

## Box I-1

Post-crisis economic  
developments and  
Central Bank forecasts

Appendix 2 discusses the accuracy of the Central Bank's output and inflation forecasts for 2011. This Box looks farther back and examines how post-crisis developments in output growth compare with the Bank's November 2008 forecast, the first one prepared by the Bank after the crisis struck.

**November 2008 output growth forecast virtually spot-on**

The state of the economy and the outlook for the future were extremely uncertain in November 2008, and there was actually very little on which to base forecasts, as the scope of the financial collapse was virtually unprecedented in Iceland or elsewhere. As a result, the output forecast published in *Monetary Bulletin* 2008/3 was prepared under highly uncertain conditions.

The Bank forecast that a sharp contraction of 8.3% in 2009 would be followed by a further contraction of 1.7% in 2010 but that growth would turn positive again in 2011, by 3.2%. According

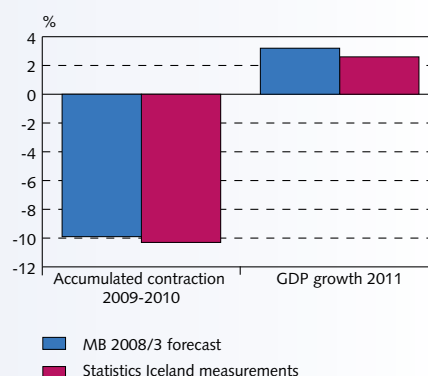
to the latest measurements from Statistics Iceland, the contraction in 2009 was somewhat less than forecast, or 6.6%, while the contraction in 2010, at 4%, was larger than projected. An examination of the entire 2009-2010 contraction reveals, however, that the Bank's November 2008 forecast was almost spot-on: the forecast provided for an accumulated 9.9% loss of output, whereas Statistics Iceland measurements indicate that the contraction was 10.3%. The forecast of 3.2% output growth in 2011 was also very close to Statistics Iceland's measurement, which was 2.6% (the previous Statistics Iceland estimate, from June 2012, assumed 3.1% growth for 2011).

A closer look at the quarterly developments in GDP reveals even more clearly how accurate the November 2008 forecast was. As is mentioned above, the contraction in 2009 was overestimated. From Q1/2010 through the end of the forecast horizon, however, GDP develops almost exactly in line with the Statistics Iceland measurements, and at the end of the horizon, in Q3/2011, it is almost identical to the Statistics Iceland measurement (the difference is 0.01%). The deviation in the annual output growth forecast for 2010 therefore reflects only the base effects from the previous year; that is, that the actual contraction in 2009 was smaller than that in the forecast.

Finally, Chart 2 shows that the forecast of the trough of the downturn materialised in full, both as regards timing (Q1/2010) and the output level at that time. The estimate of output loss from the pre-crisis peak to the post-crisis trough is therefore borne out almost entirely: the peak-to-trough loss was forecast at 16.3%, while the actual loss was 16.7%.

Chart 1

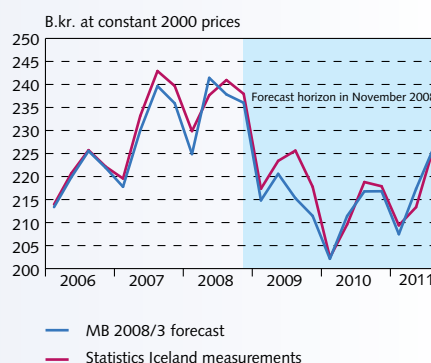
MB 2008/3 forecast of contraction and post-crisis recovery



Sources: Statistics Iceland, Central Bank of Iceland.

Chart 2

Gross domestic production - comparison to MB 2008/3



Sources: Statistics Iceland, Central Bank of Iceland.