Eurozone growth forecasts cut

■ European Commission blames high oil price and strong euro ■ Headline figure down from 2% to 1.6% ■ Germany and Italy expected to fare the worst

By Ralph Atkins in Frankfurt and Raphael Minder in Brussels

Surging oil prices and the strong euro have forced the European Commission to cut substantially its forecast for eurozone growth this year, heightening fears about the global impact of the slowdown.

The Commission said it expected eurozone growth of just 1.6 per cent in 2005, compared with its forecast last October of 2 per cent and the 2 per cent estimated growth in 2004.

Among the more dramatic downgrades, the Commission expected growth of only 0.8 per cent this year in Germany, compared with 1.5 per cent forecast previously, and 1.2 per cent in Italy, compared with its former prediction of 1.8 per cent growth. The forecast for the UK, which is not in the eurozone, was unchanged at 2.8 per cent.

The cuts came as John Snow, the US Treasury secretary, described high energy prices as "extraordinarily unwelcome".

"The American economy seems to be on a good path but I do worry about energy," he told a conference. "We're not an economy geared to $60 [a barrel] oil."

Underscoring official concern about continuing high oil prices, the Commission's report warned that the "persistence of higher oil prices and their increased volatility have adverse implications for the growth outlook over the forecast horizon".

The Commission pointed out that industrialised countries had reduced their oil dependence since previous oil shocks. But the downgrades were a blow to EU policymakers after last month's Brussels summit attempted to revise the continent's competitiveness agenda.

Michael Hume, economist at Lehman Brothers, said the eurozone was "like an albatross" around the neck of the global economy. "The eurozone is not going to be doing much in terms of contributing to world trade or addressing global imbalances."

Brussels' revisions follow similar moves by the International Monetary Fund and the European Central Bank. But its forecasts remained more optimistic than those of many private sector economists, particularly after economic indicators in the past few weeks. Eurozone purchasing managers' indices last week pointed to near stagnation in manufacturing.

Joaquin Almunia, European Union economics commissioner, was upbeat yesterday about the composition of EU growth over the next two years. "In 2005, the recovery will change from an external demand impulse to an internal demand impulse," he said. "Private consumption and investment will contribute in a bigger way. In some important countries, there is a situation of pent-up demand."

The Commission also foresaw an acceleration in employment growth, which was "expected to create 3m new jobs in the EU during 2005-06". The eurozone unemployment rate would remain at 8.8 per cent this year, before falling to 8.5 per cent in 2006.

The Commission observed widening differences within the eurozone last year. Robust consumption growth had boosted France and Italy, compared with Germany and Italy, it said. The French economy was forecast to grow by 2 per cent this year, after 2.5 per cent in 2004, and the Commission expected it to grow above the eurozone average again in 2006.

For 2006, the Commission forecast eurozone growth of 2.1 per cent.

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AIRLINES FACE $5.5BN LOSS THIS YEAR AS FUEL COSTS SURGE, WARNS IATA CHIEF

The global airline industry could lose $5.5bn (€4.2bn) in 2005 because of continuing high crude oil prices, according to a warning delivered yesterday by Giovanni Bisignani, chief executive of the International Air Transport Association, write FT reporters.

The total losses by the world's airlines in the five years from 2001-05 would then exceed $40bn, threatening the survival of several US airlines in particular.

The forecast $5.5bn loss for 2005 is based on an average price of $43 a barrel for the European benchmark Brent crude.

The May Brent crude futures contract rose yesterday by $9 cents to $57.10 a barrel on the International Petroleum Exchange in London.

The US benchmark West Texas Intermediate for September delivery hit $60.05 a barrel in New York – a record high for any oil futures contract in nominal terms and more in real terms than the first oil shock in the early 1970s and during the first Gulf war.

The oil price surge was most marked in futures contracts delivered over the summer, when increased driving and travel most affects global oil demand.

In his speech to the AirFinance conference in New York, Mr Bisignani warned that the air transport industry remained "fragmented, constrained and quite frankly in many places a financial disaster". He urged governments to deregulate the industry and open it to global capital markets; to reduce the burden of taxation and to regulate monopoly suppliers, such as airports.

"We see record profits at airports, when airlines have record losses. Airlines do the flying and everybody else makes the money," Mr Bisignani said.

He added that with annual growth of 6 per cent, global air passenger traffic was growing at twice the rate of gross domestic product. "The problem is that the more we sell, the more we lose."

With fuel now accounting for 20 per cent of costs, around 30 per cent of the costs facing airlines were outside their control, said Mr Bisignani.

Reporting by Kevin Done, Kevin Morrison and Javier Blas in London