Italy

A long lasting stagnation

The new Government has approved the update of the economic and financial document, planning to raise the deficit to 2.2% of GDP in 2020. The 2020 Budget Law is estimated to amount to EUR 30 bn. Some measures contained in the budget, such as the cut of the fiscal wedge, are expected to sustain the economy with a positive effect on growth, despite an increasing uncertainty. In Q2, GDP increased by 0.1 y/y, as stocks negatively contributed to the overall growth, while exports continued to rise. Domestic demand suffered from the mixed evolution of labour market and the further delay of the full recovery of the housing market.

A new Government coping with old problems

After the August political crisis, a new coalition between the Five Star Movement and the Democratic Party has been formed. The new Government, still chaired by Giuseppe Conte, has approved the update of the economic and financial document. In 2020, the Government plans to raise the deficit to 2.2%, from 1.4% expected under the current legislation. The 2020 Budget Law, which will be approved by the end of the year, is estimated to amount to EUR 30 bn. The deactivation of the safeguard clauses on indirect taxation will cost EUR 23 bn. Other measures contained in the budget, such as the cut of the fiscal wedge and the confirmation of business incentives for high-tech investment, are expected to sustain the economy. In 2020, GDP is now forecasted to increase by 0.6%, despite an increasing uncertainty.

A persisting stagnation

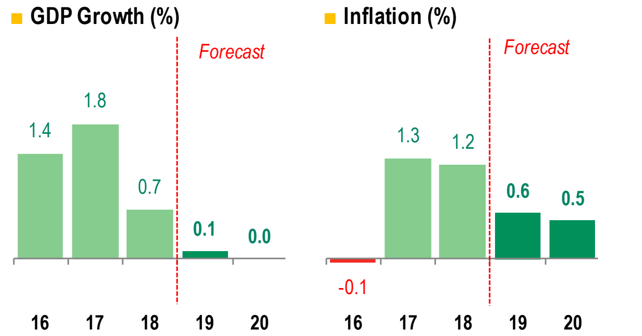
In the last one year and a half, the Italian economy has lost momentum. In Q2 2019, real GDP slightly increased (+0.1% both q/q and y/y). The breakdown of GDP data was mixed. For the fourth quarter in a row, stocks negatively contributed to the overall GDP increase (-0.2%), offsetting the positive support of domestic demand. Consumption continued to increase moderately (+0.1% q/q), also as a consequence of the still mixed evolution of labour market. In Q2, employment rose above 25.5 million, while the number of hours worked declined, (more than 500 million below Q1 2008). Capital expenditure rose by almost 0.4% q/q, as a result of a strong increase of investment in machinery and equipment, while construction investments declined.

In Q2, the contribution of net exports was positive, as exports rose more than imports. Although increasing, Italian sales abroad suffer from the uncertainty of the global outlook. According to trade balance data, in the first seven months of 2019, the value of exports rose by 3.2% thanks to a strong increase in the sector of pharmaceutical products (+28%), in that of food products and in that of textile products and clothes, while exports of means of transports declined by almost 5%. Italian firms benefited from a solid demand from the US (+9.2%) and from the UK (+8.9%), while sales to Germany significantly slowed (+1.1%).

The slowdown of manufacturing

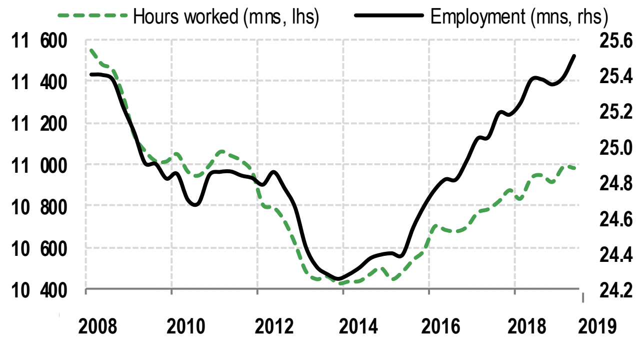
In Italy, the slowdown of economic activity mainly reflects the worsening of conditions in the manufacturing sector. In the last one year and a half, value added fell by 1.2%, to more than

1- Growth and inflation



Source: National accounts, BNP Paribas

2- Labour market



Source: Istat

9 percentage points below the 2008 level. In the first seven months of 2019, industrial activity contracted by almost 1%. Given the strong relationship with exports, the decline of production had broader repercussions in the sector of means of transport, in that of textile products and clothes, in that of metal products and in that of machinery and equipment.

In Q2, value added of services has continued to experience only a moderate evolution, with the annual growth rate slightly positive (+0.2%). Value added declined by 0.7% y/y in the sector of financial and insurance activities and by 1.1% in that of professional activities, while real estate activities rose by almost 1%. From April to June, the slow recovery of value added of construction came to a halt, declining by 1.1%.

Housing market: recovery further delayed

In Q1 2019, according to Istat estimates, the prices of residential properties decreased by 0.8% y/y. A distinctive feature of the long period of decline in the Italian real estate sector is the divergence in trends between the new homes and the existing ones. During the first quarter of 2019, the prices of existing homes fell by 1.3% y/y, the ninth consecutive decline in a row, while new housing prices rose for the sixth consecutive quarter.

On the whole, the decline of house prices from 2010 (first year for which official data are available) amounts to 17.2%, totally due to existing homes, whose prices at the beginning of 2019 were 23.7% lower than they were in 2010. Prices of newly built houses were just 0.8% higher than eight years before.

In the same period (2010-Q1 2019), house prices increased by 48% in Germany, in France by 8.6%, while in Spain they decreased by about 9%.

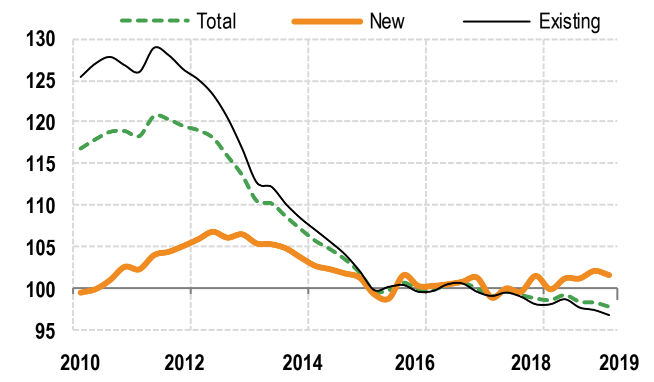
Should prices in Italy remain unchanged until the end of the year, 2019 would record a -0.8% with respect to 2018.

On the contrary, real estate transactions in Italy have been positive for sixteen quarters now. Between January and March 2019 residential property sales (non-seasonally adjusted) rose by 8.8% y/y (from 9.3% in the previous quarter) to almost 139,000 deals. Growth was positive in all areas of the country, in particular in the North East regions (+11.8% y/y) and in the Central ones (+10.7% y/y). Growth was particularly strong (+8.2% y/y) in the eight main Italian cities (in terms of resident population). In particular, double-digit increases were observed in Rome, (+11.9%), Milan (+11.3%), Genoa and Bologna (+15.2 and +12.9% respectively). In Palermo transactions slowed to +2% after having recorded a +18.5% at the end of 2018.

According to estimates by the Italian *Agenzia delle Entrate*, in 2018 (last data available) the combination of a declining price trend and an increase in sales led to a +5.2% in house market turnover, amounting to EUR 94.3 bn, 53 of which were concentrated in the Northern regions. Among the various areas, the largest increase was recorded in the North East (+9.4%), while in both the Central and Southern regions the increase in turnover barely reached +4%. In terms of turnover-per-housing unit, the drop amounted to 2,100 euros, mainly due to the reduction observed in the Center (-5,200 euros per unit) and in particular in Lazio (-6,250 euros per housing unit).

For the months to come, some qualitative analyses forecast an extension of the current sluggish phase: the monthly survey conducted last August by the Bank of Italy on the state of the sector shows that the share of experts reporting downward pressure on property prices remains stable compared to the previous months, and so does the margin of discount on offer prices. According to the same survey, the share of purchases financed by mortgages is growing, exceeding 80%, while the loan to property ratio is stable at 74.2%. The survey conducted by Nomisma (an Italian think thank) on household purchase intentions does not reveal substantial changes in the near future: in 2019 the number of households expected to buy a house is slightly decreasing compared to the previous year, while the percentage of those who claim to be looking for their first home is growing (to 74.8% from the previous 65.9%).

3- House prices trend



Source: BNL calculations on Istat data

Italy remains one of the countries with the highest percentages of home ownership in Europe: in 2017 (last data available) 72.4% of households owned their own place (a percentage just slightly less than that of 2010) compared to 77.1% in Spain (down from 79.8% in 2010) 64% in France and 51.4% in Germany. The Italian home ownership reaches 83% when referred to the richest households (those with an income over 60% of the median value) while in the case of those with the lowest incomes (less than 60% of the median) the rate drops to 52%.

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