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Snap

## Italy: Production drop may help downgrade growth forecasts in budget

The soft industrial production numbers aren't exactly a gamechanger but could help the government justify a possible downward revision of growth forecasts in the amended budget draft that needs to be submitted to Brussels no later than tomorrow

### Modest decrease on the month, driven by investment goods

The industrial production soft patch continued in September, albeit less markedly than the consensus expected.

The seasonally adjusted index contracted by 0.2% month on month (from +1.7% in August), while the working-day adjusted version, better suited to monitor the trend, expanded by 1.3% YoY (from -0.8% in August).

The monthly contraction was driven by investment goods (-1.6% MoM), while intermediate goods were up 1.1% on the month. The 0.3% expansion of consumer goods builds on a 0.7% expansion of non-durables and a 1.9% contraction of durables, reflecting softening car production.

### No big news from the sector breakdown

Sector-wise, a glance at the annual working-day readings helps us better understand the trends in place.

Here energy production leads the pack (+7% YoY), followed by pharmaceuticals (5.1% YoY) and machinery and plants (+4.5% YoY). Transport equipment (+1.5% YoY) confirms the slowdown of previous months, as do sectors such as rubber, plastics and non-metal minerals (-1.5% YoY) and wood and paper (-2.7% YoY), good indicators for the construction pipeline. All in all, the sector breakdown confirms previous patterns with a warning signal coming from short-term developments in investment goods.

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As it is the case with summer data, a usual caveat in interpretation applies as monthly readings could be affected by hard-to-pin-down volatile seasonality issues. Average monthly data for the quarter shows a quarter on quarter contraction of 0.2% in 3Q18 - a number consistent with the flat reading of the preliminary estimate of 3Q18 GDP. Recently released PMI data for October, in contraction territory both in the manufacturing and in the services domains, point to a flat GDP reading also in 4Q18.

This would make the government forecast for 1.2% average GDP growth in 2018 impossible to meet.

### **New budget draft may include growth forecast downgrades**

Tomorrow is the deadline for the Italian government to submit a revised draft budget to the EU Commission.

We don't expect the government to amend its 2.4% deficit/GDP target, often considered as the unmovable political standpoint. However, on the back of poor data releases, we believe the new draft might include less optimistic GDP projections and/or the inclusion of automatic spending cuts to ensure that the 2.4% target is an absolute maximum.

This would be a small signal of flexibility towards softening the confrontational stance towards the EU, in an environment where the Italian government is being increasingly isolated within the EU Council.

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