Foreword

The Unipro Annual Report, edited by the Association's Corporate Culture and Study Centre, as usual constitutes a milestone that goes beyond the form of simple back-up documentation to become a tool for studying more recent phenomena and understanding the underlying scenario on which future evaluations of the industry's economic megatrends will develop.

This approach stresses the special attention devoted to analysing the inevitable repercussions of the international tensions that led to the war that broke out in March 2003, as well as to the structural modification of the cosmetics market that has been under way for the last couple of years.

The factor that underwent the most extensive change in 2003 proved to be the component of demand found in the end market: after years of sustained growth, there was a slowdown in the growth rate even of the Italian cosmetics market, which in 2003 was worth more than 8,300 million Euros, although the trend itself remained positive, as the market grew at a rate of 3.8% over the previous year.

Slightly later than in other European countries, Italy has also felt the effect of the far-reaching tensions and the dynamics related to distribution, which have made their mark on a market that is certainly drowsy and influenced by a particularly prolonged economic and financial crisis.

A certain contraction in the sales of some channels had already been in evidence for some time, especially in the perfume shop channel. In 2003, the phenomenon seems to have come back within standard parameters, although it is now clear that we are facing some real structural changes: this is demonstrated by the fact that many firms have embarked on a revision of their distribution strategies that will certainly have important repercussions in the years to come, generating new and more dynamic actions on outlet markets and channels of distribution.

This is because 2003 saw the situation in the other channels grow stronger, especially the more innovative among them, such as the pharmacy and the herbalist's shop, confirming that buying choices have become more heterogeneous and Italian consumers have learned to pay more attention to specialised outlets in recent years.

As far as the corporate structures in the sector are concerned, the phenomena of concentration, acquisition and transformation of new groups continue apace. This is in fact a particularly effervescent moment for Italy's domestic industry, as it can build on its consolidated production capacity, which is related to qualified services and product innovation, but is in some cases influenced by what is now a rather insufficient average size.
A special commitment will have to be devoted to these small and medium-sized enterprises, particularly with regard to policies aimed at achieving internationalisation, both of production and of market. This is demonstrated by the recent establishment within Unipro of the Cosmexport Consortium, whose purpose is to provide direct services for member firms whose dimensions and structures preclude an ability to undertake initiatives of foreign promotion without the aid of suitable supports and facilities.

Unipro therefore declares its mission of providing service and support to help the firms working in this industry to flourish, ever keeping an alert eye on the evolution and the sudden changes at work in the economic scenario, but without neglecting the rôle of scientific and legislative benchmark provider that the Association has acquired over the years.

Alberto Donati
President, Unipro

The Cosmetic Industry

Influenced to a significant degree by the ponderous yet diversified trend in the home market, Italy's domestic industry marked up a wafer-thin increase in turnover, + 2.2%, in 2003, reaching a value of just over 7,150 million Euros.
Totally out of character with recent years, which had always traced positive curves, exports were down by 2.2%, to a volume that did not get through the 1,800 million Euros mark. The main reason for this appears to be the weak dollar, as this is the currency used to transact the majority of Italian cosmetics firms' commercial dealings.

The influences that are making themselves felt on the domestic market are obviously more significantly present on outlet markets, firstly because of the considerable tensions in terms of oil prices and secondly, as far as Italian and other European exporters are concerned, because of the blunting of our competitive edge brought about by the increase in value of the Euro against the dollar.

TURNOVER LOCAL MARKET PER CHANNEL

(Millions of Euros)

Distribution Channels	2002 Value	2002 Var. %	2003 Value	2003 Var. %
Traditional Channels:	**4.575,7**	**0,5%**	**4.770,5**	**4,3%**
- Chemists	517,6	3,6%	560,2	8,2%
- Perfumeries	1.273,9	-5,2%	1.288,6	1,2%
- Mass distribution and Other retail (*)	2.423,1	3,8%	2.552,4	5,3%
- Door to door sales and mail order selling	361,1	-3,7%	369,3	2,3%
Professional Channels:	**591,0**	**3,8%**	**588,8**	**-0.4%**
- Beauticians sales	160,4	3,0%	157,5	-1,8%
- Woman Hairdressers consumption	358,9	4,2%	359,6	0,2%
- Men Hairdressers consumption	71,7	3,6%	71,7	-
Export	**1.836,3**	**3,7%**	**1.795,9**	**-2,2%**
Total Turnover of Cosmetic Industry	**7.003,0**	**1,6%**	**7.155,2**	**2,2%**

(*) Including herbalist shops with a 2002 turnover of 116,9 millions of Euros and a 2003 turnover of 125,8 millions of Euros, with an increase of 7.7%

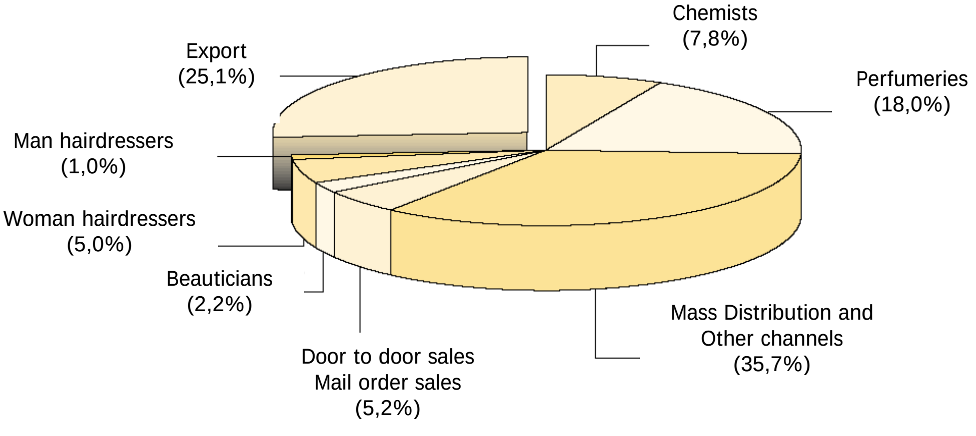
It must be remembered that consumers are turning to alternative channels and products which, in some cases, replace the traditional ones.
Corporate investment strategies are adapting to take these new opportunities into account; the uncertainty that abounds among the factors external to both domestic and international markets is quite significant in this respect.

If we look at how the turnover is distributed among the various channels, we find the more consistent volumes, as usual, moving through perfume shops and department stores, although the increasingly widespread trend towards specialisation is confirmed by the pharmacy (+8.2% over 2002) and sales through herbalist shops (+7.7%), the two channels with the most vigorous increases in turnover.

The overall growth in turnover was certainly slowed down by perfume shop sales, which only increased by 1.2%, and sales through professional channels, which for the first time in a decade actually fell off – though only very slightly (-0.4%).

Despite the expected price tensions attributable first to the introduction of the Euro and then to the increase in its international currency value, at the end of 2003 there was a mean increase in prices of only around 3%, in line with the trend in previous years, although there is still evidence of Italian entrepreneurs' concerns about the marginal profitability anticipated for the coming period, because of the numerous difficulties encountered in retail, especially in the specialised channels.

PERCENTAGE DISTRIBUTION OF TURNOVER BY DISTRIBUTION CHANNEL IN 2003

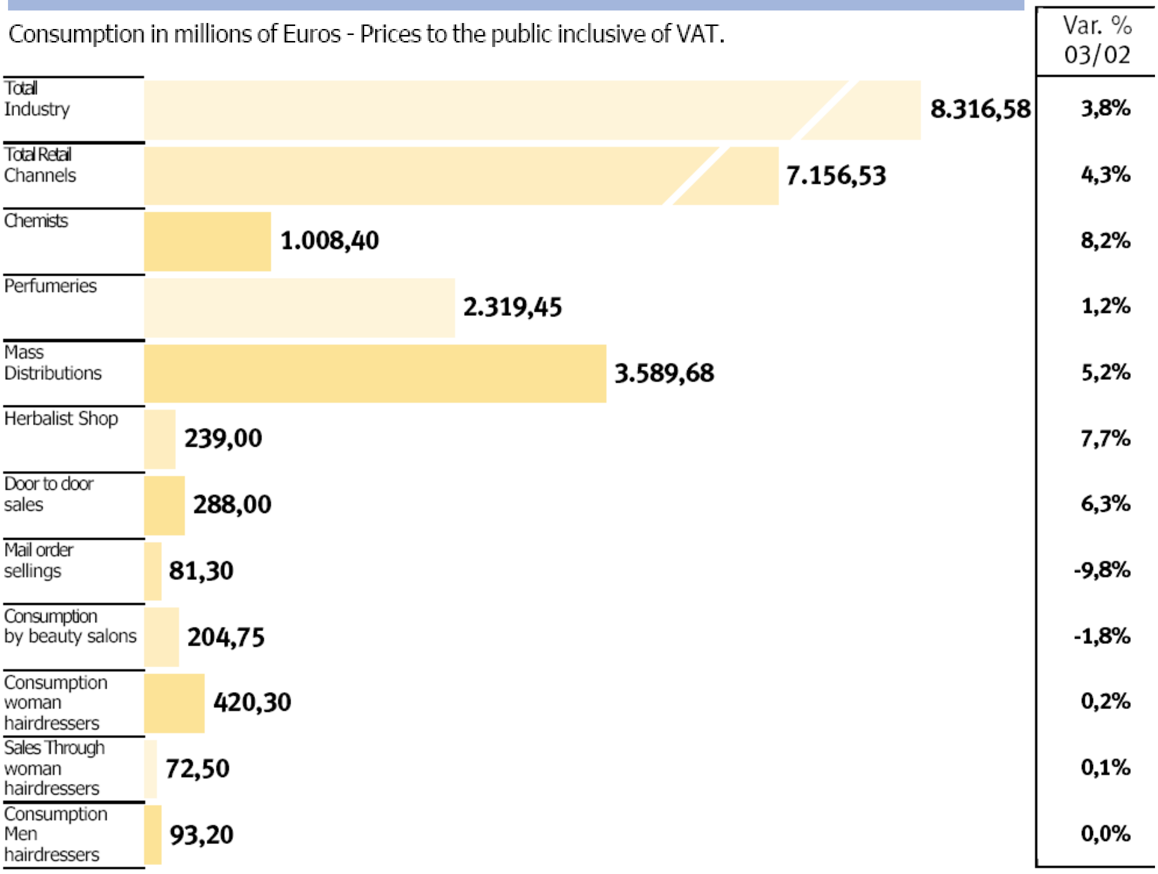


Distribution channels

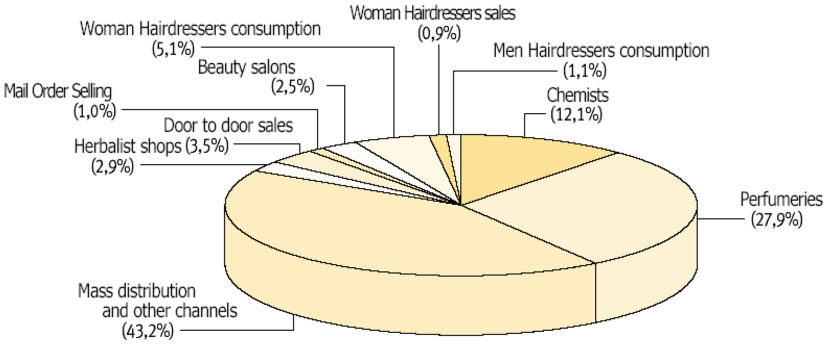
The fact that the domestic market managed to hold its ground, with its value actually growing by 3.8% in 2003, constitutes the confirmation for the cosmetics industry that the Italian consumer is adopting an increasingly specific and qualified approach to the product. Consumers are increasingly aware of the need to satisfy their needs related to the concept of wellness and not only of beauty. Despite the fact that some quite considerable disturbing factors remain, this explains why cosmetics consumption has achieved the quantum leap from a luxury acquisition to a necessary commodity. It also explains why the cosmetics industry can still chalk up positive trends, going against the grain of other contiguous sectors, such as fashion, footwear, glasses and costume jewellery.

TOTAL MARKET FOR COSMETICS PRODUCTS IN 2003

Consumption in millions of Euros - Prices to the public inclusive of VAT.



PERCENTAGE DISTRIBUTION OF CONSUMPTION BY DISTRIBUTION CHANNELS IN 2003



If we now analyse the admittedly decelerated 2003 growth trends by channel, we find that pharmacies, herbalist shops, door-to-door sales and of course the large organised department stores all recorded more dynamic trends in value of consumption, although the lion's share of the volume sold is still the preserve of the large chain stores and the perfume shops, which alone account for more than 70% of all Italian domestic cosmetics consumption.

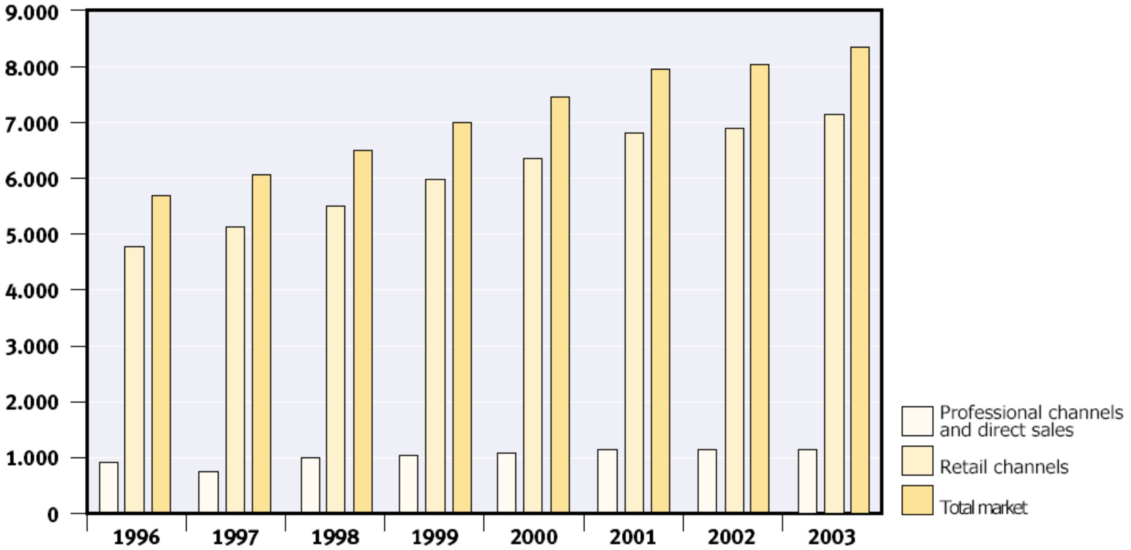
After a few years of crisis, there is an appreciable revival in the air, at least on the value side of the perfumery market (+1.2%), which has given the Italian cosmetic market the boost it needed to pass the 8,300 million Euros threshold.

TRENDS IN DISTRIBUTION CHANNELS IN THE COSMETICS INDUSTRY

DISTRIBUTION	PERCENTAGE VARIATIONS		
	Consumption	Quantity	Prices
Chemists	8,2%	5,2%	2,9%
Perfumeries	1,2%	-2,3%	3,5%
Other Channels	5,3%	2,7%	2,6%
TOTAL TRADITIONAL CHANNELS	**4,3%**	**1,4%**	**2,9%**
Door to door sales and mail order sellings	2,3%	1,1%	1,2%
Sales to Beauty Salons and Beauticians	-1,8%	-3,2%	1,5%
Consumption by Woman Hairdressers	0,2%	-3,7%	4,0%
Consumption by Men Hairdressers	-	-3,8%	4,0%
TOTAL	**3,8%**	**0,8%**	**2,9%**

EVOLUTION IN COSMETICS CONSUMPTION PERIOD 1996 - 2003

Real values, prices to the pubblic, VAT included



In terms of prices, 2003 practically confirmed the same kinds of pricelist revisions that had been applied in previous years, with a mean increase of 2.9%.

Although it has documented the undisputed predominance of the retail channel, demonstrating an increasingly evident preference for product specialisation and diversification, from the beginning of the nineties to the present day the evolution in cosmetics consumption has attributed a rôle to the professional channels that has long since ceased to be marginal. Nevertheless, in 2003, these channels suffered a slowdown that afflicted beauty salons more acutely. This phenomenon is a temporary one, however, related more to economic trends than to structural phenomena.

It is worth taking a separate look at the herbalist's shop, which has only merited a category of its own in recent years and has been found to enjoy some quite considerable growth dynamics, although its market volumes are still very small, certainly less than the door-to-door sales that also benefited from a significant increase in 2003.

Before analysing the individual channels in detail, it is worth remembering that the Italian market's substantial buoyancy was part of a situation, also at European level, that produced more dynamic results than in 2002: after taking a downturn for the first time in the last decade, the German market has clawed its way back, with an increase of 2.3%, while France, whose demand had fallen off in previous years, grew by 2.8%. Only Spain, with a growth rate of 6.8%, seems to have been immune to the slowdown in demand, confirming that it is not yet suffering the effects of market maturity.

CHEMISTS

Achieving a total consumption in excess of 1,008 million Euros, making it the third largest channel by volume after the large department store chains and the perfume shops, sales through the pharmacy channel in 2003 recorded the highest growth index of all the channels, +8.2% at current prices.

This channel, which now accounts for 12.1% of the Italian market, was the one that practised the best development strategies: the combined action of the pharmacists themselves, of the expansion of the range of products they offer and of the firms that developed increasingly channel-specific marketing methods and therefore invested in suitably dedicated products was what brought about the channel's significant increase. Consumers who prefer to go to the pharmacy are expressing particularly acute, selective buying options: for this reason, the products in highest demand are the ones that express a value that goes well beyond the mere product formula, especially in the case of body and facial care.

PERFUMERIES

Although this is the channel that has suffered more than any other from the changes in buying habits in recent years, the perfume shop follows the large department store chain as the retail channel that accounts for the highest value of cosmetic consumption. In 2003, in fact, the volume of goods sold through this channel was about 2,320 million Euros, accounting for 27.9% of the Italian market.

It is worth noting that, while consumption through this channel increased by 1.2% in current price terms, prices increased in the channel by 3.5%. It should also be considered that alcohol-based products still account for the lion's share of the volumes sold here, grossing a value of 690 million Euros, but they are also the product category that registered one of the most striking market contractions, with a fall of 3.2%.

A significant impact was made in this channel by the increase of important product families, such as bodycare products, up by 6.7% to a volume of more than 265 million Euros, and body hygiene products, up by 12.3%, with consumption approaching 100 million Euros. This confirms the trend towards specialisation and diversification of product categories that has marked the perfume shop channel in recent years and enabled producers to maintain their operating margins.

Businesses are very concerned by the fact that the uncertainties about this channel's future evolution remain unsolved, as this compounds the difficulties involved in renewal, especially of that component in the product range that is related more closely to the concept of selectivity. No less evident is the irreversible phenomenon of this channel's replacement by the large department stores, which in recent years have absorbed significant product shares that used to be distributed only in the perfume shops until a short while ago.

MASS DISTRIBUTION

This is certainly the channel that has proved most skilful in recent years at interpreting what has meanwhile become a structural change in consumer buying habits. Achieving the largest quota of absorption of cosmetic product consumption, more than 3,800 million Euros or 43.2% of the entire market in 2003, large scale distribution continued its slow but irresistible process of swallowing up market shares that used to be the preserve of other channels.

As a matter for fact, the move being made by consumers towards more specialised channels and their tendency to go for more specific products has not influenced the growth trend, on the contrary: facilitated by the phenomenon of replacement mentioned above, this channel achieved a growth rate of 5.3% in 2003, one of the highest in the entire market, even though the price trends are in line with the market average.

Once again, the category of products that sold best in 2003 was haircare, grossing more than 915 million Euros, followed by body hygiene at 780 million Euros, although the categories that marked up the most vigorous increases were bodycare and handcare products and the new phenomenon of skin hygiene products for children, confirming the choice of very dynamic, targeted distribution strategies, with a special focus on prices, though without neglecting individual product quality.

DIRECT SALES CHANNELS

The loss of volumes recorded in previous years seems to have stopped, just as there seems to be a weakening of the difficulties encountered in developing a method of distribution that has always had a harder time finding its feet in Italy than in other countries.
This year, in fact, the share of the market covered by door-to-door and mail order sales reached 4.5% of the whole cosmetics sector, with a volume verging on 370 million Euros and a growth rate that was at last positive, even though it remained lower than the market average.

There is still much uncertainty with regard to what weight may be attributed to a new phenomenon that could influence the development of these channels: online sales are difficult to quantify at the moment, but are certainly more in tune with those categories of consumers who feel themselves closer to this new class of distribution.

BEAUTY SALONS

After more than three years of constant expansion, the channel of cosmetic product sales through beauty salons, which benefits from an increasingly extensive use of these facilities by new categories of consumers, as well as from increasingly aggressive industry campaigns, stalled slightly in 2003.

The trend in this channel in 2003 actually went against the mainstream of other channels, with a volume that weighs in at nearly 205 million Euros, or 2.5% of the whole domestic market. Nevertheless, the reduction of 1.8% does not appear to depend on changes in the channel's structure so much as on macroeconomic events that simply influenced this channel more than others. This may also be attributable to the channel's still rather small share of the market and to uncertainties stemming from the lack of standard market penetration strategies remarked on by many businesses.
The channel's health is also influenced by the increase in prices, up by 1.5% in 2003, which confirms that manufacturers' trust in this type of distribution is still pending.

HERBALIST SHOPS

As mentioned in the introduction to this report, herbalist shops have only recently been acknowledged as a new channel in their own right for statistical surveys in this industry. In 2003, they accounted for a volume of nearly 240 million Euros, a significant 7.7% up on the previous year, second only as a growth rate to that achieved by the pharmacies, in a channel that now takes care of nearly 3% of the whole domestic cosmetics market.
This evident dynamic can be sourced to the recent expansion in points of sale, all aligned with the potential of a channel that is still in an early stage of evolution and establishment.

The types of cosmetic products that sell best through herbalist shops confirm the potential of a channel that obviously puts the accent on cosmetics for facial care, hygiene and bath products, body products and haircare products, all of course featuring contents with a clearly naturalist vocation.

HAIRDRESSING SALONS

Despite a substantial slowdown in their rates of growth, in 2003 the professional channels confirmed their significant weight on the cosmetics market, accounting for a value of nearly 600 million Euros, up 0.2% on the previous year.

Once again, the phenomenon appears to be more macroeconomic than structural in nature, deriving from a partial reduction in consumption in the earlier part of the year. In the light of the potential that may well develop as a result of the new law governing the profession, the years to come will certainly demonstrate this channel's real potential.

A reading of the data about the product categories in question here confirms the approach of relating sales to the professional services provided by the channel, although there are also signs of new developments for such products as lotions, conditioners and masks, which are reviving after years of moderate consumption, a sign that the manufacturers are still paying lively, qualified attention.
In the light of such phenomena, the increase in prices is normal. In 2003, they were up by 4%, somewhat higher than the industry's average, confirming that the channel is still dynamic and in a phase of evolution.