

April 2nd, 2019

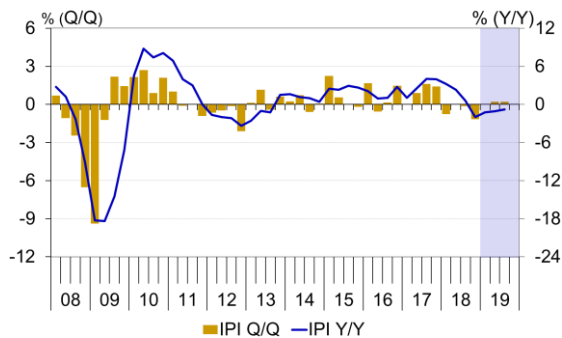
Eurozone GDP Growth remains sluggish

- GDP growth is expected to remain weak over the forecast horizon with the lowest growth rate in the first quarter driven by positive contribution of internal demand with similar growth rates for consumption and investment
- Annual headline inflation is less dynamic in 2019 than in the preceding year, mainly due to lower energy prices
- The outlook is subject to mostly downside risks such as an escalation of trade conflicts and a hard Brexit

GDP remained weak

Faced with a slowing global economy and weak growth in world trade, GDP growth in the Euro area remained weak in the last quarter of 2018, expanding only by 0.2% (after 0.1% in Q3). GDP increased by 1.8% in the Euro area in 2018, compared to +2.4% registered in 2017. This slowdown can be attributed to weakening growth of gross fixed capital formation and net foreign demand. Among the largest member states, Germany was stagnating (0% q-o-q) in Q4 and Italy registered a slight decline (-0.1%). On the other hand, the slight expansion in France continued at a moderate pace (0.3%) and Spanish GDP increased again strongly by 0.6%.

FIGURE 1 | Eurozone Industrial Production Index
Seasonally and working day adjusted



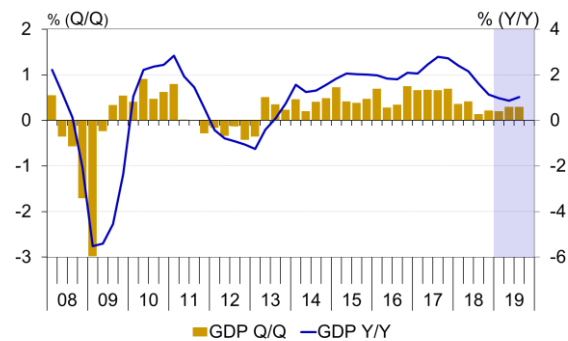
Source: Eurostat and Ifo-Istat-KOF Forecasts

A further decrease in the economic sentiment indicator (ESI) suggests that the economic slowdown is likely to continue. The sentiment in the manufacturing sector has been moving continuously downwards, whereas services and consumer confidence have recovered slightly during the last months. The construction confidence indicator is stagnating at a high level.

Due to weak foreign demand and country-specific factors, industrial production declined by 1.2% in Q4 compared to Q3. Yet in January, it increased again by 1.4% (m-o-m), with highest growth in energy and non-durable consumer goods. Industrial production is

expected to stagnate in Q1 and then pick up in subsequent quarters (+0.2% for both Q2 and Q3 2019).

FIGURE 2 | Eurozone GDP Growth
Seasonally and working day adjusted



Source: Eurostat and Ifo-Istat-KOF Forecasts

Growth in the Euro area is believed to remain subdued in the first quarter (0.2%) and should pick up slightly afterwards, resulting in a steady expansion of GDP by +0.3% in the following quarters.

The labor market remained strong as the number of persons employed increased again by 0.3% in Q4. In February, the unemployment rate remained stable at 7.8%, its lowest level since late 2008. Favorable labor market conditions together with wage increases should keep supporting private consumption expenditures also in the coming quarters. Private consumption expenditures are expected to increase by +0.3% in Q1 and expand by +0.4% in the following two quarters.

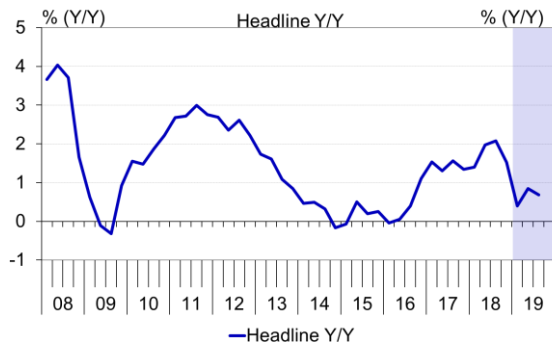
The current level of capacity utilization decreased for the second time in a row in Q1 2019, yet the level is still very high. This indicates that the investment dynamics should stay robust. Gross fixed capital formation is projected to increase in Q1 by +0.3% and then slightly accelerate in Q2 and Q3 2019 (+0.4%).

Inflation dynamics have slowed down

The ECB announced recently their intention to keep the policy interest rates unchanged at their present levels at least until the end of 2019. It also announced new TLTROs to keep supporting credit growth.

FIGURE 3 | Eurozone Inflation

Harmonized Index of Consumer Price (HICP), y-o-y growth rates



Source: Eurostat and Ifo-Istat-KOF Forecasts

Since the end of December, the oil price has recovered slightly, but still registers under the level seen a year ago. According to Eurostat's flash estimate, the euro area HICP index recorded at 1.4% in March. In the coming months, inflation dynamics are assumed to remain stable at +1.4% in the second quarter and to slowdown to +1.2% in the third quarter of 2019. The inflation forecast is based on the technical assumption that the Brent oil price remains stable at 67 USD per barrel and that the exchange euro/dollar exchange rate stays at 1.14 over the forecast horizon.

Many downside risks in sight

The Eurozone outlook is surrounded by many downside risks. There are considerable uncertainties considering potential trade conflicts with the United States, the precarious outcome of Brexit and the general slowdown of the world economy. On the other hand, financial markets have calmed down since the volatility seen in December 2018.

Table 1 | Forecast Overview

	Q1 19		Q2 19		Q3 19		2019
	q/q	y/y	q/q	y/y	q/q	y/y	Overhang*
Industrial Production	0,0	-1,3	0,2	-1,1	0,2	-0,8	-0,7
Gross Domestic Product	0,2	1,0	0,3	0,9	0,3	1,0	0,9
Private Consumption Expenditures	0,3	0,8	0,4	1,0	0,4	1,3	1,0
Gross Fixed Capital Formation	0,3	3,1	0,4	1,9	0,4	1,7	1,9
Headline Inflation	-0,7	1,4	1,6	1,4	0,2	1,2	1,3

Change in %, seasonal and working day adjusted

Source: ifo-Istat-KOF Forecasts

*Overhang describes the annual growth rate when zero growth is expected for the last quarter

Methodological note

This quarterly publication is prepared jointly by the German ifo Institute, the KOF Swiss Economic Institute, and the Italian Statistical Institute Istat. The forecast results are based on consensus estimates building on common macroeconomic forecast methods by the three institutes. They are based on time-series models using auxiliary indicators from business surveys by national institutes, Eurostat, and the European Commission. The joint three-quarter forecast covers Eurozone industrial production, GDP, consumption, investment, and inflation. Further country-specific and global economic analysis is available by:

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