Euro Area: Main Economic Indicators
(Percent change)

	2005	2006	2007	2008	2009	2010	2011	2012
							Staff projection	
Demand and Supply								
Real GDP	1.7	3.1	2.9	0.4	-4.1	1.8	2.0	1.7
Private consumption	1.8	2.1	1.7	0.4	-1.1	0.8	1.0	1.2
Public consumption	1.6	2.2	2.2	2.3	2.5	0.7	-0.1	0.0
Gross fixed investment	3.2	5.4	4.7	-0.8	-11.4	-0.8	3.7	2.8
Final domestic demand	2.1	2.8	2.4	0.5	-2.7	0.5	1.3	1.3
Stockbuilding 1/	-0.2	0.1	0.2	-0.2	-0.9	0.5	0.0	-0.1
Domestic Demand	1.9	3.0	2.6	0.4	-3.4	0.9	1.2	1.2
Foreign balance 1/	-0.2	0.1	0.2	0.1	-0.7	0.8	0.8	0.6
Exports 2/	5.1	8.6	6.3	0.9	-13.1	11.2	6.9	4.8
Imports 2/	5.8	8.5	5.8	0.8	-11.9	9.3	5.3	3.8
Resource Utilization								
Potential GDP	1.6	1.6	1.8	1.5	0.5	0.9	1.1	1.3
Output gap	-0.3	1.2	2.3	1.2	-3.5	-2.7	-1.9	-1.4
Employment	1.0	1.7	1.8	0.7	-1.9	-0.5	0.3	0.5
Unemployment rate 3/	9.1	8.4	7.6	7.7	9.5	10.1	10.0	9.6
Prices								
GDP deflator	2.0	1.9	2.4	2.1	1.0	0.8	1.4	1.6
Consumer prices	2.2	2.2	2.1	3.3	0.3	1.6	2.6	1.8
Public Finance 4/								
General government balance	-2.5	-1.3	-0.6	-2.0	-6.3	-5.9	-4.2	-3.3
General government structural balance	-2.7	-2.3	-2.1	-2.6	-4.3	-4.0	-3.0	-2.4
General government gross debt	70.1	68.5	66.3	69.9	79.4	85.5	87.8	88.3
Interest Rates 3/ 5/								
EURIBOR 3-month offered rate	2.2	3.1	4.3	4.6	1.2	0.8	1.4	…
10-year government benchmark bond yield	3.4	3.9	4.3	4.4	4.0	3.8	4.4	…
Exchange Rates 5/								
U.S. dollar per euro	1.24	1.26	1.37	1.47	1.39	1.33	1.4	…
Nominal effective rate (2000=100)	126.6	127.0	132.3	138.8	140.6	130.9	133.8	…
Real effective rate (2000=100) 6/	121.5	120.8	124.4	128.4	128.9	118.6	119.8	…
External Sector 4/ 7/								
Current account balance	0.1	-0.1	0.1	-1.5	-0.3	-0.4	0.1	0.3

Sources: IMF, *World Economic Outlook*; Global Data Source; DataStream; Eurostat; and ECB Monthly Bulletin.
1/ Contribution to growth.
2/ Includes intra-euro area trade.
3/ In percent.
4/ In percent of GDP.
5/ Latest available data for 2011.
6/ CPI based.
7/ Based on ECB data, which excludes intra-euro area flows.

This page intentionally left blank

Statement by Mr. Fayolle, Executive Director for France
on behalf of the Euro Area Authorities
July 18, 2011

In my capacity as President of EURIMF, I submit this Buff statement on the Article IV consultation with the euro area. It reflects the common view of the Member States of the euro area and the European Union in their respective fields of competence.

The authorities of the euro-area Member States are grateful for open and fruitful consultations with staff and for their constructive policy advice. The authorities welcome the staff's Spillover Report and broadly concur with its findings. The authorities also stress their commitment to free trade and the conclusion of the Doha round.

The authorities emphasise that the efforts to implement a comprehensive response to the ongoing debt crisis have been forcefully stepped up over the recent months. These new efforts include reinforced commitments to fiscal consolidation and structural reform, the macroeconomic adjustment programmes in several countries, strengthening financial mechanisms for countries in distress, rigorous stress tests of the banking and insurance sectors and improvements in economic and fiscal governance. In spite of these bold efforts market volatility remains high. In this context, the authorities reiterate their resolve to take all the necessary actions to preserve the integrity and stability of the euro area.

Short-term economic outlook

The economic recovery in the euro area continues to make headway, even though at a moderate pace. While the external environment continues to support exports, the recovery is broadening out, with domestic demand contributing increasingly to growth. However, there are considerable differences in the pace of recovery across the euro area Member States. Labour markets, which on average showed remarkable resilience during the crisis, stabilised in the course of 2010 and are set to improve gradually, but dispersion in unemployment rates remain high. The authorities share staff's view on the outlook. Economic growth in the euro area is expected to continue along a trajectory of around 2%. While investments contributed significantly to growth in the beginning of 2011, private consumption is expected to pick up modestly this year and its gradual recovery will be underpinned by slowly improving labour-market conditions, moderate income growth, and lower saving rates. Despite the positive prospects for economic growth in the euro area as a whole, uncertainty remains high and downside risks to the outlook are present.

Monetary policy and the outlook for price stability

The ECB early July decided to increase its key interest rates by 25 basis points, after having raised them by 25 basis points in April, in the light of upside risks to price stability. Inflation in the euro area is currently at 2.7% (June Eurostat flash estimate and May realisation), mainly reflecting higher energy and commodity prices. Looking ahead, inflation rates are likely to stay above 2% over the coming months. Risks to the medium-term outlook for price developments remain on the upside, in particular related to risks of higher than assumed

increases in energy prices. The underlying pace of monetary expansion is continuing to gradually recover, while monetary liquidity remains ample with the potential to accommodate price pressures in the euro area. Recent price developments should not give rise to broad-based inflationary pressures over the medium term, thus there is a need to keep inflation expectations firmly anchored in line with our aim of maintaining inflation rates below, but close to, 2% over the medium term. Upside risks to price stability will continue to be very closely monitored.

As regards the non-standard measures, the ECB in June decided to continue its refinancing operations as fixed rate tender procedures with full allotment in the third quarter of 2011. It furthermore suspended the application of the minimum credit rating threshold in the collateral eligibility requirements for bonds issued or guaranteed by the Portuguese government, as it had done before with Greek and Irish sovereign bonds. The provision of liquidity and the allotment modes for refinancing operations will be adjusted when appropriate, taking into account the fact that all the non-standard measures taken during the period of acute financial market tensions are, by construction, temporary in nature.

Fiscal policy

The authorities share staff assessment of the fiscal situation, in particular on the consolidation needs and the plans put forward by Member States to this end. Fiscal consolidation is a priority for the euro area as a whole, albeit with different degrees of urgency across the countries. Fiscal plans in the Stability Programmes broadly reflect this priority: they show considerable reduction in the general government deficit, with the euro area improving its fiscal positions every year, to reach an average deficit of 1.3% of GDP in 2014. Overall, the time profile of the consolidation plans is front-loaded and based mainly on expenditure reductions. Such a consolidation strategy will lead to halting and eventually reversing the increase in government debt as from 2012. The authorities agree that this hinges upon the rigorous and full implementation of the budgetary plans. Moreover, fiscal windfalls from higher than expected growth should be used for faster deficit reduction. Therefore, in the country-specific recommendation finalising the first European Semester, adopted by the Council last week, the Council called on Member States to take and implement all the measures planned and needed to ensure the achievement of their national fiscal targets and to comply with the recommendations under the excessive deficit procedure. This is essential to ensure trust by the public and markets in the sustainability of euro area public finances.

Financial stability mechanisms

Euro area Member States have significantly strengthened the stability mechanisms for countries in distress. It has been decided that the effective lending capacity of the temporary European Financial Stability Facility will be brought to € 440 bn, and a permanent European Stability Mechanism (ESM) has been agreed. The treaty which establishes the ESM was signed by euro are Member States on 11 July, and the ESM will be effective as from July 2013.

The main features of the ESM, including the conditions for granting assistance, were agreed and announced already in March 2011. If indispensable to safeguard the financial stability of

the euro area as a whole, the ESM may provide financial assistance to an ESM Member, subject to strict economic policy conditionality under a macro-economic adjustment programme, commensurate with the severity of the economic and financial imbalances experienced by that ESM Member. The ESM will have an effective lending capacity of € 500 bn. The Board of Governors may decide, as an exception, to arrange for the purchase of bonds of an ESM Member on the primary market, with the objective of maximising the cost efficiency of the financial assistance.

The ESM will enjoy preferred creditor status *vis a vis* all official and private creditors, other than the IMF, to which it will be junior. However, this seniority over creditors other than the IMF will not apply to loans made by the ESM in support of programs that had already received financial support from European countries as of the date of the signature of the ESM treaty. An adequate and proportionate form of private-sector involvement will be sought on a case by case basis where financial assistance is received by an ESM Member, in line with IMF practice. The nature and the extent of this involvement will depend on the outcome of a debt sustainability analysis and will take due account of the risk of contagion to other Member States and third countries. If it is concluded that a macro-economic adjustment programme can realistically restore public debt to a sustainable path, the beneficiary country will take initiatives aimed at encouraging the main private investors to maintain their exposure. If it is concluded that a macro-economic adjustment programme cannot realistically restore the public debt to a sustainable path, the beneficiary ESM Member shall be required to engage in active negotiations in good faith with its non official creditors to secure their direct involvement in restoring debt sustainability. In the latter case, the granting of financial assistance will be contingent on the ESM Member having a credible plan for restoring debt sustainability and demonstrating sufficient commitment to ensure adequate and proportionate private-sector involvement. Progress in the implementation of the plan will be monitored under the programme and will be taken into account in the decisions on disbursements.

Collective Action Clauses (CACs) will be included in the terms and conditions of all new euro-area government securities with maturity above one year from July 2013, in such a way as to preserve market liquidity and in a standardised manner which ensures that their legal impact is identical. The detailed legal arrangements for including CACs in euro area government securities will be finalised by the end of 2011.

Financial sector

The authorities are in the midst of an ambitious and intensive programme of regulatory reform for the financial services sector, which includes better supervision and regulation for financial services, greater consumer and investor protection, and the development of appropriate mechanisms for crisis management. At the same time, fostering and deepening the single market for financial services remains a central policy objective.

The establishment on January 1, 2011 of the new supervisory framework marked a major step in the implementation of the reform agenda. The authorities welcome the European Financial Stability Framework Exercise and its findings. The authorities think that the track