

U.S. Virgin Islands Economic Review *Bureau of Economic Research (BER)*

May 2004

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Introduction

Over the past year there was improvement in some sectors of US Virgin Islands economy. The US economic expansion, gains from federal tax cuts, and lower interest rates resulted in increased tourism and business and financial activity. The strong performance of these two sectors helped to support growth and bolstered government revenues. However, the gains from tourist and local consumer spending, business activity, and mortgage refinancing were not strong enough to offset the drag from declines in the construction, trade, transportation and utilities, professional and business, information and other services sectors.

Although, on balance, the economy is recovering, there is still one notable and glaring observation: job growth is nonexistent. The labor market remained in a slump and ended fiscal year 2003 with a net loss of 1,570 jobs. Employment fell in every sector, but the financial activities, leisure and hospitality, and education and health sectors. The construction sector, a primary driver of employment growth over the past couple of years, lost the majority of the jobs due to the completion of major private sector capital projects.

Nonetheless, personal income spurred by tax cuts and lower mortgage rates sustained the economy last year. The gross territorial product (GTP) is estimated to have grown by 3.2 percent. Growth in total personal income was estimated at 2 percent. Despite a 3.6 percent drop in total nonagricultural wage and salary jobs (payroll employment), the economy improved on the strength of consumer spending.

Job growth remained elusive for the first half of fiscal year 2004, and only a modest improvement is expected for the remaining months of the fiscal year. However, the economy is better positioned to experience a more-balanced expansion in fiscal year 2005, given the continued expansion of the US economy, and planned and ongoing capital investment projects such as the HOVENSA's \$400 million desulphurization unit and the \$45 million Carambola Hotel and Convention Center on St. Croix; the \$150 million Yacht Haven Hotel and Marina and the \$9.3 million Red Hook Terminal on St. Thomas; and the \$16 million Enighed Pond development, and the \$12.5 million Grand Bay Resort on St. John.

Prospects for growth, therefore, are favorable with expectations centering on the tourism and tourism-related construction and the financial services sector. Underpinning the expectations for growth are the

assumptions that federal monetary and fiscal stimulus will continue, and business investment will continue to exhibit strong growth. Issues relating to the financial sector, specifically legislation in the US congress to create strict standards for Virgin Islands residency under the US tax code, are an emerging concern for the economy. The financial service sector is among the strongest performer adding over \$100 million to the economy. Proposed changes to tighten the residency requirement for economic development incentive benefits have the potential to disrupt the buoyant growth of this sector, at least in the short-run.

Prospects for the local economy are dependent as much on recovery in the external economy, as on the nature and pace of fiscal stabilization. The 2003 fiscal year ended with a deficit, after financing, of \$4.6 million. A deficit of \$9.6 million is projected for fiscal year 2004 and \$92.4 million for fiscal year 2005.

The persistent nature of the deficit requires solutions that are not one-time in nature, do not include additional borrowing, deferrals or fund shifting. The government is, therefore, taking steps to address the structural imbalance between revenue and expenditure, and to improve public sector financial management through the use of a new financial management system. Options to strengthen revenue administration and collections are also being evaluated and implemented. Departments, for example, can no longer overspend their budget allotments. The Bureau of Internal Revenue (BIR) has acquired additional support staff

and implemented a new financial management system to identify delinquent tax receivables and to increase collection.

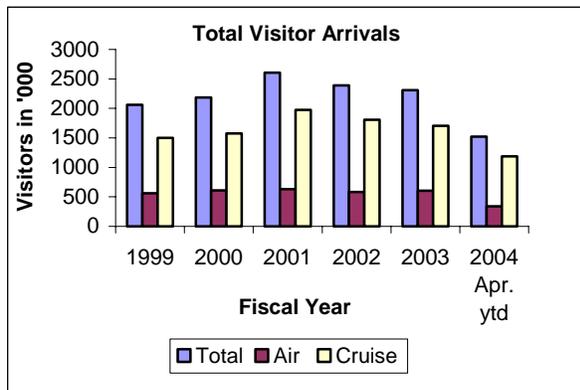
To raise revenues some taxes have been increased such as the highway users' tax and stamp tax. A 4 percent excise tax has also been imposed on personally imported items above \$1000. As part of the expenditure reduction measures, the government stipulated a 5 percent cut in personnel expenditures and recently proposed an additional 2 percent cut, directed a 50 percent cut in overtime, eliminated three paid holidays, and increased health benefit cost sharing to 35 percent for employees and 65 percent for the government.

2004 in review and outlook for 2005

Although recent statistics hint at a nascent recovery in the job market, many of the same conditions that characterized the economy last year remained for the first half of fiscal year 2004. The labor market malaise continued, with nonfarm employment falling by 1.6 percent during this six-month period when compared to the corresponding period in 2003. Employment fell in the construction, trade, transportation and utilities, professional and business, information and other services sectors. Job growth, albeit marginal, occurred in the manufacturing, education and leisure and hospitality sectors. Business activity within the financial activities sector created the strongest job growth during this period, although there was some slowing from the previous year.

Tourism

The buoyant comeback of the tourism industry towards the end of 2003 continued into the first half of fiscal year 2004. Total visitor arrivals grew by 12.5 percent for the six-month period, moving to 1,523,757 from 1,354,493 for the corresponding period last fiscal year. Total overnight visitors increased by 5.6 percent to 338,019 from 320,123. Cruise passenger arrivals increased 14.6 percent to 1,185,738 from 1,034,370 for the first six months of fiscal year 2003.



On a calendar year basis, first quarter visitor arrivals totaled 842,158—an increase of 10.9 percent. Air visitor arrivals, which totaled 182,756 for this period, increased a marginal 1.1 percent over the corresponding period last year. Cruise ship passenger arrivals, which totaled 1,659,402, were up by 14.0 percent over 2003, in spite of the fact that there have been no cruise ship calls to St. Croix. The Territory has witnessed an 18.8 percent increase in cruise ship calls for the first quarter of calendar year 2004.

The Bureau is projecting that total visitor arrivals will reach 2.6 million in fiscal year 2005. Air arrivals are projected to increase by 2.8 percent to 637,000 and cruise passenger arrivals are forecast to grow by 8 percent and reach 1.9 million.

The hotel occupancy rate averaged 66.1 percent March 2004 year-to-date compared to 66.5 percent for the corresponding period in 2003. The occupancy rate for the St. Thomas and St. John district averaged 69.7 percent compared to 72.1 percent in 2003, while the rate for St. Croix averaged 54.3 percent compared to 47.8 percent in 2003.

There are currently 5,059 hotel and condominium rooms in the Territory, down from 5,093 in 2003. Through March 2004, there were 455,377 available room nights—about 1 percent less than the 458,377 room nights available in the corresponding period last year. Occupied room nights March 2004 year-to-date which totaled 301,001 were also 1 percent less than the same period in 2003.

Manufacturing

The manufacturing sector accounts for 5 percent of nonagricultural jobs. This sector, which is dominated by petroleum products, rum, and watches, has experienced a severe decline in employment in recent years. Most of the job losses occurred in the watch industry. Prior to 1997, the watch industry had about 700 workers. Currently there are only 115 jobs in the watch industry. With fewer firms in the watch industry,

try, watch shipment has decreased more than 50 percent in the past five years. In 2003, approximately 482,000 watches were exported compared to over 1,000,000 before 1997. From January to March 2004 watch shipment dropped 15.2 percent to 67,520 from 79,606 the corresponding period last year.

Hovensa, an oil refinery owned jointly by Amerada Hess and Venezuela's national oil company, *Petróleos de Venezuela*, is the Territory's largest manufacturer and the industry's strongest performer. Hovensa and its subcontractors employ about 1,600 workers. In 2002, the oil company completed a \$535 million coker unit with the capacity to process 58,000 barrels of crude daily. The coker enables the refinery to process heavy crude into marketable oil products. Hovensa processes 440,000 barrels daily of refined petroleum products. In 2003, the company shipped \$4.8 billion of refined petroleum products to the United States, a 48 percent increase over 2002.

In early 2005, the company plans to build a \$400 million desulphurization unit to remove sulfur from fuel. This unit is needed to meet stricter Environmental Protection Agency standards. The strike which paralyzed Venezuela at the end of 2002, forced Hovensa to delay construction of the unit. Venezuela, the world's fifth largest oil exporter, supplies Hovensa with more than 50 percent of its crude.

The rum industry consists of one company, *Virgin Islands Rum Industries, Ltd.*, a sub-

siary of *Todhunter International, Inc.*, which is fifty percent owned by *Angostura Inc.*, a Trinidad and Tobago company. The industry has about 50 employees and produces *Cruzan* and *Old St. Croix* brand rum as well as bulk shipments for other labels. About 5,973.3 million proof gallons of bulk rum were shipped to the United States in 2003. Approximately 1,461.6 million proof gallons were shipped for the first four months of 2004.

The number of jobs in manufacturing jobs averaged 2,038 for the first half of fiscal year 2004, up slightly from 2,023 for the same period in fiscal year 2003. The gain in jobs came entirely from Hovensa. The performance of the manufacturing sector should continue to improve over the next year with increased efforts by the University of the Virgin Islands technology park, the VI Port Authority and the Economic Development Authority to attract new industries to the Territory.

Construction

The end to construction of the coker unit and the completion of projects in the tourism sector brought a significant slow-down in economic activity in the construction sector. During the construction of the coker unit some 2,000 construction jobs were added to the economy. Most of those jobs have disappeared, and have not been replaced with new ones. In fiscal year 2002, the construction sector was the strongest performer, averaging 3,182 jobs. In fiscal year 2003, the number of construction jobs fell to 1,737, and further to 1,660 for the

first half of fiscal year 2004.

In 2003, permit value—a leading indicator of growth in the industry—fell a marginal 1.4 percent. Private residential construction increased 31.6 percent and private non-residential construction increased 75.3 percent during this period. Lower interest rates helped to fuel the strong growth in private residential and non-residential permit values. Public construction permits value, on the other hand, was weak during this period decreasing 55.6 percent.

For the first quarter of calendar year 2004, total construction permit increased a healthy 82.8 percent. Private residential construction increased 90.5 percent and private non-residential construction increased 75.1 percent during this period. Public construction permits value was also up by 82.8 percent.

Construction is expected to be strong over the next year supported by major hotel and casino construction, the upgrade and expansion of roads, housing and seaports, and the development of commercial and residential properties. The construction of Hovensa's desulfurization unit, which should begin in 2005, is expected to create 400 construction jobs. Additionally, the Yacht Haven Hotel and Marina is expected to add 120 jobs. Ongoing fiscal and monetary stimulus should continue to boost private residential construction and real estate development.

Trade, Transportation and Utilities

The trade, transportation and public utilities sector had an average of 8,334 jobs in fiscal year 2003, down slightly from 8,345 a year earlier. Jobs in this sector, which currently average 8,249, decreased by 1.2 percent for the first six month of fiscal year 2004 when compared to the corresponding period last fiscal year. Employment in this sector is unlikely to change for the remainder of 2004, but should improve in 2005.

Trade

The number of jobs in the trade sector decreased by 1.3 percent to 6,905 in fiscal year 2003. There was an average of 6,192 retail jobs and 713 wholesale jobs. The number of jobs in trade has not improved during the first six months of fiscal year 2004. Retail trade jobs currently averaged 6,130—2.3 percent lower than the corresponding period in fiscal year 2003. Wholesale trade jobs averaged 687 for this six-month period, 6.7 percent lower than last year.

Employment levels in trade are expected to be flat for the rest of fiscal year 2004. However, trade jobs and retail jobs in particular are expected to increase in fiscal year 2005 as the economy expands and spending grows.

Financial Services

This sector showed the strongest job growth in fiscal year 2003 averaging 2,304 jobs or 16 percent more jobs than the previous fiscal year. Lower interest rates and

the resulting growth in business and residential mortgage fueled the growth in this sector. Growth continued unabated for the first six months of fiscal year 2004, up 8.2 percent over the same period last fiscal year. This sector has averaged 2,395 jobs for the 2004 fiscal year, and is expected to improve moderately in the 2005 fiscal year.

Leisure and Hospitality

The leisure and hospitality sector—which is comprised of hotels and other lodging places, restaurants and food services, and arts and entertainment—held approximately 6,811 jobs in fiscal year 2003, about 1.2 percent more than the previous fiscal year's average of 6,770. For the first six months of fiscal year 2004, there was an average of 6,762 jobs in this sector, down slightly from the corresponding period in the 2003 fiscal year. This year-to-year decline resulted primarily from jobs losses in restaurants and food stores, and arts and entertainment. Hotels and other lodging places experienced an increase in jobs, but not enough to offset the drop in jobs in restaurants and food stores.

An improvement in jobs in the tourism and hospitality industry is forecast for fiscal year 2005, in tandem with anticipated growth in business travel and tourist-related industries.

Public-and private-sector employment

Public sector jobs, which account for 30 percent of all jobs in the Territory, have

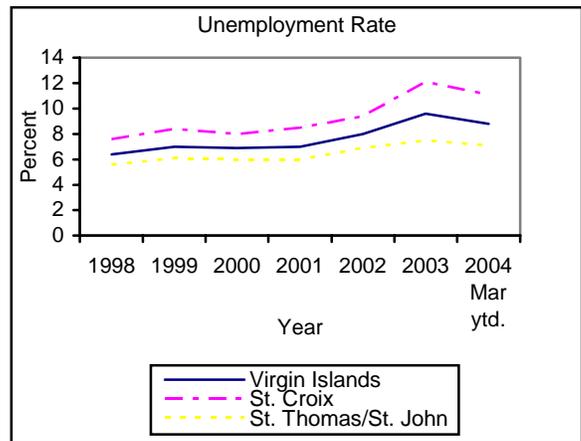
been declining in recent years. Efforts by the administration to reduce local government jobs through attrition, retirement and the elimination of vacant positions have been met with some success. There are currently 12,415 public sector jobs (11,503 local government and 912 federal government). While the federal government jobs increased marginally by 1.7 percent fiscal year 2004 year-to-date, the number of local government jobs has fallen by about 1 percent. Local government jobs are expected to decline even further in fiscal year 2005 in line with the government's cost cutting initiatives. There is expected to be no major change in federal government jobs.

About 70 percent of the Territory's jobs are provided by the private sector. Average employment in the private sector fell by 1.9 percent for the first six months of fiscal year 2004 to 28,959 from 29,526 for the same six-month period in fiscal year 2003. The Bureau expects the number of private sector jobs to grow during fiscal year 2004 on account of increase investment in tourism and other related capital projects.

Employment and unemployment

Nonagricultural wage and salary employment fell by 3.6 percent in fiscal year 2003—to 41,833 from 43,406 the previous fiscal year. March 2004 fiscal year-to-date averaged 1.6 percent less than in fiscal year 2003, decreasing to 41,411 jobs from 42,062 jobs.

According to the Bureau of Labor Statistics, the labor force fell to 48,460 in fiscal year 2003 from 49,346 in fiscal year 2002. For the first half of fiscal year 2004, the labor force has averaged 47,582. Civilian employment declined 1.2 percent for the first half of fiscal year 2004, down to 43,415 from 44,062 for the corresponding period in fiscal year 2003. The Territory's civilian unemployment rate, which averaged 9.5 in fiscal year 2003, has fallen to 8.8 percent in fiscal year 2004.



The rate for St. Croix grew nearly 3 percentage points to 12.9 percent in fiscal year 2003. The rate has since fallen to 11.1 percent March 2004 fiscal year-to-date. The rate for the St. Thomas and St. John district averaged 7.2 percent in fiscal year 2003 and has remained steady in fiscal year 2004.

V.I. NONAGRICULTURAL WAGE AND SALARY EMPLOYMENT
Annual Average, Calendar Years 1996-2002

INDUSTRY	1996	1997	1998	1999	2000	2001	2002
TOTAL NONAGRICULTURAL	41,340	41,500	41,690	41,140	42,050	44,367	43,129
CONSTRUCTION AND MINING	2,520	1,880	1,530	1,690	1,950	3,697	3,017
MANUFACTURING	2,340	2,230	2,420	2,430	2,480	2,191	2,148
DURABLE GOODS	670	660	620	600	610	695	683
INSTRUMENTS & RELATED PRODUCTS	300	270	260	240	280	307	292
NONDURABLE GOODS	1,670	1,570	1,800	1,830	1,870	1,496	1,465
FOOD & KINDRED PRODUCTS	260	260	250	260	260	262	270
PRINTING & PUBLISHING	200	190	240	230	230	214	198
TRANSPORTATION, COMM., & PUB. UTILITIES	2,280	2,360	2,370	2,360	2,450	2,507	2,446
WATER TRANSPORTATION	460	450	480	480	480	543	532
TRANSPORTATION BY AIR	500	490	480	510	570	556	552
COMMUNICATIONS	750	750	790	770	760	781	738
WHOLESALE TRADE & RETAIL TRADE	9,320	9,440	9,110	8,820	8,950	9,602	9,788
WHOLESALE TRADE	1,070	1,150	1,150	1,090	1,080	1,116	1,108
RETAIL TRADE	8,250	8,290	7,960	7,730	7,870	8,486	8,680
FOOD STORES	1,340	1,260	1,160	1,070	1,130	1,174	1,204
EATING & DRINKING PLACES	1,990	2,050	2,090	2,010	2,100	2,294	2,296
JEWELRY, LIQUOR, GIFT & REL. STORES	2,080	2,090	2,090	1,970	2,050	2,101	2,134
FINANCE, INSURANCE, & REAL ESTATE	1,800	1,870	1,880	1,940	1,950	1,931	1,918
BANKING	890	890	890	910	920	878	838
REAL ESTATE	540	610	620	680	680	655	679
SERVICES	9,020	9,980	10,620	10,450	11,240	12,113	11,195
HOTELS & OTHER LODGING PLACES	2,580	3,340	3,820	4,030	4,230	4,054	3,934
BUSINESS SERVICES	1,260	1,370	1,420	1,210	1,280	1,916	1,968
AUTO & MISCELLANEOUS REPAIR SERV.	1,530	1,520	1,480	1,380	1,930	2,050	1,223
LEGAL SERVICES	370	380	400	420	410	420	416
EDUCATIONAL SERVICES	730	730	740	740	730	723	726
TOTAL PRIVATE SECTOR	27,280	27,760	27,930	27,690	29,020	32,041	30,512
GOVERNMENT	14,060	13,740	13,760	13,450	13,030	12,326	12,617
FEDERAL	990	860	880	880	860	905	905
TERRITORIAL	13,070	12,880	12,880	12,570	12,170	11,438	11,796

SOURCE: V.I. Department of Labor, Bureau of Labor Statistics.

Labor Force Data

U.S. Virgin Island: Calendar Years 1995:2004

Year	Virgin Islands				St. Croix				St. Thomas & St. John			
	Labor Force	Civilian Employed	Unem- ployment Monthly	Unem- ployment Rates	Labor Force	Civilian Employed	Unem- ployment Monthly	Unem- ployment Rates	Labor Force	Civilian Employed	Unem- ployment Monthly	Unem- ployment Rates
1995	47,810	45,070	2,740	5.7	19,970	18,480	1,490	7.4	27,840	26,590	1,250	4.5
1996	45,760	43,370	2,380	5.2	18,670	17,780	890	4.8	27,090	25,590	1,490	5.5
1997	46,200	43,500	2,700	5.9	19,100	17,830	1,270	6.7	27,100	25,670	1,430	5.3
1998	46,690	43,690	3,000	6.4	19,380	17,910	1,470	7.6	27,310	25,780	1,530	5.6
1999	46,400	43,140	3,260	7.0	19,300	17,690	1,610	8.3	27,100	25,360	1,650	6.1
2000	47,730	44,500	3,230	6.8	19,820	18,250	1,570	7.9	27,910	26,250	1,660	5.9
2001	49,670	46,140	3,530	7.1	21,610	19,840	1,770	8.2	28,290	26,300	1,760	6.2
2002	49,300	44,980	4,320	8.8	20,320	17,990	2,330	11.5	28,980	26,990	1,990	6.7
2003	48,170	43,640	4,530	9.4	19,960	17,460	2,500	12.5	28,210	26,180	2,030	7.2
2004	47,473	43,417	4,057	8.5	19,470	17,367	2,103	10.8	28,003	25,050	1,953	7.0

Note: data for 2004 is a 3-month average.

Source: VI Department of Labor, Bureau of Labor Statistics

Labor Force Data

U.S. Virgin Island: Fiscal Years 2000-2004

Year	Virgin Islands				St. Croix				St. Thomas & St. John			
	Labor Force	Civilian Employed	Unem- ployment Monthly	Unem- ployment Rates	Labor Force	Civilian Employed	Unem- ployment Monthly	Unem- ployment Rates	Labor Force	Civilian Employed	Unem- ployment Monthly	Unem- ployment Rates
2000	47,181	43,873	3,224	6.8	19,571	18,023	1,557	8.0	27,602	25,934	1,668	6.1
2001	49,476	46,104	3,372	6.8	21,287	19,600	1,687	7.9	28,400	26,504	1,685	5.9
2002	49,346	45,203	4,143	8.5	20,621	18,452	2,169	10.5	28,895	26,835	1,973	6.8
2003	48,460	43,833	4,627	9.5	20,096	17,533	2,585	12.9	28,342	26,300	2,042	7.2
2004	47,582	43,415	4,167	8.8	19,545	17,367	2,178	11.1	28,037	26,048	1,992	7.1

Note: data for 2004 is a 3-month average.

Source: VI Department of Labor, Bureau of Labor Statistics

U.S. Virgin Islands Tourism Statistics, Calendar Years 1995-2003

Year	Total Visitors		Air Visitors		Cruise Visitors		Tourist Rooms				
	Number (000s)	Percent Annual Change	Number (000s)	Percent Annual Change	Number (000s)	Percent Annual Change	Room Nights Available (000s)	Room Nights Occupied (000s)	Average Stay (Nights)	Occupancy Rate (%)	Total Rooms
1995	1,741.3	-9.4	570.0	-16.0	1,171.3	-5.8	1,793.4	1,047.8	4.4	59.0	5,154
1996	1,778.7	2.1	462.3	-18.9	1,316.4	12.4	1,374.9	711.0	4.3	51.6	4,087
1997	2,128.0	19.6	508.8	10.1	1,619.0	23.0	1,544.4	824.6	4.2	53.3	4,401
1998	2,138.9	0.5	523.4	2.9	1,615.5	-0.2	1,742.2	914.4	4.4	52.5	4,929
1999	1,964.3	-8.2	560.1	7.0	1,403.6	-13.1	1,742.0	967.9	4.4	55.7	4,849
2000	2,396.6	22.0	628.2	12.2	1,768.4	26.0	1,815.2	1,059.7	4.5	57.7	4,997
2001	2,501.0	4.4	609.6	-3.0	1,891.4	7.0	1,838.4	1,051.3	4.5	55.7	5,045
2002	2,336.7	-6.6	598.0	-1.9	1,738.7	-8.1	1,857.5	1,057.5	4.4	57.0	5,092
2003	2,394.7	2.5	620.8	3.8	1,773.9	2.0		1,051.5	4.4	57.2	5,045