COMMISSION OF THE EUROPEAN COMMUNITIES

Brussels, 19.5.2004
SEC(2004) 626 final

Recommendation for a

COUNCIL RECOMMENDATION TO THE NETHERLANDS

with a view to bringing an end to the situation of an excessive government deficit

(presented by the Commission)

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, has been addressed to the Council, according to Article 104(5) of the Treaty. The Commission has recommended that the Council shall decide accordingly, in conformity with Article 104(6). In addition, the Commission is herewith 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.

Recommendation for a

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THE COUNCIL OF THE EUROPEAN UNION,

Having regard to the Treaty establishing the European Community, and in particular Article 104(7) thereof;

Having regard to the recommendation from the Commission;

Whereas:

(1) According to Article 104 of the Treaty, Member States are to avoid excessive government deficits.

(2) The Stability and Growth Pact is based on the objective of sound government finances as a means of strengthening the conditions for price stability and for strong sustainable growth conducive to employment creation.

(3) The Amsterdam Resolution of the European Council on the Stability and Growth Pact of 17 June 1997 solemnly invites all parties, namely the Member States, the Council and the Commission to implement the Treaty and the Stability and Growth Pact in a strict and timely manner.

(4) The Council has decided on 2 June 2004, in accordance with Article 104(6), that an excessive deficit exists in the Netherlands.

(5) Having decided on the existence of an excessive deficit in the Netherlands, the Council, in accordance with Article 104(7) of the Treaty and Article 3 of Council Regulation (EC) No 1467/97, is required to make at the same time recommendations to the Member State concerned with a view to bringing that situation to an end within a given period. The Council recommendation has to a establish a deadline of four months at the most for effective action to be taken by the Netherlands to correct the excessive deficit as well as a deadline for the correction of the excessive deficit, which should be completed in the year following its identification unless there are special circumstances.

(6) In the view of the Council, budgetary consolidation measures should secure a lasting improvement in the general government balance, while being geared towards enhancing the quality of the public finances and reinforcing the growth potential of the economy. The overall fiscal strategy of the Dutch authorities appears to conform with this orientation.

(7) When defining the recommendations to correct the excessive deficit, the following factors should be taken into account: (i) the worsening in cyclical developments which contributed to the deterioration of the budgetary situation in 2003 was abrupt and unexpected and it made the effort to bring the deficit below 3% of GDP larger than expected in the 2003 budget and 2002 stability programme update; (ii) according to the Commission, in 2003 the cumulated shortfall of real GDP below estimated potential amounted to 1.7% of GDP; (iii) the Commission, in its Spring 2004 forecast of 7 April 2004, projects that the general government deficit will be 3.5% of GDP in 2004 and 3.3% of GDP in 2005, assuming there to be no policy changes while real GDP growth would reach 1.0% in 2004 and 1.6% in 2005; (iv) the additional savings measures for 2004 that the government promptly adopted on 16 April 2004 are equivalent to around 0.6 percentage point of GDP and were not taken into account in the Commission Spring 2004 forecast and (v) the Dutch government announced its intention to implement in 2005 additional measures with the aim of ensuring a general government deficit below 3% of GDP, which have not yet been specified.

(8) If the macro-economic outturn is in line with the Commission Spring 2004 forecast and the measures decided upon on 16 April 2004 yield the planned amount, corrective measures of a mainly structural nature in 2005 amounting to half a percentage of GDP would lead to a deficit below the 3% of GDP Treaty reference value from that year onwards.

HEREBY RECOMMENDS

The Dutch authorities should put an end to the present excessive deficit situation in accordance with Article 3(4) of Council Regulation (EC) No 1467/97. The Council establishes the deadline of 2 October 2004 for the Dutch government to take action regarding corrective measures in 2005, mainly of a structural nature, amounting to half a percentage point of GDP.

In addition, the Council urges the Dutch authorities to ensure that budgetary consolidation towards a position close to balance or in surplus is sustained after the excessive deficit has been corrected in particular through a reduction in the cyclically-adjusted deficit by at least 0.5 percentage point of GDP per year.

This recommendation is addressed to the Kingdom of the Netherlands.

Done at Brussels, 2 June 2004

For the Council
The President
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