Italy

Outlook

	Average 11-15	2016	2017	2018	2019	2020	2021	Forecasts 2022	Forecasts 2023
GDP growth (%)	-0.7	1.4	1.7	0.8	0.5	-9.1	6.6	3.4	-0.2
CPI inflation (%)*	1.6	-0.1	1.3	1.2	0.6	-0.2	1.9	7.7	4.8
Fiscal balance (% of GDP)	-3.0	-2.4	-2.4	-2.2	-1.5	-9.7	-7.3	-5.6	-3.9
Primary fiscal balance (% of GDP)	1.7	1.5	1.4	1.5	1.9	-6.1	-3.7	-2.1	-0.8
Public debt (% of GDP)	125.8	134.8	134.2	134.4	134.1	155.3	150.8	147.0	147.1
Reference rate (%)*	0.6	0.0	0.0	0.0	0.0	0.0	0.0	0.6	2.2
Current balance (% of GDP)	0.3	2.6	2.6	2.6	3.3	3.7	2.5	-1.0	-2.0

Note: * Annual average. CaixaBank Research forecast for GDP, CPI and interest rates.
Source: CaixaBank Research, based on data from AMECO, Oxford Economics, the ECB (via Refinitiv) and the Italian government.

- **The Italian economy surprised us positively in Q2 2022** by recording a quarter-on-quarter growth of 1.1% (0.1% in Q1 2022). This was due to the boost provided by the removal of almost all of the restrictions associated with COVID-19, though this momentum may not continue.

- **Of the EU's largest economies, Italy, together with Germany, is one of the countries most affected by the huge increase in the price of natural gas** caused by the war in Ukraine. Russian gas imports represent 40% of Italy's total gas imports. In addition, its dependence on gas for generating electricity is very high (using almost 48% of its gas), as Italy was the first European country to close its nuclear power plants at the start of the 1990s. 25% of electricity is generated from nuclear energy in half of the European countries.

- Currently, **inflation is at a record high** and a significant correction in the short-term is not likely, due to the increasing risks of Europe's energy scenario (one of the most ,notable being the *indefinite* closure of Nord Stream 1 and 2). In this context, household expenditure has remained stable until now thanks to the "pent-up" demand, but it is expected to drop significantly in the upcoming months.

- Moreover, **the political situation in Italy represents another source of uncertainty**. Following Mario Draghi's resignation as prime minister, the right-wing coalition led by Giorgia Meloni's Fratelli d'Italia party (a national-conservative and right-wing populist party) won a landslide victory in the elections held on 25 September. The new government will be formed within the next few weeks and the financial markets are waiting to see which ministers are appointed to key positions, such as the Ministries of Finance and Foreign Affairs. Some of the coalition's parties have toned down their Eurosceptic messages, but they continue to be in favour of reducing taxes and implementing populist spending measures. In addition, they seem to be opposed to reforming the tax system and liberalising competition rules, two of the key reforms proposed by Draghi within the framework of the NGEU funds. Therefore, the first key test for the new Government will be the budget, which must be approved before the end of the year, and which could become a source of tension with Brussels.

  This increase in uncertainty could limit the ECB's capacity to contain risk premia, which is of particular concern with a public debt exceeding 150% of GDP. In fact, the ECB has developed a new instrument (the Transmission Protection Instrument) to purchase sovereign debt from countries with risk premia increasing in an "undesirable or disorganised" way.

  As a consequence, all signs point to the fact that there will be a drop in activity in Q4 2022 and Q1 2023, with a –0.2% change in GDP in 2023. In addition, **the growth risks are clearly tilted to the downside**.

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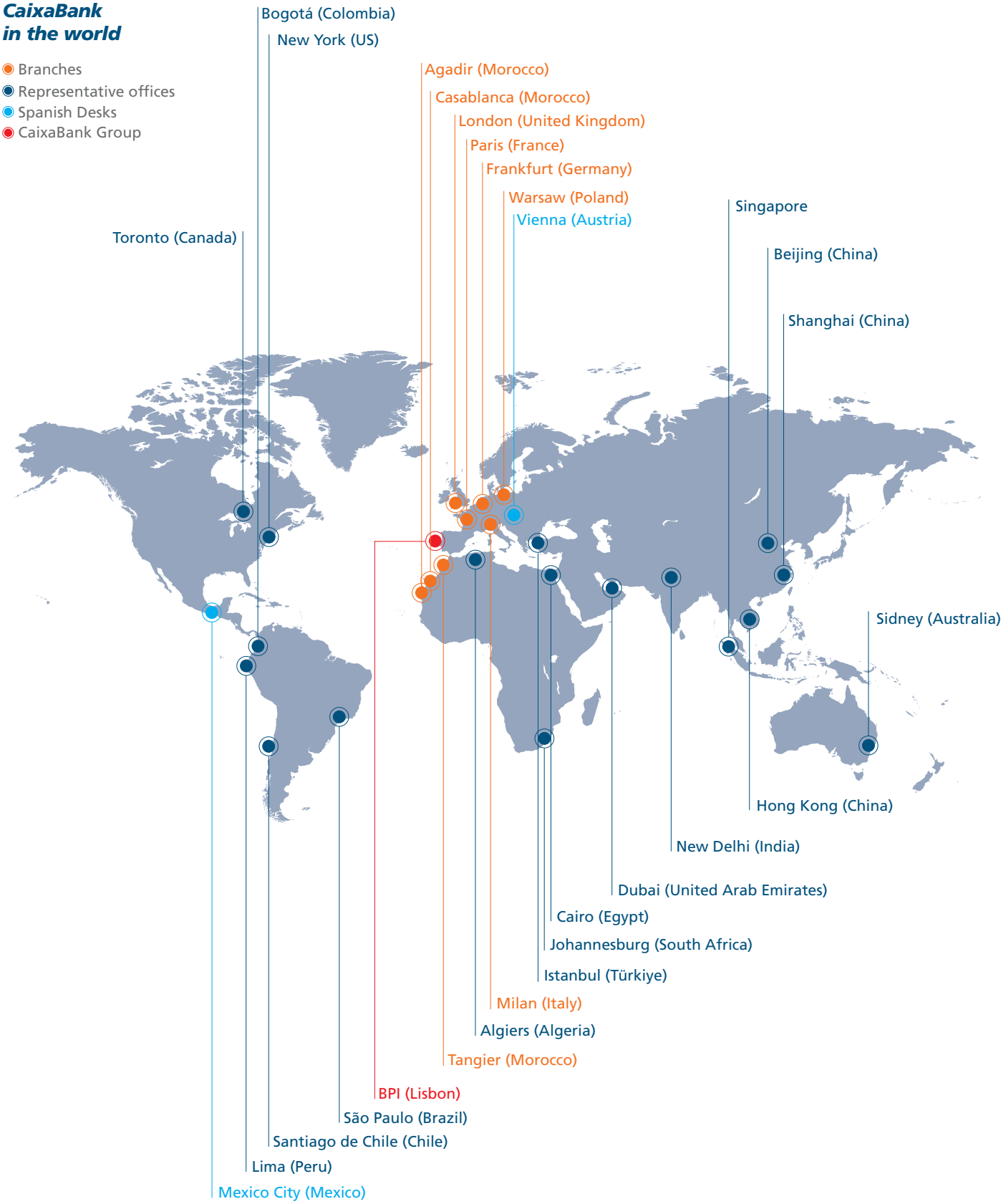

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