



Dipartimento  
del Tesoro

# **From the Stability Program to the DBP... and on to the next one**

Riccardo Barbieri Hermitte  
Department of the Treasury  
Economy and Finance Ministry

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# 2019 Stability Program

## 2019-2022 macroeconomic forecast

Policy scenario					
(% change yoy)	2018	2019	2020	2021	2022
<b>Real GDP</b>	<b>0.9</b>	<b>0.2</b>	<b>0.8</b>	<b>0.8</b>	<b>0.8</b>
<i>Domestic demand net of inventories</i>	<i>1.0</i>	<i>0.5</i>	<i>0.9</i>	<i>0.8</i>	<i>0.7</i>
<i>Inventories</i>	<i>0.0</i>	<i>-0.2</i>	<i>0.0</i>	<i>0.0</i>	<i>0.0</i>
<i>Net export</i>	<i>-0.1</i>	<i>0.0</i>	<i>-0.1</i>	<i>0.0</i>	<i>0.1</i>
<b>Nominal GDP</b>	<b>1.7</b>	<b>1.2</b>	<b>2.8</b>	<b>2.6</b>	<b>2.3</b>
<b>GDP deflator</b>	<b>0.8</b>	<b>1.0</b>	<b>2.0</b>	<b>1.8</b>	<b>1.6</b>
<b>Compensation per employee</b>	<b>2.0</b>	<b>1.2</b>	<b>1.5</b>	<b>1.3</b>	<b>1.6</b>
<b>Productivity (on GDP)</b>	<b>0.1</b>	<b>0.3</b>	<b>0.5</b>	<b>0.2</b>	<b>0.3</b>
<b>Unit labour cost (on GDP)</b>	<b>1.9</b>	<b>0.9</b>	<b>0.9</b>	<b>1.1</b>	<b>1.3</b>
<b>Employment (FTE)</b>	<b>0.8</b>	<b>-0.1</b>	<b>0.3</b>	<b>0.6</b>	<b>0.5</b>
<b>Unemployment rate</b>	<b>10.6</b>	<b>11.0</b>	<b>11.1</b>	<b>10.7</b>	<b>10.4</b>
<b>Current account balance</b>	<b>2.6</b>	<b>2.5</b>	<b>2.4</b>	<b>2.4</b>	<b>2.4</b>

Source: ISTAT and Government projections for 2019-2022 (2019 Stability Program, 9 April 2019)

# 2019 Stability Program: fiscal projections

## The outlook for the public finances

<b>Policy scenario</b>						
<i>% of GDP</i>	<b>2017</b>	<b>2018</b>	<b>2019</b>	<b>2020</b>	<b>2021</b>	<b>2022</b>
<b>General government balance</b>	<b>-2.4</b>	<b>-2.1</b>	<b>-2.4</b>	<b>-2.1</b>	<b>-1.8</b>	<b>-1.5</b>
<i>Structural balance (1)</i>	<i>-1.4</i>	<i>-1.4</i>	<i>-1.5</i>	<i>-1.4</i>	<i>-1.1</i>	<i>-0.8</i>
<i>Change in the structural balance</i>	<i>-0.4</i>	<i>-0.0</i>	<i>-0.1</i>	<i>0.2</i>	<i>0.3</i>	<i>0.3</i>
<i>Flexibility granted</i>	<i>0.39</i>	<i>0.00</i>	<i>0.18</i>	<i>0.0</i>	<i>0.0</i>	<i>0.0</i>
<b>Output gap</b>	<b>-1.8</b>	<b>-1.5</b>	<b>-1.7</b>	<b>-1.6</b>	<b>-1.6</b>	<b>-1.6</b>
<b>Interest expenditure</b>	<b>3.8</b>	<b>3.7</b>	<b>3.6</b>	<b>3.6</b>	<b>3.7</b>	<b>3.8</b>
<b>Public debt (2)</b>	<b>131.4</b>	<b>132.2</b>	<b>132.6</b>	<b>131.3</b>	<b>130.2</b>	<b>128.9</b>

(1) Net of one-off measures and cyclically adjusted. Discrepancies, if any, are due to rounding.

(2) Gross of financial support to Eurozone countries.

Source: ISTAT, Bank of Italy and Government projections for 2019-2022 (2019 Stability Program, 9 April 2019)

# From the Stability Program to the 1 July mid-year update

- In early June, European Commission's art.126(3) Report concluded that EDP was warranted
- Italian government lowered official deficit projection for 2019 with mid-year Budget update...
- ...and introduced a further 1.5 billion expenditure cut via a decree law.
- Commission eventually reversed its recommendation in response to Italy's 1 July package
- Government also committed to deliver a broadly compliant 2020 Draft Budgetary Plan

# 1 July package

	million euros	% of GDP
<b>General government net lending - 2019 Stability Program (A)</b>	<b>-42123</b>	<b>-2,37</b>
<b>Update revenue estimates, June 2019 (B)</b>	<b>6240</b>	<b>0,35</b>
<i>of which:</i>		
<i>tax revenues</i>	2900	0,16
<i>social security contributions</i>	600	0,03
<i>other revenues</i>	2740	0,15
<b>Updated expenditure estimate, June 2019 (C)</b>	<b>1020</b>	<b>0,06</b>
<b>Net change in net lending estimate (D = B+C)</b>	<b>7260</b>	<b>0,41</b>
<b>Updated net lending estimate (E = A+D)</b>	<b>-34863</b>	<b>-1,96</b>
<b>Adjustment Budget (F)</b>	<b>-1154</b>	<b>-0,06</b>
<i>of which:</i>		
<i>Development and Coesion Fund</i>	-500	-0,03
<i>App 18</i>	-100	-0,01
<i>Revenue Agency</i>	-50	0,00
<i>Local public transportation</i>	-300	-0,02
<i>Fund for social policies, Fund for scholarships, Universities etc.</i>	-204	-0,01
<b>Updated net lending estimate including Adjustment Budget (G = E+F)</b>	<b>-36017</b>	<b>-2,03</b>
<b>Expenditure freeze (D.L. n.61, 1/7/2019) (H)</b>	<b>1500</b>	<b>0,08</b>
<b>Total of package</b>	<b>-34517</b>	<b>-1,94</b>
<b>Nominal GDP (2019 Stability Program)</b>	<b>1777899</b>	

Source: MEF

# Stability Program update (30 September)

- 2019 deficit forecast raised to 2.2% of GDP, still lower than in the Stability Program (2.4%).
- Deficit target for 2020 set at 2.2% of GDP (from 2.1% in SP2019), 1.8% in 2021 and 1.4% in 2022.
- Projected changes in the structural balance +0.3pp in 2019, -0.1 in 2020 and +0.2 in 2021-2022.
- Additional flexibility of 0.2 pp of GDP to be requested for 2020 for unusual events in order to finance expenditures to mitigate hydrogeological risk and improve environmental sustainability.
- Budgetary plan includes the repeal of the 2020 VAT hike, a cut in the tax wedge on labour and resources for the Green New Deal
- Financing to come from a Spending Review, measures to improve tax compliance and combat fraud, environmental taxes and cuts in harmful subsidies.

# Updated macroeconomic forecast

## Stability Program Update (September 2019)

Policy scenario					
(% change yoy)	2018	2019	2020	2021	2022
<b>Real GDP</b>	<b>0.8</b>	<b>0.1</b>	<b>0.6</b>	<b>1.0</b>	<b>1.0</b>
<i>Domestic demand net of inventories</i>	<i>1.1</i>	<i>0.6</i>	<i>0.8</i>	<i>0.9</i>	<i>0.8</i>
<i>Inventories</i>	<i>-0.1</i>	<i>-1.1</i>	<i>-0.2</i>	<i>0.1</i>	<i>0.2</i>
<i>Net export</i>	<i>-0.3</i>	<i>0.6</i>	<i>0.1</i>	<i>-0.1</i>	<i>0.0</i>
<b>Nominal GDP</b>	<b>1.7</b>	<b>1.0</b>	<b>2.0</b>	<b>2.7</b>	<b>2.6</b>
<b>GDP deflator</b>	<b>0.9</b>	<b>0.9</b>	<b>1.3</b>	<b>1.7</b>	<b>1.7</b>
<b>Compensation per employee</b>	<b>2.2</b>	<b>1.3</b>	<b>1.3</b>	<b>1.9</b>	<b>1.9</b>
<b>Productivity (on GDP)</b>	<b>-0.1</b>	<b>-0.4</b>	<b>0.2</b>	<b>0.4</b>	<b>0.1</b>
<b>Unit labour cost (on GDP)</b>	<b>2.2</b>	<b>1.7</b>	<b>1.1</b>	<b>1.5</b>	<b>1.8</b>
<b>Employment (FTE)</b>	<b>0.8</b>	<b>0.5</b>	<b>0.4</b>	<b>0.6</b>	<b>0.9</b>
<b>Unemployment rate</b>	<b>10.6</b>	<b>10.1</b>	<b>10.0</b>	<b>9.5</b>	<b>9.1</b>
<b>Current account balance</b>	<b>2.5</b>	<b>2.7</b>	<b>2.7</b>	<b>2.6</b>	<b>2.5</b>

Source: ISTAT and Government projections for 2019-2022 (Update of the Economic and Financial Document 2019)

# Real GDP forecast - components

September 2019 forecast: GDP components

Policy scenario					
	2018	2019	2020	2021	2022
<b>GDP</b>	<b>0.8</b>	<b>0.1</b>	<b>0.6</b>	<b>1.0</b>	<b>1.0</b>
<b>Imports</b>	3.0	0.7	2.3	3.3	3.4
<b>Final national consumption</b>	0.7	0.3	0.5	0.7	0.5
<b>Household consumption and NPISH</b>	0.8	0.4	0.7	0.8	0.6
<b>Government expenditure</b>	0.4	-0.2	-0.2	0.3	0.1
<b>Investment</b>	3.2	2.1	2.2	2.3	2.2
- machinery, equipment and intangibles	2.6	1.5	2.0	2.0	2.3
- transport equipment	8.8	0.3	2.2	1.6	1.5
- construction	2.9	3.1	2.3	2.6	2.2
<b>Exports</b>	1.8	2.8	2.2	2.9	3.1

Source: ISTAT and Government projections for 2019-2022 (Update of the Economic and Financial Document 2019)



# Updated budgetary plan of the new government

## Draft Budgetary Plan 2020

<b>Policy scenario</b>						
<i>% of GDP</i>	<b>2017</b>	<b>2018</b>	<b>2019</b>	<b>2020</b>	<b>2021</b>	<b>2022</b>
<b>General government balance</b>	<b>-2.4</b>	<b>-2.2</b>	<b>-2.2</b>	<b>-2.2</b>	<b>-1.8</b>	<b>-1.4</b>
<i>Structural balance (1)</i>	<i>-1.4</i>	<i>-1.5</i>	<i>-1.2</i>	<i>-1.4</i>	<i>-1.2</i>	<i>-1.0</i>
<i>Change in the structural balance</i>	<i>-0.6</i>	<i>-0.1</i>	<i>0.3</i>	<i>-0.1</i>	<i>0.2</i>	<i>0.2</i>
<i>Flexibility granted</i>	<i>0.39</i>	<i>0.00</i>	<i>0.18</i>	<i>0.20</i>	<i>0.00</i>	<i>0.00</i>
<b>Output gap</b>	<b>-1.8</b>	<b>-1.4</b>	<b>-1.8</b>	<b>-1.7</b>	<b>-1.3</b>	<b>-1.0</b>
<b>Interest expenditure</b>	<b>3.8</b>	<b>3.7</b>	<b>3.4</b>	<b>3.3</b>	<b>3.1</b>	<b>2.9</b>
<b>Public debt (2)</b>	<b>134.1</b>	<b>134.8</b>	<b>135.7</b>	<b>135.2</b>	<b>133.4</b>	<b>131.4</b>

(1) Net of one-off measures and cyclically adjusted. Discrepancies, if any, are due to rounding.

(2) Gross of financial support to Eurozone countries.

Source: ISTAT and Government projections for 2019-2022 (Update of the Economic and Financial Document 2019)

# Highlights of the 2020 Budget

## New commitments

- Repeal of 2020 VAT hike
- Cut in the tax wedge on labour
- Competitiveness and investment incentives (incl. reinstatement of ACE)
- Public investment and Green New Deal

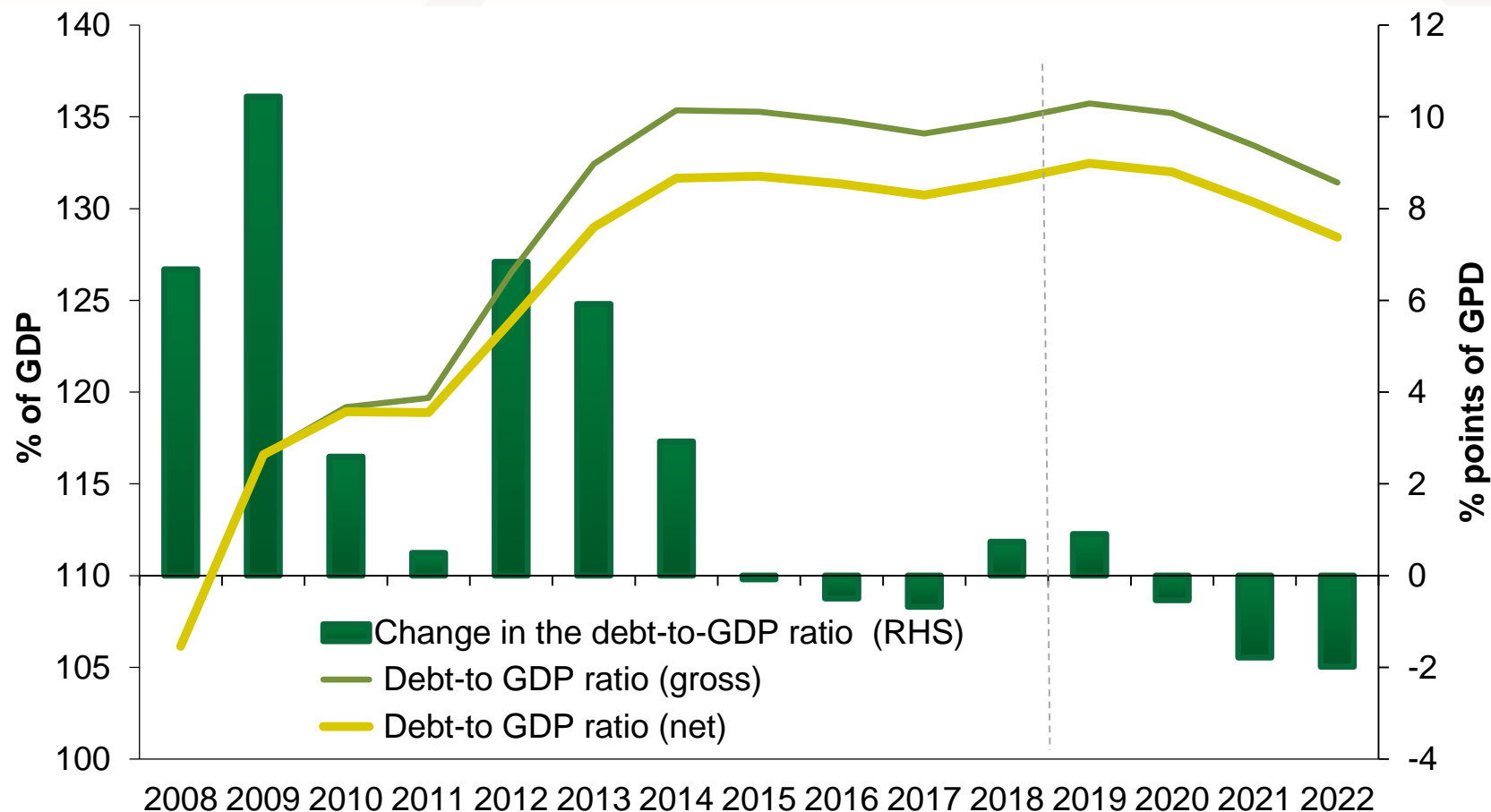
## Financing measures

- Expenditure cuts (incl. Spending Review for central government)
- Environmental and health-protection taxes
- Cuts in harmful subsidies
- Anti tax evasion and fraud measures
- Gaming and betting taxes

# Commission Opinion on Italy's 2020 DBP

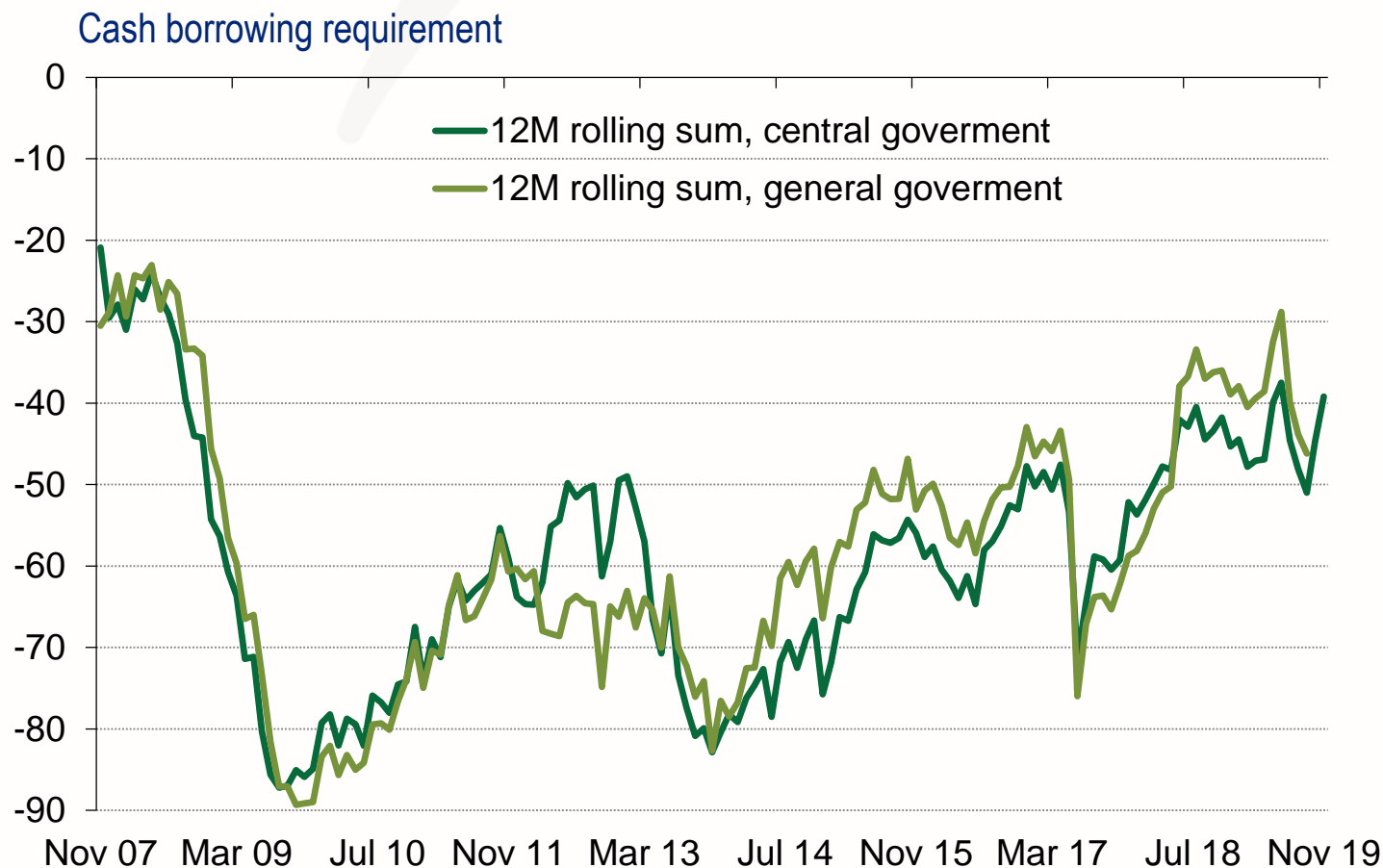
- DBP is at risk of non-compliance with the provisions of the SGP.
- Risk of significant deviation from the required adjustment towards the MTO and risk of non compliance with the debt reduction benchmark in 2019 and 2020.
- The Commission invites: *“the authorities to take the necessary measures within the national budgetary process to ensure that the 2020 budget will be compliant with the SGP and to use any windfall gains to accelerate the reduction of the debt-to-GDP ratio.”*
- Progress made with regard to the structural part of the fiscal recommendations in the context of the European Semester: shift taxation away from labour and combat tax evasion.
- Further progress recommended within the next European Semester.

# Looking forward to the next Stability Program: Debt-to-GDP ratio



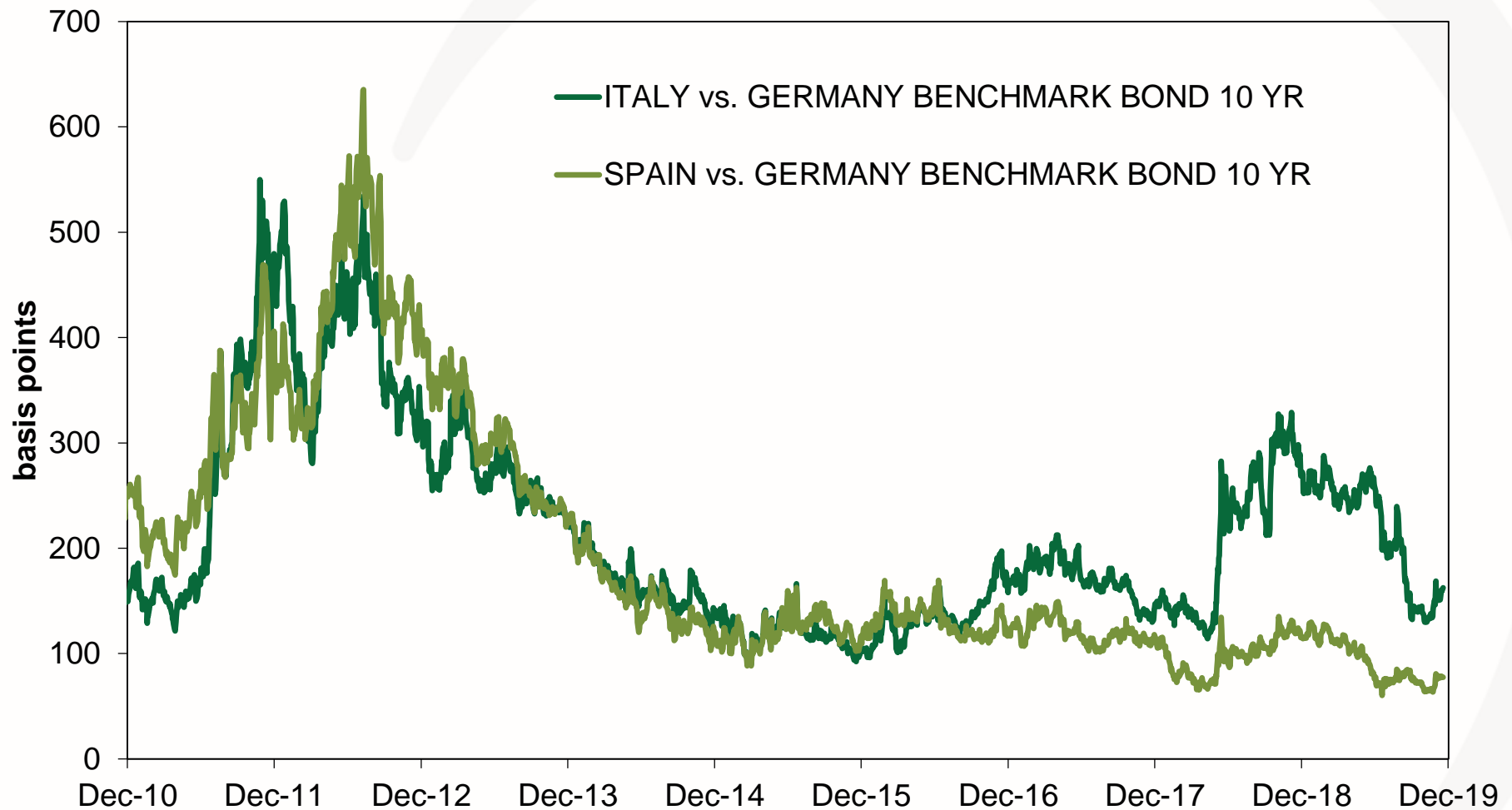
Source: ISTAT, Bank of Italy and government projections for 2019-2022 (Update to EFD 2019).

# Budget execution



Source: MEF

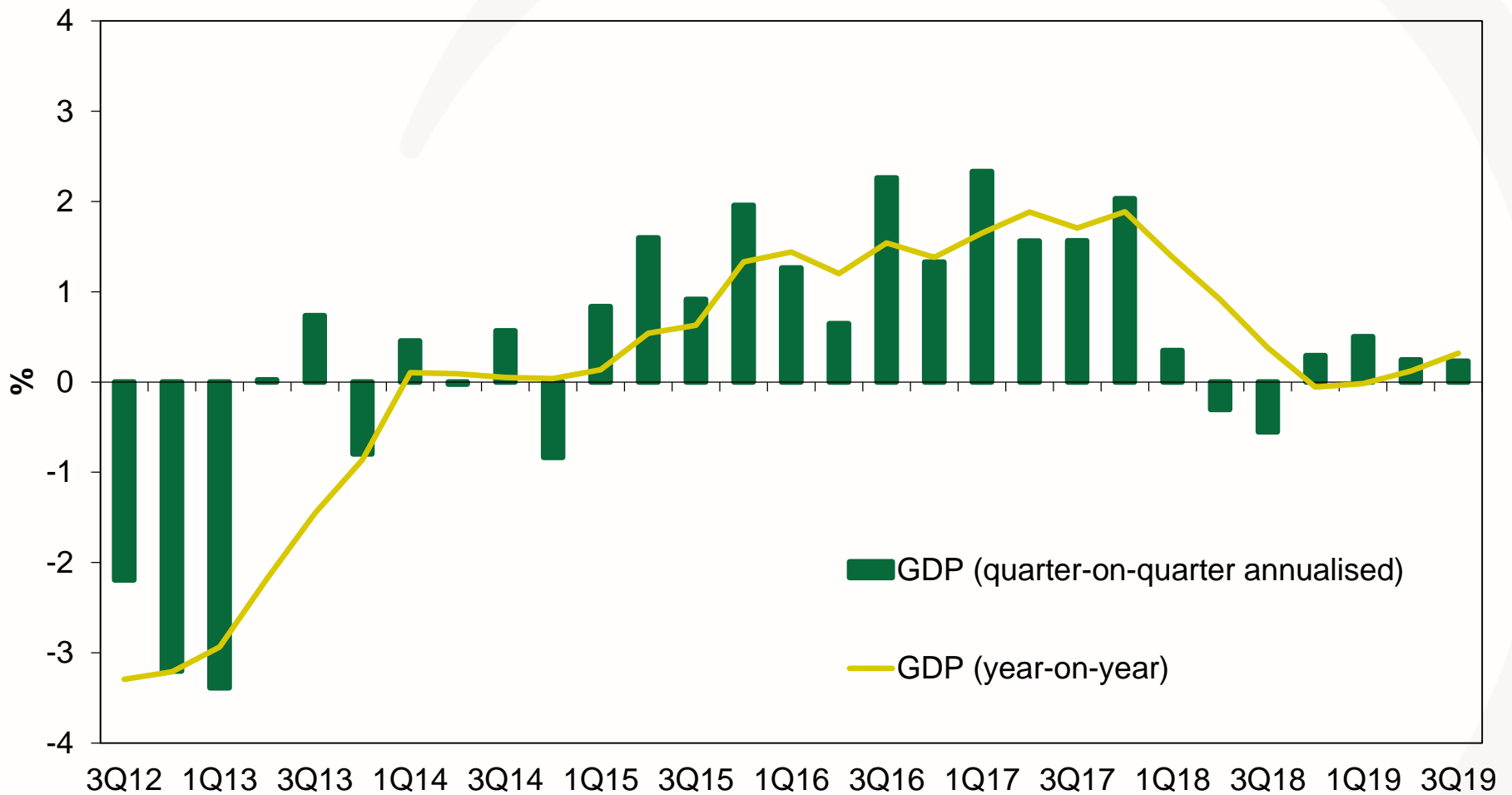
# Sovereign bond spread



Source: Thomson Reuters Dastastream



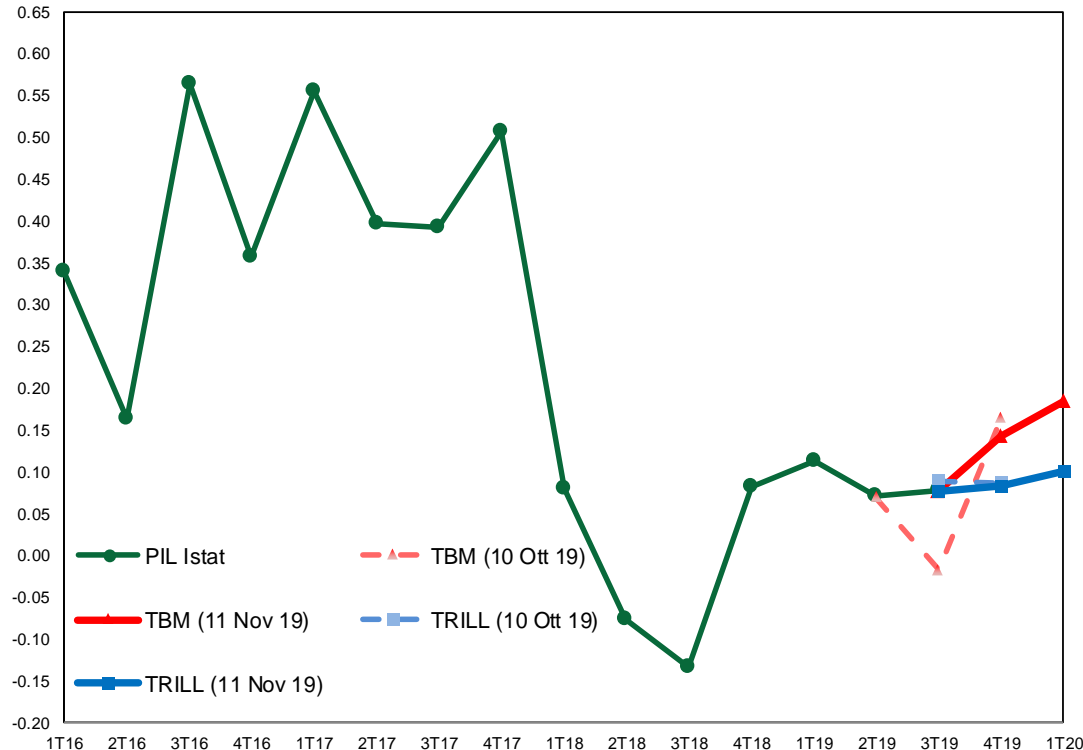
# Real GDP growth



Source: ISTAT

# Projections for Q4 point to slightly positive growth

Real GDP growth forecasts, percent q-o-q



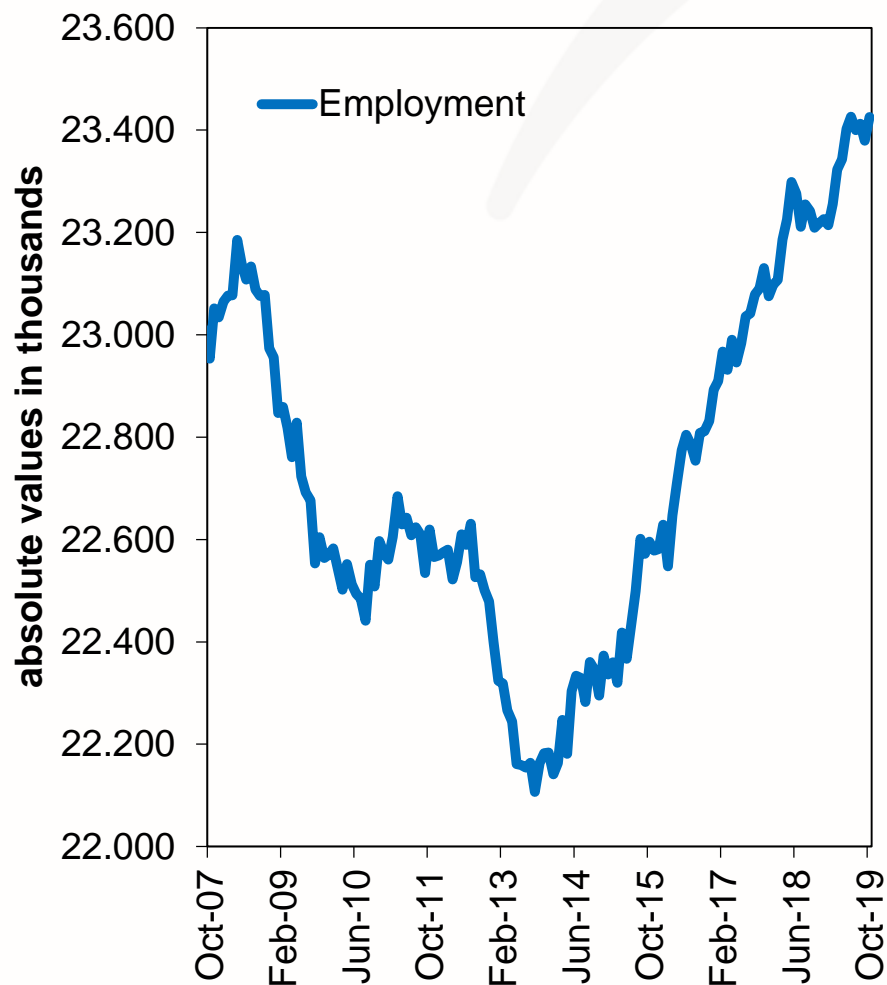
- Real GDP grew by close to 0.1% q/q in the first three quarters of 2019.
- Treasury nowcasting models indicate a 0.1% q/q increase also in Q4.
- If so, 2019 would record Q4/Q4 growth of 0.3-0.4% and an annual growth rate of 0.2%.

Note: TBM: Treasury Bridge Model; TRILL: Treasury Italian Leading Indicator.

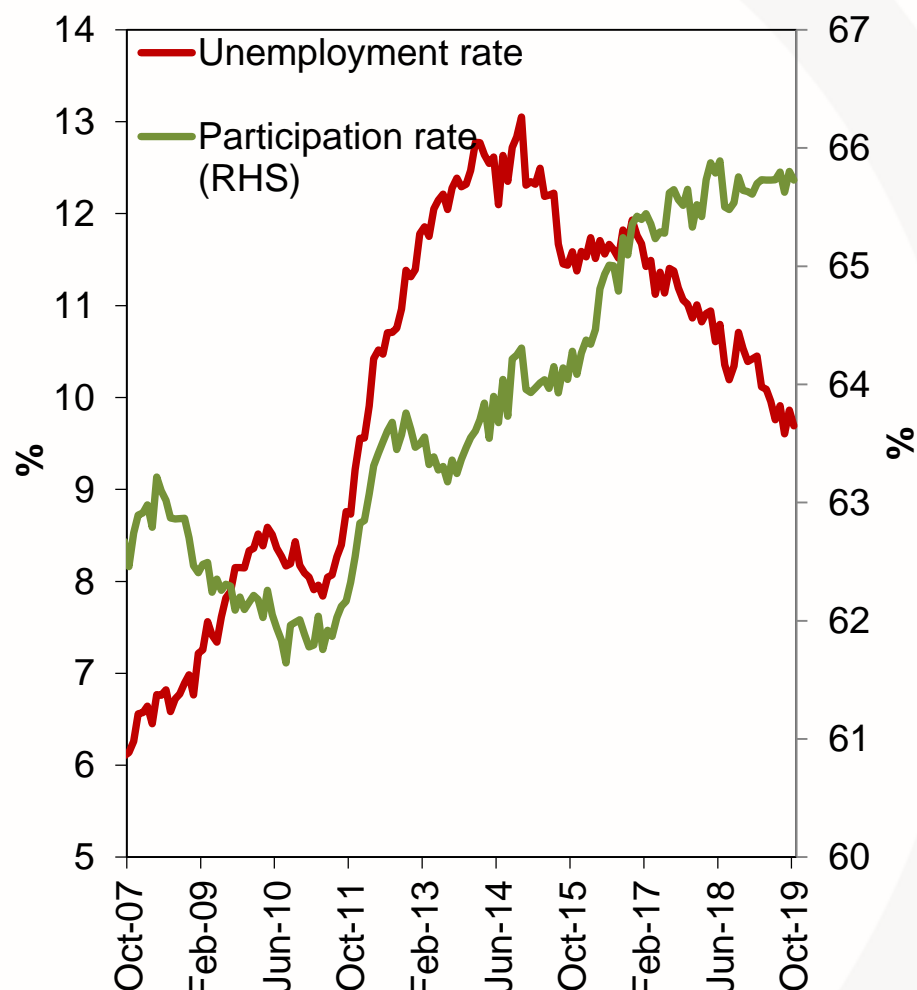
Source: Istat and MEF projections



# Employment still growing moderately

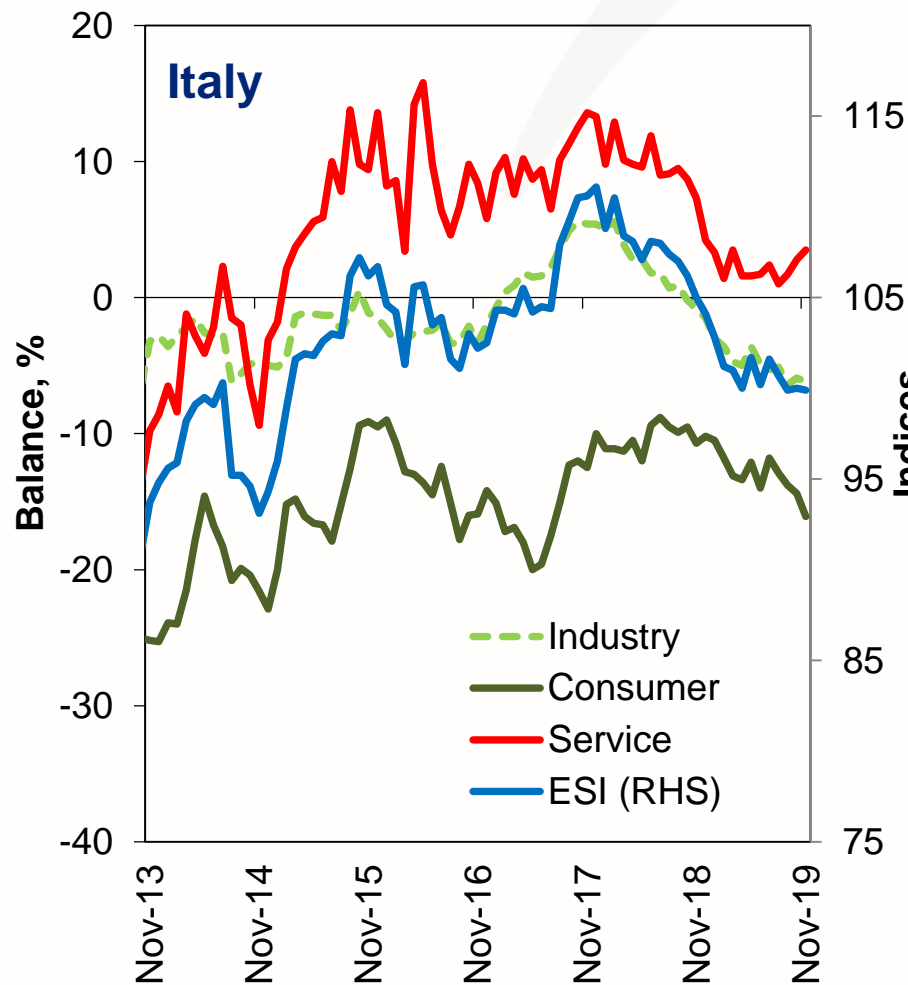


Source: ISTAT

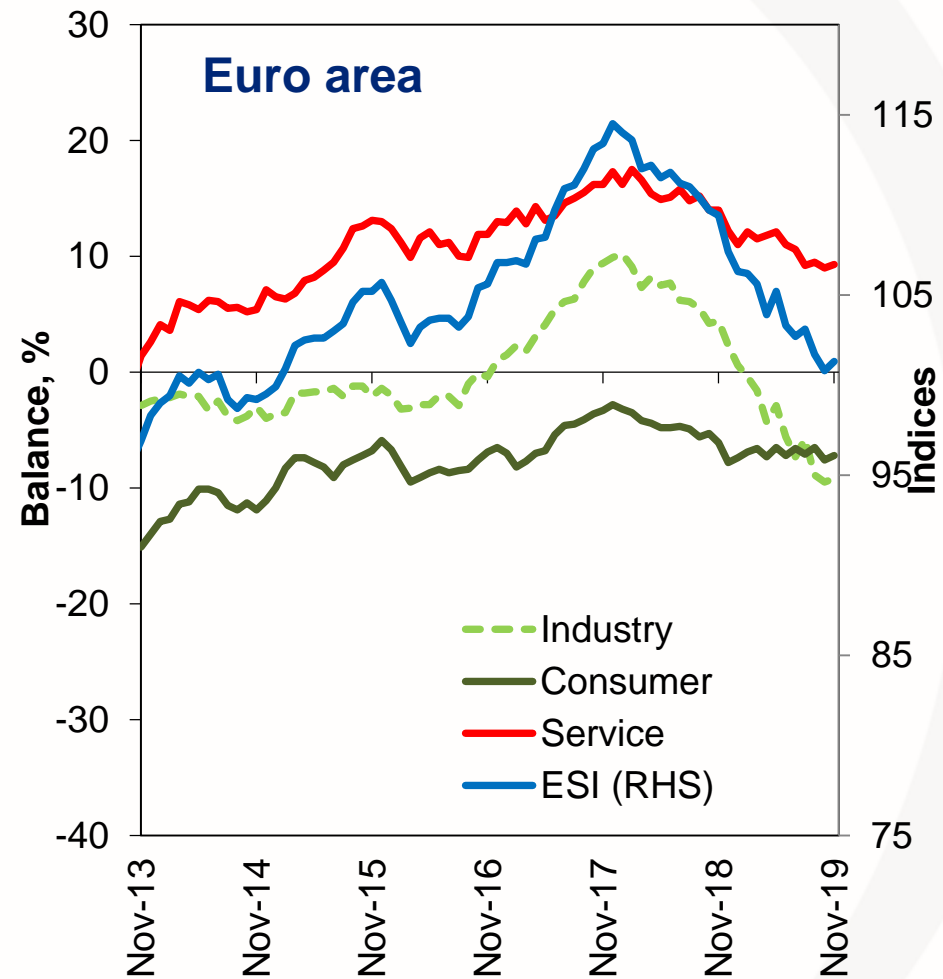


Source: ISTAT

# Sentiment stabilizing as confidence recovers in services

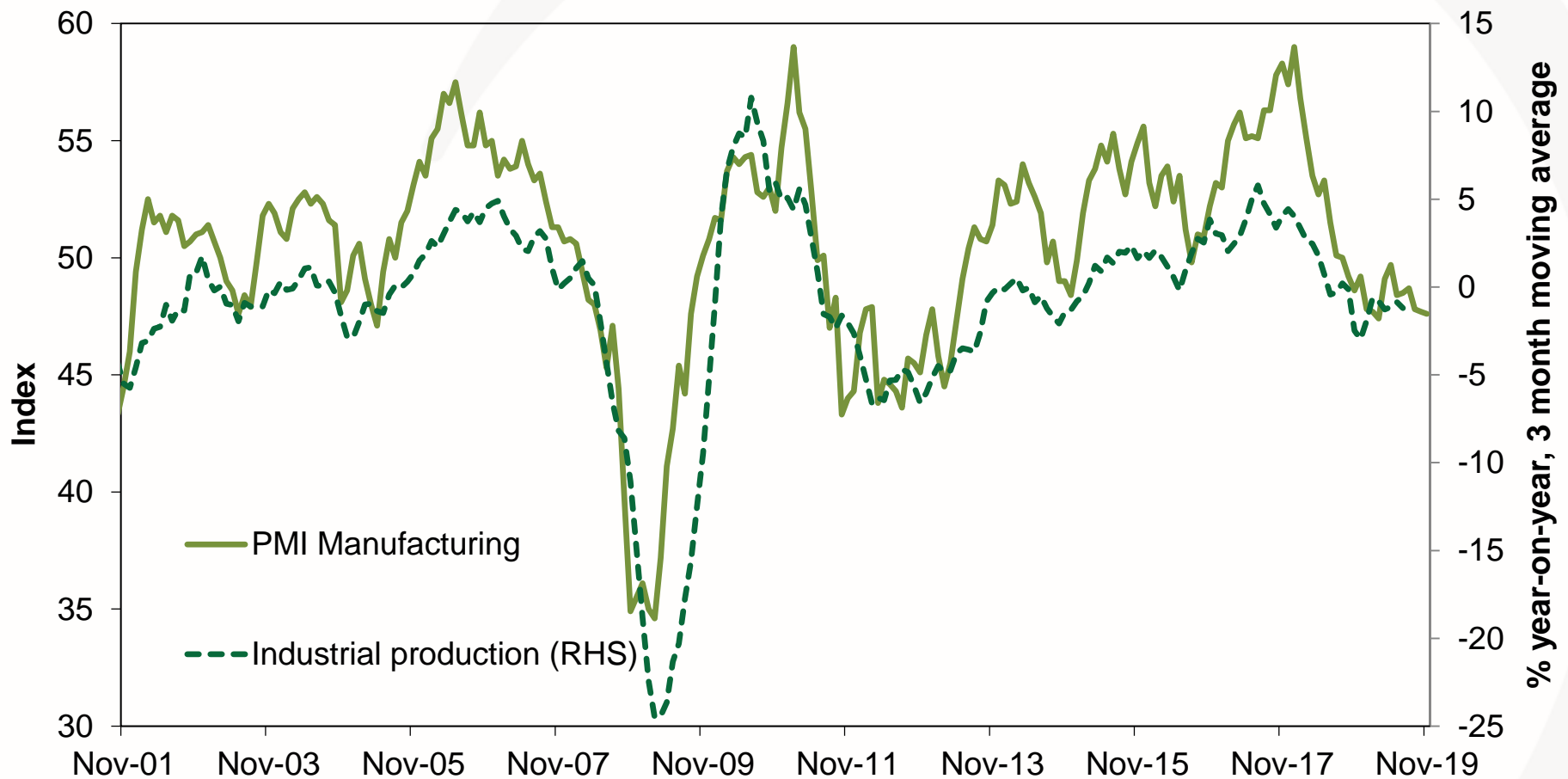


Source: European Commission



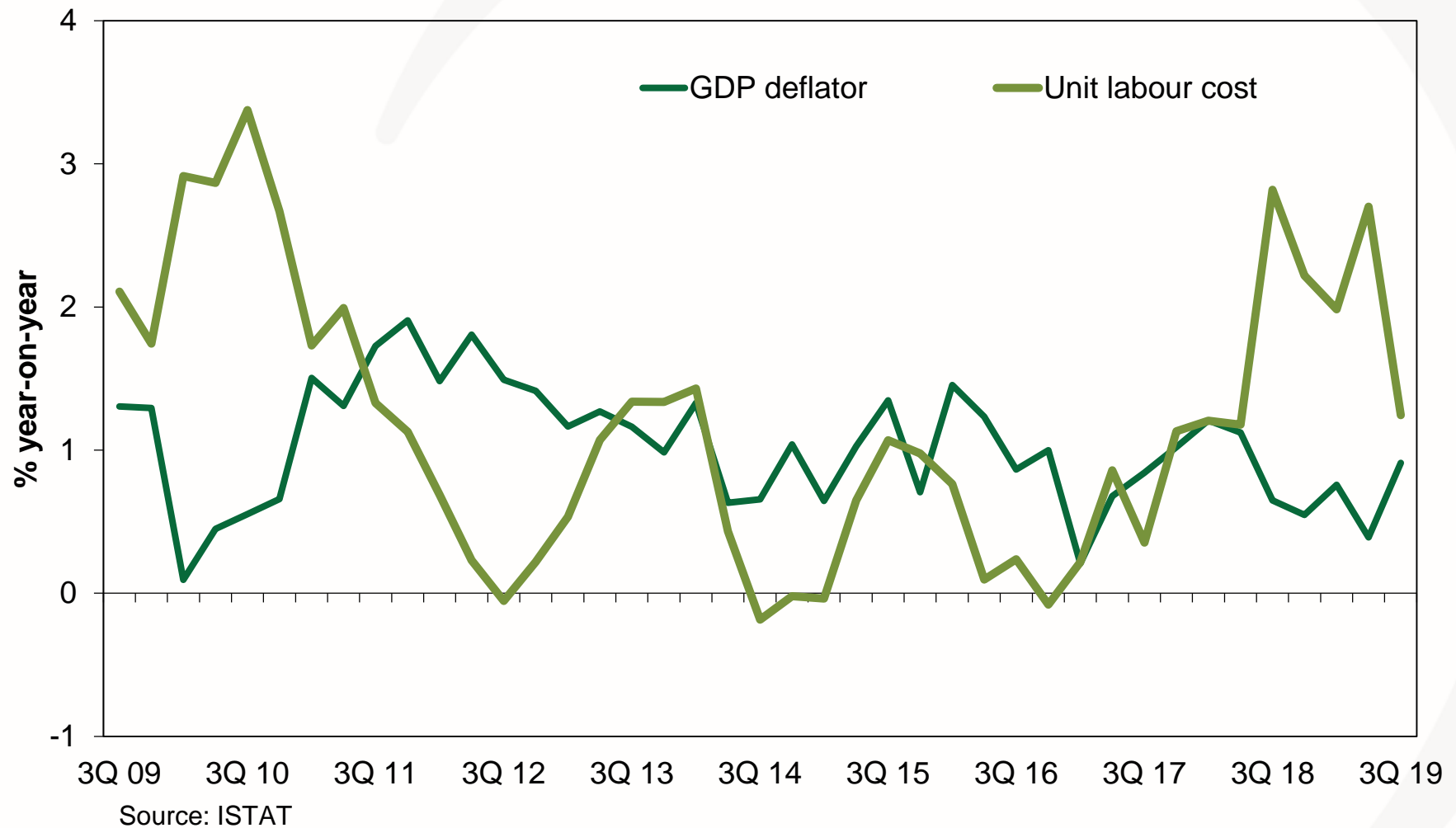
Source: European Commission

# PMI still points to slight contraction in manufacturing



Source: IHS Markit, ISTAT

# GDP deflator and wages remain subdued



# Summing up

- 2019 real GDP growth in line with Stability Program forecast, nominal growth may fall short.
- 2020 growth and fiscal targets within reach if financial conditions moderately supportive.
- Tentative signs of improvement in global cycle, but risks are skewed on the downside.
- Solid performance of public finances in 2019; lower takeup of new policies, revenue growth.
- But given the remaining safeguard clauses, 2021 budget will be challenging...
- ...as will be the achieving a balanced policy mix of revenue increases and expenditure cuts.

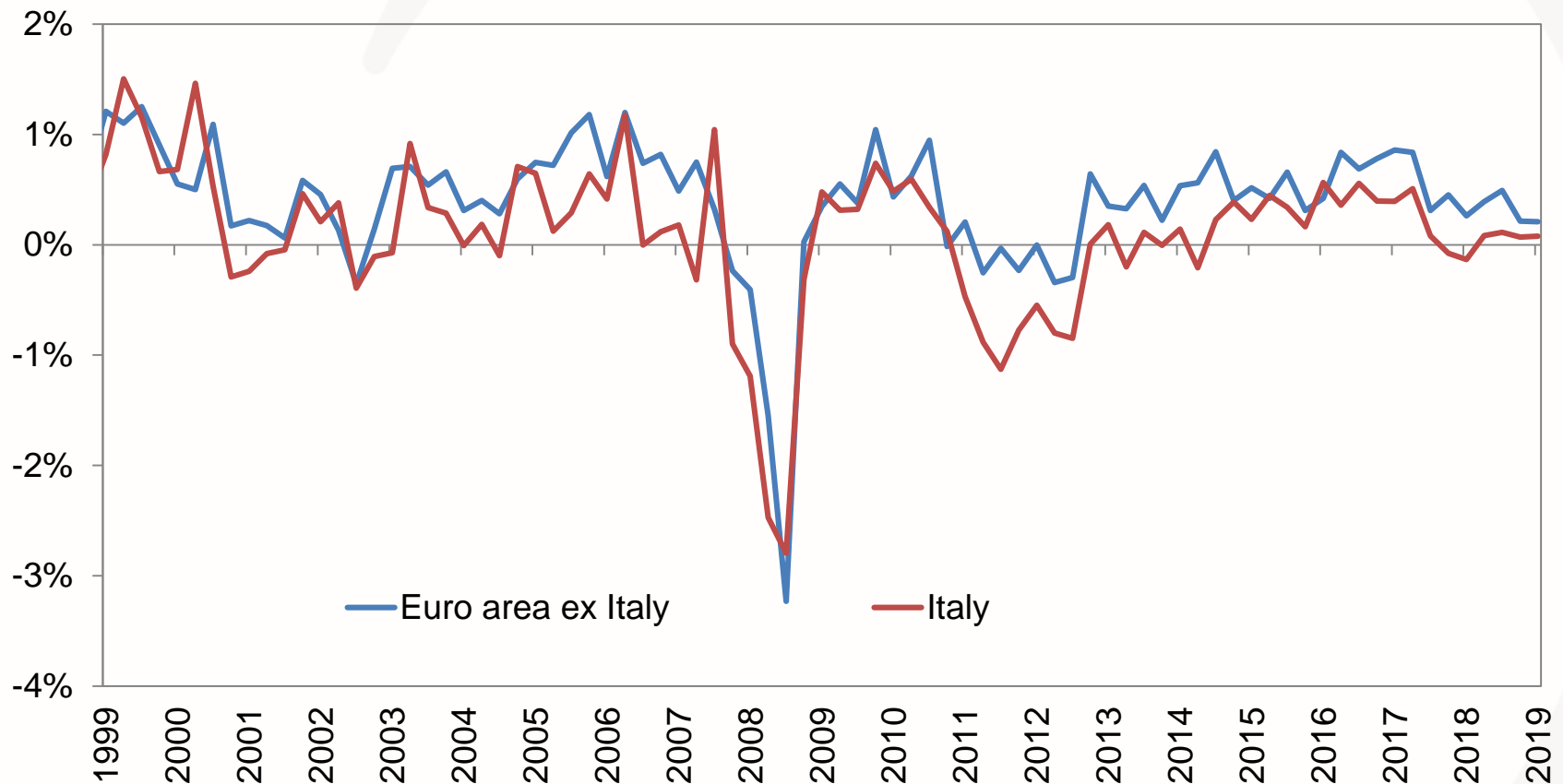


# Background slides



# Growth gap vs. Euro area is narrowing

Real GDP growth, percent, q-o-q



Source: MEF calculations on Istat and Eurostat data



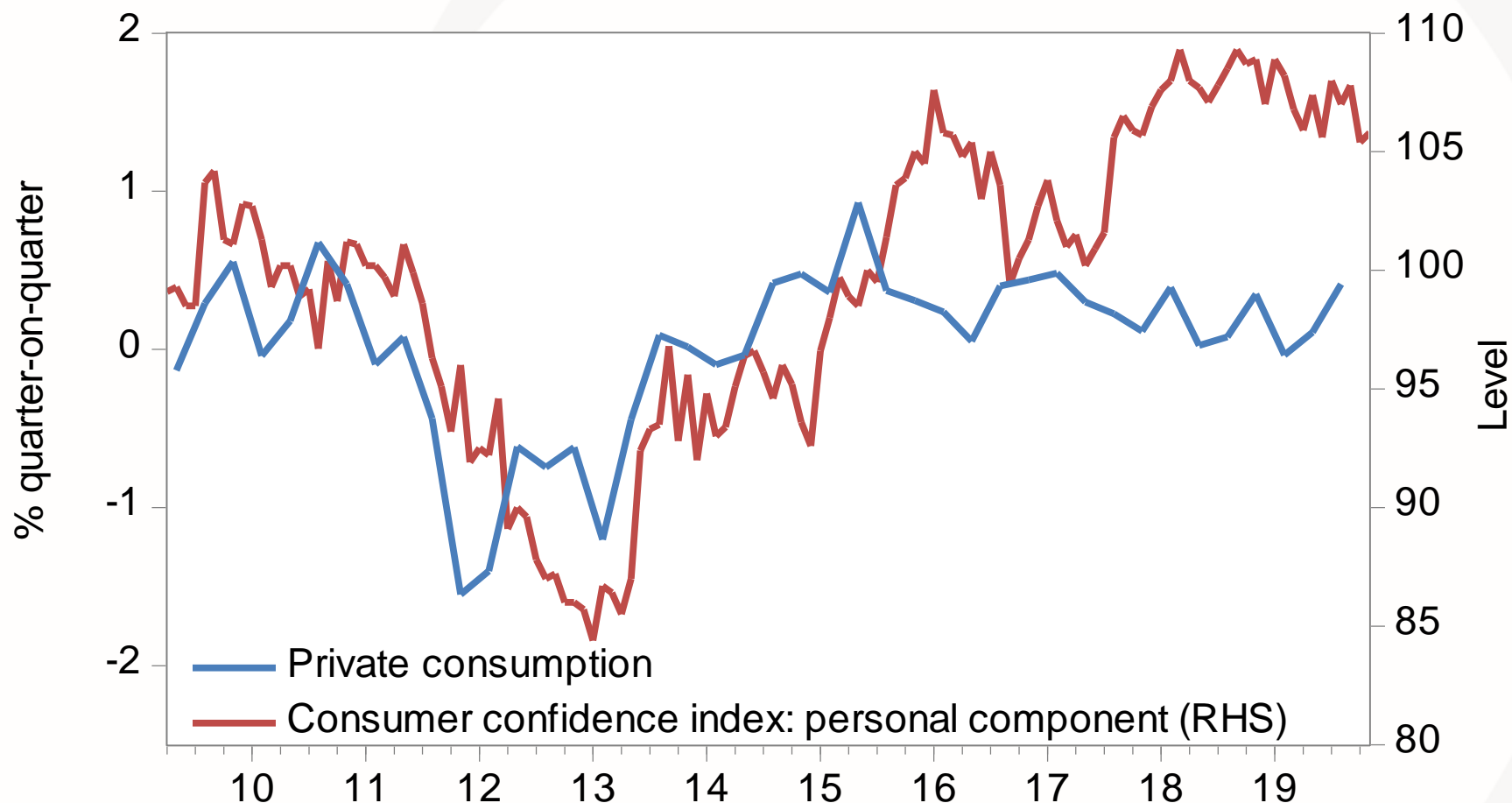
# Industrial production outperforming Germany

Relative industrial production index, Italy vs. Germany (2015=100, 3mma)



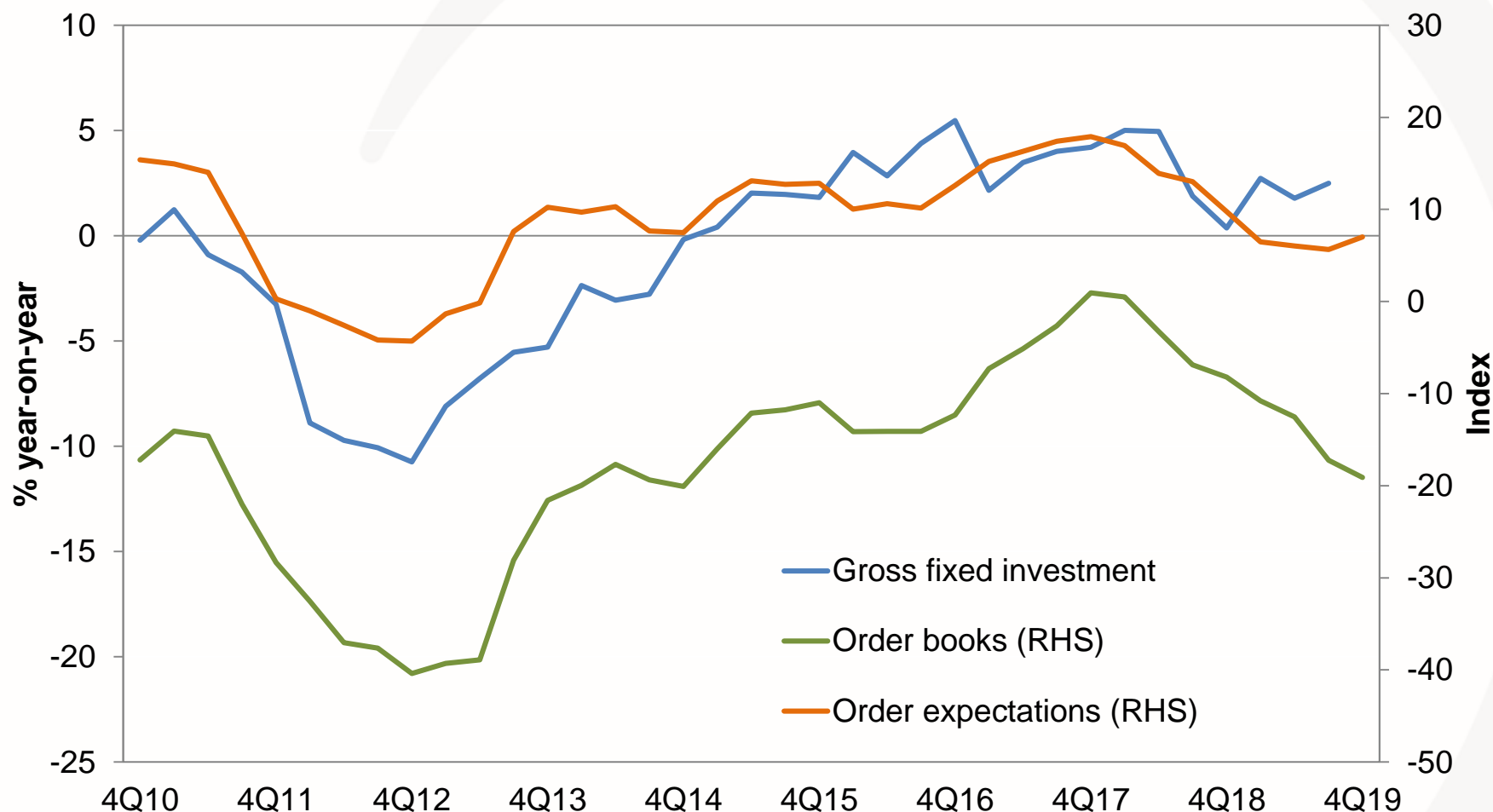
Source: MEF computations on Destatis and Istat data

## Households less optimistic about personal conditions



Source: ISTAT

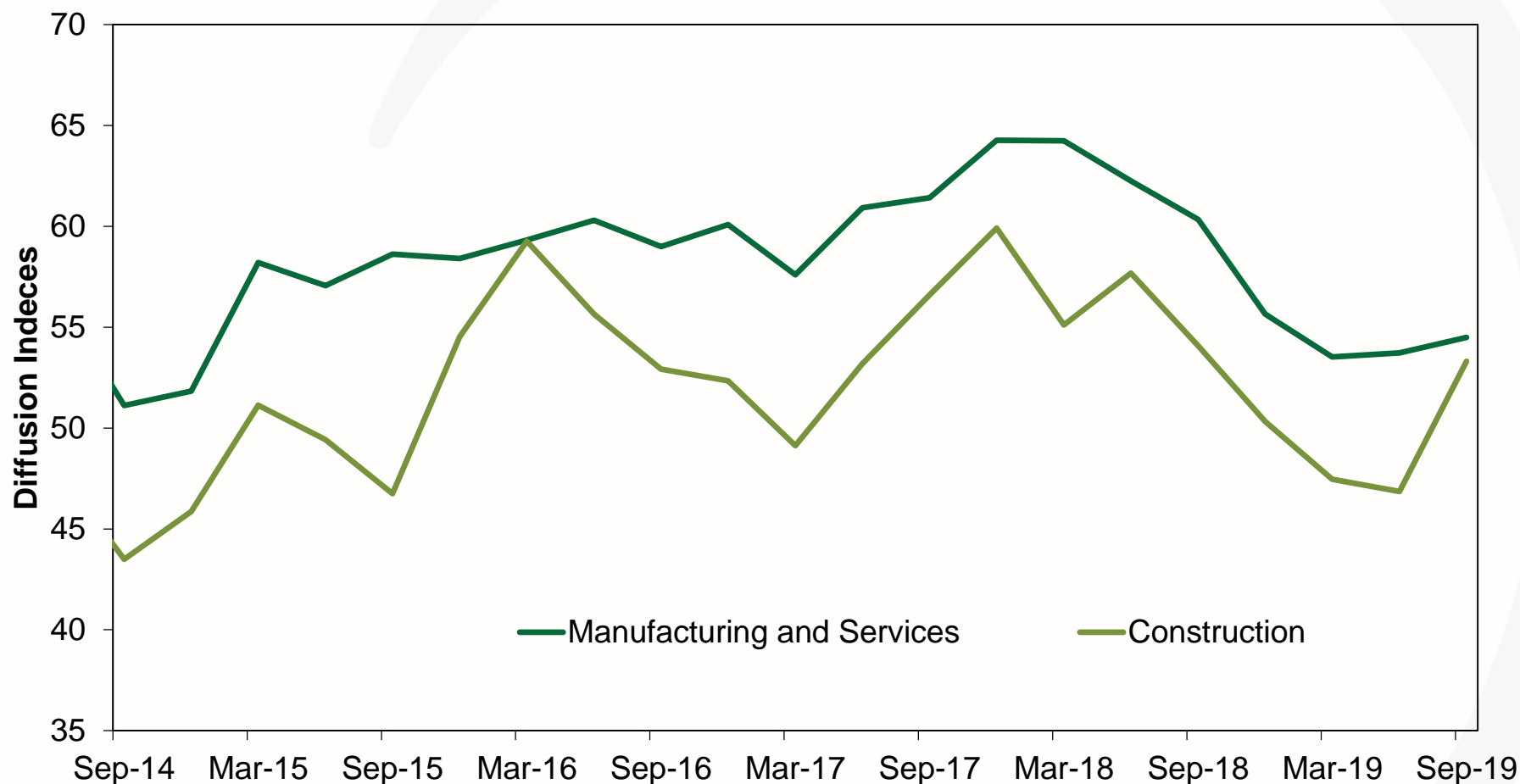
## Capital goods producers a little more optimistic...



Note: Order books and order expectations data refer to November 2019.

Source: ISTAT

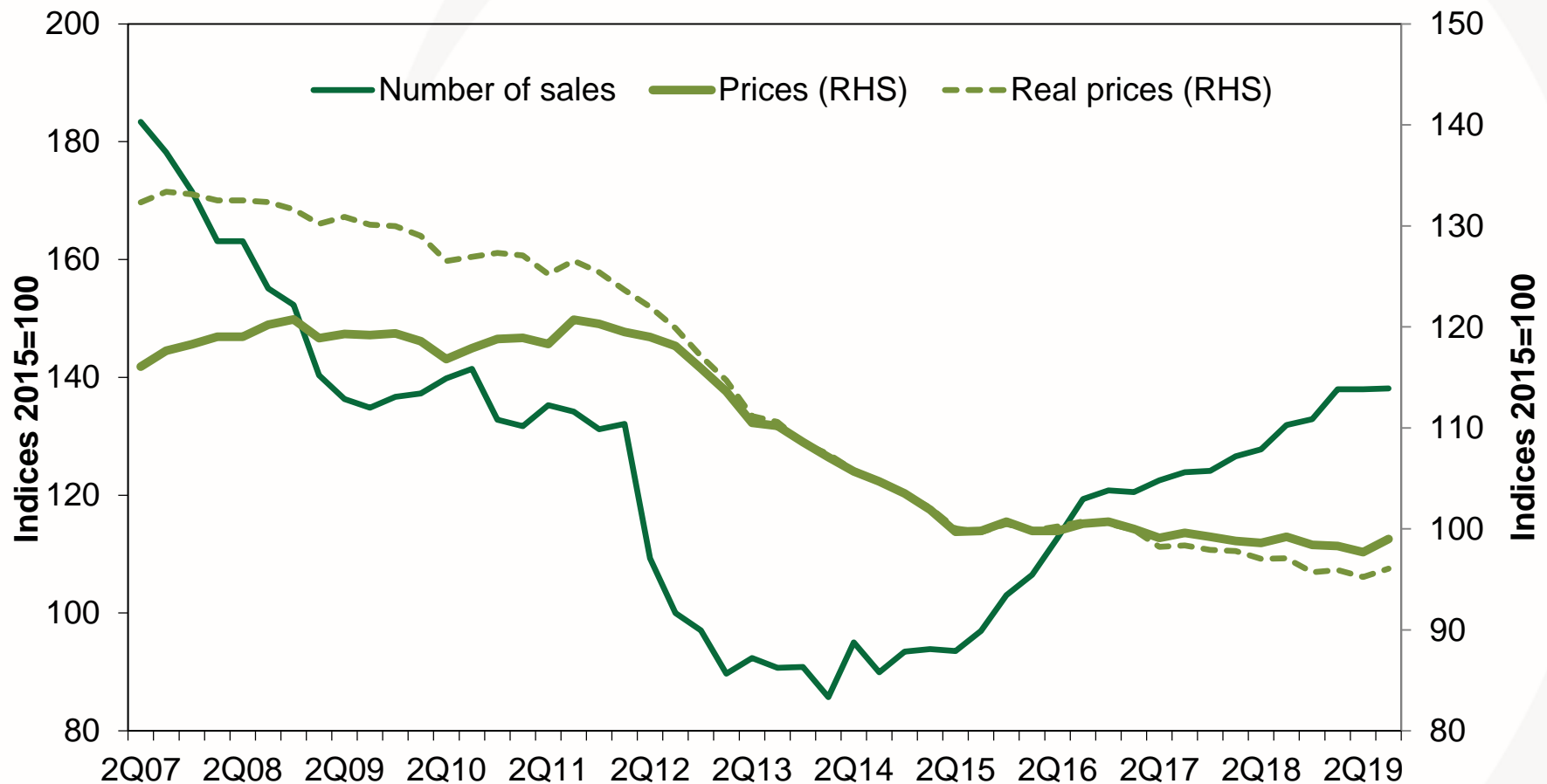
## ...as firms' investment intentions improve slightly



Source: Bank of Italy, Survey of Inflation and Growth Expectations (3Q - 2019), October 2019

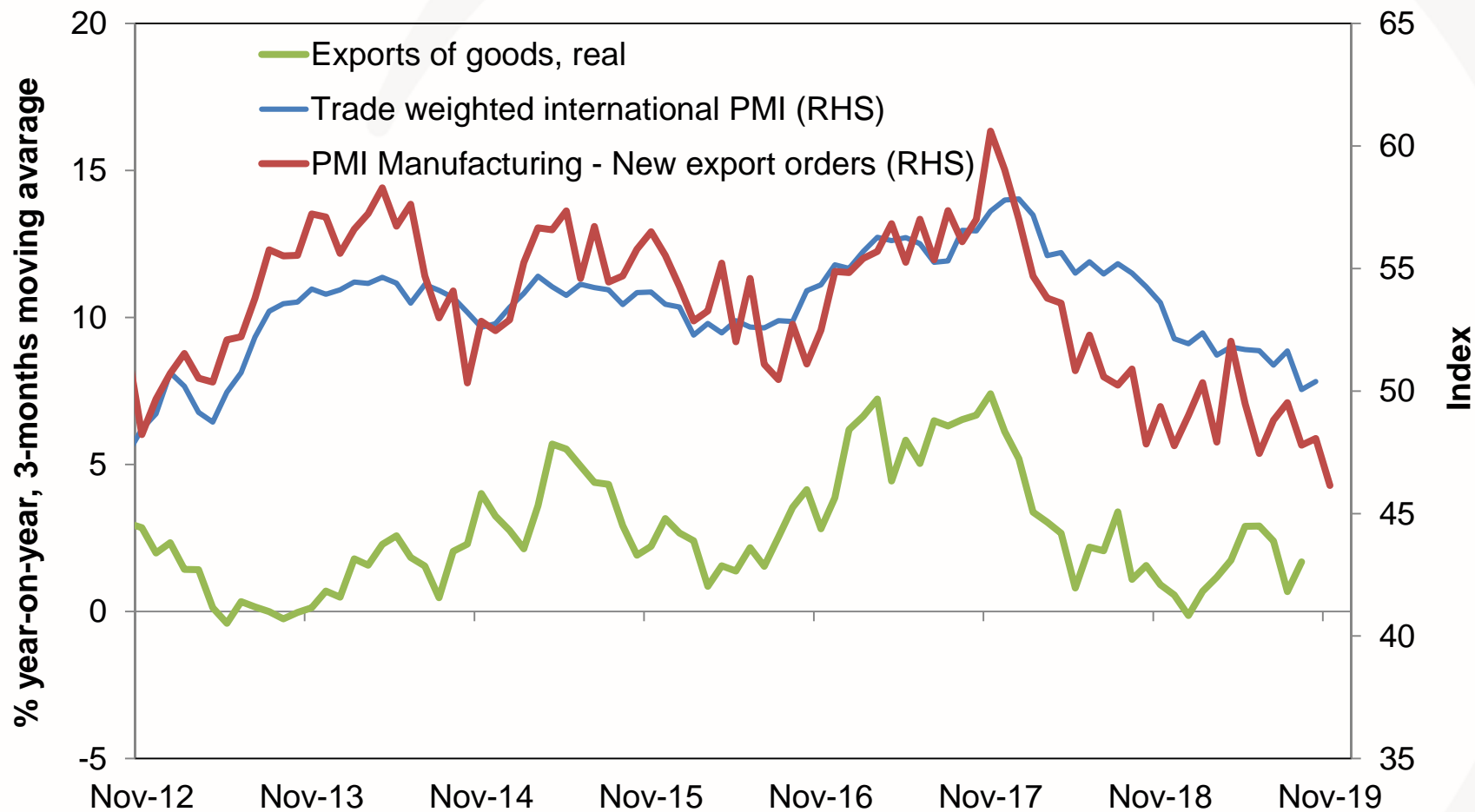
# Property market volumes recover as prices stay low

## Residential property



Source: Bank of Italy

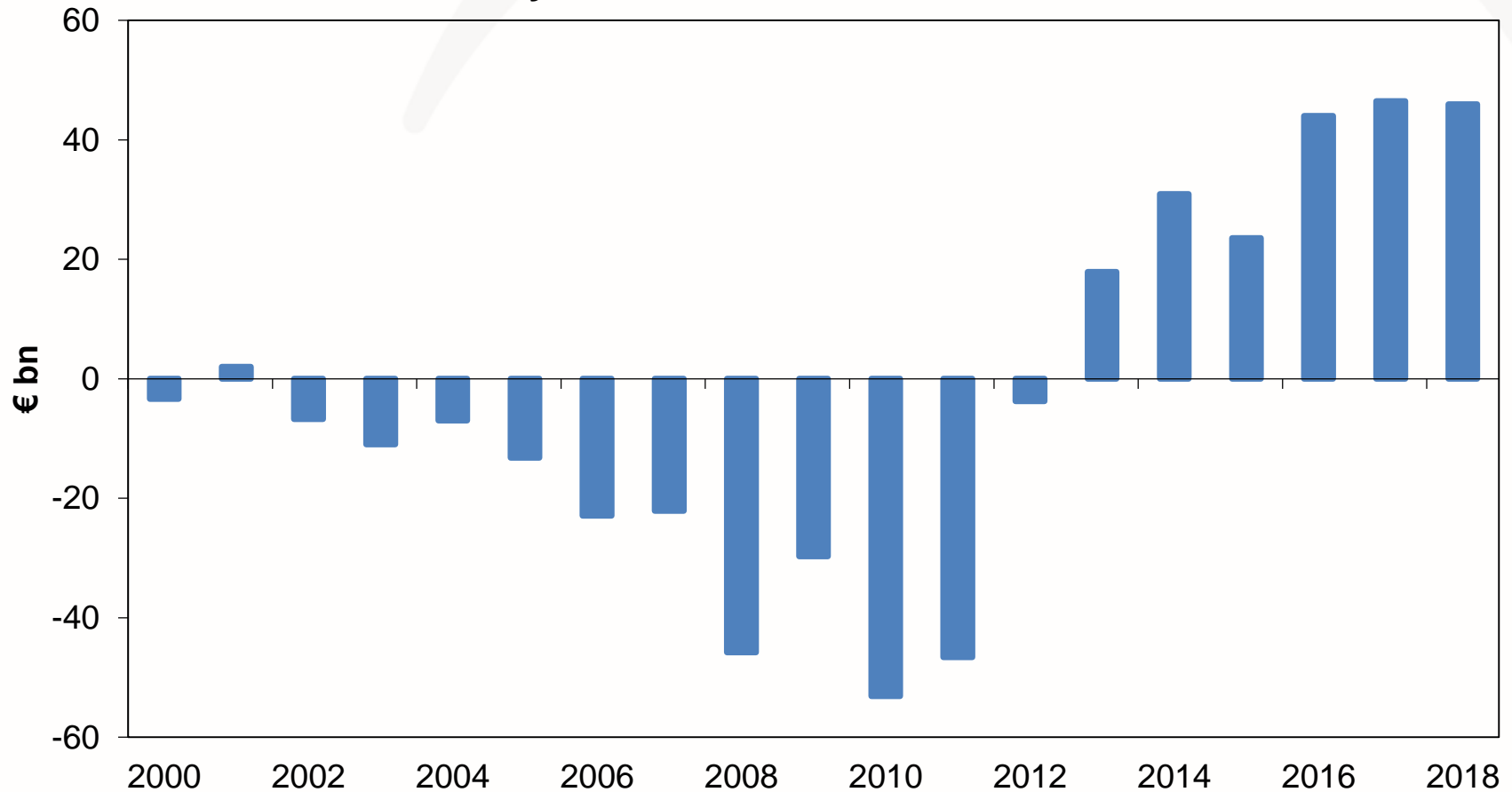
# Exports growing moderately despite global trade slump



Source: MEF calculation based on ISTAT and MARKIT data

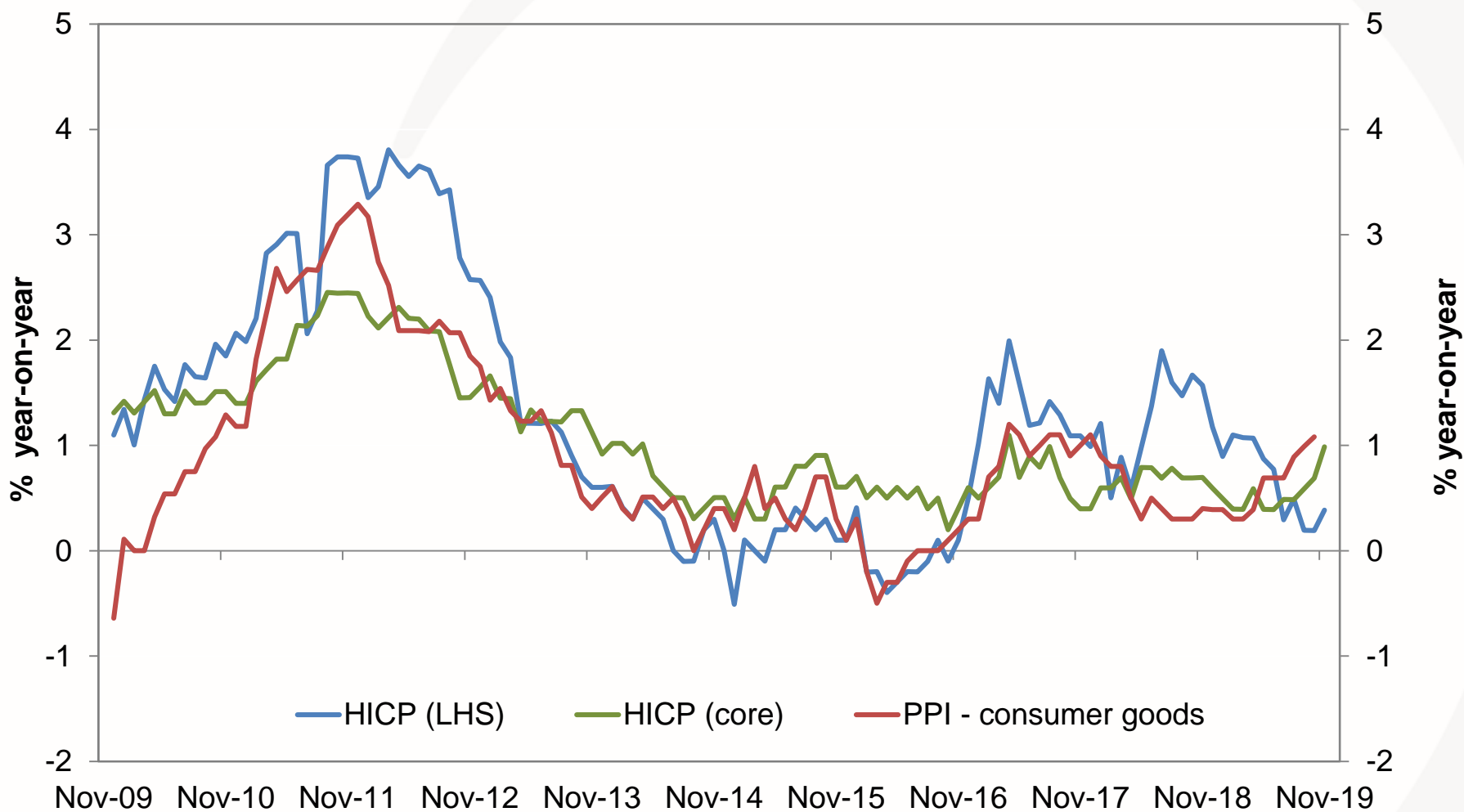
# Current account surplus set to remain large

Italy's current account balance



Source: Bank of Italy.

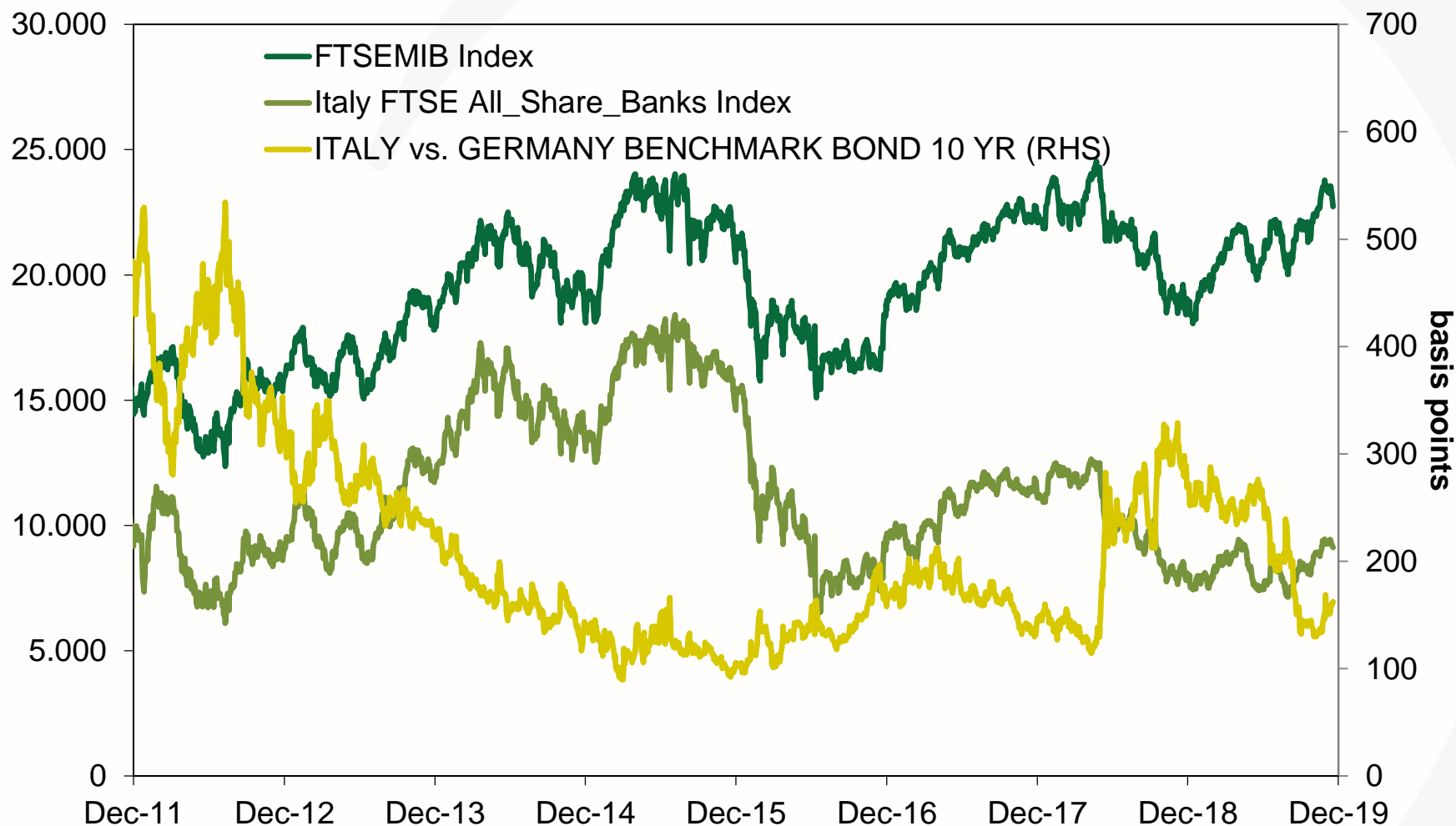
# Headline inflation drops, following energy prices



Source: ISTAT

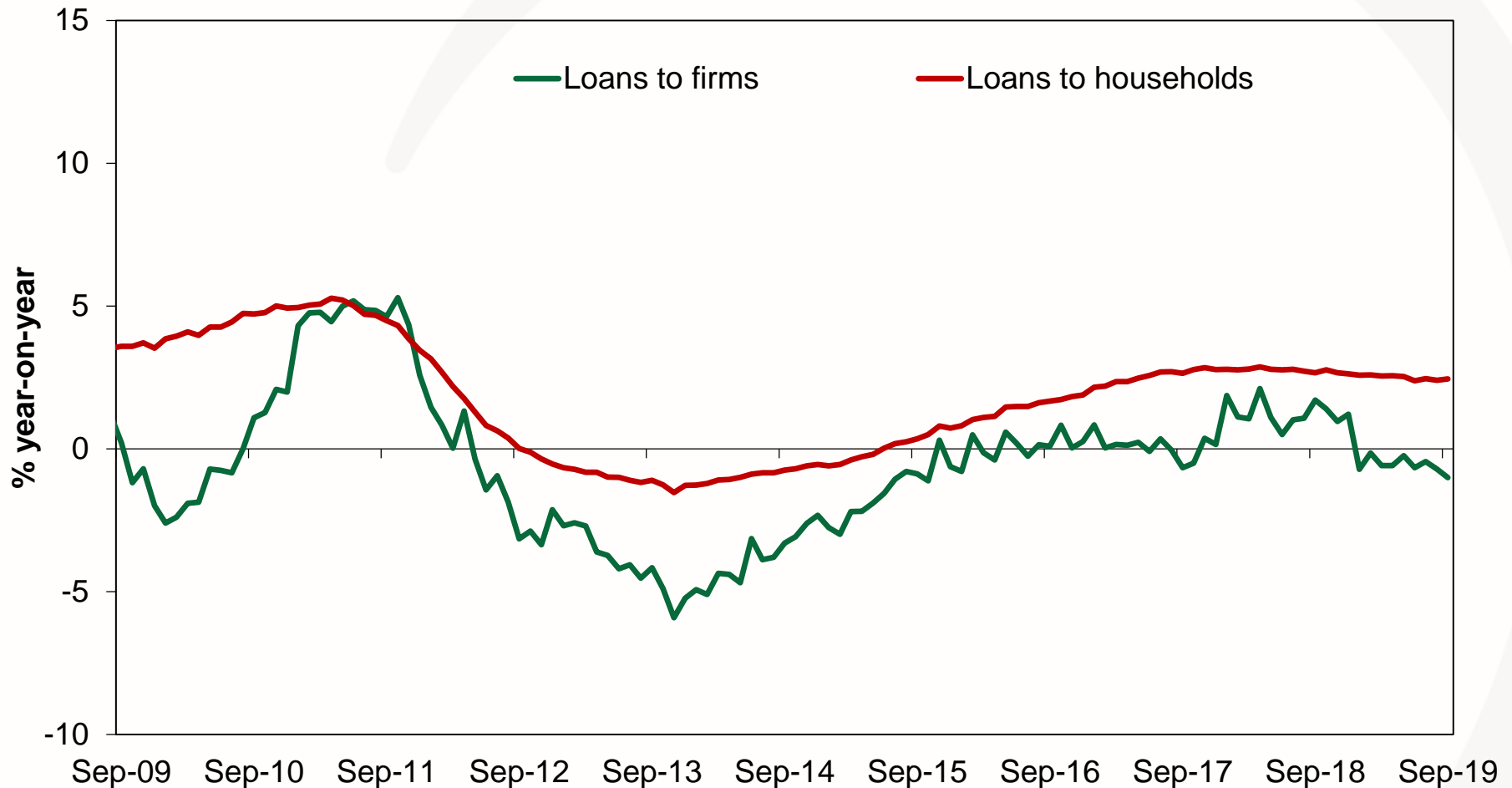


# Stock market has recovered its 2018 H2 losses



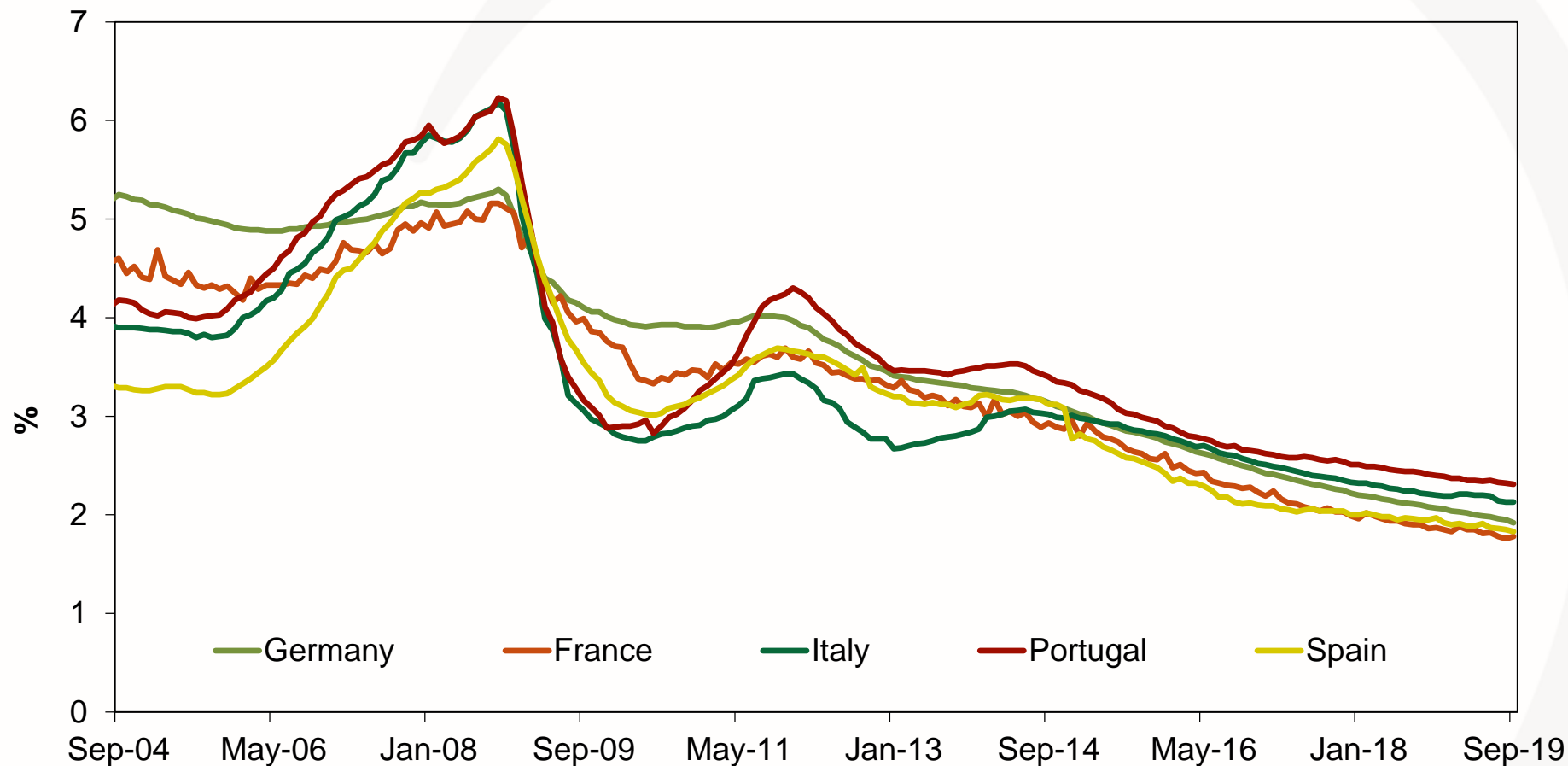
Source: Thomson Reuters Dastastream

## Bank lending to households growing moderately



Source: Bank of Italy

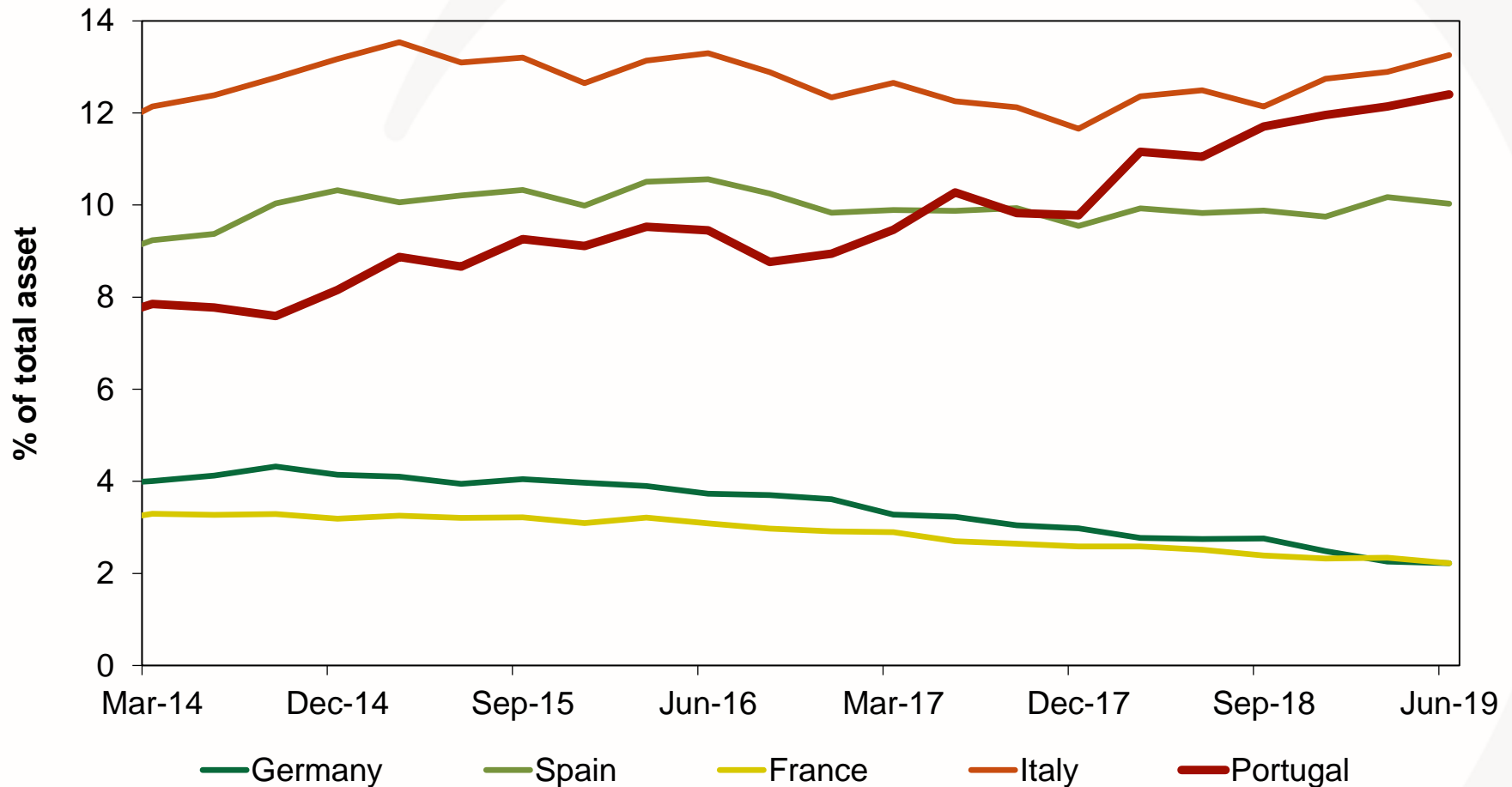
## Bank lending rates remain low



Note: annual interest rates on loans (outstanding amounts).

Source: ECB, Thomson Reuters Dastastream

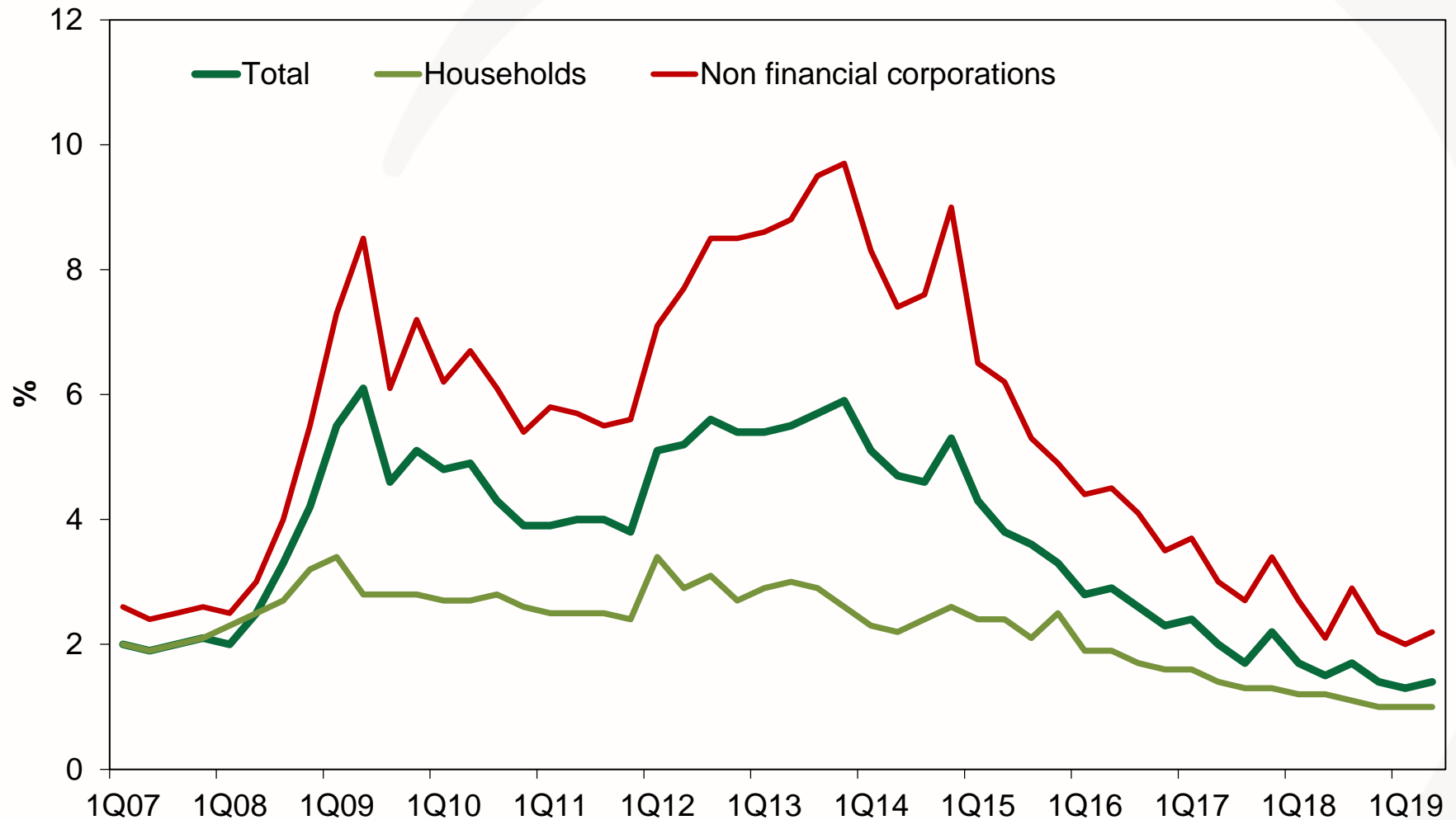
# Banks' holdings of government bonds remain high



Note: series refer to both long and short term securities.

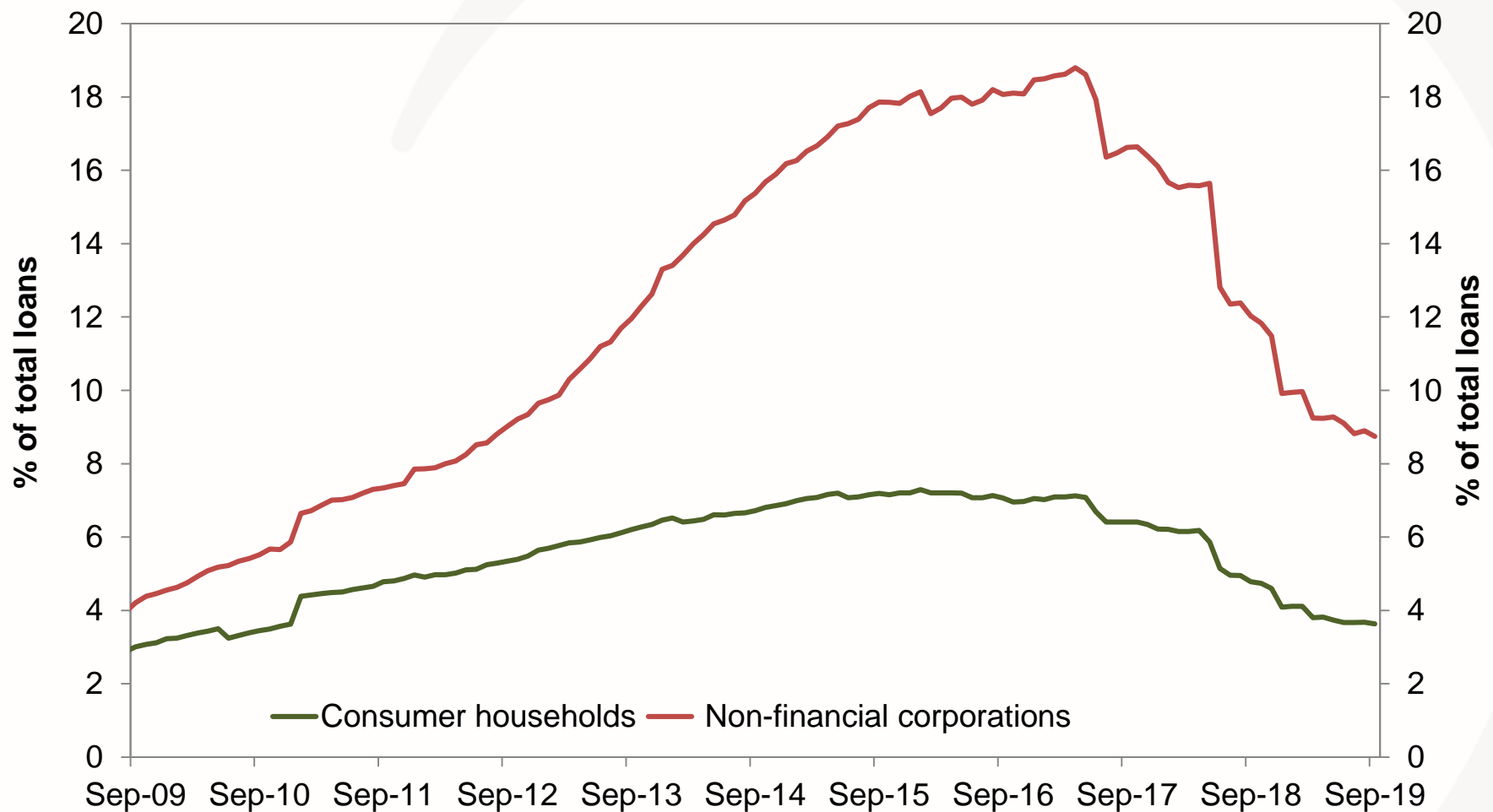
Source: ECB

# New non-performing loan rate close to pre-crisis levels



Source: Bank of Italy

## NPLs as a share of bank loans keep falling



Source: Bank of Italy

# Italian systemically relevant institutions are well capitalised

Q2 2019							
<i>EUR billions, percentages</i>							
Country	Total risk exposure amount	Total capital		Tier 1		CET1	
		<i>Amount</i>	<i>Ratio</i>	<i>Amount</i>	<i>Ratio</i>	<i>Amount</i>	<i>Ratio</i>
France	2,505.22	459.14	18.33%	393.58	15.71%	364.62	14.55%
Germany	1,176.19	211.13	17.95%	181.58	15.44%	168.59	14.33%
<b>Italy</b>	<b>1,075.29</b>	<b>178.38</b>	<b>16.59%</b>	<b>154.42</b>	<b>14.36%</b>	<b>143.09</b>	<b>13.31%</b>
Greece	173.62	28.59	16.47%	27.13	15.63%	27.13	15.62%
Spain	1,455.22	222.56	15.29%	193.87	13.32%	173.06	11.89%
Portugal	123.48	18.79	15.22%	17.03	13.79%	15.90	12.88%

Note: Significant institutions at the highest level of consolidation for which common reporting (COREP) and financial reporting (FINREP) are available. Countries are ordered by Total capital ratio.

Source: ECB.

