

Box 6

RESULTS OF THE ECB SURVEY OF PROFESSIONAL FORECASTERS FOR THE FOURTH QUARTER OF 2014

This box reports the results of the ECB Survey of Professional Forecasters (SPF) for the fourth quarter of 2014. The survey was conducted between 16 and 23 October 2014, and 61 responses were received.¹ Compared with the previous round, inflation expectations were revised downwards slightly further by between 0.1-0.2 percentage point. They currently stand at 0.5%, 1.0% and 1.4% for 2014, 2015 and 2016, respectively. Long-term inflation expectations were revised downwards by 0.06 percentage point to stand at 1.80%. Real GDP growth expectations were revised downwards by between 0.2-0.3 percentage point, to 0.8% for 2014, 1.2% for 2015 and 1.5% for 2016. Unemployment expectations remained stable for the short term but were revised upwards slightly for longer-term horizons.

Inflation expectations for 2014-16 revised further downwards

The SPF average point forecasts for inflation in 2014, 2015 and 2016 stand at 0.5%, 1.0% and 1.4%, respectively (see the table). The current low level of inflation is assessed to be driven by a combination of external factors (primarily the fall in oil prices, weak import prices and the lagged impact of the past appreciation of the euro) and domestic factors (ample excess capacity and rebalancing in some euro area countries). The expected pick-up in inflation is seen as being driven by a number of developments. In particular, these include ongoing, albeit moderate, economic growth, the recent depreciation of the euro and supportive monetary policy, as well as an expected stabilisation of, and even slight increase in, oil prices.

Compared with the previous survey round in the third quarter of 2014, there were downward revisions of between 0.1-0.2 percentage point for 2014-16. These downward revisions were broad-based, with around 85% of respondents revising down their forecasts for 2014 and 2015, and 60% doing so for 2016. The main factors cited as being behind these downward revisions were lower oil prices and weaker than expected economic activity. On the other hand, the depreciation of the euro was cited as a counterbalancing factor in these revisions.

Overall, the expected path of inflation for the period 2014-16 in the SPF for the fourth quarter of 2014 is slightly lower (around 0.1 percentage point) than that forecast in the September 2014 ECB staff macroeconomic projection exercise, whilst SPF expectations for 2014 and 2015 are exactly in line with the October 2014 Consensus Economics and Euro Zone Barometer surveys.

1. The survey collects information on expectations for euro area inflation, real GDP growth and unemployment from experts affiliated with financial or non-financial institutions that are based in the EU. Data are available on the ECB's website at www.ecb.europa.eu/stats/prices/indis/forecast.html/index.en.html

Results of the SPF, ECB staff macroeconomic projections, Consensus Economics and the Euro Zone Barometer

(annual percentage changes, unless otherwise indicated)

HICP inflation	Survey horizon			
	2014	2015	2016	Long-term ¹⁾
SPF Q4 2014	0.5	1.0	1.4	1.8
Previous SPF (Q3 2014)	0.7	1.2	1.5	1.9
ECB staff macroeconomic projections (Sep. 2014)	0.6	1.1	1.4	-
Consensus Economics (Oct. 2014)	0.5	1.0	1.3	1.9
Euro Zone Barometer (Oct. 2014)	0.5	1.0	1.3	1.8
Real GDP growth	2014	2015	2016	Long-term ¹⁾
	2014	2015	2016	Long-term ¹⁾
SPF Q4 2014	0.8	1.2	1.5	1.7
Previous SPF (Q3 2014)	1.0	1.5	1.7	1.8
ECB staff macroeconomic projections (Sep. 2014)	0.9	1.6	1.9	-
Consensus Economics (Oct. 2014)	0.8	1.2	1.5	1.6
Euro Zone Barometer (Oct. 2014)	0.8	1.2	1.6	1.6
Unemployment rate ²⁾	2014	2015	2016	Long-term ¹⁾
	2014	2015	2016	Long-term ¹⁾
SPF Q4 2014	11.6	11.3	10.9	9.5
Previous SPF (Q3 2014)	11.6	11.3	10.8	9.4
ECB staff macroeconomic projections (Sep. 2014)	11.6	11.2	10.8	-
Consensus Economics (Oct. 2014)	11.6	11.3	-	-
Euro Zone Barometer (Oct. 2014)	11.6	11.3	11.0	10.3

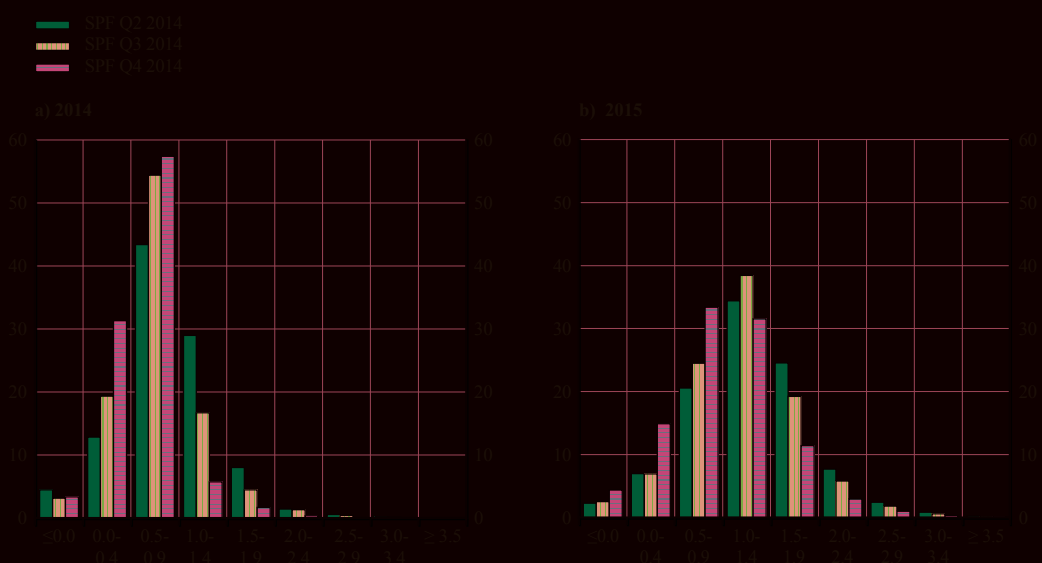
1) Long-term expectations refer to 2019 (2018 for the Euro Zone Barometer).

2) As a percentage of the labour force.

Turning to the aggregate probability distributions, compared with the previous SPF round, the means of the aggregate probability distributions for expected inflation in 2014-16 have shifted further towards lower outcomes (see Chart A). Whilst the most likely (modal) outcome has remained in the same bin for 2014 (i.e. 0.5-0.9%), it has shifted downwards for 2015

Chart A Aggregate probability distribution of average annual inflation expectations for 2014 and 2015 in the latest SPF rounds

(probability in percentages)



Source: ECB.

Note: The aggregate probability distribution corresponds to the average of individual probability distributions provided by respondents to the SPF.

(to 0.5-0.9%) and for 2016 (to 1.0-1.4%). According to survey participants, there is a relatively high probability of inflation remaining below 1% in 2015 (53%) and in 2016 (28%), however, the probability of negative inflation remains low: 3% for 2014, 4% for 2015 and 2.3% for 2016.

A comparison of the estimated mean of the aggregated probability distribution with the average of the point forecasts suggests that the risks to the baseline inflation outlook are generally perceived to be to the downside, and increasingly so over the forecast horizon.² The qualitative comments suggest that downside risks stem primarily from oil prices, weak economic activity and the possibility of inflation expectations becoming unanchored. However, the euro exchange rate and monetary policy actions are cited as sources of upward risk.

Longer-term inflation expectations for 2019 revised marginally downwards

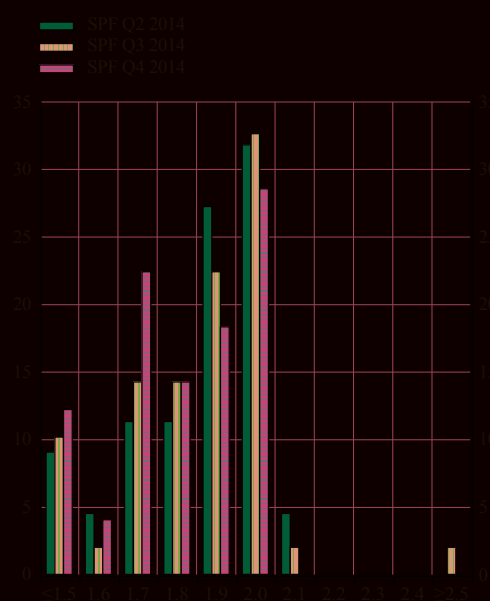
The average point forecast for longer-term inflation expectations (five-years ahead – 2019) declined by 0.06 percentage point (measured at two decimals) to 1.80%, from 1.86% in the previous round. Based on a balanced panel of respondents who participated in both of the last two rounds (41 of the 49 who gave long-term expectations in this round), four revised their longer-term expectations upwards and seven of them revised them downwards – and 30 were unchanged. The median of the point forecasts also declined to 1.8%, although the largest portion (29%) of respondents continues to provide a point forecast of 2.0% (see Chart B).

The long-term inflation expectations from the SPF are in line with the latest inflation expectations for 2018 from the October 2014 Euro Zone Barometer and are 0.1 percentage point below those for 2019 from the October 2014 Consensus Economics survey.

The aggregate probability distribution shifted towards lower outcomes compared with the previous SPF round. The probability of inflation being at or above 2.0% declined to 32%, from 36% in the third quarter of 2014, while the probability of inflation being below 1% increased to 12%, from 11% in the previous round. The probability of negative inflation rates remained low at 1.2% (up from 0.9%). On average, the balance of risks around the point forecast is assessed to be to the downside (as has been the case for the past four years), with the estimated mean of the aggregated probability distribution standing at around 1.7% compared with the mean point estimate of 1.8%.

Chart B Cross-sectional distribution of longer-term (five years ahead) inflation point forecasts

(percentage of respondents)



Source: ECB

2. The difference between the mean point estimate and the estimated mean of the aggregated probability distribution can be regarded as an indication of the direction and magnitude of the balance of risks perceived by SPF respondents to their forecasts. For more information on uncertainty measures, see the box entitled "Measuring perceptions of macroeconomic uncertainty", *Monthly Bulletin*, ECB, January 2010.

Disagreement over longer-term inflation expectations, as measured by the standard deviation of the point forecasts, decreased compared with the previous round. The aggregate uncertainty surrounding longer-term inflation expectations, as measured by the standard deviation of the aggregate probability distribution, also decreased slightly (see Chart C).

Real GDP growth expectations decreased for all horizons

The average point forecast for real GDP growth in 2014 and 2015 decreased by 0.2 percentage point, to 0.8%, and by 0.3 percentage point, to 1.2%, respectively, compared with the previous survey round. The corresponding forecast for 2016 decreased by 0.2 percentage point to 1.5% (see the table). These downward revisions were broad-based: for 2014 and 2015 around 90% of the respondents revised their forecasts downwards compared with the previous survey round. For 2016, two-thirds of the respondents lowered their forecast.

The qualitative comments provided by the respondents indicate that the downward revisions for 2014 were driven by disappointing figures for GDP growth in the second quarter, as well as persisting low business confidence in some euro area countries, and a more pessimistic outlook for key export markets.

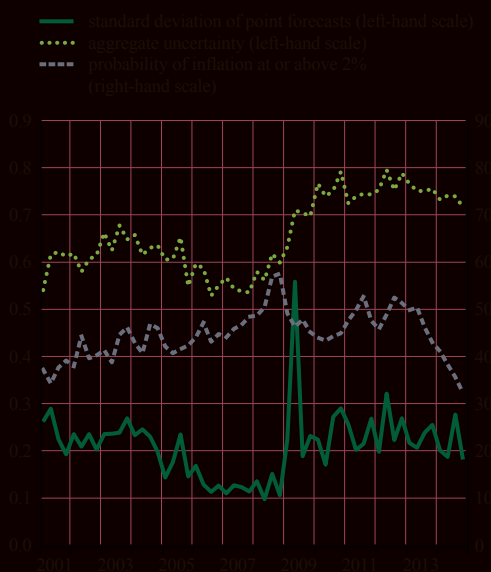
This survey round included an additional question as to whether the recent lower economic activity was expected to be a temporary phenomenon or part of a more sustained weakness in the economy. The respondents indicated that, so far, they regarded the fall in activity as a temporary phenomenon, although the responses suggested that the baseline forecasts were partly the result of recent geopolitical tensions translating into lower confidence and a wait-and-see attitude on the part of investors for the short-term horizon.

For 2014, the average SPF point forecast is 0.1 percentage point lower than the September 2014 ECB staff macroeconomic projections and 0.4 percentage point lower for both 2015 and 2016. Compared with the other survey results, the average SPF point forecast is in line with the October survey results from Consensus Economics and the Euro Zone Barometer (for real GDP growth) for 2014 and 2015, but slightly lower than the result from the Euro Zone Barometer for 2016.

The aggregate probability distributions have shifted towards lower outcomes for all horizons, but most notably for 2014 and 2015 (see Chart D). For 2014, respondents now assign the highest probability (59%) to the interval between 0.5% and 0.9%. For 2015, the highest probability (36%) continues to be assigned to the interval between 1.0% and 1.4%, compared with 31% before.

Chart C Disagreement and uncertainty about longer-term inflation expectations

(percentage points; percentages)

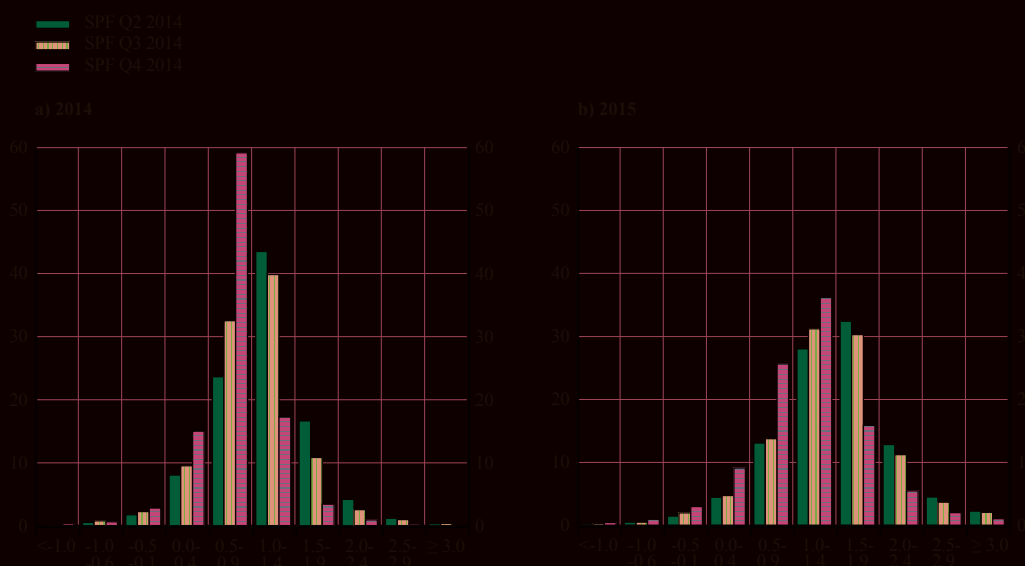


Source: ECB

Note: Aggregate uncertainty is defined as the standard deviation of the aggregate probability distribution (assuming discrete probability density function with probability mass concentrated in the middle of the interval).

Chart D Aggregate probability distribution of GDP growth expectations for 2014 and 2015 in the latest SPF rounds

(probability in percentages)



Source: ECB.

Note: The aggregate probability distribution corresponds to the average of individual probability distributions provided by respondents to the SPF.

The balance of risks has become more clearly tilted to the downside. The qualitative comments by the respondents identify geopolitical tensions, mainly in Ukraine and Russia, but also in the Middle East, as by far the main risk surrounding their forecasts (mentioned by two-thirds of the respondents). Other risks cited are lower than expected external demand (mainly from China and the United States) as well as inadequate progress with reforms in some euro area countries. However, respondents also see some upside risks, such as an unexpectedly quick recovery of exports, also driven by exchange rate developments, and a strong decrease in financial fragmentation in the euro area, leading to greater consumption and investment than assumed in the baseline.

Longer-term growth expectations decreased

Longer-term growth expectations, as measured by the average point forecast (for 2019), decreased by 0.1 percentage point to 1.7%. As in previous survey rounds, the SPF results for that horizon remain higher than the corresponding Consensus Economics and Euro Zone Barometer forecasts, which stand at 1.6%. The aggregate probability distribution of long-term growth expectations remains tilted to the downside.

Unemployment rate expectations stable for the short term but revised upwards for the longer term

The average point forecasts for the unemployment rate are 11.6% for 2014, 11.3% for 2015 and 10.9% for 2016, with the modest nature of the recovery seen as reducing unemployment only at a very slow pace. Compared with the previous round, expectations

for 2014 and 2015 have remained unchanged, while for 2016 they have been revised upwards by 0.1 percentage point (see the table).

The latest SPF expectations for the unemployment rate are in line with private sector forecasts for 2014 and 2015, but are 0.1 percentage point lower than the result from the Euro Zone Barometer for 2016. Compared with the September 2014 Macroeconomic Projection Exercise, the SPF expectations are slightly more pessimistic for 2015 and 2016, with expectations being 0.1 percentage point higher.

Risks to the short and medium-term baseline forecasts remain tilted to the upside and are related to a more modest recovery than anticipated. Additionally, some respondents saw the risks relating to a sustained period of low growth and low inflation as preventing firms from investing and thus from employing staff. Furthermore, it was mentioned that recent high cyclical unemployment could become structural if not addressed by more structural reforms, thus becoming potentially more persistent. Smaller downside risks to the unemployment outlook are mostly associated with stronger than envisaged effects of the implemented structural and labour market reforms and higher labour mobility across sectors and countries.

The average point forecast for longer-term unemployment rate expectations (9.5% for the reference year 2019) is 0.1 percentage point higher than in the previous SPF round. The aggregate probability distribution has shifted slightly towards higher outcomes compared with the previous SPF round.

Other variables and conditioning assumptions

Other information provided by the respondents (changes in their assumptions) implied significant downward revisions to the short-term interest rate, the oil price in US dollars and the euro exchange rate against the US dollar, while expectations for the growth rate of compensation per employee remained rather stable. The oil price is expected to average at USD 91.7 per barrel in the fourth quarter of 2014 and to increase gradually to USD 95.8 in the third quarter of 2015 and then further again to levels around USD 98.8 in 2016. The forecast for the euro exchange rate against the US dollar is significantly lower compared with the previous SPF round, and is now expected to stand at 1.27 in the fourth quarter of 2014 and then to gradually decline, to stand at 1.24 in the third quarter of 2015 and at 1.23 in 2016. Assumptions for growth in compensation per employee were revised downwards by 0.1 percentage point for this year and next year, standing at 1.3% year on year in 2014 and 1.5% in 2015, but remaining unchanged in 2016, at 1.8%. For the five-year ahead horizon, forecasters expect a slightly lower growth rate than anticipated in the previous survey round, of 2.1%. The mean assumption for the ECB's main refinancing rate is broadly flat for the next four quarters, implying a downward revision for the short term, but a more significant one for the medium term. It is assumed that it will stand at around 0.07% until 2015 and reach a level of 0.16% in 2016.