

## Box 5

## THE DEVELOPMENT OF PROJECTIONS FOR EURO AREA GROWTH IN 2009

This box reviews how projections for euro area growth in 2009 have developed since the beginning of 2008. It shows how much the outlook for 2009 has deteriorated over the past year and when the largest revisions were observed.

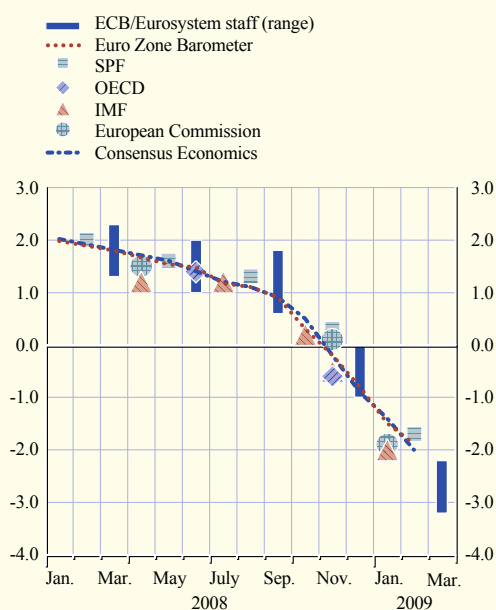
Chart A shows the development of projections for euro area growth for 2009 between the beginning of 2008 and the cut-off date for this issue of the Monthly Bulletin. It shows the projections of various institutions (namely the ECB/Eurosystem staff who produce projections that are expressed in terms of ranges, the European Commission, the IMF and the OECD) and private sector forecasters (i.e the Survey of Professional Forecasters (SPF), the Euro Zone Barometer and Consensus Economics). While the Euro Zone Barometer and the projections of Consensus Economics are issued on a monthly basis, the other projections are published less often. The ECB/Eurosystem staff macroeconomic projections for 2009 were published in March, June, September and December 2008, as well as in March 2009, while those of the SPF were available one month earlier on each occasion. The European Commission published its growth projections for 2009 in April and November 2008 and an interim forecast in January 2009. The projections of the IMF for GDP growth in 2009 were published in April, July and October 2008 and January 2009, with an exceptional forecast published in November 2008. The OECD projections for 2009 were available in June and November 2008.

Chart A shows that from early 2008 the outlook for euro area GDP growth in 2009 was revised downwards in all projections. While at the beginning of 2008 growth of around 2.0% was expected for 2009, projections in January and February 2009 ranged between -1.5% and -2.0%. The pace of the downward revisions was relatively modest in the first half of 2008, but then accelerated somewhat in October, with expected growth rates falling to zero between November and December in all projections. The timing and extent of the downward revisions partly reflect the frequency of updates and the production and publication dates of the individual forecasts.

The downward revisions to the economic outlook for 2009 clearly reflect the emergence of increasingly negative information on the economic situation. A number of factors may have played a role in the strengthening of the downward revisions from October 2008 onwards. Monthly indicators with a bearing on the current and short-term outlook for growth deteriorated markedly over 2008, particularly in the second half. Chart B shows developments

Chart A Development of projections for euro area growth in 2009

(annual percentage changes)



Sources: ECB, European Commission, IMF, OECD, Euro Zone Barometer and Consensus Economics.

Note: The dates on the x-axis correspond to the publication dates of the various estimates. The time span between the cut-off date for information used and the actual publication date varies across projections.

in the Purchasing Managers' Index (PMI) for manufacturing and services, along with year-on-year growth rates for industrial production and new orders. The deterioration in these indicators accelerated from September 2008 onwards, around the time of the deepening of the financial turmoil and Lehman Brothers' default.

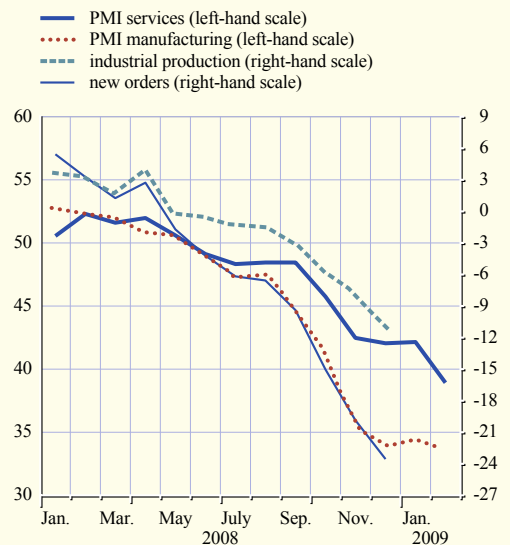
The revisions to the projected growth for 2009 were also partly related to the negative carry-over effect of the deteriorating outlook for the second half of 2008. This effect is defined as the impact that the pattern of growth recorded in the course of one year has on the annual average growth rate in the following year.<sup>1</sup> Unexpectedly weak data in the last quarter of 2008 have, therefore, also had a marked downward impact on annual growth expectations for 2009. With Eurostat estimating GDP growth of -1.5% for the fourth quarter of 2008, the carry-over effect on 2009 now amounts to -1.3 percentage points. It is worth noting here that had the estimate for the fourth quarter of 2008 been 1 percentage point higher (i.e. -0.5% rather than -1.5%), then the carry-over into 2009 would have been significantly less negative, at -0.5 percentage point rather than -1.3 percentage points, which illustrates the sensitivity of this carry-over effect to data releases late in the year.

Overall, the sharp falls in the projections for euro area GDP growth in 2009 – common across various different institutional and private forecasters – highlight the difficulty of anticipating economic developments in such an uncertain situation. Notably, the sharp falls observed in order books, trade and industrial production when the financial turmoil deepened had not been foreseen in mid-2008 and were, therefore, major contributors to the downward revisions of the different projections.

<sup>1</sup> See also Box 8 in the March 2005 issue of the Monthly Bulletin.

**Chart B PMI indicators, industrial production and new orders**

(left-hand scale: percentage balances; right-hand scale: annual percentage changes)



Sources: Eurostat and Markit.