

Economic resilience in an uncertain world

Implications for Europe and the Netherlands

DeNederlandscheBank

EUROSYSTEEM

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17 February 2026

Thank you for the invitation.

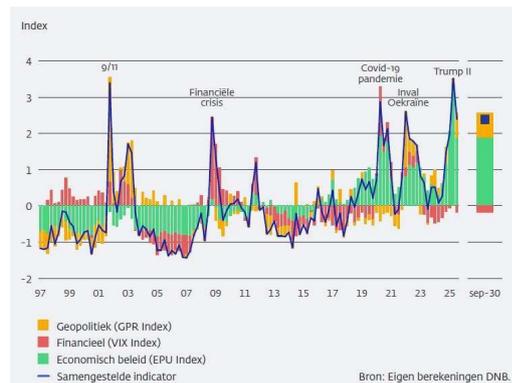
I'd like to talk about how the global economy is handling this period of exceptional uncertainty, and what it means for Europe and the Netherlands. And please note this is an economic analysis, not a forecast or political statement.

Let's start with an observation that might seem surprising...

The puzzle: everything changed, yet nothing did

- Geopolitical tensions have gone up
- Trade fragmentation went up
- Uncertainty went up

Yet growth, employment and markets remain resilient



We are currently experiencing a period of exceptional geopolitical and economic uncertainty.

Consider this graph – it shows an uncertainty index. And as you can see, the spikes in uncertainty – such as the war in Ukraine and the second Trump administration – consist of a mix of different factors, such as geopolitical risk and economic policy uncertainty.

If you focus solely on the headlines, you would expect a much weaker economy.

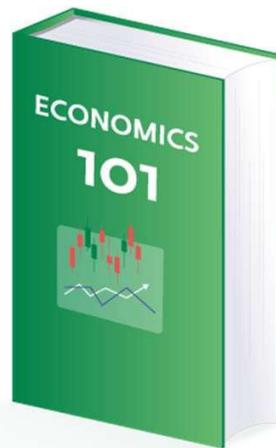
However, if you look only at macroeconomic data or the stock markets, the outlook seems stable.

So, the key question isn't the presence of risks, but understanding why these have not yet fully materialised.

So how can these two views be reconciled? Economic theory can help us find an answer to this question.

What would economic theory predict?

- Trade goes down
- Inflation goes up
- Investments go down
- Volatility goes up



Geopolitical tensions are materialising in fragmentation, tariffs and greater uncertainty.

Economic theory suggests that such shocks have a negative impact on growth, inflation, and markets.

Typically, they:

- Reduce trade and productivity
- Increase inflation
- Increase risk premia
- Weaken investment and confidence

So, the theory points in one direction but the outcomes look different, and we need to understand why.

Transmission channels: how do shocks reach the economy?



That brings us to the key question: how do these shocks impact the economy, and how quickly do they take effect?

There are four main channels:

1. Trade and supply chains: factors such as sanctions, tariffs, fragmentation, and bottlenecks play significant roles.
2. Energy and commodities: price volatility, supply security, and transition risks all contribute.
3. Financial markets: risk premia, capital movements, and fluctuations in foreign exchange rates affect outcomes.
4. Confidence and expectations: uncertainty can cause businesses to postpone investments and consumers to become more cautious.

While all four channels influence the economy, their effects vary in strength and timing. So, what is our level of exposure to these channels?

The Netherlands is particularly exposed



And zooming in, what makes the Netherlands especially vulnerable?

Small open economies like the Netherlands are particularly sensitive to external shocks due to our significant trade openness, our strong integration in global value chains, and heavy reliance on critical imported inputs.

Dutch firms depend more heavily on the US market compared to many of their EU peers, with several vulnerable sectors directly affected by recently imposed US tariffs (DNB Financial Stability Report, Spring 2025).

The DNB Spring Projections (June 2025) indicate that increasing trade tensions and US tariffs have already resulted in downward revisions to Dutch growth projections, primarily through weaker business investment and declining exports.

While openness is an economic advantage, our elevated exposure means external shocks will impact the Netherlands sooner and more acutely, rendering the economy sensitive to shifts in global trade policy and geopolitical risks.

Let's illustrate this by looking at some examples and the first channel: trade.

Trade fragmentation: why are the effects delayed?

- Offsets mask costs
- Firms absorb shocks
- Adjustment take time



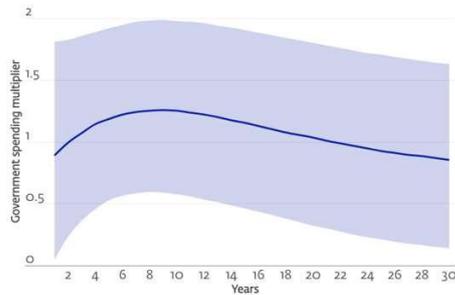
Example 1: Trade is the first geopolitical channel. Even when trade disruptions occur, the damage tends to be limited. Why?

- Tariffs and restrictions raise costs, but firms often respond by frontloading imports, absorbing part of the increased cost, and diverting trade towards lower-tariff partners. This delays the immediately visible impact. As a result, costs accumulate gradually, and inflation effects emerge at a later stage.
- Longer-term effects like reshoring, duplicate capacity and reduced efficiency materialise only over time.

Although fragmentation progresses gradually, it remains persistent. On the other hand, not every geopolitical event slows economic growth. In theory, some developments –such as higher defence spending – may actually boost growth.

Higher defence spending: economic trade-offs

Economic opportunities for Europe



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...but constraints for the NL



Tight labour market leads to inflation risks



Roughly half of defense spending leaks abroad through imports



Small defense industry leads to limited national spillovers

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Example 2: is it possible that some geopolitical responses actually support growth – and therefore explain resilience?

Historically, increased defence expenditure has been associated with economic growth, and higher average GDP figures across Europe (see left figure).

In the **short term** it might boost demand, employment and GDP.

But the economy has limited capacity, and countries like the Netherlands depend on imports from abroad.

This leads to several challenges in the medium term, such as labour constraints and limited domestic defence capacity, both of which can create inflationary pressures.

So, what may seem like economic stimulus now, could result in inflationary pressures or bottlenecks in the future.

Long-term opportunities for the Netherlands are in targeted **dual-use technologies** that complement European expertise.

But long-term goals can only be achieved with predictable policies and European cooperation.

So, even strategically essential policies such as defence spending come with trade-offs.

If adverse trade effects are delayed and fiscal expansion supports demand, it becomes easier to understand why financial markets still seem relatively stable.

Why are financial markets calm?

- Markets price expectations
- AI: transformative, but profitable?
- Fiscal support: cushioned shocks
- Corrections happen suddenly, not gradually



Example 3: Markets may appear stable because:

- Markets reflect expectations rather than headlines.
- AI is transformative, but profitability is essential, so there is a risk of over-optimism.
- Fiscal support has cushioned shocks.
- In the US, hopes of a more dovish Fed have supported markets, but financial markets often underestimate risks until sudden corrections occur.

It's important to emphasise that **markets reflect expectations, not predictions of the future**. So, apparent stability should not be confused with the absence of vulnerability.

This can explain why the economy looks resilient, but we should not let our guard down.

This is not a reason to relax

- Inflation persistence through second round effects
- Financial stability risks from a sudden repricing of risks
- Dollar dependence and financial spillovers
- Policy uncertainty becomes an economic shock



Recent resilience reflects both stronger structural buffers, such as better -capitalised banks and lower leverage, alongside temporary factors such as delayed trade effects, fiscal support and stable markets, but some vulnerabilities remain.

Several significant risks must be considered:

- Persistent inflation due to second-round effects
- Financial stability concerns arising from abrupt risk repricing
- Reliance on the dollar and associated financial spillovers
- Policy uncertainty translating into economic shocks

It is crucial to recognise that the primary concern lies not with isolated shocks, but in the interaction of multiple factors. This is why waiting for definitive data signals can be costly.

So, what does this mean for policy?

Implications for central banking



- Price stability & shocks
- Financial stability risks
- Importance of independence

As part of our mandate, we at DNB are responsible for maintaining price stability and financial stability.

Geopolitical shocks typically exert inflationary pressure in the short to medium term, mainly through adverse supply shocks. The effects on demand are variable and tend to fluctuate over time.

As a result, inflation dynamics are increasingly influenced by cost-push factors. While monetary policy can help mitigate these pressures, it may not be able to fully counteract them.

Consequently, a credible and independent central bank is essential to anchor inflation expectations in the face of persistent supply-side uncertainties.

Fiscal space is tightening

- Crisis support raised debt levels
- Ageing and interest burden rising
- Climate, defence, digital needs expanding



Fiscal policy constrained in uncertain times



But central banks cannot address these challenges alone. In a world of repeated supply shocks, resilience depends just as much on fiscal policy, and here, the room for manoeuvre has changed.

- Fiscal support during the pandemic and the energy crisis prevented much deeper economic harm, but it also pushed public debt higher across several euro-area countries.
- We face rising ageing costs, higher interest payments, and growing investment needs in climate, defence and digital.
- And the new EU fiscal rules require credible medium-term plans.

In other words: fiscal policy is becoming more constrained in a world where uncertainty is rising.

This leads us to consider the European dimension. Fiscal constraints are not solely national concerns: they also influence Europe's ability to respond effectively in an increasingly fragmented global environment.

Europe: less fragmentation, more integration

- Completed single market
- Savings and Investments Union
- Faster and more effective decision making



In this fragmented world, Europe cannot afford internal division. However, the need for decisive action now far outweighs the pace at which we make decisions together.

Europe managed to withstand recent shocks by implementing effective and coordinated policy responses spanning fiscal, monetary, micro-prudential and macroprudential approaches. Coordinated action strengthens Europe's ability to absorb global shocks and plays a vital role in its financial safety net.

What Europe needs is:

- A fully integrated single market in services, energy, digital, and defence production
- A Savings and Investments Union to direct capital toward European priorities
- Swift and efficient decision-making to respond to geopolitical and economic shocks

Europe will increasingly need innovative ways of working together, such as differentiated integration, coalitions of the willing, or even a separate 28th regime when full harmonization takes too long. Achieving strategic autonomy does not require everyone to progress at the same pace, but that those who are ready to advance more quickly should be enabled to do so.

Many major challenges are best addressed at the European level, and this raises the question of how countries like the Netherlands can contribute to shaping this integration.

What should the Netherlands do?

- Re-engage actively in Europe
- Reduce domestic policy uncertainty
- Think strategically at the product level



Speed and clarity are economic assets



The Netherlands benefits from European integration, which is why we should assume an active leading role in shaping its development.

There are three priorities for the Netherlands:

- Actively re-engage in Europe:
 - urgency is high in defence cooperation and in industrial and technological capacity,
 - support coalitions of the willing and differentiated integration
- Reduce domestic policy uncertainty
- Think strategically at the product level, avoiding blunt sector-wide protectionism

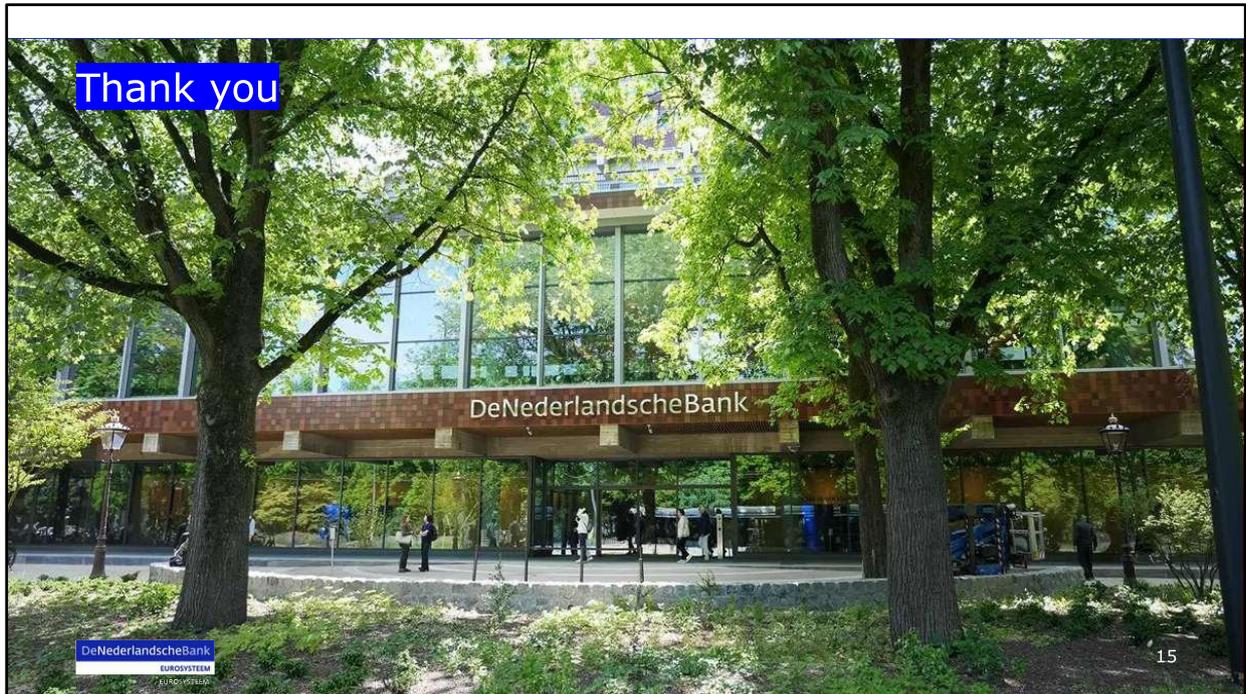
In an increasingly fragmented global economy, the ability to make swift and well-informed decisions has emerged as a critical economic advantage. It is essential for governments to reclaim their roles and enhance the effectiveness of European integration.

In conclusion

- The absence of a crisis in the numbers is not a proof of resilience
- Good policy is about acting before risks crystallize
- This applies to Europe, to the Netherlands and to central banking

These choices matter not just for growth, but also for the stability of the economic system.

- Just because the numbers don't show a crisis doesn't mean the system is resilient.
- Effective policymaking means taking action before potential risks become reality.
- This principle holds true in Europe, the Netherlands, and within central banking.



Thank you.

Any questions?