not overburdening public enterprises with incompatible objectives, addressing domestic skills shortages through all available means, and expediting the passage into law of competition and regulatory frameworks.

While welcoming the authorities' commitment to adopt the GDDS as a framework to improve statistics, Directors called on the authorities to address data weaknesses, in particular by broadening the coverage of public sector data and accelerating the provision of data on the national accounts and the balance of payments.

Public Information Notices (PINs) are issued, (i) at the request of a member country, following the conclusion of the Article IV consultation for countries seeking to make known the views of the IMF to the public. This action is intended to strengthen IMF surveillance over the economic policies of member countries by increasing the transparency of the IMF's assessment of these policies; and (ii) following policy discussions in the Executive Board at the decision of the Board.

Netherlands Antilles: Selected Economic Indicators

	1997	1998	1999	2000
	(Percent change[1])			
Domestic Economy				
Real GDP	1.4	-2.1	-1.9	-2.3
Unemployment rate (in percent of labor force)[2]	15.3	16.7	16.5	14.0
Consumer prices (period average)	3.1	1.2	0.8	4.7
Money, credit, and interest rates				
Broad money	2.6	3.7	7.1	2.2
Domestic credit	-0.6	0.4	8.3	4.7
Interest rate on 12 month deposits (in percent)	3.7	3.6	3.6	3.6
Government bond yield (in percent)	8.7	8.6	8.8	8.8
Exchange rates				
Exchange rate regime	Fixed exchange rate at 1.7895 NA guilder/U.S.dollar since December 23, 1971			
Real effective exchange rate[3]	5.5	0.8	-2.1	2.4
Public Finance (in percent of GDP)				
General government balance	-3.2	-2.4	-3.8	-3.2
Public debt	60.8	67.1	72.6	69.8
Balance of payments				
Current account balance (in percent of GDP)	-4.3	-4.0	-8.3	-8.4
Trade balance (in percent of GDP)	-38.0	-36.9	-39.3	-39.8
Official reserves (in millions of U.S. dollars)[4]	214	248	265	261
Official reserves (in months of merchandise imports)[4]	1.9	2.2	2.2	2.1

Sources: Data provided by the authorities; and IMF staff estimates.
[1]Unless otherwise noted.
[2]Curacao only in 1998 to 2000.
[3](+) = appreciation.
[4]Reserves of the central bank, excluding gold, end of period.