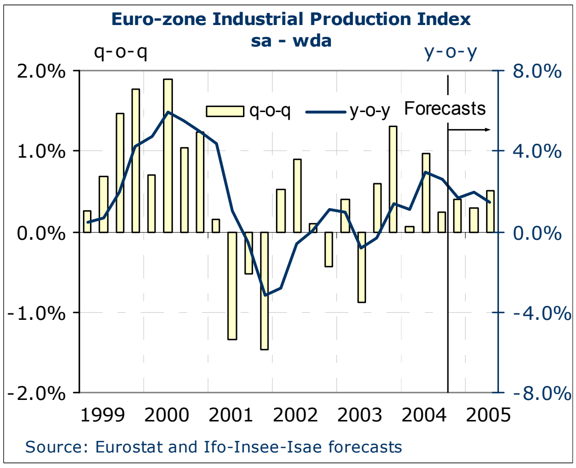
A less supportive environment

After a slowing in Q3, more intense than expected, GDP in the euro zone should grow at a rate of 0.4% (q-o-q) during the three subsequent quarters. This only moderate growth pace is also confirmed by the end of the improvement in the Ifo-Insee-Isae business surveys over the past months. Industrial production is estimated to grow by 0.4% in Q4 2004. The growth rate is then likely to decline to 0.3% due to weaker exports in Q1 2005, before increasing to 0.5%. With regard to domestic demand, the growth rate of private consumption should stabilise at 0.3% per quarter until Q2 2005. Inflation (HICP) should fall from 2.3% in Q4 to 1.9% in Q2, provided that oil prices continue to ease and that the euro/dollar exchange rate remains close to the current level within the time horizon of our forecasts.

Industrial output should grow moderately

After a weak Q3, production is likely to accelerate again in Q4; supported by a temporary rebound in France and in Italy, it is likely to grow by 0.4% (q-o-q). The continuingly weak domestic demand, the past appreciation of the euro and a slowdown of the world economy are likely to contribute to a moderate growth in industrial output.

In Q1 2005, a lower rise in exports will lead to a renewed deceleration of output to 0.3%, as pointed out by both lower export order books and fewer incoming foreign orders. Industrial production will show a slight strengthening starting in mid-2005. In the run-up to an expected increase in investment activity, industrial output should be supported by the manufacturing of intermediate products; in Q2, it should rise by 0.5%.



2005 Forecasts, % changes, sa - wda

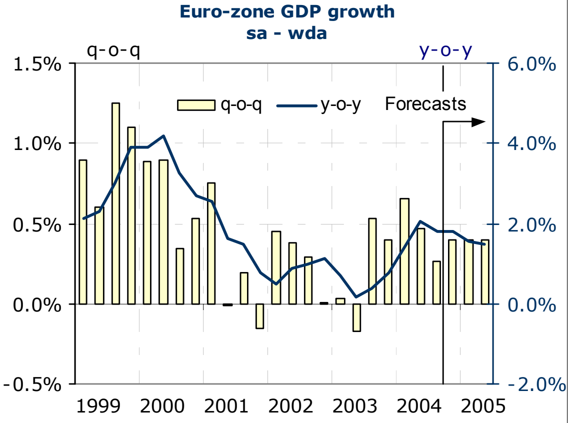
q-o-q / *y-o-y*	Q3-2004	Q4 - 2004 estimations	Q1 - 2005 forecasts	Q2 - 2005 forecasts	2004 estimations
IPI	**0.2** / 2.6	**0.4** / 1.7	**0.3** / 1.9	**0.5** / 1.4	2.1
GDP	**0.3** / 1.8	**0.4** / 1.8	**0.4** / 1.5	**0.4** / 1.5	1.8
Consumption	**0.1** / 0.9	**0.3** / 1.2	**0.3** / 0.8	**0.3** / 1.0	1.0
Inflation	2.2	2.3	2.2	1.9	2.1

Source: Eurostat and Ifo-Insee-Isae forecasts

GDP growth should remain lustreless

In line with industrial output, GDP also slowed in Q3. Foreign demand will continue to be the determining factor of growth in the euro zone for the end of 2004. In the course of 2005, with the slowing of the world economy, this factor should clearly weaken. Instead, private investment activity should gain momentum. In the next few quarters, GDP growth is likely to stabilise at 0.4% per quarter. The average growth rate in 2004 would thus amount to 1.8% (on a working-day adjusted basis).

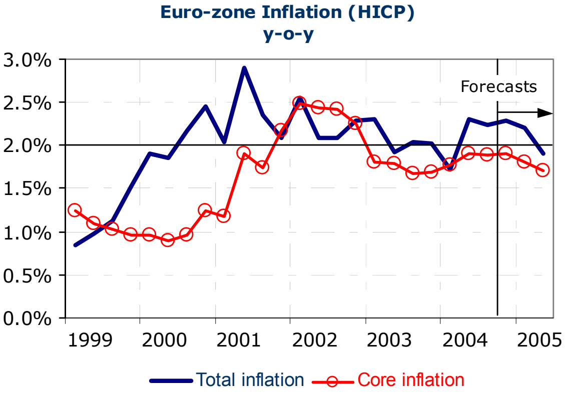
Private consumption should stabilise in the forecast period at a quarterly growth rate of 0.3%, in line with the low levels of consumer confidence. The unfavourable labour market situation should contribute to the weakness of real income growth. Purchasing power could be supported by falling energy prices.



Source: Eurostat and Ifo-Insee-Isae forecasts

Inflation should ease to 1.9% in mid-2005

The inflationary tensions due to past oil price hikes should decrease until mid-2005, thanks to falling oil prices, the appreciation of the euro and the ongoing slack in the economy. Under the assumption of a continuing decrease in the Brent price to around $38 per barrel in Q2, combined with a euro/dollar exchange rate around 1.35 on average in the first half of the year, inflation is expected to fall gradually from its recent Q4 peak (2.3%) to 2.2% in Q1 and 1.9% in Q2 2005. Core inflation should remain stable before ebbing in H1 2005.



Source: Eurostat and Ifo-Insee-Isae forecasts

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

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Next release: **April 14, 2005 (day of Eurostat GDP second release)**
Next forecast horizon: **2005 Q3**