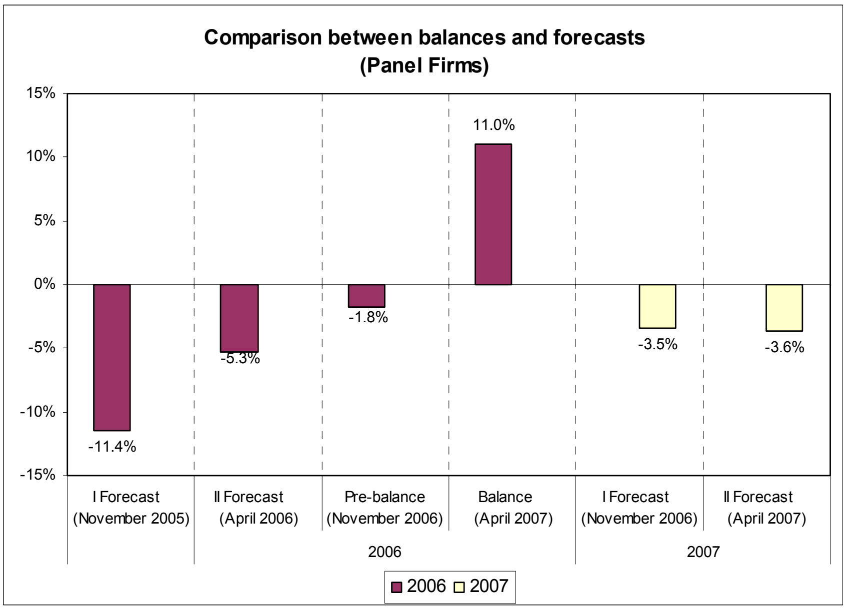
ISTITUTO DI STUDI E ANALISI ECONOMICA
Piazza dell'Indipendenza, 4 00185 Roma tel.: + 39-0644482.1 fax: + 39-0644482229

Date: **May 24, 2007**
TEL.: **06/444821**

THE MANUFACTURING FIRMS' FINAL ESTIMATE FOR CAPITAL SPENDING IN 2006 STAGES AN INCREASE

- **The bi-annual ISAE Investment Survey, carried through March-April 2007, recorded a 8.2% growth for capital spending in 2006, according to the final estimate of manufacturing and mining firms**
- **However, the same firms forecast for 2007 a fall in expenditures of 4.4%. The drop could be entirely traced to the negative indications of small-sized firms**
- **Over time, the evaluations for 2006 expenditures were strongly upgraded by firms participating in all the surveys conducted in the last 18 months. Forecasts for 2007 remained, instead, virtually stable between the November 2006 and the April 2007 surveys, for firms that responded to both surveys**
- **For 2008, the largest share of the panel (67%) anticipated stability (42%) or an increase (25%) in capital expenditures**
- **Both in 2006 and 2007, most investments were implemented with the purpose of replacing worn-out plant and equipment and expanding production capacity. Furthermore, in order of decreasing importance, rationalization, environmental protection and "other investment objectives" were mentioned**
- **Traditional annual questions on the utilization of leasing for financing capital spending showed that 35% of the respondents resorted to this financial instrument in 2006. The share of total investments financed through leasing decreased to 17% (compared to 21.3% in 2005)**



The next Investment Survey on Manufacturing and Extractive Firms will be released in December 2007

The next ISAE surveys are scheduled as follows:
May 29, 2007: *ISAE Monthly Survey on Traditional Retail Trade and Large Distribution (reference period: May), ISAE Monthly Business Services Survey (reference period: May), and ISAE Monthly Survey on Construction (reference period: April)*
June 6, 2007: *ISAE International Comparison of Consumer and Business Surveys (reference period: May)*

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)

Investments in 2006 and forecasts for 2007

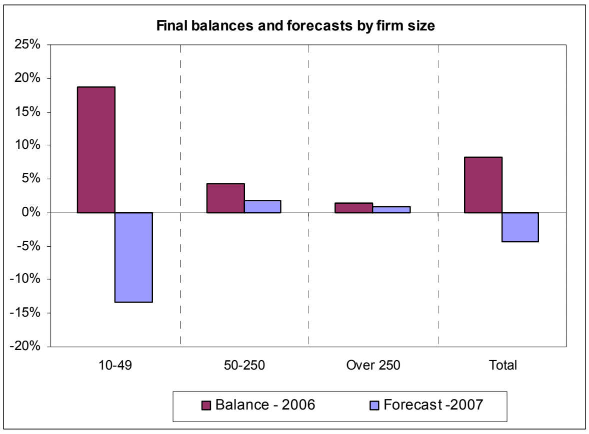
In March-April 2007, ISAE carried out its traditional twice-yearly investment survey on manufacturing and extractive firms. The survey covered only firms which actually implemented or planned investment activity in the 2005-2007 three-year period. Replies were obtained from about 1,900 out of the 4,000 firms participating in the monthly ISAE survey.

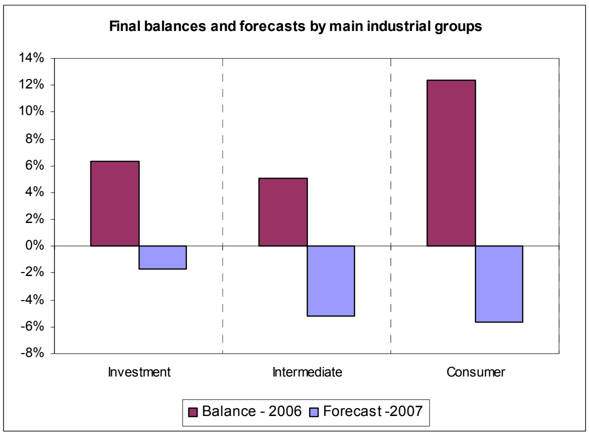
Final data for 2006 showed that investments in the manufacturing and extractive firms sectors grew 8.2%. However, the same firms forecast for 2007 a reduction in expenditures of 4.4% The sorting out of data according to firm size indicated that the expansion in 2006 was particularly marked for small firms (18.7%). Large and medium-seized firms showed, instead, a more moderate rise, equal to 4.2% for the former and to an even lower 1.4% for the latter. For 2007, in contrast with the markedly pessimistic forecasts of small firms, which expected a 13.4% cut in investments, medium-sized firms planned to increase capital expenditures by 1.7%, while larger ones planned a modest 0.8% rise.

The classification by sectors showed that in 2006 the increase in investment spending was particularly strong in the intermediate goods segment (12.3%). For investment and consumer goods, growth in capital expenditures amounted to 6.3% and 5%, respectively. On the other hand, pessimism about expectations for 2007 pervaded all sectors and, in particular, intermediate (-5.7%) and consumer goods firms (-5.2%). The investment goods enterprises were, instead, less pessimistic (-1.7%).

Comparison between forecasts and results for 2006

Out of the 1,900 firms that replied to the spring 2007 ISAE survey, about 1,300 responded to all the surveys conducted between November 2005 and April 2007, providing information on capital spending developments in 2006. The examination of these replies allowed to make preliminary considerations on the time evolution of Italian manufacturing firms' investment forecasts.





The evaluation of investments made in 2006 both progressively and significantly improved over the last 18 months: in November 2005 firms expected a decline in expenditures of 11.4%. They upgraded their forecast for the first time in April 2006, when they anticipated a fall in spending of -5.3%, and again last November when their advance estimate was equal to -1.8%. Ultimately, the same firms gave a positive final estimate of +11%. The revision characterized all size groups and mainly small firms, which initially made a highly negative forecast (-17.3% in November 2005). The forecast was gradually upgraded in April 2006 (to -10.8%) and in November 2006 (to -4.6%), whereas in April 2007 the final estimate turned positive to +20.8%. Likewise, large enterprises started by making a negative forecast in November 2005 (-3.5%) and in April 2006 (-0.9%), and finally forecast virtual stability in November 2006 (-0.7%) and growth in the last survey (+2.1%). Finally, medium-sized firms started with a negative forecast 18 months ago (-7.8%), but gradually revised it upwards in April 2006 (-1.3%), in November 2006 (+0.8%) and, mainly, in April 2007 (+7.8%). The upgrading was widespread across sectors but was particularly marked for producers of intermediate goods: in this sector, the negative forecasts of November 2005 and April 2006 (-14% and -3.5%, respectively) were upgraded in November 2006 (-2.1%) and again in April 2006, when the final estimate showed a growth of 14.3%. Likewise, producers of investment goods revised their forecast from -7% in November 2005 to -10.2% in April 2006, and again to -3.6% in November 2006 and to +6.6% in April 2007. Lastly, in the consumer goods sector, the initial negative forecast (-13%) turned positive to +10.3% in the final estimate of April 2007.

Comparison between forecasts for 2007

Widespread and virtually constant pessimism distinguished the forecasts for 2007, according to the overall panel of 1.640 firms which responded also to the previous survey. On the whole, the firms of the ISAE panel which answered to both surveys, anticipated a fall of 3.6% in investment expenditures in November 2006 and of 3.5% in the last survey. The result largely stemmed from the negative indications of small enterprises (-8.1% in November and -12.9% at present). Large firms – though slightly scaling down their predictions – forecast, however, an increase in capital expenditures (+1.4% in November 2006 and +0.8% in April 2007), whereas medium-sized firms anticipated a fall in expenditures of 2.5% in November but a rise of 5.2% currently.

The industry breakdown of data showed that the producers of intermediate goods and, above all, of investment goods downgraded their forecasts (from -2.4% to -4.9% and from +2.5% to -0.9%, respectively), while producers of consumer goods became less pessimistic in the last six months (they revised their forecast for the current year from -9.2% in November to -4.3% in the last survey).

Qualitative forecasts for 2008

With regard to the qualitative forecasts for the investment trend in 2008, most surveyed firms (67% of the sample) planned the same (42%) or a larger amount (25%) of investment spending compared to the previous year. Instead, 32% of the sample expected a cut in capital expenditures. However, the sorting out of data by size groups showed some significant dissimilarities. Among large firms (with more than 250 employees), 44% planned a rise in expenditures with respect to the previous year, 38% expected stability, while only 18% forecast a decline. Among medium-sized firms (employing 50-249 people), instead, the percentage of those anticipating a cut in investment spending prevailed (46%), whereas 40% planned stability and barely 14% predicted a rise. Finally, only 13% of small firms (with fewer than 50 employees) expected for 2007 an increase in capital expenditures over the year earlier, 37% anticipated a fall and the remaining 50% considered that investments would remain unchanged.

Purposes of investment

According to surveyed firms, both in 2006 and 2007, the main aims for capital spending were the replacement of worn-out plant and equipment (34% of the replies in 2006 and 35% in 2007) and the extension of production capacity (33% in the same two years). Furthermore, in order of decreasing importance, rationalization (21% in 2006 and 20% in 2007), environmental protection (6% in 2006 and 7% in 2007) and “other investment objectives” (6% in both years) were mentioned.

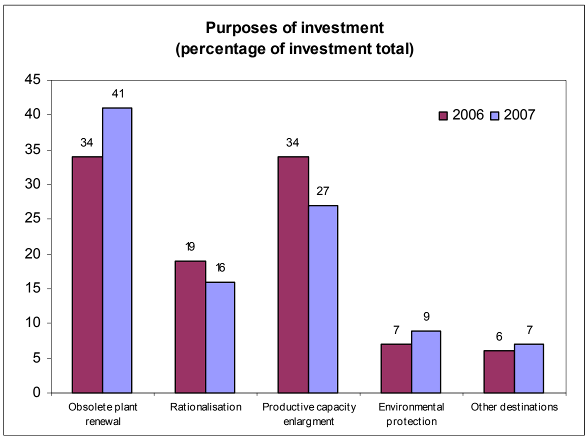
The analysis of size groups showed that in 2007 41% of small firms wanted to replace worn-out plant and equipment (38% in 2006), 17% pointed to the streamlining of production processes (18% in 2006), 35% wanted to expand production capacity, 3% aimed at environmental protection (from 4%) and 6%

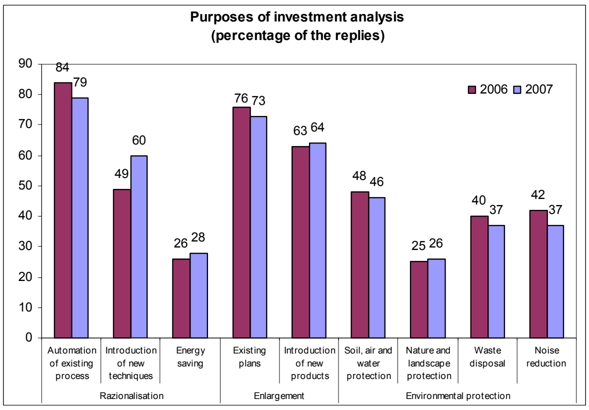
mentioned "other investment objectives" (from 5%). For medium and large firms, expenditures for the replacement of worn-out plant and equipment, which moved from 35% to 30% and from 30% to 33%, respectively, remained in line with the overall data, while those for the extension of production capacity posted diverging trends. Medium-sized firms actually expressed the intention of increasing such expenditures from 30% to 37%, large firms, on the contrary, planned a cutback from 34% to 27%. The share for rationalization and for "other investment objectives" remained virtually unchanged: 20% for medium and 23% for large firms in the first case, and 7% in both size groups for the latter case. Finally, noteworthy was the rise, for large firms, in the share of investments aimed at environmental protection (from 6% to 10%).

Expenditures for rationalization, extension of production capacity and environmental protection

Also in the first half of this year, expenditures for rationalization were mainly oriented towards automation and mechanization of existing producing processes (84% of the replies in 2006 and 79% in 2007), followed, in decreasing order, by expenditures for the introduction of new production techniques (observed for 49% and 60% of the sample in the two years) and by investments designed to save energy (26% in 2006 and 28% in 2007).

As for the extension of production capacity, in 2006 investments were mainly implemented within the existing production programmes (76% of the firms in 2006, down to 73% in 2007), while those designed to extend the product range regarded 63% and 64% of the respondents in the two years. Finally, among the expenditures for environmental protection, also in 2007, even though the shares generally declined with respect to the previous year, the larger amount was intended for the protection of soil, air and water (48% of firms made such expenses in 2006 and 46% in 2007). Also investments for waste management acquired an important role (40% in 2006 and 37% in 2007), followed by expenditures for the reduction of noise (42% in 2006 and 37% in 2007). Lastly, the proportion of firms that channelled or planned to channel funds for the protection of nature and landscape increased compared to the previous year (from 25% to 26%).





Leasing

Traditional annual questions on the utilization of leasing for financing capital spending showed that 35% of the respondents resorted to this financial instrument in 2006, a lower share than in 2005 (45%). Firms that forwent its utilization were mainly small ones (only 46% used it, as opposed to 60% in 2005) and, to a lesser extent, large firms (down from 36% to 25%). On the contrary, the percentage of medium-sized firms using this financial instrument rose to 34% from 33% in the previous survey.

Accordingly, the share of total investments financed through leasing lowered to 17% from 21.3% in 2005. This form of financing became less important for small firms (the share amounted to 28.6% compared to 39.6% in 2005) and also, though to a lesser extent, for large ones (to 5.8% from 6.8% in the previous survey). The role of leasing improved slightly, instead, for medium-sized firms (from 12.4% to 14.8%).

More in detail, according to surveyed firms, leasing was mainly used for purchasing producing machinery and equipment (76% of respondents), industrial warehouses (28%) and transportation equipment (27%). The classification by firm size showed that small and medium-sized firms resorted to leasing mainly to finance the purchase of machinery (75% and 82% of the answers), transportation equipment (25% and 31%) and warehouses (23% and 17%). Lastly, large firms used leasing mainly for investments in producing equipment (73%), warehouses (51%), transportation equipment (26%) and, by a higher than average amount, for purchasing machinery and equipment for office automation (22% of the replies).