COVID-19 impact on the Netherlands

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Short but sharp recession

- **Our baseline scenario sees GDP contracting 3.5%**
- **Consumer spending dries up, hospitality industry hit very hard…**
- **… but offline-to-online substitution limits total fall in consumer spending to an estimated 5% in 2020**
- **In such times as these, the open Dutch economy is vulnerable: trade plunges into a downward spiral**
- **Investments can rebound when government measures to contain COVID-19 are lifted**
- **COVID-19 need not inflict lasting damage on production capacity if supply-side activity rapidly revives**
- **Growth will only resume the upward trend in the course of 2021**
- **Downward risks are substantial, negative sentiment and uncertainty can cause further disruption**

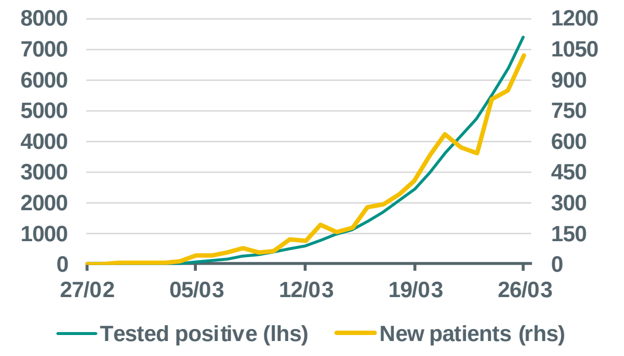
Economic shock hitting the Netherlands in stages

The outbreak of the new corona virus is damaging the economy in a stage-by-stage process. When the virus first took hold in China, production capacity and production chains were paralysed. Both supply and demand of products and services from China went into rapid decline, which also hit Dutch trade (see also: Short insights: China: 2020 growth forecast cut further on Covid-19). On average, some 2.5% of total goods exports from the Netherlands go to China, while some 9% of total goods imports into the Netherlands come from China.

Next, the virus spread to other countries, disrupting import and export chains around the world (see also: Corona shock deeper and longer for weakened economy). For eurozone countries like Germany and Italy this shock, so we expect, was sufficient in itself to bring on a recession. Italy, Europe's first infection hotspot, was already in dire economic straits before the outbreak and must now brace itself for an economic battering. When COVID-19 emerged in the Netherlands, the Dutch economy entered the third damaging stage due to the government's measures to contain the virus. On 27 February the National Institute for Public Health and the Environment (RIVM) reported the first corona infection in the Netherlands. Since then, negative domestic supply and demand effects have dealt a further blow to the economy.

Positive tests in the Netherlands on 25 March

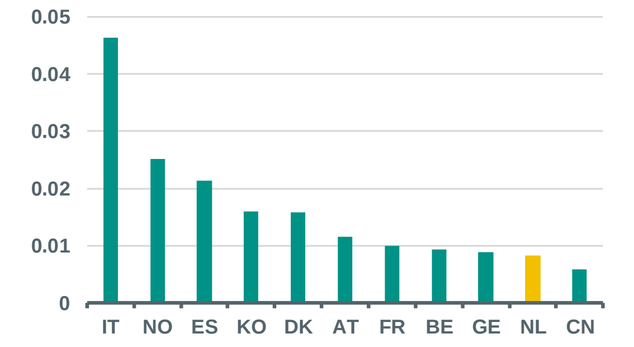
Number of positive tests (individual)



Source: RIVM and Johns Hopkins University

Biggest pressure on Italy

Positive tests as a percentage of total population



Source: RIVM and Johns Hopkins University

We assume that the current measures will last two months

A crisis of this magnitude is uncharted territory and the attendant uncertainty makes it difficult to arrive at an exact estimation of the economic impacts. As a guideline, we have formed a set of assumptions. First of all, we expect the Dutch government's mitigation measures to remain in place for about two months. The exact period may be somewhat longer, but as the measures are also scaled up in intensity over time, our basic assumption is tenable for the time being. We then foresee a step-by-step scaling down of the restrictions, with the most damaging measures – such as the closure of bars and restaurants – the first to be lifted. We assume that by that time the effects of a 'lockdown' are already largely feeding through to the economy due to households and businesses staying at home or closing their doors of their own accord.

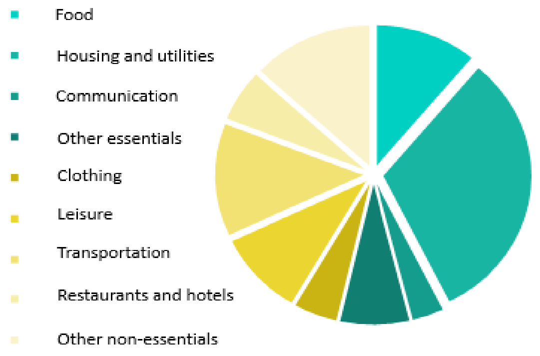
Our baseline scenario also takes account of the extensive measures being taken by government and other authorities to limit the economic fallout. Both the Dutch government and the European Central Bank (ECB) have announced generous measures to shore up the economy (see the list of measures at the bottom of this article).

A sharp but short recession

COVID-19 has effectively brought part of the economy to a standstill. We expect gross domestic product (GDP) to shrink roughly 3.5% this year. The main economic contraction in the Netherlands will take place in the first and, above all, second quarters (-1.3% and -4.5% qoq respectively). Assuming that most restrictions will be lifted in June, the economy can then start to revive in the summer.

Consumption breakdown in the Netherlands

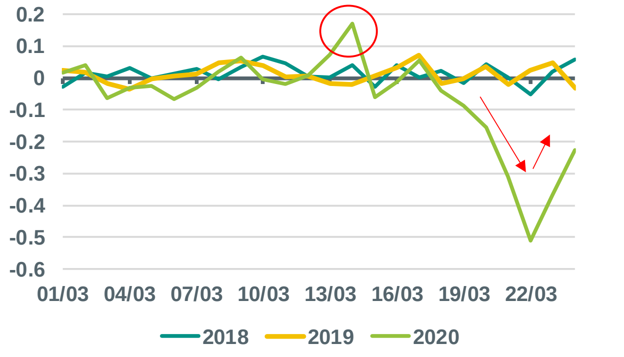
Green: almost unaffected, Yellow: badly affected



Source: Statistics Netherlands (CBS) and ABN AMRO Group Economics

COVID-19 hitting consumer spending

Aggregated debit card transactions, y-axis is deviation from trend



Source: ABN AMRO Group Economics

Consumer spending drying up

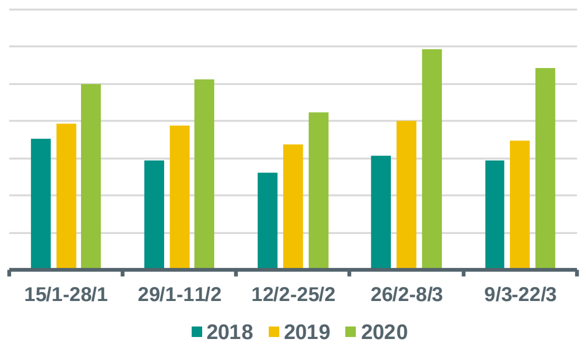
Consumer spending has a huge impact on economic growth, so our assumptions in this respect merit closer inspection. We distinguish between consumer spending that is expected to be hit hard by the corona virus (some 40% - yellow in the above pie diagram) and spending that will be largely unaffected (some 60% - green in the diagram). Restaurants and leisure activities will suffer severely (yellow category), while housing and communication spending will remain largely intact (green category). Spending on transport is also in the yellow category (badly affected) because many people will work from home, refrain from day trips and avoid public transport.

With our real time consumption indicators[1] we can measure which consumer spending categories are essential as well as the extent of the drop in consumption per category. The hospitality industry is being hit hard. Since bars and restaurants were forced to close on 12 March, hospitality spending has plummeted by some 75%. Transport-related expenditures has also plunged, with total spending on petrol, public transport and parking down some 35% on the same week last year.

[1] As the corona virus is a new phenomenon for economists and most official consumption data are published with a time lag of weeks or even months, it is difficult to estimate the direct impact of the spread of the virus on the Dutch economy. That is why we have developed real time indicators to measure consumption using debit card transaction data as our input. Based on the millions of payment transactions going through the bank systems each day, we calculate the consumption volume both in aggregated terms and broken down by services and products. We are thus better able to inform our clients about the real state of the Dutch economy and help policymakers make good choices based on quantitative analysis.

Online spending on the rise

Aggregated online transactions in 2020 compared to the two Saturdays of 2018 and 2019



Source: Statistics Netherlands (CBS) and ABN AMRO Group Economics

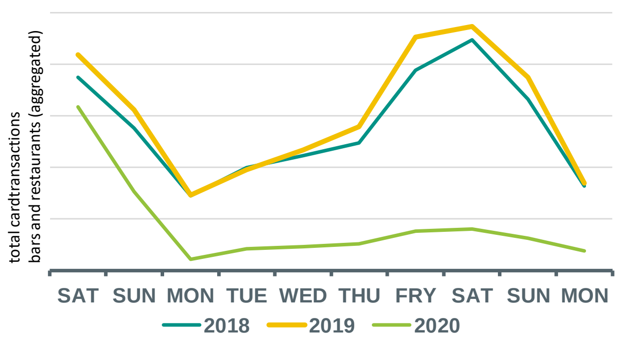
Hoarding is not what it seems

But two other trends are also coming to the fore. First, we see a clear shift from offline to online shopping. Some of the products and services that consumers formerly bought in physical shops are now being purchased online. Second, we see a substitution effect: consumers are spending less in bars and restaurants, but all the more in the supermarket. The phenomenon of 'hoarding' that has been widely reported on in the media is actually in part a rational substitution due to people eating more at home rather than in restaurants or the company canteen.

Our data show that the consumer spending categories which we assume to have been hard hit (yellow in the pie diagram) have declined by some 13% since the government's announcement on 12 March. We expect this percentage to decrease further as some one-time expenditures (such as electronics and pharmacy) disappears. Historical data show that the green category remains virtually intact during an economic downturn. All in all, total consumer spending is likely to fall by some 5% in 2020.

Hospitality the biggest loser....

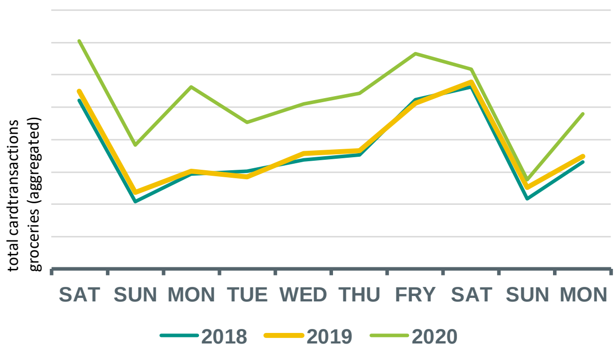
Aggregated hospitality debit card transactions, first SAT = 14 March 2020 compared with Saturdays of 2018 and 2019



Source: ABN AMRO Group Economics

… more spent on groceries

Aggregated supermarket debit card transactions, first SAT = 14 March 2020 compared with Saturdays of 2018 and 2019



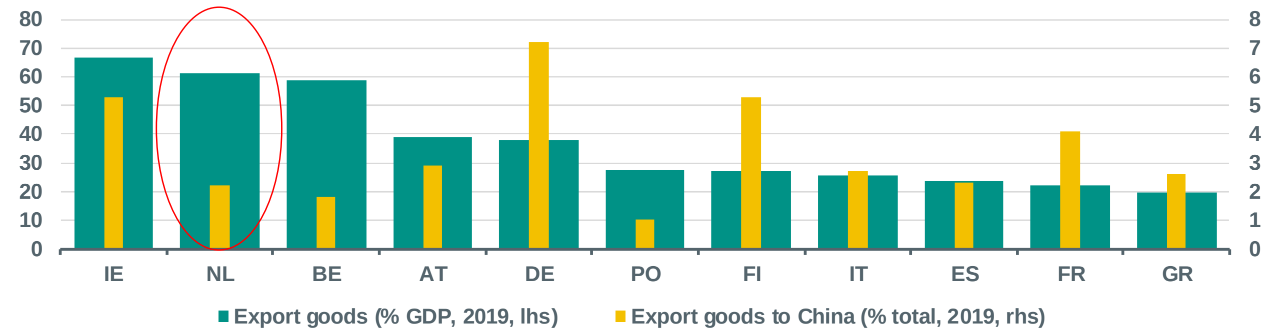
Source: ABN AMRO Group Economics

Imports and exports in a downward spiral

The Netherlands is an open economy: of every euro earned by Dutch industry, 70 cents come from exports. The Netherlands also exports large volumes of intermediary goods. In our globalised world, production chains have become so interconnected that the closure of a single strategically vital company can disrupt entire chains. The corona virus is also spreading rapidly among our main trading partners, such as Germany, France and the UK. The resulting drop in consumer spending in these countries will spark a correspondingly sharp fall in imports and exports. Italy has halted the production of non-essential goods. On average, some 4% of the Netherlands' total exports go to Italy and this is now expected to evaporate entirely to 0%. In addition, trade is being impeded by the newly introduced border controls, the grounding of aircraft and the loss of transport staff. We therefore expect exports to shrink 6% in 2020.

Netherlands vulnerable to loss of foreign demand

Figures from 2019, Greece's of 2018



Source: Eurostat and ABN AMRO Group Economics

Great uncertainty over investments

Whether the current situation leads to a prolonged (and deep) or short-lived recession depends largely on how investments shape up. The composite purchasing managers index (flash) for the eurozone sunk in March to 31.4, the lowest level ever measured. Nevertheless – assuming a lifting of the COVID-19 measures in June – we expect investments to rebound fairly quickly. Whilst losing more than 3 months of income is clearly a bitter pill to swallow for businesses, the government and banks are acting to provide them with sufficient liquidity to weather the storm. Empirical studies of the fallout from natural and nuclear disasters show that such shocks need not impair production capacity on a lasting basis. With government life support keeping existing production structures largely intact, supply-side economic activity can recover more rapidly once COVID-19 disappears. However, history shows that government intervention is not the perfect antidote for preventing loss of production, bankruptcies and unemployment. For 2020 we therefore foresee a decrease in investments of 8%.

Key Figures Dutch economy

	2019	2020	2021
	% changes		
GDP	1.8	-3.5	2.5
Private consumption	1.4	-5.0	4.5
Government consumption	1.6	3.5	1.5
Investments	5.3	-8.0	-1.0
Exports	2.3	-6.0	5.5
Imports	3.0	-6.0	5.0
Consumer prices (CPI)	2.6	1.1	1.4
	levels		
Unemployment (% labour force; av.)	3.4	4.0	4.5

Estimates: ABN AMRO Group Economics

All sectors in the firing line

This situation is taking a huge toll on sectors and individual companies. The greatest pain is felt among the sectors that supply directly to consumers, such as hospitality and retail operators. The sudden collapse in demand is also sending a shock wave down the entire chain. The restaurant ban, for instance, has knock-on effects for hospitality suppliers, food processing companies and the agricultural sector. The closure of hospitality establishments and retail outlets, in turn, is affecting the transport sector. Industry noticed the consequences of the production halt in China at an early stage, but the restrictions in the eurozone – our biggest trading partner – are causing even greater problems. Recruitment agencies are being hit by a sharp decline in demand for temporary staff. The real estate sector, by contrast, is not expected to suffer until a later stage, notably as house and office prices are relatively slow to respond to the current situation. Industry, construction and technology in particular will contend with diminishing investments.

Volume growth by sector in the Netherlands

	2019	2020	2021
% changes			
Agriculture	1.0	-2.0	1.0
Food	1.0	-3.0	2.0
Industry	-1.0	-10.0	8.0
Construction	4.0	-4.5	-2.5
Real Estate**	7.0	1.5	-4.0
Retail	2.5	-8.0	6.0
Leisure	1.4	-15.0	10.0
Transport & Logistics	1.5	-6.0	4.0
Telecom, Media & Technology	3.0	-1.0	0.5
Business Services	3.0	-4.0	-0.5

Estimates: ABN AMRO Sector Advisory

* forecast based on added value

** Real Estate forecast concerns value movement of real estate

Growth not to resume until 2021

We expect catch-up consumption to make up part of the deferred demand in a step by step process after June. Consumers are unlikely to immediately ramp up their spending to the ‘old’ level, preferring to spread this return to normality over the second half of 2020.

Although businesses can use various schemes (such as short-time working) to retain staff for the time being, we already see signals of the jobless rate creeping higher. In February, unemployment stood at 2.9% of the labour force. We think this number will have jumped to more than 4.5% in the summer. Due to the decline in unemployment in the past three months, this increase is not yet clearly visible in the year average (see ‘Key Figures Dutch Economy’ table). This figure, however, conceals the wealth losses that households are set to suffer. In recent years the Netherlands has seen a growing army of flexible workers. Many of these flexible employees will now be given less hours or jobs.

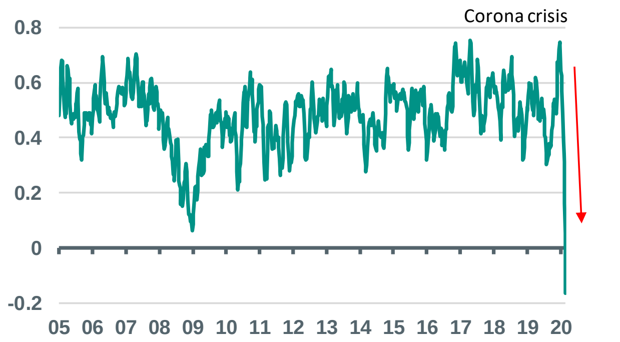
We think that growth will not start climbing to a higher level until 2021. In addition, GDP growth will remain subdued as it will take a while for the disrupted international supply chains for materials and semi-finished/finished products to recover. Investments are also set to remain weak for some time before embarking on a gradual recovery.

Significant downward risks…

Our scenario assumes that the measures to stem COVID-19 can be lifted in early June. The longer these measures remain in place, the more difficult it will be for businesses to keep their head above water, making a rapid increase in the number of bankruptcies inevitable. Another major danger is negative sentiment. Our aggregated sentiment index based on news articles shows that media sentiment since late February has been just as negative as during the financial crisis in 2009. Amidst this uncertainty, households will put off large purchases such as a new home or car. Uncertainty about their sales prospects will also cause businesses to rein in investments, thereby thwarting potential growth. Panic in the financial markets can also spill over into the real economy. The extreme volatility currently seen in the financial markets makes it difficult to price in future risks.

Sentiment in news very negative

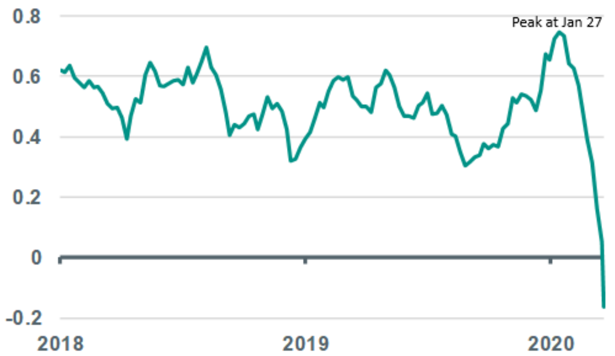
Sentiment measured by BERT model in news articles about the economy



Source: ABN AMRO Group Economics

Sentiment peaked in January 2020

Sentiment measured by BERT model in news articles about the economy



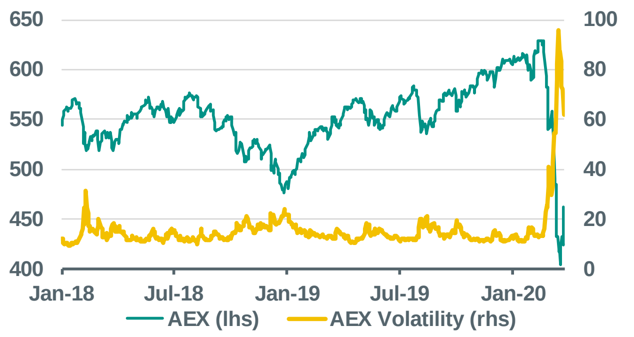
Source: ABN AMRO Group Economics

… but we do not assume a financial crisis

Many fear a repeat of the financial crisis that hit the Netherlands in 2008/2009. That crisis arose due to fundamental flaws in the financial system. The collapse of large financial institutions in the United States had disastrous consequences for the rest of the world. This banking crisis caused a severe erosion of confidence in the financial sector. The COVID-19 crisis can be seen as a exogeneous shock to the system, in contrary to the Global Financial Crisis which was a endogenous shock. The ECB has announced an unprecedented support package (see table at the end of this article), which helps to restore the confidence in the banking sector. Moreover, the DNB will give temporary assistance to banks to help credit lending to the economy and absorb any potential spike in loan loss provisions. Over time, the DNB will compensate the softening of the systemic buffers by gradually increasing the countercyclical capital buffer to 2%. Overall, the regulatory buffer removals across Europe will assist those banks which could get close to struggling on capital requirements and on a wider-level it will help to not invoke panic in the markets. One of the justifications to remove the buffers is to free up lending capacity. However, banks will try to actively reduce their provided credit lines which will act as a negative to lending conditions for corporates. The most at risk companies will see their credit lines reduce first. This is positive for the solvency of banks (and reduces systemic risk), however, it will be negative for the financial conditions in the economy.

AEX volatility peaks

AEX Index and VAEX Index



Source: Thomson Reuters Datastream, ABN AMRO Group Economics

In short, a global recession that is deep but short

Almost all countries in the world will sink into recession simultaneously – a synchronous global recession. However, due to the massive intervention of governments and central banks, combined with the natural waning of the exogenous COVID-19 shock, prolonged negative growth will be averted. In addition, the Netherlands is relatively well-prepared for a recession. The Dutch government has sufficient fiscal latitude to stimulate the economy. The current Dutch debt (49.3% of GDP) is relatively low and has been under the Maastricht ceiling of 60% of GDP since 2017. This exogenous shock also comes at a time when the economy was running at full steam and some cooling had already been factored in. Moreover, confidence in institutions is robust at the present moment. A survey of the current affairs programme *EenVandaag* showed that about 95% of the Dutch population supports the new corona measures.

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Dutch government measures for cushioning the negative economic impacts

The Dutch government has also announced several emergency measures to dampen the direct economic damage from the virus (see table below). The measures are largely aimed at the prevention of bankruptcies.

The speed and flexibility with which the government announced its aid package has boosted confidence among businesses and consumers. But whether the measures can be smoothly rolled out at such short notice remains to be seen. To illustrate the scale of the challenge, the number of short-time working applications averaged 200 annually in recent years; a far cry from the 78,000 submitted in recent weeks. Transport, retail and travel businesses have ground to a virtual standstill. So it is vital that they can quickly access the support pledged through the measures set out in the table below.

Once it has finalised the emergency measures, we also expect the government to come up with a fiscal stimulus package - either through tax reductions or by accelerating planned spending on infrastructure maintenance and construction.

Continues on next page

Government measures		
Measure	**Explanation**	**Amount**
Temporary Job Retention Scheme	Shorter working week for staff. State pays unemployment benefit for hours not worked so that employer can continue paying staff wages.	Retention of 90% of salary
Expanded SME Guarantee Scheme (BMKB)	SMEs can borrow on softer terms from banks	EUR 300 million
Extra support for independent entrepreneurs	Supplementary income for 3 months on lenient terms and/or business capital loans for the self-employed	
Business Finance Guarantee Scheme	The cabinet proposes to raise the ceiling for the business finance guarantee scheme. This scheme provides SMEs and large corporates with a 50% guarantee for bank loans and bank guarantees (minimum EUR 1.5 million – maximum EUR 50 million per company)	Increase from EUR 400 million to EUR 1.5 billion, minimum EUR 1.5 million – maximum EUR 50 million per company
Lower interest rate on Qredits microloans for small businesses	Small businesses that are affected by corona are offered a loan repayment holiday	Period of 6 months, interest reduced to 2%
Relaxation of tax payment deferral rules and lower penalties	Applies to income, corporate, wage and turnover tax (VAT)	
Temporary guarantee for agricultural and horticultural SMEs	Agricultural and horticultural SMEs are eligible for temporary working capital guarantees	
Compensation scheme for affected sectors	The details are still to be finalised	
Covid-19 hardship compensation	Immediate cash assistance for SMEs	EUR 4000 per business

Source: Dutch national government

Measures of the European Central Bank (ECB)

Central banks around the world have acted swiftly to mitigate the impact of the COVID-19 outbreak on the financial stability. The Federal Reserve (Fed), for instance, has taken macroprudential measures while also lowering its basic policy rate by 150 basis points in total to 0%. In addition, the Fed has announced an unlimited asset purchasing programme. Whether this will be effective is open to question - because rate cuts will hardly motivate liquidity-strapped businesses to make extra investments. This is also evident from the Financial Condition Index (FCI) which pointed to further tightening in the second week of March. The ECB has left interest rates on hold (the deposit rate is already -0.5%), but has taken all sorts of mitigating measures while also announcing the *Pandemic Emergency Purchase Programme (PEPP)* of EUR 750 billion on 18 March (see table below).

ECB Measures	
Measure	**Explanation**
Expansion of bond-buying programme (no limits)	EUR 1100bn in 2020 (maximum limit of 33% per investment class no longer applicable), including EUR 750 billion PEPP
Flexible deviation from capital key (total amount that central banks can borrow from the ECB)	
Acute liquidity support for banks	Extra long-term loans at – 0.5%
Expansion of TLTROs	from EUR 2000bn to EUR 3000bn
Introduction of lower limit for the risk weighting of mortgage loans to be postponed	
The system risk buffer to be reduced from the current 3%	Differs per bank

Source: ECB en DNB