

US Virgin Islands Economic Review

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Economic Review

The pace of economic recovery gathered stride one again in the first quarter of fiscal year 2011, subsequent to a brief break in the fourth quarter of fiscal year 2010. Gain in output and job creation strengthened but remained restrained, reflecting continuing soft demand in the United States, the US Virgin Islands main market.

The recovery, however weak, is encouraging since a critical milestone was passed on the jobs front. Private sector jobs turned around in the fourth quarter of fiscal year 2010 after three years of losses and continued to improve in the first quarter of fiscal year 2011. The number of first quarter private-sector jobs grew 2.1 percent over fiscal year 2010. Finally, more sectors were exhibiting job growth with only trade and the financial activities sectors not participating in the modest recovery.

Marginal job gains in the service-producing sector were led by other services (which include repair and maintenance, personal care, grant-making and giving, and private household services), which increased 13.9 percent; accommodation and food which grew 6.3 percent; leisure and hospitality with job gains of 6 percent; arts and entertainment and professional and business services up 3.6 percent and 3.1 percent, respectively. Goods-producing industries (which include construction and manufacturing) also exhibited year-on-year growth. Construction jobs grew 4.1 percent, but manufacturing jobs were flat in the first quarter.

The other positive indicator that showed the economy was improving was initial unemployment claims gradually declined to 272 in December from 315 in November and

329 in October. The drop in claims signaled that lay-offs were trending downward and the job market was slowly recovering.

Even though the economy is recovering, it is not robust and masks a number of continuing weaknesses. The unemployment rate, for example, remained high linked to the slow growth of demand from consumers and meager business investment. The housing and real estate market continues to be depressed as observed from lower construction spending manifested through the drop in value of residential and commercial building permits. Furthermore, operational issues and financial losses in Hovensa are profoundly affecting jobs in the manufacturing and constructions sectors in particular and the performance of the economy in general.

Although jobs data showed growth last year and private sector hiring was slowly improving, the gains were not sufficient to lower the unemployment rate which hovered around 8 percent last year and averaged 8.3 percent in the first quarter of fiscal year 2011. The slow improvement in jobs means that the unemployment rate will remain close to 8 percent this year.

Furthermore, despite promising signs that have recently emerged, a weak job market, the government's projected \$75.1 million budget deficit in fiscal year 2011 and \$131.5 in fiscal year 2012, operational and financial problems in the refined-petroleum industry and rising energy costs will present tough challenges over the next two years.

So far this fiscal year, general fund tax revenue collections were 35 percent ahead of year-ago levels. Individual income tax collections were 44 percent above last year's

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first quarter collections, gross receipts advanced 9 percent, excise 5 percent, but corporate tax collections were 18 percent lower. Despite the improved collections from October to December 2010, revenues continue to be short of needs and significantly below pre-recession levels.

Government proposed a number of austerity measures to off-set the significant drop in government revenues brought about by the economic downturn, and to address the severity of its budget imbalance. These measures include lay-offs, various tax increases, a freeze on hiring, a two-year freeze on salaries and compensation, deferment of negotiated wage increases, and non-compensation for three legal holidays.

Government cutbacks, accordingly, will likely trickle throughout the economy, thereby offsetting job gains to an extent. However, the prospects for real economic growth should be enhanced as costs are brought under control and revenue-raising measures are implemented.

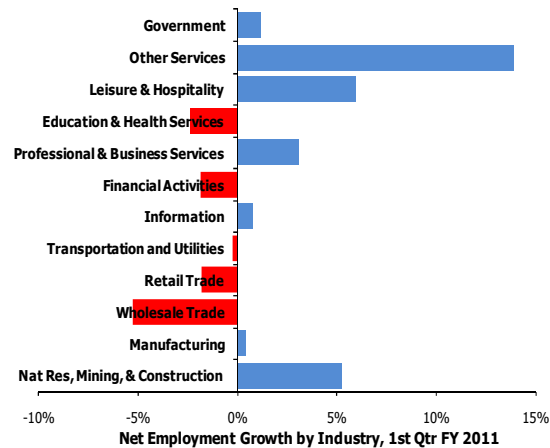
Economic Outlook

Fiscal years 2011 and 2012 will be generally similar to fiscal year 2010 exhibiting improved, but soft job gains and lackluster economic activity. While the recovery is envisaged to continue, growth in the economy will be slow and uneven. Employment is projected to expand, but only sufficient to allow for marginal improvement in the unemployment rate. Therefore, the unemployment rate will still be close to 8 percent in 2011, before giving way to greater improvement in 2012. As such, the outlook calls for continuing economic recovery with modest output and employment expansion.

Major Sector Performance 1st Quarter FY 2011

Small gains carried over in the first quarter to the other services, leisure and hospitality and construction sectors, and expanded to the professional and business services and information sectors which until now were losing jobs. The jobs recovery is depicted in the following chart which shows employment change by industry for the first quarter of fiscal year 2011 compared to the first quarter a year earlier.

Employment is a lagging indicator of economic recovery, meaning that job growth would not manifest until months after recovery began. The most recent jobs report showed that 2011 is generally better than 2010, and even though the recovery is faulty and not fully crystallized, the job gains bolster the claim that economic recovery is on the way.

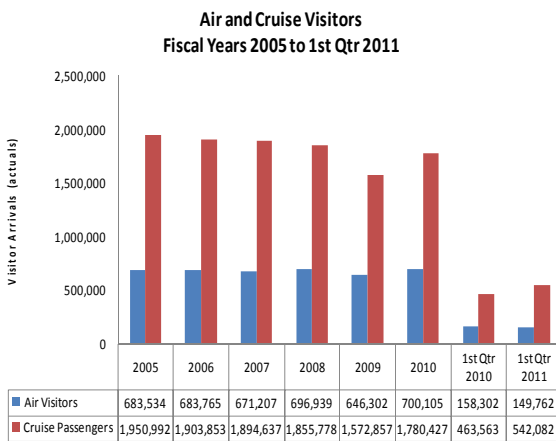


Tourism

Tourism performance has been solid in the past year, but tempered this quarter as reflected in lower air arrivals and hotel stay.

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Even so, total visitor arrivals increased in the first quarter on the strength of cruise passenger visits as shown below.



A total of 691,844 visitors arrived in the first quarter, representing growth of 11.3 percent over the 621,871 visitors recorded for the corresponding period in 2010. There were 542,082 cruise visitors, a solid 16.9 percent increase over last year's first quarter 463,563 arrivals. Air visitor arrivals, on the other hand, continued an undesirable trend observed since September of last year, i.e. consecutive monthly decline in arrivals. The number of visitors by air declined 5.4 percent to 149,762 from 158,302 in the first quarter of fiscal year 2010. This marked the first quarterly decline in a year-and-a-half.

In an effort to boost visitor arrivals in the coming year, the Virgin Islands Tourism Department developed a 2011 marketing plan with emphasis on social media, events marketing, spotlight on the bridal market, and a focus on developing the territory's tourism product. For example, the department employed the use of *Facebook* and *Twitter* to lure new and returning visitors, and to interact directly with travelers. It also initiated a number of promotions such as the *Sizzlin' Sampler* and

Winter Escape which offer free hotel nights and other add-ons to visitors who stay for specific periods.

With these and other efforts afoot, the latest assessment calls for a modest increase this year in overall visitor arrivals. While cruise passengers arrivals will continue to be strong, the pace of growth will likely slip during the months of summer. On the other hand, air arrivals are not expected to enjoy buoyant growth in the second half of this fiscal year.

Leisure and Hospitality

Key hotel performance indicators were negative in the first quarter when compared to a year ago. Occupied room nights declined 5.5 percent to 228,529 from 241,802 occupied room nights in the first quarter of fiscal year 2010.

The Territory's hotel occupancy rate also decreased to 49.5 percent in the first quarter from 53 percent the same quarter a year before. St. Thomas and St. John averaged 51.5 percent, down from 57.1 percent in the first quarter 2010. The rate for St. Croix improved to 43.1 percent from 40.2 percent for the corresponding period in 2010. Hotels collected \$2.1 million in room revenues, a 28.4 percent decrease from \$2.9 million in collections in the first quarter of fiscal year 2010.

The number of jobs in the leisure and hospitality industry averaged 7,234, a 6.0 percent increase from last year's first quarter average of 6,826 jobs. Most of the job increase occurred in restaurants and food establishments which grew 13.8 percent to an average 2,788 jobs, followed by arts and entertainment which held 912 jobs and grew 3.6 percent. The accommodation and food

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subsector which had 6,322 jobs or 87 percent of jobs in the leisure and hospitality sector experienced a 1.1 percent increase in jobs.

Manufacture

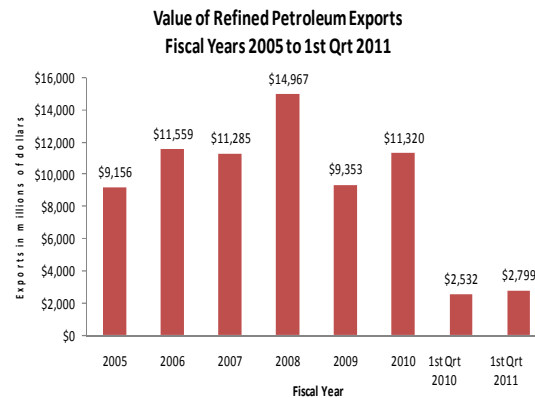
The manufacturing sector has been the powerhouse for economic growth in the past few years as output from this sector has been far greater than in all sectors. This sector's industrial primary products include refined petroleum products, rum, and watches all of which are produced on St. Croix. While added value produced in manufacturing sector as a proportion of gross territorial product (GTP) is about 21 percent, this sector has a large impact on other sectors and on St. Croix's economy particularly.

Oil Industry

Hovensa owns a petroleum refinery located on St. Croix and is the second largest refinery in the United States. The refinery is a joint venture between subsidiaries Hess Corporation and Petr leos de Venezuela, S.A. The refinery, which has a capacity of about 500,000 barrels per day, produces a variety of products and supplies heating oil and gasoline primarily to the US East and Gulf Coast with crude mainly from Venezuela. The refinery is the territory's largest private employer, directly employing 1,400 employees and another 900 employed by contractors.

In 2010, the refinery lowered its production capacity by almost 30 percent, from 525,000 barrels a day to 350,000 barrels per day to improve its financial performance and resolve ongoing emissions and operating issues. Nevertheless, refined petroleum first quarter 2011 exports increased 10.5 percent to \$2.8 million from \$2.5 million in the first

quarter of fiscal year 2010 as shown below. The table also shows annual exports of refined-petroleum products which topped \$15 billion in 2008.



Manufacturing jobs barely improved in the first quarter. The number of jobs averaged 2,116, up a marginal 0.4 percent over the corresponding period last year. The manufacturing sector jobs are expected to decline this year, primarily the result of reduction in Hovensa's workforce as part of the refinery's cost-cutting measures and efforts to improve its financial position.

Rum Industry

Cruzan rum distillery made fewer shipments in the first quarter, 2,574 proof gallons compared to 2,654 proof gallons in the fiscal year 2010—about a 3 percent decline. In the first quarter, the Territory received about \$45 million in excise tax revenues from the cover-over program, or a 38 percent increase from last year's first quarter \$33 million. Under the cover-over program, the Federal government imposes and collects Federal excise taxes on rum produced in the US Virgin Islands and exported to the United States. For each proof gallon of rum produced, the Federal government collects

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\$13.50 in excise taxes, with \$13.25 rebated to the Territory. In fiscal year 2010, the Territory received about \$100 million in excise taxes revenues, \$30.5 million more or an 11 percent increase over fiscal year 2009 rum excise taxes.

The outlook bodes well for the rum industry. The government signed two 30-year agreements, one with Cruzan VIRIL to expand the rum distillery, thereby increasing rum production by 50 percent. A similar agreement was signed with Britain's Diageo PLC, the world's leading spirits, wine and beer company for the construction and operation of a high-capacity distillery on St. Croix. The distillery will begin production in 2011, and by 2012 will supply the rum used to make all Captain Morgan branded products for the United States. Revenues from the sale of Cruzan and Diageo's rum products are projected to generate over \$100 million annual from each distillery.

Watch Industry

Continuing in decline, production and exports in industry were cut by half in fiscal year 2010. The one remaining company shipped 52,035 watches in the first quarter compared to 75,686 watches in the same period in 2010.

Construction

The construction sector is investment-led and, therefore, it is one of the sectors hit hardest by the fall-out in the housing and real estate market. But the pace of construction is slowly improving, though nowhere near the level of activity prior to 2008. The slow economic growth is hindering project starts in all segments of the construction market.

Overall, approved total building permit values were flat in the first quarter as there were \$57.2 million in approved projects, almost the same as the \$57.6 million in the first quarter of fiscal year 2010. Private residential construction values declined 7 percent to \$27.5 million from \$38 million in fiscal year 2010 first quarter. Private non-residential construction values declined 32.7 percent to \$13 million from \$19.6 million in the first quarter fiscal year 2010. Road construction and other infrastructure upgrades led to \$16.5 million of public sector approved permits in the first quarter following two previous quarters of inactivity.

The number of construction jobs continued to improve, averaging 2,034 in the first quarter compared to 1,953 for fiscal year 2010, a 4.1 percent increase.

Trade, Transportation and Utilities

The trade, transportation, and utilities sector is sensitive to consumer spending which helps to explain the continuing weaknesses in this sector. Nonetheless, the sector is improving slowly as consumers are spending a little more and the pace of job losses has eased. It remains though one of the sectors with negative job growth. The number of jobs declined 1.8 percent in the first quarter, with an average of 8,194 jobs compared to 8,345 in the first quarter last fiscal year.

Retail trade jobs, which account for 74 percent of all jobs in this sector and 90 percent of jobs in trade, declined 1.8 percent in the first quarter, with jobs averaging 6,033 compared to 6,145 in the first quarter of fiscal year 2010. Wholesale trade jobs declined 5.2 percent to an average of 651 from 687 last year. Jobs in transportation, warehouse and

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utility were reduced by 1.4 percent to 1,492 from last year's average of 1,514 jobs.

Financial, Insurance and Real Estate

Data on the financial sector and real estate market are released annually and 2010 data will not be available until the middle of this year. The latest available data from 2009 on the financial services and real estate sector showed a drop in activity relative to home sales and real estate development. Relative to home sales, the number of homes sold in the Territory declined 11 percent in 2009 to 298 from 335 in 2008. The average home price declined just 1.4 percent to \$456,295 from \$462,687 in 2008.

While home prices were lower on St. John and St. Croix, 13 percent and 7 percent respectively, St. Thomas experienced an 11 percent increase in the price of homes sold. The average sale price moved up to \$487,930. This compares to an average sale price of \$1,006,144 on St. John and \$356,954 on St. Croix. The market for condominiums also declined. The average \$251,832 sale price of condominiums declined 8 percent Territory-wide while the number sold declined 43 percent to 152 from 266 in 2008.

In 2009 economic activities declined in the banking sector. The combined total assets of commercial banks domiciled in the US Virgin Islands at the end of 2009 declined to \$2,504.4 billion. Total assets fell by just \$145.2 million or a 5.5 percent decline over the previous year's total assets of \$2,649.6 billion.

Total bank deposits—which consist of savings demand accounts, demand deposits and time deposits—decreased by 8.9 percent or by \$207.1 million to \$2,115.5 billion from \$2,322.6 billion in 2008. However, overall

deposits of private individuals, partnerships and corporations increased marginally to \$1,730.4 billion from \$1,688.4 billion in 2008.

The number of jobs in finance, insurance, and real estate declined 1.8 percent in the first quarter 2011 to an average 2,352 from 2,396 in fiscal year 2010.

Professional and Business Services

This sector experienced job losses in the fourth quarter last fiscal year, reversing second and third quarter job growth. Jobs improved in the first quarter of the current fiscal year to 3,441, up 3.1 percent year-on-year from 3,340 jobs in the first quarter of fiscal year 2010.

Labor Force Trends

Civilian employment fell 2.1 percent in the first quarter, for a net loss of 988 jobs. Even though the number of civilian jobs is off from 2008, it is improving gradually each quarter. There were 47,114 persons employed in civilian jobs in the first quarter of fiscal year 2011 compared to 48,101 in fiscal year 2010. There were 20,259 employed on St. Croix and 26,855 on St. Thomas and St. John. Each district experienced a 2.1 percent decline in civilian jobs in the first quarter. In fiscal year 2010, St. Croix had 20,684 employed persons in the first quarter, while St. Thomas and St. Croix had 27,418 employed persons.

Non-Agriculture Wage and Salary Employment

There were 43,923 persons employed in the nonagricultural wage and salary jobs in the first quarter, a 1.7 percent increase over last fiscal year's first quarter of 43,171 job average. The goods-producing sector employment

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increase 2.2 percent with some job growth in both the manufacturing and construction sectors. The service-producing industries had net job growth of 1.7 percent. Even though job growth was soft, it signaled continuing improvement in most sectors.

Public and Private Sector Jobs

The number of private sector jobs increased 2.1 in the first quarter, continuing the

upward trend from the fourth quarter last fiscal year. Private sector jobs averaged 30,898 compared to 30,271 in fiscal year 2010.

Public sector jobs increased an insignificant 1.0 percent. Federal government jobs declined 2.1 percent to an average 962 from 983 in fiscal year 2010. Local government jobs averaged 12,062, up slightly by 1.2 percent from fiscal year 2010 first quarter average of 11,918.

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FISCAL YEAR ECONOMIC INDICATORS

United States Virgin Islands

Fiscal Years 2009-2011

Series	Fiscal Year					
	2009	2010	Percent Annual Change	1st Quarter		Percent Quarterly Change
				2010	2011	
Labor Force	52,891	51,513	-2.6	52,350	51,391	-1.8
Civilian employed	49,242	47,368	-3.8	48,101	47,114	-2.1
Civilian unemployed	3,649	4,145	13.6	4,249	4,278	0.7
Unemployment rate (%)	6.9	8.1	1.1	8.1	8.3	0.2
Total Nonfarm	44,101	43,918	-0.4	43,171	43,923	1.7
Total Private	31,069	30,872	-0.6	30,271	30,898	2.1
Production Sectors	4,416	4,197	-5.0	4,061	4,150	2.2
Natural Resources & Construction	2,183	2,079	-4.8	1,953	2,034	4.1
Manufacturing	2,233	2,117	-5.2	2,108	2,116	0.4
Trade, Transportation & Utilities	8,464	8,258	-2.4	8,345	8,194	-1.8
Wholesale Trade	697	671	-3.7	687	651	-5.2
Retail Trade	6,162	6,072	-1.5	6,145	6,033	-1.8
Transp., Warehousing, Utilities	1,606	1,515	-5.7	1,514	1,510	-0.2
Service Sectors	16,059	16,142	0.5	15,872	16,284	2.6
Information	779	767	-1.6	774	780	0.8
Financial Activities	2,481	2,371	-4.4	2,396	2,352	-1.8
Professional & Business Services	3,351	3,297	-1.6	3,340	3,444	3.1
Education and Health	2,403	2,513	4.6	2,535	2,474	-2.4
Leisure & Hospital	7,044	7,195	2.1	6,826	7,234	6.0
Arts and Entertainment	880	894	1.7	880	912	3.6
Accommodation & Food	6,165	6,300	2.2	5,946	6,322	6.3
Accommodation	3,664	3,582	-2.2	3,496	3,534	1.1
Food Services & Drink	2,501	2,718	8.7	2,450	2,788	13.8
Other Services	2,130	2,193	3.0	1,993	2,270	13.9
Government	13,032	13,047	0.1	12,900	13,024	1.0
Federal	1,000	967	-3.3	983	962	-2.1
Local	12,032	12,080	0.4	11,918	12,062	1.2
General fund revenues (\$1,000)						
Individual	327,955	334,434	2.0	54,886	78,923	43.8
Corporate	50,732	60,999	20.2	8,880	7,289	-17.9
Real Property	26,277	22,050	-16.1	3,831	14,648	282.3
Trade and Excise	21,442	18,976	-11.5	5,353	5,624	5.1
Gross Receipts	126,152	134,523	6.6	27,198	29,549	8.6
Visitor Arrivals						
Air	646,302	699,740	8.3	158,308	149,762	-5.4
Cruise	1,572,857	1,780,427	13.2	463,563	542,082	16.9