INTERNATIONAL MONETARY FUND

IMF Country Report No. 13/258

KINGDOM OF THE NETHERLANDS—ARUBA

August 2013

2013 ARTICLE IV CONSULTATION

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 2013 Article IV consultation with the Kingdom of the Netherlands—Aruba, the following documents have been released and are included in this package:

- **Staff Report** for the 2013 Article IV consultation, prepared by a staff team of the IMF, following discussions that ended on April 26, 2013, with the officials of The Kingdom of the Netherlands—Aruba on economic developments and policies. Based on information available at the time of these discussions, the staff report was completed on June 11, 2013. 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.
- **Informational Annex** prepared by the IMF.
- **Press Release** (PR) summarizing the views of the Executive Board.

The document listed below has been or will be separately released.

Selected Issues Paper

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

Copies of this report are available to the public from

International Monetary Fund • Publication Services
700 19th Street, N.W. • Washington, D.C. 20431
Telephone: (202) 623-7430 • Telefax: (202) 623-7201
E-mail: publications@imf.org Internet: http://www.imf.org

International Monetary Fund
Washington, D.C.

INTERNATIONAL MONETARY FUND

KINGDOM OF THE NETHERLANDS—ARUBA

STAFF REPORT FOR THE 2013 ARTICLE IV CONSULTATION DISCUSSIONS

June 11, 2013

KEY ISSUES

Context: Aruba has a long history of macroeconomic stability anchored around a 40-year old pegged exchange rate regime against the USD. However, two major shocks in recent years, the global financial crisis and the shutdown of oil refining, have reversed years of low fiscal deficits and rapidly increased both public and external debt. Recovery is projected to be slow with real GDP reaching its pre-crisis level only in 2018. Fiscal consolidation is planned to start this year, but the authorities have a way to go before rebuilding the lost fiscal space.

Risks: Short-term risks are tilted to the downside given high dependence on tourism and oil imports. Upside medium-term risks include resumption of oil refining and growth take-off from investment in the renewable energy sector.

Policy recommendations: The main policy challenge is to ensure a steady recovery while rebuilding fiscal policy space. Aruba's sizable public debt (67 percent of GDP at end-2012) and the pegged exchange rate regime argue for an ambitious consolidation to bring public debt below 60 percent of GDP by 2018. The authorities' goal to balance the budget by 2016 is a step in the right direction, but measures are not yet clearly identified. Ensuring a steady recovery will need safeguarding competitiveness through continued market diversification in tourism, and keeping wage growth in line with productivity developments. With slack in the economy, and adequate international reserves, the accommodative monetary policy stance remains appropriate. Given Aruba's high external debt, financing through FDI will be critical for future growth initiatives, including plans to create a growth pillar anchored on renewable energy.

Approved By
Ranjit Teja and Vivek Arora

Discussions took place in Oranjestad during April 15-26, 2013. The staff team comprised Ms. Rahman (head), Mr. Stepanyan (EUR) and Ms Shi (MCD), with assistance from Ms. Fang and Ms. Arantes (both EUR). Messrs. Snel and Mosch (OED) participated in key policy meetings.

CONTENTS

INTRODUCTION 4

RECENT DEVELOPMENTS, OUTLOOK AND RISKS 4

A. Recent Economic Developments 4

B. Outlook and Risks 5

REBUILDING POLICY SPACE, SUPPORTING RECOVERY 8

A. Fiscal Policy: Ambitious Consolidation Needed 8

B. Monetary and Financial Sector Policies: Maintain Stability 11

C. Structural Policies: Preserve Competitiveness and External Stability 12

SUSTAINING LONG-TERM GROWTH POTENTIAL 15

STAFF APPRAISAL 18

TABLES

1. Selected Economic Indicators, 2010–14 23
2. Real Growth, 2008–18 24
3. Operations of the Central Government, 2009–18 25
4. Public Debt, 2008–12 26
5. Central Bank Survey, 2008–14 27
6. Monetary Survey, 2008–14 28
7. Balance of Payments, 2008–18 29
8. Financial Soundness Indicators, 2007–12 30
9. External Debt, 2006–12 31
10. International Investment Position, 2006–11 32

FIGURES

1. Aruba has a History of Macroeconomic Stability Relative to its Peers 6
2. Recent Shocks Have Taken Their Tolls 7

3. Monetary Policy has Maintained Financial Stability 13
4. Despite Shocks, Aruba's Price Competitiveness Remained Stable 17

BOXES

1. Valero Oil Refinery: Recent Developments and Impact on Aruba's Economy 19
2. Recent Reforms in Pension and Health Care Schemes 20
3. Medium-Term Fiscal Consolidation: How Much and How 21

APPENDIX

Debt Sustainability Analysis 33

INTRODUCTION

1. **Aruba is a highly open, tourism-dependent economy with a long history of macroeconomic stability (Figure 1).** Over eighty percent of the economy depends directly or indirectly on tourism making Aruba the second highest tourism-dependent country in the world. The fixed exchange rate against the USD (unchanged since 1971), supported by conservative fiscal, credit and prudential policies, has provided macroeconomic stability to Aruba's very open economy by maintaining low inflation and keeping imbalances checked until recent shocks. Prudent management of the economy, in turn, together with political stability and high social development, has earned Aruba investment grade ratings from S&P and Fitch.

2. **The main policy challenge is to ensure a steady recovery while rebuilding policy space.** Recent repeated shocks have held down economic recovery and exhausted authorities' policy space. The overall fiscal balance widened sharply from pre-crisis low deficits to a deficit of 8½ percent of GDP in 2012 and public debt rose beyond what is considered prudent for a small and prone-to-shock economy like Aruba. Ambitious fiscal consolidation, relying on both revenue and expenditure measures, is needed to bring public debt below 60 percent of GDP. Ensuring a steady recovery will also require safeguarding competitiveness and maintaining financial stability.

3. **The Fund's previous advice focused on ensuring fiscal sustainability through the development of a medium-term adjustment program**. Recommendations highlighted the need to include revenue measures, such as introduction of a VAT, and to improve financial situation of Aruba's pension and health care schemes. The authorities have taken certain measures to address the latter (Box 2), but more needs to be done to ensure the financial soundness of these schemes and fiscal consolidation is planned to start this year.

RECENT DEVELOPMENTS, OUTLOOK AND RISKS

A. Recent Economic Developments

4. **The economy faced two major shocks in the last four years (Figure 2).** The first was the global financial crisis, which hit Aruba's tourism sector in 2009, and the second was the shutdown of oil refining by Valero Aruba Refinery twice for a total of 27 months during 2009-12 reflecting poor profitability (Box 1). Real output plunged by a cumulative 15 percent during 2009-10. Although tourism, the mainstay of Aruban economy, rebounded quickly partly thanks to the aggressive market diversification efforts, real GDP took a second dip in 2012 by close to 1¼ percent. Output remains 12 percent below its pre-crisis level, with recovery slower than others in the Caribbean region. Unemployment, although declining, remains high at 9½ percent at end-2012.

5. **The external sector has weathered these shocks relatively well**. The non-oil current account (CA) balance, mostly reflecting developments in the tourism sector, has improved since mid-2000 reaching a balanced position in 2012 (Figure 2). The overall CA balance, however, after being in surplus for years, showed volatilities in recent years reflecting oil sector developments. Valero's shutdown and large income payments drove the overall CA into double-digit deficits in 2010-11, while in 2012 a surplus of 5 percent of GDP was registered partly due to one-time sale of

inventories by Valero. Both external debt and net IIP position deteriorated in recent years, although roll-over risks are low given 90 percent of external debt is long-term, mostly owed to parent companies. Gross international reserves remained around 5 months of non-oil imports during recent turbulence.

B. Outlook and Risks

Staff's Views

6. **In 2013, real output is projected to grow by 2.3 percent.** A delay in externally-financed large investment projects is expected to cause a significant drop in private investment for two years in a row. Robust tourism growth and some pick-up in consumption due to deflation will support the subdued near-term recovery. A two percent deflation is projected in 2013 reflecting large utility price reductions in late 2012, and declining food and energy prices. Water and electricity tariff rates were reduced by 33 and 16 percent, respectively in August and November 2012 due to cost savings from more fuel-efficient equipments. In the absence of oil exports, the overall CA balance is projected to show a deficit of 9½ percent of GDP in 2013.

7. **Under the baseline scenario, real GDP is expected to reach its pre-crisis level only in 2018 (Figure 2).** Recent market diversification measures and the recovery in US domestic demand are expected to hold real growth in tourism exports to around 2 percent, but the gaps in investment and non-tourism exports left by Valero's closure will linger. The overall CA deficit is expected to narrow in the medium term in line with a higher services' surplus, but remain sizable due to income and transfer outflows, and oil trade deficits.

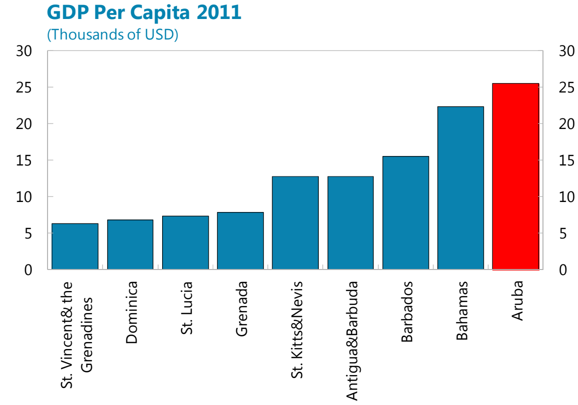
8. **Short-term risks are tilted to the downside, while medium-term risks are balanced (see Risk Assessment Matrix).** Renewed slowdown in the global economy, particularly in the US, poses significant short-term risks for Aruba. Similarly, dependence on imported oil exposes Aruba to risks of higher oil prices materializing from geopolitical events. Staff's baseline medium-term scenario conservatively assumes Valero's refining operation to stay inactive. If the company finds a strategic buyer and future prices of heavy crude ensure profitability, oil refining may resume providing a boost to growth and the CA balance. Similarly, if investments in wind and solar energy manage to further push down electricity costs or succeed in exporting services to South America, it will lift growth and competitiveness. However, failure to rein in financial deficits of the old age pension system (AOV) poses downside risks as does a further delay in investment projects.

The Authorities' Views

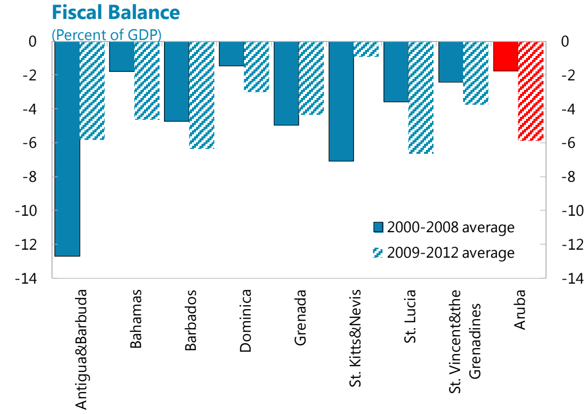
9. **There was broad agreement with the staff's analysis of economic outlook and risks.** The authorities also viewed the recovery to be gradual due to the loss of oil refining. In the short run, they considered political/policy uncertainties in Venezuela important, carrying both negative (lower tourist flows) and positive (higher investment flows) risks. Since political uncertainties in Venezuela have so far not had any negative impact on tourism inflows to Aruba, staff considers negative spillovers to be limited.

Figure 1. Aruba has a History of Macroeconomic Stability Relative to its Peers

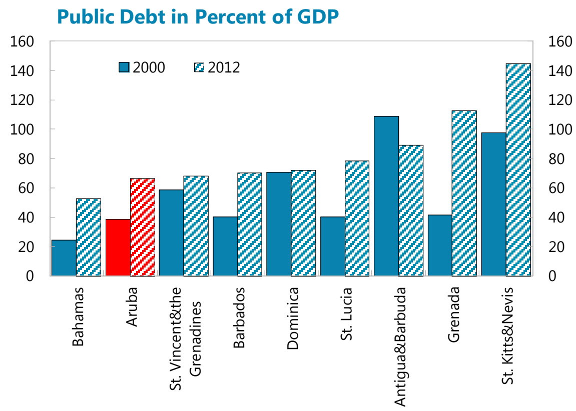
Aruba is a high income country…



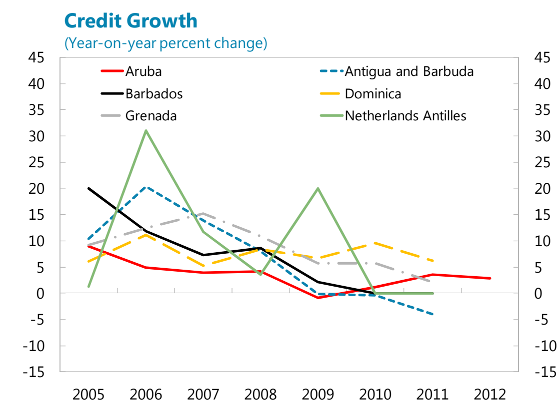
…with low fiscal deficits (until recent shocks),



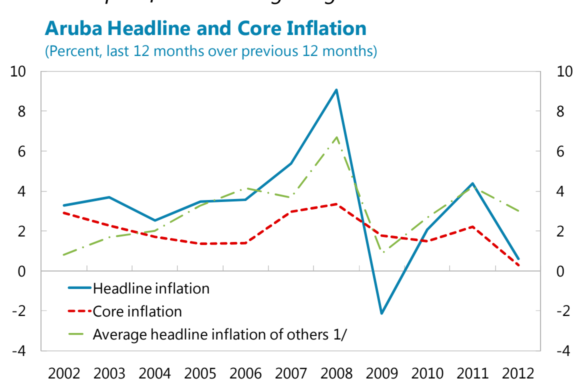
..moderate public indebtedness,



..and a cautious credit policy

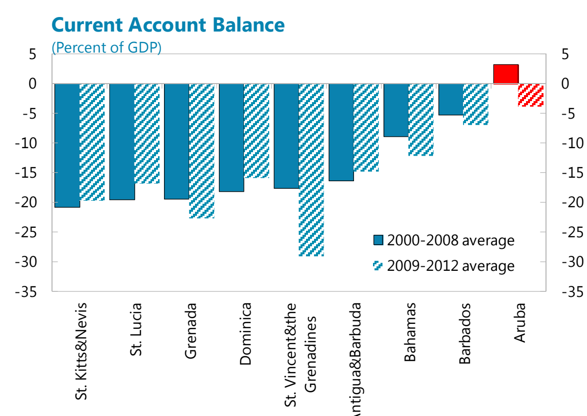


…which kept inflation in single digits..



1/ Includes Antigua and Barbuda, Bahamas, Barbados, Dominica, Grenada, St. Kitts and Nevis, St. Lucia, St. Vincent and the Grenadines.

…and external imbalances in check.



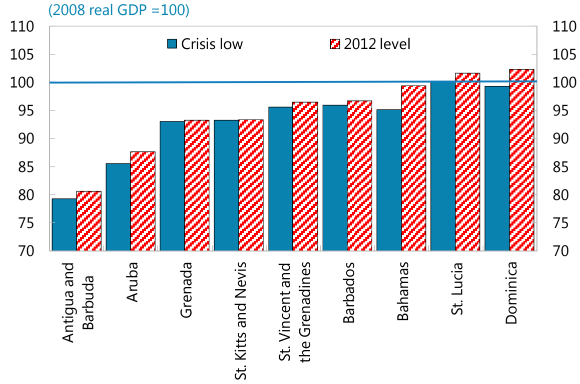
Sources: Central Bank of Aruba (CBA); Aruba Central Bureau of Statistics (CBS); IMF *World Economic Outlook*(WEO); and IMF staff calculations.

Figure 2. Recent Shocks Have Taken Their Toll

Aruba experienced one of the largest output drops…

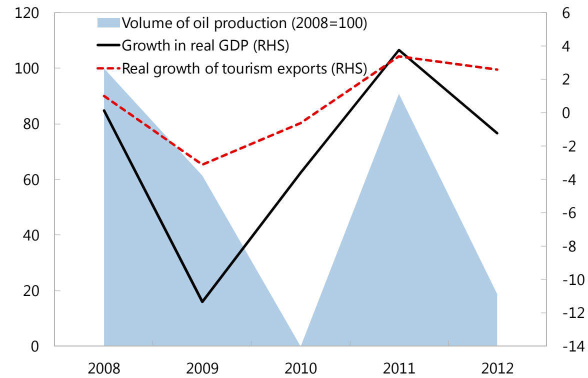
Crisis Low Real GDP and Recovery in 2012

(2008 real GDP =100)



….as the economy underwent <u>two</u> shocks.

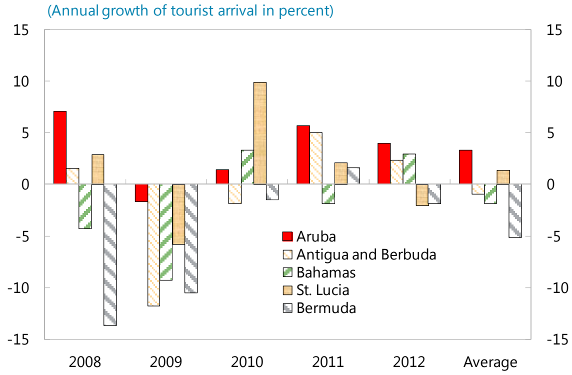
Aruba: Oil Production, Tourism Exports and Real GDP



Although tourism rebounded quickly,

Tourism Performance, 2008-12

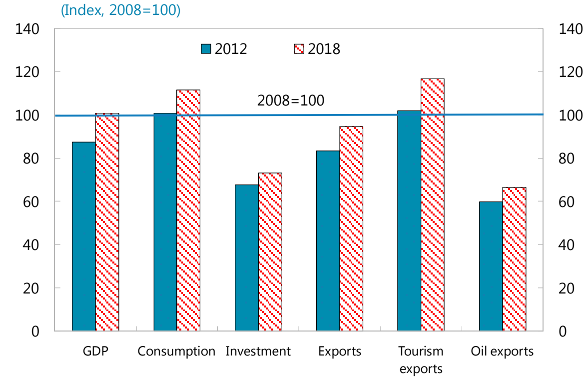
(Annual growth of tourist arrival in percent)



…Valero's shutdown has created large gaps in investment and oil exports.

Aruba: Real Economic Recovery

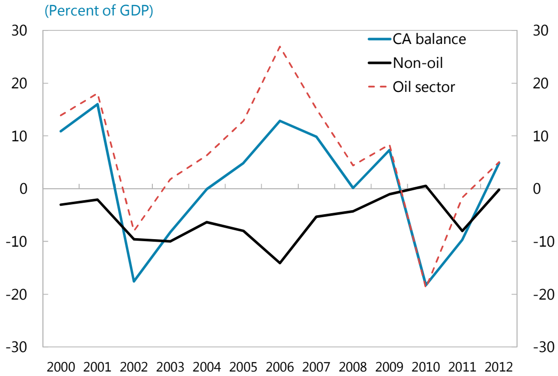
(Index, 2008=100)



External sector, particularly the non-oil sector, has held up well…

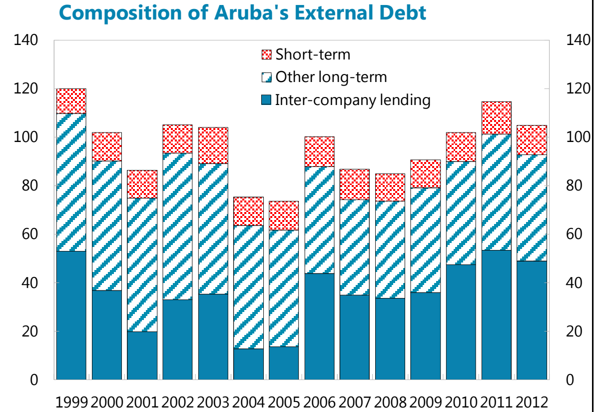
Aruba Current Account Balance

(Percent of GDP)



…although debt has increased.

Composition of Aruba's External Debt



Sources: CBA; CBS; IMF WEO; and IMF staff calculations.

REBUILDING POLICY SPACE, SUPPORTING RECOVERY

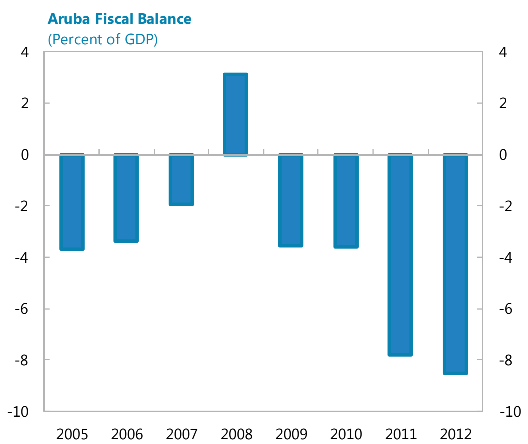
The main policy challenge is to rebuild fiscal space while ensuring a steady recovery through maintaining financial stability and safeguarding competitiveness.

A. Fiscal Policy: Ambitious Consolidation Needed

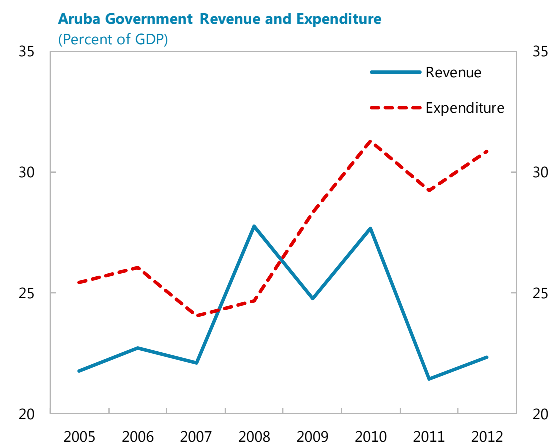
Background

10. Aruba's fiscal position deteriorated sharply in recent years. Preliminary data suggests that the overall fiscal balance recorded a deficit of 8½ percent of GDP in 2012. The authorities have undertaken notable reforms in recent years to address the deteriorating pension and health related expenditure, including introducing a mandatory general pension scheme (Box 2). These measures, along with the collection of tax arrears, were not sufficient to contain the rapid widening of the deficit, which had been a combined result of halving of the business turnover tax (BBO) rate, rising public sector wage bill and spending on goods and services. Public debt reached 67 percent of GDP at end-2012, and the financing of the deficit, despite a successful bond issuance last year (a 10-year bond of 253 million USD at a coupon of 4.6 percent which was 6 times over-subscribed), has substantially eroded government deposits.

Overal fiscal position deteriorated sharply in recent years



...as revenues fell and expenditure rose.



Source: CBA; CBS; and IMF staff calculations.

11. Fiscal consolidation is planned to take hold this year. The 2013 draft budget aims to nearly halve the deficit to 4½ percent of GDP through higher dividend payments from state-owned enterprises, containment of wage and other current expenditures and a highly optimistic growth outlook (5½ percent in real terms). With staff's growth assumptions and identified measures, a reduction of the deficit to 6 percent of GDP in 2013 is feasible but requires vigilance. Public debt will rise further to 72 percent of GDP, with financing needs reaching 11 percent of GDP. The authorities are contemplating issuing an external bond similar to the one issued in September 2012 in the European market. With excess liquidity in the banking sector, maintaining current level of domestic financing is not likely to be a problem.

12. In the medium term, headline fiscal deficits will remain elevated. Under the baseline scenario, annual interest payments in the order of 4 percent of GDP will keep headline deficits elevated and public debt is projected to pass 80 percent of GDP in 2017. This level of debt risks unsustainability if shocks materialize (Appendix 1). Financial deficits of the AOV and payments for the investment projects under the Public Private Partnerships (PPP), which are not included in staff's baseline scenario, will further widen the deficit. Due to depletion of reserve assets, staff estimates that AOV's financial deficits may add around 1 percent of GDP annually to the fiscal deficit beginning in 2014. The annual fiscal costs from PPP projects that have been signed or under discussion may amount up to another 1 percent of GDP starting in 2016.

Staff's Views

13. Ambitious targets and strong implementation are needed to reverse the unsustainable fiscal dynamics. Aruba's exposure to external shocks, a narrow economic base, a fixed exchange rate regime, and sizable interest burden call for the creation of fiscal policy space. For 2013, staff recommends a reduction of the deficit to 6 percent of GDP relying on authorities' measures to reduce wage-related and goods and services expenditure. There are downside risks to achieving this target due to parliamentary elections in September. For the medium-term, staff recommends a consolidation of about 8 percent of GDP to reach a small surplus and bring debt to below 60 percent of GDP.

Fiscal consolidation during 2014-18
(in percentage points of GDP)

	Baseline projection 1/	Authorities' plan 2/	Staff's proposal
Revenue	-0.6	0.8	2.9
Primary expenditure	2.6	4.7	4.8
Interest	-0.9	0.5	0.2
Total	1.1	6.0	7.9
Government debt at end-2018 (percent of GDP)	83.0	61.0	58.0

Source: Aruba authorities and Fund staff estimates.

1/ Reflects only measures announced in the authorities' Financial Economic Memorandum of December 2012.

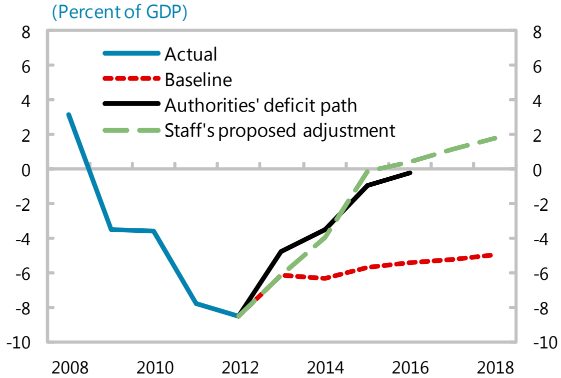
2/ Targets balanced budget starting 2016.

14. Both expenditure and revenue measures will be needed. With a large wage bill (74 percent of tax revenue), and sizable subsidies, expenditure measures would need to lead the consolidation (Box 3). The remainder can be met through indirect tax revenues, either by increasing current indirect taxes, such as the BBO (at 1.5 percent, Aruba has the lowest consumption tax rate when compared to its peers), and excise taxes and import duties, or through adopting a value-added tax (VAT) designed to fit Aruba's specific needs. Since the latter will likely warrant technical assistance and long preparatory time, the authorities would need to start now if they choose to go this way. Aruba's income and profit tax rates are the highest in the region leaving little room for a rate increase, but collection can be improved by reducing exemptions to foreign investors and intensifying collection of arrears, which the authorities are pursuing.

15. The recommended fiscal consolidation is not likely to be a major drag on economic recovery. Available data does not allow staff to compute fiscal multipliers for Aruba, but estimates for similar very open economies show these to be small, particularly for *current* expenditure and tax multipliers.[1] In the past, Aruba had achieved a much higher debt reduction within a similar timeframe (from 60 to 40 percent of GDP during 1993-99), although growth dynamics were more favorable.

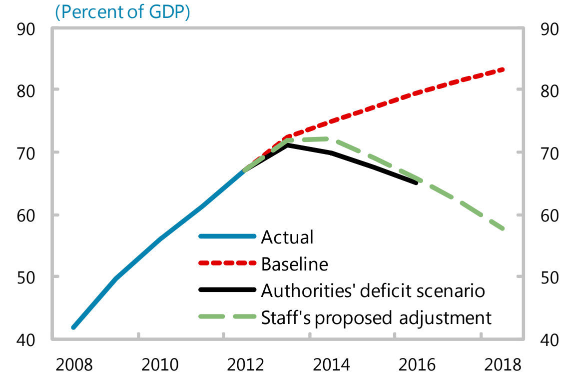
Going forward, substaintial consolidation is needed

Scenario Analysis of Fiscal Deficits
(Percent of GDP)



...to ensure saft debt levels.

Scenario Analysis of Public Debt
(Percent of GDP)



Sources: Aruban authorities; and IMF staff calculations.

16. Financial liabilities from the AOV and the PPP need to be contained. For the PPP, staff recommended putting a limit on the size of the PPP-related expenditure commitments. Possible reform measures to contain future transfers to AOV include: (i) raising the statutory retirement age from its current level of 60 years; (ii) increasing pension contribution rates; and (iii) reducing pension benefits. Given the current level of payroll taxes and relatively moderate replacement rate, the focus should be on the first measure.

The Authorities' Views

17. The authorities broadly agreed with the need for fiscal consolidation, but had yet to articulate a detailed plan and differed on measures. They plan to achieve a balanced budget in 2016 largely relying on expenditure cuts, and some measures are subject to discussions in the Social Dialogue. The authorities did not see room for increasing the BBO rate due to concerns for reduced purchasing power, but thought there was scope for increasing import duties, excise taxes and levies. They were also more optimistic in terms of revenue boost from the collection of corporate tax arrears and the introduction of the ASYCUDA customs administration system. In addition, they anticipate savings in interest costs through debt refinancing arrangements with the Netherlands, which is contingent on Aruba ensuring sustainable public finances as well as introducing a fiscal rule and establishing a Fiscal Council. The authorities are currently considering various options for a fiscal rule, including nominal expenditure ceilings and debt rules, to be implemented in the longer-run together with a Fiscal Council. Staff and the authorities agreed that prior to the adoption of any fiscal rule, budgetary and fiscal monitoring infrastructure would need to

[1] Estimates for ECCU countries show that only the public investment expenditure multiplier is statistically different from zero, while tax and consumption multipliers are not. See *The Eastern Caribbean Economic and Currency Union—Macroeconomics and Financial Systems*, Washington: International Monetary Fund (2013).

be substantially improved: a timely budget preparation, multi-year planning, and regular submission of budgetary executions to the parliament. Currently, these deficiencies in the budgetary process hinder effective fiscal monitoring and planning.

B. Monetary and Financial Sector Policies: Maintain Stability

Background

18. Monetary policy remained unchanged during 2011–12. Restrictions on capital mobility allow for some room for monetary policy action in Aruba despite the pegged exchange rate regime. The CBA's main policy instrument, the reserve requirement (RR), has been left unchanged at 11 percent since January 2010 in light of adequate reserves, low core inflation, and weak output (Figure 3). Credit growth somewhat decelerated in 2012 to around 3 percent. At end-2012, excess liquidity of the banking system stood at almost 9 percent of GDP, a reflection of weak demand and lack of competition among banks.

19. Commercial banks have weathered recent shocks without major strains. Preliminary data shows that the nonperforming loans ratio has come down substantially since 2010 with profitability indicators recovering in recent months. The aggregate capital adequacy ratio (CAR) stood at 19½ percent at end-2012, well above the regulatory minimum of 14 percent and higher than in the pre-crisis period. The authorities' latest stress test results show that even under the most severe credit shock, the CAR of the aggregate banking sector remains above the regulatory minimum. The authorities have also taken a number of steps to enhance the AML/CFT framework and, on this basis, have requested Aruba's removal from the Financial Action Task Force (FATF) and Caribbean Financial Action Task Force (CFATF) follow-up processes, which will be considered by the FATF in June and the CFATF in November.

20. The authorities have recently strengthened their framework to monitor international reserves. A multi-tier monitoring system was introduced in September 2012 whereby four thresholds of international reserves are set and followed.[2] When actual reserves fall below any of these thresholds, a policy response is triggered, starting from tightening of the monetary policy to capital controls to adjustment to the peg (in the extreme case), depending on the severity of the shortfall.

Staff's Views

21. With slack in the economy and projected deflation, an accommodative monetary policy stance remains appropriate. Staff projects subdued credit growth in the near-term due to both weak demand and tight credit standards. In case credit demand picks up, the authorities should stand ready to mop up the excess liquidity by increasing the RR. Staff welcomes the strengthened framework for monitoring international reserves, which will further contribute to warding off balance of payments risks.

[2] These thresholds are (i) 35% of exports, 10% of broad money and 95% of short-term debt coverage; (ii) 3-month of CA payments coverage; (iii) 100% of short-term debt in remaining maturity coverage; and (iv) 20% of broad money coverage.

The Authorities' Views

22. The authorities plan no near-term change in the monetary policy and are contemplating moves to enhance policy transmission. They are considering legal changes that would allow the CBA to hold government papers of more than 6 months maturity as a first step toward open market operations. The authorities are also considering options to increase competition, including allowing an additional player in the banking sector, and introducing a law to cap the interest rate on consumer loans to further consumer protection and reduce borrowing costs.

C. Structural Policies: Preserve Competitiveness and External Stability

Background

23. Aruba seems to have maintained its competitiveness in tourism through recent shocks. Its market share in the Caribbean has held up well in tandem with growth in visitors' nights and a quick recovery (Figure 4). Aruba's reputation as a "high-end" destination and dominance of time-share participants among stay-over visitors provide revenue stability. In addition, authorities' marketing efforts and additional airlifts from South America have provided resilience. Overall wage level in the economy does not appear to be out of line with its competitors and electricity costs are among the lowest in the region.

Aruba: Exchange Rate Assessment Results

	Macro Balance	External Sustainability	Equilibrium Real Exchange Rate	Average
Underlying Current Account Balance (2017) (percent of GDP)	-6.5	-6.5		
Current Account Norm (percent of GDP)	-7.3	-4.1		
Implied Overvaluation (percent of REER)	-2.6	7.9	-0.4	1.6

Source: Staff caluations based on CGER methodology.

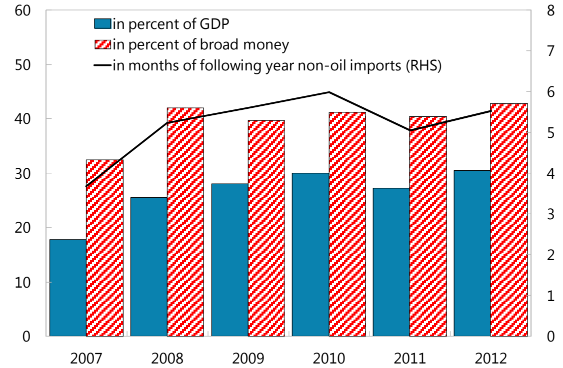
24. The CPI-based real effective exchange rate (REER) has remained relatively stable and CGER-based estimates show no major misalignment (Figure 4). Reflecting a narrow production base and the large need for imports that is typical to island economies, the CA norm shows a sizable deficit. Estimates based on the CGER methods suggest that the exchange rate is broadly in line with fundamentals. The macroeconomic balance approach and estimation of equilibrium REER show a small undervaluation, while the external stability approach, stabilizing Aruba's NFA at its end-2012 level (-123 percent of GDP), shows an overvaluation of around 8 percent. However, stabilizing the NFA at such high levels and maintaining sizable CA deficits, even if justified by fundamentals, poses both stability and financing risks.

25. Structural competitiveness shows a more mixed picture. Aruba's labor market is highly regulated with a tedious lay-off process that is often associated with hefty severance pay and court settlements favoring employees. The newly-enacted labor law somewhat relaxes restrictions, such as making it easier to lay off employees above the retirement age, but places more restrictions on hiring temporary workers and allowing overtime work, which are relevant for the labor-intensive tourism sector. In addition, costs of doing business are also high in terms of licensing requirements

Figure 3. Monetary Policy has Maintained Financial Stability

Monetary policy has aimed to ensure adequate reserves.

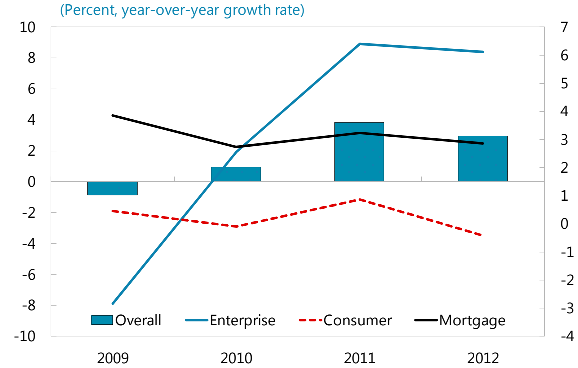
Aruba: Official Reserve Adequacy



Credit growth slowed down in 2012…

Private Sector Credit Growth

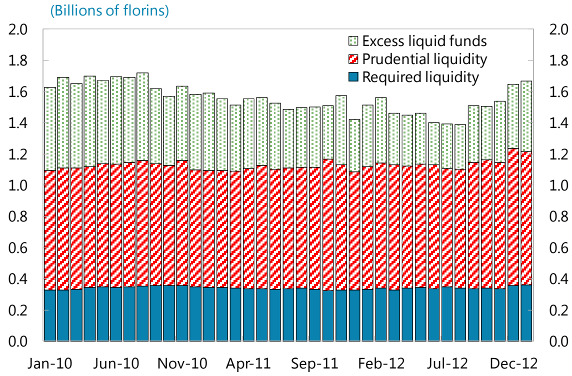
(Percent, year-over-year growth rate)



…keeping the banking system highly liquid.

Aruba Liquidity

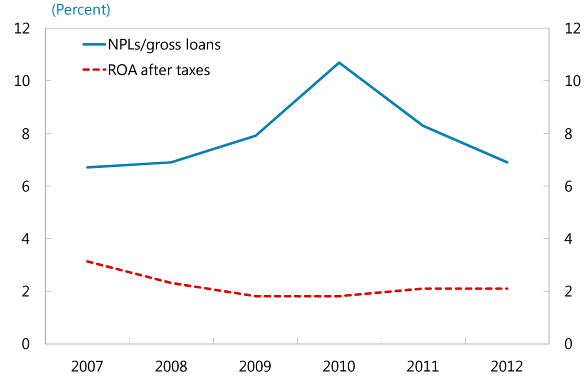
(Billions of florins)



Despite improvement in financial soundness…

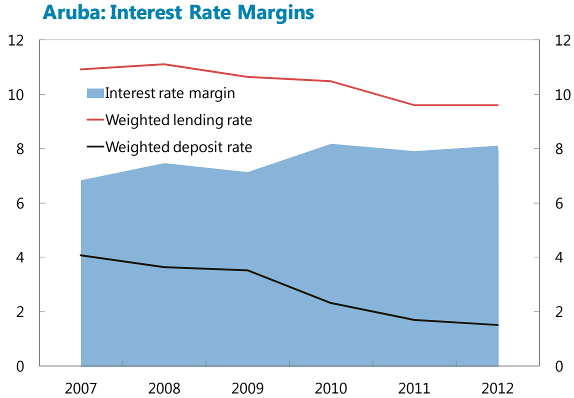
Aruba Financial Indicators

(Percent)



.a lack of competition keeps borrowing costs high

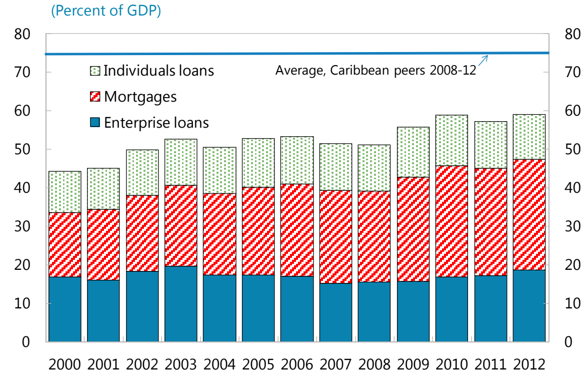
Aruba: Interest Rate Margins



…resulting in a relatively low credit stock.

Composition of Credit to Private Sector

(Percent of GDP)



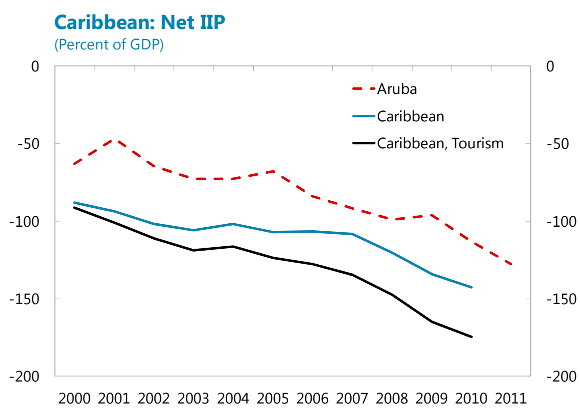
Sources: CBA; CBS; and IMF staff calculations.

that could take between 3 to 6 months, unclear rules and involvement of multiple government departments. Similarly, banks impose a fee for many types of financial transactions making access to finance and business operations costly and cumbersome.

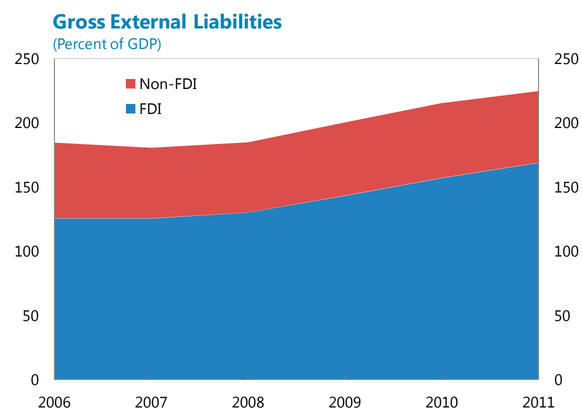
Staff's Views

26. A steady recovery requires maintaining both price and structural competitiveness. Recent initiatives to diversify the tourism market and reduction in utility costs are a welcome effort. With the U.S. accounting for 60 percent of tourists, there is scope for further diversification. Similarly, the authorities' plan to set up a second windmill park will likely reduce utility costs further. In addition, increasing flexibility in the labor market and reducing costs of doing business will help Aruba's adjustment to external shocks and facilitate economic diversification. Recent increase in gross international liabilities mostly reflects FDI inflows, somewhat reducing sustainability concerns. Going forward, availability of such options would hinge on maintaining price and structural competitiveness.

Net IIP has deteriorated in line with peers



…however, widening was dominated by FDI



Sources: Milesi-Ferretti and Lane (2012)'s External Wealth of Nations database update; Central Bank of Aruba; and IMF staff estimates.

The Authorities' Views

27. The authorities agreed with staff's analysis but did not consider structural competitiveness to be a big obstacle. Compared to other Caribbean countries, they viewed Aruba's multilingual population, high standards of living, safety and security, the Dutch legal system and modern port facilities for cruise lines as sources of strong non-price competitiveness. Also, Aruba is one of the few countries in the region where the US customs and border patrol offers clearance at the airport facilitating travel back to the US. They also expect the recently established Aruba Investment Agency, a one-stop shop for investors, to ease business set up procedures.

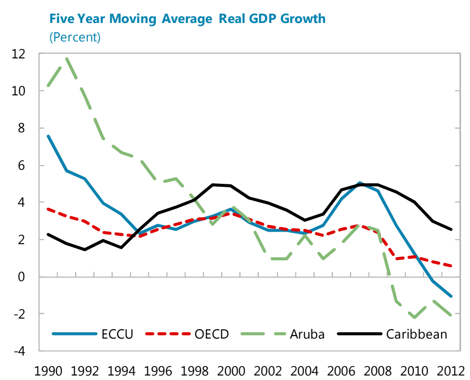
SUSTAINING LONG-TERM GROWTH POTENTIAL

Aruba needs to increase productivity and labor participation to sustain its current potential growth.

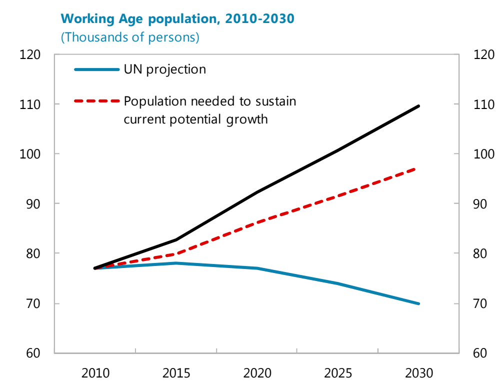
Background

28. After a strong performance in the 1990s, output growth slowed down in the last decade reflecting declining productivity. Like its peer countries that rely heavily on the labor-intensive, low-tech tourism sector, productivity experienced a trend decline. As the economy's reliance on tourism increased further, with declining volume of refining and construction activities, the contribution of productivity worsened.

Growth has slowed down since the 1990s.



There are headwinds from adverse demographics.



Source: CBA; CBS; UN; and IMF staff calculations.

29. Access to credit has been somewhat of an obstacle to growth for domestic enterprises. Credit growth, particularly to enterprises, has been low during the last decade as banks feel there is a shortage of credit-worthy borrowers due to a lack of initial capital, proper documentation, limited number of profitable opportunities, high risks, and legal challenges with loan recovery. The government and the private sector are taking initiatives to educate general population about basic financial management and how to set up small businesses.

30. In addition to these existing challenges, Aruba faces strong headwinds to potential growth. Absent new migration, the working age population will decline from 56 to 45 percent by 2030. The authorities' simulations show that, with unchanged productivity, considerable labor migration will be needed to support the current potential growth rate of 1½ - 2 percent beyond 2015. However, such high level of migration is likely to put pressure on housing, existing infrastructure, and the already burdened health and education services.

31. The authorities are pursuing a new growth pillar anchored around the renewable energy sector. Taking advantage of Aruba's location and abundant solar and wind resources, the government of Aruba has a strategy of: (i) making Aruba more dependent on renewable energy; (ii) turning Aruba into a gateway between South America, the U.S. and Europe for commerce and investment, and (iii) establishing research laboratories. The wind energy currently supplies 15 percent of total energy needs. A second windmill park, planned to be built next year, could raise the ratio to 25 percent. The Netherlands Organization for Applied Scientific Research (TNO) established its Caribbean Branch Office in Aruba in 2011 for education and research with the intention to export services to South America.

Staff's Views

32. The looming demographic challenge and declining productivity call for urgent labor market actions. Aruba needs a comprehensive labor market reform to increase both participation and productivity. Raising the mandatory general retirement age and better-targeting of social benefits would help increase the labor force participation rate. But even with reforms, grim demographics probably imply a need to rely on migrant workers. A sustainable migration policy in the context of social dialogue is therefore desirable.

33. Developing the renewable energy sector offers potential but is not without challenges. A capital- and technology-intensive growth pillar centered on natural resources offers the right long-term path for economic diversification. But a shortage of skilled labor may pose challenges to its successful take-off. These initiatives will also require large upfront investment. Staff would advise financing these projects through FDI and pace it accordingly in order to preserve the external sustainability and keep debt servicing costs to manageable levels.

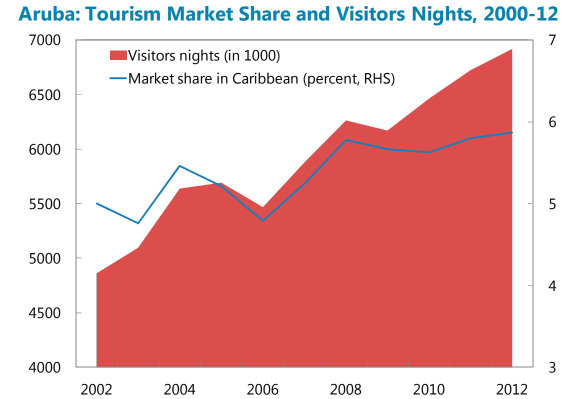
The Authorities' Views

34. The authorities are sanguine about Aruba's growth prospects from the renewable energy sector. In addition, they view renewable energy to play a catalytic role helping Aruba to grow into a business gateway to South America in knowledge- and technology-intensive industries. While they acknowledge constraints regarding skilled labor, they see scope to bring back Aruban engineers working abroad. The authorities also mentioned partnership with the Carbon War Room and view increasing the share of renewable energy to 100 percent in the long run as achievable, although technical discussions suggest that scaling up wind energy substantially will entail significant challenges in terms of storage and stabilization given Aruba's grid isolation. The authorities agreed with the staff on importance of financing through FDI.

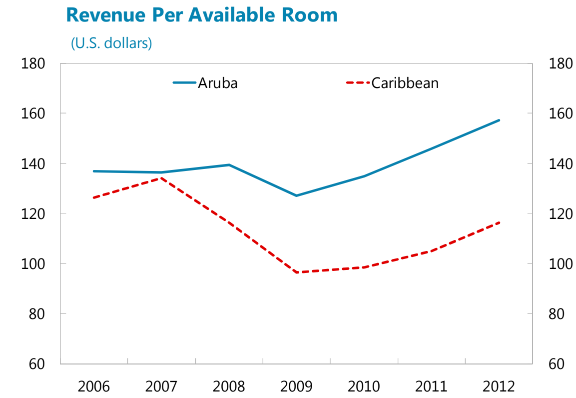
35. The authorities are also cautiously optimistic about the outcome of on-going off-shore gas exploration. The government of Aruba has signed a production sharing contract for exploration, development and production of oil and gas with REPSOL in December. Recently, REPSOL concluded its 2D seismological mapping in the continental seabed and plans to follow up with a 3D mapping in early 2014. The interest of REPSOL is a result of its recent success in Venezuela where a large gas-pocket was discovered. If gas reserves are found, the production will only begin in the long-run.

Figure 4. Despite Shocks, Aruba's Price Competitiveness Remained Stable

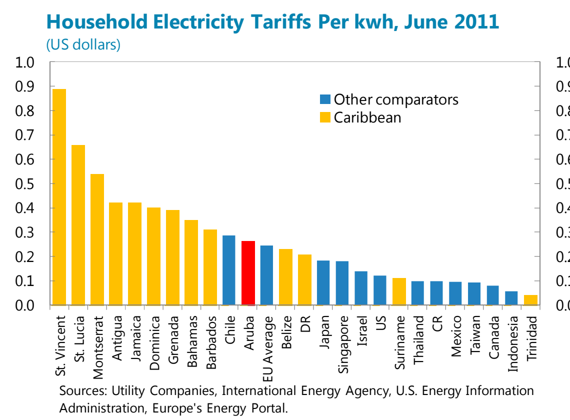
Tourism sector has seen strong growth in visitors



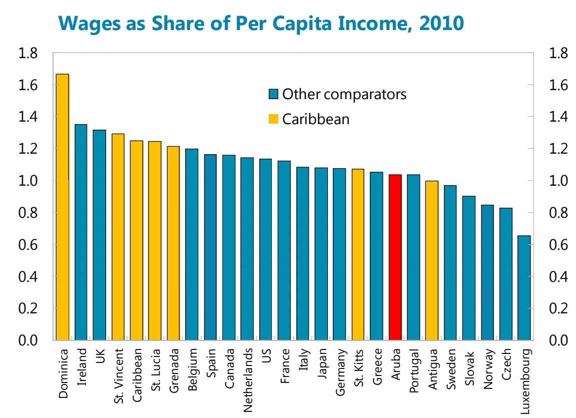
..and revenue per room.



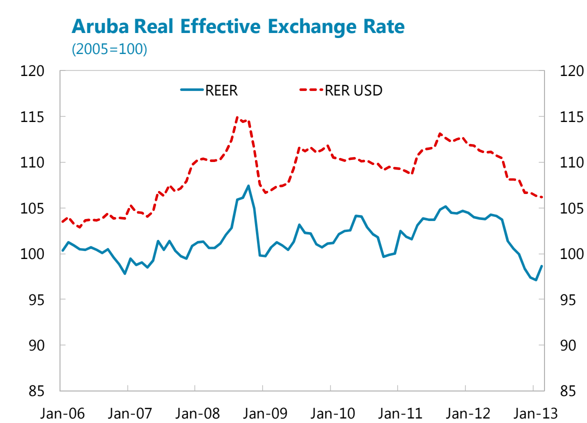
Electricity costs are among the lowest in the region



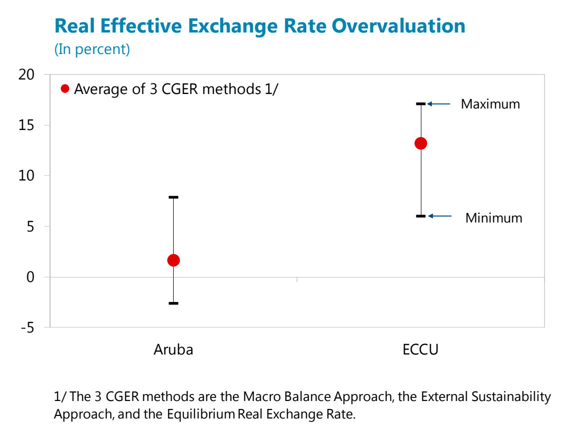
...and wages do not seem uncompetitive.



Real effective exchange rate has remained broadly stable...



...and CGER-based estimates show no major misalignment.



Sources: CBA; CBS; Aruba Tourism Authority; Aruba Cruise Tourism Authority; Utility companies; International Energy Agency; US Energy Information Administration; Europe's Energy Portal; National pension companies for ECCU countries; OECD; INS; and IMF staff calculations.

STAFF APPRAISAL

36. Aruba is recovering slowly from recent shocks. Two major shocks in the last four years, the global financial crisis and the shutdown of oil refining by Valero, have caused a recession that is deeper than in most other Caribbean countries. Although tourism, the mainstay of Aruban economy, rebounded quickly, Valero's shutdown has left harder-to-fill gaps in investment and non-tourism exports, with real GDP projected to reach its pre-crisis level only in 2018.

37. Downside risks dominate in the near-term, but medium-term prospects could be brighter. With a high dependence on tourism and oil imports, Aruba faces downside risks from renewed weaknesses in the global economy and higher oil prices. In the medium-term, there are upsides from resumption of oil refining by Valero, and large scale investment in renewable energy.

38. Putting the fiscal deficit on a downward path is an immediate policy priority. The authorities' efforts to counter the recession through cuts in the BBO rate and higher current expenditure have rapidly increased central government's deficit and debt. In the absence of exchange rate policy options, rebuilding fiscal space is an immediate priority. Staff recommends a reduction of the overall deficit to 6 percent of GDP in 2013. To ensure this outcome, staff recommends resisting possible expenditure pressures during the election year.

39. In the medium-term, ambitious fiscal consolidation is needed. Without additional measures, the central government's fiscal deficits will remain elevated in the medium term posing risks to public debt sustainability. Financial deficits of the AOV and payments for the PPP are likely to further widen the deficit beginning as early as 2014. Staff recommends a consolidation of around 8 percent of GDP during 2014-18 to bring debt down to below 60 percent of GDP. To contain fiscal pressures from financial liabilities of the AOV and the PPP, it is important to implement further pension reforms and put a limit on the size of the PPP-related expenditure commitments.

40. Competitiveness needs to be strengthened to ensure a steady recovery. Aruba has managed to maintain its competitiveness in tourism through recent shocks. The non-oil CA balance has improved in line with strong performance in the tourism sector through recent initiatives to diversify source markets. With the US accounting for 60 percent of tourists, staff sees further scope for market diversification. To ward off risks from a large negative IIP position, and elevated financing requirements, Aruba would also need to strengthen its price and structural competitiveness through higher flexibility in the labor market and more enabling business conditions.

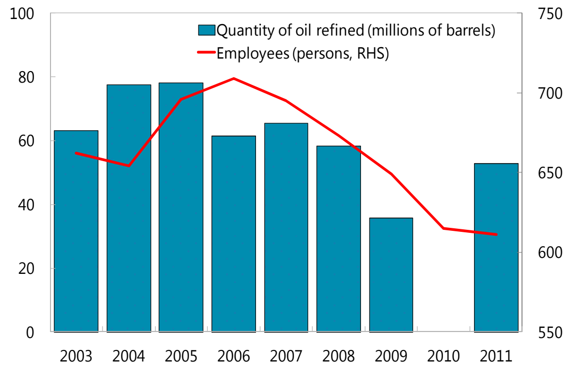
41. The accommodative monetary policy stance is appropriate. With slack in the economy, projected deflation and subdued credit growth, staff sees no need for monetary tightening. The banking system's excess liquidity has increased substantially since mid-2012. In case credit demand picks up, a very low risk at this point, the authorities would need to mop up the excess liquidity by increasing the RR.

42. It is envisaged that the next Article IV consultation discussions with Aruba will be held in 24 months time.

Box 1. Valero Oil Refinery: Recent Developments and Impact on Aruba's Economy

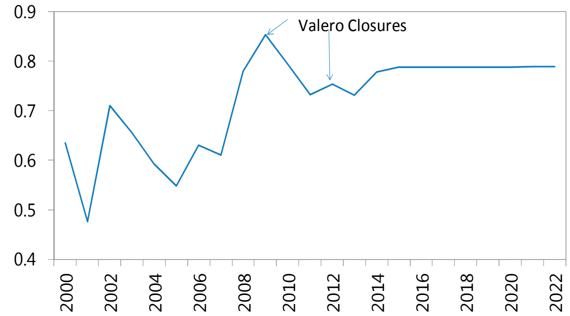
Valero refines heavy crude, which is cheaper than the light variety but costlier to refine. The profitability depends on (i) the price differential between the heavy and the light varieties; and (ii) the cost of fuel oil used in the refining operation. Rising prices of heavy crude and fuel oil since mid-2000 have caused Valero to repeatedly close down its production.

Aruba Oil Industry



Sources: Central Bank of Aruba and staff calculations.

Heavy crude price (in % of light crude)



Source: GLJ Petroleum Consultant LTD., Projections as of January 2013

After a shutdown for 18 months (July 2009 -December 2010), Valero resumed its refining in 2011 only to suspend indefinitely in March 2012. The company started to reduce its workforce and look for a strategic buyer. The number of payroll employees and sub-contractors went down (from 639 to 574, and from 1470 to 385, respectively between end-2011 and July 2012).
In May 2012, Valero announced it had received and accepted a USD 350 million purchase offer from Petro China Company. But the deal was put on hold pending elections in Venezuela. In September 2012, Valero announced it would stop refining and shift its function to storage and transshipment. The workforce was further reduced in November, leaving fewer than 100 people on its payroll.

The refinery's shutdown is estimated to have had a sizable impact on growth and CA developments in 2012. As of 2011, Valero's direct and indirect share in GDP was 7½ percent. For 2013, the impact is mostly to be felt through higher unemployment, which may be attenuated by the opening of the Ritz Carlton in November 2013, and possibly lower consumption. The fiscal impact is likely to be small given Valero's continued commitment to pay USD 10 million in annual corporate income taxes to the government.

It is unclear when and whether Valero will resume its refining operations, which depends on the success in finding a strategic partner (Valero is also in talks with Venezuelan state-owned refinery) and developments in heavy crude prices. In addition to storage and transshipment, Valero is exploring alternative business options, such as installing a liquefied natural gas terminal and a waste to energy unit.

Box 2. Aruba—Recent Reforms in Pension and Health Care Schemes

The Government of Aruba undertook a number of measures as part of the social dialogue during 2010-12 aimed at improving the worsening financial situation of pension and health care schemes.

APFA (civil servants pension fund) reforms

- In 2009-10, the civil servants pension fund's finances looked increasingly unsustainable and the authorities developed a recovery plan for APFA. The government recognized the shortfall in the coverage of pension liabilities and committed to additional annual contributions until the coverage ratio reaches 100 percent.
- The government also reformed the benefits by (i) changing the basis for calculations from final wage to average wage; (ii) netting out AOV pensions from the benefits; and (iii) increasing retirement age from 55 to 60 years.

General old age pension (AOV) reforms

- Due to population aging AOV has been running deficits since 2009. To mitigate the worsening situation, the government: (i) increased the cap on pensionable income; (ii) changed benefits base from gross to net income; (iii) individualized premium contributions; and (iv) introduced incentives for those willing to postpone retirement beyond the mandatory age of 60.
- Albeit a move in the right direction, these measures proved insufficient to reverse the worsening of the AOV balance. Its reserves are now projected to be depleted in 2013, which means that starting 2014 the burden of covering the deficits will fall on the budget.

Mandatory general pension

In 2012, the government introduced a mandatory pension for the private sector, with contributions set to gradually increase to 6 percent in 2014. In the longer term, this is expected to ensure a higher replacement rate for total pensions and thus reduce pressures on AOV to increase its benefit payments.

General health care system (AZV) reforms

- Aruba's general health care system runs large deficits and more than 30 percent of its spending has to be covered by transfers from central budget. The government undertook a number of measures to contain the AZV-related spending pressures, including increasing the premium rate by 2 percentage points and introducing caps on spending through agreements on lump-sum payments with providers.
- Most recent AZV projections suggest, however, that health care costs will be increasing and simply containing the budget transfers will most likely create arrears in the health care sector. Going forward, more reforms are necessary to increase revenues and contain costs by shifting part of the costs to beneficiaries. Regional comparison shows that Aruba's public spending on health care as percent of GDP is one of the highest in the region.

Box 3. Aruba—Medium-Term Fiscal Consolidation: *How Much and How?*

How Much?

The detrimental effects of very high levels of public debt have recently been examined for the Caribbean region. Greenidge et al. (2012) find that at 55-56 percent of GDP the debt's effect on economic growth turns from positive to negative. Although such thresholds are estimated to be higher for developed economies (80-90 percent of GDP) and emerging market countries (60-80 percent of GDP), for small island economies like Aruba, a lower threshold seems prudent given higher risk premia on interest rates (compared to advanced economies) and lower potential growth (compared to emerging market economies).

Staff considers a reduction in the public debt below 60 percent of GDP by 2018 as an appropriate target. Such an adjustment will, first of all, rebuild the fiscal space lost in the aftermath of the crisis to address risks related to contingent liabilities, particularly growing ageing and health care related cost pressures. It will also lower financing risks for the government, boost the economy's resilience to shocks, and improve its growth prospects.

How?

Reaching an overall balanced budget in 2015 and ensuring surpluses of 1 percent of GDP on average thereafter will enable Aruba reach the above debt target. A combination of expenditure and revenue side measures will be needed:

Additional fiscal consolidation measures, 2014-18 1/
(in percentage points of GDP)

Indirect taxes	3.0
Wages	2.0
Goods and services	0.7
Transfers and subsidies	2.0
Savings from interest expenditure	0.2
Total	7.9

1/ Compared to staff's projected 2013 outcome.

- Targeting a gradual reduction in wage-related costs to their 2009 levels will produce savings of around 2 percent of GDP.
- A reduction of spending on goods and services should be targeted through raising the efficiency of public spending. Also, transfers and subsidies will need to be contained and reduced. Altogether, these categories of spending can produce savings of around 2½ percent of GDP.
- More revenues should be raised from indirect taxes. The introduction of a VAT is one potential measure; however, this would require proper preparation. Near-term measures could include raising the rate of the turnover tax (BBO) back to its original level of 3 percent and increasing excise taxes, thus contributing substantially (up to 3 percent of GDP) to the consolidation efforts.
- Steady implementation of the above measures will gradually improve the underlying balance which in turn can generate savings from lower interest expenditure to the tune of 0.2 percent of GDP.

Aruba: Risk Assessment Matrix

	Source of Risks	Relative Likelihood	Impact if Realized
Short-term risks	*Downside*: Fiscal policy shock in the US, and stalled or incomplete recovery of Euro area policy commitments	Low/Medium	High Aruba's tourism and economy is highly dependent on developments in the global economy, particularly the US.
	Downside: Global oil shock triggered by geopolitical events	Low	Medium Aruba is entirely dependent on imported oil for domestic consumption
Medium-term risks	*Upside:* Further reduction in electricity prices through the wind and solar energy	Medium	Medium Impact on production costs, exports of tourism, investment and real GDP.
	Upside: Valero resuming refining operations	Medium	Medium/High Impact on real GDP and employment is likely to be medium, while on the CA will be high.
	Downside: Investment projects further delayed or postponed	Low	Low Medium-term recovery relies modestly on a boost in private investment.
	Downside: Failure to put the PAYG pension system on a sustainable footing	Medium	Medium/High Fiscal deficits will rise by 1 percent of GDP annually beginning in 2014.

Note: The Risk Assessment Matrix (RAM) shows events that could materially alter the baseline path (the scenario most likely to materialize in the view of IMF staff). The relative likelihood of risks listed is the staff's subjective assessment of the risks surrounding the baseline. The RAM reflects staff views on the source of the risks and overall level of concern as of the time of the discussion with the authorities.

Table 1. Aruba: Selected Economic Indicators, 2010–14

I. Basic Data, Social and Demographic Indicators

Area (sq. km)	180	Infant mortality (per thousand)	13.3
Population (thousands)	102.7	Literacy rate (percent)	97.3
GDP (millions of U.S. dollars)	2,544	Percent of population below age 15 (percent)	18.8
GDP per capita (thousands of U.S. dollars)	24.8	Percent of population age 65+ (percent)	10.9
Unemployment (2012, percent)	9.6	Life expectancy at birth (years)	75.1

II. Economic Indicators

	2010	2011	2012	2013	2014
				Projections	
			(Percent change)		
Real GDP	-3.6	3.7	-1.2	2.3	3.0
Real domestic demand	-4.0	1.7	-1.7	-1.5	2.6
Consumption	-0.9	1.8	1.6	1.3	1.7
Private	-0.3	3.9	0.5	1.6	1.6
Public	-2.4	-3.2	4.5	0.7	1.8
Gross investment	-10.8	1.5	-10.2	-9.5	5.7
Exports of goods and services	-10.2	14.4	-5.3	3.7	2.2
Imports of goods and services	-9.0	8.8	-5.0	-1.7	1.8
			(Percent change)		
Consumer prices					
Period average	2.1	4.4	0.6	-1.5	1.5
End-period	-0.7	6.1	-3.7	0.7	2.3
			(Percent of GDP)		
Central government operations					
Revenues	27.7	21.4	22.3	23.6	23.0
Expenditures	31.3	29.3	30.9	29.7	29.4
Of which: capital	1.1	1.2	1.7	0.9	1.0
Overall balance	-3.6	-7.8	-8.5	-6.2	-6.4
Gross central government debt (percent of GDP)	55.9	61.2	67.0	72.3	75.0
Savings and investment (percent of GDP)					
Gross investment	31.0	32.6	29.7	27.0	29.0
Foreign saving	18.3	9.6	-4.9	9.4	9.0
Domestic saving	12.7	23.0	34.6	17.6	20.0
Balance of payments					
Current account balance	-18.3	-9.6	4.9	-9.4	-9.0
Oil	-18.8	-1.7	5.0	-7.8	-7.4
Non-oil	0.5	-8.0	-0.1	-1.6	-1.6
FDI	6.5	18.2	-5.6	3.4	5.1
Gross foreign assets of central bank (millions of U.S. dollars)	724	712	787	820	860
Gross foreign assets of central bank (months of non-oil imports of follow	5.1	4.9	5.2	5.1	5.1
External debt (percent of GDP)	101.7	114.5	104.8	109.5	107.8
		(millions of local currency, unless otherwise indicated)			
Monetary					
NFA	1,309	1,286	1,342	1,400	1,432
NDA	1,845	1,873	2,077	2,121	2,278
Credit to private sector (year-on-year percent change)	1.2	3.5	2.8	3.1	4.0
Broad money	3,155	3,159	3,419	3,521	3,710
Deposits (year-on-year percent change)	-0.3	-0.1	8.2	3.0	5.3
Memorandum items:					
Nominal GDP (millions of Aruban florins)	4,279	4,566	4,555	4,613	4,860
Nominal GDP (millions of U.S. dollars)	2,391	2,551	2,544	2,577	2,715

Sources: Aruban authorities; and IMF staff estimates and projections.

Table 2. Aruba: Real Growth, 2008–18

(Percent change)

	2008	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018
					Prel.			Projections			
GDP	0.2	-11.3	-3.6	3.7	-1.2	2.3	3.0	2.9	2.3	2.1	1.8
Consumption	-4.2	-1.6	-0.9	1.8	1.6	1.3	1.7	1.9	1.9	1.9	1.8
Private	-5.7	-4.4	-0.3	3.9	0.5	1.6	1.6	2.0	2.0	2.0	1.9
Public	-0.2	5.4	-2.4	-3.2	4.5	0.7	1.8	1.7	1.5	1.5	1.5
Investment	2.0	-16.6	-10.8	1.5	-10.2	-9.5	5.7	4.2	3.5	2.6	2.2
Private	1.0	-17.7	-10.8	2.9	-14.2	-6.8	5.8	4.2	3.6	2.7	2.2
Public	27.8	6.0	-10.1	-21.3	69.9	-36.8	4.7	3.5	1.5	1.6	1.6
Imports	-1.7	-7.6	-9.0	8.8	-5.0	-1.7	1.8	1.7	1.8	1.7	1.7
Exports	1.7	-14.1	-10.2	14.4	-5.3	3.7	2.2	2.0	1.7	1.6	1.5
Tourism exports	1.0	-3.1	-0.6	3.4	2.6	3.5	2.3	2.3	2.0	1.9	1.8
Non-tourism exports	2.6	-28.1	-26.6	40.0	-18.8	4.0	2.0	1.5	1.2	1.0	0.8
Memorandum items:											
CPI (average)	9.0	-2.1	2.1	4.4	0.6	-1.5	1.5	1.5	1.7	1.7	1.7
Core CPI (average)	3.3	1.8	1.5	2.2	0.3	1.2	1.2	1.2	1.2	1.2	1.2
U.S. CPI (average)	3.8	-0.3	1.6	3.1	2.0	1.6	1.6	1.7	2.0	2.1	2.1
U.S. core CPI (average)	2.3	1.7	1.0	1.7	2.1	1.7	1.7	2.0	2.0	2.0	2.0
GDP deflator	4.8	2.7	-0.8	2.8	1.0	-1.0	2.2	1.8	2.0	2.0	2.1
GDP per capita (Aruban florins)	43,881	42,233	46,787	44,581	44,309	44,711	46,933	48,982	50,923	52,834	54,721
GDP per capita (U.S. dollars)	24,515	23,594	26,138	24,905	24,753	24,978	26,220	27,364	28,449	29,516	30,570
Population	101,646	102,057	102,135	102,411	102,792	103,174	103,555	103,937	104,318	104,699	105,081
Unemployment (percent)	6.9	11.3	10.6	8.9	9.6	8.5	…	…	…	…	…

Sources: Aruban authorities; WEO; and IMF staff estimates and projections.

Table 3. Aruba: Operations of the Central Government, 2009–18 1/

(In percent of GDP)

	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018
				Prelim.	Proj.					
Total revenue	24.8	27.7	21.4	22.3	23.6	23.0	23.0	23.0	23.0	23.0
Tax revenue	20.8	25.0	18.8	20.1	20.6	20.6	20.6	20.6	20.6	20.6
Income and profit	7.6	8.3	7.8	9.0	9.0	9.0	9.0	9.0	9.0	9.0
Commodities	5.6	5.8	6.0	6.1	6.2	6.2	6.2	6.2	6.2	6.2
Property	1.5	1.5	1.3	1.5	1.5	1.5	1.5	1.5	1.5	1.5
Services	1.4	1.5	0.7	0.5	0.9	0.9	0.9	0.9	0.9	0.9
Turnover (B.B.O.)	3.8	6.9	1.9	1.9	1.9	1.9	1.9	1.9	1.9	1.9
Of which: oil refinery tax settlement	0.0	5.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Foreign exchange	0.9	1.0	1.1	1.0	1.0	1.0	1.0	1.0	1.0	1.0
Nontax revenue	4.0	2.7	2.7	2.2	3.0	2.5	2.5	2.5	2.5	2.5
Grants	1.2	0.1	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Other	2.9	2.5	2.7	2.2	3.0	2.5	2.5	2.5	2.5	2.5
Total expenditure and net lending	28.3	31.3	29.3	30.9	29.7	29.4	28.7	28.4	28.3	28.0
Current non-interest expenditure	23.0	26.4	24.6	25.4	24.8	24.1	23.6	23.1	22.7	22.4
Wage related costs	12.7	14.2	13.9	14.9	14.4	13.9	13.5	13.1	12.8	12.5
Wages	7.0	7.8	7.8	8.4	8.0	7.7	7.5	7.3	7.1	7.0
Employers contributions	2.3	2.7	2.7	3.0	2.9	2.8	2.7	2.6	2.6	2.5
Wage subsidies	3.4	3.7	3.4	3.6	3.5	3.4	3.3	3.2	3.1	3.1
Goods and services	4.5	5.4	5.1	5.4	4.5	4.5	4.5	4.5	4.5	4.5
Transfers to AZV	2.9	3.5	2.1	2.3	2.5	2.4	2.3	2.2	2.1	2.0
Other	2.8	3.4	3.5	2.7	3.4	3.4	3.4	3.4	3.4	3.4
Subsidies	0.6	0.6	0.7	0.8	0.9	0.9	0.9	0.9	0.9	0.9
Other transfers	1.7	1.3	1.7	2.0	2.5	2.5	2.5	2.5	2.5	2.5
Contributions/settlements	0.5	1.5	1.1	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Capital expenditure	1.8	1.1	1.2	1.7	0.9	1.0	0.7	0.7	0.7	0.7
Investment	0.9	0.7	0.8	1.3	0.4	0.5	0.7	0.7	0.7	0.7
Development fund spending	0.8	0.3	0.5	0.5	0.5	0.5	0.0	0.0	0.0	0.0
Net Lending	1.0	0.8	0.5	0.5	0.4	0.4	0.4	0.4	0.4	0.4
Primary balance	-0.9	-0.6	-4.8	-5.3	-2.5	-2.5	-1.6	-1.2	-0.8	-0.5
Interest expenditure	2.7	3.0	3.0	3.2	3.7	3.9	4.0	4.2	4.4	4.5
Overall balance	-3.5	-3.6	-7.8	-8.5	-6.2	-6.4	-5.7	-5.4	-5.2	-5.0
Overall balance including transfers to AOV and PPP payments 2/						-7.1	-6.5	-6.9	-6.8	-6.9
Deficit Financing	3.6	3.6	7.8	8.5	6.2	6.4	5.7	5.4	5.2	5.0
Domestic	3.2	2.4	6.1	2.5	2.0	4.8	4.2	4.0	3.9	3.7
Disbursed	5.1	7.1	10.5	1.6	0.9	5.1	5.2	6.1	7.6	4.7
Repaid	-2.0	-4.2	-2.4	-2.1	-0.4	-0.2	-1.0	-2.1	-3.8	-1.0
Sale of assets	...	...	...	...	1.4	...	...	...	...	...
Deposits	0.1	-0.5	-1.9	3.0	0.0	0.0	0.0	0.0	0.0	0.0
Foreign	0.4	1.3	0.9	6.6	4.2	1.5	1.5	1.4	1.4	1.3
Disbursed	1.4	2.6	1.8	9.8	9.2	4.6	2.7	2.2	2.7	3.9
Repaid	-1.0	-1.2	-0.9	-3.2	-5.0	-3.1	-1.2	-0.8	-1.4	-2.6
Change in Unmet financing requirements 3/	0.0	-0.1	0.8	-0.6	0.0	0.0	0.0	0.0	0.0	0.0
Memorandum items:										
Nominal GDP (millions of Aruban flroins)	4,473	4,279	4,566	4,555	4,613	4,860	5,091	5,312	5,532	5,750
Gross debt	49.8	55.9	61.2	67.0	72.3	75.0	77.2	79.4	81.5	83.4
Domestic debt	25.7	29.7	35.3	34.9	36.5	39.4	41.9	44.1	46.2	48.1
Foreign debt	24.1	26.2	25.7	32.1	35.8	35.5	35.4	35.3	35.3	35.3
Gross assets 4/	2.3	2.9	4.6	1.6	1.5	1.5	1.4	1.3	1.3	1.2
Net debt	47.5	53.0	56.5	65.4	70.7	73.5	75.8	78.1	80.2	82.1
Stock of unmet financing requirements 3/	1.4	1.4	2.1	1.5	1.5	1.5	1.5	1.5	1.5	1.5

Sources: Aruban authorities; and IMF staff estimates and projections.

1/ The table is presented on adjusted cash basis.

2/ AOV pension scheme will require transfers from the government starting 2014. PPP contracts coming on stream will require payments starting 2016.

3/ Unmet Financing Requirements are accrued but unpaid obligations of the central government, and include arrears.

4/ Central government deposits. Does not include the assets of the public pension funds which at end-2011 were valued at more than 40 percent of GDP.

Table 4. Aruba: Public Debt, 2008–12

(Percent of GDP, unless otherwise indicated)

	2008	2009	2010	2011	2012
Gross debt	41.7	49.8	55.9	61.2	67.1
Domestic debt	20.2	25.7	29.7	35.3	35.0
Negotiable	10.5	15.0	20.1	22.5	22.6
Tbills	0.8	0.9	0.9	0.5	1.4
Cash certificates	0.0	0.2	0.0	0.2	0.0
Government bonds	9.7	14.0	19.1	20.9	21.1
Nonnegotiable	9.7	10.7	9.7	12.8	12.9
Short-term	1.0	1.2	1.1	1.3	1.2
APFA	0.3	0.3	0.2	0.4	0.3
Suppliers credit	0.3	0.4	0.4	0.5	0.7
Other	0.5	0.6	0.5	0.3	0.3
Long-term	8.7	9.5	8.6	11.6	11.5
APFA	4.3	4.7	4.9	4.5	4.5
Svb	1.9	2.1	2.2	2.1	2.1
Private loans	2.4	2.6	1.5	5.0	4.8
Other	0.0	0.0	0.0	0.0	0.0
Foreign debt	21.5	24.1	26.2	25.3	32.1
Netherlands	3.0	3.0	2.6	2.2	2.0
Development cooperation	2.9	3.0	2.6	2.2	2.0
Commercial loans	0.0	0.1	0.0	0.0	0.0
EIB	0.3	0.3	0.3	0.2	0.2
USA	3.0	4.6	6.7	6.3	14.6
Commercial debt	15.1	15.9	16.3	16.6	15.2
GDP (millions of florins)	4,914	4,473	4,279	4,566	4,555
GDP (millions of U.S. dollars)	2,745	2,499	2,391	2,551	2,544

Sources: Aruban authorities; and IMF staff estimates.

Table 5. Aruba: Central Bank Survey, 2008–14

(millions of Aruban florins)

	2008	2009	2010	2011	2012	2013	2014
					Prelim.	Projections	
Net Foreign Assets	1,089	1,150	1,131	1,066	1,185	1,243	1,315
Gross Foreign Assets	1,255	1,255	1,297	1,274	1,410	1,468	1,540
Gross Foreign Liabilities	-8	-3	-1	-1	-4	-4	-4
Valuation Changes	-159	-102	-165	-207	-221	-221	-221
Net Domestic Assets	-270	-280	-169	-295	-138	-137	-137
Central Government Deposits	-99	-96	-76	-184	-45	-45	-45
Development Funds Deposits	-85	-105	-8	-33	-14	-14	-14
Other Domestic Entities (net)	-4	-1	-1	-1	-1	-1	-1
Other Items (net)	-82	-78	-84	-78	-77	-76	-76
Reserve Money	819	870	962	771	1,048	1,107	1,179
Bank Notes Issued	212	201	198	204	225	204	205
Bank Reserves	607	669	764	567	823	903	974
Demand	144	195	206	132	210	230	248
Time	463	474	558	435	613	672	725
			(Percent change, year on year)				
NFA	58.8	5.6	-1.6	-5.7	11.1	4.9	5.8
NDA	81.0	3.9	-39.6	74.5	-53.4	-0.7	0.0
Reserve Money	52.7	6.2	10.6	-19.8	36.0	5.6	6.5
			(Percent of GDP)				
Government Deposits at Central Bank	3.7	4.5	2.0	4.7	1.3	1.3	1.2
Central Government	2.0	2.2	1.8	4.0	1.0	1.0	0.9
Development Fund	1.7	2.3	0.2	0.7	0.3	0.3	0.3

Sources: Central Bank of Aruba; and IMF staff estimates.

Table 6. Aruba: Monetary Survey, 2008–14

(millions of Aruban florins)

	2008	2009	2010	2011	2012	2013	2014
					Prelim.	Proj.	
Net foreign assets	1,269	1,475	1,309	1,286	1,342	1,400	1,432
Central bank	1,089	1,150	1,131	1,066	1,185	1,243	1,315
Commercial banks	180	325	178	220	157	157	117
Net domestic assets	1,721	1,688	1,845	1,873	2,077	2,121	2,278
Domestic credit	2,350	2,367	2,532	2,598	2,848	2,924	3,064
Net claims on the government	-189	-150	-16	-39	135	129	158
Deposits	-297	-298	-283	-341	-207	-179	-162
At central bank	-184	-201	-84	-216	-59	-59	-59
Government	-99	-96	-76	-184	-45	-45	-45
Development Funds	-85	-105	-8	-33	-14	-14	-14
At commercial banks	-113	-97	-199	-125	-148	-120	-103
Government	-6	-5	-48	-29	-26	-26	-26
Development Funds	-107	-92	-151	-96	-121	-94	-77
Claims	108	148	267	302	342	308	321
From central bank	24	25	26	28	29	29	29
From commercial banks	83	123	241	275	313	279	292
Claims on the private sector	2,540	2,517	2,547	2,637	2,712	2,795	2,906
From central bank	6	6	7	7	7	7	7
From commercial banks	2,534	2,511	2,540	2,630	2,705	2,788	2,899
Securities	23	22	28	21	18	19	19
Loans and advances	2,511	2,489	2,513	2,609	2,687	2,769	2,880
Enterprise loans	762	702	716	779	845	879	914
Mortgages	1,161	1,210	1,238	1,277	1,308	1,354	1,408
Individuals loans	588	577	560	553	534	537	558
Other items net	-629	-679	-686	-726	-770	-802	-786
Money supply (M2)	2,990	3,164	3,155	3,159	3,419	3,521	3,710
Money (M1)	1,397	1,541	1,373	1,555	1,830	1,885	1,986
Currency in circulation outside banks	181	175	175	183	200	206	217
Demand deposits	1,216	1,367	1,198	1,372	1,630	1,679	1,769
Local currency	1,082	1,224	1,060	1,212	1,456	1,499	1,580
Foreign currency	134	142	138	160	175	180	190
Quasi money	1,594	1,622	1,782	1,604	1,589	1,636	1,723
Savings deposits	763	830	887	915	935	963	1,014
Local currency	757	824	881	908	929	957	1,008
Foreign currency	6	7	7	7	6	6	6
Time deposits	831	792	895	689	654	673	709
Local currency	823	785	891	685	650	670	705
Foreign currency	8	7	4	4	4	4	4
			(Percent change, year-on-year)				
Net foreign assets	77.1	16.2	-11.2	-1.8	4.3	4.3	2.3
Net domestic assets	-7.0	-1.9	9.3	1.5	10.9	2.1	7.4
Credit to the private sector	4.2	-0.9	1.2	3.5	2.8	3.1	4.0
Broad money	16.5	5.8	-0.3	0.1	8.2	3.0	5.3
Deposits	17.5	6.4	-0.3	-0.1	8.2	3.0	5.3
			(Percent of GDP)				
Credit to the private sector	51.6	56.1	59.4	57.6	59.4	60.4	59.6
Government deposits	6.0	6.7	6.6	7.5	4.5	3.9	3.3
Central Government	2.1	2.3	2.9	4.6	1.6	1.5	1.5
Development Fund	3.9	4.4	3.7	2.8	3.0	2.3	1.9
Broad money	60.8	70.7	73.7	69.2	75.1	76.3	76.3
Memorandum items:							
Money multiplier	3.7	3.6	3.3	4.1	3.3	3.2	3.1
Loan to total deposit ratio (percent)	69.4	67.1	66.5	71.0	68.0	…	…

Sources: Central Bank of Aruba; and IMF staff estimates.

Table 7. Aruba: Balance of Payments, 2008–18

(In millions of U.S. dollars)

	2008	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018
						Projections					
Current account	4	182	-437	-246	124	-243	-245	-231	-216	-200	-179
Trade balance	-562	-501	-1,130	-737	-651	-1,034	-1,097	-1,146	-1,199	-1,254	-1,311
Oil sector	275	254	-428	126	182	-188	-188	-190	-194	-198	-202
Exports	5,366	1,863	145	5,043	1,243	74	78	81	85	88	92
Imports	5,091	1,609	573	4,918	1,062	262	266	272	279	286	294
Non-oil sector	-837	-755	-702	-862	-833	-846	-909	-956	-1,005	-1,056	-1,110
Exports	90	89	119	137	145	147	155	162	169	176	183
Imports	928	844	821	999	978	993	1,064	1,118	1,174	1,233	1,293
Services	812	836	879	835	942	978	1,049	1,121	1,197	1,278	1,365
Exports	1,603	1,529	1,559	1,679	1,758	1,809	1,924	2,038	2,153	2,274	2,400
Of which: tourism exports	1,348	1,220	1,249	1,349	1,399	1,464	1,554	1,637	1,723	1,814	1,908
Imports	792	693	681	844	817	831	875	916	956	995	1,034
Income (net)	-114	-69	-115	-229	-91	-116	-122	-128	-133	-139	-144
Current transfers	-131	-83	-70	-116	-75	-71	-74	-78	-81	-85	-88
Financial and capital account	312	-59	338	237	-87	274	286	271	239	240	216
Capital account	157	34	8	3	1	0	0	0	0	0	0
Financial account	155	-93	330	233	-89	274	286	271	239	240	216
Direct investment (net)	12	-33	156	465	-143	88	140	130	51	51	52
Portfolio (net)	60	4	11	11	149	93	28	28	28	29	30
Financial derivatives (net)	-10	-1	0	0	2	…	…	…	…	…	…
Other	92	-63	163	-243	-97	92	118	113	160	159	134
Loans (net)	-30	-1	22	-22	-33	…	…	…	…	…	…
Currency and deposits (net)	143	-73	177	-46	14	…	…	…	…	…	…
Other (net)	-21	12	-35	-174	-78	…	…	…	…	…	…
Errors and omissions	-7.4	-8.3	6.0	-3.5	-5.1	0.0	0.0	0.0	0.0	0.0	0.0
Overall balance	309	115	-93	-13	31	31	40	41	23	41	38
Financing											
Increase (-) in international reserves	-309	-115	93	13	-31	-31	-40	-41	-23	-41	-38
Memorandum items:											
Central Bank Net Foreign Assets (millions of U.S. dollars)	697	699	724	712	785	816	857	897	920	961	999
Gross Foreign Assets (millions of U.S. dollars)	701	701	724	712	787	818	859	899	922	963	1001
(months of following year non-oil imports)	5.6	5.8	5.1	4.9	5.2	5.1	5.1	5.1	5.0	5.0	5.0
(percent of broad money)	42	40	41	40	41	42	42	…	…	…	…
Gross Foreign Liabilities (millions of U.S. dollars)	4.2	1.7	0.7	0.4	2.1	2.1	2.1	2.1	2.1	2.1	2.1
External Debt (percent of GDP)	84.8	90.5	101.7	114.5	104.8	109.5	107.8	106.4	107.5	108.1	107.9
GDP (millions of U.S. dollars)	2745	2499	2391	2551	2544	2577	2715	2844	2968	3090	3212

Sources: Aruban authorities; and IMF staff estimates and projections.

Table 8. Aruba: Financial Soundness Indicators, 2007-12

(Percent, unless indicated otherwise)

	2007	2008	2009	2010	2011	2012
Capital						
Tier 1 capital to risk weighted assets	7.2	8.3	10.6	11.3	11.9	12.0
Tier 1 and Tier 2 capital to risk weighted assets	13.0	14.7	17.8	18.5	18.9	19.6
Asset quality						
NPLs to gross loans	6.7	6.9	7.9	10.7	8.2	6.9
NPLs net of allocated provisions to gross loans	4.0	3.9	4.5	6.9	4.6	3.5
NPLs net of allocated provisions to regulatory capital	32.6	28.5	27.4	40.9	27.1	19.3
Large exposures to capital	102.8	98.8	77.1	68.6	70.0	83.7
Earnings and profitability						
ROA after taxes	3.1	2.3	1.8	1.8	2.3	2.1
ROE after taxes	38.4	24.7	17.4	16.8	21.7	19.0
Net interest income to gross income	60.5	62.4	62.8	64.5	65.3	65.4
Non-interest expenses to gross income	65.7	71.1	75.0	75.2	68.0	72.8
Liquidity						
Liquid assets to total assets	29.0	34.7	30.1	28.6	26.1	28.3
Liquid assets to short term liabilities	82.6	88.7	71.5	75.6	62.5	63.0
Loans to deposits	74.7	69.4	67.1	66.5	71.0	68.0
Sensitivity to market risk						
NFA to regulatory capital	47.1	54.6	73.0	45.1	59.9	43.5
Interest rate margin (percentage points)	6.8	7.5	7.2	8.4	7.4	7.0

Source: Central Bank of Aruba.

Table 9. Aruba: External Debt, 2006–12

(Percent of GDP)

	2006	2007	2008	2009	2010	2011	2012
Government 1/	22.7	21.9	21.5	24.1	26.2	25.4	32.3
Short-term (trade credits)	0.2	0.1	0.0	0.1	0.1	0.1	0.1
Long-term	22.5	21.8	21.5	24.0	26.1	25.2	32.2
Bonds and notes	15.0	15.0	16.2	18.7	21.4	21.4	28.2
Loans	6.6	6.0	5.1	5.1	4.5	3.7	3.8
Trade credits and advances	1.0	0.8	0.3	0.1	0.2	0.2	0.2
Centrale Bank van Aruba	0.4	0.1	0.2	0.1	0.0	0.0	0.1
Commercial banks	12.9	13.7	11.9	12.1	12.5	11.0	11.6
Short-term	11.4	12.2	10.7	10.8	11.4	9.9	10.6
Long-term	1.4	1.6	1.1	1.3	1.1	1.1	1.0
Bonds and notes	0.8	0.7	0.0	0.0	0.0	0.0	0.0
Loans	0.3	0.1	0.1	0.1	0.1	0.1	0.1
Of which: currency and deposits	0.4	0.7	1.0	1.1	0.9	0.9	0.9
Other debt liabilities	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Other sectors 2/	20.5	16.2	17.7	18.5	15.6	14.6	14.7
Short-term	0.4	0.3	0.3	0.5	0.3	0.3	0.3
Long-term	20.1	15.9	17.4	18.0	15.3	14.4	14.4
Bonds and notes	7.4	4.8	5.6	5.9	2.6	2.5	2.5
Loans	12.6	11.0	11.6	11.8	12.0	11.2	11.3
Direct investment: intracompany lending	43.7	34.9	33.5	35.8	47.5	53.4	48.9
Gross external debt	100.2	86.7	84.8	90.5	101.7	114.5	104.8
Short-term	12.4	12.7	11.2	11.5	11.8	13.2	12.1
Long-term	87.8	74.1	73.6	79.0	90.0	101.3	92.7

Sources: Aruban authorities; and IMF staff calculations.

1/ Including official entities.

2/ Include nonmonetary financial institutions, public and private nonfinancial corporations, nonprofit institutions serving households and households.

Table 10. Aruba: International Investment Position, 2006–11

(Percent of GDP)

	2006	2007	2008	2009	2010	2011
Net position	-84.2	-91.9	-99.1	-96.3	-113.3	-127.8
Assets	100.2	88.5	85.6	103.8	101.8	96.8
Direct investment	25.7	23.3	22.3	24.5	25.7	24.2
Portfolio	21.0	20.1	14.7	19.4	22.8	20.6
Equity securities	14.1	14.3	10.1	13.1	16.3	13.7
Debt securities	6.8	5.7	4.6	6.4	6.5	6.9
Bonds and notes	4.0	4.6	3.4	4.4	4.4	5.5
Monetary authorities	0.0	0.0	0.0	0.0	0.0	0.0
General government	0.0	0.0	0.0	0.0	0.0	0.0
Banks	0.1	0.0	0.0	0.0	0.0	0.0
Other sectors	3.9	4.6	3.4	4.4	4.4	5.5
Money market instrumen	2.8	1.2	1.2	1.9	2.1	1.4
Other	36.7	27.4	23.1	31.9	23.0	24.1
Trade credits	0.0	0.0	0.0	0.0	0.0	0.0
Loans	2.4	2.4	2.7	3.3	3.3	3.5
Currency and deposits	33.9	24.4	19.8	28.2	18.8	19.9
Monetary authorities	0.0	0.0	0.0	0.0	0.0	0.0
General government	0.0	0.0	0.0	0.0	0.0	0.0
Banks	10.9	11.8	13.0	16.5	13.9	13.1
Other sectors	23.0	12.6	6.8	11.6	4.8	6.8
Other assets	0.5	0.6	0.5	0.4	0.9	0.8
Reserve assets	16.8	17.8	25.5	28.1	30.3	27.9
Liabilities	184.4	180.5	184.7	200.2	215.1	224.6
Direct investment	125.5	125.5	130.2	143.2	157.0	168.9
Portfolio	23.2	20.6	21.9	24.7	24.1	24.4
Equity securities	0.0	0.0	0.0	0.0	0.0	0.0
Debt securities	23.2	20.6	21.9	24.7	24.1	24.4
Bonds and notes	23.2	20.6	21.9	24.7	24.1	24.4
Monetary authorities	0.0	0.0	0.0	0.0	0.0	0.0
General government	15.0	15.0	16.2	18.7	21.4	21.4
Banks	0.8	0.7	0.0	0.0	0.0	0.0
Other sectors	7.4	4.8	5.6	5.9	2.6	3.1
Money market instrumen	0.0	0.0	0.0	0.0	0.0	0.0
Other	35.8	34.4	32.7	32.3	34.0	31.3
Trade credits	1.2	0.9	0.3	0.2	0.2	0.3
Loans	20.5	17.8	17.5	17.9	17.8	16.0
Monetary authorities	0.0	0.0	0.0	0.0	0.0	0.0
General government	6.6	6.0	5.1	5.1	4.5	4.1
Banks	0.9	0.6	0.6	0.5	1.0	1.2
Other sectors	13.0	11.3	11.9	12.3	12.3	10.8
Currency and deposits	11.3	12.3	11.0	11.5	11.3	9.2
Monetary authorities	0.4	0.1	0.2	0.1	0.0	0.0
General government	0.0	0.0	0.0	0.0	0.0	0.0
Banks	10.9	12.2	10.9	11.4	11.3	9.2
Other sectors	0.0	0.0	0.0	0.0	0.0	0.0
Other liabilities	2.8	3.4	3.8	2.7	4.7	5.8
Monetary authorities	2.4	3.0	3.2	2.3	3.8	4.5
General government	0.0	0.0	0.0	0.0	0.0	0.0
Banks	0.3	0.3	0.4	0.2	0.2	0.6
Other sectors	0.0	0.0	0.2	0.3	0.7	0.7

Sources: Central Bank of Aruba; IMF staff estimates.

Appendix. Debt Sustainability Analysis

Table I. Aruba: Public Sector Debt Sustainability Framework, 2008-2018

(In percent of GDP, unless otherwise indicated)

	Actual					Projections						
	2008	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018	**Debt-stabilizing primary balance 9/**
Baseline: Public sector debt 1/	41.7	49.8	55.9	61.2	67.0	**72.3**	**75.0**	**77.2**	**79.4**	**81.5**	**83.4**	**1.5**
o/w foreign-currency denominated	21.5	24.1	26.2	25.7	32.1	35.8	35.5	35.4	35.3	35.3	35.3	
Change in public sector debt	-4.0	8.1	6.2	5.2	5.8	5.3	2.7	2.3	2.2	2.1	1.9	
Identified debt-creating flows (4+7+12)	-5.3	7.7	5.9	4.3	8.7	3.9	2.7	2.3	2.2	2.1	1.9	
Primary deficit	-5.4	0.9	0.6	4.8	5.3	2.5	2.5	1.6	1.2	0.8	0.5	
Revenue and grants	27.8	24.8	27.7	21.4	22.3	23.6	23.0	23.0	23.0	23.0	23.0	
Primary (noninterest) expenditure	22.3	25.7	28.2	26.3	27.6	26.1	25.5	24.7	24.2	23.9	23.5	
Automatic debt dynamics 2/	0.2	6.8	5.3	-0.5	3.4	2.8	0.2	0.6	1.0	1.3	1.4	
Contribution from interest rate/growth differential 3/	0.2	6.8	5.3	-0.5	3.4	2.8	0.2	0.6	1.0	1.3	1.4	
Of which contribution from real interest rate	0.2	1.6	3.4	1.4	2.6	4.3	2.3	2.7	2.7	2.8	2.9	
Of which contribution from real GDP growth	-0.1	5.2	1.9	-2.0	0.7	-1.5	-2.1	-2.1	-1.7	-1.6	-1.4	
Contribution from exchange rate depreciation 4/	0.0	0.0	0.0	0.0	0.0	...	...	...	...	...	...	
Other identified debt-creating flows	0.0	0.0	0.0	0.0	0.0	-1.4	0.0	0.0	0.0	0.0	0.0	
Privatization receipts (negative)	0.0	0.0	0.0	0.0	0.0	-1.4	0.0	0.0	0.0	0.0	0.0	
Recognition of implicit or contingent liabilities	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	
Other (specify, e.g. bank recapitalization)	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	
Residual, including asset changes (2-3) 5/	1.3	0.4	0.3	0.9	-2.9	1.4	0.0	0.0	0.0	0.0	0.0	
Public sector debt-to-revenue ratio 1/	150.2	200.8	202.2	285.5	299.9	306.4	325.3	335.2	344.6	353.6	361.8	
Gross financing need 6/	2.7	7.7	10.2	12.2	14.8	12.9	10.9	9.1	9.4	11.6	10.0	
in billions of U.S. dollars	0.1	0.2	0.2	0.3	0.4	0.3	0.3	0.3	0.3	0.4	0.3	
Scenario with key variables at their historical averages 7/						**72.3**	**75.0**	**77.7**	**80.5**	**83.4**	**86.3**	**2.0**
Scenario with no policy change (constant primary balance) in 2013-2018						**72.3**	**75.0**	**78.1**	**81.6**	**85.4**	**89.4**	**1.6**
Key Macroeconomic and Fiscal Assumptions Underlying Baseline												
Real GDP growth (in percent)	0.2	-11.3	-3.6	3.7	-1.2	2.3	3.0	2.9	2.3	2.1	1.8	
Average nominal interest rate on public debt (in percent) 8/	5.4	5.8	5.8	5.7	5.3	5.5	5.6	5.6	5.7	5.8	5.8	
Average real interest rate (nominal rate minus change in GDP deflator, in	0.6	3.2	6.6	2.8	4.3	6.5	3.4	3.8	3.6	3.8	3.7	
Nominal appreciation (increase in US dollar value of local currency, in per	0.0	0.0	0.0	0.0	0.0	...	...	...	...	...	...	
Inflation rate (GDP deflator, in percent)	4.8	2.7	-0.8	2.8	1.0	-1.0	2.2	1.8	2.0	2.0	2.1	
Growth of real primary spending (deflated by GDP deflator, in percent)	3.4	1.9	6.1	-3.5	3.9	-3.4	0.9	-0.6	0.5	0.4	0.3	
Primary deficit	-5.4	0.9	0.6	4.8	5.3	2.5	2.5	1.6	1.2	0.8	0.5	

1/ Central government gross debt. 2012 numbers are preliminary.

2/ Derived as [(r - p(1+g) - g + ae(1+r)]/(1+g+p+gp)) times previous period debt ratio, with r = interest rate; p = growth rate of GDP deflator; g = real GDP growth rate; a = share of foreign currency denominated debt; and e = nominal exchange rate depreciation (measured by increase in local currency value of U.S. dollar).

3/ The real interest rate contribution is derived from the denominator in footnote 2/ as r - π (1+g) and the real growth contribution as -g.

4/ The exchange rate contribution is derived from the numerator in footnote 2/ as ae(1+r).

5/ For projections, this line includes exchange rate changes.

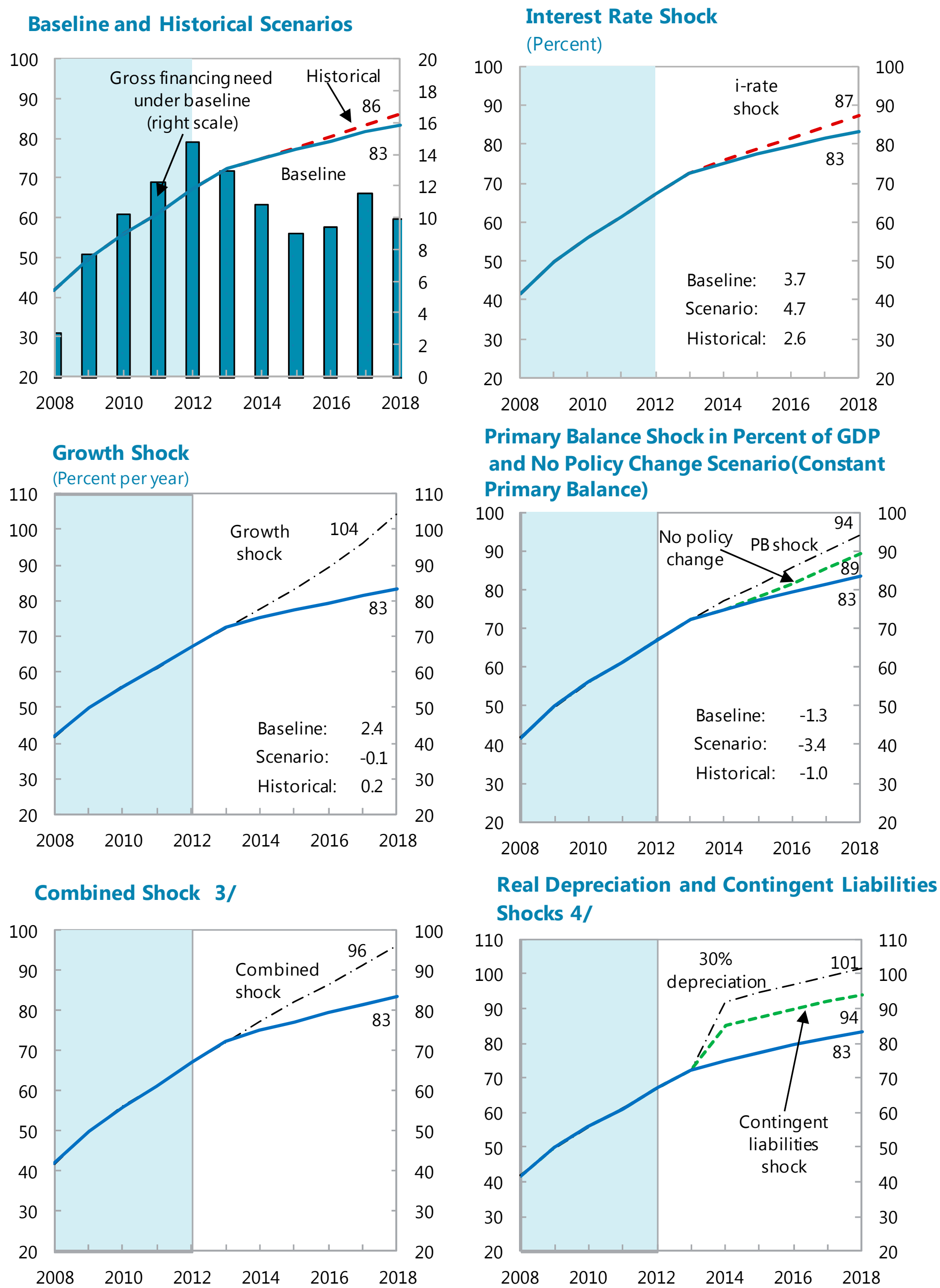
6/ Defined as public sector deficit, plus amortization of medium and long-term public sector debt, plus short-term debt at end of previous period.

7/ The key variables include real GDP growth; real interest rate; and primary balance in percent of GDP.

8/ Derived as nominal interest expenditure divided by previous period debt stock.

9/ Assumes that key variables (real GDP growth, real interest rate, and other identified debt-creating flows) remain at the level of the last projection year.

Figure I. Aruba: Public Debt Sustainability: Bound Tests 1/ 2/
(Public debt in percent of GDP)



Sources: International Monetary Fund, country desk data, and staff estimates.
1/ Shaded areas represent actual data. Individual shocks are permanent one-half standard deviation shocks. Figures in the boxes represent average projections for the respective variables in the baseline and scenario being presented. Ten-year historical average for the variable is also shown.
2/ For historical scenarios, the historical averages are calculated over the ten-year period, and the information is used to project debt dynamics five years ahead.
3/ Permanent 1/4 standard deviation shocks applied to real interest rate, growth rate, and primary balance.
4/ One-time real depreciation of 30 percent and 10 percent of GDP shock to contingent liabilities occur in 2010, with real depreciation defined as nominal depreciation (measured by percentage fall in dollar value of local currency) minus domestic inflation (based on GDP deflator).

Table 2. Aruba: External Debt Sustainability Framework, 2008–2018

(In percent of GDP, unless otherwise indicated)

	Actual							Projections						
	2008	2009	2010	2011	2012	10-Year Historical Average	10-Year Standard Deviation	2013	2014	2015	2016	2017	2018	Debt-stabilizing non-interest current account 6/
Baseline: External debt	84.8	90.5	101.7	114.5	104.8			**109.5**	**107.8**	**106.4**	**107.5**	**108.1**	**107.9**	**-3.1**
Change in external debt	-2.0	5.7	11.2	12.8	-9.7			4.7	-1.7	-1.4	1.1	0.5	-0.2	
Identified external debt-creating flows (4+8+9)	-4.7	1.2	19.1	-5.0	-2.4			5.7	3.8	3.3	4.3	3.6	3.0	
Current account deficit, excluding interest payments	-2.8	-9.9	15.2	6.2	-7.3			7.0	6.6	5.6	4.8	4.0	3.1	
Deficit in balance of goods and services	-504.9	-265.0	-162.4	-532.9	-235.9			-159.7	-160.6	-161.3	-162.3	-163.5	-164.9	
Exports	257.1	139.3	76.3	268.9	123.7			78.8	79.4	80.2	81.1	82.1	83.3	
Imports	-247.8	-125.7	-86.1	-264.1	-112.3			-81.0	-81.2	-81.1	-81.2	-81.4	-81.6	
Net non-debt creating capital inflows (negative)	-0.2	0.3	-2.6	-7.3	2.2			-1.4	-2.1	-1.8	-0.7	-0.7	-0.6	
Automatic debt dynamics 1/	-1.7	10.8	6.6	-3.9	2.7			0.1	-0.7	-0.5	0.1	0.3	0.6	
Contribution from nominal interest rate	2.4	2.5	2.5	2.4	2.5			2.5	2.5	2.5	2.5	2.5	2.5	
Contribution from real GDP growth	-0.1	10.6	3.4	-3.6	1.4			-2.4	-3.2	-2.9	-2.3	-2.2	-1.9	
Contribution from price and exchange rate changes 2/	-4.0	-2.2	0.7	-2.8	-1.1			...	...	...	...	...	...	
Residual, incl. change in gross foreign assets (2-3) 3/	2.7	4.5	-7.9	17.7	-7.4			-1.0	-5.5	-4.7	-3.1	-3.1	-3.2	
External debt-to-exports ratio (in percent)	33.0	65.0	133.4	42.6	84.7			139.0	135.7	132.7	132.6	131.5	129.5	
Gross external financing need (in billions of US dollars) 4/	0.7	0.5	1.1	1.0	0.6			1.0	1.1	1.1	1.1	1.1	1.2	
in percent of GDP	26.3	20.7	47.6	40.5	24.2			40.0	39.3	38.0	37.3	36.7	35.8	
Scenario with key variables at their historical averages 5/								**109.5**	**104.8**	**100.5**	**97.9**	**95.3**	**92.8**	**1.7**
Key Macroeconomic Assumptions Underlying Baseline														
Real GDP growth (in percent)	0.2	-11.3	-3.6	3.7	-1.2	0.2	5.1	2.3	3.0	2.9	2.3	2.1	1.8	
GDP deflator in US dollars (change in percent)	4.8	2.7	-0.8	2.8	1.0	2.7	1.8	-1.0	2.2	1.8	2.0	2.0	2.1	
Nominal external interest rate (in percent)	2.9	2.6	2.6	2.6	2.1	2.9	0.5	2.4	2.4	2.4	2.4	2.4	2.4	
Growth of exports (US dollar terms, in percent)	5.7	-50.7	-47.6	276.1	-54.1	24.2	95.2	-35.5	6.2	5.8	5.5	5.4	5.4	
Growth of imports (US dollar terms, in percent)	15.1	-53.8	-34.5	227.1	-57.6	18.6	80.1	-27.0	5.7	4.6	4.5	4.4	4.2	
Current account balance, excluding interest payments	2.8	9.9	-15.2	-6.2	7.3	3.2	9.5	-7.0	-6.6	-5.6	-4.8	-4.0	-3.1	
Net non-debt creating capital inflows	0.2	-0.3	2.6	7.3	-2.2	-1.7	14.8	1.4	2.1	1.8	0.7	0.7	0.6	

1/ Derived as [r - g - r(1+g) + ea(1+r)]/(1+g+r+gr) times previous period debt stock, with r = nominal effective interest rate on external debt; r = change in domestic GDP deflator in US dollar terms, g = real GDP growth rate, e = nominal appreciation (increase in dollar value of domestic currency), and a = share of domestic-currency denominated debt in total external debt.

2/ The contribution from price and exchange rate changes is defined as [-r(1+g) + ea(1+r)]/(1+g+r+gr) times previous period debt stock. r increases with an appreciating domestic currency (e > 0) and rising inflation (based on GDP deflator).

3/ For projection, line includes the impact of price and exchange rate changes.

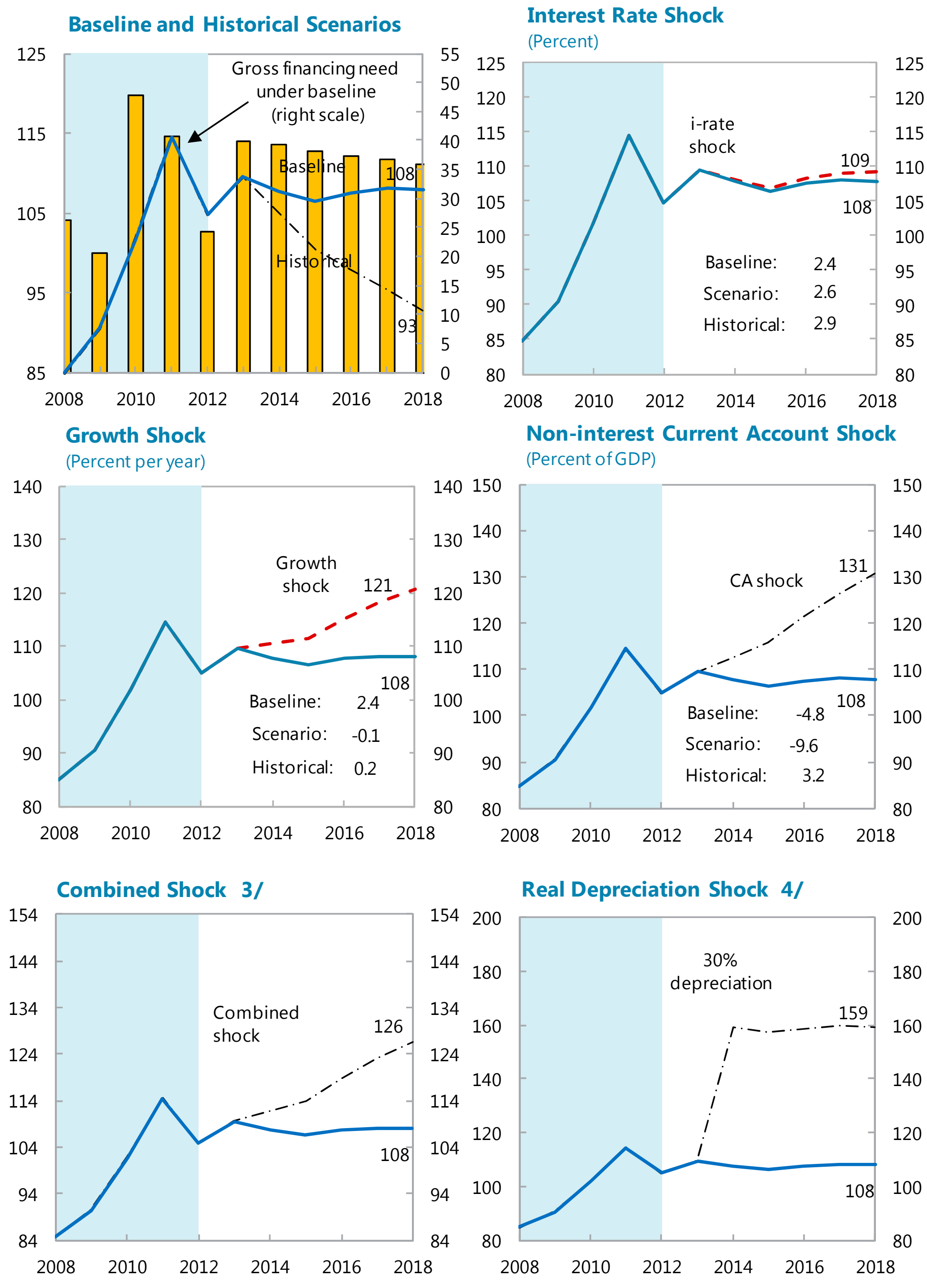
4/ Defined as current account deficit, plus amortization on medium- and long-term debt, plus short-term debt at end of previous period.

5/ The key variables include real GDP growth; nominal interest rate; dollar deflator growth; and both non-interest current account and non-debt inflows in percent of GDP.

6/ Long-run, constant balance that stabilizes the debt ratio assuming that key variables (real GDP growth, nominal interest rate, dollar deflator growth, and non-debt inflows in percent of GDP) remain at their levels of the last projection year.

Figure II. Aruba: External Debt Sustainability: Bound Tests 1/ 2/

(External debt in percent of GDP)



Sources: IMF country desk data; and staff estimates.

1/ Shaded areas represent actual data. Individual shocks are permanent one-half standard deviation shocks. Figures in the boxes represent average projections for the respective variables in the baseline and scenario being presented. Ten-year historical average for the variable is also shown.

2/ For historical scenarios, the historical averages are calculated over the ten-year period, and the information is used to project debt dynamics five years ahead.

3/ Permanent 1/4 standard deviation shocks applied to real interest rate, growth rate, and current account balance.

4/ One-time real depreciation of 30 percent occurs in 2010.

INTERNATIONAL MONETARY FUND

KINGDOM OF THE NETHERLANDS—ARUBA

STAFF REPORT FOR THE 2013 ARTICLE IV CONSULTATION DISCUSSIONS—INFORMATIONAL ANNEX

June 11, 2013

Prepared By

Haiyan Shi and Vahram Stepanyan, with assistance from Ms. Fang and Ms. Arantes

CONTENTS

FUND RELATIONS 2

STATISTICAL ISSUES 3

FUND RELATIONS

(As of April 30, 2013)

Membership Status: The Kingdom of the Netherlands joined the Fund on December 27, 1945; Article VIII. Aruba has accepted the obligations under Article VIII as part of the Kingdom of the Netherlands.

General Resources Account

	SDR Million	Percent of Quota
Quota	5,162.40	100.00
Fund holdings of currency	3,610.57	69.94
Reserve Tranche Position	1,551.89	30.06
Lending to the Fund	1,116.35	

SDR Department

	SDR Million	Percent of Allocation
Net cumulative Allocation	4,836.63	100.00
Holdings	4,559.91	94.28

Outstanding Purchases and Loans

None

Latest Financial Arrangements

None

Projected Obligations to Fund[3]

(SDR million; based on existing use of resources and present holdings of SDRs):

	Forthcoming				
	2013	2014	2015	2016	2017
Principal					
Charges/interest	0.14	0.22	0.22	0.22	0.22
Total	0.14	0.22	0.22	0.22	0.22

Implementation of HIPC Initiative

Not Applicable

Implementation of Multilateral Debt Relief Initiative (MDRI)

Not Applicable

Implementation of Post-Catastrophe Debt Relief (PCDR)

Not Applicable

Exchange Rate Arrangements

Aruba has a conventional peg; the Aruban florin has been pegged to the U.S. dollar at Af. 1.79 per US$1 since January 1, 1986. Prior to that, Aruba's currency was called the Antillean florin, which maintained a peg against the US dollar (1 US$ = ANG 1.79) since 1971.

Aruba maintains an unapproved foreign exchange restriction arising from the foreign exchange tax on payments by residents to non-residents (1.3 percent of the transaction value).

Last Article IV Consultation

Discussions for the 2013 Article IV consultation were held in Oranjestad from April 15 to 26, 2013. The staff report for the 2010 Article IV Consultation (IMF Country Report No. 10/270, October 7, 2010) was considered by the Executive Board on October 20, 2010. Consultations with Aruba are conducted on a 24-month cycle.

[3] When a member has overdue financial obligations outstanding for more than three months, the amount of arrears will be shown in this section.

STATISTICAL ISSUES

I. Assessment of Data Adequacy for Surveillance
General: Data provision is adequate for surveillance.
Real Sector Real sector data are compiled by the Central Bureau of Statistics (CBS). The CBS has published national accounts data for 1995 through 2011. On the expenditure side, data on changes in inventories are lacking. Moreover, the data on imports and exports of goods and services do not match BOP statistics, reflecting different methodological approaches and raw sources. CPI data are compiled and published on a monthly basis. **Government Accounts** Government finance statistics are prepared and published on a regular basis, but not reported to STA. The presentation of the fiscal accounts could be improved in several respects. First, a residual expenditure category "items not identified elsewhere" that can amount to 3 percent of GDP should be disaggregated. Second, below-the-line financing does not add up to the fiscal deficit without further adjustments. Third, each financing category has a component "other" (in addition to disbursements and amortizations) whose nature is not clear. And fourth, the authorities combine commercial bank financing and central bank financing into one aggregate category "net recourse to the monetary system". This item should be disaggregated. **External Sector** The CBA reports quarterly balance of payments and an annual international investment position (IIP) statistics. Monthly data on the official reserve position are published with a lag of one month. A breakdown in holdings of gold and foreign currency is provided. Data on foreign liabilities of the monetary sector—including a breakdown by maturity and instrument—and the central government are published on a quarterly basis, with a lag of about one quarter. A debt survey covering both public and private sectors provides information on the amount, currency denomination of foreign debt outstanding, as well as on disaggregation by instrument and amortization payments coming due. Areas requiring improvement include: (i) making external debt data consistent with debt flows in the balance of payments, and (ii) report maturity schedules on private sector external debt. **Monetary accounts** The methodology used by the Central Bank of Aruba (CBA) for compiling monetary statistics published in CBA's Monthly Bulletin, Quarterly Bulletin, and Annual Statistical Digest is broadly consistent with the IMF's Monetary and Financial Statistics Manual 2000 (MFSM). The CBA reports monetary data to STA on a timely basis. The authorities submit the data in the format of Standardized Report Forms developed by STA.

Aruba—Table of Common Indicators Required for Surveillance

(As of April 16, 2013)

	Date of Latest Observation	Date Received	Frequency of Data /6	Frequency of Reporting /6	Frequency of Publication /6	Memo Items: Data Quality—Methodological Soundness	Memo Items: Data Quality—Accuracy and Reliability
Exchange Rates	Current	Current	M	M	D and M		
International Reserve Assets and Reserve Liabilities of the Monetary Authorities /1	2/13	4//13	M	M	M		
Reserve/Base Money	2/13	4/13	M	M	M		
Broad Money	2/13	4/13	M	M	M		
Central Bank Balance Sheet	2/13	4/13	M	M	M		
Consolidated Balance Sheet of the Banking System	2/13	4/13	M	M	M		
Interest Rates /2	2/13	4/13	M	M	M		
Consumer Price Index	12/12	4/13	M	M	M		
Revenue, Expenditure, Balance and Composition of Financing /3—General Government /4	2012	4/13	Q	N/A	Q		
Revenue—Central Government	2/13	4/13	M	N/A	M		
Stock of Central Government Debt /5	Q4/2012	4/13	Q	N/A	Q		
External Current Account Balance	Q4/2012	5/13	Q	A	Q		
Exports and Imports of Goods and Services	Q4/2012	5/13	Q	A	Q		
GDP/GNP	2012	4/13	A	N/A	A		
Gross External Debt	2012	4/13	A	N/A	A		
International Investment Position	2011	4/13	A	A	A		

1/ Includes reserve assets pledged or otherwise encumbered.
2/ Both market-based and officially determined, including discount rates, money market rates, rates on treasury bills, notes and bonds.
3/ Includes foreign, domestic bank, and domestic nonbank financing.
4/ General government consists of the central budget and the Development Fund of Aruba. Composition of financing published only annually.
5/ Including by domestic and foreign holders and instruments.
6/ Daily (D); weekly (W); monthly (M); quarterly (Q); annually (A); irregular (I); and not available (NA).

Press Release No. 13/303
FOR IMMEDIATE RELEASE
August 9, 2013

International Monetary Fund
Washington, D. C. 20431 USA

IMF Executive Board Concludes 2013 Article IV Consultation with the Kingdom of the Netherlands—Aruba

On June 26, 2013, the Executive Board of the International Monetary Fund (IMF) concluded the Article IV consultation with the Kingdom of the Netherlands—Aruba[1] and considered and endorsed the staff appraisal without a meeting on a lapse-of-time basis.[2]

Aruba is a highly open economy with a long history of macroeconomic stability. Over eighty percent of the economy depends directly or indirectly on tourism making Aruba the second highest tourism-dependent country in the world. The long-standing fixed exchange rate against the US Dollar, supported by conservative fiscal, credit and prudential policies, has provided macroeconomic stability by maintaining low inflation over the years and keeping imbalances checked until recent shocks.

The economy faced two major shocks in the last four years: the global financial crisis, which hit Aruba's tourism sector in 2009, and the shutdown of Valero oil refinery for a total of 27 months during 2009-12 reflecting poor profitability. Although tourism rebounded quickly partly thanks to aggressive market diversification efforts, real GDP took a second dip in 2012 by close to 1¼ percent after increasing by 3¾ percent in 2011. Output remains 12 percent below its pre-crisis level, with recovery slower than others in the Caribbean region.

---

[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.

[2] The Executive Board takes decisions under its lapse-of-time procedure when the Board agrees that a proposal can be considered without convening formal discussions.

The external sector has held up well through these shocks. The non-oil current account (CA) balance, which mostly reflects developments in the tourism sector, has improved since mid-2000 reaching a balanced position in 2012. The overall CA balance, however, after being in surplus for years, showed volatilities in recent years reflecting oil sector developments. In 2012, it recorded a surplus of 5 percent of GDP.

The fiscal position worsened significantly in recent years. Preliminary data suggests that the overall fiscal balance recorded a deficit of 8½ percent in 2012. Notwithstanding measures taken in the pension and health sectors and efforts to collect tax arrears, the deficit widened sharply from pre-crisis years due to the tax rate cut and increased current expenditure. Fiscal consolidation is appropriately planned to start this year.

In 2013, real output is projected to grow by 1¼ percent. Robust tourism growth and some pick-up in consumption from projected deflation will support the subdued near-term recovery. A two percent deflation is projected in 2013 reflecting large utility price reductions in late 2012, and declining food and energy prices. The CA balance is projected to record a deficit of 9½ percent of GDP in 2013 due to the loss of oil exports.

Executive Board Assessment

In concluding the 2013 Article IV consultation with the Kingdom of the Netherlands—Aruba, Executive Directors endorsed the staff's appraisal, which made the following observations:

Aruba is recovering slowly from recent shocks. Two major shocks in the last four years, the global financial crisis and the shutdown of oil refining by Valero, have caused a recession that is deeper than in most other Caribbean countries. Although tourism, the mainstay of Aruban economy, rebounded quickly, Valero's shutdown has left harder-to-fill gaps in investment and non-tourism exports, with real GDP projected to reach its pre-crisis level only in 2018.

Downside risks dominate in the near-term, but medium-term prospects could be brighter. With a high dependence on tourism and oil imports, Aruba faces downside risks from renewed weaknesses in the global economy and higher oil prices. In the medium-term, there are upsides from resumption of oil refining by Valero, and large scale investment in renewable energy.

Putting the fiscal deficit on a downward path is an immediate policy priority. The authorities' efforts to counter the recession through cuts in the business turnover tax rate and higher current expenditure have rapidly increased central government's deficit and debt. In the absence of exchange rate policy options, rebuilding fiscal space is urgent. A reduction of the overall deficit to 6 percent of GDP in 2013 is appropriate. To ensure this outcome, directors recommend resisting possible expenditure pressures during the election year.

In the medium term, ambitious fiscal consolidation is needed. Without additional measures, the central government's fiscal deficit is projected to remain elevated posing risks to public debt sustainability. Financial deficits of the old age pension system (AOV) and payments for investment projects under the Public Private Partnerships (PPP) are likely to further widen the deficit beginning as early as 2014. A consolidation of around 8 percent of GDP during 2014-18 is appropriate, which would bring debt down to below 60 percent of GDP. To contain fiscal pressures from financial liabilities of the AOV and the PPP, it is important to implement further pension reforms and put a limit on the size of the PPP-related expenditure commitments.

External competitiveness needs to be strengthened to ensure a steady recovery. Aruba has managed to maintain its competitiveness in tourism through recent shocks partly due to authorities' strong initiatives to diversify source markets. With the US accounting for 60 percent of tourists, directors see further scope for market diversification. To ward off risks from a large negative net international investment position, and elevated financing requirements, Aruba would also need to strengthen its price and structural competitiveness through higher flexibility in the labor market and more enabling business conditions.

The accommodative monetary policy stance is appropriate. With slack in the economy, projected deflation and subdued credit growth, directors see no need for monetary tightening. The banking system's excess liquidity has increased substantially since mid-2012. In case credit demand picks up, a very low risk at this point, the authorities would need to mop up the excess liquidity by increasing the reserve requirement.

Aruba: Selected Economic Indicators, 2010–14

	2010	2011	2012	2013	2014
				Projections	
	(Percent change)				
Real economy					
Real GDP	-3.6	3.7	-1.2	2.3	3.0
Real domestic demand	-4.0	1.7	-1.7	-1.5	2.6
Consumption	-0.9	1.8	1.6	1.3	1.7
Private	-0.3	3.9	0.5	1.6	1.6
Public	-2.4	-3.2	4.5	0.7	1.8
Gross investment	-10.8	1.5	-10.2	-9.5	5.7
Exports of goods and services	-10.2	14.4	-5.3	3.7	2.2
Imports of goods and services	-9.0	8.8	-5.0	-1.7	1.8
	(Percent change)				
Consumer prices					
Period average	2.1	4.4	0.6	-1.5	1.5
End-period	-0.7	6.1	-3.7	0.7	2.3
	(Percent of GDP)				
Central government operations					
Revenues	27.7	21.4	22.3	23.6	23.0
Expenditures	31.3	29.3	30.9	29.7	29.4
Of which: capital	1.1	1.2	1.7	0.9	1.0
Overall balance	-3.6	-7.8	-8.5	-6.2	-6.4
Gross central government debt (percent of GDP)	55.9	61.2	67.0	72.3	75.0
Savings and investment (percent of GDP)					
Gross investment	31.0	32.6	29.7	27.0	29.0
Foreign saving	18.3	9.6	-4.9	9.4	9.0
Domestic saving	12.7	23.0	34.6	17.6	20.0
Balance of payments					
Current account balance	-18.3	-9.6	4.9	-9.4	-9.0
Oil	-18.8	-1.7	5.0	-7.8	-7.4
Non-oil	0.5	-8.0	-0.1	-1.6	-1.6
FDI	6.5	18.2	-5.6	3.4	5.1
Gross foreign assets of central bank (millions of U.S. dollars)	724	712	787	820	860
Gross foreign assets of central bank (months of non-oil imports of following year)	5.1	4.9	5.2	5.1	5.1
External debt (percent of GDP)	101.7	114.5	104.8	109.5	107.8
	(millions of local currency, unless otherwise indicated)				
Monetary					
NFA	1,309	1,286	1,342	1,400	1,432
NDA	1,845	1,873	2,077	2,121	2,278
Credit to private sector (year-on-year percent change)	1.2	3.5	2.8	3.1	4.0
Broad money	3,155	3,159	3,419	3,521	3,710
Deposits (year-on-year percent change)	-0.3	-0.1	8.2	3.0	5.3
Memorandum items:					
Nominal GDP (millions of Aruban florins)	4,279	4,566	4,555	4,613	4,860
Nominal GDP (millions of U.S. dollars)	2,391	2,551	2,544	2,577	2,715

Sources: Aruban authorities; and IMF staff estimates and projections.