Rabobank

Country report

THE NETHERLANDS

Summary

The Netherlands has weathered the crisis relatively well. The Dutch economy shrunk in 2009 by 3.9%, and has by now made up half of that loss. The Dutch economy remains highly competitive, continuing its track record of structural trade surpluses, further expanding its net international investment position, all of which is endorsed by the flexible labour market and low unemployment rate. However, the crisis has also caused structural damage. The financial position of the government has worsened due to interventions in the financial sector and structurally lower revenues. In addition, age-related expenditure will rise in the near term. This has left the government with a task to restructure its finances. In our opinion the cabinet has planned the wrong measures to cope with these tasks, which reduces the chances of success. Additional challenges are formed by the labour and housing market.

Things to watch:

- Government finances: keep track of progress in austerity program
- Labour market: the consequences of the decrease in the work force
- Housing market: price developments and development of number of forced sales.

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Netherlands

National facts	
Type of government	Constitutional monarchy
Capital	Amsterdam
Surface area (thousand sq km)	42
Population (millions)	16.5
Main languages	Dutch (official)
	Frisian (official)
Main religions	None (42%)
	Roman Catholic (30%)
	Protestant (20%)
Head of State (queen)	Beatrix
Head of Government (prime-minister)	Mark Rutte
Monetary unit	EUR

Economy	2010	
Economic size	*bn USD*	*% world total*
Nominal GDP	782	1.25
Nominal GDP at PPP	674	0.91
Export value of goods and services	572	3.08
IMF quotum (in mln SDR)	5162	2.38
Economic structure	*2010*	*5-year av.*
Real GDP growth	1.7	1.5
Agriculture (% of GDP)	3	3
Industry (% of GDP)	25	25
Services (% of GDP)	73	72
Standards of living	*USD*	*% world av.*
Nominal GDP per head	47161	479
Nominal GDP per head at PPP	40633	348
Real GDP per head	41297	516

Social and governance indicators	rank / total
Human Development Index (rank)	7 / 169
Ease of doing business (rank)	30 / 183
Economic freedom index (rank)	15 / 179
Corruption perceptions index (rank)	7 / 178
Press freedom index (rank)	1 / 178
Gini index (income distribution)	30.9
Population below $1 per day (PPP)	N/A

Foreign trade			2010
Main export partners (%)		*Main import partners (%)*	
Germany	30	Germany	19
Belgium	15	China	14
France	11	Belgium	10
UK	9	US	9
Main export products (%)			
Machinery and transport equipment			34
Chemicals and related products, n.e.s.			16
Mineral fuels, lubricants, and related materi			15
Food, drinks and tobacco			15
Main import products (%)			
Machinery and transport equipment			36
Mineral fuels, lubricants, and related materi			19
Chemicals and related products, n.e.s.			13
Food, drinks and tobacco			11
Openness of the economy			
Export value of G&S (% of GDP)			73
Import value of G&S (% of GDP)			65
Inward FDI (% of GDP)			-1.6

Source: EIU, CIA World Factbook, UN, Heritage Foundation, Transparency International, Reporters Without Borders, World Bank.

The open Dutch economy has benefited in 2010 from the recovery in world trade, as can be seen in the improvement in export volume. Exports grew by 10.6% in 2010, making up for the losses of 2009. The economy as a whole grew in 2010 with 1.7%. Both private and government consumption contributed positively, while business investment declined further.
For 2011 we expect this trend to continue. International trade will again be the main driver of economic growth. Domestic dynamics will remain weak as private consumption and business investment will grow moderately. The overall government finances are in a relatively good shape. However, the discretionary policy measures adopted during the financial crisis and the rise in ageing-related expenses will force the government to implement austerity measures in the coming years, depressing growth to some extent. The unemployment rate in the Netherlands will remain low from an international perspective, and decrease from 5.4% in 2010, to 5.0% in 2011.
Overall, the Dutch economy is in relatively good shape, with a trade surplus for several decades, high competiveness, a low level of unemployment, an extensive pension scheme and relatively healthy government finances. Although the current state of the Dutch economy is improving, some aspects need some extra attention.

Government finances

As stated above Dutch public finances have deteriorated since the start of the crisis. In 2007 the budget balance showed a small surplus of 0.2% of GDP and a debt to GDP ratio of 45%. In 2010 the budget deficit ended up to be 5.4% of GDP and debt to GDP had risen 62.7% of GDP. The reason for the worsening of the government finances is two-sided. First, via discretionary stimulus measures (including the intervention in the financial sector). But although there were billions of euro's involved in these discretionary stimulus measures, the main cause of the deterioration of the government finances was the structural loss of revenues. Revenues will not be fully recover as economic activity will be structurally lower. The gap between lower revenues and the level of expenses has to be narrowed. Besides the crisis-related structural revenue shortfalls, age-related expenditure will rise faster than the tax base in the years to come. Taking into account the structural loss of revenues and the growing age-related expenditure, this leaves the Netherlands with a structural financing gap of around 27 billion euro's (4.2% of GDP). The new government (2010) has announced austerity measures of 18 billion euro's by the end of 2015 to diminish the budget deficit to 0.9% of GDP in 2015.

Our main criticism on the austerity measures is that they are incoherent and lack long-term vision. A large share of the austerity measures is for instance to be delivered by downsizing the government, which in our view has a low probability of success. A better option would have been to implement structural reforms, like for example reform of the social security system, healthy care or the housing market (the rental market and the market for home owner occupied houses in tandem).[1] An addition constraint is the minority position of the cabinet in the Lower House. They have tolerance support of the Party for Freedom on the austerity measures, but for other policies they have to find support by the opposition. Another constraint could rise due to their expected minority position (seats of the Party for Freedom included) in their Upper House (elections were held on the 2nd of March 2011; on the 23th of May these elected representatives will vote for the members of the Upper House). Furthermore a lack of urgency may arise as the headline budget balance is improving faster than expected, while the structural shortage will remain unchanged.

An additional risk to the Dutch government's financial position are the loans and the guarantees it has provided to among others the financial sector and some European countries. Although most of the financial institutions have partly redeemed their loans to the government, the exposure is still estimated to be €47.1 billion[2]. In addition, Dutch public government has accepted €13.4 billion exposure to Greece and Ireland in the form of guarantees. This can potentially grow to €69 billion.[3,4]

Labour market

During the crisis the unemployment rate has been rising moderately. However, since March 2010 the unemployment rate declines, and currently fluctuates around 5%. In the upcoming years the labour force will start declining since the baby boom generation leaves the labour market. This will result in a shortage of labour supply in an already tight labour market. In addition, the structural mismatch, due to the lack of supply of high and technical labour and excess supply of low educated people, will hinder the unemployment levels to decrease. In this setting there might arise a situation in which wages rise considerably, which will cause significantly higher costs of labour for employers, eroding competitiveness and hurting the prime strength of the Dutch economy.

Housing market

The Dutch housing market is characterized by low levels of forced sales and stable prices developments. Cause is the fixed interest rate on mortgages and the fact houses are a pure

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[1] The cabinet assumes that we budget deficit will be brought back to 0.0% of GDP by 2015. We however doubt that this goal will be reached for the reasons stated above. We therefore follow the figures of the CPB.

[2] Rijksoverheid (2011) "Garantieoverzicht 2009-2011", 17 februari 2011

[3] CPB (2011) "Positie Griekenland slecht, te strenge aanpak werkt niet", CPB Policy Brief 2011/03

[4] Including the indirect guarantees provided by the ECB and the IMF, as being a member of these institutions

consumption good. The loan-to-value and debt-to-GDP ratios of Dutch mortgages are however high from an international perspective. Negative prices developments over the last two years, of respectively 3% and 2% and restrictions to provide mortgages will result in further declines in house prices going forward. And as a consequence the collateral for banks will decrease. This will not be problem as long as the number of forced sales remains at low levels. Also, these gross metrics do not appreciate the fact that Dutch households have a net substantial net wealth position due to their extensive pension scheme.

Netherlands

Selection of economic indicators	2006	2007	2008	2009	2010	2011e	2012f
Key country risk indicators							
GDP (% real change pa)	3.4	3.9	1.9	-3.9	1.7	1.5	1.3
Consumer prices (average % change pa)	1.2	1.6	2.5	1.2	1.3	1.8	1.6
Current account balance (% of GDP)	9.3	6.7	4.3	4.6	6.5	5.5	5.1
Total foreign exchange reserves (mln USD)	10802	10270	11476	17871	18471	N/A	N/A
Economic growth							
GDP (% real change pa)	3.4	3.9	1.9	-3.9	1.7	1.5	1.3
Gross fixed investment (% real change pa)	7.5	5.5	5.1	-12.7	-4.9	2.0	1.7
Private consumption (real % change pa)	-0.3	1.8	1.1	-2.5	0.4	1.1	1.0
Government consumption (% real change pa)	9.5	3.5	2.5	3.7	1.5	0.3	-0.6
Exports of G&S (% real change pa)	7.3	6.4	2.8	-7.9	10.9	4.8	3.2
Imports of G&S (% real change pa)	8.8	5.6	3.4	-8.5	10.6	3.5	2.6
Economic policy							
Budget balance (% of GDP)	0.5	0.2	0.5	-5.4	-5.2	-4.3	-3.5
Public debt (% of GDP)	47	45	58	61	64	66	69
Money market interest rate (%)	3.1	4.3	4.6	1.2	0.8	1.0	1.9
M2 growth (% change pa)	8	11	9	2	0	5	2
Consumer prices (average % change pa)	1.2	1.6	2.5	1.2	1.3	1.8	1.6
Exchange rate LCU to USD (average)	0.8	0.7	0.7	0.7	0.8	0.8	0.8
Recorded unemployment (%)	5.5	4.5	3.8	4.8	5.5	4.9	4.7
Balance of payments (mln USD)							
Current account balance	63333	52590	37294	36437	50500	42000	38000
Trade balance	47586	57256	61812	50970	57500	49200	43500
Export value of goods	389585	465004	535605	424320	479200	489100	480400
Import value of goods	342000	407750	473790	373350	421700	439800	436900
Services balance	9369	12137	13080	7932	6900	6800	5000
Income balance	16703	-608	-20320	-12165	1200	2500	5100
Transfer balance	-10325	-16198	-17273	-10290	-15200	-16500	-15600
Net direct investment flows	-57029	71020	-60899	5193	-37610	-8320	-5920
External position (mln USD)							
Total foreign exchange reserves	10802	10270	11476	17871	18471	N/A	N/A
International investment position	22900	-50690	15580	135660	N/A	N/A	N/A
Total assets	3088090	3782040	3339030	3491380	N/A	N/A	N/A
Total liabilities	3065190	3832730	3323450	3355720	N/A	N/A	N/A
Key ratios for balance of payments, external solvency and external liquidity							
Trade balance (% of GDP)	7.0	7.3	7.1	6.4	7.4	6.4	5.8
Current account balance (% of GDP)	9.3	6.7	4.3	4.6	6.5	5.5	5.1
Inward FDI (% of GDP)	1.0	15.9	0.6	4.2	-1.6	2.7	3.7
International investment position (% of GDP)	3.4	-6.5	1.8	17.0	N/A	N/A	N/A

Source: EIU