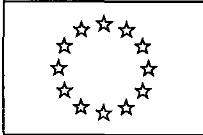

COMMISSION OF THE EUROPEAN COMMUNITIES

Brussels, 15.1.2002
SEC(2002) 40 final

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Recommendation for a

COUNCIL OPINION

in accordance with the third paragraph of Article 5 of Council Regulation (EC) n° 1466/97 of 7 July 1997 on the updated Stability Programme of the Netherlands, 2000-2004

(presented by the Commission)

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EXPLANATORY MEMORANDUM

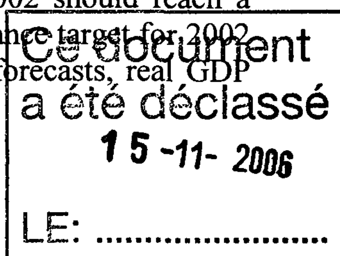
Council Regulation (EC) No. 1466/97, on the strengthening of the surveillance of budgetary positions and the surveillance and co-ordination of economic policies[1], stipulated that countries participating in the single currency were to submit stability programmes to this Council and the Commission by 1 March 1999. In accordance with Article 5 of the Regulation, the Council had to examine each stability programme based on the assessments prepared by the Commission and the Committee set up by Article 114 of the Treaty (the Economic and Financial Committee). The Commission adopted a recommendation on each programme. On the basis of this recommendation and after having consulted the Committee set up by Article 114, the Council delivered an opinion, following its examination of the programme.

The Netherlands's first stability programme covering the period 1999-2002 was submitted on 4 November 1998 and assessed by the Council on 1 December 1998[2].

According to the Regulation, the updated stability programmes, to be presented annually, may be examined by the Council in accordance with these same procedures.

The Netherlands submitted its updated stability programme, covering the period 2000-2004, on 17 October 2001. The Commission services have carried out a technical evaluation of this updated programme, which warrants the following assessment.

> The 2001 update of the stability programme of the Netherlands, which covers the period 2000-2004 was presented on 17 October 2001. Prepared during the Summer in parallel with the draft budget for 2002, which was tabled to Parliament on 18 September, the update relied on macroeconomic assumptions which rapidly emerged as outdated.
>
> The Netherlands Bureau for Economic Policy Analysis revised twice its macroeconomic projections for 2001 and 2002: a first time, on 1 November, in order to take into account the estimated effects of the 11 September events and, on 8 December, within the framework of its regular Winter revision. The real GDP growth projections for 2001 and 2002 were substantially downward revised from 2% in both years to 1% in 2001 and 1 ¼% in 2002.
>
> However, the Ministry of Finance did not genuinely revise its own projections for the general government balance in 2001 and 2002: for 2001, the government surplus, previously estimated at 1% of GDP, was reduced to 0.7% of GDP mainly in order to take into account a transaction amounting to 0.3% of GDP; for 2002, the government decided not to revise its budgetary forecasts at all. In a letter of the Minister of Finance to the Commission on 6 December 2001, the latest CPB projections are conveyed; however, it is mentioned that the projection of the CPB related to the general government surplus in 2002, at 0.4% of GDP, is not endorsed by the Ministry of Finance; it only considers this forecast as a useful point of reference and that eventually the forthcoming Ministry of Finance estimate for 2002 should reach a comparable level. Thus, at this stage, the precise government balance target for 2002 is unknown. It is to be noted that in the Commission Autumn forecasts, real GDP



[1] OJ L 209, 2.8.1997
[2] OJ C 3, 6.1.1999

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growth is expected to reach 1.5% in 2001 and 2002, and the government surplus 1.3% of GDP in 2001 and 0.5% of GDP in 2002.

For the years 2003 and 2004, which fall beyond the term of the present government - a general election will take place in May 2002 – the estimates are a technical trend-based cautious scenario under the assumption of unchanged policies from 2002. They are primarily meant to determine the additional margin which will be available for debt reduction or tax alleviation. The letter of the Minister of Finance includes medium-term projections of the CPB – issued in November 2001, previous the latest revision concerning the years 2001 and 2002 – which differ from the medium term forecast included in the regular 2001 update.

Under these circumstances, the assessment of the 2001 update is particularly uneasy, blurred by the uncertainty surrounding the projection for the general government balance in 2002 and the inconsistency of the different series provided.

In 2001, while economic activity decelerated sharply, real GDP growth slowing down from 3.5% in 2000 to 1% in 2001 (latest CPB projection), the deterioration in the general government balance, although significant, was less dramatic, the surplus falling from 1.5% of GDP to 0.7% of GDP, close to the estimates of the 2000 update. In fact, buoyant tax revenues induced by the increase in indirect taxation and fast progress in disposable income, cushioned the impact of the cuts in income tax decided in the fiscal reform and that of the deceleration in activity. The government debt ratio to GDP continued to decrease rather rapidly mainly due to developments in nominal GDP and interest rates.

As far as 2002 is concerned, clearly the government is not willing to modify the budget at such an early stage despite the changes in the macroeconomic projections. In the 2002 budget, the government did not strictly apply the fifty-fifty formula for revenue allocation to debt reduction or tax alleviation; only about one third of the estimated additional revenues in 2002 will be allocated to tax cuts. With this decision the government, in compliance with the Council recommendation of March 2001 as well as with the Broad economic policy guidelines, had in view to counter inflationary risks, strengthen the budgetary balance and better prepare for the consequences of the ageing population. At the same time, the government expenditure was constrained by the ceiling in real terms, which is agreed to reach 1 ½% per year for total expenditure and be lifted to 3.5% for expenditure in health care, education and safety. Under more severe macroeconomic conditions than assumed in the budget, the government is likely prone to let the automatic stabilisers play fully in the course of 2002; due to the existing comfortable situation of the Dutch public finance, a significant safety margin exists not to trespass the 3% deficit threshold. As the general government financial position is expected to be in surplus throughout the period covered, the different budgetary projections presented comply with the requirements of the Stability and Growth Pact.

For the years 2003 and 2004, the regular 2001 update provided a trend based cautious scenario, real GDP growth being expected to reach 2 ¼% in yearly average and the general government surplus 1% of GDP in both years; under these assumptions the available margins for discretionary policy were expected to reach 0.2% of GDP in 2003 and 0.3% of GDP in 2004. These figures have not been revised by the Ministry of Finance; however, in the medium-term CPB projections, provided for information, the trend based real GDP growth in 2003 and 2004 has been slightly

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revised upwards to 2 ½% in both years, while the general government balance is corrected downward to 0.2% of GDP in 2003 and 0.5% of GDP in 2004, implying a significant reduction in the available margins in both years.

The Netherlands seems to be in a good position to meet the budgetary consequences of the ageing population and the budgetary strategy outlined in the programme is compatible with improving the sustainability of public finances. However, in the short-term, delays in the public debt reduction, resulting from unfavourable economic developments, cannot be ruled out.

Structural reforms are underway aiming at improving the efficiency of government expenditure, in particular in health care, education and social infrastructure, as well as increasing the participation rate and competitiveness.

Based on this assessment, the Commission has adopted the attached recommendation for a Council opinion on the Stability Programme update of the Netherlands and is forwarding it to the Council.

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Recommendation for a

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in accordance with the third paragraph of Article 5 of Council Regulation (EC) n° 1466/97 of 7 July 1997 on the updated Stability Programme of the Netherlands, 2000-2004

THE COUNCIL OF THE EUROPEAN UNION,

Having regard to the Treaty establishing the European Community,

Having regard to Council Regulation (EC) No 1466/97 of 7 July 1997 on the strengthening of the surveillance of budgetary positions and the surveillance and co-ordination of economic policies[3], and in particular Article 5(3) thereof,

Having regard to the recommendation of the Commission,

After consulting the Economic and Financial Committee,

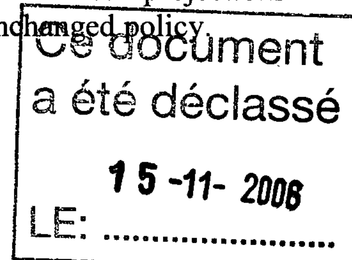
HAS DELIVERED THIS OPINION:

On [22 January 2002], the Council examined the updated Stability Programme of the Netherlands, which covers the period 2000-2004.

Real GDP growth decelerated sharply in 2001 to about 1% from 3.5% in 2000; the deterioration in the general government balance, although significant, but partly due to the implementation of the tax reform as from 1 January 2001, was less dramatic, the surplus falling from 1.5% to an estimated 0.7% of GDP; the government debt ratio continued to decrease mainly due to developments in nominal GDP and interest rates.

The Council notes that, since the presentation of the 2001 updated stability programme, the macroeconomic projections for 2001 and 2002 have been significantly revised downwards by the Netherlands Bureau for Economic Policy Analysis, in order to take into account the full impact of the international economic downturn and the estimated effects of the 11 September events; the Dutch authorities, while acknowledging the economic slowdown and its impact on budgetary conditions, have not revised the 2001 update, as the Council would have preferred. Such a revision would have allowed, i. a., a clearer understanding of the budgetary policy for 2002.

The Council notes that for 2003 and 2004, which are beyond the term of office of the present government, the budgetary estimates in the updated programme are technical projections based on a cautious macroeconomic scenario under the assumption of unchanged policy.



[3] OJ L 209, 2.8.1997

The Council notes that despite the economic slowdown, a general government surplus is projected to be maintained throughout the period of the programme in full compliance with the Stability and Growth Pact objective of a fiscal position close to balance or in surplus; the Council considers that the progress already made by the Netherlands in improving the general government budgetary position provides adequate margin in order to cope with the budgetary impact of normal macroeconomic fluctuations without breaching the 3% of GDP deficit threshold.

The Council notes the non-application in the 2002 budget of the fifty-fifty rule of allocation of additional revenues to debt reduction and tax alleviation; it acknowledges that the modification of the rule was implemented in view to comply with the Council recommendation of March 2001 as well as with the Broad economic policy guidelines, but also in view to strengthen the budgetary position and better prepare for the consequences of the ageing population. The Council notes that the implementation of overall expenditure targets made possible increased government spending in priority areas and reduction in the tax burden, while respecting the requirements of the stability and growth pact. The Council welcomes the structural reforms underway, which aim at improving the efficiency of government expenditure in particular in health care, education and social infrastructure, as well as increasing the participation rate and competitiveness.

The Council notes that the programme outlines a comprehensive strategy for improving the sustainability of public finances and meeting the consequences of population ageing which seems adequate; it encourages the government to maintain the effort towards reducing the debt ratio and improving labour supply and employment rate in order to achieve these objectives.

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