

The Netherlands: Domestic momentum stays

The Dutch economy continues to grow above potential thanks to strong domestic demand, and as long as hard Brexit and trade war fears don't materialise, we forecast GDP growth of 2.8% this year and 2.5% for 2019, which is still above the Eurozone average



Source: Shutterstock

Soft indicators fell, but still point to strong growth ahead

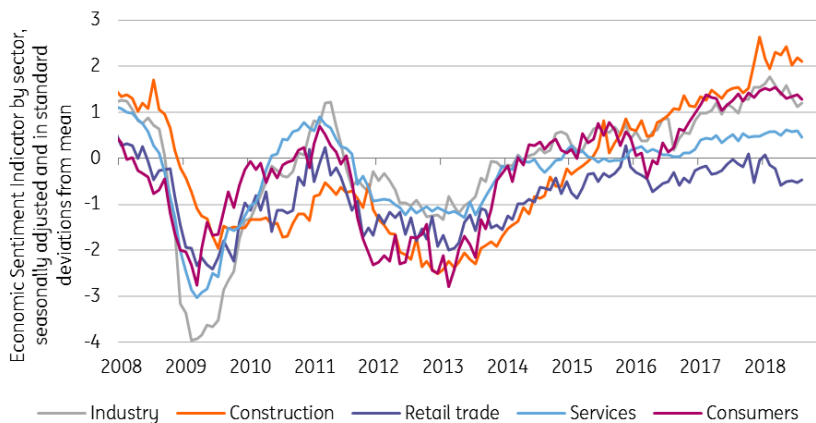
The outlook for the Dutch economy is still rosy, even though a number of survey indicators are currently lower than when they were at the peak, around the turn of the year.

We forecast GDP growth of 2.8% for this year and 2.5% for 2019, which in both years is above the potential growth rate and the Eurozone average.

Strong domestic demand makes Dutch GDP growth less vulnerable to risks abroad than in recent years

While geopolitical tensions seem to have affected the mood, the sentiment is still more positive than the historical average in services and industry and especially in construction. Purchasing managers' index shows the industry is more optimistic about domestic order positions than new export orders, however continuing export growth may be combined with downward risks for foreign demand. Fortunately, strong domestic demand makes Dutch GDP growth less vulnerable to risks abroad than in recent years.

Survey indicators lower but still above historical average



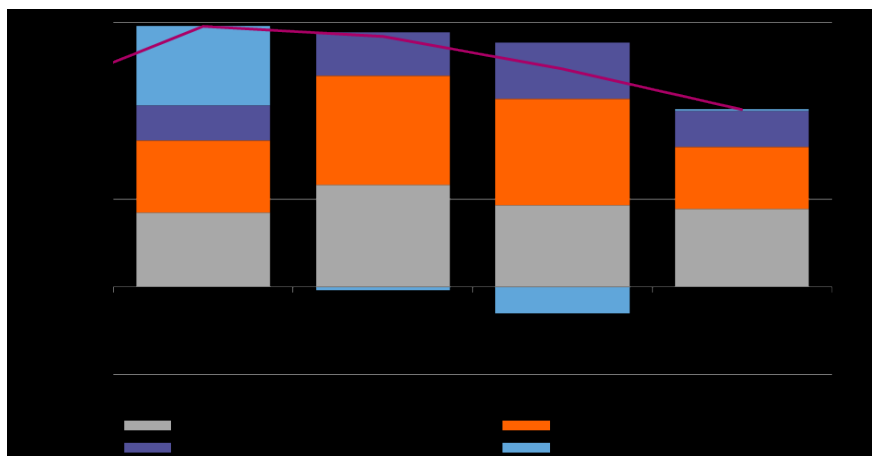
Source: DG ECFIN via Macrobond

Consumption acceleration keeps economy pacing forward

The mood in retail is still subdued and consumers haven't been going on spending sprees, despite 17 quarters of positive GDP growth in a row and domestic demand recently providing the most forceful push.

While a value-added tax hike in 2019 might somewhat limit the acceleration of household consumption, we expect consumers to start being less thrifty by the end of this year and in 2019. The continuous tightening in the labour market and wage growth that has finally begun to accelerate supports our view.

Domestic demand driving high growth



Source: Statistics Netherlands via Macrobond, ING estimates for 2018-2020

Import growth outpaces moderate exports growth

Due to an unusual and unexpectedly weak first quarter, Dutch exports are expected to grow at a subdued pace of 2.5% this year. Accordingly, we project weak import growth of 2.9%. Together, this drives the annual net contribution of foreign trade to nearly zero.

Current account surplus is expected to remain around 10% of GDP

During 2018 and 2019, export growth is projected to maintain its pace, although slightly below historical averages. On the back of further improvements of households' disposable income, businesses continuing to buy (foreign) equipment and the government restricting gas production (and hence net gas exports) in the earthquake-stricken province of Groningen, percentage-wise imports may grow faster than exports in the quarters ahead.

Nevertheless, the current account surplus is expected to remain around 10% of GDP.

Tighter labour market to limit further unemployment falls

The labour market continues to reflect strong growth, but employment growth might have reached its peak in the second quarter of 2018, recording 2.5% YoY.

We forecast unemployment to fall a little further, reaching 3.5% in 2019, after 3.9% in 2018

While unemployment fell to 3.8% mid-2018, the falls are slowing, also because more people are (re)entering the labour force. Growing businesses will continue to hire more people, but find it increasingly difficult to do so. More than one in four businesses is reporting shortages of workers as a factor limiting production.

We forecast unemployment to fall a little further, reaching 3.5% in 2019, after 3.9% in 2018. Persisting labour demand is starting to show up in wages. Wage growth remained very modest in recent years but agreed collective wage agreements showed an upward jump from 1.9% to 2.3% in half a year.

Policy boosts consumer price inflation in 2019

Increasing wage pressures are hardly visible in inflation figures yet.

Food, clothing and communication are currently keeping headline consumer price inflation at moderate levels, just above 1%. Fuel and energy price have caused headline inflation to rise from 1.4% in 2017 to a projected 1.8% in 2018.

We expect inflation to rise further to 2.6% in 2019, primarily due to an increase in the reduced VAT

rate (from 6% to 9%). Food items and some services (e.g. theatre and hairdresser) will see the largest increases in prices. Also, wage pressure will start to feed into output prices during 2019.

All industries growing, except gas

All industries are growing in 2018 except gas production, which is likely to shave off 0.1 to 0.2% points off GDP growth both in 2018 and 2019.

Once the political goal to entirely shut off the gas tap in the Northern Province of Groningen has been achieved, this may cost between 0.5% to 1% of GDP beyond our forecast horizon.

Commercial services, including IT and job agencies, construction and health care are the sectors that grow at the highest rates. The solid growth in commercial services, which is responsible for more than half of capital formation, contributes heavily to the steady investment outlook of around 6% in both 2018 and 2019.

Public finances in line with European norms despite fiscal expansion

Fiscal policy is largely in check, with a fiscal balance close to 1% of GDP in 2017 and years to come. For the long-term, only a minor consolidation challenge remains.

The Rutte-III government uses cyclical tax revenues to offset falling gas revenues as well as to spend more and cut taxes. There is procyclical additional spending on defence, education, R&D, civil service and infrastructure in 2018, which will increase in 2019. In 2019, labour taxes will be lowered, while energy taxes will rise. Government debt was 56.4% of GDP at the end of 2017, below the European norm of 60% GDP. We expect the drop to continue and fall below 50% of GDP in 2020.

Above potential growth in 2019 again?

Compared to previous business cycles, the positive output gap is small. From a domestic point of view, the economy has ample space to grow above the estimated potential rate of 1.7%. We expect GDP growth in 2019 to come in around 2.5%, conditional on foreign downwards risks such as a hard Brexit, or major escalation of the trade war not materialising.

For 2020 we expect a normalisation towards potential.

The Dutch economy in a nutshell (%YoY)

	2017	2018F	2019F	2020F
GDP	2.9	2.8	2.5	2.0
Private consumption	1.9	2.6	2.1	2.0
Investment	6.1	5.8	6.2	3.2
Government consumption	1.1	2.0	2.7	1.7
Net trade contribution (%-point)	0.9	0.0	-0.3	0
Headline CPI	1.4	1.8	2.6	2.0
Unemployment rate (%)	4.9	3.9	3.5	3.5
Budget balance (% of GDP)	1.1	0.9	1.1	1.2
Government debt (% of GDP)	56.4	53.1	51.0	48.0

Source: Statistics Netherlands via Macrobond, all forecasts ING estimates

Author

Marcel Klok

Senior Economist, Netherlands

marcel.klok@ing.com

Disclaimer

This publication has been prepared by the Economic and Financial Analysis Division of ING Bank N.V. (“ING”) solely for information purposes without regard to any particular user’s investment objectives, financial situation, or means. *ING forms part of ING Group (being for this purpose ING Group N.V. and its subsidiary and affiliated companies)*. The information in the publication is not an investment recommendation and it is not investment, legal or tax advice or an offer or solicitation to purchase or sell any financial instrument. Reasonable care has been taken to ensure that this publication is not untrue or misleading when published, but ING does not represent that it is accurate or complete. ING does not accept any liability for any direct, indirect or consequential loss arising from any use of this publication. Unless otherwise stated, any views, forecasts, or estimates are solely those of the author(s), as of the date of the publication and are subject to change without notice.

The distribution of this publication may be restricted by law or regulation in different jurisdictions and persons into whose possession this publication comes should inform themselves about, and observe, such restrictions.

Copyright and database rights protection exists in this report and it may not be reproduced, distributed or published by any person for any purpose without the prior express consent of ING. All rights are reserved. ING Bank N.V. is authorised by the Dutch Central Bank and supervised by the European Central Bank (ECB), the Dutch Central Bank (DNB) and the Dutch Authority for the Financial Markets (AFM). ING Bank N.V. is incorporated in the Netherlands (Trade Register no. 33031431 Amsterdam). In the United Kingdom this information is approved and/or communicated by ING Bank N.V., London Branch. ING Bank N.V., London Branch is authorised by the Prudential Regulation Authority and is subject to regulation by the Financial Conduct Authority and limited regulation by the Prudential Regulation Authority. ING Bank N.V., London branch is registered in England (Registration number BR000341) at 8-10 Moorgate, London EC2 6DA. For US Investors: Any person wishing to discuss this report or effect transactions in any security discussed herein should contact ING Financial Markets LLC, which is a member of the NYSE, FINRA and SIPC and part of ING, and which has accepted responsibility for the distribution of this report in the United States under applicable requirements.

Additional information is available on request. For more information about ING Group, please visit www.ing.com.