

Economic Developments and Outlook

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Summary

The outlook for the Dutch economy in the 2020-2022 period is dominated entirely by the COVID-19 pandemic and government measures to curb the spread of the coronavirus. The economic damage that occurred in the first and second quarters of 2020 is so extensive that a deep, almost worldwide recession is inevitable. Gross domestic product (GDP) in the Netherlands is projected to fall by 6.4% in 2020, marking the largest contraction in post-war history, almost twice as large as during the credit crisis (2009). Private consumption shows an unprecedented contraction of 7.6%. Corporate investment (excluding housing) slides by 13.9%, with exports down 10.9%. Government spending provides some relief, with growth of 3.1%. After 2020 a slow but steady recovery sets in, with GDP growing by 2.9% in 2021 and 2.4% in 2022. The expenditure categories that shrink most in 2020 show the biggest recovery in subsequent years.

Employment is set to suffer severely in both 2020 and 2021. As a result, unemployment will climb to 4.6% of the labour force in 2020, rising further to 7.3% in 2021 and falling to 5.7% in 2022. HICP inflation will be low throughout the projection horizon. Inflation this year is set to stay low (0.8%), particularly due to the sharp

drop in oil prices. Although businesses face additional costs, the dominant factor in subsequent years will be the impact of sluggish demand, with inflation edging slightly higher to 1.1% in 2021 and 1.5% in 2022. The Netherlands' public finances will see a historically large reversal in 2020, from a comfortable surplus to a deficit of 6.4% of GDP. The Dutch government will remain in deficit in 2021 and 2022. Following a sharp increase of over 9 percentage points in 2020, the debt-to-GDP ratio will rise steadily in subsequent years, reaching an average of 63.1% in 2022.

A great deal of uncertainty surrounds the future trend in the rate of COVID-19 infections and the necessity, duration and effectiveness of future containment measures. Scenarios can be helpful in situations like this, particularly given the greater-than-usual uncertainty surrounding our projections. Accordingly, it has been decided within the European System of Central Banks (ESCB) to draw up two alternative scenarios in addition to the projection. These show a GDP contraction in 2020 ranging from 3.4% in the mild scenario to 11.8% in the severe scenario. Rather than defining the extreme upper and lower limits to possible outcomes, the scenarios illustrate the high degree of uncertainty around the baseline projection.





1 The Dutch economy in 2020-2022



1.1 Deep economic contraction due to pandemic¹

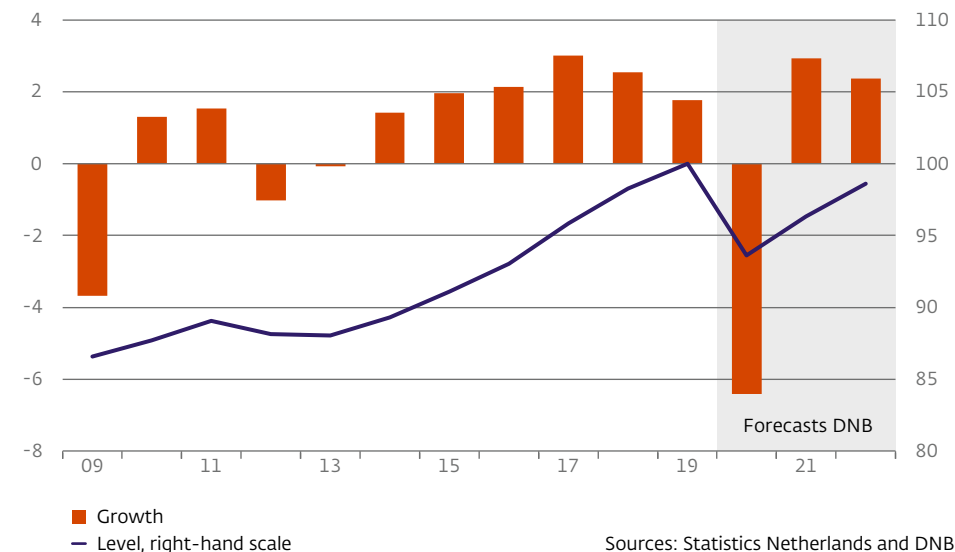
The outlook for the Dutch economy in the 2020–2022 period is dominated entirely by the COVID-19 pandemic. Governments around the world have taken measures to limit the spread of the coronavirus. In addition, governments and monetary authorities have intervened with large support packages and easing measures to cushion the economic impact of the outbreak. The first wave of infections now appears to be under control in large parts of the world. The resulting economic damage is so extensive that a deep global recession is inevitable.

The current economic downturn has its roots outside the economy. It is first and foremost a medical crisis, and the economic developments are to a large extent connected with the control of the pandemic. The great uncertainty surrounding the pandemic means that the associated economic developments are also highly uncertain. In common with the ECB and other organisations, DNB has therefore decided on this occasion to publish different scenarios (Chapter 3), with the middle scenario being presented as the baseline projection. This is not intended to reflect the probability of the two alternative scenarios, although at present the risks to the baseline projection appear more to the downside than the upside.

Gross domestic product (GDP) in the Netherlands is projected to contract by 6.4% in 2020 (see Figure 1). That downturn is almost twice as deep as during the credit crisis in 2009. GDP per capita falls back to the 2015 level at a single stroke. The projection is subject to great uncertainty, particularly in terms of the extent to which restrictions can be eased and infections remain under control. It has been assumed that the measures introduced in March will be eased after three months, but that attempts to gain full control of the virus are only partially successful. Hence there will be occasional flare-ups of infections, so restrictions – albeit less draconian –

Figure 1 Gross domestic product

Volume; year-on-year percentage changes and 2019 = 100



Sources: Statistics Netherlands and DNB.

have to stay in place until a medical solution becomes available in mid-2021. In these circumstances the economy may return to above-average growth from the second half of 2020, but without staging a full recovery. Some businesses, particularly those involving extensive social interaction, will maintain restrictions. Consumer behaviour will also be affected by the risk of a second wave of infections and firms will postpone their investments amid the persistent uncertainty. GDP growth is projected to be 2.9% in 2021 and 2.4% in 2022. At the end of 2022, however, GDP will still be around 1% lower than at the end of 2019.

¹ The assumptions underlying the development of relevant world trade, exchange rates, international commodity prices and interest rates are based on information available on 20 May 2020.

The starting point for this exceptional economic projection is March 2020, when many countries introduced increasingly strict policies to limit interpersonal contact. On 11 March the WHO declared that the virus outbreak, which was initially limited to China, had escalated into a pandemic. Historically, it is the first pandemic in which practically every government in the world has intervened fundamentally in the social and economic lives of its citizens. Governments in most countries have judged that short-term economic harm is preferable to much greater longer-term economic damage, with health being paramount. [Box 1](#) analyses the impact of containment measures on public health and the economy based on an epidemiological model.

The Dutch government began an 'intelligent lockdown' in March, drastically curtailing travel and shutting down hospitality and leisure activities as well as large sections of public services, including education and healthcare. Partly for that reason, some retailers found it was no longer profitable to stay open. Many firms also had to contend with a sudden halt in supplies from the Netherlands or abroad, forcing them to curtail or shut down production. An immediate supply shock therefore occurred in the final weeks of March, estimated to be equivalent to around one-fifth of the economy (-19% GDP). This shock was unevenly spread across sectors. The worst affected was hospitality, with an initial downward shock estimated at 87% of added value. Other badly hit sectors were culture, sport and recreation (-71%), other services (-42%), rental and other business services (-40%), wholesale and retail trade (-33%) and transportation and storage (-33%).

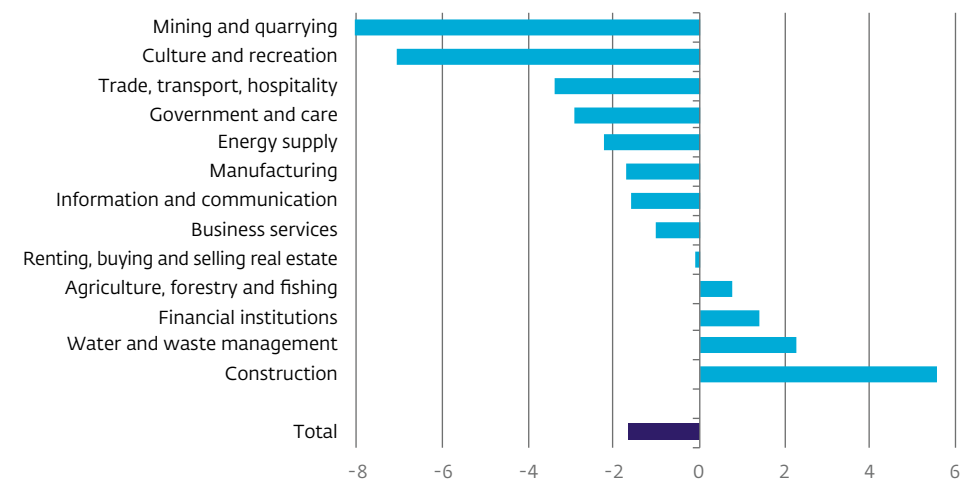
Since the containment measures were introduced at the end of the quarter, the effect of the initial shock is only partly reflected in first-quarter GDP growth. The contraction in the first quarter amounted to 1.7% compared to the previous quarter, marking an end to a long succession of 23 quarters of growth. Figure 2 shows how this contraction was spread among the sectors in the first quarter. The sectors showing a sharp contraction match the picture described above, with culture and recreation, hospitality and government among the sectors worst affected by the

containment measures. The biggest contraction, in mining and quarrying (-8.0%), is connected with the longer-term phasing out of natural gas extraction. Construction, having been little impacted by the containment measures, saw continued strong growth in 2020Q1. A further factor is that the construction sector posted lower-than-expected growth at the end of 2019.

The biggest adverse effects of the COVID-19 shock are expected to be felt in the second quarter, reflecting not only the impact of the lockdown but also the knock-on effects on expenditure. Households, businesses and foreign customers are expected to significantly reduce their expenditure amid slumping confidence, mounting uncertainty and loss of income. Producer confidence in manufacturing fell to an all-time low of -28.7% in April, below the lowest level seen in the credit crisis in February 2009. Consumers are also very gloomy, with a confidence indicator

Figure 2 Added value by sector in 2020Q1

Quarter-on-quarter percentage changes; volume



Source: Statistics Netherlands.

falling from -2 in March to -20 and -31 in April and May respectively, the biggest two-month fall since records began in 1986. A cautious recovery is expected to begin in the third and fourth quarters of 2020, aided by the partial phasing out of the containment measures and supported by the government's expansionary policy. However, due to the steep fall in the first half, the picture for 2020 as a whole remains one of a very sharp GDP contraction (-6.4%), the biggest in post-war history.

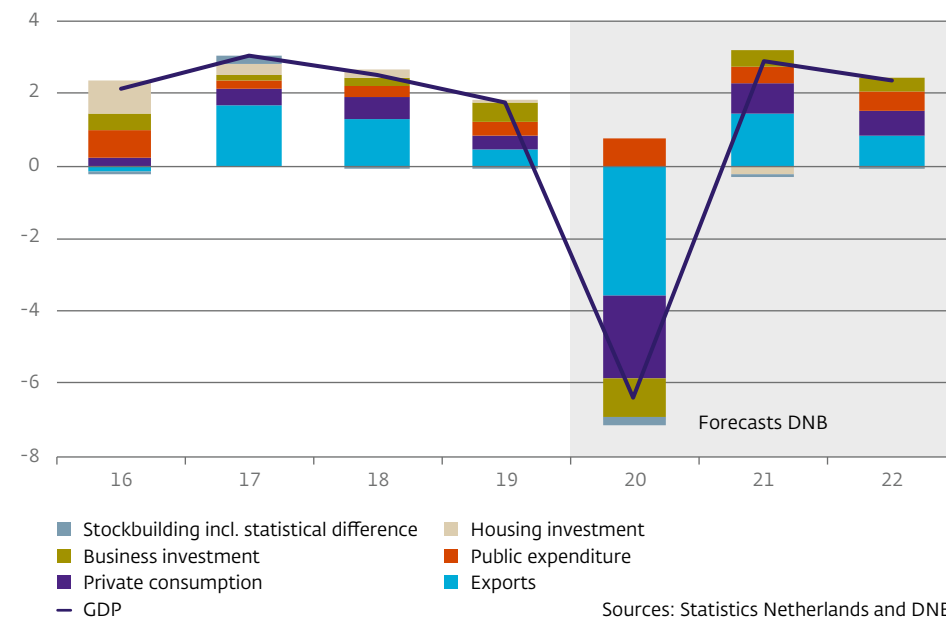
The projections for growth of GDP and the expenditure components can be found in the [Key Data](#). Private consumption is set to fall by an unprecedented 7.6% in 2020. Corporate investment (excluding housing) slides by 13.9%, with exports falling by 10.9%. Government spending provides some relief, with growth of 3.1%. Figure 3 shows the composition of GDP growth over the projection horizon, with the concomitant parts of final and intermediary imports having being deducted for each expenditure category. In 2020 the bulk of the contraction is associated with the steep fall in exports of goods and services, which make up a large part of GDP. The upturn in 2021 can also be attributed largely to exports. Domestic spending makes the biggest contribution to economic growth in 2022.

1.2 Employment shrinks, unemployment rises rapidly

The COVID-19 shock is having a major impact on the labour market, as is evident from the recent figures. In April unemployment rose to 314,000 people, or 3.4% of the labour force, compared to 2.9% in March. That is by far the biggest increase since 1992 (international definition). Total employment (in persons) is projected to fall by 1.4% in 2020 (see Figure 4). This is a sharper contraction than any seen since 1977, although it is still less severe than might be expected given the forecast GDP contraction. This is partly due to government policy aimed at preserving employment through wage cost subsidies (the NOW scheme). In addition, the labour market usually responds to economic developments with a time lag. Firms are reluctant to make immediate cuts to their workforce, particularly with labour market

Figure 3 Sources of GDP growth

Year-on-year percentage changes and contributions in percentage points



Note: Net contributions to GDP growth. The final and cumulative intermediary imports have been deducted from the related expenditure categories.

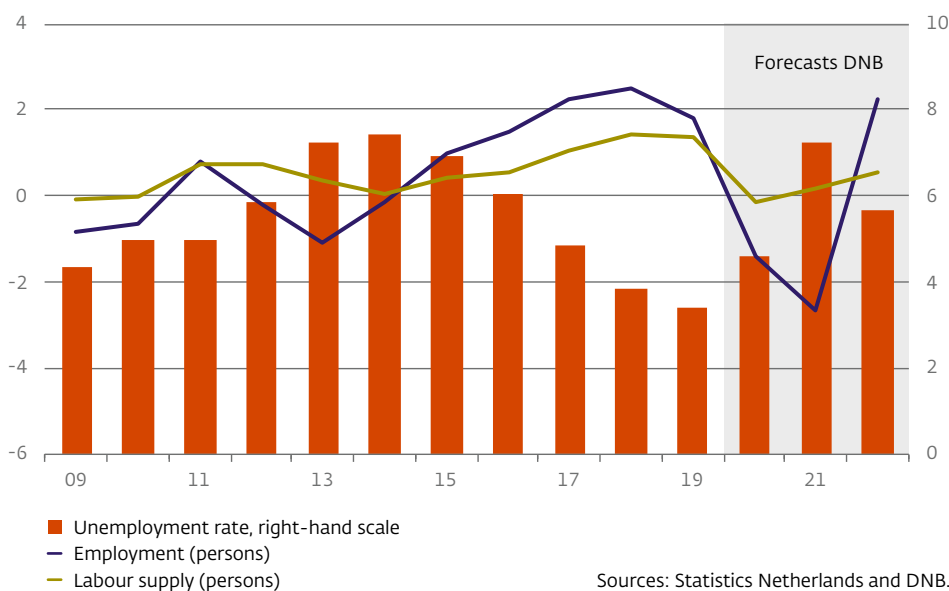
tightness fresh in their mind, and will first try to reduce working hours per person (labour hoarding). Moreover, it is not always possible to terminate employment contracts immediately. Even in a bankruptcy it can take several weeks for the firm to be dissolved and personnel formally dismissed. These factors mean that employment (in persons) falls even more sharply in 2021 (-2.7%) than in 2020. In the projection for 2022 the number of persons employed will increase by 2.3% after the economy has shown several quarters of growth and firms resume hiring after a time lag. Section 2.4 considers the developments and outlook with regard to flexible labour.

The labour market adjusts faster in terms of hours than in terms of the number of persons. The number of hours worked is expected to fall by 6.5% this year, more or less in line with the GDP contraction. The number of hours worked also responds faster to the economic recovery. The number of hours worked grows by 2.3% in 2021 and 3.0% in 2022.

The projected economic contraction will constrain the supply of labour in the years ahead. The number of people in employment or looking for work is expected to decrease by 0.1% this year, a level comparable to the contractions in 2004 and 2009. From next year the labour supply is expected to see limited growth of 0.2% in 2021

Figure 4 Labour market

Year-on-year percentage changes and percentage of labour force



and 0.6% in 2020. By way of comparison, the supply increased by an average of 1.4% per year in 2018 and 2019. Aside from demographic trends, various mechanisms are simultaneously at play in the development of the labour supply. First, the contraction in employment depresses the growth in supply, as not everyone who loses their job looks immediately for a new one. Whereas in April 2020 the number of people in paid employment fell by 160,000, unemployment rose by 30,000 and the labour supply showed a net decrease of 130,000 people. In addition, people who have not previously been active in the labour market will be discouraged from looking for work (discouraged workers). The chance of finding a job has fallen substantially in recent months. Between the end of December and the end of March, the number of vacancies fell by 60,000, the largest quarterly fall on record. Finally, other households have a more pressing need to look for work (added worker effect). If the breadwinner is made redundant or has to work fewer hours, the partner will also look for more work to supplement their income.

The contraction of employment ultimately means that unemployment rises to an average of 4.6% of the labour force in 2020. The sustained contraction of employment (in persons) causes unemployment to rise to 7.3% next year. That means around 700,000 people have no job but are actively looking for one, a figure that is comparable to the most recent low point in the labour market in 2014. From 2022 the labour market begins a gradual recovery, reducing the average unemployment rate in that year to 5.7%.

In terms of unemployment alone, the impact of the recession is understated. The unemployment rate is only one of the indicators of tension in the labour market. Broader indicators, such as labour market slack, are likely to show that more people are being affected. Labour market slack is the total of unemployment, part-time workers seeking to work more hours, discouraged workers and jobseekers who are not immediately available (within two weeks). In the first quarter of 2020 labour

market slack reached a record low of 8.8% of the labour force, after peaking at 16.5% in 2014. If this level is reached again in the years ahead, over 1.5 million people will be looking for work or extra hours.

1.3 Wage growth slows

As last year, contractual wage growth in the business sector is expected to average 2.3% this year (see Figure 5). Growth of compensation per employee, comprising contractual wages, wage drift and employers' social contributions, will nevertheless be lower this year than in 2019. Less is expected to be paid out on bonuses and other incidental remuneration this year, so wage drift will depress compensation per employee by almost 1 percentage point.

Few wage agreements have so far been concluded for 2021 and 2022. The rise in contractual wages in the new collective labour agreements will be substantially lower than in the recent agreements and will decrease to 0.7% in 2022. Employees' negotiating power is decreasing due to the rapid easing of the labour market. Although a contraction of nominal wages is unusual in the Netherlands, employers can reduce their wage costs by cutting incidental remuneration. The contribution from incidental pay is expected to be negative in every year of the projection horizon. Compensation also continues to lag behind inflation, so wages fall in real terms. That has a negative impact on purchasing power, but contributes positively to the development of employment.

The wage cost subsidy (NOW) leads to a particular development of labour productivity and unit labour costs in 2020. In firms that continue to receive that subsidy, wage costs and employment hold steady, whereas production falls. This contributes to a substantial fall in labour productivity per employee in 2020, while unit labour costs rise strongly (7.8%). Since the support measures are not expected to

Figure 5 Compensation per employee (private sector)

Year-on-year percentage changes and contributions in percentage points, in FTEs



continue in 2021, the relationships between production, employment and wage costs normalise from next year.

This year's substantial fall in labour productivity boosts firms' labour income share (LIS), which rises by almost 3 percentage points to 76.0%. From next year labour productivity recovers, while real labour costs decrease. The growth in real labour costs will therefore lag behind labour productivity growth in 2021 and 2022, with the result that the LIS falls to 73.9% in 2022.

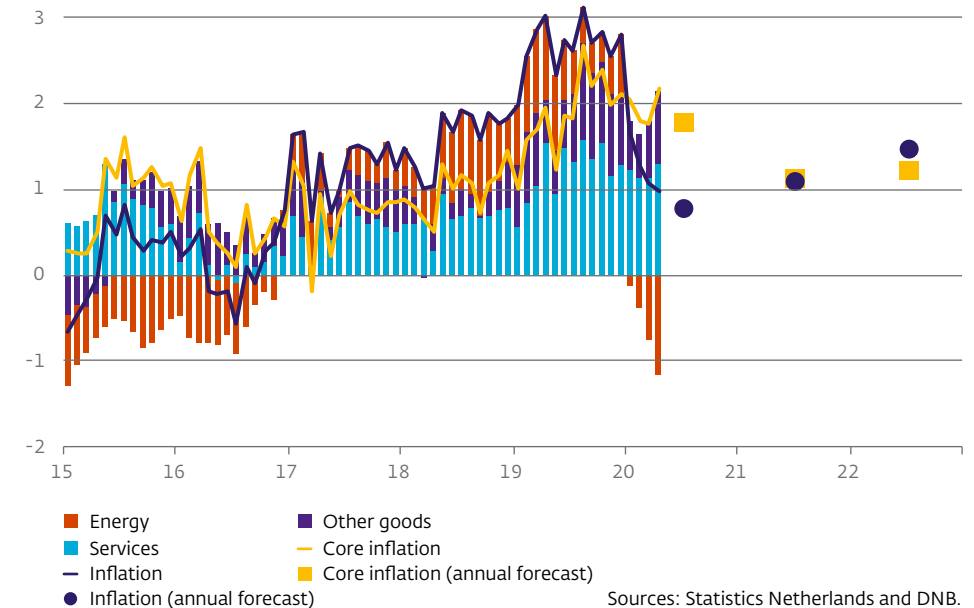
1.4 Lower inflation and falling house prices

Inflation is projected to fall sharply to 0.8% in 2020, whereas in 2019 it was still 2.7% (see Figure 6). The sharp drop in inflation has two clearly identifiable causes. First, the 2019 inflation figure was high because the VAT and energy tax rates were raised in January 2019. Without these tax changes, inflation would have been 1.3% in 2019. The second major cause is the sharp fall in energy prices in 2020. Energy (electricity, gas and other fuels) was almost 13% cheaper in April 2020 than in April 2019. This price fall was largely due to the reduction in energy tax in January 2020 and the recent spectacular drop in oil prices. Adjusted for the energy price changes, inflation stood at 2.2% in 2019 and is projected to be 1.8% in 2020. The energy price development therefore depresses inflation by around 1 percentage point this year.

The projection for HICP inflation is heavily impacted by the pandemic. The inflation projection is complicated in part by measurement problems. A practical consequence of the shutdown of activities across various sectors is that Statistics Netherlands cannot record prices charged by airlines and restaurants, for example, so these have been estimated. What has happened to the prices of their services will only become clear when aircraft take off again and restaurants receive diners. The COVID-19 shock also impacts inflation in two opposite ways. On the one hand firms incur extra costs, mainly to keep customers and staff at a one-and-a-half-metre distance, which can lead to higher prices. Unit labour costs also rise sharply in 2020, with a lagging impact on inflation. On the other hand the projection includes a deep recession, with decreasing tightness in product markets and hence downward price pressure. This second, downward effect predominates up to the end of 2021. This is mainly reflected in core inflation, which falls from 1.8% in 2020 to 1.1% in 2021. In 2022 the downward price pressure eases due to the pick-up in global economic activity,

Figure 6 HICP inflation and core inflation

Year-on-year percentage changes and contributions in percentage points



Note: Core inflation = total excluding food and energy.

putting upward pressure on import and energy prices. HICP inflation rises again slightly to 1.5% in 2022, with core inflation of 1.2%. The inflation projections are very uncertain, however, precisely because we do not know how prices will react in the current pandemic situation.

The effects of the COVID-19 shock on the housing market have so far appeared limited. House prices are nevertheless likely to come under pressure. This is due to movements in three fundamentals, namely the sharp decline in consumer confidence, rising unemployment and lower income growth. Households are therefore expected to be less inclined to move house or take on a new or possibly higher mortgage. On the other hand, the housing market remains very tight and a rapid turnaround of sentiment in the housing market is possible if the pandemic develops favourably once containment measures are eased. Given these uncertainties, the projection for 2020 is based on a 4.3% rise in prices, with a downturn in the second half of the year. The timing and extent of the house price fall are very difficult to gauge, but previous declines have shown that once a house price fall starts it can acquire its own momentum and persist for some time. The projection sees prices falling by an average of 2.1% in 2021 and 3.7% in 2022. That is a small decrease compared to the downturn seen in the wake of the credit crisis, when prices fell by almost 20%.

Box 1 The impact of a virus outbreak and containment measures on public health and the economy

In response to the coronavirus outbreak, containment measures have been introduced around the world to curb the infection level. Although these measures appear to be having the desired effect, they come at a high economic cost. Households and businesses have been forced to cut or postpone their spending, causing a partial shutdown of the economy. In this box we show the effects of a pandemic and the corresponding containment measures on public health and the economy. It is based on a stylised epidemiological model that is integrated into a macroeconomic model.² The probability of infection depends partly on economic interactions: the more people consume or work, the more contact they have with each other and the greater is the infection risk.

We use the model to simulate a virus outbreak and then look at what happens to the number of infections, the mortality rate and the economy, which in this simple model is represented by private consumption. Figure 7 shows that the pandemic leads to a deep and protracted fall in consumption, even without any containment measures in place. This is because consumers are anxious about infection and go out less. It is only when the infection rate has peaked that consumption gradually rebounds. Alternatively the government can opt for *generic containment measures*, requiring all households to stay at home more often. These measures, which remain in force for a year in the simulation, exacerbate the economic recession, but also lower the peak infection level because there are fewer interactions between people. A decrease in the number of infections ultimately means fewer deaths due to the virus. The model thus shows that generic containment measures have a short-term economic cost but are beneficial for public health. The health benefits will translate into economic benefits in the long run, as a lower death toll means

² Eichenbaum, M., Rebelo, S. and Trabandt, M. (2020). The macroeconomics of testing and quarantining. NBER Working Paper No. 27104. National Bureau of Economic Research.

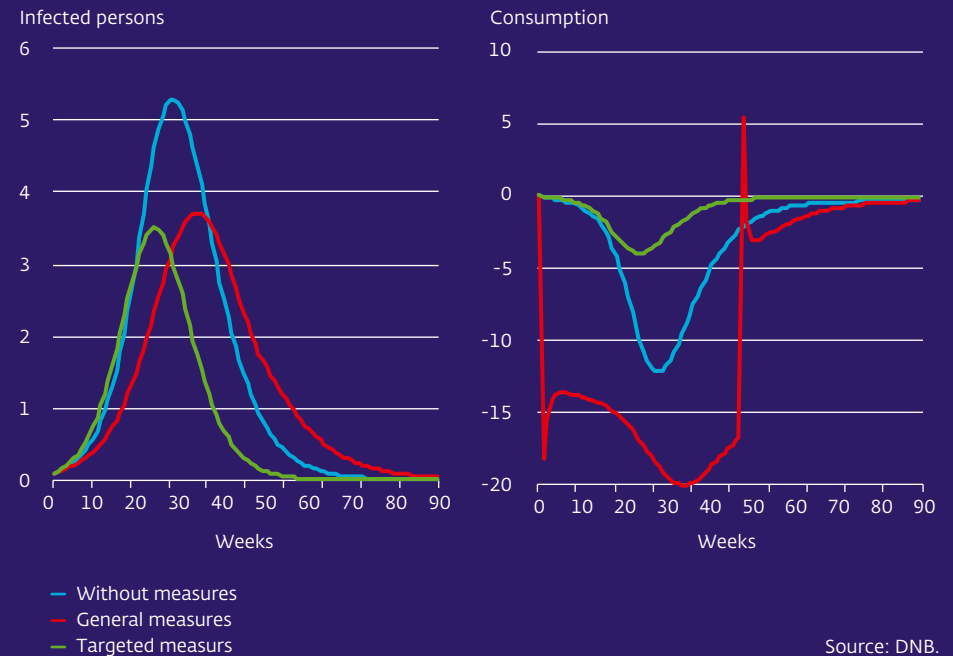
less contraction in the labour supply, so domestic production and consumption will ultimately fall less than if no containment measures had been in place.

To limit the economic cost, the government can also opt to take *targeted containment measures*, with part of the population being tested for COVID-19 infection. People who test positive go into quarantine. Those who test negative or who are not tested fall outside the scope of the measures and can therefore continue their economic and social activities. The figure shows the simulations for these targeted measures. Since people who test positive go into quarantine and do not come into contact with others, the infection risk and the peak infection level fall dramatically compared to the scenario without measures. Although the peak infection level with targeted and generic measures is roughly the same, the economic cost of targeted measures is considerably lower, because a large part of the population can maintain the same level of consumption expenditure.

Overall, the model shows that a virus outbreak leads to a recession even without containment measures, because, as a precaution, people consume and work less away from home. Generic containment measures exacerbate the recession, because the entire population is forced to reduce its economic activity. The advantage, however, is that the number of infections and the death toll fall. The short-term economic cost must therefore be weighed against the immediate health benefits, which translate into economic benefits in the long run. Targeted containment measures, where only people who test positive are placed in quarantine, drastically reduce the economic cost and help with an orderly easing of the measures.

Figure 7 The impact of a pandemic on public health and the economy

Percentage of population and percentage of long-term average prior to outbreak



Source: DNB.



2 A closer look at expenditure and public finances



2.1 International assumptions for the projection

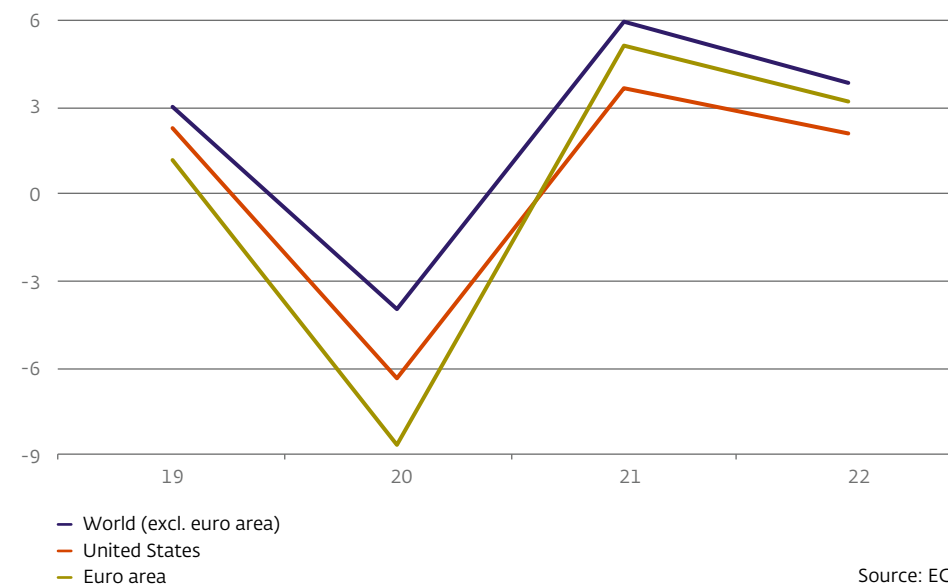
The pandemic deals a heavy blow to the pace of growth of the global economy. The projection assumes that the GDP growth of countries outside the euro area will fall from 3% in 2019 to -4.0% in 2020, an adjustment of over -7 percentage points compared to the forecast six months ago. In 2009, at the time of the financial crisis, global GDP (excluding the euro area) was still growing slightly (0.2%). A marked global recovery is projected for 2021, with growth reaching 6.0% before normalising to 3.9% in 2022, around the multi-year average (2010-2019) in the period preceding the COVID-19 outbreak. Global GDP over the entire 2020-2022 period nevertheless remains below the end-2019 level.

The United States has been the epicentre of the pandemic since the end of March and the economy is consequently being hit hard. The projection assumes that the US economy will contract by 6.4% in 2020 before returning to growth of 3.6% in 2021. The deep downturn in 2020 is due in part to the sharp contraction of private consumption, which substantially impacts the relatively closed US economy. On the other hand, the expanded emergency package (around USD 3,000 billion) enacted by the US government and the Federal Reserve System (Fed) will support the economy, but it will be unable to prevent a steep rise in unemployment in 2020. [Box 2](#) examines a possible US recession that is deeper than the one included in the projection. This poses a downside risk to the global outlook and hence also to the outlook for the Dutch economy.

The assumptions for GDP growth in the euro area and the rest of the world show a similar course ([Key data](#) and Figure 8). The European Central Bank (ECB) projects euro area GDP growth of -8.7% in 2020. In the euro area the pandemic has kept countries such as Italy, Spain and France in its grip for a long time. The measures aimed at curbing the spread of the virus have put a firm brake on economic growth

Figure 8 Forecasts of GDP-growth

Percentage changes



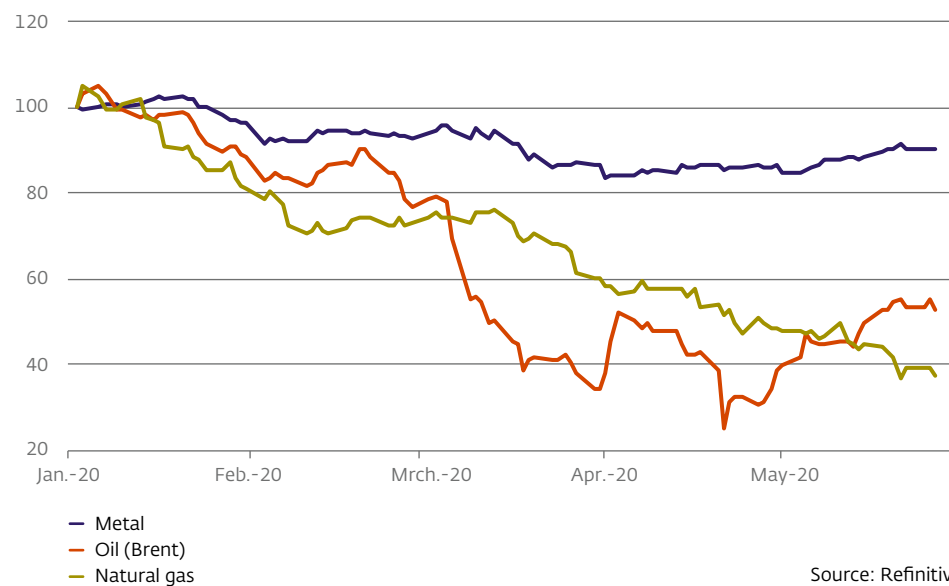
but also brought down the rate of infections. At the beginning of April the number of new infections per million people in the euro area was around 50 per day, whereas at the beginning of June it was around 20 per day. For 2021 the ECB expects euro area GDP to grow by 5.2%, followed by 3.3% in 2022.

In response to the deteriorating economic outlook the ECB launched the Pandemic Emergency Purchase Programme (PEPP) at the end of March. The ECB is purchasing EUR 750 billion of assets to reduce the risk of serious disruption to the monetary transmission mechanism. In mid-May it also started lending to banks in order

to support liquidity in the euro area financial system. Partly as a result of these measures the outlook for European short and long-term interest rates is more or less unchanged in this projection compared to the forecasts six months ago. In addition to the monetary measures, the Eurogroup agreed a support package of EUR 540 billion at the beginning of April and the European Banking Authority (EBA) called on the national authorities and the SSM (Single Supervisory Mechanism) to show flexibility and pragmatism in the supervision of banks. Finally, the European Commission has recently proposed a fund of EUR 750 billion, comprising EUR 500 billion of grants and EUR 250 billion of loans.

Figure 9 Commodity prices

Index, 2 January 2020 = 100; US-dollars



Source: Refinitiv.

The sudden deterioration of the global outlook has weighed heavily on commodity prices (see Figure 9). From mid-January to the end of March, prices of base metals fell by around 15%, natural gas by 38% and crude oil by 65% (a decrease of around USD 40 per barrel). The containment measures have considerably reduced demand for energy, partly as a result of travel restrictions and a weakening of industrial activity. Oil prices also fell because the OPEC+ countries (organisation of oil-exporting countries including Russia and other non-OPEC oil exporters) failed to reach agreement at the beginning of March. OPEC+ has now reached an agreement to curb its oil production. The projection assumes that the oil price will average USD 36.0 per barrel in 2020 before rising to USD 40.7 per barrel in 2022.

2.2 Gloomy outlook for Dutch exports

The international assumptions underlying the projection imply that world trade relevant to the Netherlands contracts by almost 13% in 2020, a deeper contraction than at the time of the financial crisis. A marked recovery is expected in 2021 with growth of 7.5%. It is assumed that international production lines, partly disrupted by the pandemic, will recover and give fresh impetus to world trade in 2020 and 2021. In 2022 the growth of relevant world trade will normalise towards the multi-year average (2012-2019) of around 3% (see Table 1). At the end of 2022 relevant world trade is around 1% below the end-2019 level.

It is not surprising that Dutch exports are hit hard given the steep fall in international trade. Although the first-quarter contraction of relevant world trade was less severe than might have been expected, many sectors were hit hard. For example, the export value of floriculture, including flowers, plants and bulbs, was 22% lower in March 2020 than a year earlier. The Netherlands is the second-largest exporter of agricultural products in the world after the United States. With a share of around 10%, floriculture is the largest component of agricultural exports. Exports to Italy,

Table 1 Dutch exports and competitiveness

Percentage changes

	2019	2020	2021	2022
Volume				
Relevant world trade (1)	1.6	-12.9	7.5	4.6
Exports of goods and services (2)	2.3	-10.9	7.5	4.1
domestically produced	-0.4	-10.2	6.7	2.8
re-exports	6.3	-11.9	8.7	6.0
Trade performance (2-1)	0.6	2.3	0.0	-0.4
Exports of goods and services excl. energy	2.3	-11.4	7.9	4.8
domestically produced (3)	-0.1	-11.1	7.3	3.9
re-exports	6.0	-11.9	8.7	6.0
Market performance (3-1)	-1.8	2.1	-0.2	-0.6
Price				
Competitor prices (4)	1.6	-2.0	0.3	1.8
Exports of goods and services	0.3	-2.7	-0.1	1.6
domestically produced, excl. energy (5)	1.2	-0.3	0.4	1.3
Price competitiveness (4-5)	0.4	-1.6	-0.1	0.5

Sources: DNB and ECB.

the fifth-largest export destination for floriculture, were hit particularly hard, falling by 63% in March compared to a year earlier.

The projected value of exports (goods and services) falls by a total of 10.9% in 2020, with the domestically produced component (excluding energy) falling by 11.1%. Re-exports are also suffering badly due to the global nature of the COVID-19 shock.

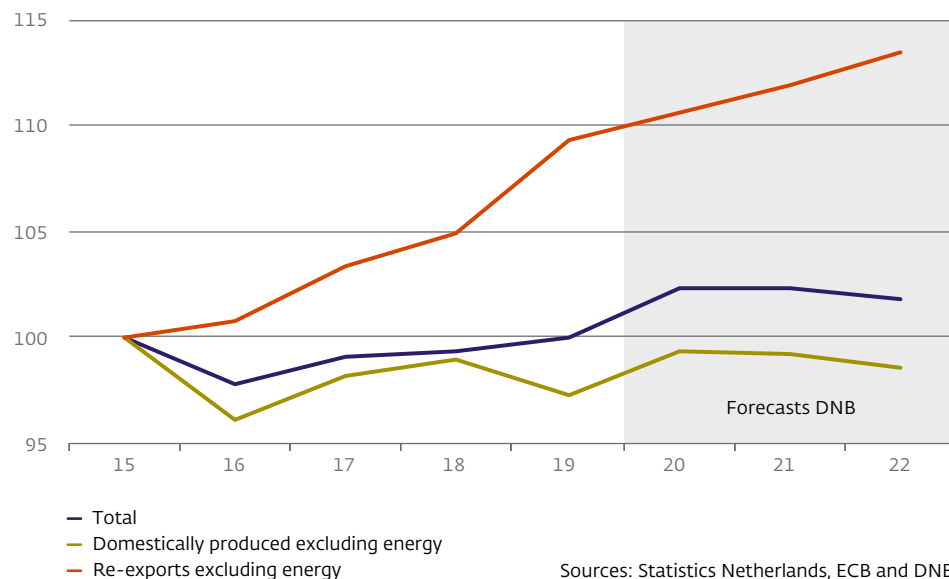
In March 2020, goods imports from China and Hong Kong, around two-thirds of which were intended for re-export, were 9% lower than a year earlier. The total decrease in re-exports in 2020 amounts to 11.9%, an exceptionally sharp fall after the 6.0% growth in 2019.

In line with the expected development of relevant world trade, Dutch exports stage a partial recovery in 2021 after the downturn in 2020. In 2021 growth normalises towards the rate typically seen in the years prior to the virus outbreak. The growth of domestically produced exports (excluding energy) will more or less keep pace with growth in relevant global trade in the years ahead. At the end of the projection horizon the market share of 'Made in Holland' exports is broadly back to the same level as in 2018 (see Figure 10).

After decreasing in 2019, the current account balance falls further in the subsequent years. In 2020 it is expected to have fallen back to 7.8% of GDP, from 10.2% in 2019. The current account balance also fell during the credit crisis. The main cause of the current decline is a decrease in the trade balance as projected exports fall faster than imports. Net primary income and current transfers also contribute negatively to the current account balance. The primary surplus has decreased every quarter since the beginning of 2019, because foreign investors in Dutch non-financial corporations saw their income, such as dividends, increase more than in the converse situation. Over the projection horizon the primary surplus turns into a deficit and the current account surplus decreases to 7.0% GDP in 2022.

Figure 10 Market share exports of goods and services

2015 = 100; volume



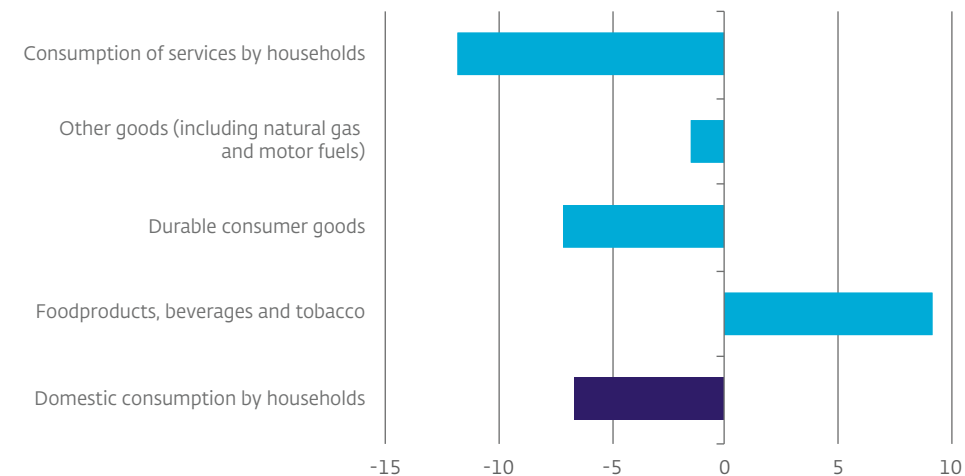
Note: Index is the category in question divided by relevant world trade.

2.3 Consumers keep a tight hold of their purse strings in 2020

Due to the containment measures, private consumption in the first quarter contracted by 2.7% compared to the previous quarter, the biggest fall since 1987. Monthly figures for March show that consumers spent 6.7% less than in March 2019. Consumer spending was down particularly on services (hospitality, recreation and culture) and durable goods (cars and clothing), whereas spending on food was higher (see Figure 11). Retail shows the same picture. Turnover of clothing stores

Figure 11 Domestic consumption by households in March 2020

Year-on-year percentage changes; volume, adjusted for shopping days



Source: Statistics Netherlands.

in March, for example, was down 40.7% on a year earlier, while online turnover in March was almost 30% higher than a year earlier. Online shopping, combined with the increased turnover at supermarkets and drugstores, therefore partly offset the losses at other retailers.

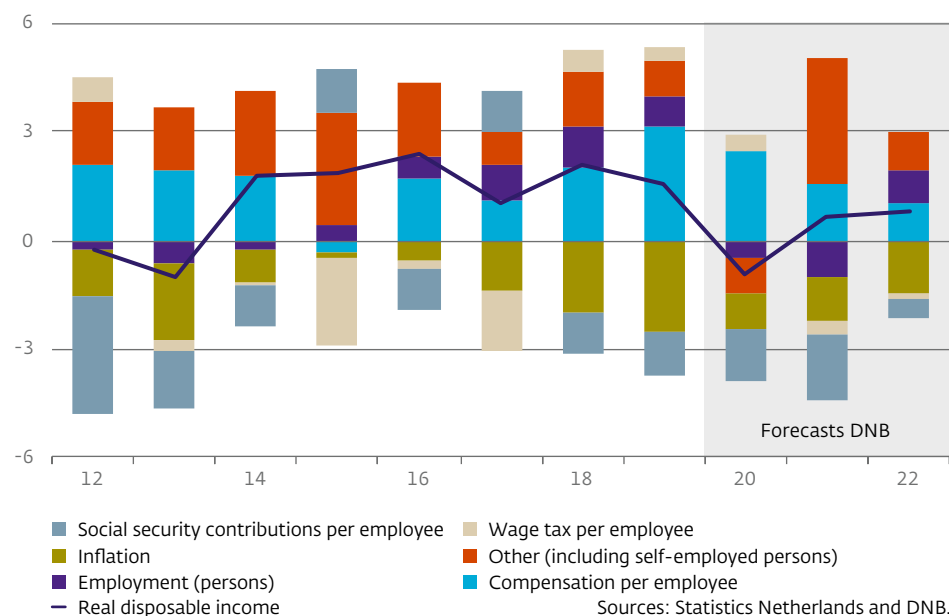
Due to the steep decline in the first and second quarters, private consumption is expected to contract by 7.6% this year, partly forced and partly for precautionary reasons. Since household income falls less sharply than consumption, households' free savings rise substantially this year. The individual savings rate, or free savings as a percentage of households' disposable income, rises from 2.8% in 2019 to 8.9% in 2020. In 2009, consumers also cut back on their spending, but the rise in the individual savings rate then was just 2.7 percentage points. Households will use the

extra savings to support spending in the coming years. Partly for this reason, 2021 and 2022 see consumption recovering by 4.1% and 2.9% respectively. But that will not be sufficient to bring consumption back to pre-virus levels at the end of the projection horizon. This is due to lower household demand on the back of lower consumer confidence, rising unemployment and falling house prices. Moreover, household disposable income decreases due to the consequences of the pandemic.

Real household disposable income is expected to shrink by 1.0% this year. This is mainly due to the decrease in other income, including self-employed income (see Figure 12). Real disposable income also decreases due to the contraction of

Figure 12 Real disposable household income

Year-on-year percentage changes and contributions in percentage points



employment. Income rises again slightly by 0.6% in 2021, mainly because other income bounces back strongly. In line with the labour market recovery in 2022, compensation of employees also recovers, so households see their real disposable income rise by 0.8% in that year.

2.4 Flexible labour: job losses and shifting employment

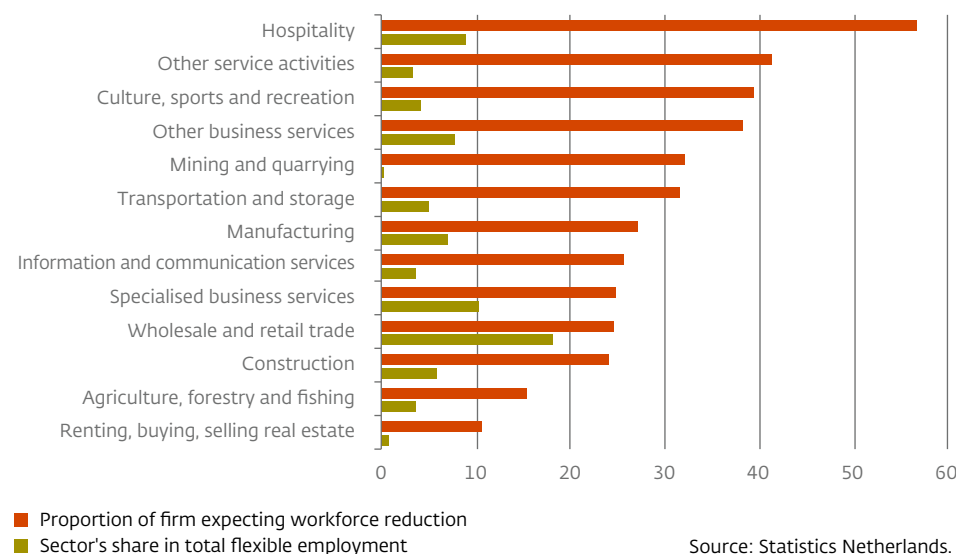
The projection has employment falling by 1.4% in 2020 and 2.7% in 2021. In 2019, one-third of the working population, around 3 million people, were in flexible employment or self-employment. This is the group most likely to suffer the primary impact of the recession. Employees with short-term temporary, agency and on-call contracts often have the least job security, with flexible employees having less redundancy protection than permanent staff. The large number of self-employed people who have applied for income support (the TOZO scheme) since the containment measures were introduced indicates that they have seen rapid falls in turnover.

Experiences of the 2008-2009 financial crisis nevertheless suggest that flex workers will not necessarily be the primary victims. At that time, employment fell first among flexible employees, and after a year the number of agency staff had fallen by 20%, but in the longer term it was permanent employees who saw the biggest job losses in terms of numbers. Eventually, the financial crisis boosted flexible employment. In subsequent years employment grew primarily due to flexible jobs, with growth particularly in the number of on-call and self-employed workers. Shifts were also seen in the first weeks of the current downturn. Around 45,000 agency staff (of a total of around a quarter of a million) lost their jobs up to the beginning of May, although just under half of them immediately found work elsewhere.

According to the latest Statistics Netherlands business survey (COEN), 29% of Dutch businesses expect their workforce to shrink in the next three months. The proportion is above average among businesses in hospitality (57%), other services (41%), culture and recreation (39%), other business services (38%) and transport (31%)

Figure 13 Development and components of employment

Percentages



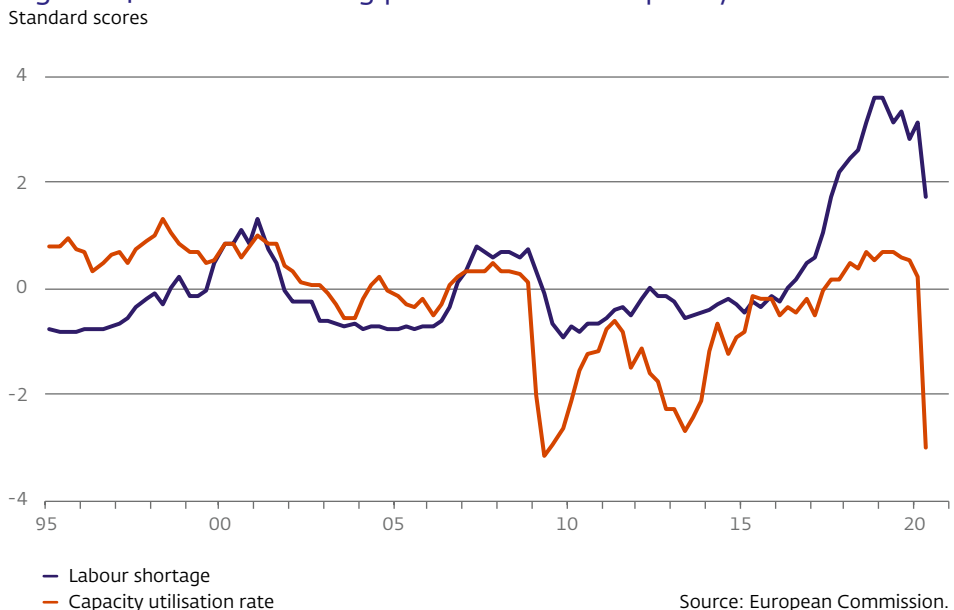
Note: The proportion of firms expecting a workforce reduction in the next three months in 2020Q2 (COEN survey). The relevant sector's share in the total number of workers in flexible jobs (employed and self-employed persons, EBB). Based on sectoral classification from 2018 and employment position classification for 2019.

(see Figure 13). These are the sectors that employ particularly large numbers of flex workers. Almost 30% of people in flexible employment or self-employment work in these five sectors, which account for 20% of total employment. It is estimated that at the beginning of this year these sectors employed almost 492,000 people in less secure, flexible jobs (short-term temporary, agency or on-call). A further 263,000 self-employed persons were working in these sectors. The other 1.7 million vulnerable flex and self-employed workers were in other sectors.

2.5 Decreasing investments with temporary upturn in lending

The strict government measures to curb the spread of the virus, both in the Netherlands and abroad, have abruptly changed the conditions under which businesses operate. Figure 14 illustrates this. The number of industrial and other firms having or claiming to have a high rate of capacity utilisation has fallen in a short period from the highest level this century to the low point seen in the economic downturn in 2013. Additional surveys show that businesses do not expect a major contraction of their workforce in the short term, but do expect a major negative impact on their investment plans. Firms are currently having to contend with a great deal of extra uncertainty about the course of the measures and the pandemic, and the consequences for their future sales. In the projection the rise in investments in 2019 (6.8%) turns into a substantial contraction of 13.9% in 2020. In the following two years, this contraction is largely reversed with growth of 7.3% and 6.2%.

Figure 14 Factors limiting production and capacity utilisation rate



A sudden turnaround can also be seen on the financing side in the first quarter of 2020. Banks report a sharp drop in demand for loans for investment and an equally sharp rise in demand for working capital at the beginning of April 2020. The containment measures are causing liquidity problems for many firms (see [Box 3](#) Liquidity in Dutch business). Where possible, firms used their existing credit lines in the first months of the lockdown, partly as a precaution and partly to meet their ongoing obligations. Bank lending to non-financial corporations rose sharply in March and April 2020 (1.8% and 0.7% month-on-month respectively). The projection shows lending growing by 1.4% in 2020, the first positive growth figure since 2012.

The fact that credit growth is sustained in these severe economic circumstances is due not only to strong demand for credit. On the supply side banks have built up more solid buffers since the credit crisis, so a shortage of capital no longer necessarily constrains lending growth. Another factor is that bank supervisory authorities have temporarily eased the capital requirements and allowed flexible interpretation and fulfilment of prudential rules. For example, payment holidays can be granted more readily without an increase in buffer requirements. The government also has expanded the existing guarantee schemes and introduced new ones, making it less risky for banks to grant loans to solvent companies. Banks are nevertheless growing increasingly cautious and a majority indicate a tightening of credit standards in the second quarter, for the first time since mid-2017. This will eventually act as a drag on credit growth. The projection assumes that the supply conditions will become tighter, but that the banking sector is sufficiently capitalised to continue meeting demand for credit. Demand for credit will nevertheless decrease if the initial liquidity requirement is met, while demand for bank lending for corporate investment shrinks. The projection for the years ahead shows bank lending contracting by 5.0% (2021) and 2.9% (2022).

2.6 Downturn in public finances

Dutch public finances were in a strong starting position at the outbreak of the pandemic. The debt-to-GDP ratio fell further to 48.6% in 2019, while the budget balance that year was a surplus of 1.7% of GDP. As a result of the pandemic and the support packages to mitigate the economic damage, the budget balance this year turns into a deficit of 6.4% of GDP (see Table 2). The government will also remain in deficit in 2021 and 2022. Following a sharp increase of over 9 percentage points in 2020, the debt-to-GDP ratio will gradually rise in subsequent years, reaching more than 63.1% in 2022 on average. The structural balance also shows a deficit in 2020 and the remainder of the projection horizon, although this indicator must be interpreted with particular caution due to the specific circumstances.

Table 2 Public sector key data

Percentage of GDP

	2019	2020	2021	2022
Public expenditures	41.9	49.8	47.1	46.4
Taxes and social security contributions	39.2	38.8	38.0	38.1
Other income	4.4	4.6	4.3	4.0
Primary balance	2.5	-5.7	-4.1	-3.6
EMU balance	1.7	-6.4	-4.8	-4.3
Structural balance (EC method)	0.4	-2.9	-2.4	-2.9
EMU debt	48.6	57.9	60.9	63.1

Source: DNB.

In 2020 the public expenditure on the support packages increases substantially, and the measures up to and including the second support package of 20 May have been included in the projection. The substantial measures in the support packages include, for example, wage cost subsidies as part of the NOW scheme and self-employment income support (TOZO). In 2021 public expenditure as a percentage of GDP decreases, on the assumption that there are no support measures in 2021.

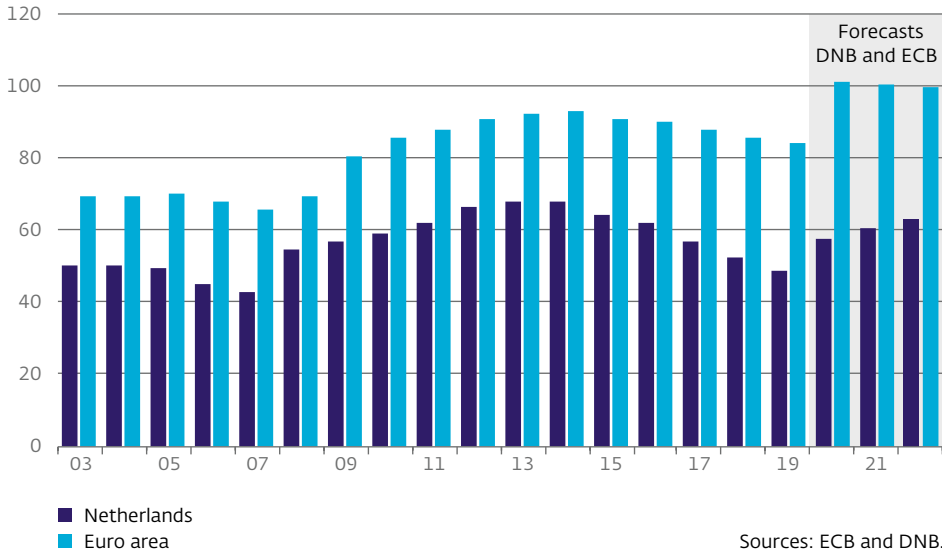
Although total public spending falls on a net basis in 2021, that does not apply to all components. Expenditure on unemployment benefit, for example, increases due to the growing number of unemployed people. Care expenditure and old-age pension benefits also rise, although this would have happened even without the COVID-19 outbreak. As a result, public expenditure as a percentage of GDP in 2022 is considerably higher than in 2019.

The collective tax burden decreases in 2020 and 2021 due to the decline in economic activity and the reductions in household and business taxes announced before the virus outbreak. In 2022 the collective tax share remains almost unchanged, so it is lower in 2022 than in 2019.

In order to limit the economic effects of the virus outbreak, it is important that the automatic stabilisers and the support measures can work freely. This causes the debt-to-GDP ratio to rise by almost 15 percentage points in a three-year period. The Dutch government's debt-to-GDP ratio would nevertheless remain below the level seen after the financial crisis. The sustainability of government debt would not be at immediate risk. Figure 15 shows that the average debt-to-GDP ratio in the euro area also rises sharply in 2020, so Dutch government debt should remain a relatively attractive investment. The rise in the debt-to-GDP ratio shows that it is important to allow the debt-to-GDP ratio to fall in good times, so that there is a buffer to absorb unexpected setbacks.

Figure 15 Public sector debt, Netherlands and euro area

Percentage of GDP



Sources: ECB and DNB.

Box 2 Sensitivity of the Netherlands to a deeper recession in the US

The COVID-19 pandemic has severely hit the population in large parts of the US, causing major damage to the economy as a result. The labour market situation in particular has deteriorated rapidly (see Figure 16). In just two months since mid-March, 36.5 million benefit claims have been filed, causing the unemployment rate to surge to over 15% of the labour force. As jobless people in the US often lose their health insurance, households are hit especially hard, further increasing the economic uncertainty and vulnerability. Confidence in the economy has plummeted. The Composite PMI, for example, a confidence index based on surveys of purchasing managers, reached the lowest point ever recorded in April (27.0 versus 53.3 in January), pointing to an unprecedented sharp fall in GDP. This negative economic picture is borne out by the historically large contraction of industrial production in April (down -11.2% QoQ). It is not inconceivable, therefore, that real GDP growth in the US will turn out lower than projected, particularly if the government underestimates the seriousness of the situation. Given the importance of the US to global trade and the global outlook, the question is how sensitive the Dutch economy would be to a deeper recession in the US.

Both Dutch imports and exports are sensitive to developments in the US economy. In 2019 almost 6% of Dutch exports were destined for the US and 10% of our imports came from the US.³ Moreover, due to a sharper downturn in the US economy, the Netherlands may suffer much greater damage due to indirect negative trading effects on other countries. The projection assumes real GDP growth in the US of -6.4% in 2020. By way of a sensitivity analysis it is assumed

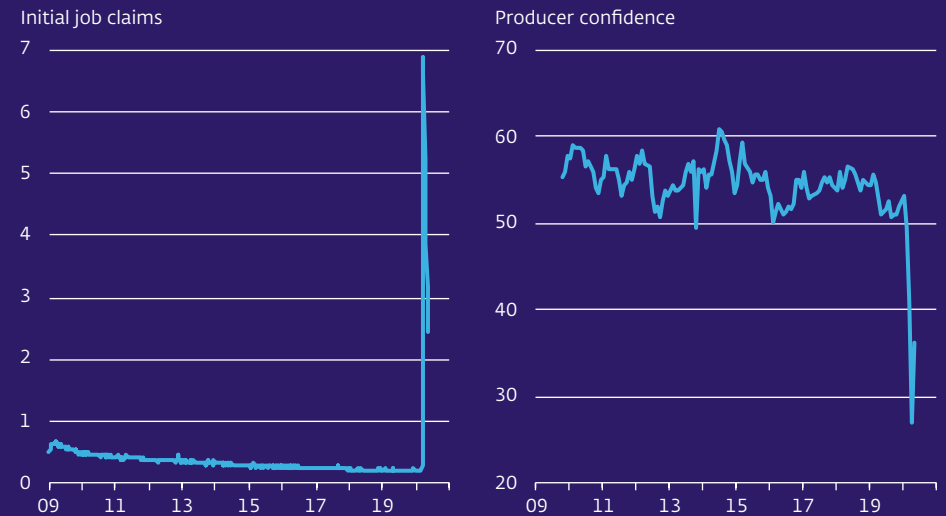
³ In terms of added value, and taking account of the role of global value chains, the dependence on the US is even greater. Around 11% of the added value generated by exports from the Netherlands goes to the US (including intermediate deliveries through other countries). In the case of added value imported by the Netherlands, over 14% comes from the US (source: Trade in Value Added database OECD, 2015).

here that US consumption expenditure in 2020Q2 and 2020Q3 is 10% lower than projected, with US financial risk premiums rising further (by +50 bps) and consumer and producer confidence both falling further (by -10%).⁴ Overall this means a deeper recession for the US, with real GDP growth below -11% in 2020 (see Table 3).

The sharply lower US GDP growth negatively impacts other countries' import and export volumes and hence world trade. Growth in the euro area falls by 0.5 percentage points in 2020 to -9.2%. The volume of world trade relevant to the Netherlands is heavily impacted and in 2020 grows by over 2 percentage points less than projected. This leads to lower growth in exports of Dutch goods and services (see Table 4). As a result of the reduced demand, lower consumption expenditure and lower corporate investment, economic growth in the Netherlands falls by an average of almost 0.5 percentage points per year. The analysis shows that in the event of a more severe recession in the US Dutch GDP will be hit almost twice as hard as euro area GDP in 2020 and 2021. Unemployment reacts with a time lag and in 2021 is 0.5 percentage points higher than in the projection.

Figure 16 Rapid deterioration of US economy

Millions of claims and diffusion-index



Sources: St. Louis FED and IHS markit.

Note: Composite PMI index and initial job claims (weekly).

⁴ If these uncertainty and confidence effects spread to other countries, the economic effects outlined for the Netherlands may prove even more negative.

Table 3 Assumptions for deeper recession in United States

Percentage deviations from baseline scenario, unless stated otherwise

	2020	2021
For United States:		
Gross domestic product (%-changes)	-11.1	3.6
(Deviation from projection)	(-4.7)	(0.0)
For euro area:		
Gross domestic product (%-changes)	-9.2	5.1
(Deviation from projection)	(-0.5)	(-0.1)
For the Netherlands:		
Relevant world trade	-2.1	-1.5
Euro exchange rate (USD)	1.5	2.0
Competitor prices	0.1	-0.1
Oil prices	0.4	-1.4
Equity prices	-2.5	-4.5

Source: DNB.

Notes: Assumptions were simulated using NiGEM (version 2.20), incorporating an initial estimate of the global impact of the COVID-19 pandemic in the baseline projection. It is assumed that economic agents adapt their expectations ("backward-looking"). GDP, expenditure components and world trade are in real terms.

Table 4 Results for the Netherlands

Percentage changes, unless stated otherwise

	2020	Deviation from projection	2021	Deviation from projection
Gross domestic product	-7.0	(-0.6)	2.6	(-0.3)
Private consumption	-7.7	(-0.1)	3.5	(-0.6)
Business investment	-14.2	(-0.3)	5.4	(-1.9)
Exports of goods and services	-12.9	(-2.0)	7.7	(0.2)
Imports of goods and services	-12.3	(-1.6)	8.8	(-0.1)
Harmonised consumer price index	0.8	(0.0)	1.1	(0.0)
House prices, existing own homes	4.3	(0.0)	-2.5	(-0.4)
Unemployment (% of labour force)	4.6	(0.0)	7.8	(0.5)
EMU balance (% of GDP)	-6.5	(-0.1)	-5.1	(-0.3)

Source: DNB.

Box 3 Liquidity in Dutch business

Many Dutch businesses are experiencing a big drop in turnover as a result of the pandemic. The longer this situation persists, the more doubtful are businesses' survival chances. Although they can cut costs, many businesses experience a squeeze on liquidity. This is reflected in a deterioration of operating cash flow (EBITDA), defined as earnings before interest, tax, depreciation, amortisation and impairment. Many businesses therefore also see falls in their interest coverage ratio (ICR), which measures the ratio of operating cash flow to debt interest. The question is what proportion of businesses have insufficient liquidity to meet debt interest payments (ICR<1), putting the sustainability of their debt under pressure.

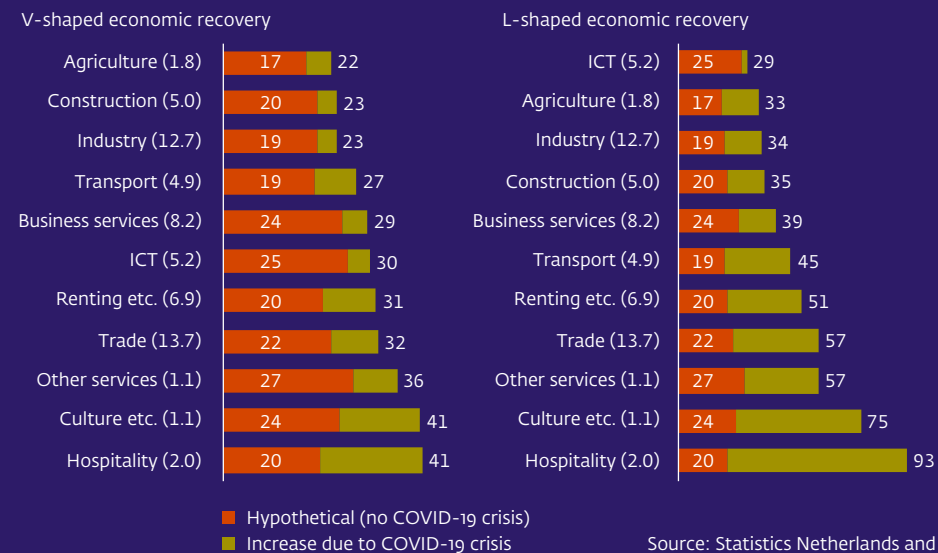
We estimate this in this box, using the individual company balance sheets and income statements of all private and public limited companies in the Netherlands. Since the decrease in turnover of individual businesses is unknown, we perform calculations under two different assumptions: 1) a V-shaped business cycle recovery, with the economy recovering rapidly and after the second quarter moving quickly back to the pre-crisis level, and 2) an L-shaped trajectory, with the economy contracting sharply for the rest of 2020 and no recovery taking place.

Typically around one business in five will be unable to meet interest payments from operating cash flow. The NOW scheme enables businesses severely affected by the lockdown to keep their cash flow reasonably intact, but it cannot prevent a rise in the number of businesses with insufficient cash flow. In the case of an L-shaped business cycle recovery, the proportion of businesses getting into difficulty will be substantially higher.

Figure 17 reports the estimated percentage of businesses with liquidity difficulties due to the COVID-19 shock in a number of sectors (ICR<1). The biggest problems are expected in hospitality, culture, sport and recreation, other services and trade.

Figure 17 Firms facing liquidity stress (ICR<1)

Percentage of total number of firms, per sector



Note: Sector share in 2018 GDP is given in brackets, sectors classified at SBI section level

In the hospitality and culture, sport & recreation sectors, around four out of 10 businesses are unable to meet interest expenses from operating cash flow in a V-shaped trajectory. Together these sectors accounted for 3.1% of GDP in 2018 (figures between brackets). In the case of an L-shaped trajectory, most of the businesses in these sectors encounter liquidity difficulties. The question remains to what extent businesses in the severely affected sectors are sufficiently able to absorb these losses by drawing on their reserves.

3 Alternative scenarios for the Dutch economy

A great deal of uncertainty surrounds the macroeconomic effects of the COVID-19 pandemic. Much will depend on the further spread of the virus, the necessity, intensity and effectiveness of the containment measures, the time required to develop an effective medical treatment or vaccine and in particular how households, businesses and governments react. To give an idea of the possible economic effects of the pandemic, this chapter describes two alternatives to the projection presented in the previous chapters. These mild and severe scenarios differ from the projection mainly in terms of the development of the pandemic and the government responses to it, the strength of the economic rebound and the extent of the permanent economic damage.⁵ These scenarios are not intended to show the extreme margins around the projection. Given the enormous uncertainty, no probability is attributed to any of the scenarios, although the risks to the baseline projection are clearly to the downside. Each scenario is an internally consistent projection based on alternative, previously defined assumptions. The actual position may still turn out different, however, in both a positive and negative sense.

Mild scenario

It is not inconceivable that the economy will recover faster than expected in the baseline projection. In this mild scenario it has been assumed that the virus outbreak is brought under control earlier, so uncertainty among households and businesses decreases and the economy restarts faster. The underlying assumption is that the

containment measures (such as business shutdowns, *social distancing*, homeworking, schools closures etc.) will be effective and that medical progress is made in terms of testing capacity and treatment methods. It has been assumed that the lockdown period continues until early May and is followed by a transition period up to the end of June in which the containment measures are eased and the affected business sectors gradually reopen. Assuming that there are no further virus flare-ups, a rapid economic recovery begins in the third quarter of 2020.

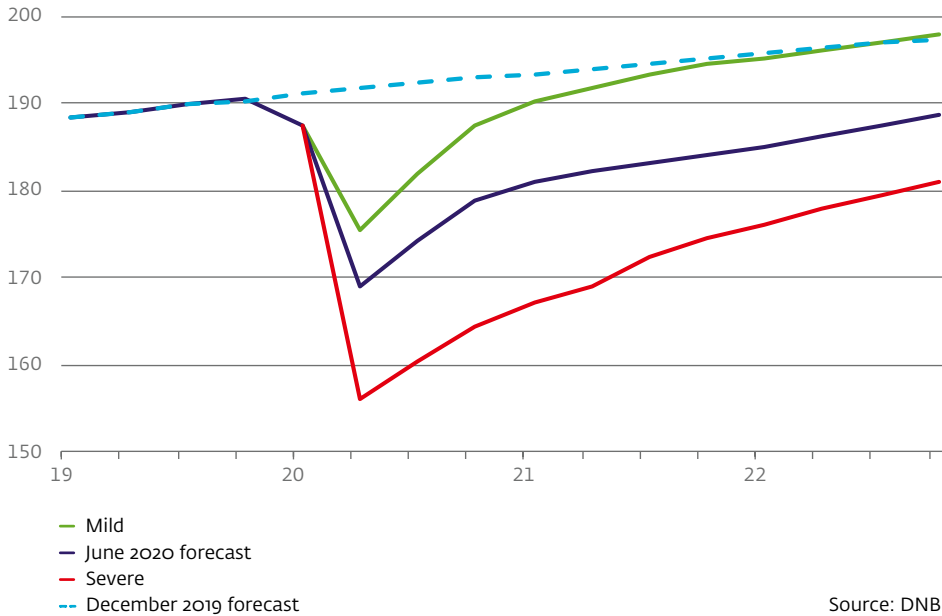
As more businesses ramp up their activity in the second half of 2020, the economy rebounds strongly from the very low production level in the second quarter of 2020. Economic growth consequently picks up sharply in the third and fourth quarters of 2020, after which the quarterly growth figures gradually return to their normal pace. Although the mild scenario sees a fast and strong rebound in the economy, the GDP level does not return to the level in DNB's last December forecast until the end of the projection horizon (see Figure 18).

Table 5 shows the underlying assumptions of the two alternative scenarios. As global trade turns out more favourable in the mild scenario, the Dutch economy is not as severely affected as in the projection (see Table 6). Consumption expenditure and corporate investment also fall less in 2020, so the recession is limited to -3.4% in 2020, while GDP growth at 5.1% in 2021 is considerably higher than in the projection. Unemployment peaks at just below 6% of the labour force in 2021, before falling to

⁵ Furthermore, due to the exceptional economic circumstances, the GDP growth figures are prone to greater measurement uncertainty than is normally the case, so they may ultimately turn out higher or lower.

Figure 18 Output loss caused by COVID-19 pandemic

GDP volume; EUR billions, base year 2015



Source: DNB.

4% in 2022. In line with the severe economic downturn in 2020, the housing market cools, but the persistent housing shortage precludes any fall in prices. At the same time, the budget deficit turns out lower than in the projection. The negative impact of the recession on potential growth and labour productivity remains minimal in the mild scenario.

Table 5 Assumptions for COVID-19 scenarios

Percentage changes, unless stated otherwise

	Mild			Severe		
	2020	2021	2022	2020	2021	2022
Volume of relevant world trade	-8.3	10.2	4.6	-19.4	5.7	4.4
Short-term interest rate in the euro area (%)	-0.4	-0.4	-0.4	-0.4	-0.4	-0.4
Long-term interest rate in the Netherlands (%)	-0.5	-0.6	-0.5	0.0	0.1	0.2
Euro exchange rate (USD)	1.09	1.08	1.08	1.09	1.08	1.08
Competitor prices	-1.3	0.5	2.1	-3.5	-0.5	1.6
Oil price (UK Brent in USD per barrel)	36.2	37.2	40.7	36.2	37.2	40.7

Source DNB.

Severe scenario

The severe scenario assumes a longer lockdown period with strict containment measures continuing until the end of June 2020. This is followed by a long transition period until mid-2021. In contrast to the baseline projection, efforts to halt the spread of the virus during the lockdown are unsuccessful. In this scenario there is a risk of a serious resurgence of infection (a 'second wave'). Stringent measures therefore remain necessary in the transition period until an effective medical treatment or vaccine becomes available in mid-2021. The uncertainty and negative confidence effects therefore continue for longer than in the projection and economic activity is inhibited for an extended period. The economy barely rebounds in the second half of 2020 and goes into a severe recession.

Table 6 Outcome of COVID-19 scenarios

Percentage changes, unless stated otherwise

	Mild						Severe					
	2020	Deviation from projection	2021	Deviation from projection	2022	Deviation from projection	2020	Deviation from projection	2021	Deviation from projection	2022	Deviation from projection
Gross domestic product	-3.4	(3.0)	5.1	(2.2)	2.2	(-0.2)	-11.8	(-5.4)	2.2	(-0.7)	4.6	(2.2)
Private consumption	-4.6	(3.0)	5.5	(1.4)	3.7	(0.8)	-15.5	(-7.9)	6.6	(2.5)	10.1	(7.2)
Business investment	-10.5	(3.4)	10.6	(3.3)	6.0	(-0.4)	-26.2	(-12.3)	2.7	(-4.6)	16.0	(9.6)
Exports of goods and services	-6.3	(4.6)	10.2	(2.7)	4.2	(0.1)	-16.4	(-5.5)	5.6	(-1.9)	3.7	(-0.4)
Imports of goods and services	-6.6	(4.1)	10.4	(1.5)	6.0	(1.1)	-17.5	(-6.8)	7.1	(-1.8)	7.0	(2.1)
Consumer confidence (level)	-23.4	(2.9)	-20.0	(11.9)	-0.9	(8.8)	-31.6	(-5.3)	-48.9	(-17.0)	-15.6	(-5.9)
Negotiated wages, private sector	2.3	(0.0)	1.1	(0.1)	2.0	(1.3)	2.3	(0.0)	0.5	(-0.5)	0.0	(-0.7)
Harmonised consumer price index	0.8	(0.0)	1.2	(0.1)	2.0	(0.5)	0.6	(-0.2)	0.8	(-0.3)	0.8	(-0.7)
House prices, existing own homes	4.9	(0.6)	0.8	(2.9)	1.3	(5.0)	4.0	(-0.3)	-4.1	(-2.0)	-7.3	(-3.6)
Unemployment (% of labour force)	4.1	(-0.5)	5.7	(-1.6)	4.0	(-1.7)	5.0	(0.4)	9.2	(1.9)	8.0	(2.3)
EMU balance (% of GDP)	-3.4	(3.0)	-1.7	(3.1)	-0.9	(3.4)	-10.2	(-3.8)	-8.2	(-3.4)	-7.2	(-2.9)
EMU debt (% of GDP)	53.2	(-4.7)	52.1	(-8.8)	51.2	(-11.9)	65.1	(7.2)	72.0	(11.1)	75.4	(12.3)

Source: DNB.



The loss of production in the severe scenario is much greater than in the projection, with the final GDP level at the end of 2022 still far below DNB's last December forecast. The impact on potential growth is stronger and more protracted in the severe scenario due to the bigger fall in investments, the substantially lower capital goods stock and rising natural unemployment. Extended disruption of international value chains and increasing protectionism also lead to considerable and persistent negative productivity effects in this scenario.

The picture outside the Netherlands is much more negative in the severe scenario than in the projection. Global trade growth is more than 6 percentage points lower in 2020. This leads to a much lower volume of Dutch goods and services exports (see Table 6). Reduced foreign demand and falling corporate investments and consumption expenditure push economic growth to an all-time low of -11.8% in 2020. Unemployment responds as usual with a time lag and is approximately 2 percentage points higher on average than in the projection in 2021 and 2022.

Economic recovery does not begin until mid-2021. Although the impact on inflation initially remains limited, a further slump in demand, lower wage growth and increasing price competition result in a more moderate inflation picture, particularly in 2022. Inflation in that year remains at 0.8%. The severe recession deepens the downturn in the housing market, causing house prices to fall further than in the projection. Consistent with the much lower growth, longer-term support measures and higher unemployment, public finances deteriorate rapidly, leading to budget balances on average 3 percentage points of GDP lower than in the projection. This results in a budget deficit of more than 10% of GDP in 2020. Public debt in 2022 amounts to around 75% of GDP, more than 10 percentage points higher than in the projection. The severe scenario assumes that although banks are affected by the sharp recession, they can continue to fulfil their role as financial intermediaries, including during an economic recovery once a vaccine or medical treatment becomes available. [Box 4](#) considers the possibility of deeper problems in the financial sector as a result of the COVID-19 pandemic.



Box 4 Greater tensions in the financial sector

The COVID-19 shock also affects the financial sector, particularly if the recession is protracted. Although there is no assumption of a system crisis, real economic effects impact the financial system in both the projection and the two scenarios, because business failures rise, jobs are lost, credit risks increase, financing conditions deteriorate and liquidity may dry up. This harms banks' profitability, which was already under pressure due to persistently low interest rates. Risks to financial stability consequently increase further, both in the short term and in the longer term.

An important difference as compared to the 2008 credit crisis is that the cause of the current downturn does not lie within the financial sector itself. Even so, the Dutch banking sector is more resilient than it was in 2008, when the financial crisis hit, due in part to the stricter regulations and higher buffer requirements in recent years. Furthermore, governments and central banks are endeavouring to limit the economic and financial consequences of the pandemic through extensive stimulus packages

and liquidity support. The ECB extended liquidity provision to banks and introduced the Pandemic Emergency Purchase Programme (PEPP), under which a total of EUR 750 billion in sovereign and corporate bonds will be purchased. Governments have announced a wide array of compensation, deferral and guarantee schemes in a bid to prevent liquidity problems among businesses from causing unnecessary bankruptcies and job losses. In the Netherlands, public expenditure on these measures is estimated to top EUR 30 billion in 2020.

DNB has conducted stress tests to investigate vulnerabilities in the Dutch banking sector under severe economic conditions.⁶ In the most severe stress test scenario there is still a deep economic contraction in 2021 and economic activity is considerably lower for an extended period. It should be emphasised that the intention in a stress test is not to predict the economic effects of the COVID-19 shock. Rather, the specific focus is on the impact of negative economic scenarios on the buffers that banks maintain.

⁶ Financial Stability Report, June 2020

Key data in forecast for the Dutch economy

Percentage changes, unless stated otherwise

	2019*	2020	2021	2022
Volume of expenditure and output				
Gross domestic product	1.8	-6.4	2.9	2.4
Private consumption	1.4	-7.6	4.1	2.9
Public expenditure	1.9	3.1	1.9	1.9
Business investment	6.8	-13.9	7.3	6.4
Housing investment	1.9	-0.8	-6.7	-0.6
Exports of goods and services	2.3	-10.9	7.5	4.1
domestically produced	-0.4	-10.2	6.7	2.8
re-exports	6.3	-11.9	8.7	6.0
Imports of goods and services	3.0	-10.7	8.9	4.9
domestically used	1.0	-10.0	9.0	4.3
Wages and prices				
Negotiated wages, private sector	2.3	2.3	1.0	0.7
Compensation per employee, private sector	2.4	1.9	1.0	0.8
Unit labour costs	3.0	7.8	-4.1	0.8
Prices of domestically produced exports	0.7	-2.5	0.1	1.7
Harmonised consumer price index	2.7	0.8	1.1	1.5
House prices, existing own homes	6.9	4.3	-2.1	-3.7
Labour market				
Employment (persons, growth)	1.8	-1.4	-2.7	2.3
Labour supply (persons, growth)	1.4	-0.1	0.2	0.6
Unemployment (persons x 1,000)	314	434	702	553
Unemployment (% of labour force)	3.4	4.6	7.3	5.7

	2019*	2020	2021	2022
Public sector and financial				
EMU balance (% of GDP)	1.7	-6.4	-4.8	-4.3
EMU debt (% of GDP)	48.6	57.9	60.9	63.1
Current account (% of GDP)	10.2	7.8	6.6	6.5
Mortgage loans (based on end-of-period)	1.8	0.5	-0.3	-0.4
Bank lending to NFCs (based on end-of-period)**	-1.3	1.4	-5.0	-2.9
International assumptions				
Volume of relevant world trade	1.6	-12.9	7.5	4.6
Volume of GDP				
US	2.3	-6.4	3.6	2.1
euro area	1.2	-8.7	5.2	3.3
emerging markets	3.5	-3.0	7.0	4.7
Short-term interest rate in the euro area (%)	-0.4	-0.4	-0.4	-0.4
Long-term interest rate in the Netherlands (%)	-0.1	-0.2	-0.2	-0.1
Euro exchange rate (USD)	1.12	1.09	1.08	1.08
Competitor prices	1.6	-2.0	0.3	1.8
Oil price (UK Brent in USD per barrel)	64.2	36.2	37.2	40.7
Commodity prices excluding energy (USD)	-3.7	-2.5	3.5	3.0

Sources: DNB and ECB.

* Annual figures have been calculated based on seasonally adjusted quarterly figures and may therefore deviate marginally from the most recent National Accounts.

** Excluding cash pooling, adjusted for securitisations and breaks.



Figures

Data