

# U.S. Virgin Islands Economic Review

Bureau of Economic Research

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## Economic Highlights

*The economy performed well in 2007 with real economic growth about 3.6 percent.*

*The strongest performing sectors were manufacturing, construction, tourism and business services.*

*Refined petroleum products, which value nearly \$11 billion, account for 95 percent of total exports.*

*Approximate 7.4 million proof gallons of rum were exported to the United States.*

*The civilian employment increased 2 percent to 49,287 from 48,312.*

*The territory's unemployment rate declined from 6.3 percent to 6.0 percent. The rate for St. Thomas/ St. John decreased from 5.4 to 5.2 percent and from 7.5 percent to 7.1 percent for St. Croix.*

*A total of 2,570,676 visitors came to the Territory in fiscal year 2007. Air visitors totaled 676,039 and cruise passengers totaled 1,894,638.*

*General Fund gross revenues were \$944 million. Individual income tax was \$427 million, gross receipts \$147 million, corporate income tax \$154 million, trade and excise tax \$24 million and real property tax \$54 million.*

## Overview

Reservations about the durability of the expansion of the economy of the US Virgin Islands can now be set aside in light of its reasonably good performance in 2007. The economy held firm in line with projections for real Gross Territorial Product (GTP) growth of 3.6 percent. Growth was supported by gains in output in manufacturing, construction, tourism and business services.

Not all sectors posted growth, however. The Financial Activities and the Information sectors were two that under-performed. The Financial Services sector continued to lose jobs, a fall-out from the American Job Creation Act 2004 which changed requirements for residency and source of income under the Economic Development Commission (EDC) incentive program. Job losses in the telecommunication industry caused a decline in employment in the Information sector. The manufacturing sector has also shed some jobs, the result of the closure of a pharmaceutical company.

Despite inflationary pressures, higher interest rates and a weaker residential housing market, macroeconomic indicators are holding up. The economy experienced an overall improvement in the job market. The Territory's unemployment rate—a simple measure of economic health—has steadily declined from 6.3 percent last fiscal year to 6.0 percent this fiscal year. There were 975 more jobs in the economy this year, most of which were created in the private sector. Inflation remained contained despite the effects of a rise in fuel prices. Excluding fuel prices, other consumer items have risen only modestly in 2007.

Strong growth in revenues associated with higher income, business and consumer spending strengthened the fiscal situation and boosted fiscal year 2007 revenues to record levels. With the exception of corporate income tax which declined to \$153 million after correcting for business estimated payments, other major tax revenues were above target. Individual income receipts set a new record at \$427 million, gross receipts \$147 million and trade and excise \$24 million. Preliminary general fund gross revenues for fiscal year 2007 were \$944 million, up 7 percent from \$882 million in fiscal year 2006.

## Economic Outlook

Manufacture, construction, tourism and business activity will continue as the primary movers of economic activity in the year ahead. Growth is expected to moderate as the effects of a slowdown in the US economy feed through. Exogenous factors, including a run-up in oil prices and rising interests rates have begun to impact the local economy and cloud the outlook for business investment and consumer spending. Tighter credit conditions, the housing downturn and higher oil prices are likely to squeeze economic growth as investors and consumers' spending contract. Although yet to emerge, a decline in consumer spending is anticipated as consumers grapple with rising costs for food and other consumer goods, utility, consumer loans and interest rates on credit cards.

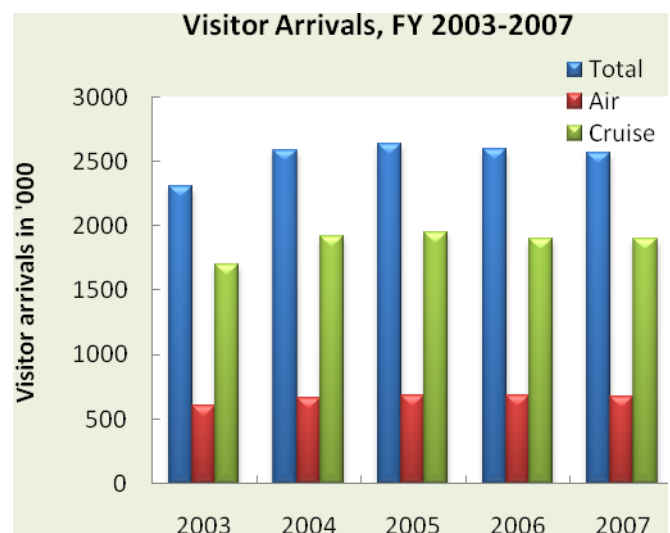
So far though, the economy is moving along buttressed by fairly strong consumer and business spending. Added to this, increased demand for oil, tight inventories and geopolitics are keeping crude prices and refined products at higher levels resulting in strong growth in output in the manufacturing sector. Higher oil prices have a two-edged impact on the economy. The economy is impacted by oil-led inflation as consumers pay more for goods and services, but at the same time the economy benefits from huge profits that the oil industry generates.

To the extent that there continues to be a strong demand for oil, consumers spending remain at modest levels and business continue to invest in major development projects, the economy should remain on course and demonstrate modest growth in 2008. The prospects for growth become more uncertain, however, as the risks to the economy heighten and create deterioration in consumer and business confidence. Evidence is mounting that the US economy has weakened dramatically, thereby threatening growth in the near term.

## Sectoral Performance

### Tourism

Visitor arrival performance was sub-par in fiscal year 2007. Air arrivals were down by 1.7 percent and cruise passenger arrivals were at the same level as the 2006 fiscal year. There were 676,039 air visitors during this period compared to 687,811 air visitors for fiscal year 2006. There were 1,894,637 cruise passengers compared to 1,903,533 the year before, a miniscule 0.5 percent decrease. In total, there were 2,570,676 visitors, down 0.8 percent from fiscal year 2006.



The slump in air visitor arrivals continued for most of 2007. This trend appears to be reversing in recent months, however, primarily due to the launching in May the *90th Anniversary Transfer Day* promotion spearheaded by the Virgin Islands Department of Tourism in conjunction with the Virgin Islands Hotel and Tourism Association. This program gave a desired jump to the industry and created a lift in air visitor arrivals beginning in August. Other major special events such as the Caribbean music entertainment network Tempo's second year bash on St. Croix in October and the Iron Man race also held on St. Croix positively impacted air arrivals. The result was the first quarter of

fiscal year 2008 registered a 16 percent year-on-year increase. New marketing and promotional efforts such as the *Winter Escape* promotion which gives a \$200 gift card and a \$100 resort credit or a discount on the room for bookings made February 3-16, 2008, and the St. Croix Air Credit program which gives a \$250 credit per person on stays of seven nights or more will likely turn the tide and lead to stronger arrivals in 2008. Approximately 700,000 air visitors are projected for 2008.

The lack of robustness of the cruise industry is attributed to a drop in demand for Caribbean cruises blamed on unfavorable economic factors in the US—such as higher energy prices and a weakening housing market which are affecting consumers discretionary income—and not a loss of allure or popularity for the region as have been suggested. According to Carnival Cruise Line—the largest cruise passenger carrier in the Caribbean—their ships carried an unprecedented 2.9 million passengers to the Caribbean in the 2007 season, more than any other year. Carnival also reported that they saw much more strength in their bookings for the second half of 2007 and early 2008. Further, according to the Cruise Line International Association (CLIA), the Caribbean is the most sought after cruise destination by far, with the region featured on nearly half of all itineraries of North American cruise operators.

Against this backdrop of stronger bookings to the region as well as an aggressive effort on the part of the new administration to bring cruise ship passengers back to St. Croix, cruise passenger arrivals to the Territory in 2008 are projected at 1.9 million. First quarter fiscal 2008 has registered a 4 percent increase over the corresponding period in 2007, signaling stronger performance in 2008.

## Manufacture

The manufacturing sector accounts for 12 percent

of GTP. The major commodities produced by this sector, in addition to watches, are refined petroleum products and rum. This sector was a strong performer in the past year, with both the volume and value of its major export—refined petroleum products and rum—rising sharply.

This sector accounts for 5 percent of jobs in the economy. The number of manufacturing jobs averaged 2,256 in fiscal year 2007, a 2.5 percent decline from fiscal year 2006. The closure of Pralex Corporation pharmaceutical company resulted in the loss of 50 jobs.

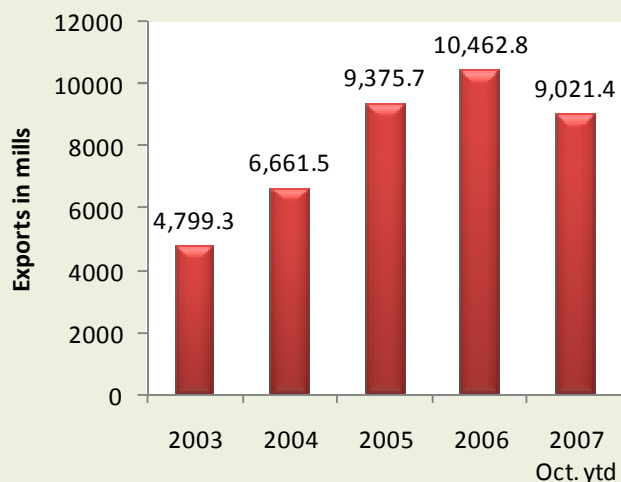
This sector is expected to continue to perform well in 2008 with increased production in the oil and rum industries.

## Oil Industry

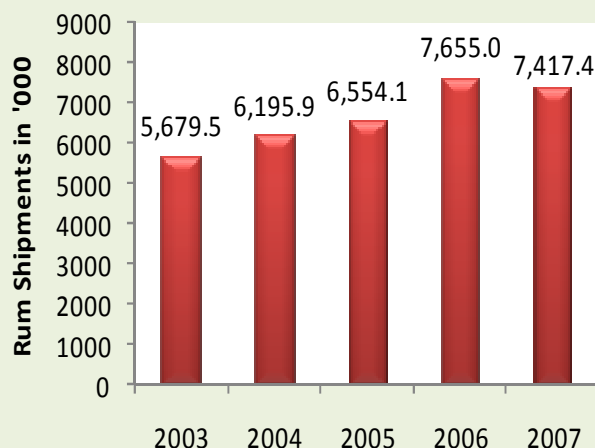
Hovensa, L.L.C., a limited liability company formed by a wholly owned subsidiary of Hess Corporation and a wholly owned subsidiary of Petróleos de Venezuela, S.A. (PDVSA) is the Territory's largest manufacturer and the industry's strongest performer. The refinery processes crude from all over the world, although the majority of crude is supplied from Venezuela. It has crude oil processing capacity of 495,000 barrels per day (BPD). The refinery also operates a Fluid Catalytic Cracking unit capable of producing 175,000 BPD of gasoline. Approximately 1,200 people are employed at the refinery.

Nearly \$11 billion of refined petroleum products were exported to the US last year—a 12 percent jump over the previous year. Indications are that the value of 2007 exports will top that number. October 2007 year-to-date figures, the most recent available, show the value of refined petroleum products exported to the US was \$9.02 billion.

**Refined Petroleum Exports to the US,  
2003-2007**



**Rum Shipments to the United States,  
2003-2007**



Strong demand for oil as well as fallen supplies pushed the cost of a barrel to a record \$97. As of this writing, a cost of a barrel of oil has fallen to \$93. Although the price of oil has fallen in the past week, neither a drop in the value nor volume of export is anticipated in 2008.

### Rum Industry

A large percentage of manufacturing shipments come from rum production, the industry's next strongest performer. The rum industry consists of a single company, Cruzan VIRIL, Ltd., a wholly-owned subsidiary of The Absolut Spirits Company, Inc., a New York-based company and V&S Vin & Sprit AB, a Swedish-based international wine and spirits company. The company has about 60 employees and manufactures Cruzan and Old St. Croix brand rum as well as bulk shipments for other labels. Rum produced in the US Virgin Islands is exported to the US primarily in bulk, and sold to local and regional bottlers for sale under a variety of private label and regional brand names. Cruzan Rum is purported to be the fifth-leading premium brand in the United States in according to statistics published by Impact Adams Liquor Handbook, a leading spirits industry publication.

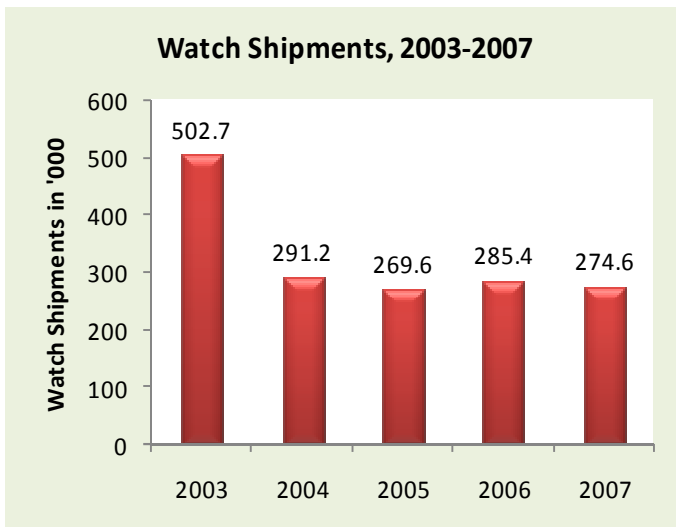
The industry shipped 7.4 million proof gallons of rum to the US in 2007 for which the Territory received \$86.7 in excise taxes. Some 7.6 million proof gallons of rum is projected for export in 2008. The federal government imposes and collects federal excise taxes on rum produced the Virgin Islands and exported to the United States. The current assessed excise tax rate in \$13.50 price per proof gallon and the Cover Over rate (the rate at which excise taxes are transferred back to the Virgin Islands) is \$13.25.

The outlook for this industry is one of solid growth. In anticipation for increased production, the company is currently constructing additional space to house 40,000 additional barrels. The company has in place a five-year marketing agreement with the government, whereby rum revenues that exceed the 2005 threshold will be share along a 65/35 percent split. The 35 percent the company receives will be used to promote and market the brand.

### Watch industry

Output from the watch industry has declined significantly since the late 1990s when over 1,000,000 watches were exported. The industry which is made up of three companies—Belair

Quartz, Hampden Watch, Co., and Tropex Watch Co., employs about 118 workers. Approximately 274,625 watches were exported in fiscal year 2007 down from 285,428 the previous year. The watch industry continues to struggle in the face of high unit costs and increased competition which have affected output. The US Department of Commerce ruling in May 2007 which increased the cap on the values of watches imported duty-free from the US Insular Areas to the US mainland may lead to stronger output. The value of export watches increased from \$800 to \$3,000 per watch value and watch movements from \$35 to \$300 per watch movement value. This change was due to the increase in the price of gold.



## Construction

The construction sector accounts for an estimated 4.6 percent of GTP. Activity in the construction sector, as measured by the number and value of approved development and the value of building permits, has softened signaling the completion of major tourism-related development, housing and seaports, and the development of commercial and residential properties. The value of construction permits—an indicator of current and of future activity—declined by 37 percent in fiscal year 2007 from the previous year. Despite this drop, there are new projects on the drawing

board that should keep the industry afloat. Foremost among these projects are four on St. Croix: a \$47 million Gallows Bay Marina, a \$250 million Golden Resorts 400-room hotel, casino and convention center, and \$60 million William and Punch 300-room hotel and casino and 125 luxury home development, and Stanford Caribbean \$50 million aviation hangar and 900-sq. ft. office building.

On St. John, a \$5 million Coral Bay 116-slip marina and office building, the \$54 million Pond Bay Club luxury resort, the \$50.8 million Calabash Boom housing development and the \$50.8 million Sirenusa 47-private homes development are among the projects that will create activity. St. Thomas also has a number of projects which include the \$80 million 70-room boutique hotel at Yacht Haven Grande slated for 2008, the \$120 million Ritz Carlton luxury homes development, \$15 million East-End Plaza retail and commercial office space, \$60 million Dolphin cove housing development, and the \$13 million Long Bay Road expansion phase 1.

The number of construction jobs averaged 3,144, in fiscal year 2007 nearly 200 jobs more than the previous fiscal year. Most of these jobs resulted from retrofitting and maintenance projects in the oil industry. There was an average 3,370 jobs in the industry in the first quarter of fiscal year 2008.

## Leisure and Hospitality

The leisure and hospitality—which is comprised of hotels and other lodging places, restaurants and food services, and arts and entertainment—accounts for 7 percent of GTP and 16 percent of total employment. This industry averaged 7,320 jobs in fiscal year 2007, and had a year-over-year job growth rate of 2.3 percent. The job growth driver was the arts, entertainment and recreation super-sector. Delving deeper, activity in amusement, gambling and recreational sub-sector is driving the growth. An expanding hotel

and villas industry and new restaurants, such as Yacht Haven Grande Wikked, Grande Cru and Fat Turtle, added to the gains in the leisure and hospitality sector.

### Trade, Transportation and Utilities

The trade, transportation and public utilities sector holds the second largest share of jobs in the economy, averaging—8,635 jobs in 2007, up 1.0 percent over the last fiscal year.

### Retail and Wholesale Trade

The trade sector contributes 12 percent to GTP. Retail trade accounts for 10 percent and wholesale just about 2 percent. There were about 6,973 jobs in the trade sector in fiscal year 2007—about 1.0 percent over fiscal year 2006. Retail trade jobs averaged 6,194 and were up 1.3 percent, while wholesale trade jobs averaged 779, down by 2 percent from last fiscal year. Trade jobs and retail jobs in particular are expected to increase modestly in fiscal year 2008 with the opening of new retail stores at Yacht Haven Grande and Crown Bay Carnival Center.

### Financial Services and Real Estate

The Financial services sector continues to show decline in jobs, albeit marginal. Job in this sector fell by 1.0 percent in fiscal year 2007 compared to 2006. The number of jobs averaged 2,576, down from 2,602 in fiscal year 2006.

The decline of this sector points to uncertainties in the Economic Development Commission (EDC) program brought about by the American Job Creation Act 2004 that drastically changed the residency requirement. Because of the stiffer residency requirements a number of EDC beneficiaries closed their operations, thereby drastically reducing substantial tax revenues.

The recent US Treasury Regulations (TD9297) effective November 14, 2006 which relaxed the rules governing residency requirements under

the tax laws, may ease some concerns and allow for the EDC program to rebound. The relaxed rule allows taxpayers to average the 183-day residency over a period of three years instead of requiring they spend 183 days each tax year in the Territory. Taxpayers are still required to spend at least 60 days in the Territory.

## Employment

Employment statistics indicate that 49,287 persons were employed in the 2007 fiscal year compared to 48,312 in 2006. This represents growth of 2 percent. Of the 49,287 employed, 21,193 were employed on St. Croix and 28,094 on St. Thomas and St. John.

The improvement in the economy is manifested in the labor market. The Territory's civilian employment has grown from 48,312 to 49,287 in 2007. There were 21,193 persons employed in the St. Croix district and 28,094 persons in the St. Thomas and St. John district.



The Territory unemployment rate fell from 6.3 percent to 6.1 percent. The rate for St. Croix fell from 7.5 percent to 7.1 percent, while the rate for St. Thomas and St. John fell from 5.4 percent to 5.2 percent.

## Public-and private-sector employment

### Wage and Salary Employment

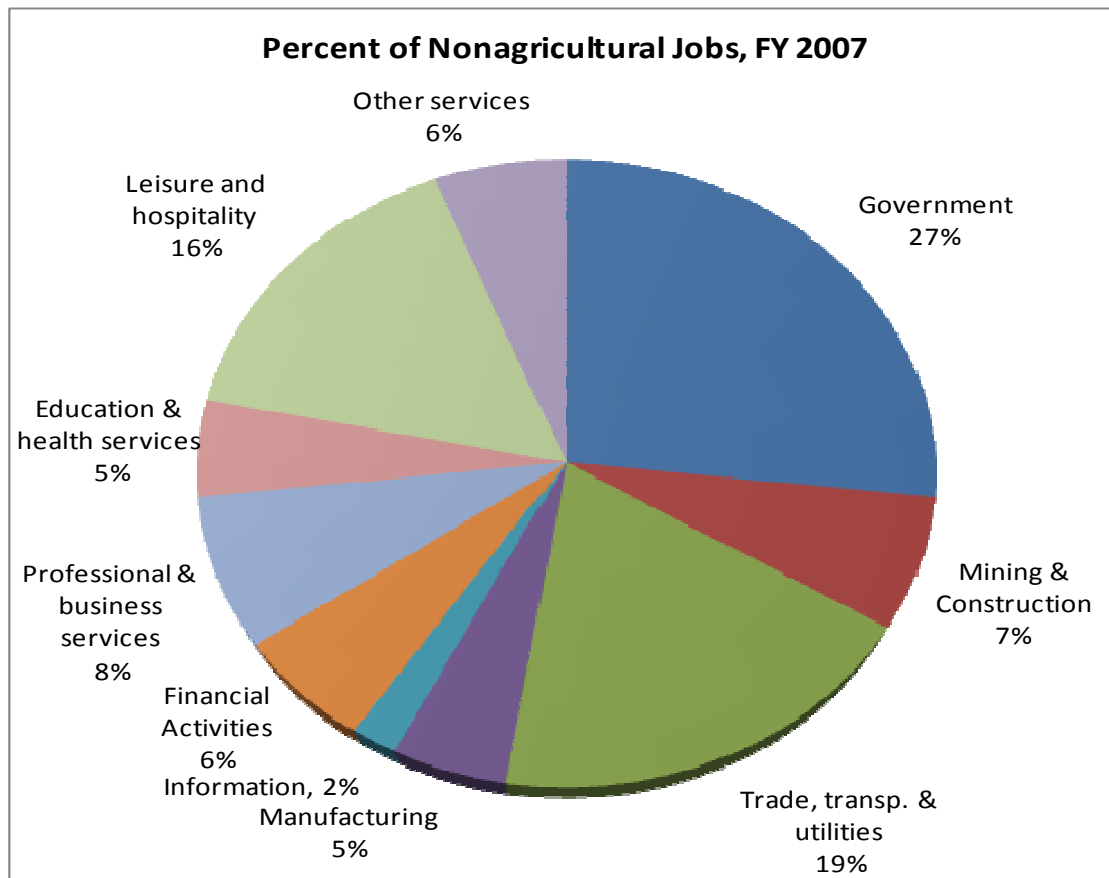
There are 45,787 persons employed in non-agricultural wage and salary jobs in fiscal year 2007 compared to 44,930 in fiscal year 2006, an increase of 1.9 percent. Nine in ten jobs in the US Virgin Islands are in the service-producing industries and one in every ten jobs in the goods producing industries.

Government; trade, transportation, and utilities; and leisure and hospitality are the industries with the largest number of jobs. These three sectors account for 62 percent of all jobs. Professional and business services, construction and financial activities account for 8 percent, 7 percent and 6 percent, respectively. Manufacturing and educational and health services account for 5 percent each, while other

services and information account for the remainder of the jobs.

Public sector jobs increased about 2.0 percent in fiscal year 2007. The increase occurred in both federal and local government jobs. Local government jobs averaged 11,690, up 1.9 percent over fiscal year 2006, while federal government jobs averaged 848 or a 1.7 percent increase from last fiscal year.

The private sector is the largest employer in the Territory, employing 7 in every 10 persons. This sector has improved in the past year adding more than 600 jobs. There were 33,248 private sector jobs, up 2 percent from 32,620 in fiscal year 2006. Continued improvement in jobs in this sector rests on the buoyancy of the tourism industry, capital investment and the general strength of the economy.



**Labor Force Data**  
**U.S. Virgin Island: Fiscal Years 2003-2007**

Year	Virgin Islands				St. Croix				St. Thomas & St. John			
	Labor Force	Civilian Employed	Unemployment	Unemployment Rates	Labor Force	Civilian Employed	Unemployment	Unemployment Rates	Labor Force	Civilian Employed	Unemployment	Unemployment Rates
2003	48,460	43,833	4,627	9.3	20,096	17,533	2,585	12.9	28,342	26,300	2,042	7.2
2004	49,536	45,694	4,092	8.3	20,275	18,178	2,097	10.4	29,261	27,266	1,995	6.8
2005	50,867	47,178	3,689	7.3	20,751	19,941	1,810	8.3	29,116	27,237	1,880	6.6
2006	51,565	48,312	3,253	6.3	22,462	20,774	1,687	7.5	29,103	27,538	1,565	5.4
2007	52,430	49,287	3,141	6.0	22,771	21,193	1,619	7.1	29,617	28,094	1,522	5.2

Source: VI Department of Labor, Bureau of Labor Statistics

**V.I. NONAGRICULTURAL WAGE AND SALARY EMPLOYMENT**  
**Annual Average, Fiscal Years 2002-2007**

INDUSTRY	FISCAL YEARS						% CH. 07/06
	2002	2003	2004	2005	2006	2007	
<b>TOTAL NONAGRICULTURAL</b>	43,406	41,833	42,276	43,711	44,930	45,787	1.9
<b>TOTAL PRIVATE SECTOR</b>	30,876	29,207	29,821	31,391	32,620	33,248	1.9
<b>CONSTRUCTION AND MINING</b>	3,181	1,737	1,695	2,213	2,960	3,144	6.2
<b>MANUFACTURING</b>	2,107	2,023	2,062	2,210	2,315	2,256	-2.5
<b>TRANSPORTATION, WAREHOUSE, &amp; PUB. UTILITIES</b>	1,344	1,429	1,490	1,651	1,643	1,662	1.2
<b>WHOLESALE TRADE &amp; RETAIL TRADE</b>	6,997	6,905	6,871	6,896	6,909	6,973	0.9
<b>WHOLESALE TRADE</b>	729	713	705	769	794	779	-1.9
<b>RETAIL TRADE</b>	6,268	6,192	6,166	6,127	6,115	6,194	1.3
<b>INFORMATION</b>	928	877	876	891	845	809	-4.3
<b>FINANCIAL ACTIVITIES</b>	1,987	2,304	2,483	2,569	2,602	2,576	-1.0
<b>PROFESSIONAL AND BUSINESS</b>	3,288	3,103	3,277	3,391	3,452	3,492	1.2
<b>EDUCATION AND HEALTH</b>	1,936	2,168	2,182	2,204	2,323	2,376	2.3
<b>LEISURE AND HOSPITALITY</b>	6,727	6,811	7,119	7,101	7,132	7,374	3.4
<b>OTHER SERVICES</b>	2,213	1,839	1,845	2,357	2,378	2,310	-2.9
<b>GOVERNMENT</b>	12,530	12,626	12,449	12,320	12,311	12,539	1.9
<b>FEDERAL</b>	909	906	875	853	834	848	1.7
<b>TERRITORIAL</b>	11,621	11,720	11,575	11,467	11,477	11,690	1.9

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