

## Box 10

**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 assumptions about interest rates and both oil and non-energy commodity prices are based on market expectations in the two-week period ending 11 May. The assumptions about short-term interest rates as measured by the three-month EURIBOR are based on forward rates,<sup>1</sup> reflecting a snapshot of the yield curve at that point in time. These assumptions imply a rising profile, from an average of 3.1% in 2006 to an average of 3.9% in 2007. Market expectations for euro area ten-year nominal government bond yields imply a slightly rising profile, from an average of 4.0% in 2006 to an average of 4.3% in 2007. Based on the path implied by futures markets, annual average oil prices are assumed to be USD 70.3 per barrel in 2006 and USD 73.9 per barrel in 2007. The annual average increase in non-energy commodity prices in US dollars is assumed to be 27.6% in 2006 and 5.4% in 2007.

The technical assumption is made that bilateral exchange rates remain unchanged over the projection horizon at the levels prevailing in the two-week period ending 11 May. This implies a EUR/USD exchange rate of 1.27 and an effective exchange rate of the euro that is 0.7% higher than the average for 2005.

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 11 May 2006.

<sup>1</sup> For the first time, the Eurosystem projections are based on the technical assumption that short-term market interest rates move in line with market expectations rather than, as previously assumed, remain constant over the projection horizon. This change is of a purely technical nature. It was introduced in order to further improve the quality and the internal consistency of the macroeconomic projections and does not imply any change in the ECB's monetary policy strategy or in the role of projections within that strategy.