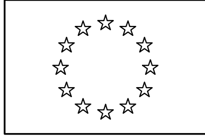

COMMISSION OF THE EUROPEAN COMMUNITIES

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COMMISSION OPINION

on the existence of an excessive deficit in the Netherlands – Application of Article 104(5) of the Treaty establishing the European Community

EXPLANATORY MEMORANDUM

On 7 April 2004, the Commission published its Spring 2004 forecasts.[1] According to these forecasts, which took into consideration data reported by the Dutch Authorities on 31 March 2004, the general government deficit in 2003 reached 3.2% of GDP in 2003, thus exceeding the 3% of GDP Treaty reference value, and increased substantially relative to the 2002 deficit (1.9% of GDP). Based on this prima facie evidence, the Commission initiated the Excessive Deficit Procedure for the Netherlands on 28 April 2004, with the adoption of the report as foreseen in Article 104(3) of the Treaty.[2]

The application of the excessive deficit procedure (EDP) is governed by Article 104 of the Treaty and by Council Regulation (EC) No 1467/97 "on speeding up and clarifying the implementation of the excessive deficit procedure", which is part of the Stability and Growth Pact.[3]

The Commission report according to Article 104(3) of the Treaty concluded that the excess of the 3.2% of GDP deficit in 2003 over the 3% of GDP Treaty reference value did not result, in the sense of the Stability and Growth Pact, from an unusual event outside the control of the Dutch authorities, nor was it the result of a severe economic downturn, which is defined in the Pact as an annual fall of real GDP of at least 2%. However, it occurred in a context of strongly negative growth, with real GDP growth at -0.7% in 2003, and a negative output gap of around 2% of GDP emerging. This largely explains the deterioration in the general government balance, which was further aggravated by a greater-than-expected weakening in receipts and higher-than-expected local government deficits while expenditure targets were largely met. Concerning developments in 2004, the Commission Spring forecast projects a general government deficit of 3.5% of GDP. After the publication of the Commission Spring forecast, the government adopted additional savings measures on 16 April 2004, equivalent to 0.6 % of GDP, with the objective of reducing the deficit to below 3% of GDP again in 2004, in line with the achievement in earlier years. According to the Commission report the achievement of this objective depends on the measures yielding the expected results and on not having second-round effects on economic activity and the budgetary outcome. Hence, there is a likelihood that the deficit could remain at or just above the 3% of GDP reference value in 2004.

The Commission report, based on the Commission Spring forecasts, also concluded that the debt-to-GDP ratio reached 54.8% of GDP in 2003, below the 60% reference value of the Treaty. Moreover, it noted that the Commission projects the debt ratio to reach 56.3 % of GDP in 2004, which is above the 54.5 % of GDP projected by the Dutch authorities in the 2003 stability programme update but below the reference value of 60% of GDP.

Article 104(4) of the Treaty states that "the Committee provided for in Article 114 (i.e. the Economic and Financial Committee) shall formulate an opinion on the report of the Commission". The Committee issued its opinion on 12 May 2004, subscribing to the assessment made by the Commission in its report. In particular, the EFC concluded that in

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[1] The Commission Spring 2004 forecast is available at the following website: http://europa.eu.int/comm/economy_finance/publications/european_economy/2004/ee204en.pdf.

[2] The full text of this report is available at the following website: http://europa.eu.int/comm/economy_finance/about/activities/sgp/country/edp/edprep2004_nl.pdf.

[3] OJ L 209, 2.8.1997.

2003 the Netherlands did not comply with budgetary discipline regarding the deficit as defined in Article 104 of the Treaty, which suggests that an excessive deficit exists in the Netherlands.

The EFC also considered that there is a likelihood that the general government deficit may remain at or just above the Treaty's reference value again in 2004, despite additional measures decided by the Dutch authorities, while the general government gross debt ratio would remain below the Treaty's reference value of 60 % of GDP in 2004.

The Commission, having examined all the relevant factors taken into account in its report and having regard to the opinion of the EFC, is of the opinion that an excessive deficit exists in the Netherlands. This opinion, adopted by the Commission on 19 May 2004, is herewith addressed to the Council, according to Article 104(5) of the Treaty. The Commission recommends that the Council shall decide accordingly, in conformity with Article 104(6). In addition, the Commission is submitting to the Council a recommendation for a Council recommendation to be addressed to the Netherlands with a view to bringing the situation of an excessive deficit to an end, according to Article 104(7) of the Treaty.

COMMISSION OPINION

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GENERAL CONSIDERATIONS

According to Article 104 of the Treaty, Member States have to avoid excessive government deficits. Decisions on the existence of an excessive deficit are governed by the excessive deficit procedure (EDP) specified by Article 104 of the Treaty and Council Regulation (EC) No 1467/97 "on speeding up and clarifying the implementation of the excessive deficit procedure", which is part of the Stability and Growth Pact.

Article 104(2) of the Treaty requires the Commission to monitor the development of the budgetary situation and of the stock of government debt in the Member States with a view to identifying gross errors. In particular, the Commission has to examine compliance with budgetary discipline on the basis of two criteria, one for the ratio of the planned or actual government deficit to gross domestic product (GDP) and one for the ratio of government debt to GDP. The statistical data on these variables are provided by the Commission on the basis of reporting by the Member States.[4]

Article 104(3) of the Treaty requires the Commission to prepare a report if the requirements under one or both of the criteria of Article 104(2) are not fulfilled or if, notwithstanding the fulfilment of the requirements under the criteria, the Commission is of the opinion that there is a risk of an excessive deficit in a Member State. The Commission report also takes into account whether the government deficit exceeds government investment expenditure and all other relevant factors, including the medium-term economic and budgetary position of the Member State, as required by Article 104(3) of the Treaty. Based on data for the year 2003 reported by the Dutch authorities, which were incorporated in the Commission's Spring 2004 forecast, the Commission has adopted such a report for the Netherlands on 28 April 2004.

Subsequently, and in accordance with Article 104(4), the Economic and Financial Committee has formulated an opinion on the report of the Commission on 12 May 2004.

Article 104(5) of the Treaty requires the Commission to address an opinion to the Council if the Commission considers that an excessive deficit in a Member State exists or may occur. In order to reach a conclusion on whether an excessive deficit exists or may occur, the Commission considers that account should be taken of: (i) the conclusions of its own report, namely whether the requirements under one or both of the criteria of Article 104(2) of the Treaty are not fulfilled, and the relevance of all other factors mentioned in Article 104(3) and (ii) the opinion of the Economic and Financial Committee on the report of the Commission. On the basis of these elements, the Commission has established a number of considerations for the Netherlands.

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[4] Government account data are to be reported before 1 March and 1 September, in accordance with Council Regulation (EC) No 3605/93 amended by Council Regulation (EC) No 475/2000 and by Commission Regulation (EC) No 351/2002.

CONSIDERATIONS CONCERNING THE NETHERLANDS

1. The actual general government deficit amounted to 3.2 % of GDP in 2003 therefore exceeding the 3% of GDP reference value of the Treaty, while it increased substantially relative to the 2002 deficit (1.9% of GDP).

2. The excess of the deficit over the 3% of GDP reference value in 2003 does not result, in the sense of the Stability and Growth Pact, from an unusual event outside the control of the Dutch authorities, nor does it result from a severe economic downturn, which is defined in the Pact as a fall in annual real GDP of at least 2%. However, it occurred in a context of strongly negative growth, with real GDP growth at -0.7% in 2003 and with a negative output gap of around 2% of GDP emerging. This largely explains the deterioration in the general government balance, which was further aggravated by a greater-than-expected weakening in receipts and higher-than-expected local government deficits, while expenditure targets were largely met.

3. The level reached by the general government deficit in 2003 is 2.7 percentage point of GDP above the value planned in September 2002 when the budget for 2003 was adopted. The rise in the deficit (from 1.9% of GDP in 2002 to 3.2% of GDP in 2003) occurred despite substantial savings measures of around 1.2 percentage point of GDP, which allowed an improvement in the cyclically adjusted balance by 0.6 percentage point compared to 2002. This suggests that the fiscal stance was tightened appreciably in 2003.

4. The breach of the 3% of GDP reference value for the deficit in 2003 finds its origin in the prolonged economic downturn, that started in 2001, coupled with the fact that the Dutch government finances were in a more vulnerable position ahead of the slowdown than commonly appreciated at the time. Following the deterioration of the cyclically adjusted deficit in 2001 and 2002, the fiscal stance was tightened in 2003. However, due to the marked deceleration in economic activity, this did not prevent the nominal deficit from increasing sharply.

5. Gross fixed government investment as a share of GDP was 3.2% of GDP in 2002 and3.5% of GDP in 2003, compared to a general government deficit of 3.2% of GDP. Thus, it is worth noting that the general government investment to GDP ratio did not fall during the downturn and that it has remained higher than the headline deficit to GDP ratio until 2003.

6. In its Spring 2004 forecasts, based on the assumption of no-policy change, the Commission projects the general government deficit in the Netherlands to reach 3.5% of GDP in 2004. The Commission forecast did not incorporate the additional savings measures, amounting to 0.6% of GDP, decided upon by the Dutch government on 16 April 2004 with a view to bringing the deficit below 3% of GDP, in line with the achievement in earlier years. According to the Commission report the achievement of this objective depends on the measures yielding the expected results and on not having second-round effects on economic activity and the budgetary outcome. Hence, there is a likelihood that the deficit may remain at or just above the 3% of GDP Treaty reference value again in 2004.

7. The gross government debt to GDP ratio reached 52.6% of GDP in 2002 and amounted to 54.8% in 2003 but remained below 60%. In its Spring 2004 forecasts, the Commission projects gross government debt in the Netherlands to reach 56.3% of GDP in 2004. Hence, even under the no policy change assumption the 60% Treaty reference value would not be breached in that year.

CONCLUSION

The monitoring of the budgetary situation in the Netherlands and, in particular, the examination of compliance with the criteria laid down in Article 104(2) have led the Commission to prepare a report in accordance with Article 104(3) of the Treaty. The Commission, having examined the relevant factors taken into account in this report and having regard to the opinion of the Economic and Financial Committee, is of the opinion that an excessive deficit exists in the Netherlands.