



DATA/Date: **May 11, 2004**  
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**AFTER THE CONTRACTION OF 2003, MANUFACTURING AND EXTRACTIVE FIRMS EXPECT A FURTHER INVESTMENT CONTRACTION IN 2004; MORE FAVOURABLE SIGNALS EMERGE FOR 2005, WHEN – ACCORDING TO MOST ISAE RESPONDENTS – THE EXPENDITURE FOR EQUIPMENT AND MACHINERY SHOULD GROW AGAIN COMPARED TO 2004**

- The Bi-Annual ISAE Investment Survey carried out between February and March 2004 and limited to firms which made investments in the three years 2002-2004, points to a nominal contraction in investments of manufacturing and extractive firms equalling to 3.4% at the end of 2003. The deterioration concerns in particular small and medium-sized firms, while expenditure of large firms has grown by about 17%
- For the year 2004, firms expect to further reduce their expenditure by about 10%, and the contraction is even larger for small and medium-sized firms (-13% for both), while large firms expect to reduce their expenditure by 7.6% (in nominal terms)
- It is worth noticing that, at the beginning of each year, ISAE respondents are generally very cautious on their prospects of accumulation for the ongoing year. As a matter of fact, over the past four years, the final balances were better than the original forecasts in three cases
- Favourable indications come from data on the investment trend for 2005: indeed, firms raise their Autumn estimates and most respondents (46% as against 13% of the previous Survey) expect a growing expenditure for equipment and machinery in 2005. Thus, the balance of this variable grows up to 18, which is the highest figure in the past 9 Surveys (March 2000-March 2004)
- With regard to the investment allocation - unlike what was signalled by last Autumn's Survey - most expenditure is aimed at the productive capacity enlargement (35% in 2004), followed by obsolete plant renewal (28%), rationalisation (25%), investments for environmental protection (7%, which are considered for the first time in this Survey) and sundry targets (5%)
- A more thorough analysis of the expenditure destination in 2004 shows an acceleration in allocations for process and product innovation. Indeed firms allocating funds for rationalisation signal their intentions to introduce new productive techniques (57% of replies as against 38% in the previous Survey), followed by investments for automation and mechanisation (47%) and investments to save energy (36%). 68% of respondents signal that their expenditure for enlargement is aimed at the introduction of new products (69% are going to insert them within the existing production processes)
- With reference to environmental protection, the 2003 investments were mainly aimed at soil, air and water protection (41% of replies), waste disposal (32%), noise reduction (18%) and nature and landscape protection (9%). In 2004 the expenditure for waste disposal prevails (33%), followed by soil, air and water protection (27%), noise reduction (17%) and nature and landscape protection (11%)
- Finally, in 2003, the percentage of respondents resorting to leasing increased (52% as against 32% in the Autumn Survey, referring to 2002). The percentage incidence of leasing on the overall expenditure for investment equalled 7.3%, which is however below the 2002 figure (11%)

*Next Bi-Annual Investment Survey will be published on December 2004.*

Next ISAE Surveys are scheduled as follows:

**May 20, 2004:** ISAE Monthly Consumer Survey (Reference month: May)

**May 26, 2004:** ISAE Monthly Business Survey on Manufacturing and Extractive Firms (Reference month: May)

**May 28, 2004:** ISAE Monthly Survey on Traditional Retail Trade and Large Distribution (reference month: April) and ISAE Monthly Business Service Survey (Reference month: May)

The full text of ISAE Surveys (either hardcopy or electronic) is available on sale (for further information see web site [www.isae.it](http://www.isae.it))

## General results

Between February and March 2004, ISAE carried out its traditional Bi-Annual Investment Survey on Manufacturing and Extractive Firms (representing about 27% of the overall expenditure for investments). The Survey – comprising only firms which invested in the three-year period 2002-2004 – gathers 830 of the 4,000 firms composing the ISAE monthly sample (about 51% of the panel in terms of workers).

According to ISAE respondents, in 2003 there was a nominal contraction in investments of manufacturing and extractive firms equalling to 3.4%. Thus the 2003 contraction eventually proved smaller than the March forecasts (-10.7%) and than the November figures (-18.6%). For the year 2004, firms expect to further reduce their expenditure by about 10% (which means less than the substantial stability expected last Autumn). Indeed, it is worth noticing that, at the beginning of each year, ISAE respondents are generally very cautious on their prospects of accumulation for the ongoing year. As a matter of fact, over the past four years the final balances were better than the original forecasts in three cases.

Favourable indications come from data on the investment trend for 2005: indeed, firms raise their Autumn estimates and most respondents (46% as against 13% of the previous Survey) expect a growing expenditure for equipment and machinery in 2005. Indeed, data broken down by firm size show that large firms are particularly optimistic.

With regard to the investment allocation - unlike what was signalled by last Autumn's Survey – in both 2003 and 2004 most expenditure is aimed at the productive capacity enlargement: in particular, in 2004, 35% of expenditure is aimed at this goal, followed by obsolete plant renewal (28%), rationalisation (25%), investments for environmental protection (7%, which are considered for the first time in this Survey) and sundry targets (5%).

A more thorough analysis of the expenditure destination in 2004 shows an acceleration in allocations for process and product innovation. Indeed firms allocating funds for rationalisation signal their intentions to introduce new

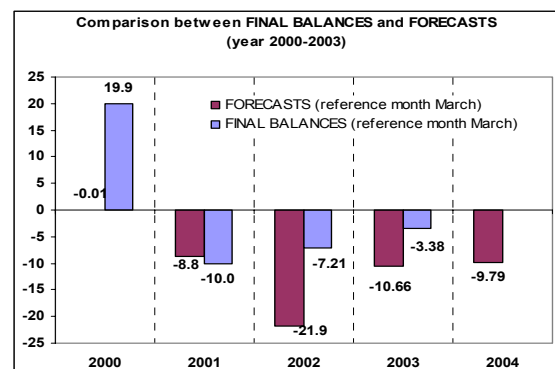
productive techniques (57% of replies as against 38% in the previous Survey), followed by investments for automation and mechanisation (47%) and investments to save energy (36%). 68% of respondents signal that their expenditure for enlargement is aimed at the introduction of new products, while 69% are going to insert them within the existing production processes.

Finally, in 2003, the percentage of respondents resorting to leasing increased (52% as against 32% in the Autumn Survey, referring to 2002). The percentage incidence of leasing on the overall expenditure for investment equalled 7.3%, which is however less than 11% in 2002.

## Investments for 2003 and forecasts for 2004

ISAE respondents signal an investment contraction in 2003 equalling 3.4% in nominal terms, which is less than the figure forecast last Autumn (-18.6%). The deterioration concerns in particular small and medium-sized firms, while the growth rate of large firms is definitely positive (about 17%).

For the year 2004, firms forecast to further reduce their expenditure by about 10%, even though, at the beginning of each year, ISAE respondents are generally very cautious on their prospects of accumulation for the ongoing year. Indeed, small firms are particularly pessimistic on their accumulation prospects for 2004, as they expect to reduce investments by about 13% (as against -11.1% forecast in November), while medium-sized firms estimate a contraction by about 13% (which runs counter the positive estimate made in Autumn, namely 4.1%). Conversely, the contraction foreseen for firms with at least 250 employees equals 7.6%, which is larger than the figure forecast in the previous Survey (4.2%).



## Forecasts for 2005

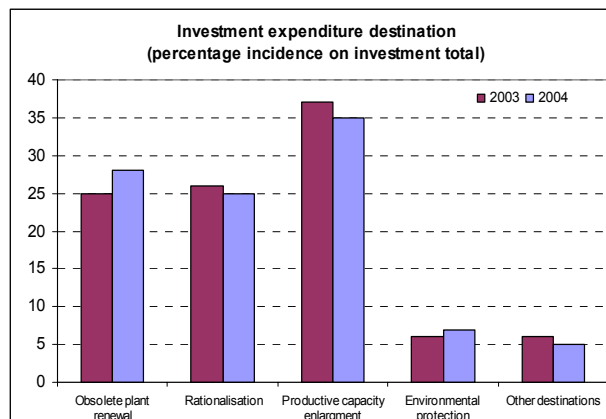
Rosier indications come from qualitative forecasts on investments for 2005. The share of firms expecting they will rise their investment expenditure (46% of the sample) is larger than the number of firms foreseeing a reduction (28%). Thus, the balance equals 18 (-32 in the Survey of October/November 2003), which is the highest figure in the past nine Surveys between March 2000-March 2004.

Data by firm size show that the optimistic approach prevails in large firms (68% of the sample intend to raise their expenditure, 15% will maintain it unchanged, while 17% intend to invest less than 2004). Conversely, most firms with less than 50 employees expect an investment contraction in 2005 (47%, while 42% will maintain it unchanged and 11% wish to raise it). Medium-sized firms are also cautious: 41% of the sample expect a substantial stability in their investment expenditure, 38% intend to diminish it and 21% declare they want to invest more than in the current year. Turning to single sectors, the optimistic approach dominates in mechanics and transport equipment (58 and 87% respectively). Quite the reverse, negative signals emerge from paper, printing and publishing (65% of negative replies), from extraction and early processing of metallic and non-metallic minerals (44% of firms wish to reduce expenditure in 2005), from various manufacturing sectors including wood and furniture (62% of the sample wish to invest less) and foodstuff (55% of negative replies). Finally, 71% of textile dealers intend to maintain the expenditure unchanged.

## Main investment destination

With reference to investment destination, unlike what signalled in last Autumn's Survey, most expenditure for 2003 and 2004 is aimed at the productive capacity enlargement. In particular, looking at data for 2004, 35% of expenditure is devoted to enlarge the firms' productive capacity, followed by expenditure for obsolete plant renewal (28%), rationalisation (25%), environmental protection (7% which is considered for the first time in this kind of Survey) and sundry destinations (5%). The analysis by firm size shows that investments aimed at obsolete plant replacement or renewal prevail in small firms (32% of expenditure in 2004, which points to a

decreasing trend compared to 40% in 2003). Conversely, expenditure for enlargement prevails in large firms (42% in 2004 compared to 47% in 2003). Finally, firms with 50-249 employees prefer to invest for the replacement of obsolete equipment and machinery (34% of expenditure).

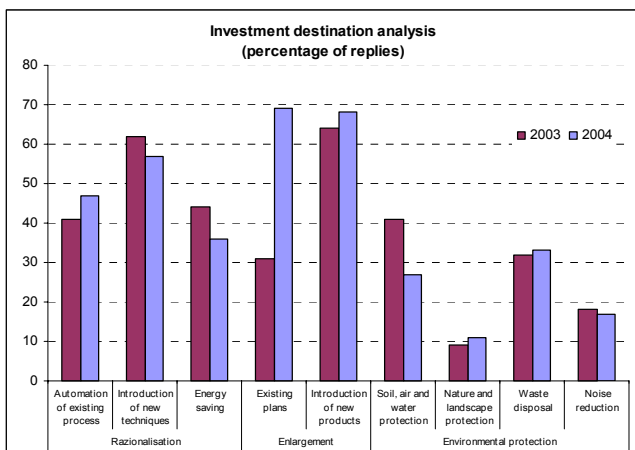


## Expenditure for productive capacity rationalisation and enlargement

A more thorough analysis of expenditure shows in 2004 an accelerating trend in process and product innovation. Indeed, firms investing in rationalisation report their intentions to invest in new production techniques (57% of replies, as against 38% of the Autumn Survey), followed by automation and mechanisation (47% as against 55% of the previous Survey) and in energy saving (36% compared to 13% of the Autumn Survey). For large firms, investments aimed at the introduction of new production techniques represent the main source for rationalisation expenditure: 64% of respondents indicate they spend for that target, as against 28% who invest for the existing process automation and 59% who invest to save energy. The main rationalisation target for small and medium-sized firms is the automation of existing processes (according to 66 and 71% of respondents respectively). However, also small (52% of respondents) and medium-sized firms (47%) attach a considerable importance to expenditure for new production processes.

With reference to enlargement, 68% of firms (45% in the previous Survey) devote expenditure to the introduction of new products and 69% of respondents (41% in Autumn) allocate it for enlargement within the existing production

process. By breaking down data by firm size, it emerges that the introduction of new products brings about investments in large firms in particular (83%), while small and medium-sized firms prefer to invest in the productive capacity enlargement within the existing production processes.



### Expenditure for environmental protection

Starting from the present Bi-Annual Investment Survey of Spring 2004, ISAE includes environmental protection among the possible investment destinations. This means investigating from a qualitative viewpoint the role environmental protection plays in determining firms' investment decisions. Thus, the item "environmental protection" was added to the list of possible investment destinations. Apart from that, a further specific demand was included under the general item "expenditure for environmental protection", namely which is the specific target. To this end, the distinction between "environmental areas" adopted at the international level and at the national level by ISTAT was chosen and simplified according to the operational needs of ISAE. Four "environmental areas" were selected, namely soil, air and water protection, landscape protection, waste disposal and noise reduction<sup>1</sup>. In this case, firms are requested to indicate – similarly to what happens for enlargement and rationalisation expenditure – whether expenditure for environmental protection is aimed at one or more of those areas.

<sup>1</sup> Compared to the official ISTAT classification, the sectors "Air and climate", "Waste water management", "Soil and ground water" were pooled together in the item "Soil, air and water protection".

As already indicated, according to the ISAE respondents, in 2004 7% of expenditure for investments was allocated for environmental protection, which is slightly more than in 2003 (6%). Turning to single sectors, the expenditure for environmental protection plays a leading role in various manufacturing sectors (25% of expenditure in 2004 as against 14% in 2003) and in transport equipment (10% of expenditure in 2004 compared to 8% in 2003). Conversely, the share devoted to environmental protection in mechanics is quite low (3% of total expenditure in this sector in 2004, while it was 4% in 2003). Looking at the firm size, the share is slightly larger in small firms (9%) and in medium-sized ones (7%) compared to large firms (5%). Besides, among the 830 firms surveyed by ISAE, 41% answered the question about environmental protection, which proves they considered that item. Indeed, 32% of small firms reported they had spent for environmental protection, as against 48% of medium-sized firms and 68% of large firms.

### Firms which made investments for environmental protection

Firm size	Sample	Share	Firms which made investments for environmental protection	Percentage of firms which spent for environmental protection
Small firms	490	59%	160	32%
Medium-sized firms	255	31%	123	48%
Large firms	85	10%	58	68%
Total	830	100%	341	41%

Looking at the expenditure destination by environmental area, in 2004 33% of ISAE respondents invest in waste disposal (32% in 2003), 27% for soil, air and water protection (41% in 2003), 17% for noise reduction (18% in 2003) and 11% for nature and landscape protection (9% in 2003). The share of firms which made forecasts for 2004 divided by area was smaller than the number of firms which provided their final balances for 2003.

## Leasing

The traditional yearly questions on leasing as a form of investment financing show that most firms (52%) resorted to leasing in 2003, which depicts a growing trend compared to 2002 (32%). The leasing incidence on total investments is however decreasing and equals 7.3% (11% in 2002). That form of financing had a major role in small and medium-sized firms (with incidence equalling 14.2% and 16.6% respectively) and a smaller role in large firms (the incidence being worth 2.3%). Turning to single sectors, that form of financing was mainly used in paper, press and publishing (28.1%) and in chemicals, rubber and plastics (14.1%). Conversely it had a modest role in the transport equipment (1.6%).

On the other hand, a growing resort to leasing was observed in particular in large firms (the share of large firms reporting they had resorted to leasing rises from 17 to 55%).

The contemporary growth of the number of firms resorting to leasing and the reduction in the leasing incidence on total investments of the overall sample (and for large firms in particular) may be explained as a contraction in firms' average leasing expenditure (large firms in particular).

Going in detail, leasing was particularly used in investments for transport equipment (48% of firms) and for industrial plants. Also the item "other reasons" proved to be particularly important (for 50% of respondents), and this category comprises real estate leasing excluding the purchase of industrial plants.

