

Box 7

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 15 November 2012. 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 average level for these short-term interest rates of 0.6% for 2012, 0.2% for 2013 and 0.3% for 2014. The market expectations for euro area ten-year nominal government bond yields imply an average level of 3.8% in 2012, 3.6% in 2013 and 4.0% in 2014. Reflecting the path of forward market interest rates and the gradual pass-through of changes in market rates to lending rates, both short-term and long-term bank lending rates are expected to bottom out in 2013 and to rise gradually thereafter. Credit supply conditions are expected to weigh negatively on economic activity in the euro area in 2012 and 2013 and to be relatively neutral in 2014. As regards commodity prices, on the basis of the path implied by futures markets in the two-week period ending on the cut-off date, the price of a barrel of Brent crude oil is assumed to average USD 111.7 in 2012, USD 105.0 in 2013

and USD 100.5 in 2014. The prices of non-energy commodities in US dollars are assumed to fall by 7.5% in 2012 and by 1.5% in 2013, before increasing by 3.3% in 2014.¹

Bilateral exchange rates are assumed to remain unchanged over the projection horizon at the average levels prevailing in the two-week period ending on the cut-off date. This implies an exchange rate of USD per EUR of 1.28 throughout the projection horizon. On average, the effective exchange rate of the euro is assumed to depreciate by 5.5% in 2012 and by 0.9% in 2013.

Fiscal policy assumptions are based on individual euro area countries' national budget plans that were available on 23 November 2012. 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. The prices of other non-energy hard commodities are assumed to follow futures until the fourth quarter of 2013 and thereafter to evolve in line with global economic activity.