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MANUFACTURING AND EXTRACTIVE FIRMS SIGNAL A SLIGHT RISE IN THEIR INVESTMENT EXPENDITURE FOR 2004 AND FORESEE A REDUCTION IN 2005: LESS NEGATIVE EXPECTATIONS EMERGE FOR 2006

- **The Bi-Annual ISAE Investment Survey carried out between February and March 2005 and limited to firms which made or planned investment activity in the three years 2003-2005, points to a nominal rise in investments of manufacturing and extractive firms equalling to 1% at the end of 2004. Forecasts for 2005 are still negative, with an estimated 9.5% contraction in expenditure for machinery and equipment.**
- **Qualitative forecasts for 2006 are moderately favourable: most respondents (66%) expect a stable or growing expenditure compared to the previous year, with prevalent expectations for stability (55%) and a considerable share of firms expecting a further expenditure reduction (33%).**
- **With regard to the investment destination, most expenditure is aimed at obsolete plant renewal (44% of expenditure in 2004 and 42% in 2005), while 28% and 26% of expenditure is aimed at productive capacity enlargement in 2004 and 2005 respectively. Expenditure for rationalisation (18 and 20%), investments for environmental protection (5% in both years) and other sundry targets (6 and 7%) follow.**
- **The percentage of respondents resorting to leasing decrease compared to 2004 and equals 43%.**
- **The comparison between replies of the firms which answered the three Surveys made between April 2004 and April 2005 shows that the figures for 2004 and the forecasts for 2005 (even though they are negative) show signals of improvement.**

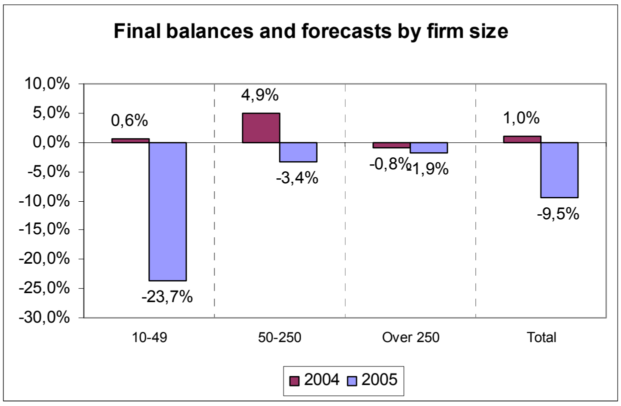
Next Bi-Annual Investment Survey will be published on December 2005.

Next ISAE Surveys are scheduled as follows:
May 26, 2004: *ISAE Monthly Survey on Traditional Retail Trade and Large Distribution (reference month: April)* and *ISAE Monthly Business Service Survey (Reference month: May)*
June 1, 2005: *Comparative Business Surveys for Italy, Germany and France (Reference month: May)*

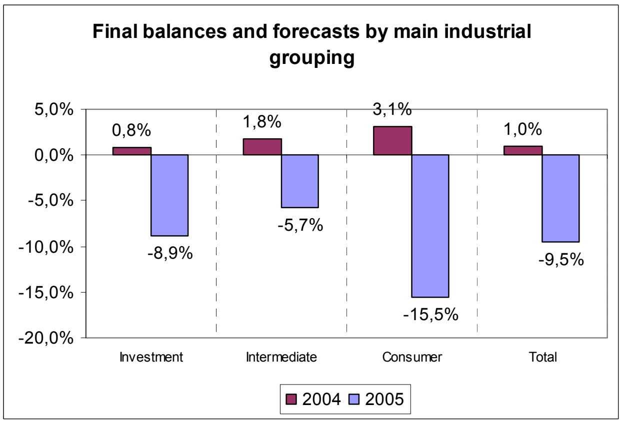
The full text of ISAE Surveys (either hardcopy or electronic) is available on sale (for further information see web site **www.isae.it**)

General results

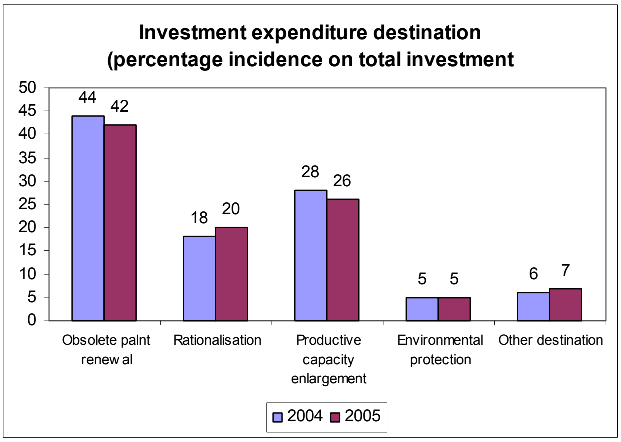
Between February and April 2005, ISAE carried out its traditional Bi-Annual Investment Survey on Manufacturing and Extractive Firms. For the first time, interviews by mail were accompanied by telephone interviews, which raised the rate of reply: all in all, about 1,900 firms (which really made investments in the three-year period 2004-2006) out of the 4,000 firms composing the ISAE monthly sample took part in the interview. In terms of employees, those firms account for about 66% of the ISAE panel.

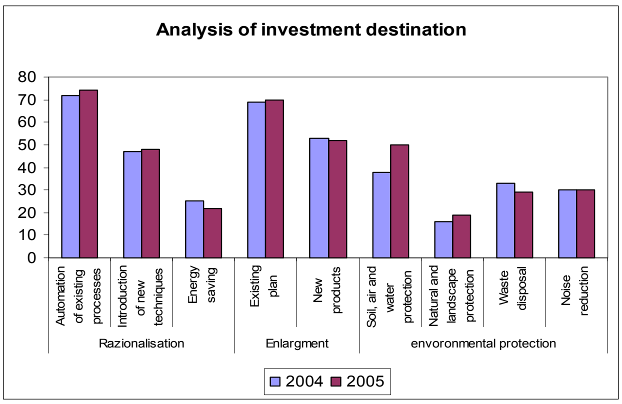


According to ISAE respondents, investments in the manufacturing and extractive sector increased in 2004 by 1%; the same respondents foresee for 2005 an expenditure reduction worth 9.5%. Looking at data by firm dimension, medium-sized firms raised their expenditure by 4.9%, small firms by 0.6%, while large firms reduced their investments by 0.8% in 2004. Small firms' forecasts seem to be particularly pessimistic for 2005, with an estimated 23.7% deterioration. Though less pessimistic, also large and medium-sized firms register negative investment variations equalling -1.9% and -3.4% respectively.



Breaking down data by sector, the investment rise for 2004 is particularly wide-spread in investment goods (+0.8%), intermediate goods (1.8%) and consumer goods (3.1%). Similarly, the investment reduction foreseen for 2005 is common to the three categories, while consumer goods show the largest slowdown (-15.5%; -8.9% in investment goods and -5.7% in intermediate goods).





Forecasts for 2006

Moderately favourable indications come from qualitative forecasts on investments for 2006. Most firms (66% of respondents) expect that they will rise (11% of the sample) or at least maintain (55%) their investment expenditure, while 33% of the sample expect a further investment reduction. Data broken down by firm dimension are rather homogeneous. 58% of large firms expect an unchanged investment expenditure as against 2005, 9% expect an expenditure rise and 33% expect a reduction. Most medium-sized firms (51% of respondents) expect their expenditure to remain unchanged, while 13 and 36% of the sample foresee an expenditure rise and contraction respectively in 2006. Finally, 9% of firms with less than 50 employees expect an expenditure growth and 36% of respondents forecast an expenditure cut, while the remaining 51% feel the investment expenditure shall remain unchanged.

Heterogeneous indications come from data by sector. The most pessimistic approach is emerging in foodstuff, where 54% of firms expect a fall in their investment expenditure (5% foresee a rise and the remaining 41% expect stability). Among other sectors, manufacturing industries in general and paper, press and publishing (46%) show relative pessimism. The extractive sector and the processing of either ferrous and non-ferrous minerals and mechanics are among the most optimistic sectors, in both of them 19% of respondents forecast a rise in investment expenditure.

Main investment destination

Looking at the destinations, most investments are aimed at obsolete plant substitution and renewal both for 2004 (44% of respondents) and for 2005 (42%). That is followed by expenditure for productive capacity enlargement (26% in 2005 as against 28% in 2004), rationalisation expenditure (20 and 18% respectively), sundry investments (7 and 6%) and, finally, environmental protection (5% in both years). The analysis by firm size shows that investments for obsolete plant substitution and renewal prevail in small and medium-sized firms (36 and 31% in 2004 and 33 and 34% in 2005 for small firms and 35 and 32% in 2004 and 33 and 29% in 2005 for medium-sized firms respectively), while expenditure for plant substitution and renewal take up a particular importance in large firms (52 and 54% in 2004 and 2005 respectively).

The analysis by sector outlines that investments for productive capacity enlargement were made in particular in mechanics and chemicals (only for 2005). Environmental expenditure was pursued in particular by firms operating in textiles and clothing both in 2004 and in 2005 (15 and 17% in 2004 and 2005 respectively), and by operators in extraction and processing of ferrous and non-ferrous minerals (15% in 2005).

Expenditure for productive capacity rationalisation and enlargement and for environmental protection

Rationalisation investments are mainly aimed at the automation and mechanisation of existing productive processes (72 and 74% of replies for 2004 and 2005 respectively). They are followed by investments to introduce new production techniques (which are relevant for 47 and 48% of the sample in the two years) and save energy (25 and 22% of respondents). Compared to the previous Bi-Annual Survey, the share of expenditure aimed at automation within the process and product innovation is growing to the detriment of the percentage allocated to save energy. Signals in this sense are homogeneously diffused to all sectors both in terms of firm size and of areas.

Turning to plant enlargement, 69 and 70% of firms in 2004 and 2005 respectively resort to those investments within the existing productive plans, while 53 and 52% of entrepreneurs adopt those investments to introduce new products. Breaking down data by firm size, the introduction of new products brings about investments in large firms in particular (indeed, 70% of large firms in 2004 and 65% in 2005 allocate part of their investments to enlarge plants with the aim of introducing new products), while looking at different sectors, those investments prevail in chemicals, rubber and plastics and in the means of transportation (75 and 71% in 2005 respectively).

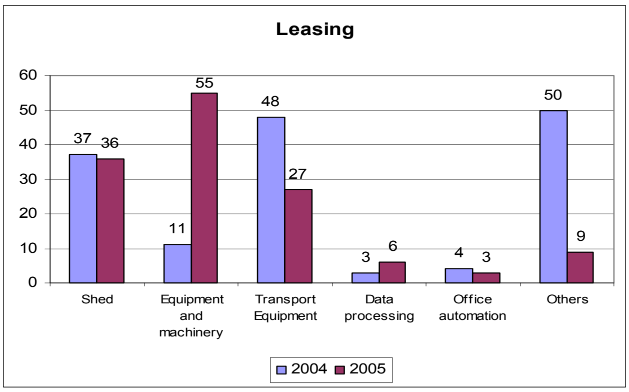
Looking at environmental protection, most investments in 2004 and 2005 aim at soil, air and water protection (38 and 50% of respondents invest in the two years respectively). They are followed by expenditure for noise reduction (46 and 39% of the sample declare they made those investments in the two years considered) and investments for waste disposal (which are relevant for 20% of the sample in both years). Conversely, only 16 and 19% of respondents respectively make investments for nature and landscape protection.

Leasing

The traditional yearly questions on leasing as a form of investment financing show that 43% of firms resorted to leasing in 2004, which proves a decreasing trend compared to 2003 (52%). In particular, small firms increased their use of leasing (50% of small firms adopted that formula).

The leasing incidence on total investments is however growing and equals 17.6% (7.3% in 2003). That form of financing had a major role in small and medium-sized firms (with an incidence equalling 30.5% and 12.4% respectively) and a smaller role in large firms (the incidence being worth 5.9%). Turning to single sectors, that form of financing was mainly used in textiles (31.4%) and in paper, press and publishing (30.2%), while it had a modest role in extraction and in the processing of ferrous and non-ferrous minerals (13.6%).

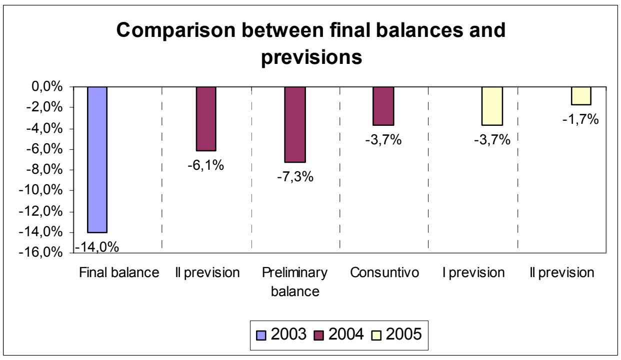
Going in detail, ISAE respondents resorted to leasing for investments in means of production (55% of firms) and in industrial plants (48%). A similar distribution was observed in small and medium-sized firms, while in large firms expenditure for means of transportation (41%) replaced that for means of production.

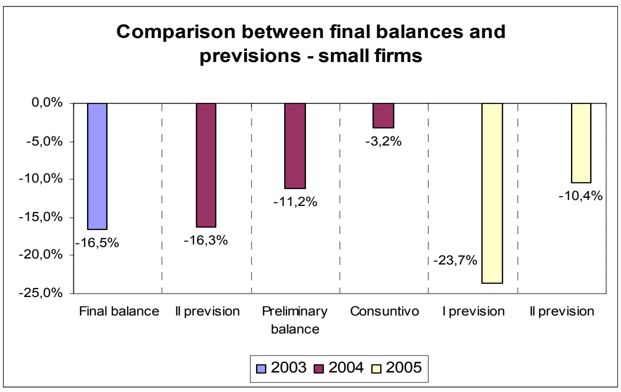


Comparison between balances and forecasts for the three-year period 2003-2005

To provide a rough analysis of the reviews made by firms in their evaluations of the accumulation process, attention was only focused on the replies of firms which answered to the three surveys made between April 2004 and April 2005. The sample thus consists of 345 firms, whose 2003 final balances – surveyed in April 2004 – show that the investment variation in 2003 was strongly negative (-14%). In particular, the fall in small and medium-sized firms equalled 16.5 and 22.3%, while for large firms it was worth 6.8%. Looking at sectors, the 2003 investment contraction almost completely came from intermediate goods (-24.1%; -4.5% in investment goods), while consumer goods registered a positive variation equalling 2.4%.

Always in April 2004, ISAE respondents forecast an investment reduction in 2004 equalling 6.1%: this means expectations further deteriorated last Autumns, when firms were expecting a 7.3% expenditure contraction. However, according to the latest ISAE Survey, the 2004 final balance showed a smaller investment reduction (3.7%).





The review seems to be mainly due to medium-sized firms, which showed a process similar to the overall manufacturing trend, which an initial forecast envisaging a 11.3% fall, further worsened in Autumn 2004 (-15.6%) and then improved to -10%. Heterogeneous behaviours were observed in small and medium-sized firms: indeed small firms had strongly negative expectations on 2004 in April (-16.3%) and then became less pessimistic last November (11.2%) and even lesser in the latest Survey (-3.2%). Large firms declared they were expecting a moderate expenditure rise in 2004 (1%) and then observed a -2% contraction in Autumn 2004 and a -1.4% cut in the latest Survey. Looking at data by sector, investment goods producers showed a forecast, pre-balance and final balance trend similar to the one of the manufacturing sector (-5.6%, -10.8% and -6% respectively). Conversely, intermediate goods gradually improved their forecasts, passing from an expected investment expenditure cut worth 12.5% up to a moderately positive final balance worth + 0.9%). Consumer good producers were initially characterised by strongly negative expectations (-13.7%) followed by less drastic expectations in Autumn 3004 (-8%) and worsened again in the latest Survey (-12.8%).

For 2005. firms expected an expenditure cut worth 3.7%; the forecast improved in April 2005, with an expected investment contraction worth 1.7%. The expectations growth concerned in particular small firms, which had originally showed a marked pessimism (-23.7%) and then became relatively more optimistic (-10.4%) in April 2005. Medium-sized firms were initially optimistic for 2005 (the November 2004 forecast equalled +4.9%) and then diminished expectations in the latest review (-3.6%), while large firms remained substantially stable in forecasting a moderate expenditure reduction in 2005 (the November 2004 estimate was -2.2%, while the latest one was worth - 3.1%).

Looking at data by sector, expectations of consumer good producers are stable, though considerably negative (namely, -12% the first expectations and -11.9% the second one). In investment goods, a worsening is observed, as expectations pass from -1.4% to -4.6%, while a strong improvement is observed in intermediate goods, passing from an expected fall worth -1.4% to an 8% expected growth in 2005.