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Report Highlights: Italy's 2005 wine production dropped 8 percent from 2004 to 49 million hectoliters, due to unfavorable weather. This year's vintage is not reported to be very good, especially for red wines. CY 2004 wine exports recovered after the sharp 2003 decline, with the U.S. still the leading destination. U.S. bulk wine exports to Italy rose dramatically in 2004 and 2005. After bottling, the wine is re-exported to other EU countries.

Includes PSD Changes: Yes
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SECTION I. SITUATION AND OUTLOOK

Italian wine production in 2005 is estimated at 49 million hectoliters, or 8 percent less than in 2004. This is the third smallest crop in the last 50 years. Weather conditions were generally unfavorable in 2005, with too much rain during most of the summer and early fall. The 2005 vintage quality cannot be rated as very good, especially for the red wines. Production of controlled appellation wines still represent about 30 percent of total volume, although this percentage continues to grow slowly, and is mainly concentrated in the north and in Tuscany.

The prolonged difficult market situation for Italian wine, which started in 2004/05, pushed Italian authorities to ask the EU to implement a huge crisis distillation of about 6 million hectoliters. The Commission approved only 2 million hectoliters. Despite the smaller 2005 crop, a new crisis distillation request is likely to be made this year, too.

Domestic wine consumption continues its decades-long decrease, as the number of regular consumers shrinks. Only wine consumption for special occasions is growing.

Italian wine exports in 2004 rose 7 percent in volume and 6 percent in value, mainly as a result of increased sales of both bulk and bottled table wines. The U.S. continues to be the leading export market for Italian wines in value terms (26 percent of the total) followed by Germany and the U.K. Strong competition from other producing countries (such as Australia), however, is challenging Italian exports in both North America and northern European markets.

U.S. wine exports to Italy rose dramatically in 2004 and even more in 2005, due to the decision of a leading Californian company to ship very large amounts of bulk wine to Italy to be bottled locally and then re-exported to other EU countries, mainly the U.K.

SECTION II. STATISTICAL TABLES

WINE

PSD Table

Country Commodity	Italy Wine	(1000 MT)(1000 HL)					
		2003	Revised	2004	Estimate	2005	Forecast
		USDA Official [Estimate[1]	USDA Official [Estimate[1]	USDA Official [Estimate[1]
		Market Year Begin	08/2003	08/2004	08/2005		
TOTAL Grape Crush	0	61564	0	72735	0	68923	
Begin Stock (Ctrl App)	0	12046	0	12000	0	13000	
Begin Stock (Other)	0	20794	0	18484	0	20830	
TOTAL Beginning Stocks	0	32840	0	30484	0	33830	
Prod. from Wine Grapes	0	44086	0	53275	0	49074	
Prod. from Tabl Grapes	0	0	0	0	0	0	
TOTAL PRODUCTION	0	44086	0	53275	0	49074	
Intra-EU Imports	0	1618	0	1411	0	1500	
Other Imports	0	91	0	395	0	500	
TOTAL Imports	0	1709	0	1806	0	2000	
TOTAL SUPPLY	0	78635	0	85565	0	84904	
Intra-EU Exports	0	9227	0	10926	0	11000	
Other Exports	0	4224	0	4009	0	4000	
TOTAL Exports	0	13451	0	14935	0	15000	
Dom.Consump(Cntrl App)	0	9400	0	9300	0	9200	
Dom.Consump(Other)	0	25300	0	27500	0	26500	
TOTAL Dom.Consumptio	0	34700	0	36800	0	35700	
End Stocks (Cntrl App)	0	12000	0	13000	0	13000	
End Stocks (Other)	0	18484	0	20830	0	21204	
TOTAL Ending Stocks	0	30484	0	33830	0	34204	
TOTAL DISTRIBUTION	0	78635	0	85565	0	84904	

ITALIAN WINE IMPORTS BY COUNTRY OF ORIGIN

ITALIAN WINE IMPORTS BY COUNTRY OF ORIGIN						
	Quantity (1000 Hectoliters)			Value (Million Euros)		
	2002	2003	2004	2002	2003	2004
Grand Total	822	1447	1625	204	232	248
France	361	407	346	163	168	170
Germany	21	25	33	3	3	4
Greece	6	6	6	1	1	1
Spain	233	843	819	12	35	36
Portugal	82	75	230	11	12	15
Other EU countries	36	33	14	6	5	4
Total EU	759	1404	1469	197	224	232
U.S.	2	3	110	1	1	8
Australia	3	3	8	1	1	2
Croatia	4	4	3	0	0	0
Argentina	2	5	7	0	1	1
Chile	4	12	16	1	2	2
Hungary	21	16	21	1	1	2
Other Countries	27	16	12	4	3	3

Source: ISTAT

1 Euro = \$0.946 in 2002

1 Euro = \$1.131 in 2003

1 Euro = \$1.244 in 2004

ITALIAN EXPORTS OF WINE & MUST

	ITALIAN EXPORTS OF WINE & MUST QUANTITY (1.000 Hectoliters)			VALUE (Million Euros)		
	2002	2003	2004	2002	2003	2004
DOC/DOCG Wines	4,496	3972	4,112	1,429	1285	1,358
- in bottles	4,176	3688	3,829	1,388	1245	1,322
- in bulk	320	284	283	41	38	36
Sparkling wines	1,103	1086	1,159	165	172	190
Table wines	8,716	6900	7,697	920	957	1,030
Spumanti	872	844	810	215	228	244
Total wines	15,187	12802	13,778	2,729	2640	2,822
Must	446	357	344	22	22	25
Grand total	15,633	13159	14,122	2,751	2,662	2,847

Source: ISTAT

1 Euro = \$0.896 in 2001

1 Euro = \$0.946 in 2002

1 Euro = \$1.244 in 2004

ITALIAN WINE EXPORTS BY COUNTRY OF DESTINATION

ITALIAN WINE EXPORTS BY COUNTRY OF DESTINATION						
	Quantity (1000 Hectoliters)			Value (Million Euros)		
	2002	2003	2004	2002	2003	2004
Grand Total	15,187	12,802	13,778	2,729	2,640	2,822
France	1,830	976	1,023	89	73	78
Germany	5,453	4,577	5,058	732	678	708
U.K.	1,362	1,323	1,506	271	280	311
Belgium	229	200	211	40	40	43
Netherlands	278	256	272	55	52	57
Denmark	234	214	235	59	57	71
Spain	78	99	147	14	17	29
Sweden	327	285	235	66	63	58
Austria	363	326	378	68	66	71
Other EU Countries	488	337	295	55	45	46
Total EU	10,752	8,593	9,360	1,449	1,371	1,472
U.S.	2,001	2,035	2,088	718	710	739
Switzerland	599	536	606	172	174	191
Canada	443	447	489	127	127	140
Japan	354	305	291	115	110	104
Russia	31	58	55	12	18	21
Australia	43	41	32	11	10	11
Other Countries	964	787	889	125	120	144

Source: ISTAT

1 Euro = \$0.946 in 2002

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ITALIAN EXPORTS OF WINE & MUST

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PRODUCTION**General**

After the recovery in 2004, Italian wine production in 2005 shrank again, and is estimated to be below 50 million hectoliters (MHL) for the third time in the last 50 years. According to preliminary estimates made by ISTAT (the Official Institute of Statistics), the final production totaled 49,074,000 hectoliters, 8 percent less than in the previous year. Weather conditions in 2005 were generally unfavorable for the crop's development, although conditions varied by production area and even within each area. Continuous rains during most of the summer and the first part of the fall badly affected the crop, particularly the red grapes, from both quantity and quality standpoints. The situation appears, in general, less unfavorable for the white wines, whose quality gained partial advantage from the relatively high temperature extremes between nights and days during the summer. Excessive rains, on the other hand, created some problems with rot and mold, and lower than optimal sugar content.

Almost every one of Italy's 20 regions saw a decline in 2005 wine production, with only Apulia and Sicily registering increases over 2004. While Sicilian wine was favored with a sunny fall that boosted quantity, Apulian wine quality suffered from high humidity in September. Veneto's wine production decrease was such that it lost its place as the major producing region to Apulia.

Wine grapes are produced in all twenty Italian regions. The following table shows the breakdown of wine production by region during the most recent years.

Italian wine production

Italian wine production (1,000 hectoliters)

Regions	Average 1995- 1999	2000	2001	2002	2003	2004	2005
Piedmont	3,132	2,938	3,324	2,329	2,282	3,263	2,937
Valle d'Aosta	31	27	18	16	18	22	18
Lombardy	1,525	1,360	1,286	1,123	856	1,168	993
Trentino Alto Adige	1,127	1,177	1,230	1,063	1,076	1,269	1,051
Veneto	7,628	8,825	8,668	6,847	7,369	8,843	7,075
Friuli Venezia Giulia	1,137	1,152	1,111	1,006	1,113	1,344	1,143
Liguria	154	169	104	93	106	91	87
Emilia Romagna	6,249	6,915	7,116	5,682	5,305	7,155	6,082
Tuscany	2,611	2,540	2,220	2,319	2,274	3,166	2,533
Umbria	889	966	879	776	812	1,078	862
Marche	1,800	1,609	1,683	1,258	940	1,248	1,123
Latium	3,282	3,733	3,008	2,859	2,441	2,492	2,243
Abruzzo	4,192	3,689	3,441	3,808	3,319	3,585	3,227
Molise	364	310	342	307	274	322	295
Campania	2,113	2,013	1,717	1,761	1,655	1,878	1,784
Apulia	8,706	7,782	6,877	5,580	6,089	7,610	8,181
Basilicata	511	473	391	309	284	341	341
Calabria	811	613	884	531	476	485	497
Sicily	8,968	7,106	7,149	6,209	6,553	6,964	7,661
Sardinia	875	693	845	729	856	943	943
Grand Total	56,104	54,088	52,293	44,604	44,096	53,275	49,074

Source: ISTAT

As can be seen from the above table, the four leading regions (Veneto, Apulia, Sicily and Emilia- Romagna) account, on average, for more than half of total Italian wine production. About half of Italian wines are white, and the remaining half are red and a small amount of rose'.

DOC and DOCG wines represent an increasing share of total Italian production. Controlled Appellation wines (DOC wines) come from carefully delineated areas, have specific requirements regarding the maximum grape yields per hectare, the minimum alcohol content and other quality characteristics, and are subject to EU regulations. Currently, in Italy there are 311 DOC wines (vs 306 one year ago), while the number of DOCG wines (Guaranteed Appellation of Origin) rose from 30 to 32.

Many of the most valuable, well-known Italian wines are DOCG (i.e. Asti Spumante, Barolo, Barbaresco, Chianti, Brunello di Montalcino). While normal DOC wines can be sold at the retail level in containers of up to 60 liters, DOCG wines can only be sold in bottles of 5 liters

or less and must have all the appropriate official identification marks. The DOC & DOCG wine share of total domestic output keeps growing and is estimated to have exceeded 30 percent. The bulk of Italian production, however, is still table wines. Most DOC & DOCG wines come from the north of the country, especially Trentino Alto Adige, Friuli Venezia Giulia, Piedmont, which account for over two thirds of the total, and Tuscany. In most of the south, DOC and DOCG wines are only a minor part of total output.

Planted Area

After the sharp declines reported in the 80's and 90's, Italian vine area still continues to fall, although at a much slower rate. The 2005 area is officially reported at 764,000 hectares, or half of the area of the early 80's.

The current CAP (Common Agricultural Policy) for the wine sector calls for a general prohibition on new vine planting through 2010. At the same time, it provides a special fund for the conversion and restructuring of vineyards, aimed at obtaining better quality wines. EU allocations for Italy in 2004/05 MY were about 103 million euros, which were applied to 14,633 hectares of vines. Most of the allocations are spent in southern Italy, where quality wines are still rare.

Distillation

The CAP provides two different distillation programs: optional distillation, which is automatically initiated at the beginning of each marketing year, and "crisis" distillation, which aims at supporting the market in the event prices for a certain type of wine or in a delimited production region show a significant decline within a certain period of time. During 2004/05, contracts approved under optional distillation totaled 2 million hectoliters, about the same volume as in the previous year. The shrinking domestic market for wine led Italian authorities to ask the EU to introduce a crisis distillation program of about 6 million hectoliters, but the Commission last September approved crisis distillation for 2 million hectoliters of surplus table wine produced in Italy in 2004/05. This volume was considered inadequate by the Italian wine sector, unhappily citing similar Commission decisions for larger volumes for other member states. The growth of unsold stocks of wine will induce many Italian producers to increase the volume distilled under the optional distillation program in the coming marketing year. At the same time, as domestic table wine prices continue to be markedly lower than in the previous two marketing years, a new crisis distillation could be requested and approved even in 2005/06, despite the remarkable production decline reported in current year.

Prices

Domestic wine producer prices rose in 2003/04 due mainly to reduced domestic supply, but then declined sharply throughout the 2004/05 marketing year, consequent to larger domestic supply and falling consumption. According to ISMEA, grower prices averaged 24 percent less than in the previous year for red table wines and 16 percent less for quality red wines (DOC/DOCG). Prices of white wines, too, dropped dramatically, although at slightly lower rates: down 20 percent for table wines and down 12 for quality wines. This situation has not changed in the first part of the new marketing year despite the decrease in production. During August-December 2005, red and white table wine prices were 26 and 21 percent lower respectively than during the same period of 2004, while quality wine prices dropped 28 and 9 percent. This situation reflects the overall European trend of declining consumption and rising competition from new wine producing countries.

Production Policy

The current CAP for the wine sector was fully implemented in 2000/01 and will expire in 2007 when major changes are likely to be implemented, as has occurred in most of the other agricultural sectors. These could include the introduction of decoupled (partial or full) payments to the vine growers, and major changes to the distillation programs, which the Commission believes have not been effective in supporting sectoral development. The Commission's view is that current programs keep the demand for low quality wines artificially high without solving the surplus problem. This is why the implementation of decoupled payments is not seen unfavorably by some of the leading Italian farmer organizations.

CONSUMPTION

Per capita domestic wine consumption in 2004 fell below 50 liters for the first time. Thirty years ago this figure was over 100 liters. During the 90's, decreasing wine consumption was, at least partially, offset by a growth in beer consumption, but in the most recent years Italian consumers have exhibited an increasing preference for mineral water and soft drinks. The strong increase in retail prices of supposed quality wines, moreover, has encouraged many traditional consumers to either buy cheaper table wines or switch beverages. Wines bought for home consumption by Italian families are purchased mainly at supermarkets, with a declining share from traditional retailers and wine shops.

Per capita consumption of beverages in Italy (liters)

	1998	1999	2000	2001	2002	2003	2004
Beer	26.9	27.1	28.1	28.9	28.2	30.1	29.4
Mineral water	144.2	148.1	165.0	172.0	182.9	182.0	178.0
Soft drinks	57.0	58.0	54.9	56.1	65.6	68.9	67.9
Cold tea	3.9	4.0	4.4	4.7	4.5	5.2	5.2
Wine	52.0	51.5	51.0	50.0	51.0	50.5	49.8
Fruit juices	9.6	10.1	10.8	11.2	10.9	16.4	16.4
Spirits	1.4	1.3	1.2	1.1	0.9	0.8	0.8
Total	295.0	300.1	315.4	324.0	344.0	353.9	347.5

STOCKS

Increased output and stagnant domestic demand led 2004/05 wine ending stocks to grow remarkably. They are not expected to decline in 2005/06, despite lower production, as the negative consumption trend continues. The final stock volume, however, will depend on the actual quantities distilled. This latter amount is included in our PSD table in the "domestic consumption, other" line.

INTERNATIONAL TRADE

Italian wine exports in 2004 recovered partially after the sharp decrease in 2003, but still remained well below the levels reached in both 2001 and 2002 when exports exceeded 15 MHL. According to official statistics, 2004 exports increased by about 7 percent in volume and 6 percent in value. Inexpensive wines have fared better in export than the high cost DOC and DOCG wines. Bulk table wine export sales grew by 12 percent. Exports of bottled table wines, too, rose 11 percent reflecting, basically, foreign buyer interest in cheap wines of adequate quality. Sales of DOC/DOCG wines in 2004 rose only 3 percent in volume and 5 percent in value, after the sharp decline in the previous year. These wines represent only 30 percent of the total export quantity, but account for about half of total export value.

2004 export data by destination confirm the U.S as the leading market for Italian wines in terms of value (over a quarter of total exports), while Germany remains the primary market by volume. Exports to France are mainly bulk table wines, where they compete with cheap Spanish wine. The strong Euro has not affected significantly Italian exports to the U.S., despite robust competition from other countries, primarily Australia.

Preliminary data for 2005 indicate further growth in Italian wine exports, although export volumes have grown by 9 percent, but value only by 2. The reason for this is much larger exports of table wines, both bottled and bulk, and reduced profit margins on the quality wines. Exports to the U.S. were stable in quantity, but declined in value. The Italian wine industry is very concerned about the growing price and quality competition on the world market from "new" wine producing countries, such as Australia, Chile, Argentina and South Africa.

Italian wine imports were until recently a negligible share of the total Italian wine market, and were usually prestige products, such as Champagne, Port, and Sherry from other EU countries. Recently, however, imports have been rising rapidly, first because of available inexpensive Spanish bulk wines, which are blended domestically, and, second, starting in 2004, because of significant shipments of U.S. bulk wine.

Shipments from the United States, up to 2003, were exclusively bottled wines, coming mainly from California, growing steadily to a total of about 3 million euros thanks to the marketing activities of some leading U.S. brands, and a reputation for good quality. These products are now available in supermarkets and hypermarkets as well as in top restaurants and hotels. Beginning in 2004 US wine exports to Italy began to register a tremendous rate of growth, reaching 110,000 hectoliters in 2004 (valued at 17.8 million euros) and exceeding 425,000 hectoliters in January-October 2005 (valued at 34 million euros). Most of this new growth is in California bulk wine, shipped to Italy for bottling, and subsequently sold in other EU countries, mainly the U.K. This bulk trade has assisted a brand of California wine widely marketed in Europe to be competitive by reducing tariff, transportation, and bottling costs, the last of which is relatively low in Italy and expensive in California. The bulk exports to Italy could continue to grow, or disappear as rapidly as they appeared depending on the economics of shipping and bottling in the EU. It is interesting to note that the increases in US bulk shipments of wine to Italy almost exactly match the decrease in US wine shipments to the UK. If Intra EU trade statistics are accurate, Italian exports of wine to the UK should also register a similar increase.

FOREIGN MARKET DEVELOPMENT

The Italian Trade Commission (ICE), an agency of the Ministry of Production Activities still is, as in the past, the main public institution to provide export and promotion assistance in foreign markets. Funds used by ICE to promote Italian food and agricultural products, including wines, are provided by the Ministries of Production Activities and Agriculture, as well as the 20 Italian regions, which use ICE as their primary means for promoting their products. Furthermore, some leading trade and farmer associations and many private companies, along with cooperatives and consortia, give ICE contributions to carry out promotion abroad.

Currently ICE has no specific export promotion program for wine, which is included in the general promotional programs for Italian foods and beverages. The 2006 promotional plan of ICE recently passed the Parliament as part of the Budget Law with cuts of expenditures in certain areas, but not in the food and agricultural sector. In general, ICE's yearly expenditures for food and beverage promotion are about 30 million euros (\$ 36 million) of which 4 million euros are from the budget of the Ministry of Productive Activities. The

Ministry of Agriculture has so far allocated some 5 million euros to be spent for the most valuable Italian food products, such as those having recognized appellation of origin and Geographic Indicators, but this program is supposed to terminate in June. In coming years the Ministry of Agriculture will fund "Buonitalia", an agency directly financed by the same ministry, that will promote Italian foods with ICE. The remaining 20 million euros are come from the Italian regions and the private sector, as mentioned above. Out of the total, it is estimated that about one fourth to third is spent to promote wine. The major events include workshops, wine tastings, and point of sale promotions. The main target countries are the U.S., U.K., Canada, Switzerland and Japan. Focus is increasingly given to some growing markets, such as South Korea, Taiwan, Hong Kong, Singapore, and China. The Ministry of Productive Activities allocation is spent almost entirely at fairs and shows, where the cost of national pavillions is shared with private companies on differing bases according to the market, with a higher private share in "mature" markets (like western Europe and the U.S.), and a larger public share in emerging markets (especially China and other far eastern markets). Other activities include financing trade teams to Italy, and organizing wine tastings.