ITALY

TOWARDS AN UNCERTAIN RECOVERY

In Q2 2020, real GDP fell by 12.8%, dropping down to values recorded in the 1990s. A weakened domestic demand was the main driver of the recession, with households reducing their expenditure and investment falling by 15%. The contraction became widespread. The real estate sector sent mixed messages: in Q1 2020 prices went up while transactions experienced a sharp decline. Latest data have signaled a rebound of the economy, even if the scenario remains uncertain. The strength of the recovery will depend on the behaviour of businesses and households, which will in turn be affected by the evolution of the pandemic. In the real estate sector, both prices and transactions should experience a sharp decline by the end of the year. Transactions should only partially recover in 2022.

BACK TO THE 1990S

Italy was the first Western economy where the epidemic took hold. Severe restriction measures to contain the propagation of the Covid-19 were implemented some weeks before other countries. The limitation of people movements and of social interactions and the closure of many productive activities had a negative impact on the economy. In Q2 2020, at the height of the national lockdown, real GDP collapsed by 12.8% q/q (-5.5% in Q1 2020). Net exports contributed negatively (-2.4%), as exports declined more than imports (respectively -26.4% and -20.5%), The contribution of inventories was also negative (-0.9%). On annual basis, the economy contracted by 17.7%, dropping down to values observed at the beginning of the 1990s.

The economic contraction was widespread. In the manufacturing sector, which had already been experiencing a slowdown of activity since the beginning of 2018, value added declined by 22.2% in Q2 (-9.1% in Q1). In the first half of 2020, production fell by more than 30% in the transportation sector as well as in that of textile, clothes and shoes, while the areas of food and pharmaceutical products slightly declined. In the services sector, which was the only one to have recovered the losses of the previous two recessions, value added fell by 11% in Q2 (-4.7% in Q1). As a consequence of stringent restrictions on travel, turnover in accommodation and food services activities declined by more than 60%. According to current account data, international tourism receipts in Italy collapsed from EUR 12 billion in Q2 2019 to EUR 1.8 billion in Q2 2020, with the number of foreign travellers falling from 25.9 to 4.9 million.

SLUGGISH DOMESTIC DEMAND

In Q2, domestic demand was the main driver of the impressive drop in GDP, with a 9.5% negative contribution.

Private consumption fell by 6.7% in Q1 and 11.3% in Q2, accounting for more than 10 percentage points of the economic contraction recorded in the first half of the year. Italian consumers reduced their expenditure by more than EUR 45 billion, mainly cutting down on services and durable goods spending. Households economic conditions worsened further. Despite the introduction of a temporary prohibition to lay off workers, from Q4 2019 to Q2 2020, the number of persons in work declined by more than 750 thousand, with the employment rate in June falling to about 1.5 percentage points below the peak reached in 2019, while that of hours worked collapsed by almost one fifth. Consumer confidence data suggest that the propensity to save has remained high in Q2, after having increased above 12%, the highest value in the last fifteen years. Although declining from the record reached in April, the amount of household's bank deposits is still EUR 23 billion higher than in December 2019.

GROWTH AND INFLATION (%)

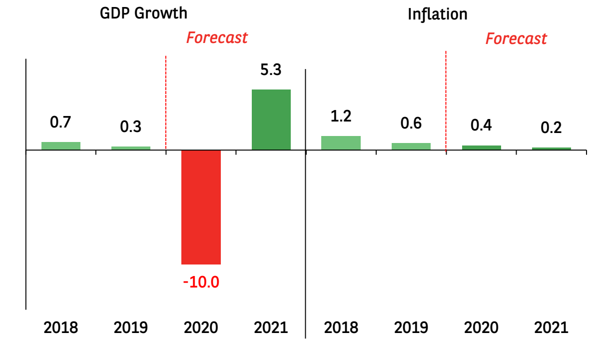

CHART 1 SOURCE: BNP PARIBAS GLOBAL MARKETS

LABOUR MARKET

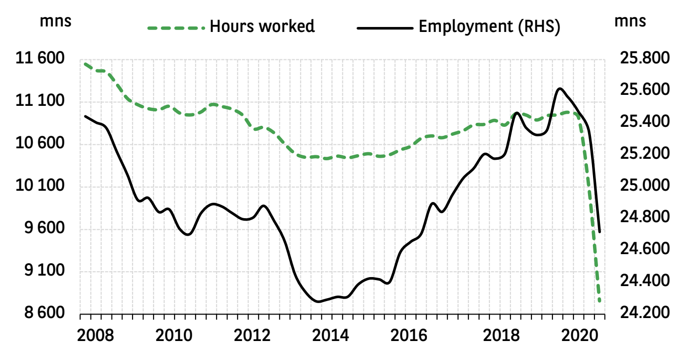

CHART 2 SOURCE: BNL CALCULATIONS ON ISTAT DATA

The recent dynamics of domestic demand also mirrored the huge decline in investment (-15% in Q2 and -7.5% in Q1), which subtracted about 4 percentage points from GDP. Since the beginning of the crisis, expenditure on gross fixed capital formation has declined by EUR 17 billion. From Q4 2019 to Q2 2020, investment in machinery and equipment fell by 25% and those in means of transport by 38%. Italian firms remained extremely cautious, owing to the persisting uncertainty about the economic outlook. According to trade balance data, in Q2, exports declined by 15% q/q, with means of transport, clothes, shoes and machinery contracting strongly, while sales abroad of food and pharmaceutical products ncreased slightly.

A STILL UNCERTAIN RECOVERY AHEAD

Latest available data have signalled a rebound of the Italian economy in Q3. The reopening of global trade supported exports, which increased strongly in May and June, after having collapsed in the previous two months. With the gradual reopening of activity, industrial production rose by more than 60% from the trough reached in April. The cancellation of the general quarantine and the easing of social restrictions supported domestic demand, with retail sales rebounding in May and June, though slightly declining in July. Besides, in June, the number of persons in work rose by 85 thousand.

The worst seems to be behind us, however the outlook remains extremely uncertain. After the Q3 rebound, a slowdown of activity is expected between the end of the year and the beginning of 2021. The strength of the recovery will depend on the behaviour of businesses and households, which will be determined by the evolution of the pandemic.

CONSTRUCTION SECTOR: VALUE ADDED

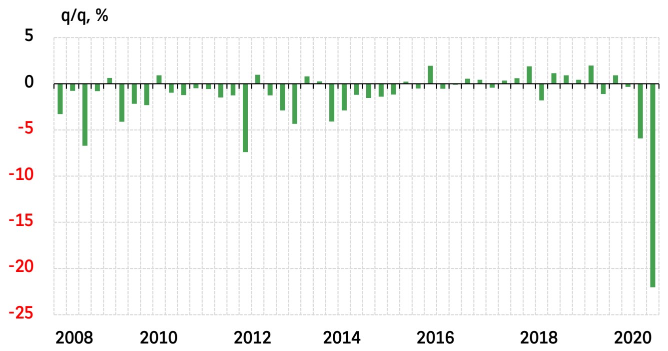

CHART 3 SOURCE: BNL CALCULATIONS ON ISTAT DATA

MIXED SIGNALS FROM THE REAL ESTATE SECTOR

In Italy, the real estate sector sends mixed messages. Between January and March 2020, according to Istat (*Istituto Nazionale di Statistic*a) estimates, the price of residential properties has increased by 1.7% yoy, the largest increase since Q2 2011. The performance is due both to newly built houses and (above all) existing ones whose prices have increased by 0.9% and 1.9% yoy respectively, showing a clear acceleration compared to Q4 2019. On a quarterly basis house prices have increased by 0.9%. The restrictive measures introduced in March to stop the spread of the Covid-19 pandemic did not have a significant impact on the prices of residential properties, whose sales were finalized before the outbreak of the sanitary crisis. In the quarters to come, however, house prices are expected to record a sharp decline.

On the whole the decline of house prices from 2010 (first year for which official data are available) to Q1 2020 amounts to 15.8%. This decline is due to a significant price decrease of existing homes, with prices 22.2 % lower at the beginning of 2020 than in 2010. Newly built houses prices were just 1.5% higher than eight years ago.

On the contrary, the measures introduced in March to stop the pandemic have drastically limited the possibility of signing new notarial deeds since March, leading to a sharp decline in real estate transactions. Between January and March 2020, residential property sales (non-seasonally adjusted) declined by 15.5% y/y (from -3.3% in the previous quarter) to about 117,000 deals (14,000 less than in the same quarter of the previous year). The decline was homogeneous in all areas of the country, with negative peaks in Milan (-19.3%), Naples (-19.5%) and Genoa (-19.2%). In Rome transactions declined by 14.8%. According to some preliminary estimates in Q2 2020, the decline in real estate transactions should have been much deeper than in Q1. By the end of the year, transactions should be less than 500,000 from 603,000 in 2019. The recovery in 2022 will probably be only partial.

The overall construction sector has suffered dramatically from the lockdown and the ensuing recession. According to Istat data, in Q2 2020 the value added in the sector declined by 22% compared to Q1 2020 and 26% with respect to the same quarter in the previous year.

As a consequence, the sector has suffered a decline in employment: in the first half of 2020, employment has decreased by 40,000 units compared to the same period in 2019, accounting for about 3% of the overall loss recorded by the entire economy in Italy over the same period.

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