# Italy

## A moderate recovery, in a mixed scenario

*In Q1 2019, Italy came out of recession. The overall scenario remained mixed. The GDP annual growth rate was negative. Imports strongly declined and exports slightly increased, with a positive contribution of net exports. Both households and firms remained cautious, postponing consumption and investment. Cyclical indicators suggest a disappointing evolution in coming months, making more challenging the fulfilment of public finance objectives. The Italian Government approved an update of the 2019 Budget, with the public deficit around 2% of GDP, reaching an agreement with the European Commission and avoiding the disciplinary procedure.*

In Q1 2019, Italy partly recovered from a mild recession in the second half of 2018. Although real GDP rose by 0.1% q/q, the annual growth rate was negative (-0.1%), for the first time since 2013. The breakdown of GDP data was mixed. The 0.5% net exports contribution mainly reflected the contraction of imports (-1.5%). Italian sales abroad rose by 0.2% q/q. In Q1, domestic demand added 0.2% to the overall growth, while stocks subtracted 0.6%. Value added of construction rose by 2.4% q/q, despite activity remaining feeble, as signalled by the evolution of new building permits. Value added of services declined by 0.2% q/q, with a significant contraction in the financial sector and in that of professional activity, while manufacturing recorded a slight increase.

### The immediate outlook is gloomy

Despite the moderate recovery in Q1, expectations remain uncertain. Business confidence worsened, hovering around the lowest level in the last four years. Italian firms remain extremely cautious. In Q1 2019, the 0.6% increase in investment was the result of higher expenditures on construction, while that on machinery and equipment and that on means of transport declined by 2.2% and 5% q/q. Production fell both in March and in April, with a bigger decline in machinery and equipment sector, in metal products and in the transport sector.

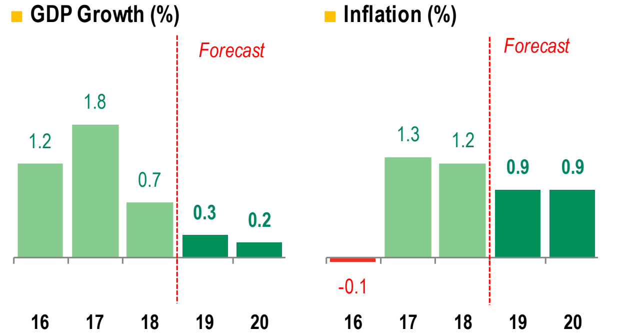
The worsening of confidence also affects Italian consumers, with a negative effect on private spending. This happened despite signs of improvement in the labour market, with the unemployment rate falling to 9.9% in May. In Q1, despite a 0.9% increase of purchasing power, consumption rose by only 0.1% q/q, as households increased their savings rate to 8.4%.

As cyclical indicators disappoint, it will be more challenging for the government to reach its public finance objectives. In June, the European Commission stated that Italy was experiencing excessive macroeconomic imbalances. The Italian Government approved an update of the 2019 Budget, reaching an agreement with the Commission and avoiding the disciplinary procedure. In 2019, the public deficit is expected to be around 2% of GDP, about EUR 7 bn lower than previous estimates, benefiting from higher revenues and lower expenditures.

### Firms have improved their situation over the long run

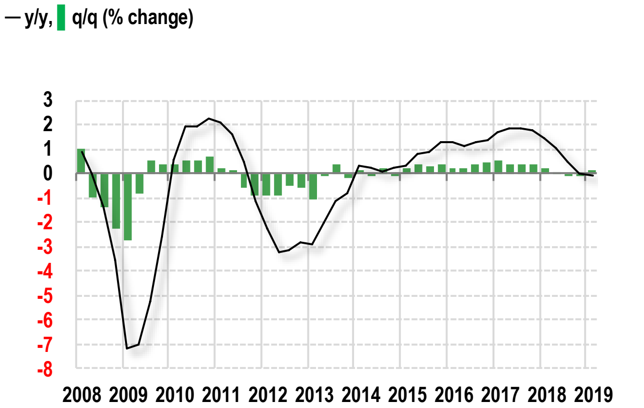
Economic and financial conditions of Italian firms have improved. In 2018, the leverage ratio was around 40%, about 9 percentage points below the 2011 level. Benefiting from tax incentives, firms made significant new capital injections, while cutting debts. The improvement of the financial structure was also the result of the cleansing which occurred during the crisis leading to the disappearance of weaker companies. In 2018, value added of firms reached the highest level in the last twenty years. Besides, firms benefited from lower interest expenditure, as the rise of Government bond yields has not yet impacted the cost of credit. In 2018, the average cost of financial debt was 1%, from more than 6% in 2008. Italian non-financial corporations also took advantage from the decline of tax payments, with a saving of more than EUR 20 bn with respect to 2007. Despite these improvements, the recovery of

**1- GDP growth and inflation**




*Source: National accounts, BNP Paribas*

**2- Italy: real GDP**




*Source: Istat*

profitability is still disappointing, as labour costs increased more than value added. In Q1 2019, the gross operating surplus to value added ratio declined to 40.7%.

## Tourism: a support for the economy

In 2018, international tourism turnover amounted to EUR 1,226 bn, +2.9% compared to 2017. United States continued to be the country with the highest receipts. The market share of Italy grew slightly, reaching 3.4%, the sixth highest value in the world after those of US, Spain, France, Thailand and the United Kingdom. In 2018 total expenditure by foreign travellers to Italy rose by 6.5%, amounting to about EUR 41.7 bn (a little slowdown after +7.7% in 2017) while the number of visitors increased by 3.7%. International tourism receipts account for 2.4% of GDP in Italy, 8% in Greece and Portugal, 5% in Slovenia and Spain. The Italian value is lower than the average of both the European Union and the Euro area. According to balance of payments data, in Italy international tourist receipts account for about 40% of total exports of services and about 7% of total exports of goods and services. The balance of travel, which is structurally positive, reached EUR 16.2 bn. The surplus of Italy's tourism balance in relation to GDP is higher than the European average and, among the main Euro area countries, it ranks second after the Spanish one.

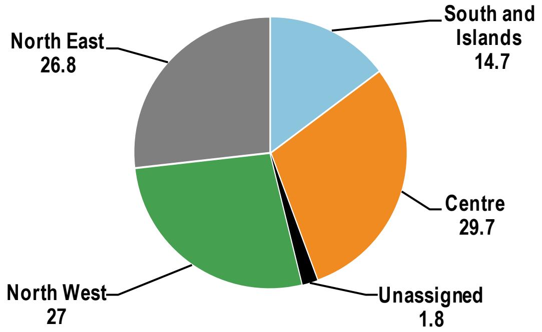
The growth of the tourism sector in Italy has been taking place since the end of the international financial crisis: valued at current prices, in 2018 international tourism receipts were almost 50% higher than in 2009, while spending of domestic residents travelling abroad was 25% higher than in 2009. Overall, in 2015 (the last year for which these data are available), tourism-related industries in Italy represented 5.9% of the total value added of the country.

Visitors from the Euro area contributed the most to 2018 growth, both in terms of number and tourism receipts. Germany, along with the United States and France, is still the largest importer of Italian tourism services. Spending by German tourists in Italy rose by 8.2% y-o-y, those from France and United Kingdom by 9% and 17.2% respectively. These three countries generate over a third of total Italy's tourist revenues. Outside the EU, US is the largest importer of tourist services from Italy.

The regions of the center of Italy, with a higher tourist appeal due to the presence of a large number of art cities, are still the favourite destinations of foreign travellers, with almost 30% of total arrivals in 2018. The Southern regions and the islands reached a 15% share of total arrivals from abroad. This last area, despite the progress made in recent years, still presents a gap between international tourism revenues and the "tourism potential". In the south of Italy and the islands are indeed located about three quarters of the Italian sea coasts and national natural parks; these regions also host a large number of museums and archaeological sites.

In 2018 foreign travels of Italians amounted to 65.7 million, with an expenditure of EUR 25.5 bn (+1.8% and +3.8% respectively compared to 2017). The expenditure of Italian travellers who visited other countries in the Euro area grew more than the average in three countries: Greece, Spain and Germany. Among the destinations outside the European Union, the trend in spending was particularly strong in North America, and especially in the United States.

**3- Foreign travellers expenditure**
(2018; % of total)




*Source: BNL calculations on Bank of Italy data*

The tourism sector in Italy is characterized by the presence of small and very small firms. According to Istat in 2016, around 97% of firms in this sector employed less than 10 persons (compared to 95% in the total industry and services). Firms with 20 or more employees only represent 0.9% of the total (compared to 1.8% in industry and service sectors). However, the presence of multinational hotel chains and other tourist services, including transport services, supplied by foreign companies operating in Italy is significant. Foreign invested enterprises in the tourism sector in Italy employ 6.1% of total employees in the sector and produce about 14% in terms of both the added value and the turnover. In the 2012-2016 period, firms in the tourism sector recorded a positive performance: their value added increased by 12.5% in nominal terms, against a change in the broader service sector of +11.2% and of 8.8% in the total industry and services. The increase in the value added in the tourism sector was due to a marked decline in the costs, rather than to an increase in firm's turnover.

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