FOSTERING ECONOMIC RESILIENCE IN ARUBA; FROM ROOTS TO ROUTES

Speech by Jane Semeleer, President of the Centrale Bank van Aruba, on the occasion of the CBA Economic Symposium on Fostering Economic Resilience in Small Island States on September 6, 2019.
Excellencies,

Distinguished guests,

Ladies and gentlemen,

Bon dia and bon bini to the first Economic Symposium of the Centrale Bank van Aruba (CBA) on the important topic of “Fostering Economic Resilience in Small Island States”.

1. Introduction

After seeing the devastating destruction by hurricane Dorian on The Bahamas, it is a shocking reality that Caribbean small islands, including Aruba, face major economic, social, and environmental vulnerabilities. With increasing geopolitical uncertainties, accelerating digital disruptions, and mounting ecological fragilities, the quest for economic resilience has become the prime directive for the sustainable development of small island states.

It is, therefore, no surprise that across the world, institutions such as the IMF, the World Bank, and the United Nations, in addition to several small island states, have placed economic resilience at the fore of their policies and programs.

To this end, in 2017 the IMF and the Government of Jamaica organized the High Level Caribbean Forum on “Unleashing Growth and Strengthening Resilience”, during which the IMF published an important book with the same title of the Forum.

During that Forum former IMF Managing Director, Mrs. Christine Lagarde, stated:

“Stronger economic growth is the essential foundation for a more resilient Caribbean. It is also a foundation for building defenses. Unfortunately, economic growth in the Caribbean has been low for several decades. This has led to rising social and economic challenges, including poverty, inequality, unemployment, and crime. While many authorities in the
Caribbean were successful in their efforts to create a stable macroeconomic environment, growth still remains elusive” (IMF, 2017).

We are honored today to have Dr. Inci Otker as one of our keynote speakers, who was the editor and a co-author of the previously mentioned IMF publication. This book, which is freely available online, is a must read to all policy advisors and policy decision makers. Dr. Otker also recently authored an article “Building Resilience in developing countries vulnerable to large natural disasters. Unfortunately, it is also an area unassessed in Aruba. So we look forward to Dr. Otker’s presentation and guidance this morning.

2. The Caribbean struggle with economic resilience

The IMF’s aforementioned book addresses several macroeconomic and structural challenges in the Caribbean, and discusses resilience-enhancing policies to confront the economic growth deficit in the Caribbean.

When reviewing the historical track record of select Caribbean states based on Table 2.1 of the aforementioned book, there are two interesting observations:

a. In general, Caribbean small states have shown less prominent real economic growth relative to non-Caribbean small states;

b. And yes, tourism-intensive Caribbean economies are weaker performers when compared to commodity exporters.

But what else is striking about this table?

Aruba is (and sadly remains) notoriously absent in international studies and regional benchmarks. It was at this important juncture in time, that we decided to fill as much as possible the Aruban void, and to conduct a comparative study of the Aruban economy vis-à-vis other select Caribbean economies based upon available data. This study, done by the Research team of the CBA under the guidance of Dr. Ryan R. Peterson, is titled “Fostering
Economic Resilience: from Roots to Routes”, and it is now available on the website of the CBA.

There are several reasons, some historical and some structural, why Aruba is not included in comparative Caribbean studies:

a. Firstly, Aruba is a sub-national island jurisdiction and part of the Kingdom of the Netherlands. As a non-independent island economy, it is, therefore, excluded from independent small states.

b. Secondly, Aruba is a high-income country with a relatively high nominal GDP per capita, making it less interesting for studies that address developing or fragile small states.

c. Thirdly, there is limited available data on Aruba. And if and when data is available, there are too many gaps in order to conduct reliable and timely analysis.

Not only are we excluded from international comparative studies, but evidence-based policy development in Aruba also remains deceptively elusive.

So, the key questions that emerge, which we will be addressing today during the symposium, are:

- How resilient is Aruba’s economy, when compared to other Caribbean small states?
- And more importantly, regardless of how we compare, how can Aruba strengthen its economy by fostering economic resilience?

In the fall of last year, our colleague at the CBA, Division Manager Mrs. Edwina Pereira, successfully defended her PhD on an interesting study titled “Small and Smart?”

In one of the first scientific studies to explicitly include Aruba and to conduct a comparative analysis of Aruba and the Caribbean, later in the morning Dr. Pereira will share some of her interesting findings and lessons learned, and shed light on the economic vulnerability and
resiliency of Aruba, with specific emphasis on the role of political-economic institutions. We look forward to her presentation.

Economic resilience is not a new concept, although its explicit consideration and inclusion in small island policies are of more recent nature. Already in 1978, thus more than 40 years ago, the renowned Caribbean economist Dr. William Demas stated that “… more fundamentally, the per capita income figure conceals the lack of internal economic resilience in the face of adverse economic impact of external origin. Thus, the Caribbean economies, in spite of high levels of per capita income, are riddled.”

Too often, we assume that high income equals high prosperity. Yet, high income and high nominal GDP levels may hide structural economic weaknesses and severe macroeconomic challenges. For one, a high GDP does not consider income distribution nor does it say anything about the degree of social inclusiveness, which are also important indicators and ingredients for a sustainable development.

3. What is the state and future of economic resilience in Aruba?

Over the past years, and with international discussions on the Sustainable Development Goals (the so-called SDGs), there is a growing need to take a deep dive beneath the surface of GDP and economic growth to be able to understand the structural and inner workings of small island economies in terms of economic resilience.

One important finding was that there is no ‘one-size-fits-all’ solution to economic resilience. This means that any successful comprehensive economic reform should be evidence-based and contextualized to the local realities of small island economies. The question is thus: what is the current state and future of economic resilience in Aruba?

While many resilience-enhancing economic reforms have been introduced in the Caribbean and Aruba, their track record performance remains mixed. It should be clear that simply
replicating foreign models or ‘copy-pasting’ policies to foster economic resilience in island states is unlikely to prove effective over time.

Furthermore, the pendulum swing of national policies over time, in addition to the disturbing structural lack of continuity, are huge barriers to fostering economic resilience.

Beyond policies, we also need to sincerely question our models and our assumptions. If we don’t, the alternative is that we simply proceed by doing the same thing (“business as usual”) and expecting, somehow magically, a better and more sustainable result. Yes, we need to continuously ask ourselves:

a. How can Aruba foster and strengthen its internal resilience in the face of adversity and increased turbulence?
b. Are our existing assumptions correct?
c. Are our present models sufficient?
d. Are our current policies adequate?
e. Are we able to continue walking along the same path or do we need to change route?
f. Are our social, political and financial institutions resilience ready? Should we assess that or not? How should we do that?

I’m not saying that these questions are simple and the needed actions to address deficiencies easy, but that they deeply matter if we are striving for the sustainable wellbeing of our island. As we know well, the things that matter most in life require unrelenting persistence, unselfish commitment, and incessant passion.

4. So what is this concept of economic resilience?

In quickly summarizing 50 years of theorizing, there are basically two schools of thought or “paradigms” on economic resilience particularly regarding small island states.

Traditionally, from a macroeconomic perspective, economic resilience is defined as the capacity of an economy to withstand and recover from external adversity. The usual
The metaphor is that of “bouncing back” after a shock or crisis. The capacity to withstand and recover from shocks without losing fundamental functionality, and adversely impacting growth in the medium term, is based on having continuously in place adequate foreign exchange reserves, fiscal space, and economic stabilizers.

The second paradigm of economic resilience looks beyond the absorption capacity of economies, and focuses on the capability to adapt, change, and learn. By analogy, this is bouncing forward, thus not just bouncing back. Resilient economies are also characterized by the capacity to redesign and reinvigorate growth beyond recovery.

Rather than assume a static balance, economic resilience is viewed from evolutionary economic perspective, and is inspired by the works of Charles Darwin and Joseph Schumpeter. In evolutionary economic terms, what is the rate of participation and innovation in the labor market; how productive are investments; what is the pace of technological progress; and what is the ease of doing business?

While the two schools of thought are different, they complement each other in a holistic way. Similar to transformation of a caterpillar into a butterfly, economic resilience reflects the dual capability to absorb and adapt, and to buffer and rebuild. In essence, the cultivation of strong roots and the creation of new routes.

The rise and importance of economic resilience, especially in small-island states, are largely explained by the long-standing recognition that smaller and relatively more open economies face significant vulnerabilities, due to their extreme exposure and susceptibility to external shocks and risks. The economic vulnerabilities of the Caribbean island states are well-acknowledged.

5. Perils in paradise. Small island economies increasingly experience major disruptions

Exposed to global currents and turbulences, small island economies have increasingly experienced disruptions and disasters over the past two decades. Examples are:
a. Financial crises and economic recessions, related among others to the 9-11 event and the financial crisis of 2008 and the resulting commodity distress, and

b. more recently, the Brexit tribulations and the U.S. trade tensions with China and Europe, which are challenging the existing global economic landscape.

c. Closer to home, the socio-political turmoil in Venezuela, while the rising tensions in Brazil and Argentina compound existing risks and threats.

d. Lastly, natural disasters and climate change have deeply left their mark in the Caribbean. Hurricanes, earthquakes, and floodings occur almost annually and are a huge burden on government finances, business investments, and economic growth.

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In general, these social, economic, and environmental disturbances are not new. What is relatively new is the fact that over the past two decades these individual developments are accelerating and converging. There is, thus, an aggravating effect on economic vulnerability.

6. Beyond external shocks; why internal preparedness is crucial

Next to external shocks, there are also internal stressors or hidden threats that amplify economic vulnerability. Unlike sudden events and unexpected disasters, internal stressors describe the slow-burning challenges in small-island economies.

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Like the lazy frog in a slowly heating water, these are developments that “simmer” for an extended period of time before surging and surpassing existing thresholds. The slow-burn is oftentimes not directly or immediately visible. It is a hidden threat that remains dormant until it surges to the surface, as shown on the slide which depicts garbage recovered from Aruba’s seabed.

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Too often and regretfully, it suddenly becomes obvious in the rear-view mirror, when it has already transpired. The threat of a slow-burn starts as a very small flame, yet may develop into a raging wild fire if not recognized and resolved in a timely and diligent manner.

When internal pressures and stress build up over time and suddenly arise, they often are labeled as a ‘debt crisis’, a ‘social crisis’, or a ‘waste crisis’. Important to note here is that unlike external shocks, internal burns are usually caused by neglect, complacency or willful ignorance.

7. So how economically vulnerable is Aruba?

Based on regional data and standard economic indicators, evidence indicates that Aruba is one of the most vulnerable economies in the Caribbean, especially when compared to select tourism-dependent economies. In relative terms, Aruba scores the highest on trade openness, which reflects the combination of imports and exports to GDP. More importantly, the high concentration and specialization in tourism are additional sources of Aruba’s economic vulnerability.

We also notice that Caribbean small states tend to be more vulnerable than other regional small states. These findings should not be surprising in light of Aruba’s long-standing tourism growth, dating back to the 1960s, and the subsequent tourism boost during the 1990s and thereafter.

The evidence does, however, raise an interesting question as to mitigating and reducing the economic vulnerability of Aruba: Can Aruba mitigate trade openness and tourism concentration?

While some may argue that these are a given, from a macroeconomic perspective there are some policy degrees of freedom to moderate import and export dependency by, for example, fostering domestic renewable energy generation, domestic food production, and export diversification.
Fossil fuel and food imports are two of the main contributors to total imports and are a notable source of price volatility and inflation in Aruba. Strengthening the external sector, thus, entails not only diversifying service exports, but also substituting imports, which is not a new concept at all. With recent innovations, this concept is even more interesting to venture upon. Minister Xiomara Ruiz-Maduro will enlighten us on this important topic in her presentation, which we look forward to.

Now what happens when you are a small open economy with a high degree of vulnerability, and faced with external shocks and internal pressures?

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The evidence indicates that the combination of these structural conditions and events have a concentrating and amplifying impact, and put a major strain on economic growth. In terms of Aruba’s realized and potential economic growth, the findings reveal that the increasing economic vulnerability of Aruba is transmitted into significant economic volatility.

Not only is Aruba one of the most vulnerable economies in the Caribbean, it has one of the highest rates of economic volatility. The metaphor of a bouncing ball going up and down, yet stuck in the same place for a long while, is no exaggeration.

When comparing Aruba to regional averages, what stands out is, first of all, the relatively high and increasing volatility in real GDP growth. In research terms, the (standard) deviation from the average long-term growth path is considerable. In simpler and direct terms: When things are good in Aruba, they are really good. But when things are bad, they are awful.

Additionally, while economic volatility has increased, real output diminished in less than two decades to an estimated 1.9 percent. The long-term effect has been a structural unwinding of our economy, with medium-term projections of no more than 1.1 percent real output.

8. How can Aruba bounce forward?
When the economy is faced with a flux of external shocks and internal stressors, and fluctuates at that rate, it demands a huge amount of resilience to safeguard stability and secure sustainable growth and development.

Henceforth, the question is not only how does Aruba “bounce back”, but more importantly, how does it “bounce forward”? 

In the study that the CBA conducted, macroeconomic analysis suggests that Aruba lags considerably in terms of economic resilience. Whereas the Aruban economy is highly vulnerable and volatile, the capacity to absorb shocks and adapt to change is disappointingly limited.

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Although it is not the worst performer amongst Caribbean small island peers, Aruba certainly does not measure up to the required economic resilience. Aruba lags other Caribbean small states. While one could contend that these other small states are larger commodity exporters, this would not address the deficiency in required economic resilience, which our economy badly needs in terms of its vulnerable state.

So how do we foster economic resilience in Aruba?

In CBA’s recent publication, “Fostering Economic Resilience: from roots and to routes”, several policy recommendations are provided for fostering economic resilience. As the five anthems of the local cayena flower, the report presents five pillars for economic resilience.

Some of the pillars are well-known and have been communicated by the CBA, and other institutions, for many decades now. Other pillars are of more recent times and are slowly evolving within the Aruban economy. What is important is not the individual pillar, but the integration and synergy between the pillars to build a strong foundation that supports and fosters sustainability at the same time.

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The first pillar addresses fiscal sustainability and the need to create fiscal space. When comparing Aruba to other Caribbean small states and relative to time, Aruba has one of the
highest debt and tax burdens. There is, thus, limited fiscal space to absorb any shock or counter a crisis, without having a big negative impact on the other sectors of the economy.

While the fiscal and tax reforms are underway, concerted efforts need to be placed on improving tax compliance and tax administration, in addition to controlling government expenditures. Tax sustainability is a new concept and should have the urgent attention of the Government as well. Miss Shekinah Dare of the Centrale Bank van Curacao & Sint Maarten will provide some insights on this concept. We look forward to her presentation as well.

Fiscal innovation in terms of an independent fiscal council and an independent tax authority are certainly within reach. Likewise, the adoption of digital tax governance is highly recommended.

The second pillar focuses on maintaining monetary stability and safeguarding the value of our florin. Assuring adequate foreign exchange reserves is essential and is one of the core mandates of the CBA. In comparison to its Caribbean peers, Aruba lags slightly in terms of comparative reserve adequacy.

Recently, the IMF confirmed that the level of reserves is currently sufficient, yet prudence and diligence are advised. The pressure on monetary reserves stems not only from external shocks, but also from excessive public debt repayments and interest payments. Fiscal reform is, thus, not only relevant to debt management but also crucial to monetary and financial stability.

In a related fashion, the third pillar focuses on strengthening the external sector by diversifying imports and exports. Reducing oil imports and accelerating renewable energy capacity would have a large positive contribution to both monetary and economic stability.

Although Aruba ranks average in the Caribbean, and whereas initial steps have been made, concerted efforts need to be accelerated to build a 'fossil-free' economy. Similar to renewable energy, several local agricultural programs have been launched, yet need nurturing in order to grow into sustainable ventures.
While the first three pillars are necessary to strengthen the absorption capacity of the Aruban economy and would enhance the required buffers, they are not sufficient. Yes, we need to do more and work smarter.

The fourth pillar focuses on improving the flexibility and productivity of the labor market. When comparing Aruba to the Caribbean, two developments stand out:

a. Our general unemployment rate is relatively low, yet youth unemployment and ‘non actives’ are high.

b. More concerning is the low and diminishing labor participation over time, which indicates a “shrinking” labor market and/or an increase in the informal market.

c. To add to this mix, there is a structural decline in labor productivity since the turn of the century and relatively stagnant income distribution.

Similar to fiscal and energy reforms, revamping and redesigning the labor market are urgently required to improve youth employment and employability, reinvigorate workforce participations and to reshape the skillsets needed for this century, as well as to address labor market rigidity with responsible regulation and legislation.

It goes without saying that education innovation and educational reform need to be implemented in tandem with labor and energy reforms.

And then there is one last pillar left for fostering economic resilience.

Integral to the first four pillars are technology and innovation, i.e., the fifth pillar. These are needed to foster the innovation capability of the Aruban economy. Technological advancements and digital technologies play an important role in realizing the benefits of fiscal reform, energy reforms, new food production techniques, and labor productivity and skills.

More importantly, innovation and entrepreneurship are at the heart of a thriving commerce and private sector. While there are many initial efforts underway, united and coordinated national efforts need to be further strengthened.
9. Conclusion

Let me conclude by emphasizing once more that while fiscal reforms, reserve adequacy, economic diversification, labor market flexibility, and technological innovation are all important, it is the synergy between these pillars and the joint policy actions that foster economic resilience.

The value chain of economic resilience is, thus, only as strong as the weakest shackle. This puts a premium not only on the individual government reforms and private sector initiatives, but underscores the fundamentals of strengthening our institutional capacity and foresight.

Similar to the cayena pistil that supports the anthem, we need institutional capabilities to implement comprehensive economic reforms to nurture economic resilience. Beyond the “usual suspects” of fiscal and monetary institutions, several other non-financial institutions are pivotal and include:

   a. Labor institutions and employers;
   
   b. Educational institutions and agencies;
   
   c. Social institutions and non-governmental agencies; and last but not least
   
   d. Innovators and entrepreneurs to redesign our economy and reinvigorate productivity.

Henceforth, fostering the economic resilience of Aruba relies on both public and private sectors, as well as on the civil society. This institutional “trinity” is not a ‘nice to have’; it is a ‘must have’!

Without the co-lead of the private sector, fostering any comprehensive economic reform is bound to fail. Ultimately, public institutions, although essential, can only create the right conditions and the correct environment to foster economic resilience.
Distinguished guests,

Ladies and gentlemen,

Yes, Aruba is small, and it has faced some stormy weather in its relatively young history. And yes, we have braved adversity and have overcome many challenges and obstacles. However, times are transforming, and living within the boundaries of a small-island state, we should never lose sight of our frail environment and ecology, as well as the well-being of our community.

Remember that no calm sea ever made a strong and agile captain. Because of their fragility, small economies need to be driven by unwithering aspirations and uncanny abilities to be able to thrive with tenacity and innovate with integrity. This combined with the right mix of nimbleness and agility, we can transform our economy and foster the badly needed resilience. We don’t need a crisis to achieve this, believe me!

Allow me to finish with a famous quote by Richard Buckminster Fuller “We are called to be architects of the future, not its victims.”

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Thank you for your attention!

Masha danki!

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