# Country report **THE NETHERLANDS**

**Summary**

In the aftermath of the financial crisis the Dutch economy managed to recover as it was able to benefit from expanding world trade. Lately however the economy has slowed down, ending up in recession in the latter half of 2011. Despite the worsened growth forecasts for the short run, the Dutch economy remains highly competitive, continuing its track record of external current account surpluses, further expanding its net international investment position. Furthermore, the labour market is characterized by a low unemployment rate. However, the crisis has also placed government finances on a less stable footing due to interventions in the financial sector and structurally lower revenues. Additional spending cuts are needed to comply with European budget standards and the government's self-imposed rules. In addition, age-related expenditure will rise in the near term. In our opinion the government should restructure its finances by taking structural reforms instead of resorting to across the board spending cuts.

**Things to watch:**

- Government finances: additional austerity measures on their way
- Labour market: employment under pressure in the short run
- Housing market: price developments and development of forced sales
- Pension funds coverage ratios: decisions on pensioners' benefits and the retirement age

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## Netherlands

| National facts | | |
|---|---|---|
| Type of government | Constitutional monarchy | |
| Capital | Amsterdam | |
| Surface area (thousand sq km) | 42 | |
| Population (millions) | 16,6 | |
| Main languages | Dutch (official) | |
| | Frisian (official) | |
| Main religions | None (42%) | |
| | Roman Catholic (30%) | |
| | Protestant (20%) | |
| Head of State (president) | Beatrix | |
| Head of Government (prime-minist | Mark Rutte | |
| Monetary unit | EUR | |
| **Economy** | | **2011** |
| *Economic size* | *bn USD* | *% world total* |
| Nominal GDP | 841 | 1,22 |
| Nominal GDP at PPP | 722 | 0,91 |
| Export value of goods and services | 658 | 3,00 |
| IMF quotum (in mln SDR) | 5162 | 2,38 |
| *Economic structure* | *2011* | *5-year av.* |
| Real GDP growth | 1,3 | 1,4 |
| Agriculture (% of GDP) | 3 | 3 |
| Industry (% of GDP) | 24 | 25 |
| Services (% of GDP) | 73 | 72 |
| *Standards of living* | *USD* | *% world av.* |
| Nominal GDP per head | 50469 | 468 |
| Nominal GDP per head at PPP | 43323 | 351 |
| Real GDP per head | 41687 | 513 |

| Social and governance indicators | rank / total |
|---|---|
| Human Development Index (rank) | 3 / 187 |
| Ease of Doing Business Index (rank) | 31 / 183 |
| Index of Economic Freedom (rank) | 15 / 179 |
| Corruption Perceptions Index (rank) | 7 / 183 |
| Press Freedom Index (rank) | 3 / 178 |
| Gini index (income distribution) | 30,9 |
| Population below $1.25 per day (PPP) | n.a. |

| Foreign trade | | | 2010 |
|---|---|---|---|
| *Main export partners (%)* | | *Main import partners (%)* | |
| Germany | 30 | Germany | 18 |
| Belgium | 15 | China | 15 |
| France | 11 | Belgium | 10 |
| UK | 9 | US | 8 |
| *Main export products (%)* | | | |
| Machinery and transport equipment | | | 35 |
| Chemicals and related products, n.e.s. | | | 17 |
| Mineral fuels, lubricants, and related materi | | | 17 |
| Food, drinks and tobacco | | | 14 |
| *Main import products (%)* | | | |
| Machinery and transport equipment | | | 36 |
| Mineral fuels, lubricants, and related materi | | | 22 |
| Chemicals and related products, n.e.s. | | | 13 |
| Food, drinks and tobacco | | | 10 |
| *Openness of the economy 2011* | | | |
| Export value of G&S (% of GDP) | | | 78 |
| Import value of G&S (% of GDP) | | | 70 |
| Inward FDI (% of GDP) | | | 0,5 |

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

The Dutch economy has recovered after the 2009 recession due to expanding world trade. However, in the latter half of 2011 the economy ended up in a recession as net foreign trade was no longer able to drive the economy. Looking forward, a contraction of the economy by 0.8% is expected in 2012. This is mainly due to a sluggish development of world trade as the situation on the financial markets, government spending cuts and the high oil price in the highly developed economies continue to leave their mark. Domestic dynamics will remain weak as private consumption and business investment are expected to decline. Consumers are hesitant as there is much uncertainty over additional austerity measures, while house prices decline and pension benefits are uncertain. Business investment remains low in the face of underutilisation of existing production capacity. Weakening growth forecasts result in a deterioration of public finances, forcing the government to implement additional spending cuts. Overall, nevertheless, the Dutch economy is in relatively good shape. Growth was above the euro area average during most of the decade leading to the crisis, the current account exhibits sizable surpluses, and the fiscal position is still relatively strong. Furthermore, competitiveness is high and unemployment is low when compared internationally.

### Government finances

Dutch public finances have deteriorated since the start of the crisis. The budget deficit widened from 0.2% of GDP in 2007 to 4.2% in 2011. Meanwhile the debt-to-GDP ratio has risen from 45% in 2007 to 65% in 2011. Discretionary stimulus measures (including interventions in the financial sector) and a structural loss of revenues account for the widening gap between government expenditures and tax income in recent years. To bring public finances in check the Rutte-government (2010) committed itself to implementing austerity measures of € 18 billion by the end of 2015. At the time of taking office it was thought these measures would reduce the budget deficit to 0.9% of GDP in 2015. However, due to worse-than-expected economic growth forecasts and unforeseen expenditures it recently appeared that the current term of government would conclude in 2015 with a budget deficit of 3.3% of GDP, more than 2%-point higher than the amount the Dutch government forecasted at the time of taking office. According to its own rules as well as European rules, the government had to find additional spending cuts. An estimated 9 billion in additional spending cuts are needed in order to comply with the European deficit standard of 3% in 2013. After seven weeks of negotiation on a new austerity package between the ruling minority government and Geert Wilder's Freedom Party (PVV), talks collapsed on 21 April. Following this event Prime Minister Mark Rutte offered resignation of his government on 23 April. Rutte's demissionary government will seek to secure parliamentary approval of budget cuts in cooperation with some opposition parties.

The government has previously expressed concerns that slackening budget discipline will come at the expense of Dutch creditworthiness and will consequently bring about a downward spiral of increasing interest expenses and rising government debt. However, thus far the Netherlands still enjoys safe haven status, as interest on newly issued government paper is among the lowest in Europe.[1] Looking forward, the problem with Dutch government finances will primarily stem from an aging population and resulting expenditure increases on health-care and state pensions. As a result Dutch government debt is, according to the calculations of the European Commission (2009), at risk of doubling over the next two decades.[2]

We underscore the need to balance public finances but also believe that the government should look for measures which do not harm the long-term growth capacity of the economy. Too much austerity comes with the risk of bringing about a negative spiral of spending cuts and slowdown in (potential) growth. The risk is that the government will resort to a series of small measures and cuts across the board (as it did in 2010). However, we believe it is important that policymakers take reforms which structurally curb the (future) growth in government spending, whilst avoiding an unnecessary slowdown in short-term economic growth. This will include reforms of the social security system, housing market and health care. However, if the Netherlands wants to meet its austerity target, there is no escaping of short-term budgetary spending cuts and tax and premium increases. The fact that Dutch politicians have been pushing hard in Europe for rock-solid budget agreements means they have left themselves with limited (moral) room for manoeuvre.

**Labour market**

The Dutch labour market has shown resilience in the midst of the difficult economic times. Unemployment has risen only modestly during the crisis, mainly because strong pre-crisis profitability coupled with the fear of future labour shortages from population aging have kindled labour hoarding by firms. Unemployment has been climbing somewhat over the latter half of 2011. Until recently the rising unemployment could be attributed to the fact that the number of persons looking for work rose more quickly than the number of jobs. Lately the situation has changed, with employment starting to decrease. For the remainder of 2012 employment will remain under

[1] Piljic, D. and H.W. Stegeman (2012), The Netherlands – Deservedly core, Special Report 2012/3.
[2] European Commission (2009), Sustainability report 2009, European Economy 9, Brussels.

pressure. Employment in the market sector is shrinking because production is not expected to pick up. Planned reductions in the numbers of government workers will lead to a decrease in employment in public administration and education as well. The labour supply is anticipated to remain approximately stagnant. Looking somewhat further ahead, the labour force will start declining as the baby boom generation leaves the labour market.

**Housing market**

House prices have declined by a cumulative 11% since 2008 Q3. Annualized transactions have dropped to 110.000, while the stock of homes for sale increased to just over 220.000. For 2012 we expect house prices to decline by 5%, caused by a combination of carry-over from 2011 (which explains half of the decrease) and the fact supply continues to outstrip demand. On the plus side we do not expect a 'hard landing' of house prices given that the Dutch housing market is characterized by low levels of forced sales. This is due to low unemployment, fixed interest rate on mortgages and the fact that houses are a pure consumption good.

**Pension funds**

Coverage ratios of pension funds are low amid widespread uncertainty over future benefits. After a temporary improvement, the average coverage ratio dropped under 95% in Q3 of 2012 and has since recovered to just short of 100%. Continued frailty of financial markets, low interest rates and increasing life expectancy are to be blamed for the insufficient recovery of coverage ratios. The authorities agreed that a reduction in retirement benefits (through lowering of the replacement rate or further raising of the retirement age) is thus required to re-establish solvency, as they do not consider desirable an increase in contributions.[3] Some of the largest pension funds have already announced plans to cut pensions in 2013 if coverage ratios improve insufficiently.

[3] Nevertheless, tripartite discussions among government, employers, and employees on ensuring solvency have been laborious and slow moving. The opinion of the State Advocate in support of grandfathering existing risk-sharing arrangement has cast further doubts on the proposal.

## Netherlands

| Selection of economic indicators | 2007 | 2008 | 2009 | 2010 | 2011 | 2012e | 2013f |
|---|---|---|---|---|---|---|---|
| *Key country risk indicators* | | | | | | | |
| GDP (% real change pa) | 3,9 | 1,8 | -3,5 | 1,6 | 1,3 | -0,8 | 1,3 |
| Consumer prices (average % change pa) | 1,6 | 2,5 | 1,2 | 1,3 | 2,3 | 2,0 | 1,7 |
| Current account balance (% of GDP) | 6,7 | 4,3 | 4,2 | 6,6 | 7,8 | 8,2 | 7,7 |
| *Economic growth* | | | | | | | |
| GDP (% real change pa) | 3,9 | 1,8 | -3,5 | 1,6 | 1,3 | -0,8 | 1,3 |
| Gross fixed investment (% real change pa) | 5,5 | 4,5 | -10,2 | -4,4 | 5,7 | -3,0 | 2,0 |
| Private consumption (real % change pa) | 1,8 | 1,3 | -2,6 | 0,4 | -0,9 | -0,6 | 0,7 |
| Government consumption (% real change pa) | 3,5 | 2,8 | 4,8 | 1,0 | 0,4 | -1,0 | -0,7 |
| Exports of G&S (% real change pa) | 6,4 | 2,0 | -8,1 | 10,8 | 3,8 | -0,7 | 2,7 |
| Imports of G&S (% real change pa) | 5,6 | 2,3 | -8,0 | 10,6 | 3,5 | -1,6 | 2,4 |
| *Economic policy* | | | | | | | |
| Budget balance (% of GDP) | 0,2 | 0,5 | -5,5 | -5,0 | -4,2 | -4,0 | -3,2 |
| Public debt (% of GDP) | 45 | 58 | 61 | 63 | 65 | 69 | 70 |
| Money market interest rate (%) | 4,3 | 4,6 | 1,2 | 0,8 | 1,4 | 1,0 | 0,8 |
| M2 growth (% change pa) | 11 | 9 | 2 | 0 | 4 | 5 | 4 |
| Consumer prices (average % change pa) | 1,6 | 2,5 | 1,2 | 1,3 | 2,3 | 2,0 | 1,7 |
| Exchange rate LCU to USD (average) | 3,7 | 3,7 | 3,7 | 3,7 | 3,7 | n.a. | n.a. |
| Recorded unemployment (%) | 4,5 | 3,9 | 4,8 | 5,5 | 5,2 | 5,4 | 5,6 |
| *Balance of payments (mln USD)* | | | | | | | |
| Current account balance | 52677 | 37488 | 33801 | 51308 | 65700 | 63900 | 60400 |
| Trade balance | 57352 | 61118 | 46804 | 51641 | 58800 | 61600 | 58700 |
| Export value of goods | 465768 | 530193 | 419794 | 480705 | 551900 | 529500 | 548900 |
| Import value of goods | 408420 | 469070 | 372990 | 429060 | 493100 | 467800 | 490200 |
| Services balance | 12158 | 13087 | 7932 | 10572 | 10200 | 8600 | 7600 |
| Income balance | -610 | -19482 | -10683 | 3532 | 13900 | 10400 | 12400 |
| Transfer balance | -16223 | -17235 | -10251 | -14436 | -17200 | -16800 | -18400 |
| Net direct investment flows | 71020 | -57554 | 10860 | -64864 | -31080 | -29200 | -30700 |
| *External position (mln USD)* | | | | | | | |
| International investment position | -50690 | 34530 | 170170 | 212540 | n.a. | n.a. | n.a. |
| Total assets | 3782040 | 3345010 | 3522390 | 3576700 | n.a. | n.a. | n.a. |
| Total liabilities | 3832730 | 3310480 | 3352220 | 3364160 | n.a. | n.a. | n.a. |
| *Key ratios for balance of payments, external solvency and external liquidity* | | | | | | | |
| Trade balance (% of GDP) | 7,3 | 7,0 | 5,9 | 6,6 | 7,0 | 7,9 | 7,5 |
| Current account balance (% of GDP) | 6,7 | 4,3 | 4,2 | 6,6 | 7,8 | 8,2 | 7,7 |
| Inward FDI (% of GDP) | 15,9 | 1,1 | 4,6 | -2,0 | 0,5 | 1,4 | 1,8 |
| International investment position (% of GDP) | -6,5 | 3,9 | 21,4 | 27,2 | n.a. | n.a. | n.a. |

Source: EIU

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