



QUARTERLY EURO AREA AND EUROPEAN UNION ACCOUNTS FOR INSTITUTIONAL SECTORS (EUROPEAN SECTOR ACCOUNTS)

Detailed analysis for the period 1999Q1 – 2006Q4

Published on 1 June 2007

European sector accounts show detailed economic developments by institutional sector. At present, the accounts are only calculated at current prices (in nominal terms) and do not yet permit an analysis of volume changes such as economic growth or price developments (such as inflation).

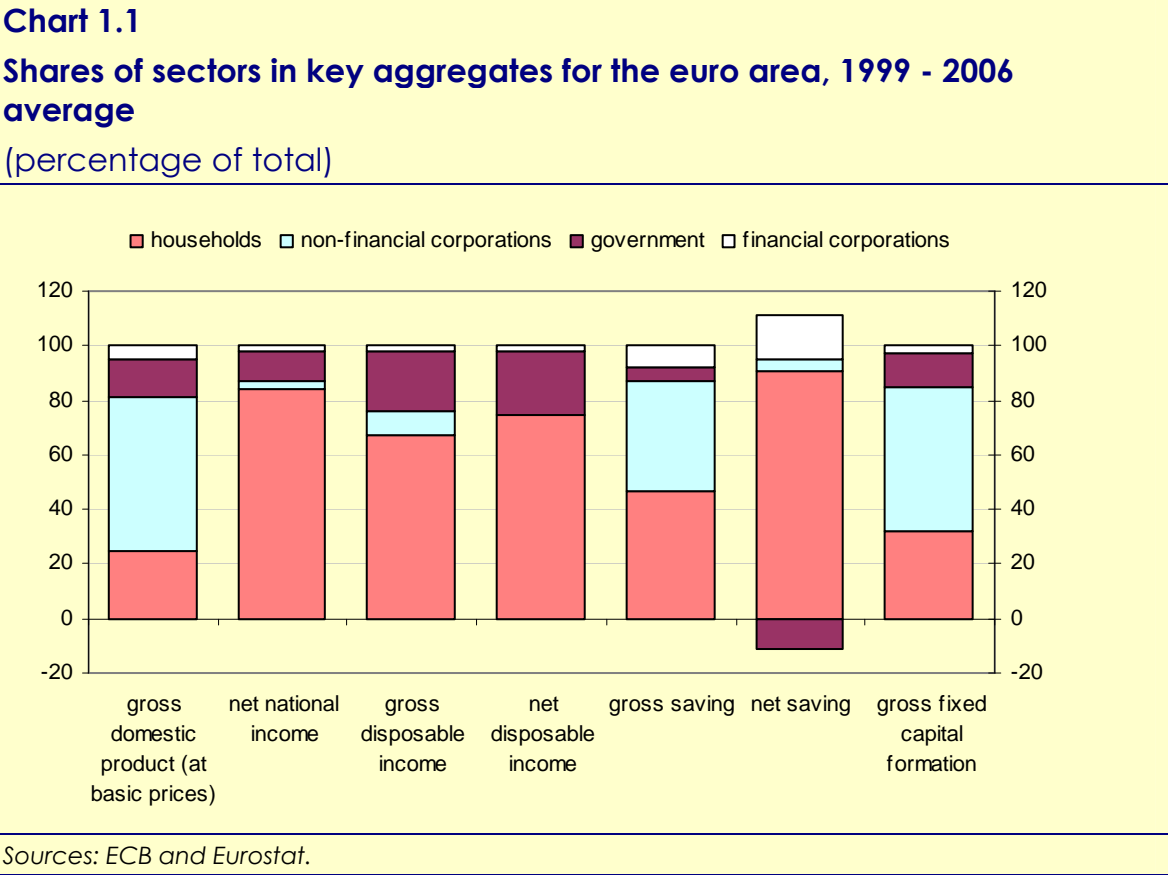
The charts included in this section present some salient characteristics of the euro area/EU economy as a whole, as well as specific features of the households and non-financial corporations sectors.

Data for the European Union are only presented when there is a limited impact of exchange rate movements of the euro against other European currencies.

Most of the charts analyse the contributions of components to the annual growth rate of an aggregate. Such annual growth rates are calculated as the percentage change of the item concerned between the reference quarter and the same quarter of the previous year, so that seasonal effects are eliminated. As a consequence, the growth rates for a given quarter in fact refer to the average change over the four previous quarters.

1. Overview of the relative economic importance of the institutional sectors

Chart 1.1 shows the structural shares of each institutional sector in several key economic indicators for the euro area. A chart for the European Union would reveal similar features.



The biggest share of GDP originates in non-financial corporations (on average 57% in the period 1999-2006), while slightly less than one-quarter is generated by household production activities, including the imputed value of the services from owner-occupied dwellings. The government accounts for 14% of GDP. Most value added created in the corporate and government sectors is passed on to households in the form of wages, salaries and employers' social contributions. The dominant share of national income thus accrues to the household sector. Subsequently, this share is somewhat reduced by means of taxes, net social insurance payments and other transfers, which are largely paid to the government. This results into the disposable income, which is available for consumption or saving. Both households and government spend a large proportion of their disposable income on consumption. As a result, the share of households and government in saving is smaller and the share of financial and non-financial corporations is larger than their shares in disposable income. Net saving of the government is negative. For non-

financial corporations, disposable income broadly equals their gross saving, which is broadly equivalent to retained earnings plus depreciation allowances in business accounting. Households and non-financial corporations undertake most of the gross fixed capital formation (32% and 53% respectively).

2. Contributions of each institutional sector to the macroeconomic developments

Chart 2.1 shows the contribution of each sector to the annual nominal growth rate of euro area gross value added (GVA) at basic prices (which is equal to GDP at market prices minus taxes plus subsidies on products). The gross value added of non-financial corporations delivers not only the largest contribution to GDP growth, but it is also quite volatile. The contribution of value added generated in the household sector fluctuates less, partly because of the stabilising influence of the imputed rent on owner-occupied dwellings. The contributions of the financial corporations and government sectors are rather small.

Although in the past year the growth of nominal euro area GDP has picked up from the trough between 2002 and the end of 2005, with the exception of an upswing in late 2003 and early 2004, it has not reached the growth rates of the beginning of this century.

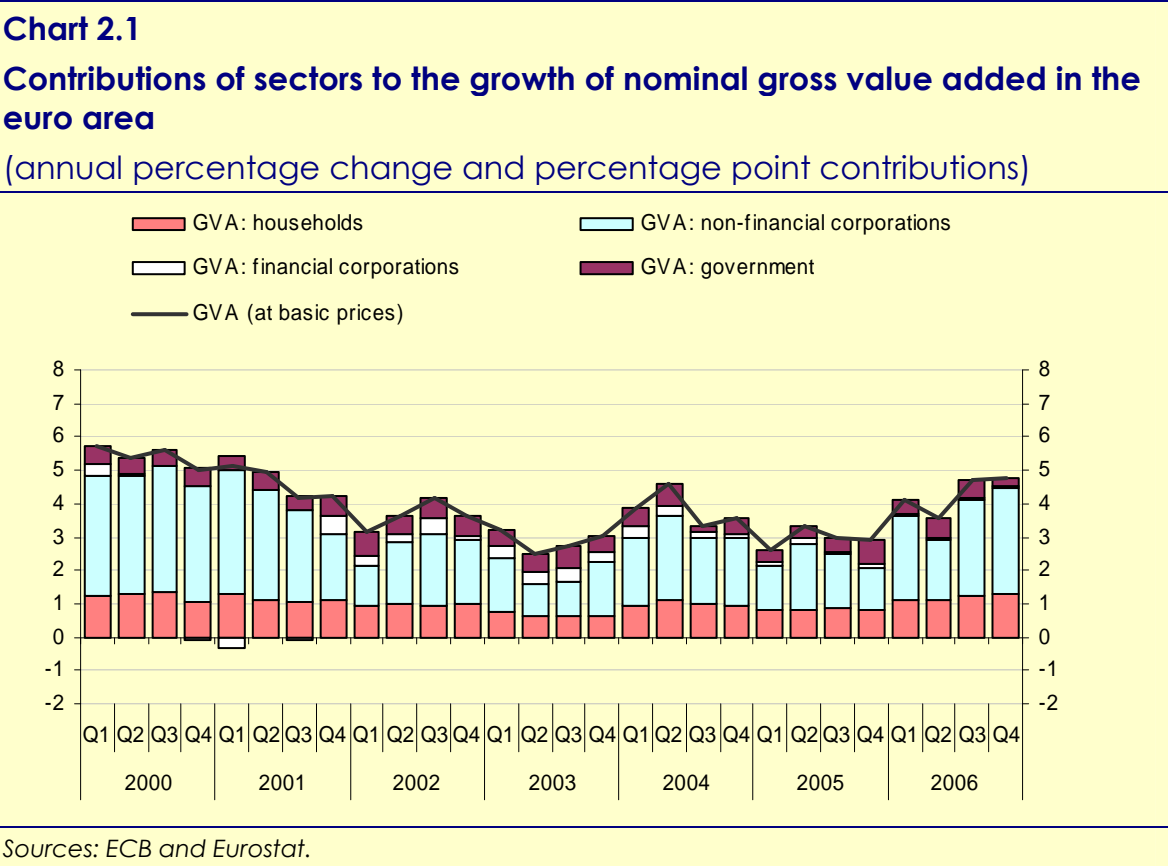
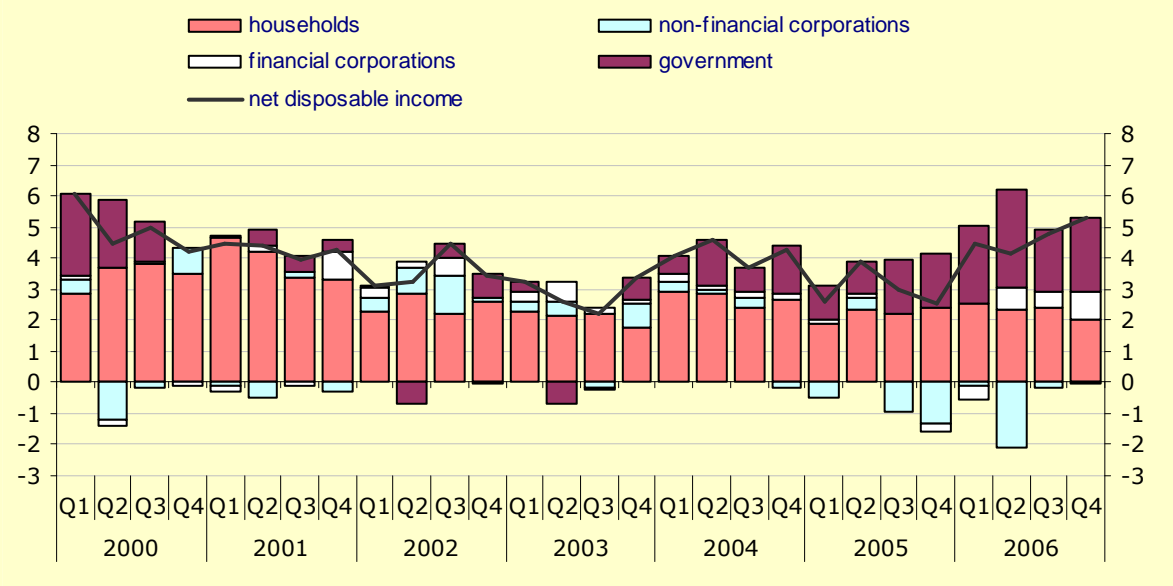


Chart 2.2 shows that the contribution of the government sector to the growth of euro area gross disposable income was generally higher in years with a higher overall growth rate, reflecting developments in tax earnings and changes in the balance of social security contributions and payments, such as unemployment insurance premiums and benefits. The contribution of households to the growth of disposable income was the highest at the beginning of the period shown in this chart.

Chart 2.2
Contribution of sectors to the growth of nominal net disposable income in the euro area

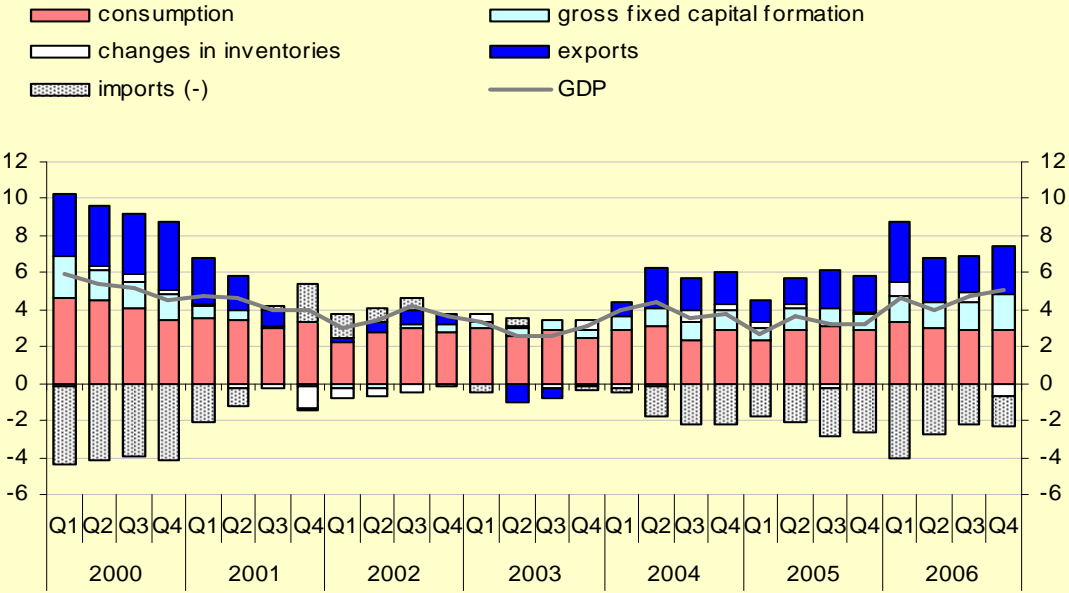
(annual percentage change and percentage point contributions)



Sources: ECB and Eurostat.

Chart 2.3 presents the decomposition of euro area GDP growth rates by expenditure components. If domestic demand is fulfilled by imports, this implies less domestic production and thus a lower GDP. In turn, if imports decline, which happened in most of 2002, this provides a positive contribution to GDP growth. Consumption growth provides a relatively stable contribution to GDP growth, although it has been most buoyant at the beginning of this century. The contributions of investment (gross fixed capital formation) and changes in inventories fluctuate over the business cycle.

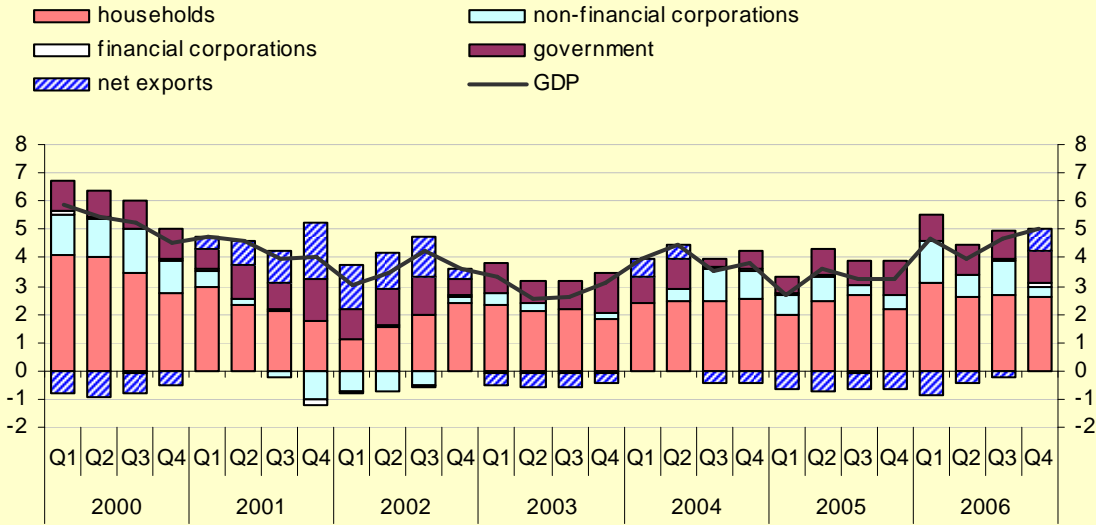
Chart 2.3
Contributions of expenditure components to the growth of nominal GDP in the euro area
 (annual percentage change and percentage point contributions)



Sources: ECB and Eurostat.

Chart 2.4 shows the contributions of the individual sectors' total final expenditures (consumption and capital formation) to the growth rate of euro area GDP. The household sector contributes most (mainly through its final consumption). In most of 2002, the non-financial corporations reduced their investment and thus provided a negative contribution to GDP growth.

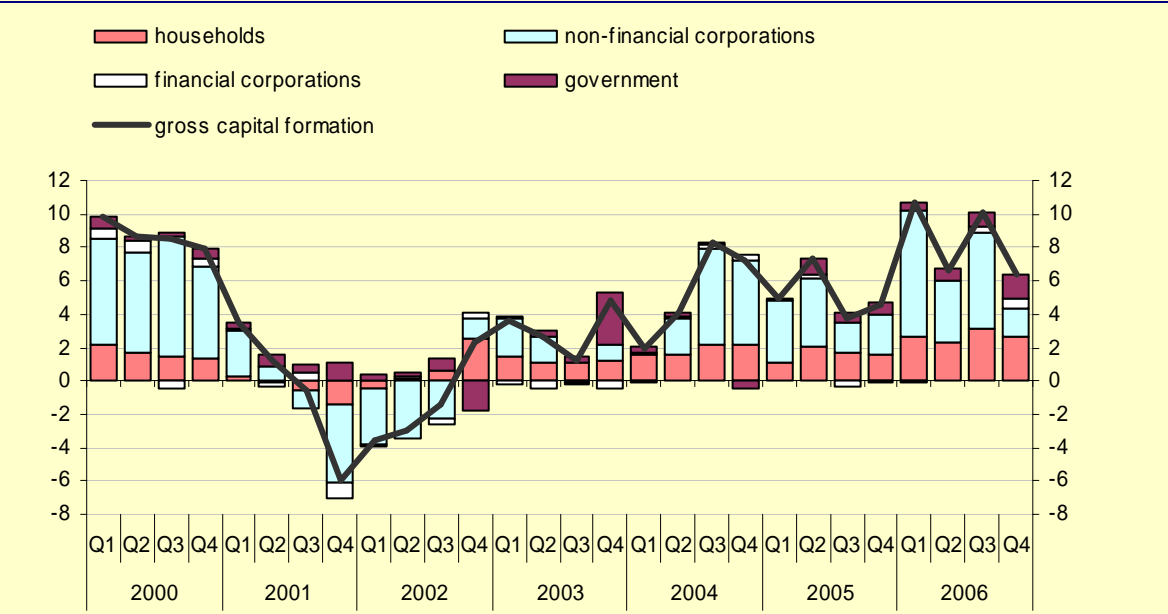
Chart 2.4
Contributions of expenditures by sector to the growth of nominal GDP in the euro area (annual percentage change and percentage point contributions)



Sources: ECB and Eurostat.

The **growth rate of euro area capital formation** (in current prices) declined sharply between 2000 and 2001, became very negative by the end of 2001, and picked up again afterwards (see **Chart 2.5**). To a very large extent, this reflects developments in the non-financial corporations sector. The contribution of the households sector remained more stable and was positive in all quarters except at the junction between 2001 and 2002.

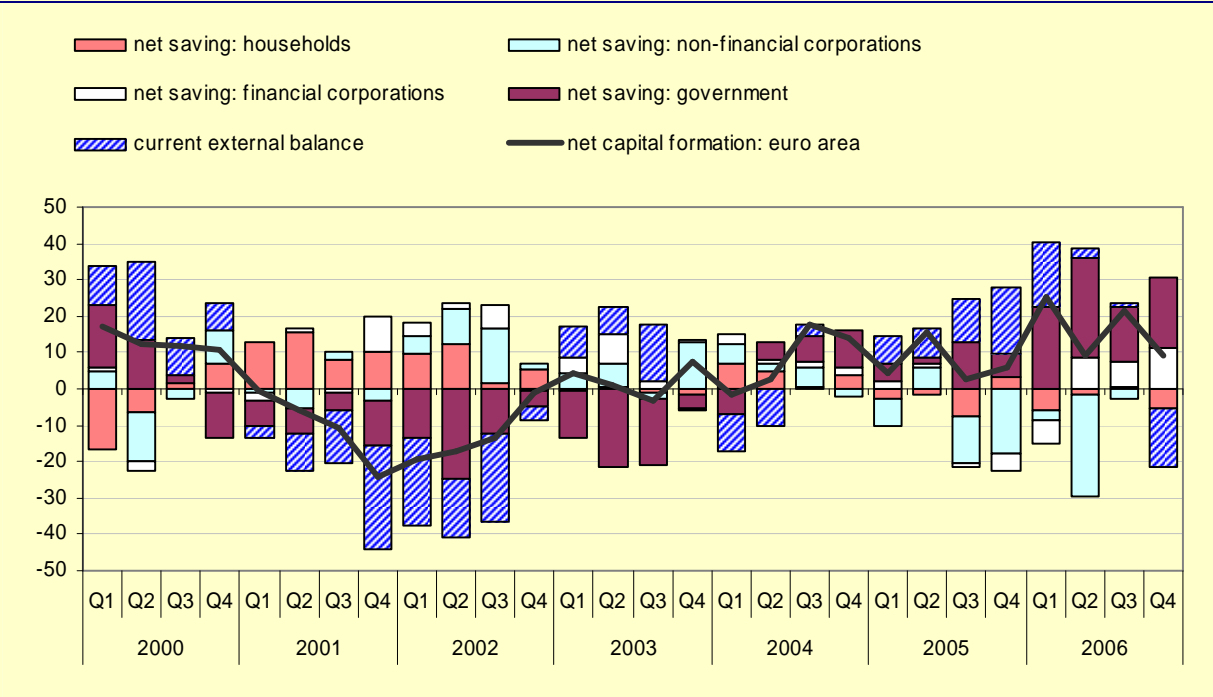
Chart 2.5
Contributions of sectors to the growth of nominal gross capital formation in the euro area
 (annual percentage change and percentage point contributions)



Sources: ECB and Eurostat.

Chart 2.6 shows the euro area saving-investment balance, specified by sector. The net capital formation¹ of an economy is financed by the net saving of the resident sectors and the rest of the world². Until 2002, the net capital formation declined and government deficits widened while savings of households and corporations mostly increased. The euro area current account turned into surplus (shown as negative bars in the graph) with the excess of its saving financing investment abroad. As shown in Chart 2.3, the increased saving of households was associated with a sluggish development of their consumption, which, together with the decrease in the growth rate of capital formation, contributed to a lower growth of GDP observed during that period. At the beginning of 2003, the growth of net capital formation became again positive. In the course of 2005 and early 2006 growing euro area current account deficits contributed to an upswing in capital formation growth.

Chart 2.6
Contributions of net saving by sector to the growth of net capital formation in the euro area
 (annual percentage change and percentage point contributions)



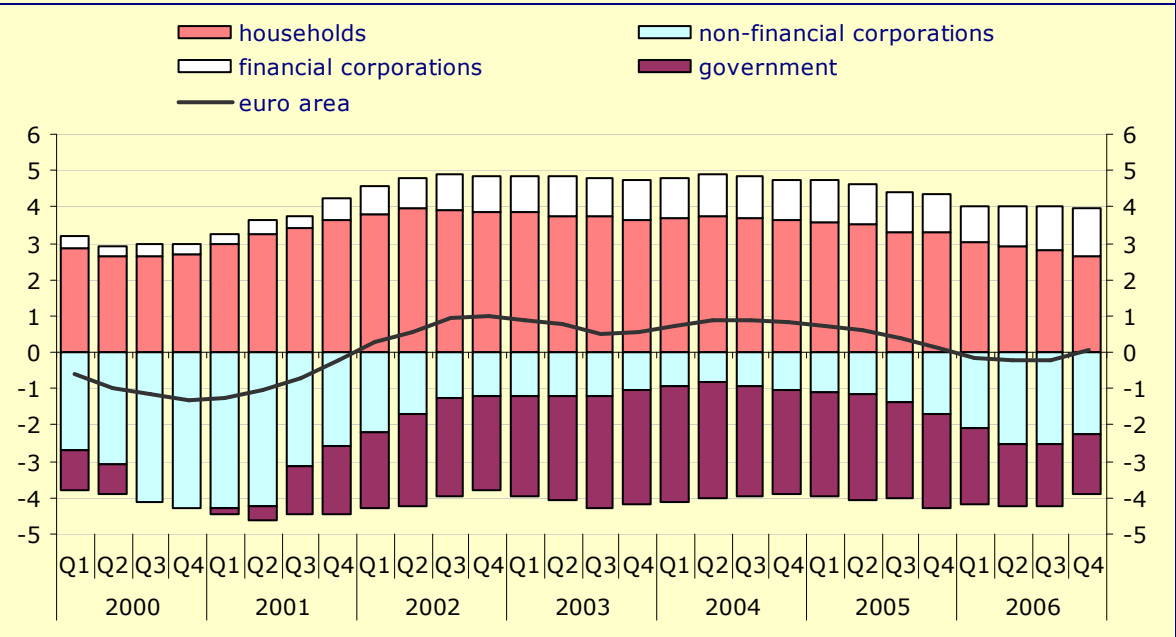
Sources: ECB and Eurostat.

¹ Plus acquisitions less disposals of non-produced non-financial assets.

² In this graph, the current external balance is shown from the viewpoint of the rest of the world, i.e. a positive external balance means that the rest of the world has a surplus on its current account with the euro area and is thus financing the resident economy. Conversely, the euro area then has a deficit on its current account with the rest of the world.

The result of the different developments of investment and saving by sector can also be seen in **Chart 2.7**. The difference between savings plus net capital transfers on the one hand and gross capital formation³ on the other hand is **net lending** (if positive) or **net borrowing** (if negative) of a sector. Net lending of households as a percentage of gross euro area disposable income increased in 2001, mostly related to a higher growth of household saving. The reduction in net borrowing by non-financial corporations in 2001 and 2002 was mostly related to the reduction in the growth rate of their gross fixed capital formation. At the same time, the government deficits widened (their net borrowing increased). The euro area economy became a net lender to the rest of the world until 2005. In 2005 and 2006, euro area consumption and investment again displayed higher growth rates, which also impacted import growth, and the saving ratio declined.

Chart 2.7
Contributions of sectors to the net lending (+) / net borrowing (-) of the euro area (as a percentage of gross disposable income, based on four-quarter-cumulated sums)



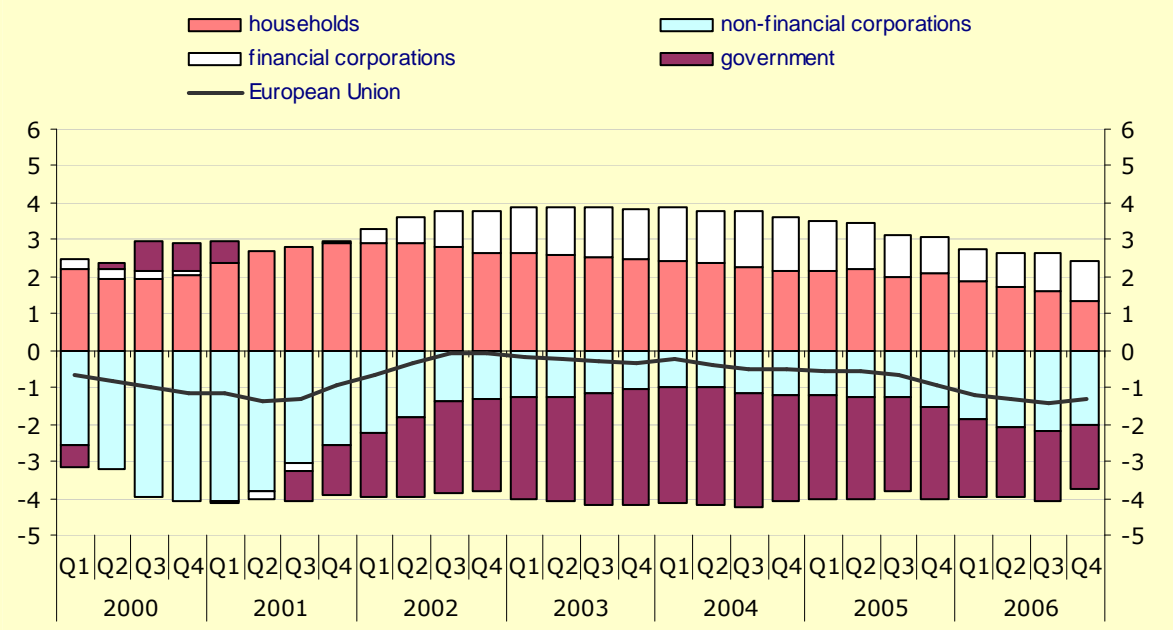
Sources: ECB and Eurostat.

³ Plus acquisition less disposal of non-produced non-financial assets.

Contrary to the euro area, the European Union hardly got a net lending position over the period (see **Chart 2.8**). This was mainly caused by lower household savings. The latter started decreasing in 2002 already, whereas they were remaining high in the euro area. Net borrowing stabilized in the last quarter of 2006, at around 1.5% of the EU national disposable income.

Chart 2.8

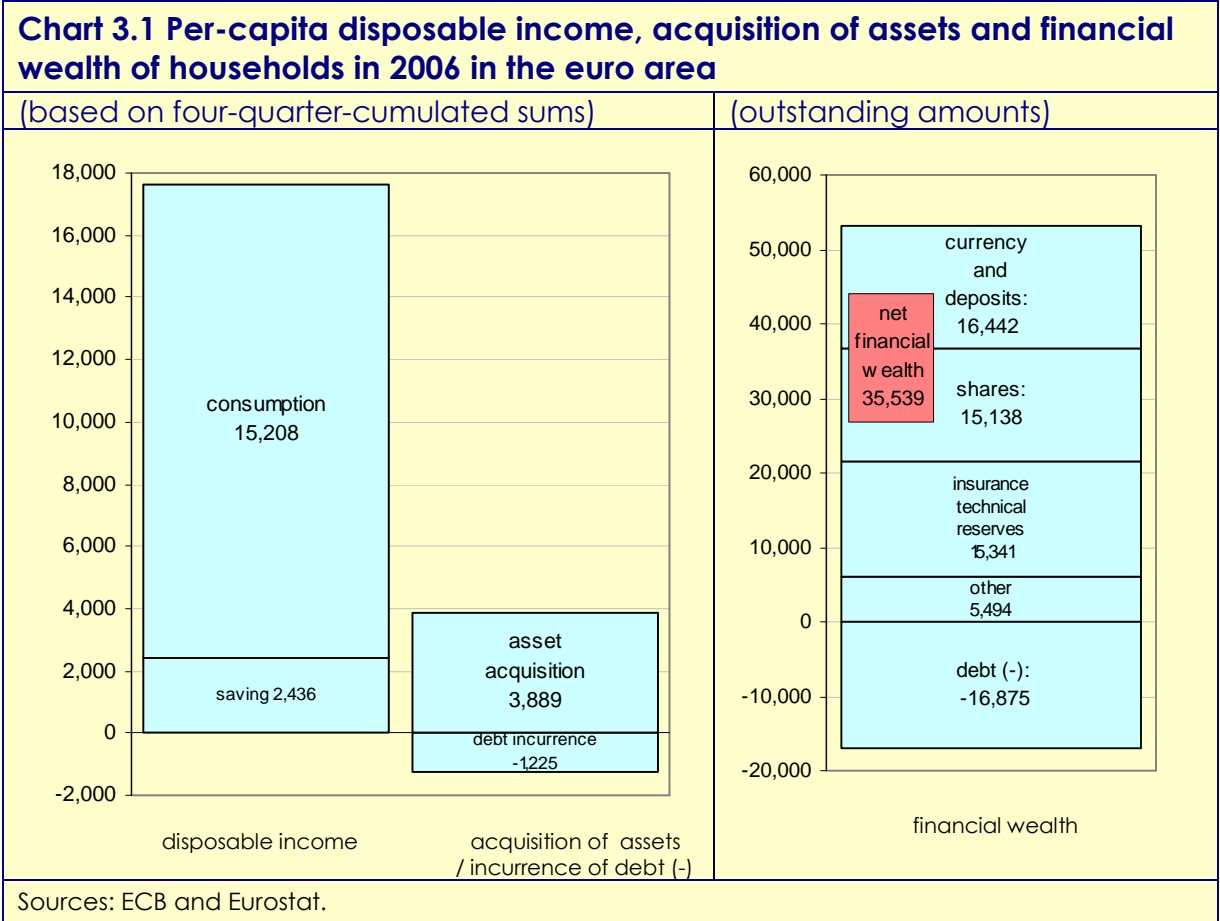
Contributions of sectors to the net lending (+) / net borrowing (-) of the European Union (as a percentage of gross disposable income, based on four-quarter-cumulated sums)



Sources: ECB and Eurostat.

3. Households and non-profit institutions serving households (NPISH)

Chart 3.1 provides euro area household per-capita values for several main household indicators for the year 2006.⁴ **Average gross disposable income** (plus net adjustment for the change in net equity of households in pension funds reserves) of households equalled €17,645 per euro area citizen. Of this income, €15,208 was **consumed** and €2436 was **saved** by each person on average. About ¾ of this saving (€1829 per person) was invested in non-financial assets, like dwellings, while the rest was lent to other sectors. This net lending broadly corresponded to a **financial investment** (increase in bank deposits, acquisition of shares, etc.) of about €2057 per person and an **incurrence of debt** of €1225 (for instance, by taking a mortgage loan for a house purchase).



⁴ Source of population data: Eurostat ESA 95 Transmission programme.

At the end of 2006, the average net financial wealth of each euro area citizen amounted to about €35,820. This equals the outstanding amounts of households' financial assets (€53,342 per person) minus their liabilities (€16,859). The largest proportion of the households' financial assets has been invested in currency and deposits (€16,438 per capita) followed by shares, including the value of ownership rights in unquoted corporations (€15,348), and the value of their reserves with pension funds and life insurance corporations (€15,341). The value of the other financial assets such as debt securities and derivatives represent about €6,216 per person.

Chart 3.2 shows the growth rate of euro area households' disposable income (in current prices), which accelerated through the first quarter of 2001, then declined through the first quarter of 2002 and remained roughly constant thereafter. The most important source of households' income growth is the growth of compensation of employees (that is, wages and salaries plus employers' social contributions). The contribution from gross operating surplus and mixed income (which accrues to self-employed households and home owners) was fairly stable during the years under review. Net receipts of property income and such (interest received minus interest paid, dividends, etc.) contributed to the high growth rates in the period 2000-2001 and weighed (negatively) on the low growth rate in 2002. During the downturn of 2001 and 2002, net social benefits (e.g. unemployment benefits received minus premiums paid) provided a positive contribution to gross disposable income of households. Taxes had a significant (negative) contribution during conjunctural upswings that is in 2000, 2005 and 2006.

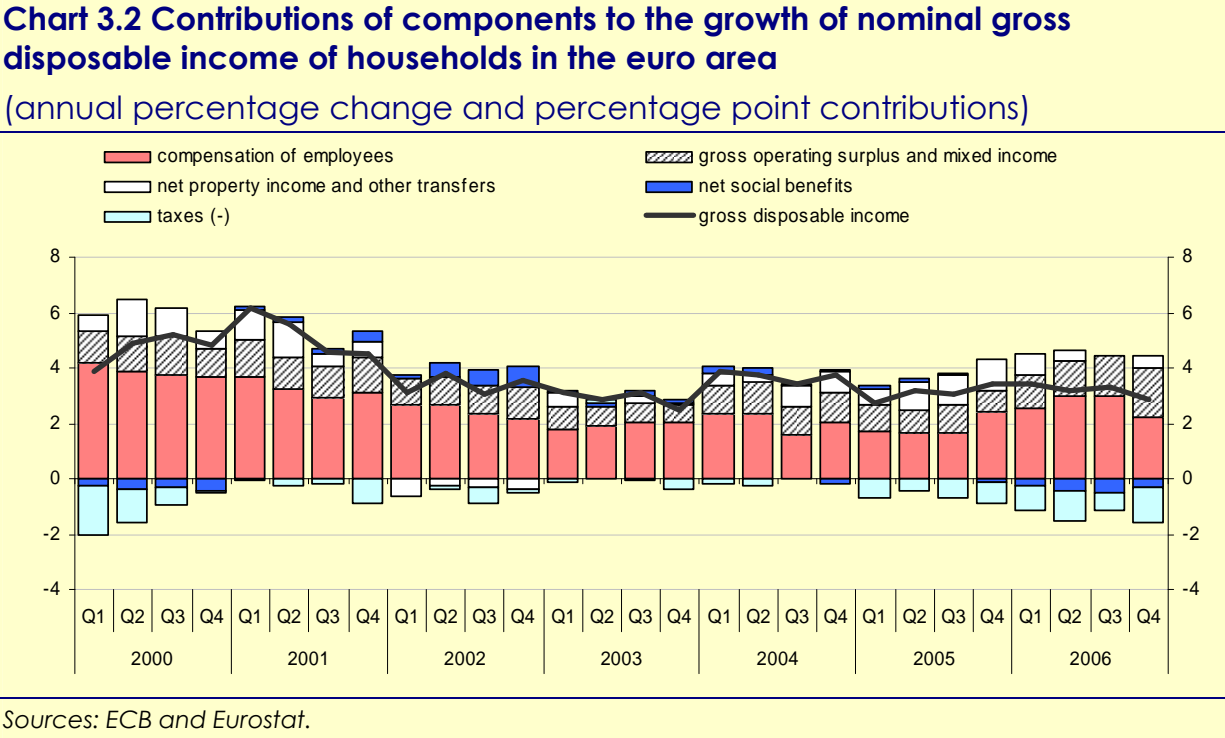
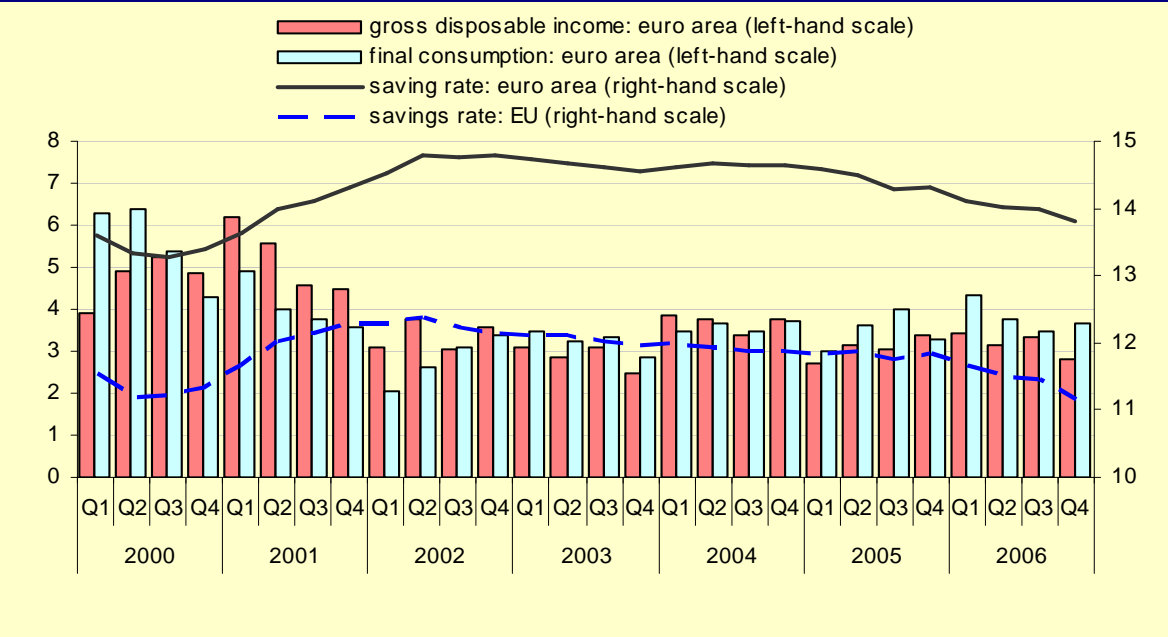


Chart 3.3 shows the growth rate of euro area households' **gross disposable income** compared with that of their **consumption**. If the former surpasses the latter, the households saving rate increases. After a trough in 2000, the household saving rate reached a maximum in 2002 and has declined since 2005 in the euro area. Household saving rates were lower in the EU and they started decreasing in 2002 already.

Chart 3.3 Growth of nominal consumption and nominal gross disposable income of households¹⁾ and the saving rate²⁾

1) annual percentage change
 2) percentage of gross disposable income (including net adjustment for the change in net equity of households in pension funds reserves), based on four-quarter-cumulated sums



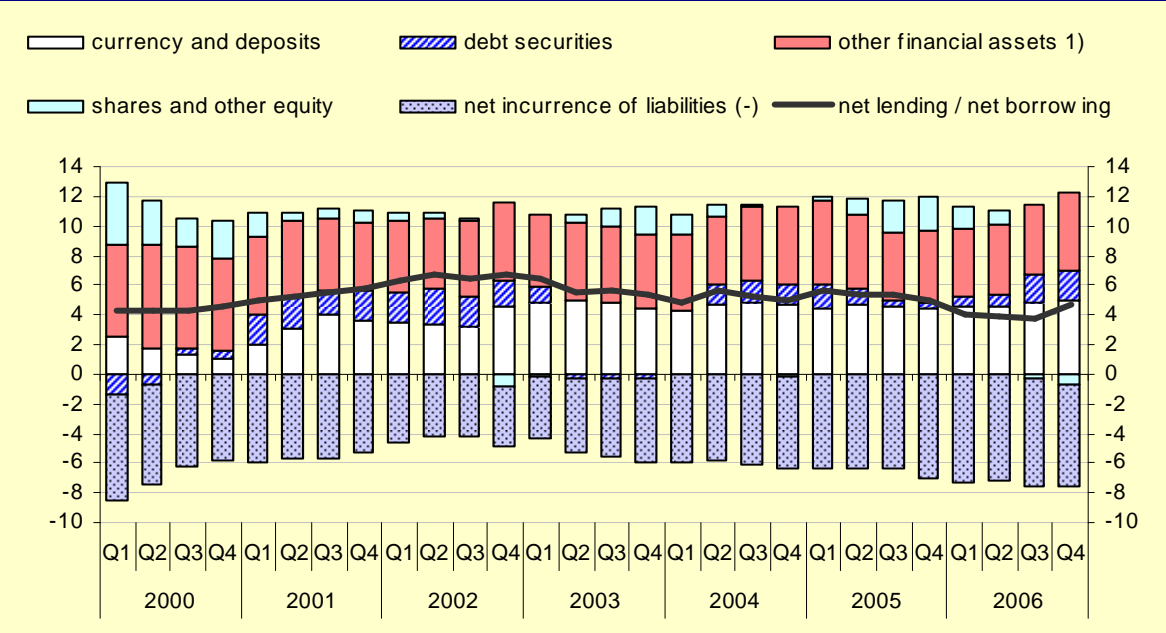
Sources: ECB and Eurostat.

Chart 3.4 shows the financial investment of euro area households by type of financial instrument, as well as their incurrence of loans and other liabilities. Net lending of households fluctuates between 4% and 7% of their disposable income, and their net acquisition of financial assets between 10% and 13%. Whereas in 1999 and 2000 shares and other equity, which includes mutual fund shares, attracted a sizeable proportion of household's financial investments, the importance of these financial instruments declined in 2001 while in 2002 households were net sellers of shares and other equity. Currency and deposits regained their traditionally larger share in 2001 and 2002. Investments in other financial assets, such as the increase in households' life insurance and pension fund reserves were much more stable.

Chart 3.4

Net acquisition of financial assets, net incurrence of liabilities and net lending / net borrowing of households in the euro area

(percentage of gross disposable income (including net adjustment for the change in net equity of households in pension funds reserves), based on four-quarter-cumulated sums)



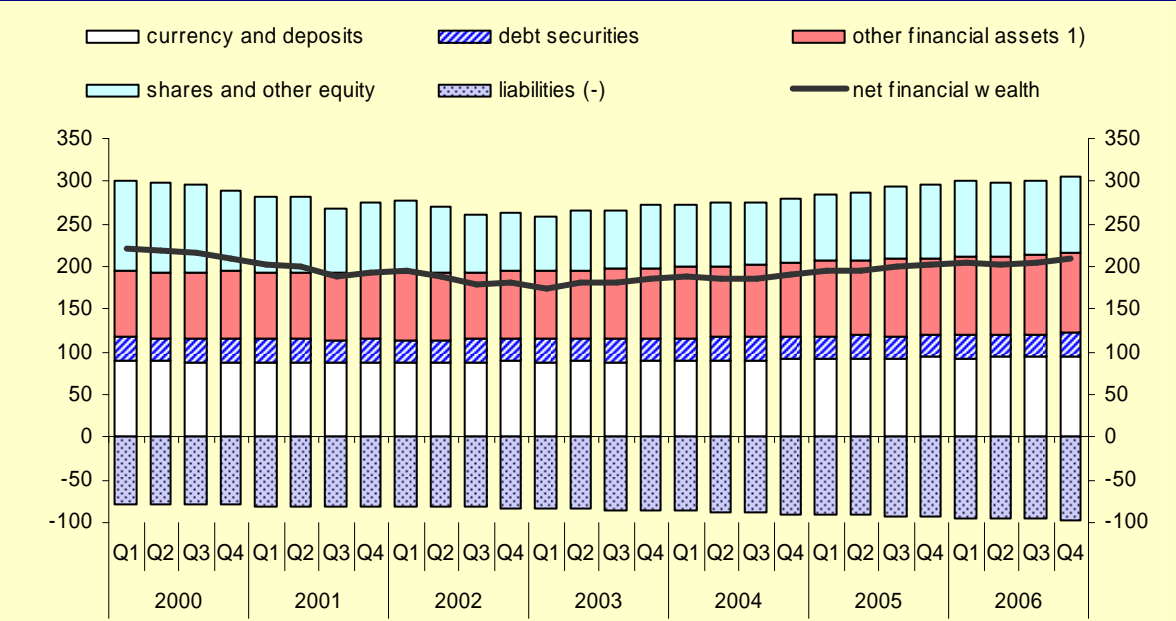
Source: ECB

1) Insurance technical reserves, financial derivatives, loans granted and other accounts receivable.

The households sector is by far the richest sector in the economy. Its wealth is composed of non-financial assets, mainly residential property, and net financial wealth. The latter equals the difference between the market value of their financial assets and their liabilities, such as mortgage loans. The financial wealth is presented in the financial balance sheets (**Chart 3.5**). At the end of 2006, the **net financial wealth** of euro area households was 5.5 trillion euro; this is close to 200% of their gross disposable income. A similar ratio had already been reached in 2000. Subsequently, their relative net financial wealth eroded to a low of 162%, mainly due to valuation losses on the stock markets. Another reason for the relatively slow increase in net financial wealth has been the comparatively fast growing indebtedness of households since 2003. At the same time household debt mostly serves to finance house purchases and the euro area housing wealth has not yet been incorporated in these accounts. While at the end of 2006 the overall **indebtedness** of the euro area household sector was about 90% of its gross disposable income, its **financial wealth** equalled almost 290%. As was also shown in Chart 3.1, this financial wealth was mainly invested in deposits, shares and other equity (including mutual funds shares), and pension fund and life insurance reserves.

Chart 3.5
Household financial assets, liabilities and net financial wealth in the euro area

(percentage of gross disposable income (including net adjustment for the change in net equity of households in pension funds reserves), based on four-quarter-cumulated sums)

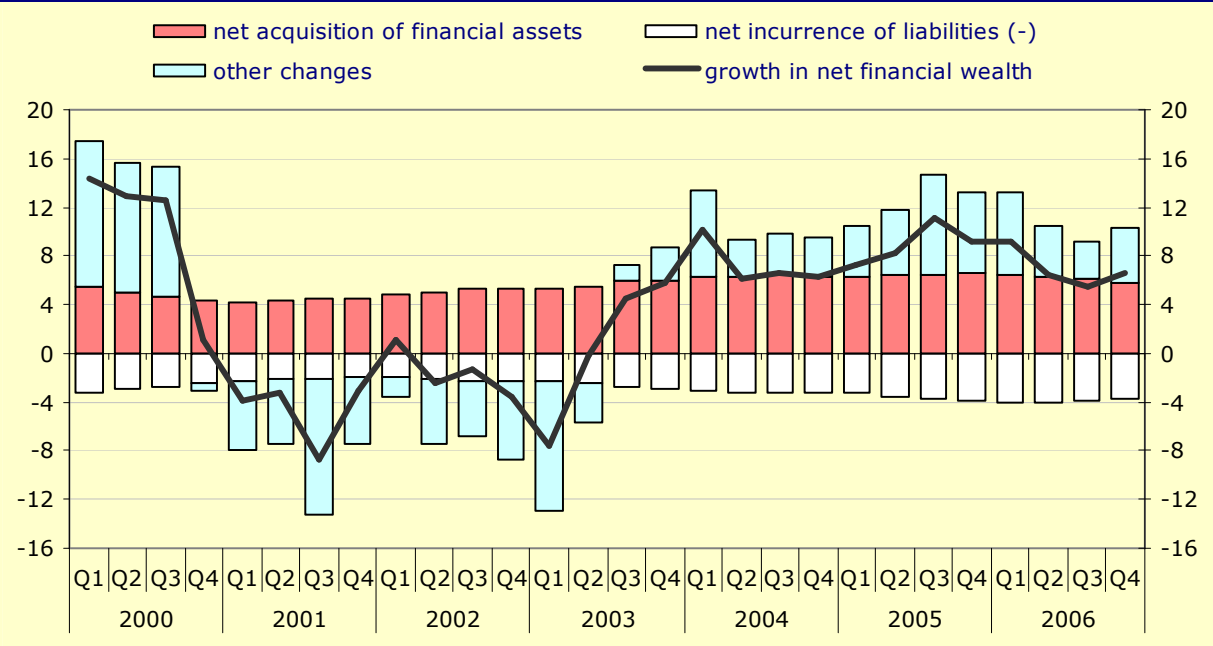


Source: ECB

1) Insurance technical reserves, financial derivatives, loans granted and other accounts receivable.

The **changes in the net financial wealth** of euro area households are predominantly related to their net acquisitions of financial assets, their incurrence less redemption of loans, and changes in the prices of their financial assets (**Chart 3.6**). Between 2000 and 2006, the growth rates of the net financial wealth of euro area households fluctuated in particular because of the changes in share prices, while their net lending grew at a fairly stable pace.

Chart 3.6
Financial assets, liabilities and net financial wealth of households in the euro area
 (annual growth rates and percentage point contributions)



Source: ECB

4. Non-financial corporations

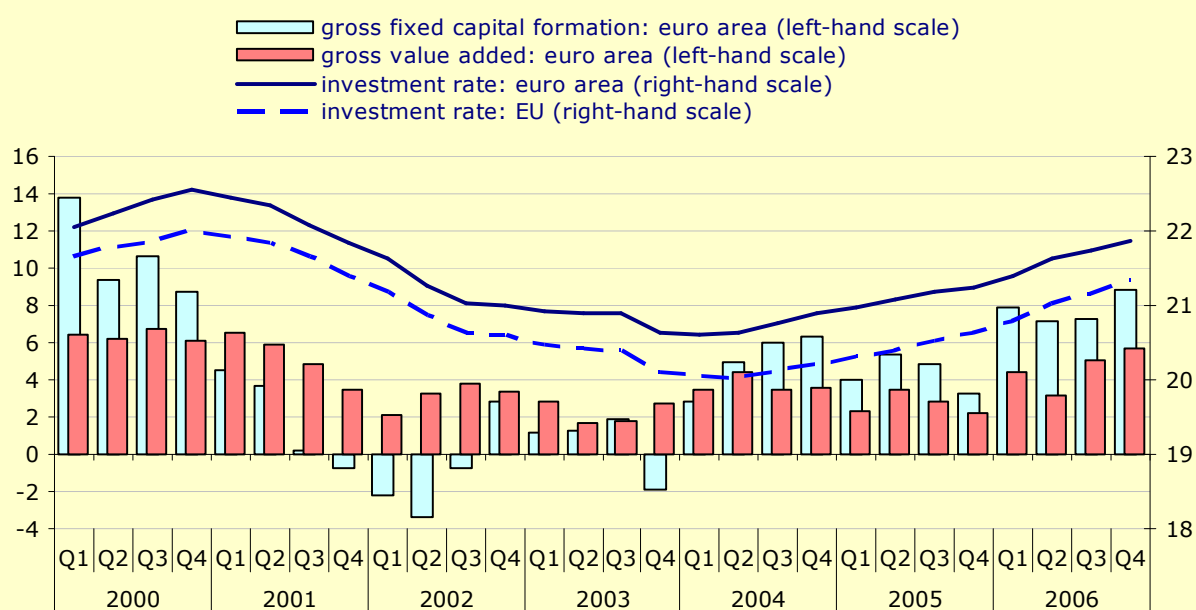
Chart 4.1 compares the growth of gross value added with that of investment in fixed assets (gross fixed capital formation) of the euro area non-financial corporations. The annual percentage change of investment started its decline already in 2000, before the slowdown in value added growth, and its fall was deeper. Only since the second quarter of 2004 investment growth has remained above the growth in value added. This information can also be summarised in the gross **investment rate** defined as the gross fixed capital formation divided by the value added of non-financial corporations. Chart 4.1 shows that investment rates developed quite similarly for the euro area and the EU showing an increase since 2004 after the fall recorded in 2001 and 2002.⁵

Chart 4.1

Growth in gross fixed capital formation and gross value added by non-financial corporations¹⁾ and the investment rate²⁾ in the euro area and in the European Union

1) annual percentage change

2) percentage of gross value added, based on four-quarter-cumulated sums

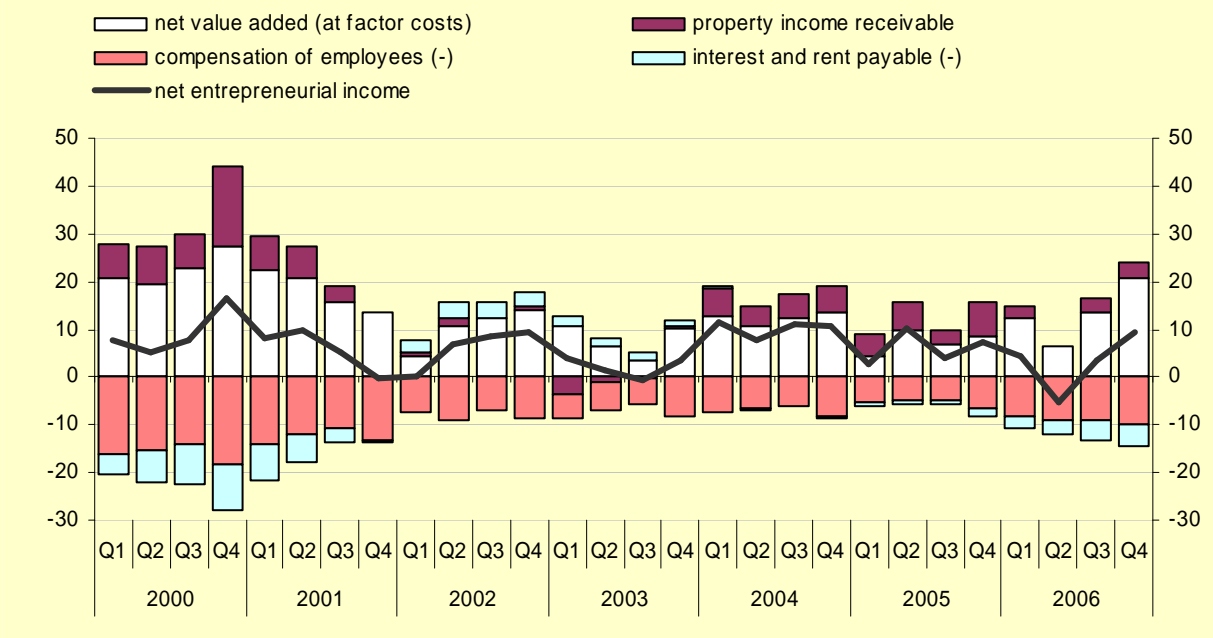


Source: ECB and Eurostat

⁵ For the EU an outlier has been removed in the second quarter of 2006.

Chart 4.2 depicts the growth of net entrepreneurial income⁶ of non-financial corporations in the euro area. **Net entrepreneurial income** is a core macro-economic indicator for corporations, which approximates the concept of pre-tax corporate profits in business accounting. Income originating in production (i.e. value added) has been the main contributor to the growth of this aggregate. Property income receivable, which includes dividends and retained earnings from foreign direct investment, grew quite fast at the beginning of this century, but reinforced the slowdown in value added in 2001 and 2002. On the contrary, a reduction in interest and rent payable, especially in 2002 and 2003, supported entrepreneurial income growth during that period.

Chart 4.2
Contributions of components to the growth of net entrepreneurial income of non-financial corporations in the euro area
 (annual percentage change and percentage point contributions)

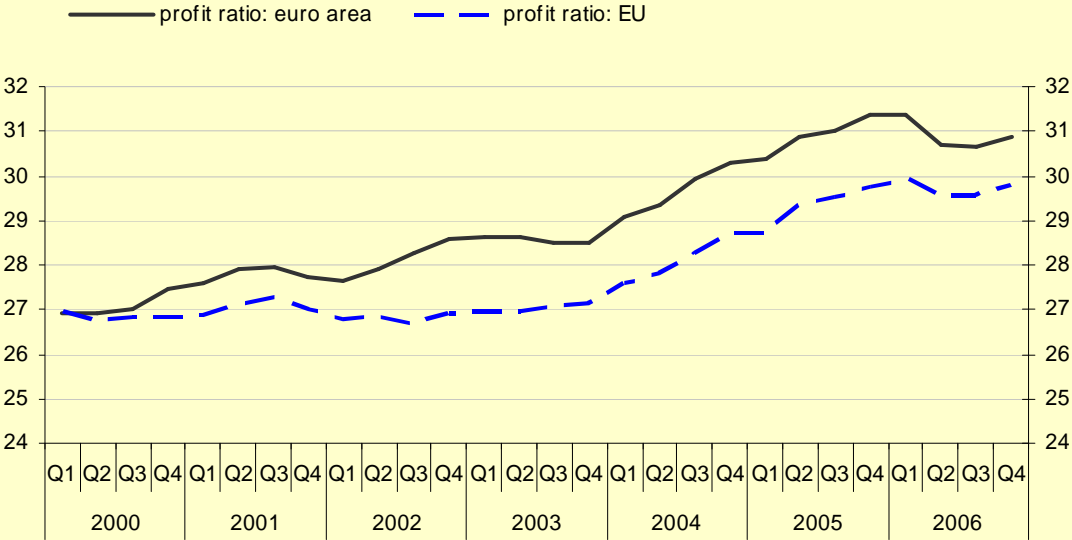


Source: ECB and Eurostat

⁶ Net entrepreneurial income equals net value added plus subsidies on production and property income receivable from financial assets owned by non-financial corporations (including profits of foreign subsidiaries), minus compensation of employees, taxes on production and imports, , and interest and (land) rents payable.

Chart 4.3 shows the development of net entrepreneurial income as a percentage of net value added for the euro area and the EU. Starting from identical levels in 2000, the profit ratio of the euro area started growing in 2001 already, creating a gap of one percentage point with the European Union. This gap remained almost unchanged during the increase observed since 2002 in both areas.

Chart 4.3
Profit ratio of non-financial corporations in the euro area and the European Union
 (net entrepreneurial income as percentage of net value added, based on four-quarter-cumulated sums)



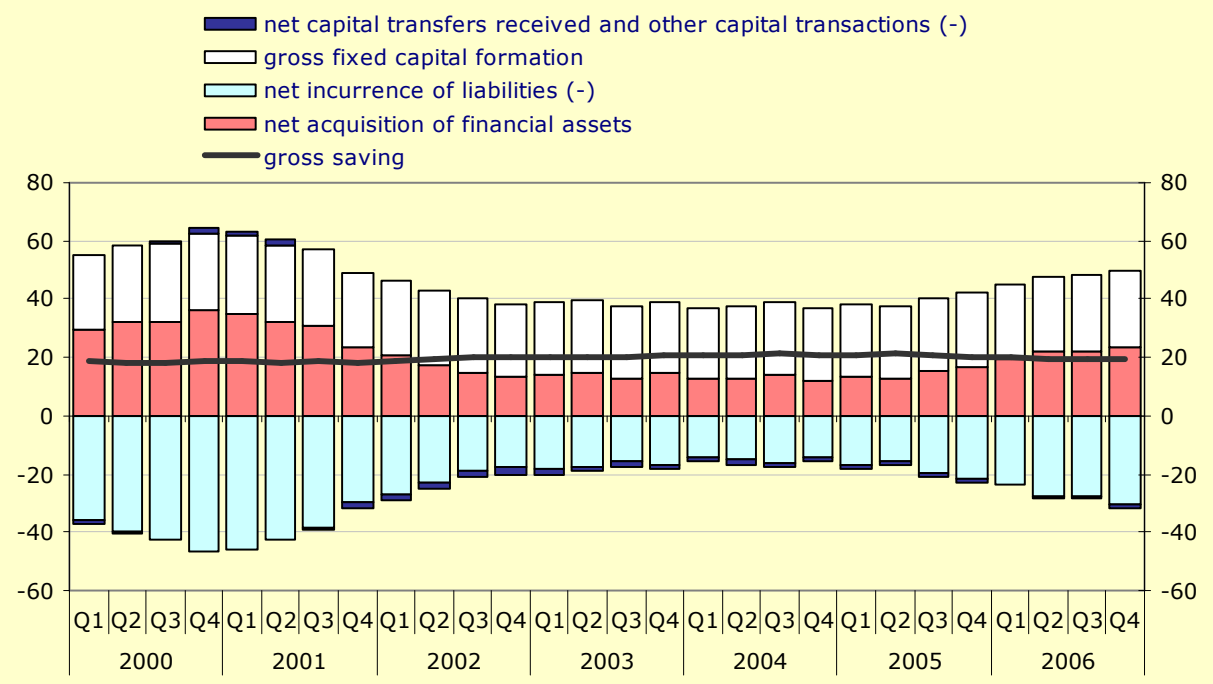
Source: ECB and Eurostat

Non-financial corporations finance their (financial and non-financial) investment internally via gross saving (broadly equivalent to retained earnings plus depreciation allowances in business accounting) and externally via the net issuance of debt and equity (**Chart 4.4**). Between 1999 and 2001, euro area non-financial corporations were particularly active in mergers and acquisitions, at a time when the prices of shares and other equities were reaching a peak. This entailed a relatively large net acquisition of financial assets during this period. The subsequent subdued economic growth contributed to a substantial relative decrease in the borrowing of non-financial corporations. In 2005 non-financial and financial investment picked up again and so did external financing.

Chart 4.4

Gross saving, net acquisition of non-financial and financial assets and net incurrence of debt of non-financial corporations in the euro area

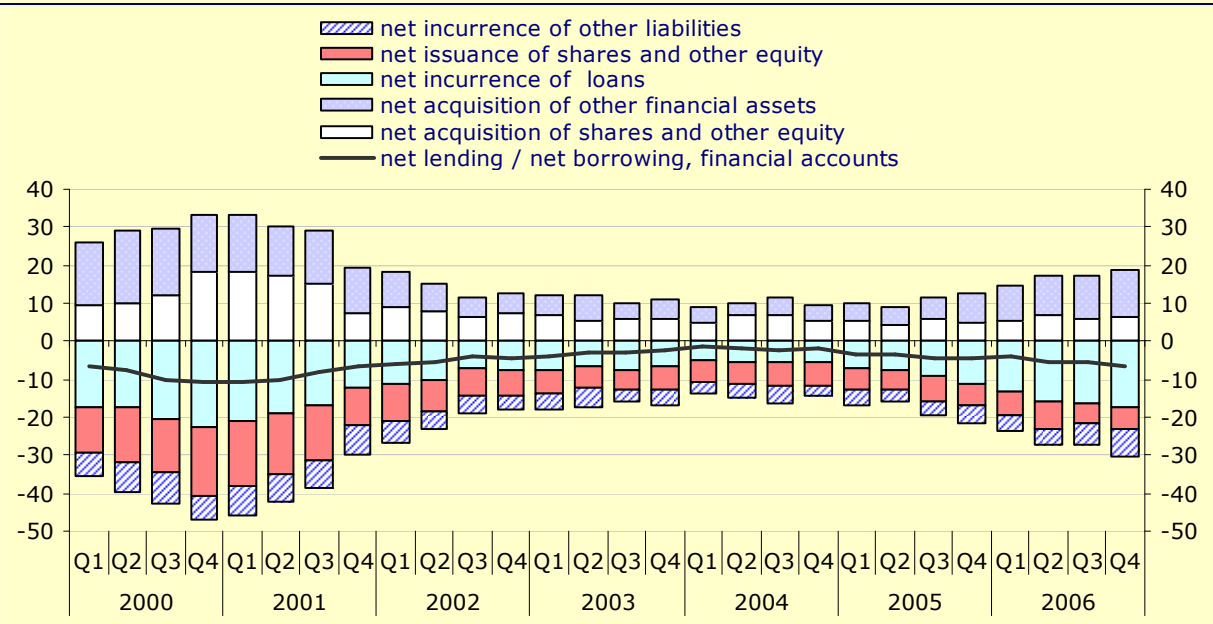
(percentage of net value added, based on four-quarter-cumulated sums)



Source: ECB and Eurostat

Chart 4.5 presents a breakdown of the financial transactions of non-financial corporations. In particular, it shows that during the mergers and acquisitions boom of 1999 to 2001 (refer to the relatively large net acquisition of shares and other equity) a large part of the financing occurred via the issuance of shares and other equity. Thereafter equity financing remained more subdued. In 2005 and 2006, it was mainly loan financing that drove the growth in the net incurrence of liabilities.

Chart 4.5
Net acquisition of financial assets, net incurrence of debt and net lending (+) / net borrowing (-) of non-financial corporations in the euro area
 (percentage of net value added, based on four-quarter-cumulated sums)



Source: ECB