Consumer prices rose by 0.4% in July, while the annual rate of inflation fell by 0.1 of a percentage point to 3.8%. July's rise was underpinned by prices influenced by seasonal fluctuations (package holidays, food and non-alcoholic beverages, and clothing and footwear) as well as another increase in excise duties on tobacco and the rise in liquid fuel prices. Higher oil prices (going up by about 37% this year) can account for practically the whole difference between the projected and actual annual inflation rate. Despite the significant rise in oil prices, these prices still seem to be causing mainly direct effects, while any strong indirect effects or rises in other prices caused by expensive oil have not yet been recorded. Hence, the narrow inflation indicators continue to fall gradually.

The **European Commission** published its Quarterly Report on the Euro Area in July, analysing the general economic situation as well as the **impact of high oil prices** on the euro-area economies. It estimates that this year's rise in oil prices should not have a particularly big negative impact on economic growth in the euro area: a 25% rise in oil prices could reduced GDP growth by 0.3 of a percentage point in the euro area this year and push inflation up by an average of 0.2 of a percentage point (see p. 19). It should be noted that if the level of end-June prices is retained (USD 35 per barrel), oil prices would rise by 12% compared to the average of 2003 (11% more than assumed in the European Commission's spring forecasts).

The European Commission also estimates that a **recovery of euro-area economies** did take place in the first quarter, including the three largest member-states and Slovenia's most important trading partners: Germany, France and Italy. The 1.3% year-on-year GDP growth chiefly stemmed from accelerated export growth, resulting from robust global demand, and an increased rise in private consumption seen for the first time after 2001, while the impulse of investment consumption was weaker than in the last quarter of 2003. All short-term economic indicators show positive trends, especially those for the industrial sector, while household confidence indicators reflect greater uncertainty. This implies that a strong acceleration of economic activity is unlikely to happen in the short run, while the recovery seems stable and sustained. Hence, the European Commission estimates that the forecast of 1.7% economic growth for 2004 is realistic.

These developments in the EU are in line with the assumptions of the IMAD's spring forecasts for 2004, and the **current economic indicators for Slovenia** are in line with expectations. While data on merchandise trade for May are still unavailable because of changes in the monitoring of export-import flows due to Slovenia's membership in the EU (see p. 4), favourable export trends are estimated to have continued from the first four months, coupled with robust growth in manufacturing's production volumes (see p. 14). Short-term indicators for the second quarter show that strong growth in private consumption continued from the end of 2003 (see p. 13): employment rose in April and May (see p. 10), household borrowing from banks continued to increase fast in the second quarter and recorded its strongest growth after 1999 in the first six months of this year (see p. 8), while savings growth was at an all-time low (see p. 7). Domestic banks' high external borrowing was maintained in May (see p. 4). Corporate external borrowing seen in the first five months was lower than in the same period last year, however, corporate foreign currency borrowing from domestic banks retained high growth rates throughout the first six months (see p. 8). The gross wage per employee rose by 2.9% in real terms in the private sector and fell by 1.8% in the public sector in the first five months over the same period last year (see p. 11).

The Slovenian government submitted the **draft Strategy of Slovenia's Development** for public debate in July. Its main target is that Slovenia should achieve the average level of development of the enlarged EU within ten years. Economic growth will therefore have to be increased by at least 1.5 percentage points. This can be achieved by combining investment in three areas, each contributing about a third: (a) investment in people – improving the educational attainment structure (human capital) and raising the employment rate; (b) investment in technological development – improving the economic effectiveness of investment in R&D and increasing expenditure on R&D to 3% of GDP and; (c) improving the institutional framework – creating an environment that fosters entrepreneurship and foreign direct investment – deregulation, bolstering the economy's competitiveness, boosting labour market flexibility, privatisation or the improved regulation of infrastructure activities, and improving the efficiency of both the public and government sectors.