

SUR/08/48

May 28, 2008

**The Acting Chair's Summing Up**  
**Kingdom of the Netherlands—Netherlands—2008 Article IV Consultation**  
**Executive Board Meeting 08/44**  
**May 21, 2008**

Executive Directors agreed with the thrust of the staff appraisal. They noted that sizeable fiscal consolidation and stability-oriented macroeconomic policies, complemented by broad-based structural reforms, have underpinned an extended period of strong growth, outperforming the EU average, and have shielded the economy from the recent global financial turmoil. Directors considered that, despite an expected deceleration in growth following the U.S. economic slowdown, near-term prospects remain favorable, with real GDP expected to continue expanding above the EU average. They acknowledged, however, that the outlook is subject to greater-than-usual uncertainty.

Directors noted that imminent population aging—which will shrink working age population starting early in the next decade—and comparatively low productivity growth could pose considerable challenges to long-term fiscal sustainability and external competitiveness. It will therefore be important to make early progress on labor and product market reforms aimed at raising the employment rate and stimulating faster productivity gains.

Given the expected above-potential output and tight labor market, most Directors agreed that a somewhat tighter fiscal stance for 2008 and 2009 would be appropriate from both long-term sustainability and cyclical perspectives, while acknowledging that the scope for reducing current expenditures might be limited at the present juncture of an economic downturn. Should growth turn out to be markedly lower than projected, automatic stabilizers should be allowed to operate fully. Directors welcomed the commitment of the government to a medium-term structural surplus target of 1 percent of GDP, although most saw scope for a further gradual improvement in the structural primary balance (net of gas proceeds), noting that frontloading the fiscal adjustment would limit the size of the needed fiscal correction and distribute the burden more equitably across generations.

Directors concurred that fiscal adjustment should rely on spending restraint and a broadening of the tax base, given relatively large tax wedges on labor income. Possible sources of savings include efforts to control health care spending, improvements in public sector efficiency, an increase in the effective retirement age, and a reduction in

unemployment benefits. Directors also called for increased transparency of tax expenditures to strengthen budgetary discipline.

Directors welcomed the ongoing efforts and the recent announcement of new measures to ease growing labor shortages and the impact of population aging. In this regard, reforms of the tax system and social entitlements should aim to reduce the effective marginal tax rates on second family earners, target tax incentives to induce participation by the elderly, and tighten the enforcement of work availability requirements and reassessments of disability status. Directors encouraged the authorities to further liberalize the rigid employment protection legislation and to adopt other measures with a view to further enhancing labor mobility.

Directors welcomed the authorities' "innovation pillar" and additional efforts to reduce red tape to promote productivity growth. Noting that barriers to entrepreneurship and product market regulation remain relatively high, Directors recommended careful liberalization to facilitate the emergence of innovative firms, which can make greater use of productivity-enhancing information technologies.

Directors observed that the Dutch financial system is healthy and well poised to weather the global turmoil, and they strongly welcomed the enhanced supervisory and regulatory framework. In view of growing risks associated with cross-border financial integration and increased use of structured products, Directors underscored the importance of strengthening cooperation and information-sharing among supervisors in home and host countries, as well as transparency in reporting complex products, while increasing cost efficiency and equity capital.

Directors noted the staff's assessment that overvaluation of the Dutch housing market is only minor, while stressing that high household mortgage indebtedness, and house price developments in general, warrant careful monitoring. They saw benefit in regulatory action to reduce high loan-to-value ratios, improve the measurement of related collateral, and fine-tune capital requirements for loans with different risks. Gradual removal of mortgage interest deductibility would contribute to decrease loan-to-value ratios, thereby lowering households' vulnerability to house price swings and interest rate shocks.

Directors commended the authorities' continued commitment to high levels of Official Development Assistance.

It is expected that the next Article IV consultation with the Netherlands will be held on the standard 12-month cycle.