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COMMISSION STAFF WORKING DOCUMENT

Analysis of the Draft Budgetary Plan of the NETHERLANDS

Accompanying the document

COMMISSION OPINION

on the Draft Budgetary Plan of the NETHERLANDS

{C(2013) 8008 final}

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1. INTRODUCTION

The Netherlands has submitted is Draft Budgetary Plan for 2014 on 30 September 2013 in compliance with Regulation (EU) No 473/2013 of the Two-Pack together with a report on effective action and an Economic Partnership Programme as recommended by the Council in June 2013.

The Netherlands is currently subject to the corrective arm of the Pact. The Council opened the Excessive Deficit Procedure for the Netherlands on 2 December 2009 and recommended to correct the excessive deficit by 2013. On 21 June 2013, the Council concluded that the Netherlands had taken effective action but adverse economic events with major implications on public finances had occurred, and issued revised recommendations. The Netherlands was given a deadline of 1 October 2013 to take effective action to ensure a sustainable correction of the excessive deficit by 2014.

Section 2 of this document presents the macroeconomic outlook underlying the Draft Budgetary Plan and provides an analysis based on the Commission Forecast. The following section presents the recent and planned fiscal developments, according to the Draft Budgetary Plans, including an analysis of risks to their achievement based on Commission Forecast. In particular, it also includes an analysis of the measures underpinning the Draft Budgetary Plan. Section 4 discusses the recent and planned fiscal developments in 2013-2014 (also taking into account the risks to their achievement) against the obligations stemming from the Stability and Growth Pact. Section 5 provides an analysis of the fiscal structural reforms presented in the Economic Partnership Programme, as requested in the latest Council recommendations. Section 6 summarises the main conclusions of the present document.

2. MACROECONOMIC DEVELOPMENTS UNDERLYING THE DRAFT BUDGETARY PLAN

Before submission to the European Commission, the 2014 budget was presented to Parliament on 17 September 2013. As every year, it was accompanied by a fresh CPB Netherlands Bureau of Economic Policy (CPB) forecast, covering 2013 and 2014 (see Box 1). Budget projections are based on this independent CPB forecast. After shrinking 1¼% in 2013, real GDP is expected to expand by ½% in 2014 in this scenario, even though household consumption would continue to shrink (by 1%). Household consumption is expected to be dragged down by deleveraging, real wage decreases, rising unemployment and wealth effects from housing and pension assets.

Box 1: The macro economic forecast underpinning the budget in the Netherlands

Every draft budget is accompanied by a fresh forecast of the CPB Netherlands Bureau for Economic Policy Analysis (CPB). The government traditionally uses the CPB's forecast to present the budgetary and economic effects of the planned measures. This tradition will be formalised in the law transposing the TSCG into national legislation. Although the CPB is administratively part of and mainly financed by the Ministry of Economic Affairs, it is independent as far as the contents of its works are concerned. Since its foundation in 1945, it is has built up a strong reputation as regards independence and quality.

Exports, government spending and investments are expected to experience positive growth rates. As it was the case in the last years, re-exports will grow faster than domestically produced exports, strengthening the position of the Netherlands as a trading nation. Due to a stronger demand for goods and services from the main trading partners and somewhat weak internal demand, the current account surplus is expected to increase to some 10% of GDP in 2014, with the rise mainly due to cyclical conditions.

As most firms had increased their prices after the VAT increase of October 2012, its inflationary effect is expected to phase out. Having reached 2¾% in 2013, CPI inflation is thus forecast to fall back to 2% in 2014.

After years of decreasing consumption and weak internal demand, firms have been shedding workers they previously hoarded. Hence, the average unemployment rate in 2013 is expected to be 7% while reaching 7½% at the end of the year. It is expected to stabilise at that level in 2014. This is a sizeable increase from the unemployment rate of 5.3% registered in 2012.

Compared to the 2013 Commission Autumn Forecast (Table 1), projected economic growth in the Draft Budgetary Plan is slightly lower in 2013 and slightly higher in 2014. This also influences the general government budget balance and explains parts of the difference between the Draft Budgetary Plan and the Commission Forecast in this respect. The developments of the components of GDP are quite similar in the Draft Budgetary Plan and the Commission Autumn forecast, with a few exceptions. Figures for government consumption differ also in view of the most recent amendments to the consolidation package[1] and the expected increase in economic growth in 2014 in the Draft Budgetary Plan stems more heavily from investments and less from net exports in the Commission forecast compared to the Draft Budgetary Plan. Both forecasts share a very similar view on price developments and the current account. Regarding the labour market, the Commission forecast is slightly more pessimistic. This difference also stems from the fact that in the final budget plan the government plans to effectively shift some educational expenditure from 2014 into 2013.

The macroeconomic scenario used for the Draft Budgetary Plan and the Autumn Forecast share similar risks, which are mainly on the downside. Recent short-term indicators give some early indication of an improvement in economic activity as also embedded in the baseline projections of both forecasts. If these indications turn out to be illusive, a more negative development could result.

[1] The macroscenario of the Draft Budgetary Plan is the one provided by CPB and includes only the first version of the consolidation package presented with the initial budget proposal in September 2013. The Commission forecast includes the amended version the government agreed upon with three opposition parties in the October 2013 budget agreement.

Table 1. Comparison of macroeconomic developments and forecasts

	2012	2013			2014		
	COM	SP	DBP	COM	SP	DBP	COM
Real GDP (% change)	-1.2	-0.4	-1¼	-1.0	1.1	½	0.2
Private consumption (% change)	-1.6	-1.6	-2.1	-2.1	0.3	-1.0	-1.1
Gross fixed capital formation (% change)	-4.0	-2.1	-8.9	-8.5	2.3	1.8	0.9
Exports of goods and services (% change)	3.2	2.8	2.7	2.8	4.2	3.3	3.2
Imports of goods and services (% change)	3.3	2.0	0.0	0.1	4.2	3.7	2.7
Contributions to real GDP growth:							
- Final domestic demand	-1.7	-1.1	-2.7	-2.6	0.6	0.0	-0.4
- Change in inventories	0.2	-0.2	-0.8	-0.8	0.1	0.5	-0.1
- Net exports	0.2	0.9	2.4	2.4	0.4	0.1	0.7
Output gap[1]	-2.4	-3.3	-4.1	-3.4	-2.5	-3.7	-3.2
Employment (% change)	-0.2	-0.4	-1.0	-0.8	0.1	-0.2	-0.6
Unemployment rate (%)	5.3	6.3	6.9	7.0	6.4	7.6	8.0
Labour productivity (% change)	-1.0	0.0	-0.2	0.2	0.9	0.8	0.7
HICP inflation (%)	2.8	2.8	2.9	2.7	1.7	1.8	1.7
GDP deflator (% change)	1.3	1.6	1.5	1.6	1.6	1.4	1.4
Comp. of employees (per head, % change)	1.9	2.2	1.5	-0.1	2.7	3.0	1.7
Net lending/borrowing vis-à-vis the rest of the world (% of GDP)	7.4	8.8	10.0	9.3	9.0	10.2	9.2

Note:

[1]In percent of potential GDP, with potential GDP growth recalculated by Commission services on the basis of the programme scenario using the commonly agreed methodology.

Source :

Stability programme (SP); Draft Budgetary Plan (DBP); Commission services' 2013 Autumn Forecast (COM); Commission services' calculations.

3. RECENT AND PLANNED FISCAL DEVELOPMENTS

3.1. Deficit developments

For 2013, the headline deficit forecast for 2013 is virtually the same in the macroeconomic scenario underlying the Draft Budgetary Plan and the Commission 2013 Autumn forecast (Table 2) and below the target set in the EDP recommendation. The headline deficit of the general government is expected to drop to 3.3% of GDP in 2013. The 2013 update of the Stability Programme expected a slightly higher deficit. Since the spring, economic developments have been worse than expected, implying shortfalls on the revenue side. However, on the basis of quarterly data published by Statistics Netherlands (CBS), the forecast 2013 general government deficit is lower than in the spring, because it does not include a sizeable deficit impact for the nationalisation of SNS Reaal. The CBS and Eurostat are currently discussing the statistical recording of this transaction. Overall, the differences in expected revenues and expenditure are marginal between the Draft Budgetary Plan and the Commission forecast.

For 2014, the Commission forecast and the Draft Budgetary Plan both expect the headline deficit to be higher than foreseen in the Stability Programme, mainly due to economic activity being weaker than previously expected. The higher-than-expected deficit reflects the particular composition of growth, with some tax-rich components such as private consumption turning out to be particularly anaemic.

Table 2. Composition of the budgetary adjustment

(% of GDP)	2012	2013			2014			Change: 2012-2014
	COM	SP	DBP	COM	SP	DBP	COM	DBP
Revenue	**46.4**	**46.7**	***47.1***	**46.9**	**47.0**	***47.6***	**47.6**	**1.2**
of which:								
- Taxes on production and imports	11.4	12.0	*11.9*	11.8	12.2	*12.1*	12.1	0.7
- Current taxes on income, wealth, etc.	10.9	11.1	*11.1*	11.0	10.8	*11.2*	11.2	0.3
- Capital taxes	0.2	0.2	*0.2*	0.2	0.2	*0.2*	0.2	0.0
- Social contributions	16.6	16.8	*16.7*	16.7	17.0	*17.3*	17.3	0.7
- Other (residual)	7.2	6.6	*7.2*	7.2	6.8	*6.8*	6.8	-0.4
Expenditure	**50.5**	**49.9**	**50.2**	**50.2**	**50.4**	**51.0**	**51.0**	**0.5**
of which:								
- Primary expenditure	48.6	48.0	48.4	48.3	48.6	49.2	49.1	0.6
of which:								
Compensation of employees	9.8	9.7	9.6	9.6	9.5	9.4	9.4	-0.4
Intermediate consumption	7.6	7.6	7.3	7.4	7.4	7.2	6.8	-0.4
Social payments	24.0	23.8	24.8	24.7	24.0	25.1	25.1	1.1
Subsidies	1.3	1.2	1.3	1.3	1.1	1.2	1.2	-0.1
Gross fixed capital formation	3.3	3.1	3.3	3.3	3.2	3.3	3.3	0.0
Other (residual)	2.5	2.6	2.1	2.1	3.4	3.0	3.2	0.5
- Interest expenditure	1.9	1.9	1.8	1.9	1.8	1.8	1.9	-0.1
General government balance (GGB)	**-4.1**	**-3.4**	**-3.2**	**-3.3**	**-3.0**	**-3.3**	**-3.3**	**0.8**
Primary balance	**-2.2**	**-1.3**	**-1.3**	**-1.4**	**-1.6**	**-1.5**	**-1.5**	**0.7**
One-off and other temporary measures	0.0	0.0	0.5	0.6	0.0	0.0	0.2	0.0
GGB excl. one-offs	**-4.1**	**-3.4**	**-3.7**	**-4.0**	**-3.0**	**-3.3**	**-3.5**	**0.8**
Output gap[1]	-2.4	-3.3	-4.1	-3.4	-2.5	-3.7	-3.2	-1.3
Cyclically-adjusted balance[1]	-2.7	-1.5	-0.9	-1.5	-1.6	-1.2	-1.5	1.5
Structural balance (SB)[2]	**-2.7**	**-1.5**	**-1.4**	**-2.1**	**-1.6**	**-1.2**	**-1.7**	**1.5**
Change in SB	*1.1*	*0.9*	*1.4*	*0.6*	*-0.1*	*0.2*	*0.4*	-
Two year average change in SB	*0.7*	*1.1*	*1.2*	*0.9*	*0.4*	*0.8*	*0.5*	-
Structural primary balance[2]	-0.8	0.4	0.4	-0.2	0.2	0.6	0.2	1.4
Change in structural primary balance		*1.0*	*1.3*	*0.6*	*-0.2*	*0.2*	*0.3*	-
Expenditure benchmark								
Applicable reference rate[3]	0.39	0.4	0.4	0.4	-0.14	-0.14	-0.14	-
Deviation[4] (% GDP)	-0.7	-4.9	n.a.	-2.9	-2.2	n.a.	-0.2	-
Two-year average deviation (% GDP)	-0.9	-5.0	n.a.	-1.8	-3.5	n.a.	-1.5	-

Notes:

[1]Output gap (in % of potential GDP) and cyclically-adjusted balance according to the programme as recalculated by Commission services on the basis of the programme scenario using the commonly agreed methodology.

[2]Structural (primary) balance = cyclically-adjusted (primary) balance excluding one-off and other temporary measures.

[3] Reference medium-term rate of potential GDP growth. The (standard) reference rate applies from year t+1, if the country has reached its MTO in year t. A lower rate applies as long as the country is adjusting towards its MTO, including in year t.The reference rates applicable to 2014 onwards have been updated in 2013.

[4] Deviation of the growth rate of public expenditure net of discretionary revenue measures and revenue increases mandated by law from the applicable reference rate. The expenditure aggregate used for the expenditure benchmark is obtained following the commonly agreed methodology. A positive sign implies that expenditure growth exceeds the applicable reference rate.

Source:

Stability programme (SP); Draft Budgetary Plan (DBP); Commission services' 2013 Autumn Forecast (COM); Commission services' calculations.

On the expenditure side, especially the higher unemployment rate in 2014 (7.6% in the Draft Budgetary Plan compared to 6.4% in the Stability Programme) leads to increased government expenditure compared to earlier projections. This is the case even though the Draft Budgetary Plan incorporates a larger additional consolidation package than the Stability Programme. For 2014, the Draft Budgetary Plan estimates ex ante consolidation measures adding up to some EUR 12 bn in total (around 2% of GDP). Around half of the measures reflect the impact on 2014 of consolidation packages with a multi-year coverage which had already been initiated in earlier years, while the other half pertains to the additional measures incorporated in the 2014 draft budget. The envisaged ex ante size of the additional consolidation package for 2014

Table 3. Debt developments

(% of GDP)	2012	2013			2014		
		SP	DBP	COM	SP	DBP	COM
Gross debt ratio[1]	**71.3**	**74.0**	**75.0**	**74.8**	**75.0**	**76.1**	**76.4**
Change in the ratio	5.5	2.7	3.7	3.6	1.0	1.1	1.6
Contributions[2]:							
1. Primary balance	**2.2**	**1.3**	**1.3**	**1.4**	**1.6**	**1.5**	**1.5**
2. "Snow-ball" effect	**1.9**	**1.2**	**1.6**	**1.5**	**0.0**	**0.4**	**0.6**
Of which:							
Interest expenditure	1.9	2.0	1.9	1.9	1.9	1.8	1.9
Growth effect	0.8	0.3	0.9	0.7	-0.8	-0.4	-0.2
Inflation effect	-0.9	-1.1	-1.2	-1.1	-1.1	-1.0	-1.0
3. Stock-flow adjustment	**1.5**	**0.3**	**0.8**	**0.7**	**-0.6**	**-0.8**	**-0.5**
Of which:							
Cash/accruals difference		0.0	-0.1		0.0	0.0	
Net accumulation of financial assets		0.2	1.0		-0.4	-0.8	
of which privatisation proceeds		n.a.	n.a.		n.a	n.a.	
Valuation effect & residual		-0.8	-0.3		-1.9	-1.4	

Notes:

[1] End of period.

[2] The snow-ball effect captures the impact of interest expenditure on accumulated debt, as well as the impact of real GDP growth and inflation on the debt ratio (through the denominator). The stock-flow adjustment includes differences in cash and accrual accounting, accumulation of financial assets and valuation and other residual effects.

Source:

Stability programme (SP); Draft Budgetary Plan (DBP); Commission services' 2013 Autumn Forecast (COM); Commission services' calculations.

was enlarged from EUR 4.3 bn (0.7% of GDP) to EUR 6 bn (1% of GDP) in the course of this year. With expenditure growth constrained by domestic expenditure ceilings, the shortfall in growth is expected to translate into lower revenue, which accounts for the projected increase in the deficit. The headline deficit for 2014 is the same in the Commission forecast and the Draft Budgetary Plan, mirroring the similarities in the underlying macroeconomic scenarios. The estimates of levels and changes in the structural balance differ somewhat, however, partly mirroring some differences in output gap projections and partly due to a somewhat different composition of measures. Downside risks to the fiscal outlook for 2014 stem from implementation risks notably concerning planned savings from subnational layers of government and health care. A stronger-than-forecast economic recovery constitutes an upward risk.

3.2. Debt developments

General government consolidated gross debt has increased markedly since 2007, mainly due to persistently high deficits. The debt ratio was over 71% of GDP in 2012 and is expected to increase further in the coming years[2] (Table 3). The 2013 Stability Programme of the Netherlands foresees an increase of the debt ratio until 2014 (to 75% of GDP) and a subsequent decrease of the debt ratio, the latter predicated on an earlier vintage of multi-annual projections As the economic outlook has deteriorated since the submission of the Stability Programme, the Draft Budgetary Plan expects the gross debt ratio to increase further, to around 76% of GDP in 2014.

[2] Especially at the beginning of the crisis substantial interventions in the financial sector were made. As a large part of the cost of these interventions have already been paid back, the total effect on the 2012 debt ratio is rather small. The effect of European rescue operations also only had a limited effect on the gross debt level.

The debt ratio projection for 2014 in the 2013 Commission Autumn forecast is slightly higher than the one in the Draft Budgetary Plan. This results from a slightly less optimistic real GDP growth projection for 2014 compared to the macroeconomic scenario underpinning the draft budgetary plan, but a similar GDP deflator for 2014. Risks to public debt developments mainly stem from headline deficits that could turn out to be higher than expected and nominal growth falling short of the projections. Risks stemming from outstanding government guarantees, although substantial in size, appear very limited.

3.3. Measures underpinning the draft budgetary plan

As a reaction to an economy that is undergoing a more severe downturn than previously estimated, the government announced an additional consolidation package and incorporated this in its draft budget[3]. The stated goal of these additional measures (see Table 4) is to have an ex ante impact on the deficit to the amount of an additional EUR 6 bn (1% of GDP), thus in line with the amount of additional measures compatible with the EDP recommendation. On 11 October the government reached an agreement with opposition parties, changing the composition (but not the overall size) of the package in order to secure adoption by the Parliament. The budgetary effects of most of the measures presented in the package are estimated in a detailed manner and in line with standard elasticities.

The consolidation package presented in the Draft Budgetary Plan also includes additional measures decided on since the spring that have an effect in 2013. These of course had not been incorporated in the Commission Spring 2013 forecast underlying the EDP recommendation. These measures are deficit-increasing and add up to around EUR 2.4 bn (0.4% of GDP). The largest of these measures is a temporary reduction in an employers' social security premium effective in the fourth quarter of 2013, thereby reducing social security revenues by EUR 1.3 bn (0.21% of GDP) for 2013 as a whole. Furthermore, additional outlays on expenditure for 2013 would be equivalent to some EUR 0.1% of GDP. Compared to the baseline projections of the EDP recommendation, the implied loosening for 2013 is more than offset by a change in the classification of the budgetary impact of the nationalisation of bank-insurer SNS Reaal. On the basis of quarterly data published by Statistics Netherlands (CBS), the forecast 2013 general government deficit is lower than in the spring, because it does not include a sizeable deficit impact for the nationalisation of SNS Reaal. However the CBS and Eurostat are currently discussing the statistical recording of this transaction.

Deficit decreasing measures for 2014 had already been part of the coalition agreement of the current government and had been incorporated in the baseline of the the multi-annual path of the 2013 budget. Inter alia these concern: a reduction of development aid (EUR 0.75 bn), a tax increase on social housing corporations (EUR 1.1 bn), expenditure measures in health care (EUR 0.3 bn), an increase of the unemployment insurance premium (EUR 1.3 bn), a cut in subsidies for companies (EUR 0.2 bn), an increase in several excise duties (EUR 0.4 bn) and an increase in an income tax deduction, reducing revenues by EUR 2.3 bn. In total, all measures that were already planned before the new consolidation package incorporated in the 2014 budget and the Draft Budgetary Plan were estimated to have an ex ante deficit-decreasing effect for 2014 of EUR 6 bn, around 1% of GDP.

3 An initial draft budget for 2014 was presented to Parliament in September 2013. After the budget agreement with some opposition parties in October 2013 the budget proposal was amended accordingly and the authorities sent an addendum to the Draft Budgetary Plan, including detailed information on the agreed changes. The Draft Budgetary Plan as assessed in this document pertains to the total of measures, including the addendum received by the Commission after the October 2013 budget agreement.

The main measures of the additional consolidation package embedded in the 2014 budget and the Draft Budgetary Plan are the following, expressed in ex ante terms. As regards expenditure, in health care, EUR 1.48 bn (0.24% of GDP) will be cut, increasing to EUR 2.15 bn in 2017. The most important measure in this area is the intention of the government to save EUR 0.75 bn (0.12 % of GDP) on expenditure on pharmaceuticals, with savings progressively increasing to almost EUR 1 bn in 2017. Part of these savings will have to be realised by private insurance companies and from negotiations among other care providers aimed at further cost reductions, also involving employees in the sector.

In 2014, the package foresees a discretionary increase in social security payments. In addition to a cut in transfers to disabled people of EUR 0.1 bn, the government plans to gradually transform several subsidies for households into a single scheme. This will increase expenditure in 2014 but should lead to overall savings in the subsequent years (around EUR 1.2 bn in 2017).

The package also includes savings on public administration. Although details still have to be formulated, most civil servants will experience a freeze in their overall compensation. After three years of nominal wage freezes, the authorities do intend, however, to allow some increase in nominal wages and plan to achieve this through changes in other working conditions such as adapting the number of holidays and a reduction in pension premium payments. The intended savings amount to EUR 0.75 bn (0.12% of GDP). Ministries will get a small generic cut on their budgets and additionally will not get an increase of budgeted expenditure due to inflation as previously foreseen, in all saving around EUR 1 bn (0.17% of GDP). In accordance with national budgetary rules, subnational governments have to contribute proportionally to any consolidation effort. On top of previously agreed generic cuts, central government payments to subnational governments will be reduced by EUR 0.34 bn (0.06% of GDP) in 2014. Partly offsetting these generic cuts in central government expenditure, additional outlays are planned, mainly for education and to a more limited extent also for defence purposes. For education, increased expenditure of around EUR 0.65 bn (0.1% of GDP) is allocated largely to 2013.

On the revenue side the draft budget includes several tax increases. Putting severance payments in companies for the sole purpose of (temporary) tax avoidance will not be possible anymore, increasing income tax revenues by an estimated EUR 2.1 bn (0.35% of GDP) in 2014. Even though the government has calculated it in a conservative way, the exact amount the government will receive in 2014 is subject to a large degree of uncertainty.

People with high income will pay a "crisis levy" in 2014, expected to yield EUR 0.5bn (0.08% of GDP). Income tax brackets will not be adjusted for inflation, which the Draft Budgetary Plan estimates to yield EUR 0.98 bn (0.16% of GDP). "Green" taxes will be increased, yielding around EUR 0.48 bn (0.08% of GDP) in 2014. Taxes on labour will be decreased through different measures, reducing government revenues by an estimated EUR 2.3bn (0.38% of GDP). Additionally, several other measures are planned concerning the taxation of companies, resulting in an overall tax increase of EUR 0.9 bn (0.15% of GDP).

Table 4. Main discretionary measures reported in the Draft Budgetary Plan

A. Discretionary measures taken by General Government – revenue side

Components	Budgetary impact (% GDP) (as reported by the authorities)		
	2013	**2014**	**2015**
Taxes on production and imports	0.0	0.2	0.2
Current taxes on income, wealth, etc.	0.0	0.3	0.3
Capital taxes	0.0	0.0	0.0
Social contributions	-0.2	0.0	-0.1
Property Income	0.0	0.0	0.0
Other	0.0	0.0	0.0
Total	-0.3	0.4	0.3

Note:

The budgetary impact in the table is the aggregated impact of measures as reported in the DBP, i.e. by the national authorities. A positive sign implies that revenue increases as a consequence of this measure.

Source: Draft Budgetary Plan

B. Discretionary measures taken by General Government – expenditure side

Components	Budgetary impact (% GDP) (as reported by the authorities)		
	2013	**2014**	**2015**
Compensation of employees	0.1	-0.2	-0.2
Intermediate consumption	0.1	-0.1	0.0
Social payments	0.0	-0.2	-0.4
Interest Expenditure	n.a.	n.a.	n.a.
Subsidies	0.0	0.0	0.0
Gross fixed capital formation	0.0	-0.1	-0.1
Capital transfers	0.0	0.0	0.0
Other	0.0	0.0	0.0
Total	0.2	-0.6	-0.7

Note:

The budgetary impact in the table is the aggregated impact of measures as reported in the DBP, i.e. by the national authorities. A positive sign implies that expenditure increases as a consequence of this measure.

Source: Draft Budgetary Plan

4. COMPLIANCE WITH THE PROVISIONS OF THE STABILITY AND GROWTH PACT

4.1. Compliance with EDP recommendations

For 2013, the headline deficit is expected to reach 3.3% of GDP, below the target specified in the EDP recommendation (see Box 2). The improvement in the structural balance, adjusted for changes in potential growth and unexpected revenue shortfalls, is estimated to be 0.9% of GDP, above the recommended effort of around 0.6% of GDP. For 2014, the headline deficit is forecast to reach 3.3% of GDP, above the nominal target that would ensure the correction of the excessive deficit by 2014, as recommended by the Council. On the basis of the Commission 2013 Autumn Forecast, the fiscal effort corrected for changes in potential growth and unexpected revenue shortfalls would reach 0.5%, which is below the EDP recommended value of around 0.7% of GDP. However, a bottom-up assessment which estimates the size in the fiscal effort for 2014 on the basis of the additional discretionary revenue measures and the expenditure developments under the control of the government[4] between the EDP scenario and the Commission Autumn forecast, shows that the Netherlands has taken additional measures for 2014 adding up to around 1% of GDP, which is in line with the amount of measures deemed necessary to reach the structural targets spelled out in the EDP recommendation. This estimate is consistent with amounts from individually specified and quantified measures as reported in the Draft Budgetary Plan.

Box 2. Council recommendations addressed to the Netherlands

On 21 June 2013, the Council recommended the Netherlands under Art. 126(7) of the Treaty to correct its excessive deficit by 2014. To this end, the Netherlands should reach a headline deficit target of 3.6% of GDP in 2013 and 2.8 % of GDP in 2014, which is consistent with an improvement of the structural balance of around 0.6% and 0.7% of GDP in 2013 and 2014 respectively, based on the Commission services updated 2013 spring forecast. The Netherlands should implement the multiannual measures already adopted with the 2013 budget, while standing ready to compensate them if their yield would prove less than currently foreseen, and implement additional measures sufficient to achieve a correction of the excessive deficit in 2014. The Council establishes the deadline of 1 October for the Netherlands to take effective action and, in accordance with Article 3(4a) of Regulation (EC) No 1467/97, to report in detail the consolidation strategy that is envisaged to achieve the targets.

On 9 July, the Council also addressed recommendations to the Netherlands in the context of the European Semester. In particular, in the area of public finances the Council recommended to the Netherlands to reinforce and implement the budgetary strategy, supported by sufficiently specified measures, for the year 2014 and beyond to ensure a timely correction of the excessive deficit by 2014 in a sustainable manner and achieve the structural adjustment effort specified in the Council recommendations under the EDP. Protect expenditure in areas directly relevant for growth such as education, innovation and research. After the correction of the excessive deficit, pursue the structural adjustment effort that will enable the Netherlands reaching the medium-term objective by 2015.

4.2. Other considerations

Although the main aim of the additional consolidation package recently agreed upon (see section 3.3) is to reduce the general government budget deficit, the budgetary plans aim at safeguarding expenditure on education (government spending on education as a percentage of GDP (COFOG expenditure category 9) is expected to slightly increase in 2014). Progress with respect to the country specific recommendation on public finances as regards supporting the long-term growth prospects of the Netherlands will be assessed more comprehensively in the European Semester.

[4] Expenditure net of interest payments and non-discretionary change in the unemployment benefits, expressed in real terms.

5. ANALYSIS OF THE ECONOMIC PARTNERSHIP PROGRAMME

The Economic Partnership Programme closely mirrors the Draft Budgetary Plan. The government confirms plans to introduce a number of fiscal structural reforms with potentially significant effect on public finances both in the short and the long run. It also proposes some new measures aimed at improving the sustainability of public finances. To this end, the Netherlands is currently transposing the Treaty on Stability, Coordination and Governance in the Economic and Monetary Union (TSCG) into national legislation. The *Sustainability of Public Finances Act* will codify a number of procedures that are already used but will also set up new mechanisms; for example, the long standing practice of the use of fixed expenditure ceilings and the fact that budget policy are to be based on CPB forecasts will become legal requirements. The act also specifies that all layers of government are jointly responsible for achieving budgetary targets set by Council recommendations for correcting an excessive deficit or the (progress towards the) medium term objective. These measures should help the Netherlands improve its fiscal framework and comply with the requirements of the Stability and Growth Pact and the Directive on national budgetary frameworks[5].

As discussed in the Staff Working Document for the 2013 European Semester the statutory retirement age in the first pillar will be increased in steps to 67 years and subsequently linked to life expectancy. A matching increase of the statutory retirement age in the second pillar is currently awaiting approval of parliament. The government is also planning to decentralise substantial parts of the long-term care system to municipalities, which it hopes would improve the efficiency of the system and will have a substantial positive effect on public finances.

Concerning the housing market, the government has introduced a number of measures with substantial effects on market functioning and public finances in the long run. As discussed in the Staff Working Document accompanying the recommendation for a Council Recommendation on the EDP[6], mortgage interest deductibility will be gradually reduced and for new cases limited to annuity repayment of the loan. In the long term, the ensuing limitation in mortgage interest deductibility will substantially reduce the fiscal subsidy granted to mortgage-financed housing. Moreover, it was recently announced that the limit that can be insured under the National Mortgage Guarantee Scheme will be reduced in steps from currently EUR 290.000 to EUR 225.000 as of 1 July 2016. This should further reduce the exposure of the government to mortgage-related risks.

The government also plans to continue with reforms of the labour market, mainly to improve incentives to enter the labour market, which will also impact public finances. Some transferable tax credits, for instance for second-income earners, will continue to be progressively phased out. As of 2016, termination of employment contracts will be simplified and unemployment benefits will be reformed. Overall, these labour-market reforms are expected to have a limited budgetary impact. Their exact modalities and the speed of implementation depend on the implementation of agreements with social partners.

Although detailed information on the measures is given, the Economic Partnership Programme information regarding the specific challenges and risks during the implementation of the measures is absent. Implementation risks are partly related to the need to secure support in both Houses of Parliament. In addition, there are also risks related to the budgetary effects of savings measures, in particular planned savings from efficiency-improvements of the long-term care sector.

5 This discussion does not preclude any formal assessment of the transposition of the TSCG and/or Directive 2011/85/EU. A formal assessment will follow after the deadline for transposition.

6 http://ec.europa.eu/europe2020/pdf/nd/swd2013_netherlands_en.pdf

6. SUMMARY

The measures outlined in the Draft Budgetary Plan of the Netherlands aim to address the Council EDP recommendation, while it is expected that the headline deficit will not be brought below 3% of GDP in 2014.The Netherlands also aims at safeguarding expenditure in areas directly relevant for growth, in particular educational expenditure. A more comprehensive analysis of progress will follow in the European Semester.

Annex. EDP related tables

Table A1. Baseline scenario underlying the EDP recommendation

% of GDP	2012	2013	2014
Revenues	46.4	47.3	47.2
Current revenues	46.1	47.0	46.9
Discretionary measures with impact on current revenue (EUR bn)	0.1	1.7	0.2
Expenditure	50.4	50.8	50.7
Real GDP growth (%)	-1.0	-0.8	0.9
Nominal GDP growth (%)	-0.2	0.6	2.6
Potential GDP growth (%)	0.2	0.0	0.3
Structural balance	-2.6	-2.0	-2.3
General government balance	-4.1	-3.6	-3.6
p.m CAB methodology revenue elasticity	0.88	0.88	0.88
p.m Apparent revenue elasticity	-7.7	-1.6	0.8
p.m Output gap (% of pot. Output)	-2.5	-3.3	-2.7
Source: Commission Staff Working Document accompanying the document Recommendation for a Council Recommendation with a view to bringing an end to the situation of an excessive government deficit in the Netherlands (COM(2013) 392 final)			

Table A2. EDP scenario underlying the EDP recommendation

% of GDP	2012	2013	2014
Real GDP growth (%)	-1.0	-0.8	0.3
Potential GDP growth (%)	0.3	0.0	0.2
Structural balance	-2.6	-2.0	-1.3
General government balance	-4.1	-3.6	-2.8
p.m Output gap (% of pot. output)	-2.6	-3.4	-3.3
Source: Commission Staff Working Document accompanying the document Recommendation for a Council Recommendation with a view to bringing an end to the situation of an excessive government deficit in the Netherlands (COM(2013) 392 final)			

Table A3. Current estimates of the macroeconomic and fiscal developments

% of GDP	2013	2014	2015
Revenues	46.4	46.9	47.6
Current revenues	46.75	46.40	45.55
Discretionary measures with impact on current revenue (EUR bn)	9.3	4.8	-3.2
Expenditure	50.4	50.2	50.9
Real GDP growth (%)	-1.2	-1.0	0.2
Nominal GDP growth (%)	0.0	0.6	1.7
Potential GDP growth (%)	0.2	0.0	0.1
Structural balance	-2.7	-2.1	-1.7
General government balance	-4.1	-3.3	-3.3
p.m CAB methodology revenue elasticity	0.88	0.88	0.88
p.m Apparent revenue elasticity	-2.8	1	0.7
p.m Output gap (% of pot. Output)	-3.4	-3.2	-2.3
Source: Commission 2013 Autumn Forecast			

Table A4. Adjustment of apparent structural effort for the revision in potential growth – details of calculation

	Potential GDP growth underlying the Council Recommendation (%)	Potential GDP growth at the time of assessment (%)	Forecast error (%)	Structural expenditure (% of potential GDP)	Correction coefficient α (% of nominal potential GDP)
	(1)	(2)	(3)=(1)-(2)	(4)	(5)=(3)*(4)/100
2013	0.0	0.0	0.0	47.8	0.0
2014	0.3	0.1	0.2	47.2	0.1
2015	-	-	-	47.5	-

Table A5. Adjustment of apparent structural effort for the unexpected revenue windfalls/ shortfalls – details of calculation

	Change in current revenues (yoy) (billions of national currency)		Discretionary current revenue measures (billions of national currency)		Nominal GDP growth assumptions (%)		Current revenues in year t-1 (billions of national currency)		Revenue gap (billion of national currency)*	Correction coefficient β (% of nominal potential GDP)
	2013EDP	2013AF	2013EDP	2013AF	2013EDP	2013AF	2013EDP	2013AF		
	(1)	(1')	(2)	(2')	(3)	(3')	(4)	(4')	(5)=[(1')-(2')-ε*(3')*(4')]-[(1)-(2)-ε*(3)*(4)]	
2013	7.3	4.6	10.0	9.3	0.6	0.6	276.8	276.5	-1.9	-0.3
2014	7.0	9.4	0.0	4.8	2.6	1.7	284.1	281.1	-0.1	0.0
2015		4.6		-3.2		3.9		290.5		