

INTEGRATED EURO AREA ACCOUNTS FOR THE FOURTH QUARTER OF 2012¹

The integrated euro area accounts, released on 29 April 2013 and covering data up to the fourth quarter of 2012, offer comprehensive information on the income, spending, financing and portfolio decisions of institutional sectors in the euro area. The euro area's external balance improved further in the fourth quarter, mirroring an increase in the trade balance that arose from growing external demand and declining internal demand – largely driven by retrenching corporate sectors (both non-financial and financial) and government. Non-financial corporations (NFCs) remained in a net lending position (instead of their traditional expansionary net borrowing), with continued cutbacks in fixed investment and inventories, and still elevated (albeit declining) retained earnings. NFC margins fell to very low levels. Government deficits were reduced anew, reflecting resilient revenue despite contracting economic activity, and contained expenditure. Households' disposable income declined in nominal terms in the fourth quarter (and sharply in real terms, namely by 2.6%). Buffering the impact on consumption, consumers reduced their savings ratios sharply, to record lows. From a balance sheet point of view, households' net wealth declined slightly, while deleveraging by NFCs continued. Financial corporations' capital ratios increased significantly in the quarter, as a result of recapitalisation, high retained earnings and holding gains.

Euro area income and net lending/net borrowing

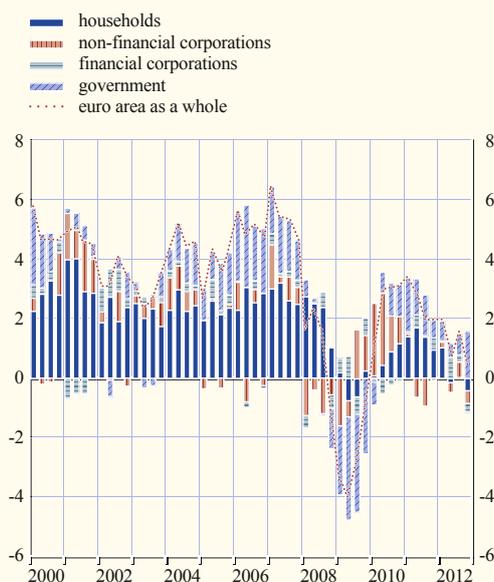
In line with slowing nominal GDP growth (and contracting real GDP), the rate of increase in nominal gross disposable income in the euro area declined to 0.6%, year on year, in the fourth quarter of 2012. Extensive sectoral rebalancing was observed: government income increased, while private sector income decreased (see Chart A).

With euro area consumption expanding less markedly than incomes (in particular, on account of declining government consumption), overall euro area gross saving increased slightly, year on year, in the fourth quarter of 2012. Savings (retained earnings) of both financial corporations and NFCs declined, year on year, as did those of households (the saving ratio fell sharply again, to a historically low level). The government sector, by contrast, reduced its dissaving significantly, with gross saving in the fourth quarter of 2012 turning slightly positive on a seasonally adjusted basis. Fixed capital formation declined in all sectors in the euro area, by 4%, all in all and year on year, in the fourth quarter of 2012. Investment by households, NFCs and governments contracted by 2.6%, 3.7% and 9.3% respectively. Destocking continued in the fourth quarter (in the amount of around €4 billion, seasonally adjusted). The year-on-year decrease in capital formation was more marked than that in fixed capital formation.

¹ Detailed data can be found on the ECB's website (available at <http://sdw.ecb.europa.eu>).

Chart A Gross disposable income in the euro area – contribution by sector

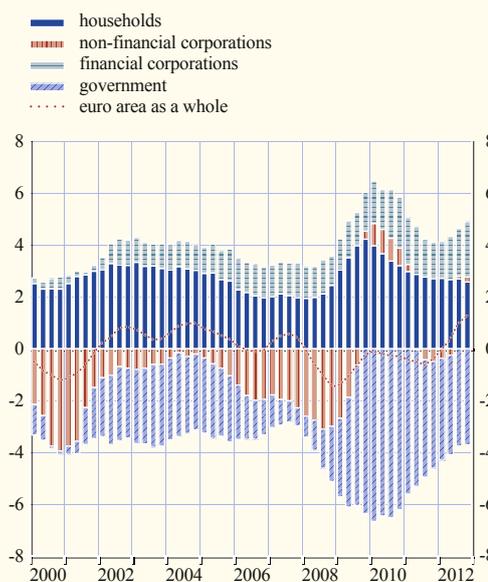
(annual percentage changes; percentage point contributions)



Sources: Eurostat and ECB.

Chart B Net lending/net borrowing of the euro area

(percentages of GDP; four-quarter moving sums)



Sources: Eurostat and ECB.

As capital formation decreased and savings increased slightly, the euro area's net lending position again improved markedly, to 1.2% of GDP on a four-quarter-sum basis in the fourth quarter of 2012, which corresponded to a rising current account surplus. From a sectoral point of view, this improvement reflected a reduction of the government deficit in seasonally adjusted terms, while households' net lending remained stable (although declining, year on year). Financial corporations' net lending rose to a record level (of close to 2.5% of GDP, seasonally adjusted, in the fourth quarter), notably as a result of capital transfers received, while that of NFCs decreased slightly (see Chart B). On the financing side, cross-border flows remained subdued, although non-residents stepped up their purchases of debt securities issued by euro area residents other than banks in the fourth quarter of 2012.

Behaviour of institutional sectors

In the fourth quarter, *households'* nominal income declined by 0.6%, year on year, after having increased by 0.1% in third quarter, impacted by a persistent and significant "fiscal drag" (net transfers by households to the government) that reduced income growth by 0.8 percentage point in the fourth quarter of 2012. At the same time, compensation of employees (notably that of government employees) and gross operating surplus/mixed income grew less strongly, thus contributing most to the decline in income growth (see Chart C). In real terms, households' income declined sharply again, namely by 2.6%, year on year. In order to cushion the impact on consumption, consumers continued to tap their savings. Their saving ratio fell sharply again, to a record low of 12.2%, seasonally adjusted (see chart D). Housing investment contracted in year-on-year terms, but less markedly than savings, so that households' net lending fell somewhat. Growth in both financing and financial assets continued to edge down, with ongoing portfolio

Chart C Households' nominal gross disposable income

(annual percentage changes; percentage point contributions)

- compensation of employees
- gross operating surplus and mixed income
- net property income
- direct taxes
- net social benefits and contributions
- real gross disposable income
- gross disposable income



Sources: Eurostat and ECB.

Chart D Households' income, consumption and saving ratio

(annual percentage changes; percentage of gross disposable income, seasonally adjusted)

- income growth (left-hand scale)
- ... nominal consumption growth (left-hand scale)
- saving ratio – seasonally adjusted (right-hand scale)



Sources: Eurostat and ECB.

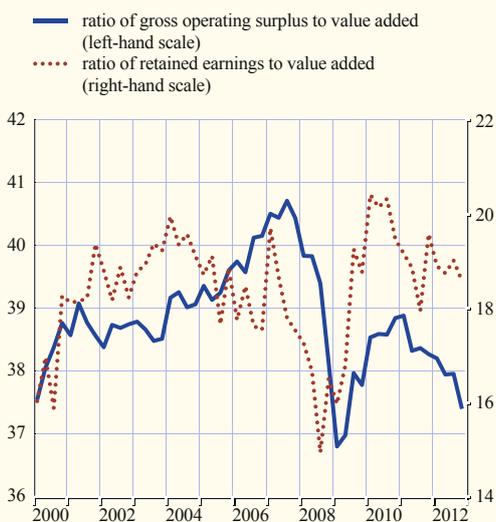
shifts into bank deposits, subdued additions to insurance technical reserves and disposals of debt securities. Household net wealth fell marginally, year on year, as net saving and gains on equity broadly offset holding losses on housing (see Chart G). Households' leverage ratios rose further to record highs.

The gross operating surplus of *NFCs* decreased anew (given that wages still rose faster than the value added), with business margins dropping to very low levels in the fourth quarter (see Chart E). Together with rising income taxes and net dividends paid, this led to a year-on-year decline in *NFCs*' savings (i.e. retained earnings), despite falling net interest paid and significant earnings on foreign direct investment. However, retained earnings remain elevated despite very low operating margins, due to low net interest paid, high earnings abroad, low (albeit rising) tax payments and low distributed dividends. Given the ongoing decline in fixed capital expenditure and destocking, *NFCs*' retained their unusual net lending position (see Charts B and F). With respect to their financing, *NFCs* favoured bond issuance (€115 billion) over the last four quarters, instead of using bank loans (-€107 billion, in part reflecting bank restructuring in Spain). Intra-sector lending (loans granted by other *NFCs* and trade credit, which is particularly important for small and medium-sized enterprises in buffering bank financing constraints) slowed. *NFCs* added further to their already ample liquidity buffers (which stood at €2.9 trillion). Deleveraging continued, also helped by higher prices on equity held.

Reflecting consolidation measures, the seasonally adjusted *government* deficit declined further in the fourth quarter (with net borrowing standing at 3.7% of GDP on a four-quarter-sum basis), owing to resilient revenues (taxes), despite contracting activity, and to contained expenditure.

Chart E Non-financial corporations margins

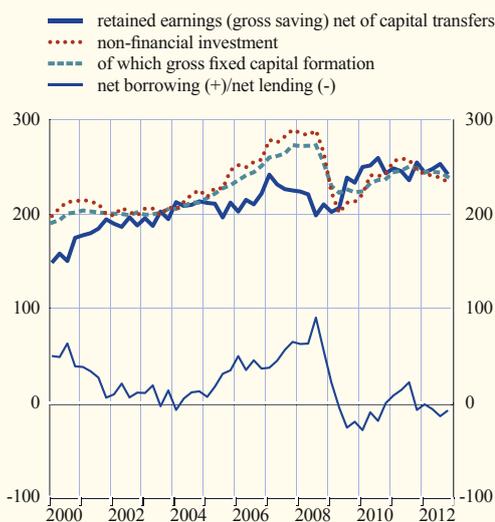
(percentages, seasonally adjusted)



Sources: Eurostat and ECB.
Note: Seasonal adjustment by the ECB.

Chart F Non-financial corporations' saving, capital investment and net lending(-)/net borrowing(+)

(EUR billions, seasonally adjusted)



Sources: Eurostat and ECB.
Note: Seasonal adjustment by the ECB.

Year-on-year growth of total expenditure (other than capital transfers) stabilised in nominal terms, with both compensation of employees and fixed capital formation declining by 1.8% and 9.3% respectively. As a result, government gross saving turned positive, on a seasonally adjusted basis, for the first time since the fourth quarter of 2008. Significant capital transfers were spent on the recapitalisation of banks in the fourth quarter of 2012. Government debt issuance continued to fund high deficits and significant increases in financial assets, which reflected, in particular, sizeable inter-government lending, the provision of capital for the European Stability Mechanism (€33 billion) and some bank recapitalisations (those treated as financial transactions). Debt securities issued by governments were bought by non-residents and investment funds.

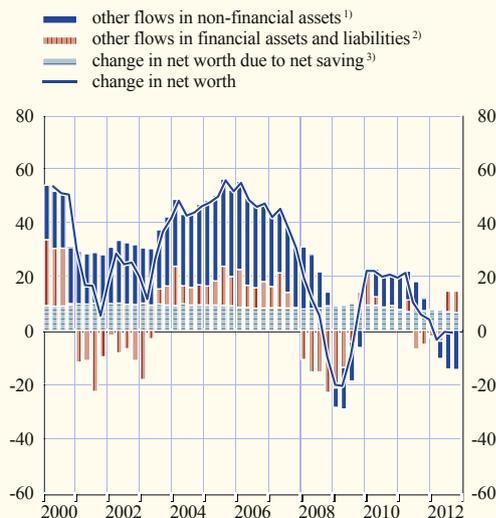
Although remaining at elevated levels, *financial corporations'* disposable income declined in the fourth quarter of 2012, reversing significant gains in previous quarters, as net dividends earned fell back and value added plus net interest earned continued to contract. Given still sizeable net retained earnings (€40 billion in the fourth quarter), significant recapitalisations – via capital transfers and injections of equity by the government (about €35 and €20 billion respectively) or equity issuance on the market (€33 billion) – and holding gains on assets, financial corporations' net assets at market value (an aggregate measure of their “capital”) rose sharply (see chart H). Additions to the balance sheets of financial corporations remained subdued on a consolidated basis.

Balance sheet dynamics

The net worth of households fell marginally, year on year, in the fourth quarter of 2012, namely by the equivalent of 0.3% of income (as opposed to increases in both 2010 and 2011, with a peak of 21.8% having been recorded in the second quarter of 2011). The positive influence of net saving (6.4% of income in the fourth quarter, after 6.9% in the third quarter) and of holding

Chart G Change in the net worth of households

(four-quarter moving sums; percentages of gross disposable income)



Sources: Eurostat and ECB.
 Note: Data on non-financial assets are estimates by the ECB.
 1) Mainly holding gains and losses on real estate (including land).
 2) Mainly holding gains and losses on shares and other equity.
 3) This item comprises net saving, net capital transfers received and the discrepancy between the non-financial and the financial accounts.

Chart H Capital ratios of financial institutions excluding mutual funds

(percentage of total assets)



Source: ECB.
 Note: In the chart, "equity" comprises shares and equity other than mutual fund shares. "Capital" is defined as the difference between financial assets and liabilities other than equity. Assets and liabilities are valued at market value. The ratio of "notional capital to assets" is calculated on the basis of transactions in capital and assets, i.e. excluding holding gains/losses on (changes in prices of) assets and liabilities.

gains on their financial portfolios (7.9% of income) broadly offset the significant holding losses (14.6% of income) on non-financial assets (i.e. housing) (see Chart G).

Financial corporations posted significant holding gains on their financial assets in the fourth quarter of 2012, both on equity holdings (recovering stock markets) and on debt securities held (falling bond yields). Overall, the portfolios of debt securities held generated holding gains for financial intermediaries, in the case of both sovereign debt and private debt for the year 2012 as a whole. This contributed to the sharp increase in financial corporations' capital ratios, as measured in the national accounts (net assets at market value) (see Chart H).