

Survey on Inflation and Growth Expectations

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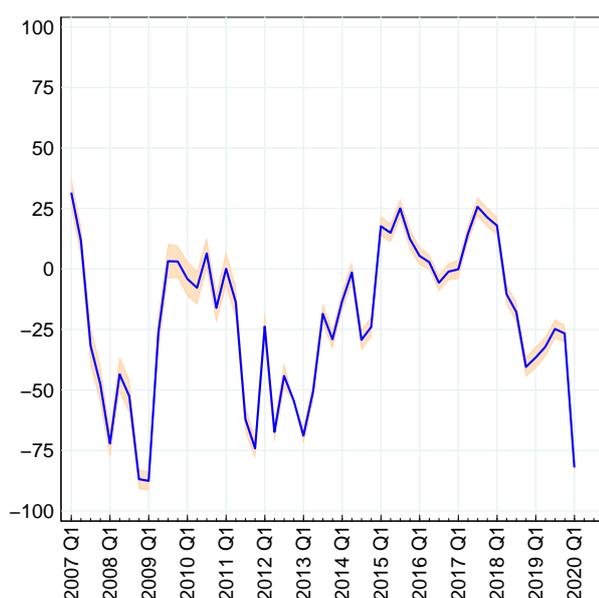
Main results

According to the survey conducted between 3 and 26 March 2020 among Italian firms with 50 or more employees, current and prospective assessments of the general economic situation and of firms' own operating conditions have worsened significantly. The deterioration mostly reflects the spread of the COVID-19 epidemic and the impact of the initial containment measures which, according to firms' responses, led above all to a sharp decline in both domestic and foreign demand. These assessments, although very negative, were made before more restrictive measures were introduced at the end of March.

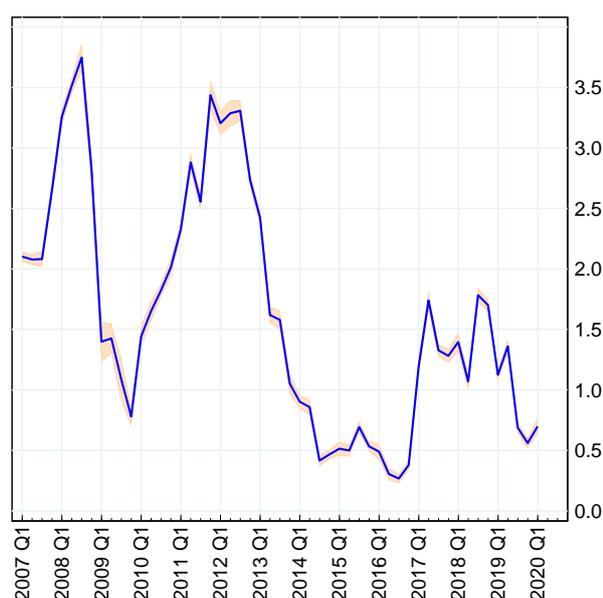
The negative developments in sales, which are expected to continue into the current quarter, have influenced the assessments of investment conditions, which have worsened significantly despite the largely stable credit conditions. Firms plan to reduce their investment expenditure over the course of 2020, especially in the first part of the year. Employment expectations have also worsened in all sectors, but to a limited extent.

Consumer inflation expectations have risen slightly over all time horizons, driven by the modest increase of prices in January. Conversely, firms' own prices slowed compared with the previous quarter and a further slowdown is expected over the next 12 months.

General state of the economy (1)
(balance between positive and negative assessments with respect to the previous quarter)



Consumer price inflation expectations over the next 12 months (1)
(percentage changes on the preceding 12 months)



(1) The shaded areas represent the 95% confidence intervals. Construction firms are included from 2013 Q3. See Tables s1 and s4 of the statistical appendix.

Survey on Inflation and Growth Expectations¹

Assessments of the economic situation worsen markedly, reflecting the spread of the COVID-19 epidemic

In the first quarter of 2020, the share of firms that reported a worsening in the overall economic situation compared with the previous quarter rose to more than 80 per cent (from about 30 per cent in the previous survey), reaching a level comparable to that observed during the global financial crisis and the sovereign debt crisis. The share of firms reporting an improvement was practically nil.

For 70 per cent of firms, there is zero probability that the overall economic situation will improve over the next three months. For more than 90 per cent of firms, the probability is no greater than one in four. This appears to be associated with an overall deterioration in their own business conditions in the second quarter, for which about 65 per cent of firms reported a worsening (compared with 18 per cent in the previous survey) and 30 per cent of firms indicated no change (Figure 1).

The negative assessments reflect above all the spread of the COVID-19 epidemic and the impact of the initial containment measures put in place. About 65 per cent of firms had already registered negative effects on their business at the time of the survey, and 85 per cent of them expect negative repercussions over the next three months. However, at the cutoff date of the survey, the strictest measures placing restrictions on non-essential activities had not been adopted yet.

The negative effects of the epidemic are mainly linked to the fall in demand, both foreign and domestic

For over three fifth of firms in industry excluding construction, the negative effects of the pandemic stem from the fall in both domestic and foreign demand. In the service sector, firms attached greater importance to the former compared with the latter (84 and 23 per cent of firms respectively). Firms' business would appear to be affected, though less evenly, by difficulties in the supply of production inputs, especially in industry excluding construction, and by workforce shortages, especially in services (see Table c19 of the [Statistical Appendix](#)).

For firms in industry excluding construction and in services, the balance between expectations of an increase and of a reduction in overall demand in the first quarter, which has been negative since the end of 2018, worsened further, to -30 percentage points (Table 1). The balance became negative in construction as well (-12 percentage points), after being positive for almost two years.

... which is expected to remain weak in the current quarter

Firms expect a further contraction in demand in the second quarter of this year. The share of firms that forecast a fall rose by 40 percentage points in industry excluding construction and in services (to 57 per cent) and by 25 per cent in construction (to 33 per cent), reflecting a reduction in the assessments pointing both to stability and to an increase. The fall in overall demand, current and expected, appears to be connected to both foreign and domestic demand in

industry, and mainly to domestic demand in services. Assessments of developments in sales in Germany and China, which the firms active in those markets expect to fall by 32 and 50 per cent respectively, appear to have contributed to the negative forecasts of foreign demand.

Assessments of investment conditions worsen significantly ...

The balance between judgments of an improvement and of a worsening in investment conditions widened significantly compared with the previous survey (from -15 to -60 percentage points; Figure 3), reaching levels comparable to those recorded during the two previous crises, despite the fact that assessments of credit access conditions have remained practically stable. The fall, which occurred across all sectors, was marginally more intense for firms in industry excluding construction

¹ The survey report was prepared by Marco Bottone and Michele Loberto.

The survey data were collected exclusively for the purpose of economic analysis and have been processed in aggregate form, in compliance with privacy regulations. We would like to thank the 787 firms with 50 or more employees (of which 356 in industry excluding construction, 328 in services and 103 in construction) that participated in the March 2020 survey. We would also like to thank the firms that participated in the survey after the cutoff date for the analyses presented in the current report. The data provided by these firms will be used in future publications by the Bank of Italy and will be available in the BIRD (Bank of Italy Remote Access to Micro Data) system. The survey questionnaire, the statistical appendix and the methodological note are available on the Bank's website:

https://www.bancaditalia.it/statistiche/basi-dati/bird/inflazione-e-crescita/questionario-inflazione/documenti/en_quest_1_trim_2020.pdf?language_id=1

https://www.bancaditalia.it/pubblicazioni/indagine-inflazione/2020-indagine-inflazione/03/dati_2020_03_eng.zip?language_id=1

https://www.bancaditalia.it/pubblicazioni/metodi-e-fonti-note/metodi-note-2019/methods_and_sources.pdf?language_id=1

(from -18 to -65 points) compared with that observed in services (from -12 to -57 points) and in construction (from -10 to -53 points).

... leading to an abrupt reduction of the investment plans for 2020

Firms' assessments of investment expenditure point to a significant reduction in investment in the first half of this year compared with the second half of last year. The balance between expectations of an increase and a decrease became markedly negative, falling to -26 percentage points, the lowest figure ever reached since the data for this variable started being collected in 2013. The drop was widespread across all sectors and in line with the assessments reported for investment conditions. The contraction in investment expenditure could ease up moderately in

the second half of the year: the balance between expectations of an increase and of a decrease in investment for 2020 as a whole stands at about -20 percentage points in all sectors.

Employment expectations also worsen, though less sharply

The employment expectations for the second quarter point to a reduction in the workforce across all sectors, though the worsening compared with the previous survey appears to be relatively more moderate than that observed for demand and for investment. Developments in employment appear slightly more unfavourable in industry excluding construction, where the balance between the share of firms planning to expand their workforce and the share planning to reduce it declined further, to -9 percentage points (compared with -3 points in the previous survey).

While still negative, the balance is narrower for firms in services (-5.5 points) and in construction (-6 points), which in the last quarter had forecast positive developments in employment.

Inflation expectations rise slightly ...

In line with the temporary, modest improvement in the consumer price index recorded in December and January, in the first quarter of 2020 the inflation rate expected by firms rose slightly on average, offsetting the reduction registered in the December survey. Compared with the previous survey, the expectations are higher by 0.1 percentage points over the 6- and 12-month horizons (at 0.5 and 0.7 respectively; Figures 4, 5 and 6), by 0.2 percentage points over the 24-month horizon (0.9 per cent)

and by 0.3 percentage points over the 3- to 5-year horizon (1.1 per cent).

... while firms' selling prices slow

The current and expected fall in demand has held back selling prices: compared with the December survey, their year-on-year change was slightly negative on average in industry excluding construction and in construction (from 0.7 to 0.6 per cent and from 1.0 to 0.7 per cent respectively; Figures 2.1, 2.2, 2.3), while it was positive by only 1 percentage point in services (where it reached 0.6 per cent). For the next 12 months,

firms in industry expect price dynamics to be significantly weaker compared with the expectations formulated in the previous survey (from 1.0 to 0.3 per cent and from 1.3 to 0.6 per cent respectively); service firms instead revised upwards their expectations compared with the previous survey (from 0.6 to 0.5 per cent). Compared with the December survey, the downward revision in selling prices was mainly driven by the contraction in demand and, to a lesser extent, the fall in commodity prices.

Table 1

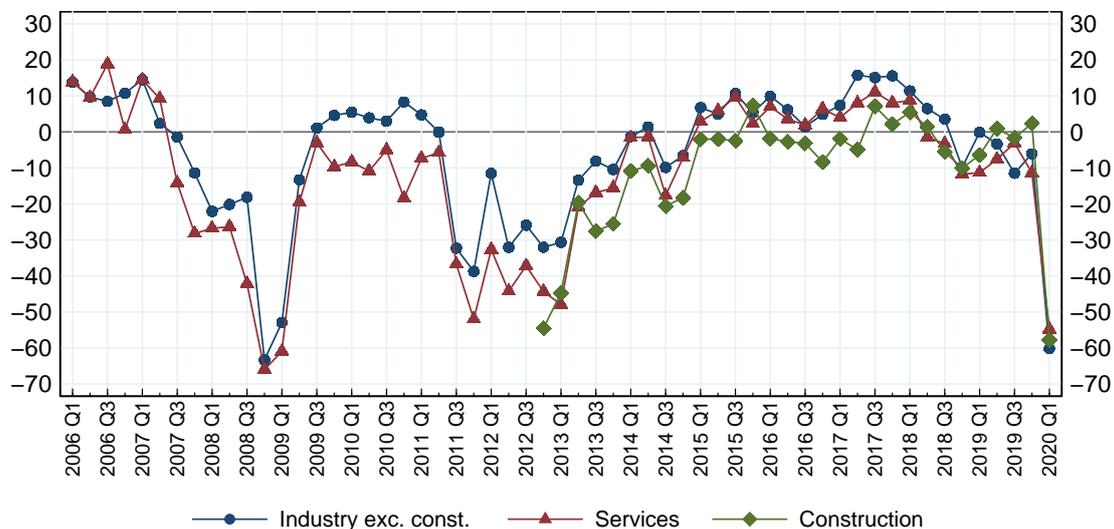
Main findings (1)
(per cent and percentage points)

	Industry exc. const.		Services		Construction		Total	
	2019 Q4	2020 Q1	2019 Q4	2020 Q1	2019 Q4	2020 Q1	2019 Q4	2020 Q1
	per cent							
Inflation expectation 6 months ahead	0.5	0.5	0.4	0.5	0.5	0.5	0.4	0.5
Inflation expectation 12 months ahead	0.6	0.7	0.5	0.7	0.6	0.6	0.6	0.7
Change in own prices 12 months ahead	1.0	0.3	0.5	0.6	1.3	0.6	0.7	0.5
	Balance between reports of improvement and deterioration (percentage points)							
	Judgments on the previous quarter							
General economic situation	-27.0	-84.5	-27.2	-80.1	-18.8	-79.3	-26.7	-82.1
Total demand	-5.1	-32.3	-2.6	-35.5	11.2	-12.1	-3.1	-32.9
Foreing demand	4.7	-23.2	1.7	-14.3	—	—	3.8	-20.5
Investment conditions	-17.6	-65.0	-12.2	-56.4	-10.0	-52.6	-14.5	-60.1
	Forecast 3 months ahead							
Total demand	6.9	-48.7	5.7	-47.2	18.9	-18.2	6.9	-46.4
Foreing demand	16.0	-46.8	9.1	-26.6	—	—	13.9	-40.8
Firms' economic conditions	-6.1	-60.2	-11.4	-54.8	2.3	-57.8	-8.3	-57.4
Employment	-3.2	-9.0	3.7	-5.5	1.4	-6.1	0.4	-7.1
	Forecast of investment expenditure							
H1 2020 on H2 2019	4.5	-30.7	10.7	-22.4	2.2	-23.5	7.4	-26.2
2020 on 2019	1.1	-22.0	10.4	-21.8	4.9	-20.7	5.9	-21.8

(1) The statistical appendix is available at http://www.bancaditalia.it/pubblicazioni/indagine-inflazione/2020-indagine-inflazione/03/dati_2020.03.eng.zip?language_id=1

Figure 1

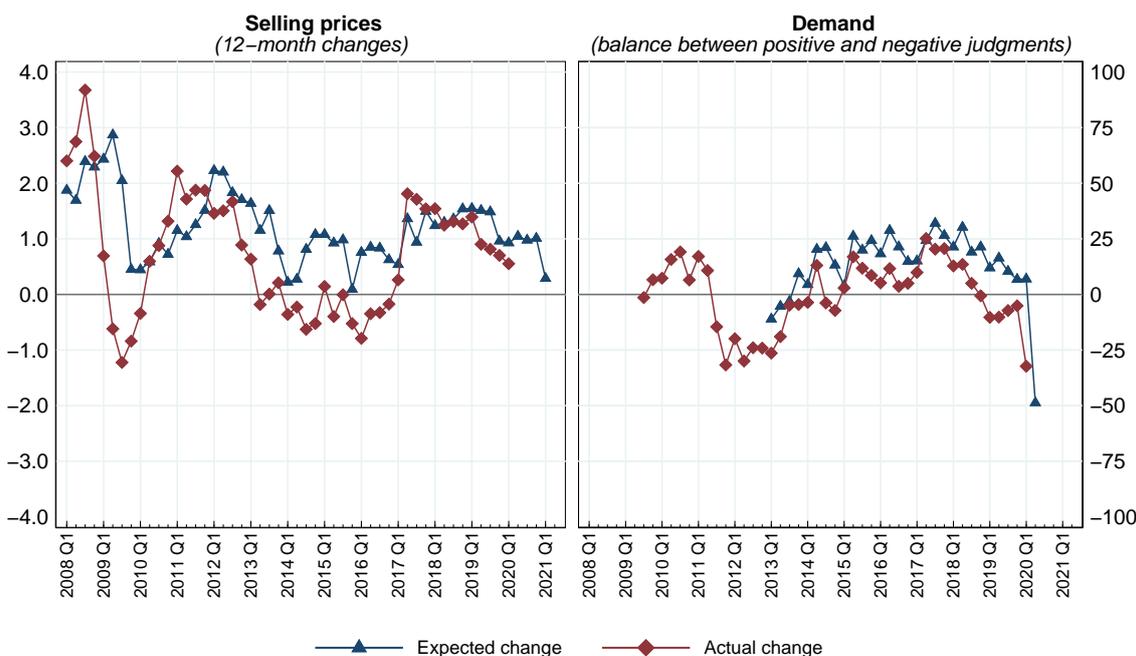
Three-month forecast of the firm's business conditions (1)
(percentage points)



(1) Balance between expectations of an increase and expectations of a decrease.

Figure 2.1

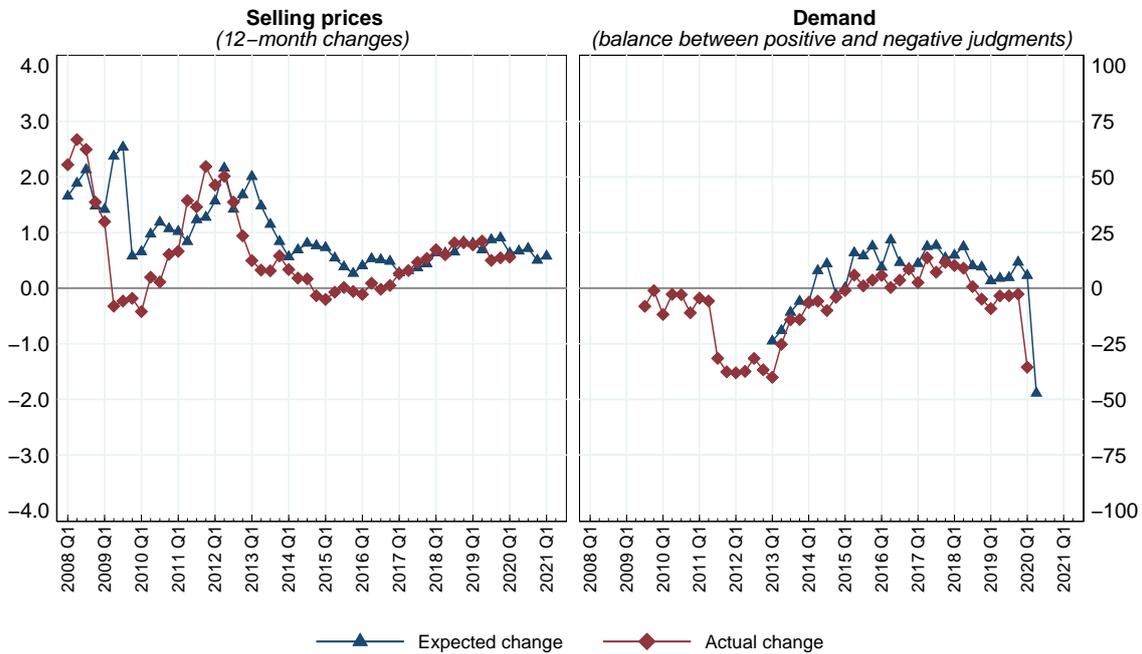
Expected and actual changes in selling prices and demand (1)
(industry excluding construction)



(1) Winsorized estimates: values outside the range between the 5th and the 95th percentiles are set at the threshold values of those percentiles.

Figure 2.2

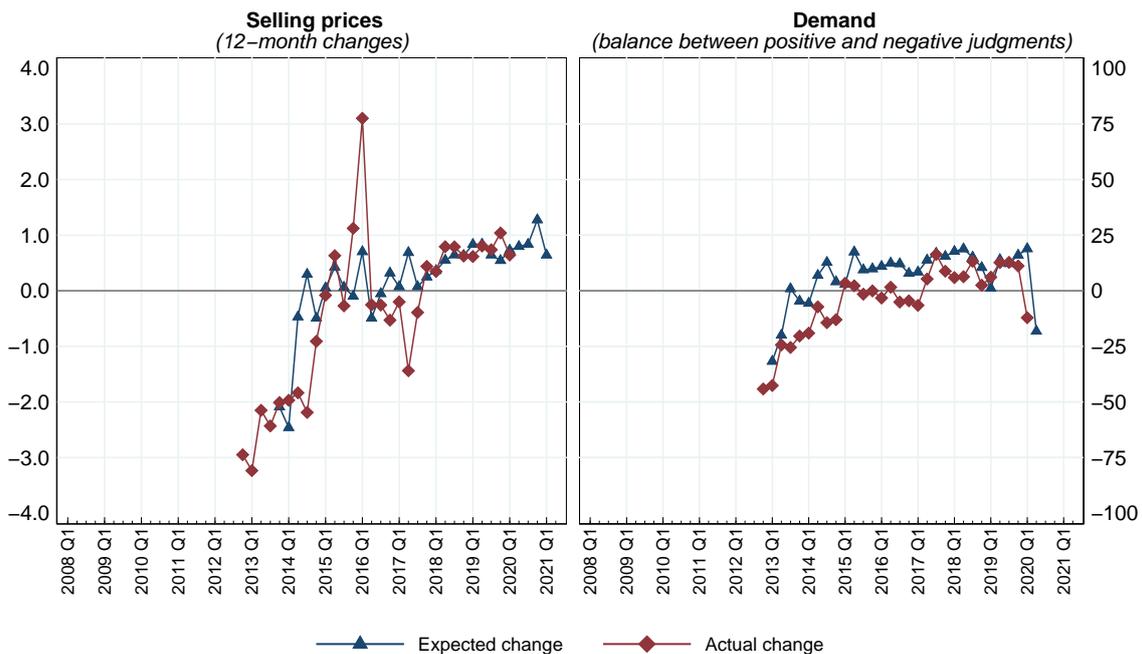
Expected and actual changes in selling prices and demand (1)
(services)



(1) Winsorized estimates: values outside the range between the 5th and the 95th percentiles are set at the threshold values of those percentiles.

Figure 2.3

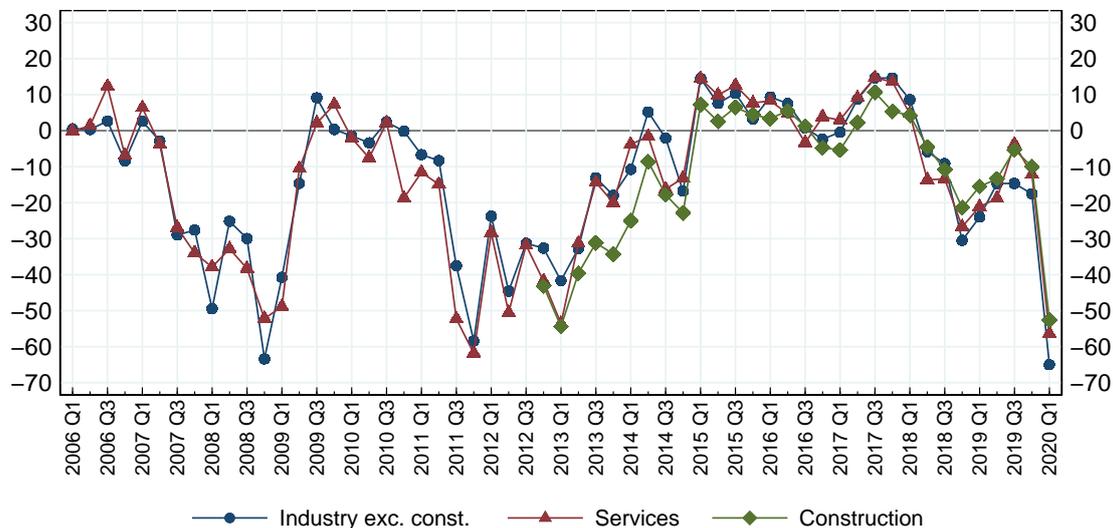
Expected and actual changes in selling prices and demand (1)
(Construction)



(1) Winsorized estimates: values outside the range between the 5th and the 95th percentiles are set at the threshold values of those percentiles.

Figure 3

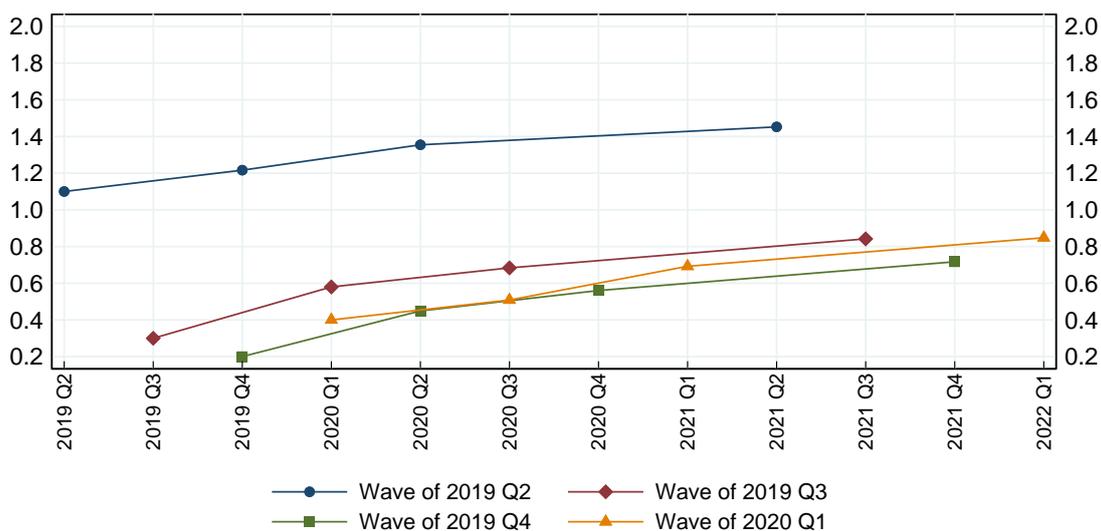
Conditions for investment with respect to previous quarter (1)
(percentage points)



(1) Balance between positive and negative judgments.

Figure 4

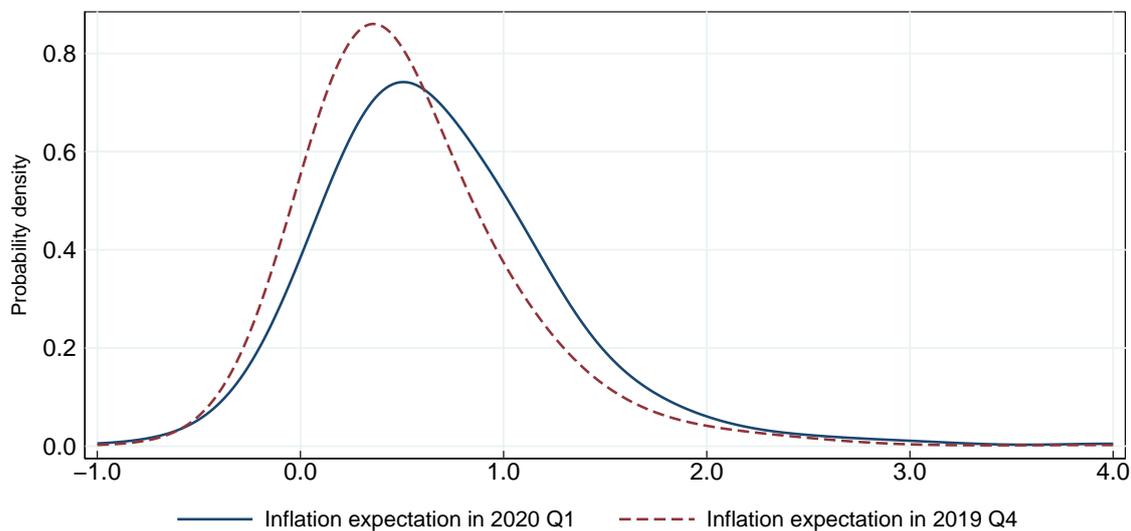
Expectations of consumer price inflation in Italy (1)
(percentage changes on year-earlier period)



(1) The first point in each curve is the latest definitive inflation data available at the time of the survey, which is given to the interviewees in the questionnaire as a point of reference for expressing their expectations; the second point is the average of the interviewees' forecasts for the next six months; the third point is the average of the interviewees' forecasts for the next twelve months; the fourth point is the average of the interviewees' forecasts for the next twenty-four months.

Figure 5

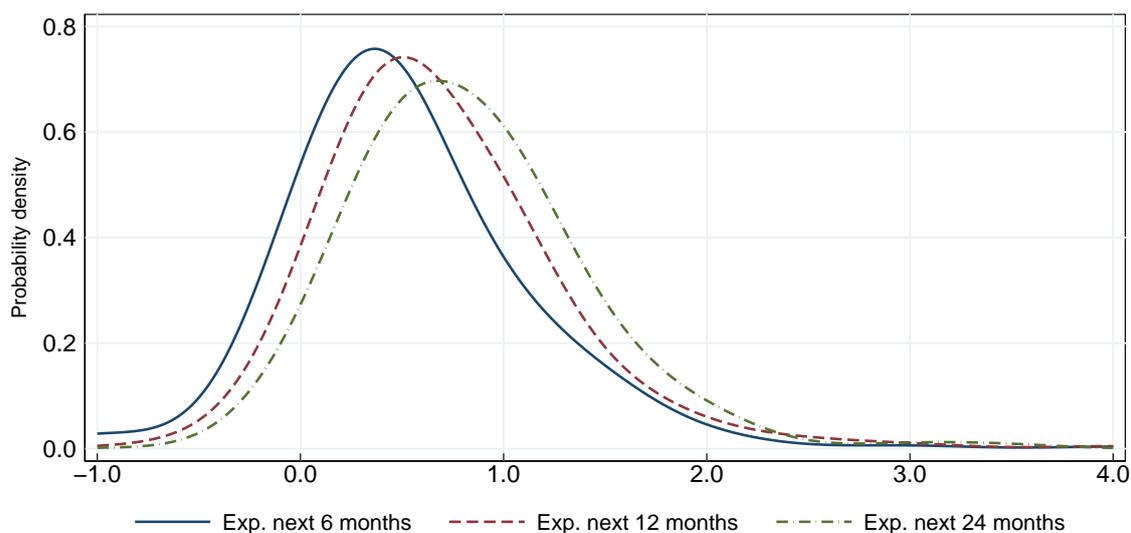
Expectations of the inflation rate over the next 12 months (1)
(non parametric estimates)



(1) The estimates are obtained using a Gaussian kernel density with a bandwidth equal to 0.3.

Figure 6

Expectations of the inflation rate over the next 6, 12 and 24 months (1)
(non parametric estimates)



(1) The estimates are obtained using a Gaussian kernel density with a bandwidth equal to 0.3.

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