

A still sluggish recovery

After an improvement in H2 2003, euro-zone GDP is expected to keep growing at a moderate pace of 0.3% (q-o-q) in Q1 2004 and 0.4% in both Q2 and Q3. As shown in Ifo-Insee-Isae business surveys, the industrial climate has become hesitant since January, possibly because of concerns about past exchange rate movements: the IPI is likely to remain flat for the first two quarters of 2004 and increase by 0.3% in Q3. GDP growth would tend to be based more on domestic demand. Private consumption should recover and reach a 0.4-0.5% growth rate, even though consumer confidence remains low. Inflation (HICP) is expected to stabilise at 1.7% (y-o-y) until Q3 2004.

Still waiting for a robust recovery in the industrial sector

Quarterly growth in euro-zone industrial output is expected to remain nil in both Q1 and Q2 2004. The latest official data have been already pointing in this direction, as also are the Ifo, Insee and Isae business survey indicators. The business climate has shown no further progress for the last two months despite very supportive international demand. Specifically, expectations regarding production declined slightly.

However, industrial production is likely to increase slightly in Q3, finally taking advantage of a lasting upturn in international economic activity. A rise of 0.3% is therefore expected in Q3 2004.

Lustreless GDP growth

In this context, GDP is expected to follow a moderate growth rate path for the first three quarters of 2004: 0.3% (q-o-q) in Q1, followed by 0.4% in both Q2 and Q3. Held back by weak industrial production, GDP would be underpinned by the good results from non-industrial sectors. In particular, the March surveys of the European Commission highlight the optimism being shown in the construction sector.

Figure 1

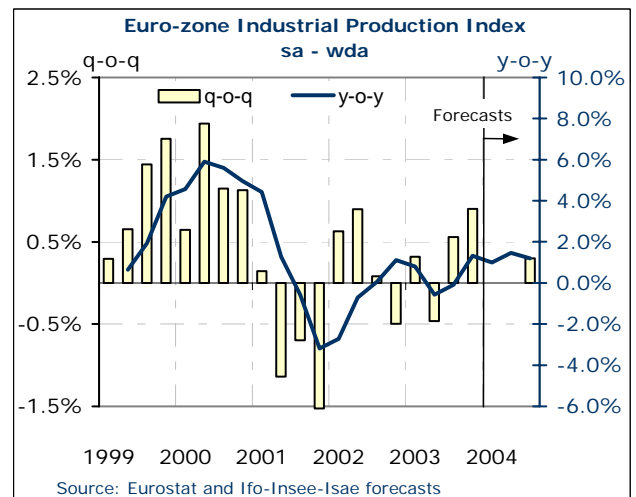


Table 1

2003/2004 Forecasts, % changes, sa - wda

q-o-q y-o-y	Q4 - 2003	Q1 - 2004 estimations	Q2 - 2004 forecasts	Q3 - 2004 forecasts
IPI	0.9 1.3	0.0 1.0	0.0 1.5	0.3 1.2
GDP	0.3 0.6	0.3 0.9	0.4 1.4	0.4 1.4
Consumption	0.0 0.6	0.4 0.6	0.5 1.0	0.4 1.3
Inflation	2.0	1.7	1.7	1.7

Source: Ifo, Insee, Isae, Eurostat.
Forecasts: Ifo, Insee, Isae

On the demand side, the maintenance of favourable financing conditions should bolster domestic demand. The first two quarters are likely to see acceleration in household consumption, rising by 0.4-0.5% (q-o-q) in Q1 to Q3 after lifeless growth in H2 2003. Consumption in Italy and Germany would simply recover after sharp decreases in Q4 2003. Moreover, tax cuts in the first part of 2004, in France and especially in Germany, should give a fillip to consumption. But growth rates would remain moderate, partly because of stubbornly low consumer confidence. Indeed, the stagnation of employment has continued to hold back household incomes. The high perceived inflation may also have contributed to the low consumer confidence.

Inflation resilient at 1.7%

The relative slowdown in prices of foodstuffs, combined with the assumption of a decrease in the Brent price to \$29/barrel (\$32 in Q1), would be offset by the effects of the end of the euro appreciation and tensions characterising non-oil commodities. The dollar/euro exchange rate is assumed to stay around 1.25 (as in Q1). As a consequence, inflation should remain stable at 1.7% in both Q2 and Q3, setting slightly below the expected level of core inflation.

Figure 2

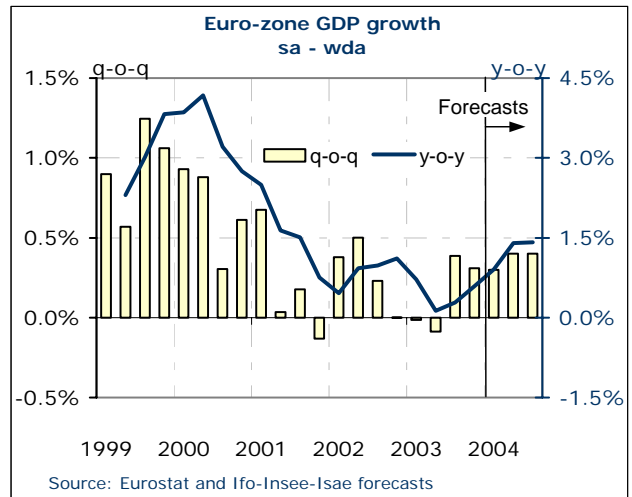
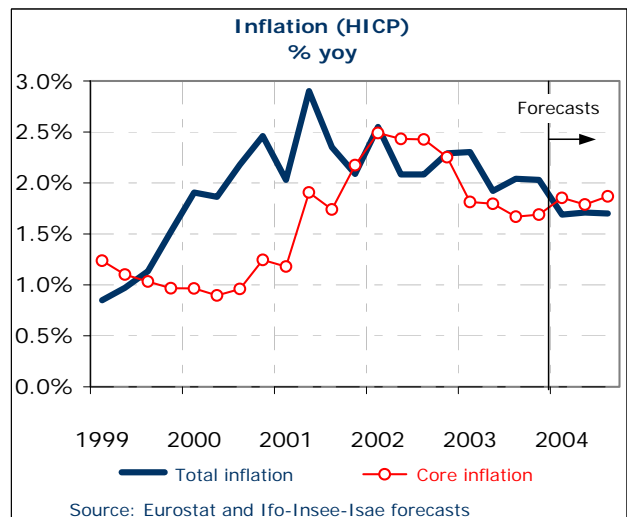


Figure 3



Methodological note

This publication is jointly produced by the German Ifo Institute, the French Insee institute and the Italian Isae institute. The forecasts are built up with the help of different forecasting tools shared by the three institutes, using time series models based on business surveys by national institutes, Eurostat and the European Commission.

A joint two-quarter-ahead forecast will be made on a quarterly basis for industrial production, GDP, consumption and inflation for the euro zone. The release of the forecast coincides with the quarterly national accounts second release by Eurostat.

More in-depth economic diagnoses for each country (Germany, France, Italy), can be found in:

- [Ifo Konjunkturprognose](#), Ifo
- [Conjoncture in France](#), Insee.
- [Abridged Quarterly Report](#), Isae

Next release:

Next forecast horizon:

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July 15, 2004 (day of Eurostat GDP second release)

2004 Q4