INTERNATIONAL MONETARY FUND
Public Information Notice

EXTERNAL RELATIONS DEPARTMENT

Public Information Notice (PIN) No. 10/17
FOR IMMEDIATE RELEASE
February 2, 2010

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

IMF Executive Board Concludes 2009 Article IV Consultation with the Kingdom of the Netherlands—Netherlands

On January 11, 2010, the Executive Board of the International Monetary Fund (IMF) concluded the Article IV consultation with the Kingdom of the Netherlands—Netherlands.[1]

Background

The Netherlands has proven markedly vulnerable to the global crisis given its large financial sector and strong trade and financial linkages. Amid collapsing exports and investment, GDP is expected to have contracted by about 4 percent in 2009, with a negative output gap keeping inflation subdued. Unemployment has remained low so far, partly because of government-subsidized temporary reduced-hours schemes. External competitiveness remains adequate.

While the mortgage and housing markets have been relatively stable so far, banks have suffered major losses, particularly from foreign troubled assets and sizeable declines in asset prices, requiring substantial state intervention. Insurance sector profits and solvency as well as pension funds' average funding ratios also dropped sharply.

Government assistance to the financial sector has included capital injections, nationalization, and government guarantees. In addition, deposit insurance and

---

[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. An explanation of any qualifiers used in summings up can be found here: http://www.imf.org/external/np/sec/misc/qualifiers.htm.

systemic liquidity were enhanced in line with EU-wide measures. The state is committed to restoring the intervened banks to health, and is actively engaged in their ongoing restructuring. Pension funds have been given a longer period of five years to restore funding ratios. Reforms of executive compensation are also being contemplated to further buttress the financial system.

Large fiscal deficits of 4½ percent of GDP and 6 percent of GDP are expected in 2009 and 2010, respectively, reflecting the cyclical downturn, a discretionary stimulus package, and expenditure ceilings based on favorable growth prospects that were not adjusted downward in line with declining GDP. Public debt has surged as a result of the ongoing budget relaxation and the financial sector assistance. Together with higher estimates of long-run aging pressures, the worsening budget position has raised the estimated fiscal sustainability gap substantially to about 8 percent of GDP.

The authorities are laying the groundwork for ambitious fiscal consolidation from 2011 onward, as recovery firms. Measures totaling 1¾ percent of GDP have already been announced. Moreover, nineteen working groups have been set up to formulate by Spring 2010 proposals for savings of up to 20 percent of budget expenditure. Another group is tasked with reexamining tax policy within the same time-frame. Plans are also underway to embed Dutch obligations under the Stability and Growth Pact into law, to help strengthen the commitment to deficit reduction.

Executive Board Assessment

Executive Directors noted that the Netherlands has been dealt a severe blow by the global crisis given its large financial sector and strong trade and financial linkages. While the mortgage and housing markets appear relatively stable, banks have suffered major declines in asset quality, profits, and capital, and lending conditions have tightened. The fiscal position has weakened considerably because of the cyclical downturn, sizable stimulus to buoy economic activity, and massive financial sector bailout. Against this background, real GDP is expected to suffer an unprecedented fall in 2009, with a rather modest recovery expected in 2010.

Directors welcomed the authorities' prompt and comprehensive actions to mitigate the effects of the crisis, while agreeing that the authorities' focus should gradually turn to an exit from the exceptional support measures as the economy recovers.

Directors concurred that the authorities' interventions in the financial sector have been appropriate. Nonetheless, they stressed that additional bank capital, particularly equity, might be required because of the likely losses associated with the ongoing recession, the need to augment existing capital buffers, and an expected increase in lending when the crisis subsides. Directors also underscored that further measures, in concert with the EU, will be needed to ameliorate the counter-cyclicality of bank capital, and the transparency and robustness of valuation.

In addition, Directors emphasized that the financial system should be bolstered by regulatory and supervisory reform to strengthen capital standards for securitizations, resecuritizations, and high-LTV-ratio mortgages. A reduction of incentives for high LTV

loans, such as mortgage interest deductibility, is desirable. Directors also considered that cross-country supervision and resolution, as well as deposit insurance and fiscal burden-sharing, should be strengthened together with EU regulators.

Directors welcomed the authorities' early preparations for the eventual exit from financial sector support measures. They advocated completion of institution-specific restructuring and divestment plans for the large entities in which the state has injected equity or quasi-equity. Directors encouraged continued careful monitoring of vulnerabilities in the financial sector during the exit process.

Directors supported the accommodative budgetary stance envisaged by the authorities for 2009-10. A continuing fiscal relaxation is warranted in light of sizable negative output gaps and the still fragile prospects for economic recovery. However, Directors expressed concerns that the significant contribution of recurrent spending to the fiscal loosening will prove difficult to reverse.

Directors welcomed the authorities' plans for strong and credible fiscal consolidation starting in 2011 provided economic growth firms, given a fiscal sustainability gap much larger than in recent years. They recommended erasing the sustainability gap gradually, but with sufficient frontloading to lend credibility to the endeavor.

Directors noted that there is limited scope to raise tax rates, while efficiency enhancements should create scope to reduce spending without jeopardizing public service provision. Pension, health, and old-age-care reforms are crucial to containing—particularly aging-related—expenditure. Directors therefore looked forward to the proposals for spending cuts and tax reforms by the government working groups.

Directors noted that Dutch budgeting rules could be modified in the future to amend expenditure ceilings in order to reduce procyclicality and allow for discretionary fiscal impulses in case of sharp contractions. Many Directors cautioned, however, that adding excessive flexibility to the fiscal rules could weaken their usefulness as a disciplining device, lower transparency, and hamper fiscal planning.

Directors emphasized that additional structural reforms would alleviate the adverse impacts of the crisis and population aging on growth. They noted the staff's assessment that the real effective exchange rate is broadly in equilibrium. A number of Directors, however, were of the view that the Netherlands's relatively high unit labor costs could possibly lead to concerns with regard to external competitiveness going forward.

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.

Netherlands: Selected Economic and Social Indicators

	2005	2006	2007	2008	2009 1/	2010 1/
Real economy (change in percent)						
Real GDP	2.0	3.4	3.6	2.0	-4.0	1.3
Domestic demand	1.4	4.0	2.3	2.7	-3.7	0.8
CPI (harmonized)	1.5	1.7	1.6	2.2	0.9	1.0
Unemployment rate (in percent)	4.7	3.9	3.2	2.8	3.5	4.9
Gross national saving (percent of GDP)	26.3	29.3	27.3	28.0	25.0	25.2
Gross investment (percent of GDP)	19.0	20.0	19.7	20.5	18.0	18.3
Public finance (percent of GDP)						
General government balance	-0.3	0.6	0.3	0.8	-4.5	-5.9
Structural balance	-0.3	0.4	-1.1	-1.0	-4.0	-4.7
General government debt	51.8	47.4	45.5	58.2	58.9	63.9
Interest rates (percent)						
Money market rate 2/	2.1	3.0	4.0	3.8	1.1	...
Government bond yield 2/	3.4	3.8	4.3	4.2	3.8	...
Balance of payments (in percent of GDP, unless otherwise indicated) 3/						
Trade balance	7.4	7.2	7.0	6.5	5.4	5.3
Current account	7.3	9.3	7.6	7.5	7.0	6.8
Exports of goods and services	66.6	70.1	71.6	72.8	64.2	64.5
Volume, growth (in percent)	6.0	7.3	6.7	2.7	-9.8	1.0
Imports of goods and services	58.0	61.6	63.0	64.8	56.6	57.2
Volume, growth (in percent)	5.4	8.8	5.1	3.7	-9.2	0.8
Net oil exports (billions of US$)	-1.4	-0.5	-3.7	2.2	1.5	1.8
Net foreign direct investment	-13.2	-8.5	11.5	-7.0	-3.8	-3.8
Official reserves, excl. gold (US$ billion) 2/	9.0	10.8	10.3	11.5	12.5	...
Exchange rate						
Exchange rate regime						
U.S. dollar per euro	1.19	1.32	1.46	1.36	...	...
Nominal effective rate (2000=100) 2/	100.0	100.5	102.3	105.0	...	...
Real effective rate (2000=100) 2/ 4/	100.0	99.7	100.7	102.9	...	...

Sources: International Financial Statistics; OECD; Eurostat; Dutch authorities; and IMF staff estimates.
1/ Staff projections.
2/ As of July for 2009.
3/ Transactions basis.
4/ Based on relative normalized unit labor costs.