



Date: **October 24, 2008**
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MANUFACTURING FIRMS' CONFIDENCE PLUNGES IN OCTOBER

- The seasonally adjusted confidence index (2000=100) fell to 77.7 from 81.8 in the previous month, reaching its lowest value since September 1993
- Italian entrepreneurs were decidedly more pessimistic about the current state of demand and production prospects. Inventories edged down, though only moderately
- Confidence declined across all main productive sectors. The index dropped from 80.3 to 74.9 for investment goods and from 78.5 to 73.2 for intermediate goods, while it declined more moderately for consumer goods (from 87.1 to 83.9)
- At the regional level, the fall was particularly noticeable in the North West (from 81.1 to 75.3), whereas it was less marked in the North East (from 81.5 to 78), the Centre (from 85.7 to 83.4) and the *Mezzogiorno* (from 85.2 to 80.9)
- In a long-term perspective, manufacturing firms' confidence came in clearly higher than during the severe recessions of the early seventies and eighties. However, the index was close to the low posted during the 1993 crisis and was already markedly lower than immediately after the September 11 terrorist attacks and during the recession of the early 2000s

IN THE 3Q 2008 INDUSTRIAL PLANT UTILIZATION CONTINUES TO DECLINE

- The rate of operating capacity decreased from 75.7% to 75.4%, reaching the low recorded in the second quarter of 1999. Accordingly, also the number of work hours diminished and the share of respondents considering their rate of capacity utilization "more than adequate" increased
- Negative indications came from the flow of new orders as well. Moreover, the proportion of firms complaining of obstacles limiting productive activity rose, especially because of insufficient demand
- Short-term expectations for the volume of exports also abruptly fell and firms' perception of their competitive position worsened
- Lastly, the length of production assured by current order books diminished and inventories of raw materials and semi-finished products edged down

MODERATE SIGNALS OF TIGHT CREDIT FOR MANUFACTURING FIRMS EMERGES

- According to the September survey, in the third quarter of 2008 the share of firms complaining about deteriorating conditions for access to bank credit increased
- Among those who sought funding, the proportion of firms that failed to obtain bank credit increased (to 8% from 6.9% in June)
- The failure to obtain credit was mainly caused by explicit denial by the bank (for 5.8% of the sample) and, to a lesser extent, by firms' refusal of too onerous credit terms (for 2.2% of the cases)

Data on November shall be released on November 26, 2008

The next ISAE surveys are scheduled as follows:

October 28: *ISAE Monthly Survey on Traditional Retail Trade and Large Distribution (reference period: October), ISAE Monthly Business Services Survey (reference period: October) and ISAE Monthly Survey on Construction (reference period: September)*

November 5: *ISAE International Comparison of Consumer and Business Surveys (reference period: October)*

The full text of ISAE Surveys (either hardcopy or electronic format) is available for sale (for further information see the web site www.isae.it)

General results

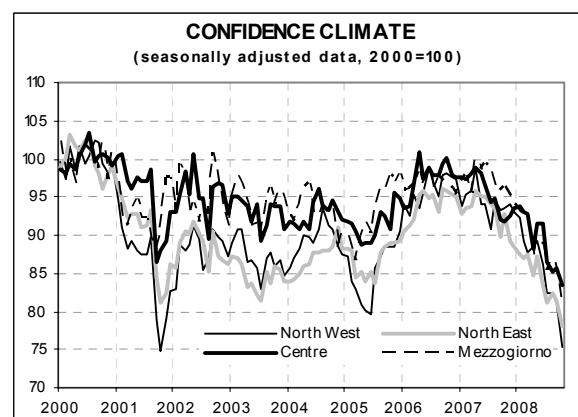
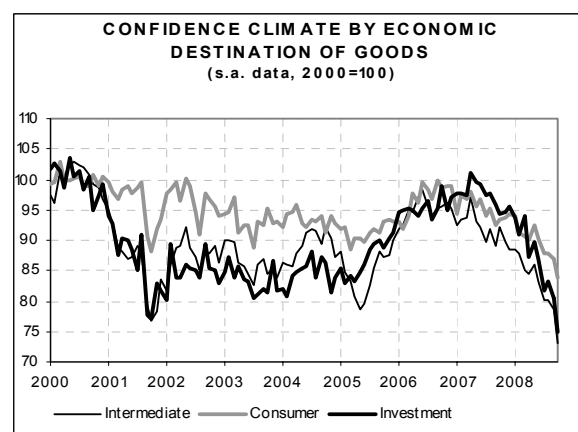
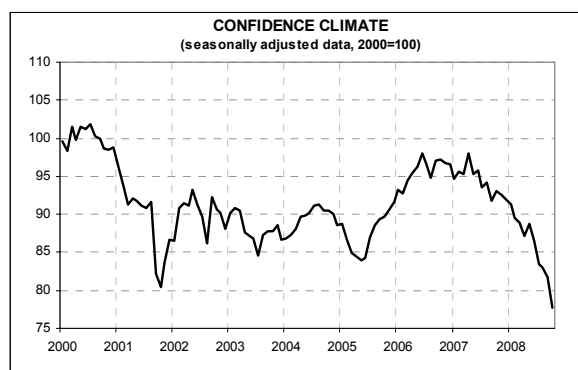
According to the ISAE Survey, carried out on a panel of about 4000 firms between October 1 and October 20, the confidence climate of manufacturing and mining firms diminished in October. The seasonally adjusted index (2000=100) decreased from 81.8 in the previous month to 77.7, the lowest level since September 1993. The deterioration was due to the sharp drop in the opinions on orders and production expectations. Inventories, instead, edged down slightly. Also demand expectations markedly worsened while those for the country's general economic situation plummeted.

The deterioration in the confidence indicator characterized all sectors and regions. The fall was particularly sharp for investment goods (from 80.3 to 74.9, a low last reached in December 1993) and for intermediate goods (from 78.5 to 73.2, the worst result since August 1993), while confidence declined more moderately for consumer goods (from 87.1 to 83.9, also in this case a low last seen in August 1993). At the regional level, the deterioration was widespread too. The fall was particularly noticeable in the North West (from 81.1 to 75.3), whereas it was less marked in the North East (from 81.5 to 78), the Centre (from 85.7 to 83.4), and the *Mezzogiorno* (from 85.2 to 80.9).

In a long-term perspective, manufacturing firms' confidence came in clearly higher than during the severe recessions of the early seventies and eighties. However, the index was close to the trough recorded during the 1993 crisis and was already markedly lower than immediately after the 9/11 terrorist attacks and during the recession of the early 2000s.

Also the traditional ISAE quarterly survey on operating capacity gave overall negative indications for the third quarter of 2008. The rate of plant utilization decreased from 75.7% to 75.4%, hitting the low posted in the second quarter of 1999. Accordingly, the number of work hours diminished as well and the share of respondents considering their rate of capacity utilization "more than adequate" increased. Negative signals came from the flow of new orders too.

Moreover, the proportion of entrepreneurs complaining of obstacles limiting productive activity rose, especially because of insufficient demand. Short-term expectations for the volume of exports abruptly fell as well, and firms' perception of their competitive position worsened. Lastly, the length of production assured by current order books diminished and inventories of raw materials and semi-finished products shrunk.



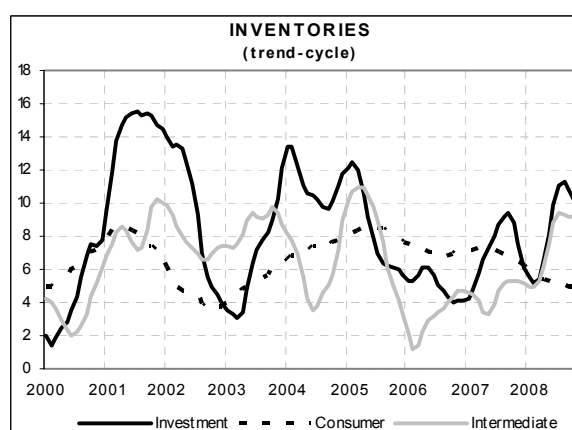
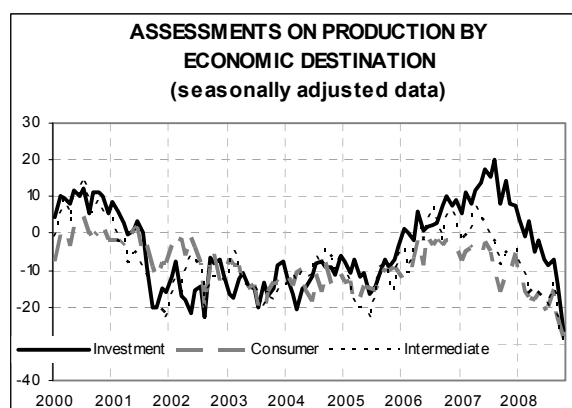
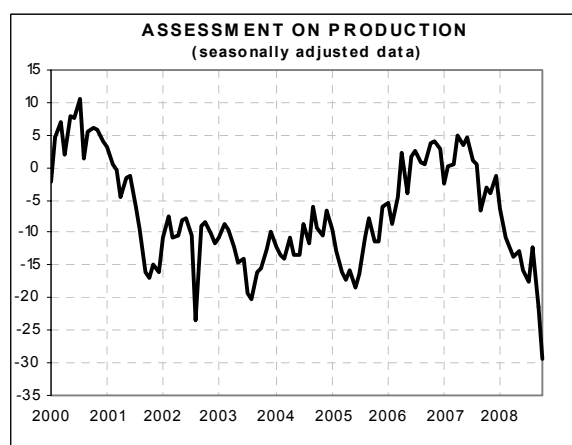
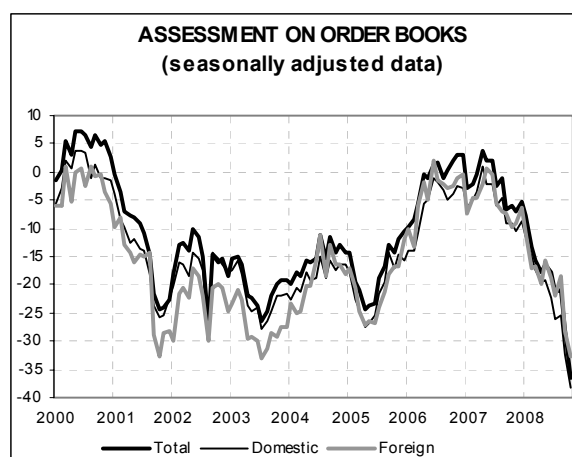
Situation in the reference period (October 2008)

In October, manufacturing firms were again more pessimistic about the current trend in orders and production. The balance for total orders declined from -28, in the previous month, to -36. Also these data confirmed that firms' assessments stood at the lowest level since the 1993 crisis. The fall in demand distinguished both domestic and, above all, foreign markets (the balance lowered from -32 to -38 and from -28 to -33, respectively). The evaluation of company liquidity sharply diminished as well, moving from -7 to -14. The opinions on the current level of production also declined (from -21 to -29). Inventories decreased somewhat (the balance lowered from 9 to 6), returning slightly below this decade's average level.

The fall in demand mainly characterized producers of consumer goods (from -29 to -34). The drop was only slightly lower in the investment and intermediate goods sectors (from -18 to -39 and from -32 to -40). As for the opinions on domestic orders, the balance fell for intermediate and investment goods (from -34 to -41 and from -30 to -38). Assessments on domestic orders of consumer goods continued instead to be negative, but they worsened less than in September (moving from -31 to -35). With regard to foreign markets, the opinions on orders of intermediate and investment goods posted a decline, compared to the previous month, similar and only slightly higher than the one for consumer goods.

As for company liquidity, the level slumped for investment goods (from 32 to 22), declined for intermediate goods (from 28 to 24), and stayed virtually stable for consumer goods.

Inventories remained basically unchanged for intermediate and consumer goods, whereas they clearly shrunk for investment goods (from 15 to 6).



Outlook for the following three months

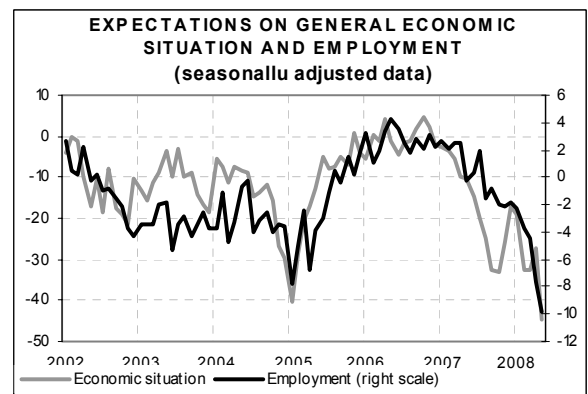
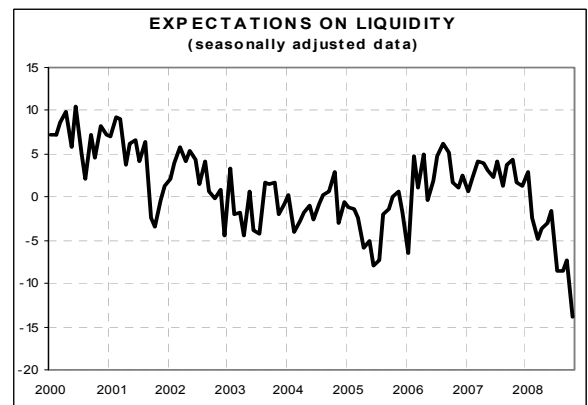
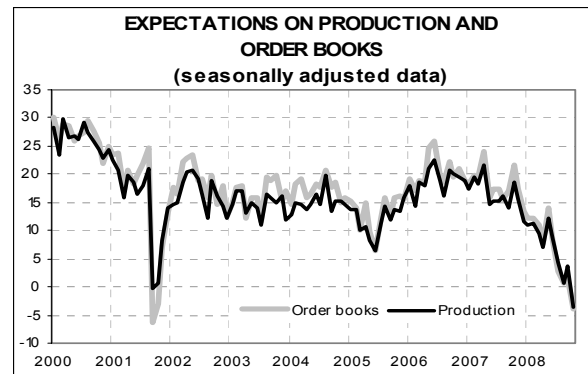
In October, prospects for main company variables and for Italy's general economic conditions markedly worsened compared to the previous month.

The balances related to expectations for orders and production decreased from 1 to -4 and from 4 to -4, respectively. Negative forecasts were predominant for the first time since September 2001. Firms also predicted a fall in employment in the following months (from -8 to -10). Moreover, expected inflationary pressures for selling prices eased (from 11 to 6). Prospects for company liquidity clearly diminished as well (from -7 to -14). Finally, a real collapse – connected to the ongoing financial markets crisis and the resulting deterioration of the general economic prospects – distinguished expectations for Italy's future economic conditions (the balance plunged from -27 to -45).

At the sector level, for consumer goods demand expectations remained stable, whereas those for production and company liquidity decreased (from 7 to 4 and from -4 to -9, respectively). Forecasts for the overall economy plummeted instead (from -27 to -49). Also in the intermediate goods sector, clearly unfavourable indications prevailed. Demand and production prospects lowered from 2 to -12 and from 2 to -9. In the same sector, firms also expected an easing of inflationary pressures (the balance for selling prices diminished from 9 to 1) and showed deep mistrust for the Italian general economic situation (from -28 to -53).

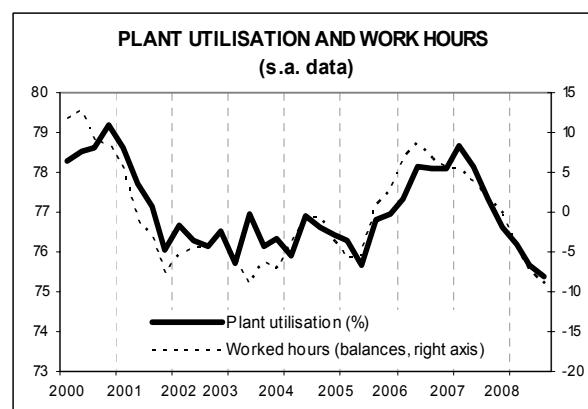
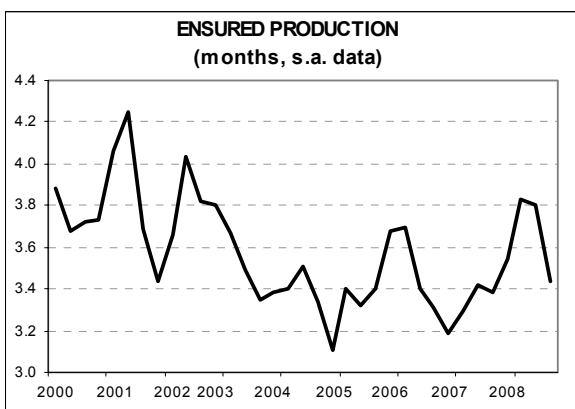
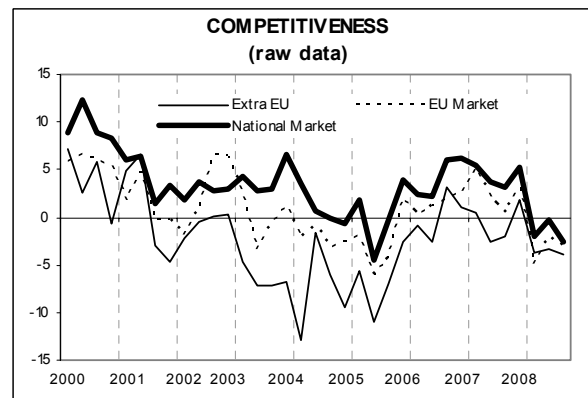
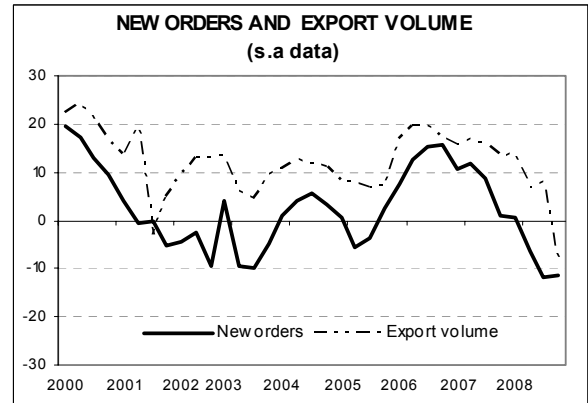
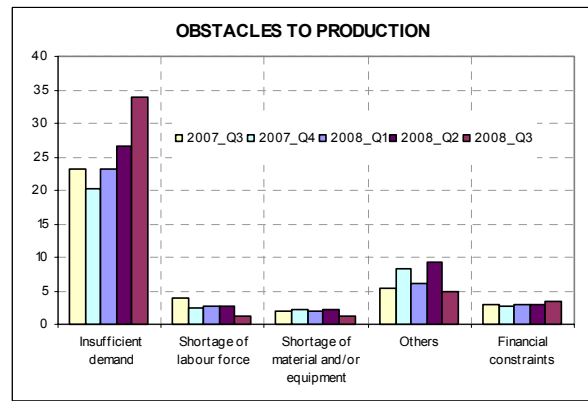
Manufacturing firms' confidence climate and balances of indicator-building series

	Confidence climate	Order-book level	Inventories	Expectations on production
July 2008	83.5	-21	10	4
Aug 2008	82.9	-21	9	1
Sept 2008	81.8	-28	9	4
Oct. 2008	77.7	-36	6	-4



Main quarterly survey results (third quarter 2008)

Also the traditional ISAE quarterly survey on operating capacity gave overall negative indications for the third quarter of 2008. The capacity utilization rate actually continued to decline, reaching 75.4%, compared to 75.7% in the previous quarter, thus hitting the lowest level since the second quarter of 1999. Moreover, the share of firms considering capacity utilization to be “more than enough” according to the level of their order books and to demand prospects further increased. Negative indications also came from the trend in the number of work hours (the balance declined from -7 to -9) and from the flow of new orders (the balance remained practically stable, in negative territory). Furthermore, with respect to factors limiting production, a further increase characterized the share of firms perceiving the existence of obstacles related to insufficient demand (from 27% to 34% of the sample). The number of firms complaining about shortage of labour force diminished instead (from 3% to 1%). Firms also predicted sharp deterioration for exports during the following quarter (the balance declined from 8 to -8), along with a moderate worsening in their competitive position, which mainly fell in the domestic market (from 0 to -3). Lastly, the length of production assured by order books decreased (from 3.8 to 3.4 months), while inventories of raw materials and semi-finished products continued to decline (from -6 to -7).



Regional breakdown of ISAE survey results

The deterioration in confidence was widely spread across the country. The seasonally adjusted index clearly dropped in the North West (from 81.1 to 75.3) and the *Mezzogiorno* (from 85.2 to 80.9), while in the North East and the Centre the decline was more moderate (from 81.5 to 78 and from 85.7 to 83.4, respectively). Opinions on orders and production expectations worsened everywhere. Inventories of finished products were however considered to be declining. The opinions on the rate of capacity utilization confirmed the overall negative situation highlighted by the confidence climate.

North West

Confidence dropped for the fifth month in a row, reaching the worst showing since October 2001. The fall was mainly due to the sharp decrease in the balance for the opinions on the level of orders (both foreign and, mainly, domestic ones) and to the worsening in production prospects. Instead, inventories of finished products diminished slightly. Also the rate of operating capacity lowered.

North East

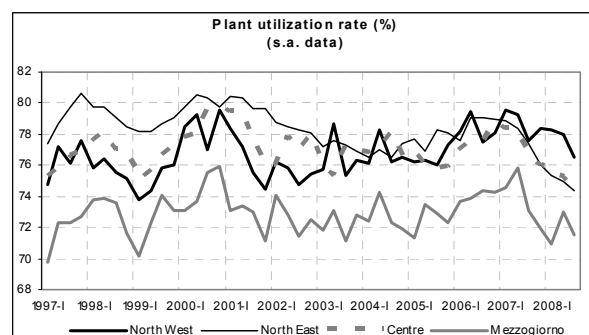
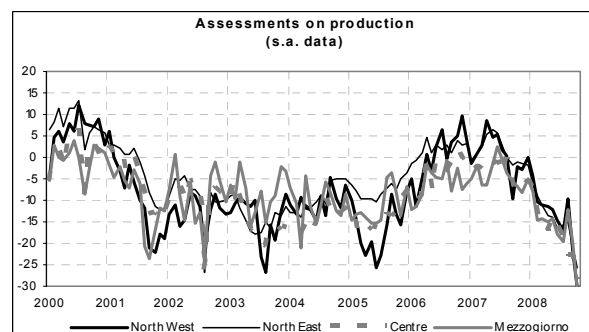
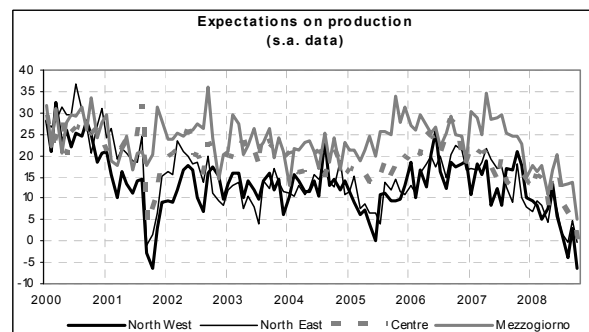
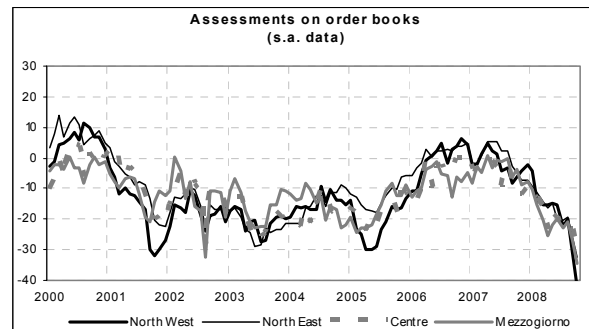
In this area, the confidence indicator deteriorated for the second straight month, coming in at its lowest level since 1996. The fall essentially stemmed from the decline in production expectations and from highly negative assessments on orders (both domestic and foreign), which came along with stability for the opinions on inventories. Also in this area, the rate of plant utilization declined.

Centre

Following the moderate recovery posted in September, confidence started to worsen once more, reverting to its May 1996 level. The opinions on demand (both domestic and foreign) and production expectations deteriorated, whereas the number of entrepreneurs considering inventories below normal levels increased. As for capacity utilization, the rate moderately declined also in October.

Mezzogiorno

In this area as well, confidence decreased for the second consecutive month, losing over five points and hitting the worst result since 1993. The fall mirrored the negative trend in the opinions on orders and in production expectations, which came along with a de-stocking of inventories. Lastly, following the recovery posted in the previous quarter, the industrial capacity utilization rate resumed a downward trend.



Focus: for manufacturing firms' access to credit

Starting from March 2008, ISAE added to the Manufacturing Firms' Survey four questions designed to assess entrepreneurs' opinions on access to bank credit. Questions were addressed quarterly in March-September 2008 and will be included monthly from next November.

The Survey showed that, in the last quarter, the share of Italian firms complaining about deteriorating credit access conditions increased (the percentage reached 27.3% of the sample, compared to 22.2% and 23.4% in March and June 2008)¹. Firms reporting worsening credit conditions were mainly those in the Centre (29.2% of the sample), followed by North Eastern ones. In the *Mezzogiorno* such a percentage visibly increased, though it remained below the national average (26%). According to firm size, credit conditions were considered particularly negative by 32.4% of medium-sized firms (26.2% of small firms and 27.9% of large ones).

However, discouragement did not seem to have emerged. Firms which formulated their opinion on the basis of direct contacts with the bank increased (reaching 49.3% of the sample, compared to 50.7% of firms which relied on their personal beliefs). Mostly firms in the *Mezzogiorno* and large-sized ones continued to make their judgement according to their personal beliefs (in both cases, nearly 60% of surveyed firms). However, a noticeable increase characterized the number of firms that contacted credit institutions for information purposes only, without actually asking a loan (30%, as opposed to 19.1% in March and 26.6% in June).

Instead, among those who actually applied for a loan, 62% obtained it, while in 8% of the cases the loan was denied. Total new loans declined compared to both March (71.5%) and June (66.5%). The share of firms which were refused credit was noticeably above the national average in the Centre (14%) and the

Mezzogiorno (10.2%). According to firm size, small firms mainly complained about failure to obtain credit (8.4% of firms which actually applied for it, compared to 6.4% for large firms and 7.6% for medium-sized ones).

The failure to obtain bank credit was mainly caused by explicit denial by the bank (for 5.8% of the sample) and, to a lesser extent, by firms' rejection because of too onerous credit terms (for 2.2% of the cases). The proportion of firms that were refused credit was on the rise with respect to March (4.3%) and June (3.3%). For firms in the Centre, the failure to obtain credit was mainly attributable to explicit denial by the bank (for 9.8% of the cases), whereas in the *Mezzogiorno* firms' refusal of excessively costly conditions was more important (5.7% of the cases). Lastly, the splitting out of data by firm size showed that the failure to obtain credit was in general due to the bank's explicit denial, but, in the case of small firms, 2.4% of the total had to refuse the loan because of too onerous credit conditions.

¹ According to the Bank of Italy-II Sole 24 Ore Quarterly Survey, carried out in September, the percentage stood at 26.7%.

Tab. 1 – Italian manufacturing firms’ opinions on credit access conditions

(percentages)

	More favourable			Unchanged			Less favourable			Don't know		
	Mar. 08	June 08	Sept. 08	Mar. 08	June 08	Sept. 08	Mar. 08	June 08	Sept. 08	Mar. 08	June 08	Sept. 08
Total Manufacturing Firms	6.0	3.9	3.5	69.7	67.4	64.2	22.2	23.4	27.3	2.1	5.3	5.0
Small Firms	7.1	4.2	4.4	69.0	66.9	65.2	22.0	23.3	26.2	1.9	5.6	4.2
Medium-sized Firms	3.1	2.5	1.7	76.4	62.4	60.0	18.0	30.0	32.4	2.5	5.1	6.0
Large Firms	3.3	3.6	1.3	69.0	72.0	63.8	25.2	20.2	27.9	2.5	4.1	7.0
North West	5.3	2.4	3.8	68.1	68.9	65.6	24.0	23.5	26.4	2.6	5.2	4.2
North East	7.7	4.9	3.8	69.3	65.7	63.6	21.6	24.3	27.7	1.4	5.2	4.9
Centre	4.7	4.6	2.6	73.4	70.0	62.8	20.5	20.7	29.2	1.4	4.7	5.4
South	5.3	6.5	2.7	72.6	62.4	63.7	18.6	24.2	26.0	3.5	6.8	7.6

Tab. 2 – Factors affecting firms’ judgement on credit access conditions

(percentages)

	Recent contacts with banks			Personal opinions		
	Mar. 08	June 08	Sept. 08	Mar. 08	June 08	Sept. 08
Total Manufacturing Firms	48.6	45.9	49.3	51.4	54.1	50.7
Small Firms	48.6	45.4	50.6	51.7	54.6	49.4
Medium-sized Firms	50.9	49.0	55.6	49.1	51.0	44.3
Large Firms	48.0	45.5	40.6	52.0	54.5	59.4
North West	51.3	47.4	52.0	48.7	52.6	48.0
North East	52.6	48.0	49.2	47.4	52.0	50.8
Centre	38.8	42.7	47.0	61.2	57.3	53.0
South	39.4	37.0	40.5	60.6	63.1	59.5

Tab. 3 – Loan obtainment or client's inquiry
(percentages)

	Loan granted - Yes			Loan granted - No			Client's inquiry		
	Mar. 08	June 08	Sept. 08	Mar. 08	June 08	Sept. 08	Mar. 08	June 08	Sept. 08
Total Manufacturing Firms	71.5	66.5	62.0	9.4	6.9	8.0	19.1	26.6	30.0
Small Firms	72.2	65.0	61.9	10.0	7.2	8.4	17.8	27.8	29.8
Medium-sized Firms	71.5	73.7	64.2	7.4	5.6	7.6	21.1	20.7	28.2
Large Firms	67.7	70.6	60.3	8.9	5.7	6.4	23.6	23.6	33.3
North West	67.1	67.0	59.9	9.7	5.1	6.6	23.2	28.0	33.5
North East	75.3	69.3	64.4	8.7	5.7	6.2	15.9	25.1	29.4
Centre	75.1	62.0	60.6	10.7	12.5	14.0	14.2	25.5	25.4
South	72.9	62.3	64.5	10.1	9.9	10.2	17.0	27.9	25.3

Tab. 4 – Reasons for credit refusal
(percentages)

	Loan denied by the bank			Client's refusal because of too onerous bank credit conditions		
	March 08	June 08	Sept. 08	March 08	June 08	Sept. 08
Total Manufacturing Firms	4.3	3.3	5.8	5.1	3.6	2.2
Small Firms	4.4	3.3	6.0	5.7	3.9	2.4
Medium-sized Firms	5.6	3.2	7.6	1.8	2.4	0.0
Large Firms	4.5	5.7	4.8	4.4	0.0	1.6
North West	4.6	2.8	5.4	5.1	2.3	1.2
North East	2.4	2.2	4.2	6.3	3.5	2.0
Centre	6.5	6.6	9.8	4.2	5.9	3.1
South	5.9	5.0	4.5	4.2	4.9	5.7

Focus: the fall in confidence in a long-term perspective

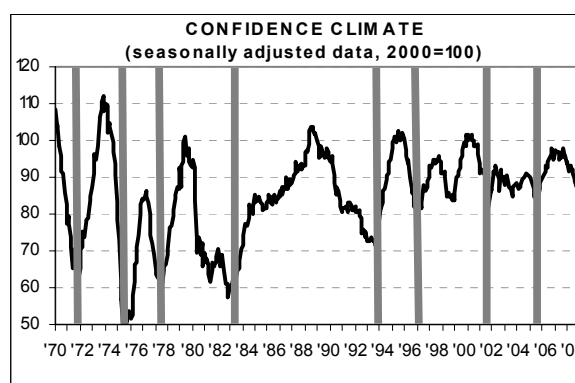
Since March 1962, ISCO and, subsequently, ISAE carried out monthly surveys on manufacturing firms. The available time series allowed to examine the current Italian industrial confidence crisis in a historical perspective. From this standpoint, the monthly fall in confidence recorded in October – though it brought the indicator back to a low last seen in September 1993 – did not constitute a particularly exceptional event. Sharper monthly falls (of about 10 points) actually occurred in periods of higher volatility of the economic cycle, in the presence of strong exogenous shocks, such as those related to the price of oil in 1973-74 and 1979-80, and after the terrorist attacks of September 2001.

On the other hand, the current value of the indicator was higher than the one reached during the deep recessions of the seventies and eighties, though it came close to the level which characterized the recession of the early nineties. More in detail, considering the dating of the Italian economic cycles proposed by ISAE², in 1970-2006 one can identify 7 points of minimum (see Table). The value of the confidence indicator recorded during the identified troughs shows that the minimum posted during the mid seventies’ cycle was 25 points lower than the current value, while the troughs of the early seventies and eighties were more than 10 points lower. However, the minimum reached by the confidence climate in the mid-nineties (the last trough recorded by the ISAE dating) was actually not very far from the current value, which is already below the September 2001 level of the indicator, following the 9/11 terrorist attacks, and the last cyclical minimum identified in February 2005.

Italian business cycle dating and confidence climate

Cycles	First trough	Peak	Last trough	Confidence climate
I	Oct-71	Mar-74	May-75	65.0
II	May-75	Feb-77	Dec-77	53.4
III	Dec-77	Mar-80	Mar-83	64.6
IV	Mar-83	Mar-92	Jul-93	62.2
V	Jul-93	Nov-95	Nov-96	71.6
VI	Nov-96	Dec-00	Feb. 05	81.6
VII	Feb-05			86.7

Source: ISAE



² See ISAE (2006), “Datazione del ciclo industriale e passaggi di regime dei settori manifatturieri”, in Rapporto ISAE “Le previsioni dell’economia italiana – l’industria tra stasi e modifiche strutturali”, Rome, February 2006 – web site: [www.isae.it/Rapporti_trimestrali/Rapporto ISAE febbraio 2006.pdf](http://www.isae.it/Rapporti_trimestrali/Rapporto_ISAE_febbraio_2006.pdf)