

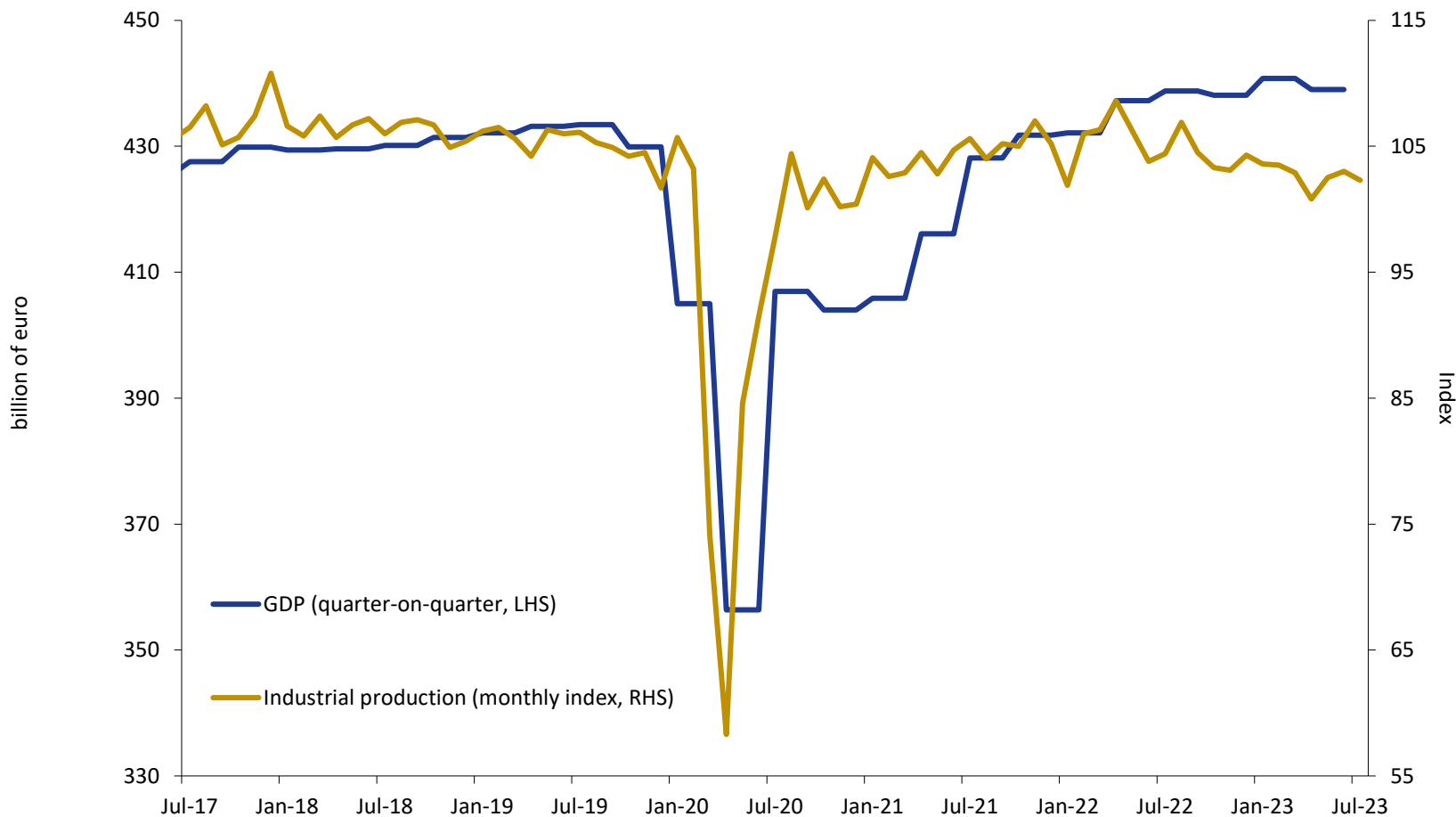
# ITALY

5 October 2023

## National Economic Outlook

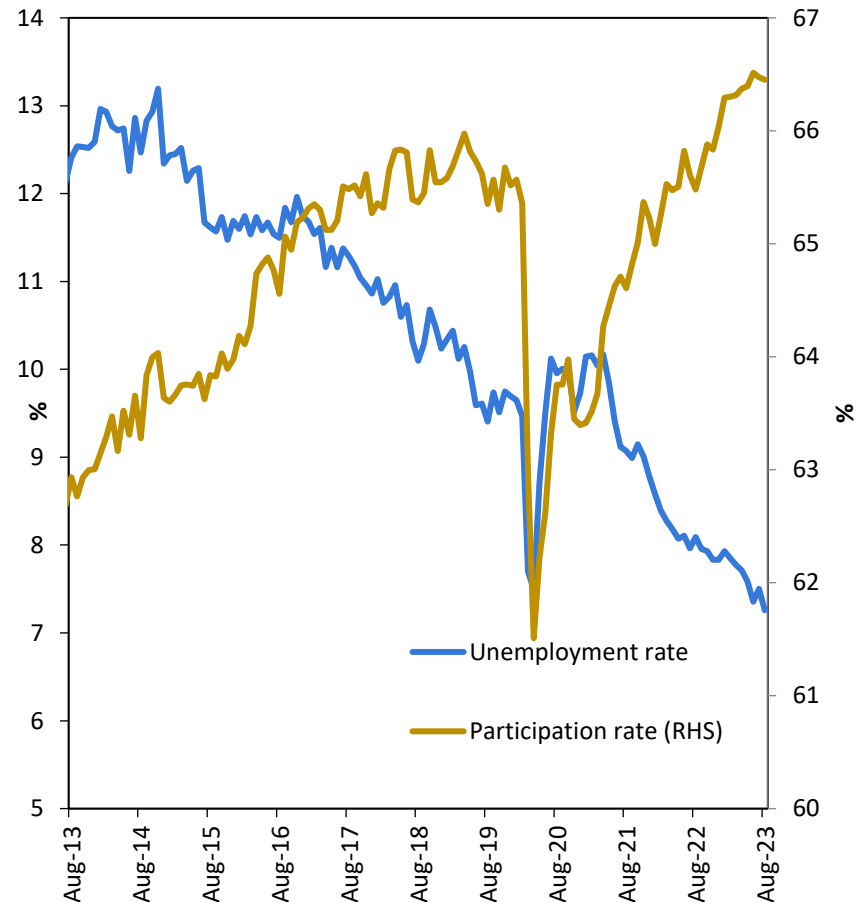
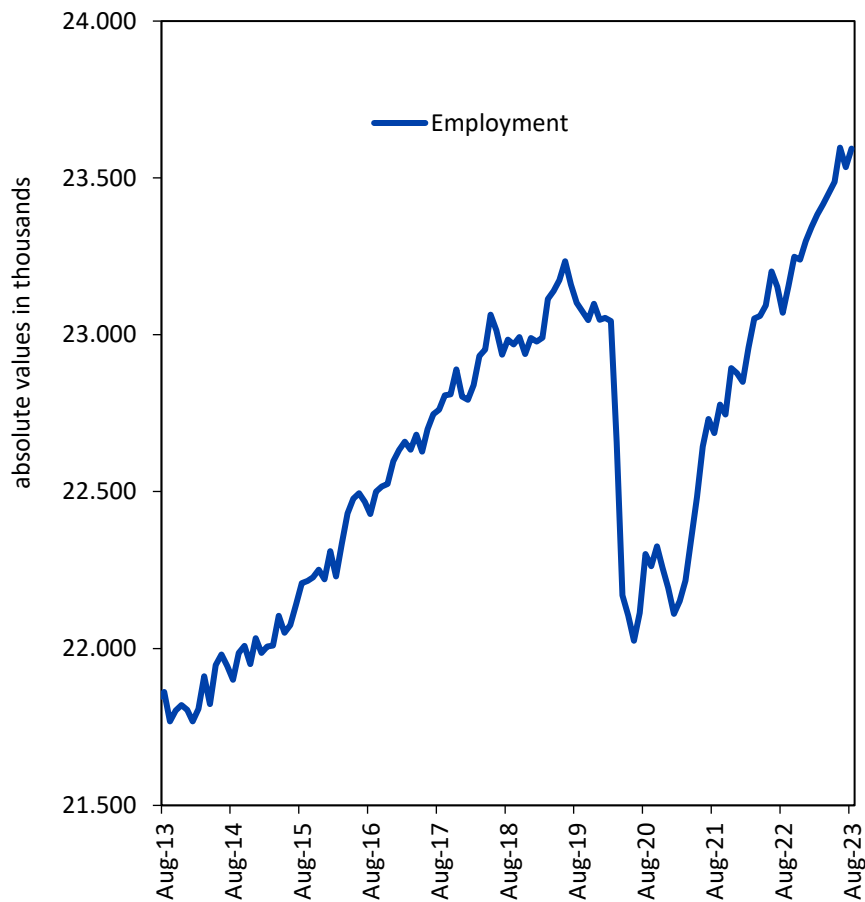


## Real GDP edged down in Q2, amid a continuing decline in industry



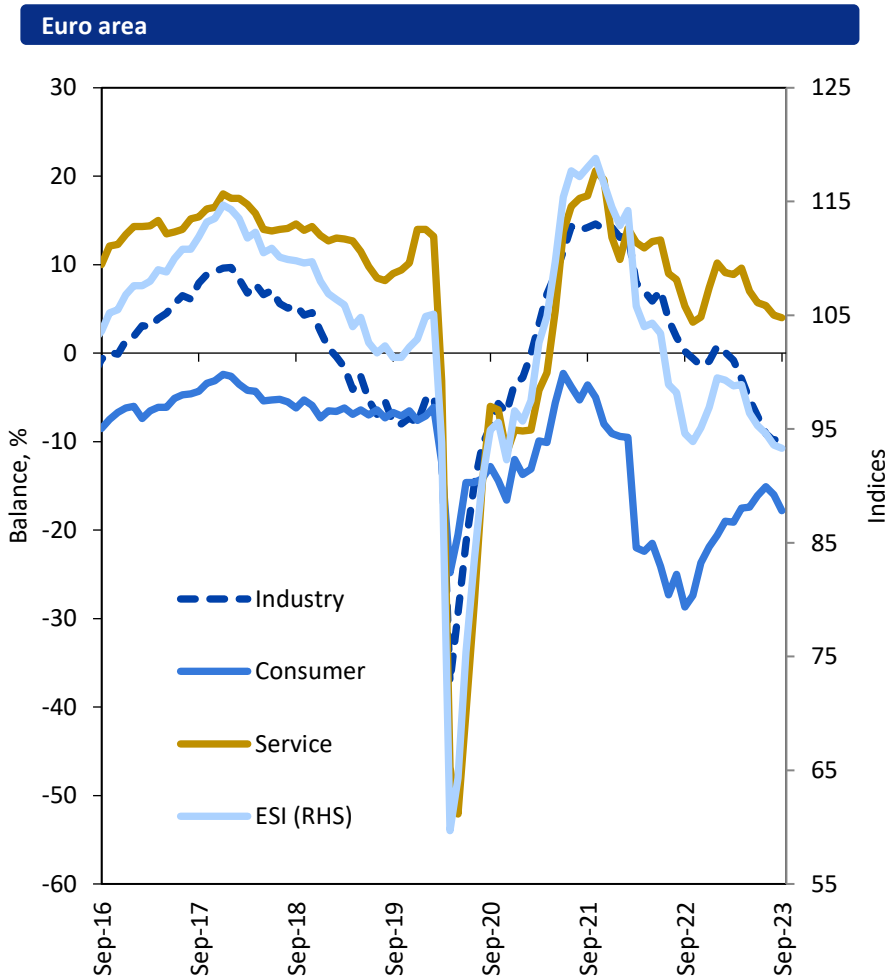
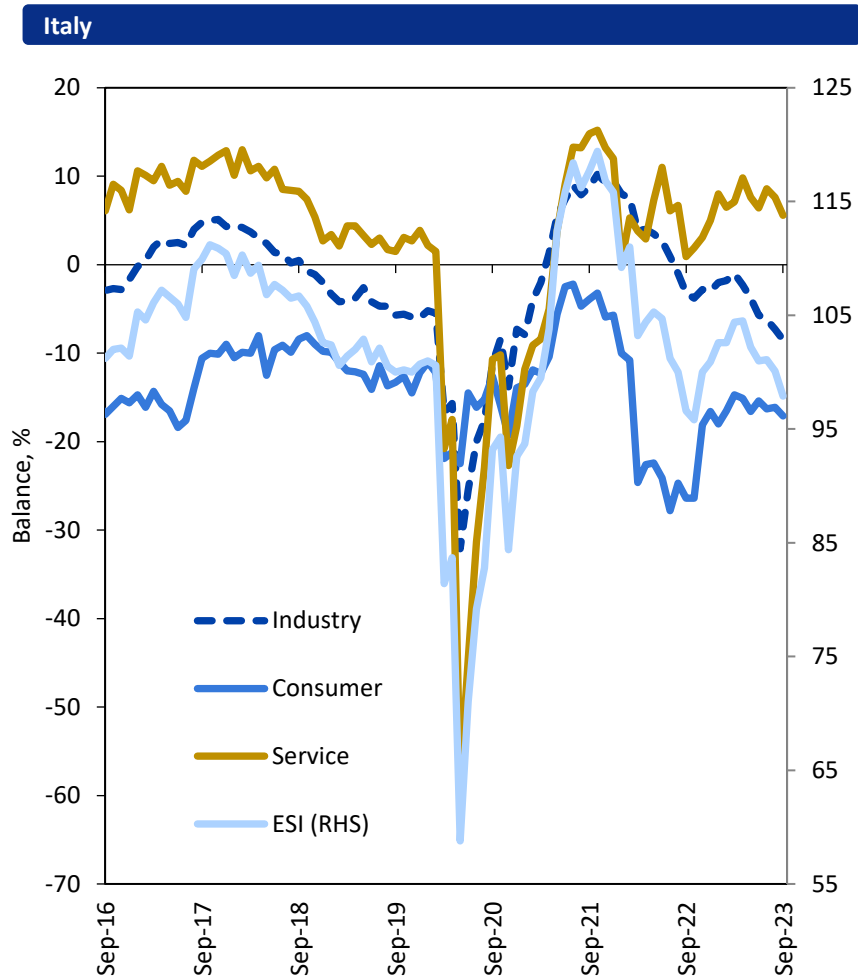
Source: ISTAT and MEF calculations

# Unemployment rate down, as employment rises above pre-crisis highs



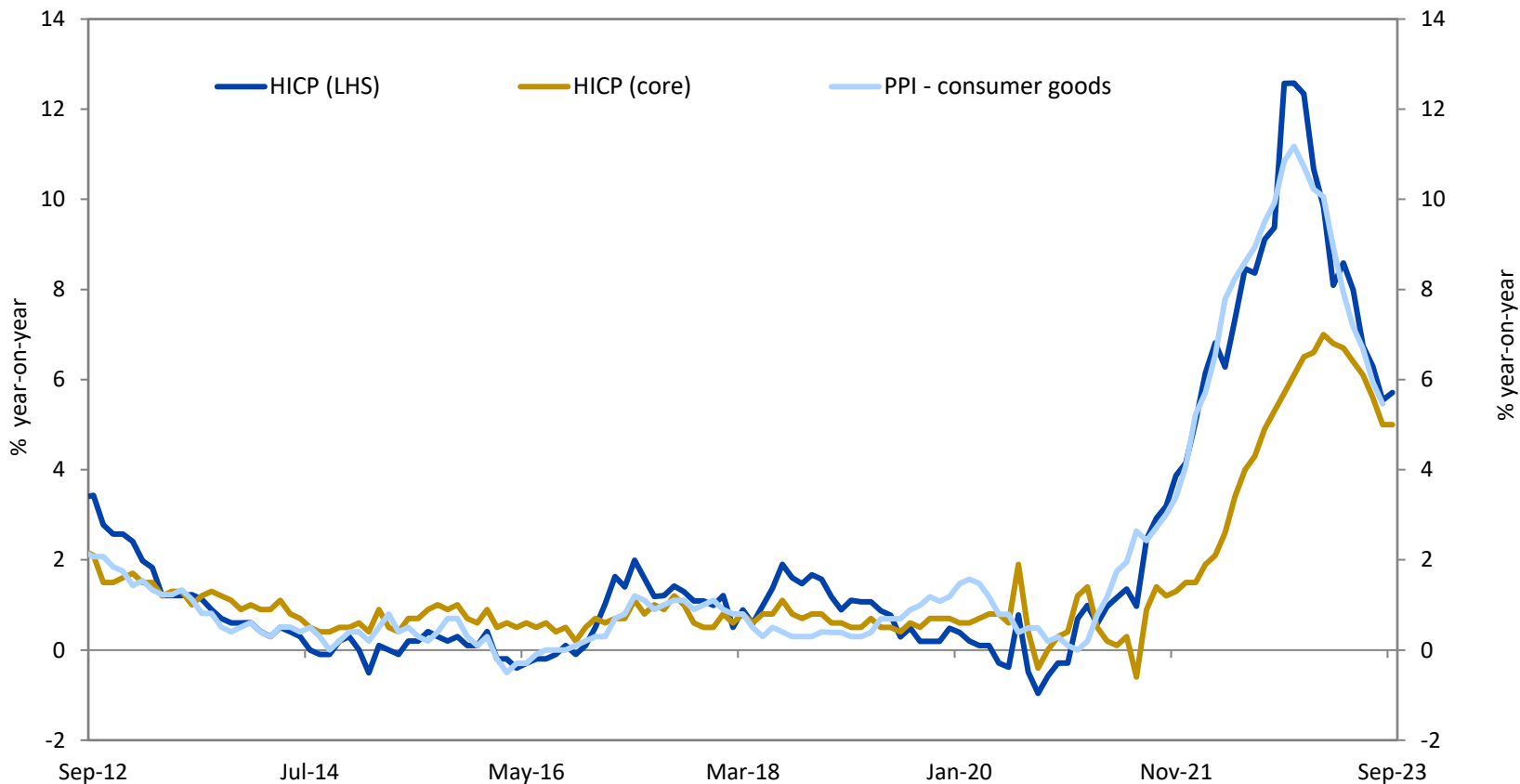
Source: ISTAT

# Economic sentiment slightly down in Q3: prospects are still uncertain



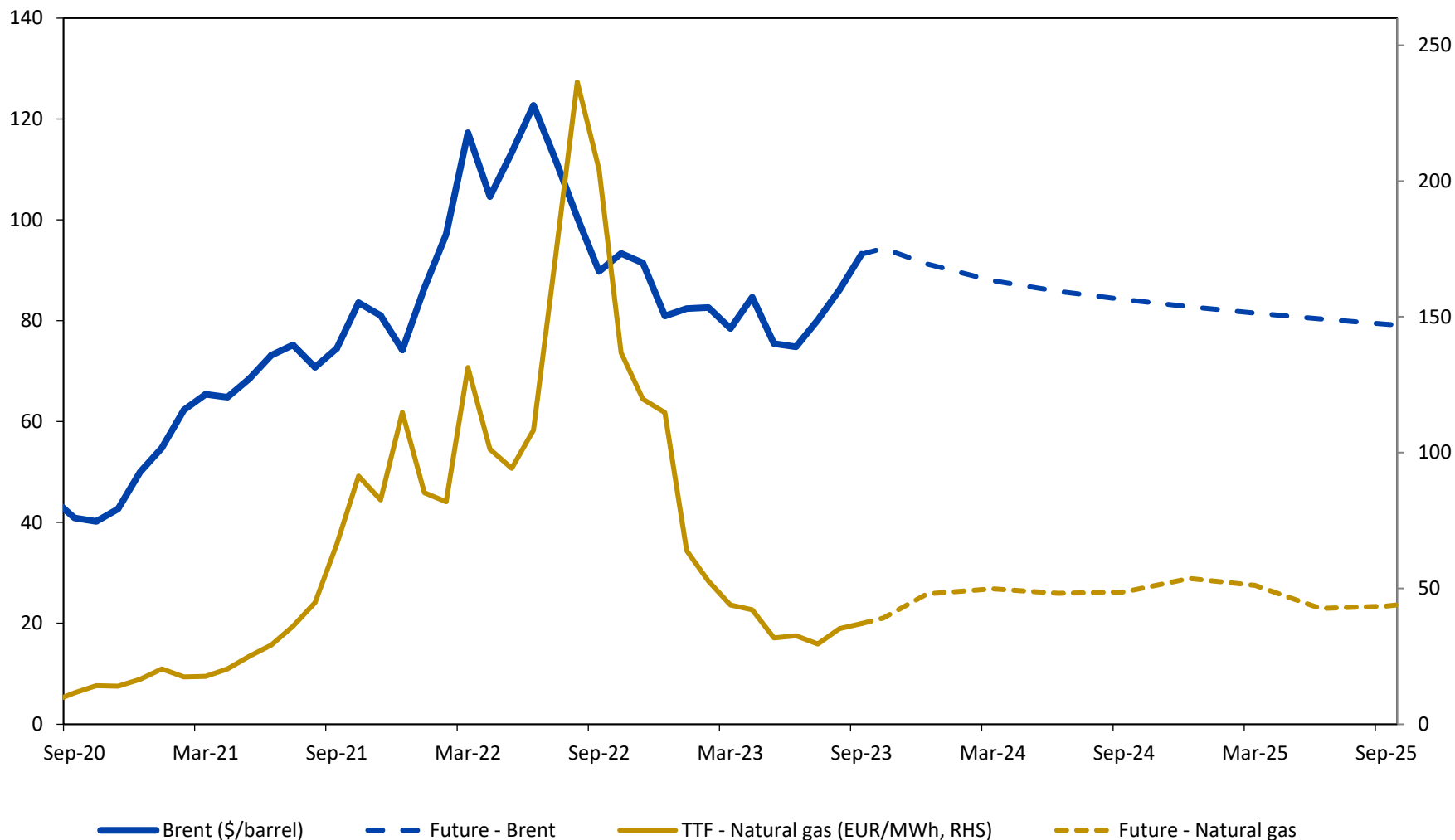
Source: European Commission

# Inflation rate falling and likely to fall further in Q4



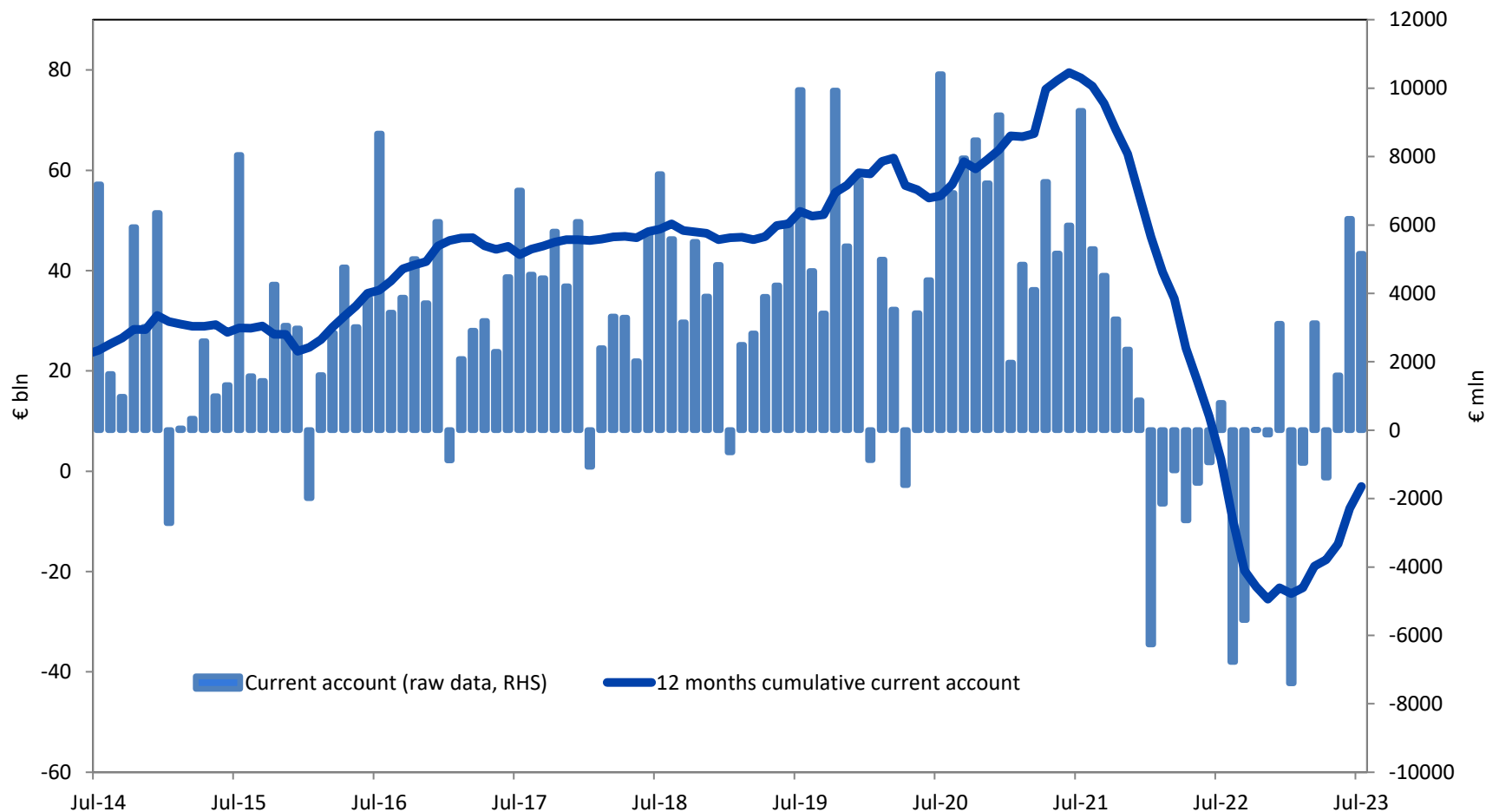
Source: ISTAT

# Oil and fuels prices rising, threatening the disinflation process...



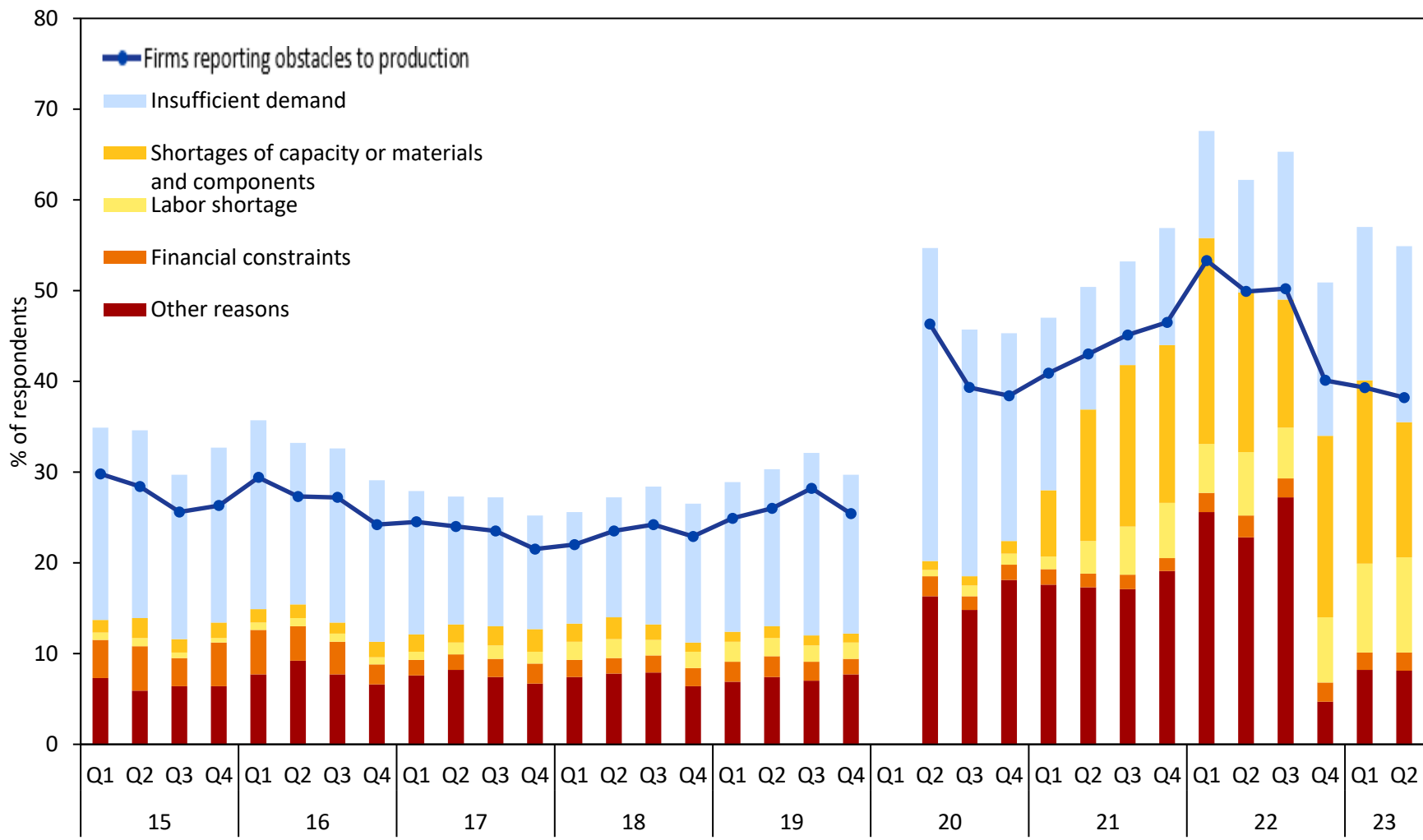
Source: Refinitiv Datastream

## ...and the sharp improvement in the current account balance



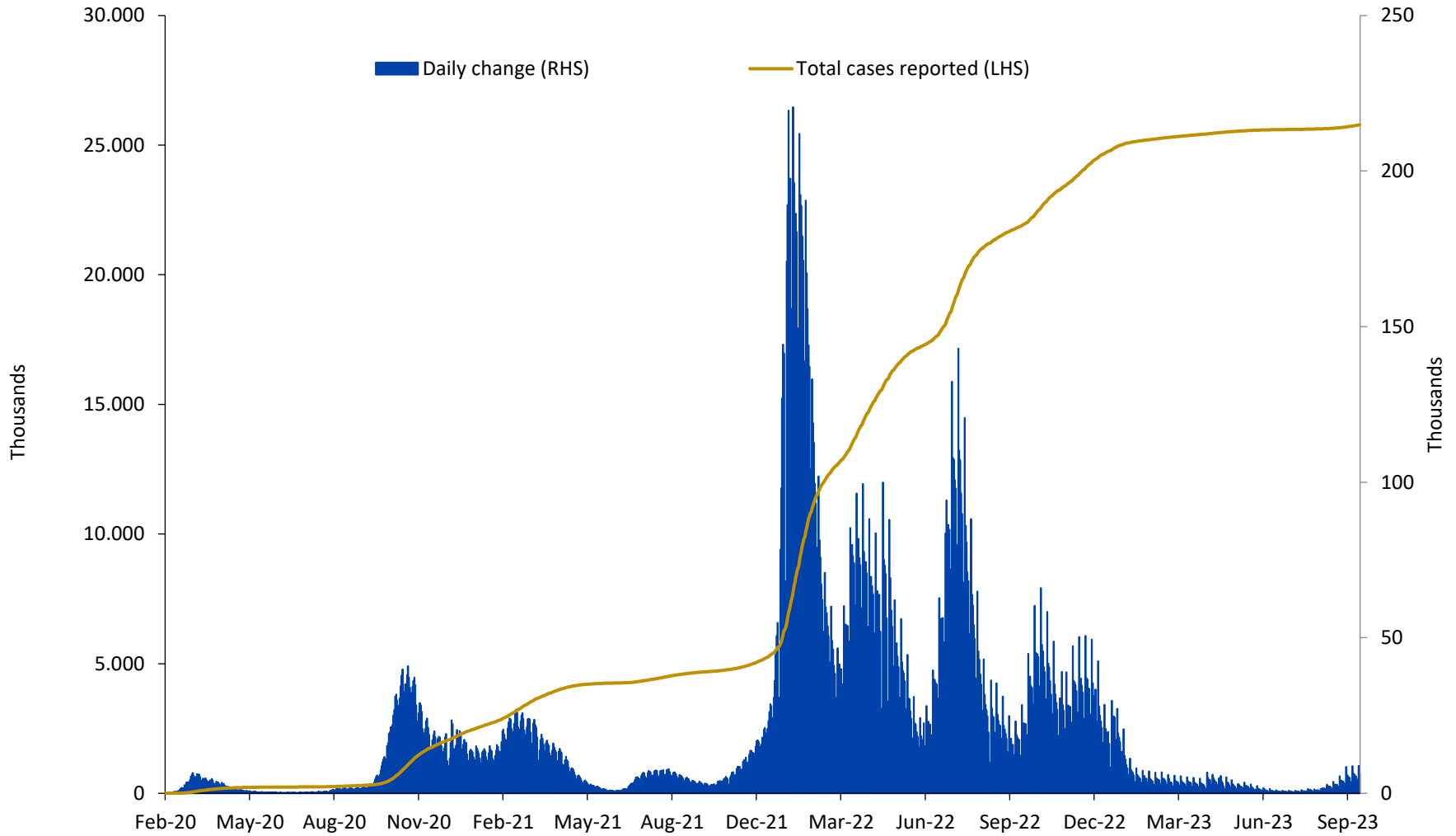
Source: Bank of Italy

# Shortages and delays along value chains appear to be easing



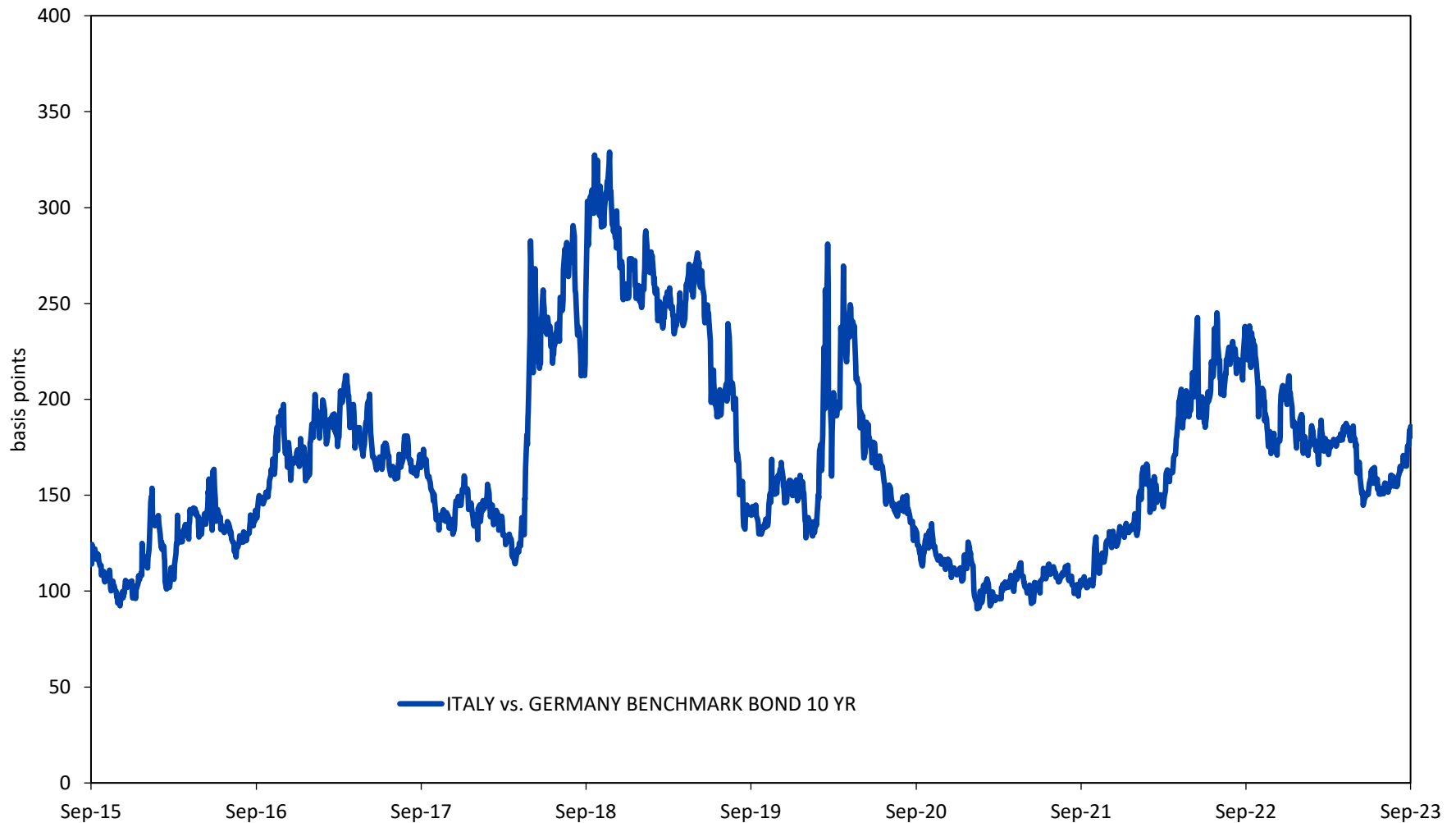
Source: ISTAT. Note: firms may select multiple reasons.

# Total Covid-19 infections ticking higher



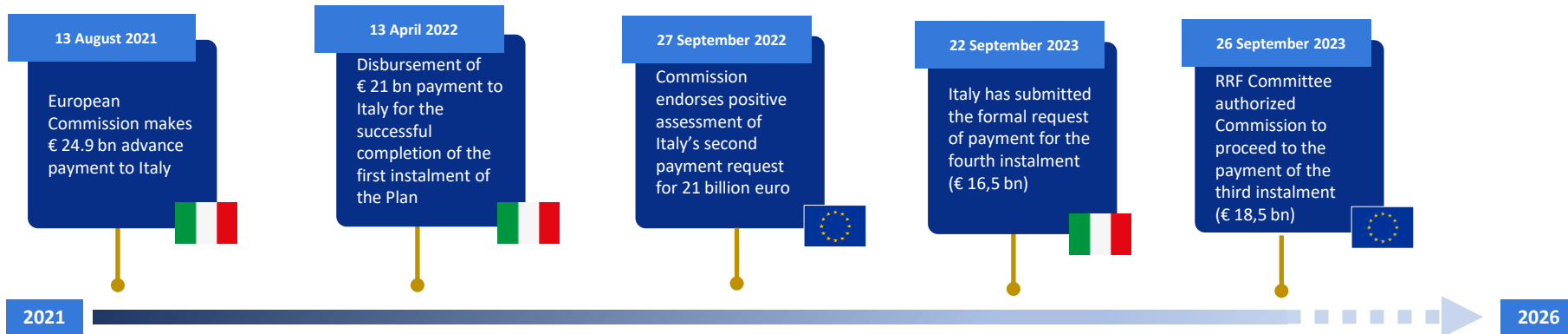
Source: Refinitiv

## Sovereign spread widening but still way below the 2022 highs



Source: Refinitiv

# Recovery and Resilience Plan: third instalment approved by EFC



# NGEU-RRF: updated expected expenditures

Recovery and Resilience Facility - NADEF 2023 (€ MLN)								
	2020	2021	2022	2023	2024	2025	2026	TOT
<b>RRF Grants</b>								
Additive projects	0	1,197	6,496	9,515	10,168	12,175	6,762	<b>46,313</b>
Existing projects	0	2,041	7,012	5,751	2,435	2,969	2,376	<b>22,584</b>
<b>Total</b>	<b>0</b>	<b>3,238</b>	<b>13,508</b>	<b>15,266</b>	<b>12,603</b>	<b>15,144</b>	<b>9,137</b>	<b>68,897</b>
<b>RRF Loans</b>								
Additive projects	6	145	1,179	3,471	19,867	28,701	24,834	<b>78,202</b>
Existing projects	1,475	2,149	2,551	4,567	9,107	13,034	11,517	<b>44,400</b>
<b>Total</b>	<b>1,480</b>	<b>2,294</b>	<b>3,730</b>	<b>8,038</b>	<b>28,974</b>	<b>41,735</b>	<b>36,351</b>	<b>122,602</b>
<b>RRF Total</b>								
Additive projects	6	1,343	7,675	12,986	30,034	40,876	31,595	<b>124,516</b>
Existing projects	1,475	4,189	9,563	10,319	11,542	16,003	13,893	<b>66,984</b>
<b>Total</b>	<b>1,480</b>	<b>5,532</b>	<b>17,238</b>	<b>23,305</b>	<b>41,577</b>	<b>56,878</b>	<b>45,488</b>	<b>191,499</b>

Recovery and Resilience Facility - Difference with respect to DEF 2023 (NADEF-DEF, € MLN)								
	2020	2021	2022	2023	2024	2025	2026	TOT
<b>RRF Total</b>								
Additive projects	-2	1	-15	-9,399	-1,926	5,696	5,645	<b>0</b>
Existing projects	234	-37	-413	-1,369	-445	2,502	-473	<b>0</b>
<b>Total</b>	<b>233</b>	<b>-36</b>	<b>-428</b>	<b>-10,767</b>	<b>-2,371</b>	<b>8,197</b>	<b>5,172</b>	<b>0</b>

# NGEU-RRF: updated expected expenditures

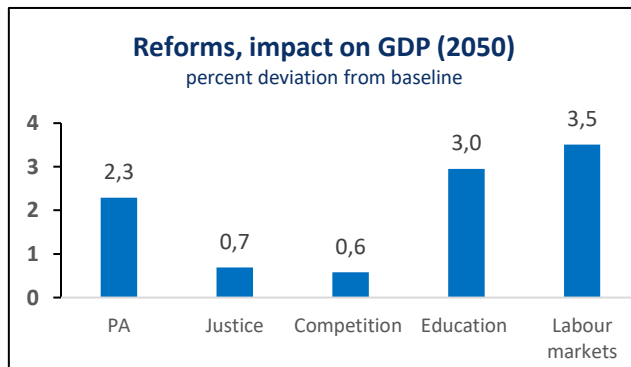
Recovery and Resilience Facility, NADEF 2023 (€ MLN)								
	2020	2021	2022	2023	2024	2025	2026	TOT
Additive projects	6	1,343	7,675	12,986	30,034	40,876	31,595	<b>124,516</b>
Existing projects	1,475	4,189	9,563	10,319	11,542	16,003	13,893	<b>66,984</b>
<b>Total</b>	<b>1,480</b>	<b>5,532</b>	<b>17,238</b>	<b>23,305</b>	<b>41,577</b>	<b>56,878</b>	<b>45,488</b>	<b>191,499</b>
<i>of which:</i>								
Public investment	1,475	2,630	3,685	7,315	24,666	34,320	30,963	<b>105,054</b>
Other capital expenditures	6	2,876	12,288	13,676	7,917	11,650	9,606	<b>58,019</b>
Current expenditures	0	27	877	2,069	8,052	10,138	4,639	<b>25,802</b>
Financial transactions	0	0	389	244	942	770	280	<b>2,624</b>

Recovery and Resilience Facility, difference with respect to DEF 2023 (NADEF-DEF, € MLN)								
	2020	2021	2022	2023	2024	2025	2026	TOT
Additive projects	-2	1	-15	-9,399	-1,926	5,696	5,645	<b>0</b>
Existing projects	234	-37	-413	-1,369	-445	2,502	-473	<b>0</b>
<b>Total</b>	<b>233</b>	<b>-36</b>	<b>-428</b>	<b>-10,767</b>	<b>-2,371</b>	<b>8,197</b>	<b>5,172</b>	<b>0</b>
<i>of which:</i>								
Public investment	227	-71	-598	-9,480	-11,230	-5,771	-4,039	<b>-30,963</b>
Other capital expenditures	6	8	-310	103	6,035	9,824	8,509	<b>24,175</b>
Current expenditures	0	27	92	-1,120	2,357	3,974	706	<b>6,036</b>
Financial transactions	0	0	389	-270	467	170	-4	<b>752</b>

# Macroeconomic impact of RRP

## MAIN REFORMS

- ✓ Public administration
- ✓ Justice
- ✓ Competition and public procurement
- ✓ Education and research
- ✓ Active labour market policies

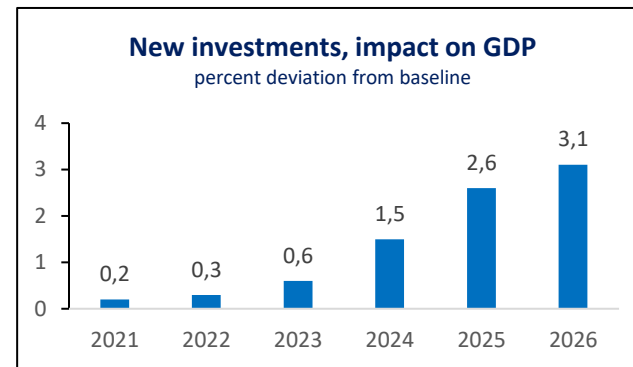


*Note: Simulations based on the RRP Milestones and Targets. MEF elaboration.*

- **Structural reforms could raise GDP by 10%**
- In a low (high) scenario GDP would be 4.5% (16.3%) above the baseline in the long run

## NEW OVERALL INVESTMENTS

Source of financing (€/bln)	
RRF	124.5
React-EU	13.9
National funds	46.2
<b>Total</b>	<b>184.7</b>



*Note: Simulations based on the updated RRP investment timeline. Preliminary results. MEF elaboration.*

# RepowerEU

- It is a European Plan meant to strengthen the strategic autonomy of the EU by diversifying its energy supplies and ending its dependency on Russian fossil fuel imports. It takes the form of a new RRP chapter;
- Italy intends to add to the new RePowerEU resources (about 2.8 bln) funds from dismissed NRRP projects and, possibly, from the Development and Cohesion Fund (FSC). The overall proposal is currently under evaluation by the European Commission;
- The draft Italian RePowerEU Chapter focuses on:
  - improving the transmission grid and distribution networks, addressing the overall strategic strengthening of energy distribution networks, including gas, in view of the conversion of facilities to hydrogen transport;
  - energy transition (hydrogen valley, green skilling, biofuels, tax credits to reduce energy waste and increase clean energy production);
  - measures and incentives for the decarbonisation of companies, to support energy-related production chains (in the perspective of the circular economy and the reuse of rare materials).
- Legislative simplification on renewable energy and regulations to curb speculation in energy commodity derivatives are also included.

## Recent measures adopted on tax credits (superbonus 110)

Decree law 11 abolished the possibility, as of last 17 February, to transfer tax credits related to building renovation bonuses (mainly the superbonus), in order to contain the impact of these credits on net borrowing of the general government sector as defined according to ESA criteria.

Following ISTAT data revision, driven by EUROSTAT recent clarification on the accounting treatment for tax credits, Italy's deficit figures have been significantly revised upwards in the previous years, because of their recognition in full at the time they are granted rather than when used.

Recent amendments to the decree include the extension of the deadline: to 30 September 2023 (from 31 March) to pay the 110% and complete the work on single-family units; and to 30 November (from 31 March) to send the communication to the Revenue Agency to secure credits acquired before 17 February .

Also, the transfer of tax credits is allowed for several cases concerning disadvantaged areas and social categories, i.e. social housing, non-profit organisations, and 'sismabonus' works.

It is granted the possibility, to banks and insurance companies with 'full' tax drawers, of using 2022 credits deriving from building bonuses to purchase ordinary BTP with a maturity of at least 10 years. More in general, tax credits could be used to offset social security debts (over 10 years instead of 4).

Finally, it was announced the establishment of a platform to solve the issue related to tax credits accrued by construction companies but no longer transferrable to third parties.

## Energy price mitigation measures have been largely phased out (1)

The **DL No. 34 of 30 March** extended only some support measures against the energy crisis to the second quarter of 2023, continuing the process of phasing out started at the end of 2022.

The decree extends the reinforcement of the social bonuses on bills, even increasing the ISEE limits for numerous households; the reduction of the general system charges on gas bills; the reduction to 5% of the VAT rate on gas; the tax credits for firms (energy and gas-intensive and not) but with a reduction of the percentage coverage.

The last **DL No. 79 of 28 June** further reinforces the process of phasing out, by extending only a few support measures to the third quarter of 2023.

The decree extends the reinforcement of social bonuses on bills; the zeroing of the general system charges on gas bills; the reduction to 5% of the VAT rate on gas for combustion, district heating and thermal energy.

The tax credits for companies instead expired on 30 June. Thus, another support measure has been removed as not longer needed.

Also because of the lowering energy prices, the gross impact of the two Decrees amounts to only 0.2% of GDP (less than 4 bn), contributing to the reduction of the overall energy package in 2023 with respect to 2022.

## Energy price mitigation measures have been largely phased out (2)

The **DL No. 131 of 29 September 2023** provides some measures to limit the impact of the high energy prices in the fourth quarter of 2023.

The decree extends the reinforcement of the social bonuses on bills, confirming higher ISEE thresholds for both standard and numerous households. The bonus is even integrated with a contribution to cope with the heating costs. The social bonus continues to represent the pillar of the support measures in favour of the most fragile households.

Given the surging fuel prices observed in the last months, the decree also introduces a contribution in favour of poor households (beneficiaries of the 'social card') for the purchasing of fuels. It is a targeted measure, more efficient rather than a linear cut in excise duties.

Finally, the reduction of the general system charges on gas bills and the reduction to 5% of the VAT rate on gas for combustion, district heating and thermal energy are extended until the end of the year.

The updated energy package amounts to 1.3% of GDP, more than halved compared to 2022 (2.8% of GDP). More than 56% of measures in 2023 are targeted to most vulnerable households and firms, increasing from the, already high, share of 46% registered in 2022.

The Government confirms the objective to fully withdraw the energy measures by 2024, in line with the EC recommendations.

# Official macroeconomic forecast

## Official macroeconomic forecast – Stability Program Update (27 September 2023)

<i>Policy scenario</i>					
<i>(% change yoy)</i>	2022	2023	2024	2025	2026
<i>Real GDP</i>	3.7	0.8	1.2	1.4	1.0
<i>Domestic demand net of inventories</i>	5.0	0.9	1.3	1.3	1.0
<i>Inventories</i>	-0.8	-0.3	0.1	0.0	0.0
<b>Net export</b>	<b>-0.5</b>	<b>0.2</b>	<b>-0.2</b>	<b>0.1</b>	<b>0.0</b>
<b>Nominal GDP</b>	6.8	5.3	4.1	3.6	3.1
<b>GDP deflator</b>	3.0	4.5	2.9	2.1	2.1
<b>Compensation per employee</b>	3.2	4.0	2.3	2.1	1.8
<b>Productivity (on GDP)</b>	0.2	-0.5	0.5	0.3	0.3
<b>Unit labour cost (on GDP)</b>	3.0	4.6	1.8	1.8	1.5
<b>Employment (FTE)</b>	<b>3.5</b>	<b>1.4</b>	<b>0.7</b>	<b>1.1</b>	<b>0.7</b>
<b>Unemployment rate</b>	<b>8.1</b>	<b>7.6</b>	<b>7.3</b>	<b>7.2</b>	<b>7.1</b>
<b>Current account balance</b>	<b>-1.2</b>	<b>0.8</b>	<b>1.3</b>	<b>1.8</b>	<b>1.9</b>

Source: ISTAT and Government projections for 2023-2026 (Update to Economic and Financial Document 2023)

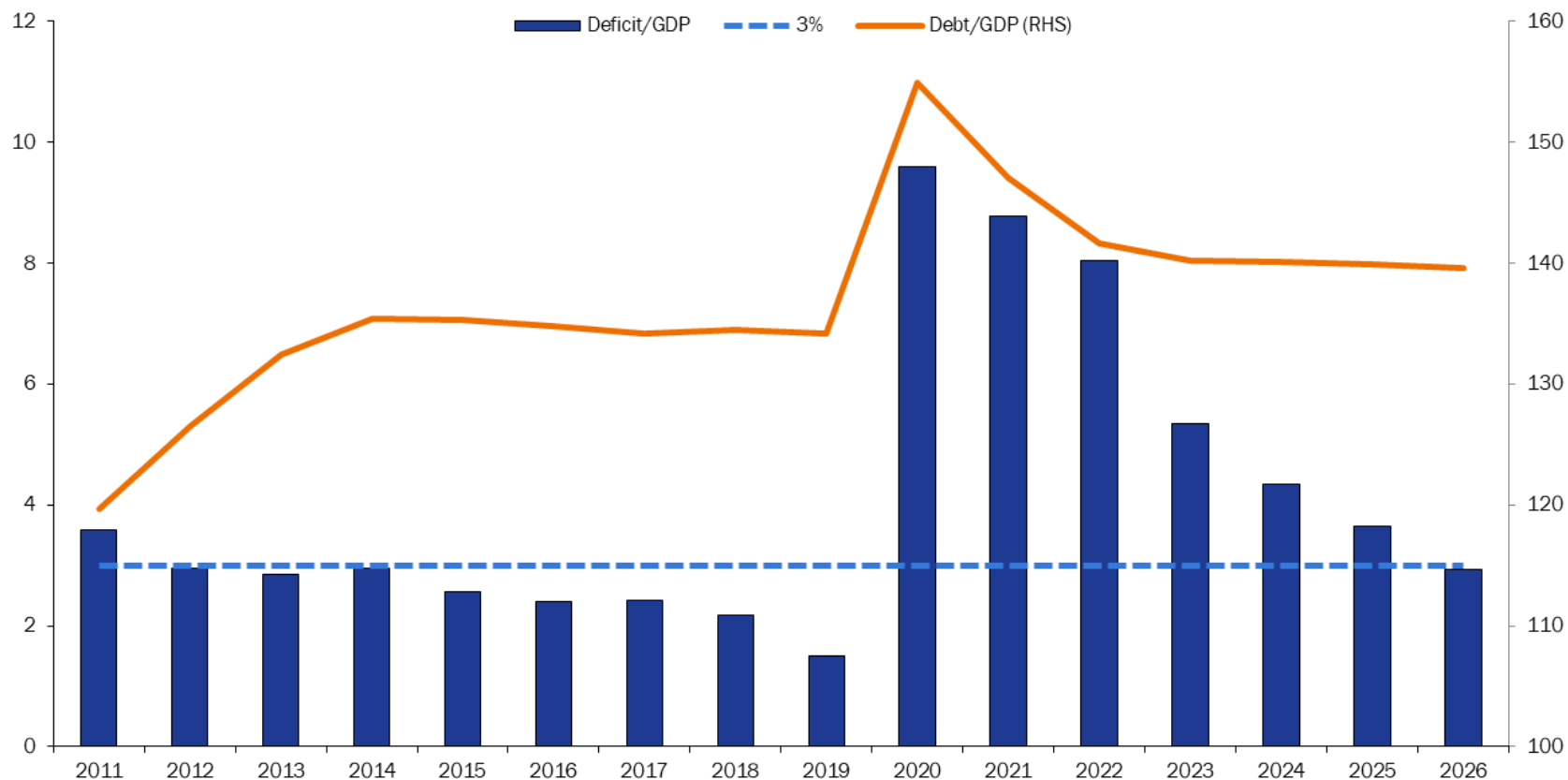
## Budgetary projections

POLICY SCENARIO						
Policy scenario						
<i>percent of GDP</i>	2021	2022	2023	2024	2025	2026
<b>General government balance</b>	<b>-8.8</b>	<b>-8.0</b>	<b>-5.3</b>	<b>-4.3</b>	<b>-3.6</b>	<b>-2.9</b>
General government primary balance	-5.3	-3.8	-1.5	0.2	0.7	1.6
<b>Interest expenditure</b>	<b>3.5</b>	<b>4.3</b>	<b>3.8</b>	<b>4.2</b>	<b>4.3</b>	<b>4.6</b>
<b>Public debt (1)</b>	<b>147.1</b>	<b>141.7</b>	<b>140.2</b>	<b>140.1</b>	<b>139.9</b>	<b>139.6</b>

(1) Gross of financial support to Eurozone countries.

Source: For 2021 and 2022, ISTAT estimates. Government policy scenario projections for 2023-2026 (Italy's Update of the Stability Programme 2023).

## Budget deficit set to decline sharply in 2023-2026, debt ratio to lag



Source: ISTAT and Bank of Italy for 2011-2022; Government policy scenario projections for 2023-2026 (Update of the Economic and Financial Document 2023).

## Update of the Stability Program 2023 and planned fiscal measures

The worsening of the public finance perspectives presented in Stability Program Update is mainly due to i) the slowing down of the economic growth; ii) the higher costs related to the superbonus; iii) the impact of the ECB monetary policy on government bonds yields and on interest spending.

The restraints to the economic growth, the prolonged high inflation, the risks and uncertainty in the international geopolitical context, require the fiscal policy to be oriented towards the support of the household purchasing power and business activity.

The Government sets the new deficit-to-GDP targets to 5.3% in 2023, 4.3% in 2024, 3.6% in 2025 and 2.9% in 2026.

The moderately expansionary fiscal stance in 2023-2025 does not preclude the objective of bringing back the deficit under the 3% threshold by 2026.

The next Budget law will pursue a reduction in the tax burden, through the extension of the social security contribution cut for low-income workers, and the start of the programmed reform of the tax system, oriented to increase its simplicity, its efficiency and to make the system more growth- and environmentally-friendly.

The fiscal plan is compliant with the European recommendation to limit the nominal growth of net primary expenditure below 1.3% in 2024; it will ensure the relevant improvement of the structural balance in the coming years, as to place the debt-to-GDP ratio on a path of plausible and continuous reduction.

## The impact of the building renovation bonuses

In the Annual national accounts release of 22 September, Istat revised the impact on net borrowing deriving from the superbonus and the external redecoration scheme in 2022, from 2.6% to 2.8% of GDP.

The higher cost with respect to the ex-ante expectations is due both to the higher take-up by the citizens and also to the inflationary pressure on construction sector prices that has pushed up the nominal value of the allowances.

Following the Eurostat opinion of 26 September, the tax credits related to these bonus are treated as 'payable' until 2023, and consequently recorded in expenditure, as investment grants, for the full amount of the credit accrued in the year in which the taxpayer incurred the expenditure giving rise to the tax benefit.

Given the abolition of the transferability of the tax credits since 17 February 2023, the credits accrued in 2024-2025 will be treated as 'non-payable', and then accounted as lower revenues consistently with the accounting of the tax deductions as a reduction of tax revenues for the portion of the credit due in the year (cash terms).

Following this opinion and the recent data from monitoring activities, the impact on net borrowing of the superbonus in 2023 is revised upward from 0.7% to 1.8% of GDP. Then, the impact on the net borrowing in 2024 and 2025 is revised downwards as it is split in the following years as a tax revenues reduction.

Overall, the building renovation bonuses have a massive impact on the deficit of the last and next years. Albeit relevant, the contribution to growth of the two incentives has most likely not been sufficient to compensate for their costs, determining an overall negative impact on the public finances.

## The exceptionally high SFAs reflect the impact of the superbonus on public debt dynamics

The expected flow of tax credits related to private buildings, increased due to the upward revision of the overall cost of the superbonus, exerts significant pressure on public debt

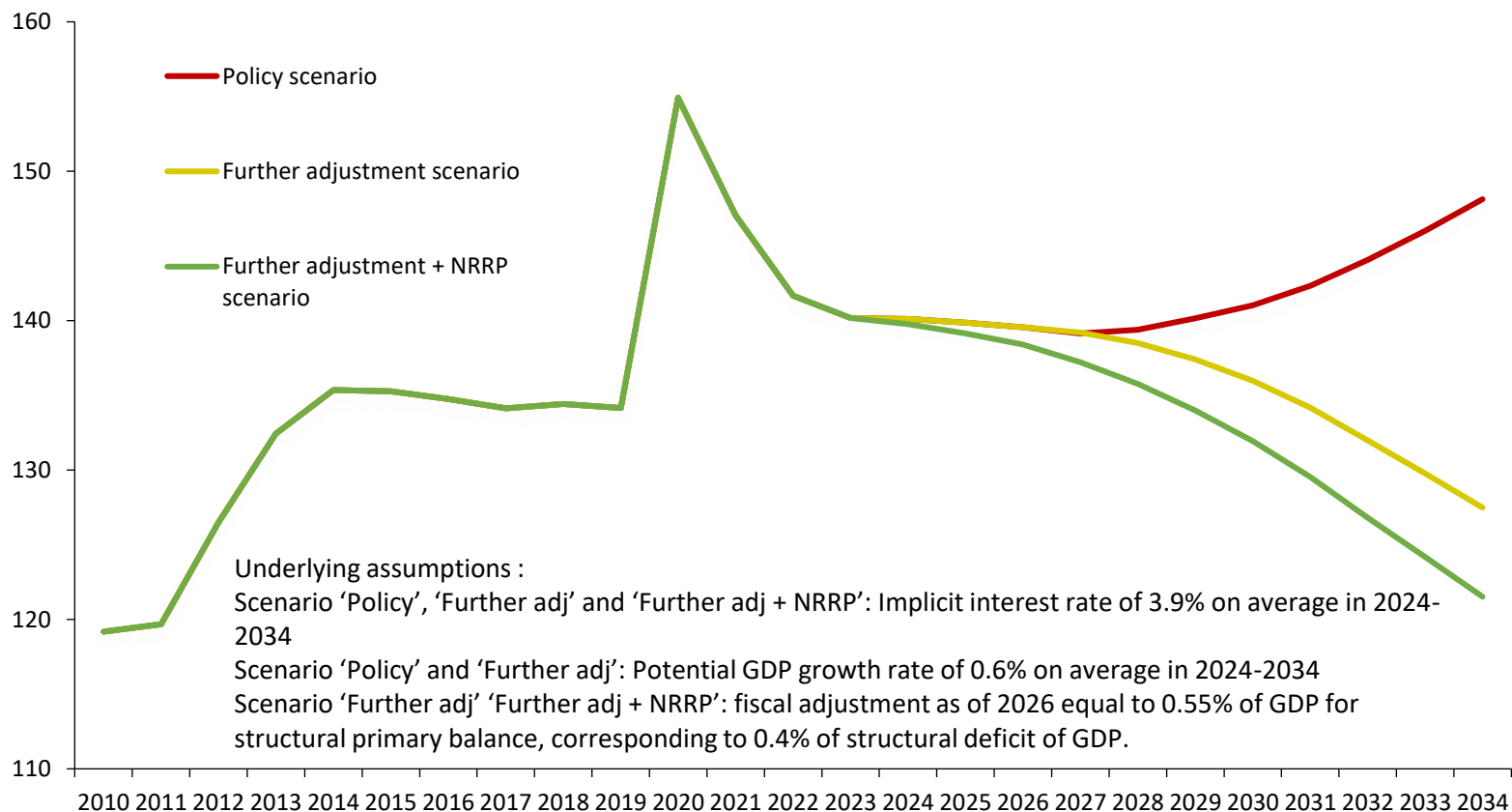
Said pressure is captured by the stock-flow adjustment (SFA) component, which includes the difference between cash and accrual items. In the baseline scenario under existing legislation, the SFA is projected to stay well above 1% in 2024-2026, even increasing in 2025 respect to the Stability Program forecast.

To compensate for the effect of the superbonus, the Government is planning an ambitious program of privatizations and valorizations of public assets, which will generate revenues for about 1% of GDP in the next three years.

Moreover, the Treasury liquidity holdings are projected to decrease after the exceptional increase during the pandemic. The retrieve to normal levels will contribute to cash requirements of the general government without increasing the public debt.

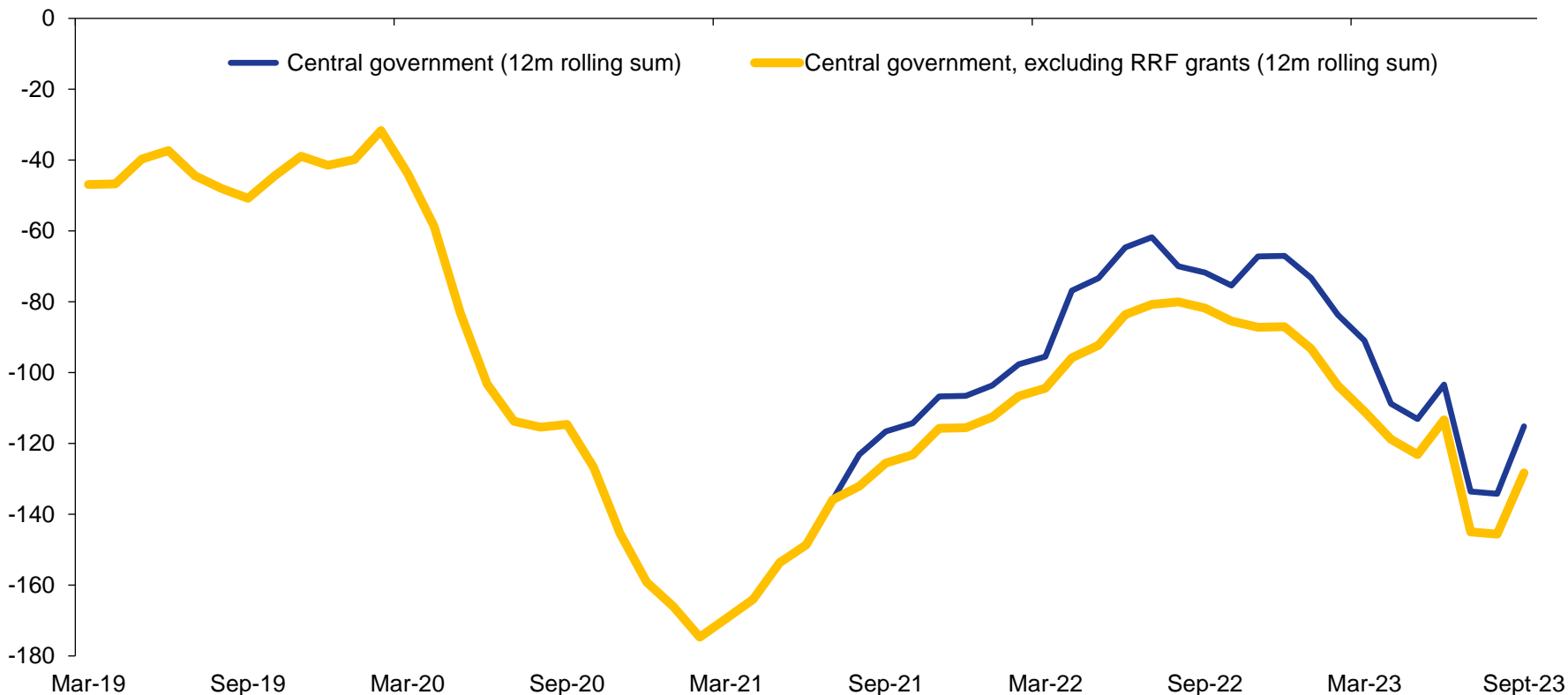
As a result, the SFAs projected in the policy scenario are lowered towards 1%, in relevant reduction compared with the forecasts in the Stability Program, contributing to ensure the gradual reduction of the debt-to-GDP ratio.

# DSA highlights the need for a higher primary surplus after 2026



Source: Projections consistent with 2023 Update to Economic and Financial Document 2023

# Cumulative net cash borrowing requirement



Source: Monthly cash data from RGS.

Source: Monthly cash data from RGS.

## Euro Area fiscal policy stance in 2023

### Growth lost momentum in the first half of 2023

- The EC still forecasts a slowdown in 2023 (0.8% real EA GDP growth), revising downward the rate compared to spring projections (-0.3 pp)
- Demand was curbed by high inflation and monetary tightening
- Risks are tilted to the downside / uncertainty is high

### What role for fiscal policy?

- The general escape clause remains in force this year
- The EC recommends (as of May 2023):
  - define medium-term fiscal strategies to ensure debt sustainability and raise the growth potential
  - avoiding broad-based support to aggregate demand
  - better targeting of energy subsidies to the most vulnerable households and firms and introducing a two-tier energy pricing system
  - Maintain a high level of public investment

## The European Commission's Economic Governance Reform proposal

- Medium term debt-reduction plans for countries whose debt to GDP ratio is above 60% should span over a 4-year horizon...
- ... targeting a structural primary balance such that the DSA points to a public debt ratio on a plausibly declining path
- The country-specific net expenditure path would be the single operational indicator
- The adjustment path can be extended to 7 years if the Member State commits to new reform and investment initiatives
- General and country-specific escape clauses for extraordinary events (pandemics, wars) would remain but revised
- Enforcement would be more rigorous

## **ECONOMIC GOVERNANCE REVIEW:** Agree on a renewed fiscal framework by year-end (before the deactivation of the General Escape Clause)

### Main steps:

- 9 November 2022: European Commission published its orientations
- 14 March 2023 - ECOFIN : Member States identified areas of convergence and areas for further work on a reformed framework
- 26 April: European Commission presented its legislative proposals including suggestions from MS such as minimum adjustment required and a numerical debt benchmark
- 28-29 June - European Council: commitment to finalise the legislative work in 2023
- 16 September - Informal ECOFIN: confirming the commitment to finalise the negotiation by end-2023

## ECONOMIC GOVERNANCE REVIEW: main areas of negotiation

- **Institutional balance:** ensuring a rules-based multilateral system, enhancing transparency, preserving flexibility; defining the roles and the decision-making process of all the institutions involved
- **Common safeguards:** expenditure rule calibrated on the basis of country-specific debt situations, possibly introducing benchmarks on debt reduction to seize credible fiscal strategy
- **Fiscal space for investments and incentives for reform:** Possibility of extending the adjustment period due to commitments on reform and investments; some preferential treatment for co-financing EU funds including RRF loans, public investments and expenditures in defence
- **Credible enforcement and ownership:** stronger national ownership, better enforcement of the new fiscal discipline, preserving equal treatment of all Member States

## Key points

- **Strong performance of the economy in 2021-2022. GDP level revised up.**
- **Employment still growing on trend**
- **Inflation falling, as food and energy shock receding**
- **Current account swings back into surplus**
- **Budget deficit targets overachieved net of the superbonus impact**
- **Impact of RRP and innovation policies still in the pipeline.**
- **Outlook more uncertain, weak growth in Q3, forecasts revised down.**
- **Higher oil and fuels prices could slow the disinflation process**
- **Limited fiscal space for new policies. Impact of superbonus will linger.**
- **Cash borrowing requirement will stay high due to impact of tax credits...**
- **...and interest rates and sovereign spread.**
- **Rating agencies will have to assess recent and forthcoming policy moves**

Thank you for your attention

Find out more on the official website:  
[dt.mef.gov.it](https://dt.mef.gov.it)