

EDITORIAL

INFLATION BELOW 2% IN 2009

Prices rose constantly in 2008 to reach a peak of greater than 4% growth in the summer. The forces that pushed inflation up can be generally summarised in terms of two factors: energy prices and food prices. These were both fuelled in past months by factors originating in the international economic context.

The inflation scenario changed suddenly after the summer. It was changes in the world business cycle which caused the scenario to transform. The sharp downwards revision of the outlook for growth caused marked falls in energy, foodstuff and industrial raw materials prices.

The fall in oil prices resulted in a marked deceleration in inflation in a very short period of time, falling to 3.5% in October and to below 3% in November.

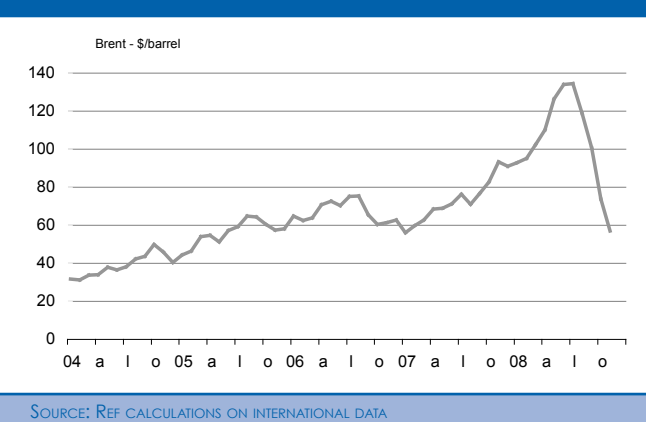
The future course of inflation in general can be traced by considering forecasts for exogenous variables and for the national economy. The disinflationary phase will broaden further in 2009 and it may even bring total inflation close to 1% by the middle of the year. The forecast is based on the reversal of the trend for energy inflation which will become negative in 2009. This will be accompanied by inflation for foodstuffs which will continue to decelerate. In this respect, although the knock-on effect of past increases in cereal prices onto consumer prices has not yet run its course, it is reasonable to expect that price levels will soon stabilise. This is in fact what emerges from available data at the top of the supply chain for producer prices, not only from ISTAT (national office for statistics) but also from the INDIS-Unioncamere Prezzi e Mercati (Prices and Markets) observatory sources.

2008 will end with inflation below 3% with a decelerating effect on the year to come. The effects will tend to be prolonged, partly as a result of the recession

scenarios expected on the consumer front, which will help to create a general climate of price moderation.

One reason why the downturn in the business cycle will affect price trends is because the weakening of end consumer demand will tend to reduce the market power of companies and this will also have its effect on price levels for non foodstuff goods and services. The change in the direction of the business cycle will also reduce the risks of wage acceleration considerably which might have resulted from the erosion of the purchasing power of available income that has occurred in the last year.

SERVICE PRODUCT CONSUMER INFLATION





DOMESTIC PRICES 2008: INFLATION AT ITS HIGHEST LEVELS IN THE SUMMER, BUT WITH A CHANGE IN STORE FOR THE AUTUMN

Consumer inflation rose to exceed 4% over the summer, a level not seen in our price statistics for many years. The strongest driver of inflation was energy products, fuelled by oil prices. However the fall in oil prices created the conditions for a rapid reversal of the trend. The inflation rate has decreased since September as a result of falling energy prices and the outlook for coming months is one of broad probabilities of further falls in inflation. In addition to falling crude oil prices, there is also the statistical effect of a favourable comparison with the same period of the previous year, both for food and energy prices. Gloomy prospects for the growth of the Italian economy will nevertheless have an even greater effect in 2009, and this will have a negative impact on household income and consumption.

ITALY: BREAKDOWN OF INFLATION

ANNUAL % CHANGE

Settori	Avg	Avg	Jun-08/	Aug-08/	Oct-08/
	2006	2007	Jun-07	Aug-07	Oct-07
Food	1,7	2,8	6,0	6,2	5,1
Processed food	2,0	2,7	6,4	6,6	5,6
Fish and seafood	4,2	3,2	4,2	2,2	2,3
Fruit and vegetables	-0,8	3,3	5,0	4,5	3,4
Industrial goods	1,1	1,2	1,6	1,6	1,5
Medical products	0,3	0,5	1,1	1,1	1,1
Clothing	1,3	1,4	1,8	1,8	1,7
Footwear	1,1	1,2	1,5	1,4	1,4
Furniture and furnishings	1,9	2,1	2,4	2,5	3,0
Household appliances	-1,0	-0,5	0,1	0,1	0,0
Radio, Tv, etc.	-9,3	-10,5	-8,0	-10,8	-13,1
Photog. equip., optical instr.	1,1	1,0	1,7	1,7	1,7
Household goods	1,5	2,5	3,0	3,0	3,1
Tools and equip. for house	2,1	3,0	3,1	3,1	3,0
Products for personal care	0,7	1,2	1,7	1,8	1,8
Newspapers, books	1,8	2,8	2,1	2,6	2,3
CD, magnetic tape	0,5	-0,2	-0,6	-3,6	-3,6
Games, toys, sport equip.	0,3	1,0	0,8	0,7	0,7
Miscellaneous goods	8,9	5,0	6,5	6,5	6,3
Motor cars and access.	1,7	1,7	1,5	2,0	2,0
Energy	8,1	1,5	14,7	14,5	10,4
Heating oil and fuels	6,1	0,7	18,2	15,2	8,0
Electricity and gas	10,8	1,9	9,1	13,4	14,3
Services	2,3	2,0	3,2	3,7	3,5
Personal care, recreation	1,5	-1,6	2,0	2,0	2,5
Housing	2,3	3,8	4,2	4,2	4,2
Transport	2,9	2,6	5,7	9,4	6,9
Health	2,3	2,6	3,4	3,3	3,6
Financial and n.e.c.	1,9	1,3	1,7	1,7	2,1
Restaurants and hotels	2,5	2,6	2,7	2,7	2,4
Regulated prices	0,3	0,9	0,2	0,0	0,0
Nationally	-1,2	-1,2	-1,8	-1,8	-1,8
Locally	2,8	4,0	3,1	2,4	2,5
Rents	2,5	2,4	2,5	2,7	3,0
Tobacco	6,3	4,2	2,7	5,4	5,4
All-items	2,1	1,8	3,8	4,1	3,5
All-items excluding fresh food and energy	1,7	1,8	2,9	3,1	2,9

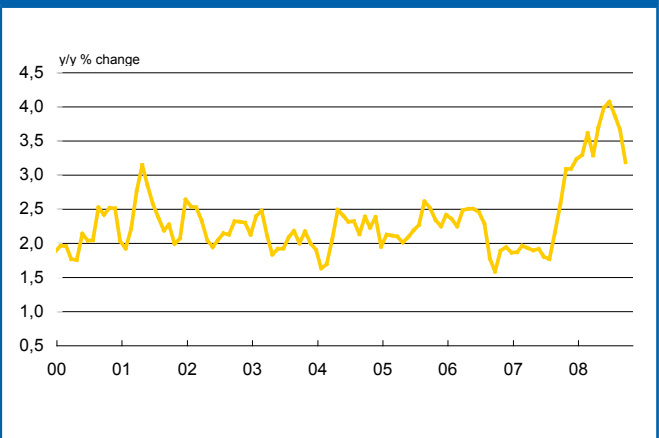
SOURCE: REF CALCULATIONS ON ISTAT DATA (NIC)

INTERNATIONAL PRICES

EUROPEAN INFLATION: THIS WILL CONTINUE TO FALL AGAIN IN 2009

European inflation has risen to levels never before reached in the history of the monetary union, hit by growth in oil prices and in agricultural raw materials prices. In fact energy products and foodstuffs, which account for approximately 30% of total household spending, have generated most of the acceleration. Nevertheless the inflation scenario changed completely in the autumn, because the sharp fall in oil prices suddenly changed the risk from one of high inflation to one of low inflation. The fall in raw material prices together with the recession forecast for the European economy will result in disinflation which will bring the rate of growth in inflation in the area below 2% for 2009.

EURO AREA CONSUMER INFLATION



SOURCE: REF CALCULATIONS ON EUROSTAT DATA

FOCUS

AN END TO RISING RAW MATERIALS PRICES

Raw materials prices have risen greatly in recent years due to a combination of factors on both the demand and the supply side. The pressures on both energy and food prices can be explained by market fundamentals. The conditions arose during the summer for a reversal of the trend in raw materials prices. The change in the scenario for world growth lies at the basis of that reversal.

AGRICULTURAL COMMODITIES - PRICE INDEX



SOURCE: S&P GOLDMAN SACHS INDEX, INDICE 1990=100



FORECASTS

INFLATION IS MOVING TOWARDS 1%

The prospects for Italian inflation have changed radically since the international financial crisis burst. The most visible consequences today are those resulting from the collapse of oil prices. There will be a marked deceleration in inflation in 2009 driven by falls in electricity and gas tariffs, by the stabilisation of foodstuff prices and by a consumer recession which will help to pull down private sector service prices, ranging from restaurants to bars and leisure services. Inflation will hit a new record low in the middle of next year. The risks are of low inflation.

INFLATION IN ITALY: HISTORICAL DATA AND FORECASTS						
ANNUAL % CHANGE						
	2005	2006	2007	2008	2008	2009
	Avg	Avg	Avg	Mar	Avg (*)	Avg (*)
Consumer prices (NIC)						
Food	0,1	1,7	2,8	5,1	5,4	2,4
- ex fresh food	0,8	2,0	2,7	5,6	5,7	2,8
Non-energy industrial	0,9	1,2	1,2	1,5	1,4	1,8
Energy ⁽¹⁾	8,9	8,2	1,5	10,4	10,3	-4,7
Services	2,9	2,3	2,3	3,5	3,3	2,6
Admistrd prices ⁽²⁾	0,0	0,3	0,8	0,0	0,3	1,6
Rents	2,4	2,5	2,4	3,0	2,6	2,9
All-items	1,9	2,1	1,8	3,5	3,3	1,8

(*) Forecasts
 (1) Including regulated energy prices (electricity, gas, etc.)
 (2) Excluding energy (electricity, gas, etc.)

SOURCE: REF CALCULATIONS ON ISTAT DATA (NIC)

FOODSTUFFS

FOODSTUFF INFLATION SLOWS

Foodstuff inflation has slowed in recent months from highs of greater than 6% during the year. The trend seems to be common to all sectors, although for the time being it seems to be affected by a natural year-on-year change in the trend due to a favourable base effect rather than to an end to the period of price increases. The prospects for the next few months are nevertheless positive. The signals from the top of the supply chain, given by producer prices, suggest a genuine phase of price stabilisation.

