© 2004 International Monetary Fund

September 2004
IMF Country Report No. 04/300

Kingdom of the Netherlands—Netherlands: 2004 Article IV Consultation—Staff Report; Staff Statement; and Public Information Notice on the Executive Board Discussion

Under Article IV of the IMF's Articles of Agreement, the IMF holds bilateral discussions with members, usually every year. In the context of the 2004 Article IV consultation with the Kingdom of the Netherlands—Netherlands, the following documents have been released and are included in this package:

- the staff report for the 2004 Article IV consultation, prepared by a staff team of the IMF, following discussions that ended on **June 7, 2004,** with the officials of the Kingdom of the Netherlands—Netherlands on economic developments and policies. **Based on information available at the time of these discussions, the staff report was completed on July 21, 2004.** The views expressed in the staff report are those of the staff team and do not necessarily reflect the views of the Executive Board of the IMF.

- a staff statement of **September 8, 2004** updating information on recent developments.

- a Public Information Notice (PIN) summarizing the **views of the Executive Board as expressed during the September 8, 2004, Executive Board discussion** of the staff report that concluded the Article IV consultation.

The document listed below have been or will be separately released.

Selected Issues Paper

The policy of publication of staff reports and other documents allows for the deletion of market-sensitive information.

To assist the IMF in evaluating the publication policy, reader comments are invited and may be sent by e-mail to publicationpolicy@imf.org.

Copies of this report are available to the public from

International Monetary Fund • Publication Services
700 19th Street, N.W. • Washington, D.C. 20431
Telephone: (202) 623-7430 • Telefax: (202) 623-7201
E-mail: publications@imf.org • Internet: http://www.imf.org

Price: $15.00 a copy

International Monetary Fund
Washington, D.C.

INTERNATIONAL MONETARY FUND

KINGDOM OF THE NETHERLANDS—NETHERLANDS

Staff Report for the 2004 Article IV Consultation

Prepared by the Staff Representatives
for the 2004 Consultation with the Netherlands

Approved by Ajai Chopra and Michael T. Hadjimichael

July 21, 2004

The 2004 Article IV discussions were held in Amsterdam and The Hague during May 27–June 7, 2004, and included the conclusions and recommendations of the recent FSAP. The staff team comprised Messrs. Feldman (head), Bell, and Hofman, Ms. Zhou (all EUR), and Mr. Swinburne (MFD). It met with the Finance Minister, the Governor and other representatives of the central bank (DNB) and financial supervision, senior staff of several government ministries and agencies, including the Bureau for Economic Policy Analysis (CPB), the Competition Authority (NMa), and the head of the Social and Economic Council, representatives of labor unions and employer organizations, banking and pension fund economists, and academics.

After early elections in January 2003, a center right coalition government comprising the Christian Democrats, Liberals, and the center-left D66 took office in May 2003; its term is through 2007.

In concluding the 2003 Article IV consultation on July 30, 2003, Executive Directors expressed concern about the significant slowdown in economic activity since 2000 and the sharp deterioration in the fiscal position. While commending the government for taking measures to strengthen the public finances over the medium term, Directors identified raising the employment rate and carrying out further product market reform as key structural issues.

The quality of policies in the Netherlands has been favorably recognized by the Fund for some time. During the 1980s and 1990s, consistent with the Fund's emphasis on fiscal discipline and structural reforms, it was possible both to cut taxes and turn large fiscal deficits into surpluses as a result of tight control over public expenditures. At the same time, incentives to work were enhanced by labor market reforms; wage moderation was supported by cuts in taxes and social security contributions; competitiveness was thereby strengthened; unemployment fell sharply as the economy grew; and reforms in financial and other product markets reinforced these positive outcomes. However, the implementation of measures supported by the Fund in recent years to raise labor participation and productivity and consolidate the public finances have become all the more important in light of the depth of the recent economic slowdown and the accompanying deterioration in the fiscal position.

The Netherlands accepted the obligations under Article VIII and, apart from certain security restrictions, maintains an exchange system free of restrictions (Appendix I). It subscribes to the Fund's Special Data Dissemination Standard and data provision is timely and adequate for surveillance purposes (Appendix II).

The authorities released the mission's concluding statement and agreed to the publication of the staff report.

Contents Page

Executive Summary 4

I. Background 5

II. Report on the Policy Discussions 7
  A. Economic Performance and Near-Term Outlook 7
  B. Fiscal Policy 8
  C. Boosting Potential Growth..11
  D. Financial Sector Assessment...15
  E. International Trade and Development Assistance 16

III. Staff Appraisal 17

Text Box 1: FSAP: Summary of Key Recommendations...16

Figures
1. GDP, Unemployment and Inflation 21
2. Labor Costs and Employment...22
3. Competitiveness Indicators...23
4. Components of Expenditure 24
5. Developments in Asset Prices...25
6. Developments in Household Balance Sheets..26
7. Consumer Prices 27
8. Monetary Conditions 28
9. Cyclical Indicators 29
10. Labor Market Indicators..30

Tables
1. Basic Data 31
2. General Government Accounts...33
3. Indicators of External and Financial Vulnerability...34

Appendices
I. Fund Relations 35
II. Statistical Data Issues 36
III. Aging and the Public Finances in the Netherlands 38

Main Websites for Dutch Data

Data in this Staff Report reflects information received by July 7, 2004. In many cases more recent data can be obtained directly from the following internet sources:

Statistics Netherlands (CBS)... http://www.cbs.nl

The Netherlands Bank (DNB)... http://www.dnb.nl

Ministry of Finance.. http://www.minfin.nl

Bureau for Economic Policy Analysis (CPB)... http://www.cpb.nl

Additional information on Dutch economic statistics can be found at the Fund's SDDS website http://dsbb.imf.org/Applications/web/sddscountrycategorylist/?strcode=NLD and at the Statistics Netherlands Data Portal:
http://statline.cbs.nl/StatWeb/Start.asp?lp=Search/Search&LA=EN&DM=SLEN.

EXECUTIVE SUMMARY

Background and outlook: The economy is beginning to emerge from an extended downturn. Improving exports are driving the recovery, while domestic demand is expected to take longer to recover. Downside risks to the outlook for growth, especially from domestic sources, are a concern in the context of the nascent recovery. Meanwhile, against a background of soft labor market conditions and economic slack generally, inflationary pressures are low. With the general government balance deteriorating by almost 5½ percentage points of GDP between 2000 and 2003 and breaching the 3 percent Maastricht ceiling in the latter year, the authorities are determined to bring the deficit below 3 percent of GDP in 2004. Various structural reforms are in the works, but discord on certain plans has led to a marked cooling of the relationship between the government and social partners.

Policy discussions centered on the following key issues:

- The **fiscal policy stance** to nurture the emerging recovery while ensuring fiscal sustainability. Staff estimated that the 2004 deficit will narrow in underlying structural terms by 0.6 percentage point of GDP. This adjustment would strike an appropriate balance between the need to consolidate the public finances and avoid disruptions to the recovery. All agreed on the goal of sustaining fiscal consolidation in the medium term, with a view to preparing for aging and buttressing confidence.

- The **operations of the expenditure-based fiscal framework.** Among recent rule changes, one is aimed at avoiding the use of cyclical expenditure windfalls to fund permanent spending increases—as had happened in recent periods. Staff was supportive but preferred a stronger formulation of the expenditure rule to preclude new spending. Also, staff stressed that enhancing the transparency of the expenditure ceilings would facilitate their accessibility to a broader audience, adding an additional element of clarity and discipline to the system.

- With a view to the challenges of aging, the **need to boost potential growth by raising participation and productivity.** Important progress is being made: the authorities have planned a major overhaul of the disability scheme—a long-acknowledged haven of hidden unemployment—and the abolition of tax incentives for early retirement (both effective from 2006). While the mission welcomed these steps, it urged that reforms be undertaken in a comprehensive way—notably including the unemployment insurance scheme (where reform plans were more limited)—to avoid shifts from one category of inactivity into another. Staff also pointed to the potential benefits of reducing the minimum wage and increasing wage dispersion. The authorities acknowledged the economic reasoning behind these recommendations, but considered implementation politically difficult in light of a cultural preference for an egalitarian wage distribution.

- The **health of the financial system**. The FSAP found that, overall, the financial system is sound, resilient to adverse shocks, and well supervised.

I. BACKGROUND

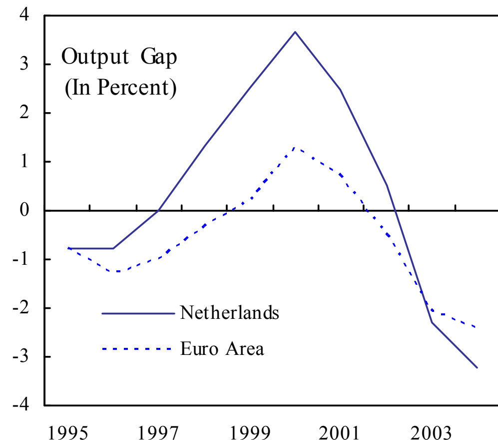
1. ***The Dutch economy has experienced a pronounced boom-and-bust cycle since the mid-1990s—with the boom accompanied by a build up of macroeconomic imbalances and a loss of competitiveness.*** Growth averaged 3.6 percent during 1995–2000, but then declined steadily to average only 0.2 percent during 2001–03; unemployment and inflation broadly mirrored this pattern, albeit with a lag (Table 1 and Figure 1). The comprehensive economic reforms that started in the 1980s helped lay the foundation for robust growth by raising incentives to work, expanding the labor force, and buttressing competitiveness. This contributed to buoyant export growth while capital spending expanded sharply. However, by the end of the 1990s, the economy was overheating: the unemployment rate fell below the estimated NAIRU of about 4 percent; and wage pressures—long pent-up under successive economy-wide wage-moderation agreements—surfaced in force in the late 1990s, fueling a significant bout of wage inflation (Figure 2). This put upward pressure on consumer prices (with inflation peaking at over 5 percent in 2001) and weakened external competitiveness—though trade shares have been fairly stable since the mid-1990s (Figure 3).

2. ***The unwinding of imbalances, along with a weakening external environment, contributed to the sharp slowdown of activity in recent years—with growth turning negative in 2003 for the first time in twenty years.*** Investment declined significantly as the rapid growth earlier was based on what now appears to have been unrealistic expectations of future economic growth (Figure 4). The collapse of equity prices (Figure 5) weakened corporate balance sheets, another factor dampening investment. Meanwhile, export growth fell off sharply as the impact of weak external demand was accentuated by the appreciation of the euro and especially the lagged effects of the rapid growth in wage costs. As wage growth moderated and social security contributions were increased, private consumption growth also fell and became negative in 2003, also reflecting uncertainties over pensions, future reforms, and employment prospects.

3. ***Wealth and policy effects amplified the cycle.*** Wealth effects were larger than in most other countries in the euro area, with the DNB estimating that asset and housing price increases added an average of 1–1½ percentage points to real GDP growth between 1998 and 2000. This was a key factor explaining the comparative resilience of Dutch private consumption through 2001. Meanwhile, the private sector became increasingly indebted (Figure 6). Rising housing prices, the low interest rate environment, and mortgage products which maximize tax write-offs by delaying principal repayments led to households raising their debt ratio from 109 percent of disposable income in 1995 to some 200 percent in 2002. On the policy front, the sensitivity of pension fund regulation to market conditions in assessing solvency, and the pension funds' exposure to equities, may have also amplified the cycle: contribution rates were cut during the stock market boom of the late 1990s, only to be

hiked during the bust in recent years.[1] This exacerbated the adverse effect on labor costs arising from the delayed response of wages to labor market conditions.[2] While the monetary stance is broadly appropriate for the Netherlands' at the current economic conjuncture, it was too loose through much of the late 1990s, contributing to the boom.[3]

4. ***Inflation is now tame, and there is little pressure from the wage front looking ahead***. In parallel with a widening output gap (text figure) and the slowing growth in wages and unit labor costs, year-on-year underlying inflation has declined rapidly with second-round effects of higher commodity prices not yet evident (Figure 7). Moreover, because of earlier rapid wage growth and related concerns about competitiveness, the social partners had agreed to a nominal wage freeze agreement for 2004 and 2005—tied to the government softening or postponing reforms to disability and unemployment benefits and early retirement. While agreement for 2005 has now collapsed because of discord on some aspects of these reforms (discussed later), the appreciated euro, generally subdued pace of economic activity, and slack labor market conditions are expected by the Dutch authorities and staff to keep a lid on price and wage pressures. The latter will have favorable effects on competitiveness.



5. ***The fiscal balance deteriorated markedly.*** Between 2000 and 2003, the general government balance worsened by almost 5½ percentage points of GDP as a result of both cyclical and structural effects (Table 2). Structural effects—amounting to roughly 2 percentage points of GDP—included the 2001 tax reform and increases in health care and education spending. The deficit in 2003 was larger than the initial target of 2.3 percent of GDP and ended up breaching the 3 percent Maastricht ceiling. Slower-than-expected growth reduced revenue and, after years of running close to balance, the local governments

---

[1] Average contribution rates were increased by 4 percentage points from 2001 to 2004, to some 14 percent.

[2] While delivering wage moderation on average, the Dutch wage bargaining system has tended to react sluggishly to changes in economic circumstances. This was analyzed in *Wage Bargaining in the Netherlands* (IMF Country Paper No. 03/240).

[3] Compared with current Taylor-rule estimates of a broadly appropriate monetary stance for the Netherlands, the OECD estimates that short-term interest rates in the late 1990s were 3 percentage points lower than indicated by a Taylor-rule relationship.

surprisingly recorded a deficit of 0.6 percent of GDP in 2003. In addition, although the spending ceilings were met through 2002, temporary expenditure windfalls were used to fund permanent increases in other spending. As a result, in the new coalition agreement in 2003, there was a modest ratcheting up of the ceiling, which was also exceeded by a small margin.

II. REPORT ON THE POLICY DISCUSSIONS

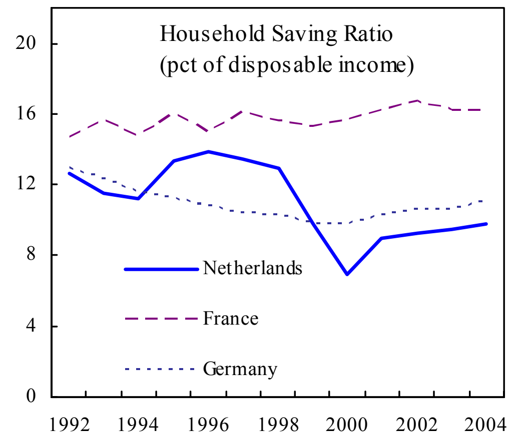
6. ***Discussions focused on the key short- and medium-term challenges of nurturing the emerging recovery and enhancing prospects for growth and fiscal sustainability in the face of an aging population***. While fiscal policy needs to be well anchored in a convincing medium-term framework to bolster confidence, an important near-term issue, in light of short-run fragilities, was striking the right balance between needed fiscal adjustment on the one hand and avoiding disruptions to the recovery on the other. All agreed on the longer-term benefits of raising both the labor participation rate and productivity. Decisively implementing reforms to achieve these objectives would be mutually reinforcing in creating employment, enhancing competitiveness, boosting potential growth, and achieving fiscal saving to ensure adequate resources for an aging population. The authorities, as described below, are in fact moving ahead with important reforms, though political resistance is a damper to the more extensive efforts recommended by staff.

A. Economic Performance and Near-Term Outlook

7. ***There was consensus that the long-awaited recovery is now in train—but with slow growth expected at least through the current year.*** Staff projected growth of about 1 percent in 2004 and about 1¾ percent in 2005. The latest growth projections (released after the mission) of the CPB and the DNB appear somewhat wide ranging: the central bank forecasts ¾ and 2 percent, respectively, for 2004 and 2005; the CPB 1¼ percent for both years. The difference mainly reflects diverging views on the strength of private consumption. In all the projections, improving exports, with needed support from continued wage moderation, were seen as the main driver—contributing to a gradual pickup in investment.[4] Moreover, macroeconomic policy settings were considered appropriate: notwithstanding fiscal tightening (see below), the ECB policy rate (Figure 8) was seen as broadly in line with the requirements of the Dutch economy (being, as noted before, Taylor-rule consistent).

8. ***Various uncertainties to the outlook were acknowledged, with staff emphasizing downside risks.*** In the staff's view, downside risks from domestic fragilities were especially pronounced. In particular, staff pointed to households' exposure to income and interest rate risk, noting that a combination of faster-than-expected increases in interest rates and unemployment could trigger a drop in housing prices. More generally, with weak near-term

[4] Staff projects export growth to be somewhat below and then in line with market growth (from the WEO exercise) in 2004 and 2005, respectively.



growth unlikely to make a significant dent in still rising unemployment, even modest changes to the wage and employment outlook could prompt a reassessment of income prospects and therefore consumption plans. All these factors were accentuated by high household debt, which may yet result in a renewed increase in household savings. The authorities considered their projections sufficiently conservative to be subject to both downside and upside risks, indicating that mitigating factors like the dominance of fixed interest mortgages and the generally limited housing supply cushioned the effects of high debt levels. The possibility of a stronger-than-expected external recovery was also recognized, with the authorities additionally indicating that investment could surprise on the upside because of this and if business confidence were to remain buoyant (Figure 9). Nevertheless, the authorities concurred that even if upside and downside events were about evenly balanced, the potential impact of the downside was relatively larger in magnitude and a matter of concern.

B. Fiscal Policy

9. ***The authorities have taken a series of measures to comply with the 3 percent Maastricht ceiling in the current year*** (text table). These included various packages to try to bring the 2004 deficit from an estimated 3.8 percent of GDP at the time of the budget was published (in September 2003) to 2.3 percent. However, as shown in the table and discussed in ¶5, the outturn for 2003 (a deficit of 3.2 percent) was worse than envisaged when the 2004 budget was prepared. This, along with slower-than-expected growth in 2004, resulted in a revised projection for the 2004 deficit (of 3.4 percent). Thus, additional measures were taken in the 2004 spring budget memorandum to just meet the 3 percent ceiling. Overall, measures of close to 2 percent of GDP barely stabilize the deficit at the 3 percent ceiling. The measures do lead to a ½ percent of GDP narrowing of the structural deficit. The balance is taken up by a ½ percent of cyclical weakening and 1 percent of structural weakening (health care, local authority spending, and shortfalls in corporate tax receipts). The staff viewed the correction of the structural deficit as striking an appropriate balance between the need to consolidate the public finances and avoid disruptions to the recovery.

Budget Balance of the General Government, 2003-04
(In percent of GDP)

	2003	2004
Baseline projections in the 2004 Budget Memorandum, without policy measures	-2.3	-3.8
Total 2004 policy measures 1/		1.5
Measures in Strategic Accord		0.6
Measures in Global Agreement		0.6
Supplementary measures in 2004 Budget		0.3
Baseline projections in the 2004 Budget Memorandum, with policy measures	-2.3	-2.3
Revisions (in April 2004) to the 2003 outcome and 2004 projection	-3.2	-3.4
Additional measures in the 2004 Spring Budget Memorandum 2/		0.4
EMU balance, with additional policy measures		under -3.0

Sources: The Dutch Ministry of Finance.

1/ Includes structural spending measures (for example, a public-sector wage freeze, a nominal freeze of benefits, and the introduction of health care deductibles) and modest revenue increases (for example, by keeping the gas surcharge and increasing health care premiums).

2/ Includes structural measures (equivalent to 0.2 percent of GDP), comprising increased health care and disability premiums, streamlined health care benefits, and lower construction costs through more competitive bidding; and second-round effects.

10. ***The authorities are addressing certain risks to the execution of the 2004 budget***. They explained that they were caught off guard by the deterioration in the local authorities' overall fiscal balance. To better coordinate the execution of the central and local governments' budgets in 2004, they have established regular contacts with large municipalities, especially on their net lending activities (mostly related to net purchases of land). Staff noted that the large rises in health care spending amid a shift to a more demand-driven system raised other concerns. In addition to recent measures to contain health care costs (for instance, benchmarking and higher co-payments), staff therefore also welcomed the suggestion in last year's coalition agreement to consider reimposing direct budgetary controls on health care spending if necessary.

11. ***With a view to bolstering confidence and taking advantage of the cyclical upturn to prepare for the cost of aging, there is a need for sustained fiscal consolidation in the medium term.*** In this context, the authorities had stipulated in the initial 2004 budget that the structural deficit should not exceed 0.5 percent of GDP in 2007 and targeted cumulative underlying adjustment of 0.7 percentage point of GDP between 2003 and 2007. Measures included modest base-broadening tax policies, a cut of 10,000 civil servants, a general cut in subsidies, a reduction in the coverage of the basic public healthcare package, and compulsory private health insurance starting in 2006. While the fiscal position has worsened since the budget was prepared, the government has not yet revised its target. Staff, for its part, advocated structural adjustment of at least 0.5 percentage point of GDP per year through the government's term (2007), also with a view to the longer-term aspects of aging (see ¶12). This would imply aiming for about structural balance by the end of the current government's term in 2007 and a limit of about 1 percent on the average growth of real primary expenditure

during 2003–07, compared with actual average growth of 3.2 percent in the four years to 2003.[5] In identifying additional measures, staff encouraged the authorities to consider areas that would improve incentives for work and offer complementarities to product and labor market reforms, including through the tax-benefits system and phasing out mortgage interest deductions over the medium term, which could also limit rent subsidies.

12. ***The authorities' fiscal strategy on aging for the medium and longer term entails running down debt to use the saving on interest payments to cover higher aging costs.*** Appendix III presents long-term debt and fiscal sustainability scenarios in the context of this and other strategies, finding the situation is manageable but requires sustained fiscal adjustment.

13. ***The discussions turned to the operations of the fiscal framework and possible avenues to help secure continued adjustment, anchored by the medium-term expenditure ceilings.***[6]

- The authorities pointed to recent improvements: the decision, welcomed by staff, to devote revenue windfalls solely to debt reduction, thus avoiding a procyclical bias from the past; and the intention that cyclical expenditure windfalls (related, for example, to unemployment and other social spending) will not be used to fund spending on other items without further consideration. While recognizing the difficulty in determining whether spending windfalls are cyclical, staff preferred a stronger formulation of the latter to preclude new spending.

- With a view to reinforcing fiscal discipline, staff also supported the authorities' renewed intention of not allowing reallocation across the spending subceilings—an approach that has not been followed consistently in practice as below-ceiling expenditure in one category has been used to accommodate overspending in another.

- Staff considered that enhancing the transparency of the ceilings would facilitate their accessibility to a broader audience, adding an additional element of clarity and discipline to the system. In this regard, staff saw merit in aligning the spending ceilings more closely with national accounts concepts, and focusing the ceilings solely on spending by discontinuing the practice of treating nontax revenues as negative expenditures. More transparent and accessible ceilings would also help in communicating policy, with the potential advantage of

---

[5] While such an expenditure limit would be tough, it would be less stringent than might first appear because it rebases to the high growth of preceding years.

[6] An accompanying selected issues paper on fiscal policy analyses the fiscal framework in more detail.

enhancing confidence.[7] The authorities saw staff recommendations on the latter point as worthy of further consideration. It was also noted that significant revisions to the system would best be made every four years when a new government sets out to explain its fiscal policy intentions.

- Wide-ranging health sector reforms, to be introduced in 2006, carry the prospect of greater choice and efficiency in meeting the needs of patients. However, in light of the uncertainties over how resource demands will evolve in practice and the experience with overruns in the past, staff was of the view that cost control may continue to be a budgetary issue. There was general agreement on the need to reduce reporting lags in the health sector, with the authorities indicating that efforts were already underway in this connection.

C. Boosting Potential Growth

14. ***Fiscal consolidation aside, meeting the challenges of looming population aging would be helped by boosting potential growth.*** The authorities and the staff agreed that recent growth performance was weighed down by low participation of specific groups in the Dutch labor market as well as a secular decline in productivity growth.

Raising labor market participation

15. ***While low participation has been persistent for particular groups, some proposed reforms are stretching the limits of the "polder" model of social consensus.*** The tight labor market of the late 1990s and its attendant adverse implications for competitiveness highlight the importance of boosting labor supply. Participation is especially low among older, partially disabled, and low-skilled workers, and the authorities and staff viewed policies related to disability and sickness benefits, early retirement, and inactivity traps as particularly relevant. Administrative aspects of benefits systems were also seen as important. In this regard, the authorities reported on the success of the recent decentralization, which reduced inflows into welfare, as an encouraging illustration of the potential gains from setting the right incentives.[8] Most government officials and staff also agreed on the merits of undertaking reforms in a comprehensive way, notably including the unemployment insurance scheme, to avoid the risk of shifts from one category of inactivity to another. However, initiating such reform is already proving difficult in the context of the consensus-oriented policy model: the debate within

---

[7] For example, there was concern that the string of deficit-reducing spending measures enacted over the last two years could be misinterpreted as an over tightening of policy. The interpretation would more likely be in line with policy intentions when seen as responding to an initial loosening and bringing spending back within rising expenditure under the pre-set ceilings.

[8] These included incentives to favor reintegration into the labor force over welfare benefits as municipalities could keep unused funds from their social welfare budget.

government on reforming unemployment insurance is still ongoing; and, following recent discussions on the reform of early retirement, the government's relationship with the social partners has cooled to the point that the labor unions have withdrawn from their commitment to a wage freeze in 2005.

16. ***The government is moving ahead with the removal of fiscal incentives for early retirement.*** In addition to making participation in collective early retirement schemes voluntary, the government intends to implement its original plan to fully abolish the tax deductibility of early retirement savings and has announced its intention to suspend the administrative extension to unorganized firms of those parts of wage contracts that require participation in early retirement schemes. While staff saw the changes as fostering greater intergenerational and actuarial fairness in early retirement arrangements, these plans had caused major upset with the trade unions, who saw disadvantages for older workers.[9] In a broader context, the mission suggested that the official retirement age (currently 65, with the effective retirement age around 61 years) take into account changes in life expectancy (Figure 10).

17. ***Disability is a long-acknowledged haven of hidden unemployment and the sheer size of current disability schemes underscores the urgency of implementing reform plans.*** Disability schemes harbor close to one million beneficiaries, equivalent to about 13 percent of employment. The authorities considered that some partial reforms over the last few years (for example, the introduction of a gatekeeper function and so-called experience-rated insurance premia based on firms' existing participation in disability schemes) had contributed to the recent decline in new applicants. They were also planning a more sweeping overhaul, which aims to restrict access only to the fully disabled while introducing stricter criteria and examinations. For the partially disabled, incentives to work would be substantially strengthened, to foster their reintegration into the workforce.[10] The mission welcomed these plans, stressing that in addition to durably and significantly reducing new inflows, it would be important to rigorously reassess the existing stock of cases on the basis of the new criteria as planned.

18. ***The authorities have plans to further limit the generosity of unemployment benefits.*** They have phased out the so-called follow-up unemployment benefit. This benefit

---

[9] Collective early retirement schemes are more costly for younger workers because contributions are paid over a longer period and assessed at a flat percentage rate of the individual wage.

[10] Under the new scheme, partially disabled who work would be entitled to a wage subsidy bridging 70 percent of the difference between the old and new wage. By comparison, when unemployed, the partially disabled would receive regular unemployment benefits and, after a time, welfare.

had added another 2½ years to the (up to) 5 years of main benefits available and thereby had acted as a channel to effectively retire at 57½ years of age. In addition, the authorities plan to eliminate short-term benefits and tighten the eligibility requirements for the main unemployment benefits. Staff encouraged the authorities to follow through with these plans. However, it noted that further reform—in particular with respect to the relatively long duration of the main unemployment benefits—would be beneficial.[11] While further buttressing incentives to work, such action would also tend to diminish the risk that a tightening of other social security arrangements would result in a rise in applications for unemployment benefits.

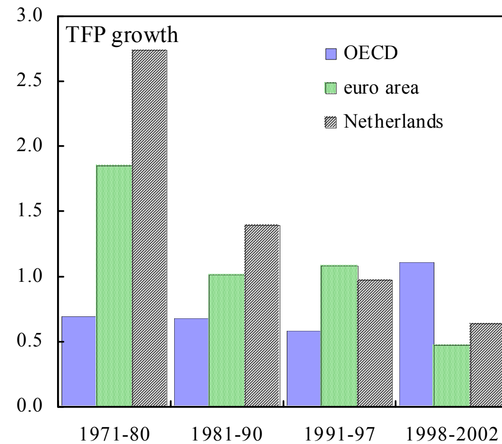
19. ***Female participation is high, though associated with a large share of part-time work.*** Workers are legally entitled to work part time with regular benefits and staff asked whether, in the presence of fixed labor costs, such arrangements elevated the overall cost of labor. The authorities, and various employers with whom staff talked, felt that part-time arrangements were working very well. However, to raise hours worked, the authorities stressed the need to strengthen certain incentives, notably through better and more available childcare.

20. ***High replacement rates and means-tested benefits imply significant inactivity traps at the lower end of the wage scale.*** To reduce inactivity traps, the authorities are gradually increasing the earned-income tax credit. However, in light of the associated high budgetary costs and the still high (effective) marginal tax rates for low-wage earners who take a job, staff suggested further measures, including a redesign of rent subsidies. Staff also pointed to the potential benefits of lowering the minimum wage, which forms both the basis for determining the level of several social benefits and directly limits labor demand at lower skill levels. In particular, the mission argued that lowering inactivity traps and stimulating not only labor supply but also the demand for low-skilled labor would seem particularly relevant in the context of an aging population and the likely associated increase in demand for personal services. The authorities noted the complex economic and political aspects of such a comprehensive reform package and highlighted their plans to abolish certain local benefits for specific groups as an area where there already was political consensus and administrative capacity for substantial reform.

[11] This is consistent with recent research by Coles and Masters (2004), "Duration-Dependent Unemployment Insurance Payments and Equilibrium Unemployment," *Economica*, Vol. 71, who demonstrate adverse effects from a longer duration of unemployment benefits, even if the overall generosity of unemployment insurance stays unchanged.

Reversing the decline in productivity growth

21. ***In addition to raising participation, potential growth would be enhanced by an acceleration of productivity growth***. While the exact extent of the slowdown in productivity growth is difficult to measure and the overall level of productivity is comparatively high,[12] the authorities and the staff agreed that reversing the secular decline in productivity growth would be an important element in lifting the economy's capacity to cope with population aging.



- With a view to recommending policies that would boost innovation, productivity, and growth, the authorities have established the high-level "Innovation Platform" under chairmanship of the Prime Minister. The mission suggested that an important item on the agenda should be the removal of obstacles to a quicker reallocation of resources into innovating sectors. In this context, the mission welcomed the authorities' stepped-up effort to reduce the administrative burden and supported their intention to extend the focus of this effort to revising the specific content of regulations.

- The mission also suggested that focus be placed on labor markets where liberalization efforts have in general lagged behind product market reform. Employment protection is still at a comparatively high level, hinders flexibility, and serves as an implicit tax on new hiring. Greater wage differentiation would, among other things, open a channel to realizing returns from investment in human capital—a relevant complement to the government's attempts to raise the importance of private financing of higher education. It would also be helpful in attracting labor to higher productivity companies and sectors.

- While the authorities appreciated the reasoning behind these suggestions, implementation was considered politically difficult, with traditional preferences for an egalitarian wage distribution running counter to introducing greater wage differentiation.

---

[12] An accompanying selected issues paper analyzes productivity developments in detail. Among its findings are that productivity growth tends to be particularly low in heavily protected sectors. The paper also notes evidence that Dutch companies engage in less risky experimentation than, say, U.S. firms, which in turn may affect innovation and reflect the regulatory burden in the Netherlands.

22. ***The benefits from further improvements in the functioning of product markets were also discussed***. The staff and the authorities considered the Netherlands as being at the forefront of product market reforms in Europe, including through the comprehensive opening of most network sectors. Nevertheless, some sectors, for example construction and nontraded services, have remained protected while also recording particularly weak productivity growth. Against this background, the recently established competition agency (NMa) has quickly gained credibility and begun to focus its enforcement efforts on these sectors. In addition, the authorities saw benefits in persevering with efforts to open new avenues for competition in markets with strong existing incumbents. Examples included the approval of new electricity generation facilities and international transmission lines, and efforts to unbundle network transmission and production. To further improve NMa's effectiveness, staff supported proposals to strengthen the agency's powers to investigate and its ability to impose penalties, including, importantly, on individuals within companies rather than just the companies themselves. Against a backdrop of recent corporate scandals, an improved corporate governance framework has been introduced and is expected to be adopted in legislation soon (the so-called Tabaksblat code).

D. Financial Sector Assessment

23. ***Overall, the financial system is sound, resilient to potential adverse shocks, and well supervised***. The Dutch financial system is dominated by a small number of large complex financial institutions (LCFIs) which are sectorally integrated—offering, for example, both banking and insurance services—and internationally oriented. The FSAP found that the banking sector is well capitalized and diversified, with asset quality and profitability holding up relatively well in the recent slowdown. Potential risks from high debt levels and house prices, or from the international environment, appear comfortably within the capacity of the banks to manage them. Indeed, the authorities noted that the prospect of a steeper yield curve would tend to favor banks on balance, given the factors mitigating the effects of higher rates on local borrowers. While insurance companies and especially pension funds remain exposed to any significant fall of equity prices, they have remained reasonably liquid and are now in a rebuilding phase, underpinned by firm supervisory action.

24. ***The FSAP appraised pending financial supervision legislation and made recommendations to help preserve long-term financial stability.*** A significant overhaul of legislation is underway, with a view to further strengthening the domestic supervisory regime and formalizing the organizational restructuring of supervision on a sectorally-integrated basis. The authorities confirmed that the preparatory work is well in hand. Staff welcomed the planned legislation, which is particularly appropriate given the challenges arising from the local systemic importance of LCFIs and the substantial international character of their activities, which places an added premium on supervisory coordination across sectors and borders. The most important recommendations are summarized in Box 1. The authorities broadly concurred with the recommendations. They noted that some measures had already been taken to limit mortgage interest tax deductibility, but that a further phasing out, notwithstanding potential benefits, would be a challenge politically.

Box 1: FSAP: Summary of Key Recommendations 1/

- Spelling out clearly the role of the Minister or Ministry of Finance, as applicable, in those few areas where autonomy is not fully delegated to the supervisor.
- Ensuring that the Authority for Financial Markets has the power to cooperate with securities supervisors internationally even when there is no "domestic interest."
- Continuing to work with cross-border counterparts to further improve securities settlement arrangements.
- Ensuring that the new pensions supervisory arrangements allow sufficient flexibility in the specified timeframe for making up shortfalls in the coverage ratio, to prevent procyclical effects, but without allowing unduly prolonged adjustment.
- Continuing the development of the framework for dealing with crisis situations, both through further work with other supervisors internationally, and through completing the review of the domestic deposit guarantee scheme.
- Continuing the development of macro prudential surveillance to help strengthen the early identification of risks and vulnerabilities.
- Over the medium term, phasing out tax deductibility of mortgage interest, preferably in a gradual fashion to avoid disruptive effects.

1/ More detail on the findings and recommendations is contained in the accompanying Financial System Stability Assessment (FSSA).

E. International Trade and Development Assistance

25. ***The Netherlands has a solid track record in supporting multilateral trade liberalization and meeting the U.N. target for Official Development Assistance (ODA)***. The authorities welcomed the increased stature of middle- and low-income countries in multilateral trade negotiations—noting that improving these countries' negotiation capacities has been an area for Dutch technical assistance. Concerning the Doha round, the authorities still saw a window (albeit small) for concluding negotiations in the current year on the coattails of the EU's initiative on agricultural trade liberalization. Moreover, as a large exporter of high-value agricultural goods, they felt the Netherlands could compete well in a more liberalized agricultural trading system. Notwithstanding the difficult budgetary situation as of late and the need to consolidate the public finances, the Netherlands has consistently exceeded the ODA target of 0.7 percent of GNP.

III. Staff Appraisal

26. ***While the Netherlands' success in the 1980s and 1990s demonstrated the virtues of strong policies, the sudden and sharp reversal of economic fortunes since the beginning of the decade is now dominating the economic policy debate.*** Annual growth has declined steadily since 2000, while an aging population and decline in productivity growth have raised concerns about falling potential growth looking ahead. Meanwhile, the public finances weakened significantly during 2000–03, for structural as well as cyclical reasons. And the fiscal deficit breached the 3 percent Maastricht ceiling in 2003. The depth of the recent economic slowdown and deterioration in the fiscal position underscore the need for fiscal consolidation and structural reform.

27. ***The authorities have begun to deal with fundamental issues to ensure a healthy economy, but more actions are required.*** Structural reforms to raise both labor participation and productivity are key to boosting longer-term economic prospects and are in the works. These reforms will also help to deal with the challenges of population aging, as will the fiscal adjustment initiated by the authorities. However, stronger and more concrete medium-term fiscal consolidation plans and structural reform are needed.

28. ***The government's determination to hold the 2004 fiscal deficit to just under 3 percent of GDP is commendable and fits well with economic circumstances.*** While some of the structural weaknesses in spending might have been guarded against, the budget has clearly been hit by shocks that would have been difficult to foresee. Against this background, the authorities' determination to offset these structural weaknesses was appropriate. Looking forward, a recovery is expected but growth is projected to be slow through this year and downside risks, especially from domestic sources, are a concern. In this context, fiscal policy strikes the right balance between needed fiscal adjustment on the one hand and the confidence effects this would engender, and avoiding excessive tightening and associated disruptions to the recovery on the other. Moreover, based on announced measures, the deficit target seems achievable. However, risks stem in particular from health care costs and the budget situation of the local governments. Closer cooperation between the central and local governments should help keep the deficit of local governments in check. Recent measures to contain health care costs—through, for example, benchmarking and higher co-payments—are also welcome, but the suggestion in the coalition agreement to reimpose direct budgetary controls may still be needed.

29. ***Continued fiscal adjustment is essential and the authorities should adopt ambitious medium-term fiscal targets that ensure fiscal sustainability and deal with the impact of population aging.*** The broad outline of the authorities' strategy of using debt reduction to save on interest payments to cover the cost of aging is sensible. However, the fiscal slippage over the last few years, including structural expenditure increases, and the upward revision to future health care costs since the strategy was articulated, clearly call for more determined efforts to ensure fiscal adjustment over the medium term. Structural fiscal adjustment of at least ½ percentage point of GDP per year through the government's term would take

advantage of the cyclical upturn to prepare for the cost of aging while also being sufficiently ambitious to bolster confidence. Thus, even with the budget deficit below the 3 percent ceiling, it is important to be diligent in pursuing continued underlying consolidation of the public finances. In identifying measures, the authorities are encouraged to consider a gradual phasing out of mortgage interest deductions and areas that would improve incentives for work, including the tax-benefits system. Structural reforms to raise labor productivity and participation would also help to deal with the costs from aging.

30. ***The multi-year fiscal framework, anchored on medium-term expenditure ceilings, is an important instrument for securing fiscal adjustment over time.*** Thus, recent efforts to strengthen the framework are commendable. These include the authorities' decision to devote revenue windfalls solely to debt reduction, thus avoiding a pro-cyclical bias. Their rule to not use cyclical expenditure windfalls to fund spending on other items without further consideration is another move in the right direction, but should, in practice, be strengthened to preclude new spending. Fiscal consolidation would also be supported by avoiding the past practice of allowing over performance under one subceiling to raise spending under another. Thus, the authorities need to follow through with their renewed intention of avoid such reallocations. While wide-ranging health sector reforms, to be introduced in 2006, carry the prospect of greater choice and efficiency in meeting the needs of patients, cost control may continue to be a budgetary issue. Consequently, further budgetary safeguards could be needed. Finally, enhancing the transparency of the expenditure ceilings would facilitate their accessibility to a broader audience, adding additional clarity and discipline to the system, while helping in communicating policy and reinforcing confidence.

31. ***Decisive implementation of structural reforms to raise labor participation and productivity would be mutually reinforcing.*** This would be the case, in particular, in creating employment, enhancing economic growth, boosting competitiveness, and achieving fiscal savings to ensure adequate resources for an aging population. Without significant action in these areas, the kind of support that society would like to provide to an aging population may simply not be possible without unduly burdening future generations.

32. ***While the authorities have initiated important reforms to raise participation, a more comprehensive approach would be beneficial.*** The authorities' determination to reform existing disability schemes is welcome in light of the excessive number of participants, and it is essential to follow through with plans to restrict access to the fully disabled, use stricter criteria and examinations, strengthen work incentives for the partially disabled with a view to reintegrating them into the workforce, and rigorously reassess existing cases on the basis of the new criteria. Plans to remove fiscal incentives for early retirement are another important step to foster higher labor participation. However, to avoid shifts from one category of inactivity to another, reforms should be done in a comprehensive way, to include especially further reducing the generosity of unemployment benefits. Both the demand for and supply of low-skilled labor would be increased by lowering the minimum wage and addressing inactivity traps. The latter includes reforming the benefits and tax system with a view to making work pay. In addition, the recent decentralization of the

provision of welfare benefits highlights the potential gains from setting incentives right and underscores the importance of how benefits systems are administered. In determining the retirement age, the authorities are encouraged to take into account changes in life expectancy.

33. ***In addition to boosting participation, raising the economy's potential will require an acceleration of productivity growth.*** While the overall level of productivity is comparatively high, its growth rate has slowed considerably in recent years. It is therefore encouraging that the government has embraced the challenge of boosting productivity growth through establishing a high-level "Innovation Platform," while stepped-up efforts to reduce the administrative burden, including by revising the content of regulations, are clearly very helpful in this regard. Nevertheless, more needs to be done to facilitate resource reallocation. Employment protection is still at a comparatively high level, hindering flexibility and implicitly taxing new hiring. Greater wage differentiation would, among other things, be helpful in attracting labor to higher productivity companies and sectors and in opening a channel to realizing returns from investment in human capital—a relevant complement to the government's attempts to raise the importance of private financing of higher education.

34. ***While the Netherlands has been at the forefront of product market reform in Europe, some nontradable sectors have remained protected and their productivity record has been particularly weak.*** Against this background, the recent enforcement efforts of the competition agency are welcome. However, that agency's effectiveness could be improved further by broadening and strengthening its powers to investigate and impose penalties. Regulators should also persevere with efforts to open new avenues for competition in markets with strong existing incumbents. The introduction of an improved corporate governance framework is welcome.

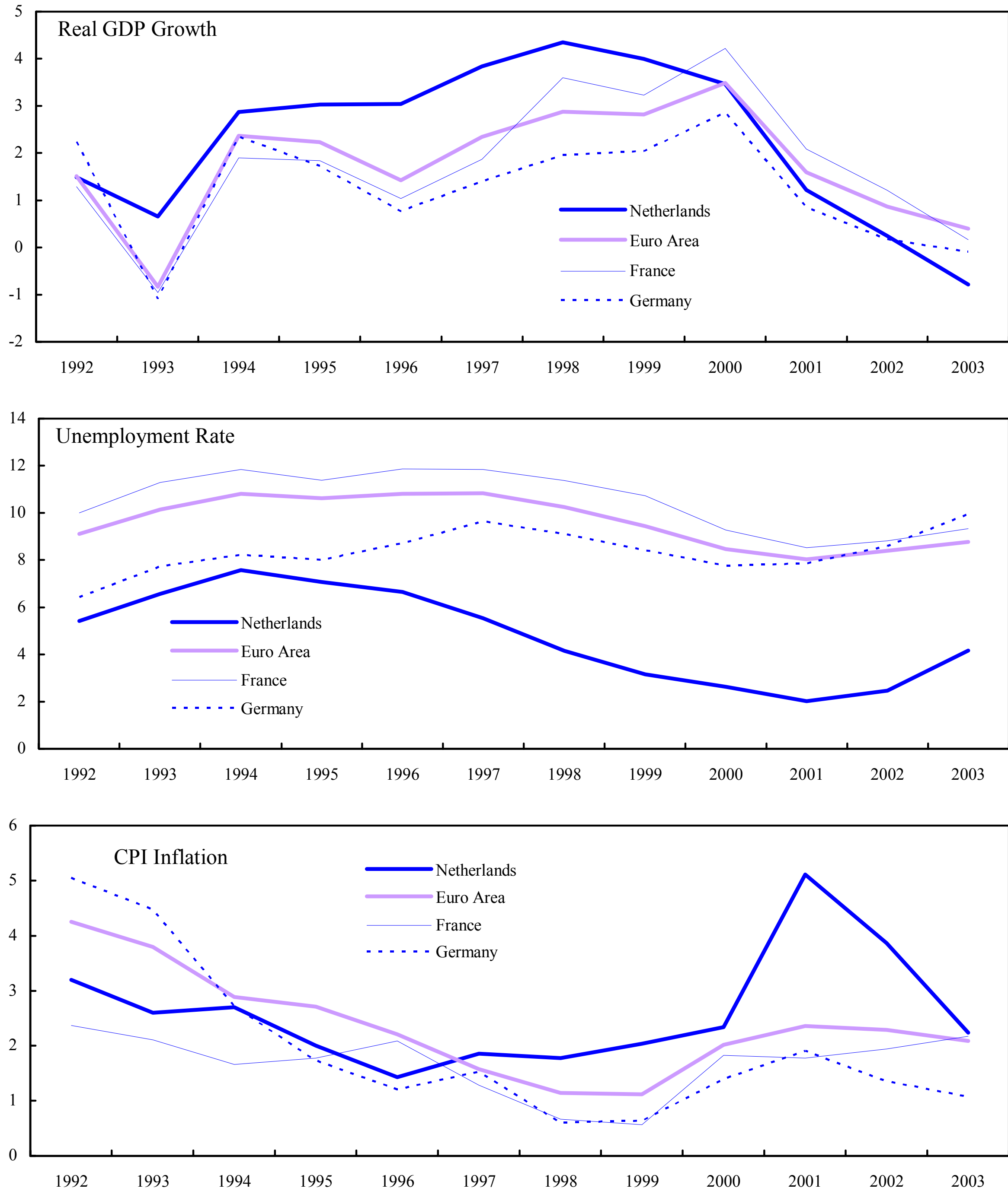
35. ***While the financial system is sound, resilient to potential adverse shocks, and well supervised, FSAP recommendations are relevant for pending legislation and preserving longer-term financial stability.*** In those few areas where autonomy is not fully delegated to the supervisors, new legislation should spell out clearly the role of the Minister and the Ministry of Finance as applicable. Other relevant actions should include ensuring that the Authority for Financial Markets has the power to cooperate fully with securities supervisors internationally; continuing to work with cross-border counterparts to improve securities settlement arrangements; allowing sufficient flexibility for making up shortfalls in the coverage ratio of pension funds to prevent procyclical effects, but without unduly prolonging adjustment; continuing to develop the frameworks for crisis management and macro-prudential surveillance; and phasing out tax deductibility of mortgage interest over the medium term, in a gradual fashion to avoid disruptive effects.

36. ***The authorities' support for overseas development assistance and trade liberalization is commendable.*** Even in the face of budgetary pressure and consolidation, the Netherlands still exceeds the United Nations' target of 0.7 percent of GNP.

37. While data are adequate for surveillance, it would be helpful to shorten the lag with which annual fiscal data, consistent with the national accounts, become available, and to start compiling such fiscal data on a quarterly basis.

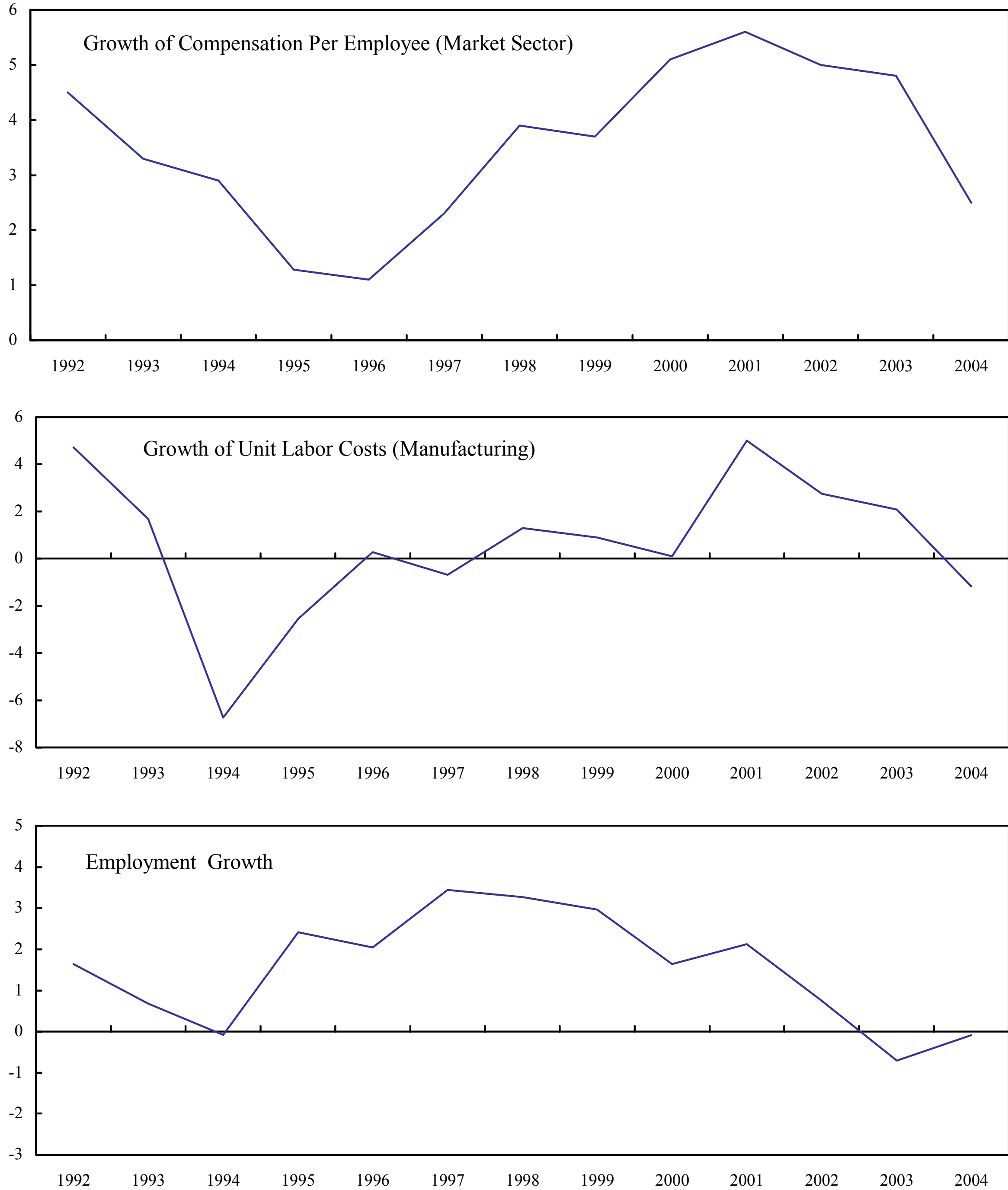
38. It is recommended that the next Article IV consultation with the Netherlands remain on the 12-month cycle.

Figure 1. Netherlands: GDP, Unemployment and Inflation
(In Percent)



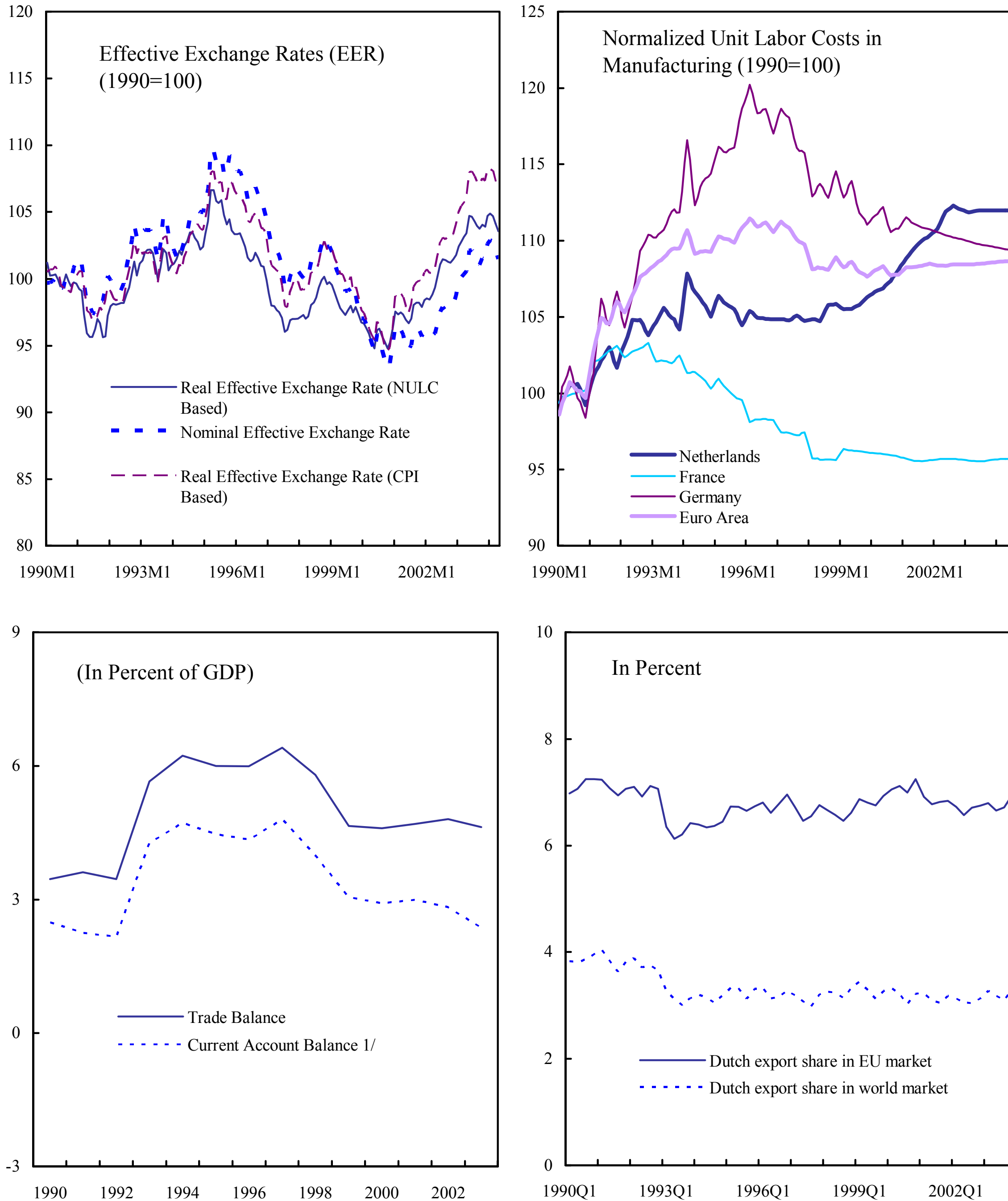
Source: WEO.

Figure 2. Netherlands: Labor Costs and Employment
(In Percent)



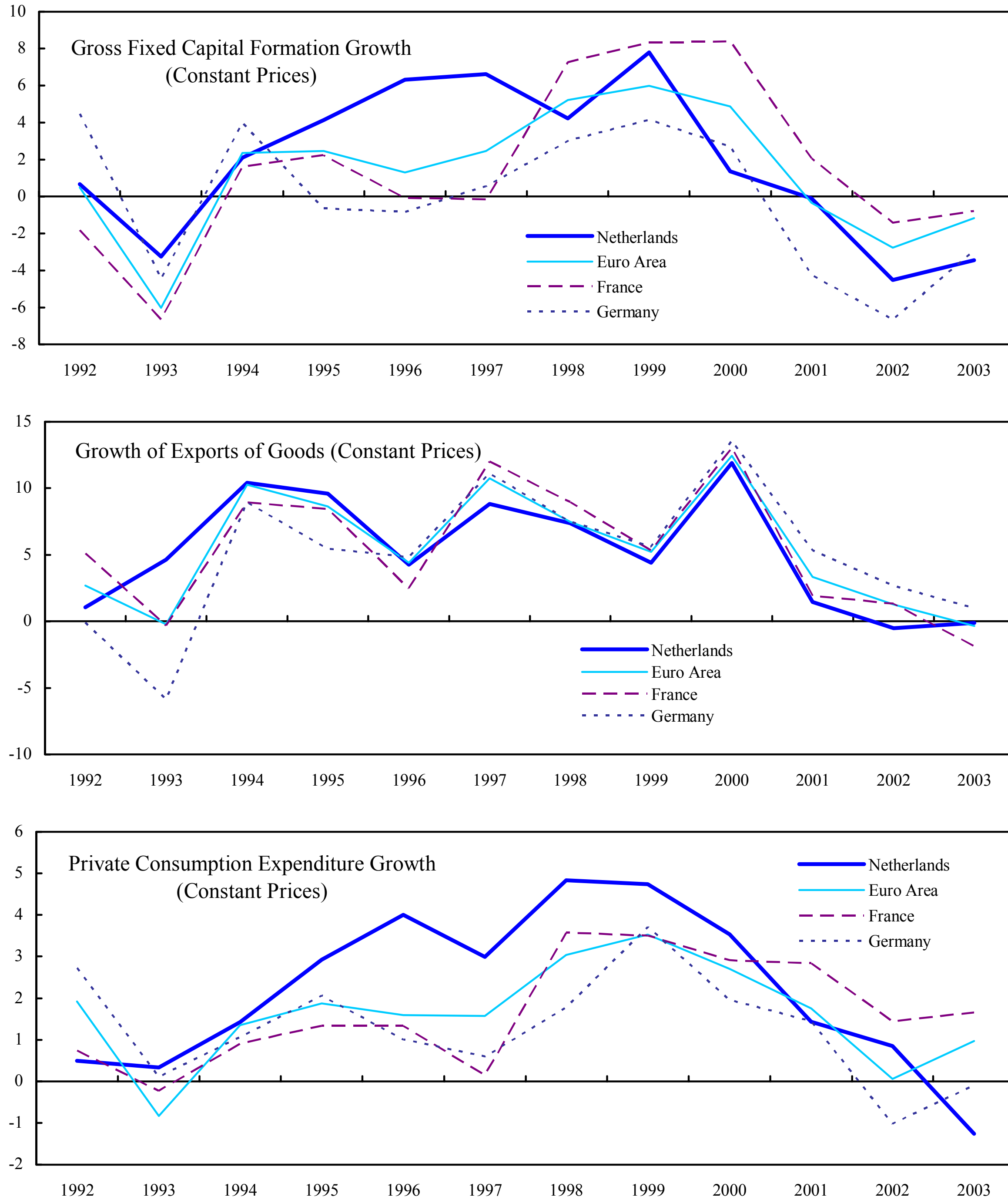
Sources: CPB and IMF, WEO.

Figure 3. Netherlands: Competitiveness Indicators



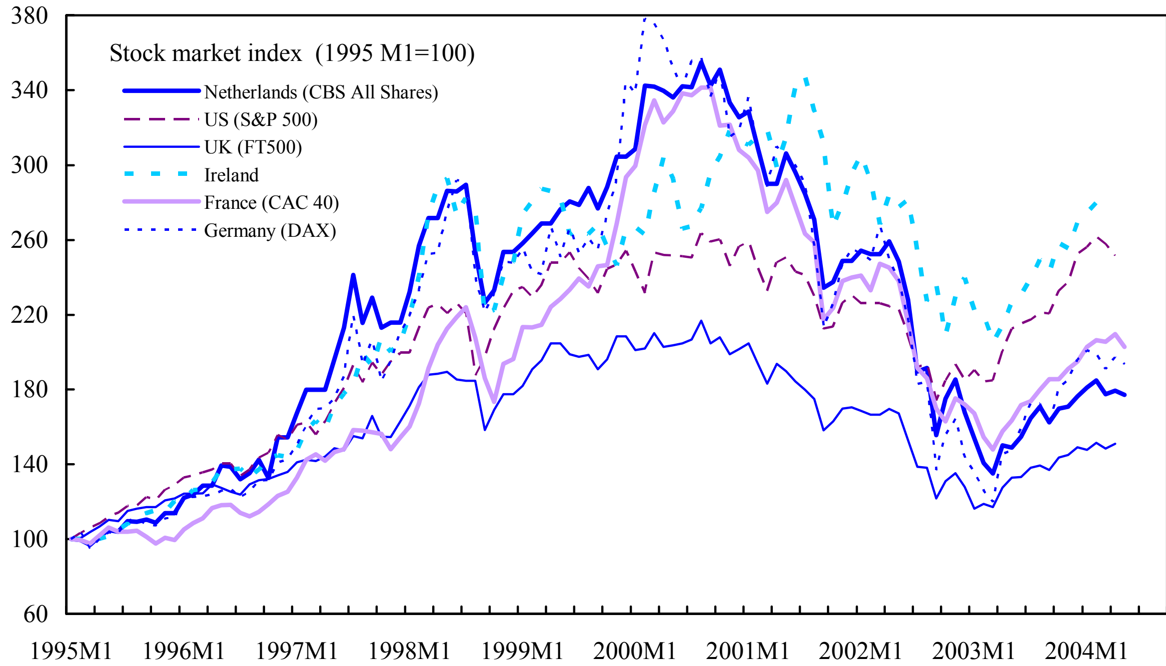
Source: IMF, INS, DOT, and WEO
1/ Excluding net investment income from abroad.

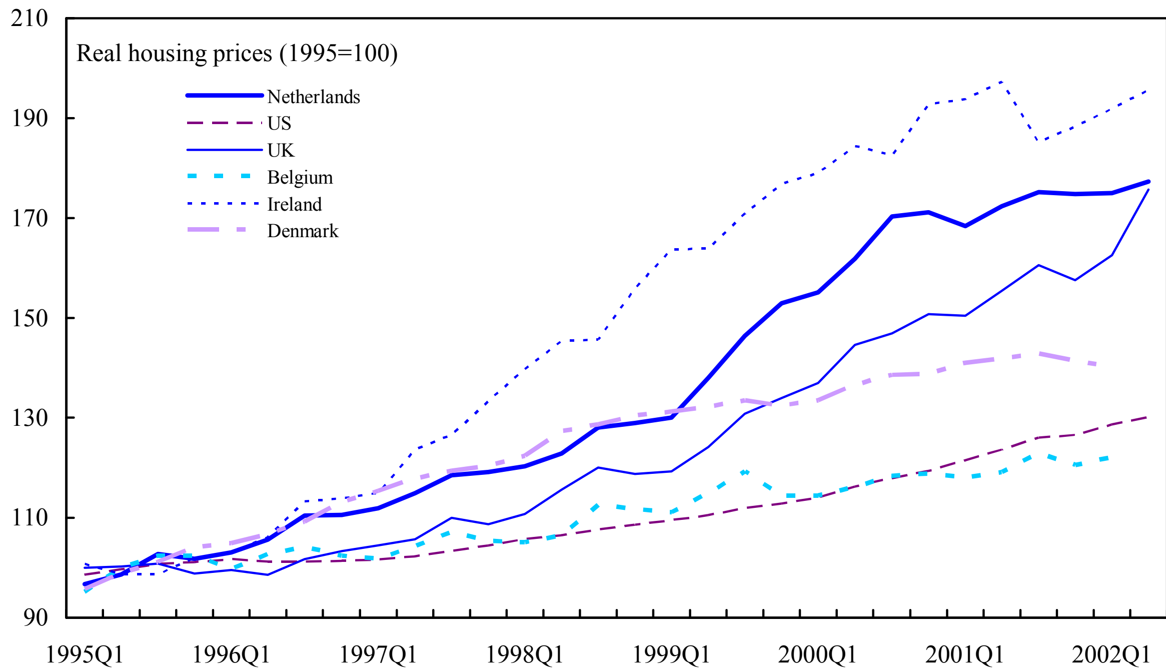
Figure 4. Netherlands: Components of Expenditure
(In Percent)



Source: WEO.

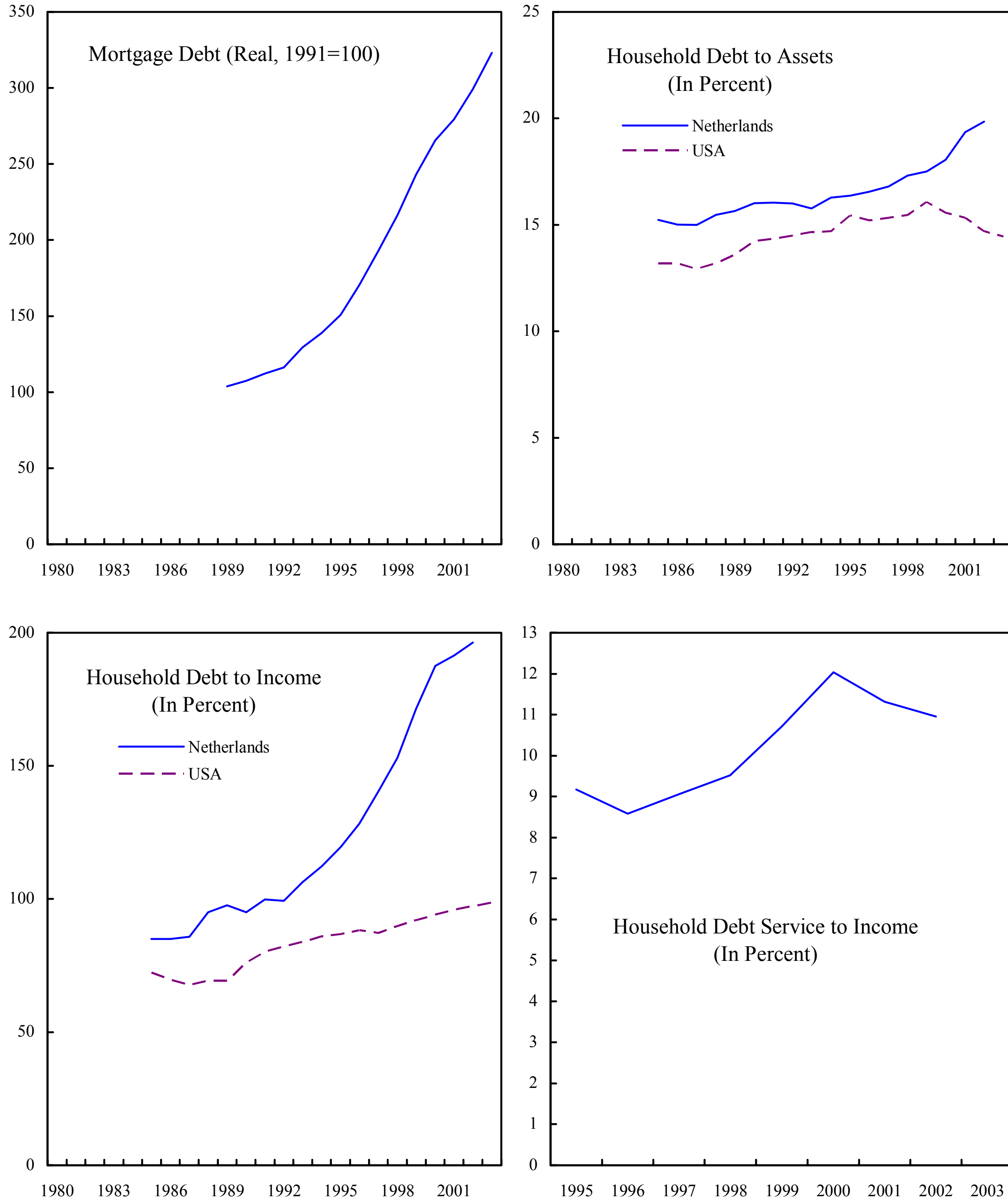
Figure 5. Netherlands: Developments in Asset Prices





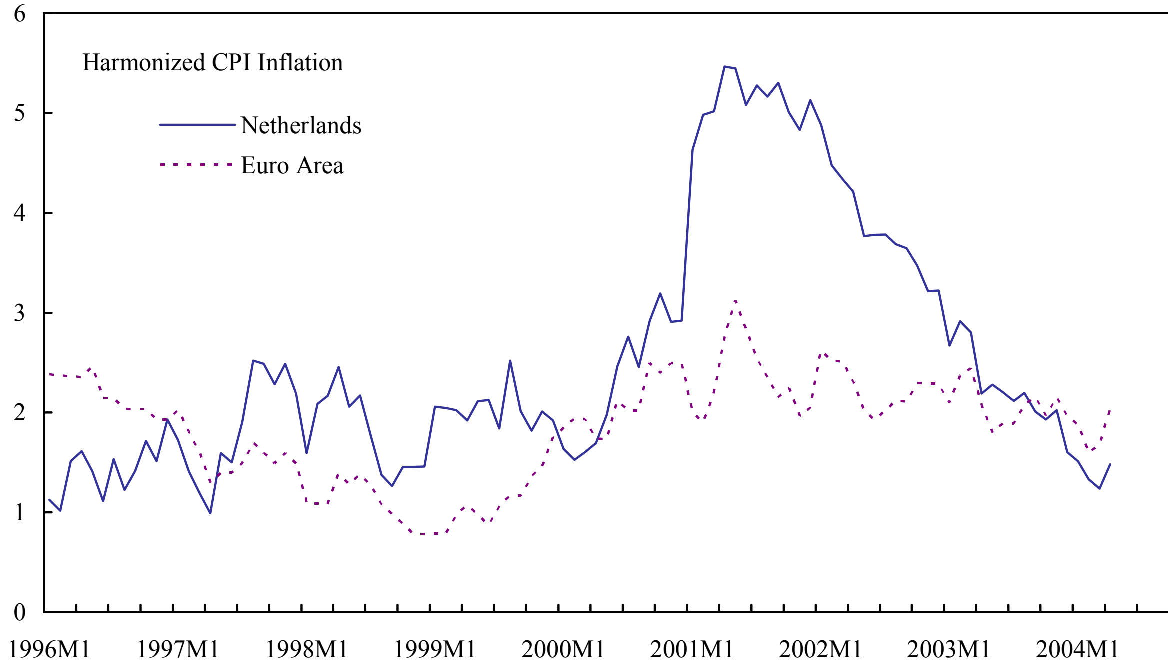
Sources: BIS, WEFA, and IMF staff estimates.

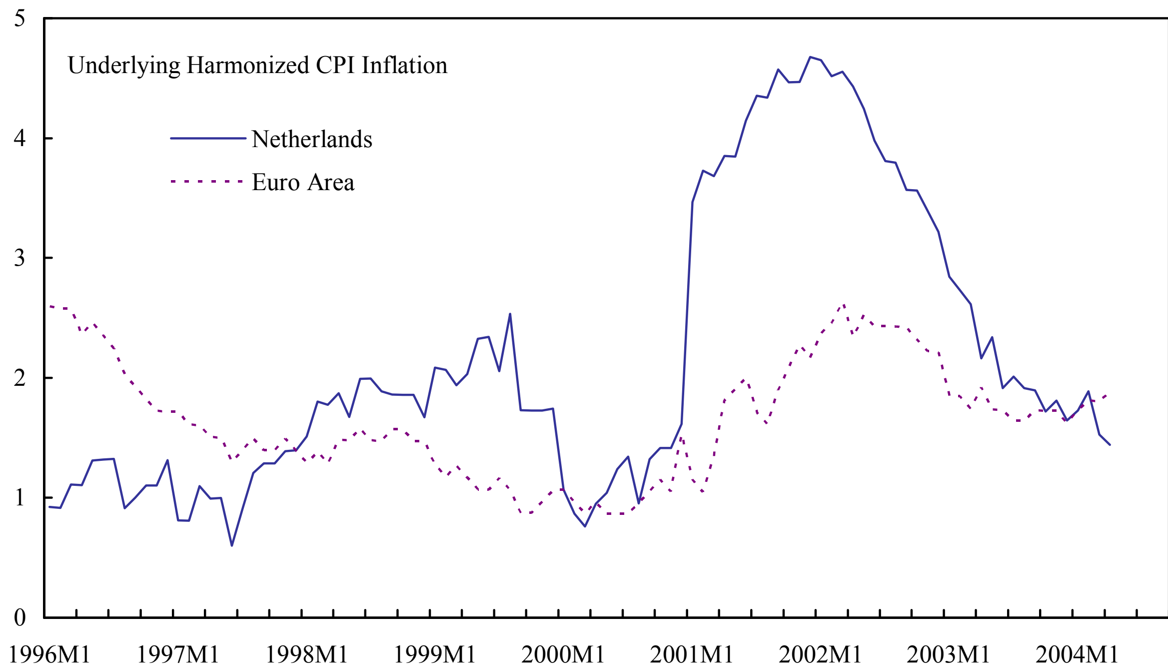
Figure 6. Netherlands: Developments in Household Balance Sheets



Sources: CBS; BIS; Authorities; and staff estimates.

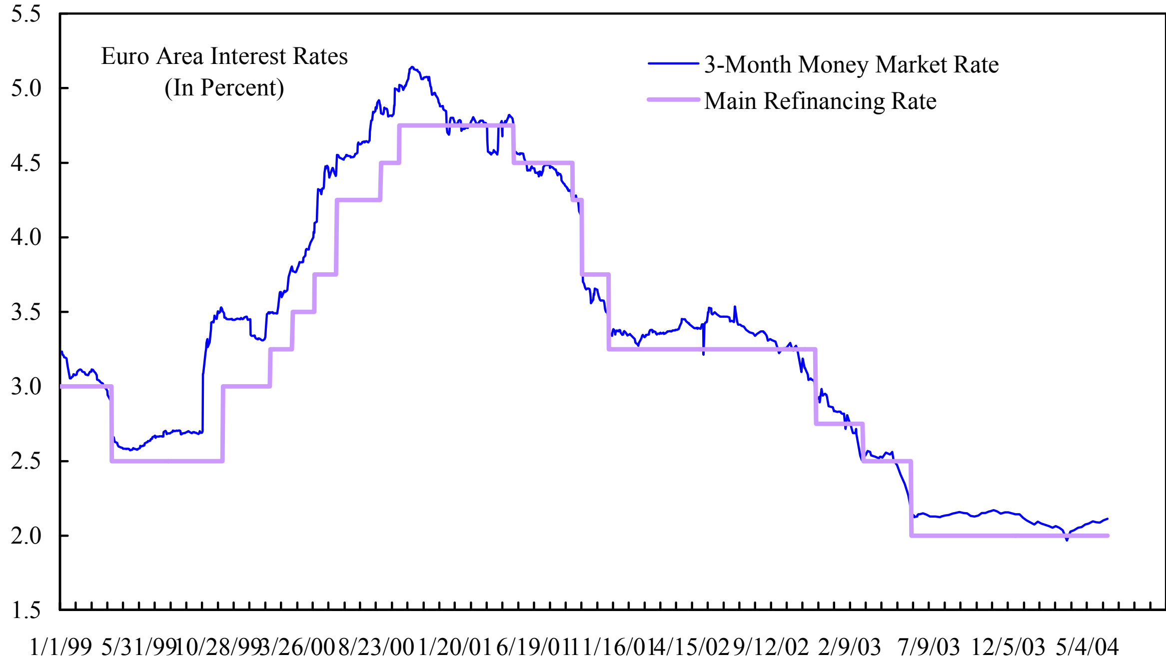
Figure 7. Netherlands: Consumer Prices
(Year-on-Year Percent Change)

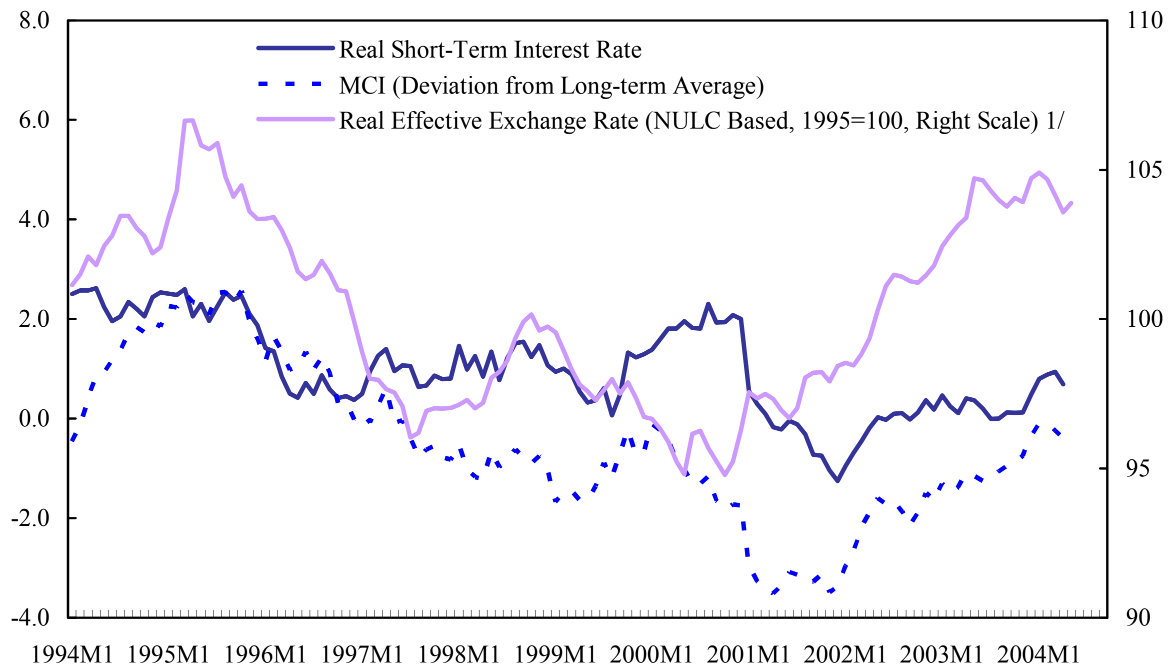




Sources: Eurostat, Cronos Database.

Figure 8. Netherlands: Monetary Conditions

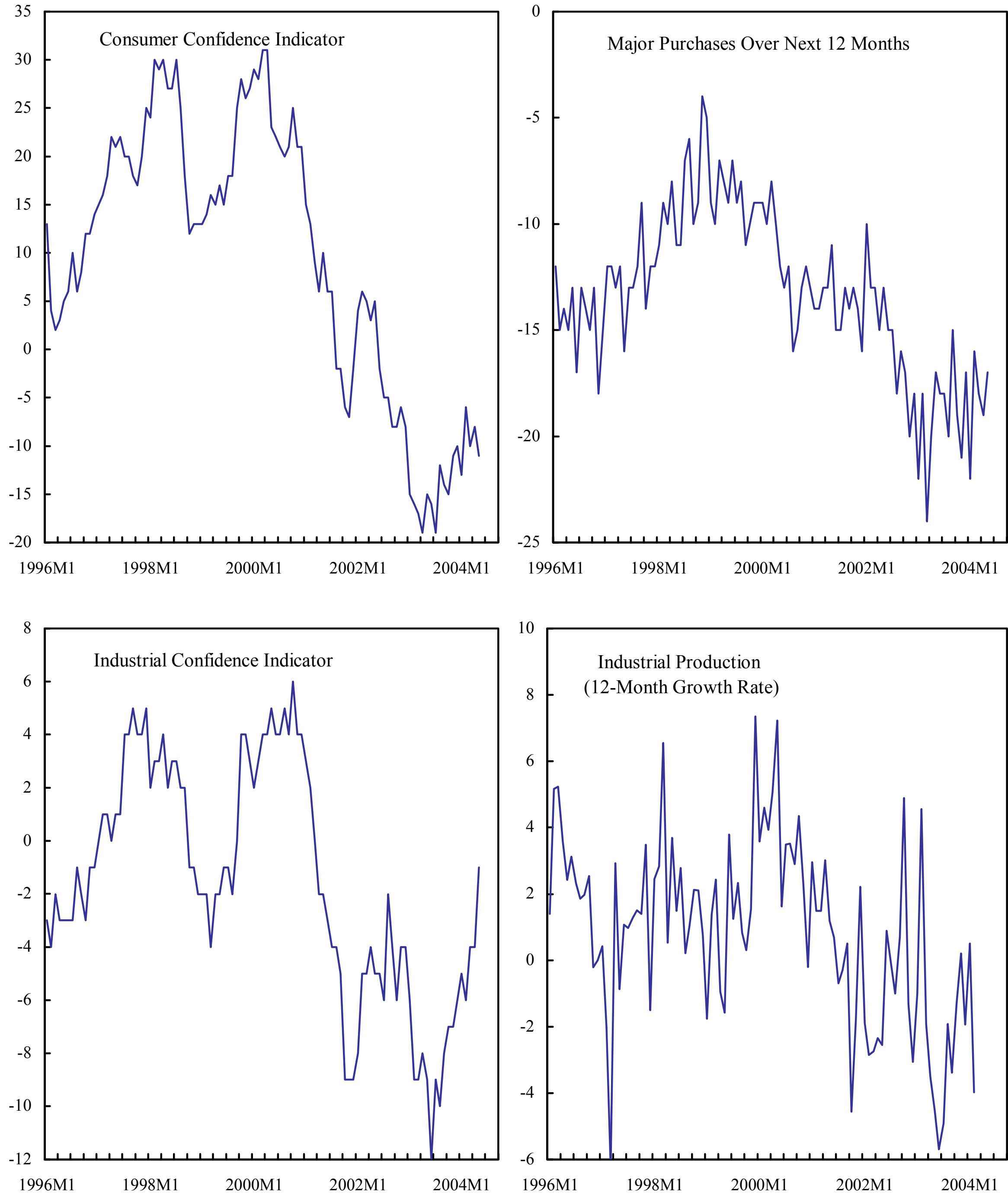




Source: IMF, IFS.

1/ An increase implies less accomodative conditions.

Figure 9. Netherlands: Cyclical Indicators



Source: WEFA, Intline Database; and IMF, IFS.

Figure 10. Netherlands: Labor Market Indicators

Source: OECD.

Table 1: Netherlands: Basic Data

Land area (2002)	41.5 thousand sq. km.
Population (2002)	16.1 million
Population characteristics and health:	
Life expectancy at birth (2000)	75.3 (male), 80.6 (female)
Fertility rate (2001)	1.7 children/woman
Infant mortality rate (2001)	5.4 per 1,000 live births
Population per sq. km. of land area (2002)	388 persons

National accounts 2001	(In billions of euros)	(In percent of GDP)
Private consumption	213.1	49.7
Public consumption	100.3	23.4
Gross fixed investment	93.0	21.7
Stockbuilding	0.2	0.1
Exports of goods and nonfactor services	280.3	65.3
Imports of goods and nonfactor services	257.8	60.1
GDP	429.1	100.0

	1999	2000	2001	2002	2003	2004 Proj.	2005 Proj.
	(Annual percentage change, unless otherwise indicated)						
National accounts (constant prices)							
Private consumption	4.7	3.5	1.4	0.8	-1.2	0.1	1.5
Public consumption	2.5	2.0	4.2	3.8	2.7	-0.2	0.3
Gross fixed investment	7.8	1.4	-0.1	-4.5	-3.2	1.7	1.9
Total domestic demand	4.3	2.6	1.7	0.1	-0.4	0.5	1.3
Exports of goods and nonfactor services	5.1	11.3	1.7	0.1	0.1	1.7	5.5
Imports of goods and nonfactor services	5.8	10.5	2.4	-0.2	0.6	0.9	5.1
Net foreign balance 1/	-0.1	1.1	-0.4	0.2	-0.3	0.6	0.6
Gross domestic product	4.0	3.5	1.2	0.2	-0.7	1.1	1.8
Output gap (in percent of potential output)	2.5	3.6	2.5	0.5	-2.2	-3.1	-3.3
Prices, wages, and employment							
Consumer price index (year average)	2.0	2.3	5.1	3.9	2.2	1.3	1.0
GDP deflator	1.6	3.9	5.4	3.4	2.9	2.1	1.1
Hourly compensation (manufacturing)	2.9	3.7	4.2	3.7	2.6	0.7	0.5
Unit labor costs (manufacturing)	0.9	0.4	5.0	2.8	2.6	-0.4	-0.7
Employment	3.0	1.6	2.1	0.7	-0.6	--	0.6
Unemployment rate (in percent)	3.2	2.6	2.0	2.5	4.1	5.1	5.6
NAIRU	4.9	4.6	4.2	3.9	4.0	4.1	4.0

Table 1. Netherlands: Basic Data (concluded)

	1999	2000	2001	2002	2003	2004 Proj.	2005 Proj.
	(Annual percentage change, unless otherwise indicated)						
Personal sector							
Real disposable income	0.8	1.4	3.3	0.5	-1.0	0.4	1.0
Household savings ratio 2/	9.7	7.0	9.0	9.3	9.5	9.8	9.4
External trade							
Exports of goods, volume	5.3	11.1	1.0	-1.3	3.4	1.5	5.6
Imports of goods, volume	6.4	10.1	1.3	-0.7	2.0	0.6	5.6
Terms of trade	-1.5	-0.3	1.3	-0.1	0.6	1.1	-1.0
Merchandise balance (percent of GDP)	4.0	4.8	5.1	4.5	5.3	6.0	5.7
Current account balance (percent of GDP)	3.9	2.0	1.9	2.5	2.2	3.3	3.5
Public sector accounts (percent of GDP)							
Revenue	47.6	47.5	46.6	45.9	45.6	45.2	45.0
Expenditure	46.9	45.3	46.6	47.8	48.8	48.2	47.7
General government balance	0.7	2.2	--	-1.9	-3.2	-3.0	-2.7
Structural balance 3/	-0.7	-0.2	-0.9	-2.2	-2.2	-1.6	-1.1
Primary balance	4.5	5.3	2.7	0.6	-1.2	-0.9	-0.5
Structural primary balance 3/	3.3	3.1	1.9	0.3	-0.2	0.6	1.0
General government gross debt	63.1	55.9	52.9	52.4	55.0	56.3	57.5

Sources: Dutch official publications; International Monetary Fund, International Financial Statistics; and Fund staff estimates.

1/ Contribution to GDP growth.

2/ In percent of disposable income.

3/ For 2002, the purchase of gas rights from DSM (0.3 percent of GDO) is excluded.

Table 2. Netherlands: General Government Accounts

(In percent of GDP)

	1998	1999	2000	2001	2002	2003 1/	2004 2/	2005 2/
Revenues	46.4	47.6	47.5	46.6	45.9	45.6	45.2	45.0
Tax revenues and social sec. contr.	39.4	40.7	40.6	39.2	38.9	38.7	38.4	38.1
Tax revenues	24.1	24.7	24.6	24.9	25.0	24.3	...	...
Social security contributions	15.3	16.0	16.0	14.3	13.9	14.5	...	...
Nontax revenues	7.1	6.9	6.9	7.4	7.0	6.8	...	...
Expenditure	47.2	46.9	45.3	46.6	47.8	48.8	48.2	47.7
Social security and social assistance benefits	19.0	18.5	17.9	17.9	18.7	19.6	...	...
Social security	15.1	14.8	14.5	14.6	15.4	16.2	...	...
Social assistance	3.9	3.6	3.4	3.3	3.3	3.4	...	...
Subsidies and other current transfers	2.8	3.0	3.2	3.2	3.3	3.3	...	...
Other current spending	1.3	1.3	1.2	1.2	1.2	1.2	...	...
Other taxes on production	0.1	0.1	0.1	0.1	0.1	0.1	...	...
Unfunded employee social benefits	1.2	1.1	1.1	1.1	1.1	1.0	...	...
Capital formation (gross)	2.9	3.0	3.1	3.2	3.6	3.2	...	...
Capital transfers	0.7	0.6	0.6	0.9	0.5	0.6	...	...
Net acquisitions of non-financial assets	-0.7	-0.4	-0.9	-0.1	-0.1	0.1	...	...
Consumption								
Compensation of employees	10.1	10.2	10.0	10.1	10.5	10.9	...	...
Intermediate consumption	6.2	6.4	6.3	6.8	6.9	6.9	...	...
Property income	4.9	4.5	3.8	3.4	3.1	2.9	...	...
Unemployment insurance	1.1	1.0	0.8	0.8	0.9	...	...	...
Welfare	1.2	1.1	1.0	0.9	0.9	0.9	...	...
Defense spending	1.6	1.6	1.6	1.6	1.5	1.3	...	...
Fiscal balance 3/	-0.8	0.7	2.2	0.0	-1.9	-3.2	-3.0	-2.7
Interest receipts	0.7	0.7	0.7	0.7	0.6	0.9	...	...
Interest payments	4.8	4.5	3.8	3.4	3.1	2.9	...	...
Net interest payments	4.2	3.8	3.1	2.8	2.5	2.0	...	...
Memorandum items:								
Primary balance	3.4	4.5	5.3	2.7	0.6	-1.2	-0.9	-0.5
Structural balance (in percent of GDP)	-1.5	-0.7	-0.2	-0.9	-2.2	-2.2	-1.6	-1.1
Nominal expenditure growth (in percent) 4/	3.9	5.0	5.4	7.4	7.0	4.3	2.3	1.4
Real expenditure growth (in percent) 4/	2.1	3.4	1.4	1.9	3.5	1.3	0.1	0.3

Sources: National accounts, Ministry of Finance, CPB, and staff calculations.

1/ Estimates.
2/ Projections.
3/ For 2000 includes UMTS receipts (0.7 percent of GDP) and for 2001 includes purchase of gas rights from DSM (0.3 percent of GDP).
4/ For 2000 excludes UMTS receipts (0.7 percent of GDP) and for 2001 excludes the purchase of gas rights from DSM (0.3 percent of GDP).

Table 3. Netherlands: Indicators of External and Financial Vulnerability[1]

(In percent of GDP, unless otherwise indicated)

	1998	1999	2000	2001	2002	2003
External indicators						
Exports goods and services (annual percent change, in U.S. dollars)	4.2	0.1	4.1	0.3	4.5	18.3
Imports goods and services (annual percent change, in U.S. dollars)	5.1	2.0	3.5	0.0	4.3	17.7
Terms of trade goods (annual percent change)	0.1	-1.5	-0.3	1.3	-0.1	0.6
Current account balance	3.3	3.9	2.0	1.9	2.5	2.2
Inward portfolio investment	9.8	-1.3	2.4	-3.5	3.5	-2.3
Inward foreign direct investment	9.4	10.3	17.2	13.5	6.1	3.7
Official reserves (in US dollars, billions)[2]	32.6	19.2	17.8	17.0	17.0	11.0
Foreign assets of the banking sector (in U.S. dollars, billions)[3]	…	165.0	162.3	214.6	230.0	275.4
Foreign liabilities of the banking sector (in U.S. dollars, billions)[3]	…	205.8	204.1	253.9	274.4	293.3
Official reserves in months of imports	1.8	1.0	0.9	0.9	0.8	0.5
Exchange rate (per U.S. dollar, period average)	...	0.94	1.09	1.12	1.06	0.89
Financial Market Indicators						
Public sector debt (Maastricht definition)	66.8	63.1	55.9	52.9	52.4	55.0
Government bond yield	4.9	4.9	5.5	5.2	5.0	4.2
Government bond yield (real)	2.9	2.7	3.0	0.6	1.5	2.1
Stock market index	74.5	84.7	100.0	81.9	63.1	45.7
Spread of government bond yield with Germany	0.48	0.66	0.27	0.47	0.39	0.37
Financial Sector Risk Indicators						
Mortgage credit to total assets (in percent)	22.2	20.3	18.4	19.3	21.3	...
Provisioning/total assets	0.8	0.8	0.7	0.7	0.7	...
Classified loan to total loans (in percent)[4]	2.6	2.7	2.3	2.3	2.4	...
Provisioning to classified loans (in percent)[4]	15.5	10.0	8.0	14.2	18.4	...
Exposure to emerging markets/own funds[5]	66.4	61.2	58.5	55.1	46.3	48.5
Contingent and off-balance-sheet accounts to total assets (in percent)	18.6	21.6	21.9	20.3	19.5	16.7
Risk based capital-asset ratio	11.4	11.2	11.3	11.4	11.9	12.1

Sources: Data provided by the authorities, and IMF, *International Financial Statistics.*

[1]The interpretation of some indicators is affected by the launch of monetary union in 1999.

[2]Reserves and foreign liabilities refer to the Dutch central bank, both before and after EMU. End-of-period.

[3]From 1999 onward claims on/liabilities to non Euro Area countries only.

[4] Average of the three largest banks.

[5]Emerging markets: Africa, Latin America, Middle East (excluding Israel), and Asia (excluding South Korea, Taiwan, Province of China, Hong Kong S.A.R., and Singapore).

Netherlands: Fund Relations
As of April 30, 2004

I. **Membership Status**: Joined December 27, 1945; Article VIII.

II. **General Resources Account**:

	SDR Million	Percent of Quota
Quota	5,162.40	100.00
Fund holdings of currency	3,150.90	61.04
Reserve position in Fund	2,011.53	38.96
Operational budget transfers (net)	113.00	

III. **SDR Department**

	SDR Million	Percent of Allocation
Net cumulative allocation	530.34	100.00
Holdings	506.14	95.44

IV. **Outstanding Purchases and Loans**: None

V. **Financial Arrangements**: None

VI. **Projected Obligations to Fund**: None

VII. **Exchange Rate Arrangements**:

The Netherlands entered the final stage of European Economic and Monetary Union on January 1, 1999, at a rate of 2.20371 guilder per euro.

VIII. **Article IV Consultation**:

Discussions for the 2003 Article IV consultation were held in Amsterdam and the Hague during May 9–19, 2003. The staff report for the 2003 Article IV consultation (IMF Country Report 03/239) was considered by the Executive Board on July 30, 2003. The Article IV discussions with the Netherlands are on the standard 12-month consultation cycle.

IX. **Exchange Restrictions**:

In compliance with the relevant EU Council regulations, the Netherlands maintains exchange restrictions vis-à-vis Burma/Myanmar (No. 1081/2000); specific individuals associated with the previous government of the former Republic of Yugoslavia (No. 2488/2000); certain persons and entities with a view to combating terrorism (No. 2580/2001); Usama Bin Laden, the Al-Qaida network, and the Taliban (No. 881/2002); Somalia (No. 147/2003); Iraq (No. 1210/2003); Congo (No. 1727/2003); Sudan (No. 131/2004); Liberia (No. 234/2004); and Zimbabwe (No. 314/2004). These restrictions are solely for the preservation of national or international security and have been notified to the Fund in accordance with EBD No. 144-(52/51).

The Netherlands: Statistical Data Issues

The Netherlands publishes a wide range of economic and financial statistics. Specifically, annual and quarterly national account data are provided by the Central Bureau of Statistics; financial and balance of payments data are provided by De Nederlandsche Bank; and fiscal data are provided by the Ministry of Finance. These data are increasingly available in electronic form. Macroeconomic data are generally of high quality. Although the overall government balance is reported monthly, broader fiscal data are not available on a quarterly basis and national accounts consistent government accounts are only published with lengthy delays. There are also discrepancies between data compiled by different statistical agencies.

The frequency and timeliness of the availability of the core statistical indicators for Fund surveillance purposes are summarized in the attached table. The authorities subscribe to the Special Data Dissemination Standard, providing information about their data and data dissemination practices on the IMF Dissemination Standards Bulletin Board, with hyperlinks to national data systems.

The Netherlands: Core Statistical Indicators
As of June 29, 2004

	Int'l Reserves 1/	Central Bank Balance Sheet	Reserve/ Base Money	Broad Money	Interest Rates	Consumer Price Index	Exports/ Imports	Current Account Balance	Overall Government Balance	External Government Debt	GDP/GNP
Date of Latest Observation	5/04	5/04	5/04	5/04	6/29/04	5/04	4/04	Q4/03	4/04	2002	Q1/04
Date Received	6/27/04	6/27/04	6/27/04	4/27/04	6/29/04	6/14/04	6/14/04	4/14/04	06/02/04	1/04	6/4/04
Frequency of Data	Monthly	Monthly	Monthly	Monthly	Daily	Monthly	Monthly	Quarterly	Monthly	Annually	Quarterly
Frequency of Reporting	Monthly	Monthly	Monthly	Monthly	Daily	Monthly	Monthly	Quarterly	Monthly	Annually	Quarterly
Source of Update	DNB	ECB	DNB	DNB	Reuters	CBS 2/	CBS 2/	DNB	MoF	MoF	CBS 2/
Mode of Reporting	Electronic	Electronic	Electronic	Electronic	Electronic	Electronic	Electronic	Electronic	Electronic	Electronic	Electronic
Confidentiality	Public	Public	Public	Public	Public	Public	Public	Public	Public	Public	Public
Frequency of Publication	Monthly	Monthly	Monthly	Weekly	Daily	Monthly	Monthly	Quarterly	Monthly	Annually	Quarterly

1/ De Nederlandsche Bank= central bank.
2/ Central Bureau of Statistics.

Aging and the Public Finances in the Netherlands

The Netherlands is in a reasonably good situation to deal with the problem of population aging. Its population is relatively young (its old-age dependency ratio is among the lowest in Western Europe and will remain so in the next 50 years, according to the OECD); and its debt level is below the euro area average (54 percent of GDP in 2003 compared with 70 percent). Importantly, the Netherlands underwent a substantial fiscal consolidation during the 1990s, which led to a significant improvement in the budget balance and a large reduction in public debt. According to a study by Netherlands Bureau for Economic Policy Analysis (CPB) in 2000, entitled *Aging in the Netherlands*, the cost of aging and its implications for long-term fiscal sustainability is manageable.

The existence of the large second pillar helps alleviate, though not eliminate, the burden of aging on the public finances. The fully funded second pillar accounts for more than 40 percent of pension income, and includes occupational pension schemes, which are mandatory for workers in the public sector and for more than 90 percent of the workers in the private sector. Moreover, the taxation of private-sector pension income would provide a substantial offset to the fiscal cost of aging. The Netherlands (together with the United Kingdom) has by far the largest amount of private pension fund assets in EU countries. Assets of the Dutch occupational pension funds amounted to 121 percent of GDP in 2001, and could increase to nearly 200 percent of GDP by 2040.

To deal with the fiscal cost of aging, the CPB's study articulated a strategy of swift debt reduction, which has been supported by Fund staff. According to official estimates, rising life expectancy and a stable fertility rate are expected to nearly double the old-age dependency ratio during the next 40 years. Public spending on pensions and health care are projected to increase by more than 9 percentage points of GDP between 2001 and 2040, when the projected fiscal cost of aging peaks. However, the taxation of private-sector pension income could provide a substantial offset to these costs, projected by the CPB to raise revenue by more than 5 percentage points of GDP between 2000 and 2040. Thus, the fiscal costs, net of this revenue increase, would rise by about 4 percentage points of GDP by 2040. These costs, under the strategy, would be covered by the savings on interest payments, thus avoiding the need for tax hikes.

The methodology used in the study for analyzing the sustainability of the public finances was based on the generational accounting framework and it aimed to ensure that the government's intertemporal budget constraint was satisfied. Thus, in present value terms, government revenues (T) would be sufficient to cover expenditures (E), including the liabilities associated with aging. Age-specific benefits from the government minus age-specific tax payments to the government were calculated for the base year and extrapolated to estimate future revenues and expenditures. If the intertemporal budget constraint were not satisfied, revenues (expenditures) would need to rise (fall), with the permanent adjustment required to close the gap equal to $(r - g)(E - T)/GDP$, with r = the interest rate and g = the growth rate of GDP. A key idea is to hold tax rates constant over time in order to minimize

deadweight loss. The argument, laid out in Barro (1979),[13] is that the distortionary cost of a tax rises more than proportionally with the tax rate, implying that the total distortion is minimized when the tax rate is constant.[14]

The authorities in 2000 set a fiscal target consistent with this strategy. In particular, the overall budget balance would reach a surplus of 1¼ to 1¾ percent of GDP in 2007 and public debt would be eliminated by 2025. The underlying macroeconomic assumptions were that the real interest rate (4 percent), the inflation rate (2 percent), and average labor productivity growth (1¾ percent) are exogenous and constant; potential GDP growth declines gradually to about 1.5 percent by 2030 as the labor supply falls, but rises to 1.8 percent by 2050.

However, recent developments suggest the need for revisions. Projections of future health care costs have been revised upward. Moreover, with the rapid fiscal deterioration since 2000, achieving the above objective would now require an unrealistic reduction of public expenditure in the next three years on the order of 4 percentage points of GDP.

If recent expenditure trends were to continue through 2007 (with real spending growing by 2½ percent a year), the budget deficit would expand in the next few years and have a significantly negative impact on debt dynamics. Based on staff estimates, the stock of public debt by 2025 could be close to 50 percent of GDP (Panel A), and longer-term debt dynamics would raise concerns. This would necessitate, to restore fiscal balance, tax increases which could impair economic performance at a time when labor force reductions from aging would reduce the potential growth of the economy, or other cuts in spending. Furthermore, the experience of the last few years suggests that the assumptions on labor productivity growth may be optimistic, underscoring the need for decisive structural reforms.

The CPB has undertaken a partial update of the 2000 study. Taking into account revised projections for health care expenditures and a new target for the fiscal balance (a primary surplus of 0.4 percent of GDP in 2007), a new sustainable debt path was estimated. Consistent with the notion of tax smoothing, this was accompanied by assuming a permanent increase in taxes of 1.8 percent of GDP in 2008 (Panel B). Under this scenario, after declining through 2030, the debt would start to rise (albeit modestly), with the fiscal deficit reappearing and its size reaching about 1.0 percent of GDP by 2050.

Staff prepared an alternative scenario, also consistent with fiscal sustainability. In this scenario, the goal was to ensure fiscal balance around zero in the long run, which would also be consistent with the general principles of the stability and growth pact. The scenario also

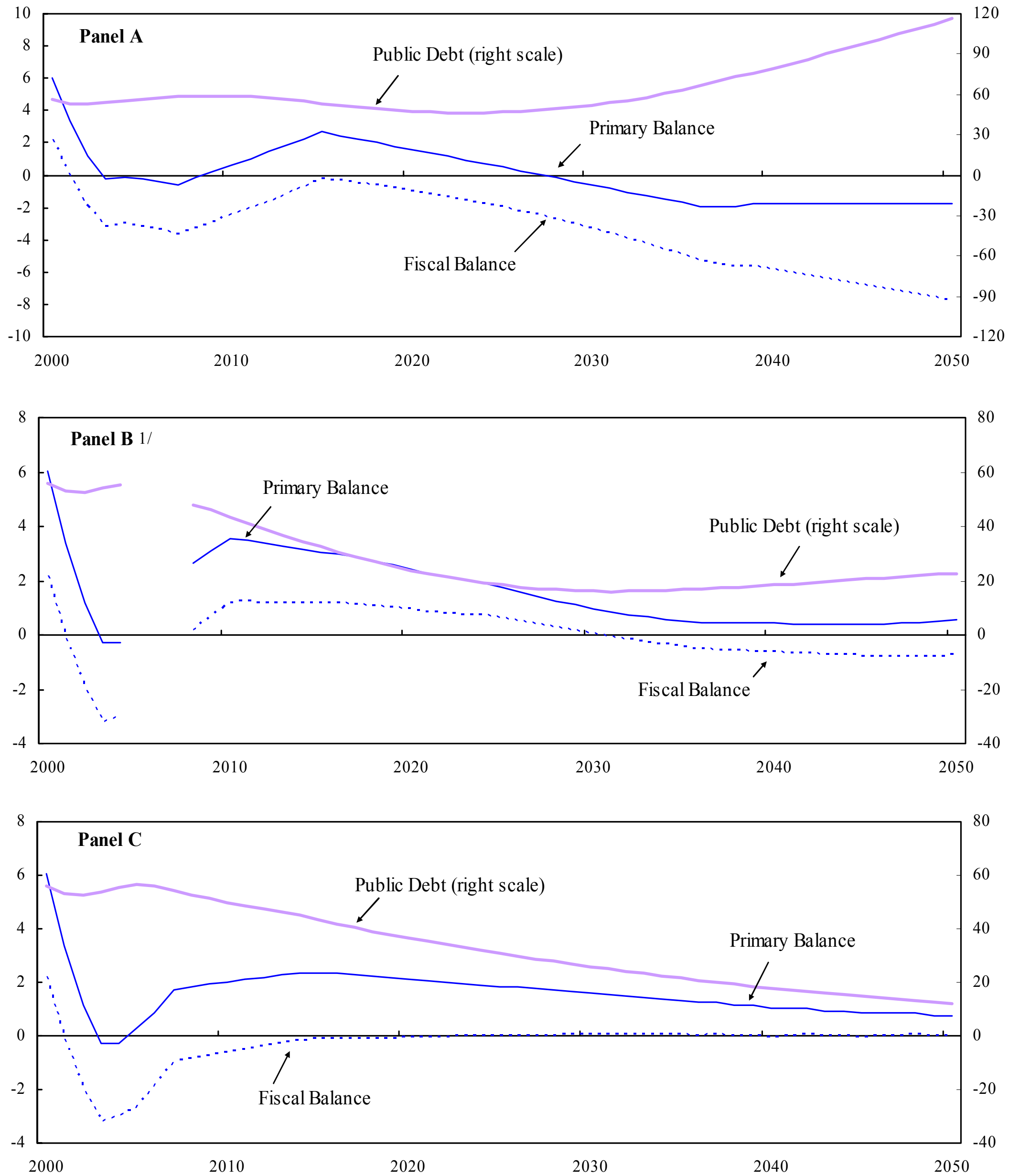
---

[13] Barro, R. (1979) “On the Determination of the Public Debt,” *Journal of Political Economy*, Vol. 87, No. 5.

[14] This rule is not equivalent to equalizing the tax burden across generations.

considers another policy option—namely no further increase in taxes in light of the potential costs due, for instance, to the increasing international mobility of the tax base or intensifying international tax competition. To meet these objectives, the scenario envisages structural adjustment of 0.5 percentage point of GDP per year during the current government term through expenditure restraint (Panel C). This would imply reaching a primary general government surplus of about 1½ percent of GDP in 2007, with the underlying structural position near balance; with a zero fiscal balance, the ratio of debt to GDP would fall. Of course, efforts to reduce distortions in the labor market that boosted potential growth and productivity by more than the baseline would alleviate some the aging problem and, in this sense, the urgency of fiscal adjustment.

Fiscal Scenarios
(In percent of GDP)



Source: CPB and Staff estimates.
1/ In the CPB update, a revised path for the fiscal balance and public debt is given only from 2008. The path to get to the primary balance target of 0.4 percent of GDP in 2007 is not specified.

Statement by the IMF Staff Representative
September 8, 2004

1. This staff statement provides information on economic developments that has become available since the preparation of the staff report for the 2004 Article IV Consultation. The new information does not alter the thrust of the staff appraisal.

2. **On GDP**:

- According to Statistics Netherlands, real GDP growth on a year-average basis was revised for 2001–03 as shown in the table below. Average growth during these years was therefore slightly stronger than previously thought: 0.4 percent, up from 0.2 percent.

Real GDP Growth

(In percent)

	2001	2002	2003
Revised	1.4	0.6	-0.9
Previous	1.2	0.2	-0.7

Source: Statistics Netherlands (CBS).

- Regarding the current year, the second quarter GDP figures were, on balance, in line with staff's overall forecast of about 1 percent real growth in 2004. The preliminary data for that quarter indicated that real GDP fell by 0.2 percent quarter-on-quarter (seasonally and working-day adjusted), but grew by 1.1 percent year-on-year. Investment dropped and was weaker than expected, but the contribution of the foreign balance was stronger than expected.

3. In the area of **fiscal policy**, a new package of multi-year fiscal adjustment measures was announced, amounting to a cumulative €750 million by 2007 (equivalent to 0.2 percent of estimated 2004 GDP). The measures, which are aimed at making some further progress toward narrowing the fiscal deficit over the medium term, are mainly in the areas of infrastructure, education, and health care. While a step in the right direction, the package, given its modest size, does not go far enough in terms of meeting staff's call for stepping-up the medium term fiscal consolidation effort.

4. In **other developments**, recent indicators are consistent with the slow recovery forecasted for this year. While both consumer and producer confidence have recovered from their lows of the summer of 2003, these indicators have failed to show significant further improvement in recent months. Year-on-year HICP inflation fell to 1.2 percent in July, despite higher oil prices.

INTERNATIONAL MONETARY FUND

Public Information Notice

EXTERNAL RELATIONS DEPARTMENT

Public Information Notice (PIN) No. 04/105
FOR IMMEDIATE RELEASE
September 17, 2004

International Monetary Fund
700 19th Street, NW
Washington, D. C. 20431 USA

IMF Concludes 2004 Article IV Consultation with the Kingdom of the Netherlands—Netherlands

On September 8, 2004, the Executive Board of the International Monetary Fund (IMF) concluded the Article IV Consultation with the Kingdom of the Netherlands—Netherlands.[1]

Background

The Dutch economy is starting to recover from a period of weak performance. Following several years of rapid expansion, GDP growth averaged only 0.2 percent during 2001-03, and turned negative in the latter year for the first time in twenty years. However, growth has strengthened in recent quarters, and staff expects the economy to grow by 1.1 percent in 2004 and by 1.8 percent in 2005. Improving exports are the main driver; domestic demand is expected to take longer to recover. Meanwhile, given soft labor market conditions and economic slack generally, price and wage pressures are likely to remain subdued for the period ahead.

In the context of the nascent recovery, downside risks to the outlook for growth are a concern with those stemming from domestic sources especially pronounced. Near-term growth is unlikely to make a significant dent in still rising unemployment, so even relatively minor changes to the wage and employment outlook could prompt a reassessment of income and therefore consumption plans. High household debt accentuates income risks, including those associated with higher interest rates.

[1] Under Article IV of the IMF's Articles of Agreement, the IMF holds bilateral discussions with members, usually every year. A staff team visits the country, collects economic and financial information, and discusses with officials the country's economic developments and policies. On return to headquarters, the staff prepares a report, which forms the basis for discussion by the Executive Board. At the conclusion of the discussion, the Managing Director, as Chairman of the Board, summarizes the views of Executive Directors, and this summary is transmitted to the country's authorities.

The fiscal balance deteriorated markedly. Between 2000 and 2003, the general government balance worsened by almost 5 ½ percentage points of GDP, resulting in a breach of the 3 percent Maastricht ceiling in 2003. While part of the deterioration reflected the working of automatic stabilizers, another part—amounting to roughly 2 percentage points of GDP—was structural. The policy measures announced by the authorities should bring the deficit down to just under 3 percent of GDP in 2004. Risks—which, to avoid another breach, would need to be addressed if they were to materialize—stem in particular from health care costs and the budget situation of the local governments.

On the structural front, the authorities have plans for a number of key reforms in the period ahead. The disability scheme is to be reformed by restricting access only to those fully disabled, while introducing stricter criteria and examinations, and strengthening work incentives for the partially disabled. Also, fiscal incentives for early retirement are to be fully removed, while participation in collective early retirement plans is to be made voluntary. In the area of unemployment insurance, follow-up benefits (which had added 2 ½ years to the maximum of 5 years of main benefits available) have already been phased out. The authorities plan to eliminate short-term benefits as well, and tighten the eligibility requirements for the main unemployment benefits. To reduce inactivity traps, the earned-income tax credit is being gradually increased. The Netherlands has generally been at the forefront of product market reform in Europe, although some sectors (e.g., construction and nontraded services) have remained sheltered.

Over the past year, the Netherlands took part in an IMF Financial Sector Assessment Program (FSAP). During this period, the authorities were in the process of concluding a substantial overhaul of the institutional setup for financial stability policy by moving to a new cross-sectional structure of supervision by objective (prudential and conduct of business) and revising the laws that underpin financial supervision.

Executive Board Assessment

Executive Directors noted that the Dutch economy is emerging from an extended downturn, with continued low inflationary pressures contributing to increased external competitiveness. Directors expressed concern, however, over the depth of the downturn, the significant weakening of the public finances in recent years, and the prospect of falling potential growth if slowing productivity growth were to continue at a time when the population is aging. Directors therefore commended the authorities for their efforts to restore fiscal balance and to strengthen the foundations for a broad-based growth. They emphasized the need to sustain such efforts, especially those geared to raising potential output growth through reforms to labor and product markets.

In light of the Netherlands' earlier record of sound fiscal and structural policies, which underpinned economic success, Directors were confident that the authorities would continue to pursue appropriate policies in these areas. While expressing concern about some of the recent structural increases in spending, they concurred that fiscal policy seems to be on the right path and praised the government's determination to hold the deficit in 2004 to below 3 percent of GDP.

Directors observed that, while a recovery is in train, growth is expected to be slow this year, and downside risks, from both domestic and external sources, are a concern. In particular, Directors were concerned about the rapid increases in house prices and household debt, and their potential impact on income and consumption. Against these downside risks, they viewed fiscal policy in 2004 as appropriately balanced between needed fiscal adjustment in structural terms and avoiding excessive tightening. However, in view of possible fiscal slippage, Directors supported measures to limit public spending through closer cooperation between the central and local governments and, if necessary, direct budgetary controls on health care spending.

Directors pointed to the benefits of an ambitious medium-term fiscal adjustment, recommending a structural improvement of at least half a percentage point of GDP per year through the government's term. They considered that such an adjustment would put fiscal policy on an appropriate path toward ensuring fiscal sustainability and dealing with the impact of population aging, while also bolstering confidence. Directors were in broad agreement with the authorities' emphasis on debt reduction to save on interest payments to cover aging costs, but stressed that stronger and more concrete medium-term fiscal consolidation plans are needed. In identifying measures, they encouraged the authorities to improve incentives for work, including measures in the tax-benefits system. Some Directors favored a gradual phasing out of mortgage interest deductions, though these Directors and others stressed the need to consider carefully the impact of this measure on the housing market and the financial system.

Directors commended the broad features of the fiscal framework, particularly the emphasis on medium-term expenditure ceilings, but noted the importance of strengthening certain aspects. In this context, they welcomed the decision to devote revenue windfalls solely to debt reduction, thus avoiding a procyclical bias. Directors also urged the authorities to eschew spending cyclical expenditure savings. In addition, they stressed that enhancing the transparency of the expenditure ceilings and the ability to monitor them would strengthen clarity and discipline in the system.

Directors were encouraged by the authorities' efforts to reform the labor market. They welcomed important reforms to raise labor force participation and work effort, including the envisaged abolition of fiscal incentives for early retirement and the plan for a major overhaul of the disability scheme, supported by tight enforcement of any stricter disability criteria. However, while acknowledging the difficulties in building consensus for reform, Directors cautioned that reforms should also include the unemployment insurance scheme, to avoid having workers shift from one category of inactivity to another. Directors also urged the authorities to address inactivity traps, including by adjusting the minimum wage, which would also enhance the demand for low-skilled labor. To further raise participation, Directors stressed the importance of taking into account changes in life expectancy in determining the retirement age.

Directors were encouraged by efforts to raise productivity growth, noting that while overall productivity is high, its growth has slowed considerably in recent years. They therefore welcomed the establishment of the high-level Innovation Platform, the

efforts under way to significantly reduce administrative burdens and improve corporate governance, and the work of the competition agency. Nevertheless, with a view to facilitating more efficient resource allocation, Directors felt that overly stringent employment protection hindered flexibility and implicitly taxed new hiring. In addition, Directors noted that greater wage differentiation would be helpful in attracting labor to higher productivity companies and sectors and in opening a channel to realize returns from investment in human capital. Directors also urged regulators to persevere with efforts to open new avenues for competition.

Directors welcomed the analysis of the FSAP and agreed with its conclusion that the financial system is sound, resilient to potential shocks, and well supervised.
They commended the pending new financial supervision legislation, which will further strengthen the supervision system and account for the cross-sectoral nature of financial institutions. To prevent procyclical effects, Directors also felt that the authorities needed to allow sufficient flexibility for making up shortfalls in pension fund coverage ratios without unduly prolonging adjustment. More generally, they encouraged the authorities to continue with their commendable efforts to strengthen securities settlement arrangements and the financial stability policy framework. Directors welcomed the implementation of strong AML/CFT measures.

Directors applauded Dutch support of trade liberalization and strongly praised the generosity of their overseas development assistance, even in the face of budgetary pressures.

Public Information Notices (PINs) form part of the IMF's efforts to promote transparency of the IMF's views and analysis of economic developments and policies. With the consent of the country (or countries) concerned, PINs are issued after Executive Board discussions of Article IV consultations with member countries, of its surveillance of developments at the regional level, of post-program monitoring, and of ex post assessments of member countries with longer-term program engagements. PINs are also issued after Executive Board discussions of general policy matters, unless otherwise decided by the Executive Board in a particular case.

Kingdom of the Netherlands—Netherlands: Selected Economic Indicators

	2000	2001	2002	2003	2004[1]	2005[1]
Real economy (change in percent)						
Real GDP	3.5	1.2	0.2	-0.7	1.1	1.8
Domestic demand	2.6	1.7	0.1	-0.4	0.5	1.3
CPI (year average)[2]	2.3	5.1	3.9	2.2	1.3	1.0
Unemployment rate (in percent)	2.6	2.0	2.5	4.1	5.1	5.6
Gross national saving (percent of GDP)	27.1	25.2	22.6	21.1	22.3	22.9
Gross domestic investment (percent of GDP)	22.2	21.7	20.5	20.1	20.1	20.4
Public finance (percent of GDP)						
General government balance	2.2	--	-1.9	-3.2	-3.0	-2.7
Structural balance	-0.2	-0.9	-2.2	-2.2	-1.6	-1.1
Structural primary balance	3.1	1.9	0.3	-0.2	0.6	1.0
General government debt	55.9	52.9	52.4	55.0	56.3	57.5
Interest rates (percent)						
Money market rate	4.4	4.2	3.3	2.3	...	...
Government bond yield	5.5	5.2	5.0	4.2	...	...
Balance of payments (percent of GDP) [3]						
Trade balance	4.8	5.1	4.5	5.3	6.0	5.7
Current account	2.0	1.9	2.5	2.2	3.3	3.5
Official reserves, excl. gold (US$ billion)	9.6	9.0	9.6	11.0	...	...
Reserve cover (months of imports of GNFS)	0.5	0.5	0.5	0.5	…	…
Exchange rate						
Exchange rate regime			Member of euro area			
Euros per U.S. dollar (June 2004)					1.2	
Nominal effective rate (1990=100)[4]	100.0	100.6	101.4	106.0	105.3	...
Real effective rate (1990=100)[4 5]	100.0	102.0	104.9	109.4	108.5	…

Sources: International Financial Statistics; information provided by the Dutch authorities; and IMF staff estimates.

[1] Staff projections.

[2] In 2001, an indirect tax increase is estimated to have boosted inflation by 1.2 percentage points.

[3] Transactions basis.

[4] Data for 2004 are for May.

[5] Based on relative normalized unit labor costs.