Ressort: Wirtschaft und Finanzen

Economic Forecast: Italy

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According to Spring 2018 Economic Forecast, European Union economic expansion is expected to continue, amid new risks. Growth rates for the EU and the euro area outclassed expectations in 2017 to reach a 10-year high at 2.4%. Growth is set to remain strong in 2018 and ease only slightly in 2019, with growth of 2.3% and 2.0% respectively in both the EU and the euro area.
As regards Italy, two days ago Fitch lowered

the outlook, from stable to negative, of five Italian banks: UniCredit, Intesa Sanpaolo, Mediobanca, Credem and BNL. The decision reflected a similar one on Italy's sovereign debt, taken last week, the ratings agency said. Following the formation of the new coalition government, Fitch expects a degree of fiscal loosening that would leave Italy's very high level of public debt more exposed to potential shocks. The long-term BBB rating remains confirmed.
On the other side, the report of 23 May 2018 of the European Commission concluded that Italy complied ex-post with the mandatory adjustment towards the medium-term budgetary objectives (MTO) in 2017 and that there was some progress in adopting and implementing growth-enhancing structural

reforms. Overall, the debt criterion should be considered as currently complied with. However, the report also concluded that the adjustment in 2018 appears inadequate to ensure compliance with the adjustment path towards the MTO in 2018.Already in 2015, 2016 and 2017, the European Commission prepared reports under the Art. 126(3) of the Treaty for Italy. Article 126 of the Treaty on the Functioning of the European Union (TFEU) lays down the excessive deficit procedure (EDP). While the 2015 and 2016 reports concluded on the basis of a consideration of all relevant factors that the debt criterion had to be considered as complied with, the 2017 report concluded that the debt criterion should be considered as not complied with and postponed

a decision on whether to recommend opening an Excessive Deficit Procedure EDP to the analysis of the Commission 2017 spring forecast.
The 2017 Country Specific Recommendations (CSRs) for Italy concluded in that respect: “In April 2017, the Government adopted the requested additional consolidation measures. Therefore, no further steps are deemed to be necessary for compliance with the debt criterion (...)”. According to the European Commission spring 2018 forecast, 2018 is expected to be the first year in the Economic and Monetary Union in which all governments achieve a nominal budget deficits of less than 3% of GDP. The euro area's

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debt-GDP ratio is also forecast to fall to 84.1% in 2019, with declines in many Member States.

However, Belgium and Italy comply with the debt criterion of the Stability and Growth Pact (SGP) only after a consideration of all relevant factors. They would not comply on the basis of the debt figures and structural balance figures alone. Italy performed a significant fiscal adjustment between 2010 and 2013, which allowed the country to exit the excessive deficit procedure in 2013, by keeping headline deficits at a level not above 3% of GDP as of 2012 (down from more than 5% in 2009) and raising the primary surplus to over 2% of GDP. However, the fiscal stance eased in more recent years, mainly by cutting the tax burden and taking advantage of the fiscal space created by lower interest expenditure, which declined steadily

from the peak of 5.2% of GDP in 2012 to 3.9% in 2016.
As a result, the headline deficit stabilized at around 2.5% of GDP, while the primary surplus fell to 1.5% in 2015, without improving since then. The structural primary balance is estimated to have worsened by some 1.6 percentage points of GDP between 2013 and 2016 (from 3.9% to 2.3% of GDP) and is expected to decline further in 2017-2018. That reduction in the fiscal stance was partly used to support private investment and facilitate the adoption/implementation of structural reforms (for instance through tax incentives), while reducing the risk of entering a low-inflation-low-growth trap. Debt refinancing risks have been alleviated in the short term by the liquidity made available

by the ECB and Italy's improved external position, which made the country less dependent on external capital flows. After increasing by around five percentage points per year on average during the double-dip recession of 2008-2013, Italy's government debt-to-GDP ratio continued to increase, but at a slower pace (1.6 percentage points on average) in 2014-2015. In 2016-2018, the debt ratio is expected to float around 133% of GDP.

In this context, the accommodative monetary conditions are decisively contributing to reducing the differential between the average interest rate paid on debt and the GDP growth rate. Overall, the high public debt remains an important source of vulnerability for the Italian economy, but the low interest rate environment is playing a significant mitigating role also by supporting a gradual economic recovery. On the other hand, the lower primary surplus, alongside with low real GDP growth and inflation, hinders the reduction of the high public debt ratio and privatization proceeds are falling short of the government plan.

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