

TECHNICAL ASSUMPTIONS

The Eurosystem staff projections are based on a series of assumptions about interest rates, exchange rates, oil prices and fiscal policies.

The technical assumption is made that short-term market interest rates and bilateral exchange rates remain unchanged over the projection horizon at the levels prevailing in the first half of November. Short-term interest rates as measured by the three-month EURIBOR are therefore assumed to remain constant at 2.28%. The technical assumption of constant exchange rates implies a EUR/USD exchange rate of 1.19 and an effective exchange rate of the euro that is 2% lower than the average for 2004.

The technical assumptions about long-term interest rates and both oil and non-energy commodity prices are based on market expectations in the first half of November. Market expectations for euro area ten-year nominal government bond yields imply a slightly rising profile, from an average of 3.5% in 2005 to an average of 3.7% in 2007. The increase in annual average non-energy commodity prices in US dollars is assumed to be 5.8% in 2005, 3.8% in 2006 and 5.2% in 2007. Based on the path implied by futures markets, annual average oil prices are assumed to be USD 60.0 per barrel in 2006 and USD 59.5 per barrel in 2007.

Fiscal policy assumptions are based on national budget plans in the individual euro area countries. They include all policy measures that have already been approved by parliament or that have been specified in detail and are likely to pass the legislative process. The cut-off date for updating the fiscal assumptions was 21 November 2005. This implies that the measures recently agreed in Germany have been taken into account in these projections.