



A fresh look at the Dutch current account surplus and its driving forces

This paper gives an updated and detailed overview on the Dutch current account surplus.

The Dutch current account has increased substantially since the late 90's, coming mostly from the trade balance in goods. Corporations are the structural driver of the Dutch savings-investment balance, with multinationals and SMEs both playing a role.

High income per person and expected ageing are reasons for a current account surplus, yet a large part of the Dutch surplus remains unexplained.

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Summary

The Dutch current account has increased substantially since the late 90's, coming mostly from the trade balance in goods. Internationally the surplus is consistently among the top surplus countries, thereby also catching attention from international organisations. The current account surplus is driven by the trade balance in goods, with a considerable contribution of re-exports. In particular, re-exports explain more than half of the trade balance, reflecting the favourable geographical position and business climate of the Netherlands, as well as its trade infrastructure. The trade in services and the primary income balance contribute little to the overall balance. But underlying inflows and outflows are substantial, reflecting the presence of multinational companies benefiting from favourable tax laws.

Corporations are the structural driver of the Dutch savings-investment balance, with multinationals and SMEs both playing a role. The positive current account balance is mirrored in the savings-investment balance, with complex interdependencies between the current account and savings/investment decisions. Up to the end of the eighties, households were the structural driver of the Dutch savings, thereafter corporations took over this role. Most of the dynamics in pre- and post-crisis years is explained by households and the government sector. Since the increase in corporate savings is a global trend, some general explanations are brought forward, such as the rise of intangibles in the economy and concentration among firms. Multinationals are often mentioned as explanation for high Dutch corporate savings. However, analysis of microdata and earlier work by DNB suggests that corporations other than multinationals, and in particular SMEs, also contribute substantially to the large Dutch savings surplus. High SME savings could be linked to fiscal incentives and strict bank lending conditions, as well as ongoing balance sheet repair.

The Dutch current account surplus can only partly be explained by economic fundamentals. International organisations (IMF, European Commission) use formal methods to assess external imbalances. The results of these assessments show that only a small part of the Dutch current account balance can be explained by fundamentals such as expected ageing and high income per capita. These outcomes are uncertain, but they give some indication of macroeconomic imbalances. Measurement issues and profit shifting activities related to globalization could complicate assessments of the Dutch current account balance. The impact of issues like retained earnings, corporate inversion or movement of intellectual property on Dutch statistics so far seems limited.

High income per person, the rate of expected ageing and the Dutch' status as financial centre contribute to the current account surplus. The current account norm in 2018 equals 3.3% of GDP, according to IMF calculations (International Monetary Fund, 2019). The gap of 7.7% consists of a policy gap of 1.5% and an unexplained residual of 6.2% of GDP. But as mentioned in chapter 5, they acknowledge that these outcomes are especially uncertain for the Netherlands. The latest calculations of the European Commission show a current account norm close to 4% of GDP in 2017 (European Commission, 2019).

The presence of multinationals has some influence on the current account but does not justify the current size of the surplus. First, the sizable saving surplus of the non-financial corporations is only partly due to multinationals; small and medium-sized enterprises do play a role as well. Second, the upward distortion of the surplus due to retained earnings of multinationals is offset by the downward distortion of the surplus caused by foreign investments of pension funds. Retained earnings show up in the saving balance of corporations while they are a claim of the investors (foreign investors in the case of Dutch multinationals and Dutch pension funds in the case of foreign companies) and adjustments of the current account for those claims would be sound.

1 Introduction

When people think of the Netherlands they think of tulips, windmills, and Amsterdam. When economists think of the Netherlands, they think of the large current account balance. For decades the Netherlands have been recording surpluses on the current account balance, and it has reached an all-time high last year. The sizeable surpluses have caught the attention of policymakers, economists, and international organisations. Since 2013 the Netherlands is identified by the European Commission as country with macroeconomic imbalances, owing to high private debt but also to the large current account surplus.¹ In general, large imbalances may provoke trade tensions and therefore jeopardise international relations. Other than that, it could indicate suboptimal economic outcomes and might lead to painful adjustments.

Is the Dutch surplus ‘too high?’ Should policies be introduced to tackle this issue? These are questions that naturally arise among economists and policymakers. This paper does not aim to answer these fundamental questions. Instead, it gives an updated and detailed overview on the Dutch current account surplus. It aims at providing a useful basis for further research into specific areas. A complexity is that the subject can be viewed from different perspectives. When policymakers refer to competitiveness, they generally refer to the trade balance. When international institutions talk about macroeconomic imbalances, this is generally related to the savings-investment balance. Although these two are identical in an accounting sense, both are influenced by different factors, which sometimes make it hard to reconcile them.

Chapter 2 gives an historical and international perspective on the Dutch current account balance and its components. Chapter 3 looks at the Dutch savings-investment balance, the counterpart of the current account balance, as well as the savings-investments balance of different economic sectors. Special focus will be on the non-financial corporations; how this sector is influenced by multinationals, and some potential causes of their savings behaviour. Chapter 4 gives a view on issues related to the measurement of current account balances, in the light of rapid globalization. External assessments and the underlying methodologies are discussed in chapter 5, and chapter 6 concludes.

2 Overview of the Dutch current account

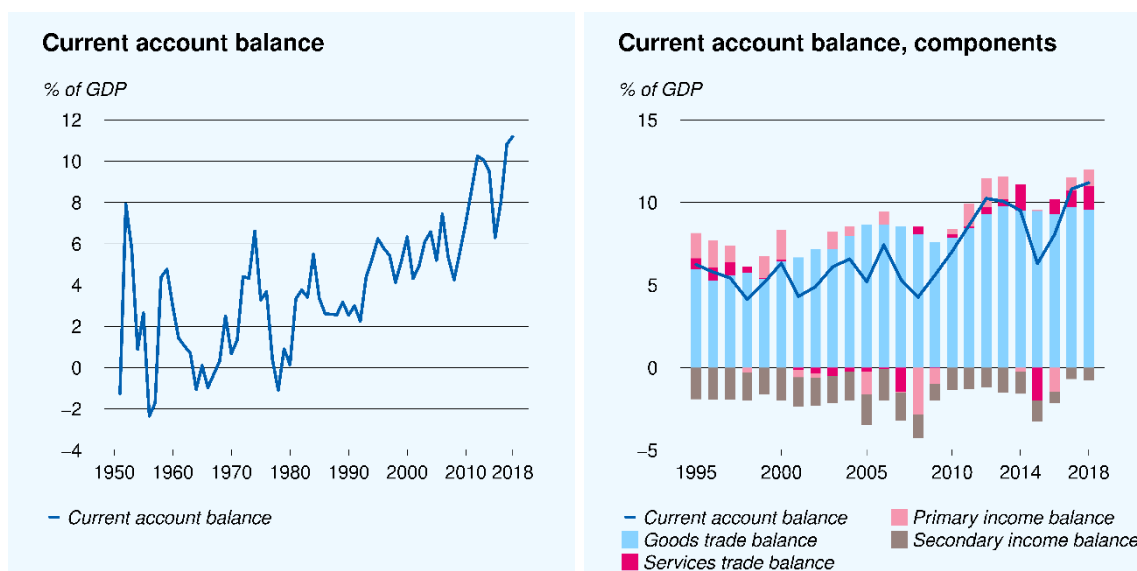
2.1 Dutch current account in historical and international perspective

The Dutch economy has been structurally recording large current account surpluses. Figure 2.1 (left) shows a steady increase since the 90’s. The surpluses have been especially large after the Great Recession, averaging 9.1% of GDP in the period 2010-2018, and peaking at 11.2% in 2018 (99.3 bln dollars). The increase has been driven by the trade balance in goods, with some volatility coming from the primary income balance (figure 2.1 right). The Dutch surplus is also substantial in international perspective, both measured in US

¹ The Commission identifies an imbalance as ‘excessive’ if it exceeds certain thresholds. For the current account balance, these thresholds are at -4% and 6% of GDP (European Commission, 2012).

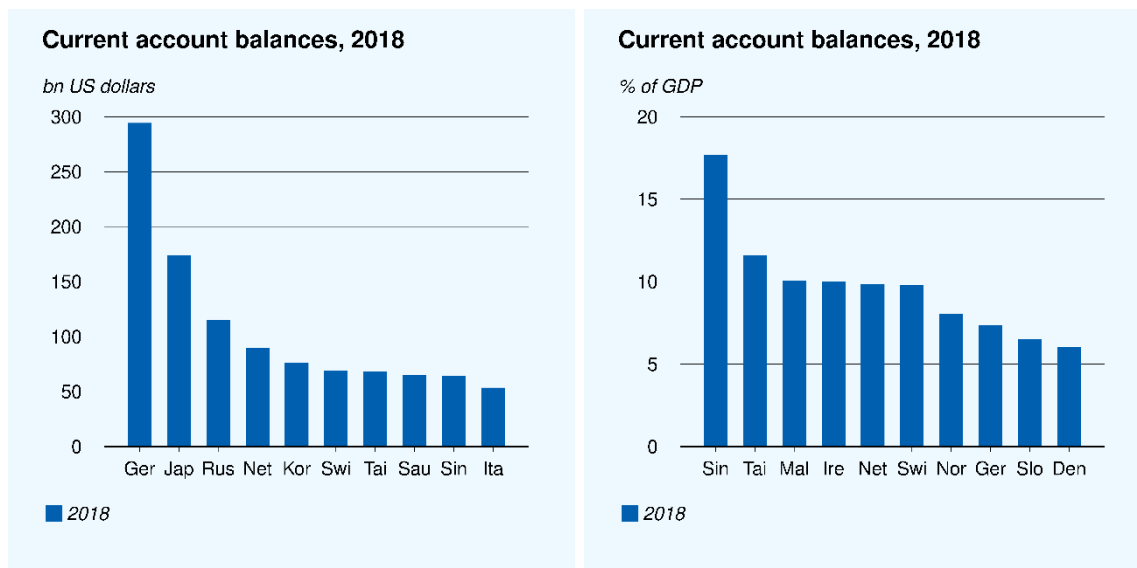
dollars and as percentage of GDP (figure 2.2). In US dollars, the Dutch surplus was the fourth biggest in 2018, after Germany, Japan and Russia. This high ranking is a persistent feature of the Dutch surplus (figure 2.3 left). Most similar are Switzerland and Germany in terms of size and persistence of the current account balance (figure 2.3 right).

Figure 2.1 Large and rising current account balance driven by trade in goods



Source: Statistics Netherlands, National Accounts

Figure 2.2 Dutch current account balance among the highest internationally (a) (b)

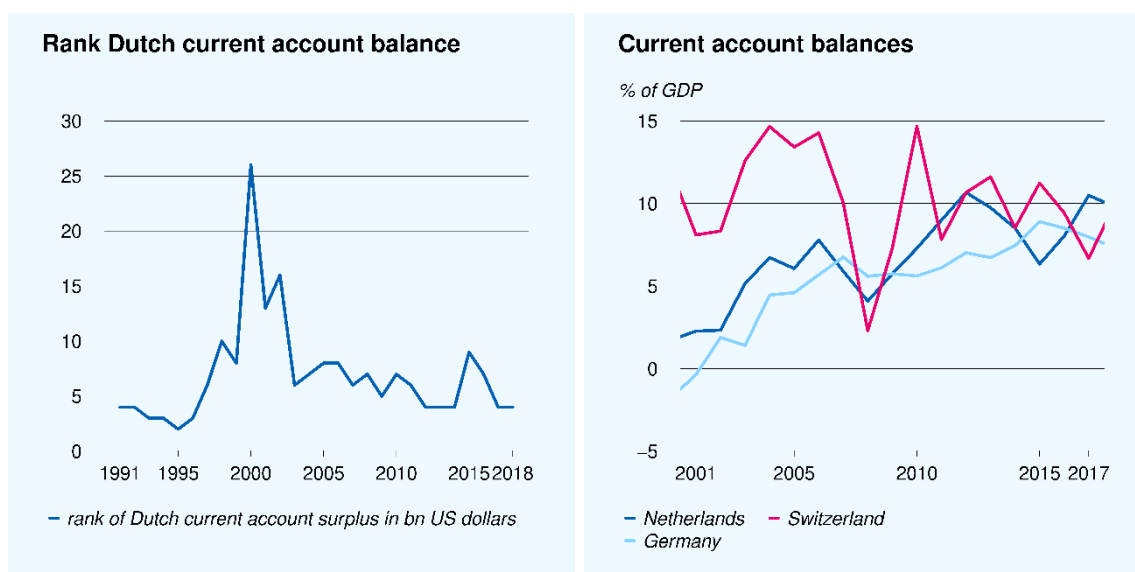


(a) Right-hand figure on the basis of advanced economies.

(b) Ger: Germany, Jap: Japan; Rus: Russia, Kor: South Korea; Net: Netherlands; Tai: Taiwan; Sau: Saudi Arabia; Sin: Singapore; Ita: Italy; Mal: Malta; Ire: Ireland; Nor: Norway; Slo: Slovenia; Den: Denmark.

Source: IMF, World Economic Outlook database

Figure 2.3 Consistently at the top of the current account ranking, among Switzerland and Germany



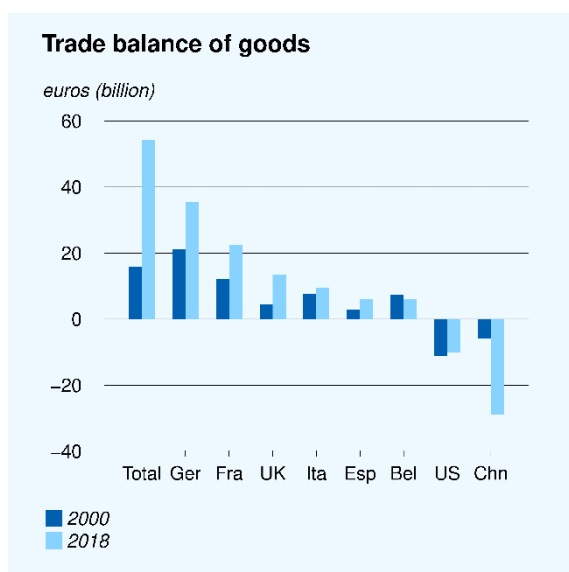
Source: IMF, World Economic Outlook database

2.2 Trade and income balances

The main driver of the level as well as the increase in the balance is the trade balance in goods. The surplus in trade of goods increased from 6% in 1995 to 9.6% of GDP in 2018 (figure 2.1). Since 2012, the trade in goods balance has been roughly stable in percentage of GDP, with the volatility in the current account balance coming from trade in services and from primary income flows. Although the bulk of gross trade flows happens through multinationals, different types of firms and in particular SMEs benefit from exports through intensive supply chains (CBS, 2018). In 2016, multinationals were responsible for three quarters of total gross exports, but this share drops to half from a value-added perspective (see also 3.6).

The bulk of the trade balance in goods comes from a few neighbouring countries. The Netherlands has large bilateral trade surpluses with Germany, France and the United Kingdom (figure 2.4). These trade balances were already large in 2000, although back then the NL-UK surplus was smaller than the surplus with Italy and Belgium. That trade flows are large with these countries is not surprising, given their economic size and proximity to the Netherlands. The Netherlands has had deficits with the US and China since 2000, and especially the increase in the deficit with China is impressive. This is related to the gateway function of the Netherlands; large amounts of goods that are shipped from China (and the US) first cross the Dutch border, before they go to their final destination elsewhere in Europe. The next paragraph shows that these re-export flows contribute significantly to the Dutch trade balance.

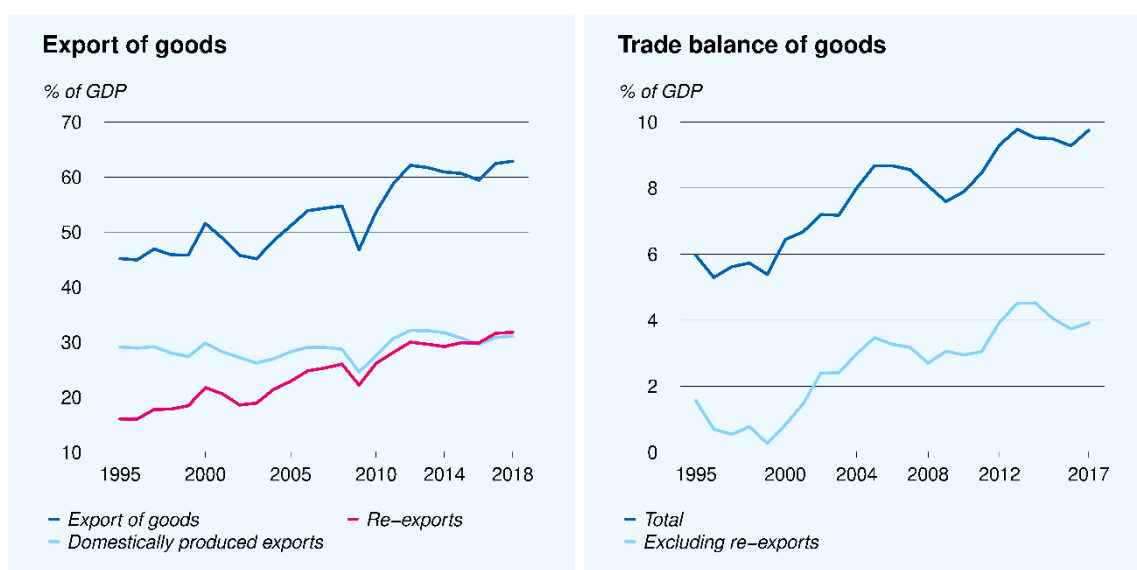
Figure 2.4 Dutch trade balance predominantly from neighbouring countries



Source: Statistics Netherlands, trade statistics

The contribution of re-exports to the trade balance is considerable. The export in goods can be broken down in two parts: the domestically produced exports and the re-exports. Re-exports have become increasingly important in the export of goods. As a percentage of GDP, re-exports increased from 16.1% in 1995 to 31.8% in 2018, also surpassing the domestically produced exports in recent years (figure 2.5 left). Although the import content of re-exports is high (value added of re-exports is relatively small), large volumes make the contribution to the trade balance considerable. Figure 2.5 (right) shows that excluding re-exports (and the import that is used for re-export) reduces the trade balance in goods by more than half.² The high re-export volumes primarily flow through the port of Rotterdam, serving as a key location for goods trade in, out and within Europe.

Figure 2.5 Growing importance of re-exports in Dutch exports of goods



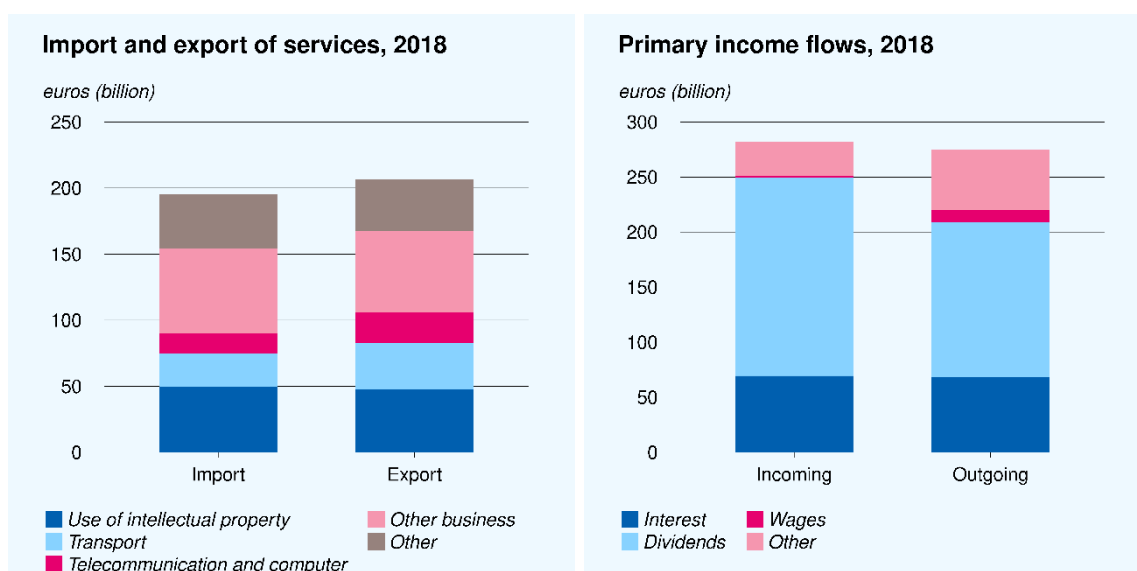
Source: own calculations based on Statistics Netherlands data

² The trade balance excluding re-exports is not the same as the trade balance of domestically produced goods. This is because the former also includes import for domestic use, i.e. consumption and investment.

The large trade balance in goods has been related to factors specific to the Netherlands, as well as global trends. The Netherlands benefits from its favourable geographical position and the supporting trade infrastructure (the harbour of Rotterdam), in combination with longer global value chains and the globalization of the economy in general. The integration within the euro area is also mentioned as an important contributor to the growing trade balance, as fixed exchange rates and the removal of trade barriers stimulate trade flows (Rojas-Romagosa & van der Horst, 2015).

The contribution of trade in services to the trade balance is small, but the underlying flows in and out of the Netherlands are substantial. Since 2014 services have been contributing more to the trade balance, with 2015 being an outlier (figure 2.1 right).³ The flows underlying the trade balance are substantial, with imports at 20% and exports at 21.5% of GDP in 2018. These trade flows are dominated by a small number of product groups (figure 2.6 left)⁴. Business services and the use of intellectual property (royalties) alone explain more than half of the trade flows. The most value added comes from transport services and telecommunication and computer services. The large trade flows in royalties are related to the attractiveness of the Netherlands as conduit country, most likely because there is no withholding tax on royalties (Lejour, Möhlmann, & van 't Riet, 2019).

Figure 2.6 Small balances hide large trade and income flows



Source: Statistics Netherlands, International trade statistics and National Accounts

The presence of many multinationals (MNEs) in the Netherlands is reflected in the substantial incoming and outgoing income flows. In 2018, the primary income received from abroad amounted to 282.1 bln dollars (36.5% of GDP), while 274.5 bln dollars was returned to foreigners. Note that retained earnings of foreign subsidiaries of multinationals are also counted as income receipts, even though these earnings are reinvested abroad (Eggelte, Hillebrand, Kooiman, & Schotten, 2014). This transaction is at the same time recorded as incoming primary income and as outgoing investment flow on the capital account. The income flows consist mainly of interest and dividends (figure 2.6 right). As with trade in services, MNEs likely use the Netherlands as conduit country for tax saving purposes (Lejour, Möhlmann, & van 't Riet, 2019), so that most of the foreign earnings do not stay in the Netherlands. A significant share of primary income receipts also comes from

³ The sharp decline in 2015 comes mostly from a single transaction of a large multinational company. It was only since the revision of national accounts in 2018 that this transaction was recorded as (mostly) an R&D purchase, worth multiple billions of dollars (Statistics Netherlands, 2018)

⁴ The numbers in the figure are from trade statistics and do not fully correspond with National Account statistics.

pension funds, since most of their funds are invested abroad. In 2018, their investment income amounted to 32.9 bln euros.⁵

3 Sectoral analysis of the savings-investment balance

3.1 The national savings-investment balance

When a country runs a surplus on the current account, it means that resources that flow into the country exceed the outflows, i.e. the country is a saver vis-à-vis the rest of the world and a net capital exporter. Put differently, the savings of this country are not entirely used for domestic investment, resulting in a savings surplus. When international organisations discuss the Dutch current account balance and recommend certain policies, these are mostly related to the savings-investment balance. This chapter therefore analyses the savings-investment balance of the Dutch economy and the underlying sectors. Non-financial corporations (NFCs) and households will be discussed in more detail, since these are in general the most relevant contributors to the surplus.

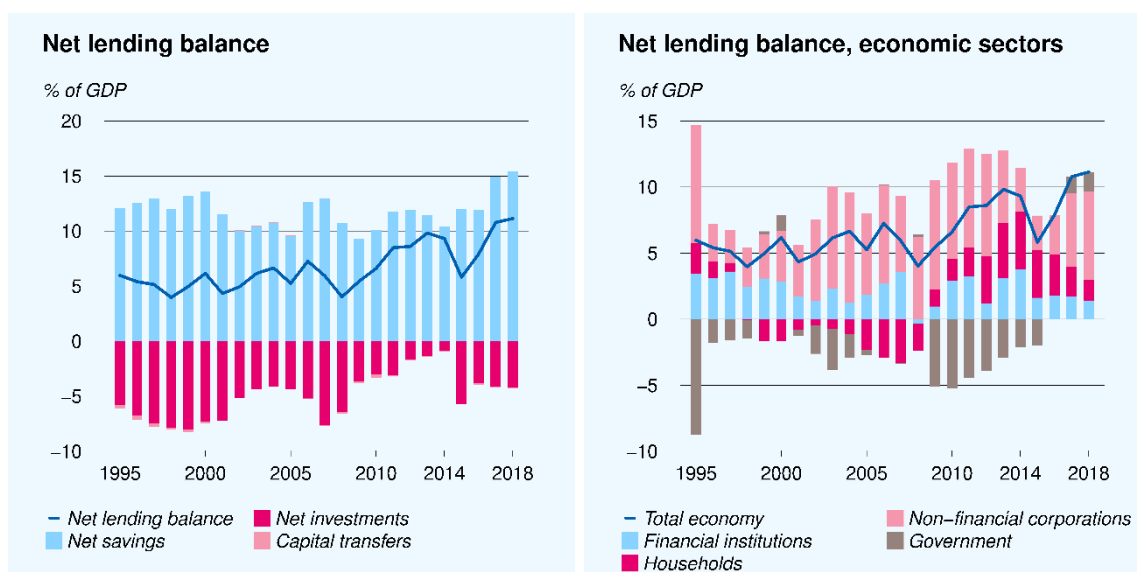
The national savings surplus increased after the Great Recession, primarily due to lower investments.

Figure 3.1 shows the net lending balance of the Dutch economy and of the different sectors. The net lending balance is equal to the savings surplus, plus the capital transactions, which are negligibly small. From now on, the net lending position is referred to as the savings surplus. As mentioned above, the savings surplus and current account balance are identical, so that the line in figure 3.1 is equal to the one in figure 2.1. From figure 3.1 it becomes clear that the savings surplus has been exceptionally high in the post-crisis period. The surplus has increased from an average of 5.5% of GDP in the period up to the crisis to 8.0% in the 2008-2018 period (table 3.1). Savings were relatively stable, although they increased in the last two years. Most of the rise in the surplus came from lower investments. In recent years, however, investment has recovered and a steep increase in savings caused the large savings surplus.

Corporations are the structural drivers of the current account surplus. Figure 3.1 (right) and table 3.1 also show the savings surplus of different sectors. Financial corporations and non-financial corporations (NFCs) are structural net savers over the entire period (with 2009 as exception for financial institutions). The savings surplus of NFCs rapidly increased in the years preceding the crisis and stayed at a high level since, thereby being the structural force behind the increase in the national savings surplus. Corporations also explain the high Dutch savings surplus in international perspective (figure 3.2 left). Most of the dynamics seem to come from households and the government, going from deficits in the pre-crisis periods to surpluses in more recent years. Table 3.1 shows that the households explain most of the change in the Dutch savings surplus, with both higher savings and lower investments (housing) contributing to this. The increase in households' net lending position in post-crisis years was quite unique for the Netherlands (figure 3.2 right). The government actually put downward pressure on the average surplus in the early post-crisis period, but large efforts to restore government finances have resulted in budget surpluses in most recent years, as figure 3.1 shows. Finally, it is noteworthy that in the last two years, all sectors have saving surpluses.

⁵ <https://opendata.cbs.nl/statline/#/CBS/nl/dataset/84098NED/table?ts=1564663973952>, recorded as 'Ink. te betalen aan pensioengerechtigden'

Figure 3.1 Dutch savings-investment balance driven by corporations

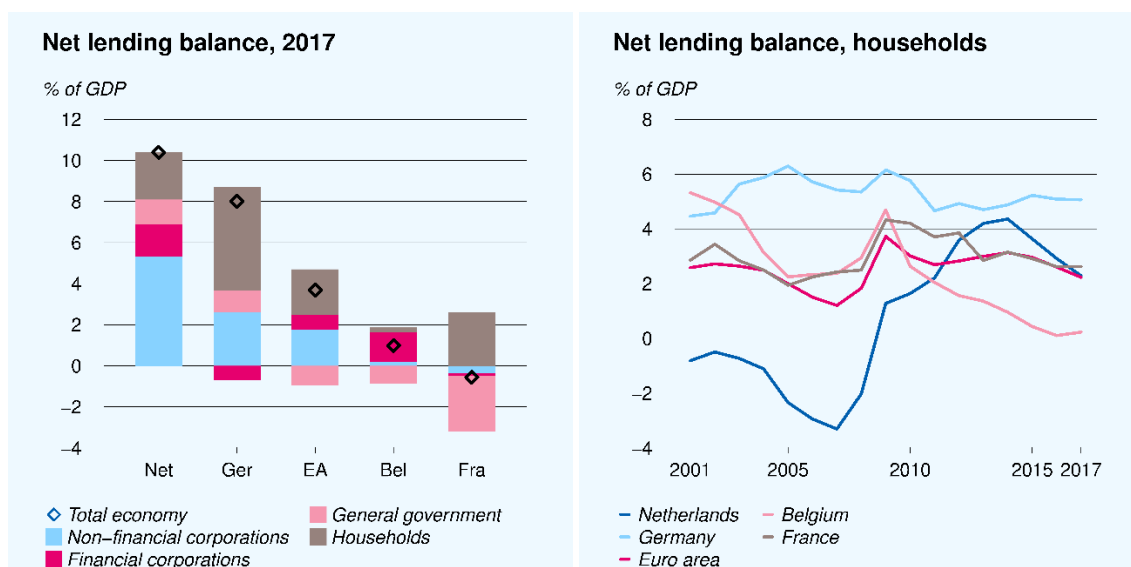


Source: Statistics Netherlands, National Accounts

Table 3.1 Savings-investment balances pre and post crisis (in % of GDP)

	Savings surplus		Savings (net)		Investments (net)	
	95-07	08-18	95-07	08-18	96-07	08-18
Total	5.5	8.0	11.9	11.8	6.2	3.7
Households	-1.1	2.3	2.6	3.9	3.5	1.6
Non-financial corporations	5.1	5.8	6.9	7.2	2.1	1.7
Government	-0.9	-2.1	0.0	-1.2	0.6	0.4
Financial institutions	2.5	1.9	2.4	1.9	-0.1	0.0

Figure 3.2 Net lending position of corporates high internationally, distinctive increase in Dutch households' savings investment balance in post-crisis era

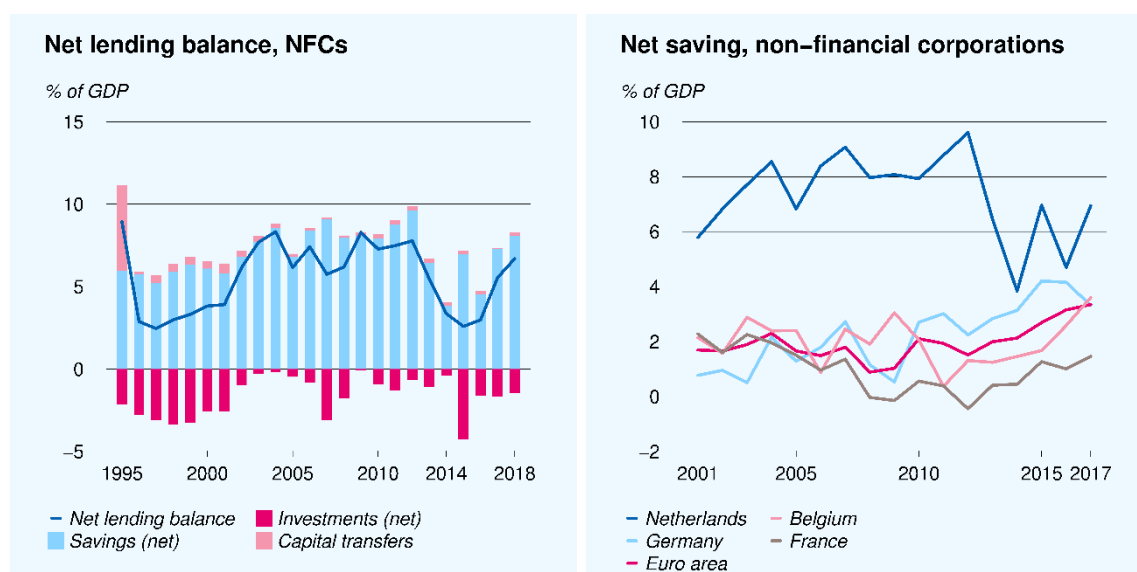


Source: Eurostat

3.2 Non-financial corporations

The net lending balance of Dutch corporations is mostly driven by savings, which are high in international perspective. Figure 3.3 shows the savings surplus of non-financial corporations (NFCs). Savings are the primary driver of the surplus, although the decline in investments since the beginning of the century has also contributed to a rising savings-investment balance. The decrease in nominal investments after the late 90's is partly related to a decline in the prices of investment goods, especially IT equipment, although this does not explain the observed decline in real investments (Jansen & Ligthart, 2014). Figure 3.3 (right) shows that the difference between Dutch NFCs and those of other countries is primarily due to higher savings.

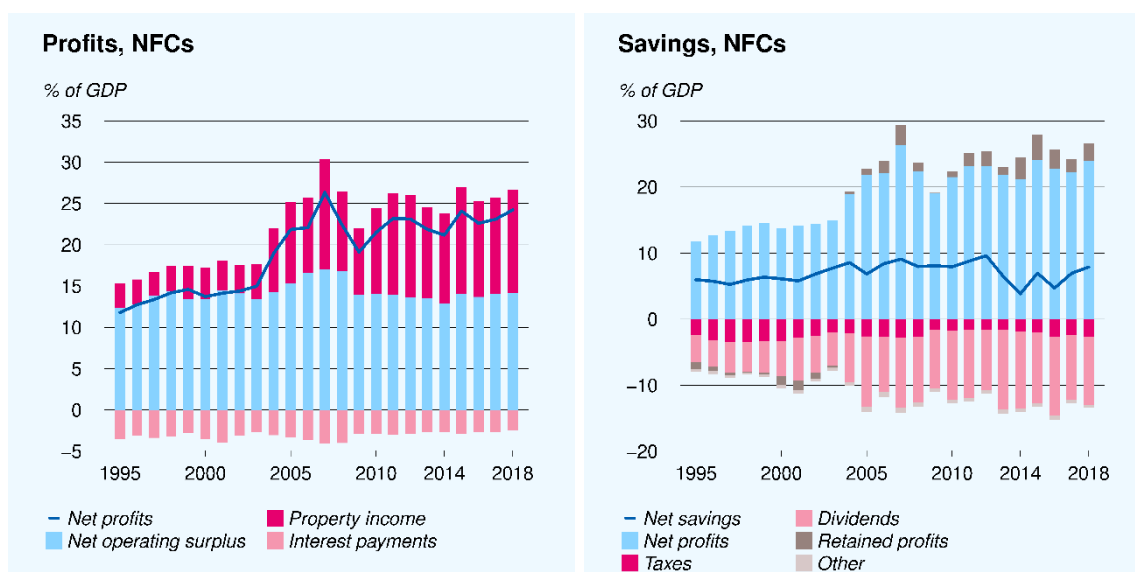
Figure 3.3 Savings of NFCs are high, also internationally



Source: Statistics Netherlands, Eurostat

Savings of corporations gradually increased, as a strong rise in profits have only partially been matched by higher profit distribution. NFCs can increase saving roughly in two ways: either by increasing their profits, or by retaining a larger share of their profits. Figure 3.4 shows the profits of NFCs and their savings (right). First, savings have been high over the entire period, as after-tax profits are not fully distributed to shareholders. This is both due to high operating surpluses and relatively low dividend pay-outs. Between 2008 and 2017, higher gross operating surplus and higher net dividend income (received dividends minus paid dividends) both were 2.1 percentage points higher than the euro area average (European Commission, 2019). The savings of Dutch NFCs also gradually increased during the last two decades, although there has been more volatility after 2012. Especially until 2012, this increase has been the result of rising net dividend income. Corporations benefited from higher dividends received from foreign subsidiaries (property income in figure 3.4), while they did not fully distribute these higher earnings to their shareholders. In this context, Shell changed its corporate structure in 2005, leading to a large and structural increase in received dividend income (Eggelte et al, 2014). Note that although dividend pay-outs are lagging behind profits, shareholders may still be compensated through share buybacks. The latter has become increasingly popular in recent years. Although share buybacks raise wealth of shareholders and therefore likely boosts consumption, it does not directly affect the current account, as opposed to dividend pay-outs. Other factors that have contributed to NFC savings are lower interest and tax payments. Since most of the earnings come from abroad, these are exempt from taxes due to the 'deelnemingsvrijstelling.' Finally, the contribution of retained profits (which are reinvested abroad) has been positive over the last decade.

Figure 3.4 Savings of NFCs high, but relatively stable



Source: Statistics Netherlands, National Accounts

3.3 Multinationals and Dutch corporate savings

Multinationals are often cited as plausible explanation for the high savings of non-financial corporations (NFCs) in the Netherlands. These MNEs often have their headquarter located in the Netherlands for reasons such as geographical position, friendly business environment and favourable tax treaties. While the profits of these companies are relatively high, they mostly invest their earnings abroad through foreign direct investment, which could explain the high net saving position of Dutch NFCs. IMF (2019) finds that the top 24 publicly listed firms contributed to about 40% of Dutch NFC gross savings in the period 2010-2017. These numbers are based on financial statements and it is not clear to what extent these could be matched with National Accounts or with the micro-statistics mentioned in the next paragraph.

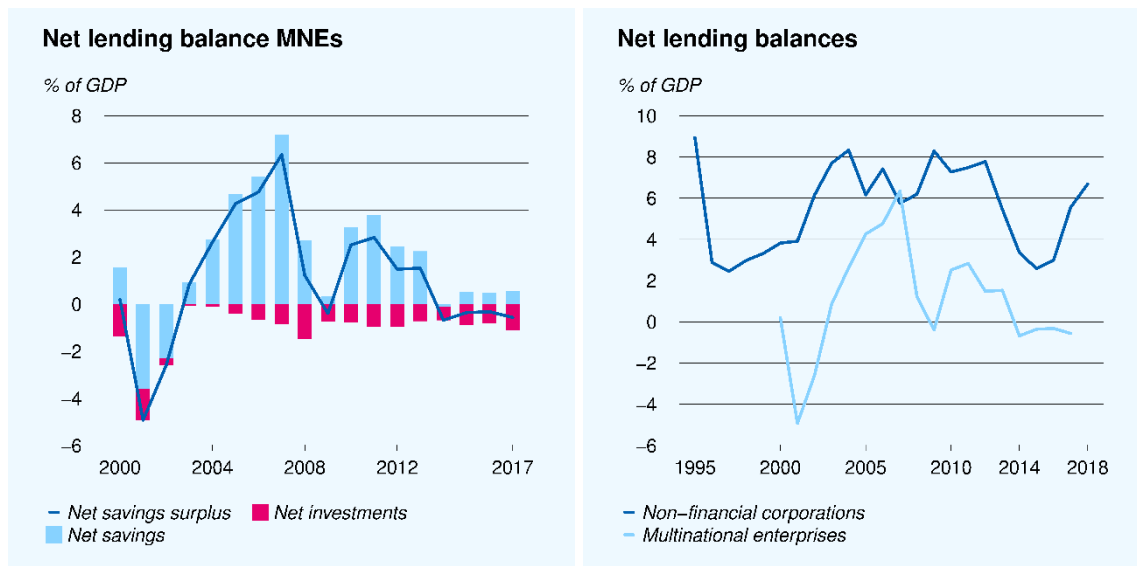
Microdata findings suggest that MNEs only partially account for Dutch corporate savings. Figure 3.5 (left) shows the savings surplus of multinationals in the Dutch economy, based on CPB calculations using micro-data from Statistics Netherlands⁶. There seems to be some co-movement between MNE and NFC savings, as figure 3.5 (right) shows. Still, the difference in levels is quite high in most years, indicating that MNEs do not fully explain the corporate savings surplus. De Nederlandsche Bank (2019) uses micro-data on all Dutch firms, and they find that SMEs are an important contributor to the savings surplus, while the savings of large firms are quite volatile. MNEs are most likely driving the latter finding. Some precaution is warranted for both of the above findings, since there is still a considerable gap between aggregated microdata on firms and National accounts data.

Savings of MNEs are quite volatile, owing much to fluctuations in foreign earnings. MNE savings peaked at 6.3% of GDP in 2007, while it is just below zero in recent years. Still, there seems to be a steady decline in savings in the post-crisis period. As mentioned, multinationals mostly invest abroad, which explains the relatively low domestic investments in the figure. Figure 3.6 sheds more light on the profits and savings of MNEs. Profits are largely driven by net property income, which in turn is almost entirely driven by received dividends from abroad. This also is the main cause of the volatility in MNEs savings. Figure 3.6 (right) shows

⁶ The data only contains investments in material assets, which makes an underestimation of total investments likely

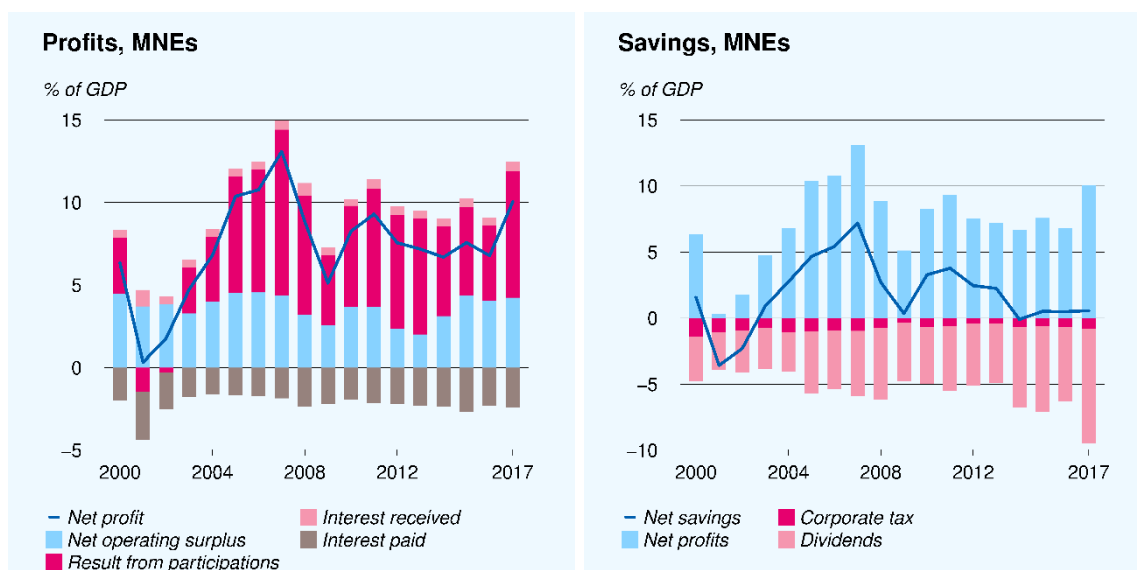
that the decrease in savings in recent years is mostly because MNEs distributed more of their earnings in the form of dividend.

Figure 3.5 Volatile multinational savings partially drive corporates' net lending balance



Source: Left figure own calculations are based on Statistics Netherlands microdata. Right figure dark blue line is based on National Accounts data and light blue line is based on Statistics Netherlands microdata.

Figure 3.6 Volatility in MNE savings driven by foreign profits



Source: own calculations based Statistics Netherlands microdata.

3.4 Possible explanations of the growing saving surplus of corporations

Since the start of the century there is a global upward trend in corporate savings. Until the 90s, corporate investments exceeded savings. But since the start of this century, increasing savings and decreasing investments resulted in positive net positions of corporations (Dao and Maggi, 2018)⁷. This is the case for all G7 countries, except for France. The difference between surplus and deficit countries within advanced economies is also mostly driven by the corporates. In the next paragraphs, we will first mention some general explanations for the rising surplus of corporates. In the last part, we will focus more on the Dutch situation.

One often cited explanation for the corporate savings surplus is the growing relevance of intangible assets in the economy. As intangible assets have less collateral value, firms have less access to credit and thus have to hold on to more internal resources such as cash (Falato, Kadyrzhanova, Sim, 2013). Firms that rely more on intangible assets and spend more on R&D also face more uncertainty over future income, so that higher savings serve as insurance against this uncertainty. Finally, as intangibles become more important, investments will shift from fixed assets towards human capital, putting downward pressure on investments as measured by national account definitions.

Concentration could also be driving corporate savings. Dao and Maggi (2019) find that firms that save much more than they invest are larger, more profitable, have high R&D spending and low effective tax rates. The latter is because larger firms can more easily exploit international differences in taxation. Phillipon and Gutiérrez (2016) find that for the US, industries in which concentration is higher, firms invest less. The reasoning is that if firms have enough market power, they have less incentive to invest. The authors also find support for the idea of short-termism, which means that changes in the ownership structure of firms has put more emphasis on short-term earnings. In practice, this means that firms use internal funds to buy back shares.

Global trends, as well as domestic factors may drive Dutch corporate savings. Abovementioned reasons could also be relevant for Dutch corporate savings. The concentration argument implies that large firms are largely responsible for corporate savings but the findings in 3.3 suggest that other firms (SMEs) are also responsible for the savings surplus. Moreover, Meijerink, Bettendorf and van Heuvelen (2019) find no evidence for increasing market power in the Netherlands. Some possible explanations are specific to the Dutch situation. Fiscal incentives could play a role in the savings of SMEs. The Dutch tax system induces owners of small to medium sized companies to retain profits in order to postpone tax payments (Jansen & Ligthart, 2014). Strict bank lending conditions could also play a role. It is shown that loan supply to Dutch SMEs is low relative to other countries, which could be related to low competition in the banking sector (Dubovik, Van Solinge & Van der Wiel, 2019). This could force companies into increasing retained earnings for financing purposes. Finally, the presence of multinationals might be related to profit shifting behaviour or measurement problems that leads to higher observed corporate saving (see chapter 4).

⁷ Generally, this increase in net positions of corporations was offset by a decline at households.

3.5 Households

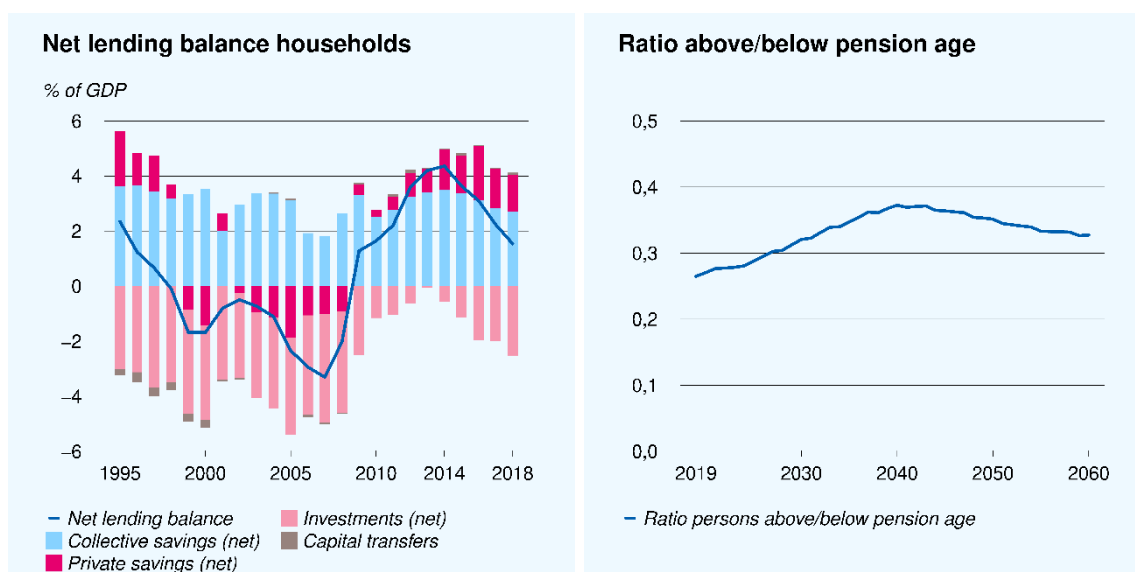
There has been a global shift in savings from households to corporations. This same shift has taken place in the Netherlands. Eggelte et al. (2014) mention three explanations for the fall in Dutch household savings. First, personal savings fall because after a long period of house price rises, households used the excess value of their homes to finance their consumption. Moreover, households increasingly took on mortgage debt to buy houses. Second, for fiscal reasons, entrepreneurs shifted their personal savings to their firm's balance sheet. Finally, collective savings steadily declined. Until the start of this century, this decline was because the gap between pension payments and pension contributions widened. Since then, pension contributions started to rise again, but this is roughly offset by declining investment income of pension funds. The last two decades collective savings fluctuate around 3% of GDP.

Dynamics in Dutch households savings surplus are largely driven by the housing market. The initial increase in the net financial balance in the years after the crisis can be largely accounted for by households, which turned from net borrower to net lender (figure 3.7). As a result of the crash on the housing market, housing investment plunged. At the same time savings increased, as households had to cut back on consumption to pay off their mortgages. Finally, procyclical behaviour of pension funds exerted additional upward pressure on household saving (European Commission, 2018). Recently the net balance of households decreased somewhat due to a recovery in housing investments, but personal savings remain at an elevated level. This could be a sign of still ongoing deleveraging (CBS, 2019). Another reason could be the gradual decline in loan-to-value ratios for homebuyers, which increases the amount of 'own money' needed to buy a house.

Structurally, households savings are driven by high pension savings which are predominantly invested abroad. Since personal savings tend to move towards zero, the structural driver of households savings are the pension savings. More than three quarters of these savings are invested abroad by pension funds, so that there is a positive effect on the national savings surplus (Eggelte et al, 2014). This might be desirable, if the returns on foreign investments exceed domestic returns, or for diversifications purposes. It also poses a risk because a large stock of foreign assets is vulnerable for changes in valuation. This was exactly what happened during the nineties, when Dutch external assets suffered large valuation losses (Rojas-Romagosa & van der Horst, 2015) Hünnekes, Schularick & Trebesch (2019) find for Germany that domestic returns have outperformed foreign returns. They also show that the Netherlands gets relatively low returns on their foreign assets. Finally, Dutch pension contributions are relatively high, possibly implying suboptimal consumption smoothing over the life cycle (European Commission, 2019)

Demographics will put downward pressure on collective household savings in the short- to medium term. With the retirement of the large baby boom generation, the number of pension-aged people relative to the (potential) labour force will increase, putting downward pressure on collective savings (figure 3.7). However, collective savings are expected to remain high, as the old-age ratio eventually decreases again while life-expectancy keeps increasing.

Figure 3.7 Collective savings structural force behind positive net lending position of households



Source: Statistics Netherlands

3.6 The savings-investment balance and the current account

The dominance of multinationals is less apparent in the savings-investment balance as it is in the trade in goods balance. One could expect a link between the trade balance in goods as dominant driver of the current account, and the savings surplus of non-financial corporations as main driver of the savings-investment balance. Between 2010 and 2016, on average three quarters of import and export of goods is done by multinationals, with the remainder of trade mostly done by SMEs (CBS, 2018). Firms do not fully distribute these earnings from trade to households, nor do they use it all for domestic investment, so that there is a savings surplus among corporations. But while trade flows are dominated by MNEs, the savings surplus seems to be distributed between MNEs and SMEs.

Gross trade flow figures underestimate the earnings from export of non-multinationals. Dutch non-multinationals are important suppliers for multinational firms, thereby also indirectly benefiting from international trade.⁸ In 2016, non-multinationals in the Dutch economy accounted for 106.4 bln euros of value added from exports, or 48.1% of total value added from exports (Statistics Netherlands, 2018). More than half of their value added is indirectly (57.7 bln), by supplying to other firms that export the goods. Earlier research by Chong et al. (2018) showed that in 2012, small firms alone accounted for 31% of Dutch value added that is due to foreign demand. These findings support the idea that SMEs also contribute to the savings surplus of non-financial corporations (paragraph 3.3).

⁸ These non-multinationals consist of non-multinational SMEs, large companies, and other sectors which cannot be defined as multinationals, such as the financial sector and the government.

4 Measurement issues

In a strongly globalized economy, traditional ways of measuring economic activity and current account balances are insufficient. Although the national accounting framework has been modernised since its establishment in the 1930s and 1940s, the innovation has not kept up with the pace of globalization (Avdjiev, Lane, Everett, & Shin, 2018). The key concept still is that of the economic area (the ‘island’) as unit of analysis, and that economic activity takes place either within the island or as transaction between islands. However, economic activity has become geographically more dispersed in the last decades, since companies and their ownership have become more global. The result is that the statistical measurement of domestic activity and external imbalances may not give an accurate picture of real economy activity (Adler, Garcia-Macia, & Krogstrup, 2019). The next paragraphs discuss some specific measurement issues that result from globalization.

Assigning retained earnings to their ultimate owner will shift savings from corporations to households, but will not affect the total savings surplus. We saw earlier that multinationals explain part of the savings surplus of NFCs, although its significance fluctuates over time. Although these savings are counted as Dutch savings, most multinational companies are predominantly owned by foreigners. Statistically, retained earnings are only assigned to the ultimate (foreign) investor if it is a direct foreign investment. In the case of portfolio investments however, only the profits that are distributed flow back to the investors. Adler, Garcia-Macia and Krogstrup (2019) call this the *retained earnings distortion*. They also state that economically it would make more sense to assign all distributed and non-distributed profits to their ultimate owner. The authors also estimate the size of this distortion on current account balances. What seems surprising at first is that they find a negligible effect on the Dutch current account balance in the period 2010-2016. However, there is an opposite effect coming from Dutch pension funds, who are large scale portfolio investors in foreign companies. Eggelte, Hillebrand, Kooiman, and Schotten (2014) already showed that in the years after the Great Recession, correcting for retained earnings does not affect the total savings surplus, since lower earnings for corporations are cancelled out by higher earnings for pension funds. Although it does not affect the total, it does imply a large shift in savings from corporates to households, as was also shown in Rojas-Romagosa & van der Horst (2015).

The effect of corporate inversions on the current account is positive and has increased over time.

Corporate inversion involves a multinational corporation changing its country of residence. This could be motivated for example by more favourable tax treatments or a better regulatory environment. When company X with its mother company in country A moves its headquarter to country B, the profits of company X will still flow from country B to country A, but only in proportion to the ownership that the foreign owner has over company X. So, if the foreign owner owns 80% of the equity shares, 80% of the profits will be assigned to the foreign owner. And if less than 10% is owned (portfolio investment), only the distributed profits will go to the foreign owner(s). This implies that corporate inversions can substantially influence national income statistics and thus the current account balance. Nelisse and Hiemstra (2019) find for the Netherlands that between 2010 and 2017, the size of the corporate inversion has increased. In 2017 the Dutch primary income balance was 9 bln dollars higher because of corporate inversions, which equals 1.2% of national income in that year.

Moving intellectual property may affect the current account, although its effect on the Dutch current account seems limited. Companies may shift intellectual property between subsidiaries for tax minimizing purposes (Nelisse & Hiemstra, 2019). Although non-produced, imported intellectual property does not count in Dutch GDP statistics, the accompanied royalties and license earnings show up as import and export of services. The net effect on GDP and the current account balance are still relatively small; in 2017, GDP was 3.2 bln dollars higher because of IP movement. This amounts to 0.2% of national income.

Dutch multinationals generally charge lower prices to subsidiaries, with an initial negative impact on the current account balance. Firms can manipulate intra-company import and export prices so as to shift profits to low-tax jurisdictions, also called ‘transfer pricing.’ We already saw that re-exports are a large driver of the trade balance in goods, and a substantial part of these re-exports are intra-company transfers. Given that the statutory tax rate in the Netherlands is not particularly low, there seems no clear incentive for MNEs to maximize their profits within the Netherlands. Mounir and van den Berg (2017) looked at transfer pricing in the Netherlands. They find on average that companies charge lower prices for their subsidiaries than to non-related parties, and that these prices are even lower if the subsidiary is located in a low-tax country. This means that transfer pricing actually lowers Dutch companies’ profits reported in the Netherlands, although one can imagine that the higher profits in foreign subsidiaries are returned to the Netherlands in the form of dividend. Moreover, the authors find the opposite effect for a very specific group of companies, the so called ‘pure re-export companies.’ These companies actually charge significantly higher prices to their foreign subsidiaries, which leads to higher profits for the Dutch companies. They do not have an explanation for this finding.

5 Assessments of current account balances

The methodologies used by the IMF and the European Commission to assess external balances are not flawless but can be used to provide a broad indication. They have to be applied with care, with substantial confidence intervals around the point estimate.

The European Commission and IMF use benchmarks derived from econometric models to assess the current account balances of countries. This paragraph describes the EC method (Coutinho, Turrini, & Zeugner, 2018), although it is largely similar to the IMF’s EBA model (Cubeddu et al., 2019; IMF, 2018). The method starts with a panel regression including 65 countries over the period 1987-2016. The regression estimates the relationship between the current account balance and a large set of potential explanatory variables. There are two groups of variables: fundamental variables, i.e. variables that do not depend on transitory economic factors or policy choices. And a group of variables with a temporary nature. Examples for the fundamentals include relative income and ageing (see theoretical underpinnings below). The output gap and the fiscal balance are examples of temporary variables. Using estimates of fundamental variables, a current account ‘norm’ is estimated for each country in the sample. These norms show the current account value that is consistent with the fundamentals of each country, free of cyclical factors or policy choices. The current account gap is then the difference between the actual current account balance and the current account norm for that country. IMF additionally calculates how much of this gap is caused by a ‘policy gap,’ i.e. how much of the deviation from the current account norm is caused by policy variables that are not on their medium-term desirable levels (Cubeddu et al., 2019). Examples of policy variables include the cyclically-adjusted fiscal balance and health expenditures.

High relative income per capita and expected ageing positively affect the current account balance. Capital normally flows from high income to low income countries, since the latter mostly have the highest growth potential and thus the highest returns on capital. This means that domestic savings are used to fund foreign investments, resulting in a positive savings-investment balance. The effect of expected ageing and demographics in general is also intuitive. For example, when a country has a large working-age population relative to the rest of the world, it has to save more to be able to finance consumption when the large group of workers retires.

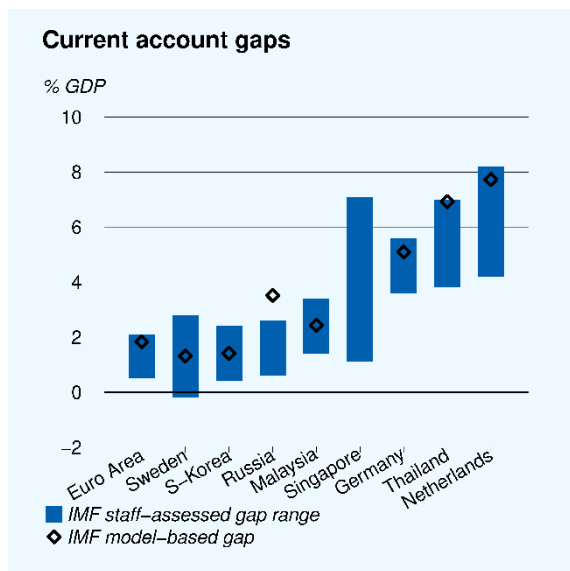
The methodologies used to assess external balances are not flawless and should be seen as providing a broad indication. First, there are large differences between countries within the sample. However, the estimated coefficients imply a structural relationship that is homogenous across countries. The IMF and the European Commission acknowledge the presence of country specific factors, therefore using expert judgement to overrule model outcomes if needed. This sometimes means a wider uncertainty range. For example, in the IMF's latest assessment of the Dutch external balance:

“The Netherlands’ status as a trade and financial center and natural gas exporter make an external assessment more uncertain than usual.”

Other issues are the dependency of results on model specification and determining what part of the current account or current account changes can be attributed to structural or temporary factors. Still, the results give an indication of macroeconomic imbalances and to what extent these are reasonable given fundamentals.

The sizable Dutch current account surplus can only partially explain by fundamentals. These are the income per person, the rate of expected ageing and the Dutch’ status as financial centre. The current account norm in 2018 equals 3.3% of GDP, according to IMF calculations (International Monetary Fund, 2019). The gap of 7.7% consists of a policy gap of 1.5% and an unexplained residual of 6.2% of GDP. But as mentioned, they acknowledge that these outcomes are especially uncertain for the Netherlands, visible in the wide range of the IMF-staff assessed current account gap (see figure 5.1). They provide an indication but have to be applied with care, with substantial confidence intervals around the point estimate. The latest calculations of the European Commission show for the Netherlands a current account norm close to 4% of GDP in 2017 (European Commission, 2019).

Figure 5.1 Countries exceeding the most their IMF current account benchmark



Source: IMF

Competitiveness as well as substantial re-exports are no proper reasons for a high current account balance in the medium term. A sudden improvement in price competitiveness will have a positive impact on exports and a negative impact on imports leading to a rise in the current account balance. However, there is no economically sound reason for an impact in the medium term of price competitiveness on the saving rate of firms and households. The savings rate should eventually fall back to the levels before the rise in competitiveness, and the impact on the current account will dissipate. The same holds for being a strong distributional centre leading to substantial re-exports. While more re-exports can have a positive impact on the current account, there is no reason this will have a permanent effect on the saving rate of firms and households and therefore on the current account.

6 Concluding remarks

The international dimension of the Dutch surplus cannot be neglected in policy making. The Netherlands is a main contributor to the euro area current account surplus.⁹ In 2018, the Dutch surplus was almost a quarter of the euro area surplus, with a Dutch share in euro area GDP of 7%. While surpluses and deficits can both be welfare enhancing and therefore economically justified, a decline in the euro area surplus can be helpful in preventing trade tensions, as escalation of trade tensions would have negative effects on the European economy. The international dimension differs at the moment from the one ten years ago. At that time, the euro area current account balance was practically zero and the substantial Dutch and German surpluses were accompanied by big deficits in euro area problem countries.

Not counting external pressure, the sizable surplus provides a comfortable position to policy makers. As a result of the sizable surplus, there is no need to worry about the impact of stronger wage rises on price competitiveness. A smaller surplus in the short to medium term due to deterioration of the competitive position would not be problematic. Moreover, other factors beyond wages contribute to the Dutch competitiveness. The current account position also means that there is a room for temporary additional government outlays.¹⁰ Both higher wages and government expenditures would raise domestic demand, which has been lagging behind international peers in the last decade.

The optimal size of the current account is hard to determine and clearly beyond the scope of this CPB Background document. The consequences of unsustainable deficits are clear, but those of a too big surplus less so. At some stage an unsustainable deficit will lead to a painful adjustment. A too big surplus means a suboptimal outcome: lower consumption now that is not sufficiently offset by higher consumption later. Also beyond the scope of this Background document is providing options to reduce the Dutch surplus. Many possibilities are suggested by international organisations, from stronger fiscal incentives for non-financial firms to pay higher dividends or invest more in the Netherlands to second-pillar pension reforms.

⁹ On the basis of aggregation of the current account balances of euro area countries. It should be noted however that the Netherlands has a trade deficit with non-euro area countries and a surplus with euro area countries.

¹⁰ See also the opinion (beschouwing) in chapter 1.2 of CPB, 2019, Macro Economic Outlook 2020. [\(link\)](#)

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