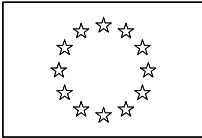


EUROPEAN COMMISSION
DIRECTORATE GENERAL
ECONOMIC AND FINANCIAL AFFAIRS

Brussels, 25 January 2005
ECFIN/ 50786/04-EN

NOVEMBER 2004 UPDATE OF THE STABILITY PROGRAMME OF THE NETHERLANDS (2004-2007)

AN ASSESSMENT

Table of contents

SUMMARY AND CONCLUSIONS 3
1. INTRODUCTION 6
2. MACROECONOMIC DEVELOPMENTS 6
3. BUDGETARY IMPLEMENTATION IN 2004 8
4. BUDGETARY TARGETS AND THE MEDIUM-TERM PATH OF THE PUBLIC FINANCES 9
   4.1. Evolution of budgetary targets in successive programmes 9
   4.2. Budgetary targets in the updated programme 10
   4.3. Sensitivity analysis 14
5. EVOLUTION OF THE DEBT RATIO 14
6. STRUCTURAL REFORM AND THE QUALITY OF PUBLIC FINANCES 15
7. THE SUSTAINABILITY OF THE PUBLIC FINANCES 17

Annex 1: Summary tables from the stability programme update 20

Annex 2: Long-term sustainability of public finances – quantitative scenarios for the Netherlands 23

SUMMARY AND CONCLUSIONS[1]

The 2004 update of the stability programme of the Netherlands, which covers the period 2004-2007, was submitted on 23 November 2004, following its approval by the government. The multi-annual projections in the update are mainly derived from the 2005 budget, which was submitted to Parliament on 21 September 2004.[2] The update complies with the data requirements of the "code of conduct on the content and format of stability and convergence programmes". [3] It covers all the areas required and provides all the compulsory variables requested, and most of the optional ones except certain data concerning potential output.

The macroeconomic scenario in the update is taken from the CPB Netherlands Bureau of Economic Policy Analysis (CPB). The update assumes a gradual recovery, with real GDP growth at 1½% in 2005, picking up to 2½% from 2006 onwards. For the period 2004-2006, the projections of key variables are quite close to those in the Commission services' autumn 2004 forecast. However, the latest available data on commodity prices, exchange rates and trade volumes suggest that macroeconomic scenario in the update for the years 2005 and 2006 is on the optimistic side. The assumptions on economic growth in 2005 in particular seem favourable. The growth assumptions for 2007 seem plausible in view of the estimated rate of potential growth and the expectation that the negative output gap would be reduced gradually during the upturn. The rates of potential growth and of the output gap derived from the update's macroeconomic scenario using the agreed methodology appear to be plausible. The programme's projections for inflation appear realistic.

The primary aim of the update's budgetary strategy is to bring the general government deficit below the Treaty reference value of 3% of GDP by 2005. To this end, it encompasses a frontloaded consolidation effort, concentrated in 2004 and 2005. The corrective measures for 2005 add up to half a percentage point of GDP. With the combined effect of fiscal consolidation and the expected gradual economic upturn, the update projects the general government deficit to fall from 3.0% of GDP in 2004 to 2.6% of GDP in 2005, 2.1% of GDP in 2006 and 1.9% of GDP in 2007. The cyclically-adjusted deficit is expected to be lower throughout the time horizon covered and to decrease from 1.6% of GDP in 2004 to 1.2% of GDP in 2005. However, the cyclically-adjusted balance is not expected to improve further in 2006 and would even deteriorate slightly in 2007, to a deficit of 1.3% of GDP. The budgetary strategy entails the use of real expenditure ceilings to control expenditure growth and the longer-term objective of sustainable public finances, in line with the strategy of the previous update. The public investment ratio is expected to remain constant over the period covered, at slightly above 3% of GDP, against an EU average of 2.4% of GDP in 2004.

The budgetary forecasts of the update appear plausible and the uncertainties to the projections are broadly balanced. Some risks to the deficit projections stem from the risks to the macroeconomic outlook. Moreover, the budgetary costs of the social agreement reached between the government and social partners on 5 November 2004 have not been incorporated in the update, while the

---

1 This technical analysis, which is based on information available up to 22 December 2004, accompanies the recommendation by the Commission for a Council opinion on the update of the stability programme, which the College adopted on 11 January 2005. It has been carried out by the staff and under the responsibility of the Directorate-General for Economic and Financial Affairs of the European Commission. Comments should be sent to ronald.albers@cec.eu.int and barbara.kauffmann@cec.eu.int.

2 The 2005 budget was adopted by Parliament with a number of amendments that did not have an appreciable impact on the main budgetary aggregates.

3 Revised Opinion of the Economic and Financial Committee on the content and format of stability and convergence programmes, document EFC/ECFIN/404/01 - REV 1 of 27.06.2001 endorsed by the ECOFIN Council of 10.07.2001.

uncertainty surrounding the implementation of reforms in the areas of health care and pensions might also lead to a higher deficit. However, these risks are mitigated by the positive impact of higher oil prices on receipts from the sale of natural gas, and by the fact that the assumptions on the tax intensity of economic activity used in the baseline scenario of the update are on the cautious side. Taking into account the balance of risks to the budgetary targets, the Netherlands appears to be on track to correct its excessive deficit by 2005, the deadline set by the Council. However, the fiscal consolidation path foreseen after the correction of the excessive deficit lacks ambition, as it would not ensure the achievement of the medium-term objective of a budgetary position of close-to-balance within the programme period. Moreover, in this period (2006-2007), the budgetary stance in the update does not seem to provide a sufficient safety margin against normal macroeconomic fluctuations breaching the 3%-of-GDP threshold.

The update expects the debt ratio to remain below the 60%-of-GDP reference value and to rise from slightly over 56% of GDP in 2004 to somewhat above 58% of GDP in each of the years 2005 to 2007, with the pick-up in nominal GPD growth largely offsetting the upward impact of persistent deficits on the debt ratio. The update expects the stock-flow adjustments to contribute slightly to increases in debt in the period 2005-2007 after debt-reducing stock-flow adjustments in the period 2000-2003 due to privatisation receipts; the size of the adjustments, however, would remain relatively limited at less than half a percentage point of GDP. These projections are quite close to the Commission services' autumn 2004 forecast. Risks to the debt ratio correspond to those for the deficit projections and appear broadly balanced.

The update briefly reviews the government's structural reform programme, which encompasses a far-reaching overhaul of the social security, pension and health care systems that is intended to improve the sustainability of public finances and to increase labour participation. It also outlines the positive impact on employment and economic activity of a reduction in the administrative burden. On balance, the reforms should help improve the sustainability of Dutch public finances. However, in several areas, such as health and pension reform, there is some doubt as to how effectively the proposed measures will influence the actual behaviour of economic agents and thus secure the intended budgetary savings. Moreover, it seems that the positive budgetary impact of structural reforms which strengthen potential growth will be felt mainly after the period covered by the update, while some of the measures that boost net revenue in the near term may not be optimal in terms of improving the structure of the economy, for instance the increase in the marginal wedge for low-to-medium incomes.

The Netherlands is in a relatively favourable position with regard to the long-term sustainability of public finances, despite important projected budgetary cost of an ageing population. However, despite ongoing reforms in the areas of social security, pensions and health care, its current policies do carry some sustainability risks. The strategy outlined in the programme is mainly based on measures aimed at raising labour participation and at containing age-related expenditures. Given the projected increase in the old-age dependency ratio, further reforms that would modify the trends in age-related expenditures and raise further participation rates are a key factor in ensuring sustainability over the longer-term.

Overall, the economic policies outlined in the update are partly consistent with the country-specific broad economic policy guidelines in the area of public finances. The budgetary framework with expenditure ceilings is adhered to, and budgetary adjustment to correct the excessive deficit is well under way. However, the expected reduction in the headline deficit in 2006 and especially 2007 is quite slow, and the cyclically-adjusted balance would not be reduced by at least 0.5 percent of GDP in each year. Moreover, the attainment of a fiscal position close to balance or in surplus is not anticipated within the time span covered by the update.

In view of the above assessment, the Netherlands is recommended to take the necessary measures to ensure that a budgetary position close to balance is achieved and maintained after the correction of the excessive deficit.

Comparison of key macroeconomic and budgetary projections

		2004	2005	2006	2007
Real GDP (% change)	**SP Nov. 2004**	**1¼**	**1½**	**2½**	**2½**
	COM Oct. 2004	1.4	1.7	2.4	n.a.
	SP Oct. 2003	*1*	*2½*	*2½*	*2½*
HICP inflation (%)	**SP Nov. 2004**	**1¼**	**1¼**	**1½**	**1½**
	COM Oct 2004	1.2	1.3	1.4	n.a.
	SP Oct. 2003	*1.5*	*1½*	*1½*	*1½*
General government balance (% of GDP)	**SP Nov. 2004**	**-3.0**	**-2.6**	**-2.1**	**-1.9**
	COM Oct 2004	-2.9	-2.4	-2.1	n.a.
	SP Oct. 2003	*-2.3*	*-1.6*	*-0.9*	*-0.6*
Primary balance (% of GDP)	**SP Nov. 2004**	**-0.1**	**0.3**	**0.7**	**0.8**
	COM Oct 2004	0.0	½	0.9	n.a.
	SP Oct. 2003	*0.6*	*1.2*	*1.8*	*2.1*
Cyclically-adjusted balance (% of GDP)	**SP Nov. 2004**[1]	**-1.6**	**-1.2**	**-1.2**	**-1.3**
	COM Oct 2004	-1.4	-1.0	-1.0	n.a.
	SP Oct. 2003[1]	-0.7	-0.3	-0.2	-0.2
Government gross debt (% of GDP)	**SP Nov. 2004**	**56.3**	**58.1**	**58.6**	**58.3**
	COM Oct 2004	55.7	58	58.4	n.a.
	SP Oct. 2003	*54. 5*	*53.7*	*53.0*	*52.2*

Note:
[1]Commission services calculations on the basis of the information in the programme

Sources:
Stability programmes (SP); Commission services autumn 2004 economic forecasts (COM); Commission services calculation. Forecast growth rates in the update have been rounded to the nearest quarter of a percentage point

1. INTRODUCTION

The 2004 update of the stability programme of the Netherlands (henceforth 'the update'), which covers the period 2004-2007, was submitted on 23 November 2004, following its approval by the government. The multi-annual projections in the update are mainly derived from the 2005 budget, which was submitted to Parliament on 21 September 2004 and adopted with some modifications that did not have an appreciable impact on the main budgetary aggregates.

The update complies with the "code of conduct on the content and format of stability and convergence programmes".[4] It covers all the areas in the model structure and provides all compulsory variables requested, and most of the optional ones except certain data concerning potential output. Deviations from the required definitions exist with respect to a few relatively minor details.[5]

2. MACROECONOMIC DEVELOPMENTS

The macro-economic scenario in the update is taken from the autumn forecast of the CPB Netherlands Bureau of Economic Policy Analysis (henceforth CPB) for 2004 and 2005. The projections for 2006 and 2007 were directly taken from older multi-annual CPB forecasts for the period 2003-2007 released in July 2003 and therefore do not link to the most recent forecasts up to 2005 in a fully consistent way. For the period 2004-2006 the projections of key variables are quite close to those in the Commission services autumn 2004 forecast, which, however, seems on the optimistic side in view of recent developments. The forecasts for real GDP growth in the Commission services autumn forecast for 2004 and 2005 are slightly higher. The update shows a somewhat stronger growth contribution from the foreign balance and a slightly lower contribution from domestic demand in 2005 and 2006. By contrast, unemployment projections in the update are somewhat higher throughout compared to the autumn forecast. According to both forecasts, inflation would decelerate to slightly above 1% in 2005, before picking up moderately in the following year.

Risks to the macro-economic scenario of the update for the period 2004-2006 are skewed to the downside. The projection of real GDP growth for 2005 in particular seems high, in view of the latest available data and indicators on economic activity, trade, and commodity and exchange markets. On 9 December 2004, CPB released a revised forecast for the Dutch economy with real GDP growth estimated at 1½% in 2004 (slightly higher than in the update) and 1% in 2005 (lower by half a percentage point). For 2006 and 2007, the update expects real GDP of 2½%, with inflation and employment growth at 1½% and 1¼% respectively. The growth assumptions for the outer years of the programme seem plausible in view of the estimated rate of potential growth (cf. table 2) and the expectation that the negative output gap would be reduced gradually during the upturn. The programme's projections for inflation appear realistic.

---

[4] Compared to the Commission assessment (available at http://europa.eu.int/comm/economy_finance/about/activities/sgp/year/year20042005_en.htm), the evaluation of compliance follows a reclassification of the degree of compliance into four categories (namely "fully complies", "complies", "broadly complies" and "partly complies"), replacing the previous three-way classification ("complies", "largely complies" and "partly complies").

[5] For instance, labour productivity projections for the whole economy are not given for the years 2006 and 2007.

The update's macro-economic scenario uses external assumptions that are broadly in line with the Commission services autumn forecast as regards world trade and real GDP growth. On the external side, downside risks are related to trends in oil prices, exchange rates and relevant world trade after the finalisation of the macro-economic projections used for the update. On the domestic side, they mainly relate to private consumption. The latest available data suggest that household disposable income would be weaker in the next few years than assumed in the update. For 2005, this is partly due to a higher increase in health insurance premiums than anticipated by the government. The very low consumer confidence is an additional risk to private consumption growth. In November 2004 the index of consumer confidence[6] still stood at close to the all-time low it had reached in the summer of 2003 and from which it had recovered in the first half of 2004. The index fell back again in October, after the release of the 2005 budget. In contrast to the analysis in the update, this suggests that uncertainty among consumers concerning budgetary tightening and increasing tensions between the government and social partners has retarded the recovery of consumer confidence and private consumption.

Table 1: Comparison of macroeconomic developments and forecasts

	2004		2005		2006		2007
	COM	**SP**	**COM**	**SP**	**COM**	**SP**	**SP**
Real GDP (% change)	1.4	1¼	1.7	1½	2.4	2½	2½
Contributions:							
- Final domestic demand	0.7	¾	1	½	1.9	1½	1¾
- Change in inventories	0	¼	0.2	¼	0	0	0
- External balance on g&s	0.7	½	½	1	0.4	1	¾
Employment (% change)	-1.7	-1	½	½	1.2	1½	1¼
Unemployment rate (%)	4.6	6½	5.0	7	4.4	6½	6¼
HICP inflation (%)	1.2	1¼	1.3	1¼	1.4	1½	1½
GDP deflator (% change)	0.9	1	0.8	¾	1.0	1½	1½
Current account (% of GDP)	3.7	-	4.2	-	4½	-	-

Sources:
Commission services autumn 2004 economic forecasts (COM); Stability programme November 2004 update (SP)
Forecast growth rates in the update have been rounded to the nearest quarter of a percentage point

Table 2 presents the estimates of potential output and of the output gap that are consistent with the programme's macro-economic scenario, calculated by Commission services according to the agreed methodology, and corresponding figures from the Commission services forecasts.

6 Time series from Statistics Netherlands.

Table 2: Sources of potential output growth

	2004		2005		2006		2007
	COM	SP[3]	COM	SP[3]	COM	SP[3]	SP[3]
Potential GDP growth[1]	1.6	1.4	1.6	1.6	1.9	1.7	1.9
Contributions:							
- Labour	0.5	0.4	0.5	0.5	0.7	0.6	0.8
- Capital accumulation	0.5	0.5	0.5	0.5	0.6	0.5	0.5
- TFP	0.5	0.5	0.6	0.5	0.6	0.6	0.6
Output gap[1,2]	-2.2	-2.1	-2.1	-2.2	-1.6	-1.5	-0.9

Notes:
[1]based on the production function method for calculating potential output growth
[2]in percent of potential GDP
[3]Commission services calculations on the basis of the information in the Stability programme November 2004 update, figures may not add up due to rounding

Sources:
Commission services autumn 2004 economic forecasts (COM); Commission services calculations

The table shows that the estimates of potential growth and of the output gap are quite similar across the two forecasts. This supports the plausibility of the projections in the update for the outer years of the programme. Nevertheless, some slight divergences with respect to estimated yearly changes in the output gap do exist.

3. BUDGETARY IMPLEMENTATION IN 2004

The budgetary targets for 2004 in the previous update will be missed by a relatively wide margin. While the 2003 update projected a deficit for 2004 of 2.3% of GDP, the current one envisages a deficit of 3.0% of GDP. This substantial upward revision is due to a combination of factors. These include the impact on 2004 of the higher-than-expected deficit in 2003 (base effect, reflecting also the impact of weaker economic growth) and higher-than-foreseen deficits of local government (a deficit of 0.7% of GDP, instead of an expected balanced budget). Shortly after reporting a general government deficit of 3.2% of GDP in 2003 (see Box 1 on the excessive deficit procedure in section 4.1), the Dutch authorities adopted an additional savings package for 2004 on 16 April 2004 on top of the savings measures that had already been included in the 2004 budget. The additional consolidation effort in 2004 was equivalent to around 0.5 percentage point of GDP. Roughly half of this package consisted of structural measures, in particular higher premiums for health insurance, and lower health expenditure. The other half consisted of one-off measures, including the sale of agricultural land, the postponement of public investment projects, the early payment of profits by the central bank, and the phasing of net expenditures on development aid. These one-off measures taken together appear to imply a shift in revenues or expenditure over time and not a loss in the discounted present value of net revenues in the longer run.

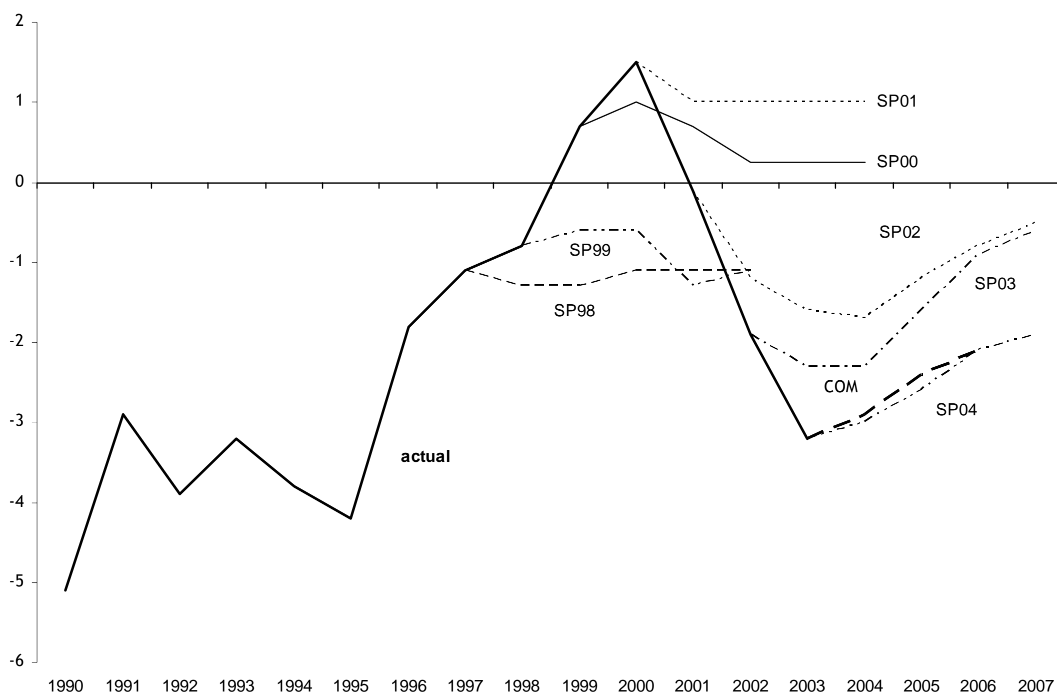
The savings implemented in 2004 should succeed to reduce the deficit compared to 2003. The projected general government deficit according to the update and the estimated outcome in the Commission services autumn 2004 forecast are quite close, at 3.0 and 2.9% of GDP respectively. The deficit forecast for 2004 in the update was confirmed by the regular Autumn note from the Minister of Finance to Parliament on budgetary implementation, released on 25 November 2004.

4. BUDGETARY TARGETS AND THE MEDIUM-TERM PATH OF THE PUBLIC FINANCES

4.1. Evolution of budgetary targets in successive programmes

Figure 1 and Table 3 give an overview of the envisaged adjustment path for the general government balance in the update, compared to previous programmes. Over the forecast horizon, the deficit would be substantially higher than foreseen in the two previous updates. This is largely due to the impact of the unexpectedly severe economic downturn, which translated into higher expenditure and lower revenue ratios than foreseen previously. As an illustration, real GDP growth is envisaged to be lower by no less than a cumulated 4¾ percentage points of GDP over the period 2003-2006 compared to the 2002 update, leading to an estimated deficit in 2006 that is more than 2 percentage points higher.

Figure 1: Evolution of budgetary targets in successive programmes



Source:
Eurostat, Commission services Autumn 2004 forecast, Stability programmes

Box 1: The excessive deficit procedure for the Netherlands

On the basis of a general government deficit of 3.2% of GDP in 2003, above the 3% of GDP reference value of the Treaty, the Council decided on 2 June 2004 that the Netherlands had an excessive deficit and recommended that this be corrected by 2005 at the latest. In particular, the Netherlands was recommended to take action regarding corrective measures in 2005, mainly of a structural nature, amounting to at least half a percentage point of GDP by the deadline of 2 October 2004. Following the expiry of the deadline, Economic and Monetary Affairs Commissioner Almunia reported on the action taken by the Dutch authorities, concluding that it appeared adequate to correct the excessive deficit. This assessment was endorsed by the Ecofin Council of 21 October 2004.

Table 3: Evolution of budgetary targets in successive programmes

		2003	2004	2005	2006	2007
General government balance (% of GDP)	**SP Nov 2004**	**-3.2**	**-3.0**	**-2.6**	**-2.1**	**-1.9**
	SP Oct 2003	-2.3	-2.3	-1.6	-0.9	-0.6
	SP June 2003 [1]	-1.0	-0.7	-0.4	0.1	n.a.
General government expenditure (% of GDP)	**SP Nov 2004**	**48.5**	**48.0**	**47.5**	**46.7**	**46.0**
	SP Oct 2003	47.8	47.4	46.3	45.7	45.2
	SP June 2003 [1]	46.8	45.9	45.7	45.2	n.a.
General government revenues (% of GDP)	**SP Nov 2004**	**45.3**	**45.0**	**44.9**	**44.6**	**44.1**
	SP Oct 2003	45.5	45.1	44.7	44.8	44.6
	SP June 2003 [1]	45.8	45.2	45.3	45.3	n.a.
Real GDP (% change)	**SP Nov 2004**	**-0.9**	**1¼**	**1½**	**2½**	**2½**
	SP Oct 2003	0	1	2½	2½	2½
	SP June 2003 [1]	¾	2¾	2¾	2¾	n.a.

Source:
Stability programmes (SP. Forecast growth rates in the update have been rounded to the nearest quarter of a percentage point)
[1] The June 2003 SP update is the revised version of the December 2002 update that was discussed by the Council

4.2. Budgetary targets in the updated programme

The budgetary strategy outlined in the update implies consolidation measures over the period up to 2007. The adjustment effort is frontloaded and concentrated in 2004 and 2005. The first strategic aim of the update is to reduce the deficit to below the 3% of GDP reference value by 2005, in line with the Council recommendation under Article 104(7). The strategy in the update also aims at taking "measures in keeping with the objective of sustainable public finances" and at limiting the possible adverse impact of budgetary consolidation on economic activity. A cornerstone of the budgetary strategy of the Netherlands is the use of expenditure ceilings in real terms, in order to control the growth of expenditure. The budgetary strategy also entails that higher-than-projected revenues should not be used to finance expenditure growth in excess of the predetermined ceilings.

Starting from a deficit of 3.2% of GDP in 2003 the update expects the deficit to be reduced only slightly in 2004, despite substantial savings measures, some of which are of a one-off nature (table 4). The modest reduction in the headline deficit in 2004, to an estimated 3.0% of GDP, results mainly from the fiscal drag of the deep and protracted economic slowdown and the slight further increase in the deficit of local government.[7] In 2005 and 2006, the deficit would decrease more rapidly, in response to consolidation measures and the projected economic upturn, whereas in 2007 the expected further reduction in the deficit is quite small (0.2 percentage point of GDP). The time profile of the primary surplus is similar, improving from a slight deficit of 0.1% of GDP in 2004 to a surplus of 0.8% of GDP in 2007. Based on Commission services calculations according to the commonly agreed methodology, the cyclically-adjusted deficit would narrow from 1.9% of GDP in 2003 to 1.2% of GDP in 2005, reflecting the fiscal adjustment effort (table 5). However, the cyclically-adjusted balance is estimated not to improve further in 2006 and, in 2007, to even increase slightly to 1.3% of GDP.

[7] The autumn note on budgetary implementation by the Minister of Finance to Parliament confirms the deficit estimate for 2004 at 3.0% of GDP, suggesting that budgetary implementation is on track.

The corrective measures for 2005 in the budget add up to half a percentage point of GDP (see box 2). They are for a large part of a structural nature, and consist both of expenditure reductions and net tax increases. The box describes the budgetary measures in the 2005 budget in greater detail. In 2006 the planned structural overhaul of the social security and pension systems would lead to some limited further net savings. The budgetary impact of these reforms, however, would gradually increase over time and yield the largest net savings beyond the forecast horizon covered. For 2007, the multi-annual projection in the update envisages no appreciable fiscal tightening.

Consolidation is mainly achieved through a fall in the expenditure-to-GDP ratio. The largest reductions in the expenditure ratio stem from public consumption expenditure and social transfers and reflect the savings measures in public administration, attempts to curb health expenditure and the impact of reforms in the social security system. The public investment ratio is expected to remain fairly constant over the forecast horizon, at slightly above 3% of GDP, against an EU average of 2.4% of GDP in 2004. The revenue ratio is expected to decrease also during the period covered, due to a number of reasons. These include the lagged impact of the economic slowdown on household income and taxable profits of corporations. Moderate wage increases also lead to a certain degression in income taxes especially in 2004 and 2005, as the upward adjustment of income tax brackets would be higher than the growth of nominal wage income. The loss in revenue from increases in tax-deductible mortgage interest payments and tax-exempt private pension premiums, estimated at around one quarter of a percent of GDP per year between 2000 and 2003, also plays a role in explaining the relatively lacklustre development of tax revenue. However, in 2005 the fall in the overall revenue ratio would be quite small reflecting increases in the tax burden in that year. The adjustment path foreseen in the central scenario of the update for 2006 and 2007 seems to lack ambition: the general government deficit would only improve relatively gradually in view of the expected economic upturn.

As regards the projected development of the balances of sub-sectors within general government, a few points merit attention. First, it is noticeable that the deficit of central government, where shortfalls on the revenue side are concentrated, would remain high over the entire horizon covered. The central government deficit is even expected to increase to 3.0% of GDP in 2007. In 2002 and 2003 the deficit of local government had increased unexpectedly, mainly due to high investment and net purchases of land by municipalities.[8] The update expects the deficits of local government to diminish gradually until 2007. By contrast, social security funds are projected to register increasing surpluses between 2004 and 2007, reflecting the combined impact of a relatively high level of premiums (which are set in conjunction with income taxes taking into account forecasts of household purchasing power) and the tightening of benefit eligibility.

[8] The programme discusses at some length the reasons behind this deterioration of the balance of local government. It adds a box on the agreed measures to reduce the deficit in the coming years. In short, the deficit of the total sub-sector local government would be subject to a maximum of 0.5% of GDP as of 2005. Further measures to limit the deficits of local authorities may be taken if the government deficit risks exceeding 2.5% of GDP.

Table 4: Composition of the budgetary adjustment

(% of GDP)	2003	2004	2005	2006	2007	Change: 2007-2004
Revenues	45.3	45.0	44.9	44.6	44.1	**-0.9**
of which:						
- Taxes & social security contributions	39.4	39	38.7	38.6	38.2	**-0.8**
- Other (residual)	5.9	6.0	6.2	6.0	5.9	**-0.1**
Expenditure	48.5	48.0	47.5	46.7	46.0	**-2.0**
of which:						
- Primary expenditure	45.6	45.1	44.6	43.9	43.3	**-1.8**
of which:						
Gross fixed capital formation	3.2	3.2	3.1	3.1	3.1	**-0.1**
Collective consumption	17.8	17.7	17.5	17.2	16.9	**-0.8**
Transfers & subsidies	22.9	22.7	22.2	22.2	21.8	**-0.9**
Other (residual)	1.7	1.5	1.8	1.4	1.5	**0**
- Interest payments	2.9	2.9	2.8	2.7	2.7	**-0.2**
Budget balance	-3.2	-3.0	-2.6	-2.1	-1.9	**1.1**
Primary balance	-0.3	-0.1	0.3	0.7	0.8	**0.9**
Sources: *Stability programme November 2004 update; Commission services calculations*						

Box 2: The budget for 2005

The 2005 budget encompasses net expenditure reductions of around 0.3% of GDP and increases in the net tax burden of 0.2% of GDP. Measures on the expenditure side include a wage freeze for civil servants and cuts in the expenditure of civil service, introduction of an own risk in public health insurance, and the phasing out of subsidies on employing low-paid workers, reduced access to unemployment benefits. Some expenditure increases are also budgeted, mainly in the areas of police and security. On the income side, the budget seeks to boost revenue by an increase in the two lowest brackets of the income tax, by higher disability premiums, increases in the premiums for public health insurance, the introduction of the obligation to pay corporate taxes for two independent public sector agencies, and an end to subsidies for buying personal computers for home use.

The 2005 budget also specifies plans to reduce access to the disability scheme and end the fiscal facilitation of pre-pension and early retirement arrangements for those currently under 55 years of age as of 2006.

Table 5 compares the estimates of output gaps and cyclically-adjusted balances derived from the programme using the commonly agreed methodology with the Commission services autumn 2004 forecast. The estimates of cyclically-adjusted balances need to be interpreted with due caution, especially in view of the rather volatile year-on-year pattern of the calculated rate of potential growth. The changes in the cyclically-adjusted balance according to the update and the autumn forecast are fairly close[9], except that the update implies a somewhat higher cyclically-adjusted deficit throughout the period 2004-2007. The cyclically-adjusted deficit would improve in 2004 and 2005, in response to the fiscal tightening. However, the update lacks ambition as regards the adjustment in 2006 and 2007 since the cyclically-adjusted deficit would not improve any further and would even deteriorate slightly in the latter year. A position close to balance or in surplus

[9] The cyclically-adjusted balances presented in the update itself are somewhat different from the ones in table 5. They were also computed with the commonly agreed methodology, but using the slightly different specification from the Working Group on Output Gaps of the EPC that was in force at the cut-off date for the calculations in the programme.

would not be reached at any point over the projection horizon. The cyclically-adjusted deficit is estimated to be reduced to 1.2% of GDP in 2005, but would stay at this level in the following year, and would even rise somewhat in 2007.

Table 5: Output gaps and cyclically-adjusted (primary) balances (CA(P)B)

	2003		2004		2005		2006		2007	Change: 2007-2004
	COM	SP[1]	COM	SP[1]	COM	SP[1]	COM	SP[1]	SP[1]	SP[1]
Budget balance[2]	-3.2	-3.2	-2.9	-3.0	-2.4	-2.6	-2.1	-2.1	-1.9	1.1
Output gap[3]	-2.0	-2.0	-2.2	-2.1	-2.1	-2.2	-1.6	-1.5	-0.9	1.2
CAB[2]	-1.8	-1.9	-1.4	-1.6	-1.0	-1.2	-1.0	-1.2	-1.3	0.3
CAPB[2]	1.1	1.0	1.4	1.3	1.9	1.7	2.0	1.6	1.4	0.1

Notes:
[1]Commission services calculations on the basis of the information in the stability programme November 2004 update
[2]in percent of GDP
[3]in percent of potential GDP
Sources:
Commission services autumn 2004 economic forecasts (COM); Commission services calculations

The budgetary projections in the programme appear broadly plausible: for the period 2004-2006 they are generally in line with the Commission services autumn 2004 forecast. The deficit projections for 2004 and 2005 and are broadly supported by the CPB forecasts released on 9 December 2004. The CPB estimates a general government deficit of 3% of GDP in 2004 and 2¼% of GDP in 2005 (taking into account the impact of the social agreement). For 2005, this is even somewhat lower than the deficit according to the update's central scenario, in spite of somewhat weaker economic growth.

Risks to the budgetary outlook for 2005 and beyond appear broadly balanced. Some risk of a higher headline deficit stems from the risk that economic activity may be weaker than expected in the update. Moreover, the budgetary costs of the social agreement reached between the government and social partners on 5 November 2004, which mitigates some of the intended measures with respect to social security and pensions, would also lead to a somewhat higher deficit than in the central scenario. The most recent government estimates suggest that the agreement would imply the deficit to be higher by around 0.1% of GDP in each of the years 2005 to 2007.[10] Risks of a higher deficit also exist with respect to the implementation of announced measures, notably in the areas of health care (also in view of earlier slippages) and the effective budgetary gain from abolishing fiscal facilities for early retirement as of 2006. However, these risks to the deficit projections are mitigated by the positive impact of higher oil prices on government receipts from the sale of natural gas, and by the cautious assumptions on the tax intensity of economic activity used in the programme's baseline. The cyclically-adjusted balance may turn out to be better than expected. This is the case since risks to the budgetary projections are broadly balanced while economic activity may well be weaker than forecast. To the extent that potential growth would not be greatly affected by a more prolonged spell of cyclical weakness, the output gap might be larger than estimated in the central scenario of the update, and hence the cyclically-adjusted deficit may turn out to be lower.

[10] CPB estimates suggest a somewhat higher cost associated with the changes to original plans due to the social agreement. According to CPB the upward impact on the deficit would increase gradually from 2005 onwards and may reach around one quarter of a percentage point of GDP in 2007.

Taking into account the balance of risks to the budgetary targets, the Netherlands appears to be on track to correct its excessive deficit by 2005, the deadline set by the Council. However, the budgetary stance in the programme does not seem to provide a sufficient safety margin against breaching the 3% of GDP deficit threshold with normal cyclical fluctuations in 2006 or 2007 as at no point would the cyclically-adjusted deficit fall within the safety margin of a deficit of no more than 0.7% of GDP. It also seems insufficient to ensure that the Stability and Growth Pact's medium-term objective of a budgetary position of close to balance is achieved after the correction of the excessive deficit. This would imply that additional measures need to be taken to attain such a medium-term objective.

The update is partly consistent with the recommendations in the updated Broad Economic Policy Guidelines, specifically those with budgetary implications. In the budgetary strategy, the framework with expenditure ceilings is adhered to, and budgetary adjustment to correct the excessive deficit by 2005 is well underway. However, the expected reduction in the headline deficit in 2006 and especially 2007 is quite slow. Moreover, in 2006 the cyclically-adjusted balance would not improve any more and even increase slightly in 2007. Hence, within the time span covered by the programme neither a reduction by at least 0.5 percentage point of GDP each year would be achieved nor of a close to balance position is not foreseen.

4.3. Sensitivity analysis

The update presents calculations that aim at evaluating the budgetary impact of several alternative scenarios. These relate to highly relevant risks from the external environment, notably higher oil prices, a stronger euro exchange rate, and higher interest rates. The sensitivity analyses presented are derived from scenarios carried out by CPB using macro-econometric models. These alternative scenarios appear relevant in the light of recent trends in commodity prices, global economic activity, and exchange rates. Overall, the estimated impact on the budget balance in any of these scenarios is relatively small. Higher oil prices would dampen economic growth but have no net effect on the general government balance, due to higher receipts from the sale of natural gas. The largest estimated impact concerns a rise in interest by 100 basis points. This would lead to a deterioration of the government balance by 0.3 to 0.4 percentage point of GDP after 2 years. A CPB scenario analysis taken from the same source as used in the update[11] suggests that 0.5 percentage point lower real GDP growth due to weaker world trade would lead to the deficit being higher by around 0.3% of GDP after three years.

5. EVOLUTION OF THE DEBT RATIO

Table 6 describes the evolution of the debt ratio and its determinants. The projections for the debt ratio in the update for the period 2004-2006 are quite close to those in the Commission services forecast. The debt ratio is expected to rise from slightly over 56% of GDP in 2004 to around 58% of GDP in 2005, due to the combination of weak nominal GDP growth and a relatively high deficit. The debt ratio would remain fairly stable in 2006 and 2007, with the pick-up in nominal GDP growth largely offsetting the impact of persistent deficits over the projection horizon.

Risks to the debt forecasts stem primarily from the risks to the deficit projections and appear broadly balanced. The stock-flow adjustment is expected to be slightly positive in the period

---

[11] CPB (2003), *JADE: a model for the Joint Analysis of Dynamics and Equilibrium*, CPB Document No. 30.

2005-2007.[12] The estimates of the stock-flow adjustment in 2004 and 2005 may be subject to changes in the indicative multi-annual plans to sell public assets in order to finance the fund on strengthening the economic structure (FES).

Table 6: Debt dynamics

	average 2000-2003	2004		2005		2006		2007
	COM	COM	SP	COM	SP	COM	SP	SP
Government gross debt ratio	**53.9**	**55.7**	**56.3**	**58.0**	**58.1**	**58.4**	**58.6**	**58.3**
Change in debt ratio (1 = 2+3+4)	-2.3	1.7	2.2	2.2	1.8	0.4	0.5	-0.3
Contributions:								
- Primary balance (2)	**-2.5**	**0.0**	**0.1**	**-0.5**	**-0.3**	**-0.9**	**-0.7**	**-0.8**
- **"Snow-ball" effect** (3)	**0.6**	**1.6**	**1.7**	**1.6**	**1.7**	**1.1**	**0.6**	**0.4**
- Interest expenditure	3.3	2.9	2.9	2.9	2.9	3.0	2.8	2.7
- Real GDP growth	-0.7	-0.8	-0.7	-0.9	-0.8	-1.3	-1.4	-1.4
- Inflation (GDP deflator)	-2.1	-0.5	-0.5	-0.4	-0.4	-0.6	-0.8	-0.9
- Stock-flow adjustment (4)	**-0.3**	**0.0**	**0.4**	**1.1**	**0.4**	**0.3**	**0.6**	**0.1**
- Cash/accruals	0.1	-	-	-	-	-	-	-
- Accumulation of financial assets	-0.5	-	-	-	-	-	-	-
of which: Privatisation proceeds	-0.2	-	-0.3	-	-0.3	-	-	-
- Valuation effects & residual adj.	0.1	-	-	-	-	-	-	-

Note:

The change in the gross debt ratio can be decomposed as follows:

$$\frac{D_t}{Y_t} - \frac{D_{t-1}}{Y_{t-1}} = \frac{PD_t}{Y_t} + \left(\frac{D_{t-1}}{Y_{t-1}} * \frac{i_t - y_t}{1 + y_t} \right) + \frac{SF_t}{Y_t}$$

Sources: Stability programme November 2004 update (SP); Commission services autumn 2004 economic forecasts (COM); Commission services calculations

[12] In the period 2000-2003 overall stock-flow adjustments were negative on average, mainly due to privatisation receipts.

6. STRUCTURAL REFORM AND THE QUALITY OF PUBLIC FINANCES

Against the background of the deterioration in public finances and the ensuing corrective budgetary measures, the government is pursuing a far-reaching overhaul of the social security and pension systems. The rationale for the reforms is on the hand to secure budgetary savings and on the other to boost labour participation. Following up on action taken already in 2003 and encompassing several measures taken in the Spring of 2004, the 2005 budget specifies a series of far-reaching measures, although some of the original proposals were modified in the social agreement between the government and social partners that was reached on 5 November 2004 in the wake of massive protests by the trade unions in return for continued wage moderation. The reforms include tighter eligibility for unemployment benefits and an end to subsidies on low-paid labour. As of 2006 this would be followed by a number of other reforms (where some of the details of implementation still need to be filled in), notably the end of fiscal facilitation of early retirement and pre-pension schemes for those currently under 55, the introduction of a new disability scheme, and a fundamental overhaul of the health insurance system. The government also intends to reduce the administrative burden in order to free resources in the private sector. The mechanical calculations by CPB on a reduction of the administrative burden by 25% presented in the update suggest a sizeable positive effect on economic activity and employment. Of course, it needs to be ensured that the reporting burden is cut in areas where it would free up resources, while acknowledging that some of the reporting is actually necessary for good governance (e.g. the efficient, reliable and timely gathering of statistics) and thus positive to the economy.

On balance, the reforms should help improve the sustainability of Dutch public finances. However, in several areas, such as pension reform, child care and health care, doubts exist about the effectiveness of the proposed measures in terms of influencing the actual behaviour of economic agents. They may thus not achieve their intended aim, for instance of raising labour participation or limiting the use of medical facilities. Furthermore, while the central wage agreement will have a beneficial effect on profitability and external competitiveness in the near term, the longer-term gains are less clear-cut. In the Dutch case, more wage differentiation across sectors is called for to promote innovation and an efficient distribution of production factors.

According to the update expenditure on security, infrastructure and education helps structural strengthening of the economy. In this respect, it is relevant to note that the update expects a large drop in real expenditure on infrastructure in 2004 (mainly owing to the finalisation of major rail projects) and a weak increase by only ½% in 2005. As regards education and life-long learning, the multi-annual projections in the 2005 budget show that the volume of total public expenditure on education would decrease by 0.3% per year on average between 2005 and 2007.[13] The ratio of public health expenditure to GDP is projected to fall from 5.7% of GDP in 2004 to 5.3% in 2007. Moreover, available projections show that the positive budgetary impact of structural reforms which strengthen the growth potential of the economy, e.g. by boosting labour participation, will mainly be realised beyond the time horizon covered by the current update. By contrast, some of the savings measures that yield most net revenue in the near term do not seem optimal from a structural point of view. They may even have undesired side effects to the extent that they may hinder matching on the labour market and discourage career breaks for education and the care for young children (deemed beneficial to human capital formation). For instance, the increase in the two lowest income tax brackets in 2005 will partly reverse the reductions of marginal tax rates for low-to-medium incomes in past years (which promoted employment growth).

---

[13] The functional classification of collective expenditure in table 5.1 of the update encompasses only part of total spending on education; the volume changes shown in that table reflect mainly employment growth in education.

Finally, the absence of any reference to work of the Innovation Platform in the current update is surprising, to the extent that the previous update discussed at some length the launching of the Platform, underlining its importance. In 2004 the Innovation Platform has produced very little concrete results, on top of initiatives that were elaborated elsewhere in the civil service, and there is again no mention of how individual members could be held accountable in a meaningful way.[14]

7. THE SUSTAINABILITY OF THE PUBLIC FINANCES

The assessment of the sustainability of Dutch public finances is based on an overall judgement of the results of quantitative indicators and qualitative features. The quantitative indicators project debt development according to two different scenarios, to take into account budgetary developments over the medium term. The "programme" scenario (baseline) assumes that the medium-term objective set up in the programme is actually achieved, while the "2004" scenario assumes that the underlying primary balance remains throughout the programme period at the 2004 level.

The graph below presents the gross debt development according to the two different scenarios. On the basis of the programme and additional information provided by the EPC, age-related expenditure is foreseen to increase by 6.4% of GDP between 2008 and 2050 (see annex for a breakdown of different age-related expenditures). Gross debt is projected to remain broadly stable during the next decade. However, when the impact of ageing population on public expenditures kicks in, the debt dynamic becomes unfavourable.[15]

On the basis of the debt projections made under these assumptions, it is possible to calculate a set of sustainability indicators to measure the gap between the current policies and a sustainable one. The S1 indicator shows the permanent change in the primary balance in order to have a debt to GDP ratio in line with the Treaty reference value in the very long run (year 2050)[16]; S2 shows the gap between the current tax policies and those that would ensure respect of the intertemporal budget constraint given the future impact of ageing on public expenditure, namely the change in the tax ratio that would equate the present discounted value of future primary balances to the current stock of gross debt. According to the latter, in order to tackle the cost of ageing entirely through a budgetary strategy the Netherlands should increase its tax ratio permanently by around 2 percentage points, and more if it fails to consolidate as planned in the update.

In interpreting these results, several factors should be taken into account.

First, the effects of the reform of the pension system, ending tax advantages for pre-pension and early retirement as of 2006. This reform should help to enhance fiscal sustainability by limiting the fiscal costs of early retirement. That said, the actual improvement in public finances in the short run would be less than in the longer run. A long transition period is granted for all those who are currently 55 or older. Hence, there is the possibility that a large part of persons that are still eligible under the transitional arrangements will retire early. In addition, social partners might (partly) offset the intended impact of the reform on the actual retirement age even in the longer run through a faster accumulation of ordinary pension rights, where premiums would still be tax-exempt. This

---

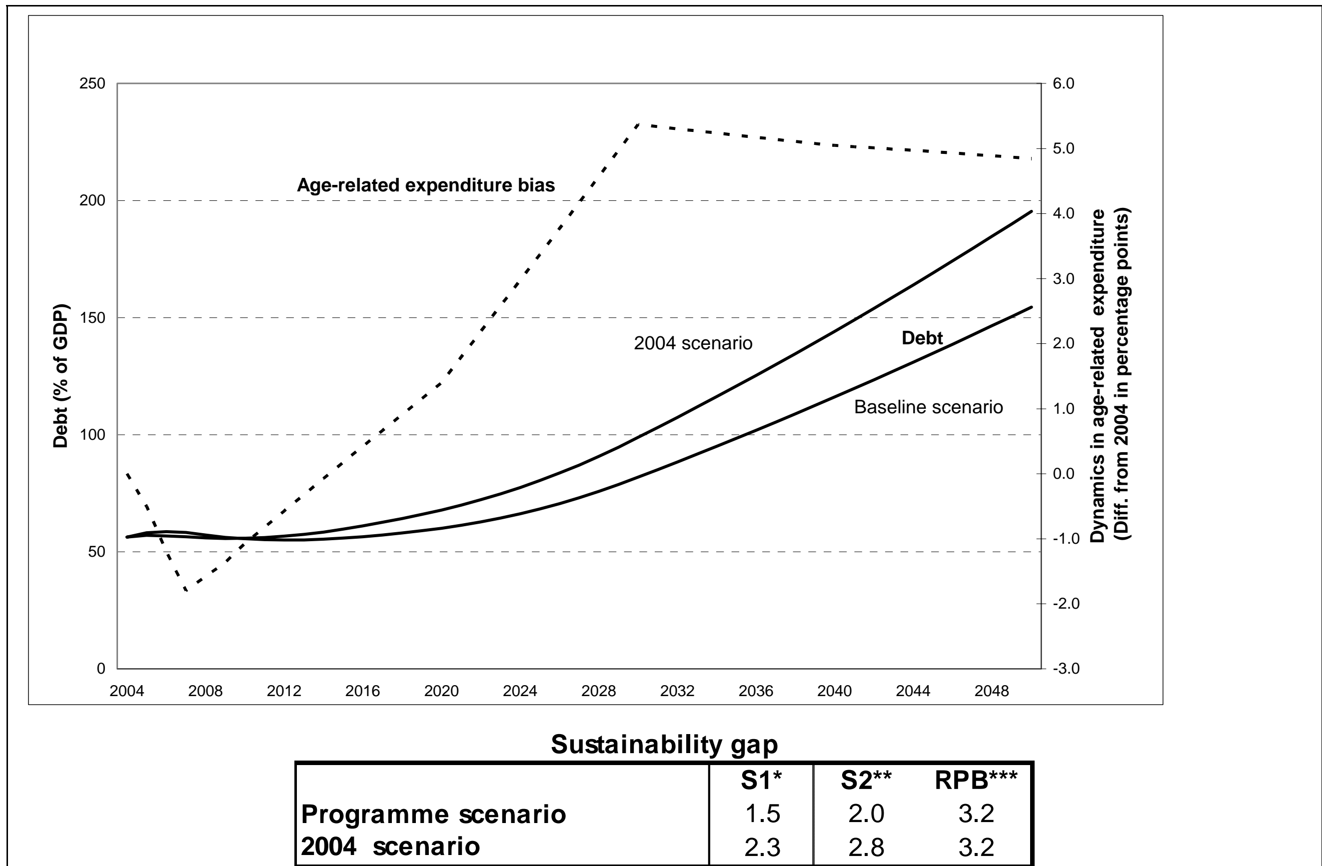
[14] It is striking that, it being founded in September 2003, the Platform took until 26 February 2004 to launch its own website.

[15] It should be recalled that, being a mechanical, partial equilibrium analysis, projections are in some cases bound to show highly accentuated profiles. As a consequence, the projected evolution of debt levels is not a forecast of likely outcomes and should not be taken at face value.

[16] The respect of the underlying debt path does not ensure sustainability over an infinite horizon, but only that debt remains below 60% up to 2050. In most cases, this would imply an increasing trend and possible unbalances after the end of the projection period.

could leave in place a high implicit tax on working until the statutory pension age, thereby not fully addressing the problem of low labour participation among persons over 55 years. Estimates of the part of the existing pre-pension premiums payments which might be relabelled as premiums for regular pension rights range from 75% (the maximum in a number of CPB estimates) and 15% (government estimates). To the extent that a larger part of pre-pension premiums would be relabelled as regular old-age pension contributions and life cycle savings than foreseen in the central scenario of the government, the budgetary savings would be less.

Figure 2: Long-term sustainability: summary results



Sustainability gap

	S1*	S2**	RPB***
Programme scenario	1.5	2.0	3.2
2004 scenario	2.3	2.8	3.2

Notes:

* It indicates the required change in tax revenues as a share of GDP over the projection period that guarantees to reach debt to GDP ratio of 60% of GDP in 2050.

** It indicates the required change in tax revenues as a share of GDP that guarantees the respect of the intertemporal budget constraint of the government, i.e., that equates the actualized flow of revenues and expenses over an infinite horizon to the debt as existing at the outset of the projection period.

*** Based on S2, the Required Primary Balance (RPB) indicates the average minimum required cyclically-adjusted primary balance as a share of GDP *over the first five years* of the projection period that guarantees the respect of the intertemporal budget constraint of the government for this period.

Second, to the extent that the reform of the disability scheme as of 2006 succeeds in reducing the number of people receiving disability benefits and boosting effective labour supply, this should help contain age related expenditure. The positive effect on public finances would be both direct, through lower benefit payments, and indirect, through higher employment and income tax receipts.

Third, limiting the increase in health expenditure is important. The new health care system to be implemented in 2006 (which is not specifically aimed at containing age related expenditures) aims at achieving this. Since important details of the reform still need to be filled in, the impact of the reform on public expenditure is difficult to assess at this juncture. Much will depend on the success

of the measures aimed at more competition among insures and consequent downward pressure on costs.

Fourth, the projections include an increase of tax revenues of around 3 percentage points of GDP between 2010 and 2050 due to the taxation of pension income. A recent advice of the Social Economic Council proposes to let pensioners with higher income also pay pension premiums, thus broadening the tax base and enhancing sustainability. To the extent that actual tax revenue from pension income should be different than currently projected, the risks to sustainability would change.

Finally, the projections shown above do not explicitly take into account the impact of the existence of a large funded second-pillar private pension system outside general government, with sizeable net assets.

Overall, the Netherlands still appears to be in a relatively favourable position with regard to long-term sustainability of the public finances. However, some risks clearly emerge on the basis of current policies. The results are broadly in line with the analysis presented in the programme, according to which a further improvement of the budget balance beyond the horizon covered by the update is required to ensure a sustainable evolution of debt.

* * *

Annex 1: Summary tables from the stability programme update

Table 1 Economic growth and related factors*

	Esa code	2003	2004	2005	2006	2007
GDP *growth* at *constant* market prices (7+8+9)	B1g	**-0.9**	**1¼**	**1½**	**2½**	**2½**
GDP *level* at *current* market prices	B1g	**454.3**	**464.5**	**475**	**494**	**514**
GDP deflator		**3.0**	**1**	**¾**	**1½**	**1½**
CPI		2.1	1¼	1¼	1½	1½
HICP		2.2	1¼	1¼	1½	1½
Compensation per employee, market sector		3.8	2½	½	2½	2½
Contractual wage rates, market sector		2.7	1½	¾	1½	1½
Labour productivity, market sector		0.8	3½	1¾	1¼	1½
Labour productivity, whole economy †		-0.3	2¼	1	-	-
Unit labour costs, manufacturing		3.5	-1½	-1¼	-	-
Employment (persons)		-0.5	-1	½	1½	1¼
Employment (% of working population)		**5.1**	**6½**	**7**	**6½**	**6¼**
Standardised unemployment rate		3.8	5¾	6¼	5¾	5½
Sources of growth: percentage changes at constant prices						
Private consumption expenditure	P3	**-0.9**	**¼**	**0**	**1¾**	**2**
Government consumption expenditure	P3	**1.8**	**½**	**½**	**1½**	**1½**
Gross fixed capital investment	P51	**-3.5**	**1¼**	**¾**	**2**	**2¼**
Change in inventories and net acquisition of valuables % of GDP	P52 + P53	**0.2**	**¼**	**¼**	**0**	**0**
Exports of goods and services	P6	**0.5**	**5**	**7½**	**5¾**	**5½**
Imports of goods and services	P7	**1.0**	**4**	**5¾**	**4½**	**4¾**
Contributions to GDP growth						
Final domestic demand (1+2+3)		**-0.5**	**¾**	**½**	**1½**	**1¾**
Change in inventories and net acquisition of valuables % of GDP (=4)	P52 + P53	**0.0**	**¼**	**¼**	**0**	**0**
External balance of goods and services (5-6)	B11	**-0.4**	**½**	**1**	**1**	**¾**

Note: Forecast growth rates in the update have been rounded to the nearest quarter of a percentage point

* For the years 2006 en 2007 the figures correspond to the medium-term projection prepared by the CPB in June 2003.

† Real GDP per employee.

Source: CPB Netherlands Bureau for Economic Policy Analysis.

Table 2 Development of public finances, 2003-2007

% of GDP	ESA Code	2003	2004	2005	2006	2007
	Net lending (B9) by sub-sectors					
General Government	S13	**-3.2**	**-3.0**	**-2.6**	**-2.1**	**-1.9**
Central government	S1311	**-2.6**	**-2.6**	**-2.3**	**-2.9**	**-3.0**
State Government	S1312					
Local government	S1313	**-0.6**	**-0.7**	**-0.5**	**-0.3**	**-0.2**
Social security funds	S1314	**-0.0**	**0.3**	**0.2**	**1.1**	**1.3**
	General government (S13)					
Total receipts	ESA	**45.3**	**45.0**	**44.9**	**44.6**	**44.1**
Total expenditures	ESA	**48.5**	**48.0**	**47.5**	**46.7**	**46.0**
Budget balance	B9	**-3.2**	**-3.0**	**-2.6**	**-2.1**	**-1.9**
Net interest payments		**2.9**	**2.9**	**2.9**	**2.8**	**2.7**
Primary balance		**-0.3**	**-0.1**	**0.3**	**0.7**	**0.8**
	Components of revenues					
Breakdown of public finances						
Taxes	D2+D5	24.9	24.4	24.8	24.7	24.3
Social insurance contributions	D61	14.5	14.6	13.9	13.9	13.9
Interest income	D41					
Other		5.9	6.0	6.2	6.0	5.9
Total receipts	ESA	45.3	45.0	44.9	44.6	44.1
	Breakdown of public expenditure					
Collective consumption	P32	17.8	17.7	17.5	17.2	16.9
Social transfers in kind	D63	8.5	8.3	8.0	8.1	8.2
Social transfers other then in kind	D62	12.7	12.9	12.7	12.7	12.2
Interest payments	D41	2.9	2.9	2.9	2.8	2.7
Subsidies	D3	1.7	1.5	1.5	1.4	1.4
Gross fixed capital formation	P51	3.2	3.2	3.1	3.1	3.1
Other		1.7	1.5	1.8	1.4	1.5
Total expenditures	ESA	48.5	48.0	47.5	46.7	46.0

[1] The EMU balance for 2000 does not include the proceeds from the auction of UMTS licences of 0.7% of GDP.

Table 3 Development of EMU debt, 2003-2007

% of GDP	ESA Code	2003	2004	2005	2006	2007
Gross debt level		**54.1**	**56.3**	**58.1**	**58.6**	**58.3**
Change in gross debt		**1.5**	**2.2**	**1.9**	**0.4**	**-0.2**
Contribution to decrease in debt ratio:						
Primary balance		**-0.3**	**-0.1**	**0.3**	**0.7**	**0.8**
Interest payments	**D41**	**2.9**	**2.9**	**2.9**	**2.8**	**2.7**
Nominal GDP growth	**B1g**	**-1.1**	**-1.2**	**-1.2**	**-2.3**	**-2.3**
Other		-0.7	0.3	0.5	0.6	0.3

Table 4 Cyclical developments, 2003-2007

% of GDP	**ESA Code**	**2003**	**2004**	**2005**	**2006**	**2007**
GDP growth at constant prices	**B1g**	**-0.9**	**1¼**	**1½**	**2½**	**2½**
Actual balance	**B9**	**-3.2**	**-3.0**	**-2.6**	**-2.1**	**-1.9**
Interest payments	**D41**	**2.9**	**2.9**	**2.9**	**2.8**	**2.7**

Note: Forecast growth rates in the update have been rounded to the nearest quarter of a percentage point

Table 5 Divergence from previous update

% of GDP	ESA Code	2002	2003	2004	2005	2006	2007
GDP growth	B1g						
Stability Programme update October 2003		**0.2**	**0**	**1**	**2 ½**	**n.a.**	**n.a.**
Stability Programme update November 2004		**0.6**	**-0.9**	**1¼**	**1½**	**n.a.**	**n.a.**
Difference		**0.4**	**-0.9**	**+ ¼**	**- 1**	**n.a.**	**n.a.**
Difference, cumulative since 2002 (in percentage points)		0.6	-0.3	-0.0	-1	n.a.	n.a.
Actual budget balance	B9						
Stability Programme update October 2003		**-1.6**	**-2.3**	**-2.3**	**-1.6**	**n.a.**	**n.a.**
Stability Programme update November 2004		**-1.9**	**-3.2**	**-3.0**	**-2.6**	**n.a.**	**n.a.**
Difference (in percentage points)		**-0.3**	**-0.9**	**-0.7**	**-1.0**	**n.a.**	**n.a.**
Gross debt levels							
Stability Programme update October 2003		52.4	54.0	54.5	53.7	**n.a.**	**n.a.**
Stability Programme update November 2004		**52.6**	**54.1**	**56.3**	**58.1**	**n.a.**	**n.a.**
Difference (in percentage points)		**0.2**	**0.1**	**1.8**	**4.4**	**n.a.**	**n.a.**

Note: Forecast growth rates in the update have been rounded to the nearest quarter of a percentage point

Annex 2: Long-term sustainability of public finances – quantitative scenarios for the Netherlands

Main assumptions - baseline scenario (as % GDP)	**2008**	**2010**	**2020**	**2030**	**2040**	**2050**	**changes**
Total age-related spending	24.3	24.8	27.3	31.2	30.9	30.7	6.4
Pensions	5.2	5.3	6.7	8.9	8.6	8.3	3.1
Health care	7.5	7.7	8.7	10.7	10.7	10.7	3.2
Education*	5.0	5.0	4.9	4.8	4.9	4.9	-0.1
Unemployment benefits	1.4	1.5	1.5	1.4	1.4	1.4	0.1
Others	5.2	5.2	5.3	5.3	5.3	5.4	0.2
*Total primary non age-related spending***	19.2						
Total revenues	45.0	45.3	46.4	48.8	48.6	48.4	3.4

* EPC projections

** constant

Results (as % GDP)	**2008**	**2010**	**2020**	**2030**	**2040**	**2050**	**changes**
Programme scenario							
Gross debt	57.1	55.6	60.0	81.9	116.1	154.5	97.4
i + 0.5*	57.4	56.4	64.1	90.6	132.3	181.7	124.3
2004 scenario							
Gross debt	56.0	55.8	67.9	98.9	144.2	195.4	139.4
i + 0.5*	56.2	56.6	72.1	108.4	162.6	227.1	170.8

* i + 0.5 represents the evolution of debt under the assumption of the nominal interest rate being 50 basis points higher throughout the projection period.