

September Report on Fiscal Monitoring 2017

A. ASSESSMENT

1. Introduction

The Advisory Division of the Council of State is charged with the independent monitoring of compliance with the (European) fiscal rules, as provided for in the Treaty on Stability, Coordination and Governance (VSCB) and article 5 of Regulation (EU) 473/2013. It is the task of the independent budget supervisor to draw up an assessment on the question whether the (European) fiscal rules are complied with. For its assessments, the Division works closely with the Netherlands Bureau for Economic Policy Analysis (CPB). The allocation of duties implies that the CPB is responsible for drawing up independent economic and budget forecasts and analyses; the Advisory Division is responsible for the more normative assessment of compliance with the (European) fiscal rules.

In principle, the Division draws up two reports per year, in April and in September, in which it offers an assessment about the expected budgetary developments and the intentions as laid down by the government in the Stability Programme and the Budget Memorandum respectively. The caretaker status of the cabinet means that the 2018 Budget Memorandum contains few new policy proposals. However, it may be expected that a new coalition agreement will have its effect on the budget for next year. The Division therefore intends to publish an interim assessment of the budget, as soon as this new coalition agreement has been incorporated in the budget and the long-term figures.

In the interest of the quality and accuracy of the assessment to be drawn up, the Division was given access to a draft version of the Budget Memorandum. The Division then drew up a draft assessment on the basis of this, which was subsequently discussed with the government. After hearing the response by the government, the Division drew up its definitive assessment. The full government response is included in this report.

This 2017 September Report is structured as follows. In this section A the report starts with the assessment. The analytical part that substantiates this assessment is included in section B. The government response is included in section C.¹

¹ Sections B and C are not included in this English translation.

2. The macro-economic and budgetary outlook

According to the most recent projections of the CPB, the Dutch economy will continue to grow strongly this year and next year.² The CPB estimates an economic growth of 3.3% for this year and 2.5% for 2018. These favourable economic prospects have a positive effect on the labour market. Employment is on the rise and unemployment continues to decrease. Whereas 6.0% of the labour force (538,000 persons) was still unemployed in 2016, this will drop to 4.9% (440,000) in 2017 and to 4.3% (390,000) in 2018. The current growth expectations are significantly better than last spring's, in the 2017 Central Economic Plan (CEP).

Public finances are also performing favourably. In 2016, the government budget showed a surplus of 0.4% GDP for the first time since 2008. This development will continue this year and next year. The actual budget balance will amount to 0.6% GDP in 2017 and 0.8% GDP in 2018. According to the current estimates, the government debt will amount to 57.2% GDP in 2017 and 53.7% GDP in 2018.

3. Assessment against the fiscal rules

In its September Report, the Division assesses whether the public finances in the current year and next year will comply with the European fiscal rules. As the actual budget deficit is below the maximum deficit of 3% GDP, as permitted under the Stability and Growth Pact (SGP), the rules from the so-called 'preventive arm' of the Pact are relevant in this assessment. These rules impose requirements on (the development of) the so-called structural budget balance (the budget balance adjusted for the economic cycle and incidental items) and on the development of the government expenses. Moreover, the government debt must be below 60% GDP, or in any case approach this threshold to a sufficient extent.

On the basis of the 2018 Macroeconomic Outlook (MEV) of the CPB, the Division concludes that Dutch public finances are expected to comply with the European fiscal rules this year and next year. According to the current projections, the structural balance in 2017 and 2018 will continue to meet the medium-term budgetary objective of -0.5% GDP that applies to the Netherlands. As the structural balance will exceed the target in 2017 and 2018, the expenditure rule can be disregarded on the basis of the work method of the European Commission. Nonetheless, the Netherlands will comply with the expenditure rule in both years. Finally, it is expected that the government debt will be below 60% GDP in both years. As a result, the government debt complies with the European debt criterion.

The Division emphasises that the current projections are based on a budget with (relatively) few new policy proposals for the year 2018. Updating the budget as a result of a coalition agreement to be concluded may change the outcome of the assessment.

² CPB, Macroeconomic Outlook 2018, September 2017.

4. Fiscal policy for the medium term

For the medium term – the period 2018 up to and including 2021 – the CPB expects an economic growth of 1.8% per year. According to the August update of the Medium-Term Outlook,³ unemployment will amount to 4.6% in 2021. Public finances will perform favourably for the medium term. For 2021, the CPB estimates an actual budget balance of 1.6% GDP. The structural balance would also amount to 1.6% GDP in 2021. According to the estimate, the government debt will continue to decrease to 45.0% GDP at the end of 2021. The sustainability balance amounts to 0.2% GDP in the update. This means that on balance there is still a slight sustainability surplus, but it is less than estimated in spring 2017. Obviously, the budgetary effect of a new coalition agreement has not been considered in these figures.

The Division notes that the estimates for the budget balance and the government debt were subject to a relatively great uncertainty in recent years. It has proven difficult for policymakers to deal with this uncertainty. In recent years there have sometimes been budget cuts, also in order to comply with the European fiscal rules. In retrospect, these were not always necessary to this extent. Such sometimes abrupt budget cuts may result in much administrative, political and social unrest and are therefore undesirable, all the more because the budget policy has often reinforced the cyclical trend from an economic viewpoint in the past twenty years.

The Division therefore repeats its comment from the 2017 Spring Report that, when setting a medium-term target for the budget balance for the next cabinet period, the volatile nature of Dutch public finances argues for keeping sufficient distance in respect of the medium-term objective ensuing from the European fiscal rules. This way, a (fiscal) policy that promotes stability and growth can be conducted consistently, in conformity with the principles and intentions of the Stability and Growth Pact.

5. Conclusion

The findings and conclusions, as well as the government response to the draft assessment (see part C), result in the following assessment by the Advisory Division of the Council of State.

- I. Based on the current projections of the CPB, the Division concludes that Dutch public finances are expected to comply with the European fiscal rules in 2017 and 2018. It should be noted, however, that the budgetary effect of a new coalition agreement to be concluded has not been considered in the estimates for the year 2018.
- II. When setting a medium-term target for the budget balance for the next cabinet period, the volatile nature of Dutch public finances argues for keeping sufficient distance in respect of the medium-term objective ensuing from the European fiscal rules. This way a (fiscal) policy that promotes stability and growth can be conducted consistently, in conformity with the principles and intentions of the Stability and Growth Pact.

³ CPB, Update Medium-Term Outlook (MLT), 16 August 2017.