Italy

Recession in the short term, demographic challenge in the long term

The Italian economy entered the third recession in the last ten years. In 2018, value added in the manufacturing sector recorded four consecutive contractions. Domestic demand disappointed, as both households and firms remained extremely cautious. Given the deterioration of the overall scenario, in the 2019 Economic and Financial Document recently approved, the Italian Government has lowered from 1% to 0.2% the GDP growth expected in 2019, with public deficit at 2.4% and the debt to GDP ratio at 132.6%. The structural deficit would worsen by 0.1%, to 1.5%. A progressive ageing of the population makes the scenario even more complicated.

In the second half of 2018, the Italian economy entered the third recession in the last ten years. Real GDP declined by 0.1% q/q in Q3 and in Q4. The annual growth rate was nil, from 1.7% a year before. The contraction reflected the negative contribution of stocks (-0.4% in Q4) and the feeble evolution of domestic demand, while net exports sustained GDP increase, as exports rose more than imports, adding 0.4% to the overall growth in the second half of the year.

A new recession, amid feeble consumption and disappointing investment

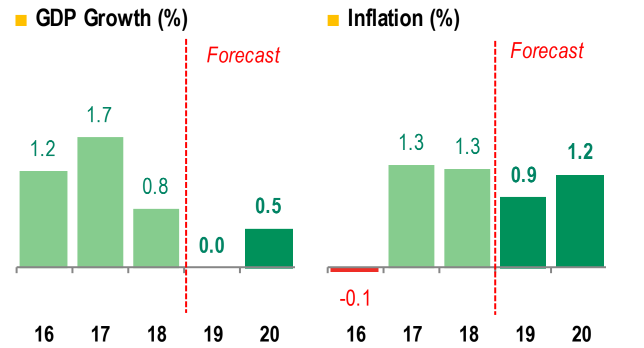
The slowdown mainly interested sectors which had supported the previous recovery. In 2018, while services and construction continued to slightly recover, value added in the manufacturing sector recorded four consecutive contractions, with the annual growth rate falling from +5% in Q3 2017 to -1.1% in Q4 2018. Production of automobiles declined by more than 15% from July to December.

The overall conditions in the labour market further deteriorated. The unemployment rate increased to more than 10.5%, with that referred to people aged 15-24 stable at 33%. The recovery of employment has come to a halt, with the number of persons in work virtually unchanged around 23.2 million. The feeble evolution of income, together with a slightly stronger increase of consumer prices, negatively impacted households' purchasing power, which declined by 0.7% in the second half of 2018. Trying to offset this disappointing evolution, Italian households have continued to reduce their propensity to save, which fell to 7.6% in Q4 2018.

From January to September 2018, households' financial wealth fell by EUR 12 bn, to EUR 4.100 bn, with a per capita loss of almost EUR 2.000. Italian consumers became extremely cautious in their spending decisions, with consumption stagnating in the last three quarters of 2018, as well as in their investment decisions, increasing the share of wealth invested on deposits, pension and insurance products.

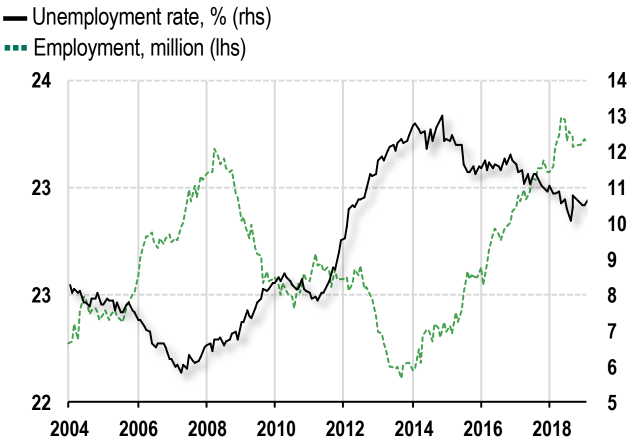
During the second half of 2018, economic and financial conditions of Italian firms slightly worsened, with profitability newly declining. Despite value added of non-financial corporations rose above EUR 800 billion, the highest value in the last twenty years, the gross operating surplus to value added ratio fell below 42%. The persisting uncertainty surrounding the overall economic scenario negatively impacted on business confidence, which has been declining for the last one year and a half, falling to the lowest level since the beginning of 2015. Investment continued to suffer a disappointing evolution, remaining almost 20 percentage points below the 2008 level.

1- GDP growth and inflation



Source: National accounts, BNP Paribas

2- Labour market



Source: Istat

A challenging fiscal balance

The Italian Government has approved the 2019 Economic and Financial Document. Higher public investment, the new income support scheme, the revision of the pension system and all the other measures approved or under discussion are estimated to have an overall positive effect on the economy, with an additional growth of 0.1%. In 2019, real GDP would grow by 0.2%, from +1% expected in the December 2018 Budget Law, while employment would decline by 0.2% and the unemployment rate would increase to 11%. The structural deficit is estimated to rise to 1.5%, from 1.4% in 2018, and the debt to GDP ratio would reach 132.6%.

The population is declining…

The financial crisis and the global recession that hit the world economy more than ten years now have produced long-lasting economic and demographic damages, through their impact on fertility and migration. The high levels of unemployment, which in many countries have characterized the years after 2008, have brought many couples to postpone pregnancies, so causing a higher than expected slowdown in the fertility rates. In Europe the effect of the global recession on fertility was particularly evident in Spain, Greece and Italy.

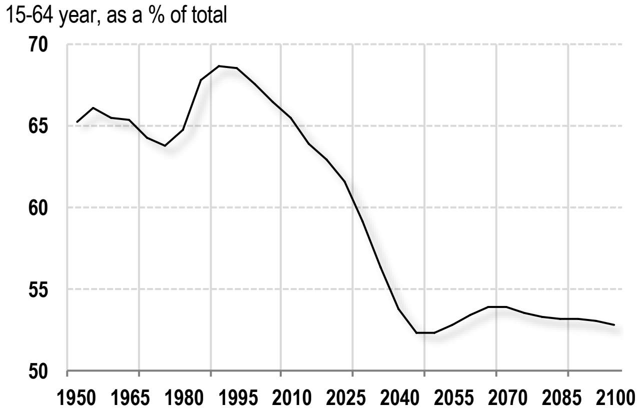
According to Istat, at the beginning of 2019, 60.4 million people were resident in Italy, a value that went down for the fourth consecutive year. Today the number of children per woman in Italy stands at 1.32, with values higher than the average in the Northern regions (around 1.37) and lower in the Southern ones (1.29 on average, with the lowest values in Basilicata, Molise and Sardinia, where the number of children per woman is close to unity). The decline in fertility has been accompanied by a decline in mortality, which has led to a significant increase in the life expectancy at birth, from 66.5 years in 1950-55 to 83.26 in 2015-20, one of the highest values in the world, after those of Japan (84,0 years), Switzerland (83.56), Spain (83.36).

… while life expectancy is growing

In turn, the increase in life expectancy has led to a significant increase in the proportion of the elderly people: the over-65 years old, in particular, that represented just 8.1% of the total Italian population in 1950, in 2019 cover up to 22.8%. In the same period, the weight of the 0-14-year-old class declined from 26.7 to 13.2%. According to some estimates by Istat and the Bank of Italy the old age dependency ratio (i.e. the ratio between the over-65s and the population between 20-64 years old) increased from 14.3% in 1950 to 37.8% in 2015 (last year available for international comparisons), the highest value in the world after that of Japan (46.2%). During the same period, the share of the working age population out of total, after having reached the maximum of 70% in the early 1980s, began to shrink, and according to recent forecasts it is expected to fall to a record low of 52.3% in 2050.

Due to these trends, the contribution of demography to Italian economic growth over the past 25 years has been negative. This can be seen by breaking down the per capita income into the product of three factors; product per person employed, employment rate and ratio between population in working age and total population. According to an estimate based on long time series between 1861 and 2016, in Italy, the most significant stimulus to the growth of per capita income came from productivity, especially during the 1950s and 1960s. The contribution of this variable became less relevant – and basically zeroed – since the beginning of the 2000s. The impact of the employment rate on growth was positive especially in the second half of the twentieth century, while the so-called "demographic dividend" (population in working age on the total), after having contributed in an important way to growth during the 1980s, since the early 1990s has become irrelevant.

3- Working age population



Source: Istat

A complicated future

According to recent Istat forecasts, Italy will see a gradual reduction in the number of "fertile age" cohorts (14-50) in the coming years, and an increase in elderly cohorts (over 65) which would lead to an increase in life expectancy at birth of male and female to 86.1 and 90.2 years respectively by 2065. By 2025 the population should remain stable, while it will suffer a substantial decline by 2045, when there would be 59 million residents, which would drop by a further 4.5 million (to 54.1) in 2065.

By 2025 the population in working age in Italy would fall to 63.2% of the total, from 64% in 2019. A drastic drop is expected by 2045 when working age population would be little more than half of the total (54.5%); the average age at that point would be close to 50 years. About one out of three residents in Italy in 2045 will be over 65 years old.

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