

Box 6

RESULTS OF THE ECB SURVEY OF PROFESSIONAL FORECASTERS FOR THE FIRST QUARTER OF 2011

This box reports the results of the ECB Survey of Professional Forecasters (SPF) for the first quarter of 2011. The survey was conducted between 14 and 18 January 2011. There were 56 responses from forecasters. The SPF collects information on expectations for euro area inflation, real GDP growth and unemployment from experts affiliated with financial or non-financial institutions that are based in the EU.¹

Inflation expectations for 2011 and 2012

Inflation is expected to be at 1.9% in 2011 and 1.8% in 2012. Compared with the previous SPF round, forecasters have revised upwards their inflation expectations by 0.4 percentage point for 2011 and by 0.2 percentage point for 2012 (see the table).² According to respondents' comments, the upward revisions compared with the previous SPF round are due almost entirely to higher oil and other commodity prices, which, however, are expected to have only a temporary impact on inflation,

1 Given the diversity of the panel of participants, aggregate SPF results can reflect a relatively heterogeneous set of subjective views and assumptions.

2 Additional data are available on the ECB's website at www.ecb.europa.eu/stats/prices/indic/forecast/html/index.en.html

Results of the SPF, Eurosystem staff macroeconomic projections, Consensus Economics and Euro Zone Barometer

(annual percentage changes, unless otherwise indicated)

| HICP inflation | Survey horizon | | | | |
|--|----------------|---------------|---------|---------------|---------------------------|
| | 2011 | December 2011 | 2012 | December 2012 | Longer-term ²⁾ |
| SPF Q1 2011 | 1.9 | 1.8 | 1.8 | 1.8 | 2.0 |
| <i>Previous SPF (Q4 2010)</i> | 1.5 | - | 1.6 | - | 1.9 |
| Eurosystem staff macroeconomic projections | 1.3-2.3 | | 0.7-2.3 | - | - |
| Consensus Economics (January 2011) | 1.8 | - | 1.7 | - | 2.0 |
| Euro Zone Barometer (January 2011) | 1.7 | - | 1.7 | - | 2.0 |
| Real GDP growth | 2011 | Q3 2011 | 2012 | Q3 2012 | Longer-term ²⁾ |
| SPF Q1 2011 | 1.6 | 1.4 | 1.7 | 1.8 | 1.9 |
| <i>Previous SPF (Q4 2010)</i> | 1.5 | - | 1.7 | - | 1.8 |
| Eurosystem staff macroeconomic projections | 0.7-2.1 | - | 0.6-2.8 | - | - |
| Consensus Economics (January 2011) | 1.5 | 1.3 | 1.6 | - | 1.7 |
| Euro Zone Barometer (January 2011) | 1.5 | 1.3 | 1.6 | 1.7 | 1.9 |
| Unemployment rate ¹⁾ | 2011 | November 2011 | 2012 | November 2012 | Longer-term ²⁾ |
| SPF Q1 2011 | 9.9 | 9.9 | 9.6 | 9.5 | 8.3 |
| <i>Previous SPF (Q4 2010)</i> | 10.0 | - | 9.6 | - | 8.3 |
| Consensus Economics (January 2011) | 9.9 | - | 9.6 | - | - |
| Euro Zone Barometer (January 2011) | 9.9 | - | 9.6 | - | 8.6 |

1) As a percentage of the labour force.

2) Longer-term expectations refer to 2015 in the Survey of Professional Forecasters, Consensus Economics and the Euro Zone Barometer.

as commodity prices are expected to stabilise in the course of 2011. Moreover, the temporarily higher input prices are expected to be passed on only partly to households, owing to the ongoing weakness in consumer demand.

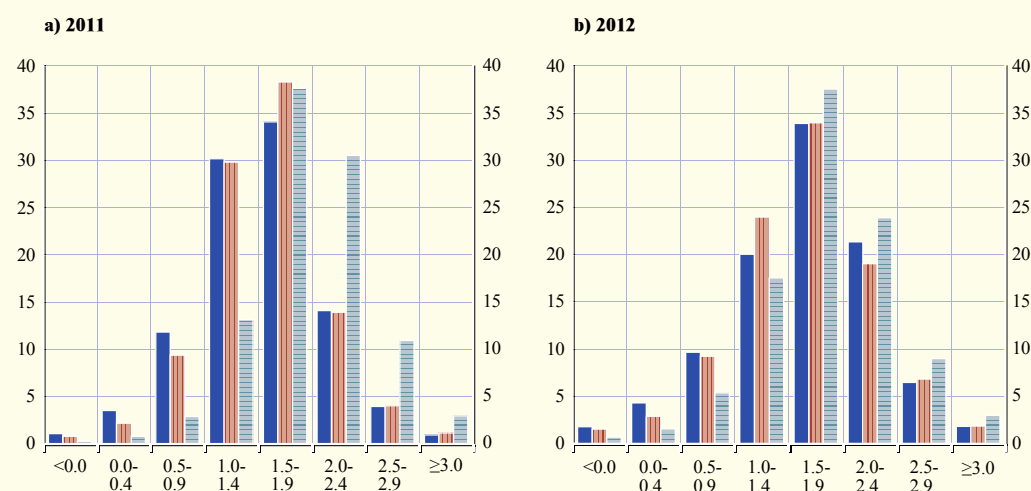
These expectations are within the ranges reported in the December 2010 Eurosystem staff macroeconomic projections for the euro area. Compared with the forecasts published in the January 2011 issues of Consensus Economics and the Euro Zone Barometer, the SPF inflation expectations are slightly higher for both years.

The SPF participants were also asked to assess the probability of inflation falling within specific intervals. Compared with the previous SPF round, the aggregate probability distribution for 2011 shifted towards higher outcomes. The respondents still assigned the highest probability (38%) to the range between 1.5% and 1.9%, and a 31% probability to the range between 2.0% to 2.4%. The probability distribution for 2012 also shifted to higher outcomes compared with the previous SPF round (see Chart A). Based on the individual probability distributions, the balance of risks to these forecasts is assessed by respondents as being broadly balanced for both 2011 and 2012. According to the participants, the key upside risks to the inflation outlook are mainly: i) instability in commodity markets, which could possibly trigger higher commodity prices and subsequently a price-wage spiral; ii) increases in levies, taxes and administered prices resulting from fiscal consolidation plans; and iii) excess liquidity in international financial markets. The main downside risks to the inflation outlook are perceived to be: i) low wage pressures owing to persistently high unemployment rates; ii) relatively modest activity and ample spare capacity; and iii) a stronger euro, which would lead to lower import prices.

Chart A Probability distribution for average annual inflation in 2011 and 2012 in the latest SPF rounds¹⁾

(probability in percentages)

■ Q3 2010 SPF
■ Q4 2010 SPF
■ Q1 2011 SPF



Source: ECB.

1) Corresponds to the average of individual probability distributions provided by SPF forecasters.

Indicators of longer-term inflation expectations

Longer-term inflation expectations (for 2015) have been revised slightly upwards, on average to 2.0% (1.95% to two decimal places) from 1.9% (1.90% to two decimal places) in the previous SPF round. The median of the point forecasts, which is less affected by extreme values than the average point forecast, also increased from 1.9% to 2.0%. The distribution of point estimates is concentrated in the range between 1.8% and 2.0%, with a point forecast of 2.0% being reported most frequently. The average point forecast is in line with the longer-term inflation expectations provided in the October 2010 issue of Consensus Economics and with those published in the January 2011 issue of the Euro Zone Barometer (both for 2015). Finally, the probability assigned to longer-term inflation standing at 2% or above increased to 48%, after 45% in the previous SPF round.

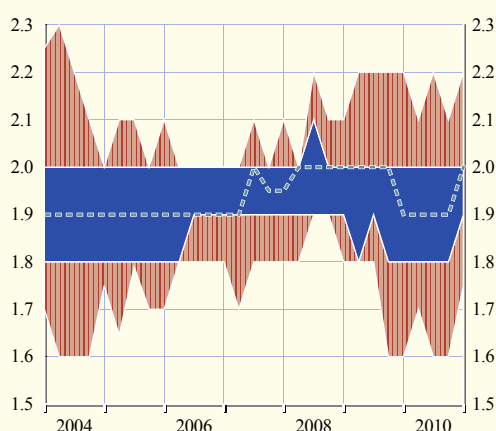
The disagreement among forecasters in their longer-term inflation expectations, as measured by the standard deviation of their point forecasts, has fallen slightly, but remains at a relatively high level. The spread between the 25th percentile (1.9%) and the 75th percentile (2.0%) has narrowed for the first time since the third quarter of 2009, while the spread between the 10th and the 90th percentiles remains wider than the relatively narrow spread observed between 2005 and 2008 (see Chart B). Aggregate uncertainty surrounding longer-term inflation expectations, as measured by the standard deviation of the aggregate probability distribution, has declined from the record high observed in the previous SPF round.³

3 For a discussion regarding uncertainty measures, see the box entitled “Measuring perceptions of macroeconomic uncertainty”, *Monthly Bulletin*, ECB, January 2010.

Chart B Longer-term (2015) inflation point forecasts of the SPF respondents

(annual percentage changes)

- range between 25th and 75th percentiles
- range between 10th and 90th percentiles
- median of the point forecasts



Source: ECB.

Chart C Longer-term inflation expectations from surveys and break-even inflation rates

(average annual percentage changes; five-day moving averages of daily data)

- SPF (for 2015)
- ▲ Consensus Economics (for 2015)
- Euro Zone Barometer (for 2015)
- implied five-year forward break-even inflation rate five years ahead, seasonally adjusted



Sources: Consensus Economics, Euro Zone Barometer, Reuters and ECB calculations.

The expectations of professional forecasters compiled in this survey can be compared with measures of inflation expectations derived from financial markets. The latter fell significantly in the course of 2010, but have rebounded again since December, albeit remaining at levels consistent with price stability. In fact, these measures incorporate not just the level of expected inflation, but also an additional premium to compensate bond investors for inflation risks. In general, they are also more volatile than survey-based measures, owing not only to the volatility of the inflation risk premium, but also to fluctuations in bond market liquidity conditions, particularly since the middle of 2008 (see Chart C).⁴ For these reasons, the volatility observed in these measures should not be interpreted mechanically as reflecting revisions in market participants' long-term inflation expectations.⁵

Real GDP growth expectations

The SPF respondents now expect euro area real GDP to grow by 1.6% in 2011. This represents an upward revision (of 0.1 percentage point) to their growth assessment for 2011 in the previous SPF round. Growth expectations for 2012 remain unchanged at 1.7% (see the table).

The SPF growth expectations for 2011 and 2012 are within the ranges reported in the December 2010 Eurosystem staff macroeconomic projections for the euro area and slightly above the latest Consensus Economics and Euro Zone Barometer forecasts for 2011 and 2012.

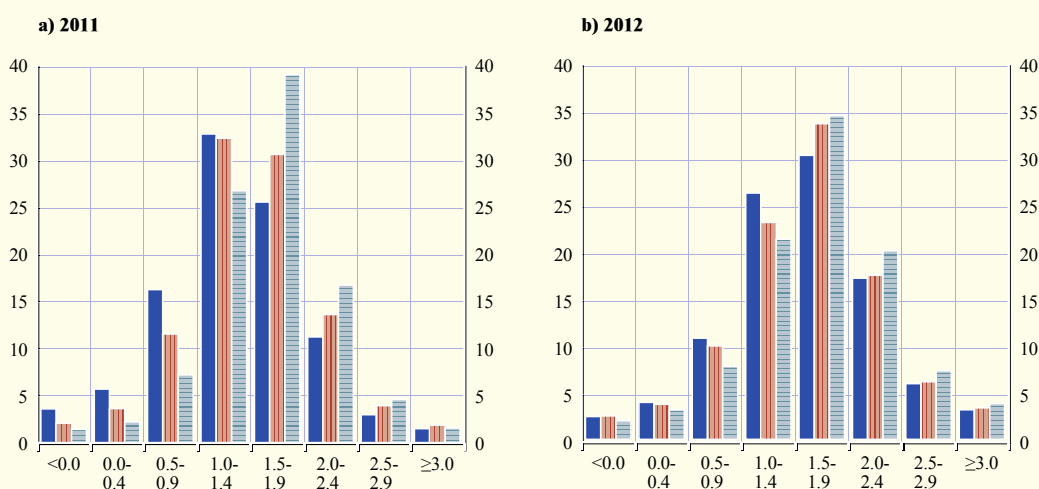
⁴ See also the article entitled "Measures of inflation expectations in the euro area", *Monthly Bulletin*, ECB, July 2006 and the article entitled "Inflation expectations in the euro area: a review of recent developments" in this issue of the *Monthly Bulletin*.

⁵ For further discussion on the impact of the financial market crisis on market-based measures of inflation expectations, see the box entitled "Recent increases in real yields and their implications for the analysis of inflation expectations", *Monthly Bulletin*, ECB, November 2008. Recent developments in financial market indicators of inflation expectations are discussed in Section 2.4 of the *Monthly Bulletin*.

Chart D Probability distribution for average annual real GDP growth in 2011 and 2012 in the latest SPF rounds¹⁾

(probability in percentages)

■ Q3 2010 SPF
■ Q4 2010 SPF
■ Q1 2011 SPF



Source: ECB.

1) Corresponds to the average of individual probability distributions provided by SPF forecasters.

The aggregate probability distribution for 2011 has shifted considerably towards higher outcomes, as respondents now assign a 39% probability to outcomes between 1.5% and 1.9%, and a lower probability (27%) to the range between 1.0% and 1.4%. With regard to 2012, the aggregate probability distribution has also shifted upwards compared with the previous SPF round, albeit to a smaller extent, and is also concentrated in the range between 1.5% and 1.9% (see Chart D).

The level of uncertainty surrounding one-year-ahead and two-year-ahead real GDP forecasts has not changed from the previous SPF round. The balance of risks to the average point forecast of real GDP growth is assessed to be on downside for both 2011 and 2012. According to respondents' comments, the main downside risks to the growth outlook are: i) stronger adverse effects stemming from ongoing fiscal consolidation and possible additional measures; and ii) the continued deleveraging and consolidation of the financial sector. In terms of upside risks, several respondents mention a further strengthening of domestic demand, both business investment and private consumption, particularly in Germany. Finally, respondents have different views on the risks to growth in the world economy.

SPF longer-term growth expectations (for 2015) have been revised slightly upwards to 1.9%. The SPF assessment is in line with that of the Euro Zone Barometer (January 2011 issue) and 0.2 percentage point higher than that of Consensus Economics (October 2010 issue). Looking at the individual probability distributions, the respondents assess the balance of risks for longer-term growth to be on the downside.

Expectations for the euro area unemployment rate

Unemployment rate expectations for 2011 have been revised slightly downwards by 0.1 percentage point, to 9.9%. Expectations for 2012 are unchanged at 9.6%. The balance of risks to expectations for both 2011 and 2012 is assessed to be on the upside. Longer-term unemployment rate expectations (for 2015) are unchanged at 8.3%, and the balance of risks to the longer-term outlook is again assessed to be on the upside.

Other variables and conditioning assumptions

According to other information provided by the respondents, they generally expect: i) oil prices to increase from around USD 91 per barrel in the first quarter of 2011 to around USD 93 per barrel in the fourth quarter; ii) average annual wage growth to be at 1.7% in 2011, rising gradually to 2.3% in 2015; iii) the euro to stand on average at USD 1.32 from the first to the third quarter of 2011 and to appreciate slightly to USD 1.33 in the fourth quarter; iv) the ECB's policy rate to remain stable at around 1.0% until the second quarter of 2011 and then to increase to 1.7% on average in 2012.