Box 2.3

Recent macroeconomic performance of the eurozone

The eurozone resumed growth since the second quarter of 2013 after a six-quarter recession amid the euro debt crisis. To fend off the deflation risk and revive the economy, the European Central Bank (ECB) announced in January 2015 an enlarged asset purchase programme. By analysing the recent economic performance of the eurozone, this note provides an update of ***Box 2.2*** in the ***2013 Economic Background and 2014 Prospects***, which covered the eurozone's situation up to the fourth quarter of 2013.

The recovery of the eurozone economy remained slow so far, with the quarter-to-quarter growth rate ranging only between 0.1% and 0.3% in the past seven quarters (***Chart 1***). For 2014 as a whole, real GDP saw disappointing growth of merely 0.9%. Analysed by GDP component, private consumption gained momentum over the course of 2014 (***Chart 2***) which was the key growth driver, followed by an improvement in the external sector. Yet, investment remained the weak spot though positive growth was resumed in 2014.

Chart 1 : Growth in the eurozone remained slow

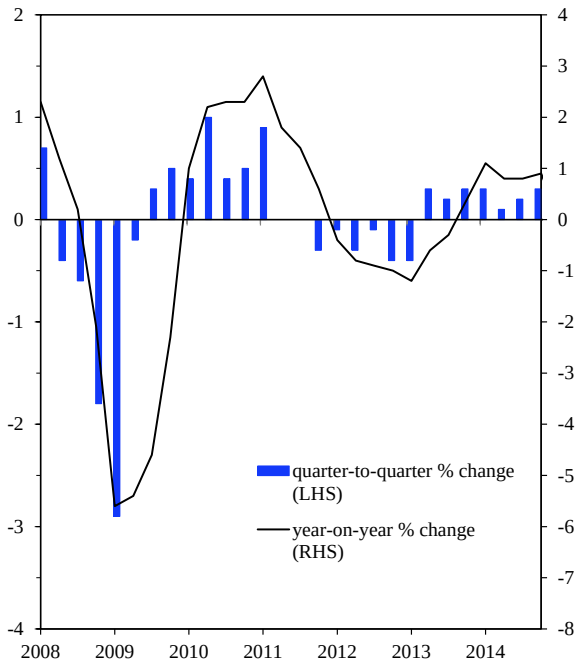
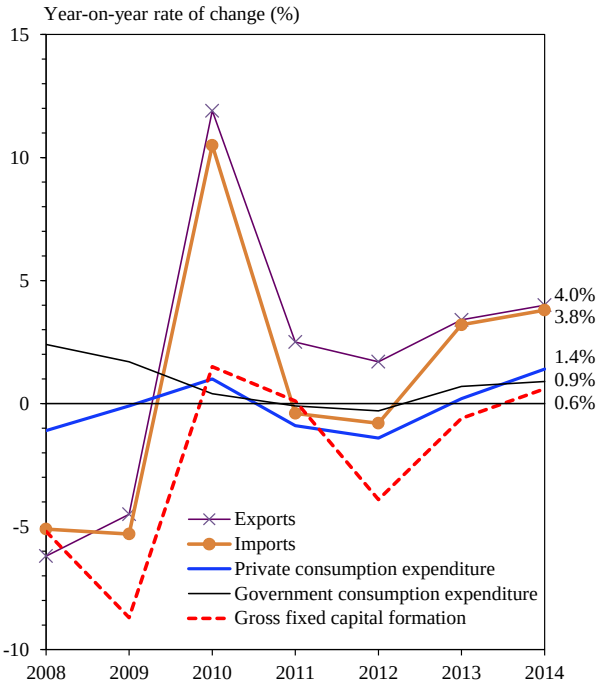


Chart 2 : Private consumption expenditure was the main growth driver in 2014



The eurozone economy showed some signs of improvement in early 2015, after the ECB's announcement of the new quantitative easing measures. PMIs rebounded in recent months and hovered at high levels, while retail sales and consumer confidence also improved in the first quarter (***Chart 3***). The slump in oil prices also raised real disposable income, adding tailwinds for the economy. Externally, trade surplus increased remarkably year-on-year in the first two months of 2015 (***Chart 4***). The depreciation of the euro, by some 12% against the US dollar during 2014, increased the price competitiveness of exports. Meanwhile, the ECB's loose monetary policy helped push borrowing costs to record low and revived credit demand gradually in recent months (***Chart 5***).

However, the recent improvement in some economic activity, fuelled largely by the ECB's monetary easing and the fall in oil prices, has yet to put the recovery on a firmer footing. For instance, industrial production in the region remained sluggish while Germany's factory orders grew only modestly of late (***Chart 6***). Most importantly, deflation risks in the region remain, CPI inflation though rebounded in recent months, was still at 0% in April. Excluding prices for energy, food, alcohol and tobacco, the core inflation, at 0.6%, also stayed well below the ECB's inflation target.

Box 2.3 (Cont'd)

Chart 3 : Consumption continued to grow along improving sentiment in early 2015

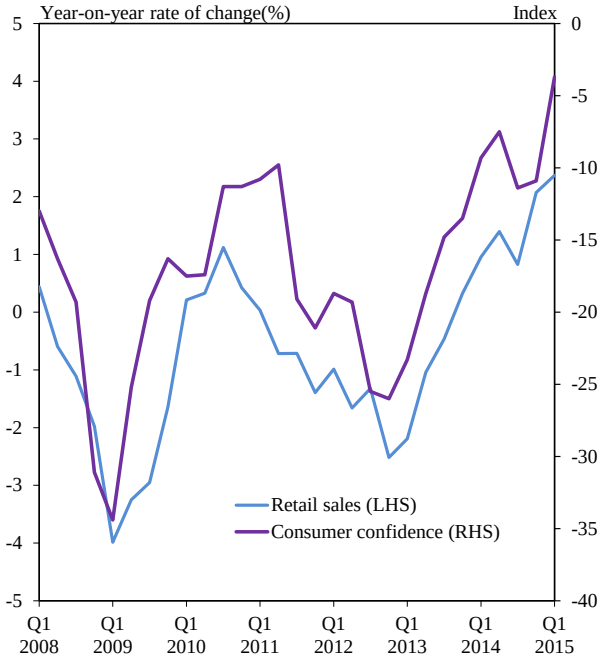


Chart 4 : Trade surplus improved

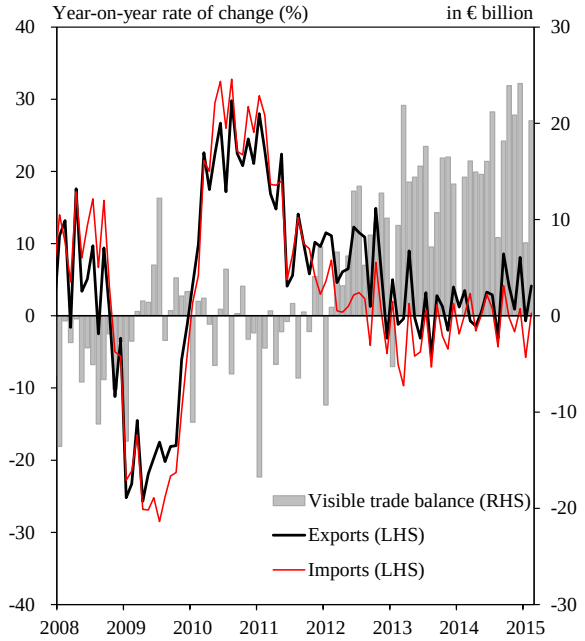


Chart 5 : Non-financial private sector loan resumed growth in early 2015

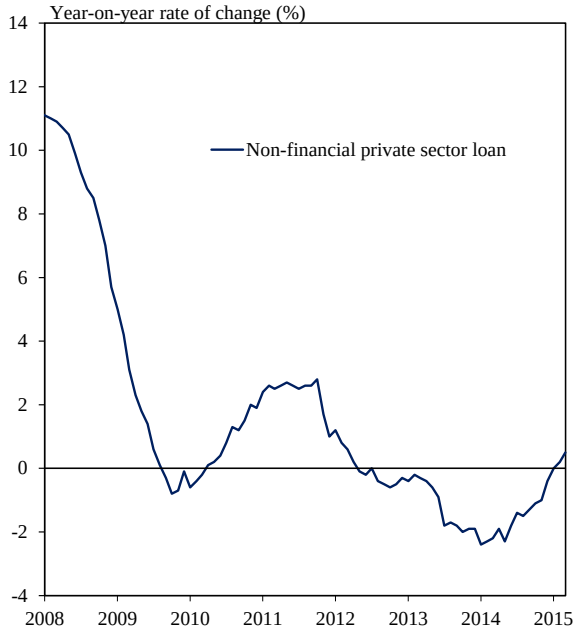
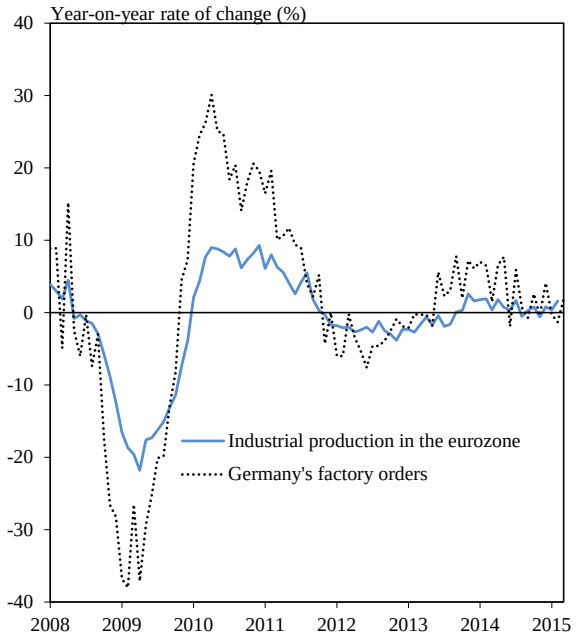


Chart 6 : Industrial production in the eurozone and Germany's factory orders remained sluggish



Indeed, the eurozone is still facing deep-seated structural problems. The heavy government indebtedness, staying at a high level of 92% of GDP for the eurozone as a whole, may also bring about short-term shocks to the region. The recent return of Greek debt issues is a vivid example. The elevated unemployment rate (at 11.3% in March) in the eurozone, especially that for the youth (at 22.7%), will continue to hamper growth dynamics. Thus reforms targeting at removing the rigidities in the labour markets, among other things, would also be needed for some member countries. Besides, geopolitical conflicts in Ukraine are also worrying.

In March, the ECB projected the region's real GDP to expand modestly by 1.5% in 2015, before growing by 1.9% in 2016 and 2.1% in 2017. Given the various challenges as discussed above, these forecasts are subject to a large degree of uncertainty.