Box 8

TECHNICAL ASSUMPTIONS ABOUT INTEREST RATES, EXCHANGE RATES, COMMODITY PRICES AND FISCAL POLICIES

The technical assumptions about interest rates and commodity prices are based on market expectations, with a cut-off date of 11 November 2010.[1] The assumption about short-term interest rates is of a purely technical nature. Short-term rates are measured by the three-month EURIBOR, with market expectations derived from futures rates. The methodology gives an overall average level for these short-term interest rates of 0.8% for 2010, 1.4% for 2011 and 1.7% for 2012. The market expectations for euro area ten-year nominal government bond yields imply an average level of 3.5% in 2010, increasing to 4.0% in 2011 and 4.3% in 2012. The baseline projection takes into account the recent further normalisation of financing conditions and assumes that bank lending rate spreads vis-à-vis the above-mentioned interest rates will remain broadly stable overall. Credit supply conditions are assumed to ease gradually over the projection horizon. As regards commodities, on the basis of the path implied by futures markets in the two-week period ending on the cut-off date, oil prices per barrel are assumed to average USD 79.5 in 2010, USD 88.6 in 2011 and USD 90.7 in 2012. The prices of non-energy commodities in US dollars are assumed to rise by 40.6% in 2010, followed by increases of 19.2% in 2011 and 2.3% in 2012.

Bilateral exchange rates are assumed to remain unchanged over the projection horizon at the average levels prevailing in the ten-working day period ending on the cut-off date. This implies a USD/EUR exchange rate of 1.34 in 2010 and 1.39 in 2011 and 2012, and an effective exchange rate of the euro that, on average, depreciates by 5.9% in 2010 before appreciating modestly by 0.8% in 2011.

Fiscal policy assumptions are based on individual euro area countries' national budget plans as available on 19 November 2010. They include all policy measures that have already been approved by national parliaments or that have been specified in detail by governments and are likely to pass the legislative process.

1 Oil and food price assumptions are based on futures prices up to the end of the projection horizon. For other commodities, prices are assumed to follow futures until the fourth quarter of 2011 and thereafter to develop in line with global economic activity.

1 The Eurosystem staff macroeconomic projections are produced jointly by experts from the ECB and the euro area NCBs. They are a biannual input into the Governing Council's assessment of economic developments and the risks to price stability. More information on the procedures and techniques used is given in "A guide to Eurosystem staff macroeconomic projection exercises", ECB, June 2001, which is available on the ECB's website. To reflect the uncertainty surrounding the projections, ranges are used to present the results for each variable. The ranges are based on the differences between actual outcomes and previous projections carried out over a number of years. The width of the ranges is twice the average absolute value of these differences. The method used, involving a correction for exceptional events, is documented in "New procedure for constructing Eurosystem and ECB staff projection ranges", ECB, December 2009, also available on the ECB's website.