

# NOTE ECONOMIC DEVELOPMENTS CURAÇAO

DECEMBER 2018

CENTRALE BANK VAN CURAÇAO EN  
SINT MAARTEN





# Centrale Bank van Curaçao en Sint Maarten

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December 2018

Simon Bolivar Plein 1  
Willemstad,  
Curaçao  
Phone: (599 9) 434-5500  
Fax: (599 9) 461-5004  
E-mail: [info@centralbank.cw](mailto:info@centralbank.cw)

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## GENERAL ECONOMIC DEVELOPMENTS

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According to preliminary figures of the CBCS, Curacao's real GDP contracted further by 1.9% in 2018, following a decline of 1.7% in 2017. Meanwhile, consumer price inflation rose to 2.4% in 2018, reflecting mainly an increase in international oil and food prices.

An analysis of the GDP by expenditure shows that the expected economic contraction in 2018 was caused by a decrease in both net foreign and domestic demand. The decline in net foreign demand was the result of a drop in exports combined with higher imports. In addition, domestic demand shrank as both private and public spending contracted. Private spending went down on the back of lower private consumption while private investment remained muted. Consumer spending dropped as a result of, among other things, a decline in disposable income because of the higher inflationary pressures and a worsened labor market. Furthermore, public spending dropped because of a decrease in both government investment and consumption. Public investment declined as the construction of the new hospital is reaching its final stages and because of fewer road infrastructure projects. The lower public consumption was caused by lower disbursements on goods & services and on wages & salaries.

A review of GDP by sector shows that the decline in private sector activities during the

first half of 2018 was attributable mainly to the transport, storage, & communication, manufacturing, construction, financial intermediation, and wholesale & retail trade sectors, mitigated by an increase in the activities in the utilities and restaurants & hotels sectors.

Real value added contracted in the transport, storage & communication sector in the first half of 2018 as a result of a decline in both harbor and airport-related activities. The poor performance of the harbor was the result of a significant drop in the number of ships piloted into the port of Curaçao, notably freighters and tankers. The decline in the number of tankers was largely related to the headwinds the refinery was facing. Meanwhile, airport-related activities dropped due to lower total passenger traffic mitigated by an increase in the number of commercial landings. The increase in commercial landings was the result of additional flights by various air carriers, including KLM, TUI, American Airlines, Copa Airlines, Jet Blue, West Jet, and Fly Always.

Real output in the manufacturing sector shrank in the first six months of 2018, primarily because of lower refining activities at the Isla refinery. The decline in crude oil supply from Venezuela, the seizure of the PDVSA assets by the American oil company ConocoPhillips, and the limited steam deliveries by the

CRU plant resulted in lower production activities at the refinery. The construction sector also posted negative results because several major construction projects were finished or in their final stages.

The negative contribution of the financial intermediation sector to real GDP during the first half of 2018 was the result of a drop in real value added of both the domestic and international financial services. The decline in domestic financial services reflected a drop in net interest income of the commercial banks, moderated by an increase in other fees & income. Meanwhile, lower wages & salaries and other operational expenses reflected the decline of the international financial services.

Furthermore, the wholesale & retail trade sector recorded a contraction in the first six months of 2018 due to fewer activities in the free zone and less domestic demand, moderated by an increase in tourism spending.

By contrast, the restaurants & hotels and utilities sectors contributed positively to GDP in the first half of 2018. Growth in the restaurants & hotels sector reflected an increase in the number of stay-over visitors, the number of visitor nights, the occupancy rate, and the number of cruise tourists. The number of stay-over visitors increased mainly because of more visitors from North America and Europe, specifically the United States, Canada, and the Netherlands. The South American and Caribbean markets declined largely because of the lack of airlift to regional destinations due to the cancellation of flights by InselAir and the continued crisis in Venezuela. The buoyant performance of

cruise tourism was related to the opening of the second mega pier and a change in itineraries by cruise lines because of the devastation caused by hurricanes Irma and Maria in popular cruise destinations in the Caribbean. The hotel occupancy rate rose also but probably reflected the increase in the number of visitors combined with fewer available hotel rooms attributable to the closure or renovation of several hotels.<sup>1</sup>

Finally, the gain in the utilities sector was supported by more water and electricity production in the first six months of 2018 compared to the first six months of 2017.

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<sup>1</sup> The Marriott Beach Resort & Casino has been temporary closed for renovation, while the Plaza Hotel Curaçao and Howard Johnson Curaçao were closed.

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## DEVELOPMENTS IN THE PUBLIC FINANCES

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During the January-June period of 2018, the government of Curaçao registered a surplus of NAf.8.0 million on its current budget, a turnaround compared to the deficit of NAf.39.7 million recorded during the first half of 2017.<sup>2</sup> The improved fiscal position was the result of a decline in government expenditures (34.0%) that surpassed the drop in revenues (31.4%). However, this development was to a great extent the result of a decision by the government of Curaçao to no longer include the income and expenditures of the social security bank, SVB, in the current budget.<sup>3</sup> As a result of this correction, nontax revenues dropped by 83.1% while on the expenditure side, the category “transfers & subsidies” registered a decline of 58.2%.

When the income and expenditures of the SVB are also excluded in 2017, the government of Curaçao recorded a surplus of NAf.154.6 million on its current budget during the first half of 2018, up from the NAf.106.2 million surplus registered during the first half

of 2017. This improvement was caused by an increase in government revenues (3.6%) combined with lower expenditures (-2.9%). The rise in government revenues stemmed primarily from an increase in nontax revenues reflecting a windfall in withholding tax grants related to the BRNC tax arrangement between the Netherlands and Curaçao.<sup>4</sup> Meanwhile, tax revenues remained practically unchanged during the January – June period of 2018 compared to the first half of 2017. The decline on the expenditures side was largely the result of lower outlays on transfers & subsidies due to fewer transfers to public companies and institutions.

The outstanding public debt of Curaçao amounted to NAf.2.815 billion at the end of the first half of 2018, an increase of NAf.9.0 million compared to the end of 2017. The domestic debt component contributed to this increase, which went up by NAf.16.7 million due mainly to higher arrears towards the social security bank, SVB. Meanwhile, the foreign debt component dropped by NAf.7.7 million to NAf.2.339 billion, caused by an amortization of a sinking bond issued in January 2015 for the financing of the new hospital. Despite the rise in total debt, Curaçao’s debt-to-GDP

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<sup>2</sup> Source: *Financiële Management Rapportage of the government of Curaçao of June 2018.*

<sup>3</sup> Based on advice from the government’s auditor (SOAB), the government of Curaçao decided to no longer consolidate the expenditures and income of the social security bank, SVB, in the government’s current budget. In May 2018, the government excluded all income and expenditures of the SVB over the period January – April 2018 from its current budget. In addition, as of May 2018, SVB income and expenditures are no longer included in the budget.

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<sup>4</sup> As part of the BRNC (Belastingregeling Nederland-Curaçao) tax arrangement, all withholding tax collected on dividends paid by Dutch companies to their parent companies in Curaçao is transferred to the government of Curaçao.

ratio dropped slightly from 50.3% at the end of 2017 to 50.1% at the end of 2018's first half because nominal GDP increased at a faster pace than the public debt.

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## DEVELOPMENTS IN THE BALANCE OF PAYMENTS

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The deficit on the current account of the balance of payments widened by NAf.262.6 million in the first half of 2018 compared to the first half of 2017 as a result of a large drop in the net export of goods and services. In addition, the income balance deteriorated while the current transfers balance improved. As the external financing into the monetary union was more than sufficient to cover the current account deficit, the gross official reserves of the Bank grew by NAf.61.8 million in the first six months of 2018, a turnaround compared to the NAf.51.3 million drop in the first six months of 2017. The average import coverage shrank from 5.0 months in 2017's first two quarters to 4.7 months in 2018's first two quarters, caused by a considerable increase in imports.

In Curaçao, net foreign demand shrank by NAf.221.0 million as the increase in imports was more pronounced than the export growth. The increase in imports stemmed mainly from more oil imports. The higher import bill can be explained by the purchase of oil products from other suppliers besides the Isla refinery<sup>5</sup> at higher costs and the increased international oil prices. Moreover, non-oil merchandise imports by the wholesale & retail trade,

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<sup>5</sup> Because of fewer oil products produced by the Isla refinery due to limited steam deliveries by the CRU plant and the decline in available crude oil following the seizure of the PDVSA assets by ConocoPhillips, Curoil N.V. purchased more oil products from other suppliers abroad.

construction, and hotels & restaurants sectors rose and tourism expenditures abroad by residents went up.

The positive export performance was led primarily by an increase in foreign exchange receipts from bunkering activities, supported by the higher average international fuel prices. Moreover, foreign exchange revenues from ship-repair activities and from business services provided to abroad, increased. Foreign exchange income from tourism activities rose as well, resulting from more receipts from cruise tourism in line with the increase in the number of cruise visitors. Despite a growth in the number of stay-over visitors, foreign exchange income from stay-over tourism shrank because of a decline in the average length of stay of Canadian and Dutch visitors. However, the refining fee of the Isla refinery declined further, caused by lower oil production. In addition, foreign exchange earnings from transportation services provided to abroad went down, resulting from fewer activities at both the harbor and the airport of Curaçao.

The deficit on the income balance of the monetary union widened by NAf.9.0 million because the decline in dividend and interest income earned from abroad exceeded the drop in dividend and interest paid to foreign investors.

Meanwhile, net current transfers into the

monetary union rose by NAf.479.2 million mostly because of an increase in transfers received from reinsurers abroad. This increase stemmed largely from the inflow of funds related to the claims of local insurance companies to pay their clients in Sint Maarten whose insured properties were damaged by Hurricane Irma in September 2017.

External financing into the monetary union rose as reflected by a worsening of the portfolio investment and loans & credits balances. In contrast, the direct investment balance improved. The portfolio investment balance deteriorated largely because of funds received from matured foreign debt securities held by institutional investors that were not reinvested abroad. These debt securities were issued in the past by the former Netherlands Antillean entities and taken over by the Dutch State under the debt relief program. Furthermore, the zero-interest loan that the government of Sint Maarten received for liquidity support from the Dutch State contributed to the deterioration of the portfolio investment balance. The worsening of the loans & credits balance was related to a deterioration of the net trade credit balance and an increase in nonresidents' deposits, mitigated by an increase in residents' foreign deposits. Net direct investments into the monetary union dropped because of increased claims of domestic direct investors on their foreign subsidiaries. Also, liabilities of domestic companies towards their foreign affiliates dropped.

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## MONETARY DEVELOPMENTS

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During 2018, the Bank kept the reserve requirement, one of its monetary policy instruments, unchanged at 18.00%.<sup>6</sup> Nevertheless, the amount of required reserves rose by NAf.27.6 million up to November 2018, as a result of the higher base amount upon which it is calculated.

Furthermore, the Bank increased its official interest rate, the pledging rate, by 0.50 percentage point to 2.00% on March 27, 2018. After being kept at the historically low level of 1.00% since December 2008, the Bank adjusted the pledging rate earlier on March 20, 2017 by 0.50 percentage point. These increases followed after the upward adjustments of the federal funds rate, its impact on the international interest rates and, hence, the domestic money market rates.

During 2018, the Bank continued to gradually reduce the amount of outstanding certificates of deposit (CDs)<sup>7</sup>. Consequently, the amount of outstanding CDs dropped from NAf.160.8 million at the end of December 2017 to NAf.8.0 million at the end of November 2018.

The current account balances of the

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<sup>6</sup> The last adjustment of the reserve requirement percentage occurred in June 2014.

<sup>7</sup> The policy of gradually reducing the outstanding amount of CDs was introduced in August 2017 after an evaluation concluded that the auctioning of CDs is not an effective instrument during a prolonged period of excess liquidity.

commercial banks at the Bank were NAf.14.3 million higher at the end of November 2018 compared to December 2017.

Up to the third quarter of 2018, broad money contracted by 0.3% due to a decrease in net domestic assets while net foreign assets increased.

Credit extension to the private sector developed rather sluggish in 2018. On an annual basis, private credit extension in the monetary union dropped by 1.2% in September 2018. Outstanding loans in both Curaçao and Sint Maarten declined by 0.9% and 2.0%, respectively. The contraction in Curaçao was the result of declines in mortgages (-2.7%), business loans (-0.2%), and in the “other loans” category (-13.3%) moderated by an increase in consumer loans (2.6%).

### Monetary and liquidity conditions

- The current account balances of the commercial banks at the central bank are still high (see Table 1).
- Low international interest rates; Fed funds rate between 2.00 - 2.25%.
- On November 30, 2018, the 1M USD Libor rate stood at 2.35% while the 3M USD Libor was 2.74%.

- Auctioning of CDs: the amount outstanding was Naf.5.4 million on December 3, 2018. The latest CD interest rate offered on the auction of December 3, 2018 was 0.18% for 4 weeks.
- For the November – December 2018 period, the reserve requirement percentage remained unchanged at 18.00% and the outstanding amount was Naf. 1,314.4 million.
- The pledging rate stands at 2.00% since March 27, 2018.

**Table 1 Liquidity conditions in the monetary union (in millions NAf.)**

	Dec 31, 2013	Dec 31, 2014	Dec 28, 2015	Dec 30, 2016	Dec 31, 2017	Nov 30, 2018
Current account balance commercial banks	231.2	388.5	490.7	500.4	817.7	832.0

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## OUTLOOK FOR 2019

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Following an accelerated expansion in both 2017 and 2018, global growth is projected to continue at a somewhat weaker pace of 3.7% in 2019 because the expansion has become less balanced and may have peaked in some major economies.<sup>8</sup> The momentum is still strong but the recently announced trade measures have lowered economic prospects. Nevertheless, risks to the medium-term global economic outlook are skewed to the downside as reflected by, among other things, policy uncertainties, rising trade barriers, tightening financial conditions, and noneconomic factors such as geopolitical tensions. Both the United States and the Netherlands, two of the main trading partners of Curaçao, are projected to grow at a slower pace in 2019. Curaçao's third important trading partner Venezuela, is suffering from an economic crisis since 2014 which is expected to continue in 2019 and beyond.

The economy of Curaçao is projected to grow by 0.4% in 2019, as both domestic and net foreign demand are projected to contribute positively to GDP. The growth in domestic demand will be supported by increases in both private and public spending. Private spending will be driven by private investment growth while private consumption will drop. The growth in private investment is supported primarily

by investments in the tourism sector such as the renovation and expansion of the Marriott Hotel, and the Majestic and Corendon projects. Furthermore, investments in the utilities and wholesale & retail trade sectors will contribute to the rise in private investments. Private consumption will decline, albeit at a slower pace than in 2018, as a result of lower disposable income due to inflationary pressures. Also, the vulnerable labor market situation as reflected by layoff petitions of several companies, will affect private consumption. In addition, net foreign demand is projected to contribute positively to real output growth because of higher exports combined with lower imports. Exports will increase primarily due to higher foreign exchange earnings from tourism, air transportation, and ship repair activities, mitigated by lower earnings from refining and bunkering activities. The gain in foreign exchange earnings from tourism activities will be supported by a growth in both stay-over tourism, notably from the United States and Europe, and cruise tourism. In addition, ship repair activities will rise as the investment in the floating docks increased the repair capacity. Despite higher private investments, imports will decline due to less construction material and services imported as the construction of the hospital is reaching its final stages. Also, the oil-import bill will drop due to lower international oil prices.

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<sup>8</sup> IMF World Economic Outlook, October 2018.

Meanwhile, inflationary pressures are expected to reach 2.2% in 2019 due to a projected drop in international oil prices, mitigated by an increase in international food prices.<sup>9</sup>

#### Downside risks to outlook 2019

There are a couple of risks that can affect the growth prospects of Curaçao in 2019. One of the main downside risks is the exposure to Venezuela, one of Curaçao's main trading partners. The crisis in Venezuela may further affect the activities in key economic sectors of the Curaçao economy such as the refinery, the tourism, harbor and financial services sectors. Furthermore, the continuing crisis can aggravate the inflow of refugees that Curaçao cannot handle on its own.

Another downside risk to the projection is the uncertain future of the refinery. Finding a strategic partner is key for the future of the refinery, as it is a vital contributor to the economy in terms of value added and employment. Further delays in the process of finding such a partner can affect private consumption and investment. Consumption may be affected because financial institutions may become reluctant to provide loans and credits to workers of the refinery and related companies.

Furthermore, the loss of correspondent banking relations can put a drag on economic growth in 2019 as it affects cross-border transactions and, thereby, increases macroeconomic uncertainties.

Another risk to the outlook is delays in the execution of private investment projects due to lengthy administrative procedures and bureaucracy. Finally, the pace of implementation of structural measures, including labor and capital markets reforms and reducing administrative barriers, may hinder the resumption of growth.

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<sup>9</sup> IMF World Economic Outlook, October 2018.

## ATTACHMENT

**Table 2 Economic key figures of Curaçao (in millions NAf.)**

	2015	2016	2017	2018
<b>Real sector</b>				
Real GDP growth (% change)	0.3	-1.0	-1.7	-1.9
Inflation (% change)	-0.5	0.0	1.6	2.4
<b>Public finances</b>				
Budget balance <sup>1</sup>	-11.4	15.9	-116.8	27.5
Debt-to-GDP ratio (%)	44.2	45.6	50.3	52.5
<b>Balance of payments of the monetary union</b>				
Current account balance	-887.4	-1,080.8	-1,120.3	-1,491.5
Capital transfers	-7.1	3.0	-2.7	16.4
External financing	804.2	1,183.8	1,004.5	1,003.3
Direct investments	278.3	241.0	628.8	30.4
Loans and credits	-62.4	569.7	52.7	939.4
Portfolio investments	588.2	373.2	323.1	33.5
Change in reserves	-27.8	-187.5	17.6	350.8
Net errors and omissions	118.1	81.5	100.9	121.1
<b>Import coverage (months)</b>	4.9	5.1	5.0	4.5

<sup>1</sup> Source 2017 figure: Financiële Management Rapportage of the government of Curaçao of September 2018. Source 2018 figure: Staff Preliminary Concluding Statement of the 2018 Article IV Mission, November 2018.

**Table 2 Economic key figures of Curaçao (in millions NAf.) cont.**

	2015	2016	2017	2018
<b>Monetary survey (monetary union)</b>				
Net domestic credit	3,744.1	4,156.2	4,161.0	-
Net domestic credit to government	-429.3	-670.2	-597.4	-
Net domestic credit to private sector	6,148.3	6,627.9	6,683.8	-
Miscellaneous	-1,974.8	-1,801.5	-1,925.4	-
Net foreign assets	4,041.8	3,973.9	4,528.0	-
Money supply	7,785.9	8,130.2	8,689.0	-
<b>Annual growth in private sector loans<sup>2</sup></b>				
Mortgages	-2.4%	-1.4%	-1.7%	-2.7%
Consumer loans	-3.0%	1.6%	4.5%	2.6%
Business loans	1.3%	-2.9%	7.6%	-0.2%
Other	-	8.7%	-18.6%	-13.4%

<sup>2</sup> 2016 refers to July – December 2018 and 2018 refers to September (annualized).

**Table 3 Economic key figures 2018**

	Curaçao	Sint Maarten	Monetary Union
Real GDP growth (% change)	-1.9	-8.1	-3.5
Inflation (% change)	2.4	2.7	2.5

**Table 4 Economic key figures 2019 (projection)**

	Curaçao	Sint Maarten	Monetary Union
Real GDP growth (% change)	0.4	2.3	0.9
Inflation (% change)	2.2	2.5	2.3

**Table 5 Monetary survey monetary union (in millions NAF.)**

	May-18	Jun-18	Jul-18	Aug-18	Sep-18
<b>Money supply (M2)</b>	8,765.9	8,922.0	8,844.6	8,685.5	8,660.4
<b>Money (M1)</b>	4,404.3	4,556.6	4,489.4	4,354.9	4,339.1
Coins & notes with the public	366.8	383.6	377.9	371.6	359.5
Total demand deposits, of which:	4,037.6	4,172.9	4,111.5	3,983.3	3,979.6
Netherlands Antillean guilders	2,680.9	2,832.2	2,781.4	2,628.5	2,618.6
Foreign currency	1,356.7	1,340.8	1,330.1	1,354.8	1,361.0
<b>Near money</b>	4,361.5	4,365.5	4,355.2	4,330.6	4,321.3
Time deposits	1,978.9	1,955.5	1,950.7	1,932.0	1,902.2
Savings	2,382.6	2,410.0	2,404.5	2,398.6	2,419.1
<b>Factors affecting the money supply</b>					
<b>Net domestic assets</b>	3,571.9	3,661.3	3,657.9	3,504.1	3,571.8
Government sector	-532.9	-479.4	-466.1	-460.0	-421.9
Former central government	-12.0	-12.0	-12.0	-13.5	-12.1
Curaçao	-385.9	-349.0	-331.2	-324.0	-313.2
Sint Maarten	-135.0	-118.4	-122.9	-122.5	-96.6
Private sector	6,606.8	6,620.7	6,604.2	6,609.4	6,651.1
Memorandum items	-2,502.0	-2,479.9	-2,480.1	-2,645.3	-2,657.4
<b>Net foreign assets</b>	5,193.9	5,260.6	5,186.6	5,181.4	5,088.6
Central bank	3,366.3	3,362.8	3,304.1	2,958.9	2,841.3
Commercial banks	1,827.6	1,897.9	1,882.5	2,222.4	2,247.3

**Table 5 Monetary survey monetary union (in millions NAf.) cont.**

	May-18	Jun-18	Jul-18	Aug-18	Sep-18
<b>Government loans by commercial banks</b>	12.8	17.5	13.8	15.6	18.1
Government of Curaçao	0.3	3.8	0.5	1.6	3.5
Government of Sint Maarten	12.5	13.8	13.4	14.1	14.5

<b>Private sector loans Curaçao</b>	4,555.6	4,575.5	4,562.3	4,562.2	4,585.1
Mortgages	1,830.3	1,801.4	1,853.2	1,829.1	1,816.5
Consumer loans	896.8	925.7	878.2	903.1	916.7
Business loans	1,739.3	1,757.8	1,745.4	1,742.2	1,762.5
Other	89.3	90.6	85.5	87.9	89.3

<b>Private sector loans Sint Maarten</b>	1,487.8	1,487.9	1,484.1	1,487.8	1,494.2
Mortgages	868.6	869.3	870.5	879.0	876.7
Consumer loans	237.5	237.3	235.9	235.9	234.0
Business loans	376.1	375.9	372.1	367.5	378.2
Other	5.7	5.4	5.7	5.5	5.3

**Table 6 Monetary sector growth rates**

	2017-III	2017-IV	2018-I	2018-II	2018-III
<b>Money supply (M2)</b>	3.2%	1.6%	2.6%	0.1%	-2.9%
<b>Demand deposits</b>					
N.A. guilders	10.2%	1.0%	4.6%	1.8%	-7.5%
Foreign currency	9.3%	8.5%	10.2%	-3.9%	1.5%
<b>Near money</b>					
Time deposits	-3.2%	-6.5%	-5.7%	2.8%	-2.7%
Saving deposits	-0.1%	6.1%	4.2%	-1.9%	0.4%

