Box 3

INTEGRATED EURO AREA ACCOUNTS FOR THE FIRST QUARTER OF 2014[1]

This box discusses the integrated euro area accounts, released on 29 July 2014 and covering data up to the first quarter of 2014. The integrated euro area accounts offer comprehensive information on the income, spending, financing and portfolio decisions, as well as on the balance sheet positions, of institutional sectors in the euro area.

Summary of the main results

The euro area's external surplus reached a new historical high of 2.3% of GDP (four-quarter moving-sum) in the first quarter of 2014, after 2.2% in the previous quarter. This increase was mirrored in a roughly equal widening of the trade surplus as a result of both a modest increase in exports and a slight decline in imports (both expressed as a proportion of GDP). The high current level of net lending by the euro area reflects the on-going deleveraging of the non-financial private sector and weak internal demand, as well as fiscal consolidation that resulted in lower government deficits. Households' nominal income growth decelerated. Real income growth declined accordingly, but remained in positive territory, in a context of weak price dynamics. Households increased their consumption and maintained their saving rate at a very low level. Housing investment stabilised after two years of decline. Non-financial corporations (NFCs) increased their net lending position further, since the growth of fixed capital expenditure, which accelerated in year-on-year terms, was more than offset by a further increase in retained earnings and by some destocking. Business margins remained at very low levels. The government deficit declined to 2.9% of GDP, from 3.0% in the previous quarter, as year-to-year growth in government receipts exceeded spending growth despite a strong recovery in government investment expenditure.

Regarding developments in indebtedness, gross debt-to-GDP ratios remained at high levels for all euro area sectors, although they continued to decline marginally in the case of NFCs and households. However, the financial picture is more favourable according to leverage measures, such as the debt-to-assets, capital and net worth ratios. The debt-to-assets ratio of NFCs continued to decline significantly in the first quarter of 2014, in view of both continued net redemptions of MFI loans to firms and holding gains on equity. Financial corporations' headline capital ratios increased moderately further to stand at high levels. Households' net worth rose again in year-on-year terms on account of continued increases in security prices and moderating holding losses on real estate. The net external asset position of the euro area deteriorated slightly, after having improved moderately in the previous quarter. This deterioration mirrored valuation losses due to relative asset price and exchange rate changes which more than offset the positive net lending position of the euro area.

1 Detailed data can be found on the ECB's website (available at http://sdw.ecb.europa.eu/reports.do?node=1000002343).

Euro area income and net lending/net borrowing

In the first quarter of 2014, the annual growth rate in nominal gross disposable income in the euro area increased (to 1.7%, year on year), reflecting the recovery in real GDP growth. This acceleration benefited the government sector and financial corporations, while NFCs' income growth remained unchanged and that of households decelerated (see Chart A).

With euro area income growing slightly faster than consumption, gross savings in the euro area accelerated in the first quarter of 2014. While the household saving ratio declined to close to historical lows, NFCs increased their retained earnings and government savings again became less negative (on a four-quarter sum basis). Growth in euro area gross fixed capital formation turned positive (2.3% in year-on-year terms), as households' investment growth returned to positive territory (0.2%) and growth in NFCs' and the government sector's investment increased (3.9% and 8.1% respectively). The minor destocking observed in the fourth quarter of 2013 continued in the first quarter of 2014, implying that gross capital formation did not grow as fast as gross fixed capital formation.

With euro area capital formation increasing and savings accelerating, the euro area's net lending increased further in the first quarter, to 2.3% of GDP on a four-quarter-sum basis, the highest level recorded since the inception of the euro. From a sectoral point of view, this improvement was driven mainly by a decline in the government deficit, to 2.9% of GDP (four-quarter moving sum) (see Chart B). NFCs continued to show a net lending position. On the financing side, robust net purchases by non-residents of debt securities and equity issued by euro area residents point to positive foreign investor sentiment towards the euro area.

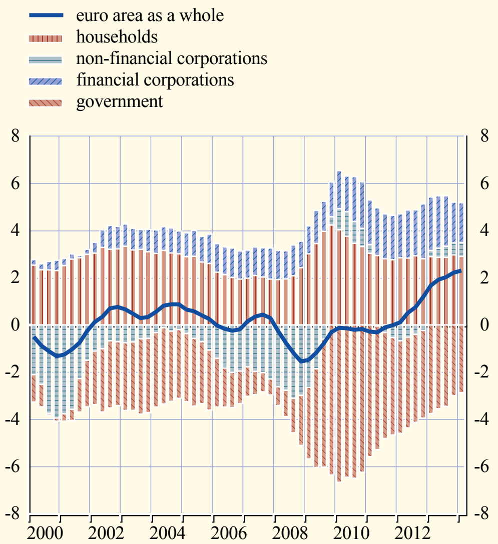
Chart A Gross disposable income in the euro area and contributions by sector

(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)



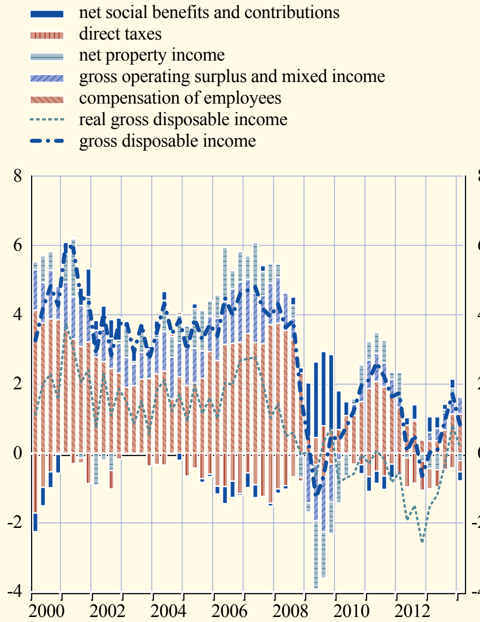
Sources: Eurostat and ECB.

Behaviour of institutional sectors

Households' nominal income growth decelerated in the first quarter of 2014 (0.8%, year on year, after 1.7% in the fourth quarter of 2013), despite a stable positive contribution from compensation of employees, some increase in that of self-employment income and a less negative contribution from direct taxes. The deceleration was driven by negative contributions from net property income and – for the first time since the end of 2011 – net social benefits received (see Chart C). In a context of weak price dynamics, real income growth remained positive, but declined to 0.2%, year on year, in the first quarter of 2014, after 0.8% in the fourth quarter of 2013. With nominal consumption recovering and outpacing income, the household saving ratio again decreased in the first quarter, to close to record lows (see Chart D). Housing investment growth returned to positive territory (0.2%, year on year) after two years of continuous decline, resulting in a decrease, on a four-quarter-sum basis, in households' net lending. Growth in household financing remained at very low levels in the first quarter of 2014, as borrowing from banks remained weak. On the assets side, households' financial investment reached a new historical low, reflecting still weak income growth and deleveraging needs in a number of countries. Households continued to allocate savings to life insurance and pension products and, to a lesser extent, to deposits and mutual fund shares, moving away from debt securities. The household leverage ratio declined as net worth increased further, year on year (see Chart I). The latter reflected continued gains on security holdings and higher net savings, which together exceeded moderating holding losses on real assets and, in particular, on real estate. The household debt-to-assets ratio also declined marginally (see Chart H).

Chart C Households' nominal gross disposable income

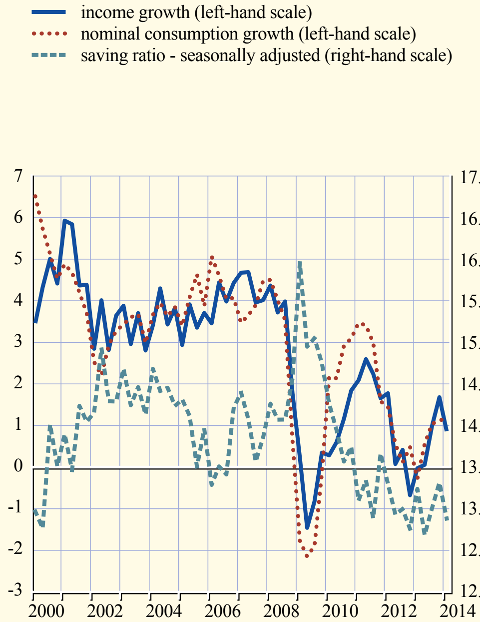
(annual percentage changes; percentage point contributions)



Sources: Eurostat and ECB.

Chart D Households' income, consumption and saving ratio

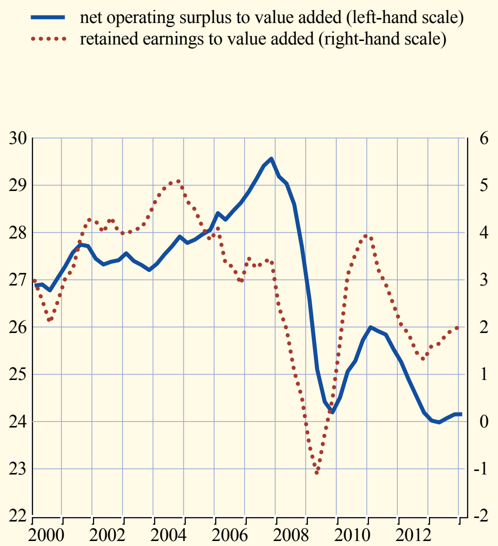
(annual percentage changes; percentages of gross disposable income, seasonally adjusted)



Sources: Eurostat and ECB.

Chart E Non-financial corporations' margins

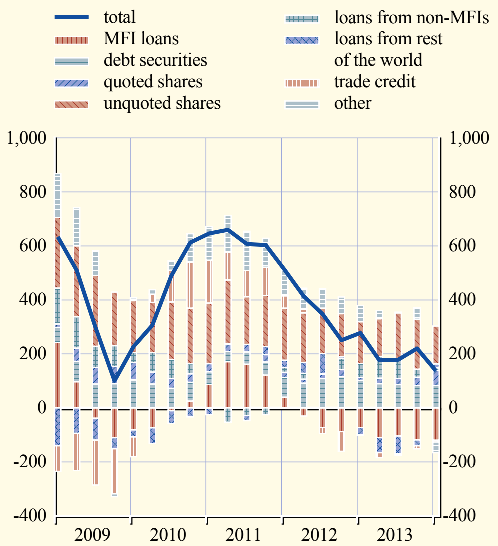
(percentages, four-quarter average)



Sources: Eurostat and ECB.

Chart F External financing of non-financial corporations

(in EUR billion; four-quarter sums)



Sources: Eurostat and ECB.
Notes: MFI loans and loans from non-MFIs (other financial intermediaries, and insurance corporations and pension funds) corrected for loan sales and securitisations. Other is the difference between the total and the instruments included in the chart.

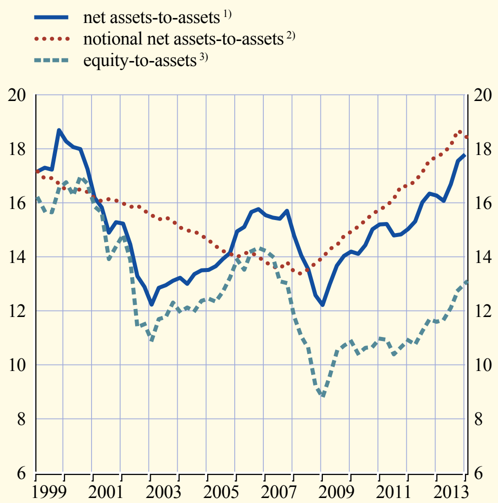
The growth of the gross operating surplus of *non-financial corporations (NFCs)* eased in the first quarter, to 1.6%, year on year, as value added growth decelerated while wages rose faster. Business margins, as measured by the ratio of the net operating surplus (i.e. net of consumption of fixed capital) to value added, moved sideways, remaining at a very low level (see Chart E). At the same time, a number of factors, including low (although stabilising) net interest paid and relatively low net dividends paid, continued to push up NFCs' savings (i.e. retained earnings). Gross fixed capital formation accelerated to 3.9%, in terms of year-on-year growth, although this was largely due to the very low level observed in the first quarter of 2013. The net lending position of NFCs increased further, owing to higher retained earnings and a decline in inventories that more than offset the growth of gross fixed capital formation. NFCs' external financing moderated in the first quarter of 2014 (see Chart F), largely reflecting a lower issuance of unquoted shares and other equity. The latter was partly explained by foreign IT firms transferring retained profits outside the euro area which, by statistical convention, are initially recorded under this instrument in firms' balance sheets. Trade credit remained weak, although it improved slightly. The weakness in intra-sectoral financing may be explained by firms using higher retained profits and deposit holdings to finance working capital. Issuance of debt securities remained buoyant and was supported by lower corporate bond yields. Together with equity issuance, it more than compensated for net redemptions of bank loans. Lending by non-MFIs and foreign entities was moderately positive, indicating that firms continued to issue bonds indirectly via conduits resident in other member countries and outside the euro area. NFCs' liquidity buffers remained at very high levels (€2.8 trillion), although they declined slightly from the previous quarter. The significant deleveraging process continued, helped by contracting bank loans and valuation gains on equity held by NFCs (see Chart H).

The *government* deficit continued to decline in the first quarter of 2014, to 2.9% of GDP on a four-quarter-sum basis. Growth in receipts increased further, standing at 2.8%, year on year. Excluding capital transfers to banks, year-on-year growth in government expenditure picked up somewhat to 2.0%. Final consumption expenditure grew by 1.6% and investment expenditure rebounded strongly, increasing by 8.1%, after having actually contracted since the fourth quarter of 2009.

In the first quarter of 2014, the year-on-year growth in the gross entrepreneurial income of *financial corporations* amounted to 7.6%, thus returning to positive territory for the first time since end-2011, as a result of both increases in value added and property income received, in particular dividends, and a slower growth of compensation of employees. Nevertheless, retained earnings moderated, reflecting the ongoing increase in the redistribution of profits to shareholders via dividends. A moderate, asset price-driven increase in the headline capital ratio masks a slowdown in the transaction-based accumulation of capital via retained earnings and equity issuance (see Chart G). The latter, however, is partly due to the restructuring of a multinational corporation, which resulted in a decline of equity. Excluding the effects of both the asset price developments and the corporate restructuring, the capital ratio declined by 0.1 percentage point on account of flat issuance activity and the moderation in retained earnings. The stock market valuation of the sector remains significantly below the market value of net assets, in spite of a slight correction of the difference during the quarter, reflecting continued market distrust. Growth of financial corporations' financial investment (excluding inter-MFI deposits and loans) decelerated further, reaching a new record low.

Chart G Capital ratios of financial institutions excluding mutual funds

(percentages of total assets)



Sources: Eurostat and ECB.
1) Assets and liabilities are valued at market value.
2) Calculated on the basis of cumulated transactions in net assets and assets, i.e. excluding holding gains/losses on assets and liabilities.
3) "Equity" comprises here "shares and other equity" other than "mutual fund shares". Interbank deposits and Eurosystem financing are netted out from assets and liabilities.

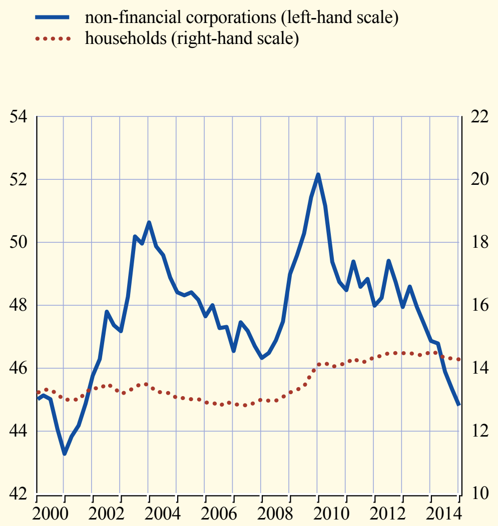
Balance sheet dynamics

In relation to developments in indebtedness, gross debt-to-GDP ratios continued to fall very slowly in the case of both NFCs and households in the first quarter of 2014, but remain at high levels. By contrast, financial sector and government indebtedness increased from the previous quarter. The picture is more favourable, however, when leverage measures, such as debt-to-assets and net worth ratios, are considered. Debt-to-assets ratios (including financial and non-financial assets) fell again in the private sector, although the pace varied from subsector to subsector. Government sector leverage increased. The international investment position (i.i.p.)[2] of the euro area showed a slight deterioration in the first quarter of 2014, to -18.0% of GDP, after -17.6% in the previous quarter. This deterioration mirrored valuation losses due to relative asset price and exchange rate changes that more than offset the positive net lending position of the euro area.

2 The i.i.p. measures the net asset position of residents vis-à-vis non-residents: assets net of liabilities (including equity).

Chart H Sectoral leverage

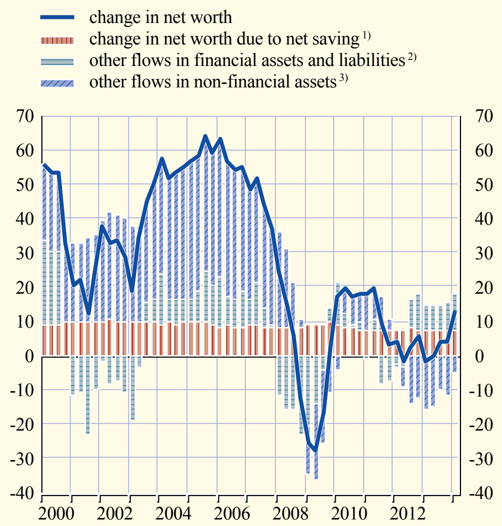
(percentages of total assets)



Sources: Eurostat and ECB.
Notes: Calculated as a ratio of total debt liabilities to total assets. Total assets comprise all financial assets and most non-financial assets.

Chart I Change in the net worth of households

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



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

The debt-to-assets ratio of NFCs declined further in the first quarter of 2014, to stand at 44.7%, which is 7.4 percentage points lower than the peak reached in early 2009 (see Chart H). The ongoing moderation is due both to continued net redemptions in corporate loans and to holding gains on equity. The net worth of households continued to rebound, again increasing on a year-on-year basis (12.8% of their annual income) (see Chart I). This improvement reflected holding gains on households' financial portfolios (amounting to 11.2% of their income) which mirrored the observed increases in stock and bond prices. Households' net savings also contributed positively to the increase in households' net worth (6.9% of their income). Together, the holding gains on financial assets and positive net savings more than compensated for moderating holding losses (-5.2% of their income) on non-financial (housing) assets. Financial corporations' headline capital ratios increased again, to stand at high levels (see Chart G).