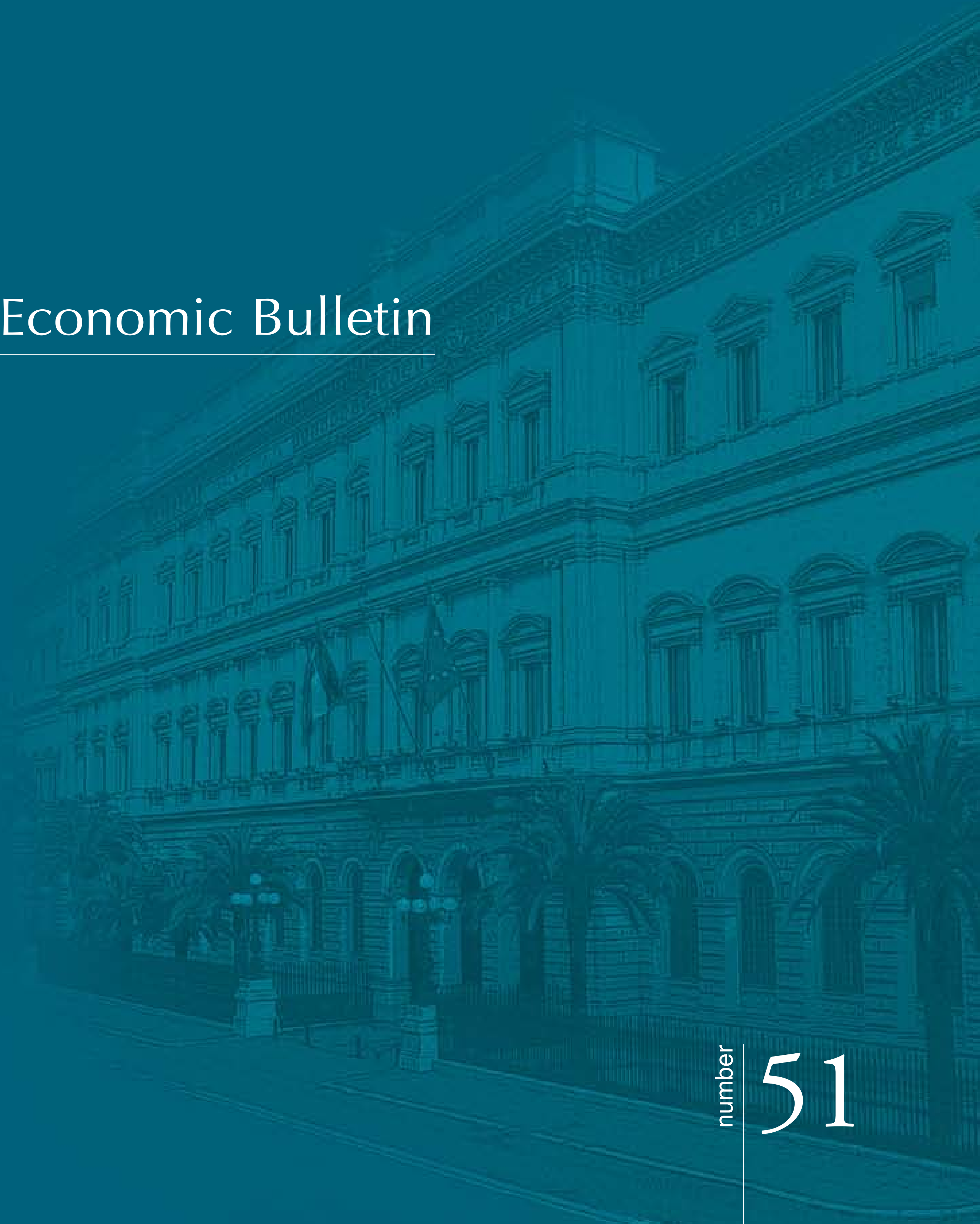
BANCA D'ITALIA
EUROSISTEMA

Economic Bulletin



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SYMBOLS AND CONVENTIONS

Unless indicated otherwise, figures have been computed by the Bank of Italy.

In the following tables:

–	the phenomenon in question does not occur
....	the phenomenon occurs but its value is not known
..	the value is known but is nil or less than half the final digit shown
::	the value is not statistically significant
()	provisional; estimates are in italics

1 OVERVIEW

The crisis of confidence has spread from the financial markets to the decisions of consumers and enterprises

After spreading rapidly to the whole financial sector and the rest of the world, in the last few months the crisis that broke out in the summer of 2007 in the US mortgage market has affected the real economy and is now influencing consumption, investment and production choices. GDP dynamics have deteriorated sharply in the leading economies and the emerging countries have also begun to suffer.

The interventions of governments and monetary authorities have prevented even more dramatic developments

With the collapse of the investment bank Lehman Brothers in September and the emergence of fears of insolvency at other intermediaries, concern about the possible collapse of financial systems intensified, world stock indices incurred heavy losses, and a significant and disorderly tightening of credit conditions loomed. Governments and central banks reacted in co-ordinated fashion at international level, ensuring a continuous flow of funds to financial institutions and the real economy, increasing bank deposit guarantees, and in many countries strengthening the capital of intermediaries in difficulty. Measures of this sort have been adopted in Italy too. This action has prevented the paralysis of financial markets. The risk premiums on interbank loans, which had soared in September and October, decreased between November and December, although they remain at historically high levels.

Cyclical indicators are negative in all the main economies and economic policies are becoming expansionary

The signs of a small and partial easing of financial tensions are counterposed to a rapidly deteriorating cyclical situation in all the main economies. In the United States, where the property market continues to languish, business and consumer confidence has diminished further. The major forecasting organizations estimate that GDP contracted sharply in the last quarter of 2008 and will continue to decline in 2009. Japan is also in recession. In China and India the pace of growth in output is declining. The weakening of economic activity has been accompanied by a brusque fall in the international prices of raw materials, especially energy, and these prices have returned to their level at the end of 2004. This has led to a pronounced slowdown in consumer price inflation in the major economies. According to the leading forecasting organizations, the slowdown in price inflation will continue in 2009, although without turning into deflation. As inflation came down and cyclical conditions worsened, there was a sharp reduction in official interest rates in the United States (where they have been brought down to virtually zero), the euro area and other countries. Important public finance programmes to support aggregate demand are planned or are already being drafted.

The euro area has gone into recession

In the euro area the fall in foreign demand and the crisis of the financial markets had its initial impact on firms' investment decisions. In the third quarter of 2008 there was a further contraction in GDP, amounting to nearly one percentage point on an annual basis. After contracting in the preceding months, in October and November the area's industrial production fell by 1.6 per cent. The €-coin indicator turned negative in November. Business and household confidence are both at historically low levels. There is growing fear of a serious deterioration in the labour market in the year that has just started. The main private-sector forecasters estimate that GDP will contract by more than 1 per cent on average in 2009.

After the coordinated reduction in October, the European Central Bank lowered its reference rates further in its meetings at the beginning *of November and December, by 50 and 75 basis points respectively. Short and medium-term inflation expectations, which worsened in the summer as energy commodity prices rose, have fallen back drastically in the last few months.*

Italy, too, in recession

Italy's GDP, which fell by 1.6 per cent on an annual basis in the second quarter of 2008, contracted by 2 per cent in the third, reflecting a slump in business investment, a decline in exports and stagnant household consumption. The deterioration in cyclical conditions grew more pronounced in the closing months of the year: the index of industrial production is estimated to have fallen by about 6 per cent in the fourth quarter on a calendar and seasonally adjusted basis. Firms' confidence has dropped to historically low levels; recent surveys of businesses indicate that investment will remain weak during this year, in a context of widespread pessimism over the outlook for demand. After more than a decade of growth, employment ceased to expand in the third quarter of the year; recourse to the Wage Supplementation Fund increased in the final part of 2008.

Bank lending slows

The rate of growth in bank lending remains high but is coming down, reflecting the prudence that the recession has induced in firms' and households' demand for credit. The slowdown in lending is sharper for small firms. In addition, the periodic credit survey conducted by the Bank of Italy signals a progressive tightening of lending conditions; according to other surveys, the percentage of firms finding it difficult to obtain financing is increasing. In Italy as in other countries, banks are adapting their balance sheet assets to the difficulty and increasing cost of funding. The abatement of the strains in the money and financial markets and the capital strengthening of banks, facilitated by the measures taken by the Government and the Bank of Italy, can help to ease lending conditions. The data for the first two thirds of December show that the recent reductions in official rates are gradually being transmitted to bank lending rates.

The general government borrowing requirement and debt are rising

The general government borrowing requirement and debt turned upwards in 2008. Both aggregates increased by approximately one percentage point with respect to GDP. The ratio of the public debt to GDP also apparently rose significantly. Tax revenue was basically unchanged. The impact of the economic downturn on revenue will be felt more strongly in 2009. The budget for the years from 2009 to 2011 approved by Parliament last summer has been supplemented, without substantially affecting the planned balances, by the Finance Law for 2009 passed in December and the decree law to sustain the economy approved by the Government at the end of November. The decree law raises €5.6 billion for 2009 and allocates it to income support for low-income households, tax reductions for firms and stimulus to investment activity.

Economic activity in Italy is projected to fall further in 2009 and stabilize in 2010

In the six months that have passed since our forecasts for the Italian economy were published in the Economic Bulletin *of last July, the global crisis has spread and intensified and the growth prospects of the world economy have deteriorated markedly. We now predict that these developments will cause the current recession to continue in Italy this year; GDP is likely to return to modest growth only in 2010, when it will benefit from a recovery in international trade. We estimate, taking account of the Government measures to support demand, that GDP will fall by an average of 2 per cent in 2009 and return to growth of 0.5 per cent in 2010. This forecast takes into account the sharper-than-expected fall in industrial production in the last part of 2008, and in particular the figure for November released on 14 January.*

Among the components of demand, industrial investment, squeezed by persistently negative or in any case highly uncertain prospects for foreign and domestic demand, is likely to be especially penalized.

Inflation is forecast to fall sharply in 2009 and remain well below 2 per cent in 2010 as well

Consumer price inflation is expected to fall to an average rate of 1.1 per cent in 2009, before edging back up to 1.4 per cent in 2010, reflecting mainly the decline in the prices of raw materials in the second half of 2008 and the forecast of their moderate recovery in the two *following years. After the temporary acceleration recorded in 2008 with the conclusion of many contract renewals, employee earnings are expected to slow in 2009; unit labour costs should benefit accordingly.*

The forecast is subject to conflicting uncertainties

Output performance could be even worse if the risks of a further weakening of the global economy were to materialize. A less negative scenario could be opened up by full and effective application of the plans already made and currently being defined in the major economies to stabilize financial markets and support aggregate demand.

There is broad agreement that in exceptionally adverse conditions economic policies must take every possible initiative to ease and shorten the recession, so long as the medium and long-term sustainability of the public finances is not compromised. This ultimately depends on the prospects for reactivating the process of economic growth.

2 THE WORLD ECONOMY

2.1 THE FINANCIAL MARKETS AND ECONOMIC DEVELOPMENTS

The financial crisis and its repercussions on real economies are intensifying

The crisis that engulfed the international financial markets from the summer of 2007 onwards and intensified last September after the collapse of the investment bank Lehman Brothers, causing trading in interbank markets to seize up and share prices to plunge, is having an impact on world economic activity. Almost all of the main advanced economies suffered a decline in GDP in the third quarter of 2008 and a further deterioration in activity in the last few months of the year owing to the precipitous fall in the prices of financial assets, the reduction in the availability of credit, the decline in household and business confidence and, in some countries, a slump in the property market. The crisis affected the emerging economies through the outflow of foreign capital following the liquidation of equity and bond investments by international banks and investment funds. These developments highlighted the vulnerability of countries with large external deficits, which suddenly became difficult to finance. As yet, there has been no clear sign of a lasting reduction in balance-of-payment disequilibria between the main areas, although the recent fall in oil prices will help shrink them in the short term. The projections for 2009 from the international organizations and private forecasters polled in December by Consensus Economics, which have been revised downwards repeatedly, point to a contraction in GDP in the main advanced countries and an abrupt slowdown in emerging economies (Table 1). The current forecasts from some of the leading private analysts are far more pessimistic.

Table 1

Selected macroeconomic projections
(percentage changes on the previous year)

	OECD			Consensus Economics (1)	
	2007	2008	2009	2008	2009
GDP					
Advanced countries					
Euro area	2.6	1.0	-0.6	1.0	-0.9
Japan	2.4	0.5	-0.1	0.4	-0.9
United Kingdom	3.0	0.8	-1.1	0.8	-1.5
United States	2.0	1.4	-0.9	1.2	-1.3
Emerging countries					
Brazil	5.7	5.3	3.0	5.5	2.1
China	11.9	9.5	8.0	9.3	7.8
India (1)	9.0	7.0	7.3	6.9	6.3
Russia	8.1	6.5	2.3	6.7	2.9
Consumer prices					
Advanced countries					
Euro area	2.1	3.4	1.4	3.3	1.4
Japan	0.1	1.4	0.3	1.6	0.1
United Kingdom	2.3	3.7	2.7	3.6	1.2
United States	2.9	4.3	1.6	4.0	0.3
Emerging countries					
Brazil (2)	4.5	6.3	5.3	6.2	5.0
China	4.8	6.1	3.0	6.1	1.7
India (1)	6.2	10.3	6.0	8.1	6.2
Russia (2)	11.9	13.6	7.5	13.8	10.6
World trade	7.0	4.8	1.9	–	–

Sources: National statistics, *OECD Economic Outlook*, December 2008; Consensus Economics, December 2008.
(1) Changes in the course of the financial year, beginning in April of the year indicated and ending in March of the subsequent year. – (2) Changes from December to December.

The monetary and fiscal authorities took strong counteraction

The actions taken to counter the financial crisis followed the lines set out by the G7 Finance Ministers and central bank Governors on 10 October. Economic policymakers in the industrial countries adopted significant measures to recapitalize banking systems (see the box “The recent measures to support the banking system in the main industrial countries"); the central banks intervened to bolster the liquidity of the money markets and facilitate the securitization of various types of loan to households and firms. As inflationary pressures eased, mainly owing to the fall in commodity prices, and against the background of a deterioration in the real economy, the central banks also eased monetary conditions considerably. In many countries the authorities announced extensive plans to support economic activity. The International Monetary Fund (IMF) offered financial assistance to some emerging economies affected by the halt in flows of foreign finance, allocating funds totalling about $45 billion.

THE RECENT MEASURES TO SUPPORT THE BANKING SYSTEM IN THE MAIN INDUSTRIAL COUNTRIES

From last October onwards, the actions of the governments of the major industrial countries to counter the growing difficulties of financial institutions and the resulting crisis of confidence have become more intensive and diverse; efforts at international coordination have multiplied. On 3 October the US Congress approved the Troubled Assets Relief Program (TARP), which authorizes the Treasury to purchase or guarantee impaired assets for which there is no liquid market (see the box "The crisis of some US financial institutions and the support action of the authorities" in *Economic Bulletin*, no. 50, October 2008). In subsequent days, partly owing to the continuous deterioration in international financial conditions, it came to be firmly believed that in order to restore stability to the markets and bolster banking activity more direct and rapid coordinated action by the leading countries was needed to strengthen the capital of the banking system and the ability to raise funds in the market.

The stages in the coordination effort – At the G7 summit in Washington on 10 October 2008 agreement was reached on the underlying principles for the measures to be adopted in each country: to support financial institutions of systemic importance; to ensure continuity of credit flows to banks, where necessary by providing temporary guarantees on a wide range of short and medium-term liabilities; to increase the existing guarantees on bank deposits; and to strengthen the capital of institutions in difficulties by means of comprehensive programmes for state participation in their capital.

Immediately after the summit, on 12 October, the Heads of State and Government of the euro-area countries agreed a common plan of action aimed at: ensuring appropriate liquidity conditions for financial institutions and facilitating their funding by means of state guarantees or insurance instruments; providing financial institutions with additional capital resources, disbursed by the public sector subject to adequate restructuring plans and any necessary measures to take account of the responsibility of shareholders and executives, while at the same time fostering the raising of private capital; ensuring sufficient flexibility in the application of accounting rules; and improving cooperation between the European countries by reinforcing existing procedures for the exchange of information. The European Council of 15 and 16 October endorsed the plan of action previously adopted by the euro-area countries, extending it to all the countries of the European Union. On 2 December the Ecofin Council estimated the resources made available by the measures already adopted in the form of government guarantees at €1,800 billion and those of the recapitalization programmes at €280 billion.

On 8 December the European Commission published guidance for the recapitalization of banking systems in order to ensure that state aid for the banks does not give recipient institutions an undue competitive advantage. In the case of "fundamentally sound" banks (which will receive temporary support in order to foster lending to households and firms) recapitalization will have to take the form of the subscription by the public authorities of liabilities issued by the banks and offering an "appropriate" yield: the Commission recommended yields of between 7 and about 9 per cent, depending on the characteristics of the instruments. However, higher rates of remuneration are also considered appropriate to encourage a swift exit by the state investor. For "distressed" banks (those facing the risk of insolvency), however, stricter requirements should apply; either a comprehensive restructuring plan or a liquidation plan will have to be presented within six months of recapitalization.

The measures adopted in the major economies – In the United States, on 14 October the guarantees provided by the Federal Deposit Insurance Corporation (FDIC) were temporarily extended without limits as to amount to some types of senior debt issued by banks before 30 June 2009, including interbank loans and commercial paper, and to non-interest-bearing deposit transaction accounts (until the end of 2009). On the same day the Treasury announced that it intended to take steps under the TARP to recapitalize financial institutions by purchasing preferred shares; by the end of December operations amounting to about $250 billion had been completed, largely involving the country's nine largest banks, whose participation in the programme was immediate; a further $20 billion was earmarked to support the auto industry. On 23 November the Citigroup banking group, which was facing mounting difficulties, agreed a substantial package of measures with the US authorities that provided for partial coverage of any losses on a portfolio of assets worth a total of about $300 billion backed by residential and commercial mortgages. The first $29 billion of losses would be borne by the bank itself, while the Treasury (via the TARP) and the FDIC would bear further losses up to $15 billion, in exchange for which they received preferred shares worth $7 billion. The remaining risk would fall almost entirely on the Federal Reserve, which would grant a loan guaranteed only by the assets in the portfolio in question. Citigroup also received a fresh capital injection of $20 billion, again financed with TARP funds, in addition to the $25 billion received previously.

In the United Kingdom, on 7 October the Government announced a sweeping plan to recapitalize the banking system, under which it undertook to purchase, via a specially created fund, a minimum of £50 billion in ordinary or preference shares in banks and building societies. Participating institutions will also be offered a temporary guarantee (for a period of up to three years, with the possibility of extension) on newly issued senior debt instruments, commercial paper or certificates of deposit; the authorities expect this measure to cover instruments worth about £250 billion. The country's eight largest banks have undertaken so far to make capital increases amounting to about £51 billion, partly using government funds (£37 billion) and partly by raising capital in the market. The Government has already subscribed new ordinary and preference shares worth £20 billion in Royal Bank of Scotland, thereby acquiring a majority shareholding of around 60 per cent, and plans to inject £17 billion into the capital of the bank resulting from the merger of HBOS and Lloyds TSB.

In Germany on 13 October the Federal Government set up a special fund of up to €100 billion that will be able to recapitalize financial institutions and, where necessary, acquire problem assets or guarantee them until maturity, up to a maximum of €80 billion; the remaining €20 billion will be used to offer guarantees on newly-issued financial instruments worth in total up to €400 billion. So far, two large German banks, among others, have had recourse to the fund: Commerzbank has received two instalments of fresh capital totalling €18.2 billion and a guarantee on new liabilities of €15 billion, and the Hypo Real Estate group has received guarantees on liabilities totalling €65 billion, of which €45 billion from the special fund.

On 12 October the French government unveiled a plan in which it undertook to guarantee up to €320 billion of securities issued by Société Française de Financement de l'Économie (SFFE) before 31 December 2009 at market rates for terms of between one and five years. The SFFE can grant loans to banks that increase their lending to individuals, firms and public authorities above the 2007 level. The French government can also offer guarantees, in exceptional and urgent cases, on liabilities issued by credit institutions on terms similar to those for SFFE loans. So far, seven banks have applied for loans totalling €5 billion from the SFFE. The French state has also undertaken to guarantee loans granted to companies in the Dexia group; as agreed with the Belgian and Luxembourg governments, the guarantee covers no more than 36.5 per cent of the loanable amount (€55 billion). The French government has also authorized a company wholly owned by the state (Société de Prise de Participations de l'État) to subscribe a maximum of €40 billion in hybrid instruments or preference shares in French financial institutions, which will count as regulatory capital; on 21 October it was announced that the company would subscribe new subordinated debt totalling €10.5 billion issued by six large groups.

On 7 October the Spanish government announced the adoption of two measures: the creation of a fund with initial capital of €30 billion (with the possibility of increasing it to €50 billion) that will be able to purchase securities from financial institutions operating in Spain; and the raising of the minimum guarantee for bank deposits from €20,000 to €100,000. On 13 October it also established a guarantee for credit institutions' new issues of senior debt instruments up to an initial ceiling of €100 billion for 2009; the guarantee may also be extended to cover interbank deposits, but only in the context of a coordinated initiative in the euro area.

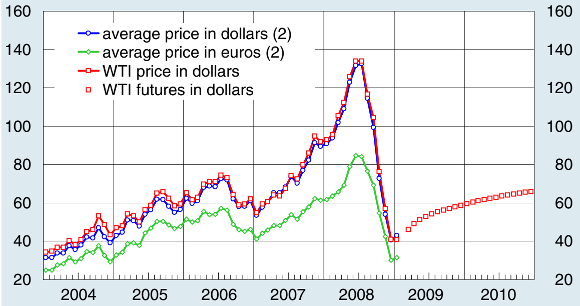
The prices of oil and non-energy commodities collapse

Oil prices have continued to fall in the last few months in response to a decrease in both current and expected demand for crude due to the effects of the financial crisis on the real economy; the contraction in demand was only partly offset by a cut in production by countries belonging to the OPEC cartel. In the fourth week of December the average price of the three main grades was around $35 per barrel, compared with a peak of $143 in July. In recent weeks price increases triggered by tensions in the Middle East and the Russo-Ukrainian crisis have been modest. On the basis of futures contracts, the price of WTI grade oil is expected to pick up in 2009, from the current level of $41 to around $60 at the end of the year, as excess supply is gradually absorbed (Figure 1). The dollar prices of the other main commodities also fell substantially.

Figure 1

Crude oil: spot and futures prices (1)

(dollars and euros per barrel)



Sources: IMF and Thomson Financial Datastream.
(1) Monthly averages for spot prices; the last data refer to 9 January 2009. – (2) Average price per barrel of the three main grades (Brent, Dubai and WTI).

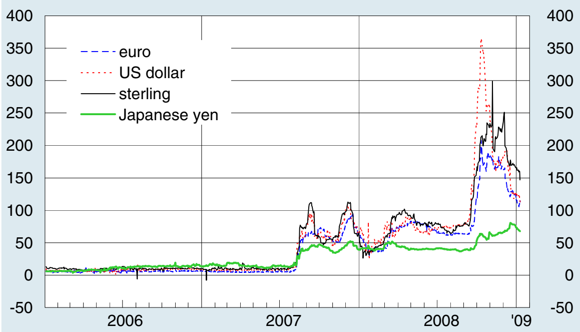
Though still strong, the strains in financial markets are easing ...

The strains in the interbank markets in the United States, the euro area and the United Kingdom, which increased tremendously after the collapse of Lehman Brothers on 15 September 2008, have eased in recent months. One measure of those strains (the three-month LIBOR - overnight index swaps spread) rose to 360 basis points on 10 October before declining to 110 basis points on 9 January. The corresponding spread for the euro fell from 210 to 110 basis points and that for sterling, which peaked at 300 basis points in early November, fell to 150 basis points (Figure 2). The extreme tensions that developed in the US commercial paper market at the beginning of the autumn have eased somewhat: the volume of commercial paper outstanding, which on 20 October had been about 20 per cent less than a month early, recovered substantially in subsequent weeks.

Figure 2

Three-month LIBOR spread to overnight index swaps (1)

(basis points, daily data)



Sources: Thomson Financial Datastream and Bloomberg.

... countered by extraordinary central bank intervention ...

The Federal Reserve adopted a number of measures to restore normal operations in the financial markets and maintain the flow of credit to the economy: it intervened repeatedly to ease tensions in the commercial paper market; in order to bolster the supply of mortgage loans it announced at the end of November that it intended to purchase asset-backed securities totalling $500 billion issued and guaranteed by the main government-sponsored enterprises (Fannie Mae and Freddie Mac); in order to support other types of lending to households and small and medium-sized firms it set up a facility for making three-year loans totalling $200 billion against asset-backed securities issued on or after 1 January 2009 and for which these types of lending constitute the underlying credit exposure; it set up substantial liquidity swap facilities with the central banks of four large emerging economies (Brazil, South Korea, Mexico and Singapore), complementing those already granted to the central banks of developed economies.

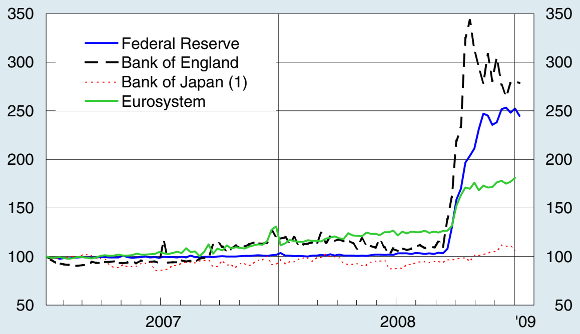
... reflected in a large increase in their balance sheets

The extraordinary actions taken by the central banks were reflected in a large increase in the assets held on their balance sheets. Between mid-September and the beginning of January the assets of the Federal Reserve increased by around 140 per cent and those of the Bank of England by slightly more (Figure 3); at the beginning of 2009 they amounted to around 16 per cent of the GDP of their respective countries. The measures to support the financial markets also led to a pronounced change in the composition of the central banks' assets, with the proportion of Treasury securities falling and that of lending to financial institutions increasing. The increase in the riskiness of the central banks' portfolios that could ensue was offset by applying substantial "haircuts" to the value of securities accepted as collateral for such lending. The corresponding increase in balance sheet liabilities consisted primarily, in the case of the Federal Reserve, in a substantial increase in reserves and deposits held with the central bank by the banking system and the US Treasury respectively.

Figure 3

Size of the balance sheets of selected central banks

(indices; 5 January 2007 = 100; weekly data)



Source: Thomson Financial Datastream.
(1) The original data for the Bank of Japan relate to ten-day periods.

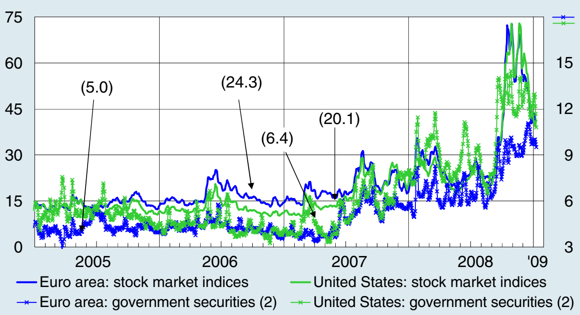
Stock markets remain extremely volatile, although there is some sign of improvement

The implied volatility of share prices on the US stock market remained very high, reflecting uncertainty about the course of the financial crisis, its impact on the real economy and the decisions the authorities would take. It peaked in the second half of November, when the difficulties of the Citigroup banking group came to a head and uncertainty increased as to the scale and timing of measures to support the main auto manufacturers; it subsided in December, returning to more or less the same level as at the beginning of October (Figure 4). The Standard & Poor's 500 index, which had fallen to a low on 20 November, had recovered by 9 January to a figure close to that recorded on 10 October (Figure 5).

Figure 4

Implied volatility (1)

(percentage points; averages for the period 1999-2006 in brackets)



Source: Based on Bloomberg data.
(1) Moving averages over 5 days. Stock market indices: VSTOXX for the euro area and VIX for the United States. Government bonds: volatility implied by the prices of options on futures on the German Bund for the euro area and on futures on Treasury notes for the United States. – (2) Right-hand scale.

The stock market of the euro area followed a similar pattern, whereas those of Japan and the United Kingdom have recovered by about 7 and 11 per cent respectively in the last three months. The fall in equity values in relation to the end of 2007 amounts to about 40 per cent in the United States, Japan and the euro area and around 30 per cent in the United Kingdom.

Bond spreads at record levels and low yields on government securities

The risk premiums on corporate bonds of all the main risk classes continued to increase to historic highs in the autumn (Figure 6); from mid-December onwards, however, signs of a reversal began to emerge, especially for the highest risk classes.

The yields on US government securities have fallen markedly in the last three months, reflecting the easing of monetary conditions, portfolio adjustment in favour of government securities and the possibility that the Federal Reserve will begin to purchase longer-term Treasury securities: between 10 October and 9 January ten-year yields fell from 3.8 to 2.4 per cent. In the euro area, the United Kingdom and Japan they declined by less, falling to 3, 3.4 and 1.3 per cent respectively (Figure 7).

Strains also persist in the financial markets of emerging economies

In the emerging countries yield differentials between long-term dollar-denominated sovereign bonds and US Treasury securities began to widen in September and have increased further since then. The differential measured by the EMBI Global Index, which was about 330 basis points at the beginning of September, reached a peak of just under 900 basis points at the end of October before coming back down to around 690 basis points on 9 January. Share prices followed a similar pattern to that observed in the main advanced countries; on 9 January they were close to the levels recorded on 10 October.

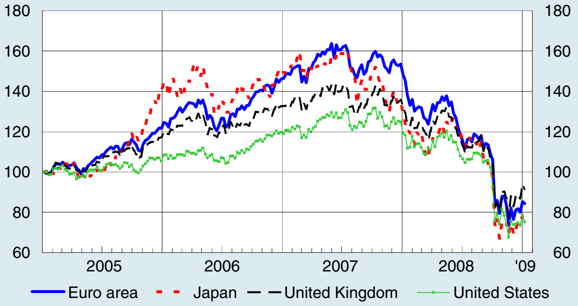
The appreciation of the dollar came to a halt in December

The performance of the dollar in relation to other leading currencies has been mixed in the last three

Figure 5

Stock market indices (1)

(end-of-week data; first week of January 2005=100)

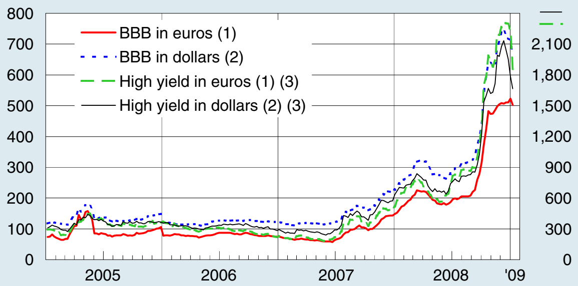


Source: Thomson Financial Datastream.
(1) Dow Jones Euro Stoxx for the euro area, Nikkei 225 for Japan, FTSE All Share for the United Kingdom and Standard & Poor's 500 for the United States.

Figure 6

Yield differentials between bonds of non-financial corporations and government securities

(end-of-week data; basis points)

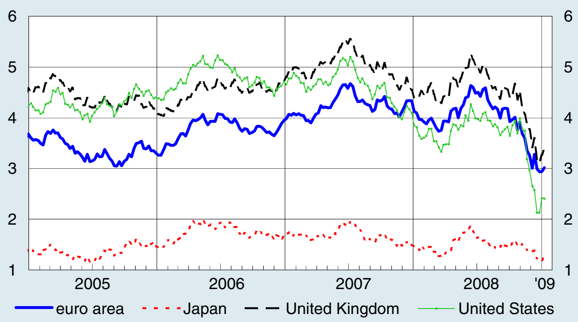


Source: Merrill Lynch.
(1) Fixed-rate bonds denominated in euros with a residual term to maturity of not less than one year issued in the Euromarket; yield differentials are calculated with respect to French and German government securities. – (2) Fixed-rate bonds denominated in dollars with a residual term to maturity of not less than one year issued in the US domestic market; yield differentials are calculated with respect to US Treasury securities. – (3) Right-hand scale.

Figure 7

Yields on ten-year government bonds

(end-of-week data; percentages)



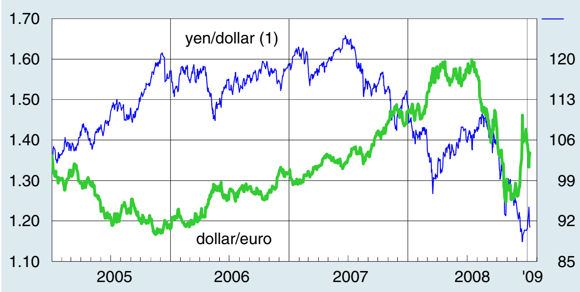
Source: National statistics.

months (Figure 8): it continued to depreciate against the yen (falling by about 8 per cent), appreciated by 11 per cent against sterling and strengthened against the euro until early December before returning to its level of three months earlier in the first few days of January. These contrasting movements are not easy to explain. The heightened perception of risk triggered the repatriation of very large amounts of capital that had previously been invested in high-yielding currencies; these flows went into the dollar and especially the yen, rather than the euro, and they put strong downward pressure on the currencies of some emerging economies, which was only partly offset by their respective central banks. The high volatility of exchange rates between the major currencies probably reflected the alternating flow of information on the deterioration in economic activity in the economies concerned and associated expectations about monetary policy. The exchange rate between the dollar and the Chinese currency has remained virtually unchanged over the last three months (during 2008 as a whole the dollar depreciated by around 6.5 per cent, comparable to the depreciation recorded in 2007). On 9 January the nominal effective exchange rate of the US currency was close to its level of three months previously and about 9 per cent higher than at the end of 2007.

Figure 8

Exchange rates

(daily data)



Source: ECB.
(1) Right-hand scale.

2.2 THE MAIN INDUSTRIAL AND EMERGING COUNTRIES

In the United States economic activity is contracting ...

The GDP of the United States fell at an annual rate of 0.5 per cent in the third quarter of 2008, reflecting the sharp fall in private consumption, the marked slowdown in exports and the continuing contraction in residential investment. Economic activity weakened further in the final quarter: payroll employment in the non-farm sector fell by about 1,950,000 between August and December (650,000 in the first eight months of the year); in October and November consumption barely responded to the rise in real disposable personal income brought about by the pronounced fall in energy prices. International organizations and private forecasters predict a sharp contraction in GDP in the fourth quarter of 2008 and the first part of 2009.

... in response to the decline in household wealth ...

The effects of the financial crisis have spilled over onto economic activity though a variety of channels. Household spending decisions have been adversely affected by the decline in net wealth, which by the end of September had fallen to about 535 per cent of disposable personal income, some 30 percentage points less than at the end of June and 100 points lower than a year earlier.

... more stringent credit conditions ...

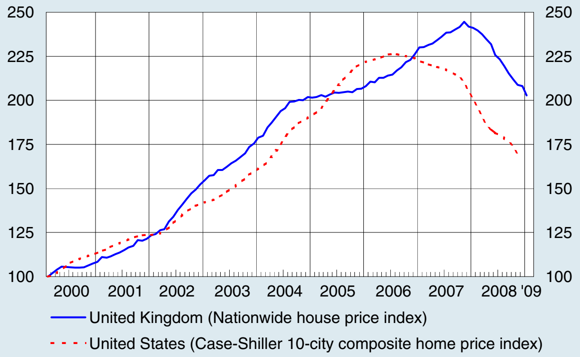
In the third quarter of 2008 the deterioration in the conditions for access to credit was reflected in a decline in net lending to non-financial corporations and an outright contraction in credit to households. The Federal Reserve's Senior Loan Officer Opinion Survey carried out in October revealed a further tightening of the supply of credit to households and firms. Gross bond issues by non-financial corporations, which had fallen steeply in the third quarter, remained small in the fourth.

... and the continuing crisis in the housing market

The impact of the fall in house prices on household wealth and mortgage defaults is one of the US economy's most vulnerable points. In November sales of new homes amounted to less than 9 per cent of the stock of unsold new dwellings, presaging a further fall in residential investment. The prices of houses in the ten largest cities, as measured by the Case-Shiller index, continued to fall (Figure 9): in October the decline in relation to the peak of mid-2006 was 25 per cent; futures prices imply a further reduction of around 12 per cent by the end of 2009. Foreclosures initiated on residential mortgages remained at a very high level in the third quarter (Figure 10).

Figure 9

Real estate market: house prices
(indices, January 2000=100)



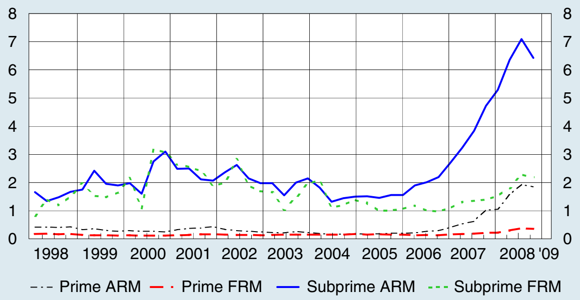
Source: Thomson Financial Datastream.

Consumer price inflation is falling rapidly

Inflation in the United States, measured by the personal consumption deflator, has fallen significantly in recent months, to 1.4 per cent in November, compared with 4.4 per cent in August, owing largely to the decline in the prices of energy products. Excluding energy and food, inflation came down from 2.4 to 1.9 per cent. Between September and December the consensus forecasts for average inflation in 2009 fell from 2.9 to 0.3 per cent.

Figure 10

Residential mortgages in the United States: foreclosures initiated as a proportion of outstanding mortgages, according to type of mortgage (1)
(seasonally adjusted quarterly data; percentages)



Source: Thomson Financial Datastream.
(1) ARM: adjustable-rate mortgages; FRM: fixed-rate mortgages.

With policy rates at practically zero, the Federal Reserve contemplates the adoption of other measures

The Federal Reserve reduced its target rate for federal funds by 50 basis points to 1 per cent on 29 October and set a target range of between 0 and 0.25 per cent on 16 December. In the press release of that day it also spelled out its determination to keep policy rates exceptionally low for some time. The latest futures prices indicate that markets expect policy rates to remain unchanged throughout the first half of 2009. The US central bank's actions to support the economy will be directed towards the adoption of measures to facilitate the extension of credit to households and small and medium-sized businesses; it is also assessing the merits of measures to influence longer-term rates more directly.

A large increase in the federal budget deficit in 2009 is foreseen

The Congressional Budget Office (CBO) recently estimated that the decision of 6 September to place the two government-sponsored enterprises (Fannie Mae and Freddie Mac) in conservatorship and thus to take control of these institutions (see the box "The crisis of some US financial institutions and the support action of the authorities" in *Economic Bulletin*, no. 50, October 2008) will contribute to increasing the federal deficit by $240 billion in the 2009 fiscal year, which began on 1 October. The programme approved on 3 October to provide support to the banking system (see the box "The recent measures to support the banking system in the main industrial countries") provides for a total allocation of $700 billion; implementation of the programme will increase the deficit for this year by a further $180 billion. The CBO's assessment reflects an estimate of the discounted value of the losses stemming from implementation of the two measures. Leaving aside the stimulus package currently under examination, the federal deficit is expected to increase from $455 billion (3.2 per cent of GDP) in the 2008 fiscal year to $1,186 billion in 2009 (8.3 per cent of GDP).

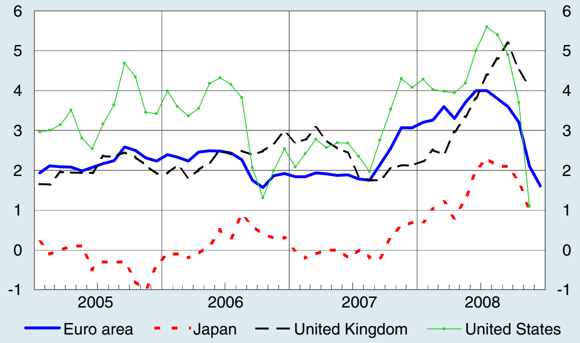
Economic activity in Japan continues to contract ...

Japan's GDP, which had already fallen at an annual rate of 3.7 per cent in the second quarter of 2008, declined by 1.8 per cent in the third, owing mainly to the continued contraction in private investment and the negative contribution from net exports. The latest Tankan Survey reported a further sharp deterioration in business confidence in the fourth quarter, affected by a tightening of the supply of bank credit and great difficulty in raising finance through the issue of commercial paper. Consumer price inflation fell from 2.1 to 1 per cent between August and November (Figure 11).

Figure 11

Consumer price inflation (1)

(monthly data; twelve-month percentage changes)



Source: Thomson Financial Datastream.
(1) For the euro area and the United Kingdom, harmonized consumer prices.

... and the monetary and fiscal authorities intervene to support the economy

The Bank of Japan reacted by reducing its monetary policy reference rate twice by a total of 40 basis points to 0.1 per cent; the markets expect official rates to remain unchanged throughout 2009. At the end of October the fiscal authorities announced measures amounting to about 4 per cent of GDP to ease the funding difficulties of small and medium-sized firms and measures worth a further 1.2 per cent to support families; at the end of December they announced further measures to strengthen the financial system.

Vigorous counter-cyclical monetary and fiscal measures in the United Kingdom

Economic activity in the United Kingdom contracted sharply in the third quarter (at an annual rate of 2.6 per cent) owing to the fall in investment, the stagnation in private consumption and the deterioration in the contribution of net exports to growth. The mechanisms whereby the financial crisis affected the real economy were similar to those operating in the United States. Households' net financial wealth continued to decline in the third quarter; the tightening of conditions for access to credit was reflected in a further pronounced contraction in the flow of lending to households and non-financial firms. The Credit Conditions Survey published by the Bank of England on 2 January showed expectations of a further restriction of credit availability in the first few months of 2009. House prices continued to fall: in December they were around 17 per cent below the peak of October 2007. Consumer price inflation reached 5.2 per cent in September, but fell to 4.1 per cent in November. Against that background, the Bank of England reduced its monetary policy rate by 150 basis points on 6 November and by a further 100 basis points on 4 December; on 8 January it lowered it by another 50 basis points to 1.5 per cent. The UK Treasury announced the adoption of counter-recessionary measures, the key provisions of which are a temporary reduction in VAT from 17.5 to 15 per cent and the bringing-forward of existing public investment; according to the Treasury, these measures will provide a boost equivalent to about 0.6 per cent of GDP in the 2008-2009 financial year ending in March 2009 and 1.1 per cent in 2009-2010.

The emerging economies see an outflow of capital and a slowdown in activity

The financial crisis also spread to the emerging economies in the third quarter of 2008. The difficulty in gaining access to international credit, together with the weakening of foreign demand, contributed to an abrupt slowdown in economic activity. In addition, commodity-exporting countries were hit by the fall in commodity prices in recent months. According to the average of the forecasts collated by Consensus Economics in December, which were revised sharply downwards from three months previously, economic activity will slow down markedly in Russia (from 6.7 per cent in 2008 to 2.9 per cent in 2009) and Brazil (from 5.5 to 2.1 per cent), and to a lesser extent in China (from 9.3 to 7.8 per cent) and India (from 6.9 to 6.3 per cent).

The reactions of the monetary and fiscal authorities

In an attempt to counteract the weakening of economic activity and with inflationary pressures rapidly abating, the central banks of many emerging economies, particularly those in Asia, relaxed monetary conditions by reducing reference interest rates and banks' reserve requirements. By contrast, currency depreciation had a greater influence on the actions of the monetary authorities in other emerging regions that are more dependent on international credit and have substantial liabilities denominated in foreign currency. Programmes to provide fiscal support to the economy were either launched or announced. The Indian Government set out a plan centring on a reduction in indirect taxation, which should provide stimulus estimated at the equivalent of around 1.5 per cent of GDP in 2009. The Chinese authorities announced a programme that includes measures to support the housing market and infrastructure investment; according to the Government's official estimates, the planned measures will amount to about 13 per cent of GDP, although this will probably be spread over several years.

2.3 THE EURO AREA

The euro area has gone into recession

In the third quarter of 2008 the GDP of the euro area declined by a further 0.2 per cent in relation to the preceding quarter. The contraction in activity was widespread; it affected all the main sectors (there was a particularly large fall of 1.3 per cent in the value added of industry including construction) and the major euro-area economies (GDP fell by 0.5 per cent in Germany and Italy and by 0.2 per cent in Spain, while in France it remained broadly unchanged). Growth in the area was held back by the stagnation in exports and private consumption. Gross fixed investment again declined, contracting by 0.6 per cent in relation to the preceding quarter; investment in construction showed a further sharp fall of 1.1 per cent, confirming the downturn in the property cycle. There was also a slight decline in spending on machinery and equipment and transport equipment; in addition, corporate investment was affected by the fall in capacity utilization rates, which as the year progressed fell to a level close to that recorded before the vigorous expansion in output in 2006-2007.

All the indicators point to a deterioration in the economic climate

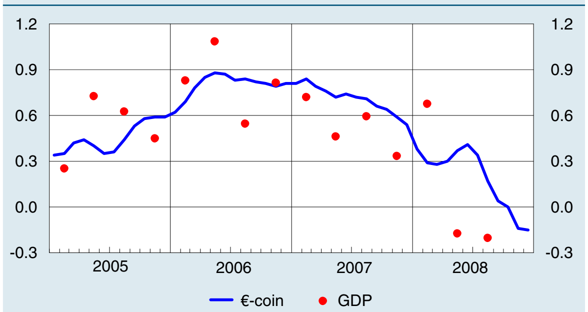
The indicators available for the fourth quarter of 2008 indicate a worsening of the downturn, especially in manufacturing. Industrial production in the euro area, adjusted for calendar and seasonal effects, which had declined by more than 1 per cent in the third quarter, fell by a further 1.6 per cent in both October and November. The €-coin indicator, which provides a monthly estimate of the change in euro-area GDP adjusted for short-term fluctuations, has fallen continuously since the spring; it turned negative in November and December (Figure 12).

The indices based on the results of interviews with purchasing managers (PMI) have fallen to

Figure 12

€-coin coincident indicator of the euro-area business cycle and GDP (1)

(percentage changes)



Sources: Eurostat and based on Thomson Financial Datastream data.
(1) For information on the construction of the indicator, see the box "€-coin: a real-time estimate of growth in the euro area" in *Economic Bulletin*, no. 46, October 2007. For GDP, quarterly data; change in relation to the preceding quarter. For €-coin, monthly data; change over three months.

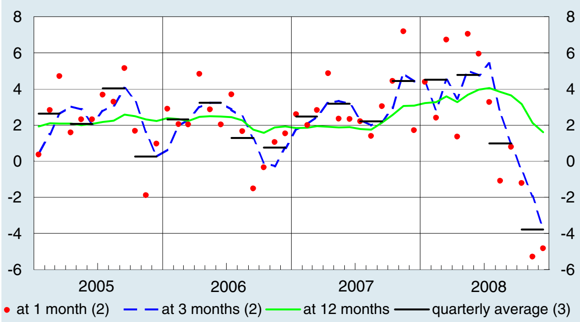
historic lows since October, as has the level of confidence evidenced by surveys carried out by the European Commission; the firms interviewed at the end of 2008 for the half-yearly investment survey expect investment to fall this year. According to our estimates, in the fourth quarter of 2008 euro-area GDP contracted much more rapidly than in the summer. Among the major countries, only Italy is estimated to have shown a fall in output for the year as a whole, with GDP declining by around half a percentage point.

The fall in commodity prices is curbing inflation

Taking account of provisional Eurostat data for December, the harmonized index of consumer prices in the euro area rose by 3.3 per cent in 2008 as a whole, compared with 2.1 per cent the previous year. Consumer price inflation touched a peak of 3.8 per cent in the third quarter but fell back sharply in the last few months of the year to a rate of 1.6 per cent in December (Figure 13), checked by the rapid fall in commodity prices. The three-month changes in the harmonized index on a seasonally adjusted and annualized basis turned negative in October, reflecting the sharp falls in fuel prices. In terms of the core index, which excludes energy and food prices, the twelve-month inflation rate remained broadly stable, at just under 2 per cent, indicating that the feared effects of the increases in commodity prices on the core components were confined, at most, to the items directly affected by these developments, such as air transport. The easing of imported inflationary pressures was also at the root of the slower rise in producer prices, which in November were 3.3 per cent higher than twelve months earlier, compared with a peak of 9.2 per cent in July. Owing to the decline in commodity prices, the indicator of manufacturing firms' input costs derived from surveys of purchasing managers fell to a very low historical level; the indicator for the services sector, which also takes account of the behaviour of labour costs, showed a less marked decline. In the first nine months of 2008 the rise in unit labour costs in the economy as a whole accelerated throughout the euro area, to 3 per cent, from 1.4 per cent in 2007. The acceleration reflected both the cyclical slowdown in the growth of labour productivity and the transient effects of the renewal of labour contracts in some countries in the area.

Figure 13

Harmonized index of inflation in the euro area (1)
(percentage changes)



Sources: Based on Eurosta and ECB data.
(1) Provisional data for December. – (2) On a seasonally adjusted and annual basis. – (3) Average, in the reference quarter, of monthly growth rates, on a seasonally adjusted and annual basis.

According to the professional forecasters polled by Consensus Economics in December, the rate of increase in consumer prices in the euro area will ease to an average of 1.4 per cent in 2009; in the second and third quarters of the year inflation may decline to a particularly low level, since the comparison will be with the corresponding period of 2008, when food and energy prices had soared.

Money supply and credit growth continue to slow

The rate of growth in bank lending to the private sector declined further, to 7.1 per cent, in the twelve months ending in November, reflecting the slowdown in lending to firms and households, especially the latter. However, the slowdown in lending for house purchases continues to be due partly to the accounting effect of securitization operations carried out largely to create securities that can be lodged as collateral for refinancing operations with the Eurosystem. The Bank Lending Survey carried out by the Eurosystem in October indicated that lending conditions would tighten further in the fourth quarter, especially for loans to house buyers. The rate of growth in the M3 money supply decreased to 7.8 per cent in November, mainly reflecting a slowdown in the less liquid components.

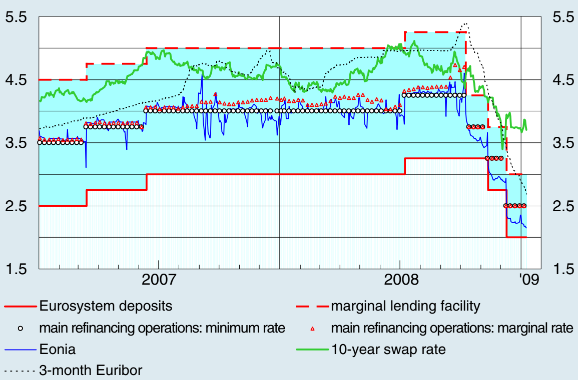
The ECB has reduced official rates appreciably

After participating in the concerted rate cut at the beginning of October, the European Central Bank has further reduced the minimum bid rate on main refinancing operations twice in the light of the substantial easing of inflationary pressures and the rapidly deteriorating outlook for growth: it cut the rate by 50 basis points on 6 November and by 75 basis points on 4 December, bringing it down to 2.5 per cent (Figure 14). The Eurosystem's monetary policy is deemed credible by the markets, as demonstrated by the indicators of inflation expectations between five and ten years ahead (calculated on the basis of inflation swaps), which are at levels compatible with the objective of price stability. The differential between rates on three-month unsecured loans (Euribor) and their secured counterparts (Eurepo) – which provides a measure of the risk premium on the interbank market – rose to a peak of 185 basis points on 10 October following the collapse of Lehman Brothers but then narrowed considerably, to stand at 102 basis points on 9 January, still an exceptionally high level. The ECB has also confirmed its commitment to bolster liquidity, deciding at the meeting of the Governing Council on 18 December that the fixed-rate tender procedure with full allotment introduced for main refinancing operations in October would continue to be used at least until the end of March 2009; at the same time it announced that, in order to facilitate the restoration of normal operations in the interbank market, the width of the corridor between rates on marginal refinancing operations and those on deposits with the Eurosystem, which had been reduced to 100 basis points in October, would be restored to 200 basis points with effect from 21 January.

Figure 14

Official interest rates and money and financial market rates in the euro area

(daily data; percentages)



Sources: ECB and Reuters

The balance sheet of the Eurosystem has expanded considerably and its composition has changed

The special liquidity management measures introduced by the ECB from the second half of September onwards had pronounced effects on the size and composition of the consolidated balance sheet of the central banks belonging to the Eurosystem; at the end of December total assets showed an increase of 40 per cent, rising to about €2,000 billion (Figure 3). The increase is far smaller than that in the balance sheets of the Federal Reserve and the Bank of England. The average daily volume of liquidity provided by means of open market operations almost doubled (to about €800 billion), while the proportion of lending for terms of three months or more remained more or less unchanged at about 60 per cent. An exceptionally large part of the liquidity provided to the financial system (a daily average of about €170 billion) was deposited by banks in their deposit facilities with the Eurosystem, presumably reflecting the accumulation of excess liquidity held by the banks for precautionary purposes.

3 THE ITALIAN ECONOMY

3.1 THE CYCLICAL SITUATION

The Italian economy has gone into recession too

After contracting by 0.4 per cent in the second quarter of 2008 compared with the previous quarter, Italian GDP fell again in the third quarter, by 0.5 per cent. The rapid deterioration in economic activity can be attributed mainly to the pronounced worsening in international conditions and the consequent fall in export demand, accompanied by persistently weak domestic demand. Italy's exports diminished sharply in the third quarter, by 1.6 per cent compared with the previous quarter, thereby reducing the growth of the economy by about half a percentage point. This had a detrimental effect on corporate investment, which contracted by nearly 2 per cent, presumably also as a result of the progressive tightening of credit conditions. Households' consumption continued to stagnate, reflecting the compression of real disposable income by the price rises consequent on the increases in the quotations of imported raw materials. Spending may also have been affected by a cautious attitude on the part of households, which probably postponed spending that was not urgent, fearing a deterioration in the economic situation and labour market conditions.

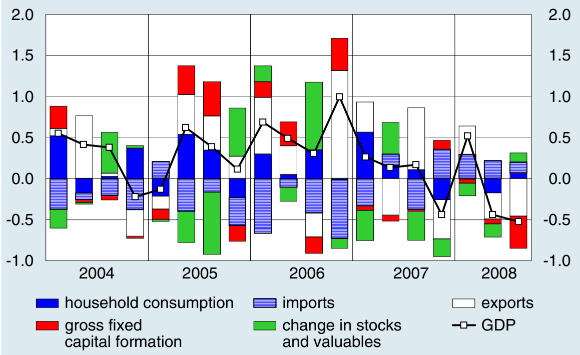
The economic situation is deteriorating

The indicators available for the last part of 2008 show a further pronounced deterioration. According to Bank of Italy estimates, the index of industrial production fell considerably on average in the fourth quarter. Business confidence deteriorated, falling to historically low levels, and this is reflected in plans to reduce corporate investment, in 2009 too. On the demand side, the disappointing performance of export orders and the recent appreciation of the euro against the other main currencies appear to

Figure 15

Contributions of the main components of demand and imports to the growth in GDP (1)

(percentage points)



Source: Istat.
(1) The formula for calculating the contributions to real GDP growth in accordance with the new methodology for price deflation based on chain linking can be found at the Istat website: www.istat.it.

Table 2

GDP and its main components

(chain-linked volumes; data adjusted for seasonal and calendar effects; percentage changes on preceding period)

	2007	2007 (1)	2008		
	Q4		Q1	Q2	Q3
GDP	-0.4	1.5	0.5	-0.4	-0.5
Total imports	-1.2	4.4	-1.0	-0.8	-0.5
National demand (2)	-0.3	1.3	-0.1	-0.3	-0.2
National consumption	-0.3	1.4	0.1	-0.1	0.1
households	*-0.4*	*1.4*	*..*	*-0.3*	*0.1*
other (3)	*0.3*	*1.3*	*0.5*	*0.3*	*0.1*
Gross fixed capital formation	0.5	1.2	-0.2	-0.3	-1.9
construction	*0.3*	*2.2*	*0.1*	*-1.0*	*-0.6*
other goods	*0.8*	*0.2*	*-0.6*	*0.5*	*-3.2*
Changes in stocks and valuables (4)	-0.2	..	-0.2	-0.2	0.1
Total exports	-1.6	5.0	1.2	-1.1	-1.6

Source: Istat.
(1) Data not adjusted for calendar effects. – (2) Including changes in stocks and valuables. – (3) Expenditure of general government and non-profit institutions serving households. – (4) Contribution to GDP growth over the preceding period, in percentage points.

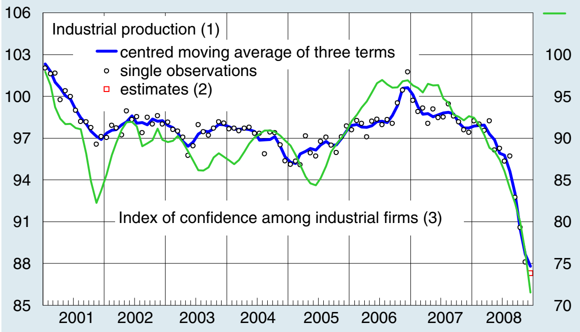
rule out a recovery in exports in the short term. Domestic orders could benefit from the effects on households' spending decisions of the sharp improvement in inflation since the autumn, but there is the risk that consumption will be held back by fear of a worsening in labour market conditions.

GDP is likely to have undergone a further contraction in the fourth quarter of 2008, of just over 1 per cent compared with the previous quarter; if this estimate is confirmed, economic activity will have contracted by 0.6 per cent on average for the year.

According to the national accounts, in the third quarter the number of employed persons remained basically unchanged compared with the previous period. Measured in terms of standard labour units, employment diminished instead by 0.7 per cent. In the same period INPS data show an increase in the number of persons authorized to receive support from the ordinary Wage Supplementation Fund.

Figure 16

Industrial production and index of business confidence
(monthly data; indices: 2000=100)



Sources: Based on ISAE, Istat and Terna data.
(1) Adjusted for seasonal and calendar effects. – (2) Based on electricity consumption and the indicators of ISAE surveys of manufacturing firms. – (3) Average of the seasonally adjusted percentage balances of the responses to questions regarding the level of demand, production expectations and stocks of finished products; moving average of three terms (right-hand scale).

The inflationary outlook has improved considerably

On the basis of preliminary estimates for December, the index of consumer prices for the entire resident population rose by 3.3 per cent in 2008, compared with 1.8 per cent in the previous year. As in the rest of the euro area, inflation accelerated until the summer and then slowed significantly (to 2.2 per cent in December), in parallel with raw material prices. In particular, the large decreases in fuel prices led in the last part of 2008 to month-on-month falls in the consumer price index, even when seasonally adjusted. According to the leading forecasters, inflation will slow even more in 2009.

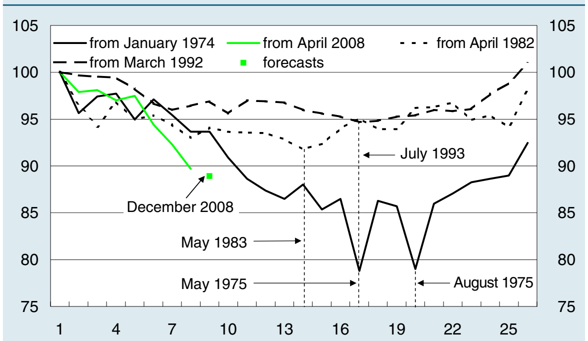
3.2 FIRMS

The recession in industry is worsening

After falling significantly last summer, the index of industrial production, adjusted for seasonal and calendar effects, fell even more sharply in the fourth quarter, by about 6 per cent on the basis of Bank of Italy estimates for December (Figure 16); on this basis the average fall for 2008 was around 4 per cent. This is one of the worst results since the end of the Second World War; the severity of the downturn is similar, so far, to that recorded during the 1974-75 crisis, when, after a year and a half, the cumulative contraction in industrial production was more than 20 per cent (Figure 17). According to the data available up to October, activity was contracting in every sector of manufacturing industry and most sharply in the sectors producing

Figure 17

Main downturns in industrial production (1)
(indices for the months from the first month of decline, set to 100)



Sources: Based on ISAE, Terna and Istat data.
(1) Adjusted for seasonal and calendar effects. For December 2008, estimates based on electricity consumption and the indicators of ISAE surveys of manufacturing firms.

intermediate and investment goods. The situation appears slightly less negative in the consumer goods sector, except for cars, where production plummeted in the last few months of 2008. The results of business opinion surveys do not point to a recovery in manufacturing activity in the short term. As in the rest of the euro area, business confidence in Italy, measured by ISAE surveys, has fallen to historically low levels in recent months; especially large deteriorations have been recorded in the outlook for orders, above all export orders (Figure 18), and production. The PMI indices compiled from interviews with purchasing managers also fell, recording the lowest values since the start of the series.

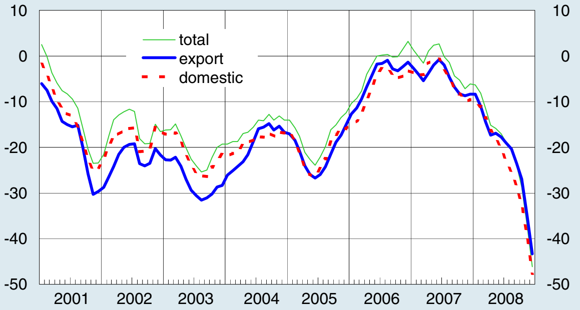
Industrial investment activity continues to weaken and a recovery is not expected in the short term

Firms' gross fixed investment fell significantly in the third quarter of 2008 (by 1.9 per cent on the previous period), dragged down by the machinery and equipment component, which contracted by 3.5 per cent. Firms' capital formation was held back by the downturn in both current demand (the capacity utilization rate fell from summer 2008 onwards, to the lowest level for about ten years) and prospective demand and by the tightening of credit conditions, against a background of weakening profitability and a further decline in the scope for self-financing.

The reduction in spending on capital goods is expected to continue in 2009; this is confirmed both by the six-monthly survey conducted last autumn by the European Commission and by the quarterly survey conducted by the Bank of Italy in collaboration with *Il Sole 24 Ore*, which found a large increase in the percentage of firms stating that the conditions for investing had worsened compared with three months earlier (66 per cent, compared with 38 per cent in the September survey).

Figure 18

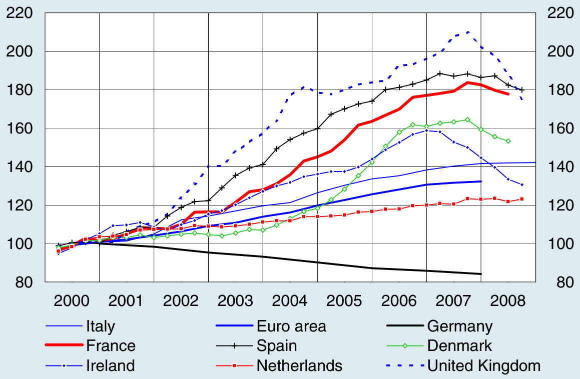
Industrial orders (1)
(monthly data)



Source: Based on ISAE data.
(1) Moving average for the three months ending in the reference month of the difference between the percentage of positive replies ("high", "increasing") and that of negative replies ("low", "decreasing") to the request to assess the level of orders. Seasonally adjusted. The replies are weighted by size, sector and location of firm.

Figure 19

House prices in Europe
(at constant prices per square metre; indices: 2000=100)



Sources: National statistics; for Italy, based on Bank of Italy, *Il Consulente Immobiliare* and Istat data.

No halt in the weakness of the construction industry

According to the national accounts, the summer saw a further decline in construction sector activity, which fell by 0.6 per cent compared with the three previous months after falling by 1 per cent in the second quarter; a similar pattern is found in the residential building sector. The data for the last few months of the year do not point to a recovery in activity. The climate of confidence among building firms fell in November to the lowest levels of the last ten years. According to preliminary data published by the Property Agency, there was a further large fall in property sales in the third quarter of 2008; according to the Bank of Italy's indicator based on data from *Il Consulente Immobiliare*, the prices of residential buildings continued to rise in the second half of the year, but the pace slowed and, net of inflation, they remained basically stable. The latest figures available for other European Union countries confirm the fall in real terms of residential property prices in 2008 (Figure 19), especially in Finland, Ireland, Spain and the United Kingdom; prices held up not only in Italy but also in the Netherlands and Portugal.

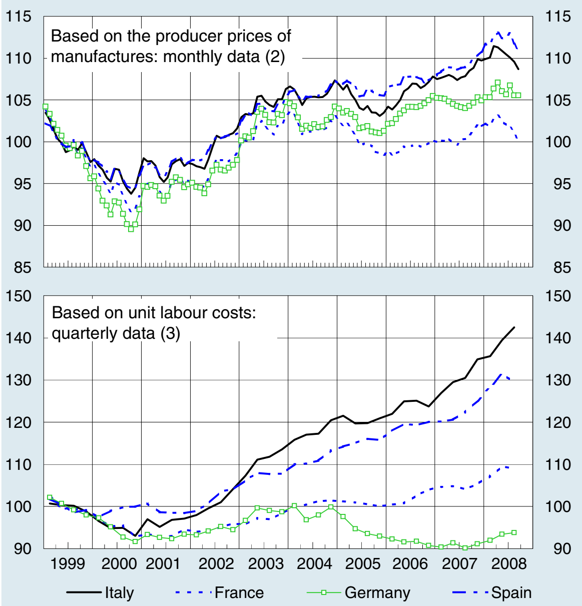
The recovery in price competitiveness continued in the autumn but may have ended at the end of the year

The interruption during the spring of the prolonged appreciation of the nominal effective exchange rate of the euro against the leading currencies and its subsequent depreciation from the summer onwards (by about 4 per cent between April and September) were behind the recovery of just over 2 percentage points in the competitiveness of Italian manufacturing firms on the basis of producer prices, in line with the developments observed in the other leading euro-area countries (Figure 20). According to preliminary estimates, in October and November there was a further improvement of about 2 percentage points compared with the previous two months. This trend may have come to a halt in December in connection with the recovery of the nominal effective exchange rate of the euro. By contrast, the three-monthly indicator based on unit labour costs deteriorated further in Italy between the second and third quarters of 2008 (by about 2 per cent); in Germany and France it remained basically unchanged.

Figure 20

Indicators of competitiveness (1)

(indices: 1999=100)



Sources: Based on IMF, OECD and Eurostat data.
(1) An increase in the index indicates a loss of competitiveness. – (2) In relation to 61 competitor countries; latest available data refer to September 2008. – (3) In relation to 24 competitor countries; latest available data refer to the third quarter of 2008.

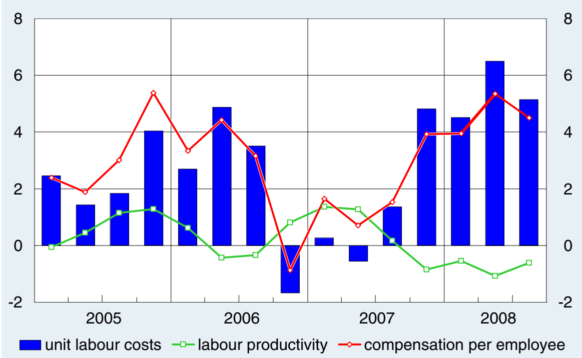
The large gap between the growth of unit labour costs in Italy and the other major countries should narrow in 2009

In the first nine months of 2008 unit labour costs increased on a twelve-month basis by 5.4 per cent on average (1.4 per cent in 2007), compared with much smaller increases for Italy's main trading partners (1.2 per cent in Germany and 2.3 per cent in France). The sharp acceleration recorded in Italy was due to the reduction of about 1 percentage point in labour productivity and the impact on per capita incomes of the temporary effects of the labour contracts signed towards the end of 2007 and early in 2008 (Figure 21). In 2009 the rate of increase in compensation per employee in the economy as a whole should slow significantly and bring that of unit labour costs closer into line with those of the other major euro-area countries.

Figure 21

Labour costs and productivity in the economy as a whole

(annual data; percentage changes on preceding period)



Source: Based on Istat data.

Firms' profitability has deteriorated ...

Estimates based on national accounts data show that firms' operating profits continued to decline in the twelve months ending in September 2008, in line with the trend which has been under way since 2004 and which became more pronounced in the second half of 2007. There was a further reduction in self-financing, partly as a consequence of the increase in net financial costs. As a ratio to value added, self-financing fell to its lowest level for fifteen years.

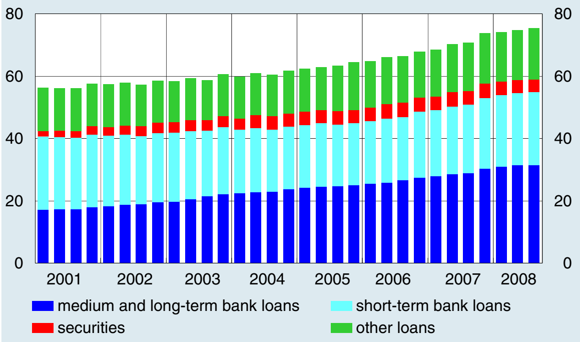
... and their borrowing requirement has increased

Despite the fall in investment (including inventories), the decline in self-financing caused firms' borrowing requirement (measured as the difference between gross investment and self-financing) to increase substantially. Firms' financial debt at the end of September amounted to 75.3 per cent of GDP, 0.6 percentage points more than at the end of June (Figure 22).

Figure 22

Corporate debt (1)

(as a percentage of GDP)



Source: Based on Bank of Italy and Istat data.
(1) The figures for the third quarter of 2008 are provisional.

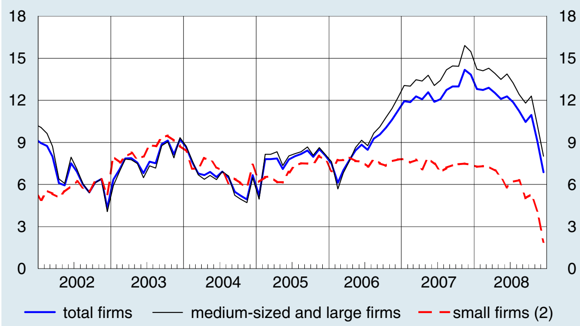
The growth in bank debt has slowed

Corporate debt towards the banking system continued to grow at a rapid pace in the third quarter of 2008 (11 per cent higher than in the year-earlier quarter after adjusting for the accounting effect of securitizations); it then slowed sharply to a twelve-month increase 6.9 per cent in November, owing partly to calendar effects. For small firms the rate of growth fell to 1.9 per cent in November (Figure 23).

Figure 23

Bank lending to firms by size of firm (1)

(monthly data; twelve-month percentage changes)



(1) Loans exclude repos, bad debts and other minor items included in the Eurosystem harmonized definition of the aggregate. The data are also adjusted for the effects of reclassifications, exchange rate variations and other changes not due to transactions. – (2) Limited partnerships, general partnerships, informal partnerships, de facto companies and sole proprietorships with up to 19 workers.

Fund-raising on the market was mainly through bond issues

In the third quarter of 2008 net issues of bonds by Italian firms amounted to about €1 billion. According to Dealogic data on gross issues, in the fourth quarter ENI and Finmeccanica made large placements totaling €2 billion. Increases in capital on the Italian stock exchange were negligible in the third quarter, larger in the fourth (€1.5 billion). Mergers and acquisitions remained few in number and small in size; on the basis of Thomson Financial data, 22 transactions were announced in the third quarter and 16 in the fourth (for a total of €1.1 billion and €1.6 billion respectively). This pattern was common to all the main euro-area countries, except Germany.

3.3 HOUSEHOLDS

Household consumption stagnates ...

On average in the first three quarters of 2008, households' consumption fell by 0.4 per cent compared with the same period in the previous year, while for 2007 as a whole it had grown by 1.4 per cent (Figure 24). This contraction in spending reflected the weakening of households' real disposable income, which, on the basis of preliminary evaluations, is estimated to have basically stagnated throughout the first nine months of the year by comparison with the corresponding period of the previous year. Set against an acceleration of nominal income, owing mainly to contract renewals that sustained employee incomes, households' purchasing power was slowed by the sharp increase in consumer price inflation which was only interrupted at the end of the summer. When account is also taken of the monetary erosion of net financial assets due to the increase in inflation, real disposable income actually fell. Spending decisions were also influenced by the loss in value of households' financial assets linked to the sharp fall in equity prices.

... influenced also by uncertainty over incomes and employment prospects

In the third quarter households' spending remained more or less stationary following a fall in the preceding three months. Widespread uncertainty over the length and depth of the recession and growing concern about developments in the labour market meant that households postponed larger purchases; this was reflected above all in a further sharp fall in spending on durable goods in the third quarter (-1.2 per cent on the preceding period). Purchases of non-durable goods were stationary compared with the falls recorded in the preceding four quarters, while spending on services picked up slightly (0.5 per cent) following a standstill in the previous quarter.

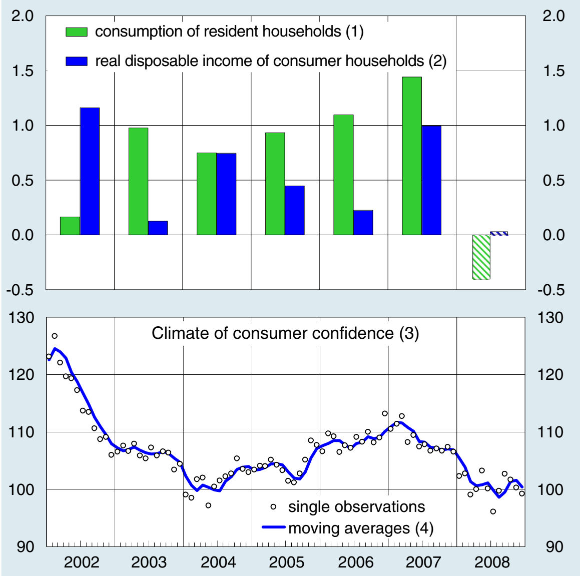
In the fourth quarter, consumer confidence remained basically stable although still at historically low levels; labour market expectations worsened considerably. Although not used in the calculation of the indicator, the opinions expressed regarding price movements did show a clear improvement. Once again, seasonally adjusted car registrations fell on average in the fourth quarter and the number of new orders from dealers did not indicate a recovery in the car market in the next few months. In October there was also a drop in seasonally adjusted retail sales (-0.6 per cent on September).

A slight increase in both households' debt and their debt servicing costs

Following six months of decline, in the third quarter of 2008 Italian households' debt as a ratio

Figure 24

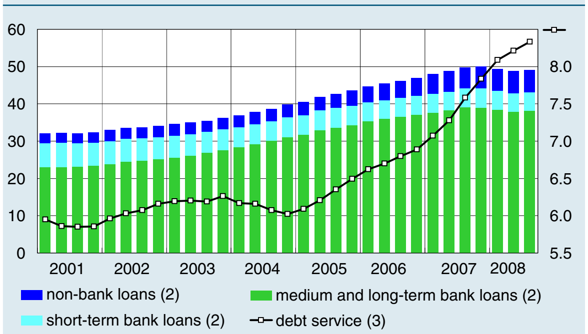
Household consumption and income and consumer confidence in Italy
(percentage rates of increase; indices)



Sources: Based on ISAE and Istat data.
(1) Chain-linked volumes; percentage changes in relation to preceding year. Data for the first nine months of 2008 are adjusted for seasonal and calendar effects. – (2) Obtained using the deflator of consumption of resident households; our estimates for the first nine months of 2008. – (3) Indices: 1980=100, seasonally adjusted data. – (4) Moving average for the three months ending in the reference month.

Figure 25

Household debt (1)
(as a percentage of gross disposable income)

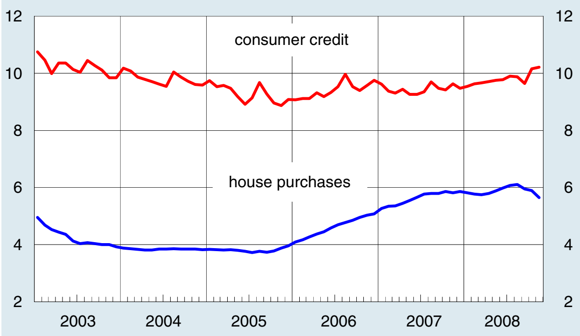


Sources: Based on Bank of Italy and Istat data.
(1) Disposable income for 2008 is estimated on the basis of quarterly national accounts data. Data on loans in 2008 are provisional. – (2) End-of-period stocks. – (3) Right-hand scale. Refers only to consumer households and to the twelve months ending in the reference quarter. Debt service includes payment of interest and repayment of principal. Interest is calculated by multiplying the outstanding stocks in each period by an average rate that takes account of the composition of the stock according to maturity and type of intermediary; repayments of principal are estimated on the basis of supervisory reports.

to their disposable income remained basically unchanged at 49 per cent, with a slight increase in the medium and long-term bank loan components (Figure 25). Nevertheless, the ratio remains very low by international standards, at around half the euro-area average and one third the level recorded in the United States and the United Kingdom. Households' debt servicing costs (interest and principal) continued to rise and were equal to 8.3 per cent of disposable income in the twelve months ending in September. Two thirds of the increase was due to larger repayments of principal and the remainder to higher interest rates resulting from banks' continuing difficulty in raising funds on the interbank and bond markets. At the end of the year, there was a fall in the interest rates for house-purchase loans (Figure 26).

Figure 26

Interest rates on bank loans to households: APRC on new business (1)
(monthly data; percentages)



(1) The data on bank lending rates refer to euro transactions and are gathered and processed using the Eurosystem's harmonized method. "New business" means contracts concluded during the reference period or contracts renegotiating previous terms and conditions. The APRC (annual percentage rate of charge) includes ancillary expenses (administrative expenses, loan examination fees and insurance) and is calculated as the average rate across all maturities, weighted by loan amounts.

3.4 FOREIGN DEMAND AND THE BALANCE OF PAYMENTS

In the third quarter of 2008 exports declined ...

In the third quarter of 2008 exports of goods and services declined by a further 1.6 per cent in volume terms by comparison with the preceding period. This reduction was entirely due to the goods component (-2.0 per cent), where sales fell in all the main outlet markets and, in particular, in Germany, France and the other EU countries. Outside the EU, the decline in the real exchange rate of the euro, which returned to its end-2007 levels, was not enough to offset the adverse effects of the weakening international economic climate. In the third quarter the reduction in exports in volume terms again involved almost every sector. The sectors worst affected were chemicals and, as a result of weakening world demand for investment goods, metal products and machinery. The contraction in exports of traditional Italian consumer goods (textiles and clothing, leather goods and footwear, furniture and wood products) continued.

... more than imports

The reduction of 0.5 per cent in total imports in volume terms compared with the previous quarter reflected the further contraction in imports of

Table 3

Italy's balance of payments (1)
(billions of euros)

	2006	2007	Jan.-Oct. 2007	Jan.-Oct. 2008
Current account	**-38.5**	**-37.4**	**-28.4**	**-39.1**
Goods	-10.2	2.9	3.3	1.4
non-energy products (2)	*37.5*	*47.7*	*39.1*	*49.1*
energy products (2)	*-47.7*	*-44.7*	*-35.8*	*-47.7*
Services	-1.3	-7.0	-5.4	-4.9
Income	-13.6	-19.7	-16.5	-24.5
Current transfers	-13.5	-13.7	-9.9	-11.2
Capital account	**1.9**	**2.7**	**1.7**	**2.6**
Financial account	**25.4**	**26.1**	**16.4**	**40.2**
Direct investment	-2.3	-37.0	-32.0	-20.1
Portfolio investment	44.3	18.1	8.5	114.2
Financial derivatives	-0.4	0.4	-0.7	5.3
Other investment	-16.7	46.1	43.1	-54.3
Change in official reserves	0.4	-1.5	-2.5	-4.9
Errors and omissions	**11.2**	**8.6**	**10.3**	**-3.6**

(1) Provisional data for September and October 2008. – (2) Based on Istat data on foreign trade.

goods (-1.2 per cent), which was partially offset by the recovery in imports of services (2.7 per cent). In both the second and the third quarters of 2008, purchases of goods from the EU in volume terms accounted for a little more than half of the total reduction, which was also influenced by the contraction in exports, due to their heavy import content.

The data for October on total foreign trade in value terms and those for November on non-EU trade indicate a further slowdown of both exports and, to a lesser extent, imports.

The deficit on the current account is increasing; the energy deficit is decreasing

In the first ten months of 2008 the deficit on the current account of the balance of payments rose to €39.1 billion, compared with €28.4 billion in the corresponding period of 2007 (Table 3); it stood at 1.9 per cent of GDP in the third quarter of the year, against 3.4 per cent in the second. The trade balance was basically in equilibrium in the period from January to October (€1.4 billion), in relation to the increase in both the surplus on non-energy products and the deficit on energy products, which rose to €47.7 billion (almost €12 billion more than in the corresponding ten months of 2007). However the energy deficit steadily decreased on a monthly basis in line with the fall in the price of oil in euros from the peak prices of last July. The deficit on services fell slightly to €4.9 billion. The rising trend of the deficit on the income account continued (reaching €24.5 billion), as a result of the worsening of the net international investment position (to -7.5 per cent of GDP at the end of June 2008), the increase in outlays on interest payments on Italian government securities in non-resident portfolios, and the large dividends paid in May and June.

The shift in the composition of foreign investment that began in August 2007 has become more pronounced

In the first ten months of 2008 the financial account showed a net outflow of €20.1 billion in direct investment; both Italian investment abroad and foreign investment in Italy slowed considerably compared with the same period in 2007. Portfolio investment continued to show substantial net inflows (€114.2 billion), owing mainly to non-residents' purchases of Italian debt securities and residents' disposals of foreign equities and fund units. The repatriation of funds invested in relatively more risky foreign assets, such as shares and fund units, which began at the onset of the financial crisis in August 2007, increased considerably in October as the financial turmoil became more acute. The large-scale purchases by non-residents of Italian government securities, in particular BOTs and BTPs, continued.

Table 4

Labour force status of the Italian population

	Average Jan.-Sept. 2007	Average Jan.-Sept. 2008	Q3 2007	Q3 2008	Change (1)
	Thousands of persons				
Total persons in work	**23,187**	**23,423**	**23,417**	**23,518**	**0.4**
Employees	**17,106**	**17,416**	**17,326**	**17,650**	**1.9**
of which: fixed-term contracts	*2,264*	*2,346*	*2,361*	*2,406*	*1.9*
part-time contracts	*2,394*	*2,580*	*2,471*	*2,594*	*5.0*
Self-employed	**6,081**	**6,007**	**6,092**	**5,868**	**-3.7**
Labour force	**24,644**	**25,087**	**24,818**	**25,045**	**0.9**
men	*14,754*	*14,883*	*14,858*	*14,900*	*0.3*
women	*9,890*	*10,204*	*9,960*	*10,145*	*1.9*
Population	**58,825**	**59,281**	**58,935**	**59,390**	**0.8**
	Percentages				
Unemployment rate	**5.9**	**6.6**	**5.6**	**6.1**	**0.5**
men	*4.8*	*5.3*	*4.4*	*4.9*	*0.5*
women	*7.6*	*8.5*	*7.4*	*7.9*	*0.5*
Participation rate (age 15-64)	**62.4**	**63.0**	**62.7**	**62.8**	**0.2**
men	*74.3*	*74.5*	*74.7*	*74.4*	*-0.2*
women	*50.4*	*51.6*	*50.7*	*51.3*	*0.6*
Employment rate (age 15-64)	**58.6**	**58.8**	**59.1**	**59.0**	**-0.1**
men	*70.7*	*70.4*	*71.3*	*70.7*	*-0.6*
women	*46.5*	*47.2*	*46.9*	*47.2*	*0.3*
North	*66.6*	*67.0*	*66.9*	*67.2*	*0.3*
Centre	*62.4*	*62.8*	*62.9*	*62.7*	*-0.2*
South	*46.5*	*46.2*	*47.0*	*46.4*	*-0.6*

Source: Istat labour force surveys.
(1) Percentage change for persons and change in percentage points for rates.

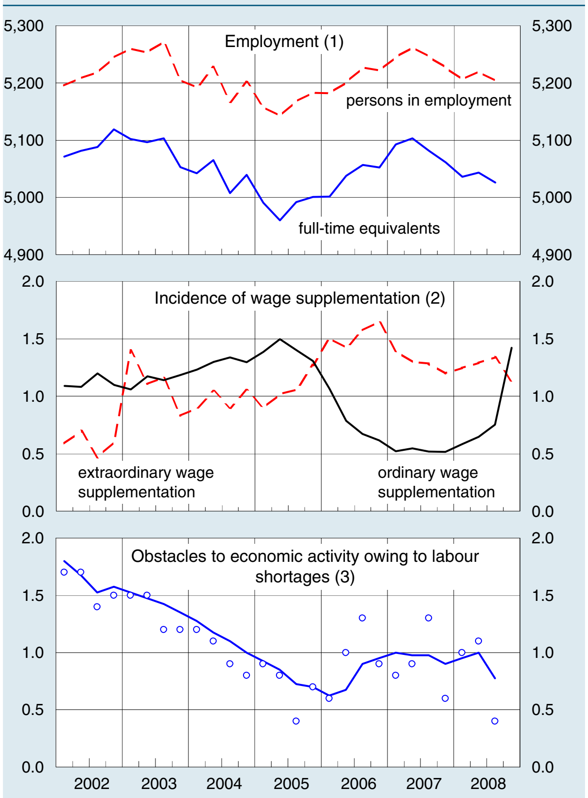
3.5 THE LABOUR MARKET

Employment is slowing, the labour input falling

According to the national accounts, the seasonally adjusted number of persons in employment in the third quarter of 2008 remained substantially unchanged with respect to the preceding period; the labour input, measured by standard labour units, fell by 0.7 per cent, partly owing to the increase in the share of part-time jobs. A similar picture emerges from Istat's labour force survey, which shows a 0.1 per cent rise in employment between the second and third quarters of 2008. Growth was concentrated in the North and the Centre (0.2 and 0.6 per cent respectively; -0.6 per cent in the South) and in sectors other than industry excluding construction. On a twelve-month basis employment grew by 0.4 per cent (around 100,000 persons; Table 4), markedly less than in the four previous quarters (between 1.2 and 1.8 per cent).

Figure 27

Employment and wage supplementation in industry excluding construction



Sources: Based on data from Istat, national accounts, INPS and ISAE *Inchiesta sulle imprese manifatturiere ed estrattive*.
(1) Total employment (persons in employment) and standard labour units (full-time equivalents) as defined in the national accounts; quarterly data. – (2) Average number of equivalent employees on ordinary or extraordinary wage supplementation in the quarter as a percentage of the number of equivalent persons in payroll employment as defined in the national accounts; partial estimates for the fourth quarter of 2008. – (3) Percentage of total firms; quarterly data and moving averages of the four surveys ending in the one indicated.

The non-Italian, female and part-time components are increasing

Compared with the third quarter of 2007 the number of non-Italian, female and payroll workers all increased (by 285,000, 127,000 and 324,000 respectively); for the first time since 1997 male employment declined, by 0.2 per cent, equal to a decrease of around 27,000 workers. The ratio of fixed-term employees to total employees remained unchanged at 13.6 per cent; the share of part-time employees rose from 14.3 to 14.7 per cent.

The employment rate remains stagnant

In the third quarter the employment rate in the 15-64 age group was roughly the same as in the third quarter of 2007 at 59 per cent; among men the rate declined by 0.6 percentage points. The labour supply expanded by 0.9 per cent, a pronounced slowdown compared with the preceding quarters; the unemployment rate rose by 0.5 percentage points to 6.1 per cent.

In the third quarter of 2008, the decline in the number of workers employed in industry excluding construction was accompanied by an increase in the number of hours authorized under the Wage Supplementation Fund, the ordinary scheme in particular (Figure 27). Recourse to the ordinary scheme accelerated strongly in the fourth quarter of the year. The ISAE survey on manufacturing and extractive firms revealed a decline in the third quarter in the number of businesses signalling labour shortages.

The acceleration in earnings reflects one-off payments

In the third quarter of 2008 de facto per capita earnings grew by 4.8 per cent compared with the same period in 2007 (by 5.1, 6.0 and 3.1 per cent in industry, private services and public services respectively). On average for the first three quarters of 2008, growth in earnings was markedly faster than in the same period of the previous year (4.8 as against 1.4 per cent), primarily due to the one-off payments associated with contract renewals; once these effects have run their course, growth in earnings should return to moderate levels in 2009, when collective contracts relating to only a little over 10 per cent of total wages will expire.

3.6 PRICE DEVELOPMENTS

Inflation is falling sharply

According to preliminary data for December, consumer price inflation measured by the index for the entire resident population (CPI) averaged 3.3 per cent in 2008, up from 1.8 per cent in the previous year. As elsewhere in the euro area, since September price developments have abruptly reversed the upward trend under way for around one year, in line with the marked decline in the prices of basic commodities on international markets. In the fourth quarter of 2008 consumer prices increased by 2.8 per cent on a twelve-month basis, compared with a peak of 4 per cent on average in the preceding quarter (Table 5); the harmonized index (HICP) showed a similar pattern.

Since last September the monthly variations in the seasonally adjusted CPI index decreased sharply and turned negative (except in October) thanks to the significant falls in fuel prices. The gradual deceleration in food prices also contributed to the decline in inflation, whose twelve-month growth rate fell to 4.7 per cent in November, from 6.2 per cent in August. After climbing slightly until August (2.3 per cent), core inflation – calculated by excluding food and energy products from the general index – declined in the following months to just over 2 per cent (Table 5).

In the last part of 2008 there was a significant decline in the price inflation for goods and services purchased most frequently by Italian households: in November, based on the indicator calculated by Istat, this component stood at a twelve-month rate of 3.3 per cent, about half the maximum level reached last July. Since the end of the summer producer prices have also fallen sharply, dropping to a twelve-month rate of 2.3 per cent in November, from 8.7 per cent in July. The marked month-on-month declines in energy prices were accompanied by smaller falls in the prices of other intermediary products, reflecting the falling prices of basic commodities and of metals in particular. Producer

Table 5

Indicators of inflation in Italy

(twelve-month percentage changes)

	HICP (1)		CPI (2)			PPI (4)
	Overall index	Excl. energy and food	Overall index	1-month	Core component (3)	Overall index
2006	2.2	1.6	2.1	–	1.6	5.6
2007	2.0	1.8	1.8	–	1.6	3.5
2008	(3.5)	….	(3.3)	–	….	….
2007 – Jan.	1.9	1.5	1.7	0.1	1.4	4.0
Feb.	2.1	2.0	1.8	0.3	1.5	4.0
Mar.	2.1	2.0	1.7	0.2	1.4	3.8
Apr.	1.8	1.8	1.5	0.2	1.3	3.3
May	1.9	1.8	1.5	0.3	1.4	3.0
June	1.9	1.9	1.7	0.2	1.4	2.7
July	1.7	1.7	1.6	0.2	1.6	2.0
Aug.	1.7	1.8	1.6	0.2	1.7	2.1
Sept.	1.7	1.7	1.7	0.0	1.5	3.5
Oct.	2.3	1.9	2.1	0.3	1.7	3.7
Nov.	2.6	1.9	2.4	0.4	1.7	4.8
Dec.	2.8	2.0	2.6	0.3	1.8	4.7
2008 – Jan.	3.1	2.1	3.0	0.4	1.9	5.4
Feb.	3.1	2.0	2.9	0.2	1.8	5.9
Mar.	3.6	2.4	3.3	0.5	2.1	6.4
Apr.	3.6	2.1	3.3	0.2	2.0	6.3
May	3.7	2.2	3.6	0.5	2.0	7.5
June	4.0	2.3	3.8	0.4	2.2	8.2
July	4.0	1.9	4.1	0.5	2.2	8.7
Aug.	4.2	2.5	4.1	0.1	2.3	8.4
Sept.	3.9	2.3	3.8	-0.3	2.1	7.3
Oct.	3.6	2.5	3.5	0.0	2.2	5.1
Nov.	2.7	2.2	2.7	-0.4	2.1	2.3
Dec.	(2.3)	….	(2.2)	(-0.1)	….	….

Sources: Based on Istat and Eurostat data.
(1) Harmonized index of consumer prices. – (2) Index of consumer prices for the entire resident population; it differs from the harmonized index primarily on account of the different method of recording the prices of pharmaceutical products and promotional sales. – (3) Overall index excluding energy and food prices. – (4) Index of producer prices of industrial products sold on the domestic market.

for food products also recorded slight declines, in line with the euro-area average, suggesting that the downward trend in the corresponding consumer prices will intensify in the coming months.

The gap between Italy and the euro-area average in the twelve-month rate of increase in the HICP widened again in 2008, to around half a percentage point on average in the third quarter, as a consequence of the acceleration of core inflation in Italy.

Disinflation will intensify in the coming months

In the latter part of 2008, as fears over the severity and duration of the recession intensified, forecasters surveyed by Consensus Economics significantly lowered their average inflation expectations for this year, to 1.6 per cent in the December survey, compared with 2.7 per cent in the summer. As in the rest of the euro area, inflation should fall to minimum levels in the third quarter, based on a comparison with the 2008 statistics. European Commission surveys also recorded a marked improvement in how households and businesses viewed price movements in the coming months. According to the quarterly survey conducted in December by the Bank of Italy in collaboration with *Il Sole 24 Ore*, weakening prospects for economic growth should lead businesses to adopt significantly more cautious pricing policies than those predicted last September, with expectations of their remaining substantially unchanged this year.

3.7 BANKS

New measures to sustain financial system stability

The actions undertaken in early October to protect savers and maintain adequate liquidity and capitalization of banks have now been supplemented by additional measures (see the boxes "The measures adopted in Italy for the stability of the financial system" and "The collaterized interbank market") designed to strengthen the system's overall ability to finance economic activity.

THE MEASURES ADOPTED IN ITALY FOR THE STABILITY OF THE FINANCIAL SYSTEM

The measures adopted in Italy to preserve the stability of the financial system are aimed at protecting savers and maintaining adequate levels of bank liquidity and capitalization.

Decree Law 155 of 9 October 2008, ratified with amendments by Law 190 of 4 December (see the box "The Italian authorities' measures for the stability of the financial system" in *Economic Bulletin* no. 50, October 2008) authorizes the Ministry for the Economy and Finance to provide a supplementary state guarantee for three years for retail bank deposits, further strengthening Italy's depositor protection system, which already offers a high level of protection.

Emergency measures are also envisaged, such as recourse to crisis management procedures in the event of a severe liquidity crisis at a bank and the simplification of lending by the Bank of Italy to intermediaries in order to cover liquidity needs. Article 1-*bis* of Decree Law 155/2008, which was introduced during the decree's ratification by Parliament and essentially reproduces the contents of Decree Law 157 of 13 October 2008, envisages three instruments to sustain bank liquidity that are regulated by the implementing ministerial decree issued on 27 November. Up to December 2009 the Ministry for the Economy and Finance may provide a state guarantee for Italian banks' new liabilities with a residual maturity of between three months and five years that are not counted in the issuer's regulatory capital. In addition, provision is made for the possibility of carrying out renewable swaps with a maximum maturity of six months between Italian government securities and newly issued bank liabilities for amounts of at least €500,000. This facility flanks the instruments already put in place by the Bank of Italy and enables banks to count on readily usable securities in order to obtain liquidity. Banks may also resort to it in order to access the new collateralized segment of the interbank market, promoted by the Bank of Italy (see the box "The collateralized interbank market").

For both the state guarantee and securities swaps, the financial instruments must be denominated in euros and envisage redemption at maturity in a single payment (bullet maturity). In addition, they must not be structured or complex securities or have a derivative component.

To facilitate the procurement of liquidity, the decree law provides for a public guarantee for operators that temporarily sell securities eligible for Eurosystem refinancing operations to banks.

For the purposes of admission to the facilities, the Bank of Italy assesses the applicant bank's compliance with the capital requirements (with reference to Tier 1 and total capital) and its profitability in the last three financial years. In line with the Community guidelines on state aid (European Commission Communication of 13 October 2008), limits are set on the expansion of banks' assets and requirements are laid down with a view to preventing banks from misusing the public aid they receive.

In line with the Eurosystem recommendations, the state guarantees carry a fixed cost (of 0.50 percentage points) for transactions with a maturity of up to one year; for transactions with longer maturity the cost reflects the issuer risk, derived from the spread on five-year credit default swaps. For securities swaps, there is a fixed fee of 1 percentage point.

With a view to ensuring an adequate level of bank capitalization, Decree Law 155/2008 also allows the Ministry for the Economy and Finance, up to 31 December 2009, to subscribe capital increases by Italian banks or bank holding companies for which the Bank of Italy has ascertained a situation of capital inadequacy. The shares purchased by the Ministry do not carry voting rights and have preference in the distribution of dividends. Such intervention must be accompanied by a stabilization and strengthening plan, which will be evaluated by the Bank of Italy taking account, among other factors, of the dividend policies approved by the shareholders' meeting. The issuer may redeem the shares, provided the Bank of Italy attests that this is not prejudicial to the solidity of its capital base.

Article 12 of Decree Law 185 of 29 November 2008, now before Parliament for ratification, empowers the Ministry for the Economy and Finance up to 31 December 2009 to subscribe financial instruments issued by listed Italian banks or bank holding companies that qualify as regulatory capital. The Bank of Italy will assess the situation of the bank's capital and the characteristics of the financial instruments. Unlike the recapitalization envisaged by Decree Law 155/2008, this measure is addressed to sound banks and is intended to strengthen their ability to meet the demand for loans. An issuer may redeem the financial instruments, provided the Bank of Italy judges that redemption is not prejudicial to the solidity of the intermediary's capital base; in addition, issuers may request conversion of the financial instruments into shares. Banks intending to avail themselves of this facility must adopt a code of ethics, particularly regarding executive compensation policies, and undertake, on the basis of a memorandum of understanding, to lend to households and small and medium-sized enterprises on appropriate terms and conditions.

The economic terms of the different recapitalization measures are now being decided. The remuneration of the equity purchased by the state will be determined in line with the Community provisions (European Commission Communication of 5 December 2008).

In conformity with the European guidelines, the public intervention is intended to be temporary.

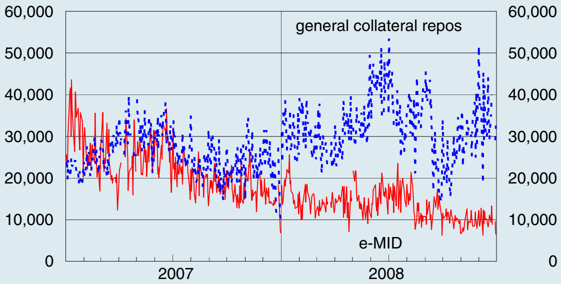
THE COLLATERALIZED INTERBANK MARKET

The financial crisis has provoked a sizable contraction in turnover and a significant increase in risk premiums on the market for liquidity. These developments have mainly concerned uncollaterlized transactions, which have been declining continuously since the summer of 2007 on the e-MID electronic interbank market, compared with the more variable profile of turnover on the general collateral segment of the regulated repo market operated by MTS (see the figure).

The drying up of the usual uncollateralized source of liquidity and the crisis of the commercial paper market have accentuated banks' dependence on the funds made available by the Eurosystem.

Figure

e-MID and general collateral repos
(daily turnover in millions of euros)



To foster the recovery of the interbank market, the Bank of Italy, together with the Italian Banking Association and e-MID SIM, have designed a trading scheme that uses the platform operated by e-MID SIM to offer participants, alongside the existing types of contract, the possibility of carrying out trades in euros anonymously and with protection from credit risk. The anonymity of bilateral contracts is made possible by the role performed by the Bank of Italy, which evaluates the collateral provided by the participating banks, provides prompt settlement of transactions if a party to a contract defaults and proceeds to realize the collateral, ensuring the performance of contracts.

The scheme envisages a partial mutualistic sharing of default risk; where the collateral provided is insufficient, the other market participants jointly make up the difference within the limit of 10 per cent of the collateral contributed at the time of their accession to the new market segment.

To expand the operational possibilities of banks in the new segment, potential collateral comprises not only instruments eligible for ECB operations, but also bank liabilities guaranteed by the state under Law 190/2008, financial instruments that may be used for securities lending transactions with the Bank of Italy, and other securities with certain characteristics (for example, their rating) deemed acceptable by the Bank of Italy on a case-by-case basis. In a subsequent phase it will also be possible to use bank loans.

The new market segment is scheduled to remain operational until 31 December 2009, but its life could be extended should market conditions warrant. Since the initiative is also aimed at lengthening the maturities of trades, contracts with a maturity of from one week up to six months are tradable on the segment; as experience is gained, trades may be extended to non-standard and shorter maturities.

Individual intermediaries may participate in the activity of the collateralized market up to the value of the collateral they have put up or 30 per cent of their consolidated regulatory capital, whichever is lower, with a ceiling of €5 billion. In addition, intermediaries whose gross exposure reaches or exceeds 20 per cent of the total of collateral provided by all the participants in the scheme may not increase their exposure further in the new market segment.

The collateralized market is reserved to Italian banks. In the future it may be extended to EU credit institutions that satisfy requirements similar to those established for Italian participants, subject to an understanding with their home-country authorities. For each banking group only a single bank may participate, but it will nevertheless be able to contribute collateral pertaining to other group banks. An advisory committee composed of the Bank of Italy, e-MID SIM, the Association of Bank Treasurers (ATIC) and the Italian Banking Association will examine any problems that arise in the functioning of the new market segment and assess proposed changes to its functions and operating characteristics.

Bank lending slows further, reflecting demand ...

The growth in bank lending in Italy, net of the accounting effect of securitizations, decreased sharply in 2008 from the rapid pace of the previous two years, falling in November to a twelve-month rate of 8.7 per cent (Figure 28) and to a seasonally adjusted annual rate of 5.7 per cent over three months. Continuing the tendency observed since the end of 2007, most of the securities deriving from securitizations were repurchased by the originating institutions themselves, in order to procure eligible instruments for Eurosystem refinancing operations. The slowdown in bank lending reflected the weakness of credit demand from firms and households. The sharp slowdown registered in November (Table 6), stemmed in part, especially for short-term credit, from the deferral to 1 December of the second payment on account of self-assessed income tax (the due date, 30 November, was a Sunday). Excluding this calendar effect, it is estimated that the growth rate would have been 1 percentage point higher. Preliminary data for a large sample of intermediaries accounting for 80 per cent of total bank lending indicate that growth picked up slightly in the first twenty days of December in response to greater use of short-term credit lines, presumably for the tax payment at the beginning of the month.

... and supply factors

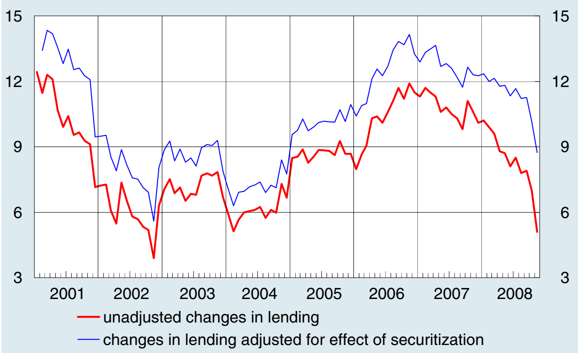
The Italian banks participating in the Bank Lending Survey completed on 7 October reported that in the third quarter they had again tightened the criteria for lending to firms (see the box "Credit supply and demand in Italy"). In lending to households, the tightening involved both loans for home purchases and consumer credit.

The quarterly survey of inflation expectations and growth in industry and services conducted in December by the Bank of Italy and *Il Sole 24 Ore* also revealed a marked worsening in the terms of access to credit since September, especially for firms that had actually applied for a new loan or an increase in an existing one. Analogous indications come from ISAE's monthly survey in December. These trends could be reflected in coming months in a further slowdown in new lending. Since the

Figure 28

The effect of securitizations on bank lending in Italy (1)

(monthly data; 12-month percentage changes)



Source: Based on Bank of Italy data.
(1) Includes other loans to resident customers assigned without recourse to entities other than MFIs.

Table 6

Main assets and liabilities of Italian banks (1)

(end-of-period data; 12-month percentage changes)

	2006	2007	November 2008	
				Stocks (2)
Assets				
Securities	5.3	7.3	49.7	340,536
Loans	11.5	10.1	5.1	1,741,613
up to 12 months	*10.8*	*7.5*	*4.2*	*589,986*
beyond 12 months	*11.9*	*11.3*	*5.6*	*1,151,627*
External assets	19.8	12.5	-2.7	396,175
Liabilities				
Domestic funding (3)	9.9	7.3	14.2	1,838,830
Deposits	8.3	4.2	9.6	1,098,668
of which (4):				
current accounts	*6.7*	*2.9*	*8.9*	*666,521*
with agreed maturity	*9.8*	*14.3*	*21.5*	*62,717*
redeemable at notice	*-0.8*	*-0.5*	*6.9*	*237,594*
repos	*29.4*	*12.1*	*15.2*	*118,183*
Bonds (3)	12.5	11.9	21.8	740,163
External liabilities	25.6	22.9	-9.4	492,717

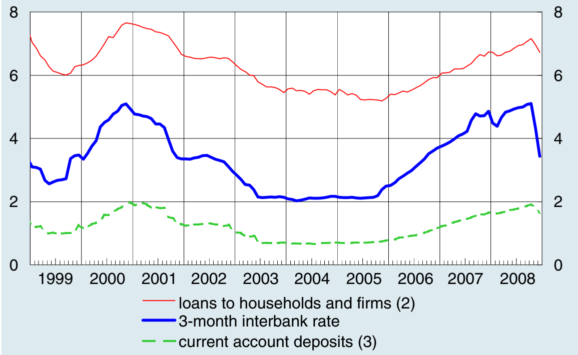
(1) The figures for November 2008 are provisional. From October 2007 onwards the data include Cassa Depositi e Prestiti S.p.A. The percentage changes are calculated net of reclassifications, exchange rate variations and other variations not due to transactions. – (2) Millions of euros. – (3) Includes bonds held by non-residents. – (4) Does not include those of central government.

end of October banks' lending rates, tracking the fall in official rates, have begun to come down, in line with expectations based on past experience (Figure 29).

Figure 29

Short-term bank interest rates (1)

(monthly data; percentages)



Sources: Based on Bank of Italy and e-MID data.
(1) The data on lending and deposit rates refer to transactions in euros and are gathered and processed using the Eurosystem's harmonized method. – (2) Average rate on loans to households and firms with a maturity of up to one year. – (3) Average rate on current account deposits of households and firms.

Loan quality has begun to be affected by the cyclical downturn

The quality of credit has started to show the effects of worsening economic conditions. Preliminary data indicate that during the third quarter of 2008 the seasonally adjusted flow of new bad debts increased in proportion to outstanding lending. The rise was sharper in the South and, by sector, in the construction industry. The default rate on loans to consumer households remained broadly unchanged.

Domestic funding accelerates, external funding slows

The twelve-month rate of growth in banks' fund-raising increased to 14.2 per cent in November, compared with 7.3 per cent in December 2007. Current account balances have risen at an accelerating pace in recent months, driven by increasing liquidity preference and, in November, by the temporary presence on firms' accounts of funds allocated for the self-assessed income tax payment deferred to 1 December. In November the growth in Italian bank bond issues accelerated to 21.8 per cent, reflecting new issues on the domestic market. About one third of this growth, however, must be ascribed to purchases by other Italian banks. The volume of intragroup interbank loans expanded further in recent months to account for some three quarters of all interbank lending at the end of November. Italian banks' net foreign borrowing diminished, owing mainly to the decline in net liabilities with non-euro-area residents.

Banks' profitability declined in the first three quarters

On the basis of consolidated quarterly financial statements, in the first nine months of 2008 the profitablity of the main Italian banking groups declined. Return on equity, calculated on an annual basis and excluding capital gains and extraordinary income, fell to 9 per cent from 11 per cent in the same period of 2007, despite an increase of 13 per cent in net interest income, higher than in the first three quarters of 2007. This increase in the earnings from traditional banking business was not enough, however, to compensate for the reduction in net fee income and the disappearance of income from trading, so gross income contracted by 5 per cent. The fall would have been greater if not for the revision of international accounting standards, which allowed banks to carry a smaller amount of assets at market value. Given broadly stable operating expenses, operating profit fell by 11 per cent. The cyclical downturn translated into significantly increased allocations to provisions and value adjustments, entirely accounted for by the component covering the deterioration in loan quality. The increase of nearly 40 per cent in this component absorbed more than a quarter of operating profit, compared with less than a fifth in the same period of 2007.

On the whole the Italian banking system has so far suffered less than others from the impact of the crisis, thanks in part to a model of intermediation based on the granting of loans and retail fund-raising. Since the onset of the turmoil the leading banking groups have made crisis-related writedowns totaling about €4.5 billion, a limited amount by comparison with the largest international banks, some of which recorded losses for the first half of 2008.

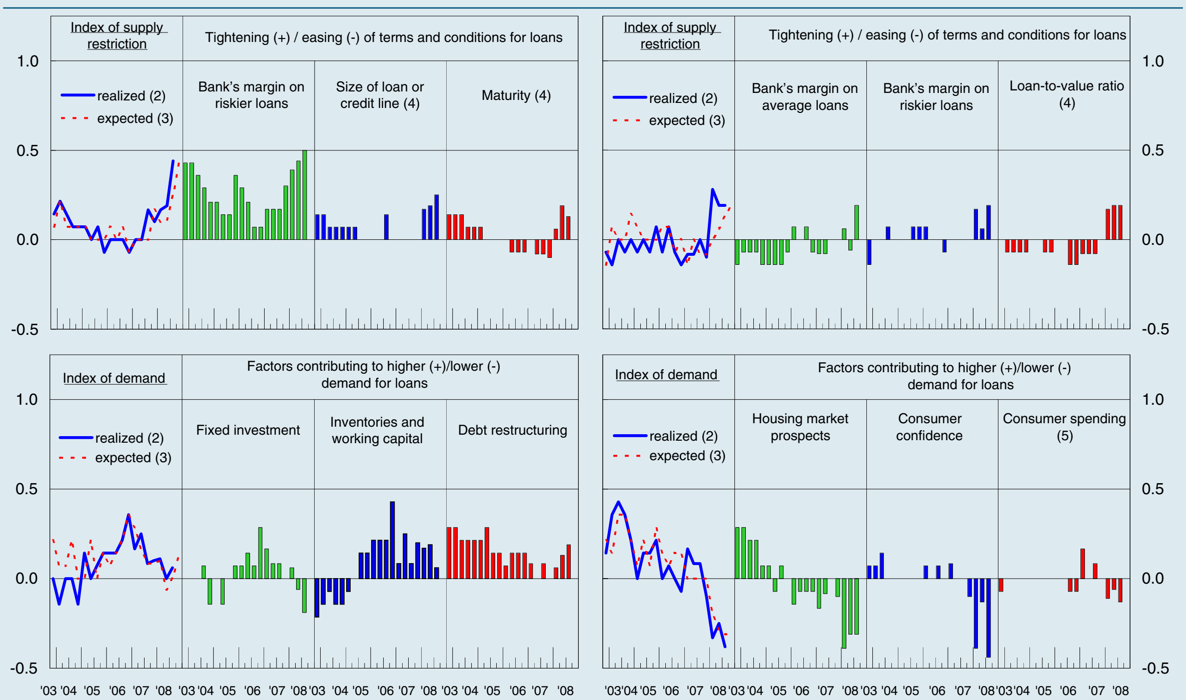
Looking to the future, the serious worsening of the economic cycle will adversely affect banks' profitability.

CREDIT SUPPLY AND DEMAND IN ITALY

According to the responses provided by the Italian banks participating in the quarterly euro-area Bank Lending Survey, in the third quarter of 2008 there was a further moderate tightening of credit standards for loans to firms (Figure A).[1] Compared with the other surveys carried out since the onset of the financial crisis, almost all the banks in the sample reported that they had made their credit supply policies more restrictive, although only moderately so. The tightening, which involved amounts, margins, maturities and specific covenants aimed at limiting risk, was mainly ascribable to the deterioration in the economic picture and the worsening of the crisis in the second half of September following the failure of Lehman Brothers (Figure B).

Figure A

Supply conditions and credit demand in Italy (1)



Source: Quarterly Bank Lending Survey for the euro area.
(1) Diffusion indices constructed by aggregating the qualitative replies from the groups participating in the survey, weighted as follows: for supply conditions, 1 = tightened considerably, 0.5 = tightened somewhat, 0 = remained basically unchanged, -0.5 = eased somewhat, -1 = eased considerably; for demand, 1 = increased considerably, 0.5 = increased somewhat, 0 = basically unchanged, -0.5 = decreased somewhat, -1 = decreased considerably. The range of variation of the index is from -1 to 1. – (2) Refers to the quarter ending at the moment of the survey. – (3) Forecasts made in the preceding quarter. – (4) Positive (negative) values indicate a greater (lesser) willingness of banks to grant large loans, long-term loans, or loans with high loan-to-value ratios. – (5) Positive (negative) values indicate that the trend in consumer spending other than for home purchases had an expansive (restrictive) effect on the demand for mortgages.

The slight recovery in businesses' demand for credit was related chiefly to debt restructuring and consolidation. For the last quarter of 2008 the respondent banks expected that credit standards for

[1] Eight leading banking groups took part in the survey, which was completed on 7 October; the results for Italy are available at www.bancaditalia.it and those for the euro area at www.ecb.int. The results of the survey on the fourth quarter of 2008 and expectations for the first quarter of 2009 are not yet available; they will be released on 6 February.

loans to firms would tighten further, by the same magnitude as in the third quarter, while credit demand would expand at about the same pace.

The deterioration in households' creditworthiness and the negative outlook for the housing market went together with less accommodating terms and conditions for mortgage loans and consumer credit. Another factor was the high cost of funding, driven up in the autumn by the financial crisis and subsequently mitigated by monetary policy interventions. The banks stated that they had increased their margins on loans to households and, especially for mortgages, lowered their loan-to-value ratios.

Demand for mortgages continued to stagnate, while the rate of growth in demand for consumer credit showed no change. The banks expected supply and demand conditions for loans to households to remain basically unchanged in the fourth quarter of 2008.

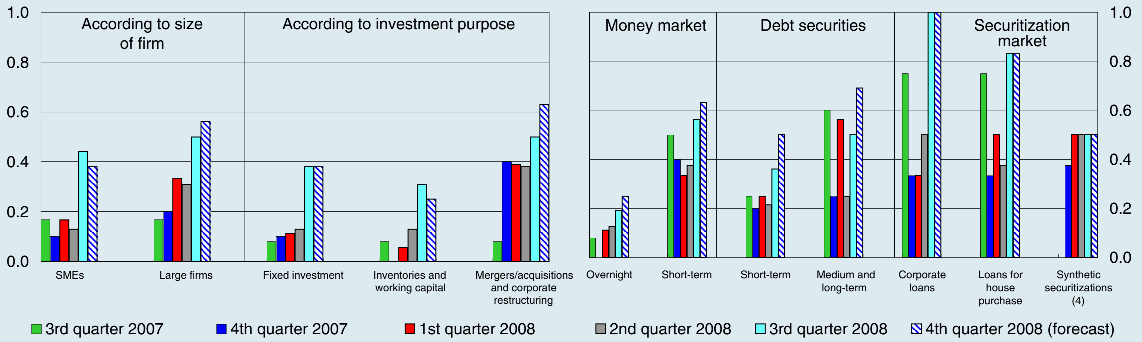
On the funding side, the indicators of difficulty in procuring funds on the wholesale market reached the highest level since the start of the crisis for nearly all the technical forms. Banks again reported that the crisis had increased the costs associated with capital requirements and in this way had affected credit supply. The expectations for the fourth quarter of 2008, formulated before the government measures to recapitalize banks and guarantee bank bonds, did not point to an attenuation of the repercussions of the crisis on credit supply and access to wholesale funding.

The Italian banks' responses to the survey were broadly in line with those of their counterparts in the rest of the euro area, although the reported tightening of credit standards for loans to firms was slightly more stringent than that recorded in the area as a whole.

Figure B

Effects of the subprime mortgage crisis in Italy (1)

Index of the effect of the crisis on the tightening of the standards for lending to firms (2) | *Index of the difficulty of obtaining funds in the wholesale market* (3)



Source: Quarterly Bank Lending Survey for the euro area.
(1) Diffusion indices constructed by aggregating the qualitative replies to the special questions on the effects of the subprime mortgage crisis added to the quarterly Bank Lending Survey. – (2) Weighted as follows: 1 = tightened considerably, 0.5 = tightened somewhat, 0 = remained basically unchanged, -0.5 = eased somewhat, -1 = eased considerably. The range of variation of the index is from -1 to 1. – (3) Weighted as follows: 1 = considerable difficulty, 0.5 = some difficulty, 0 = basically no difficulty. The range of variation of the index is from 0 to 1. – (4) These imply recourse to credit derivatives. Data for the third quarter of 2007 are not available for this indicator.

3.8 THE FINANCIAL MARKET

Another slump in share prices

The general Italian stock exchange index fell by 23 per cent in the fouth quarter, as the international financial crisis grew more acute. The fall was in line with those registered in the other main euro-area countries (Figure 30). The drop in share prices can be ascribed both to a further increase in the risk premium demanded by investors for holding equities and to the slumping current and expected earnings of listed companies. Apart from bank shares (which fell by 30 per cent), severe losses were incurred by the sectors most exposed to the deteriorating world economic situation, such as commodities (down 44 per cent), automobiles (down 44 per cent) and consumer goods (down 34 per cent). Oil company shares were less seriously affected (down 14 per cent) despite the fall in crude oil prices. For the year as a whole, Italian equities lost practically half their value (49 per cent).

Current earnings/price ratios rose still further to nearly twice their 20-year average (Figure 31). The expected volatility of share prices, after soaring in October, eased in November and December but remained at historically high levels.

The ongoing financial strains continued to discourage new listings. There was not even one in the fourth quarter and only seven for the entire year, compared with 32 in 2007. At the end of 2008 there were 294 Italian companies listed on Borsa Italiana with a total market capitalization of €375 billion (equivalent to 23.6 per cent of GDP).

Net bond issues contract

Compared with the second quarter of 2008, net bond issues by Italian companies fell by one half to €29 billion (Table 7). The decrease was accounted for chiefly by banks and, to a much lesser extent, by other financial corporations. Non-financial corporations, after making net redemptions in the second quarter, made net new issues worth almost €1 billion in the third. Bond placement gathered strength in October and November thanks to two major issues.

The risk premiums on Italian government securities are now very high ...

The yield differential between ten-year Italian Treasury bonds and German Bunds widened significantly between mid-October and the end of the year to 143 basis points, the largest spread since the introduction of the euro. In the first few days of the new year it narrowed, reaching 131 basis points on 9 January. The premiums on Republic of

Figure 30

Share prices (1)

(end-of-week data; indices, 31 December 2004=100)

Source: Thomson Financial Datastream.
(1) MIB for Italy, Dow Jones EURO STOXX for the euro area, Standard & Poor's 500 for the United States.

Table 7

Net bond issues (1)

(millions of euros)

	Banks	Other financial corporations	Non-financial corporations	**Total**
		Italy		
2006	60,371	12,349	3,426	**76,146**
2007	63,928	14,625	10,475	**89,028**
2007 – Q1	21,619	2,364	-1,199	**22,784**
Q2	15,371	7,494	7,625	**30,490**
Q3	1,793	-3,215	-706	**-2,128**
Q4	25,145	7,982	4,755	**37,882**
2008 – Q1	39,930	-3,797	-141	**35,992**
Q2	45,023	16,101	-1,417	**59,707**
Q3	15,213	13,139	824	**29,176**
		Euro area		
2006	348,200	241,591	25,676	**615,467**
2007	284,147	325,439	27,741	**637,327**
2007 – Q1	141,082	95,848	838	**237,768**
Q2	100,491	59,747	25,105	**185,343**
Q3	14,207	34,099	-5,071	**43,234**
Q4	28,367	135,746	6,870	**170,983**
2008 – Q1	34,567	9,491	-3,049	**41,008**
Q2	127,150	102,393	11,858	**241,401**
Q3	24,209	49,976	6,520	**80,705**

Sources: Bank of Italy and ECB.
(1) Bonds with a maturity at issue of more than one year, at face value, issued by resident companies belonging to the sector indicated. The nationality and sector refer to the issuer and not to the company that controls it. Net issues are equal to the difference between the face value of the securities issued and that of the securities redeemed.

Italy credit default swaps also increased. Similar if less pronounced movements were recorded for other sovereign borrowers, owing to the general increase in risk aversion and worsening budget positions (Figure 32). The spreads between Italian and German securities also reflected investors' strong preference for highly liquid assets, benefiting the Bund, which is the underlying asset for a very well-developed futures market.

... as are those on private bonds

The yield differentials between the investment-grade bonds of Italian non-financial corporations and Treasury bonds widened futher in the fourth quarter. Between mid-October and early January the total increase came to 1.6 percentage points, against a widening of 1.2 points for the equivalent corporations in terms of sector and quality in other euro-area countries. The premiums on credit default swaps on Italian banks remained practically unchanged at around the same levels as for the other main European banks.

The outflow of savings from investment funds continues

The third quarter saw further net redemptions of investment fund units in Italy, although the outflow of €28.8 billion was less than in the two previous quarters. Substantial disinvestment was recorded in other euro-area countries as well. Hedge funds had sizable outflows (€1.6 billion) for the second consecutive quarter. The average return on harmonized funds remained slightly negative (-1.4 per cent). The worst performance was turned in by equity funds (-10.1 per cent), while bond funds had a positive average return of 1.6 per cent. Individually managed portfolios also suffered a net outflow of savings (€12.3 billion); their average yield in the quarter was practically nil (-0.2 per cent).

3.9 THE PUBLIC FINANCES

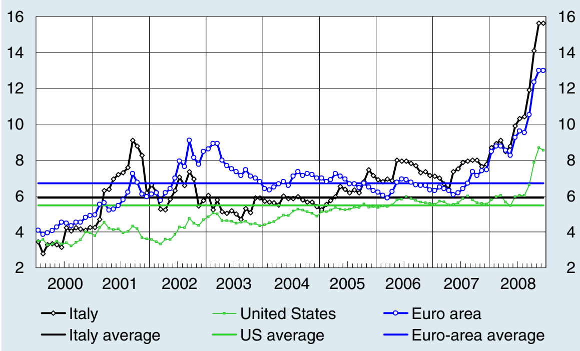
The borrowing requirement turns upwards

The state sector borrowing requirement came to €52.9 billion in 2008, €23.3 billion more than in 2007 (Figure 33). The ratio of the requirement to GDP thus rose from 1.9 to 3.4 per cent (using the estimate of nominal GDP produced by the forecasting exercise presented in section 3.10

Figure 31

Current earnings/price ratios for the main stock exchanges (1)

(monthly data; percentages)

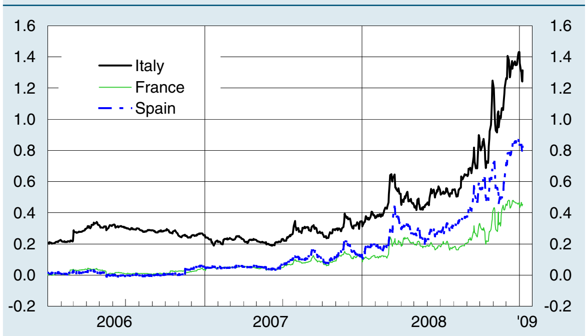


Sources: Thomson Financial Datastream and Bank of Italy data.
(1) Averages are calculated from January 1986.

Figure 32

Interest rate differentials between ten-year government securities and corresponding German securities

(daily data; percentage points)

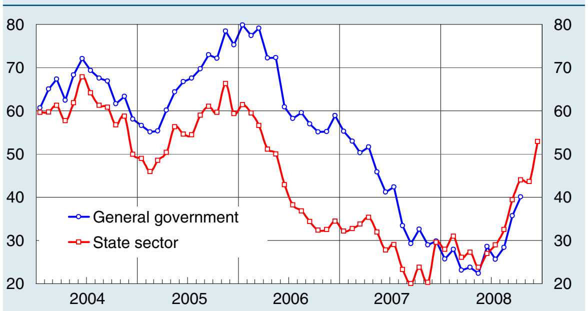


Source: Based on Bloomberg data.

Figure 33

Rolling twelve-month borrowing requirement (1)

(millions of euros)



Source: For the state sector, Ministry for the Economy and Finance.
(1) Net of privatization receipts.

below). The increase chiefly reflects the slowdown in tax revenue due to the initial effects of the cyclical downturn and to some tax reductions enacted in the last two years. Almost all of the increase in the borrowing requirement emerged in the last four months of the year, most notably in December. The surplus registered in that month fell from €12.2 billion in 2007 to just €2.9 billion, owing to the reduction in revenue, increased transfer payments to settle past health system debts, increased drawings of funds by local governments and some measures enacted at the end of November, whose effects included an increase in tax refunds (see the box "The anti-crisis decree").

THE ANTI-CRISIS DECREE

At the end of November the Council of Ministers approved a decree law to sustain the economy (Decree Law 185 of 29 November 2008). According to official estimates, its effect on net borrowing will be essentially nil in 2009 and the two following years (see table).

Table

The effects of Decree Law 185/2008 on the general government consolidated accounts (1)

(millions of euros)

	2009	2010	2011
REVENUE			
Revenue increases	**4,976**	**2,357**	**2,360**
Substitute tax on asset revaluations	2,757	123	80
Intensified tax auditing and collection	851	1,568	1,457
Recovery of general government credits	750	100	100
VAT on television services	214	270	270
Surtax on pornography	254	147	154
Other	150	150	300
Revenue decreases	**-1,827**	**-1,302**	**-1,762**
Measures for firms	-1,278	-1,151	-1,722
IRAP deductibility	*-1,090*	*-657*	*-642*
Deferral of VAT payments	*-188*	*-31*	*-31*
Corporate income tax and IRAP reductions in connection with substitute tax on asset revaluations	*0*	*-463*	*-1,049*
Measures for households	-549	-151	-39
Tax exemption of productivity bonuses	*-460*	*-128*	*0*
Tariffs and other	*-89*	*-23*	*-39*
NET REVENUE INCREASE	**3,149**	**1,055**	**599**
EXPENDITURE			
Expenditure increases	**3,765**	**1,935**	**2,065**
Measures for households	2,950	250	250
Bonus for low-income households	*2,400*	*0*	*0*
Mortgages	*350*	*0*	*0*
Unemployment benefits	*200*	*250*	*250*
Reimbursement to firms for IRAP deductibility	100	500	400
Objective Law funding	60	400	150
Transfers to State Railways	480	720	1,200
Expenditure for privatization of Tirrenia group	65	65	65
Other	110	0	0
Expenditure decreases	**-645**	**-1,000**	**-1,545**
Reduced vocational training expenditure, to finance unemployment benefits	-100	-150	-150
Reduced appropriations to finance transfers to State Railways	-480	-720	-1,200
Reduced appropriations to finance expenditure by Tirrenia group	-65	-130	-195
NET EXPENDITURE INCREASE	**3,120**	**935**	**520**
REDUCTION IN NET BORROWING	**29**	**120**	**79**

(1) Based on official estimates (Chamber of Deputies Act no. 1972).

The decree law introduces a series of expenditure reductions and revenue increases, procuring resources of €5.6 billion in 2009, €3.4 billion in 2010 and €3.9 billion in 2011, which are to be used to help low-income households, reduce taxes on firms and stimulate investment.

Households will receive two thirds of the resources allocated in 2009 (€3.5 billion). Specifically, the law provides for a one-off transfer payment to low-income households, an easing of variable-rate mortgage instalments through government assumption of liability for interest payments above a predefined level, income supplementation in the case of unemployment for some categories of workers, the extension to 2009 of the tax exemption for productivity-linked pay, and a freeze on the automatic tariff increases for some services provided directly by the state.

Firms get resources worth €1.4 billion in 2009, and the amount will increase over the next two years to €2.1 billion in 2011. The provisions include a permanent cut in corporate income tax by means of partial deductibility of IRAP and the possibility, in some cases, of paying VAT when payment for goods or services is actually received rather than when the invoice is issued.

To spur investment in infrastructure and public works, the decree law institutes new appropriations over the next 15 years, which should activate private-sector spending of some €2 billion as early as 2009. The additional budgetary outlays are set at €0.1 billion in 2009, €0.4 billion in 2010 and €0.2 billion in 2011. Additional measures envisaged, to be financed by reducing allocations to the Fund for Underutilized Areas, consist of investment grants to the State Railways group, transfers for the service contract renewal of Trenitalia S.p.A. and funds to foster the privatization of the Tirrenia group (a total of €0.5 billion in 2009, €0.8 billion in 2010 and €1.3 billion in 2011).

Apart from the reduction of the Fund for Underutilized Areas, the financing for these measures will come from the introduction of some substitute taxes on voluntary revaluations of company assets, intensified tax auditing and tax collection, accelerated recovery of general government credits, and an increase in VAT on television services.

In the first ten months of 2008 the general government borrowing requirement was €49 billion, up from €38.8 billion in the same period of 2007. It was €3.3 billion lower than the state sector requirement, whereas in 2007 it had been €0.8 billion higher.

Corporate income tax revenue declines

In 2008 total state tax revenue on a cash basis, after rising strongly for two years (9.6 per cent in 2006 and 4.8 per cent in 2007), increased by a modest 1.4 per cent in 2008 (Table 8). Contributing factors were declining corporate income tax and stagnant VAT receipts (both of which had buoyed revenue in the previous years) and a decline in the receipts from some excise taxes. The performance of the main state levies for the most part reflected the economic downturn, the full effects of which will only be felt in 2009 owing to the usual lag with which trends in tax base are translated into actual tax receipts. In 2008 corporate income tax receipts declined by 5.7 per cent after rising by 28 per cent in 2007; self-assessed personal income tax remained almost unchanged after an increase of 18.8 per cent. Among indirect taxes, VAT receipts were flat (as consumption expenditure slowed) and natural gas excise tax receipts fell considerably. These trends were partly offset by the increase in the withholding tax on interest income and the strong performance of payroll withholding tax, thanks to the still positive trend in employment and the renewal of several collective bargaining agreements with back pay, whose effects were accentuated by the structure of personal income tax.

Social contribution revenue also appears to have continued its strong growth in 2008, although the figure for the full year is likely to be lower than that for the first nine months as reflected in Istat's quarterly accounts (6.7 per cent compared with the first three quarters of 2007).

Table 8

State budget tax revenue on a cash basis (1)

	Millions of euros		Percentage changes	
	2007	2008	2007	2008
Direct taxes	**219,142**	**227,512**	**7.8**	**3.8**
Personal income tax	150,130	159,389	5.7	6.2
of which: withholding tax on employee incomes	*109,375*	*117,815*	*2.6*	*7.7*
balance	*7,440*	*7,484*	*36.2*	*0.6*
payment on account	*18,948*	*19,154*	*13.2*	*1.1*
Corporate income tax	50,520	47,617	28.0	-5.7
of which: balance	*13,143*	*12,078*	*46.4*	*-8.1*
payment on account	*36,861*	*34,740*	*22.2*	*-5.8*
Withholding taxes on interest income and capital gains	13,696	14,292	12.3	4.4
interest on bank deposits and bonds	*10,620*	*12,118*	*22.6*	*14.1*
dividends	*530*	*675*	*-27.7*	*27.4*
capital gains	*1,148*	*710*	*0.9*	*-38.2*
managed assets	*1,398*	*789*	*-15.9*	*-43.6*
One-off taxes	1,226	2,069	-78.9	68.8
Taxes on insurance companies' mathematical reserves	1,105	1,267	5.3	14.7
Other	2,465	2,878	-10.7	16.8
Indirect taxes	**190,370**	**187,738**	**1.5**	**-1.4**
VAT	119,239	119,281	4.4	0.0
Other business taxes	21,870	21,231	-12.4	-2.9
Excise duties on mineral oils	20,337	20,402	-4.8	0.3
Other excise duties and sales taxes	7,334	5,537	-2.9	-24.5
Monopolies	9,790	10,013	4.7	2.3
Lotteries	11,800	11,274	15.8	-4.5
TOTAL TAX REVENUE	**409,512**	**415,250**	**4.8**	**1.4**

Source: Based on state budget data.
(1) For 2008, provisional data.

According to data for the first ten months released by the Minstry for the Economy and Finance, local government revenue shows a sharp decline of 20 per cent in receipts from the regional tax on productive activities (IRAP) as a result of tax relief in connection with labour costs enacted with the Finance Law for 2007, which firms benefited from mainly last year. Revenue from the regional surcharge on personal income tax held broadly unchanged while that from municipal surtax rose by 18.3 per cent, owing in part to rate increases enacted in 2007, after years in which the power of regions and muncipalities to enact rate increases had been suspended.

The ratio of net borrowing to GDP increases in the first nine months

The deterioration in the public finances is also signaled by the general government consolidated accounts for the first three quarters, recently released by Istat. In the first nine months, net borrowing came to 2.1 per cent of GDP, compared with 1.2 per cent in the year-earlier period. The increased deficit reflects the sharp slowdown in revenue and an acceleration in expenditure. Specifically, primary current expenditure was 5.3 per cent higher in the first three quarters than in the same period of 2007 (when the corresponding increase had been only 1.9 per cent). The main factors in the acceleration were compensation of employees and intermediate consumption.

The available data suggest that general government net borrowing, which had diminished in the previous two years, increased last year by about 1 percentage point of GDP from the 1.6 per cent recorded in 2007.

The debt/GDP ratio also turns upwards again

General government debt increased by €71.7 billion in the year through October, compared with a rise of €49.5 billion in the year-earlier period, to €1,670.6 billion. The increase mainly reflected the rise in the overall borrowing requirement (from €35.3 billion to €49 billion) and the larger increase in the volume of assets that the Treasury holds with the Bank of Italy (€16.4 billion, as against €11.1 billion). The debt/GDP ratio is likely to have risen above 105 per cent by the end of the year (from 104.1 per cent at the end of 2007).

At the end of December, Parliament passed the Finance Law for 2009; it completes the budget for 2009-2011 passed during the summer, and leaves the planned budget objectives essentially unchanged.

3.10 FORECASTS

The global crisis ...

Since our previous forecasts in the July issue of the *Economic Bulletin* the outlook for the international and the Italian economy has worsened greatly. This deterioration was reflected in a drastic fall in energy prices (the price of crude oil in euros is now lower by about 65 per cent compared with last July's peaks), leading to an easing of inflationary pressures (see the box "Assumptions underlying the forecasts").

... is driving the Italian economy into a prolonged recession

In light of these developments, taking into account the sharper-than-expected fall in industrial production in the last part of 2008, and in particular the figure for November released on 14 January, it is now forecast that the recession will continue in Italy during 2009 and that GDP will begin to increase again in 2010, benefiting from a recovery in the world economy and international trade. After falling by an average of 0.6 per cent in 2008, it is estimated that GDP will contract by 2.0 per cent in 2009, also as a result of the negative carry-over effect of the last six months of 2008, before increasing by 0.5 per cent in 2010 (Table 9 and Figure 34), reflecting the strong decline in foreign demand and the marked reductions in firms' and households' spending plans.

ASSUMPTIONS UNDERLYING THE FORECASTS

The assumptions regarding the growth of the world economy and world trade on which these forecasts are based are those used by the World Bank in its December 2008 report *Global Economic Prospects*, which projects that the volume of world trade, already slowing sharply in 2008, will contract by 2.1 per cent in 2009 and then recover in 2010 to grow by 6 per cent.

The assumptions regarding exchange rates, interest rates and oil prices are updated to take account of the information available in the ten working days preceding 12 January. The price of Brent crude oil averages $54 a barrel this year and $63 next year, about 60 per cent less than the figure assumed in the *Economic Bulletin* published last July. Three-month interest rates, calculated on the basis of Euribor future contracts, fall from an average of 4.6 per cent in 2008 to 2.3 per cent this year and then rise slightly in 2010, to 2.6 per cent. Longer-term interest rates, corresponding to the yield of a basket of government securities with a duration of about six years, decline by 0.1 percentage points to 4.3 per cent this year and then rise to 4.6 per cent in 2010. Bilateral exchange rates are assumed to remain unchanged at the average levels observed recently, with a dollar/euro conversion rate of 1.38 over the forecasting horizon.

The projections for the public finances take account of the budget for the next three years that was approved during the summer and the measures taken by the Government in the last few months.

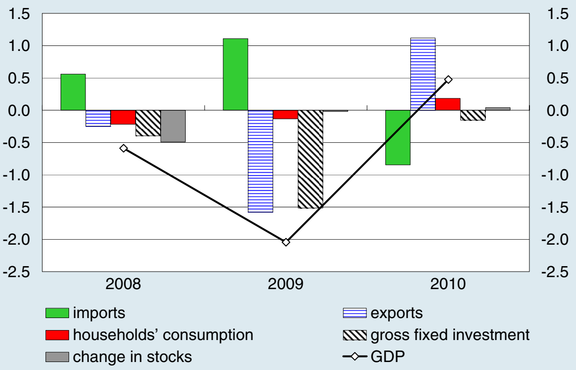
Exports should contract this year, and rise next year

It is estimated that Italian exports will return to significant growth only from 2010. On average, exports are expected to contract by more than 5 per cent this year, and increase by 4 per cent next, driven by a recovery in international trade, and also thanks to small gains in competitiveness after the large losses recorded in the last five-year period.

Figure 34

GDP growth and the contributions of the main components of demand and imports (1)

(percentages)



Sources: Based on Bank of Italy and Istat data.
(1) Adjusted for seasonal and calendar effects.

The sharp fall in investments will depress domestic demand ...

The contraction in domestic demand will gather pace this year reflecting, in particular, a sharp fall in fixed investment (by more than 7 per cent), but this is still less than the fall recorded at the time of the 1993 recession. Investment in productive capital is predicted to contract more markedly than residential investment. Contributing factors in the contraction are declining expectations for demand and business profitability and the tighter credit standards imposed by credit and financial institutions.

... which will also be affected by stagnating consumption

Consumption is expected to be less influenced by the economic downturn thanks to the positive effects of the reduction of inflation on the spending power of households, which will also benefit from the recently approved government measures in support of the less well-off. Private sector disposable income is likely to grow by an average of 0.2 per cent in real terms in 2009-10, following a fall of more than one percentage point in 2008. Consumption is expected to stagnate this year: increased spending on non-durable goods and services will offset a contraction of about 4 per cent in spending on durable goods. In 2010, as economic conditions improve, consumption is forecast to return to growth, at a rate barely slower than that estimated for GDP.

Table 9

Forecasts of the main macroeconomic variables in Italy

(percentage changes on preceding year unless otherwise indicated)

	2008	2009	2010
GDP (1)	**-0.6**	**-2.0**	**0.5**
Private consumption	-0.4	-0.2	0.3
Government consumption	1.0	0.5	0.6
Gross fixed investment	-1.9	-7.3	-0.8
Exports	-0.9	-5.5	4.0
Imports	-1.9	-3.8	3.0
Change in stocks (2)	-0.5	0.0	0.0
HICP(3)	**3.5**	**1.1**	**1.4**
GDP deflator	**3.1**	**2.3**	**1.3**
Export competitiveness (4)	**-3.7**	**0.2**	**0.3**

Sources: Based on Bank of Italy and Istat data.
(1) For GDP and its components: chain-linked volumes; changes estimated on the basis of quarterly data adjusted for seasonal and calendar effects. – (2) Contributions to GDP growth; percentage points. – (3) Harmonized index of consumer prices. – (4) Calculated by comparing the price of foreign manufactures with the deflator of Italian merchandise exports (excluding energy and agricultural products).

The balance of payments should improve

The sharp contraction in investment and exports – the demand components with the greatest import content – will presumably weaken imports, which we forecast to decrease by nearly 4 per cent for the year before rising 3 per cent in 2010. The external current account deficit is expected to diminish in 2009, thanks to the improvement in the terms of trade.

Inflation is expected to decline sharply in 2009 and rise only modestly in 2010

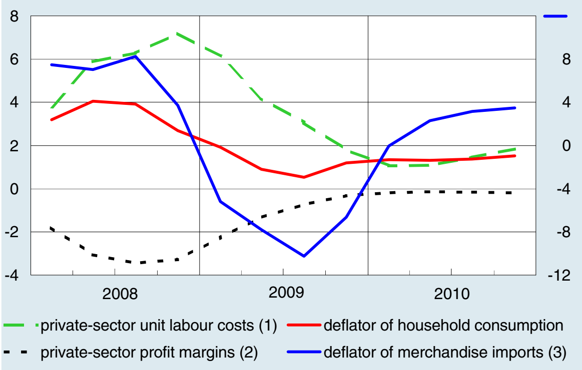
Consumer price inflation is now forecast to drop markedly in 2009 to an average annual rate of 1.1 per cent and then to rise slightly to 1.4 per cent in 2010 (Table 9,

Figure 35). This substantial downward revision of the forecasts made in July (by 0.8 percentage points for 2009 and 0.6 points for 2010) is due mainly to the fall in commodity prices in the second half of 2008 and more favourable expectations concerning their evolution for the next two years. Wage growth, after the temporary pick-up in 2008 owing to the renewal of most collective bargaining agreements, is forecast to slow down again in 2009. This will help to moderate unit labour costs, whose rate of increase, despite a further fall in productivity in conjunction with the cyclical downturn, should diminish by nearly two percentage points in 2009 to 3.8 per cent for the private sector and 3.2 per cent for the entire economy. The weakness of the economy is expected to shrink profit margins still further; domestic price inflation, as gauged by the GDP deflator, is likely to fall by nearly a percentage point to 2.3 per cent.

Figure 35

Main determinants of consumer price inflation

(percentage changes on year-earlier period)



Sources: Based on Bank of Italy and Istat data.
(1) Unit labour costs in the private sector (excluding energy and agriculture); calculated as the ratio between compensation of employees per standard labour unit and output per standard labour unit; output is value added at factor cost. – (2) Ratio between the deflator of value added at factor cost and unit labour costs in the private sector (excluding energy and agriculture). – (3) Right-hand scale.

Comparison with other forecasts

The estimates set forth in this issue of the *Economic Bulletin* paint a more starkly negative picture than those currently available from other forecasters, because they incorporate more recent data that more clearly confirm the rapid deterioration of the domestic and international economic situation. Our GDP growth estimate for 2009 is between 0.8 and 0.9 percentage points lower than the average of the other forecasts; for 2010 the difference is smaller, on the order of 0.2 to 0.3 points. Our inflation forecast for this year is lower than those of the other leading analysts by about half a percentage point, reflecting the recent further drop in oil and agricultural commodity prices and deteriorating demand expectations. For 2010, however, the differences are negligible.

The outlook remains highly uncertain

The Italian economy's prospects for growth continue to be affected by doubt concerning the severity of the crisis in some emerging economies that are still driving the expansion of world trade. These downside risks are partially counterbalanced by the possibility that economic activity will benefit by more than has been estimated both from the consumption stimulus deriving from the fall in commodity prices and from the unfolding effects of the stimulus plans that have been developed at international level. The uncertainties regarding inflation are mainly on the downside, in connection with the possibility of continued price declines for commodities and a further strengthening of the euro.

SELECTED STATISTICS

Additional tables are contained in the Statistical Appendix of the *Economic Bulletin* available on the Internet at www.bancaditalia.it/pubblicazioni

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Table A1

Sources and uses of income: United States (1)

(seasonally adjusted data; percentage changes on the previous period and contribution to growth, on an annual basis)

	GDP	Resident households' expenditure		General government expenditure		Investment		Domestic demand (2)		Exports	Imports	Net exports	Stocks
	Change	Change	Contri-bution	Change	Contri-bution	Change	Contri-bution	Change	Contri-bution	Change	Change	Contri-bution	Contri-bution
2004	3.6	3.6	2.6	1.4	0.3	7.3	1.1	4.1	4.3	9.7	11.3	-0.7	0.4
2005	2.9	3.0	2.1	0.4	0.1	6.8	1.1	3.0	3.1	7.0	5.9	-0.2	-0.1
2006	2.8	3.0	2.1	1.7	0.3	1.9	0.3	2.6	2.8	9.1	6.0	..	..
2007	2.0	2.8	2.0	2.1	0.4	-3.1	-0.5	1.4	1.4	8.4	2.2	0.6	-0.4
2006 – Q1	4.8	4.3	2.9	3.9	0.7	8.3	1.4	4.5	4.7	16.7	10.3	0.1	-0.2
Q2	2.7	2.8	1.9	1.2	0.2	-2.5	-0.4	2.0	2.1	5.5	0.1	0.6	0.4
Q3	0.8	2.2	1.5	1.7	0.3	-4.8	-0.8	0.9	0.9	3.5	3.1	-0.1	-0.1
Q4	1.5	3.7	2.6	1.6	0.3	-7.6	-1.3	0.2	0.2	15.6	2.0	1.3	-1.4
2007 – Q1	0.1	3.9	2.7	0.9	0.2	-3.4	-0.6	1.2	1.3	0.6	7.7	-1.2	-1.1
Q2	4.8	2.0	1.4	3.9	0.8	3.0	0.5	2.9	3.1	8.8	-3.7	1.7	0.5
Q3	4.8	2.0	1.4	3.8	0.8	-0.9	-0.2	2.6	2.8	23.0	3.0	2.0	0.7
Q4	-0.2	1.0	0.7	0.8	0.2	-6.2	-1.0	-1.0	-1.1	4.4	-2.3	0.9	-1.0
2008 – Q1	0.9	0.9	0.6	1.9	0.4	-5.6	-0.9	0.1	0.1	5.1	-0.8	0.8	..
Q2	2.8	1.2	0.9	3.9	0.8	-1.7	-0.3	-0.1	-0.1	12.3	-7.3	2.9	-1.5
Q3	-0.5	-3.8	-2.8	5.8	1.1	-5.3	-0.8	-1.5	-1.6	3.0	-3.5	1.1	0.8

Source: National statistics.
(1) Chain-linked volumes. Public sector investment is included in government expenditure. – (2) Includes change in stocks.

Table A2

Sources and uses of income: Japan (1)

(seasonally adjusted data; percentage changes on the previous period and contribution to growth, on an annual basis)

	GDP	Resident households' expenditure		General government expenditure		Investment		Domestic demand (2)		Exports	Imports	Net exports	Stocks
	Change	Change	Contri-bution	Change	Contri-bution	Change	Contri-bution	Change	Contri-bution	Change	Change	Contri-bution	Contri-bution
2004	2.7	1.6	0.9	1.9	0.3	1.4	0.3	1.9	1.9	13.9	8.1	0.8	0.3
2005	1.9	1.3	0.7	1.6	0.3	3.1	0.7	1.7	1.6	7.0	5.8	0.3	-0.1
2006	2.0	1.5	0.8	0.4	0.1	0.5	0.1	1.2	1.2	9.7	4.2	0.9	0.2
2007	2.4	0.7	0.4	2.0	0.3	1.1	0.2	1.3	1.2	8.4	1.5	1.1	0.3
2006 – Q1	0.5	0.7	0.4	-1.4	-0.2	-2.7	-0.6	0.2	0.2	7.7	6.2	0.4	0.7
Q2	3.0	2.5	1.4	4.3	0.7	3.6	0.8	2.9	2.7	6.2	5.8	0.3	-0.2
Q3	2.4	-2.1	-1.2	6.4	1.1	0.3	0.1	0.9	0.9	8.6	-1.3	1.4	0.9
Q4	2.5	3.5	1.9	-4.1	-0.7	6.3	1.4	2.0	1.9	3.6	0.3	0.5	-0.6
2007 – Q1	4.8	-1.0	-0.5	1.4	0.2	9.3	2.0	3.3	3.1	11.2	1.5	1.4	1.3
Q2	-0.8	1.9	1.1	6.2	1.0	-12.6	-3.1	-1.5	-1.4	7.8	4.8	0.6	-0.4
Q3	1.9	0.1	..	-2.0	-0.3	0.6	0.1	-0.1	-0.1	10.7	-1.7	1.8	0.1
Q4	2.1	0.2	0.1	8.3	1.4	-4.7	-1.1	0.8	0.8	10.9	3.6	1.3	0.3
2008 – Q1	2.4	3.6	1.9	-1.5	-0.3	-0.3	-0.1	0.5	0.5	14.5	4.1	1.8	-1.0
Q2	-3.7	-2.6	-1.4	-3.5	-0.6	-7.9	-1.8	-3.8	-3.7	-10.1	-11.5	-0.4	0.2
Q3	-1.8	1.2	0.6	-1.3	-0.2	-3.3	-0.7	-1.0	-1.0	3.4	9.6	-0.5	-0.6

Source: National statistics.
(1) Chain-linked volumes. Statistical discrepancies may cause differences between the sum of contributions and GDP growth. – (2) Includes change in stocks.

Table A3

Sources and uses of income: euro area (1)

(percentage changes on the previous period)

	Sources			Uses					
	GDP	Imports	Total	Gross fixed capital formation			Resident households' consumption expenditure (2)	General government consumption expenditure	Exports
				Construction	Machinery, equipment, sundry products & vehicles	Total			
				Chain-linked volumes					
2002	0.9	0.4	0.8	-0.6	-2.3	-1.4	0.9	2.4	1.8
2003	0.8	3.1	1.4	1.8	0.8	1.3	1.2	1.7	1.2
2004	2.1	7.0	3.4	1.2	3.5	2.3	1.6	1.6	7.4
2005	1.7	5.6	2.8	2.2	4.4	3.2	1.7	1.5	5.0
2006	2.9	8.2	4.4	4.5	6.7	5.5	2.0	1.9	8.3
2007	2.6	5.4	3.4	3.3	5.3	4.3	1.6	2.3	5.9
2006 – Q3	0.5	1.3	0.8	1.2	0.7	1.0	0.4	0.4	0.7
Q4	0.8	2.1	1.2	1.3	1.5	1.4	0.7	0.7	3.6
2007 – Q1	0.7	1.1	0.8	1.2	0.6	0.9	..	1.0	0.4
Q2	0.5	0.8	0.6	-1.0	1.6	0.2	0.7	0.2	1.2
Q3	0.6	2.2	1.1	0.9	1.1	1.0	0.4	0.5	1.9
Q4	0.3	-0.3	0.1	0.6	1.4	1.0	0.2	0.3	0.4
2008 – Q1	0.7	1.5	0.9	2.3	0.4	1.4	..	0.3	1.6
Q2	-0.2	-0.4	-0.3	-1.7	..	-0.9	-0.2	0.8	-0.1
Q3	-0.2	1.4	0.3	-1.1	-0.2	-0.6	..	0.7	..
				Implicit prices					
2002	2.6	-2.1	....	....	....	1.4	1.9	3.1	-0.4
2003	2.2	-1.8	....	....	....	1.1	2.1	2.5	-1.3
2004	1.9	1.5	....	....	....	2.5	2.1	2.0	1.0
2005	2.0	3.4	....	....	....	2.6	2.1	2.4	2.3
2006	1.9	3.8	....	....	....	2.9	2.2	2.0	2.7
2007	2.2	1.2	....	....	....	2.7	2.2	1.6	1.5
2006 – Q3	0.4	0.3	....	....	....	0.6	0.5	-0.2	0.6
Q4	0.4	-0.4	....	....	....	0.6	0.2	..	0.2
2007 – Q1	0.8	0.1	....	....	....	0.9	0.6	0.7	0.2
Q2	0.6	0.9	....	....	....	0.7	0.6	0.4	0.6
Q3	0.5	0.6	....	....	....	0.2	0.7	0.4	0.3
Q4	0.4	1.3	....	....	....	0.7	0.9	0.8	0.3
2008 – Q1	0.6	1.5	....	....	....	0.7	0.8	0.5	1.1
Q2	0.8	1.4	....	....	....	0.8	0.9	1.5	0.8
Q3	0.5	1.2	....	....	....	0.6	0.9	-0.3	0.9

Source: Eurostat.
(1) Quarterly data are seasonally and calendar adjusted. – (2) Includes expenditure of non-profit institutions serving households.

Table A4

Sources and uses of income: Italy (1)
(percentage changes on the previous period)

	Sources			Uses					
	GDP	Imports	Total	Gross fixed capital formation			Resident households' consumption expenditure	General government consumption expenditure (2)	Exports
				Construction	Machinery, equipment, sundry products & vehicles	Total			
	Chain-linked volumes								
2002	0.5	0.2	0.4	5.9	1.9	3.7	0.2	2.5	-2.9
2003	..	1.2	0.2	2.4	-4.6	-1.2	1.0	1.9	-2.0
2004	1.5	4.2	2.0	2.2	2.3	2.3	0.7	2.3	4.9
2005	0.6	2.2	0.9	0.5	0.9	0.7	0.9	1.9	1.0
2006	1.8	5.9	2.7	1.5	3.5	2.5	1.1	0.9	6.2
2007	1.5	4.4	2.1	2.2	0.2	1.2	1.4	1.3	5.0
2006 – Q3	0.3	1.6	0.6	-0.6	-1.3	-1.0	0.6	0.2	-1.1
Q4	1.0	2.6	1.3	2.9	0.8	1.9	..	0.7	4.9
2007 – Q1	0.3	1.1	0.5	0.4	-0.9	-0.3	1.0	0.4	1.3
Q2	0.1	-0.5	..	-1.2	0.6	-0.4	0.3	-0.1	-1.5
Q3	0.2	1.3	0.4	0.8	-1.1	-0.1	0.2	0.3	2.7
Q4	-0.4	-1.2	-0.6	0.3	0.8	0.5	-0.4	0.3	-1.6
2008 – Q1	0.5	-1.0	0.2	0.1	-0.6	-0.2	..	0.5	1.2
Q2	-0.4	-0.8	-0.5	-1.0	0.5	-0.3	-0.3	0.3	-1.1
Q3	-0.5	-0.5	-0.5	-0.6	-3.2	-1.9	0.1	0.1	-1.6
	Implicit prices								
2002	3.3	-0.3	2.5	3.7	2.2	2.9	2.9	2.6	1.4
2003	3.1	-1.3	2.2	2.8	0.3	1.6	2.8	3.7	0.4
2004	2.6	2.7	2.6	4.0	1.4	2.7	2.6	2.7	2.6
2005	2.1	6.2	2.9	4.6	1.2	2.9	2.3	3.3	4.0
2006	1.7	7.6	3.0	3.2	2.0	2.6	2.7	2.0	4.5
2007	2.3	2.3	2.3	3.5	1.6	2.6	2.2	0.4	3.6
2006 – Q3	-0.3	1.2	..	0.9	0.3	0.6	0.7	-2.9	1.3
Q4	..	-1.0	-0.2	0.8	..	0.5	0.1	-2.3	0.2
2007 – Q1	1.3	0.1	1.0	1.2	0.8	1.0	0.4	1.2	1.2
Q2	0.6	1.5	0.8	0.6	0.4	0.5	0.6	0.8	1.2
Q3	0.5	1.4	0.7	0.6	0.4	0.5	0.9	0.2	0.4
Q4	0.3	0.4	0.3	0.8	..	0.4	0.8	1.9	1.0
2008 – Q1	0.7	2.7	1.2	0.8	1.5	1.1	0.9	-1.6	1.7
Q2	2.1	1.5	2.0	1.1	0.3	0.7	1.4	6.2	1.2
Q3	-0.2	3.4	0.6	1.2	0.9	1.1	1.1	-3.3	1.8

Source: Istat.
(1) Quarterly data are seasonally and calendar adjusted. – (2) Includes consumption of non-profit institutions serving households.

Unit labour costs, per capita compensation and productivity: euro area (1)

(percentage changes on the year-earlier period)

	Per capita compensation	Productivity	of which: Value added (2)	of which: Employees	Unit labour costs
			Total industry excluding construction		
2004	2.9	4.2	2.8	-1.4	-1.2
2005	1.8	2.9	1.7	-1.1	-1.1
2006	3.5	3.9	3.5	-0.3	-0.3
2007	2.8	3.2	3.4	0.3	-0.3
2006 – Q1	3.6	4.6	3.7	-0.8	-0.9
Q2	3.6	4.0	3.6	-0.4	-0.4
Q3	3.9	4.0	3.8	-0.2	-0.1
Q4	3.2	4.2	4.2	..	-1.0
2007 – Q1	2.4	3.3	3.6	0.3	-0.9
Q2	3.2	3.0	3.3	0.3	0.2
Q3	2.4	3.4	3.6	0.2	-1.0
Q4	3.2	2.9	3.2	0.3	0.2
2008 – Q1	3.5	2.1	2.6	0.5	1.3
Q2	2.8	0.8	1.2	0.4	2.0
Q3	3.4	-1.3	-1.1	0.1	4.7
			Services		
2004	1.9	0.4	2.0	1.5	1.5
2005	2.1	0.5	1.9	1.4	1.6
2006	1.8	0.5	2.7	2.2	1.3
2007	2.4	0.6	2.7	2.1	1.8
2006 – Q1	1.6	0.3	2.2	2.0	1.4
Q2	2.1	0.4	2.8	2.4	1.6
Q3	1.9	0.7	3.0	2.3	1.2
Q4	1.5	0.9	3.2	2.2	0.6
2007 – Q1	2.5	1.1	3.1	2.0	1.4
Q2	2.1	0.8	2.8	2.0	1.3
Q3	2.3	0.4	2.7	2.3	1.9
Q4	2.8	0.1	2.4	2.3	2.7
2008 – Q1	2.8	-0.1	2.1	2.2	2.8
Q2	3.4	-0.3	1.6	1.9	3.7
Q3	3.3	-0.1	1.3	1.4	3.5
			Total economy		
2004	2.1	1.5	2.3	0.8	0.6
2005	1.9	0.7	1.7	1.0	1.2
2006	2.2	1.2	2.8	1.6	1.0
2007	2.5	1.0	2.9	1.8	1.4
2006 – Q1	2.1	1.1	2.5	1.3	1.0
Q2	2.4	1.2	2.9	1.7	1.2
Q3	2.4	1.3	3.0	1.7	1.0
Q4	2.0	1.6	3.3	1.7	0.4
2007 – Q1	2.4	1.5	3.4	1.8	0.9
Q2	2.3	1.1	2.8	1.7	1.2
Q3	2.3	0.9	2.8	1.9	1.4
Q4	2.9	0.7	2.5	1.8	2.2
2008 – Q1	3.1	0.6	2.3	1.6	2.4
Q2	3.4	0.3	1.6	1.3	3.1
Q3	3.5	..	0.7	0.7	3.5

Source: Based on Eurostat data.
(1) Euro-15. – (2) Value added at base prices, volumes at chain-linked prices – reference year 2000.

Table A6

Unit labour costs, per capita compensation and productivity: Italy

(percentage changes on the year-earlier period) (1)

	Per capita compensation (2)	Wages per employee (2)	Productivity	Productivity of which: Value added (3)	Productivity of which: Employees (2)	Unit labour costs
			Total industry excluding construction			
2004	4.0	3.9	1.9	0.9	-1.0	2.0
2005	2.7	3.1	0.7	-0.4	-1.0	2.0
2006	2.6	3.4	0.1	1.2	1.0	2.5
2007	2.4	2.8	-0.1	0.8	0.9	2.5
2006 – Q1	3.7	4.6	2.2	2.4	0.2	1.5
Q2	2.4	3.1	-1.0	0.5	1.6	3.5
Q3	2.4	3.1	-0.9	0.4	1.3	3.3
Q4	2.0	2.8	1.5	2.5	1.0	0.5
2007 – Q1	1.0	1.3	-0.7	1.1	1.8	1.7
Q2	2.5	3.0	0.4	1.7	1.3	2.0
Q3	2.6	3.1	0.6	1.1	0.5	2.1
Q4	3.6	3.8	-2.5	-2.4	0.2	6.3
2008 – Q1	4.6	4.5	0.2	-0.9	-1.1	4.4
Q2	4.1	3.8	-1.1	-2.3	-1.2	5.3
Q3	5.5	5.2	-2.8	-3.9	-1.1	8.6
			Services			
2004	3.1	3.4	0.9	1.6	0.7	2.3
2005	3.6	3.8	0.7	1.1	0.4	2.9
2006	2.5	2.9	0.1	2.1	2.1	2.5
2007	1.6	1.6	0.7	1.8	1.1	0.9
2006 – Q1	3.4	3.7	..	1.5	1.4	3.4
Q2	5.6	6.0	-0.5	2.0	2.6	6.1
Q3	3.6	3.9	..	2.3	2.3	3.6
Q4	-2.2	-1.7	0.7	2.6	1.9	-2.9
2007 – Q1	1.6	2.0	1.7	2.4	0.7	-0.1
Q2	-0.2	-0.1	1.6	1.9	0.3	-1.7
Q3	1.0	0.8	..	1.9	1.9	1.0
Q4	4.0	4.0	-0.5	1.2	1.7	4.5
2008 – Q1	3.7	4.3	-0.9	0.9	1.8	4.7
Q2	5.8	5.9	-1.7	0.5	2.2	7.6
Q3	4.0	4.0	-0.3	0.1	0.4	4.3
			Total economy			
2004	3.3	3.4	1.4	1.7	0.4	1.9
2005	3.2	3.4	0.6	0.7	0.2	2.6
2006	2.5	3.0	0.1	1.8	1.7	2.4
2007	1.9	2.1	0.6	1.6	1.0	1.4
2006 – Q1	3.3	3.8	0.6	1.7	1.1	2.7
Q2	4.4	5.0	-0.4	1.6	2.1	4.9
Q3	3.2	3.6	-0.3	1.6	1.9	3.5
Q4	-0.9	-0.3	0.8	2.5	1.7	-1.7
2007 – Q1	1.6	2.0	1.4	2.1	0.8	0.3
Q2	0.7	0.9	1.3	1.8	0.6	-0.6
Q3	1.5	1.5	0.2	1.7	1.5	1.4
Q4	3.9	3.9	-0.9	0.2	1.1	4.8
2008 – Q1	3.9	4.3	-0.5	0.5	1.0	4.5
Q2	5.4	5.4	-1.1	..	1.1	6.5
Q3	4.5	4.4	-0.6	-0.7	-0.1	5.1

Sources: Based on Istat and Eurostat data.
(1) There may be discrepancies between the sum of quarterly results and the annual accounts. – (2) Standard labour units. – (3) Value added at base prices, volumes at chain-linked prices – reference year 2000.

Table A7

Harmonized index of consumer prices: main euro-area countries

(percentage changes on the year-earlier period)

	ITALY		GERMANY		FRANCE		SPAIN		EURO (1)	
	Total	Total excl. energy and unprocessed food products	Total	Total excl. energy and unprocessed food products	Total	Total excl. energy and unprocessed food products	Total	Total excl. energy and unprocessed food products	Total	Total excl. energy and unprocessed food products
2003	2.8	2.7	1.0	0.9	2.2	2.2	3.1	3.0	2.1	2.0
2004	2.3	2.3	1.8	1.6	2.3	2.4	3.1	2.8	2.1	2.1
2005	2.2	2.0	1.9	1.0	1.9	1.2	3.4	2.7	2.2	1.5
2006	2.2	1.8	1.8	0.8	1.9	1.3	3.6	3.0	2.2	1.5
2007	2.0	1.9	2.3	2.1	1.6	1.5	2.8	2.7	2.1	2.0
2006 – Jan.	2.2	1.6	2.1	0.6	2.3	1.3	4.2	3.0	2.4	1.3
Feb.	2.2	1.6	2.1	0.7	2.0	1.1	4.1	3.0	2.3	1.3
Mar.	2.2	1.8	1.9	0.8	1.7	1.2	3.9	3.1	2.2	1.4
Apr.	2.3	1.9	2.3	1.0	2.0	1.3	3.9	3.2	2.5	1.6
May	2.3	1.8	2.1	0.6	2.4	1.3	4.1	3.1	2.5	1.5
June	2.4	1.8	2.0	0.8	2.2	1.4	4.0	3.1	2.5	1.6
July	2.3	1.7	2.1	1.0	2.2	1.5	4.0	3.2	2.4	1.6
Aug.	2.3	1.6	1.8	0.8	2.1	1.4	3.8	3.1	2.3	1.5
Sept.	2.4	2.0	1.0	0.8	1.5	1.2	2.9	3.0	1.7	1.5
Oct.	1.9	2.0	1.1	1.0	1.2	1.3	2.6	2.8	1.6	1.6
Nov.	2.0	1.8	1.5	1.1	1.6	1.4	2.7	2.7	1.9	1.6
Dec.	2.1	1.9	1.4	1.0	1.7	1.5	2.7	2.5	1.9	1.6
2007 – Jan.	1.9	1.6	1.8	1.7	1.4	1.4	2.4	2.8	1.8	1.8
Feb.	2.1	2.1	1.9	1.8	1.2	1.4	2.5	2.8	1.8	1.9
Mar.	2.1	2.0	2.0	1.7	1.2	1.3	2.5	2.5	1.9	1.9
Apr.	1.8	1.8	2.0	1.9	1.3	1.4	2.5	2.5	1.9	1.9
May	1.9	1.9	2.0	2.1	1.2	1.4	2.4	2.5	1.9	1.9
June	1.9	1.9	2.0	2.1	1.3	1.4	2.5	2.5	1.9	1.9
July	1.7	1.8	2.0	2.1	1.2	1.4	2.3	2.4	1.8	1.9
Aug.	1.7	1.9	2.0	2.2	1.3	1.6	2.2	2.5	1.7	2.0
Sept.	1.7	1.8	2.7	2.3	1.6	1.6	2.7	2.6	2.1	2.0
Oct.	2.3	2.1	2.7	2.2	2.1	1.7	3.6	3.1	2.6	2.1
Nov.	2.6	2.2	3.3	2.4	2.6	1.8	4.1	3.3	3.1	2.3
Dec.	2.8	2.3	3.1	2.4	2.8	1.9	4.3	3.4	3.1	2.3
2008 – Jan.	3.1	2.6	2.9	2.1	3.2	2.2	4.4	3.2	3.2	2.3
Feb.	3.1	2.5	3.0	2.2	3.2	2.3	4.4	3.3	3.3	2.4
Mar.	3.6	2.9	3.3	2.4	3.5	2.5	4.6	3.5	3.6	2.7
Apr.	3.6	2.7	2.6	1.8	3.4	2.5	4.2	3.2	3.3	2.4
May	3.7	2.8	3.1	1.8	3.7	2.4	4.7	3.3	3.7	2.5
June	4.0	3.0	3.4	1.8	4.0	2.5	5.1	3.4	4.0	2.5
July	4.0	2.7	3.5	1.8	4.0	2.4	5.3	3.5	4.0	2.5
Aug.	4.2	3.2	3.3	1.9	3.5	2.3	4.9	3.5	3.8	2.6
Sept.	3.9	3.0	3.0	1.7	3.3	2.3	4.6	3.4	3.6	2.5
Oct.	3.6	3.0	2.5	1.5	3.0	2.3	3.6	2.9	3.2	2.4
Nov.	2.7	2.8	1.4	1.4	1.9	2.1	2.4	2.7	2.1	2.2

Source: Eurostat.
(1) Weighted average of the indices of the countries belonging to the euro area at the date indicated.

Balance of payments (current account and capital account): Italy

(millions of euros)

	Current account						Capital account			
	Total	Goods	Services	Income	Current transfers		Total	Intangible assets	Capital transfers	
					Private	Public			Private	Public
2004	-13,077	8,854	1,179	-14,817	-1,477	-6,816	1,700	-38	-26	1,764
2005	-23,628	536	-541	-13,624	-1,676	-8,323	998	69	-66	995
2006	-38,506	-10,203	-1,272	-13,573	-5,473	-7,985	1,890	-100	-60	2,050
2007	-37,366	2,941	-6,978	-19,675	-6,762	-6,891	2,674	-69	71	2,671
2006 – Q4	-9,034	143	-1,732	-3,695	-1,549	-2,200	1,136	26	14	1,096
2007 – Q1	-12,471	-2,133	-3,345	-4,077	-1,278	-1,638	1,132	-1	29	1,104
Q2	-10,186	1,044	-1,091	-8,184	-1,742	-213	-32	-27	-15	10
Q3	-4,515	2,807	-871	-2,724	-1,620	-2,106	572	25	-30	577
Q4	-10,194	1,223	-1,671	-4,689	-2,123	-2,934	1,002	-65	87	980
2008 – Q1	-15,683	-1,482	-3,100	-6,135	-2,029	-2,936	1,224	23	-21	1,223
Q2	-13,390	641	-318	-12,131	-1,524	-58	873	-26	14	885
Q3	(-7,666)	(619)	(-242)	(-4,396)	….	….	(365)	….	….	….
2006 – Oct.	-3,238	168	-23	-2,205	-575	-603	106	23	2	81
Nov.	-2,813	-104	-748	-1,059	-524	-378	-83	2	-33	-52
Dec.	-2,983	79	-962	-431	-450	-1,219	1,114	2	44	1,068
2007 – Jan.	-5,505	-2,265	-1,444	-1,443	-524	170	259	-3	10	252
Feb.	-3,474	-892	-822	-1,209	-174	-377	266	-6	8	263
Mar.	-3,492	1,024	-1,079	-1,426	-579	-1,432	607	7	11	589
Apr.	-4,725	-635	-896	-2,095	-516	-584	-4	-8	..	5
May	-4,358	319	-209	-3,470	-541	-456	18	-18	-4	40
June	-1,103	1,360	14	-2,619	-685	827	-46	..	-10	-35
July	2,351	3,078	313	-230	-525	-285	35	21	-21	35
Aug.	-2,881	320	-1,053	-1,100	-459	-589	36		5	31
Sept.	-3,985	-591	-131	-1,394	-637	-1,232	500	3	-14	511
Oct.	-1,274	1,591	-82	-1,512	-797	-474	65	-47	1	111
Nov.	-3,884	693	-923	-2,502	-668	-485	153	-11	81	83
Dec.	-5,036	-1,061	-667	-675	-658	-1,975	784	-7	4	786
2008 – Jan.	-6,118	-2,753	-810	-1,675	-607	-273	322	9	23	290
Feb.	-3,416	771	-1,174	-2,228	-464	-321	275	17	-32	290
Mar.	-6,149	500	-1,116	-2,232	-958	-2,342	627	-4	-12	643
Apr.	-4,365	-347	-320	-2,310	-755	-633	22	-14	-6	43
May	-6,572	1,075	-562	-6,010	-557	-518	38	-4	1	41
June	-2,453	-87	564	-3,812	-212	1,094	813	-7	19	801
July	1,262	3,380	684	-1,554	-741	-507	33	-10	-5	47
Aug.	-4,039	-1,191	-1,104	-596	-512	-635	45	-1	10	36
Sept.	(-4,889)	(-1,570)	(178)	(-2,246)	….	….	(287)	….	….	….
Oct.	(-2,400)	(1,575)	(-1,193)	(-1,816)	….	….	(101)	….	….	….

Lending by Italian banks by geographical area and sector (1)

(12-month percentage changes)

	General govern-ment	Finance and insurance companies	Non-financial corporations (a)		Households		Firms = (a) + (b)				Total
				under 20 employees (2)	Producer (b) (3)	Consumer		Manufac-turing	Construc-tion	Services	
						Centre and North					
2007 – Mar.	4.8	13.7	11.1	4.1	6.3	8.6	10.7	4.7	14.4	12.1	10.3
June	4.8	9.8	11.5	4.2	5.5	8.1	10.9	5.7	14.7	10.5	9.8
Sept.	-0.1	7.7	12.7	5.5	5.7	8.5	12.1	7.1	15.3	12.1	10.1
Dec.	7.9	5.6	13.2	6.8	5.2	8.2	12.4	6.5	13.5	11.1	10.6
2008 – Mar.	6.0	14.2	13.1	7.1	3.9	5.3	12.3	8.6	13.3	10.6	11.0
June	8.7	5.7	12.3	6.9	2.3	3.1	11.4	7.5	11.5	11.3	9.0
Sept.	9.0	3.8	11.4	5.8	1.8	1.8	10.6	5.6	11.1	9.8	7.8
Nov.	8.5	0.6	7.0	2.0	-1.0	0.0	6.3	..	..	..	4.7
						South and Islands					
2007 – Mar.	-9.5	-1.7	17.2	9.0	9.6	12.7	15.8	13.8	21.2	18.1	12.9
June	2.5	4.4	15.4	9.4	9.2	12.0	14.3	11.3	20.9	16.2	12.6
Sept.	-3.8	-4.8	16.3	10.4	8.9	12.2	14.9	12.4	21.3	16.4	12.6
Dec.	-3.6	-7.0	10.8	9.8	6.6	10.5	10.1	7.3	18.5	9.7	9.2
2008 – Mar.	0.7	-3.8	11.0	9.7	5.0	6.0	9.9	6.1	17.5	9.5	7.9
June	-0.7	-0.8	11.4	8.6	3.6	2.9	10.0	4.5	15.2	11.4	6.7
Sept.	3.8	14.1	9.2	6.9	1.9	3.0	7.9	2.8	13.1	9.0	5.8
Nov.	6.0	13.2	6.8	5.3	-2.3	1.3	5.2	..	..	..	4.0
						ITALY					
2007 – Mar.	2.5	13.2	11.8	4.8	7.1	9.4	11.3	5.8	15.5	12.8	10.7
June	4.4	9.7	12.0	5.0	6.4	9.0	11.4	6.4	15.7	11.2	10.2
Sept.	-0.7	7.4	13.1	6.1	6.5	9.3	12.4	7.7	16.3	12.7	10.4
Dec.	6.4	5.3	12.9	7.2	5.5	8.7	12.1	6.6	14.4	10.9	10.4
2008 – Mar.	5.4	13.7	12.8	7.5	4.2	5.5	11.9	8.3	14.0	10.5	10.5
June	7.4	5.6	12.2	7.1	2.6	3.0	11.2	7.2	12.1	11.4	8.7
Sept.	8.5	4.1	11.1	6.0	1.8	2.0	10.2	5.2	11.4	9.8	7.5
Nov.	8.3	0.9	7.0	2.5	-1.3	0.3	6.2	2.5	8.6	6.8	4.6

(1) Statistics for November 2008 are provisional; they include data for Cassa Depositi e Prestiti S.p.A. since October 2007. Loans do not include repurchase agreements, bad debts and some smaller items included in the Eurosystem harmonized definition. The breakdown by geographical area is according to customers' place of residence. Net of the effects of reclassification, exchange rate changes and other modifications not due to transactions. – (2) Limited partnerships and general partnerships with fewer than 20 employees. Informal associations, de facto companies and sole proprietorships with 6-19 employees. – (3) Informal associations, de facto companies and sole proprietorships with up to 5 employees.

Table A10

Financing of the general government borrowing requirement: Italy

(millions of euros)

	Currency and deposits	*of which:* PO funds	Short-term securities	Medium and long-term securities	MFI loans (1)	Other operations (1)	*of which:* change in central bank current accounts	Borrowing requirement	*of which:* financed abroad
2005	20,743	-4,177	-924	39,899	6,888	4,061	1,197	70,666	5,277
2006	7,476	-4,957	4,847	33,105	68,073	-54,677	-8,230	58,824	-7,013
2007	-13,977	-28,447	5,562	22,516	-2,525	14,779	13,142	26,355	-6,196
2005 – Q1	2,510	-516	11,204	45,886	2,627	-33,130	-34,293	29,096	2,718
Q2	12,725	149	9,287	20,745	1,894	-15,573	-14,842	29,078	3,477
Q3	2,758	-1,577	2,547	-19,414	341	29,464	28,813	15,696	419
Q4	2,751	-2,233	-23,963	-7,317	2,026	23,300	21,519	-3,203	-1,337
2006 – Q1	10,657	-891	18,406	13,007	2,474	-11,612	-16,246	32,932	-24
Q2	1,162	-1,615	7,154	28,742	-696	-25,553	-26,568	10,808	655
Q3	232	-1,210	-7,819	5,993	56,489	-39,102	12,948	15,792	1,289
Q4	-4,575	-1,240	-12,893	-14,637	9,806	21,590	21,637	-708	-8,934
2007 – Q1	-1,537	-3,474	20,684	7,523	-261	-5,506	-5,753	20,902	-527
Q2	-16,496	-13,509	345	28,729	-2,143	-8,731	-8,936	1,704	2,433
Q3	-2,330	-8,550	3,074	-2,809	-1,126	7,061	5,459	3,871	-6,288
Q4	6,387	-2,914	-18,541	-10,927	1,005	21,955	22,372	-121	-1,814
2008 – Q1	1,313	-1,111	25,905	23,405	266	-33,225	-31,203	17,664	466
Q2	934	-1,266	8,186	-11,268	3,804	5,509	5,968	7,164	-5,721
Q3	-2,295	-947	-1,120	4,054	-5,695	16,058	17,012	11,001	-2,287
2007 – Jan.	3,209	-263	12,347	-1,820	-96	-11,445	-11,383	2,195	-759
Feb.	-2,029	204	3,027	5,059	235	-3,549	-3,489	2,742	-291
Mar.	-2,718	-3,415	5,310	4,284	-400	9,488	9,120	15,965	524
Apr.	-4,256	-4,597	99	4,990	2,597	7,554	7,549	10,984	352
May	-3,081	-1,584	2,261	18,326	-2,704	-4,732	-5,066	10,069	506
June	-9,159	-7,329	-2,015	5,413	-2,036	-11,553	-11,419	-19,350	1,575
July	-203	-4,856	377	110	-301	-2,262	-3,963	-2,280	-2,647
Aug.	-1,558	-1,934	358	-728	-1,693	3,798	3,887	178	-448
Sept.	-569	-1,760	2,340	-2,191	868	5,526	5,534	5,973	-3,193
Oct.	-35	-580	5,213	5,095	385	-1,843	-1,859	8,817	70
Nov.	404	-1,152	-380	-5,344	1,635	8,634	8,860	4,949	460
Dec.	6,017	-1,182	-23,374	-10,678	-1,016	15,164	15,372	-13,887	-2,344
2008 – Jan.	3,013	-36	14,516	7,222	-125	-26,608	-26,459	-1,982	2,124
Feb.	-3,532	-659	4,821	1,657	-655	6,201	6,883	8,492	243
Mar.	1,833	-415	6,568	14,525	1,047	-12,818	-11,627	11,154	-1,900
Apr.	-1,102	-195	4,215	10,695	615	-2,778	-2,661	11,645	1,973
May	-1,248	-333	5,125	-19,459	1,016	23,216	23,393	8,650	-5,159
June	3,283	-738	-1,153	-2,504	2,173	-14,930	-14,763	-13,131	-2,535
July	-3,084	342	-2,111	11,941	-4,893	-7,086	-6,948	-5,232	-2,743
Aug.	643	-321	796	12,460	-2,128	-8,814	-8,007	2,957	475
Sept.	146	-968	195	-20,347	1,326	31,958	31,967	13,277	-19
Oct.	1,541	-2,403	5,424	14,006	414	-8,186	-8,178	13,199	-568

(1) As of September 2006 Cassa Depositi e Prestiti S.p.A. is included among MFIs; as of the same month its loans to general government bodies are included in the item "MFI loans".

Table A11

General government debt: Italy

(millions of euros)

	Currency and deposits	*of which:* PO funds	Short-term securities	Medium and long-term securities	MFI loans (1)	Other liabilities (1)	General government debt	*of which:* in foreign currencies	*of which:* medium and long-term	*Memorandum item:* central bank current accounts
2005	149,530	70,578	117,460	1,129,206	61,393	55,190	1,512,779	27,255	1,259,069	14,634
2006	157,006	65,622	122,307	1,163,792	130,161	8,742	1,582,009	10,740	1,309,951	22,864
2007	143,029	37,175	127,869	1,190,059	127,635	10,379	1,598,971	3,465	1,333,206	9,721
2005 – Mar.	131,297	74,239	129,589	1,136,016	57,128	53,489	1,507,519	29,260	1,265,650	50,124
June	144,021	74,388	138,877	1,156,921	59,026	52,759	1,551,605	26,844	1,284,358	64,966
Sept.	146,779	72,811	141,424	1,136,390	59,367	53,409	1,537,369	26,634	1,262,903	36,153
Dec.	149,530	70,578	117,460	1,129,206	61,393	55,190	1,512,779	27,255	1,259,069	14,634
2006 – Mar.	160,186	69,687	135,868	1,142,222	63,865	59,824	1,561,966	22,314	1,276,930	30,880
June	161,349	68,072	143,025	1,172,127	63,166	60,839	1,600,507	18,375	1,303,854	57,449
Sept.	161,581	66,862	135,204	1,178,358	120,357	8,789	1,604,289	15,116	1,314,434	44,501
Dec.	157,006	65,622	122,307	1,163,792	130,161	8,742	1,582,009	10,740	1,309,951	22,864
2007 – Mar.	155,469	62,147	142,994	1,172,531	129,900	8,989	1,609,883	5,020	1,318,815	28,616
June	138,972	48,639	143,349	1,203,468	127,756	9,194	1,622,739	4,908	1,347,193	37,552
Sept.	136,642	40,089	146,422	1,200,309	126,631	10,796	1,620,801	4,678	1,344,868	32,094
Dec.	143,029	37,175	127,869	1,190,059	127,635	10,379	1,598,971	3,465	1,333,206	9,721
2008 – Mar.	144,342	36,064	153,806	1,214,011	127,902	8,357	1,648,419	3,236	1,354,911	40,925
June	145,276	34,799	161,980	1,204,707	131,705	7,898	1,651,566	3,214	1,345,562	34,956
Sept.	142,981	33,852	161,110	1,211,560	126,011	6,944	1,648,605	3,537	1,347,019	17,944
2007 – Jan.	160,215	65,358	134,654	1,162,700	130,066	8,681	1,596,315	6,968	1,309,327	34,247
Feb.	158,186	65,562	137,682	1,168,341	130,300	8,620	1,603,129	6,845	1,314,354	37,736
Mar.	155,469	62,147	142,994	1,172,531	129,900	8,989	1,609,883	5,020	1,318,815	28,616
Apr.	151,213	57,551	143,094	1,177,513	132,496	8,993	1,613,309	4,907	1,323,777	21,067
May	148,131	55,967	145,358	1,196,808	129,793	9,327	1,629,417	4,960	1,342,994	26,133
June	138,972	48,639	143,349	1,203,468	127,756	9,194	1,622,739	4,908	1,347,193	37,552
July	138,769	43,782	143,726	1,204,119	127,455	10,894	1,624,965	4,837	1,349,187	41,515
Aug.	137,211	41,848	144,084	1,203,490	125,763	10,805	1,621,354	4,847	1,347,748	37,628
Sept.	136,642	40,089	146,422	1,200,309	126,631	10,796	1,620,801	4,678	1,344,868	32,094
Oct.	136,608	39,508	151,631	1,205,483	127,015	10,813	1,631,549	4,591	1,350,261	33,953
Nov.	137,012	38,357	151,251	1,200,388	128,651	10,587	1,627,888	3,490	1,344,858	25,093
Dec.	143,029	37,175	127,869	1,190,059	127,635	10,379	1,598,971	3,465	1,333,206	9,721
2008 – Jan.	146,042	37,139	142,390	1,198,086	127,511	10,230	1,624,259	3,431	1,341,429	36,181
Feb.	142,510	36,479	147,224	1,199,950	126,855	9,548	1,626,087	3,391	1,342,069	29,297
Mar.	144,342	36,064	153,806	1,214,011	127,902	8,357	1,648,419	3,236	1,354,911	40,925
Apr.	143,241	35,869	158,037	1,225,261	128,516	8,241	1,663,295	3,284	1,366,776	43,586
May	141,993	35,537	163,148	1,206,374	129,532	8,064	1,649,111	3,290	1,348,027	20,193
June	145,276	34,799	161,980	1,204,707	131,705	7,898	1,651,566	3,214	1,345,562	34,956
July	142,192	35,141	159,919	1,217,987	126,811	7,761	1,654,671	3,237	1,355,988	41,905
Aug.	142,835	34,820	160,784	1,231,349	124,684	6,953	1,666,607	3,435	1,366,739	49,912
Sept.	142,981	33,852	161,110	1,211,560	126,011	6,944	1,648,605	3,537	1,347,019	17,944
Oct.	144,522	31,449	166,604	1,226,133	126,428	6,936	1,670,622	3,962	1,360,608	26,122

(1) As of September 2006 Cassa Depositi e Prestiti S.p.A. is included among MFIs; as of the same month its loans to general government bodies are included in the item “MFI loans”.