Focus on growth

The IMF delivers an unexpected message to the Dutch

THE NETHERLANDS has spent the past year sinking ever deeper into economic gloom. GDP shrank by almost 1% in 2012, and forecasters expect another 0.5% contraction this year. Looking over the border, the Dutch see a German economy that managed small growth last year, and wonder where they went wrong. A visit from the professional scolds at the IMF could hardly be expected to lift the mood.

Yet on March 19th, an IMF research mission delivered a surprising message to the Dutch parliament: lighten up. The Netherlands has the trust of financial markets and is starting to tackle its long-term problems, said the IMF. Now the main tasks are to push through more structural reforms and not be panicked into further short-term austerity.

Why is the wealthy Netherlands, with its AAA credit rating and a competitive economy, doing so badly? And why is it in much worse shape than neighbouring Germany (see chart)?

The Dutch weakness is consumer spending, which has been falling for a year and a half. Household consumption last year was lower than in 2006. Consumer confidence fell to the lowest level ever measured in February. The chief source of anxiety has been house prices. Over the past decade, Dutch housing experienced a bubble comparable to those in Spain or Ireland. But house prices dropped by 6% last year and have fallen by 16.6% from their peak. Feeling poorer, homeowners have simply stopped spending.

This seems to suggest an easy solution. Once house prices hit bottom, the economy will recover. But residential-mortgage interest is fully tax-deductible. In a country where much of the middle class pays a 52% top income tax-rate, that still drives huge amounts of investment into housing. Moreover, Dutch banks have created a series of exotic "interest-only" mortgage products to maximise tax deductions, leading to the highest household-debt levels in the euro zone.

Explore our interactive guide to Europe's troubled economies.

The centrist coalition elected last autumn finally took on the thorny issue, or “hot hanging-iron”, as the Dutch expression has it. But it is uncertain whether a new law to limit mortgage-related tax deductions will stick. Meanwhile the projected budget deficit has jumped. When March’s economic projections showed further deterioration, the government proposed yet another round of austerity.

The IMF says that last December’s austerity measures go far enough; further cuts would be “pro-cyclical” and produce “policy uncertainty”. The government needs to push through structural reforms in the housing and labour markets, let house prices fall and banks deleverage. Straightening out the kinks in the Dutch economy may mean years of depressed growth. Unpredictable austerity measures will only slow the process.

Fonte: The Economist, London, v. 406, n. 8828, p. 59, 23^{rd} – 29^{th} mar. 2013.