EDITORIAL
2005 IS A YEAR OF MODERATION FOR GOODS PRICES

THE SLOWDOWN IN HOTEL AND RESTAURANT IS ACCOMPANIED BY AN ACCELERATION IN TRANSPORT PRICES

After inflation fell below 2% at the end of 2004, the first few months of the new year confirmed the moderate tone of prices across various sectors with the sole exception of private sector services.

Inflation in goods markets is under control: foodstuffs prices are deflating as a result of the large reductions in fresh food prices, vegetable prices in particular, and of the intensification of advertising activity by retailers who are grappling with falling demand and changes in consumers' purchasing habits. Despite the increases in raw materials' prices and poor progress with productivity, competitive pressure from import prices from emerging countries is helping to hold prices down in the non food sector at the different stages in the distribution chain.

As concerns services, the slow down in hotel and restaurant prices was accompanied by an acceleration in transport prices. Very moderate increases in public sector tariffs with the annual round of increases at the beginning of the year provided the background to this: public sector tariffs and regulated prices are steady at the same levels as twelve months ago. A different measurement of the degree of moderation in tariff increases is given by the basket of harmonised consumer prices which paint a picture of tariffs four percent higher.

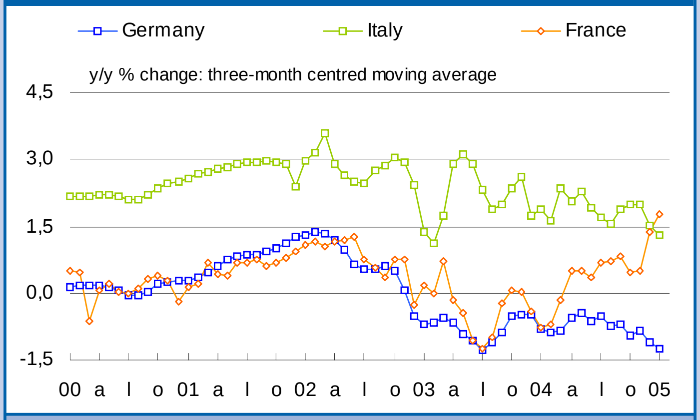
The most important factor for goods and services markets alike, is how well consumption is holding up. The most credible interpretation is that consumer preferences are guided by changes in relative prices: in a zero sum game households are allocating a greater proportion of their consumption to durable goods, such as consumer electronics products for which prices have fallen in recent years at the expense of non durable and semi-durable products such as foodstuffs, clothing and footwear, which on the contrary are much more expensive.

For the future, the recovery of raw materials' prices and the reduced margins of industrial firms reveal the need for a new price/cost balance in many mass consumption sectors. Nevertheless, in a context in which demand as a whole offers no great hopes of taking off, consumer preferences are acting as a dividing line between sectors in which recovery of costs is sustainable and other sectors for which this risks leading to a further set back for national production.

One of the special focus sections in the report addresses the recent liberalisation of imports for numerous textile and clothing products. While there is no doubt that it is replacing domestic production, against a background of falling production and employment in the sector, the final outcome in terms of consumer prices is not equally clear. The evidence available shows that the path taken of liberalising import quotas has not so far furnished appreciable benefits for consumer inflation. The loss of jobs has been accompanied by a constant rise in clothing prices which may have helped to depress the demand. The British experience suggests that competition and efficiency in retail distribution are necessary conditions for economies of cost to translate into lower prices.

The forecast for inflation, with all the relative caveats concerning the impact of these important events and future prospects for oil prices, is that the average for 2005 will continue at 2%.

INFLATION: CLOTHING AND FOOTWEAR



SOURCE: REF CALCULATIONS ON EUROSTAT DATA

DOMESTIC PRICES. INFLATION UNDER CONTROL

MODERATE PUBLIC SECTOR TARIFFS COMPENSATE FOR LIVELY PRIVATE SECTOR SERVICES PRICES

Inflation in 2004 was 2.2%, the lowest level since 1999. The decline has its roots in goods markets. Prices of foodstuffs were affected by both greater attention to prices by consumers and a change in purchasing and by the strong increase in agricultural output: annual average inflation for foodstuffs fell to 2.2% compared to levels of 3-4% in the three year period 2001-2003.

For non foodstuff goods, the slow down in inflation was encouraged by:

1. past economies of cost in the supply of raw materials as a result of the appreciation of the euro;
2. competition on the domestic market from imports from emerging countries;
3. recover of labour productivity;
4. the absence of signs of recovery in demand.

Inflation fell by 1% in the non foodstuff segment passing from 1.9% in 2003 to 0.9% in 2004: the decline in inflation on goods markets is sufficient by itself to explain the half percent fall in consumer inflation.

Inflation remained high for private sector services as a result of less exposure to national and international competition, with the slow down in financial and insurance prices causing the baton to be passed to transports services which accelerated. Inflation in the hotels, restaurants and bars sector fell due to weak consumer demand.

Lower prices towards the end of the distribution chain were in contrast to tensions affecting production prices. These pressures were seen in the gap between producer prices of consumer goods where increases in the last twelve months did not exceed 1% and inflation for intermediate goods where increases reached year-on-year rates of 7%.

ITALY: BREAKDOWN OF INFLATION

ANNUAL % CHANGE

	Avg. 2002	*Avg. 2003*	*Avg. 2004*	*Jan.05/ Jan.04*
Food	***3,6***	***3,1***	***2,2***	***-0,4***
Processed food	2,1	2,6	2,3	1,1
Fish and seafood	4,5	4,5	1,6	-0,5
Fruit and vegetables	9,8	5,3	1,7	-7,6
Industrial goods	***2,1***	***1,9***	***0,9***	***0,9***
Medical products	-1,2	0,4	1,7	1,8
Clothing	2,4	2,8	2,3	1,8
Footwear	3,5	2,9	1,9	1,6
Furniture and furnishings	1,9	1,9	2,3	2,5
Household appliances	0,3	0,2	-0,3	-0,6
Radio, Tv, etc.	-2,9	-4,1	-13,7	-12,6
Photog. equip., optical instr.	1,1	1,2	1,4	1,4
Household goods	2,1	2,2	1,8	1,2
Tools and equip. for house	2,2	2,8	2,7	2,5
Products for personal care	2,1	2,3	1,8	1,1
Newspapers, books	4,3	2,4	2,1	1,7
CD, magnetic tape	0,9	0,8	0,6	0,3
Games, toys, sport equip.	1,5	1,8	1,1	0,8
Miscellaneous goods	2,7	2,7	2,7	2,0
Motor cars and access.	2,5	1,6	0,0	1,2
Energy	***-2,8***	***3,0***	***2,6***	***5,2***
Heating oil and fuels	-1,5	2,4	5,9	8,2
Electricity and gas	-4,2	3,9	-1,5	1,5
Services	***3,9***	***3,6***	***3,4***	***3,2***
Personal care, recreation	2,8	2,3	2,3	2,2
Housing	2,6	2,9	2,8	2,8
Transport	3,7	3,5	5,1	6,9
Health	3,9	3,6	3,0	2,6
Financial and n.e.c.	5,9	7,7	3,0	2,4
Restaurants and hotels	4,7	4,1	3,5	2,6
Regulated prices	***1,5***	***0,2***	***1,4***	***0,0***
Nationally	1,1	-0,7	0,6	-1,3
Locally	3,1	4,0	3,9	2,3
Rents	***2,3***	***2,8***	***2,9***	***2,6***
Tobacco	***1,8***	***8,4***	***10,4***	***13,9***
All-items	**2,5**	**2,7**	**2,2**	**1,9**

SOURCE: REF CALCULATIONS ON ISTAT DATA

INTERNATIONAL PRICES
TENSION ON THE INPUT SIDE
THE STRONG EURO IS PROTECTING ECONOMIES IN THE AREA

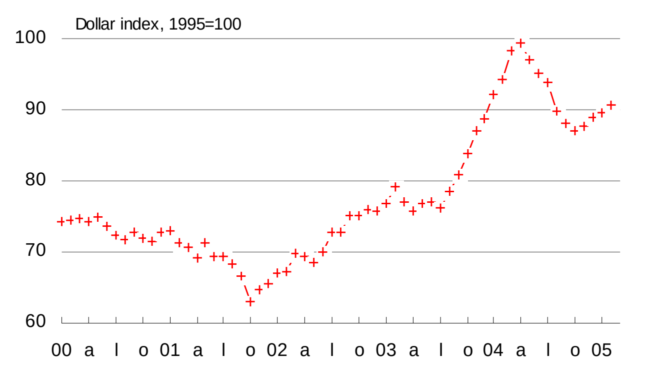
The start of the year gave a new boost to increasing oil prices: they have increased by approximately 40% since the start of the year touching a new high of $54 a barrel in the first ten days of March.

Pressures from the energy raw materials are to be added to those from other raw materials markets. Economies in the Euro Area, however, continue to be protected by the strength of the currency.

The different pressures on the input side are reflected in the dynamics of producer prices which in dollar area economies are less contained than in the Euro Area.

Pressures in the Euro Area and in the United Kingdom remained confined to the initial stages in the supply chain: consumer prices remain at rates close to 2%. The greater pressures at the upstream stages in the supply chain are to be seen in American consumer prices which have been hovering at rates of more than 3% for some months.

NON ENERGY COMMODITY PRICE INDEX



SOURCE: THE ECONOMIST

FOODSTUFFS
FOODSTUFFS DEFLATE
BUT A PHASE OF RECOVERY FOR PRODUCER PRICES IS CLOSE

The slowdown in inflation for foodstuffs took on a deflationary tone in the first few months of 2005: prices of foodstuffs were 0.4% lower in January 2005 than in the same month in 2004.

The figure summarises negative year-on-year rates for fresh fruit and vegetables (-7% year-on-year to January) and fish (-0.5% year-on-year) and a halt to increases for processed foodstuffs. A total halt on price increases has been observed in all mass consumption segments since last October and increases over the last twelve months have been of around 1%.

The price cuts are not sufficient to guarantee a lasting increase in consumption but are still the main support for quantities and levels of production.

FOODSTUFFS: BREAKDOWN OF INFLATION

ANNUAL % CHANGE

Department	*Avg. 2002*	*Avg. 2003*	*Avg. 2004*	*Jan.05/ Jan.04*
Processed food	***2,1***	***2,6***	***2,3***	***1,1***
Beverages	2,5	2,8	2,3	1,5
Packaged	2,2	2,6	2,6	1,5
Fresh food	2,8	2,1	1,8	1,1
Frozen food	2,5	2,4	1,5	0,9
Pets food	2,4	2,1	2,0	1,5
Meat	1,1	3,8	2,4	0,6
Fish and seafood	***4,5***	***4,5***	***1,6***	***-0,5***
Fruit and vegetables	***9,8***	***5,3***	***1,7***	***-7,6***
Food and beverages	***3,6***	***3,1***	***2,2***	***-0,4***

SOURCE: REF CALCULATIONS ON EUROSTAT AND EUROPEAN COMMISSION DATA

SPECIAL FOCUS
THE CHINESE SPECTRE FRIGHTENS ITALIAN TEXTILES

1ST JANUARY 2005: BARRIERS TO ITALIAN IMPORTS OF TEXTILES AND CLOTHING FROM COUNTRIES OUTSIDE THE EU COME DOWN

1st January 2005: after more than forty years of measures to regulate imports by the European Union, the United States, Canada and Norway of textile and clothing products from other countries all trade barriers have now come down.

The process of the liberalisation of trade in textile and clothing products started 10 years ago with the signing of a transitory agreement on textiles and clothing which was supposed to take the two sectors from a trade regime regulated by import quotas to a completely free regime between 1st January 1995 and 31st December 2004.

The liberalisation process regulated by the transitory agreement took place in four stages: in each stage the signatory countries were to eliminate a percentage of their import quotas.

The liberalisation achieved in the first three stages of the agreement was modest however. The EU eliminated a total of 14 quotas out of a total of 219 in the first two stages (started on the 1st January 1995 and 1st January 1998 respectively).

The effects of the start of the third stage on 1st January 2002 were decidedly greater, one reason being that China joined the World Trade Organisation in 2001. Since then China has also taken part in the import liberalisation process regulated by the transitory agreement.

Types of clothing for which imports from other countries were liberalised in 2002 include overcoats/windbreaker jackets, sportswear and underwear. The volumes of imports of these articles from countries outside the EU has increased exponentially: imports of overcoats and windbreaker jackets have grown by 97%, of sportswear by 91% and of underwear by 70%. This increase is mainly due to strong growth in imports from China.

At the same time the average unit import prices of these products from outside the EU fell by 44%, 37% and 27% respectively. The sharp fall in average unit import prices of textile and clothing products started to slow growth in producer prices of these products. There are, however, no signs of a slowdown in the relative consumer prices which have continued to increase at rates of over 2%.

The conclusion is that import and production prices have fallen in recent years and demand has fallen, but consumer prices have continued to rise.

What changes will occur from 1st January 2005 onwards?

While the import quotas permitted under the transitory agreement may have limited pressure from Asian competition on consumer clothing markets until a few months ago, the Italian market has been completely open to imports from countries outside the EU since 1st January 2005.

The structure of Italian imports of textiles and clothing is currently changing with an increase in market share by China at the expense of other non-European suppliers (such as India and Turkey), which will very probably subtract market share from Italian producers, especially in the lower bands of the market where the competition is mainly based on price.

In the medium term this could also encourage competition in the retail distribution structure, as has already been observed on the British market, with a greater role on the part of non specialist mass retailers (hyper markets and large department stores) and specialist, but mass, retailers at the expense of small retailers, with positive effects on prices.