STATE OF THE ECONOMY 2023 Q2

CENTRALE BANK VAN ARUBA

Cover design: Mangroves are hotspots of biodiversity, connecting life on land with life below the water. These ‘forests of the sea’ are essential to the health and vibrancy of our coastal ecosystems, including our community livelihoods. They provide a vital habitat for marine life, help to protect against coastal erosion and storm surges, as well as filter pollutants from the sea. Mangroves are one of nature’s most effective tools in the fight against climate change and are integral to nature.

Abstract

The Aruban Economy expanded as tourism drove domestic consumption, supplemented by increased investment activity.

In the first half of 2023, tourism remained the main engine of the Aruban economy, although it showed signs of performance normalization in Q2 2023. Increased demand from the United States, Canada, and Colombia, along with higher tourism spending, boosted the number of stay-over visitors and tourism revenue. Resilient global economic activity, driven mainly by the services sector, helped push tourism demand, although the scope for further acceleration appears limited as travel returns to pre-pandemic levels. Expanded tourism demand and the subsequent rise in domestic demand led to improved consumption despite inflationary constraints. Furthermore, private investment exhibited positive signs, albeit weighed down by continued elevated international prices, tighter global financial conditions, and uncertainty about the implementation of the B.B.O. at the border. Meanwhile, the upsurge in consumption and investment widened import levels. International transactions settled through the banking sector resulted in a net foreign exchange outflow of Afl. 106.3 million in the first half of 2023. The domestic refinancing of a foreign loan by the private sector largely drove aforementioned net outflow, as tighter global financial conditions pushed up domestic credit. Nonetheless, the level of international reserves stayed adequate and well-above the benchmarks monitored by the CBA. At the end of June 2023, higher utility tariffs, higher gasoline, food, and car prices lifted the 12-month average inflation to 5.9 percent, up from 5.5 percent at the end of 2022. However, inflation slowed down after the 12-month average peaked at the end of April 2023 (6.3 percent). The 12-month average core inflation amounted to 2.3 percent, up from 2.2 percent at the end of December 2022. With regard to government tax performance, in the first six months of 2023, total tax revenues exceeded the level registered in the first half of 2019, recovering beyond the pre-pandemic level. Compared to the same period of 2022, tax revenues surged by 29.9 percent as improved labor market conditions and economic activities led to an expansion in income and profit tax. The rise in government revenues more than compensated for the expansion in government expenditures and led to a financial surplus of Afl. 133.2 million in the first half of 2023. The latter helped to edge down government debt and, combined with the nominal GDP growth, reduced the debt-to-GDP ratio by 7.9 percentage points to 89.2 percent compared to December 2022.

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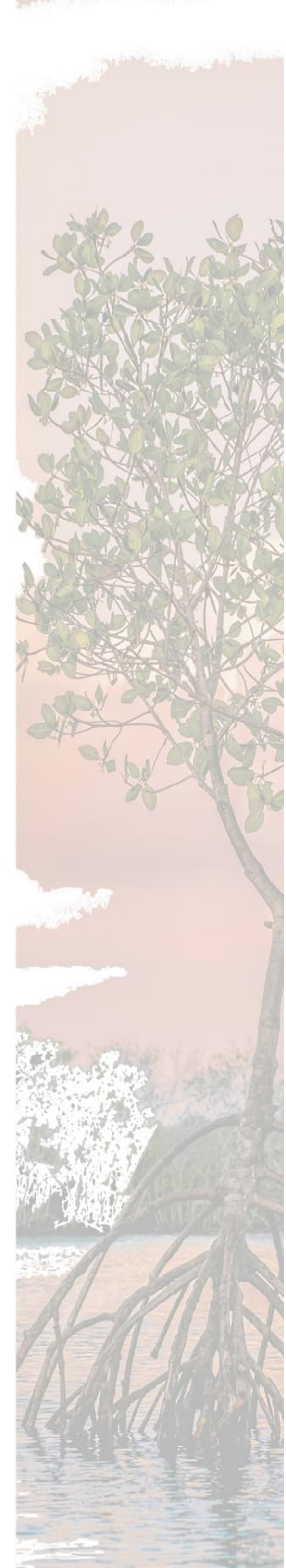
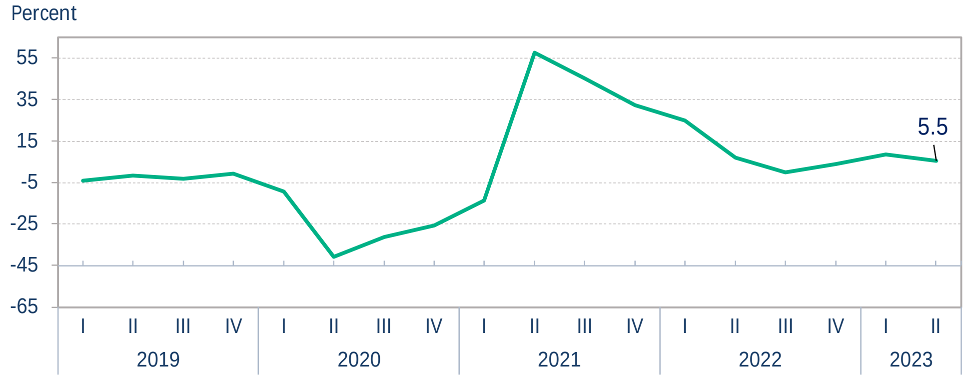


I. DOMESTIC ECONOMY

Economic growth

In the second quarter of 2023, tourism remained the main engine of economic growth, although it showed initial signs of pre-pandemic normalization in Q2 2023 (Chart 1). Growth in stay-over visitors and higher tourist spending were the principal contributors to the year-on-year increase in real GDP of 5.5 percent (Chart 1). Additionally, consumption helped boost real GDP. The latter represented the effect of improved labor market conditions, with estimated employment[1] expanding by 5.1 percent at the end of Q2 2023. Income from the turnover tax and taxes on commodities also grew, indicative of heightened consumption. The uptick in tax income was partially due to the BBO tax rate hike of 1.0 percentage point to 2.5 percent, which raised the total turnover tax rate to 7.0 percent, as of January 1, 2023. Meanwhile, for the most part, investment indicators pointed to larger investment activities in comparison to the same period of 2022. Broader consumption and investment spending led to a widening of imports.

Chart 1: Quarterly GDP growth year-over-year



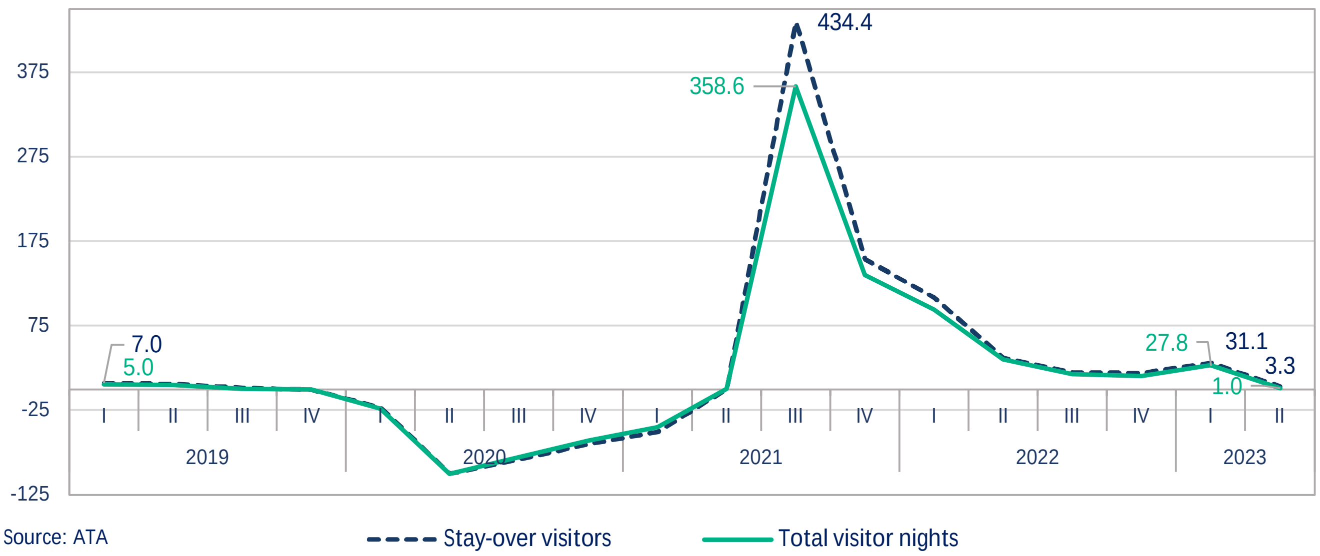
Calculations: CBA

[1] Total number of employment relationships registered at the SVB.

Tourism

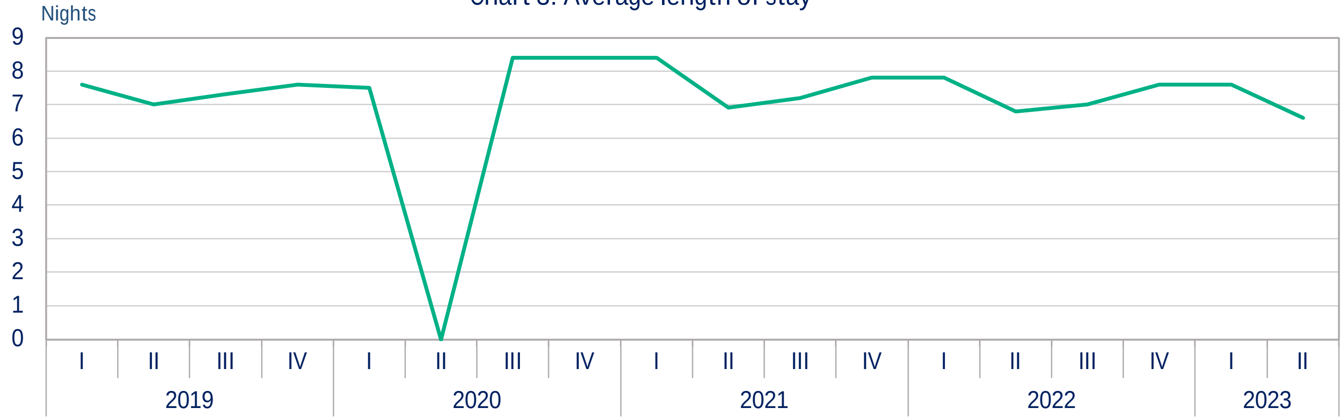
During the first half of 2023, almost all tourism-related indicators improved compared to the same period of 2022 (Table 1), though they showed initial signs of performance normalizing in Q2 2023. The number of stay-over visitors continued its rising trend since the third quarter of 2021 (quarterly growth year-on-year), but growth flattened significantly (Chart 2). The total number of stay-over visitors expanded by 15.6 percent year to date (YTD) June 2023 compared to the same period of 2022. Nonetheless, the strong jump experienced in the first quarter of 2023 (+31.1 percent YoY) leveled out in the second quarter of 2023 (+3.3 percent YoY). The high growth recorded in Q1 2023 is in part related to the pandemic in early 2022. Due to the Omicron variant, there were still lingering effects of the pandemic in Q1 2022. Total number of visitor nights jumped by 13.8 percent in the first six months of 2023 compared to 2022. However, a consistent drop in the average (intended) length of stay (ALoS) since YTD June 2020 (AloS: 7.5 nights) lowered the growth in visitor nights compared to the number of stay-over visitors (Chart 3). During the first two quarters of 2023, ALoS fell to 7.1 nights from 7.2 in the same period of 2022. Moreover, in Q2 2023, the ALoS lessened to 6.6 nights from to 7.6 nights in Q1 2023. The upswing in the number of stay-over visitors was driven primarily by visitors from the U.S. (+12.5 percent), Canada (+96.5 percent), and Colombia (+44.6 percent). In the first half of 2023, the U.S. market share in the number of stay-over visitors declined by 2.2 percentage points to 78.1 percent compared to the same period of 2022. The latter had risen consistently since the first half of 2016 (market share: 56.9 percent), peaked in the first half of 2021 (88.8 percent), and decreased for the first time during the first half of 2022 (market share: 80.3 percent). In terms of 2019-levels, stay-over visitors reached 106.1 percent, while total visitors' nights amounted to 103.6 percent, as the ALoS contracted compared to the corresponding period of 2019 (YTD June 2019: 7.3 nights).

Chart 2: Stay-over visitors and visitor nights growth (in %)



Source: ATA

Chart 3: Average length of stay



Source: ATA

Data from the hotel sector also revealed positive developments in the tourism industry (Table 1). In the first half of 2023, revenue per available room (RevPAR[2]) rose by 28.2 percent compared to the same period of 2022. This jump in RevPAR resulted from a higher hotel occupancy rate during the first six months of 2023 (79.3 percent) relative to the same period in 2022 (71.1 percent). However, the occupancy rate recorded in Q2 2023 was lower than in Q2 2022, possibly due to a greater number of available rooms caused by the addition of new hotels and slower growth in tourism nights. Additionally, a rise in the average daily rate (ADR), i.e., from US$ 316.7to US$ 364.1, contributed to a higher RevPAR.

[2] RevPAR is the product of the average daily rate and the hotel occupancy rate.

Table 1: Tourism indicators for Aruba
YTD June

	2019	2022	2023
Stay-over visitors	575,649	528,325	610,582
Average length of stay (in nights)	7.3	7.2	7.1
Total visitor nights	4,205,785	3,825,924	4,355,396
Cruise visitors	435,112	263,472	499,442
Hotel occupancy (%)	86.2	71.1	79.3
Average daily rate (US$)	301.0	316.7	364.1
Revenue per available room (RevPAR) (US$)	259.3	225.2	288.8
Tourism revenue per night (in Afl.)	337.1	424.1	456.2
Tourism revenue* (in Afl. million)	1,417.9	1,622.6	1,987.0

Sources: CBA, ATA, AHATA. Table shows 2019 for comparison with pre-COVID period.

*Only those registered at local commercial banks.

Income from tourism revenue[3] registered at local commercial banks jumped by 22.5 percent in the period under review. This rise in tourism revenue was related to the growth in total visitor nights and higher tourism spending per night. Total visitor nights expanded by 13.8 percent, while tourism revenue per night increased by 7.6 percent YTD June 2023 vs. YTD June 2022. Compared to 2019-levels, the opposite can be observed — the sizable gains in tourism revenue per night (+35.3 percent) outperformed the increase in total visitor nights (+3.6 percent) during the first half of 2023. As such, total reported tourism revenue reached 140.1 percent of the 2019-level during the first two quarters of 2023.

In the first six months of 2023, cruise tourism surpassed 2019-levels, reaching 114.8 percent of cruise visitors compared to the corresponding period in 2019. The Aruba Ports Authority (APA) reported 499,442 cruise visitors and 190 ship calls in the period under

[3] Tourism revenue corresponds to the tourism credits definition as defined by the IMF BPM 6 manual. The cut-off date for the data used was the end of August 2023.

review (Table 1). The former equals an 89.6 percent surge in cruise visitors compared to the first six months of 2022. The relatively low number of cruise visitors in the first half of 2022 stemmed from a resurgence of COVID-19 at the beginning of the year.

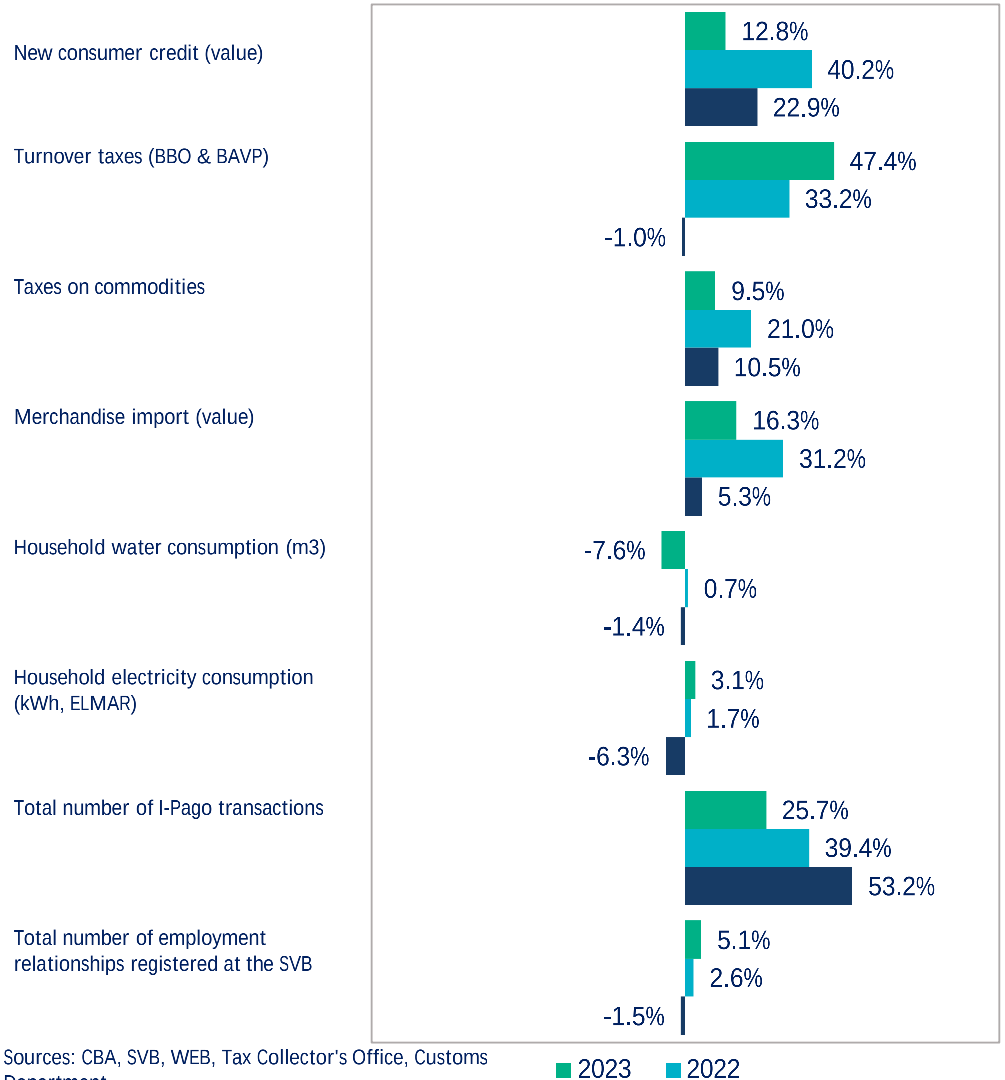
Consumption

During the first two quarters of 2023, nearly all consumption-related indicators showed at improved economic conditions (Chart 4). Turnover taxes, which recorded the most significant change, spiked by 47.4 percent in the first six months of 2023 vis-à-vis the same period a year before. While turnover taxes were positively influenced by higher local consumption and heightened tourism activity, the expansion could be ascribed to the upturn in the BBO rate of one percentage point as of January 1st, 2023. Revenue from taxes on commodities also rose (+9.5 percent) during the period under review. At the same time, greater local consumption paired with a buoyant tourism recovery drove the demand for merchandise imports. The latter experienced a rise of 16.3 percent in the first two quarters of 2023 compared to the same period in 2022.

Commercial banking data further showed larger local consumption. During the period under review, new consumer credit loans value climbed by 12.8 percent. Meanwhile, the number of new consumer credit loans also grew by 4.9 percent. The difference in the two growth rates can be explained by consumers receiving larger loans compared to 2022. The hikes in new consumer credit were influenced by an increase in the number of car purchases during the first six months of 2023. Data from the Aruba Car Dealers Association (ACDA) revealed that car purchases surged by 45.8 percent during the first two quarters of 2023, as opposed to the same period in 2022. In addition, when analyzing the June YTD outstanding value of consumer credit, car loans are the only sub-component that experienced growth (i.e., +2.1 percent). All other sub-components (i.e., personal loans, credit cards, and “other”) decreased compared to December 2022. Noticeable is that the Consumer Confidence Survey (CCS) responses did not mirror the shoot-up in car purchases: the proportion of respondents indicating that purchasing an automobile is suitable declined to 5.7 percent in Q2 of 2023 from 9.3 percent at the end of 2022.

Compared to the first two quarters of 2022, the total number of transactions processed by I-Pago surged by 25.7 percent. This was driven mainly by transactions between Afl. 0 and Afl. 250, which jumped by 43.1 percent, while transactions above Afl. 250 expanded by 11.5 percent. The higher number of transactions processed by I-Pago suggests more spending activities through the Aruban banking system. Meanwhile, the number of employment relationships registered at the Sociale Verzekeringsbank (SVB) also ascended in the first six months of 2023 (i.e., +5.1 percent) compared to the same period a year before. This expansion is higher than the one registered a year prior (i.e., +2.6 percent), which might have further elevated the propensity to consume.

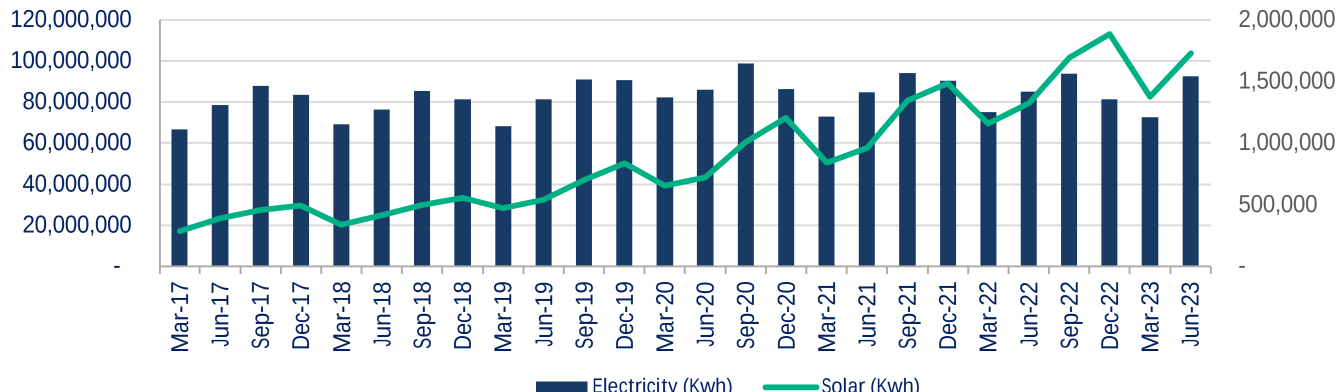
Chart 4: Consumption-related indicators
(YTD June 2023 vs. YTD June 2022 vs. YTD June 2021)



Sources: CBA, SVB, WEB, Tax Collector's Office, Customs Department

On the other hand, utility usage data painted a mixed picture of consumption. Household water consumption (in cubic meters) dropped by 7.6 percent indicating that consumers were using water more conservatively. At the same time, water sales to households (in Afl.) spiked by 13.1 percent, reflecting the higher water tariff as of 1 August 2022. Household electricity consumption in kWh (from ELMAR) went up by 3.1 percent because of both increasing prepaid and non-prepaid energy sales. During the period under review, prepaid energy consumption in kWh jumped by 9.2 percent, while non-prepaid energy sales picked up by 2.4 percent. Compared to June 2022, the number of prepaid energy connections rose by 8.1 percent, while non-prepaid connections grew by 1.0 percent. This suggests that consumers may have been more inclined to control their electricity consumption at home by using prepaid energy installations and/or that consumers seeking new energy meter connections were inclined to choose the prepaid alternative. Another explanation is that the growth in residential rentals bumped up prepaid energy installations to avoid the risk of liability for unpaid energy bills or the hassle of constant name switching on contracts. At the same time, solar energy consumption soared by 25.3 during the first six months of 2023 vis-à-vis the same period a year before (Chart 5). This occurrence was the result of higher demand for solar installations. Compared to the end of the second quarter of 2022, the number of installed residential solar connections surged by 33.6 percent.

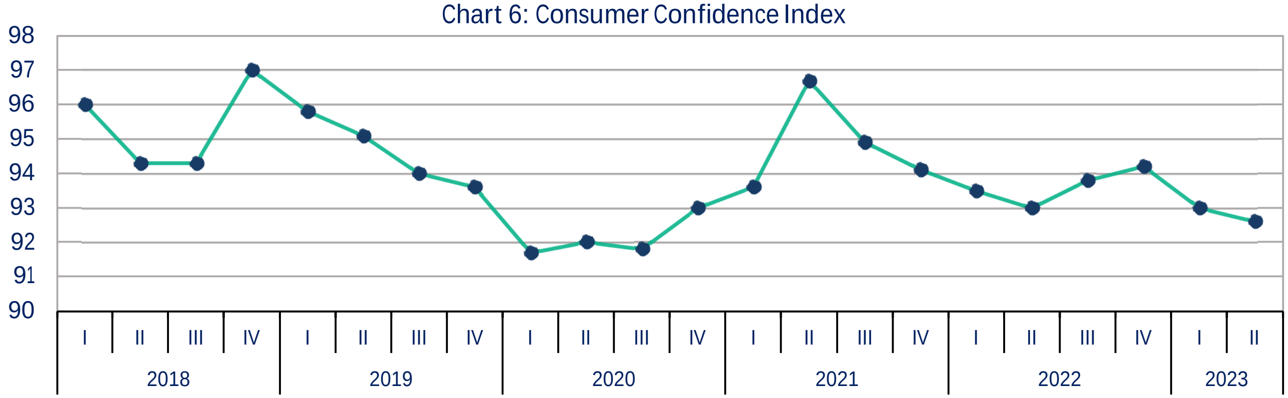
Chart 5: Household energy consumption (kWh, electricity & solar)



Source: Elmar, Web.

Despite the positive development in most consumption-related indicators, the Consumer Confidence Index (CCI) continued its downward path during the second quarter of 2023 (Chart 6). Consumers became even more pessimistic in the second quarter of 2023, the CCI contracted by 0.4 index point to 92.6 compared to the same period of 2022. This contraction reflected worsened consumer sentiments regarding future expectations as this index inched down by 0.2 index point in the second quarter of 2023 compared to the second quarter of 2022. The worsening in the future expectations index may be related to heightened uncertainties about price pressures and the proposed fiscal reform in 2023. Meanwhile, the present situation index remained unchanged at 92.7. Furthermore, on average, the YTD value of the CCI in 2023 (i.e., 92.8) was below that of 2022 (i.e., 93.3). The CCS also indicated deteriorated consumption and borrowing habits. In general, fewer respondents believed that large-scale spending, such as on automobiles and vacations, was suitable compared to the same quarter of the previous year. Moreover, the number of respondents indicating that taking out a loan and mortgage is suitable contracted during the period under review. At the end of the second quarter of 2023, the CCI remained below the pre-pandemic level of 93.6 registered in the fourth quarter of 2019.

Chart 6: Consumer Confidence Index



90-100: pessimistic
100-110: optimistic

Investment

During the first half of 2023, investment indicators continued to show a mixed signs (Chart 7). While housing and commercial mortgages recorded decreases, the value of construction permits and investment-related imports soared, compared to the same period in 2022.

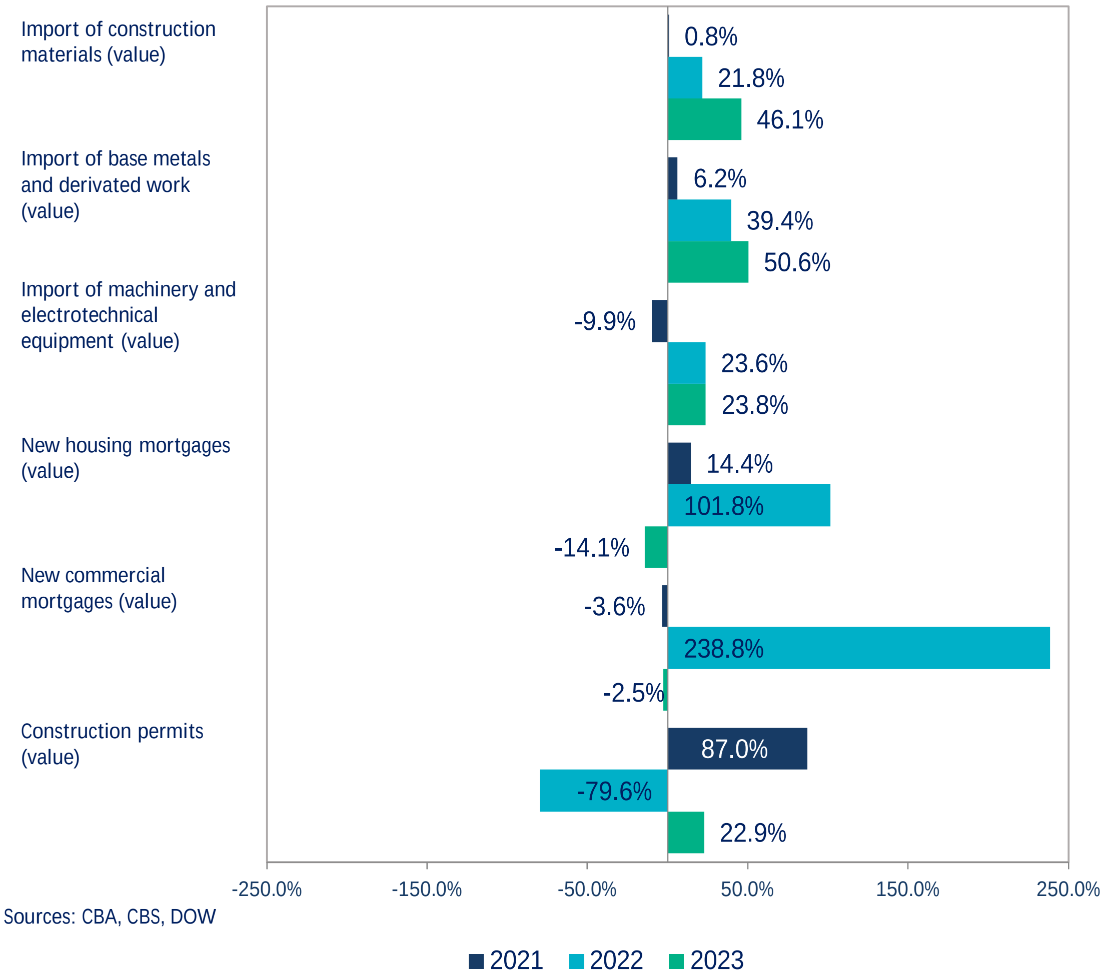
During the first two quarters of 2023, data on the value of new housing mortgages and commercial mortgages at local commercial banks displayed a reduction compared to the same period of 2022. This decline follows a surge (housing +101.8 percent, commercial +238.8 percent) in the first two quarters of 2022 compared to the same period in 2021. However, compared to 2019, the contraction in value of new housing and commercial mortgages (YTD June 2019 vs. YTD June 2018: -19.4 percent, -34.7 percent) is in line with the pattern observed in the pre-pandemic period. Specifically, the value of new housing mortgages (-14.1 percent) and new commercial mortgages (-2.5 percent) fell in Q2 2023. This diminution is a continuation of a trend that emerged during the first quarter of 2023. As a mitigating effect, estimated repayments on housing (-29.7 percent) and commercial mortgages (-17.3 percent) also dropped during the first half of 2023, compared to the same period in 2022. These developments led the value of total housing (Afl. 1,580.6 million) and commercial mortgages (Afl. 569.5 million) to surpass the Q1 2023 and Q4 2022 levels in Q2 2023. Total housing mortgages saw an uptick of 2.5 percent at the end of Q2 2023 compared to end 2022. As for commercial mortgages, the total stood 4.6 percent higher at end Q2 2023 than in December 2022. The CBA's Consumer Confidence Survey (CCS) further reflects the increased pessimism of consumers in Q2 2023 compared to the previous quarter. During this same period, more consumers (Q2 2023: 67.8 percent vs. Q1 2023: 65.4 percent) indicated that taking out a mortgage was unsuitable. Contrastingly, for commercial mortgages, the CBA's Business Perception Survey provided conflicting results — more business owners, though still a small fraction, indicated that terms and conditions for financing had improved (Q1 2023: 3.6 percent vs. Q2 2023: 6.8 percent). Furthermore, the Business Perception investment index rose (Q1 2023: 104.2 index points; Q2 2023: 105.9 index points).

As opposed to credit indicators, data on permits and imports paint a positive picture for investment in the first half of 2023 (see Chart x). In the first two quarters of 2023, total construction permits value grew (+22.9 percent) compared to the same period of 2022. The latter contrasted the decline (-79.6 percent) experienced during the same period in 2022 vis-à-vis 2021. The aforementioned rise was mainly attributed to an expansion in the value of construction permits for (1)houses (+44.1 percent), (2) stores and shopping malls (+128.1 percent) and (3) apartments (+34.4 percent). It also was mitigated, in part, by reductions in the component "other"(-44.9 percent), which includes hotels and condominiums, and by a drop in the component office buildings (-37.6 percent).

Import related investment indicators also reflected positive developments. The imported value of machinery and electrotechnical equipment jumped by 23.8 percent, while that of base metals and derivated works saw an upturn of 50.6 percent. Additionally, the value of imported construction materials rose by 46.1 percent compared to the same period in 2022. The rise in the values of investment related import indicators may have been a result of a higher value of construction permits (2022 Q3-Q4 vs 2021 Q3-Q4: +168.6 %) in the latter half of 2022. In part, this reflects persistent elevated price levels during 2022 and early 2023. Although easing in 2023, the prices of investment-related import remained high, partly as a result of internationally tight labor markets and rising core inflation[4].

[4] IMF's World Economic Outlook Update of July 2023: Near-Term Resilience, Persistent Challenges. Retrieved from: World Economic Outlook Update, July 2023: Near-Term Resilience, Persistent Challenges (imf.org)

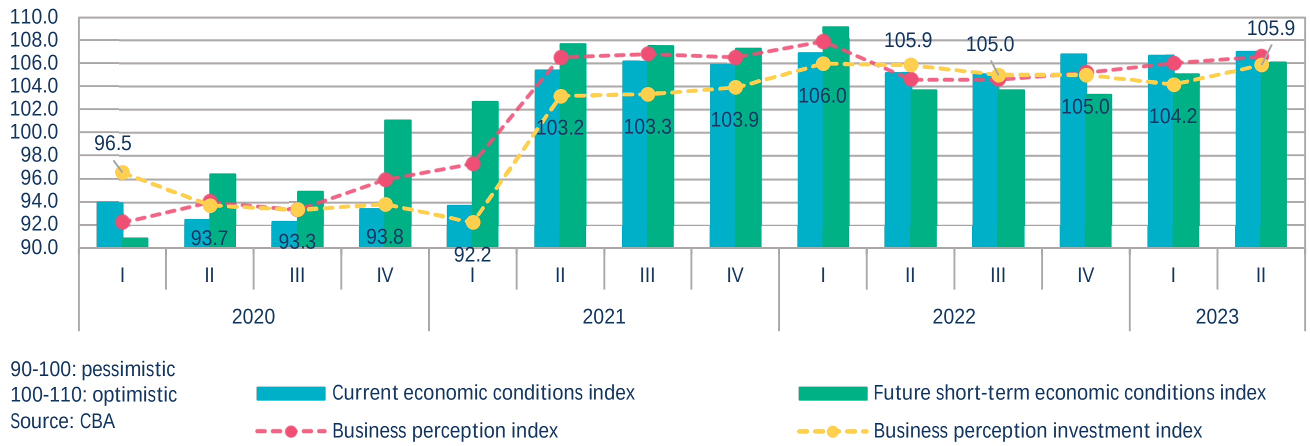
Chart 7: Investment-related indicators
(Percentage change current year vs. prior year)



Sources: CBA, CBS, DOW

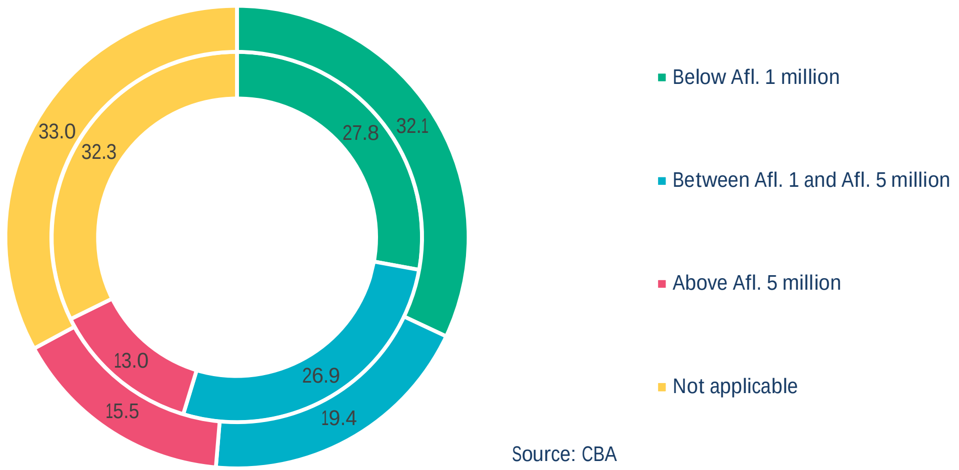
Most indices included in the CBA's Business Perception Survey declined in the first half of 2023 compared to the first half of 2022 (Chart 8). During the first two quarters of 2023, the current economic conditions index recorded an improvement (Q1-Q2 2023: 106.9 Q1-Q2 2022: 106.1). However, the future short-term index indicated a more pessimistic outlook by businesses. This may have been related to the investor uncertainty about the anticipated introduction of the BBO at the border and ongoing negotiations with the Netherlands about the refinancing of Covid-19 pandemic liquidity loans. On balance, the BPS index stayed relatively unchanged at 106.3 in the first half of 2023. On the other hand, the BPS' investment index decreased from 105.9 during Q1-Q2 2022 to 105.0 in Q1-Q2 2023. In line with the sentiment indicated in the future short-term index, the number of businesses with investment plans in the next 12 months inched down (-0.7 percentage point) in the first half of 2023 compared to the same period in the previous year (Chart 9). Of those planning to invest in the next year, more have suggested making investments with a value below Afl. 1 million (+4.2 percentage points) and above Afl. 5 million (+2.5 percentage points) compared to the same period in 2022. In comparison, fewer companies reported to have plans to invest in the next 12 months with a value between Afl. 1 million and Afl. 5 million (-7.4 percentage points) in the average of CBA's BPS in Q1 and Q2 2023 vis-à-vis Q1 and Q2 2022. Overall, the BPS points to increased optimism among businesses about the current economic situation, while at the same time being less optimistic about short-term future conditions in the first half of 2023 compared to the same period in 2022.

Chart 8: Business Perception Index



90-100: pessimistic
100-110: optimistic
Source: CBA

Chart 9: Investment plans of surveyed businesses
Inner circle: YTD Jun 2022. Outer circle: YTD Jun 2023.



Source: CBA

Consumer price index (CPI)

At the end of June 2023, the 12-month average inflation totaled 5.9 percent, 2.5 percentage points higher than in the same period in 2022 (3.4 percent) (Chart 10). However, the pace of inflation slowed after the 12-month average peaked at the end of April 2023 (6.3 percent). The components housing (+2.6 percentage points contribution), transport (+1.3 percentage points contribution), and food and non-alcoholic beverages (+1.2 percentage points contribution) mainly drove the 12-month average inflation. The components household operation (+0.4 percentage point contribution), restaurants and hotels (+0.3 percentage point contribution), miscellaneous goods and services (+0.2 percentage point contribution), health (+0.1 percentage point contribution), and recreation and culture (+0.1 percentage point contribution) registered price hikes. On the other hand, communication (-0.4 percentage point contribution) had a slight downward effect on the 12-month average inflation. The rise in the housing component resulted from the hike in utility tariffs of August 2022. The transport component, in turn, expanded due to higher prices for the purchase of vehicles and gasoline. The food component inched up, mainly caused by elevated prices for meat, bread, cereals, and dairy products. End-June 2023, the 12-month average core inflation amounted to 2.3 percent, up from 1.5 percent at the end of June 2022.

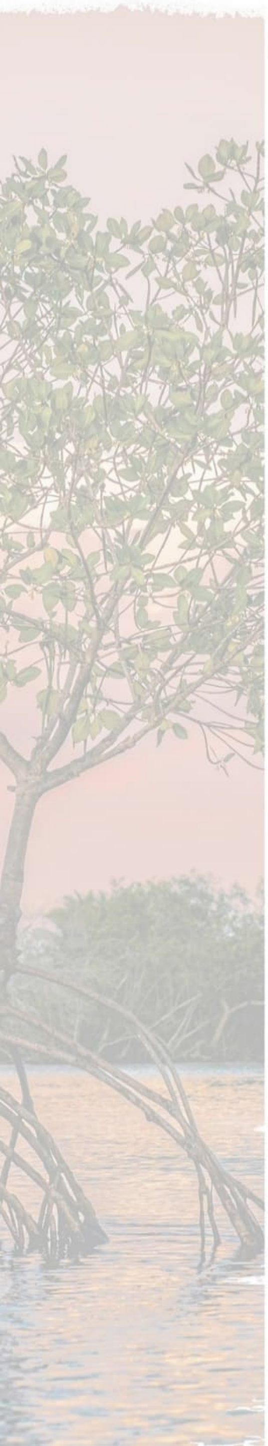
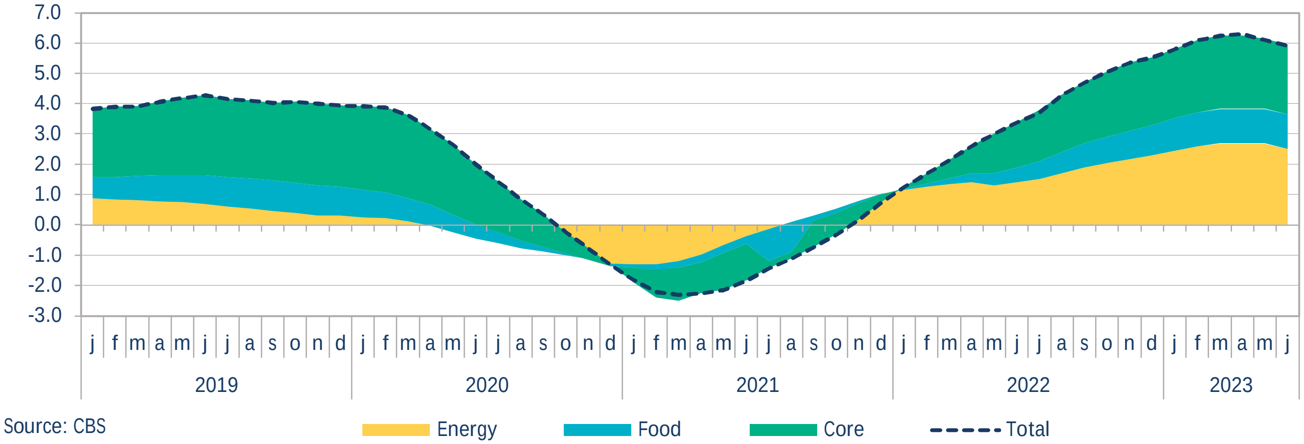


Chart 10: 12-month average rate of inflation



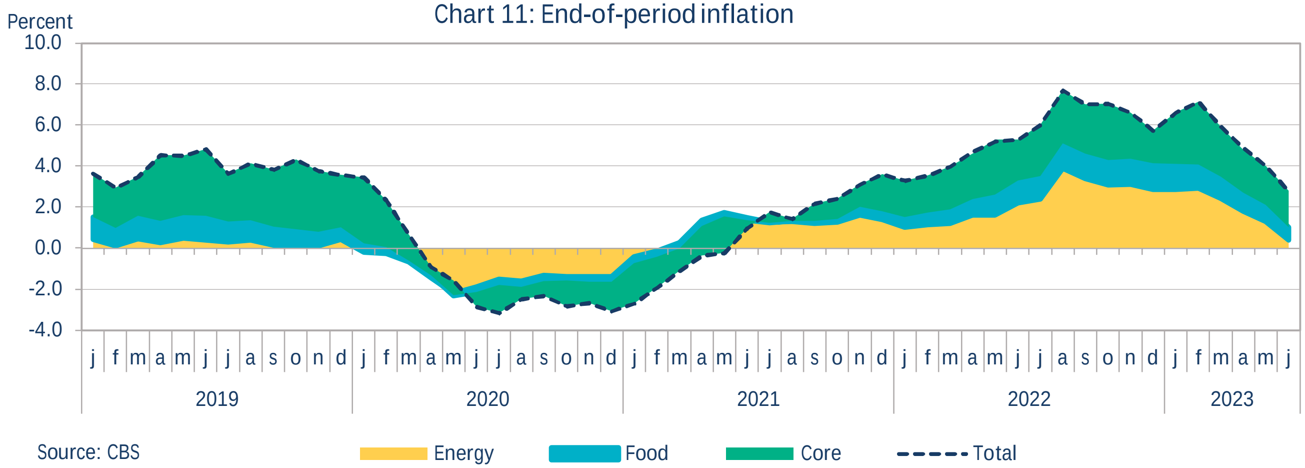
Source: CBS

At the end of June 2023, the End-of-Period (EoP) inflation reached 2.8 percent, compared to 5.3 percent at the end of June 2022 (Chart 11). The components housing (+2.5 percentage points contribution), food and non-alcoholic beverages (+0.7 percentage point contribution), miscellaneous goods and services (+0.4 percentage point contribution), restaurants and hotels (+0.3 percentage point contribution), household operation (+0.1 percentage point contribution), and health (+0.1 percentage point contribution) were the main drivers of EoP inflation. Lower prices for transport (-0.7 percentage point contribution), communication (-0.4 percentage point contribution), and recreation and culture (-0.1 percentage point contribution), on the other hand, had a mitigating effect on the EoP inflation. The significant contribution of housing to the EoP inflation stemmed from an increase in utility tariffs in August 2022. Simultaneously, the lower prices for oil on the international market and the resulting lower prices for gasoline drove the reduction in transport prices despite an increase in the purchase price of vehicles.

During the period under review, the EoP inflation continued to slide after peaking at 7.1 percent in February 2023. The decreased contributions of food (June 2023: 0.6 percentage point; February 2023: 1.2 percentage points), gasoline (June 2023: -1.3 percentage points;

February 2023: 0.3 percentage point), and the purchase price of vehicles (June 2023: 0.6 percentage point; February 2023: 0.9 percentage points) compared to February 2023 sustained the downward trajectory in the EoP inflation.

Chart 11: End-of-period inflation

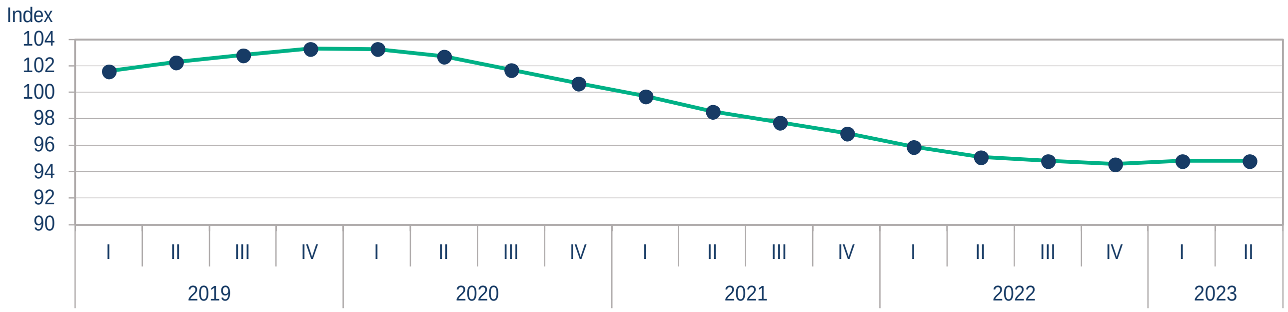


Source: CBS

International competitiveness

The real exchange rate for the Aruban florin vis-à-vis the U.S. dollar continued unchanged during the second quarter of 2023 (Chart 12). The stabilization of this real exchange rate at 94.8 index points follows the sustained improvement in Aruba's competitive position vis-à-vis that of the United States, which started in the second quarter of 2020. During this period, consumer prices rose faster in the United States than in Aruba (Chart 13). Lower prices for food and gasoline, as well as a reduction in electricity tariffs as of January 1, 2020, contributed to the deceleration in the 12-month average inflation for Aruba during the period mentioned above. At the end of June 2023, the 12-month average inflation in the United States reached 6.3 percent[5]. According to calculations from the Research Department, the core component (+3.9 percentage points contribution), food (+1.7 percentage points contribution), and energy (+0.7 percentage point contribution) contributed to total U.S. inflation. At the same time, the 12-month average inflation in Aruba amounted to 5.9 percent, pushed up by energy (+2.5 percentage points contribution), the core component (+2.3 percentage points contribution), and food (+1.1 percentage points contribution). The uptick in the energy component for Aruba during the period under review primarily reflects higher utility prices due to the hike in tariffs as of August 2022. These developments resulted in a small inflation differential (0.4 percentage point) at the end of June 2023.

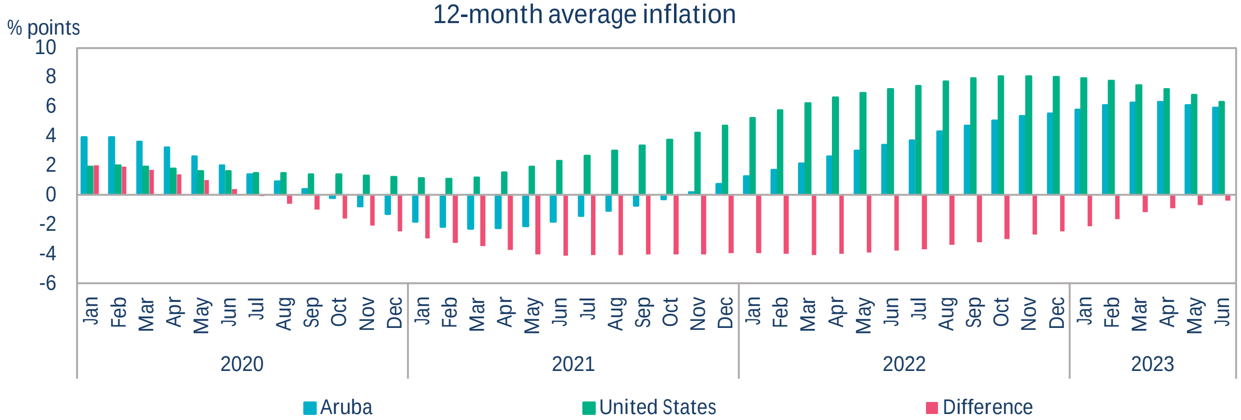
Chart 12: Real exchange rate Aruban florin vis-à-vis the U.S. dollar (2017=100)



Source: CBA

[5] Consumer Price Index, June 2023, Bureau of Labor Statistics

Chart 13: Inflation differential Aruba - USA: 12-month average inflation



Calculations: CBA

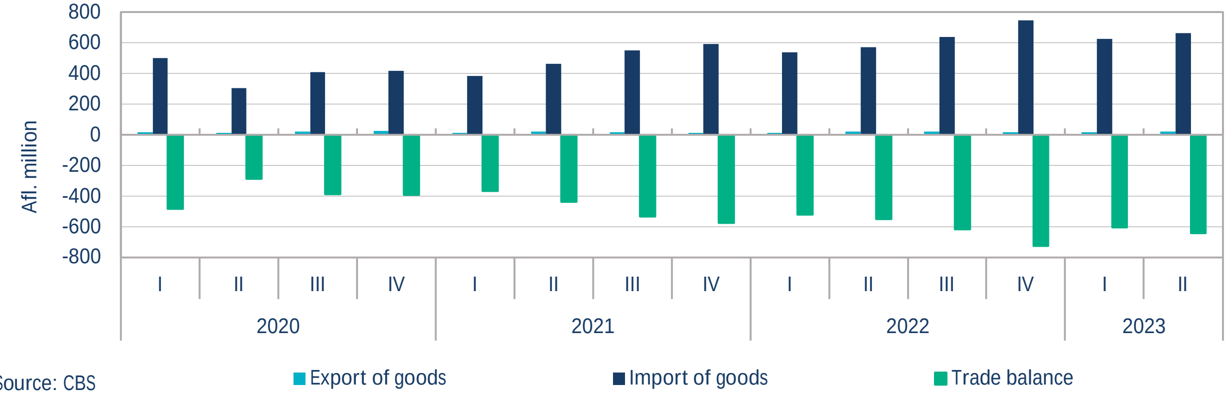
Foreign trade

At the end of June 2023, the trade deficit stood at Afl. 1,249.0 million compared to Afl. 1,073.3 million at the end of Q2 2022 (see Chart 14). The widening deficit (+16.4 percent) was largely explained by an Afl. 180.1 million expansion (+16.3 percent) in imports and was partly mitigated by an Afl. 4.4 million (+13.7 percent) increase in exports of goods compared to a year earlier.

The rise in the value of imports (+16.3 percent) was driven by demand, associated with the continued strong performance of the tourism industry and domestic demand, combined with increased price levels for imports. The components contributing the most to the higher value of imported goods include machinery and electrotechnical equipment (+23.8 percent), transport equipment(e.g., cars, motorcycles and cycles) (+47.9 percent), base metals and derivated works (e.g., iron, steel, aluminium) (+50.6 percent), and food products (+14.2 percent). Components that partly mitigated the increase in imports were the components various goods and products (e.g., furniture and mattresses) (-6.0 percent), wood, charcoal and woodwork (-17.6 percent), and arts-objects and collectors' items (-19.7 percent).

At the same time, the exports of goods (value) also grew compared to the first half of 2022. Pushing up exports (value) were the sections other goods (+15.2 percent), and art objects and collectors' items (+68.4 percent), while the export of transport equipment (cars, motorcycles and cycles) (-52.1 percent) and machinery and electrotechnical equipment (-12.5 percent) had a dampening effect.

Chart 14: Foreign trade



Source: CBS

Balance of payments

International transactions settled through the commercial banking sector gave rise to a net foreign exchange outflow of Afl. 106.3 million during the first half of 2023 (Table 2). The financial account principally caused this outcome by incurring a net outflow of Afl. 379.6 million during the period under review (2022 Q1-Q2 Afl. 144.7 million net outflow). The Afl. 216.2 million net inflow on the current account only partially mitigated the financial account deficit. Meanwhile, the capital account registered a small net outflow (-Afl. 6.3 million), while “items yet not classified” recorded a net inflow of Afl. 63.4 million.

Table 2: Balance of payments (in Afl. million)*	YTD Q2 2022	YTD Q2 2023
Current account	180.8	216.2
Goods	-979.0	-1,024.0
Services	1,197.5	1,494.7
Primary income	-54.0	-235.9
Secondary income	16.3	-18.6
Capital account	-6.1	-6.3
Financial account	-144.7	-379.6
Direct investment	113.9	88.8
Portfolio investment	-102.0	-97.9
Financial derivatives	4.7	-1.2
Other investment	-86.9	-110.1
Foreign accounts	-74.5	-259.1
Items not yet classified	4.7	63.4
Change in international reserves (excluding revaluation differences)	34.7	-106.3

Source: CBA
*Transactions recorded through local commercial banks.

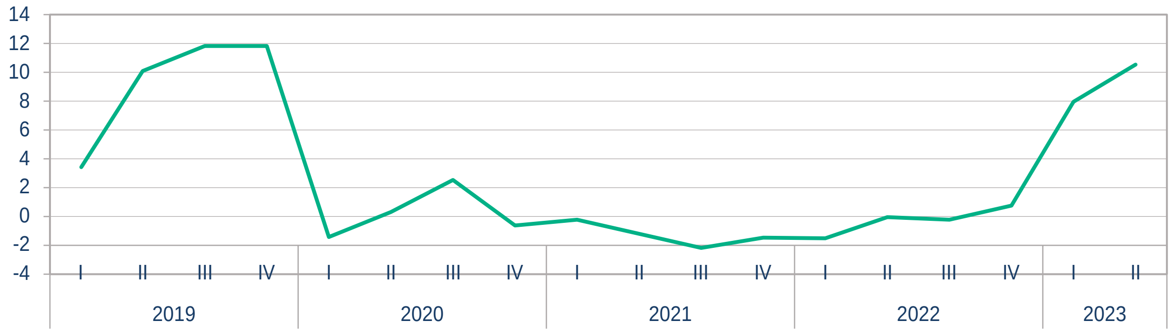
The financial account experienced a net outflow of Afl. 379.6 million, which dampened gains in the current account. The former resulted from net outflows across most components, except for direct investment. Specifically, foreign accounts had a net outflow of Afl. 259.1 million, driven by the local refinancing of a foreign loan by the private sector. Other investments added Afl. 110.1 million to the net outflows on the financial account, owing to, among others, foreign debt repayments by the utilities sector. Additionally, portfolio investment recorded a net outflow of Afl. 97.9 million mainly due to the GoA's repayments on maturing foreign loans. Financial derivatives, which are substantially influenced by hedging, had a minor role with a net outflow of Afl. 1.2 million. On the other hand, a net inflow of Afl. 88.8 million on direct investment partly mitigated the net outflows mentioned above. This expansion largely ensued from real estate purchases in Aruba and capital contribution by non-residents.

The current account noted a net foreign exchange inflow of Afl. 216.2 million in the first half of 2023. This result was chiefly caused by a net inflow related to tourism services in the amount of Afl. 1,645.2 million. Compared to the same period in 2022, the larger net inflow related to tourism services was due to the growing number of stay-over visitors and their spending per night. This gain in tourism credit, paired with heightened local consumption and higher import prices also affected the goods account. During the first half of 2023, the goods account showed a net outflow of Afl. 1,024.0 million (2022 Q1-Q2: Afl. 979.0 million), partially mitigating the large inflow on the services account. Additionally, primary income registered a large net outflow of Afl. 235.9 million. This stemmed primarily from dividend payments by the hotel and commercial banking sector, in addition to GoA's interest payments on foreign loans. Moreover, the secondary income account recorded a net outflow (i.e., Afl. -18.6 million), related to re-insurances and other current transfers of the other sector..

Monetary survey

Overall credit saw a sharp increase in the first two quarters of 2023 after remaining virtually flat since 2020. In the first half of 2023, total credit provided by local commercial banks jumped 4.9 percent. This progress was remarkably different from the development observed during the years after the onset of the COVID-19 pandemic. Looking back at June 2022, total outstanding credit dropped by 0.5 percent compared to December 2021. In the current year, the uptick in overall credit was mainly caused by larger business loans (+10.5 percent), followed by higher loans to individuals (+1.7 percent). The sharp rise in business loans (Chart 15) was principally caused by elevated demand for term loans longer than two years (+20.0 percent). The latter is the consequence of greater demand for local refinancing of existing foreign loans associated with lower interest rates on the domestic market vis-à-vis those from abroad. In addition, business mortgages also rose by 4.6 percent, likely due to a need for business spaces.

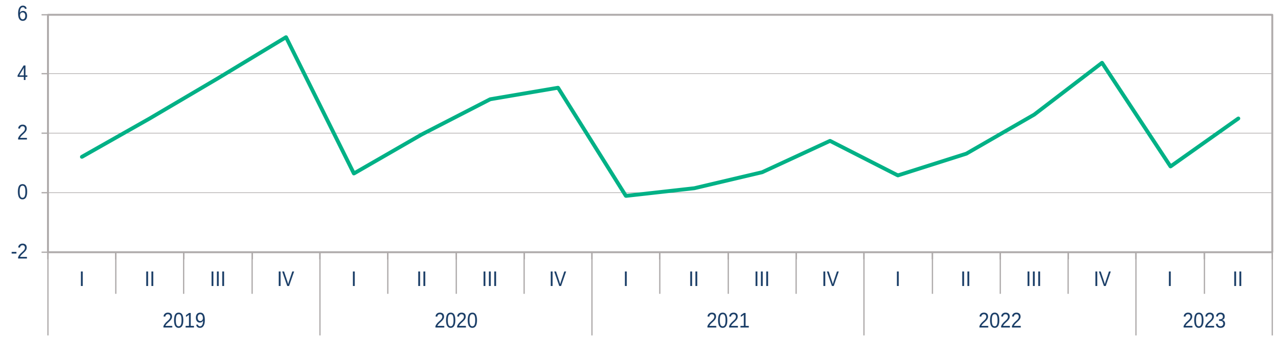
Chart 15: Loans to enterprises provided by local commercial banks - (year-to-date growth rates)



Source: CBA

Meanwhile, boosted housing mortgages (+2.5 percent) pushed up loans to individuals (+1.7 percent), mitigating the decline in consumer credit (-1.1 percent) (Chart 16). Total outstanding loans to individuals have been following an upward trend since September 2022 because of the growing demand for housing mortgages. In general, the rising demand for housing mortgages consistently outpaced the contraction in outstanding consumer credit. On the other hand, the results of the CCS did not match the progress in loans to individuals. During the second quarter of 2023, the Consumption and Borrowing Habits Index of individuals fell to 92.6 compared to 93.8 during the same period a year before.

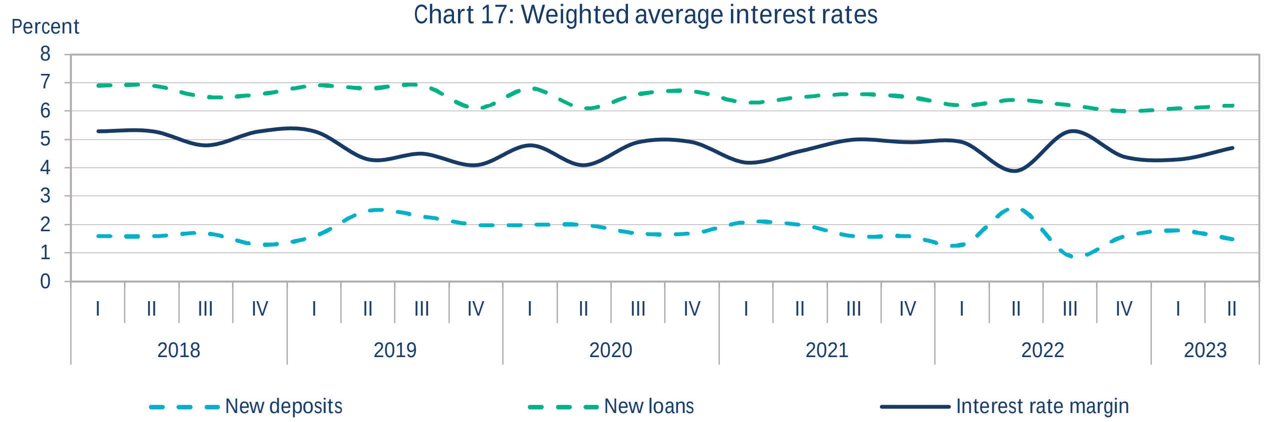
Chart 16: Housing mortgages provided by local commercial banks
(year-to-date growth rates)



Source: CBA

The quarterly weighted average interest rate margin reached 4.7 percent at the end of the second quarter of 2023, compared to 4.4 percent at the end of December 2022 (Chart 17). The rise in the interest rate margin was caused by a higher average interest rate on new loans (from 6.0 percent in December 2022 to 6.2 percent in June 2023), paired with a slightly lower average interest rate on new deposits (from 1.6 percent in December 2022 to 1.5 percent in June 2023). The uptick in interest rate on loans was predominantly affected by the interest rate on commercial mortgages, which spiked by 0.5 percentage point in June 2023 vis-à-vis December 2022. In addition, the interest rate charged on consumer credit also saw an increase of 0.2 percentage point. A drop in interest rates on savings deposits (from 1.4 percent in December 2022 to 0.9 percent in June 2023) was the main culprit of a lowered average interest rate on deposits. Lowered interest rates on time deposits with a maturity of less than 12 months (from 1.1 percent in December 2022 to 0.9 percent in June 2023) further exacerbated this decline.

Chart 17: Weighted average interest rates



Source: CBA

The financial soundness indicators remained adequate throughout the first two quarters of 2023. The capital adequacy ratio decreased to 31.9 percent from 39.8 percent in the fourth quarter of 2022. Asset quality, measured as nonperforming loans to gross loans, improved as it declined to 2.3 percent vis-à-vis 3.5 percent registered at the end of December 2022. In general, nonperforming loans have been following a downward trend since the fourth quarter of 2021, likely as a result of the buoyant recovery of the Aruban economy. At the same time, return on assets before taxes, equity before taxes, and assets after taxes remained virtually unchanged compared to the last quarter of 2022. On the other hand, return on equity after taxes inched down to 3.4 percent. The interest margin to gross income (from 52.4 percent to 54.6 percent), noninterest expenses to gross income (from 61.2 percent to 71.7 percent), and the interest rate margin (from 4.4 percent to 4.7 percent) showed increases during the period under review. The commercial banks aggregated prudential liquidity ratio (PLR) stood at 25.4 percent at the end of June 2023 (minimum required PLR: 18.0 percent), contracting by 4.4 percentage points from December 2022. This drop mirrored liquidity outflows during the first months of 2023 related to local refinancing of existing foreign loans.

Box 1: Excess liquidity within the Aruban commercial banking sector

This box discusses the excess liquidity developments within the Aruban commercial banking sector. Excess liquidity refers to the liquid funds (less pledged assets[6]) held by commercial banks above the requirements stipulated by the CBA. Explicitly, commercial banks must hold a (1) reserve requirement (part of item 2b in Table 3) and a (2) minimum prudential liquidity as stipulated by the CBA. The reserve requirement dictates the minimum reserves commercial banks must hold (unremunerated) at the CBA as a percentage of their clients' liquid deposits (items 10, 11a2 and 12 in Table 3). The minimum prudential liquidity is the minimum amount of liquidity that commercial banks need to maintain as a percentage of their total assets (less goodwill).

[6] Assets used as a collateral for a loan.

Table 3: Balance sheet of Aruban commercial banks (in Afl. million)

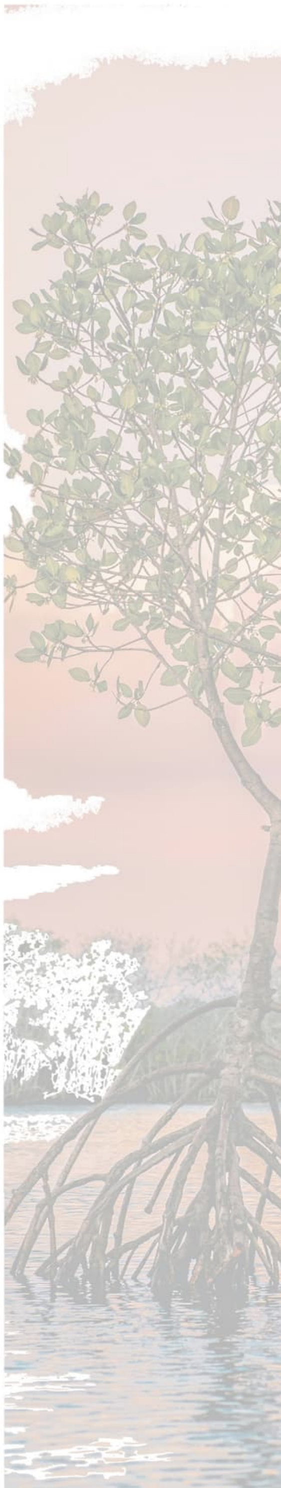
June 2023

Assets		Liabilities	
1. Cash	80.4	10. Demand deposits:	3693.2
2. Centrale Bank van Aruba	2067.9	a. Private sector	3470.2
a. Current account	552.3	b. Government	190.2
b. Time deposits	1515.6	c. Deposit money banks	32.8
1. Reserve requirement	1325.6	11. Time deposits:	1016.5
2. Other time deposits	190.0	a. Private sector	1016.5
3. Accounts at other deposit money banks	530.8	1. Maturity: ≤ 2 years	342.3
4. Investments:	551.9	2. Maturity: > 2 years	674.2
a. Short-term securities	149.9	b. Government	0.0
b. Government Bonds:	397.1	c. Deposits money banks	0.0
c. Other securities	4.8	12. Savings deposits:	1207.5
5. Loans outstanding:	3525.7	13. Borrowings:	5.2
a. Commercial	1678.3	14. Other Liabilities:	106.0
b. To individuals	2091.8	a. Accounts payable	55.2
c. To government	0.0	b. Taxes payables	5.6
d. Unearned income (-)	0.0	c. Other	45.2
e. Provision for loan losses:	244.4	15. Shareholders' equity:	938.0
6. Premises and equipment	121.2	16. Subordinated debt:	0.0
7. Other real estate owned	0.0		
8. Other investments:	26.2		
9. Accounts receivable and prepayments	62.2		
Total Assets	6966.4	Total Liabilities	6966.4

Total excess liquidity widened at the start of and during the COVID-19 pandemic (Chart 18). During the first quarter of 2020, excess liquidity jumped due to reductions in the Reserve Requirement Rate (RRR) and the minimum Prudential Liquidity Ratio (PLR). During that period, specifically in March and April 2020, the Monetary Policy Committee (MPC) of the CBA eased the RRR by 5.0 percentage points to 7.0 percent and the CBA lowered the minimum PLR by 3.0 percentage points to 15.0 percent to inject liquidity into the Aruban banking sector. These measures formed part of the monetary and prudential relief actions of the CBA to counteract the economic effects of COVID-19. Notably, despite the CBA not taking additional measures, excess liquidity continued to grow until the second quarter of 2021. During that period, a lack of credit appetite paired with liquidity support by the Government of Aruba (GoA) to businesses and individuals[7] likely contributed to heightened excess liquidity.

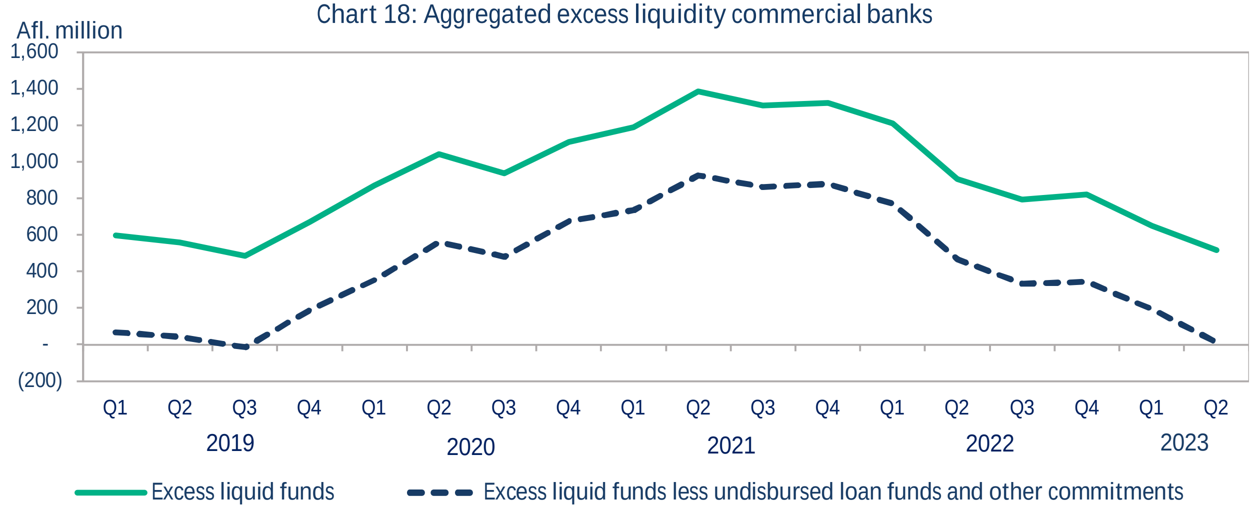
An elevated level of excess liquidity hampers the CBAs ability to influence the commercial banks' credit supply through its monetary policy. Abundant excess liquidity may be associated with a large credit potential. Consequently, if credit picks up and leads to foreign exchange outflows, the CBA will be unfavorably positioned to mitigate the downward pressure on foreign reserves unless the MPC of the CBA drastically raises the RRR or the CBA uses direct measures such as capital restrictions. However, such drastic and sudden changes are undesirable in most cases. Against this backdrop, the MPC of the CBA gradually raised the RRR from 7.0 percent in August 2021 to 25.5 percent in January 2023. This increase extracted Afl. 860.6 million from excess liquidity of the commercial banking sector. In addition, the CBA raised the PLR to the pre-COVID-19 level of 18.0 percent in September 2021, causing a further contraction of Afl. 251.6 million in excess liquidity.

The RRR remained unchanged in the first half of 2023. Despite a constant RRR, excess liquidity contracted by Afl. 302.9 million to Afl. 516.8 million during the first two quarters of 2023. This development was primarily the result of an uptick in credit demand mainly due to local refinancing of foreign loans. The latter is caused by the favorable position of the interest rate differential between Aruba and the United States for borrowers, as the lower interest rate on loans in Aruba leads to interest savings when refinancing loans locally. At the end of the second quarter of 2023, excess liquidity was Afl. 152.5 million below the pre-COVID-19 level registered in the fourth quarter of 2019.The CBA continues to monitor the excess liquidity developments and stands ready to change the reserve requirement rate, if deemed necessary.



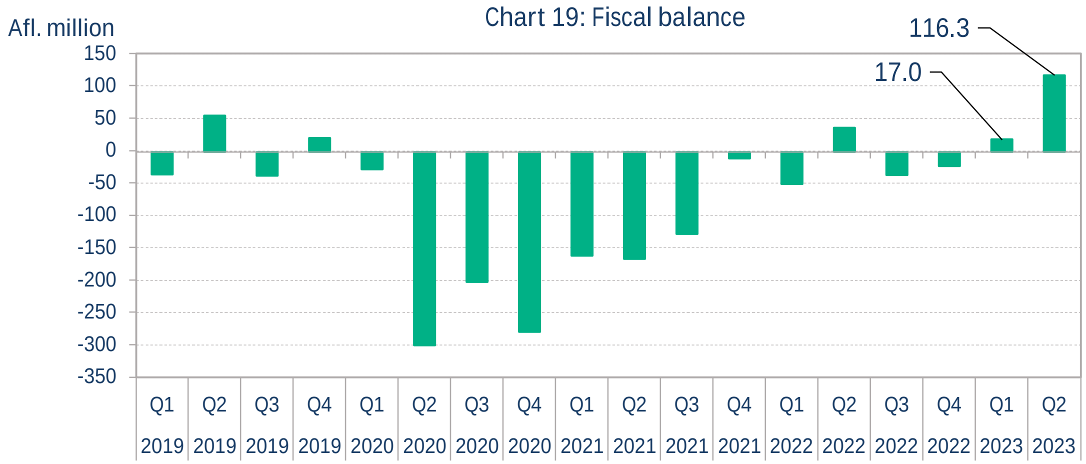
[7] To businesses: (1) Wage subsidy to employers that maintained employment links and (2) liquidity support to small and medium enterprises. To individuals: Temporary income support called "Fondo di Asistencia Social di Emergencia" (FASE) to those who lost their job or labor income.

Chart 18: Aggregated excess liquidity commercial banks



Government

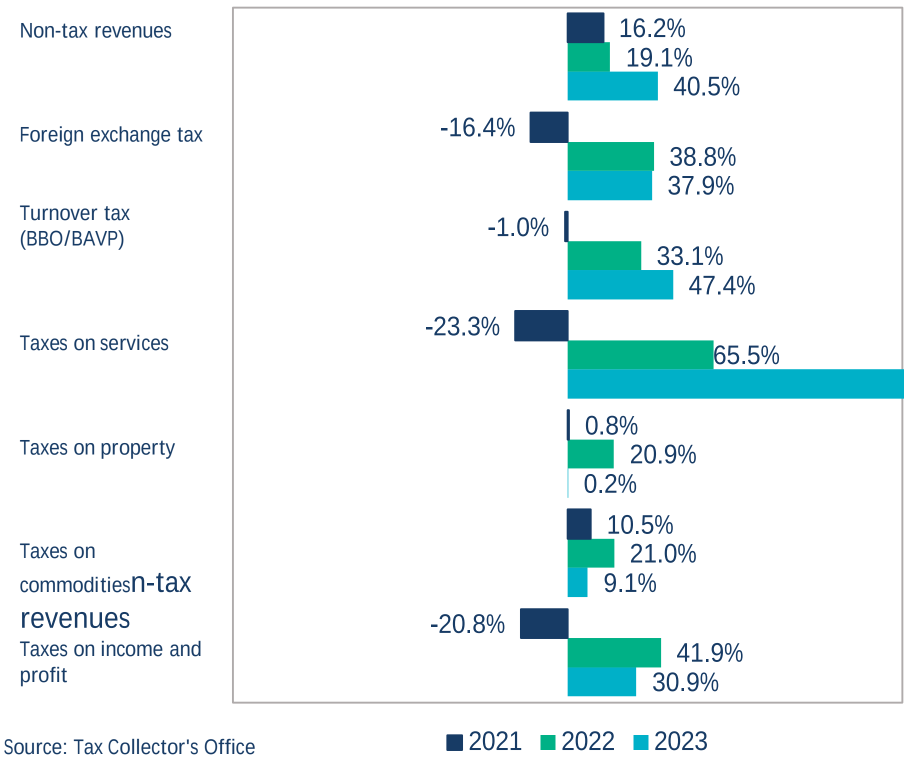
During the first half of 2023, the GoA recorded a financial surplus of Afl. 133.2 million (Chart 19). A year before, the GoA ran a deficit of Afl. 16.8 million. This turnaround represented a jump of Afl. 199.3 million (or +31.0 percent) in government revenues, although government expenditures (on a cash basis) grew by Afl. 50.4 million. Moreover, at the end of June 2023, government revenues (i.e., Afl. 842.8 million) exceeded the level (i.e., Afl. 712.8 million) registered in the first half of 2019, indicating that revenue generating activities had recovered beyond the pre-pandemic level.



Calculations: CBA
e = estimated

All tax components registered an expansion during the period under review (Chart 20). Receipts from taxes on income and profit expanded by Afl. 62.3 million (+30.9 percent), resulting from elevated income tax and wage tax revenues, coupled with robust profit tax revenues. The receipts from income and wage tax growth reflected higher income earned and improved employment conditions. Profit tax revenues boosted by Afl. 37.2 million (+44.1 percent) to Afl. 121.6 million, surpassing pre-pandemic levels, and driven by the banking, hotel and food supplier sector. Similarly, income from turnover taxes rose by Afl. 51.6 million (+47.4 percent), likely due to heightened local consumption, a surge in tourism spending, and increased prices for goods and services. In addition, the rise in the turnover tax rate at the beginning of the year also contributed to the hike in turnover tax revenue. Meanwhile, revenues from taxes on services grew by Afl. 35.6 million (+159.6 percent), primarily related to an expansion in collected hotel room tax revenues. Apart from the improved tourism activities and associated hike in hotel rates, this development paralleled the rise in the hotel room tax rate from 9.5 percent to 12.5 percent, as well as the larger share of the total hotel room tax collections that the government receives as of the first of January 2023. Income from taxes on commodities grew by Afl. 14.4 million (+9.1 percent), principally due to elevated import duties. The latter aligns with the greater value of imported goods in merchandise trade data. Moreover, foreign exchange tax also jumped by Afl. 9.9 million (i.e., +37.9 percent) as the balance of payments recorded more outflows in the first half of 2023 compared to the first half of 2022. The latter was due primarily to the aforementioned domestic refinancing of foreign loans by the hotel sector. Lastly, receipts from taxes on property edged up by Afl. 0.1 million (+0.2 percent) since the growth in land tax revenues and motor vehicle fees were more robust than the drop in transfer tax revenues.

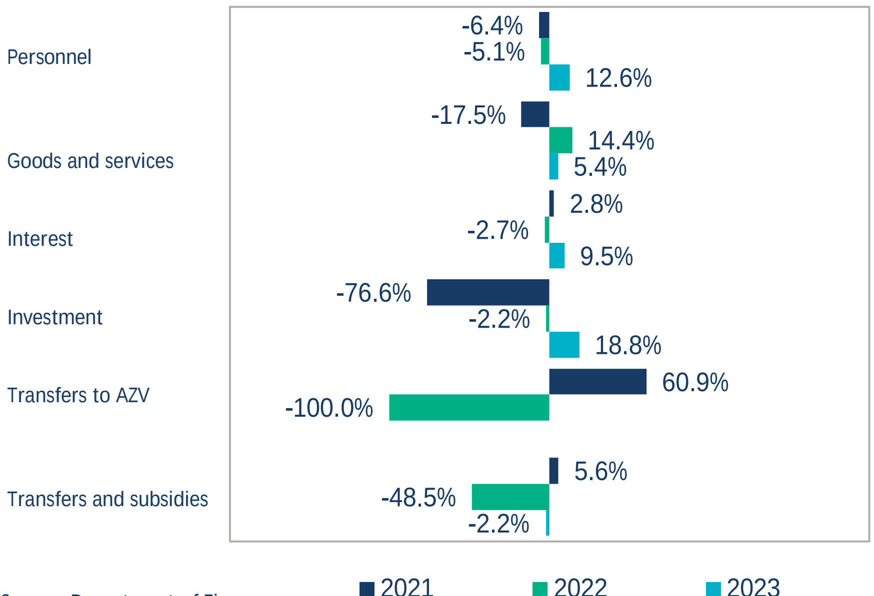
Chart 20: Government revenue
(Percentage change YTD June 2023 vs. YTD June 2022)



Source: Tax Collector's Office

Government expenses (on a cash basis) reached Afl. 707.8 million at the end of June 2023. This development marked an expansion of Afl. 50.4 million or 7.7 percent compared to the first half of 2022. All components of government expenditures, except for ‘transfers and subsidies’, showed an uptick compared to the same period in 2022 (Chart 21). The largest upward movements were noted in personnel (+Afl. 33.6 million or +12.6 percent), goods and services (+Afl. 7.6 million or +5.3 percent), and interest payments (+Afl. 11.2 million or +9.5 percent). Personnel expenses rose likely in relation to the complete roll-back of the COVID-19 curtailment of public sector wages. Meanwhile, interest payments expanded due to rising interest rates resulting from tighter global financial conditions.

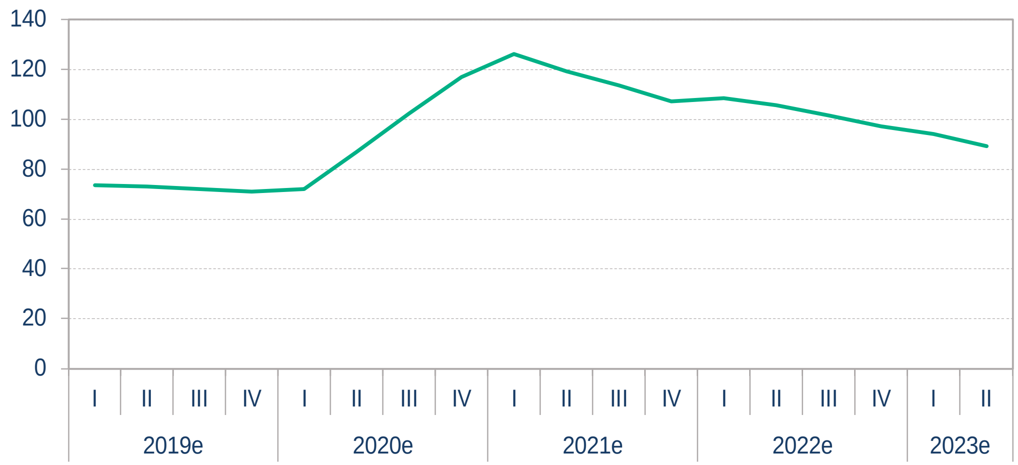
Chart 21: Government expenditure
(Percentage change YTD June 2023 vs. YTD June 2022)



Source: Department of Finance

Compared to December 2022, total government debt shrank from Afl. 5,717.6 million to Afl. 5,631.9 million in June 2023. Lower foreign debt (-Afl. 77.3 million) in the categories “other” (-Afl. 59.4 million) and the United States (-Afl. 16.3 million) predominantly brought about the decline in government debt. Meanwhile, the debt owed to the Dutch government for liquidity support (Afl. 915.5 million) stayed unchanged compared to December 2022. Domestic debt also lessened, albeit to a lower degree (-Afl. 8.4 million). This development in domestic debt was the result of decreased treasury bills stock (-36.0 Afl. million) and short-term non-negotiable debt (-Afl. 25.4 million), while government bonds stock rose (+Afl. 53.0 million). Total government debt (as a ratio to GDP) stayed above the 2019 Q4 pre-pandemic level of Afl. 4,318.9 million (or 71.1 percent of GDP), highlighting the pandemic-induced expansion of government debt. Due to the combination of nominal GDP growth with the debt contraction, the debt-to-GDP ratio fell to 89.2 percent by June 2023, marking a reduction of 7.9 percentage points compared to December 2022 (Chart 22).

Chart 22: Debt-to-GDP ratio



Calculations: CBA
e = estimated

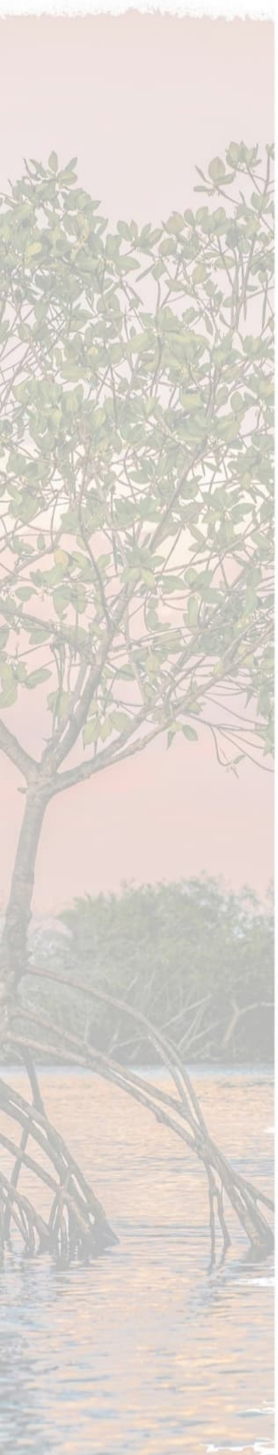
II. INTERNATIONAL DEVELOPMENTS

In July 2023, the International Monetary Fund (IMF) published its most recent World Economic Outlook (WEO). The WEO contained updates to the global growth projections presented in April 2023. In the July 2023 WEO, the IMF foresees global growth to decline to 3.0 percent in 2023 and 2024, down from the 3.5 percent estimated for 2022 (Table 4). Despite a relatively higher forecast for 2023 (+0.2 percentage point) compared to the April 2023 WEO, the anticipated expansion for 2023 and 2024 persists below the pre-pandemic average of 3.8 percent.

According to the July 2023 WEO, Emerging Market and Developing Economies mainly push up global output. The forecasted increase for the above-mentioned economies averages 4.0 percent in 2023, and 4.1 percent in 2024. Advanced Economies, on the other hand, will likely strengthen by 1.5 percent in 2023 and 1.4 percent in 2024. In addition to the discrepancy in global output growth between these two groups, there are vast differences between countries within each group. Concerning the Advanced Economies, the IMF projects that the United States output will rise by 1.8 percent in 2023 and 1.0 percent in 2024. The Euro Area, on the other hand, is foreseen to experience growth of 0.9 percent in 2023 and further expand by 1.5 in 2024. Due to weak manufacturing output, countries like Spain, which benefitted enormously from more robust services and tourism, outperformed countries like Germany within the Euro Area. From the Emerging Market and Developing Economies, Latin America and the Caribbean will likely improve by 1.9 percent in 2023 and 2.2 percent in 2024. Countries contributing to the strong performance of LAC are Brazil, due to a surge in agricultural production with spillover to activity in services, and Mexico, with a delayed post-pandemic recovery in services, and spillovers from resilient demand from the United States.

The July 2023 forecast follows the global recovery from the COVID-19 pandemic and a normalization of the global economic landscape after Russia invaded Ukraine. Consequently, supply chain challenges have mostly been resolved, and logistics costs and delivery times conform to their pre-pandemic levels. Inflation continues to be elevated, resulting in tight monetary policy stances. This development, in turn, raises borrowing costs and dampens economic activity. On a positive note, economic activity proved resilient in 2023 because of a strengthening in the consumption of services.

There are various risks to the IMF's July 2023 WEO. Despite easing the adverse risks compared to the April 2023 WEO, on balance, the risks to the June 2023 WEO remain tilted to the downside. Upside risks to the forecast include a swifter decline in core inflation and stronger-than-expected domestic demand worldwide. The latter, however, would put additional upward pressure on prices, requiring a tighter monetary policy stance. Downside risks comprise persisting inflation, financial market repricing, underperforming recovery of the Chinese economy, increasing debt distress, and deepening geoeconomic fragmentation.



As a result of the risks, the IMF put forth various policy priorities. These entail conquering inflation, maintaining financial stability and preparing for banking sector stress, rebuilding fiscal buffers while protecting the most vulnerable, easing the funding squeeze for developing and low-income countries, enhancing the supply side, and strengthening resilience to climate change.

Table 4: Projections for the world economy and selected economies (Real GDP growth, in percent)

Indicator	2022e	2023f	2024f
World	3.5	3.0	3.0
United States	2.1	1.8	1.0
Euro Area	3.5	0.9	1.5
Latin America and the Caribbean	3.9	1.9	2.2

Source: IMF

e = estimate ; f = forecast

III. CONCLUSION

In the period under review, tourism remained the main engine of economic growth, although tourism performance showed initial signs of pre-pandemic normalization in Q2 2023. Growth in stay-over visitors and tourist spending were the main contributors to the year-on-year increase in real GDP of 5.5 percent. Consumption and investment indicators were primarily positive due to increased local demand for goods and services, and more optimistic business sentiments regarding current economic conditions.

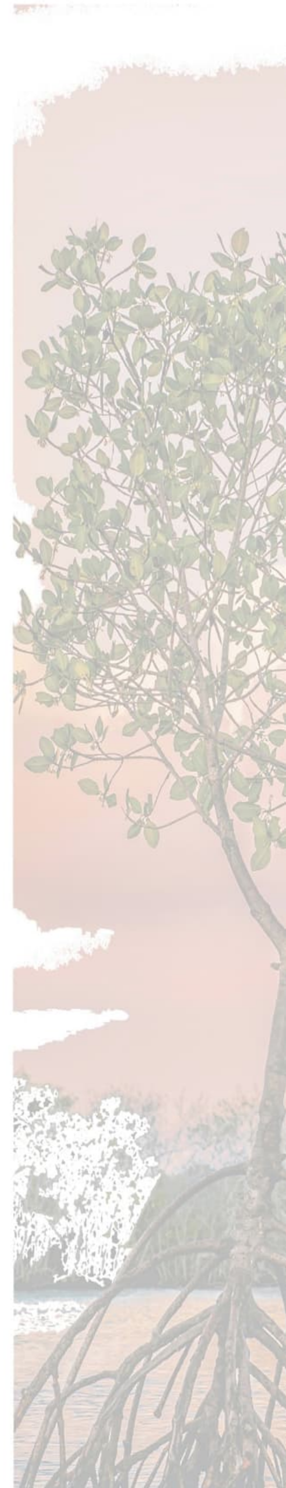
In the first six months of 2023, tourism indicators continued to be robust, albeit at a consistently slower growth rate compared to previous periods. The United States market was the primary driver of tourism demand, with the Canadian and Colombian markets increasing in significance. The hotel sector performance reflected the strong performance in tourism-related activities. The hikes in the number of stay-over visitors, total visitor nights, and tourism revenue led to an 8.2 percentage points rise in the average hotel occupancy rate to 79.3 percent., Meanwhile, the average RevPAR strengthened to $288.8, up from $ 225.2 during the period under review.

In June 2023, the 12-month average inflation accelerated to 5.9 percent, up from 5.5 percent in December 2022 and 3.4 percent in June 2022. In contrast, the End-of-Period (EoP) inflation slowed down to 2.8 percent at end-June 2023, from 5.3 percent at the end of June 2022. The easing of the inflation rate resulted largely from lower oil prices in the international market which drove down the transport component.

The real exchange rate for the Aruban florin vis-à-vis the U.S. dollar stayed unchanged during the second quarter of 2023. The stabilization of the aforementioned real exchange rate at 94.8 index points follows the sustained improvement in the competitive position of Aruba vis-à-vis that of the United States, which started in the second quarter of 2020. A narrowing inflation differential between the United States and Aruba resulted in the stabilization of the real exchange rate.

International transactions settled through the commercial banking sector gave rise to a net foreign exchange outflow of Afl. 106.3 million during the first half of 2023. This outcome was largely related to domestic refinancing of a foreign loan by the private sector and debt repayments by the utilities sector and the GoA, which led to a net outflow on the financial account of the balance of payments. The buoyant tourism performance and resulting strong tourism revenue inflows partially mitigated the net outflow on the financial account.

Overall credit increased sharply in the first two quarters of 2023 after remaining virtually flat since 2020. The uptick in overall credit was mainly caused by augmented business loans, followed by higher loans to individuals. The former is primarily the consequence of greater demand for local refinancing of existing foreign loans due to lower interest rates on the domestic market vis-à-vis those abroad.



Government revenues (excluding nontax revenue) surged in the first half of 2023 vis-à-vis the same period in 2022. Total tax revenues exceeded the level registered in the first half of 2019, indicating that tax-generating activities had recovered beyond the pre-pandemic level. The latter was mainly spurred by receipts from taxes on income and profit, resulting from elevated income tax and wage tax revenues, and coupled with robust profit tax revenues. The rise in government revenues more than compensated for the expansion in government expenditures and led to a financial surplus of Afl. 133.2 million in the first half of 2023. The latter helped to edge down government debt and, combined with the nominal GDP growth, reduced the debt -to-GDP ratio by 7.9 percentage points to 89.2 percent compared to December 2022.

In July 2023, the International Monetary Fund (IMF) published its most recent World Economic Outlook (WEO). The WEO contained updates to the global growth projections presented in April 2023. In the July 2023 WEO, the IMF foresees global growth to decline to 3.0 percent in 2023 and 2024, down from the 3.5 percent estimated for 2022. Despite a relatively higher forecast for 2023 (+0.2 percentage point) compared to the April 2023 WEO, the anticipated expansion for 2023 and 2024 persists below the pre-pandemic average of 3.8 percent.

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