

## THE WAY TO RECOVERY GETS LONGER

In 2020, real GDP fell by 8.9%, with almost 2.5 million of full-time equivalent jobs lost. The decline in consumption was the main driver of the recession, accounting for three fourths of the economic downturn. Stagnating incomes and the lack of confidence increased households' propensity to save. The services sector was the most severely affected by the crisis, with value added declining by 8.1%, while manufacturing benefitted from the moderate recovery of exports. The problems raised by the pandemic combined with -and worsened- structural issues that had been slowing down the country's economic growth up to now. In the years to come it will be hard to implement a solid growth pattern without decisive interventions that would foster innovation and productivity.

## HOUSEHOLDS WITH AN INCOME AND CONFIDENCE PROBLEM

Following the rebound in Q3 2020 (+15.9%), real GDP fell by 1.9% in Q4. The second wave of infections required new restrictive measures on mobility and economic activities. Both foreign and domestic demand made a negative contribution. Exports rose less than imports, while the contraction of consumption more than offset the increase in investments and the positive contribution of public expenditure.

In 2020 as a whole, real GDP declined by 8.9%. The decline in consumption was the main driver of the recession, accounting for three fourths of the GDP decline, much more than during the two previous recessions. Private spending fell by 10.7%, with a 6.5% negative contribution to the contraction of GDP. Italian households suffered both from the disappointing income evolution and the deterioration in confidence. In 2020, almost 2.5 million of full-time equivalent jobs were lost. From January to September, households' gross disposable income declined by more than EUR 20 billion and the propensity to save doubled, following the effects of restrictive measures and consumers adopting a more cautious behaviour.

In 2020, Italian households reduced spending on entertainment and culture, transports, restaurants and hotels, while increasing purchases on food and beverages, communication and house maintenance and services. Despite the pandemic, spending on health, which includes medical products, appliances, equipment and hospital services, declined by 6.2%. Online purchases, which accounted for 4% of total retail sales in 2019 (8% in France and 11% in Germany), rose by 35%.

## 2020: THE SEVERE CRISIS OF THE SERVICES SECTOR

The services sector, the only one that in 2019 had recovered the decline recorded during the previous two crises, suffered much more than the rest of the economy. In 2020, services value added declined by 8.1%, with a 6% negative contribution, with the number of full-time equivalent employees falling by 11%, almost 2 million less than in 2019.

The recession became widespread, but with differences among sectors. Information and communication value added rose by 1.9%, while that of financial and insurance activities fell by 2.6%. Entertainment & recreation and transportation & storage value added declined by about 15%. The hotel and catering sector was the most severely affected by the crisis: value added collapsed by 40%, with half a million of full-time equivalent jobs lost. Restrictions on cross-border travel impacted the tourism industry. Foreign travellers in Italy declined from 96.2 million in 2019 to 39 million in 2020, with expenditure contracting from EUR 44.3 billion to EUR 17.4 billion.

### GROWTH AND INFLATION (%)

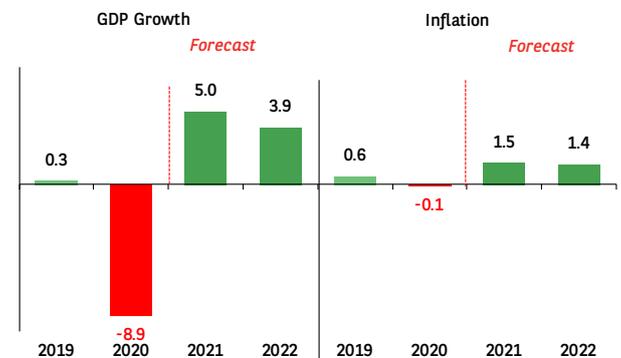


CHART 1

SOURCE: BNP PARIBAS GLOBAL MARKETS

### CONTRIBUTIONS TO GDP GROWTH

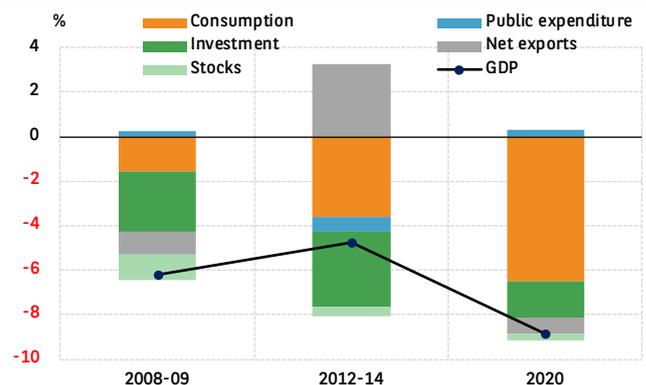


CHART 2

SOURCE: BNL CALCULATIONS ON ISTAT DATA

## A MORE RESILIENT MANUFACTURING SECTOR

In 2020, manufacturing value added declined by 11.4%, mainly as a result of the strong contraction recorded in the first half of the year, while industry stagnated in Q4. The number of full-time equivalent employees in manufacturing declined by 376,000 (-11%), falling to about 3 million.



Textile, clothes and shoes sectors continued to be strongly hit by the crisis: value added declined by almost 25%, with a severe loss in employment. The contraction was milder in the food and beverages sector as well as in that of intermediate goods, such as chemical products and rubber and plastic products. Manufacturing benefitted from the moderate increase in exports. According to trade balance data, the value of Italian sales abroad has almost totally recovered the decline of the first part of the crisis.

## NEW PANDEMIC, OLD PROBLEMS

In Italy, the problems raised by the Covid 19 pandemic combined with -and worsened- structural issues that had been slowing down the country's economic growth up to now (high public debt, a fragmented production system, low investment in education, R&D and innovation). In the years to come it will be hard to implement a solid growth pattern without decisive interventions that would foster innovation, productivity and sustainability.

At the outbreak of the Covid-19 pandemic, the latest data available showed a very fragmented productive system in Italy: micro-enterprises accounted for 95% of all Italian firms, employing 43.7% of the working population and contributing to 27.5% of the value added. In comparison with other European countries, Italian firms are smaller: they employ on average 4 persons compared to 4.5 in Spain, 5.6 in France and 11.9 in Germany. Firms' size affects both their productivity and propensity to invest. In Italy, labour productivity in a micro-enterprise amounts to EUR 30,000, vs EUR 72,680 in a large one. In the manufacturing sector, a large firm invests about EUR 14,500 per employee and per year on average, vs EUR 3,600 euros for a micro one. The prevalence of micro- and small-sized firms, and the subsequent low productivity and investment propensity, result in a scarce use of qualified personnel and digital infrastructures by Italian firms. According to the most recent Istat data, only 5.1% of the persons employed in the productive system have tertiary education or an academic diploma.

The use of digital infrastructures in Italy is strongly correlated to the firms' size: the so-called "digitally mature" companies (i.e. firms that make an integrated and advanced use of the available technologies) are mostly large firms: 23% of firms with over 500 employees, 15% of those which employ 250-499 persons and 10% of those with 100-249 employees may be defined as "digitally mature". Among small enterprises, the percentage of "digitally mature" ones does not exceed 2.3%.

The structural limits of a part of the Italian productive system also affected the capacity of adaptation and the effectiveness of the response to the challenges posed by the Covid-19 pandemic. According to a recent analysis conducted by Istat on the reaction of Italian business to the current crisis, it is possible to distinguish five clusters of firms: 1. "Static in crisis": companies that are heavily impacted by the health emergency and have not adopted specific reaction strategies; 2. "Static resilient": companies that have not implemented reaction strategies because they have not suffered from significant negative effects; 3. "Proactive in distress": companies hit by the crisis but which have put reaction strategies in place; 4. "Proactive in expansion": companies barely affected by the crisis that have not altered their previous development pattern; 5. "Proactive advanced": companies affected by the crisis, but which increased their investments compared to 2019.

At the end of 2020, about 75% of Italian companies with at least three employees had not defined any strategic framework to deal with the consequences of the crisis in the medium-long term, and about one third showed signs of crisis or distress. The five groups exhibit a strong

ITALY: THE PRODUCTIVE SYSTEM BY FIRMS' SIZE (% OF TOTAL)

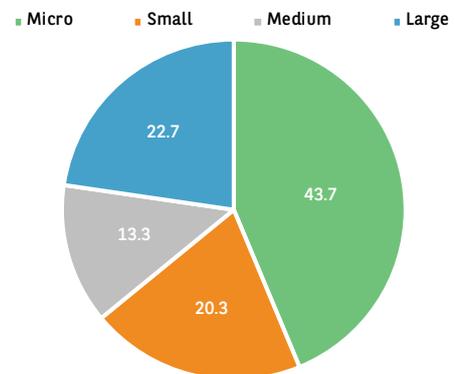


CHART 3

SOURCE: BNL CALCULATIONS ON ISTAT DATA

internal homogeneity in terms of firm size: the «static in crisis» are on average much smaller than the «proactive advanced» ones (6.5 and 47.2 employees respectively).

Even though firms' reaction to the crisis largely depends on the different impact that the lockdown measures had on the different sectors, it is obvious that the least productive units (with higher labour costs, a low-skilled workforce and a domestically-oriented business) suffered the most by far. Among the "proactive advanced" firms, the value added per person employed more than double that in "static in crisis" companies (about EUR 73,000 against EUR 33,000) and their workforce is on average more educated. As far as firms' activity is concerned, the most reactive companies are more numerous in the industrial sector, in particular chemicals, pharmaceuticals, electronics and beverages industries. In the services sector the firms that better reacted to the crisis are mainly those operating in the telecommunications, information technology, finance and insurance areas. Among the companies that suffered the most because of the crisis, regardless of the sector to which they belong, a high percentage did not make any structural investments (such as in R&D, human resources, technologies and digitization, human capital and training, internationalization, social responsibility and environmental fields) and therefore did not adopt any strategic changes to face the crisis.

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