Global and European setting

World economic activity

Slower global economic momentum in Q2

After picking up at the start of 2012, global economic activity again weakened distinctly in the second quarter. This slowdown appears to be attributable only in part to the renewed intensification of the euro-area sovereign debt crisis. The after-effects of the sharp rise in crude oil prices in the first quarter of 2012 are also likely to have played a role. This is especially true for the United States, where the loss of purchasing power owing to higher oil prices had a much greater impact than the negative spillover effects from Europe. Moreover, domestic problems have been increasingly prominent in some emerging markets. Global industrial output in April-May stagnated at the level of the first quarter, in which it grew by 1½%. However, global gross domestic product (GDP), which tends to follow a flatter path than industrial output, is likely to have risen slightly.

Pace slower in both industrial countries and emerging markets

The second-quarter dip in global growth affected most of the major industrial countries and emerging markets. Real GDP contracted slightly in the euro area and considerably in the United Kingdom, while the rate of expansion slowed elsewhere (including the United States, Japan and China). As its slowdown was only marginal, the USA became the growth leader among the major industrial countries. According to initial estimates, after seasonal adjustment, aggregate output in the USA, Japan, the UK and the euro area as a whole in the second quarter of 2012 was only slightly higher than in the first quarter. However, it was still up by 1¼% year-on-year.

Global economic activity is likely to pick up gradually in the second half of the year, although developments on the financial and oil markets pose a risk. In such an environment, the stimuli from the still very expansionary monetary policy stance in the advanced economies and the recent loosening in the emerging markets could regain the upper hand. However, after recording two consecutive rises, the ifo indicator for the world economic climate fell significantly in the third quarter.

Minimal adjustment to IMF spring forecast

At the beginning of July, the IMF made only minimal changes to its spring forecast for the global economy from April. This was based on the assumption that the unrest on the financial markets owing to the sovereign debt and banking crisis in the euro area will ease gradually, that the sharp deficit reduction in the USA currently scheduled by the expiration of legislation next year will be softened and that the loosening of macro policy in the emerging markets will prove to be effective. The flash estimate for global GDP growth in 2012 has been lowered marginally to 3.5%. However, this is due to the fact that results for the first quarter were more favourable than expected in April as well as a subsequent considerable downward revision of growth rates for the following three quarters. In regional terms, the somewhat more cautious assessment of the outlook for growth in the major emerging markets in Asia and Latin America was an important factor here. At +1.4%, there was no change in the forecast for the advanced economies as a whole. However, broken down by country, the IMF made a distinct upward revision for Germany (from +0.6% to +1.0%), improved its outlook for Japan, but lowered the rates for the UK and the group of new industrial countries in Asia (South Korea, Hong Kong, Taiwan and Singapore) rather substantially. The global GDP forecast for 2013 was reduced by ¼ percentage point to 3.9%; the adjustments for the major economic areas were fairly even. Current forecasts for the growth of global trade, at 3.8% in 2012 and 5.1% in 2013, are ¼ and ½ percentage point lower, respectively. The IMF has left its flash estimate for prices for industrial countries and emerging markets for 2012 and 2013 virtually unchanged despite the fact that it assumes oil prices to be much lower than in its April fore-

Global industrial output and world trade

2008 = 100, seasonally adjusted, quarterly, log scale

Source: Centraal Planbureau. **1** OECD excluding Turkey, Mexico, South Korea, Poland, Slovakia, the Czech Republic and Hungary.

Deutsche Bundesbank

cast. Overall, this appears to have made the assessment of the price outlook more plausible.

Temporary sharp fall in crude oil prices

A combination of weaker demand and increased supply-side risks sent crude oil prices on a roller-coaster ride throughout the reporting period. Given growing indications of slower global economic activities, prices initially fell considerably in the spring months. On the crude oil market, the substantial expansion of production in Saudi Arabia and a temporary détente in the dispute surrounding the Iranian nuclear programme were the reasons why the price for a barrel of Brent crude oil, at times, dropped well below the US$100 mark and premiums for forward deliveries contracted. On a quarterly average, the spot quotation fell to its level of the fourth quarter of 2011. However, in July, the oil price soared, *inter alia*, as a result of resurgent political tensions in the Middle East. As this report went to press, the spot price for a barrel of Brent crude oil was US$113½ whereas oil futures were again much cheaper. From mid-2012, food prices also soared. This was due, in particular, to concerns about weather-related crop failures for corn, wheat and soybeans. By contrast, prices for industrial raw materials remained subdued, in line with the gloomier global economic environment.

… dampened consumer price inflation

The temporary sharp fall in crude oil prices abruptly halted the rise in consumer prices in industrial countries in the second quarter of 2012. After seasonal adjustment, in the second quarter, the index (aggregated according to Bundesbank calculations) stood on average only slightly above the level of the first quarter, in which it rose by 0.7%. The year-on-year level contracted by ½ percentage point and, at 1.9%, fell below the 2% mark again for the first time since the final quarter of 2010. The price of the basket of consumer goods, excluding energy and food, continued to rise moderately. The year-on-year rise of 1.6% was not much lower than in the first quarter.

Selected emerging market economies

Growth remains moderate in China

In China, the pace of overall economic growth slowed again in the second quarter. Year-on-year real GDP growth fell from 8% in the first quarter to 7½%. Above all, the expansion of industrial output slowed again considerably in the second quarter. A flatter upward trend in Chinese exports owing to weak import developments in major sales markets, especially in a number of European countries, is just one of the reasons. Much more importantly, however, Chinese domestic activity continued to lose momentum. This is especially true for investments, which had always made the largest contribution to aggregate growth over the past few years. As a result, in recent months the Chinese authorities have taken a number of measures to support the economy. First, they have shortened the government planning commission's approval process for major projects and, second, pushed ahead with the govern-

ment programme to build affordable housing. Third, they have cut the regulated lending rates for commercial banks in two stages. The monetary policy scope for cutting interest rates was provided by falling consumer inflation. In July, annual CPI inflation fell to 1.8% – its lowest rate since January 2010.

Expansion abated in India

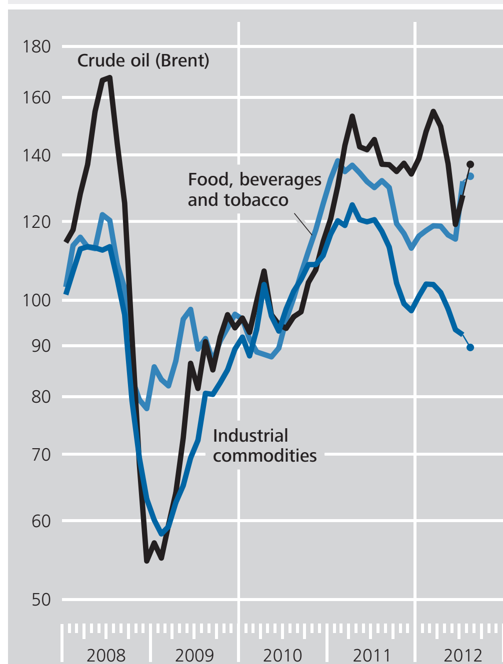
In India the upturn in aggregate economic activity again weakened considerably in the first quarter (these are the most recent data available). Year-on-year real GDP growth fell to 5½%, and thus the lowest level in three years. In the past few months, the economy is likely to have remained on this rather flat expansion path. This is indicated, not least, by slow-moving growth in industrial output. The production of capital goods, in particular, pointed sharply downwards in the second quarter, suggesting that investment demand is subdued. A notable factor seems to be that the high government budgetary deficit and the slow pace of economic policy structural reforms have increasingly undermined the confidence of investors, especially those from abroad. According to the new national consumer price index, inflation stood at 10.2% in the second quarter. As inflation remained persistently high, the Reserve Bank of India did not continue to ease monetary policy after lowering interest rates in April 2012.

Economic activity in Brazil lacking momentum

In Brazil, economic output is likely to have gone up only slightly in the spring – as was the case in the first quarter. This is indicated by the fact that output in the industrial sector, which is saddled with competitiveness problems, again fell by 1% on the previous quarter in seasonally adjusted terms. Furthermore, comparatively low growth in employment in the services sector indicates that expansion here is also subdued. To stimulate the forces for growth, the Brazilian government has announced a series of measures in recent months, including a special government investment programme for infrastructural projects. The Central Bank of Brazil has continued to cut interest rates in light of the slow economic growth and the decline in

World market prices for crude oil, industrial commodities and food, beverages and tobacco

US dollar basis, 2010 = 100, monthly averages, log scale



Sources: Thomson Reuters and HWWI. • Average of 1 to 10 August or 1 to 15 August 2012 (crude oil).
Deutsche Bundesbank

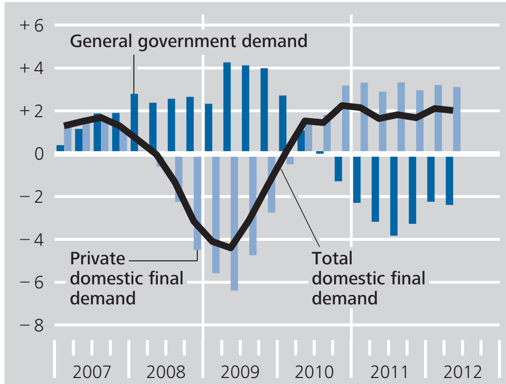
inflationary pressures. In July, consumer price inflation stood at 5.2%, compared with 7.1% in the third quarter of 2011.

Economic growth in Russia slower

Aggregate growth in Russia, as in many other countries, has lost momentum over the past few months. According to initial information from the Russian federal statistics service, year-on-year real GDP growth in the second quarter slowed to 4% after previously having amounted to 5%. This is due, in particular, to a flatter rise in industrial output, to which the marked cutbacks in oil and gas production made a contribution. Consumer price inflation, which has shown a distinct downward trend since May 2011, rose for the first time in June and July on the back of higher food prices and increases in administered prices. At last count, it stood at 5.6%.

Real domestic final demand in the United States

Year-on-year percentage change



Sources: US Bureau of Economic Analysis and Bundesbank calculations.
Deutsche Bundesbank

USA

Moderate growth path maintained …

The US economy maintained its moderate growth path in the second quarter of 2012. At just under ½% in seasonally adjusted terms, the quarter-on-quarter rise in real GDP was similar to that recorded in the first quarter. The slight slowdown is mainly due to a weaker expansion of private consumption. This, in turn, is chiefly attributable to the fact that real spending on motor vehicles fell to the level recorded at the end of 2011, likely due not least to the delayed impact of the sharp hikes in petrol prices in the first-quarter months. Given the outlook for consumption, it appears beneficial that households' disposable income has increased again considerably in real terms. Income growth in nominal terms slowed significantly because only half (329,000) the number of new non-farm jobs were created in the second quarter as in the first. Unemployment slid slightly to 8.2% on average over the second-quarter months. However, consumer price inflation diminished substantially following an easing on the crude oil market. The Consumer Price Index was up slightly from the first quarter in seasonally adjusted terms but down by almost one percentage point on the year to +1.9%. However, excluding food and energy, inflation rose slightly to 2.3%.

… despite ongoing declining government demand

Public sector demand, both at state and federal government level, fell further in the second quarter, although not to the extent experienced in the previous quarter. So far, government consumption and investment cutbacks have notably restrained economic recovery after this type of expenditure had proven to be an important means of providing support during the recession. By contrast, despite various strains, domestic private final demand in the last ten quarters has grown rather steadily at an average annual rate of 3%; however, total domestic final demand grew at a rate of only 2%. Massive tax hikes, which, under current legislation, will come into effect at the beginning of 2013 – the same time as sizeable federal spending cuts – are likely to curb private demand, too (see the box on pages 15 to 17). It is difficult to forecast the extent to which the impending drastic consolidation is already having a negative effect on the economy. Concerns are being voiced, especially in the defence industry, that the fiscal outlook is delaying the creation of new jobs and investment. Nevertheless, investment in machinery and equipment again improved somewhat in the second quarter.

Japan

Recovery still volatile

After a growth surge in the first quarter when real GDP went up by 1¼% on the quarter, Japan's aggregate output rose by a mere ¼% after seasonal adjustment in the second quarter. This slowdown was predominantly attributable to the fact that private consumption, which had previously experienced a buoyant expansion, virtually stagnated. Nevertheless, the consumption of durable goods, driven by government purchasing incentives for cars, again soared. In contrast to the previous quarter, households have now scaled back spending on other goods. Moreover, changes in inventories no longer made a contribution to aggregate growth, which was additionally reined in somewhat by foreign trade. However, both the private and the public sector substan-

Possible macroeconomic effects of the "fiscal cliff" in the United States

In recent years, temporary fiscal measures have often been advocated as a means of bolstering economic activity. What is generally overlooked, however, is that, while growth is boosted as a result of implementing such measures, it is also dampened when the measures have run their course. Under current law, the turn of 2012-13 will see various stimulus measures and tax breaks – some of which go back as far as 2001 and 2003 – expiring at the same time as automatic spending cuts take effect as part of consolidation efforts. The very fact that the term "fiscal cliff" has been coined to describe this situation points to the far-reaching effects on the US economy which are expected to stem from this abrupt reduction in the deficit.

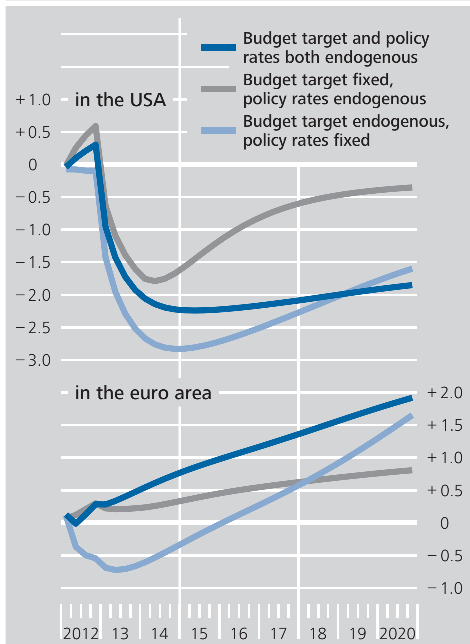
According to Congressional Budget Office (CBO) data, the combined measures would improve the balance of the US federal budget next year by 5% of gross domestic product (GDP). As the vast majority of new provisions will enter into force at the start of the year, an extensive and sudden consolidation on this scale would result in a contraction of aggregate US output in the first half of 2013. Not only would this be a technical recession, ie two successive quarters of negative economic growth; it would also meet the more comprehensive definition of a recession as applied by the National Bureau of Economic Research. Over the course of 2013, ie looking at the fourth quarter compared with the same quarter in 2012, US real GDP growth could, according to the CBO, be dampened by 1 to 6¾ percentage points, or by an average of 4 percentage points.[1] The CBO arrives at these figures by determining both model-based and historically derived multipliers for the individual fiscal measures. The cited range illustrates the uncertainty that is generally associated with such estimates.[2]

Simulations using NiGEM, the global economic model of the National Institute of Economic and Social Research (NIESR), are presented below. They make it possible not only to derive the short-term domestic effects of fiscal measures in a consistent, theoretically substantiated and econometrically estimated model framework with forward-looking agents in major markets, but also to analyse international spillover effects and long-term effects. The starting point for the simulations is provided by the CBO data on the scale of the individual measures. On the assumption that these will be implemented at the beginning of 2013, the measures are redistributed from the fiscal year, which runs from 1 October to 30 September, to the calendar year. In line with this, the income tax rate, transfer payments and (real) government consumption, all of which are contained in NiGEM, are permanently shocked. To do this, the long-term budget target, which in itself guarantees an equilibrium path of public finances in the model, is first endogenised in order to allow a sustained improvement in the budget balance. The simulations already start at the beginning of 2012 in order to identify any anticipatory effects, insofar as they can be captured in NiGEM.

1 See Congressional Budget Office, Economic Effects of Reducing the Fiscal Restraint That Is Scheduled to Occur in 2013, May 2012.
2 See F Reichling und C Whalen, Assessing the Short-Term Effects on Output of Changes in Federal Fiscal Policies, CBO Working Paper 2012-08.

Impact of the scheduled consolidation in the United States on real GDP according to NiGEM simulations

Percentage deviation from baseline



Deutsche Bundesbank

These, too, show the operation of strongly contractionary forces which may be sufficient to drag the US economy into a technical recession in the first half of 2013. Compared with the baseline, the growth rate of real US GDP in the course of 2013 will be dampened by 2¼ percentage points and its annual average rate by 1¾ percentage points. One key reason output losses will be significantly lower than in the CBO's estimates is likely to be the endogenously derived interest rate path. As general government demand for credit will decline in the long run, the real long-term interest rate will fall and private investment activity will pick up, thus cushioning the retarding impacts. As the agents in the financial markets ultimately behave in a forward-looking manner, the real long-term interest rate will already begin to fall at the announcement of drastic consolidation measures. This will lead to a slighty positive effect on aggregate output in 2012. On the other hand, the CBO assumes that heightened uncertainty about the outlook for the economy will hold back growth by roughly 1⁄10 percentage point in both summer and autumn of this year. As a confidence channel has not been built into NiGEM, such effects cannot be simulated in the model, however.

On the other hand, embedding the US economy in a global framework can yield other insights. For example, the decline in US interest rates in combination with the forward-looking behaviour of the agents in the forex market causes an immediate depreciation of the US dollar against other currencies. This depreciation is so sharp that US consumer prices – despite dampening effects stemming from the real economy – show a clear rise in comparison with the baseline. For this reason, the Fed initially responds to the announcement of consolidation by means of a considerable increase in the nominal federal funds rate, before this is reversed again in connection with the recessionary tendencies from 2013 onwards. Nevertheless, the endogenous interest rate adjustment – the long-term interest rate relevant to investment decisions arises from the expected future short-term interest rates – plays an important role in stabilising aggregate output. Thus, the medium-term output losses are markedly higher still in a simulation in which policy rates are fixed over a longer period of time.[3]

The lower aggregate demand in the United States and the euro's appreciation, which is a mirror image of the US dollar's depreciation, do, in and of themselves, place a

3 It should be noted, however, that fixing policy rates in the model represents a deception of the forward-looking agents in the financial and labour markets. In view of a shock which dampens aggregate demand, they expect an interest rate cut. In the end, it is this monetary policy shock which causes the additional output losses.

strain in the short term on economic activity in the euro area. In the wake of cheaper imports, however, euro-area consumer prices decline considerably compared with the baseline, thereby flattening the path of policy rates.[4] In the long run, economic activity on this side of the Atlantic will increase clearly compared with the baseline, in fact, and will grow at least somewhat in the world as a whole. Ultimately, the decisive factor is a global "crowding in" via an immediate lowering of the real rate of interest, which stimulates private investment in particular.

In this connection, the long-term effects on output depend on how sustained the underlying fiscal shocks are. On the assumption that they persist, the US fiscal balance shows a steady improvement compared with the baseline and the government debt to (nominal) GDP ratio will fall sharply. If, however, the budget target is endogenised only for two years, and, say, a deficit target of 2% of GDP is set, to achieve which the rate of income tax is also endogenised, most of the tax hikes will have been reversed again over the passage of time in the simulation. This means that, in the United States, the output losses become smaller compared with the baseline: in 2023, aggregate output will only be ¼% lower along with a simultaneous halving of the budget deficit to GDP ratio to the stipulated 2%.

All things considered, we find that stepping over the "fiscal cliff" will pose a temporary setback for the aggregate upturn in the US economy, but not necessarily for global recovery. In the long run, the US federal budget would be restored to health and the global interest rate level would fall. What should also be taken into consideration is that uncertainty about the long-term direction of US fiscal policy would cease to be a factor – one that is possibly placing a strain on economic activity at present.

Admittedly, there are various reasons to interpret the simulation results with caution. For example, no consideration has been given here to a not-improbable scenario in which the fiscal measures are in force only for a few weeks or months before a newly elected Congress ends up deciding to "backpedal" on consolidation. Distribution effects in conjunction with tax hikes and their effects on the economy as a whole have also been left aside. Since, in general, the current legislation is not anticipated to be implemented in full, it is doubtful whether monetary policy could actually cushion the dampening effects of these measures on the economy in time and on the outlined scale if, against all odds, the measures were indeed implemented in full. Confidence effects are not generally modelled in NiGEM: they therefore play no part in the simulations, either in the run-up to consolidation or in transmitting negative stimuli to the euro area. Nor is it possible, on the other hand, to model the macroeconomic dislocations of a crisis of confidence that, in an alternative scenario, could arise if the US federal government budget deficit were not comprehensively reduced in the near future. Prolonging the *status quo* might prevent a technical recession in the first half of 2013, but, for the time being, could also cement uncertainty about the long-term fiscal outlook.

4 The zero lower bound of the nominal policy rate is invariably maintained, however. Since it is assumed in the baseline that the policy rate will return to normal over time, there exists sufficient scope to ease monetary policy via a flattening of this (expected) interest rate path.

tially stepped up gross fixed capital formation, driven by reconstruction efforts following the devastation caused by the catastrophe in 2011. In addition to the volatile but continued economic recovery, the situation on the labour market eased. At 4.3% in June, unemployment fell to its lowest level since September 2011. Furthermore, the consumer price deflationary tendencies weakened somewhat. The price of the basket of consumer goods excluding energy and food fell by 0.5% on the year in the second quarter and therefore slightly less than in the first quarter. In total, the Consumer Price Index was 0.2% up on the year.

United Kingdom

Recession driven by downturn in construction

According to an initial estimate, aggregate output in the United Kingdom fell in the second quarter of 2012 by a seasonally adjusted ¾% from the first quarter. It was thus at its lowest level since the first quarter of 2010 and 4½% short of the high recorded in the fourth quarter of 2008. This substantial contraction of late is also due to special factors, in particular an additional public holiday to celebrate the queen's jubilee.[1] Construction was again the largest contributor to the contraction in GDP; output in this sector was nearly 10% down on the previous year. However, the sovereign debt crisis on the continent, often cited in public debate, is not likely to have had any discernible impact on this sector, which has virtually no cross-border ties. Monthly indicators are instead pointing to a sharp reduction in new public sector construction projects as a result of fiscal consolidation efforts and the end of preparations for the Olympics. Output in the rest of the production sector was down on the quarter in the second quarter but by no means by as much as in the construction sector. In the services sector, output remained virtually unchanged. Real gross value added in the public sector even increased further. The labour market also weathered the downturn in overall economic activity. Unemployment in May was at its lowest level since June 2011 (8.0%). The ongoing easing of the price climate was reflected in a fall in inflation according to the Harmonised Index of Consumer Prices (HICP) from 3.5% in the first quarter of 2012 to 2.8% in the second. Core inflation (excluding energy and unprocessed food) also fell to its lowest level since the fourth quarter of 2009 (2.3%).

New EU member states

Moderate aggregate growth

Economic output in the new EU member states as a whole (EU-7),[2] which stagnated in the first quarter, is likely to have increased moderately in the three-month period just concluded. For instance, following a sideways movement in the first quarter, real GDP was up by ¼% in Bulgaria and ½% in Romania. In Poland, for which no national accounts figures are yet available, overall economic output is likely to have again seen an expansion. However, despite positive effects stemming from jointly hosting the UEFA European Football Championship, economic activity was probably slightly weaker than in the first quarter of the year. By contrast, the Czech Republic and Hungary recorded a further decline in GDP (both -¼%). In most countries in this region, the situation on the labour market has changed only marginally over the past few months; at last count, the aggregated unemployment rate amounted to 9.7%. In this group of countries, consumer price inflation fell from 3.8% in the first quarter to 3.5% in the second quarter. It ranged from 1.8% in Bulgaria to 3.9% in Poland and 5.5% in Hungary, where the increase in turnover tax from 25% to 27% came into effect at the beginning of the year.

1 As this public holiday was in June and most data are not yet available for this month, this has also increased the uncertainty associated with the initial official GDP estimate. The likelihood of a distinct revision is thus greater than usual.
2 This group comprises the non-euro-area countries that joined the EU in 2004 and 2007.

Macroeconomic trends in the euro area

Slight decline in GDP in Q2 …

Euro-area economic output declined somewhat in the second-quarter months, representing a continuation of the downturn which began in the final quarter of 2011 and was interrupted in the first quarter of 2012 only thanks to solid growth in Germany. In seasonally adjusted terms, real GDP fell in the second quarter by ¼% on the quarter and ½% on the year. Negative economic growth in the second quarter is attributable, *inter alia,* to the continued deterioration of the economic situation in the euro-area periphery. This was due, first, to the uncertain political situation in Greece between parliamentary elections which, at times, brought the already faltering reform process to a complete standstill. Second, the sovereign debt and banking crisis intensified in Spain and Cyprus in particular, and the recession in Italy continued unabated. The negative trends in these countries continued to undermine confidence and to have a direct affect on aggregate demand in the other euro-area states via the foreign trade channel. Economic growth in the euro area was further hit by the fact that international economic ties provided a much smaller boost to growth than in the first quarter.

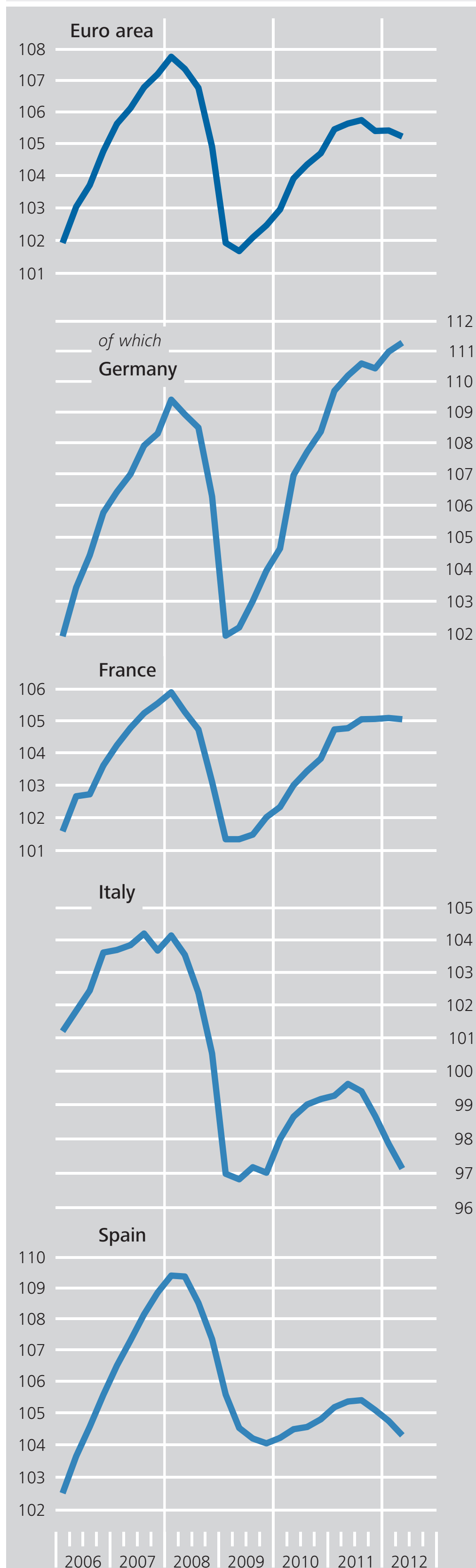
… and situation still heterogeneous across countries

According to the figures for 13 countries available to date, while GDP grew in Germany (¼%) and in a number of smaller countries and stagnated in France, it fell considerably in Italy (¾%), Spain (½%), Portugal (1¼%) and Cyprus (¾%). The economies in Belgium and Finland have also contracted this year for the first time. In Greece, where the Statistical Authority no longer publishes seasonally adjusted figures, GDP was 6¼% down on the year and 17½% down on the pre-crisis level. In the euro-area countries excluding Germany, working-day adjusted aggregate output has fallen by no less than 1% since the second quarter of 2011.

The available leading indicators, which are mostly based on surveys, do not point to a cyclical improvement any time soon. In July, the

Aggregate output in the euro area

2005 = 100, seasonally adjusted, quarterly, log scale



Source: Eurostat.
Deutsche Bundesbank

No sign of imminent turnaround revealed by leading indicators

Purchasing Managers' Index for manufacturing was still well below the expansion threshold. Furthermore, surveys of industrial confidence conducted on behalf of the European Commission continued to signal a downbeat mood. Above all, output expectations and the assessment of the order books took a further turn for the worse last month. Subsequently, aggregate output is expected to again record a moderate decline in the third quarter and, at best, a slight upturn is forecast for the last quarter. This will result in a contraction of somewhere between ¼% and ½% for 2012 as a whole.

Renewed fall in output for industry

Broken down by sector, in the spring the economic slowdown in the euro area was focused on manufacturing (excluding construction). Output in this sector fell by a similar amount (½%) as in the previous quarter and was 2½% down on the year. With the exception of the energy sector, where output increased by a seasonally adjusted 1% from the first quarter, all major industrial sectors were affected by this fall. Capital goods production was particularly hard hit – namely by 1½%. The production of intermediate and durable goods both went down by ¾% and that of non-durables stagnated at the level of a quarter earlier. The negative growth of industrial output in the second quarter entailed a renewed fall in capacity utilisation in manufacturing, removing the latter even further from its long-term average. In April-May, construction output was ¼% down on the average first-quarter level, although the prolonged period of frost in February in the more northerly member states had resulted in distinct weather-related restrictions.

Exports key pillar of economy

On the demand side, the only notable positive boost that the euro area received in the second quarter came from exports. Seasonally adjusted nominal sales to non-euro-area countries increased in the second quarter by 2% on the quarter and 9% on the year. Nominal imports, by contrast, fell by ¼% on the quarter and were up by only 2½% on the year due to persistently weak domestic demand and lower prices for crude oil and other commodities on the international markets. In unadjusted terms, euro-area foreign trade's contribution to growth is likely to have been positive in the second quarter. On the other hand, given the declining manufacture of machinery and equipment and the slowdown in construction activity, gross fixed capital formation is likely to have continued its downward slide. Similarly, lower real retail sales and new car registrations in the second quarter indicate that private consumption probably trended slightly downwards in the reporting period. According to the most recent consumer confidence surveys, consumption is not expected to pick up in the near future.

Unemployment continuing to rise in crisis countries

The labour market situation in the euro area deteriorated further in the second quarter. Seasonally adjusted standardised unemployment went up by approximately 400,000 from March to June when it totalled 17.8 million; at last count, it was 2 million higher than one year previously. The corresponding unemployment rate rose from 10.9% in the first quarter to 11.2% in the second. Unemployment growth appears to have slowed in a number of crisis countries in the second quarter; however, this contrasts with a weaker fall overall in the euro area and a slight rise in member states with relatively favourable economic growth. The number of persons in work in the euro area, which fell in seasonally adjusted terms by 0.2% in the first quarter of 2012, is likely to have slipped further of late.

Slower rise in consumer prices

In the second quarter of 2012, consumer prices rose at a much weaker pace (0.5% after seasonal adjustment) than in either of the two previous quarters. As the quarter progressed, this figure even fell to 0.1%. This was chiefly due to a steep fall in energy prices in May and June. Prices for other goods and services went up by just as much as in the previous quarter. Year-on-year headline HICP inflation was down from 2.7% to 2.5%. Annual inflation was particularly high in Italy (3.6%). However, this was due to various increases in taxes, social contributions and administered prices. HICP inflation in

France (2.3%) was slightly and in Spain (1.9% – due to the economic crisis) perceptibly below the euro-area average. In July, consumer prices were up again in seasonally adjusted terms owing to rising crude oil prices. The year-on-year rate persisted at 2.4%, as in the two previous months.