

## A marked economic slowdown

*After its good performance in Q1, euro-zone real GDP decreased in Q2. Real GDP growth is expected to lower again in Q3 (-0.1%), to stagnate in Q4, and to improve moderately in 2009 Q1 (+0.1%). Industrial production is trending down and should decline over the forecast horizon, as announced by industrial business surveys. Private consumption growth is likely to be low: real income is not expected to improve significantly in the quarters ahead, and consumer surveys report low confidence over future economic conditions. The economic slowdown and worsening credit-access conditions will likely continue to undermine investment. Assuming a stabilisation of oil prices at USD90/barrel (Brent) and an exchange rate fluctuating around USD1.40 per euro over the forecast horizon, euro-zone inflation is projected to decline from 3.6% in Q3 2008 (end-of-quarter, y-o-y) to 2.7% in Q4 and 2.3% in Q1 2009, helped by the decrease in food and energy prices.*

### Industrial production vulnerable to low prospects

Euro-zone industrial production fell by 0.8% in Q2, reflecting the erosion of business-survey confidence in the main euro-zone countries (France, Germany, Italy and Spain).

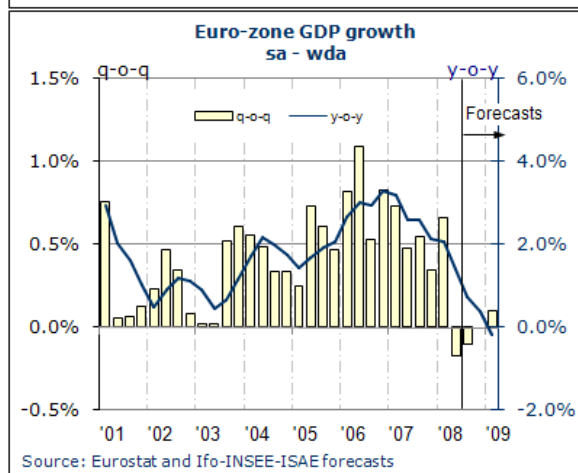
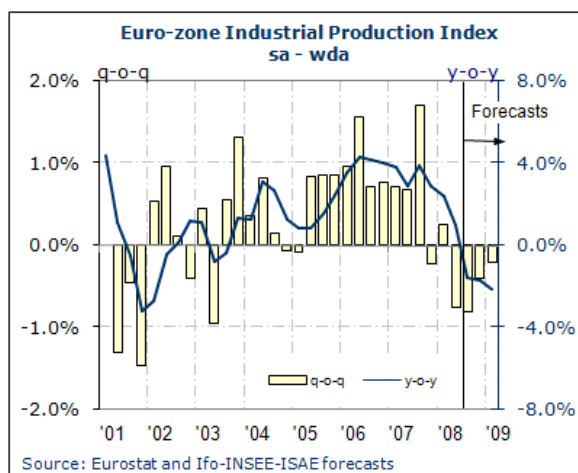
The slowdown in global demand and the decline in industrial confidence indices should continue to dampen euro-zone industrial activity in the quarters ahead. Industrial production is projected to fall by 0.8% in Q3 2008, 0.4% in Q4 and 0.2% in Q1 2009.

### Growth bottoms out

Euro-zone GDP growth should be held back by low domestic demand as in Q2. Euro-zone employment growth is expected to lose momentum in the coming quarters, as suggested by the deterioration of hiring prospects in business surveys. Despite the inflation decline underway since Q2, household purchasing power is not expected to improve over the second semester. This trend, coupled with consumers' growing concerns over economic prospects as expressed in recent surveys, should weigh on household expenditure. Private consumption should stagnate in Q3, followed by moderate gains in Q4 (+0.1%) and in Q1 2009 (+0.2%) thanks to lower inflation.

Although the impact of the financial crisis remains difficult to assess precisely, the resulting tighter credit access and higher risk aversion are likely to weigh on investment decisions. The economic slowdown, worsening credit-access conditions, and the easing of pressure on productive capacity are expected to sustain the decline in equipment investment over the next three quarters. Similarly,

construction investment should record further losses owing to the real-estate downturn that occurred in several countries (Spain, Ireland, Finland and France in particular). Since the start of 2008, short-term indicators have been sending a negative signal for non-residential investment as well.



Moreover, because of the global economic slowdown and, to a lesser extent, the euro's past appreciation, the external demand of the euro-zone is expected to remain weak in the next three quarters. External trade should not contribute significantly to euro-zone GDP growth over the forecast horizon.

All in all, euro-zone GDP is expected to decrease in Q3 (-0.1%) and to stagnate in Q4. This should be followed by a slight increase in Q1 2009 (+0.1%) thanks to a moderate recovery in household consumption.

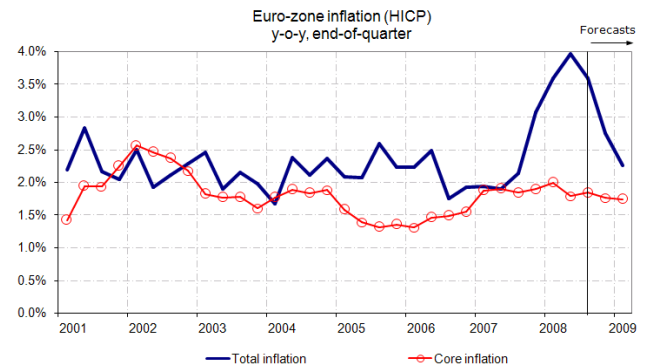
### Inflation declining but still high

Euro-zone inflation (HICP) remains at historically high levels. It is projected to decline from 3.6% in Q3 (end-of-quarter, y-o-y) to 2.7% in Q4 and 2.3% in Q1 2009, thanks to lower food and energy prices and the positive base effect of those prices. This scenario assumes a stabilisation of oil prices at USD90/barrel for Brent and an exchange rate fluctuating around USD1.40 per euro over the forecast horizon.

Core inflation is forecast to stay at around 1.8% (y-o-y), i.e., slightly below the level reached after Germany's VAT increase in January 2007, but 0.3 percentage point above the level before that measure. Sustained production costs should continue to drive up retail prices.

q-o-q	Q2 2008	Q3 2008	Q4 2008	Q1 2009	2008
y-o-y		estimates	forecasts	forecasts	forecasts
IPI	-0.8 1.0	-0.8 -1.5	-0.4 -1.7	-0.2 -2.1	0.0
GDP	-0.2 1.4	-0.1 0.7	0.0 0.4	0.1 -0.2	1.1
Consumption	-0.2 0.3	0.0 -0.1	0.1 -0.2	0.2 0.1	0.3
Investment	-1.0 2.5	-0.7 0.8	-0.5 -0.8	-0.1 -2.3	1.6
Inflation*	4.0	3.6	2.7	2.3	3.4

Source: Eurostat and Ifo-INSEE-ISAE forecasts \* end-of-quarter



Source: Eurostat and Ifo-Insee-Isae forecasts

### Methodological note

This quarterly publication is prepared jointly by the German Ifo institute, the French INSEE institute, and the Italian ISAE institute. The forecasts are produced with the help of tools shared by the three institutes, using time-series models based on business surveys by national institutes, Eurostat, and the European Commission.

Our joint two-quarter-ahead forecast covers euro-zone industrial production, GDP, consumption, investment, and inflation. Publication is timed to coincide with Eurostat's second release of quarterly national accounts.

Fuller economic analysis for each country (Germany, France, Italy) is available from:

- [Ifo Konjunkturprognose](#), Ifo
- [Conjoncture in France](#), INSEE
- [Abridged Quarterly Report](#), ISAE

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**Next release:**  
**Next forecast horizon:**

**8 January 2009 (day of Eurostat GDP second release)**  
**2009 Q2**