Economic Outlook

April 2022

Please note that the April 2022 Economic Outlook includes a balance of payment forecast while the December 2021 Economic Outlook does not. Output projections do not differ between the publications.

CENTRALE BANK VAN ARUBA

Abstract

In 2021, the Aruban economy continued its recovery path set forth in the second half of 2020. **Based on December 2021 GDP forecast estimates,** real GDP grew by an estimated 15.5 percent under the baseline scenario (17.9 percent in the optimistic scenario and 13.0 percent in the pessimistic scenario). The anticipated economic recovery in 2021 was spurred by the speedy recovery of tourism after international travel restrictions were lifted, as well as the continued implementation of the Government of Aruba's (GOA) wage subsidy and FASE programs, which helped to maintain private consumption.

In 2022, the sustained recovery of the tourism sector and the pick-up in private investment are expected to further motivate real GDP growth. The growth rate is expected to range from 3.1 percent (pessimistic) to 12.0 percent (optimistic), with a baseline real GDP growth of 7.7 percent.

Nominal growth in tourism service exports ranged between 42.4 percent (pessimistic) and 59.6 percent in 2021 (optimistic) compared to a year earlier, with baseline growth of 51.0 percent. Compared to 2021, anticipated growth in nominal tourism service exports for 2022 will vary between 19.5 percent (pessimistic) and 46.6 percent (optimistic), with an expansion of 33.8 percent in the baseline scenario. The tourism sector recovery, as well as the rebound in private investment (in 2022), will likely lead to additional income for local employees. This, in turn, is expected to push up the demand for goods and, by extension, the import of goods.

Varying intensity levels in the rate of tourism recovery drives a forecasted current account surplus of respectively Afl. 46.4 million (pessimistic), Afl. 404.0 million (baseline) and Afl. 767.5 million (optimistic) at the end of 2022. Since tourism inflows indirectly affect foreign direct investment as well as foreign government borrowings, the projected financial account surplus stands at Afl. 372.5 million in the pessimistic scenario, 480.5 million in the baseline scenario and Afl. 585.0 million in the optimistic scenario. The current and financial account give rise to anoverall balance of Afl. 648.3 million, Afl. 901.4 and Afl. 1,157.0 million under the pessimistic, baseline and optimistic scenario.

As a result, international reserves (excluding revaluation differences) are projected to rise under all scenarios in 2022. Specifically, international reserves are expected to expand to respectively Afl. 3,338.9 million, Afl. 3,685.0 million or Afl. 4,035.4 million under the pessimistic, baseline, and optimistic scenario. In 2022, international reserves are thus foreseen to remain comfortably above the threshold level of three months of current account payments. In addition, projected official reserves are expected to continue within the optimal range of the IMF ARA metric. The upswing in reserves in 2022 largely stems from the sustained tourism recovery, as well as the government financing its deficit externally. Nevertheless, the expected rise in import of goods and services forms a partially offsetting factor.

Centrale Bank van Aruba

Table of contents

1. Introduction

The Research Department (RD) of the Centrale Bank van Aruba (CBA) updated its Gross Domestic Product (GDP) estimate for 2021 based *upon the latest gains in economic development and available data up to and including October 2021*[1]*.* In addition, the RD made its first projections for the year 2022. This economic estimate and forecast follows new information on public consumption, updated expectations regarding the strength of the recovery of the tourism sector, and recent insights into public and private investment. The baseline scenarios are based on the assumption of the most likely developments with regard to the different components of GDP (i.e., consumption, investment, imports, and exports). A pessimistic and an optimistic estimate and scenario complement the baseline estimate in 2021 and scenario in 2022. These additional scenarios deviate from the baseline based on the expected speedy recovery in tourism, which in turn affects consumption, investment, and import and export levels.

Forecasts indicate that the Aruban economy will continue its path to recovery, albeit subject to heightened downside risks in 2022. In 2021, real GDP is estimated to have grown by 17.9 percent. (Chart 1). This growth in 2021 followed mainly from the resurgence in tourism exports and to a lesser extent from the heightened consumption as a result of the continued implementation of the GoA's wage subsidy and FASE programs. During 2022, real output is projected to expand by 7.7 percent under the baseline scenario, 12.0 percent in the optimistic scenario, and 3.1 percent under the pessimistic scenario. Compared to 2021, the main drivers of economic growth in 2022 are expected to be the tourism sector and private investment, while the GoA's support programs came to a halt in December 2021.

The RD of the CBA also recently updated its balance of payments (BOP) and foreign exchange reserves forecast for 2022. These forecasts are based upon available data up to and including November 2021. The latest BOP forecast follows chiefly from updated expectations regarding the strength of recovery of the tourism sector. The tourism recovery affects the BOP through (tourism) exports, imports to cater to tourism and domestic demands, and investment. The speed of economic recovery also affects the size of the fiscal deficit and subsequent government borrowing needs. To the extent that the government finances its borrowing needs on the external market, government borrowing will impact the financial account and lead to an inflow of foreign exchange.

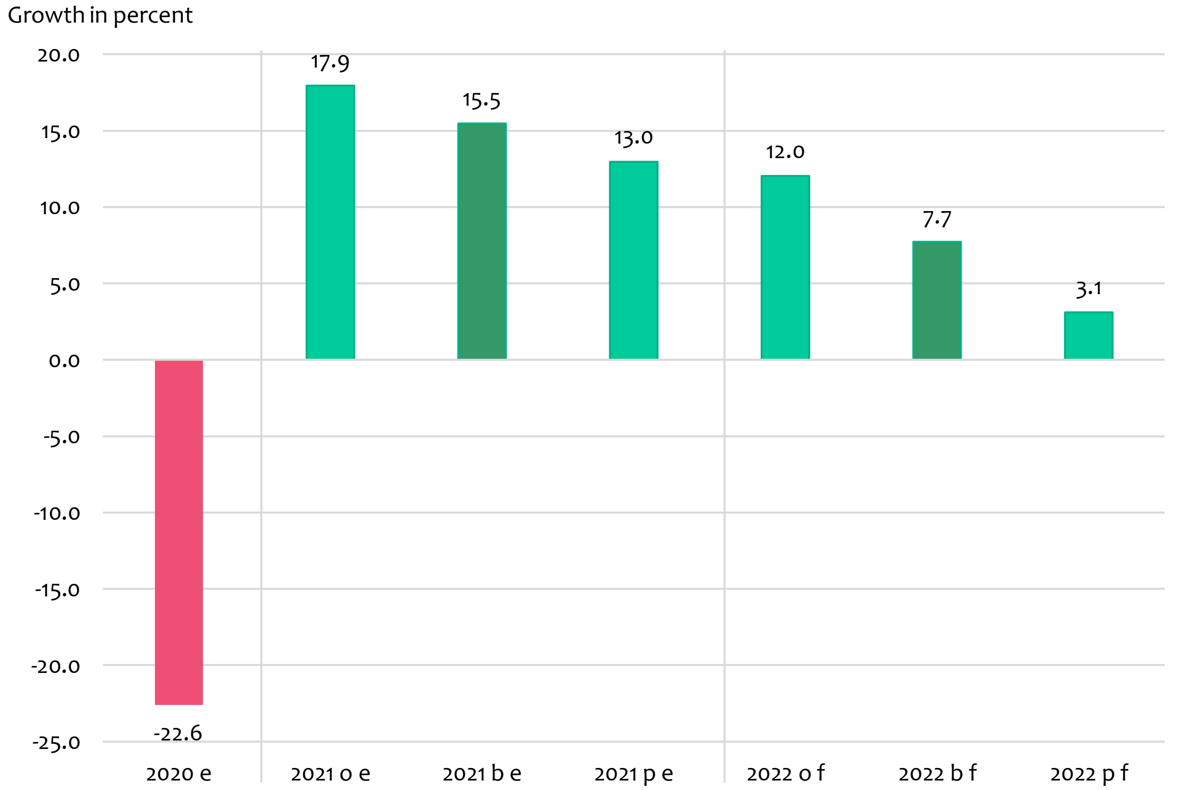
The baseline scenario assumes the most likely developments in (tourism) exports, consumption, investment, and imports. In light of the uncertainty surrounding the COVID-19 pandemic and the effect that it has on foreign exchange reserves, the RD considers a pessimistic and an optimistic scenario. These two alternative scenarios deviate from the baseline based on a downside and upside risks in the expected recovery in tourism, and government foreign borrowing needs.

Estimated international reserves (excluding revaluation differences) increase under all scenarios in 2022. Conditional on the pessimistic, baseline, and optimistic scenario, forecasted international

[1] The Real GDP growth estimates for 2021 are based on the real GDP growth forecast for 2021 (December, 2021).

reserves climb to respectively Afl. 3,338.9 million, Afl. 3,685.0 million or Afl. 4,035.4 million. As a result, in 2022, international reserves are again expected to remain well above the threshold level of three months of current account payments as monitored by the Central Bank of Aruba. As was the case in 2021, the anticipated growth in reserves will be mostly due to the resilient tourism recovery as well as the expected foreign financing of the GoA's deficit. Accelerated imports nevertheless temper the mentioned upward pressures, with imports following the tourism recovery and the associated pick-up in domestic demand.

Chart 1: Real GDP growth 2020 - 2022



Source: CBA
e = estimate, f= forecast, o = optimistic, b = baseline, p = pessimistic

2. Economic forecast

2.1 Gross domestic product and its components

Several scenarios were produced for the year 2022. For 2021, the following estimates are distinguished:

1. **Baseline estimate 2021: The tourism sector is expected to remain the primary driver of economic growth in 2021, as it continues to make a robust recovery during the year**. The number of stay-over visitors is projected to reach 69.0 percent of the 2019

level, while daily spending by tourists is anticipated to gradually decrease to $470.47 at the end of 2021 compared to $603.11 registered a year earlier. The foreseen contraction in daily spending by tourists is expected to have a dampening effect on the recuperation in the level of tourism credit, despite a significant recovery in the level of stay-over visitors. To be specific, the growth in tourism service exports is estimated at 51.0 percent compared to 2020 (with the 2021 level at 77.2 percent compared to the 2019 level). The estimate assumed that the FASE and the wage subsidy program will be discontinued as of year-end 2021. The availability of the programs is projected to drive up real private consumption by 5.0 percent under the baseline estimate. The upswing in the tourism sector paired with the government's assistance programs positively impacted the unemployment rate in 2021, which is estimated to have fallen to 9.5 percent. The baseline estimate further assumes a general increase in prices as the 12-month average inflation is foreseen to result in 0.5 percent, steered primarily by rising prices in the energy component (i.e., gasoline prices). Private investment is envisioned to decline in 2021, as there are few new construction projects in 2021. On the other hand, imports are projected to increase in 2021 following the rebound in the tourism sector and private consumption, which offset the significant decline in investment.

2. **Pessimistic estimate 2021: Compared to the baseline estimate, the pessimistic estimate assumes a slower recovery in stay-over visitors (65.0 percent of the 2019 level).** This sluggish gain leads to a lower growth in tourism service exports, which is foreseen at 42.4 percent compared to 2020. The assumed developments result in an estimated unemployment rate of 9.7 percent in 2021, which is slightly higher than the unemployment rate in the baseline scenario. Nonetheless, the picking up in the tourism sector, supported by the continuation of the FASE and wage subsidy programs are sufficient to achieve an expected growth in real private consumption of 4.9 percent. The pessimistic estimate takes into account a larger extent of delays in construction, resulting in a diminished investment amount vis á vis the baseline estimate. Nonetheless, the brisk recovery in tourism activities is enough to anticipate a positive growth in imports. The pessimistic estimate assumes the same inflation rate as in the baseline estimate.

3. **Optimistic estimate 2021: The number of stay-over visitors is expected to rise to 73.0 percent of the 2019-level.** While the rebound in the tourism sector is relatively stronger, private consumption remains relatively stable. This is due to the expected substitution of FASE or wage subsidy income for wages, while not many new jobs are anticipated to be created. As a result, disposable income is likely to remain virtually unchanged. Regarding private investment, fewer delays are expected, leading to a higher investment. Following the greater increase in investment and tourism exports, imports is projected to be more elevated.

For 2022, the following scenarios are identified:

1. **Baseline Scenario 2022: The tourism sector is anticipated to continue its recovery in 2022, topped off by a pick-up in investment.** The number of stay-over visitors in the baseline scenario is expected to amount to 95.0 percent of the 2019-level. In addition, tourism credits per night are assumed to have normalized at levels that are slightly higher than the pre-pandemic levels of 2019. Consequently, tourism service exports in nominal terms are forecasted to grow by 33.8 percent compared to 2021. With this growth, the level of tourism credits in 2022 surpasses the pre-pandemic level of tourism credits, standing at 103.4 percent of the 2019-level. The assumption is that the FASE and the wage subsidy programs will be halted by the end of 2021, and will not be available in 2022. Nonetheless, the rebound in the tourism sector is expected to lead to a lower level of unemployment compared to 2021 (7.7 percent). The latter has a positive effect on private consumption. This is complemented by a slight growth in public consumption, as (in all scenarios) government consumption and investment are expected to remain relatively stable compared to 2021, due to spending cutbacks as well as liquidity constraints. Even so, the projected relatively higher level of inflation in 2022 leads to a dampening in both private and public consumption in real terms.

   In contrast to 2021, a pick-up in investment is expected, as projects that experienced delays in 2020 and 2021 are likely to start in 2022. Imports are projected to increase in 2022, due to the expansions in total exports and private investment. The forecasted 12-month average rate of inflation for 2022 is expected to reach 2.7 percent, mainly driven by utility prices. Hereby, the assumption is that the price of oil barrels used in the production of energy will not be hedged at the same price as in 2021, but will be bought at the reigning market prices or hedged at a higher price than in 2021.

2. **Pessimistic Scenario 2022: While a recuperation is still expected in the tourism sector, and private investment is projected to strengthen, both do so at a slower pace compared to the baseline scenario for 2022.** In the pessimistic scenario, the predicted number of stay-over visitors reaches 80.0 percent of the 2019-level. As a result, tourism credits would increase by 19.5 percent in nominal terms compared to 2021, which brings it to 87.0 percent of the 2019-level. As is the case in the baseline scenario, FASE and wage subsidy programs are assumed to be discontinued in 2022. Nonetheless, unemployment is expected to drop further compared to 2021 (8.7 percent). While the latter positively affects private consumption, and public consumption is expected to edge up, the accelerated pace of inflation in 2022 is likely to have a dampening effect on private consumption and public consumption. With regard to investment, a pick-up is foreseen, albeit at a lower level than in the baseline scenario. The projected rate of inflation in the pessimistic scenario is equal to that in the baseline, i.e., 2.7 percent.

3. **Optimistic Scenario 2022: In the optimistic scenario, a stronger upswing is foreseen in the tourism sector as well as in investment, compared to the baseline scenario for 2022.** The optimistic scenario takes into account a number of stay-over visitors that exceeds the pre-pandemic level (110.0 percent of the 2019-level). The resulting growth in tourism service exports is projected at 46.6 percent in nominal terms compared to 2021. The corresponding level of tourism service exports equals a recovery of 119.7 percent in terms of the 2019-level. In the optimistic scenario, the assumption remains that the FASE and wage subsidy program are discontinued in 2022. Given the strong recovery in the tourism sector, however, the rate of unemployment is projected to be lower than in 2021 (7.4 percent). This is foreseen to have a positive effect on private consumption. Furthermore, a small expansion is anticipated in nominal public consumption. The level of inflation in 2022, however, leads to a dampening in both components in real terms. Investment is also expected to rebound, with the pace of construction more likely to be faster than in the baseline scenario. The projected rate of inflation in the optimistic scenario stands at 2.7 percent.

In all scenarios for 2022, the expected rate of inflation remains a major source of uncertainty. Globally, various factors are producing upward pressure on the level of prices, such as supply chain disruptions due to pandemic and weather disturbances. In turn, these are expected to push up the prices of imported goods. In addition, the volatility in oil prices also may result in higher utility prices domestically, particularly if the barrels of oil used in the production of water and electricity are bought at the expected market prices in 2022 or hedged at a higher price than in 2021. Consequently, the projected real GDP figures for 2022 may result lower than presented in this economic outlook.

Based on the aforementioned assumptions and scenarios, the following estimate and forecast results emerge for the respective GDP components.

1. *Baseline estimate 2021*

A real GDP growth of 15.5 percent is estimated under the 2021 baseline estimate, mainly pushed by the recovery in real tourism exports (+56.7 percent). The recuperation in tourism exports, paired with the GoA's financial support to individuals and businesses, under the execution of the FASE and wage subsidy programs, is expected to have further driven up real private consumption (+5.0 percent). The latter likely offset the small decrease in real public consumption (-0.5 percent), resulting in an expansion of 3.3 percent in real total consumption. On the other hand, real total investment is estimated to have contracted in 2021 (-20.5 percent), following decreased investment appetite in the private sector and limited fiscal space for government investment. Real imports are anticipated to have risen by 9.7 percent, derived from the movements in the other GDP components.

2. *Pessimistic estimate 2021*

The pessimistic estimate for 2021 assumes a slower recovery rate in tourism compared to the baseline estimate, while the wage subsidy and FASE programs remain in place throughout the year. Under this estimate, real GDP is estimated to expand by 13.0 percent, due primarily to growth in real tourism exports (+47.8 percent), real other exports (+19.3 percent), and real private consumption (+4.9 percent). The upward development in real private consumption compensates for the decline in real public consumption (-0.5 percent), resulting in a rise in real total consumption of 3.2 percent. Meanwhile, real investment is expected to have declined (-23.6 percent) relative to the baseline estimate. Lastly, the pessimistic estimate estimates an expansion of 6.5 percent in real imports, attributable to the increase in exports and total consumption.

3. *Optimistic estimate 2021*

The optimistic estimate presumes a real GDP growth of 17.9 percent for 2021, based on a swift recuperation of tourism sector activities as well as an expansion in private consumption. The recovery within tourism exports is due to a sharp increase in expected tourism arrivals and tourism credits. Meanwhile, total investment is likely to have decreased (-17.4 percent) compared to the baseline estimate. Despite reduced total investment, real imports are anticipated to have surged by 12.8 percent, following upward movements in real tourism export (+65.7 percent), real other exports (29.3 percent), and real private consumption (+5.1 percent).

4. *Baseline scenario 2022*

In the baseline scenario, real GDP grows by 7.7 percent compared to the 2021 baseline scenario. This growth is anticipated to be mainly driven by the expected sustained recovery in real tourism exports (+28.7 percent), and upturn in real total investment (+5.9 percent). The increase in total investment, in turn, is anticipated to follow the improvement in private investment (+6.1 percent), partly offset by a contraction in real public investment (-2.7 percent). The cessation of the FASE and wage subsidy program is expected to lead to a projected marginal decrease in private consumption (-0.9 percent). Amplified by a decline in public consumption (-0.8 percent), these developments are expected to negatively impact real total consumption (-0.9 percent), compared to the 2021 baseline scenario. Real imports are anticipated to go up by 10.0 percent, mainly due to the forecasted growth in real tourism exports (+28.7 percent), real other exports (+3.5 percent), and real total investment (+5.9 percent).

5. *Pessimistic scenario 2022*

Real GDP growth of 3.1 percent is projected under the pessimistic scenario. The lower rate of growth is expected to follow from a slower recovery in real tourism exports (+15.0 percent) and real total investment (3.8 percent), compared to the baseline scenario. Due to the relatively moderate recovery of real tourism exports and the halt of the FASE and wage subsidy program, a slightly larger contraction in real private consumption (-1.5 percent) is forecasted, compared to the baseline scenario. In addition, real public consumption (-0.8 percent) is also foreseen to decrease, leading to a downturn in real total consumption (-1.3 percent). The main driver behind the growth in real total investment is the anticipated rise in private investment (+4.0 percent), while real public investment (-2.7 percent) is expected to decline. Even though real tourism exports would rise, real other exports turn into a downturn (-1.5 percent). These developments ultimately lead to an expansion in real total exports of 10.6 percent. Following the upturns in real total exports, and real total investment, real imports expand by 4.4 percent.

6. *Optimistic scenario 2022*

Due to the anticipated stronger rebound in real tourism exports (+41.0 percent) and real total investment (+7.7 percent) in the optimistic scenario, real GDP growth of 12.0 percent is foreseen. In the optimistic scenario, the expansion in real tourism exports is matched by a rise in real other exports (+8.5 percent), leading to an increase in real total exports of 39.1 percent. While a more positive performance of the tourism sector is expected, the discontinuation of the FASE and wage subsidy program dampens real private consumption (-0.7 percent), albeit to a smaller extent than in the baseline scenario. The anticipated growth in real public consumption also remains negative (-0.8 percent), leading to a decline in real total consumption of -0.7 percent. Real total investment, on the other hand, is likely to increase due to an expansion in real private investment (+8.0 percent), which is partly counterbalanced by a drop in real public investment (-2.7 percent). Following the developments in the aforementioned GDP components, real imports is anticipated to grow by 15.2 percent.

Table 1: Growth of real GDP and its components 2020-2022 (in percent)							
Indicator	2020 e	2021 o e	**2021 b e**	2021 p e	2022 o f	**2022 b f**	2022 p f
Current Outlook							
GDP	-22.6	17.9	**15.5**	13.0	12.0	**7.7**	3.1
Consumption	-7.5	3.4	**3.3**	3.2	-0.7	**-0.9**	-1.3
Private consumption	-11.6	5.1	**5.0**	4.9	-0.7	**-0.9**	-1.5
Public consumption	3.3	-0.5	**-0.5**	-0.5	-0.8	**-0.8**	-0.8
Investment	-20.9	-17.4	**-20.5**	-23.6	7.7	**5.9**	3.8
Private investment	-21.4	-16.9	**-20.1**	-23.3	8.0	**6.1**	4.0
Public investment	-0.7	-32.1	**-32.1**	-32.1	-2.7	**-2.7**	-2.7
Exports	-45.3	54.6	**46.8**	39.1	32.7	**22.2**	10.6
Tourism exports	-51.6	65.7	**56.7**	47.8	41.0	**28.7**	15.0
Imports	-27.4	12.8	**9.7**	6.5	15.2	**10.0**	4.4

Source: CBA e = estimate, f= forecast, o = optimistic, b = baseline, p = pessimistic

2.2 Nominal growth rates

For 2021, nominal GDP growth hovered between an expansion of 11.3 percent and 16.7 percent, with an estimated baseline of 14.0 percent (Table 2). For 2022, a baseline nominal GDP growth of 12.2 percent is anticipated. This nominal output projection ranges between 6.8 percent and 17.3 percent, with the outcome depending largely on which scenario plays out.

Table 2: Growth of nominal GDP and its components 2020-2022 (in percent)							
Indicator	2020 e	2021 o e	2021 b e	2021 p e	2022 o f	2022 b f	2022 p f
Current Outlook							
GDP	-24.8	16.7	**14.0**	11.3	17.3	**12.2**	6.8
Consumption	-9.9	3.9	**3.8**	3.7	1.5	**1.3**	0.9
Private consumption	-12.8	5.6	**5.6**	5.4	2.0	**1.8**	1.1
Public consumption	-2.3	-0.3	**-0.3**	-0.3	0.2	**0.2**	0.2
Investment	-21.0	-15.9	**-19.0**	-22.2	10.7	**8.8**	6.7
Private investment	-21.5	-15.3	**-18.6**	-21.8	11.1	**9.1**	7.0
Public investment	-0.9	-30.8	**-30.8**	-30.8	0.0	**0.0**	0.0
Exports	-43.6	51.2	**43.6**	35.9	37.8	**26.7**	14.5
Tourism exports	-48.9	59.6	**51.0**	42.4	46.6	**33.8**	19.5
Imports	-26.8	16.5	**13.3**	10.0	18.0	**12.7**	7.0

Source: CBA e = estimate, f= forecast, o = optimistic, b = baseline, p = pessimistic

Box A: Inflation

This box contains explanatory notes about the inflation expectations inherent in the current GDP forecast.

Inflation: A rise in the general level of prices of goods and services that households acquire for the purpose of consumption in an economy over a period of time.
End of period (EOP) inflation: The percentage change in the general level of prices of goods and services in a period, compared to the same period in the previous year.
12-month average inflation: The average percentage change in the general level of prices of goods and services in the last 12 months, compared to the preceding 12 months.

In the current GDP forecast, the projected *12-month average inflation* rates for 2021 and 2022 are 0.5 percent and 2.7 percent[2], respectively. They follow from Consumer Price Index (CPI) data for Aruba up to and including September 2021, as well as global oil forecast data up to and including October 2021. With regard to local price developments, the assumption is that there are no changes in water and electricity prices for 2021, given that the price per fuel oil (HFO) barrel used in the production of water and electricity is hedged at lower than market prices, while for 2022, no hedge is assumed. Consequently, the price per barrel of oil used in the production of water and electricity is assumed to follow the expected higher international oil prices.

In addition to the volatility in oil prices, other major developments present risks to the inflation forecast, many of which are tilted in positive directions. These include potential fiscal measures needed to cope with the COVID-19 crisis prior to the planned fiscal reform of January 2023, as well as supply chain distortions due to pandemic, weather disturbances, and geopolitical tensions. As a result, the real GDP forecast figures, particularly those for 2022, may be lower than presented in the current outlook.

[2] At the time of analysis (November 2021), Brent crude oil prices were hovering around 80 US dollars a barrel. Hence, this forecast does not consider the recent surge in oil prices.

2.3 Outlook assumptions and risks

Given the uncertainties related to the pace of economic recovery following the COVID-19 pandemic, a number of assumptions were made to arrive at the various scenarios. The main assumptions and risks to the scenarios are:

- **Inflation.** Internationally, there is rising uncertainty about future inflation developments and the associated downside risks. As the International Monetary Fund (IMF) pointed out, inflationary pressures may prove to be non-transitory. For the year 2022, there is a substantial level of uncertainty about the general level of prices in Aruba. The source of this uncertainty is twofold. First, the price of fuel oil (HFO) barrels used in the production of water and electricity is uncertain. Local utility prices could experience upward pressure if these barrels are bought at the expected market prices in 2022 or hedged at a higher price than in 2021. Furthermore, supply chain disruptions also are bound to negatively impact the prices of the import of goods, with possible further hikes in construction materials as well as food prices. Food price shocks are no longer confined to the United States and the European Union but also have started to affect the Latin America and Caribbean regions. As such, presently, the surge in food prices is taking hold of our main regional source markets.

- **Duration and depth of the pandemic.** In all scenarios, the duration and depth of the pandemic are important factors underlying the outcomes. The impact of new COVID-19 variants, subsequent waves of contagion, as well as vaccination rates could exert significant downside risks on the results.

- **Speed of recovery.** The specific assumptions regarding the recovery of stay-over visitors and tourism credits are instrumental for the outcomes in each scenario. If tourists are more reluctant to travel and/or spend less during their stay-over than in these assumptions, the result could be lower receipts from tourism activities, stagnation in consumption recovery, and in turn a weaker rebound in economic output. Conversely, if the propensity to travel and/or visitor spending is larger than assumed in the scenarios, GDP growth could be higher than anticipated.

- **Employment wage restoration.** The assumption in the estimations is that as tourism activities recover and economic activity picks up, persons who depend on the FASE and wage subsidy programs will continue to have their pre-pandemic wages paid by their employers. This assumption implies that the businesses dependent on these programs will keep their employees and remain in business for the whole year. Moreover, the planned flexibilization of the labor laws is not taken into account. In addition, the 12.6 percent cut in the wages of public-sector employees is expected to remain in place for the foreseeable future. Taken together, these developments would likely lead to a much more cautious spending pattern, thereby negatively impacting private consumption.

- **Investment projects.** The timely execution of relatively large investment projects is always a source of downside risk for GDP projections. Moreover, setbacks in these investment projects also could reduce FDI inflows and, thus, international reserves.

- **Additional government measures.** The government may introduce additional measures to reduce its deficit, such as further lowering personnel expenses and/or introducing tax and other income-generating measures for the general public prior to the tax reform scheduled for January 1, 2023. Such measures could have a dampening effect on private and public consumption. This effect would be even greater if the government is unable to obtain full financing of its deficit or short-term liquidity support. In that case, more stringent measures could be necessary.

3. Balance of payments forecast

3.1 Main assumptions

In view of the uncertainty surrounding the COVID-19-pandemic and its effect on the BOP, the RD considers pessimistic, baseline, and optimistic scenarios for 2022. The baseline scenario is based on the most likely domestic and international developments, which affect multiple GDP components and ultimately the BOP. The pessimistic and optimistic scenarios deviate from the baseline in conformity with the expected recovery in tourism. The result is a differential impact on GDP and foreign government borrowing needs (Table 3).

The baseline growth in tourism credit is estimated at 51.1 percent in 2021 and is forecasted at 33.8 percent in 2022. The optimistic scenario shows a stronger tourism credit growth than the baseline, while the opposite holds for the pessimistic scenario. This range of tourism credit growth has direct implications for exports and, thus, the current account in the BOP. Tourism credit also has a positive correlation with GDP, which in the baseline is estimated at 15.5 percent in 2021 and projected at 7.7 percent in 2022. The variation in GDP growth across scenarios has implications for the current account, as a higher GDP increases disposable income and domestic demand and thereby imports. In addition, more vigorous GDP growth also coincides with larger investment income payments and payments for services, which again impact the current account. Besides the current account, GDP influences the financial account of the BOP as well. This is through government revenues, the fiscal balance, and the associated foreign borrowing needs. In addition, GDP influences the financial account through foreign direct investment.

Table 3: Main assumptions for the BOP estimates and scenarios

	2021e	2022f	Source
Domestic			
Tourism credit (percentage change)			
Pessimistic	42.4	19.5	
Baseline	51.1	33.8	CBA tourism forecast November 2021
Optimistic	59.7	46.6	
Real GDP (percentage change)			
Pessimistic	13.0	3.1	
Baseline	15.5	7.7	CBA GDP forecast November 2021
Optimistic	17.9	12.0	
Inflation (12-month average, percentage change)			
All scenarios	0.5	2.7	CBA inflation forecast November 2021
Repayment of foreign loans (change in Afl. million)			
All scenarios	9.7	1,086.9	CBA government forecast December 2021
Government external borrowings (change in Afl. million)			
Pessimistic	-179.4	632.4	
Baseline	-179.4	762.1	CBA government forecast December 2021
Optimistic	-179.4	888.4	
International			
Inflation USA (12 month-average, percentage change)			
All scenarios	4.3	3.5	IMF World Economic Outlook October 2021
Average WTI oil price (in USD)			
All scenarios	69.0	68.3	EIA* Annual Energy Outlook November 2021

*EIA: Energy Information Administration

The three different scenarios also share some common assumptions. These mainly include the price indicators, which in turn influence the GDP components, and subsequently the BOP. Specifically, spurred by the COVID-19 pandemic and supply chain shortages, 12-month average inflation in the US was estimated at 4.3 percent in 2021 and forecasted at 3.5 percent in 2022. The hike in oil prices along with other factors pushed up US inflation, which in turn drove up import prices (in 2021) and will likely do so again in 2022, thus affecting the value of imports.

3.2 Balance of payments and its components

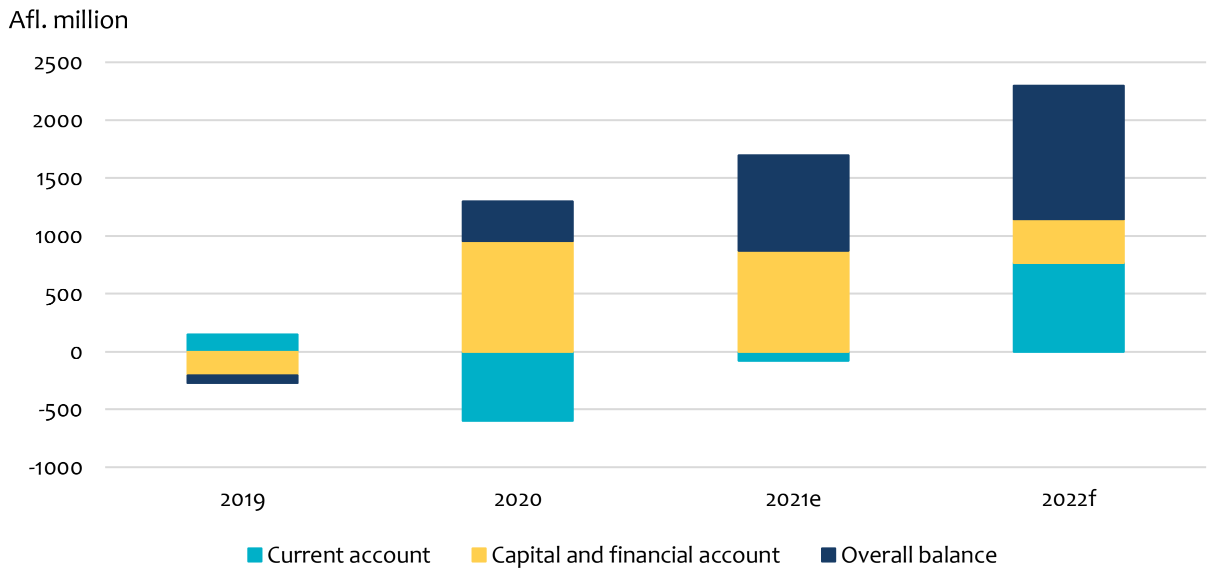
Estimate 2021

The current account is estimated to accrue an Afl. 19.9 million deficit for 2021 (Chart 2). The slight deficit was brought about by a strong recovery of tourism. The robust recovery was expected to elevate the inflow of service credits totaling Afl. 3,616.0 million, chiefly due to tourism credits. However, the pick-up in tourism credits was still insufficient to compensate for the outflow of foreign funds related to outgoing payments. The latter also was boosted by a strong recovery. As such, import payments were expected to reach Afl. 1,963.0 million, while service payments were estimated at Afl. 1,726.5 million. Furthermore, outgoing payments of investment income and current transfers contributed to the current account deficit.

The capital and financial account balances are estimated to have recorded an Afl. 872.5 million surplus in 2021. The former is slightly above the baseline level due to increased investment inflows related to a stronger tourism recovery. Government foreign borrowing and repayment needs remained equal to the baseline scenario, as the associated improvement in the fiscal balance was assumed to impact domestic financing.

All in all, the overall balance of payments is estimated to have reached Afl. 822.5 million in 2021. Consequently, international reserves (excluding revaluation differences) were estimated at Afl. 2,878.4 million.

Chart 2: Balance of payments 2019-2022 under the optimistic scenario



Source: CBA
e = estimate, f= forecast

Baseline scenario 2022

The current account is anticipated to register a surplus of Afl. 404.0 million in 2022. This surplus is principally the result of the continued momentum in tourism recovery. Accordingly, tourism credit is forecasted at Afl. 3,860.7 million, constituting a 33.8 percent boost in 2022 compared to 2021 or 103.4 percent recovery compared to 2019. Other significant inflows include the incoming receipts for services other than transport and travel[3], as well as the exports of goods, respectively totaling Afl. 363.8 million and Afl. 216.1 million. These stem from robust tourism and the associated economic recovery. In this context of a robust economic recovery, the import of goods is expected to expand to Afl. 2,121.0 million. Along those same lines, outgoing payments for services (mainly related to travel, communication, and technical & professional services) reach Afl. 1,881.5 million. Another significant outflow includes the Afl. 329.4 million in outgoing payments related to investment income (e.g., interest and dividends), in line with the economic recovery and profits made in 2021. Hence the inflows related to (tourism) service receipts and export of goods outweigh the outflows related to the import of goods, service payments, and invest income payments.

The financial account is expected to record an Afl. 480.5 million surplus in 2022. This surplus is derived from expected foreign borrowing by the GoA to cover its deficit. These loans give rise to a net inflow on the other investment account of Afl. 601.6 million. Furthermore, net foreign direct investment is projected at 125.0 million, considering the persistent recuperation in the tourism sector and the associated foreign investor confidence in the hotel sector. On the other hand, the Afl. 346.0 million in foreign bond repayments are assumed to be an attenuating factor. This brings the portfolio investment account to a net outflow Afl. 249.0 million.

In view of the surplus on both the current and financial accounts, the balance of payments is anticipated to record a surplus of Afl. 901.4 million. Consequently, projected international reserves (excluding revaluation differences) rise to Afl. 3,685.0 million in 2022.

Pessimistic scenario 2022

In 2022, the current account is expected to record a surplus of Afl. 46.4 million in the pessimistic scenario (Chart 2), resulting from a continuation of the tourism recovery, albeit at a reduced pace compared to the baseline. As a result, service credits are projected to total Afl. 3,834.0 million, primarily stemming from increased tourism credits. Tourism credits are expected to reach 87.0 percent of 2019 levels in 2022 in this scenario. The continued economic recovery pushes up import demand further from 2021, leading to a total value for import of goods of Afl. 1,986.7 million. Additionally, investment income payments will expand due to improved business performance in 2021. Nonetheless, the recuperation in the tourism sector, and thus tourism credits, is sufficient to compensate for the outflow of foreign funds related to imports and income payments.

The financial account balance is forecasted to record an Afl. 585.0 million surplus in 2022. This surplus is higher in comparison to the baseline, as the slower economic recovery is expected to push up the government financial deficit and government foreign financing needs. The former is partially mitigated by the maturing of foreign debt as the government is assumed to make Afl. 346.0 million in external bond repayments. Moreover, the external refinancing of the short-term loans provided by the Netherlands in 2020 and 2021 is anticipated to have a net zero effect on the financial account.

[3] These include construction, financial and other business services.

Additionally, foreign fund inflows related to investments are expected to expand the financial account surplus, although slightly less compared to the baseline.

On the whole, the overall balance of payments is anticipated to record an Afl. 648.3 million surplus. This surplus is smaller compared to the baseline due to the lower inflow of tourism credits related to a more gradual recovery of the tourism sector. The overall balance surplus leads to a jump in international reserves (excluding revaluation differences), which is expected to reach Afl. 3,338.9 million at the end of 2022.

Optimistic scenario 2022

In the optimistic scenario, the current account is projected to reach a surplus of Afl. 767.5 million, as the tourism recovery surpasses its 2019 performance and expands further compared to the baseline. Tourism credits are forecasted to reach 120.0 percent of 2019 levels totaling Afl. 4,470.3 million, pushing up service receipts to Afl. 5,110.9 million. Likewise, imports of goods also are anticipated to surpass 2019 levels recording outflows of Afl. 2,251.9 million, partially mitigating the tourism credit inflow. Moreover, spurred by the continued increased import demand, service payments expand to Afl. 2,006.5 million. The latter is attributed primarily to payments for other services, such as construction and financial services, among others. Additionally, increased appetite for travel by residents is expected to raise service payments related to tourism. Furthermore, investment income payments are expected to continue expanding, bolstered by stronger business performance in 2021.

The financial account balance is predicted to register an Afl. 372.5 million surplus in 2022. The latter is a contraction of the surplus compared to the baseline, as government foreign borrowing needs are projected to decrease with greater improvement in economic performance. As the government's fiscal deficit contracts further compared to the baseline, the government is expected to contribute Afl. 46.9 million to the financial account in 2022. The latter is a significant reduction compared to the previous two years. Furthermore, the refinancing of the Dutch short-term loans provided in 2020 and 2021 are assumed to have a net zero effect. Foreign fund inflows pertaining to investments help to drive up the financial account surplus and are anticipated to be higher compared to the baseline due to stronger tourism performance and investor confidence.

Overall, the overall balance of payments is anticipated to record an Afl. 1,157.0 million surplus, driven primarily by the significant surplus on the current account. As a result, international reserves (excluding revaluation differences) are anticipated to grow to Afl. 4,035.4 million in 2022.

3.3 Outlook assumptions and risks

Given the uncertainties related to the pace of economic recovery following the COVID-19 pandemic, a number of assumptions were made to arrive at the various scenarios. The main assumptions and risks to the scenarios are:

- **Volatility in oil prices and other import prices.** Internationally, there is rising uncertainty about future inflation developments, especially against the background of geopolitical tensions and supply chain disruptions. As the International Monetary Fund (IMF) pointed out, there is a risk that inflationary pressures may prove to be non-transitory. Supply chain disruptions are bound to impact the prices of the import of goods, with possible further hikes in construction materials as well as food prices. Furthermore, oil price volatility and possible hedging contracts by the utility company could affect the outlook.

- **Duration and depth of the pandemic.** In all scenarios, the duration and depth of the pandemic are important factors underlying the outcomes. The impact of new COVID-19 variants, subsequent waves of contagion, as well as vaccination rates, could bring significant risk to the results.

- **Speed of recovery.** The specific assumptions regarding the recovery of stay-over visitors and tourism credits are instrumental for the outcomes in each scenario. If tourists are more reluctant to travel and/or spend less during their stay-over than in these assumptions, this could mean lower receipts from tourism activities. Conversely, if the propensity to travel and/or visitor spending is greater than assumed in the scenarios, the current account improvement could be larger than anticipated.

- **Investment projects.** The timely execution of large investment projects is a source of risk for the balance of payments and reserves projections. Setbacks in these investment projects could reduce FDI inflows.

- **Government fiscal balance and external financing needs.** The state of government finances affects the outcome of the forecast. If the government fiscal balance improves at a greater measure than projected, government financing needs could be lower and government foreign borrowing also could possibly be lower.

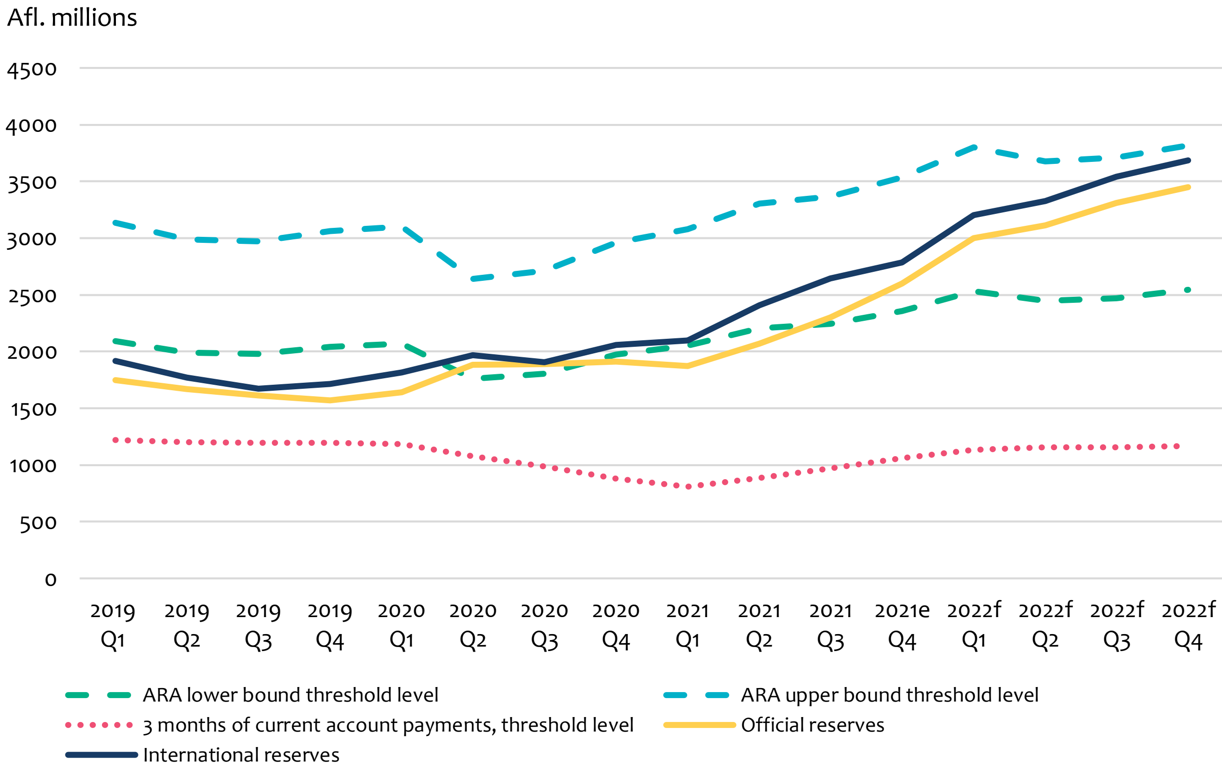
- **Compliance with (re)financing conditions and ongoing negotiations with the Netherlands.** Liquidity loans from the Netherlands are not guaranteed and negotiations are still ongoing. Moreover, refinancing conditions for the maturing short-term loans received from the Netherlands in 2020 and 2021 are not finalized. Consequently, this poses a downside risk for the inflow of foreign funds from government external borrowing and could lead to a lower reserves outcome.

4. Foreign exchange reserves forecast

Baseline scenario 2022

International reserves (excluding revaluation differences) are projected to increase to Afl. 3,685.0 million in 2022. The expected level of international reserves is persistently above the threshold of three months of current payments throughout 2022 (Chart 3). Meanwhile, official reserves (excluding revaluation differences) are forecasted at Afl. 3,448.9 million for 2022. Given that the mentioned levels of official reserves remain within the lower and upper bounds of the IMF ARA metric, official reserves remain adequate vis-à-vis this benchmark. The expected expansions in the reserves are mainly the result of foreign exchange net inflows related to tourism services and loans from the Dutch government to be provided to the Government of Aruba.

Chart 3: Official- and international reserves excluding revaluation differences under the baseline scenario



Source: CBA
e = estimate, f= forecast

Pessimistic scenario 2022

In a pessimistic scenario, international reserves (excluding revaluation differences) are expected to expand to Afl. 3,338.9 million in 2022. During 2022, international reserves are estimated to be consistently above the threshold of three months of current payments (Chart 5). Meanwhile, official reserves (excluding revaluation differences) are forecasted at Afl. 3,123.6 million in 2022. At these levels, official reserves hover between the lower and upper bounds of the IMF ARA metric. Therefore, official reserves remain adequate when benchmarked against the IMF ARA metric. The increase in reserves mostly stem from the foreign exchange net inflows related to tourism services (although lower than in the baseline scenario) and refinancing loans from the Dutch government to be provided to the Government of Aruba (which is higher than in the baseline scenario).

Optimistic scenario 2022

In a pessimistic scenario, international reserves (excluding revaluation differences) climb to Afl. 4,035.4 million 2022. In the course of 2022, international reserves are expected to remain above the threshold of three months of current payments (Chart 6). Meanwhile, official reserves (excluding revaluation differences) are anticipated to reach Afl. 3,123.6 million in 2022. At these levels, official reserves adhere to the lower and upper bounds of the IMF ARA metric. As such, official reserves remain adequate when benchmarked against the IMF ARA metric. The expansion in reserves chiefly arises from the foreign exchange net inflows related to tourism services (which is higher than in the baseline scenario) and refinancing loans from the Dutch government to be provided to the Government of Aruba (although lower than in the baseline scenario).

5. Concluding remarks

Due to the open nature of the Aruban economy and its huge tourism dependency, international developments, especially in the United States, play a significant role in its economic output. Recovery from the COVID-19 pandemic is dependent on an economic rebound in other countries, particularly the United States, the successful roll-out of the vaccine, the outbreak of new variants, and the willingness of people to travel. This willingness relates to potential safety concerns, but also to the continued adverse impact that the crisis may have had on disposable income.

Based upon available data, the Aruban economy is forecasted to continue its recovery path in 2021 and 2022. While uncertainties related to new variants of COVID-19 and waves of contagion are expected to persist, the positive performance of the tourism sector drives economic growth. The upbeat development of the tourism sector is being amplified by the availability of the GOA's FASE and wage subsidy programs in 2021, and the pick-up in investment in 2022. As outlined in the three scenarios used by the CBA, real GDP is projected to grow by 15.5 percent in 2021, but could range between 13.0 percent and 17.9 percent. For 2022, real GDP growth is forecasted at 7.7 percent, with a range between 3.1 percent and 12.0 percent. In nominal terms, this reflects an expansion of 14.0 percent, varying between 11.3 percent and 16.7 percent for 2021, and a 12.2 percent rise in GDP hovering between 6.8 percent and 17.3 percent for 2022.

The current account deficit was estimated at Afl. 19.9 million. The tourism – and ensuing economic recovery also impact investment inflows through investor confidence. As a result, the financial account is estimated to have stood at a surplus of Afl. 872.5 million. The current and financial account lead to an overall inflow on the balance of payments of Afl. 822.5 million. Accordingly, international reserves remained adequate conform the IMF ARA metric at the end of 2021. Meanwhile, official reserves remained comfortably above the threshold of three months of current account payments.

Hinging once more on the robustness of the tourism recovery, the forecasted current account surplus oscillates between Afl. 46.4 million, Afl. 404.0 million, and Afl. 767.5 million for, respectively, the pessimistic, baseline, and optimistic scenarios at the end of 2022. Tourism inflows influence government foreign borrowing through their impact on the fiscal deficit. Additionally, revenue from tourism triggers investment inflows. As a result, the financial account is projected to stand at a surplus of Afl. 372.5 million in the pessimistic scenario, Afl. 480.5 million in the baseline scenario and Afl. 585.0 million in the optimistic scenario. The current and financial account give rise to a respective balance of payments outcome between Afl. 648.3 million, Afl. 901.4 million and Afl. 1,157.0 million under the pessimistic, baseline, and optimistic scenario. Consequently, international reserves (excluding revaluation differences) vary between Afl. 3,338.9 million, Afl. 3,685.0 million and Afl. 4,035.4 million. International reserves remain adequate as they considerably exceed the threshold of three months of current account payments. Likewise, official reserves remain adequate conform the IMF ARA metric at the end of 2022 under all scenarios.