

# Monthly update Italy

2 March 2010

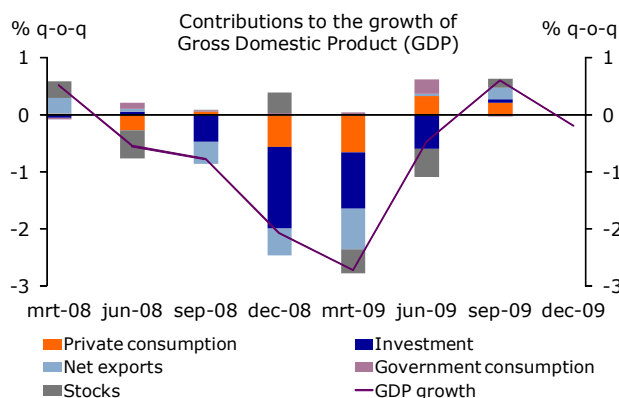
## Recovery falters, renewed recession a possibility

Year-on-year change (%)	'09	'10	'11
Gross Domestic Product	-4.9	¾	1¾
Private consumption	-1.8	½	1½
Government consumption	1.2	1¼	2¼
Private investment	-12.9	-1¼	1¾
Exports	-18.7	3½	4
Imports	-14.8	2½	3½
Inflation	0.8	1¾	¾
Unemployment (%)	7.7	8¾	9
Government balance (% GDP)	-5.4	-5¾	-5¾
Government debt (% GDP)	111.1	116¾	120

Source: Reuters EcoWin, Rabobank

The Italian economic recovery stalled after a single quarter. In 09Q4 the economy relapsed into contraction (-0.2% q-o-q). A return to growth and resumption of recovery in 10Q1 is not an established fact. On the one hand, manufacturing production starts the quarter on a weak footing and consumers seem hesitant. The completion of the last batch of car sales eligible for the cash-for-clunkers subsidy pushed up the February car sales figure (+20.6% y-o-y), but sales is expected to suffer the unavoidable relapse in the next few months. On the other hand, a reduced pace of destocking –inventory levels are now assessed at all-time lows– can possibly push growth back in black in 10Q1.

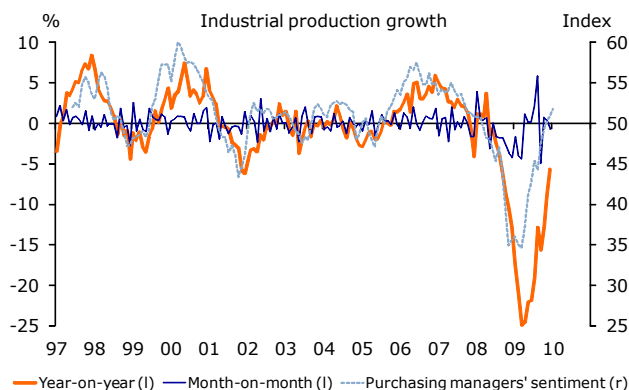
## Crisis year ends with GDP falling, yet again



Source: Reuters EcoWin

The Italian economy shrank in 09Q4 by 2.8% on the year. That looks like an improvement relative to 09Q3, when the level of economic activity fell back by 4.6% y-o-y, but the quarterly growth profile certainly does not bode so well. GDP in 09Q4 namely, shrank by 0.2% compared to the previous quarter, where 09Q3 at +0.6% q-o-q had just succeeded in ending five consecutive quarters of economic contraction. The composition of the recent growth figure will only be released later this month, but the Italian growth relapse was, in any case, stronger than that in the eurozone as a whole. There, growth fell back from 0.4% q-o-q in 09Q3 to 0.1% in 09Q4, yet managed to remain in positive territory.

## Manufacturing production a drag on economy activity



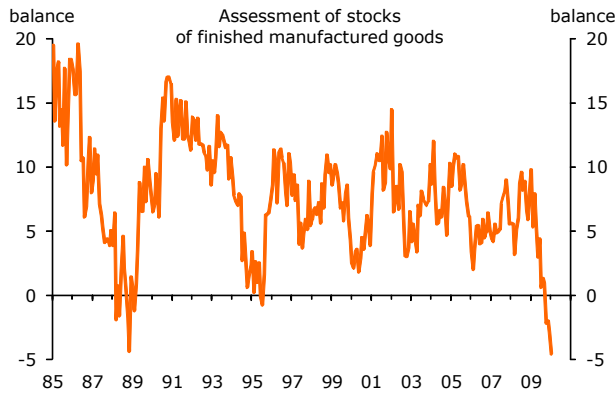
Source: Reuters EcoWin

Solid gains in the manufacturing purchasing managers' sentiment (at 51.8 in January) point to resumption of production growth on an annual basis for some months now. Actual production has failed to deliver so far. In December it did seem to take a big leap forward, production contracted by only 5.7% y-o-y after -9.0% y-o-y in November. Unfortunately, manufacturing production actually fell on a monthly basis in December (-0.7%, compared to +0.4% in November) and also shrank in 09Q4 on a quarterly basis whereas in 09Q3 it expanded by 4.5% q-o-q. The 0.8%-point lower contribution from manufacturing to GDP growth, therefore, fully accounts for the growth setback in 09Q4.

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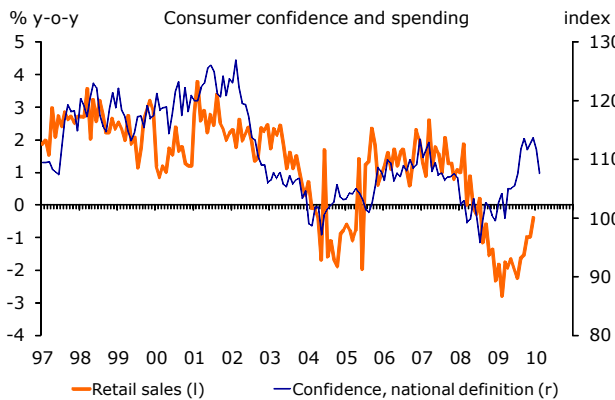
## Inventories now assessed as historically low



Source: Reuters EcoWin

09Q4 turned out to be a strong quarter in terms of manufacturing orders, gaining 5.4% on the quarter (+2.7% q-o-q in 09Q3). That bodes well for manufacturing production going forward. Growth of overseas orders suffered a setback (from 11.2% q-o-q in 09Q3 to 5.8% q-o-q in 09Q4), but domestic orders more than compensated for that. The domestic recovery of orders suggests that the end is near for the extremely rapid rates of inventory shedding that characterized most of 2009. Producers' assessment of stock levels slid further during 09Q4 and in January hit an all-time low at -4.6. Maybe as soon as 10Q1, but most certainly in 10Q2 inventories will be adding to GDP growth.

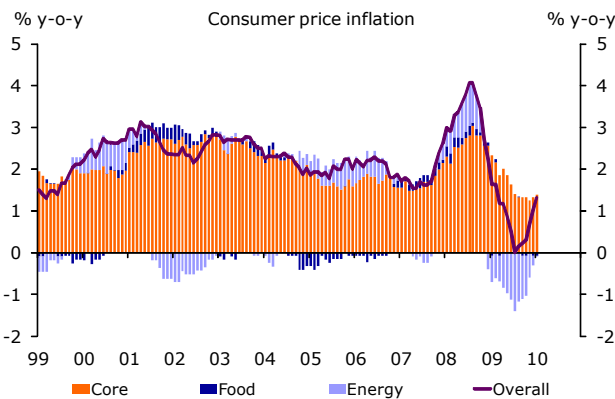
## Retail sales recovery, what recovery?



Source: Reuters EcoWin

Consumer confidence in January softened for the second month running (to 107.7). Retail sales in contrast, appeared to be on the rise, falling by only 0.4% y-o-y in December after posting -1.0% y-o-y in both November and October. Thus, the recent discrepancy between strong consumer sentiment and weak retail sales is diminishing. Unfortunately, retail sales remained stuck on a monthly basis during all of 09Q4. The improvement in the annual growth rates results only from the fact that sales have been weak now for so long that the basis of comparison in the annual growth rates becomes weaker and weaker. The bottom line is that Italy is unlikely to experience a consumer-led recovery in 10Q1.

## Inflation surprisingly rises moderately



Source: Reuters EcoWin, Rabobank

In January consumer prices rose by 1.3% y-o-y (1.1% in December) using the harmonized European definition. That constitutes a much more moderate rise than we had anticipated only last month. Energy prices in January contributed next to nothing to consumer price inflation, where we had pencilled in a substantial positive contribution. We may yet turn out to be right in that assessment. In February or March the energy contribution to inflation may reach a peak level of about 1%-point. From that angle, the softening of the pace of inflation to 1.1% y-o-y comes as a surprise. The composition is not yet known, but energy price developments are unlikely to have driven this result.

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