Analysis

DNB March projection: Economic outlook for 2021 and 2022

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April 2021

DeNederlandscheBank

EUROSYSTEEM

This memorandum sets out DNB's most recent forecasts for the Dutch economy in 2021 and 2022. This so-called interim projection is an updated version of the December forecast and, as such, it is not comprehensive. The reason for this update is the fact that the pandemic has not developed as predicted in DNB's previous projection, which was based on the assumption that the partial lockdown would be relaxed from the beginning of 2021. Partly based on this expectation, the December projection estimated GDP growth of 2.9% in both 2021 and 2022. However, in mid-December the containment measures were further tightened, effectively leading to a full lockdown, which is still in place.

The interim projection was prepared in March and is based on the recent ECB forecast for the euro area. One important change compared to December is that the most recent projection takes into account the Brexit deal between the EU and the UK, leading to an upward adjustment of world trade relevant for the Netherlands. In addition, the interim projection incorporates the latest realisation figures for the Dutch economy (as available when the projection was made) and includes updated estimates for public expenditure[1]. Overall, both are more favourable now than in the December projection.

This latest version of the projection takes into account the government's decision in March to relax the containment measures. The next major steps back to normal life are not expected until summer. As a result, economic recovery will not start in earnest until the third quarter of this year. In line with the ECB's projections, the current expectation is that the measures will not be fully phased out until the first quarter of 2022. DNB's interim projection does, however, include an alternative scenario in which the measures are completely phased out this year, in the course of the third quarter.

Economic growth

The Dutch economy contracted by 3.7% in 2020, tying with the downturn in 2009 (in the wake of the financial crisis) for the strongest economic decline since World War II. Incidentally, the contraction of the Dutch economy was relatively minor compared to other European countries. Countries such as Germany (-4.9%), Belgium (-6.4%) and France (-8.1%) all saw greater declines, as did the euro area as a whole (-6.6%).
That is why DNB expects that the second half of 2021 will stand in stark contrast to the beginning of the year. On the one hand, any developments in the first six months will mainly be driven by the recent surge in coronavirus infections and the ongoing lockdown measures. As a result, the economy will once again experience setbacks. In January, for instance, private consumption was down 13.5% compared to the year before, the second largest contraction after April 2020 (17.1%). On the other hand, the vaccination programme offers a glimpse of light at the end of the tunnel. The economy is expected to receive a significant boost in the second half of the year, as many of the containment measures will be rolled back. Overall, GDP growth is expected to reach 2.2% in 2021 (see Table 1) and 4.2% in 2022.

[1] The interim projection is based on information available on 15 March 2021.

Table 1: Key data in March 2021 projections
Percentage changes, unless stated otherwise

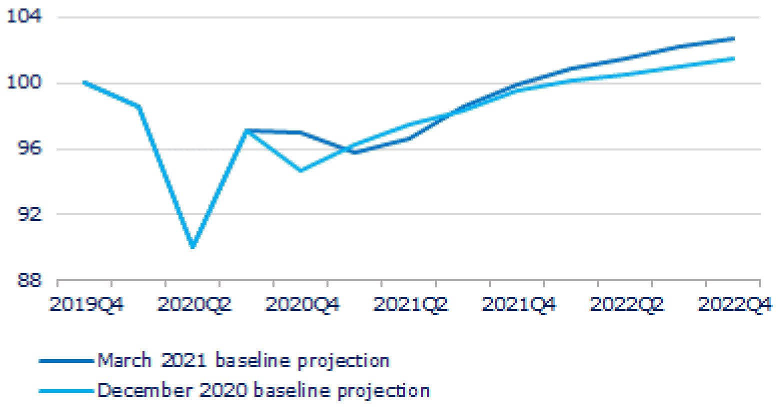
	2021	2022
Volume of expenditure and output		
Gross domestic product	2,2	4,2
Private consumption	1,0	7,2
Public expenditure	5,1	3,8
Business investment	2,2	8,6
Housing investment	-3,6	3,2
Exports of goods and services	5,3	4,3
Imports of goods and services	5,8	6,4
Prices		
Harmonised consumer price index	1,2	1,6
House prices, existing own homes	6,0	3,1
Labour market		
Employment (persons, growth)	-0,5	0,0
Labour supply (persons, growth)	0,3	0,8
Unemployment (% of labour force)	4,6	5,3
Public sector		
EMU balance (% of GDP)	-6,4	-2,6
EMU debt (% of GDP)	59,0	57,8
International assumptions		
Volume of relevant world trade	6,8	5,3
Short-term interest rate in the euro area (%)	-0,5	-0,5
Long-term interest rate in the Netherlands (%)	-0,3	-0,1
Euro exchange rate (USD)	1,2	1,2
Oil price (UK Brent in USD per barrel)	59,3	55,7

This would be the highest GDP growth since the turn of the century, on par with 2000. The recovery of private consumption, which is expected to grow by 7.2% in 2022, will be the main driver of GDP growth. In response to this boost in household expenditure, businesses will also significantly increase their investments (8.6%). In the first quarter of 2022, GDP volume is expected to equal that of the fourth quarter of 2019.

Cumulated GDP growth in 2021 and 2022 is now projected to be more than 0.5 percentage points higher than in the December forecast (see Figure 1). This is related to three developments. First, the realisations for unemployment and house prices are more favourable than in the previous projection. Second, world trade growth has been adjusted upwards, partly due to the Brexit deal between the EU and the UK. Third, the estimates for public expenditure have been adjusted upwards.

Figure 1 Gross domestic product

Volume index 2019 Q4=100



Labour market

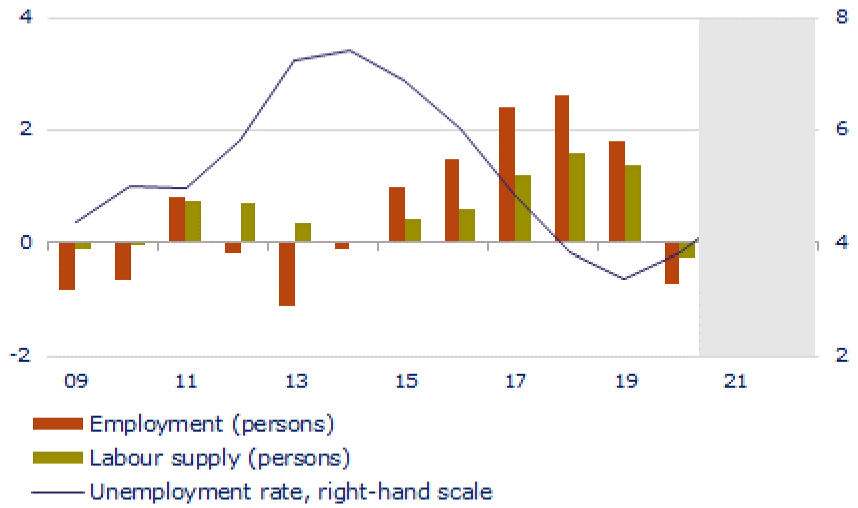
The number of employed people declined by 0.7% in 2020. While this drop is significant, it is not exceptional. In this century alone, there were three years that saw greater employment contraction: 2004, 2009 and 2013. The limited drop in employment can mainly be attributed to the Dutch government's support packages. The 3.5% contraction in the total number of hours worked, however, is unprecedented.

Employment is expected to contract by a further 0.5% in 2021 and remain stable in 2022, as the labour market shows its usual delayed response to GDP growth. The expected rise in the number of bankruptcies after the support measures are scaled down this summer also plays an important role in this regard.

As a result of the economic recovery in 2021 and 2022, the number of discouraged job seekers will decline, leading to an increased labour supply in both years covered by the projection. Overall, unemployment is expected to increase from an average of 3.9% in 2020 to 4.6% in 2021 and 5.3% in 2022 (see Figure 2).

Figure 2 Labour market

% changes and % of labour force



Public finance

As a result of the coronavirus crisis and the support packages, the budget deficit reached 4.3% of GDP in 2020. It is expected to increase further to 6.4% of GDP this year, driven mainly by higher public spending on support measures, healthcare and education (the latter under the National Education Programme). This means that the budget deficit will be higher than during the financial crisis (5.3% of GDP in 2010). In 2022, the deficit will decrease to 2.6% of GDP as a result of economic recovery and the expiry of the support measures.

The government's debt-to-GDP ratio is projected to peak at 59.0% in 2021 before declining slightly to 57.8% in 2022. As a result, public debt is forecast to remain well below the level of the previous peak of 67.9% of GDP in 2014, in the aftermath of the financial crisis.

Inflation rates

HICP inflation is expected to increase to 1.2% in 2021, up from 1.1% in 2020. This relative stability is caused by two opposing forces. On the one hand, oil prices are estimated to rise from USD 43 per barrel in 2020 to USD 59 in 2021. On the other hand, the new expenditure weights have a limiting effect on HICP inflation. Each year, Statistics Netherlands adjusts these weights on the basis of the consumption pattern of the previous year. This year, the adjustments are more substantial than usual. The pandemic and the containment measures had a significant impact on consumption patterns in 2020. In the Netherlands, this led to a downward effect on inflation. On balance, these effects cancel each other out, leading to a relatively stable inflation rate. In 2022, inflation is projected to rise to 1.6% as a result of economic recovery.

Alternative scenario: Containment measures are phased out in Q3 2021

In line with the ECB's projections, the current expectation is that the measures will not be fully phased out until the first quarter of 2022. However, given the caretaker cabinet's intention to offer everyone above the age of 18 the opportunity to get their first injection before 1 July, the measures may be rolled back earlier. DNB has therefore also conducted an exploratory analysis, based on an alternative scenario in which the measures are fully phased out in the course of the third quarter of 2021.

This would primarily affect private consumption. In this alternative scenario, consumption would be back to the pre-pandemic level of the fourth quarter of 2019 before the end of 2021. This means that consumption would recover six months earlier than in the interim projection. As a result, GDP growth would be 0.3% higher in both years than in the interim projection: 2.4% in 2021 and 4.5% in 2022 (Table 2). This would also result in slightly lower unemployment and a marginally smaller budget deficit than forecast in the interim projection.

The predictions for this scenario are highly uncertain, however. Consumption might not recover as quickly as projected, for instance, as the consumption behaviour of part of the population (especially of at-risk groups) could continue to be influenced by virus-related uncertainty for some time after the measures are lifted. On the other hand, the alternative scenario was based on the same international developments as the interim projection, which include the assumption that containment measures would not be rolled back early outside the Netherlands. Should other countries also decide to lift their measures early, GDP growth could be somewhat higher than projected due to higher external demand.