

Box 3

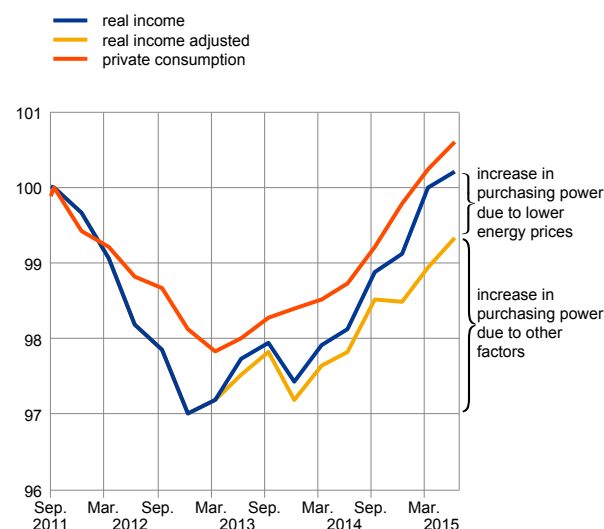
An assessment of recent euro area consumption growth

Private consumption has been continuously increasing since the first quarter of 2013, becoming the main driver behind the ongoing economic recovery in the euro area. This box examines the main driving factors behind these developments in euro area consumption growth since the first quarter of 2013, which was the latest trough to be experienced in the business cycle.¹

The decline in oil prices has been supporting private consumption growth, particularly since the second half of 2014. The purchasing power of households has increased by around 0.9 percentage point due to the fall in energy prices between the start of the recovery and the second quarter of 2015 (see Chart A).² Yet, this represented roughly only one-third of the overall improvement in households' purchasing power observed over this period. The additional improvement in purchasing power is mainly attributable to strong increases in labour income.³

Chart A
Energy and non-energy-related developments in real disposable income

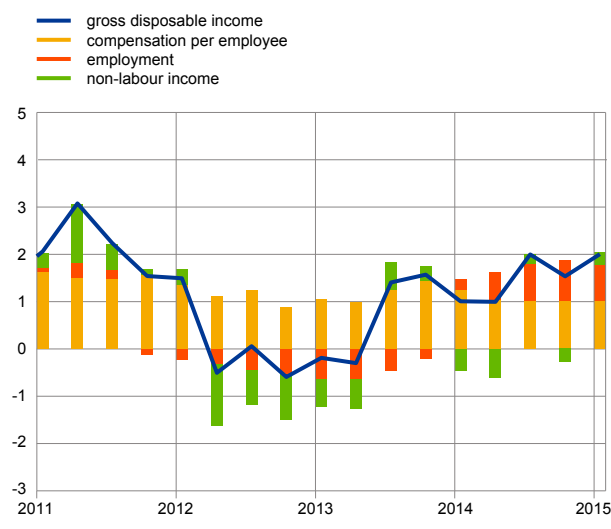
(index; Q3 2011 =100)



Sources: Eurostat and ECB staff calculations.
Note: Real income adjusted is calculated assuming constant real energy prices from the first quarter of 2013 onwards in order to approximate the "counterfactual" real disposable income that could have prevailed had oil prices not declined as observed.

Chart B
Gross nominal disposable income growth and contributions

(annual percentage changes; percentage points)



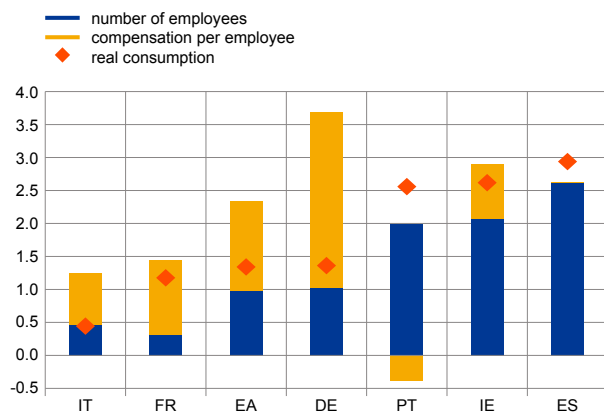
Sources: Eurostat and ECB staff calculations.
Note: Non-labour income constitutes operating surplus, property income, net social benefits and contributions, and direct taxes (inverted).

¹ As identified by the Centre for Economic Policy Research.
² Changes in the purchasing power of households due to fluctuations in energy prices are equal to the product of the energy expenditure share and the percentage rate of change in real energy prices.
³ Although the price of crude oil in EUR terms has declined by more than 40% since the second half of 2014, the decline in consumer energy prices was much lower. For example, the price of liquid fuels and fuels and lubricants for personal transportation declined by only 12% in the same period in the euro area.

Chart C

Labour income and private consumption across selected euro area countries

(percentage changes)



Sources: Eurostat and ECB staff calculations.

Note: Figures refer to average annual percentage changes between the second quarter of 2014 and the second quarter of 2015.

Private consumption has been supported by strong growth in real disposable income since the beginning of 2013, following gradual but steady improvements in the labour market. Growth of compensation per employee accelerated, albeit temporarily, in the second half of 2013. The negative contribution of employment growth to gross disposable income stabilised in early 2013 and improved steadily thereafter, turning positive in the first quarter of 2014 for the first time since 2011 (see Chart B). In line with this, the unemployment rate in the euro area stopped rising in 2013 and started to fall in 2014. Nevertheless, the current level of employment remains around 2% below its pre-crisis peak in 2008, while unemployment is still high at a rate of 11% last August.

Recent consumption growth has been higher in countries where labour markets have improved to a greater extent. In Spain, Ireland and Portugal the recovery of the labour market, in terms of both employment and wages, has been relatively strong, leading to higher increases in disposable income and real consumption growth (see Chart C). After years of households' deleveraging in these countries, higher disposable income is also helping to strengthen households' balance sheets (see Chart D). While consumption is growing, the leverage ratio continues to go down (except for France). This suggests there may now be a virtuous circle effect between a recovery in the labour market, increasing disposable income, and higher consumption growth, while the degree of household leverage continues to fall.

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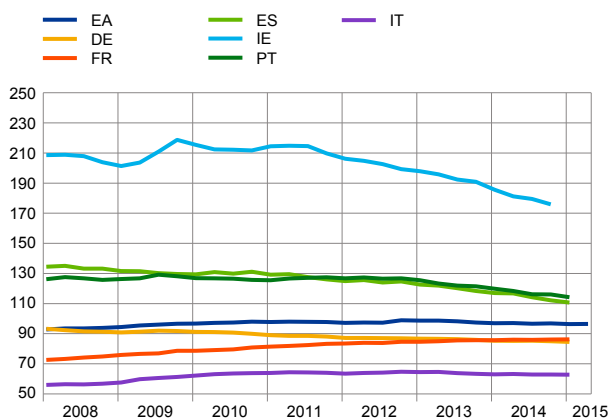
A comparison of consumption projections across several vintages of the ECB/Eurosystem staff macroeconomic projections for the euro area suggests that recent consumption developments have been broadly in line with expectations, once the oil price declines have been factored in. In

June 2014, prior to the observed sharp declines in oil prices, the Eurosystem staff macroeconomic projections envisaged moderate consumption growth of 0.7% in 2014, followed by a stronger recovery of 1.5% in 2015. Since then, consumption growth accelerated in the second half of 2014, and continued increasing steadily in the first half of 2015. This profile had already been envisaged in the March 2015 ECB staff macroeconomic projections, which was the first ECB staff exercise to account for lower oil prices that had proved more persistent than expected. This robust consumption growth projection remained unchanged in the September 2015 ECB staff macroeconomic projections, with a growth rate of 1.7% for 2015, against an outcome of 1.0% in 2014. This projection was also broadly confirmed by the latest data release for consumption growth in the second quarter of 2015.

Chart D

Household leverage across selected euro area countries

(as a percentage of disposable income)



Sources: Eurostat and ECB staff calculations.

Note: The leverage ratio is computed as the ratio of household debt over the four-quarter moving sum of disposable income.