THE BALANCE OF PAYMENTS OF ARUBA IN 2004

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1. Introduction

Aruba being a small island with little natural resources has developed into an economy characterized by an openness to international trade and investment. Residents engage in transactions with nonresidents on a daily basis involving, among other things, the importation of goods, the export of tourism services and international borrowings. All economic transactions of Aruban residents with nonresidents are recorded in its balance of payments.

The balance of payments of Aruba includes two main accounts, i.e., the current account[1] and the capital and financial account[2]. The combined balances[3] on the current account and the capital and financial account determine the overall balance, which on its turn reflects the change in net international reserves[4].

Table 1: Balance of payments of Aruba
(In Afl. million)

	2000	*2001*	*2002*	*2003*	*2004*
1. Current account (net)	389.3	577.1	-596.4	-258.4	33.1
2. Capital and financial account (net)	-456.2	-426.6	602.9	163.2	-24.1
3. Items not yet classified 1)	20.2	-20.8	32.5	34.0	5.3
4. Overall balance (1+2+3)	-46.8	129.7	39.0	-61.2	14.3
a. Oil sector	37.9	43.3	73.1	144.0	73.7
b. Free-zone sector	-5.4	-14.7	-2.8	11.4	9.7
c. Rest of economy	-79.3	101.0	-31.3	-216.6	-69.1
- Private sector	-43.8	141.2	-55.4	-76.0	-76.4
- Public sector	-35.5	-40.2	24.1	-140.6	7.3
5. Banking transactions 2)	19.9	18.5	32.9	-3.8	-11.5
6. Increase (-) in official reserves 3)	26.9	-148.2	-71.9	65.0	-2.8

Source: CBA.

1) Including errors and omissions.
2) Minus (-) sign denotes an increase in assets and a decrease in liabilities.
3) Excluding revaluation differences of gold and official foreign exchange holdings.

In 2004, the external transactions of Aruba led to an Afl. 14.3 million overall surplus on its balance of payments (Table 1), compared to an Afl. 61.2 million deficit a year earlier. This result was due to an Afl. 33.1 million current account surplus, which was offset partially by an Afl. 18.8 million deficit on the capital and financial account (including

[1] This account covers the transactions in goods, services, income and current transfers.
[2] This account includes only transactions of the nonmonetary sector and comprises mainly net capital transfers received by the government, migrants' transfers and transactions in financial instruments. Transactions representing capital inflows are recorded as positive values, while negative values represent capital outflows from Aruba to abroad.
[3] Including items not yet classified.
[4] The net international reserves are the net foreign assets of the monetary sector, comprising the Centrale Bank van Aruba (the Bank) and the commercial banks, that are presented by the categories increase in official reserves and banking transactions, respectively (see Table 1).

items not yet classified). Consequently, net foreign assets of the monetary sector increased to Afl. 652.2 million at the end of 2004, compared to Afl. 637.9 million at end-2003.

This article examines the developments of the various sub-accounts of the balance of payments in 2004 that conduced to the above-mentioned result, thereby distinguishing the oil sector and the free-zone sector from the rest of the economy[5]. The current account will be discussed in section 2, while the capital and financial account will be reviewed in section 3.

2. Current account

2.1 Total economy

In 2004, the current account (Box A) moved to an Afl. 33.1 million surplus, up from an Afl. 258.4 million deficit in the preceding year (Table 2). This improvement originated in the goods and services account that registered a turnround from an Afl. 35 million deficit in 2003 to an Afl. 322.4 million surplus in 2004. The higher net exports of the oil sector played an important role in this turnaround. Furthermore, a positive performance in the tourism sector in 2004 resulted in a remarkable increase in tourism receipts. In contrast, the deficit on the income and current transfers accounts widened by respectively Afl. 32.4 million to Afl. 104.1 million and Afl. 33.6 million to Afl. 185.3 million.

Table 2: Current account
(In Afl. million)

	2000	*2001*	*2002*	*2003*	*2004*
1. Goods and services	550.5	767.2	-252.2	-35.0	322.4
2. Income	-33.1	-87.9	-221.8	-71.7	-104.1
3. Current transfers	-128.1	-102.3	-122.5	-151.7	-185.3
4. Current account (net) (1+2+3)	389.3	577.1	-596.4	-258.4	33.1
a. Oil sector	466.4	621.1	-299.0	64.7	250.4
b. Free-zone sector	-10.6	-16.8	-67.1	12.6	12.1
c. Rest of economy	-66.6	-27.3	-230.3	-335.6	-229.4
- Private sector	20.7	51.7	-110.2	-211.5	-104.7
- Public sector	-87.3	-79.0	-120.1	-124.1	-124.7

Source: CBA.

[5] All remaining sectors of the economy after excluding the oil and free-zone sectors.

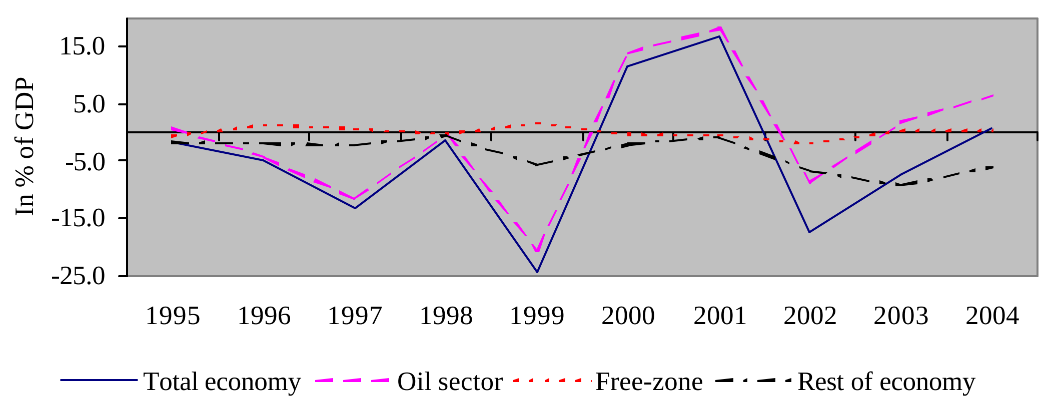
Box A. What is the current account?

The current account of the balance of payments measures the change over time in the sum of the three separate components:

a. goods and services account: This account quantifies the difference between the value of exports and imports of goods and services.
b. income account: This account records the income payments received from nonresidents and income payments made to nonresidents. The income components consist of compensation of employees and investment income. The latter comprises mainly interest and dividend payments.
c. current transfers account: This account measures the difference in the value of private and official transfer payments from and to other countries. The most important transfer payments included are pension premiums and –claims, life insurance premiums – and benefits, contributions to the Solidarity Fund and workers' remittances.

An analysis of the role of each sector shows that the transactions of the oil sector again contributed largely to the positive turnaround in the current account balance. As graph 1 illustrates, the external transactions of this sector determined predominantly the evolution of the Aruban current account balance in the period 1995-2004. In that period, the current account of Aruba recorded mainly deficits with the exception of 2000, 2001 and 2004 when surpluses were recorded due to the high net exports of the oil sector.

Graph 1: Current account balance as percentage of GDP



Furthermore, the current account deficit of the rest of the economy narrowed substantially in 2004 owing to the encouraging inbound tourism developments mentioned earlier. Still, the deficit recorded was once more at a historically high level, i.e., equal to 6 percent of the nominal gross domestic product (GDP). Noticeable is the fact that the current account balance of the rest of the economy recorded only deficits in the period 1995-2004, reflecting deficits on the goods, income and current transfers accounts, while it recorded surpluses on its services account. The current account surplus of the free-zone sector remained virtually unchanged.

The factors causing the movements in the current account of the various sectors mentioned above will be discussed in the following subsections.

2.2 Oil sector

On March 5, 2004, El Paso Corporation sold the refinery and related marine, bunkering and marketing operations to Valero Energy Corporation. The refinery raised its average daily capacity utilization from 61.8 percent in 2003 to 75.7 percent in 2004, thus increasing its throughput volume by 22.7 percent to 77.5 million barrels. Subsequently, the refinery's operating income was positively influenced by both the additional throughput volume and the higher refining throughput margins in 2004 compared to 2003.

In 2004, the current account surplus of the oil sector rose by Afl. 185.7 million to Afl. 250.4 million (Table 3), due largely to a widening goods account surplus which reflected mentioned increases in throughput volumes and refining margins. Both exports and imports of goods went up, i.e., by Afl. 1,212.9 million and Afl. 972.5 million, respectively. The expansion in the goods account surplus was offset partially by larger deficits on the services and current transfers accounts, reflecting respectively the increased payments for freight services and freight insurance premiums. These higher expenses are related directly to the increased imports of goods.

Table 3: Current account of the oil sector
(In Afl. million)

	2000	*2001*	*2002*	*2003*	*2004*
1. Goods and services	512.8	658.5	-271.5	99.8	296.1
A. Goods	904.1	1,030.7	35.5	482.6	723.0
1. Exports f.o.b.	4,336.2	4,142.1	2,513.0	3,559.0	4,771.9
2. Imports f.o.b.	3,432.0	3,111.5	2,477.5	3,076.4	4,048.9
- of which: Goods for processing	3,079.0	2,499.8	1,866.5	2,388.4	3,672.1
B. Services	-391.4	-372.1	-307.0	-382.9	-426.9
1. Receipts	5.1	8.1	7.4	8.0	9.9
2. Payments	396.5	380.3	314.4	390.9	436.7
2. Income	0.0	0.0	0.0	-0.4	0.0
3. Current transfers	-46.3	-37.4	-27.5	-34.7	-45.8
4. Current account (net) (1+2+3)	466.4	621.1	-299.0	64.7	250.4
5. Quantity of oil refined (x 1,000 barrels)	83,553	64,327	52,383	63,155	77,468

Source: CBA.

2.3 Free zone

The activities in the free-zone sector, mirrored by the export and import of goods, declined further in 2004, after reaching a peak in 2001. The export and import of goods fell by respectively Afl. 15.8 million to Afl. 64.6 million and Afl. 11.4 million to Afl. 54.8 million. Consequently, net export of goods fell by Afl. 4.4 million to Afl. 9.8 million. In contrast, net receipts from services amounted to Afl. 2.9 million in contrast to net payments for services of Afl. 0.9 million in 2003. This improvement was primarily related to an increase in retail sales to tourists. The current transfers account deficit remained almost unchanged at Afl. 0.6 million. Consequently, the current account surplus of the free-zone sector declined slightly by Afl. 0.5 million to Afl. 12.1 million (Table 4).

Table 4: Current account of the free-zone sector
(In Afl. million)

	2000	*2001*	*2002*	*2003*	*2004*
1. Goods and services	-9.1	-0.3	9.4	13.3	12.7
A. Goods	3.9	9.9	14.5	14.2	9.8
1. Exports f.o.b.	134.9	144.0	110.6	80.4	64.6
2. Imports f.o.b.	130.9	134.1	96.1	66.2	54.8
B. Services	-13.0	-10.2	-5.0	-0.9	2.9
1. Receipts	3.1	4.9	5.2	6.2	8.6
2. Payments	16.1	15.1	10.3	7.1	5.7
2. Income	-0.1	-15.9	-75.6	0.0	0.0
3. Current transfers	-1.5	-0.6	-1.0	-0.7	-0.6
4. Current account (net) (1+2+3)	-10.6	-16.8	-67.1	12.6	12.1

Source: CBA.

2.4 Rest of the economy

In recent years, the current account deficit of the rest of the economy expanded noticeably, i.e., from a relatively modest Afl. 27.3 million or 0.8 percent of GDP in 2001 to Afl. 230.3 million or 6.7 percent of GDP in 2002 and subsequently to Afl. 335.6 million or 9.3 percent of GDP in 2003 (Table 5). In 2004, this deficit narrowed to Afl. 229.4 million or 6 percent of GDP.

The key driving force behind the large current account deficits of the last few years was the strong domestic demand, arising from increased domestic investments, government expenditures and household spending. In addition, the increased outgoing workers' remittances added to the build-up of current account deficits.

Specifically, the narrower current account deficit of the rest of the economy in 2004 compared to a year earlier stemmed from a rise in net receipts from services. After three consecutive years of decline, the services account surplus climbed by a notable Afl. 267.6 million to Afl. 1,232.3 million in 2004, reflecting largely an Afl. 344.7 million or 22.8 percent surge in tourism receipts, following the bouyant performance of the tourism industry. The higher tourism receipts were offset partially by an Afl. 80.9 million rise in tourism payments to Afl. 352.2 million resulting from residents travelling abroad.

Table 5: Current account of the rest of the economy
(In Afl. million)

	2000	*2001*	*2002*	*2003*	*2004*
1. Goods and services	46.8	109.0	9.8	-148.0	13.5
A. Goods	-1,009.4	-942.8	-1,000.6	-1,112.8	-1,218.8
1. Exports f.o.b.	50.4	52.4	39.6	30.7	31.6
2. Imports f.o.b.	1,059.7	995.2	1,040.2	1,143.5	1,250.3
B. Services	1,056.2	1,051.8	1,010.4	964.7	1,232.3
1. Receipts	1,793.2	1,757.6	1,773.1	1,867.2	2,205.3
- of which: Tourism	1,438.1	1,451.7	1,465.2	1,511.2	1,855.9
2. Payments	737.0	705.8	762.6	902.5	973.0
2. Income	-33.0	-72.0	-146.2	-71.3	-104.1
1. Receipts	94.8	90.1	61.3	62.3	64.5
2. Payments	127.8	162.0	207.5	133.6	168.6
3. Current transfers	-80.4	-64.3	-93.9	-116.3	-138.9
1. Receipts	66.1	70.9	62.3	71.8	74.4
2. Payments	146.4	135.2	156.2	188.1	213.3
- of which: Workers' remittances	59.6	56.4	79.6	92.4	89.9
4. Current account (net) (1+2+3)	-66.6	-27.3	-230.3	-335.6	-229.4

Source: CBA.

The expansion in the services account surplus was cancelled out partially by increases in the deficits on the goods, income and current transfers accounts of Afl. 106 million, Afl. 32.8 million and Afl. 22.6 million, respectively. The deterioration of the merchandise account was brought about by an Afl. 106.8 million or 9.3 percent rise in merchandise imports. The latter increase reflected the expansion in inbound tourism consumption, higher investment and production activities, and also increased consumption expenditures by both the government and the private sector. The increase in the deficit on the income account was mainly the result of more payments of dividend to foreign direct investors and interest to foreign creditors, i.e., mainly by the government. Interest payments by the latter rose to Afl. 43.7 million, up from Afl. 28.5 million in 2003. Furthermore, the widening of the current transfers account deficit reflected in part an increase in payments to nonresidents related to nonlife insurance premiums, pensions and other transfers. In contrast, outgoing remittances made by migrant workers declined slightly by Afl. 2.5 million to Afl. 89.9 million.

Table 6: Current account transactions executed by the government
(In Afl. million)

	2000	*2001*	*2002*	*2003*	*2004*
1. Goods and services	-61.9	-54.9	-80.2	-88.8	-84.7
A. Goods	-5.0	-3.6	-4.0	-3.8	-7.5
B. Services	-56.9	-51.3	-76.2	-85.0	-77.2
2. Income	-23.1	-26.7	-31.7	-28.5	-43.7
3. Current transfers	-2.2	2.6	-8.4	-6.8	3.9
1. Receipts	4.1	7.1	1.1	2.5	7.3
2. Payments	6.3	4.7	9.6	9.1	3.3
- of which: Solidarity Fund	5.5	3.8	9.4	8.8	3.0
4. Current account (net) (1+2+3)	-87.3	-79.0	-120.1	-124.1	-124.7

Source: CBA.

The influence of government spending on the results of the current account of the rest of the economy should not be underestimated. The external transactions executed by the government itself contributed Afl. 124.7 million or 54.4 percent directly to the current account deficit of the rest of the economy in 2004 (Table 6) and consisted primarily of payments of interest to foreign creditors, tourism promotion, and transfers to government offices abroad. The government contributed also indirectly to the results of the current account. Specifically, by increasing its expenditure it pushed up domestic demand of the private sector, resulting in a rise of imports by this sector.

3. The capital and financial account

3.1 Total economy

In 2004, the capital and financial account (Box B) showed a reversal from an Afl. 163.2 million net inflow in 2003 into an Afl. 24.1 million net outflow (Table 7). This net outflow was the result of an Afl. 60.3 million deficit on the financial account (2003: -Afl. 16.6 million), which was mitigated partially by an Afl. 36.3 million capital account surplus (2003: +Afl. 179.8 million).

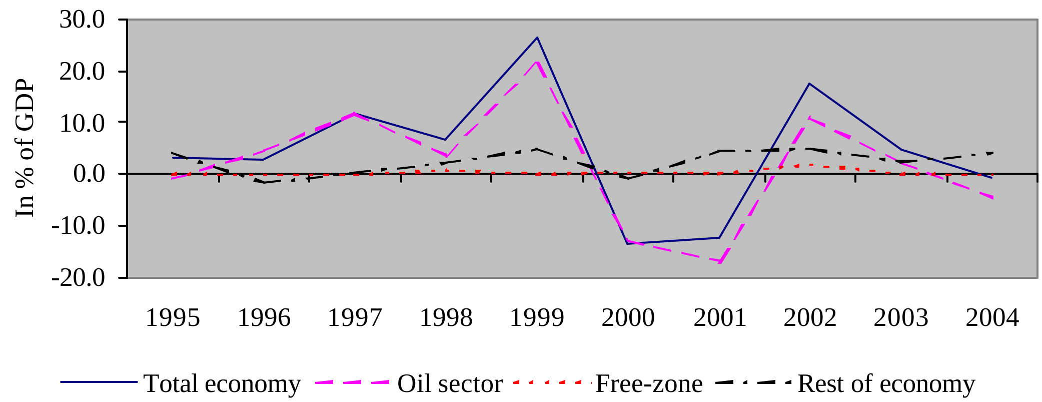
Table 7: Capital and financial account
(In Afl. million)

	2000	*2001*	*2002*	*2003*	*2004*
1. Capital account (net)	20.1	-1.8	38.1	179.8	36.3
A. Capital transfers	20.1	-2.8	40.4	179.0	33.4
B. Acquisition / disposal of n.p.n.f. assets	0.0	1.0	-2.4	0.8	2.9
2. Financial account (net)	-476.4	-424.8	564.9	-16.6	-60.3
A. Direct investment	-231.4	-492.3	542.6	311.6	249.3
B. Portfolio investment	-3.3	74.2	133.3	86.4	77.5
C. Financial derivatives	0.0	0.0	-0.1	0.0	0.0
D. Other investment	-241.7	-6.7	-110.8	-414.6	-387.1
3. Capital and financial account (net) (1+2)	-456.2	-426.6	602.9	163.2	-24.1
a. Oil sector	-428.6	-577.8	372.1	79.4	-176.7
b. Free-zone sector	5.2	2.1	64.3	-1.2	-2.4
c. Rest of economy	-32.9	149.1	166.6	85.0	155.0
- Private sector	-84.7	110.3	22.4	101.5	23.0
- Public sector	51.8	38.8	144.2	-16.5	132.0

Source: CBA.

The result of the capital and financial account was primarily brought about by the transactions of the oil sector that recorded a net capital outflow in contrast to a net capital inflow in 2003. As in the case of the current account, the developments in the oil sector influenced largely the evolution of the capital and financial account of Aruba in the period 1995-2004 (Graph 2). This account recorded predominantly surpluses, thereby mirroring the development of the current account balance. An exception to this were the deficits in 2000, 2001 and 2004. During these years, the oil sector recorded high net exports, which resulted in funds available to the oil sector that were subsequently transferred to abroad.

Graph 2: Capital and financial account balance as percentage of GDP



In contrast, the capital and financial account surplus of the rest of the economy widened further in 2004, largely because of the financial transactions of the government with overseas. As graph 2 shows, the capital and financial account of the rest of the economy recorded mainly surpluses in the period 1995-2004.

Box B. The capital and financial account

The capital and financial account has two major components, i.e., the capital account and the financial account. The capital account comprises capital transfers and acquisition or disposal of nonproduced, nonfinancial assets such as patents, copyrights, trademarks, franchises licenses and land by a government or international organization. Migrants' transfers (i.e., these transfers are contra-entries to flow of goods and changes in financial items that arise from the migration of individuals from one economy to another) and government's grants are examples of capital transfers. The financial account records transactions in Aruba's financial assets and liabilities with the rest of the world. Financial account categories include direct investment, portfolio investment, financial derivatives and other investment.

Direct investment is investment undertaken by a resident entity in one economy in an enterprise resident in another economy with the objective to obtain a lasting interest in the enterprise. Portfolio investment consists of equity and debt securities that are not classified to either direct investment or reserve assets. Financial derivatives are secondary instruments linked to, but separate from, a specific underlying financial instrument or indicator, or commodity, through which specific financial risk can be traded in its own right. Examples of derivatives include options, futures, warrants, currency and interest rate swaps. Other investment includes all financial transactions not covered in direct investment, portfolio investment, financial derivatives or reserve assets.

Capital inflows are presented as positive values, while capital outflows are shown as negative values.

3.2 Oil sector

In 2004, the transactions of the oil sector resulted in an Afl. 176.7 million net capital outflow in contrast to an Afl. 79.4 million net inflow in the previous year. This net capital outflow was brought about mainly by increases in foreign account balances of the oil sector, following a notable rise in net exports of this sector during that year.

Table 8: Capital and financial account of the oil sector
(In Afl. million)

	2000	*2001*	*2002*	*2003*	*2004*
1. Capital account (net)	0.0	0.0	0.0	0.0	0.0
2. Financial account (net)	-428.6	-577.8	372.1	79.4	-176.7
A. Direct investment	-427.0	-576.4	373.0	80.8	75.6
B. Portfolio investment	-1.3	0.0	-0.9	-1.5	0.0
C. Financial derivatives	0.0	0.0	0.0	0.0	0.0
D. Other investment	-0.3	-1.3	0.0	0.0	-252.3
3. Capital and financial account (net) (1+2)	-428.6	-577.8	372.1	79.4	-176.7

Source: CBA.

3.3 Free-zone sector

The capital and financial account transactions of the free-zone sector are in general minimal and are related mainly to loans. The large inflow in 2002 was related to an intercompany loan which was used to pay out dividends. Therefore, the inflow was offset by an Afl. 67.1 million outflow in the current account of this sector.

The financial account transactions of the free-zone companies led to an Afl. 2.4 million net capital outflow in 2004, reflecting mainly repayments of loans, compared to Afl. 1.2 million in 2003.

Table 9: Capital and financial account of the free-zone sector
(In Afl. million)

	2000	*2001*	*2002*	*2003*	*2004*
1. Capital account (net)	0.0	0.0	0.0	0.0	0.0
2. Financial account (net)	5.2	2.1	64.3	-1.2	-2.4
A. Direct investment	-0.1	0.4	65.9	-0.1	0.0
B. Portfolio investment	0.2	-1.6	0.0	0.0	0.0
C. Financial derivatives	0.0	0.0	0.0	0.0	0.0
D. Other investment	5.1	3.3	-1.6	-1.1	-2.4
3. Capital and financial account (net) (1+2)	5.2	2.1	64.3	-1.2	-2.4

Source: CBA.

3.4 Rest of the economy

In 2004, the capital and financial account surplus of the rest of the economy (i.e., excluding the oil and free-zone sectors) widened by Afl. 70 million to Afl. 155 million (Table 10). This result was brought about by a turnaround in the financial account, i.e., from an Afl. 94.8 million net outflow in 2003 to an Afl. 118.7 million net inflow in 2004. This turnaround was caused primarily by an Afl. 281.1 million decline in net other investment outflow to Afl. 132.4 million. To get a better understanding of the changes in the financial account of the rest of the economy, the financial transactions of the public and private sector will be analyzed separately.

The turnaround in the financial account was offset in part by an Afl. 143.5 million decline in the capital account surplus to Afl. 36.3 million. The capital account surplus reflected mainly an Afl. 31.1 million (2003: Afl. 30.1 million) receipt in grants from the Dutch government to the Fondo Desaroyo Aruba FDA) and an Afl. 2.6 million (2003: -Afl. 4.8 million) net inflow of migrants' transfers resulting from a change of residence. It should be mentioned that the large capital account surplus recorded in 2003 was determined largely by the Afl. 171.7 million debt forgiveness[6] by the Italian export credit insurer, SACE, following the settlement of the hotel guarantee that was issued in the past by the government. Furthermore, in 2003 the government paid Afl. 17.9 million to settle the racetrack issue.

Table 10: Capital and financial account of rest of the economy
(In Afl. million)

	2000	*2001*	*2002*	*2003*	*2004*
1. Capital account (net)	20.1	-1.8	38.1	179.8	36.3
A. Capital transfers	20.1	-2.8	40.4	179.0	33.4
- General government	17.0	0.0	37.4	183.8	30.8
- Other sectors	3.1	-2.8	3.1	-4.8	2.6
Migrants' transfers	3.1	-2.8	3.1	-4.8	2.6
Other	0.0	0.0	0.0	0.0	0.0
B. Acquisition / disposal of n.p.n.f. assets	0.0	1.0	-2.4	0.8	2.9
2. Financial account (net)	-53.0	150.9	128.5	-94.8	118.7
A. Direct investment	195.8	83.7	103.7	230.9	173.6
B. Portfolio investment	-2.2	75.8	134.1	87.8	77.5
C. Financial derivatives	0.0	0.0	-0.1	0.0	0.0
D. Other investment	-246.6	-8.6	-109.2	-413.5	-132.4
3. Capital and financial account (net) (1+2)	-32.9	149.1	166.6	85.0	155.0

Source: CBA.

In table 11, the external financial transactions of the government are presented. It is clear that in recent years, the government relied increasingly on the foreign capital market to cover its financial needs. During those years, large capital inflows were recorded in the portfolio investment account, thus contributing to a surplus on the financial account. However, in 2003 the financial account posted an Afl. 200.3 million deficit, reflecting largely the earlier mentioned agreement with the Italian export credit insurer SACE to convert the outstanding amount due into a US$ 110 million (Afl. 196.9 million) loan. As a result of this settlement, outstanding payment arrears to SACE declined by US$ 205.9 million (Afl. 368.6 million). Following the

[6] In 1992, several private companies defaulted on the debt that was incurred to finance certain hotel projects on the island. Because this debt was guaranteed by the Government of Aruba, the government then had to assume the responsibility for servicing this debt totaling, at that moment, US$ 146 million (Afl. 261.3 million). In the period 1992-2003, this debt increased to US$ 206 million because of accumulated interest. On March 7, 2003, the Parliament of Aruba approved an agreement for the settlement of the debt with SACE. Consequently, part of the outstanding amount due, including interest, was converted into a US$ 110 million (Afl. 196.9 million) loan. The remainder of the debt, amounting to US$ 96 million, was forgiven by SACE and, subsequently, was registered as a grant received in the corresponding period (See also Quarterly Bulletin 2004-IV, Centrale Bank van Aruba for further elaboration on this matter).

agreement, part of the loan was paid to SACE in 2003, i.e. US$ 55 million (Afl. 98.5 million).

In 2004, the financial account of the government showed an Afl. 100.7 million surplus in 2004, largely because of a US$ 67 million (Afl. 119.9 million) bond issue on the foreign capital market in April 2004. This transaction was recorded in the portfolio investment account. This inflow was offset partly by an Afl. 22.8 million repayment on foreign loans by the government.

Table 11: Financial account of the government
(In Afl. million)

	2000	*2001*	*2002*	*2003*	*2004*
1. Direct investment	0.0	0.0	0.0	0.0	0.0
2. Portfolio investment 1)	73.4	41.5	109.2	85.9	123.5
3. Financial derivatives	0.0	0.0	0.0	0.0	0.0
4. Other investment	-38.4	-2.7	-2.4	-286.2	-22.8
- Payment arrears 2)	36.4	36.4	36.4	-368.6	0.0
- Loans received 3)	0.0	0.0	26.9	196.9	0.0
- Repayment (-) on loans 4)	-38.1	-39.1	-65.7	-114.9	-22.8
- Other	-36.7	0.0	0.0	0.4	0.0
5. Financial account (net) (1+2+3+4)	35.0	38.8	106.8	-200.3	100.7

Source: CBA.

1) Government debt securities.
2) Payment arrears related to the debt assumption in 1992 by the government of loans to SACE of the private sector as a result of the calling of the hotel guarantees. In 2003, negotiations with SACE on these loans culminated in a repayment of part these loans and the conversion on another part in a long-term loan (see note 3).
3) In 2003, an amount of Afl. 196.9 million (US$ 110 million) was recorded as loans received related to the settlement of the hotel guarantees issue mentioned in note 2.
4) Includes an amount of Afl. 98.5 million (US$ 55 million) as repayment of a loan to SACE in 2003.

The foreign financial transactions of the private sector (i.e., excluding the oil and free-zone sectors) resulted in an Afl. 18 million net capital inflow, down from Afl. 105.5 million in 2003 (Table 12). This outcome was brought about mainly by an Afl. 57.3 million contraction in net direct investment inflow. In addition, the portfolio investment balance turned around from an Afl. 1.9 million surplus to an Afl. 46 million deficit, while the net other investment account deficit narrowed by Afl. 17.7 million to Afl. 109.6 million.

Table 12: Financial account of the private sector (i.e., excluding the oil and free-zone sectors)
(In Afl. million)

	2000	*2001*	*2002*	*2003*	*2004*
1. Direct investment	195.8	83.7	103.7	230.9	173.6
2. Portfolio investment	-75.6	34.3	24.9	1.9	-46.0
3. Financial derivatives	0.0	0.0	-0.1	0.0	0.0
4. Other investment	-208.2	-5.9	-106.8	-127.3	-109.6
5. Financial account (net) (1+2+3+4)	-88.0	112.1	21.7	105.5	18.0

Source: CBA.

The direct investment surplus narrowed in 2004, reflecting mainly an Afl. 72.1 million decline in net inflow related to intercompany debt transactions, resulting in an Afl. 4.4 million net outflow in 2004 (Table 13).

Table 13: Direct investment private sector (i.e., excluding the oil and free-zone sectors)
(In Afl. million)

	2000	*2001*	*2002*	*2003*	*2004*
1. Investment abroad	-10.8	-2.3	-1.1	-11.1	-0.6
2. Investment in Aruba	206.5	86.0	104.8	242.0	174.2
- Intercompany debt	18.7	-23.7	-18.7	67.7	-4.4
- Other investment 1)	187.8	109.7	123.5	174.3	178.6
3. Direct investment (net) (1+2)	195.8	83.7	103.7	230.9	173.6

Source: CBA.

1) Including retained earnings, real estate investment, timeshare sales and equity capital.

The turnaround in portfolio investment of the private sector in 2004 was attributable to a reversal in domestic securities from an Afl. 33.2 million net inflow in 2003 to an Afl. 11 million net outflow in 2004 (Table 14). The net inflow in domestic securities in 2003 was related to the issue of an Afl. 90 million (US$ 50.3 million) bond by the telecommunication company Setar in connection with its acquisition of a corporate status. Of this bond issue Afl. 40.3 million (US$ 22.5 million) was bought by nonresidents.

Table 14: Portfolio investment private sector (i.e., excluding the oil and free-zone sectors)
(In Afl. million)

	2000	*2001*	*2002*	*2003*	*2004*
1. Domestic securities	4.9	-10.8	-7.6	33.2	-11.0
2. Foreign securities	-80.5	45.1	32.5	-31.3	-35.1
- Equity	-80.0	10.8	-8.1	-31.5	-45.2
- Debt securities	-0.5	36.2	41.0	6.9	4.6
- Money market instrument	0.0	-1.9	-0.4	-6.8	5.5
3. Portfolio investment (net) (1+2)	-75.6	34.3	24.9	1.9	-46.0

Source: CBA.

The deficit on the other investment account of the private sector narrowed by Afl. 17.7 million to Afl. 109.6 million in 2004, mainly because of an Afl. 34.9 million smaller increase in foreign bank accounts balances of residents compared to 2003. In contrast, the outflows related to liabilities rose by Afl. 14.1 million (Table 15).

Table 15: Other investment private sector (i.e., excluding the oil and free-zone sectors)
(In Afl. million)

	2000	*2001*	*2002*	*2003*	*2004*
1. Assets	-23.6	10.7	-74.1	-56.0	-24.2
- of which: Currency and deposits	-27.6	-22.6	-57.8	-49.9	-15.0
2. Liabilities	-184.5	-16.7	-32.7	-71.3	-85.4
- of which: Loans	-221.3	-5.9	-27.0	-58.1	-58.3
3. Other investment (net) (1+2)	-208.2	-5.9	-106.8	-127.3	-109.6

Source: CBA.

4. Concluding remarks

The balance of payments of Aruba registered an Afl. 14.3 million surplus in 2004, thus improving its overall position compared to the previous year when an Afl. 61.2 million deficit was recorded. Nonetheless, it is important to reverse the current account of the rest of the economy (i.e., excluding the oil and free-zone sectors), because this account showed in 2004 for the third consecutive year a huge deficit of 6 percent of GDP. This outcome resulted despite a hike in tourism receipts.

The recent large current account deficits of the rest of the economy reflected the much larger domestic spending compared to domestic income. This spending was fueled by a strong domestic demand, in part linked to the high level of investments, which is positive for the long-run economic growth of Aruba. However, these deficits were also driven by government and household consumptive spending. This spending does not add to the productive capital stock of Aruba.

This development should be redressed, because Aruba cannot afford to run large current account deficits on a structural basis. These deficits should be financed either by raising foreign net claims on Aruba, i.e., largely by the acquirement of foreign loans, or by the use of its international reserves. The acquirement of loans may in first instance postpone the weakening of the international reserves position of Aruba, but it also entails the risk of an unsustainable external debt level and debt service obligations, which can only lead to less accessibility, or at worse conditions, to the international capital market. Illustrative is that the net capital inflows in the past to fund the current account deficits led to an increased net indebtedness of the Aruban economy.

Moreover, with regard to the government sector the net capital inflows were used primarily to finance current consumptive spending. This spending will not generate higher output in the coming years. Consequently, generations yet to come would have to consume less of their income in order to settle the ensuing repayment and interest obligations of these loans, thereby reducing their living standards. Given these risks, steps should be taken on a short term to prevent current account deficits in the future. In this regard, the government has an important role to play by tightening its fiscal stance.