Netherlands

Stagnation, but no contraction

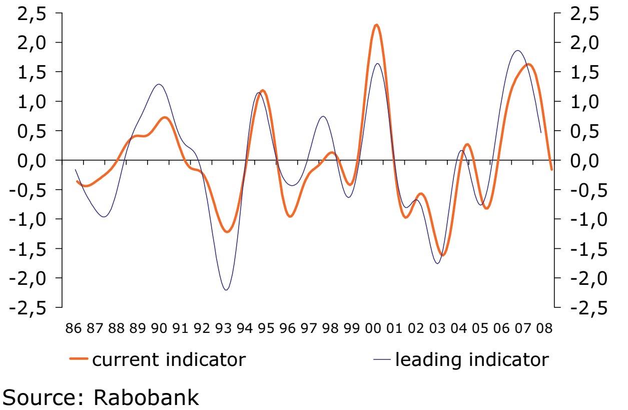
The Netherlands will not escape the global economic downturn. This caused economic growth in our country to come to a halt in the second quarter of 2008. Only in the course of next year will it be possible to report something positive on the Dutch economy again. With an annual growth rate of 2¼% this year and 1¼% next year, 2009 will not see us outperforming the rest of Europe for the first time since 2003. Nonetheless, the Dutch economy is better positioned than it was for the last growth slowdown.

Chance of a recession in the Netherlands?

Up until recently we were not all that pessimistic about the Dutch economy. After it had turned in growth of 3.5% last year – the highest growth this century – we expected a mild downturn (?) for 2008. Whereas in our last quarterly report we referred to an approaching cold front, we now have to face the fact that the Dutch economy has caught quite a bad cold. A credit crisis that keeps dragging on, high food and energy prices, a strong euro and a 'normal' cyclical economic downturn are proving a bit too much for the resilience of the Dutch economy after all. Our own economic indicator (see figure 1) is signalling a continuation of the bad news for the time being. We are therefore assuming in our forecast that growth in the Netherlands will stagnate in the coming quarters. Nor would one or two quarters that edge into the red come as a surprise to us, and there is accordingly a chance of a technical recession (a contracting economy in two successive quarters).

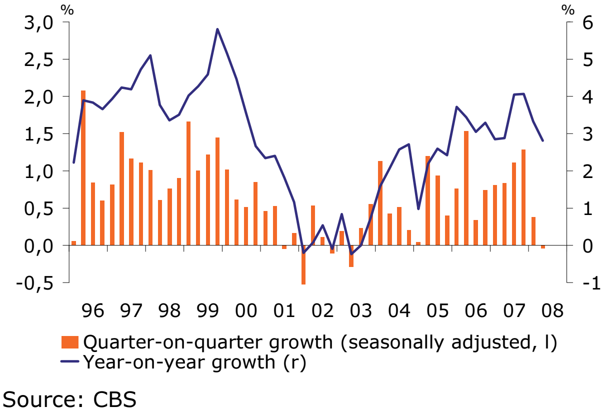
For next year, we expect economic growth to pick up slightly as global growth gathers momentum again. But full-year growth will nevertheless almost be halved to 1¼% compared to this year's rate (2¼%). This is mainly due to the fact that the exuberant growth of the end of last year had a continuing positive effect on growth this year (referred to as the carry-over effect).

Figure 1: Rabobank economic indicator



Source: Rabobank

Figure 2: Stagnating GDP growth in 2nd quarter



Source: CBS

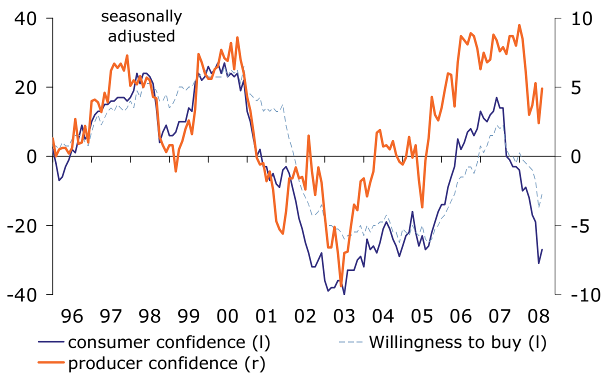
Netherlands

Consumer very downcast ...

Dutch consumers were the first to reflect concern that the bad news about the international economic situation was bound to affect their personal financial situation. Although there was not yet all that much bad news to report on the Dutch economy, consumer confidence in July continued to slide to -31, a level last seen in November 2003. Never before had consumers pegged back their economic expectations so far within a single year. It should be noted that this ties in almost seamlessly with the rest of the Eurozone.

A fall in consumer confidence is usually followed fairly soon by a slowdown in GDP growth (see figure 5). The substantial difference existing between the two series on the basis of the most recent actual figures could well indicate that the growth of the economy has come to a halt quite abruptly.

Figure 3: Consumer and producer confidence



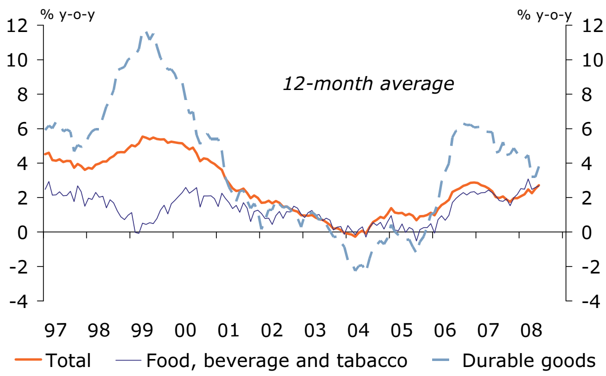
Source: CBS

As had been the case with the record decline in consumer confidence in a single month in September of last year, the assessment of the economic situation worsened sharply. Continuing bad tidings about a credit crisis that just will not go away, high oil prices and sobering economic prospects are the likely causes.

...but the worst is yet to come

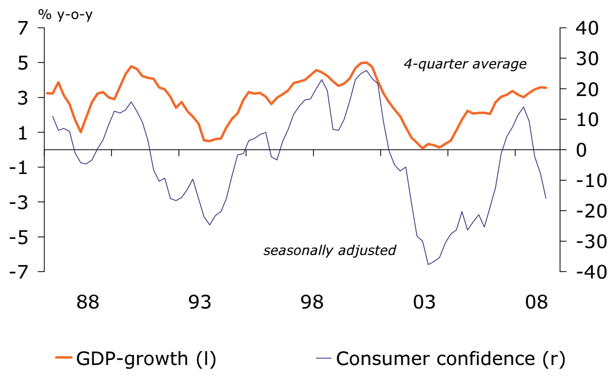
Until now growth in long-term consumption has remained on par, despite consumers' negativism. But we expect this growth of consumption to moderate significantly, in line with the purchasing propensity, during the coming period.

Figure 4: Domestic growth in consumption by product group



Source: CBS

Figure 5: Consumer confidence and GDP growth



Source: CBS

Netherlands

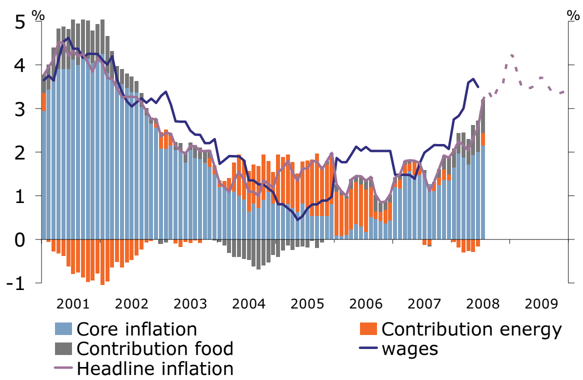
Consumers will increasingly need their cash to meet higher energy bills.

Dutch consumer price inflation spurted to 3.2% in July (2.6% in June). A steep increase, but far from unexpected. Global inflation was fuelled recently by expensive oil and high food prices. The Netherlands lagged behind this trend, especially because the six-monthly adjustment of gas prices in January was very limited (see figure 7). In that respect a part of the arrears was made up in July; gas prices were raised significantly, to a level that is 8% higher than last year. But the full oil price increase of the past year – an increase in euros of some 50% compared to the first six months of 2007 – is still not reflected in the current prices by a long way. We expect gas prices to be upped again in January by a similar percentage. Despite breaking through the 3% boundary, the Netherlands has still the lowest inflation in Europe for now. But this is set to change next year, when Dutch inflation will bound up once more owing to higher energy prices, while other European countries have already put the worst behind them in that respect.

In this light it was a wise decision not to proceed with the VAT increase as of 1 January 2009. If the VAT increase had gone ahead, the inflation rate would have rocketed up beyond 4%. Especially if contractual wage increases reach 4%, there is a chance that core inflation in the Netherlands will rise further.

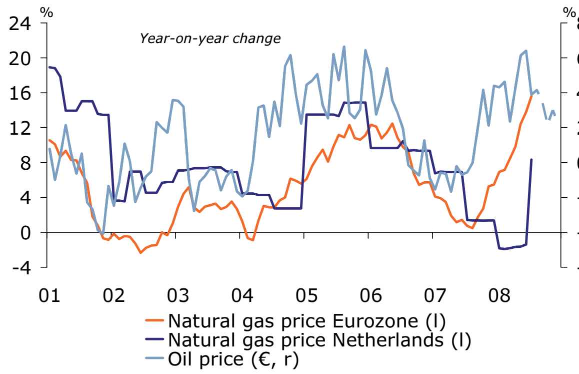
In the course of 2009, inflation will gradually moderate as the contribution of energy and food prices to overall price increases diminishes. This is likely to instil more confidence amongst consumers in the economy and their financial scope, as a result of which consumer spending may pick up again. The growth of ½% in consumer spending we expect to see in 2009 is far from exuberant, however.

Figure 6: Contribution to inflation



Source: CBS, Rabobank

Figure 7: Gas and oil prices in the Netherlands and Europe



Source: CBS, Rabobank, Reuters EcoWin

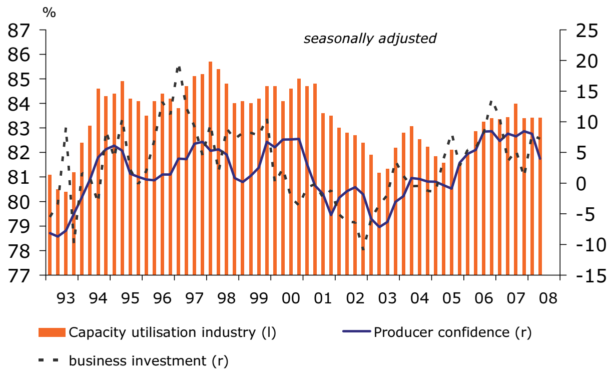
Netherlands

Outlook for producers less promising

While consumer confidence already started to subside in September, producers continued to remain optimistic for a little longer. Producers' confidence even reached a new record as recently as January. The continuing high values were attributable mainly to optimistic expectations for future production. March and April called an abrupt halt to this positive view of the future, causing a sharp decline in producer confidence (see figure 8). The rating of the order position edged down but remained positive. Capacity utilisation in July of 83.4 was level with that of April. Despite this comparatively high capacity utilisation rate, there is little cause for producers to plan enthusiastically for new investments. Domestic demand growth is virtually flat, export growth is limited and wage costs are on the rise; not really a mix to put a smile on employers' faces. In the current year the decline in investment will still be masked by incidental, non-cyclical economic investments, such as acquisitions of aircraft and the completion of energy projects. We expect a slight contraction of investments for next year.

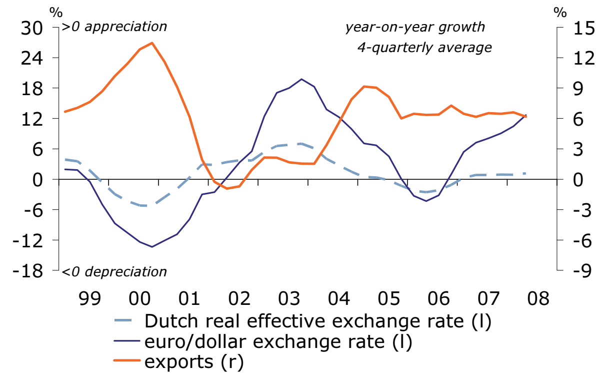
Export growth has so far remained remarkably stable. A clear slackening in export growth has only been visible in the past few months, with growth of re-exports dropping particularly sharply. In fact, it is striking that Dutch export growth remained stable for such a long time. An appreciation of the euro usually goes hand in hand with moderated export growth (see figure 9). Because the trade-weighted exchange rate has been markedly slower to rise, the effect for Dutch exports was considerably less negative. The decline in economic growth in the rest of Europe will not lead to outstanding export performance in the period ahead either. Only in the course of next year, when the European economy picks up again to some extent, will there be good news to report on regarding international trade.

Figure 8: Capacity utilisation rate, corporate investment and producer confidence



Source: CBS, Rabobank

Figure 9: Export and exchange rates



Source: CBS, Rabobank

Limited turnaround in the labour market

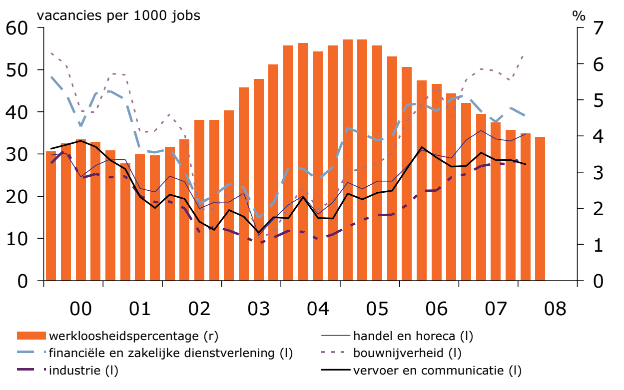
The labour market has been tight for some time. The number of vacancies reached a new record in the past quarter and unemployment is also low at 4%. There are major differences however between the percentages of vacancies by sector and unemployment by age and gender. Vacancy levels are particularly high in the construction sector (see figure 10), and almost the same as at the start of this century. In other sectors, such as financial and professional services, vacancy levels have not yet equalled their previous peak. Unemployment has declined in the past few years to the present level of around 4%. For certain groups of employees, such as men aged between 25 and 44, unemployment at 1.8% has returned to the level of 2001.

Yet the increase in the number of jobs in the current economic cycle has been considerably smaller than in the previous cycle (see figure 11). Owing to the slower growth of the working population, unemployment has fallen in the past few years. Growth of the working population can be expected, partly as a result of the ageing of the population, to slow even further. The labour market will consequently remain tight even at slower growth.
Unemployment stabilised in the first half of the year and employment growth is tapering off. We expect employment growth to be further pressured as a result of the growth slowdown. Unemployment will accordingly nudge up in the course of next year. Nonetheless contractual wages are set to rise significantly next year as well. The trade unions are aiming for compensation of inflation and because tightness is certain to continue in some segments of the labour market, this will often be successful.

Collective sector: Reintroduction of the Dutch disease?

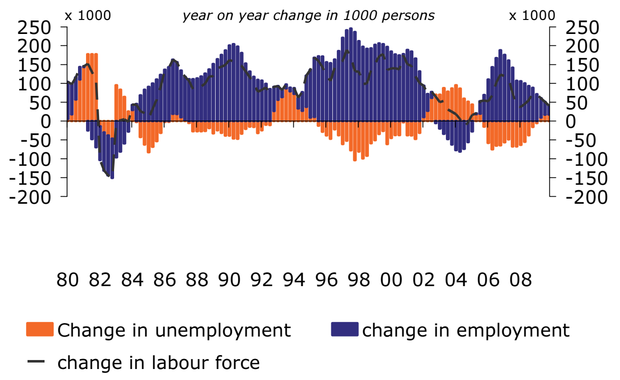
The government does not want to get burnt by the VAT increase as of 1 January 2009. The proposal, which was well founded in itself – lowering labour costs

Figure 10: Vacancy levels by sector



Source: CBS, Rabobank

Figure 11: Change in employment supply, unemployment and working population



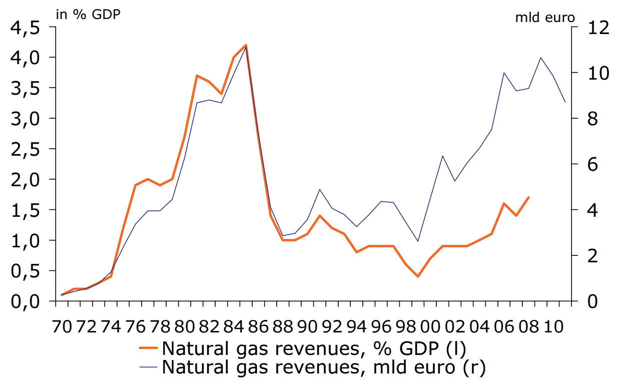
Source: CBS, Rabobank

by discontinuing the unemployment benefit contribution for employees and raising VAT by 1% – has fallen victim to unfortunate timing. Understandably, the government does not want to exacerbate the already rapid monetary depreciation. Postponement tends to end in cancellation. If the cut in the unemployment benefit contribution does go ahead – which the government has declared conditional on the conduct of the social partners – this will by default create a shortfall of EUR 1.4 billion in the central government budget. Given the other deficits (mainly deficits in child day care facilities) the question arises how the government will make up this shortfall. We fear that it will be unable to resist the temptation of the rising natural gas revenues. In 2009 natural gas revenues are expected to exceed those of 2004 by some EUR 5 billion (see figure 12). In times of disputes on how to compensate for shortfalls in the budget it is very tempting to use this cash, which is readily available. For if the government does so, there will still be a budget surplus of around 1% GDP. But this will not do the sustainability of public finances any favours.

Everything negative?

The Dutch economy is currently facing a strong cyclical economic headwind. But fundamentally the economy, especially in comparison with the US or Italy for instance, is in sound shape. Public finances are largely in order, and this downturn will accordingly not be accompanied by major interventions in the economy that can have a procyclical effect. That is a substantial difference from the previous downturn at the start of this century. Nor do we have to fear mass unemployment. Now the government, but the unions as well, must show restraint despite this. For the unions this means not asking for excessive wage increases, which would erode the Dutch competitive position. For the government this means setting course for a long-term budget surplus, and not yielding to the temptation of using incidental windfalls for long-term spending.

Figure 12: Gas revenues in the Netherlands



Source: Ministry of Economic Affairs

Table 1: Key data for the Netherlands

year-on-year %	2006	2007	2008	2009
Gross domestic product	3,4	3,5	2¼	1¼
Private consumption*	3,5	2,1	1½	½
Government expenditures*	1,8	3,0	1¼	2
Private investment	8,3	4,9	5½	-1¾
Gross fixed capital formation	7,5	4,9	5¼	-1
Exports of goods and services	7,3	6,5	3½	2½
Imports of goods and services	8,2	5,7	4	1½
Consumer price index	1,2	1,6	2¾	3½
Unemployment (% labour force)	5,5	4,5	4	4¼
Government budget (% GDP)	0,5	0,4	1	1¼
Current account (% GDP)	7,6	8,3	6¾	8

* corrected for the administrative effects of the implementation of the new Health care system in 2006

Source: CBS, Rabobank

Hans Stegeman
H.W.Stegeman@rn.rabobank.nl