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In-depth review for The Netherlands

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European Commission

The Netherlands

In-Depth Review 2023



On the basis of this in-depth review for the Netherlands undertaken under Regulation (EU) No 1176/2011 on the prevention and correction of macroeconomic imbalances, the Commission has considered in its Communication "European Semester – 2023 Spring Package" (COM(2023) 600 final) that:

The Netherlands continues to experience imbalances. Vulnerabilities relating to high private debt levels and a large current account surplus, which have cross-border relevance, persist despite some signs of reduction. The current account surplus, despite recent data revisions, and private debt are large by international standards as well as above the fundamentals of the economy. The large current account surplus dropped in 2022, driven by worsening terms of trade, with the current account in constant prices increasing, and by a widening of the deficit in primary incomes. With improving terms of trade, the surplus is expected to rebound markedly in 2023 and stabilise in 2024. Limited policy progress has been made but more needs to be done to reduce obstacles to investment. Non-financial corporation and household debt remains high: the latter is more of a concern as it makes households vulnerable to shocks, with those risks exacerbated by the high and rising overvaluation of house prices. Going forward, debt is expected to continue on its moderately decreasing path. Despite moderately falling house prices, pressure on the housing market remains, notably as new housing construction remains significantly below government targets. At the same time, debt-financed homeownership continues to be subsidised by favourable taxation, while policies regarding the private rental market risk undermining its development.

CONTENTS

1. Introduction 4

2. Assessment of macroeconomic vulnerabilities 5

LIST OF TABLES

Table 2.1: Selected economic and financial indicators (Part 1), The Netherlands 16
Table 2.2: Selected economic and financial indicators (Part 2), The Netherlands 17

LIST OF GRAPHS

Graph 2.1: Revisions to Dutch primary income balance (as % of GDP) 7
Graph 2.2: Net lending/net borrowing by sector (in % of GDP) 8
Graph 2.3: Selected graphs (Part 1), the Netherlands 12
Graph 2.4: Selected graphs (Part 2), the Netherlands 13
Graph 2.5: Components of gross fixed capital formation deflator growth and consumer price inflation 14
Graph 2.6: Impact of Dutch value added inflations on EU partners' consumer price inflation 15

1. INTRODUCTION

In 2022, over the previous annual cycle of surveillance under the Macroeconomic Imbalances Procedure (MIP), the Commission identified "macroeconomic imbalances" in the Netherlands. ([1]) These imbalances were related to high private debt and a large current account surplus, which carry cross-border relevance. The 2023 Alert Mechanism Report published in November 2022 concluded that an in-depth review (IDR) should be undertaken also this year for the Netherlands with a view to assessing the persistence or unwinding of imbalances. ([2])

The Dutch economy proved to be resilient in 2022 but growth is expected to slow in 2023 as high inflation and tightening financial conditions affect consumption and investment growth. ([3]) Real GDP in the Netherlands reached its pre-pandemic trend in Q2 2022, thereby showing a faster and more complete recovery than most other EU Member States. Despite inflation picking up significantly as a result of Russia's invasion of Ukraine, consumer spending held up well throughout 2022, and overall real GDP growth came in at 4.5%. However, the high inflation rates have eroded households' purchasing power, which is expected to result in slower private consumption growth in 2023. In addition, tightening financial conditions, labour shortages and high input prices are expected to weigh on business investment while external demand weakens. Overall, real GDP growth is forecast to slow to 1.8% in 2023. Growth is forecast to pick up to 1.2% in 2024 as inflation rates are expected to come down, leading to a modest recovery in private consumption and business investment, while sizeable public investments also underpin growth. Russia's war of aggression led to surging energy and food prices in 2022, with annual HICP inflation reaching 11.6%. Energy prices have come down since the peak in Q3 2022, but core inflation continued to pick up until early 2023 as businesses pass higher input prices onto consumers. As core inflation starts to decrease gradually and energy prices drop further, inflation is forecast to come down to 4.9% in 2023 and 3.3% in 2024. The main uncertainty with regard to the economic outlook concerns the development of energy prices, which have been volatile in the past year. In a more adverse scenario, with a cold winter in 2023/2024 and insufficient supply of gas, the growth outlook would likely worsen while inflation would pick up again.

This in-depth review presents the main findings of the assessment of macroeconomic vulnerabilities for the Netherlands. Vulnerabilities related to housing in the Netherlands are also discussed in a horizontal thematic note that was already published. ([4]) The MIP assessment matrix is published in the 2023 Country Report for the Netherlands. ([5])

([1]) European Commission (2022), European Semester Spring Package 2022, COM(2022) 600 final.

([2]) European Commission (2022), Alert Mechanism Report 2023, COM (2022) 381 final.

([3]) European Commission (2023), European Economic Forecast: Spring 2023, Institutional Paper 200.

([4]) European Commission (2023), Housing Market Developments: Thematic Note to Support In-Depth Reviews, European Economy: Institutional Papers, 197.

([5]) European Commission (2023), Country Report the Netherlands 2023, SWD(2023) 619 final.

2. ASSESSMENT OF MACROECONOMIC VULNERABILITIES

Gravity, evolution and prospects

The current account surplus, after a rebound to 7.3% of GDP in 2021, decreased to 4.4% in 2022. It continues to be among the highest in the euro area as a share of GDP and well above levels justified by fundamentals ('current account norm', ([6]) estimated at 1.6% of GDP in 2022). A persistently high trade surplus in goods and services remains the main contributor to the Dutch current account surplus. The slight downward trend in the goods surplus over the past years has been compensated by upward trending surpluses in services trade, largely driven by increasing net exports by the ICT sector and increasing charges for the use of intellectual property. The primary incomes balance is on a decreasing path. A revision to balance of payments statistics for the Netherlands has led to a reduction in the current account for all years since 2015; this is explained in Box 1.

From a sectoral and savings perspective, all domestic sectors have been contributing to the net savings surplus over the past decade, but non-financial corporations (NFC) and households are the main drivers. The NFC sector's contribution can be explained by low domestic investment rates compared to EU averages. However, research by Statistics Netherlands that led to a downward revision of the Dutch current account balance (see box 1 for more details) showed that the contribution of NFCs to the total economy's net lending had been overestimated for large parts of the last decade ([7]). More firms active in the Netherlands than previously assumed are foreign owned, with profits flowing to parent companies in the rest of the world, thus not leading to acquisition of assets abroad. Household savings are an important constituent of the Dutch current account surplus. These are driven by deleveraging pressures after the global financial crisis and high compulsory second pillar pension savings. The government budget balance has also been in surplus for several years prior to the pandemic due to rising tax revenues and consolidation efforts but entered net borrowing territory in 2020. In four quarters up to Q3 2022, the government became net lender again.

On 5 April 2023 the Commission presented a horizontal thematic note on external balances based on data up until Q3 2022, which covered the Netherlands. The note showed that the main drivers behind the decrease in the surplus in 2022 are primary incomes and rising energy prices. The balance of primary incomes as a share of GDP dropped, sparked mainly by increasing earnings of non-residents on their Dutch investments. An additional contribution to the narrowing of the current account surplus came from the energy balance, due to strongly increased

([6]) The 'current account norm' is the current account balance that can be explained by fundamentals. It is based on an empirical setup similar to IMF's EBA (Phillips, S., Catão, L., Ricci, L., Bems, R., Das, M., Di Giovanni, J., Unsal, D.F., Castillo, M., Lee, J., Rodriguez, J., and Vargas, M. (2013), "The external balance assessment (EBA) methodology", International Monetary Fund Working Paper 13/272). Fundamentals are slow-moving variables including, e.g. natural resources, demographics, or relative income. For details see Coutinho, L., Turrini, A., Zeugner, S. (2018), "Methodologies for the assessment of current account benchmarks", European Economy, Discussion Paper 86/2018.

([7]) Nelisse, R. (2021), Non-financial corporations split into subsectors, Statistics Netherlands Discussion Paper

energy prices. As a result of rising energy prices and a return to pre-pandemic consumption patterns, net lending by households decreased substantially. The horizontal note also showed that domestic absorption outgrew GDP in the Netherlands in the first three quarters of 2022 in nominal terms, while in real terms, GDP growth was slightly higher than domestic absorption growth. Net lending by non-financial corporations spiked to 11.3% of GDP in Q3 2022 due to a multinational's one-off transfer of intellectual property rights ([8]). The government sector recorded a return to net lending territory as of Q3 2022 after consecutive deficits in 2020 and 2021.

Revisions of the surplus reduced the headline number, which was temporarily below the MIP threshold of 6% of GDP in 2022. However, closing the existing investment gaps between the Netherlands and peer economies could be needed for the current account surplus to remain below the threshold as improving terms of trade are expected to lead to a rebound of the surplus in 2023 and 2024. Business investment in particular is lower than that of peer economies. Gross fixed capital formation by non-financial corporations as a share of their value added stood at 17% in the fourth quarter of 2022 in the Netherlands, compared to a Euro Area average of 23% (see graph 2.4 d). Both private and public investments are held back by a tight labour market and restrictions related to environmental regulations. In its spring budget, the government reports that in 2022, spending was EUR 2.7 billion lower than foreseen, partially due to the reasons cited above ([9]). In addition to rising interest rates these factors also drive lower investments in construction and dwellings. Building permits, an early indicator for construction activity, are around 22% lower than a year before in February 2023 and have been falling since July 2022 (see graph 2.3 f). Dwellings are also the investment category in which the gap between the Netherlands and the Euro Area average is largest. Removing obstacles that are currently holding back these investments could boost housing supply and could therefore contribute to external rebalancing as well as the better functioning of the housing market.

The current account surplus is forecast to increase to 5.9% in 2023 and 6.1% in 2024. Structural drivers underpinning high household and corporate savings over time, are expected to continue to contribute to the current account surplus with temporary factors relating to the energy prices abating. High mandatory pension savings are also expected to continue contributing to the surplus. The falling number of multinationals located in the Netherlands could have a dampening effect on the surplus over the coming years. Terms of trade are expected to be largely determined by the evolution of energy prices and are set to improve in 2023 relative to 2022. In 2024 they are expected to remain largely constant. This is forecast to lead to a rebound in the current account surplus over the next two years, reaching 6.1% in 2024.

([8]) The transaction is recorded in the capital account and therefore does not contribute to the current account surplus.

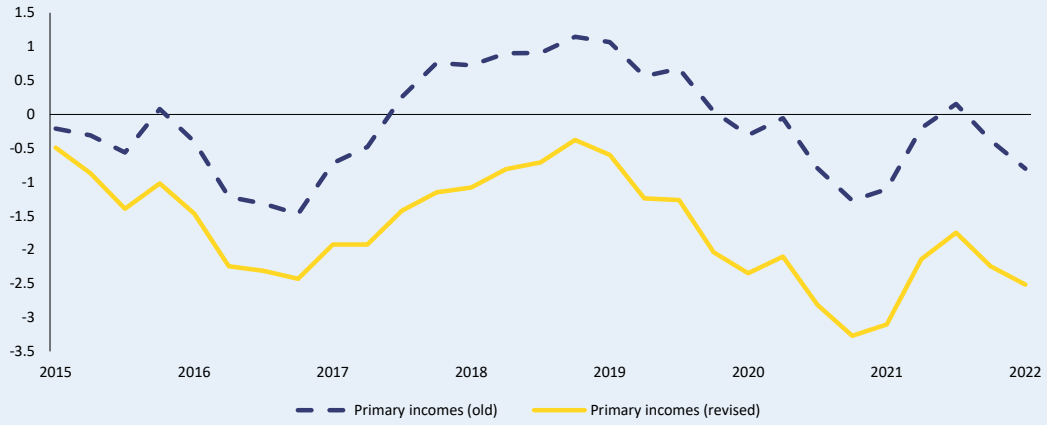
([9]) See Table 2.1.2 "Onderuitputting 2022" in Najaarsnota 2022

Box 1: Data revision of Dutch current account

The Dutch central bank has revised balance of payments statistics for the Netherlands. These revisions shift the Dutch current account surplus downwards by 1-2 percentage points per year since 2015. The revisions are the results of an improvement of statistics on the ownership structure of foreign-controlled non-financial corporations in the Netherlands as well as the recording of Dutch multinationals' income from foreign subsidiaries ([10]).

Large part of the adjustment is due to Statistics Netherlands' efforts to make use of all available information on the parent companies of firms registered in the Netherlands ([11]). As a result, more firms than previously assumed are now known to be controlled by foreign entities. These firms' retained earnings (i.e. profits used to strengthen the firms' equity or to finance investments) therefore need to be attributed to the parent enterprise, thus counting to gross national income (GNI) of the foreign country in which the parent is based instead of Dutch GNI. Mechanically, this leads to downward revisions of the primary income balance of the Netherlands as more retained earnings than previously assumed are transferred to the rest of the world. A second, smaller, revision is due to corrections to the recording of Dutch multinationals' income from foreign subsidiaries regarding the capitalisation of exploration expenses, R&D and software in the balance of payments. Taken together, between 2015 and 2020, the primary income balance as a share of GDP has been revised downwards by about 1.5 percentage points on average. The size of the revision has grown over time reaching about 2 percentage points since 2020. Primary incomes are the only current account component affected by the revisions. Revisions to the overall current account balance are therefore of equal size. As Graph 2.1 shows, the revision reinforces the trend of a widening deficit in primary incomes of the Dutch economy since 2019.

Graph 2.1: **Revisions to Dutch primary income balance (as % of GDP)**



Source: European Commission services

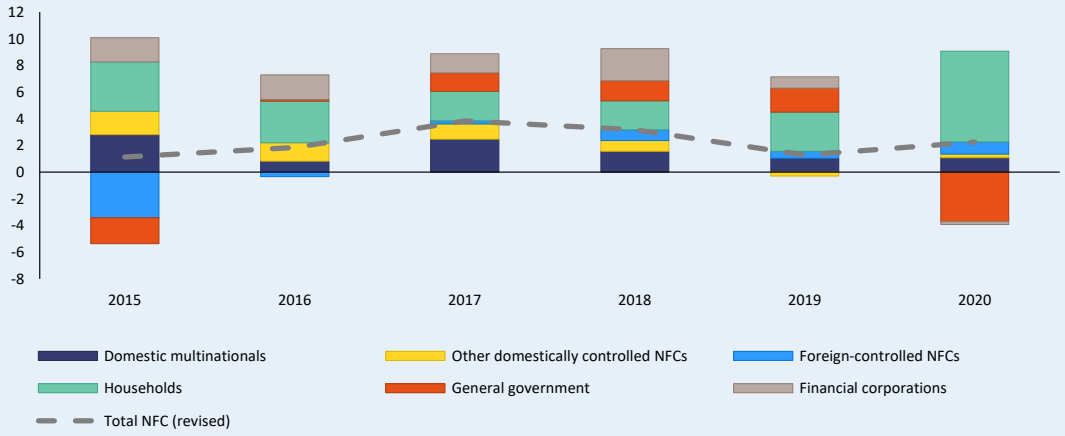
Downward revisions of the current account balance imply that the Dutch economy has made less resources available to the rest of the world. Net lending statistics show which sectors are responsible for this reduction. The majority of the adjustment comes from non-financial corporations (NFC) as their ownership status was the main subject of the analysis by Statistics Netherlands. However, the analysis showed that several NFCs located in the Netherlands have financial institutions as local parents that in turn are owned by the eventual foreign parent. Therefore, comparably small revisions were also made to financial corporations' net lending statistics. The household and government sector's contributions were not concerned. As a result of this analysis, statistics on net lending by NFCs between 2015 and 2020 can now be split up

([10]) Current account surplus revised sharply downwards (dnb.nl)

([11]) Nelisse, R. (2022). Non-financial corporations split into subsectors, CBS Discussion Papers

between different types of corporations. Graph 2.2 shows this breakdown as well as the net lending statistics for the rest of the economy. Dutch multinationals are the main contributor to the NFC sector's surplus. The combined domestically controlled NFC sector's net lending is on a downward trend over the period for which the detailed data is available. As a result of the revision, the relative role of households and the general government for the total economy's net lending has increased as these sectors were unaffected by the revisions.

Graph 2.2: **Net lending/net borrowing by sector (in % of GDP)**



Source: European Commission services

Private debt in the Netherlands stood at 215% of GDP in 2022 but is on a decreasing path. This value is composed of household debt, which accounts for 94% of GDP, as well as corporate debt, standing at 121% of GDP in 2022. In both sectors, debt levels are above prudential thresholds and significantly higher than EU and euro area averages. Despite positive growth of credit flows to the private sector since 2021, the private debt-to-GDP ratio has decreased on the back of real GDP growth and high inflation. Since its peak in 2015, private debt as a share of GDP has fallen by 46 pp. Private debt is expected to continue declining moderately while remaining significantly above the prudential threshold of 157% of GDP and EU as well as euro area averages (graph 2.3 a).

Household debt is largely composed of mortgage debt and its high level can be explained by features of the Dutch housing market and tax system that continue to incentivise debt-financed homeownership. These distortions include mortgage interest deductibility, which remains generous despite a recent reduction in the deductibility rate. In combination with high maximum borrowing limits, this is an important factor explaining the large household debt position in the Netherlands and the relatively high levels of illiquid assets and low levels of liquid assets. ([12]) This combination may put households in a vulnerable position. High mortgage debt also reinforces the procyclicality of household finances as house price corrections can lead to an erosion of net assets and result in reduced consumption by households. The majority of the stock of mortgages has interest rates fixed for more than ten years, limiting the direct impact of interest rate increases over 2022 on the financial situation of households. Among new mortgages, the share of those with variable interest rates has grown but the impact on the stock is limited due to rapidly falling transaction volumes on the housing market in 2022. Drivers of the downward trend in household debt of the past decade are stricter loan-to-value ratios after the financial crisis, complemented by

([12]) Ciurila, N., Van Heuvelen, H., Luginbuhl, R., & Smid, B. (2020). Are the savings of Dutch households optimal. CPB Notitie.

tighter capital-based macroprudential measures in 2021, imposing minimum average risk weights for the calculation of capital requirements applicable to mortgages on residential property.

The high level of corporate indebtedness is largely composed of intra-group debt of multinationals and hence represents a lower risk than the headline number suggests. According to data by Statistics Netherlands, multinationals accounted for about 70% of total corporate debt in the Netherlands in 2021. Financial stability risks stemming from corporate debt are therefore more limited than the high level suggests. The non-financial sector's debt as a share of GDP has fallen by 25 pp since 2015. Decreasing NFC debt is driven by tax measures taken by the government that limit incentives for corporations to accumulate debt as well as the attractiveness of the country as a seat for their headquarters. Additionally, bankruptcies in the Netherlands are below levels recorded prior to the pandemic despite the end of pandemic support measures. Gross non-performing loans (as a share of total loans) have also decreased further, reaching 1.2% in Q3 2022, down from 1.9% at the end of 2020.

On 5 April 2023 the Commission presented a horizontal thematic note on housing markets, which covered the Netherlands. It showed that strong house price growth in the past years has resulted in an overvalued housing market. Housing prices almost doubled in the last ten years, which has led to houses being approximately 26% overvalued in 2022 according to the Commission's model-based estimations (graph 2.3 d). Especially in the last two years house prices surged, by 15% in 2021 and 13.4% in 2022. Multiple factors contributed to the surging house prices and rising mortgage debt levels in the Netherlands, these included notably the low mortgage interest rates, the favourable tax treatment of debt-financed homeownership ([13]), insufficient and inelastic housing supply, the relatively lenient borrower limits ([14]) and the relatively high share of interest-only mortgages. In addition to this, the private rental market is relatively small and less attractive for households as it does not benefit from the same degree of subsidisation as owner-occupied housing. The overvaluation of housing has worsened affordability, with price to income and price to rent ratios standing significantly above historical averages. At the same time, the worsened affordability has resulted in the number of housing transactions coming down gradually in the past few years.

Tightening financial conditions are leading to a turning point in the housing market. Surging inflation rates have prompted the ECB and central banks outside of the euro area to raise their policy rates. As a result, interest rates of new mortgages have picked up considerably in the Netherlands, increasing from 1.6% (average of all maturities) in December 2021 to 3.83% in March 2023. ([15]) With households' borrowing capacity shrinking as a result of the higher mortgage rates, house prices have decreased by around 5.1% between the peak in July 2022 and March 2023. The drop in prices so far has been relatively limited, in part due to supply effects as the number of houses for sale has come down, likely due to prospective sellers intending to wait out the dip in prices. House prices are expected to fall further as the market adjusts to the much higher mortgage rates (graph 2.3 b and 2.3 e). External estimates of house price decreases in 2023 and 2024 range between around 6% ([16]) and 10% ([17]) and cumulatively.

Risks related to high mortgage debt levels in combination with falling house prices have increased but appear to be contained thus far. The average loan-to-value ratio has decreased since the financial crisis, mostly due to regulatory changes limiting the maximum loan-to-value

([13]) This notably includes the possibility to deduct mortgage interest payments from taxable income.

([14]) The maximum loan-to-value (LTV) ratio stands at 100%, significantly higher than most other EU countries.

([15]) https://www.dnb.nl/statistieken/dashboards/woninghypotheken/hypotheekrentes-banken/

([16]) DNB, Economische vooruitzichten en ontwikkelingen, December 2022.

([17]) ABN AMRO, Woningmarkt Monitor 2023, January 2023.

ratio and making interest-only mortgages less attractive. Nominal mortgage debt has increased by around 20% in the past ten years but debt relative to GDP has fallen from 100% in 2012 to 87% in mid-2022. According to the ESRB (February 2022), macroprudential policies and regulations were appropriate and partially sufficient with the stock and flow risks assessed as being high. Risks related to the commercial real estate sector have also increased with around 50% of loans backed by commercial real estate needing to be refinanced in the next three years. This increases refinancing and credit risks in this segment of the market. In more adverse scenarios, with a steep drop in house prices and a sharp slowdown in economic growth, the large debt position of households in combination with negative equity effects could act pro-cyclically and further worsen an economic downturn. The Dutch central bank estimates that a house price decrease of 20% could lead to 8% of owner-occupied houses being in negative equity, i.e. with mortgage debt higher than the value of the underlying collateral, while a price decrease of 30% would lead to close to 20% of houses being in negative equity. ([18])

Assessment of MIP relevant policies

The impact of recent policy steps on the structural drivers of the savings surplus is likely to remain limited. High mandatory savings imposed by the second-pillar pension system remain unaffected by the pension reform to be fully implemented by 2027. With regard to the corporate sector, a tax reform by which debt owned by controlling shareholders to their companies is partially taxed has been in force since January 2023. While the reform would help to limit the incentives for small and medium-sized businesses to retain earnings within their own company and increase incentives for investments, in practice it may only lead to a statistical effect, shifting part of small companies' savings surplus to the household sector. The impact on the overall savings surplus therefore remains uncertain. Increasing private investments would be an important step to reduce the country's current account surplus.

The authorities have focused their policy efforts on the supply side of the housing market, while steps to reduce the debt bias in the housing market remain insufficient. On the supply side, the authorities strive to build 900 000 new dwellings by 2030 in an effort to improve affordability and availability of housing. To achieve this, the authorities are aiming to speed up planning procedures and processes, take control of planning new construction at a central level and investing in removing bottlenecks to new construction projects, a measure that is part of the Dutch recovery and resilience plan (RRP). However, high inflation, labour shortages and a failure to meet environmental requirements related to nitrogen drive up the cost of new construction projects and could in practice lead to delays in delivering new dwellings. On the demand side, mortgage interest deductibility is gradually being reduced but remains generous. A substantial subsidy on debt-financed homeownership therefore remains, especially as the reduction in interest deductibility is coupled with a reduction in the imputed rent tax that is levied on owner-occupied houses. Furthermore, new policies announced by the authorities risk undermining the development of the private rental market further. Notably, the expansion of rent controls in the private sector could decrease the attractiveness of the sector for investors and lead to lower supply in this segment of the housing market. This risks increasing the bias toward debt-financed homeownership further. Tighter capital-based macroprudential measures introduced in 2021 were extended in 2022. These measures set a floor for risk weights on mortgages for banks and are expected to continue to discourage mortgage lending by banks to some degree.

The Netherlands has taken some measures to reduce tax incentives that led multinational firms to locate their headquarters in the Netherlands, which contributed to

([18]) DNB, Financial Stability Report, October 2022.

the high private debt levels as well as the current account surplus. Interest deductibility has been gradually reduced to 20% of the firm's earnings before interest, tax, depreciation, and amortisation (EBITDA). Additionally, a conditional withholding tax is levied on interest and royalty payments to affiliated companies in certain low-tax jurisdictions. This tax will be expanded to dividend payments as of 2024. These reforms are also part of the Dutch RRP. These measures have contributed to the relocation of multinationals' headquarters away from the Netherlands in recent years and are expected to continue contributing to decreasing private debt levels.

Conclusion

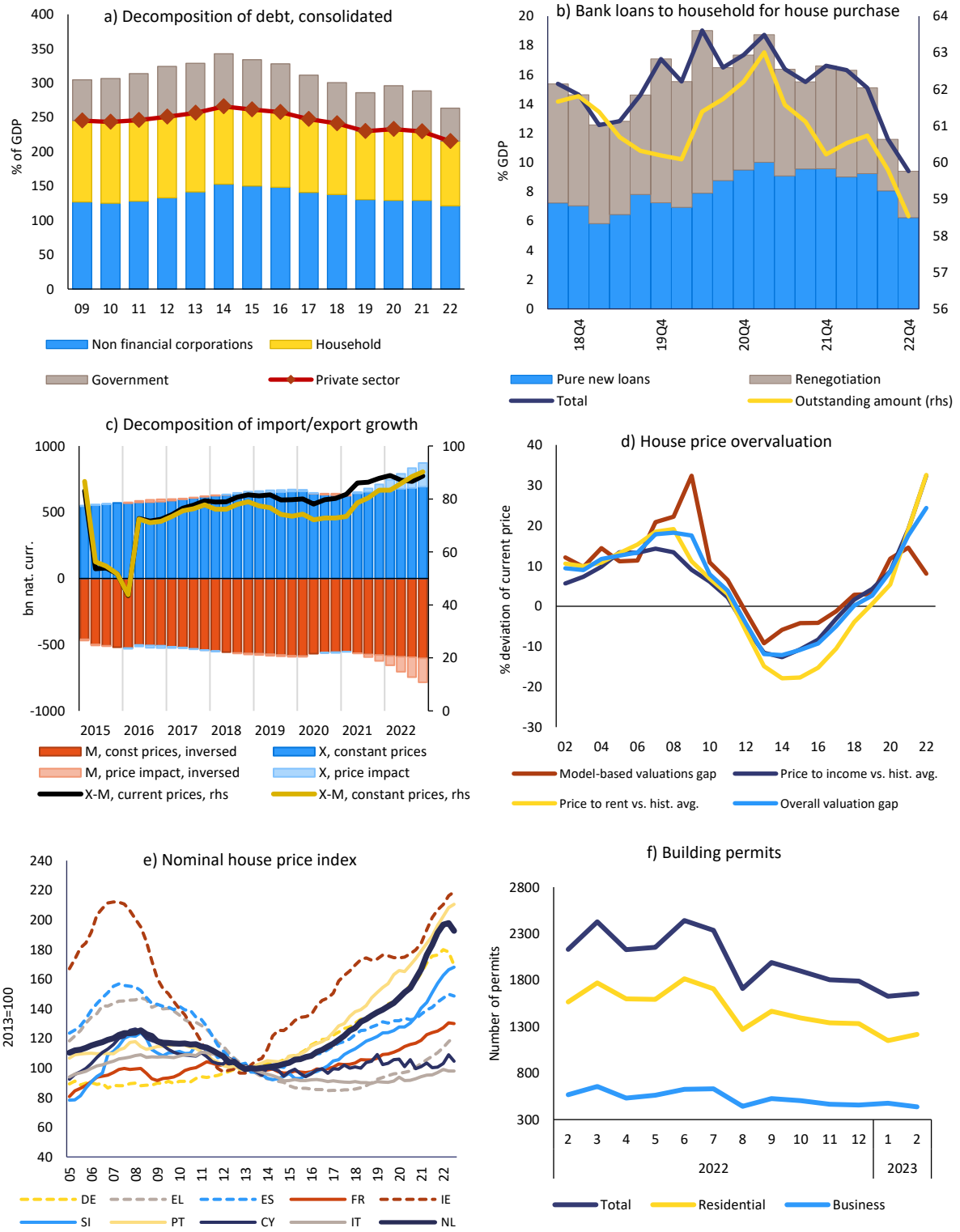
The Netherlands is facing vulnerabilities relating to high private debt levels and a large current account surplus. These vulnerabilities have cross-border relevance. The Netherlands has persistently recorded current account surpluses and private debt levels that are large both by international standards and above the fundamentals of the Dutch economy. The current account surplus stems from a large trade surplus. The drop in the surplus in 2022 can largely be explained by worsening terms of trade and a widening deficit in primary incomes. Revisions to current and historical current account series by the Dutch central bank have shifted the surplus downwards by about 2 pp. Private debt levels remain high due to both high NFC and household debt, with the latter being especially problematic as it makes households vulnerable to economic shocks, given that house prices seem to be overvalued. Going forward, the current account surplus is expected to rebound driven by improving terms of trade, while private debt is expected to continue on its moderately decreasing path. Despite moderately falling prices, risks on the housing market remain as policy changes by the government risk further increasing the homeownership bias.

Policy progress has been limited. In particular, debt-financed homeownership continues to be subsidised while policies regarding the private rental market risk being counterproductive. The efforts by the authorities to increase supply could have beneficial effects in the housing market in terms of improving affordability of housing but will only exercise their impact on house prices with a time lag. In addition, the authorities have not yet adequately addressed a ruling by the Dutch Council of State on nitrogen deposition, which could lead to large delays in current and future housing construction projects. The intentions of the authorities to regulate private rents could make the sector less attractive to investors and thereby affect rental supply. Regarding the elevated current account surplus, incentives for firms to retain earnings have only been partially addressed and high mandatory household savings through the pension system will remain in place despite the second pillar pension reform that will enter into force in 2027. Good progress has been made on reducing the incentives for firms to accumulate debt and to limit the possibilities for firms to use the Netherlands as a conduit country for tax purposes.

Based on the findings in this in-depth review, the Communication "European Semester – 2023 Spring Package" sets out the Commission's assessment as to the existence of imbalances or excessive imbalances in the Netherlands, in line with Regulation 1176/2011. ([19])

([19]) European Commission (2023), European Semester Spring Package 2022, COM(2023) 600 final.

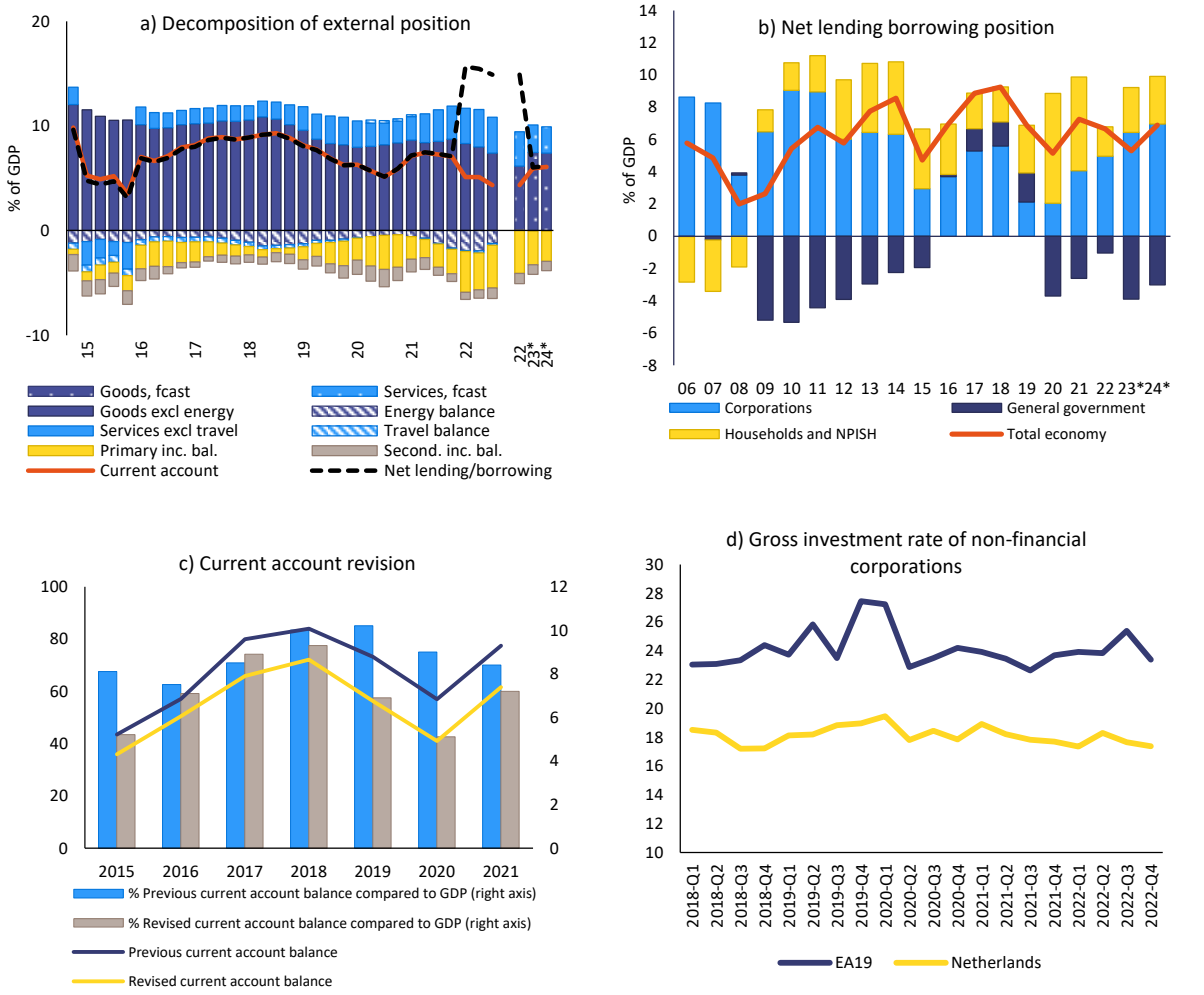
Graph 2.3: **Selected graphs (Part 1), the Netherlands**



4-quarters moving sums for all quarterly data unless stated differently; graph b: National Accounts data

Source: Eurostat, Ameco, De Nederlandsche Bank (DNB) and European Commission calculations

Graph 2.4: **Selected graphs (Part 2), the Netherlands**

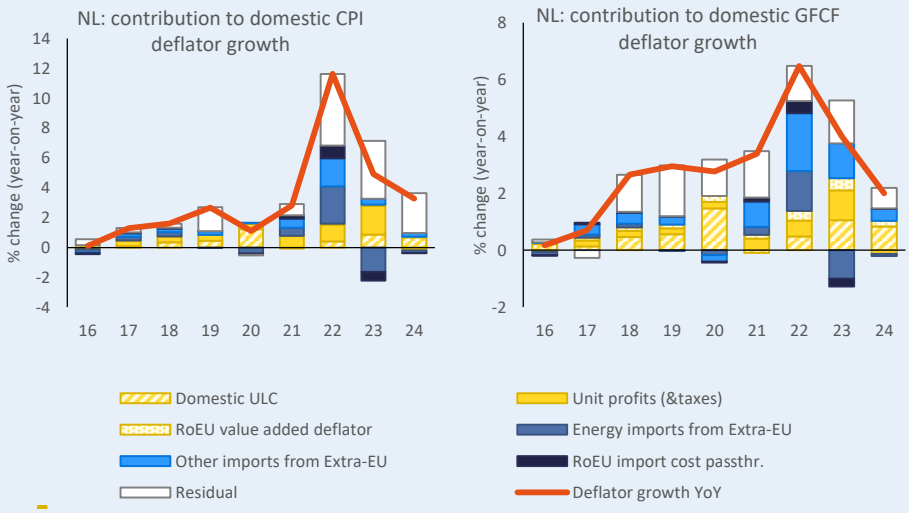


Source: European Commission services and Statistics Netherlands

Box 2: Inflation exposures and cross-border pass-through

This box sheds light on the sources of inflation in the Netherlands and its spill-overs with EU partners. The period since 2021 has been characterized by pandemic aftershocks and global supply chain disruptions compounding global inflationary pressures and a surge in commodity prices triggered by Russia's war of aggression against Ukraine. As a result, inflation in the Netherlands surged to unprecedented levels. In response, wages and profits also picked up across the EU. With input-output data, domestic inflation can be decomposed into the contribution from key cost factors. Taking into account some data limitations, the framework can be used to attribute consumer and investment price changes to i) extra-EU import price changes, which include both directly imported inflation and inflation passed through from EU partners import costs ii) domestic unit labour cost changes iii) domestic unit profit changes, including indirect taxation changes and iv) rest-of-EU value added price changes. ([20])

Graph 2.5: **Components of gross fixed capital formation deflator growth and consumer price inflation**



Source: European Commission services

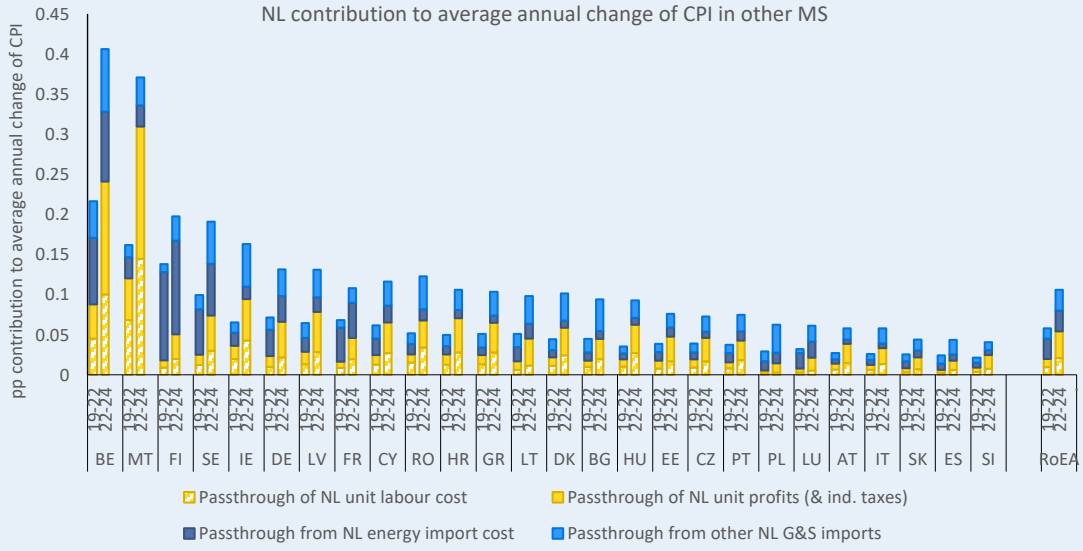
Data suggests that much of inflation in the Netherlands in 2022 reflected surging import prices, while the importance of domestic sources is expected to increase over the forecast horizon. In 2022, as shown in Graph 2.5, energy imports contributed substantially to the acceleration in consumption and investment inflation. The direct impact of non-energy imports from outside the EU was also significant, particularly for investment inflation. Spill-overs from other EU countries remained limited. Namely, import cost pass-through from EU partners increased domestic inflation somewhat, whereas value added inflation in other EU countries had a negligible impact. A relatively small part of consumer and investment inflation can be explained by the domestic value-added deflator, which covers wages and profits. This mainly reflects unit profits. Going forward, energy prices are set to lower inflation this year. The impulse from non-energy

([20]) The graphs below are based on national accounts data and the Commission's Spring 2023 forecast, which are combined through a 'Ghosh' matrix based on Eurostat's Figaro input-output available for 2015-2020. HICP is taken as the measure of the price of private consumption, including non-residents. Energy import prices from extra-EU reflect realised median prices until 2022, and energy price assumptions underlying the Spring forecast thereafter. Other goods prices reflect median European prices per industry until 2022, and forecast non-energy goods and service trade prices for 2023-2024. Value added deflators are assumed to affect all industries within a country to the same degree. Changes in import prices and value added deflators are assumed to affect demand prices with a delay of 1 month for consumption and investment inflation. For a similar analysis using an input-output-based methodology, see "Inflation Differentials in Europe and Implications for Competitiveness: Thematic Note to Support In-Depth Reviews" European Commission 2023, Institutional paper 198.

import prices is expected to subside but to remain positive. However, the contribution from both unit profits and unit labour costs is expected to increase in 2023. Spill-overs from inflation, including value added inflation, in other EU countries is set to remain marginal.

The impact of wages and profits in the Netherlands on other Members States remains limited, as domestic factors contributed only little to consumer and investment inflation. Although value added created in the Netherlands has a non-negligible impact on domestic demand in other Member States, Dutch value-added inflation remains contained vis-à-vis the significant impact from import prices in most cases. Overall, Dutch valued added inflation has contributed little to consumer inflation in the rest of the EU so far. Most exposed countries to inflation in the Netherlands are Belgium and Malta with the impact of up to 0.3 pps. p.a. over the forecast horizon (see Graph 2.6).

Graph 2.6: **Impact of Dutch value added inflations on EU partners' consumer price inflation**



Source: European Commission services

Table 2.1:**Selected economic and financial indicators (Part 1), The Netherlands**

all variables y-o-y % change, unless otherwise stated	2003-07	2008-12	2013-18	2019	2020	2021	2022	forecast 2023	forecast 2024
Real GDP	2.3	0.0	1.8	2.0	-3.9	4.9	4.5	1.8	1.2
Potential growth (1)	1.8	0.9	1.1	1.8	1.5	1.7	2.2	1.9	1.9
Contribution to GDP growth:									
Domestic demand	1.9	-0.7	1.4	2.3	-2.9	3.6	3.7	1.8	1.1
Inventories	0.0	0.0	0.1	0.3	-0.8	-0.1	0.0	-0.1	0.0
Net exports	0.3	0.8	0.2	-0.7	-0.1	1.4	0.9	0.0	0.0
Contribution to potential GDP growth (1)									
Total Labour (hours)	0.4	0.2	0.7	1.1	0.9	1.0	1.3	1.1	1.0
Capital accumulation	0.7	0.5	0.4	0.7	0.5	0.6	0.6	0.6	0.6
Total factor productivity	0.8	0.3	0.0	0.0	0.1	0.2	0.2	0.2	0.3
Output gap (2)	-0.9	-1.2	-1.0	1.4	-4.0	-1.0	1.2	1.1	0.4
Unemployment rate	5.7	5.8	7.1	4.4	4.9	4.2	3.5	3.8	3.9
Harmonised index of consumer prices (HICP)	1.7	1.9	1.0	2.7	1.1	2.8	11.6	4.9	3.3
GDP deflator	2.0	1.0	1.5	3.0	1.9	2.4	5.3	6.1	2.6
External position									
Current account balance (% of GDP), balance of payments	7.7	7.2	8.1	6.9	5.1	7.3	4.4	5.9	6.1
Trade balance (% of GDP), balance of payments	8.5	8.4	10.0	9.8	10.1	10.3	9.4	.	.
Primary income balance (% of GDP)	1.0	0.4	-0.7	-2.0	-3.3	-2.2	-4.1	.	.
Secondary income balance (% of GDP)	-1.8	-1.6	-1.2	-0.9	-1.7	-0.8	-1.0	.	.
Current account explained by fundamentals (CA norm, % of GDP) (3)	2.1	2.6	2.1	2.0	1.9	1.7	1.6	1.6	1.4
Required current account to stabilise NIIP above -35% of GDP over 20Y (% of GDP) (4)	-0.1	0.4	2.4	3.7	5.2	3.9	2.6	2.3	2.4
Capital account balance (% of GDP)	-0.4	-0.3	-0.1	0.0	0.0	0.1	10.6	.	.
Net international investment position (% of GDP)	-5.2	10.3	54.3	89.6	113.0	93.2	75.1	.	.
NENDI - NIIP excluding non-defaultable instruments (% of GDP) (5)	-67.4	-73.2	-39.3	-0.3	12.9	26.1	22.9	.	.
Net FDI flows (% of GDP)	4.6	5.8	6.0	-0.8	-10.1	9.9	8.5	.	.
Competitiveness									
Unit labour costs (ULC, whole economy)	0.8	2.3	1.1	3.2	8.5	-0.6	3.3	4.7	4.3
Nominal compensation per employee	2.3	2.2	1.3	2.8	4.8	2.2	3.9	5.5	4.8
Labour productivity (real, hours worked)	1.6	0.2	0.4	-0.7	-1.1	1.5	0.4	0.4	0.1
Real effective exchange rate (ULC)	-0.2	0.3	-0.4	0.9	4.5	-1.1	-0.3	-1.0	0.7
Real effective exchange rate (HICP)	0.6	-0.5	0.7	0.5	1.4	0.2	1.9	.	.
Export performance vs. advanced countries (% change over 5 years)	6.1	0.4	-3.5	-2.0	7.4	5.7	.	.	.
Private sector debt									
Private sector debt, consolidated (% of GDP)	228.5	243.3	255.1	229.9	233.1	229.5	215.3	.	.
Household debt, consolidated (% of GDP)	106.6	116.6	109.9	99.7	103.8	100.5	94.0	.	.
Household debt, fundamental benchmark (% of GDP) (6)	49.1	51.0	57.8	60.2	65.5	66.8	67.9	.	.
Household debt, prudential threshold (% of GDP) (6)	40.2	45.0	50.1	47.3	51.1	48.6	47.3	.	.
Non-financial corporate debt, consolidated (% of GDP)	121.9	126.7	145.2	130.2	129.3	129.1	121.3	.	.
Corporate debt, fundamental benchmark (% of GDP) (6)	106.7	96.0	94.3	93.6	101.0	102.6	104.2	.	.
Corporate debt, prudential threshold (% of GDP) (6)	62.3	68.0	76.3	73.8	81.8	76.1	74.1	.	.
Private credit flow, consolidated (% of GDP)	11.8	7.6	4.4	-0.3	-0.7	11.7	6.7e	.	.
Corporations, net lending (+) or net borrowing (-) (% of GDP)	7.9	6.9	5.0	2.1	2.0	4.0	3.8	6.2	5.9
Households, net lending (+) or net borrowing (-) (% of GDP)	-2.1	1.4	3.3	2.9	6.8	5.7	0.7	1.9	2.0
Net savings rate of households (% of net disposable income)	3.4	6.9	10.0	12.0	18.8	17.5	.	.	.

(e) estimate based on ECB quarterly data

(1) Potential output is the highest level of production that an economy can reach without generating inflationary pressures. The methodology to compute the potential output is based on K. Havik, K. Mc Morrow, F. Orlandi, C. Planas, R. Raciborski, W. Roeger, A. Rossi, A. Thum-Thysen, V. Vandermeulen, The Production Function Methodology for Calculating Potential Growth Rates & Output Gaps, COM, European Economy, Economic Papers 535, November 2014.

(2) Deviation of actual output from potential output as % of potential GDP.

(3) Current accounts in line with fundamentals ("current account norms") are derived from reduced-form regressions capturing the main determinants of the saving-investment balance, including fundamental determinants, policy factors and global financial conditions. See L. Coutinho et al. (2018), "Methodologies for the assessment of current account benchmarks", European Economy, Discussion Paper 86/2018, for details.

(4) This benchmark is defined as the average current account required to halve the gap between the NIIP and the indicative MIP benchmark of -35% of GDP over the next ten years, or to stabilise the NIIP at the current level if it is already above the indicative MIP benchmark. Calculations make use of Commission's T+10 projections.

(5) NENDI is a subset of the NIIP that abstracts from its pure equity-related components, i.e. foreign direct investment (FDI) equity and equity shares, and from intracompany cross-border FDI debt, and represents the NIIP excluding instruments that cannot be subject to default.

(6) Fundamentals-based benchmarks are derived from regressions capturing the main determinants of credit growth and taking into account a given initial stock of debt. Prudential thresholds represent the debt threshold beyond which the probability of a banking crisis is relatively high, minimising the probability of missed crisis and that of false alerts. Methodology to compute the fundamentals-based and the prudential benchmarks based on Bricongne, J. C., Coutinho, L., Turrini, A., Zeugner, S. (2019), "Is Private Debt Excessive?", Open Economies Review, 1- 42.

Source: Eurostat and ECB as of 2023-04-28, where available; European Commission for forecast figures (Spring forecast 2023)

Table 2.2:**Selected economic and financial indicators (Part 2), The Netherlands**

all variables y-o-y % change, unless otherwise stated	2003-07	2008-12	2013-18	2019	2020	2021	2022	forecast 2023	2024
Housing market									
House price index, nominal	4.1	-2.6	3.3	7.3	7.6	15.0	13.4	.	.
House price index, deflated	2.0	-3.7	2.0	4.6	6.2	11.2	5.6	.	.
Overvaluation gap (%) (7)	12.9	8.7	-8.2	2.6	8.6	17.6	24.4	.	.
Price-to-income overvaluation gap (%) (8)	11.6	5.1	-7.4	4.3	8.6	19.1	32.4	.	.
Residential investment (% of GDP)	5.9	4.8	3.9	5.1	5.4	5.5	5.4	.	.
Government debt									
General government balance (% of GDP)	-1.1	-3.8	-0.7	1.8	-3.7	-2.4	0.0	-2.1	-1.7
General government gross debt (% of GDP)	47.7	59.7	61.9	48.5	54.7	52.5	51.0	49.3	48.8
Banking sector									
Return on equity (%)	.	1.4	6.9	7.5	3.2	8.6	.	.	.
Common Equity Tier 1 ratio	.	11.5	16.4	18.9	19.3	19.3	.	.	.
Gross non-performing debt (% of total debt instruments and total loans and advances) (9)	.	2.4	2.3	1.7	1.7	1.3	.	.	.
Gross non-performing loans (% of gross loans) (9)	.	.	2.5	1.8	1.9	1.4	1.2	.	.
Cost of borrowing for corporations (%)	4.3	3.1	1.7	1.2	1.3	0.8	3.0	.	.
Cost of borrowing for households for house purchase (%)	4.4	4.6	2.8	2.0	1.8	1.7	3.4	.	.

(7) Unweighted average of price-to-income, price-to-rent and model valuation gaps. The model valuation gap is estimated in a cointegration framework using a system of five fundamental variables; total population, real housing stock, real disposable income per capita, real long-term interest rate and price deflator of final consumption expenditure, based on Philiponnet, N., Turrini, A. (2017), "Assessing House Price Developments in the EU," European Economy - Discussion Papers 2015 - 048, Directorate General Economic and Financial Affairs (DG ECFIN), European Commission. Price-to-income and price-to-rent gaps are measured as the deviation to the long term average (from 1995 to the latest available year).
(8) Price-to-income overvaluation gap measured as the deviation to the long term average (from 1995 to the latest available year).
(9) Domestic banking groups and stand-alone banks, EU and non-EU foreign-controlled subsidiaries and EU and non-EU foreign-controlled branches.
Source: Eurostat and ECB as of 2023-04-28, where available; European Commission for forecast figures (Spring forecast 2023)