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ECB staff macroeconomic projections for the euro area

1 Overview

The euro area economy stagnated at the end of 2023 amid tight financing conditions, subdued confidence and past competitiveness losses. Incoming information suggests a slower recovery in the short run than was foreseen in the December 2023 projections. Nevertheless, economic growth is projected to gradually pick up during this year as real disposable income rises, amid declining inflation and robust wage growth, and as the terms of trade improve. With the current shipping disruptions in the Red Sea unlikely to cause significant renewed supply constraints, export growth is expected to catch up with strengthening foreign demand. Over the medium term the recovery is seen to also be supported by the gradual fading of the impact from the ECB's monetary policy tightening. Overall, annual average real GDP growth is expected to be 0.6% in 2024, and to strengthen to 1.5% in 2025 and 1.6% in 2026. Compared with the December 2023 projections, the outlook for GDP growth has been revised down for 2024, owing to carry-over effects from past negative data surprises and weaker incoming forward-looking information, it is unrevised for 2025 and has been revised slightly up for 2026.¹

Inflation is projected to moderate further owing to the ongoing easing of pipeline pressures and the impact of monetary policy tightening, albeit at a more modest pace than seen in 2023. Pipeline price pressures should continue to fade with the shipping disruptions in the Red Sea expected to have only a limited upward impact. As energy prices decline, strong labour cost developments should be the dominant driver of inflation in the Harmonised Index of Consumer Prices (HICP) excluding energy and food. Nominal wage growth is set to remain elevated, driven by persistent tightness in the labour market, but it should gradually ease over the projection horizon as upward impacts from inflation compensation fade. A recovery in productivity growth should support the moderation in labour cost pressures. Profit growth is set to weaken over the projection horizon and provide a buffer to the pass-through of labour costs. Overall, annual average headline HICP inflation is expected to decrease from 5.4% in 2023 to 2.3% in 2024, 2.0% in 2025 and 1.9% in 2026. Given the weak outlook for energy inflation, headline inflation is expected to remain below HICP inflation excluding energy and food throughout the projection horizon. Compared with the December 2023 projections, HICP inflation has been revised down for 2024 and 2025, mainly owing to the direct and indirect effects from lower assumptions for energy commodity prices and lower labour cost pressures, and is unrevised for 2026.

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