

Box 6

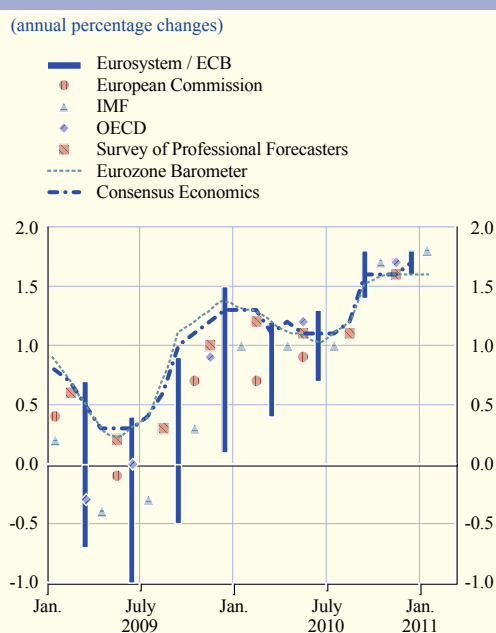
RECENT REVISIONS TO FORECASTS FOR ACTIVITY GROWTH

Since the recovery began in the second half of 2009, the pace of growth in activity has been faster than expected, prompting a series of upward revisions to GDP projections. This box looks at changes to external forecasters' and Eurosystem/ECB staff projections since the end of the recession and assesses some of the factors driving the upturn in euro area activity.

Growth is typically difficult to forecast around a turning point and the pick-up in growth since the end of the recession has surprised most forecasters (see Chart A). For example, the average projection for annual GDP growth in 2010 provided to Consensus Economics in June 2009 was 0.3%, while the Eurosystem staff projection was between -1.0% and 0.4%. The latest data from Eurostat puts year-on-year euro area GDP growth at 1.7% in 2010. Activity has been stronger than most forecasters expected in mid-2009 in all the large euro area countries (see Chart B). Forecasts from Consensus Economics in mid-2009 projected muted growth in 2010 in the three largest euro area countries and continuing falls in output in Spain and the Netherlands. The strength of the rebound in growth in Germany has caused particular surprise. By contrast, forecasters' expectations of continuing weakness in the Spanish economy proved to be closer to actual developments.

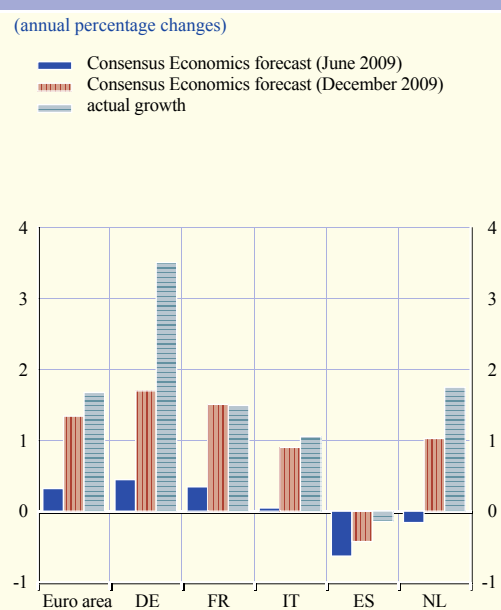
A major factor behind the swift recovery in euro area growth has been the rapid rebound in world trade, which boosted euro area foreign demand and exports. In mid-2009 the prevailing

Chart A Vintages of projections for annual GDP growth in 2010



Sources: Consensus Economics, ECB, Eurozone Barometer, IMF and OECD.

Chart B Projections for annual GDP growth in 2010 in the five largest euro area countries



Sources: Consensus Economics and Eurostat.

high uncertainty and the ongoing effects of the financial turmoil had been expected to continue to dampen global growth during the early stages of the recovery. Eurosystem staff macroeconomic projections in June 2009 were for modest growth in the euro area's export markets of around 1% in 2010 and export growth of between -2.0% and 1.0% in the same period.¹ However, the rebound in global trade proved to be much more dynamic than anticipated, with particularly strong growth in emerging markets. As global business and consumer confidence recovered and uncertainty diminished, previously postponed investments and purchases were taken up again, firms restored inventories, and trade picked up quickly. That benefited the euro area recovery: in 2010 growth in euro area export markets is estimated to have been around 12%, while euro area exports grew by nearly 11%.² Exports are also likely to have benefited from the depreciation of the euro effective exchange rate during 2010. Overall, net exports made a considerable contribution to GDP growth in 2010 (see Chart C).

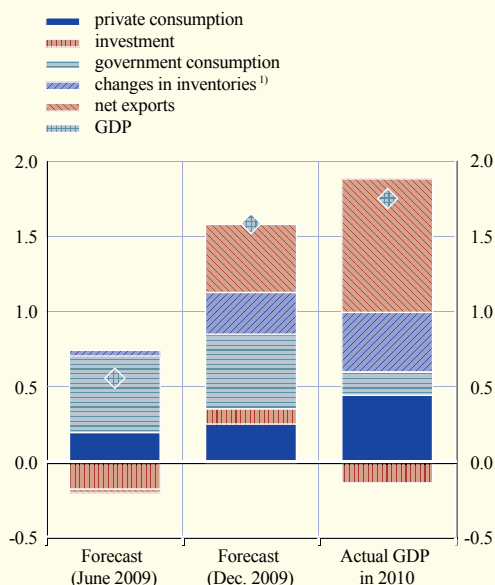
Domestic demand was also stronger in 2010 than had been expected. The uncertainty that prevailed during the depths of the recession receded relatively quickly and confidence picked up, as reflected by a modest increase in household spending and a decline in rates of saving. At the same time, the brighter prospects for domestic and global growth combined with the reduction in uncertainty prompted a sharp turnaround in the inventory cycle, which contributed strongly to growth in the early stages of the recovery.³

Overall, it appears that the series of upward revisions since the end of the recession were required mainly owing to stronger than expected global recovery. Indeed, it seems that a large part of the global downturn in 2008 and 2009 was only temporary, reflecting the strong rise in uncertainty following the sharp increase in tensions in financial markets, which led companies all over the globe to rescale or postpone investment. Projections at the time did not anticipate the temporary nature of part of the adjustment in late 2008 and early 2009 and thus underestimated the strength of the following global upturn in trade.

1 See "Eurosystem staff macroeconomic projections for the euro area", *Monthly Bulletin*, ECB, June 2009.
2 See the box entitled "ECB staff macroeconomic projections for the euro area" in this issue of the *Monthly Bulletin*.
3 See the box entitled "The current euro area recovery across expenditure components from a historical perspective", *Monthly Bulletin*, ECB, February 2011.

Chart C Contributions to euro area GDP growth in 2010 as projected by Consensus Economics

(annual percentage changes; percentage points)



Sources: Consensus Economics and ECB calculations.
Note: Contributions are calculated on the basis of projected annual growth rates for 2010 for components of demand, using current Eurostat figures for 2009 as the starting point.
1) Forecasters provide Consensus Economics with projections for private consumption, investment, government consumption, exports and imports. No projections for changes in inventories are provided. The projection for inventories in this chart is therefore calculated as the sum of the residual of the GDP projection and the contributions of the other components.