

Dutch Economy in Focus

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Second and third waves push economy into deeper dip

- ▶ **Dutch economy on course for 4.3% growth in Q3 2020**
- ▶ **That's not nearly enough to make up the 8.5% decline in Q2**
- ▶ **We expect 5.6% contraction this year and a modest recovery of 2.1% next year**
- ▶ **Investments showing some recovery from the shrinkage in 2020**
- ▶ **Global trade rebounding strongly after the Q2 dip, but not yet back to former level**
- ▶ **Unemployment still largely hidden, but gradually rising to 8.5% at year-end 2021**
- ▶ **Disposable income to stagnate in 2021 and 2022**

Growth forecast for 2020 revised down: from -5.2% to -5.6%...

The Covid-19 crisis has plunged economies around the world into a severe recession. The Dutch economy contracted 8.5% qoq in Q2 of this year, a historic low point. That said, the Netherlands still outperformed most of the surrounding countries. Average eurozone contraction ran to almost 12%. As noted in an earlier [publication](#), this downturn was partly induced by the lockdown measures, but the consumer's reaction to the virus also played a role. Being among the euro countries with the lowest economic decline in Q2 also meant that the Netherlands saw a more moderate recovery in Q3. Moreover, as the Netherlands recorded one of the highest Covid-19 infection rates per 1,000 inhabitants, the Dutch economy will end Q3 among the eurozone stragglers. All in all, we expect 4.3% growth qoq in Q3; a weak recovery compared to the sharp decline in the previous quarter. Our calculations for Q4 assume that the cabinet's current restrictions to contain the virus will remain in place until mid-December. And the cabinet may well decide to impose even stricter measures this week. In practice, that will not make much difference for Q4; stricter measures will eradicate the virus faster, so that the restrictions can be lifted earlier, leading to a stronger revival in December. We expect another quarter of negative growth in Q4, namely -1.3% qoq. Overall, this adds up to 5.6% contraction for the Dutch economy in 2020, followed by 2.1% growth in 2021.

Netherlands	2019	2020	2021
GDP	1.7	-5.6	2.1
Private consumption	1.5	-7.7	1.9
Investments	4.6	-5.4	0.2
Export	2.7	-5.8	4.6
Import	3.2	-5.6	4.5
Inflation	2.6	1.4	1.4
Wages	2.4	2.5	1.1

Source: Refinitiv, forecasts ABN AMRO Group Economics

... and the real recovery is still on hold

Pending the development and roll-out of an effective vaccine, the economy will continue to tick over at 95% of its capacity with no prospect of catch-up growth (see also [here](#)). Taking our cue from the WHO, we anticipate a vaccine becoming available in mid-2021 and being fully rolled out by the end of 2021. On top of the Covid-19 restrictions and continuing caution among consumers and businesses, second round effects will also have a stronger impact next year. Higher unemployment, tighter financial conditions and business bankruptcies will dampen the revival. Furthermore, we are factoring in a resurgence of the virus in early 2021 which, though possibly more limited in scale and less damaging to the economy than the second wave, will still impede the recovery in the first half of 2021 (our expectation: Q1 2021: 0.7% qoq; Q2: 0.9% qoq). We see Q2 producing a stronger recovery. Anticipating a vaccine breakthrough, companies will start ramping up their production capacity. The more positive sentiment will also give consumption a boost (our forecast: Q3 2021: 2.4% qoq); Q4 2.9% qoq). All in all, we foresee GDP growth of 2.1% in 2021. This entails that GDP will not yet be back at its pre-Covid level at year-end 2021.

GDP falls back to 2015 level

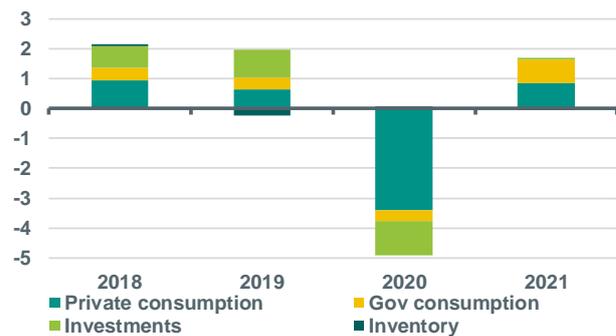
GDP, constant prices 2010; adjusted for seasonal effects and calendar days, thousands, our 2020 and 2021 forecasts in grey



Source: Statistics Netherlands (CBS)

Consumption a major drag factor

Contribution of spending components to GDP growth per year



Source: Statistics Netherlands (CBS)

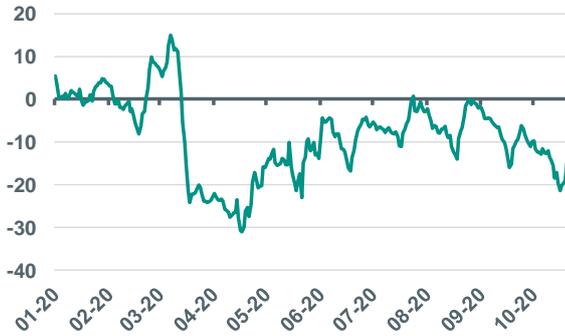
Consumption hit hard by the virus

In line with our [earlier](#) analysis, consumption continues to languish at a structurally lower level despite the lockdown being lifted in July. Across the board, consumption in Q3 remained below the 2019 level, partly due to the 1.5 metre rule, ongoing fears of infection and increased income insecurity. An analysis of our debit card transactions also shows that consumption declined further ahead of the second wave in September. This trend was reinforced by the measures that the cabinet took on 12 October. Since this 'partial lockdown', total consumer spending measured by debit and credit card transactions, online transactions and cash withdrawals has fallen back by 16% yoy on average. For comparison, during the first 'intelligent lockdown' the debit card transaction volume dropped some 20% yoy (mid-March to end of May).¹

¹ The 16% decline, incidentally, is not entirely attributable to the strict measures. Earlier we [concluded](#) that the consumer's reaction to the resurgence of the virus was another key factor. In addition, second round effects are also stronger during the second wave: higher unemployment, postponement of business investments and rising bankruptcies are hampering the economy more than during the first wave.

Falling transactions in October

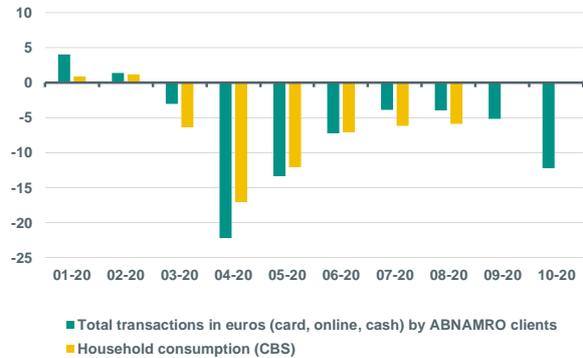
Total ABN AMRO customer transactions in euro (debit card, online, cash withdrawals), % change yoy



Source: ABNAMRO

Transactions correlate strongly with CBS data

Total ABN AMRO customer transactions in euro (debit card, online, cash withdrawals), % change yoy / Domestic consumption by households (volume, adjusted for Sunday shopping days), % change yoy



Source: ABNAMRO and Statistics Netherlands (CBS)

The top-right chart indicates a strong correlation between the ABN AMRO transaction data and the household consumption data as measured by Statistics Netherlands (CBS). Using our transaction data to estimate Q3 and Q4 consumer spending, we see that the decline of almost 13% in Q2 was followed by a recovery of 7.4% in Q3. The bottom-left chart shows the severity of the contraction in Q2. While consumption rebounded in Q3, it remains stuck at the 2014 level due to the second and – if our expectations are correct – third wave. The bottom-right chart illustrates the unprecedented blows suffered by consumer spending in the past two quarters compared to the previous crises.

Complete recovery of consumption not until after 2021

Private consumption, constant prices 2010; adjusted for seasonal effects and calendar days, thousands, our 2020 and 2021 forecasts in grey



Source: Statistics Netherlands (CBS)

Consumption receives unprecedented blow in Q2.

Private consumption, constant prices 2010; adjusted for seasonal effects and calendar days, thousands, our 2020 and 2021 forecasts in grey



Source: Statistics Netherlands (CBS)

Government consumption also lower due to Covid-19 ...

In 2020 government consumption will also depress GDP growth somewhat. This applies in particular to the quarters that saw the first and second waves sweeping through our country. Health care expenditures account for a large share of government consumption. In these months the delivery of normal healthcare was downsized, which reduced the government's total expenditures. Based partly on the measures announced in the Budget Statement, we expect the government to make a positive contribution to GDP growth in 2021. However, if a third wave materialises in Q1 2021, government spending will only pick up slowly. On balance, the public deficit as a percentage of GDP will work out less high than this year, but the public debt will continue to climb.

Partial investment recovery in 2021 after shrinkage in 2020

Like consumption, investments slumped in Q2 of this year amidst diminishing demand, global production disruptions and widespread uncertainty. Due to the second wave in the Netherlands, the recovery in Q3 will be followed by another negative investment number in Q4. But investments will decline less sharply than during the first wave. The reason is that companies have adapted to the new reality. We also assume that the restrictions imposed by our main trading partners will be less stringent than during the first wave. A renewed industrial shutdown in Italy, for instance, is unlikely in our view. As a result, demand for Dutch exports will hold up better than earlier in the year. All this will cushion the decline in investments. We expect investments to contract 5.4% yoy in 2020.

Due to the carry-over effect of the second wave, investments will continue to shrink in Q1 2021. As more information about a possible vaccine becomes available, businesses will steadily cast off their uncertainty. Buoyed by the positive sentiment alongside measures such as the job-related investment relief scheme, businesses will cautiously start to invest again, allowing private investments to stage a slow recovery in Q2 2021. We expect a faster increase in government spending - partly because of the expected expenditures from the first tranche of the national investment fund and partly because of planned investments being brought forward. Note, however, that the binding nitrogen norm will have the opposite effect of delaying new infrastructure investments. Our expectation is that government investments will increase less in 2021 than was announced in the Budget Statement. Taking government and private investments together, we foresee a very cautious recovery of 0.2% yoy in 2021.

Investments get hit in 2020, slight recovery in 2021

Private and public investments in thousands, constant prices 2010; adjusted for seasonal effects and calendar days; forecasts in dotted line



Source: Statistics Netherlands (CBS)

Trade rebounds, but not yet back to former level

The international economy rebounded in Q3. The world trade indicator of the CPB Netherlands Bureau for Economic Policy Analysis showed a strong improvement, partly driven by the rapid recovery of industrial output. As the PMI indicator for global industry shows, business confidence resurged after the relaxation of the lockdown measures. Driven by the production recovery in China, factories around the world got back to work. The Netherlands, which relies heavily on international trade, benefited from the ensuing industrial revival and the global economic recovery. In Q2 trade still made a largely negative contribution to the economy. But this was followed by a clear correction in Q3. Exports outpaced imports in that period. As a result, foreign trade was once again a significant driver of economic growth.

The positive contribution will be lower in the coming quarters and possibly even negative in Q4. The second wave is squeezing worldwide spending, raising the threat of a renewed slowdown in global trade in Q4. But this setback will be less severe than during the first wave. First of all, because the industrial production chains have been less disrupted and

factories in China remain open. Secondly, because trade has not yet recovered after the dip in Q2 and is already at an extremely low level. For 2021 we foresee a moderate trade recovery, partly due to the continuing Covid-19 measures and Brexit which will deal a blow to Dutch imports and exports at the start of 2021. The current account surplus will be less high due to the weak global economy. Corporate earnings are under pressure around the world. As a result, dividend and profit pay-outs from abroad are decreasing, leading to a lower balance on the income account. But at 8% of GDP, the Netherlands continues to run an extremely large surplus on its current account.

Confidence recovering, but fell back in October

Purchasing Manager Index World; 50 is neutral



Source: Statistics Netherlands (CBS)

Trade still a long way from former level

World trade and industrial output, % change yoy



Source: Statistics Netherlands (CBS)

Unemployment largely hidden, but gradually rising

The exceptional nature of the Covid-19 crisis is also reflected in the labour market. An estimated 35% of employed people are active in sectors that have been heavily or very heavily hit. Immediately after the outbreak of the first wave, the government acted to save the jobs of 2.8 million workers (30% of the labour force) by extending a wage cost subsidy (NOW1) to 122,000 businesses. In the subsequent period, between June and October, this wage cost subsidy was continued in order to limit the number of lay-offs. Though the number of businesses drawing this support dropped to 65,000, there are still 1.3 million employees whose wages would be in jeopardy without this lifeline. On top of this, the labour market is more flexible than ever; 36% of employees are not on permanent contracts, more than double the number compared to the crisis in 2009.

From this perspective, it is surprising that the jobless number increased by 'only' 135,000 in the first seven months of the crisis. Is this the calm before the storm and will a substantial part of the 1.3 million employees on wage cost subsidy end up losing their jobs after all?

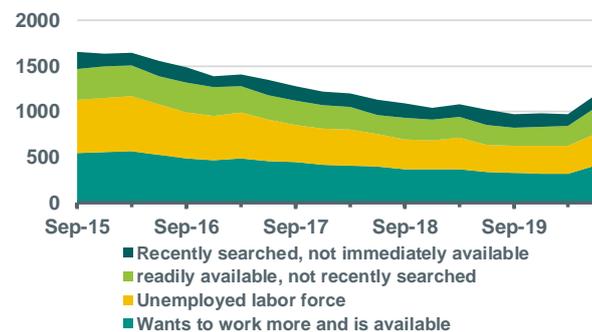
A whirlwind is unlikely, in our view, but we do foresee a gradual gathering of thunderclouds. In December of this year, unemployment will run up from the current 4.4% of the labour force to 5.6%. The second wave combined with the less favourable NOW3 conditions will result in more lay-offs, notably at SMEs which generally have smaller financial buffers than multinationals. This will push unemployment up to 4.1% on average this year. In 2021 we see unemployment rising steadily to 8.5% at the end of the year. Many large companies and multinationals have announced reorganisations which will lead to an increasing number of unemployed in 2021. Average unemployment will thus grow to 7% in that year. That is a high percentage, but still well below the 13% of workers receiving wage cost subsidy until October. Why?

The first factor is the extension of the NOW subsidy scheme for businesses in the period from October 2020 to June 2021. These support measures will push the unemployment peak forward in time. Though the conditions for receiving the bail-out cash are becoming steadily more stringent, the government has also introduced extra support measures since the second

lockdown. Since October, for instance, the compensation for overheads has been available to affected businesses in all sectors, instead of just the directly affected sectors. This, in our view, is a sensible and necessary widening of the support as revenue losses in supply chains also hit businesses that do not suffer directly from the contact restrictions. In addition, businesses will also sustain revenue losses across the entire economy if rising unemployment prompts consumers to tighten the purse strings. Secondly, the increase in unemployment is also being slowed down by the retraining programmes that the Cabinet has started up for employees who need to look for another job. The EUR 1.3bn that the Cabinet has earmarked for retraining is expected to temporarily keep about 110,000 workers from joining the ranks of jobseekers. A third reason is *labour hoarding*. Just before the pandemic struck, the Dutch labour market was exceptionally tight. With this in mind, many employers prefer to retain staff despite there being too little work at the moment. Even now an average of 10% of vacancies cannot be filled, notably in sectors such as healthcare, distribution and renewable energy. Nor do we expect all these jobs to be filled by the rising number of unemployed. The job opportunities in these tight sectors often require specialised skills, which puts them out of reach of many unemployed people. Finally, loss of employment does not equate with an increase in unemployment. Many laid-off employees do not immediately start actively looking for work or are not immediately available for work. Particularly young people and part-timers tend to fall within this category of discouraged workers. Members of the labour force who are not actively seeking and available for work or those who are working but would like to work more hours belong to the population of unused labour potential.

'Invisible' unemployment rising faster

Composition of unused labour potential (x 1,000)



Source: Statistics Netherlands (CBS)

Stagnating disposable income

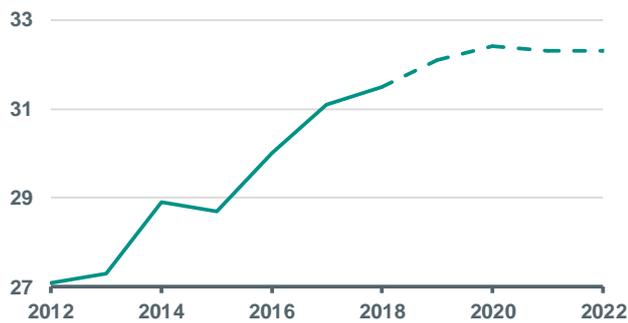
Disposable income – the net amount that a household has to spend on an annual basis – is increasingly under pressure. Disposable income held up reasonably well in 2020, notably due to the NOW scheme, the job protection scheme, unemployment benefit, the impossibility of reopening collective labour agreements (CAO) and the pension reduction system. As a result, businesses and the government are, broadly speaking, picking up the initial bill for the crisis, with household incomes not stagnating until a later stage.

We see four phenomena as a particular cause for concern in 2021 and 2022. First of all, many CAOs are due to expire in 2021. As a result, though average wage increases of 1.5% are being agreed, the total contract wage development in that year will only be 1.1%. Secondly, the pensions of around 1.4 million people will be cut in 2021. Thirdly, after the wave of self-employed people, a second wave of permanent employees will move via unemployment benefit into income support. From the second half of 2021, this income benefit will only rise by about three euros every six months, so that more and more people will be on a benefit that is falling in real terms. Fourthly, this cabinet's tax plan is designed to keep benefits and net wages artificially high in 2019, 2020 and 2021. However, if the policy remains unchanged, this effect will disappear in 2022.

These four phenomena come on top of the rising unemployment rate, which will put many household incomes under pressure as benefits are typically lower than wages. In standardised terms – i.e. adjusted for differences in household size and composition – we expect that, after years of steady increases, the average disposable income in the Netherlands will stagnate. And that is even before the adjustment for inflation. The conclusion is that real disposable income will fall in the coming two years.

Stagnating household incomes

Standardised disposable income in thousands EUR



Source: CBS, adapted by ABN AMRO

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