Dutch Economy in Focus

Group Economics
Netherlands

28 February 2019

Growth sharply lower

Nico Klene
Tel. +31 (0) 20 628 4204
nico.klene@nl.abnamro.com

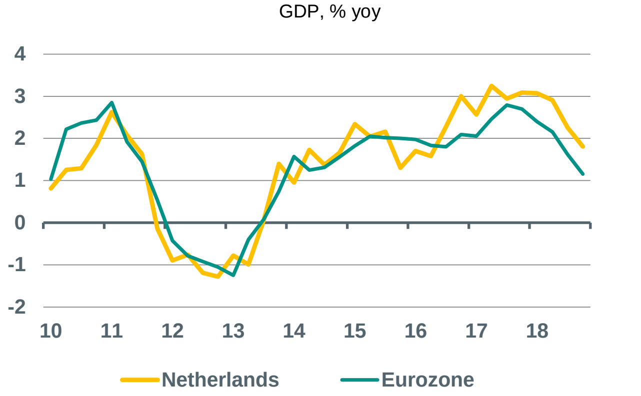
- **Dutch economic growth to fall further this year - for the second year in a row**
- **Growth forecast for 2019 again revised down: from 2% to 1.4%. Mainly due to the stuttering international economy**
- **Private consumption and investment also lose upward momentum this year. The stronger increase in government spending acts as a partial counterweight. All in all, the lion's share of this year's economic growth will be domestically-driven**
- **In 2020 economic growth may rebound somewhat on a modest recovery in the eurozone**
- **Unemployment is very low, but is showing no sign of falling further. The strong deceleration in economic growth will cause job growth to weaken. Unemployment will therefore rise again - particularly next year**
- **Inflation is a lot higher this year than last, mainly due to the increase in the low VAT rate and environmental taxes**
- **The government surplus widened further in 2018, but will narrow strongly this and next year**

Dutch economic growth decelerating strongly
The Dutch economy grew 2.5% last year. That is again significantly above the economy's potential growth rate[1], but clearly less than the 3% of 2017. A further deceleration lies ahead this year. The decline - this year and last - is mainly attributable to the slower expansion of global trade, leading to a further slackening of Dutch export growth. With the international outlook weaker than assumed until recently, we have further reduced our estimates for gross domestic product (GDP) of the eurozone and the Netherlands. We now expect Dutch GDP to increase less than 1½% (previous projection was 2%).

[1] The potential growth rate of the Dutch economy is estimated at 1½ to 1¾%.

This lower growth remains broad-based, however, with exports, consumption and investment all contributing, albeit to a lesser extent than in 2018.

Economic growth decelerated sharply



Source: Thomson Reuters Datastream

Slower growth in second half of 2018 despite good Q4

Q4 2018 saw GDP grow 0.5% relative to the previous quarter. That is clearly more than in the summer quarter, when growth slumped to a mere 0.1% due to a temporary stagnation of consumption and investment; residential investment even showed some contraction in that period. So, the better Q4 figures can be seen as a correction after the weak Q3. This does not alter the fact that growth in the second half of 2018 was substantially lower than in the first half (see graph).

Private consumption and investment regained traction in the final months of 2018.[2] Residential investment advanced strongly, more than cancelling out the contraction in the previous quarter. Government consumption also rose, after two quarters of treading water. The earlier stagnation was remarkable in view of the strong spending impulse planned in the Coalition Agreement.

Exports flagged, however, and even showed negative growth. But this figure contains a downward statistical distortion.[3] Without this distortion, exports would have risen slightly, according to Statistics Netherlands. But the fact remains that export growth has decreased.

As imports also contracted - more than exports - the GDP contribution of net exports (exports minus imports) was more positive than in the summer quarter.

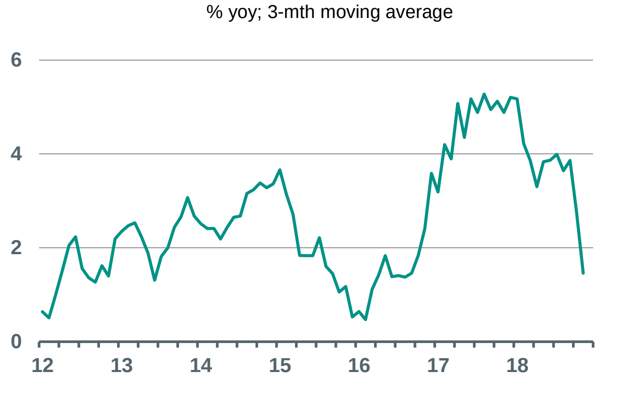
Growth in 2018 more domestic- than export-led

All in all, economic growth slowed in 2018 from 3% to 2.5%. This loss of momentum is almost entirely attributable to the much lower expansion of exports. Domestic spending, by contrast, did slightly better than in 2017. Growth thus depended mainly on domestic spending and less on exports, whereas each contributed equally in 2017.

[2] For detailed figures see the appendix.
[3] A large company formally moved part of its activities abroad, so that its goods flows are no longer recorded as Dutch imports and exports. As a result, both imports and exports turned out lower in the fourth quarter. According to Statistics Netherlands, this had no effect on the trade balance.

The various domestic spending components presented a diverse picture. Household consumption did well with clearly stronger growth than in 2017, while investment expanded less, mainly due to the further deceleration in residential investment. This, incidentally, still grew almost 7% (2017: +12%). Government consumption, finally, increased on a par with 2017 (1%). Evidently, the government has not yet managed to boost its spending. In December 2017, government consumption was still expected to rise 3% based on the plans in the Coalition Agreement.

World trade growth has slumped



Source: Thomson Reuters Datastream

Eurozone growth to remain subdued

In view of the slower expansion of global trade and the weak third quarter, we already lowered our forecasts for the eurozone and the Netherlands three months ago. At the start of this year, the economic momentum weakened further. Moreover, the leading indicators are not yet pointing to an upturn.[4] The earlier decline was partly due to incidental factors (e.g. setbacks for the German automotive industry), and partly to the tightening of the financial conditions in, notably, the US and China. This tightening will continue to make itself felt for some time to come. The uncertainty surrounding the US-China trade conflict and Brexit is also affecting business confidence. Faced with these factors, we further reduced our eurozone growth forecast for 2019 - to 0.8%.

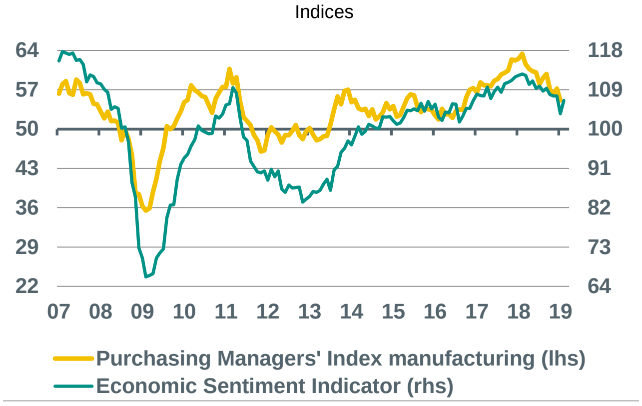
However, we do expect eurozone growth to pick up in the second half of the year partly on the back of the recovering global economy. This recovery will be helped along by more relaxed financial conditions and lower inflation, which is good for purchasing power. Growth will therefore turn out higher next year.

Dutch sentiment indicators point to slower growth

The sentiment indicators in the Netherlands also deteriorated further early this year. This is evident from consumer confidence, which turned negative in February, meaning that more consumers are pessimistic than optimistic (see graph next page). Consumer confidence, incidentally, is still just above the long-term average. This also applies - even slightly more – for the indicators of business confidence. The economic 'barometers' thus point to a further slowdown, but not to a dramatic one.

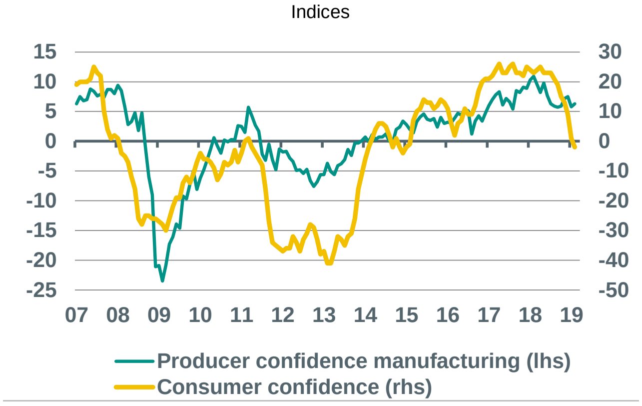
[4] See: insights.abnamro.nl/2019/02/global-daily-changes-to-our-eurozone-ecb-and-rates-forecasts/

Dutch economic barometers …



Source: Thomson Reuters Datastream

… have dropped further



Long-term consumer confidence average is about -3.

Source: Thomson Reuters Datastream

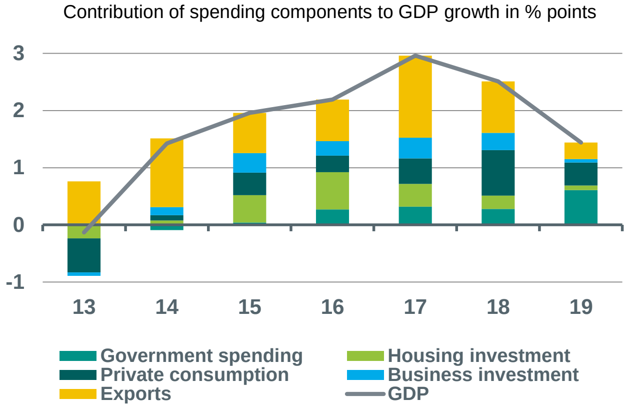
Finally we mention the purchasing managers' indices for the manufacturing sector. At 55 in January, the main PMI is still well above '50', the mark that separates growth from contraction. But striking is the decline of the export order sub-index to a level of 51. That figure tallies with the darkening picture abroad.

Dutch GDP growth forecast again revised down in 2019 - to just under 1.5%

Due to the deteriorated international outlook, we also further reduced the growth forecast for the Dutch economy to 1.4% (was 2%). Exports will again grow less than in the preceding year.[5]

However, private consumption will also rise less this year - a lot less in fact. The main reason is the smaller improvement in real disposable income. Individual purchasing power will rise more than last year, but far fewer jobs will be added due to the weaker economy. On balance, this will depress macro income growth. A further factor is the significant decrease in consumer confidence. This suggests that consumers are tightening the purse strings - presumably mainly at the start of the year.

Growth this year mainly domestically driven



Source: CPB and ABN AMRO

[5] Note, however, that the annual figure for 2019 will be strongly dampened by the distorted contraction of exports in the final quarter of 2018.

Businesses, for their part, will see their sales prospects dwindle, both at home and abroad, and will therefore be less inclined to invest. Residential investment, although still expanding strongly, is also expected to slow further.

Against this, government spending will probably increase more. We assume that a significant portion of the unspent funds carried over from 2018 will be spent this year. This plus point, however, does not weigh up against the minuses.

All in all, the lion's share of economic growth this year will be domestically driven. The moderate upturn in the economic outlook for the eurozone in the course of this year can also push Dutch growth slightly higher next year.

Why will the Netherlands outpace the eurozone in 2019?
Despite the much smaller export expansion, the Dutch economy again looks set to clearly outperform the eurozone economy this year. This is due partly to a statistical effect and partly to government measures. First of all, the statistical 'carry-over effect'. The Dutch economy grew faster than the eurozone economy at the end of last year (+0.5% versus +0.2% qoq). As a result, there is a stronger upward carry-over effect on the *average* GDP increase for 2019 in the Netherlands than in the eurozone. The difference is a quarter percentage point. In addition, government spending will rise more than the eurozone average due to the envisaged measures in the Coalition Agreement. Both factors jointly have an effect on average Dutch GDP of about 0.6% point.

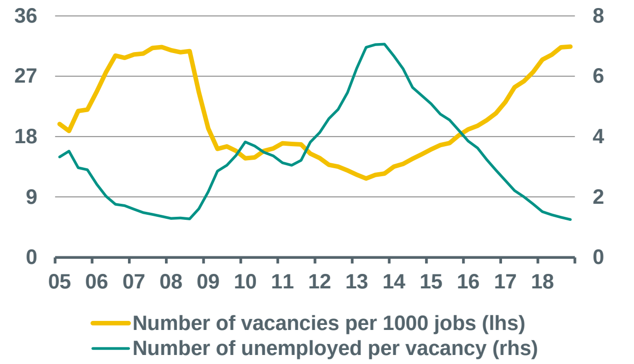
Risks have not disappeared
Dutch economic growth will thus probably weaken to below potential. And there are certain risks that may cause a further deceleration. Take, for instance, the uncertainty surrounding the trade conflict with the US and Brexit (deal or no deal?). Italian public finances can also re-emerge as a source of concern. Italian GDP growth will be much lower than forecast this year, which means that the country's budget deficit will be too high in the eyes of ‘Brussels’. And looking at the Netherlands' own economy, there is the risk that the government's planned spending impulse may again fail to materialise. On the other hand, the uncertainties may also recede more quickly than expected, paving the way for an earlier economic recovery.

Unemployment is very low – but will rise slightly next year
Unemployment fell further last year. At year-end 2018, 3.6% of the labour force was unemployed[6] versus 4.4% at the end of 2017. The figure in January was also 3.6%. Unemployment is now at the same low level as in 2008. This does not yet apply to the ‘broad’ unemployment rate. This includes more groups of people, namely also unemployed people who have *either* looked for work *or* are immediately available for work and also part-time workers who can and want to work longer hours. In the final quarter of 2018 this figure was still a bit above the low level of 2008. There still seems to be some scope for a further decrease in the broad unemployment rate.

[6] The unemployed are people looking for work *and* immediately available for work. Those who do not meet these criteria do not count as unemployed in the statistics. This includes people without work who have *either* looked for work *or* are directly available for work.

Labour market as tight as over ten year ago

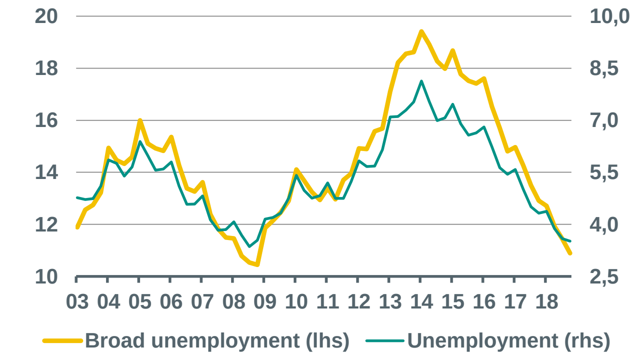
Indices



Source: Statistics Netherlands and own calculation

Broad unemployment not yet at low level of 2008

In % (broad) labour force; not seasonally adjusted



Source: Statistics Netherlands and own calculation

Last summer, the labour market was just as tight as over ten years ago, but the situation did not become more stretched in the fourth quarter.

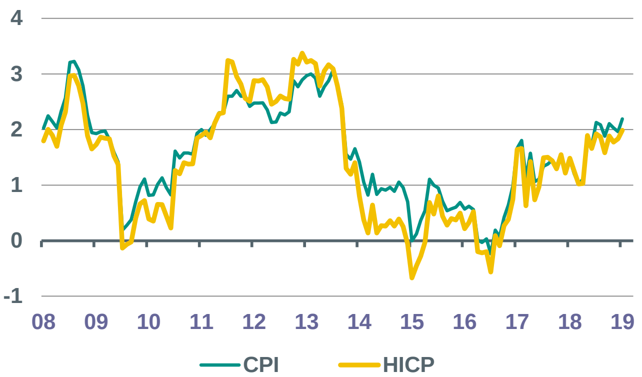
The tension in the labour market may diminish now that economic growth is continuing to flag and job growth is set to weaken. Usually, the labour market responds with a time lag to production. Unemployment will probably rise somewhat in 2020.

Inflation rose less than expected in January

CPI inflation climbed in January from 2.0 to 2.2%. HICP inflation[7] showed a similar increase. This was clearly less than we expected. At the start of the year, the low VAT rate was increased and the environmental taxes were raised more than at the start of last year. We had counted on a stronger price effect in January. This was partly because of our assumption that the full VAT increase would, as usual, be immediately passed on in the prices. The question now is whether the adjustment process may take place more gradually.

Inflation up

% yoy



Source: Thomson Reuters Datastream

[7] The harmonised figure is calculated according to standardised EU guidelines. The HICP can be used to compare developments in inflation between different countries.

Inflation could conceivably rise slightly less this year than we assumed earlier. Added to this, the oil price is now also expected to turn out lower than previously estimated. An upward inflationary effect similar to the one in 2018 can therefore now be ruled out. Partly for this reason, we have reduced our average inflation forecast.

That said, inflation will continue to creep up in the coming months. This has to do with accelerating wage growth due to the tighter labour market. In addition, base effects also play a role: twelve months ago energy prices fell during several months, while they will probably rise now. This has an upward effect on the year-on-year increase in the price level.

The effect of the higher VAT is temporary. Early in 2020 the VAT hike will drop out of the figure, allowing inflation to fall below 2%.

Government surplus to fall sharply this and next year
In the third quarter of 2018, the government's EMU surplus had widened further to about 2% of GDP. This figure relates to the period from Q4 2017 to Q3 2018. The surplus is much bigger than previously thought. One reason is that the government has spent less than intended. The number for full-year 2018 will therefore also be higher than the previous forecasts. However, if the government manages to boost its spending this year, the surplus will decrease again. In addition, lower economic growth will also strongly dampen the surplus.

Key figures Dutch economy

	2017	2018	2019	2020
		% changes		
GDP	3.0	*2.5*	*1.5*	*1.6*
Private consumption	1.9	*2.4*	*1.5*	*1.7*
Government consumption	1.1	1.1	*2.5*	*2.3*
Investment in fixed assets	6.2	4.7	*1.9*	*1.9*
Exports	5.6	*2.6*	*0.9*	*2.6*
Imports	5.2	*2.5*	*1.1*	*3.1*
Consumer prices (CPI)	1.4	1.7	*2.5*	*1.7*
Harmonised consumer prices (HICP)	1.3	1.6	*2.3*	*1.6*
Wages private sector	1.6	2.0	*2.6*	*2.6*
		Levels		
Unemployment (% labour force)	4.9	3.8	3.6	*3.7*
Current account (% GDP)	10.5	10.0	9.7	9.5
Budget balance (% GDP)	1.2	*1.5*	*0.8*	*0.3*

Revised figures in italics.

Forecasts: ABN AMRO Group Economics

APPENDIX. MACRO INDICATORS

Key Figures Dutch economy

	2016	2017	2018				2018	2019f	2020f
				Q2	Q3	Q4	Q1		
		% changes		*qoq*	*qoq*	*qoq*			
GDP	2.1	3.0	2.5	0.7	*0.1*	0.5		*1.4*	*1.6*
Private consumption	1.1	1.9	2.4	0.2	*0.0*	0.5		*1.5*	*1.7*
Government consumption	1.3	1.1	1.1	0.1	0.0	0.5		*2.5*	*2.3*
Investment in fixed assets	-7.3	6.2	4.7	0.7	*-0.1*	0.7		*1.9*	*1.9*
Exports goods & services	1.5	5.6	2.6	*1.3*	*1.1*	-1.3		*0.9*	*2.6*
Imports goods & services	-2.1	5.1	2.5	*0.3*	*1.2*	-2.1		*1.1*	*3.1*
Consumer prices (CPI - % yoy)	0.3	1.4	1.7	1.5	2.0	2.0	2.2 (Jan)	*2.5*	*1.7*
Harmonised consumer prices (HICP - % yoy)	0.1	1.3	1.6	1.5	1.8	1.8	2.0 (Jan)	*2.3*	*1.6*
Hourly wages private sector (% yoy)	1.6	1.6	2.0	1.9	2.1	2.1	2.0 (Jan)	*2.6*	*2.6*
		Levels							
Unemployment (% labour force)	6.0	4.9	3.8	3.9	3.8	3.6	3.6 (Jan)	3.6	*3.7*
Economic Sentiment Indicator (eop)	106.5	111.9	107.6	109.3	109.3	107.6	106.5 (Feb)		
Consumer confidence (eop)	21	25	9	23	19	9	-2 (Feb)		

Revised figures in italics

Forecasts: ABN AMRO Group Economics

Key figures international economy

	2016	2017	2018				2018	2019f	2020f
				Q2	Q3	Q4	Q1		
		% changes							
				qoq	*qoq*	*qoq*			
GDP eurozone	1.9	2.5	1.8	0.4	0.2	0.2		*0.8*	1.3
GDP Germany	2.2	2.5	1.5	0.5	-0.2	0.0		*0.3*	1.4
GDP United States	1.5	2.3	2.9	1.0	*0.8*	0.6		2.3	1.7
		Levels							
USD per EUR (eop)	1.05	1.20	1.15	1.17	1.16	1.15	1.15 (Jan)	*1.16*	*1.25*
3m Euribor (%, eop)	-0.3	-0.33	-0.31	-0.32	-0.32	-0.31	-0.31 (Jan)	*-0.3*	*-0.2*
10y Bund Germany (%, eop)	0.21	0.42	0.25	0.31	0.47	0.25	0.16 (Jan)	*0.2*	*0.5*
10y State, Netherlands (%, eop)	0.35	0.53	0.39	0.47	0.58	0.39	0.26 (Jan)	*0.3*	*0.6*
Oil price Brent (USD/barrel, average)	43.8	54.3	71.0	74.5	75.1	67.7	59.0 (Jan)	*70*	*76*

Revised figures in italics

Forecasts: ABN AMRO Group Economics

Find out more about Group Economics at: **https://insights.abnamro.nl/en/category/economy/**

ABN·AMRO