



BANCA D'ITALIA
EUROSISTEMA

Economic Bulletin

October 2007

number

46



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Economic Bulletin

Number 46 October 2007

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Registration with the Court of Rome No. 426, 19 September 1985

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ISSN 0393-2400

Based on data available on 10 October 2007

Printed by the Printing Office of the Bank of Italy, Rome, October 2007

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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 financial turmoil over the summer has not jeopardized the prospects for growth in the world economy

The growing difficulties of two US hedge funds specializing in sub-prime mortgages triggered a crisis in the American mortgage market in July, the repercussions of which were rapidly felt in the international financial, money and stock markets. Risk premiums rose everywhere and lenders grew more cautious; share prices fell and, more important, trading in money markets dried up. These effects were countered by the US Federal Reserve, the European Central Bank and the monetary authorities of other countries, and by injections of liquidity; in addition, the Federal Reserve cut its reference interest rates. These actions served to quell the turmoil.

Despite the greater uncertainty, the crisis does not appear so far to have caused a marked change in expectations of growth in the world economy, although they have now been revised downwards for next year to below 5 per cent by the main forecasters. In the United States, at the epicentre of the crisis, the impact is likely to be greater, with a downwards revision of expected GDP growth to around 2 per cent. The stimulus that emerging countries impart to world growth is likely to remain almost unchanged.

On the basis of the latest economic indicators, the slowdown in economic activity in the euro area in the second quarter was followed by an acceleration in the summer. According to the European Central Bank's most recent forecasts, economic growth in the euro area in 2008 should be close to the potential growth rate.

Following the slowdown in the first quarter, GDP in Italy stagnated in the spring. With the real exchange rate remaining broadly unchanged and in contrast to developments elsewhere in the euro area, Italian exports declined further, affected by the slowdown in economic activity in our main export markets.

Household consumption continued to grow at an annual rate of just under 3 per cent in both quarters, benefiting from the recovery in disposable income after the pause of the last two years.

In Italy stagnation in the spring gave way to a slight recovery in the summer

Fixed investment slowed down in line with GDP. During the first half of the year as a whole the growth in domestic demand remained weak, held in check mainly by the negative effect of the change in stocks, which was presumably attributable to gathering uncertainty about the strength of the recovery.

In the second quarter the rise in employment accelerated, partly for statistical reasons due to the recording of non-residents as part of the working population.

The inflation picture remains generally favourable, thanks to limited demand pressures, the appreciation of the euro and moderate overall wage growth. In industry excluding construction the fall in productivity and the rise in per capita labour costs – which was fuelled by the payment of a number of instalments of agreed wage increases – led to a rise of 2.8 per cent in labour costs per unit of output by comparison with the preceding six months.

According to our preliminary estimates, there was a slight acceleration in economic activity in the summer. The main growth estimates now give average rates of below 2 per cent in 2007 and of 1.3-1.5 per cent in 2008.

The impact of the financial turmoil on the Italian banking system appears to be limited

The exposure of the major Italian banking groups to the US sub-prime mortgage sector appears to be small. The large Italian banks

participating in the Eurosystem's Bank Lending Survey report that in the last three months they have had difficulty obtaining funds in the money and bond markets and foresee a moderate tightening of lending conditions in the closing months of the year. Credit risk indicators have fallen slightly and continue to be much lower than in the past.

As in the other leading international financial centres, share prices in Italy have been recovering since the beginning of September, after having fallen from the end of July onwards owing to the crisis in the market in structured credit products.

The performance of the public accounts

The public finances have steadily improved since 2006 as a result of a sharp increase in tax revenue, attributable in part to progress in reducing tax evasion and avoidance. The ratio of taxes and social security contributions to GDP will be two percentage points higher in 2007 than in 2005. It will remain stable in 2008 at a relatively high level by international standards. During 2007 the unexpected revenue has mostly been used to fund increased spending. Similar

choices have been made for the 2008 budget, which increases the deficit in relation to that on a current programmes basis.

After the considerable improvement of 2006, only modest progress has been made in reducing the budget imbalances. Bringing net borrowing down to under 3 per cent of GDP will pave the way to closing the excessive deficit procedure for Italy, but the measures needed to balance the budget have been put off to the three-year period 2009-11.

In the two years 2007-08 the ratio of primary current expenditure to GDP will remain constant at the highest levels recorded in recent decades. The key issue for the public finances in Italy is curbing primary current expenditure. Initiating a review of public spending, pursuing budget reform, and strengthening the mechanisms for making local authorities accountable are important ways of improving the use of resources in the public sector. Studies by the Ministry for the Economy and Finance show that there is ample scope for making savings without compromising the achievement of the main policy objectives.

2 THE WORLD ECONOMY

ECONOMIC DEVELOPMENTS AND THE FINANCIAL MARKETS

Turmoil in the financial markets increased uncertainty...

A sudden correction in investors' perceptions of risk occurred this summer in the financial markets of the industrial countries – and to a lesser extent in those of emerging economies – owing to heightened fears about intermediaries' losses on financial instruments linked to sub-prime mortgages in the United States (see the box “House prices and the sub-prime mortgage crisis in the United States”). The

turmoil rapidly spread to other countries, especially in Europe, where many banks hold structured financial products based on US sub-prime mortgages in their portfolios. This had a number of effects: a general increase in risk premiums, which had been extremely low by historical standards; a large though temporary fall in share prices; a sudden contraction in trading in various segments of the money market owing to the perception of greater counterparty risk; and, more generally, greater caution on the part of banks in granting credit (see the box “The recent turmoil in the money and credit markets”).

... but world growth remained strong in the first half of 2007

The financial turmoil came at a time when the overall situation in the world economy was extremely favourable. In the first half of 2007 growth continued at a sustained pace in all the major economies and accelerated further in the emerging countries. Thanks to the stimulus from the latter, world trade is expected to continue to expand strongly, albeit less rapidly than last year. The prospects for growth in the world economy have become more uncertain in recent months, revolving around a central trend that is lower than the forecasts made last July, at least for the advanced economies. The forecasts of the international organizations are being revised. Those of private analysts now indicate GDP growth rates of around 2 per cent in 2008 for both the United States and the euro area (Table 1).

Table 1

Observed and projected values of some macroeconomic variables (percentage changes on the previous year, unless otherwise indicated)

	2006	Leading private forecasters (1)	
		2007	2008
GDP			
<i>Advanced countries</i>			
Euro area	2.8	2.6	1.9
Japan	2.2	1.9	1.7
United Kingdom	2.8	3.0	2.1
United States	2.9	2.0	2.1
<i>Emerging countries</i>			
Brazil	3.7	4.8	4.5
China	11.1	11.4	10.7
India	9.7	8.5 (2)	8.2 (2)
Russia	6.7	7.4	6.8
Consumer prices			
<i>Advanced countries</i>			
Euro area	2.2	2.0	2.1
Japan	0.2	-0.1	0.3
United Kingdom	2.3	2.3	1.9
United States	3.2	2.9	2.5
<i>Emerging countries</i>			
Brazil	4.2	4.0 (2)	4.1 (2)
China	1.5	4.0	3.7
India	6.1	5.8 (2)	5.5 (2)
Russia	9.7	8.5	7.8

Sources: National statistics, Deutsche Bank, Goldman Sachs, JP Morgan, CSFB and Merrill Lynch, *Consensus Economics*, September 2007.

(1) For the advanced countries, average of forecasts of Deutsche Bank, Goldman Sachs, JP Morgan, CSFB and Merrill Lynch published on 12 October 2007; for the emerging countries, *Consensus Economics*, September 2007; for China and India, *Consensus Economics*, October 2007. – (2) Changes refer to the fiscal year (April-March). – (3) December on December.

World demand has helped to keep the prices of energy and other raw materials high. The price of WTI grade oil rose to a new record of more than \$80 at the end of September (Figure 1). News of a fall in reserves in the United States and the worsening of geopolitical tensions in the Middle East contributed to the rise. The prices of oil futures contracts indicate that in the coming months oil prices are likely to fall slightly from current levels.

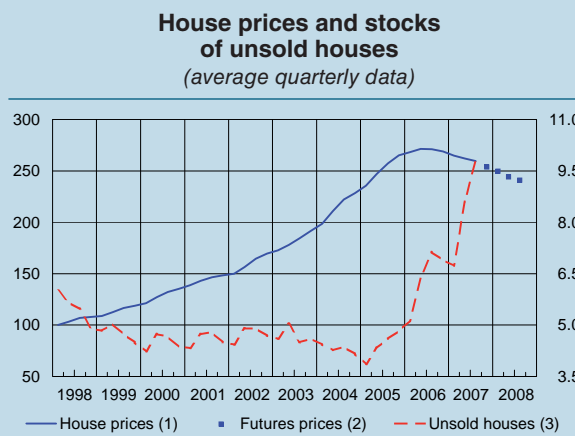
HOUSE PRICES AND THE SUB-PRIME MORTGAGE CRISIS IN THE UNITED STATES

House prices in the United States began to fall in the middle of 2006; according to the Case-Shiller index covering the 10 main metropolitan areas, in July they were 4.5 per cent lower than a year earlier. The prices of futures contracts on that index point to a further fall of 7 per cent by August 2008 (Figure A).

The decline in prices has been accompanied by a marked increase in delinquencies on mortgage loans (Figure B). It is primarily in the sub-prime mortgage sector, in other words the market in loans granted against limited personal guarantees, where payment difficulties have become more acute. Here the delinquency rate increased from 11.6 per cent at the end of 2005 to 14.8 per cent in June of this year; the increase was even large in the case of adjustable-rate mortgages, which in mid-2006 represented around two thirds of all outstanding sub-prime mortgages (Figure B).

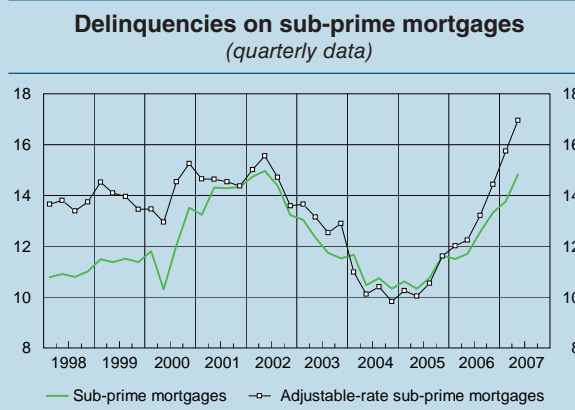
A number of factors have conspired to cause the increase in defaults: the rise in short-term interest rates (by almost one percentage point since the beginning of 2006); less rigorous assessment of the risk of insolvency by lenders because of the possibility of securitizing and reselling the mortgages they had granted; a large increase in loans with a very low initial rate (a so-called teaser rate) that will subsequently rise substantially, even without any change in market rates; the slowdown in house prices, which has limited the scope for extracting liquidity from the value of the property, causing problems mainly for borrowers who had been banking on this to meet increased payments. This combination of factors has had severe repercussions on the value of financial assets based on the securitization of sub-prime mortgages, such as mortgage-backed securities (MBSs) and collateralized debt obligations (CDOs), primarily as a result of credit downgrades by the leading rating agencies; since 9 July the prices of MBSs in the highest risk category (BBB-) fell by between 40 and 50 per cent.

Figure A



Sources: CME and National Association of Realtors.
(1) Case-Shiller 10-city composite index; 1st quarter 1998 = 100. — (2) Futures contracts on the Case-Shiller index; data relate to November 2007 and February, May and August 2008; prices quoted on 10 October 2007. — (3) Months needed to dispose of the stock of unsold houses; the figure for the third quarter of 2007 relates to August; right-hand scale.

Figure B



Source: Datastream.

THE RECENT TURMOIL IN THE MONEY AND CREDIT MARKETS

The deterioration in the outlook for the US real estate market and the accompanying increase in arrears and defaults on sub-prime mortgages at the beginning of June (see the box “House prices and the sub-prime mortgage crisis in the United States”) caused strains in the international markets in structured credit instruments directly linked to loans of this kind, such as mortgage-backed securities (MBSs) and collateralized debt obligations (CDOs). Although this class of mortgages accounts for a relatively small part of the total, the turmoil rapidly spread to a wide range of financial instruments in the main international markets. The complexity and low liquidity of structured credit instruments contributed to the problem, together with the fact that trading takes place on unregulated markets. These characteristics made it difficult to quantify the credit risk and identify the final holder, triggering a significant increase in investor uncertainty when evaluating the risks on similar structured products and inducing a widespread lessening of the willingness to assume risk.

The turmoil first spread to the entire market in asset-backed securities (ABSs), instruments that are guaranteed by loans, and then to other parts of the credit market, such as corporate bonds, and to credit default swaps (CDSs), the premiums on which provide a measure of the risk of default by major private bond issuers. In mid-August the iTraxx and CDX indices, which measure such premiums for European and US investors, showed a doubling by comparison with early June (Figure A); even larger increases were recorded by the indices for high-risk issuers (crossover indices), irrespective of their direct exposure to the sub-prime mortgage sector. In addition, from the end of June onwards the correlation between the probability of default by issuers in the iTraxx and CDX indices increased, which indicates heightened fears of systemic risks, that is to say the possibility that the crisis could spread if one or more issuers defaulted.

The tensions led to a general increase in risk premiums, prompting investors to adjust their portfolios. Yield differentials between fixed-rate corporate assets and comparable government securities widened considerably, especially for the shortest maturities; share prices fell, particularly in the banking and financial sector, and expected share price volatility increased (see the section “Economic developments and the financial markets”). The reduction in liquidity caused a sharp contraction in bond issues and placements of syndicated loans, which led to a consequent increase in the riskiness of lead managers, whose portfolios were saddled with “bridge loans” they had already granted, and had repercussions on the private equity sector. In August and September mergers and acquisitions also decreased abruptly, thus ending a long period of expansion, and the number of stock exchange listings of new companies declined. Issues of CDOs fell substantially, after several years of particularly strong growth.

The steep fall in the prices of structured credit instruments also caused serious difficulties, particularly in Europe, for some bank-related intermediaries (so-called conduits and structured investment vehicles) that had financed purchases of these long-term instruments by issuing short-term commercial paper guaranteed by real and financial assets (asset-backed commercial paper, ABCP). These intermediaries faced a sudden and drastic fall in demand for ABCP, and many had to draw on bank credit lines previously arranged with the banks to which they are related. The crisis at two German banks that had made substantial losses as a result of their exposure in the sub-prime mortgage sector through special-purpose vehicles necessitated measures to recapitalize them and the acquisition of control by other banks.

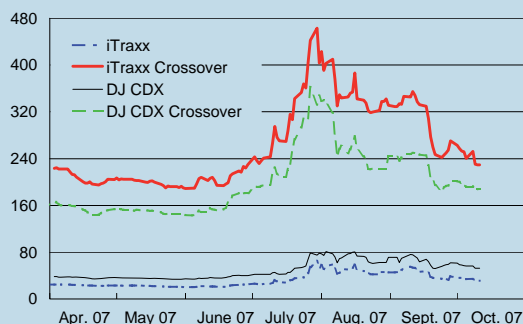
This turn of events generated strains in the interbank markets for deposits in the leading currencies. Some banks linked to the vehicle companies increased their demand for liquidity to finance the vehicles’ unexpected drawings on their credit lines; precautionary demand for liquidity also rose. At the same time, uncertainty as to the final holders of default risk caused a contraction in the supply of liquidity and a rapid general increase in counterparty risk premiums. In August and September rates on unsecured interbank deposits in euros, dollars and sterling rose sharply for medium-term

maturities, despite the fact that expectations of changes in official rates remained unchanged or were revised downwards; for three-month maturities, the interest rate differential between unsecured and secured interbank deposits widened by one percentage point in the United States and the United Kingdom and by 0.6 points in the euro area (Figure B).

Figure A

Figure B

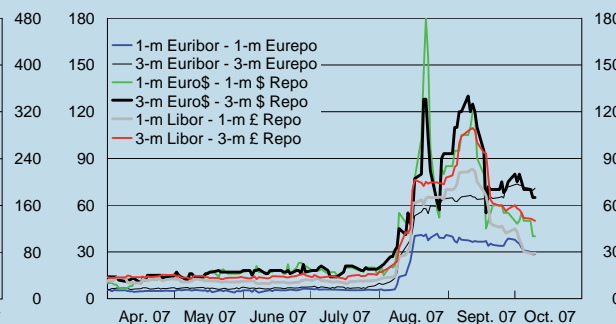
CDS indices (1)
(daily data, basis points)



Source: Bloomberg.

(1) iTraxx Europe, 5-year contract, Series 6; iTraxx Crossover, 5-year contract, Series 6; DJ CDX IG, 5-year contract, Series 7; DJ CDX Crossover, 5-year contract, Series 7.

Interest rate differentials between unsecured and secured deposits in dollars, euros and sterling
(daily data, basis points)



Sources: Bloomberg and Thomson Financial.

The leading central banks moved swiftly to counter the tensions. From 9 August onwards the ECB and the Federal Reserve carried out a series of operations to inject liquidity into the system. In the case of the ECB, the differential between the euro overnight rate (EONIA) and the official rate remained virtually nil, while in the United States the Federal Reserve kept the corresponding dollar differential negative, at an average of about -0.3 percentage points, thereby in effect bringing forward the reduction in the monetary policy target rate that was decided on 18 September. In both cases the overnight rate became highly volatile. The ECB also carried out two exceptional 90-day refinancing operations; the Federal Reserve reduced the discount rate by 50 basis points on 17 August, and at the same time lengthened the term of loans available through the discount window to one month and confirmed that it would continue to accept a wide range of financial assets as collateral. These measures limited the size of the interest rate differentials between unsecured and secured deposits for maturities of more than one month, although they nonetheless remained substantial (Figure B). By contrast, the Bank of England adopted no exceptional measures in August; at the beginning of September, in the face of mounting tensions, it announced that it was prepared to offer a larger volume of liquidity at the regular weekly auctions, thereby reducing the differential between the overnight rate and the official rate. On 14 September, confronted with the liquidity crisis at the Northern Rock bank, the UK Treasury, the Bank of England and the Financial Services Authority intervened to grant the bank exceptional funding. On 19 September the Bank of England announced a series of three-month financing operations, the first since the beginning of the crisis. As a result of these decisions and those taken by the Federal Reserve on 18 September (see the section “Economic developments and the financial markets”), the dollar and sterling differentials decreased to approximately the same levels as those for euros.

The main underlying causes of the turmoil appear to be financial, associated in part with the new model of intermediation, in which credit risk is transferred to holders other than the loan originator. In the final communiqué of the informal Ecofin meeting held on 14-15 September, the EU Finance Ministers and central-bank Governors asked the Economic and Financial Committee to launch a review, within the fora for European financial cooperation and in conjunction with similar initiatives

undertaken by international bodies such as the Financial Stability Forum and the central-bank Governors of the Group of Ten countries, on a number of problems brought to light by the recent turmoil: ways of improving the transparency of complex financial instruments, financial institutions and vehicles; ways of improving the valuation of financial instruments, risk management and stress testing aimed at assessing the effects of illiquidity; and the role of rating agencies. At their meeting on 9 October, the EU Finance Ministers approved a timetable of work on these issues, which will run until the end of 2008.

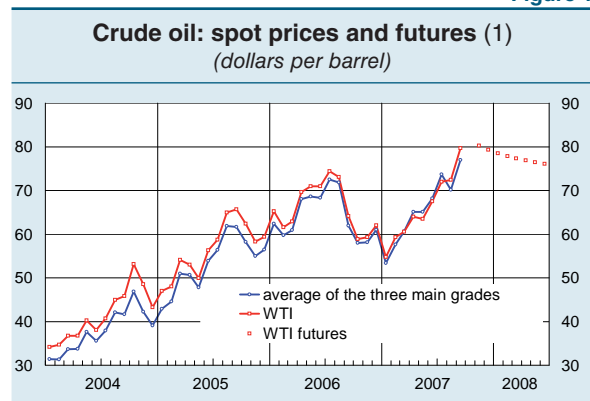
Global demand helped sustain high energy and raw material prices. At the end of September, the price of WTI grade crude reached a new all-time high, exceeding \$80 (Figure 1). News of a drop in the US reserves and the escalation of geo-political tensions in the Middle East contributed to the rise in prices. Based on the indications implicit in futures contracts, in the coming months prices should contract slightly.

The American sub-prime mortgage crisis affected the financial markets

The crisis in the US sub-prime mortgage sector, coupled with great uncertainty about the scale and distribution of individual institutions' exposure, triggered acute turbulence in the international financial markets from the second half of July onwards. The general rise in risk premiums led to a sharp fall in the prices of the riskiest assets. Between 19 July and 16 August the main international stock exchanges experienced pronounced corrections, of around 10 per cent (Figure 2). Yield differentials between comparable corporate and government bonds widened (Figure 3), with more marked increases for companies with the lowest credit rating and those in the banking and financial sectors. The price volatility of financial assets rose steeply everywhere (Figure 4). The shift in investors' portfolios towards more liquid and less risky assets, together with a downward adjustment of expectations of economic growth, led to a substantial fall in yields on the government bonds of industrial countries (Figure 5).

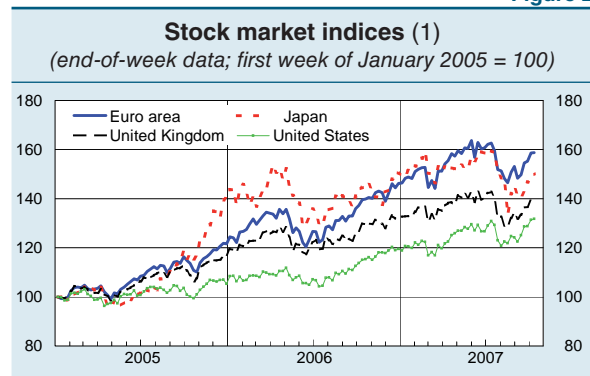
Increased risk aversion on the part of investors and uncertainty about the future performance of the world economy also affected emerging countries, although the impact was milder than on previous occasions, such as May and June 2006. There was a sudden increase in risk premiums, measured by the yield differential between these countries' long-term dollar-denominated sovereign bonds and US Treasury bonds; share prices fell by about as much as in the advanced countries; and the currencies of some countries, particularly those of Brazil, Russia and Thailand, depreciated.

Figure 1



Sources: IMF and Thomson Financial Datastream.
(1) Monthly averages for spot prices. Updated to 10 October 2007. The three main grades are Brent, Dubai and WTI.

Figure 2



Source: Thomson Financial Datastream.
(1) Updated to 10 October 2007. 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.

The turbulence eased somewhat following interventions by the central banks

The turmoil in equity and bond markets subsided after the reduction in the discount rate in mid-August by the US Federal Reserve and the repeated injections of funds by the central banks of the leading industrial countries (see the box “The recent turmoil in the money and credit markets”). Stock markets made good their recent losses; in September some share indices exceeded their previous peaks. In the industrial countries the rise in risk premiums on corporate bonds halted, and yields on government bonds rose slightly. The observed and expected price volatility of financial assets declined, as did risk premiums on the government bonds of emerging countries, but risk premiums on the interbank market remained high, reflecting a heightened perception of counterparty risk.

The dollar falls to a new historic low

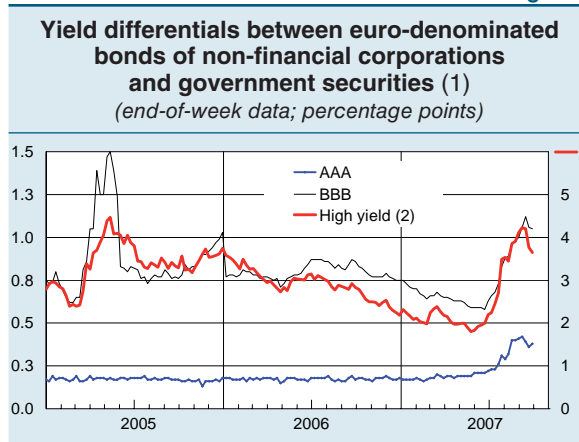
The US dollar fell to \$1.38 against the euro in July, recovered temporarily in the first half of August, but began to depreciate again in subsequent weeks, to below \$1.40 (Figure 6). Against the backdrop of the United States’ continuing external imbalance, the downward pressure on the currency was fuelled by the narrowing of yield differentials between financial assets in dollars and those in euros and of expected growth differentials between the two areas. In the third quarter the dollar also depreciated sharply (by 5.1 per cent) including against the yen, owing partly to the precipitous unwinding of a number of speculative carry trade positions in yen. It continued to weaken gradually against the renminbi (1.4 per cent). Since the beginning of 2007 the US currency has depreciated by 6 per cent in nominal effective terms, falling to its lowest level since the beginning of 1997.

THE MAIN INDUSTRIAL AND EMERGING COUNTRIES

A slowdown is expected in the United States in the second half of 2007

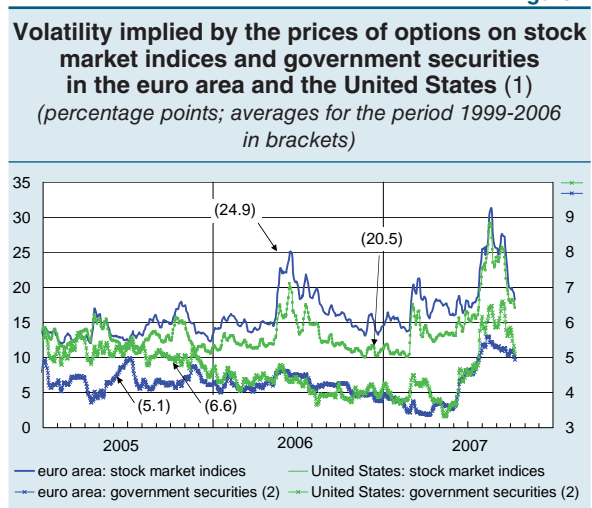
After very modest growth in the first quarter of 2007 (0.6 per cent at an annual rate), the US economy regained strength in the second (3.8 per cent). Investment in plant and equipment increased very rapidly (by 11.1 per cent), while residential investment continued to contract, although more slowly than in the two preceding quarters. The growth in household consumption slowed to 1.4 per cent, affected by

Figure 3



Source: Merrill Lynch.
 (1) Yields on fixed-rate euro-denominated Eurobonds with a residual term to maturity of not less than one year issued by corporations resident in countries whose long-term foreign currency debt has a rating of not less than Baa3 or BBB- (investment grade). Yield differentials are calculated with respect to French and German government securities. – (2) Right-hand scale. Includes only bonds of companies with a rating of less than Baa3 or BBB- (high yield).

Figure 4



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.

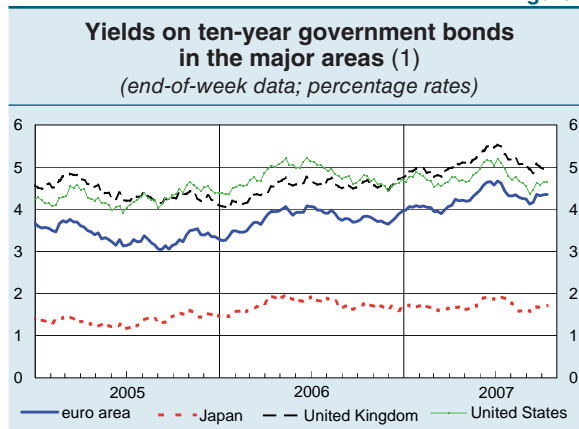
the sharp slowdown in real disposable income. Foreign demand had a positive effect on growth, as exports returned to a rate of increase (7.5 per cent) not dissimilar to that of 2006. Conflicting indications emerged in the third quarter, but overall the risks of a slowdown increased. Signs of a strengthening in consumption and exports contrasted with a deterioration in business confidence (Figure 7). The crisis in residential investment seems to have deepened in the third quarter and could continue with unabated intensity in the fourth (see the box “House prices and the sub-prime mortgage crisis in the United States”). Consumption could be adversely affected in the coming months by the fall in house prices and the adoption of stricter mortgage lending criteria.

On 17 August, at the same time as announcing measures to restore orderly conditions in the money market (see the box “The recent turmoil in the money and credit markets”), the Federal Reserve stated that it was ready to intervene to mitigate liquidity risks if circumstances demanded. Market interest rates at all maturities declined, reflecting expectations of an imminent cut in official rates in response to the growing risks to growth and the abating of inflation risks. A reduction of half a percentage point was in fact then decided on 18 September (Figure 9). At the beginning of October the prices of futures contracts on the federal funds rate indicated expectations of further reductions at the end of October and the beginning of 2008.

The leading private analysts currently expect annualized GDP growth to be around 3 per cent in the third quarter. They have revised their forecasts for the fourth quarter of 2007 and the average for 2008 significantly downwards by comparison with the end of July, to approximately 1.5 and 2 per cent respectively.

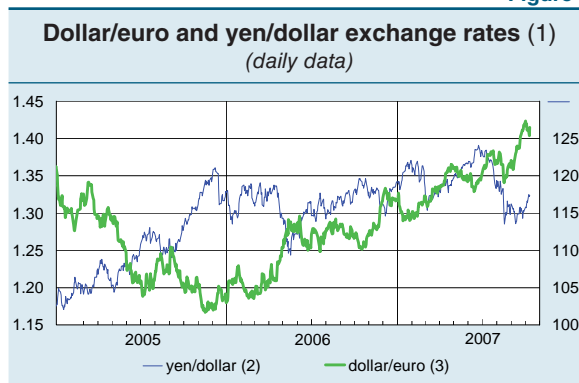
Inflation, as measured by the consumption deflator excluding food and energy, declined slightly during the summer, from 1.9 per cent in June to 1.8 per cent in August (Figure 8). Private analysts’ short-term inflation forecasts and the longer-term expectations that can be deduced from interest rate differentials between indexed and un-indexed government securities remained broadly unchanged.

Figure 5



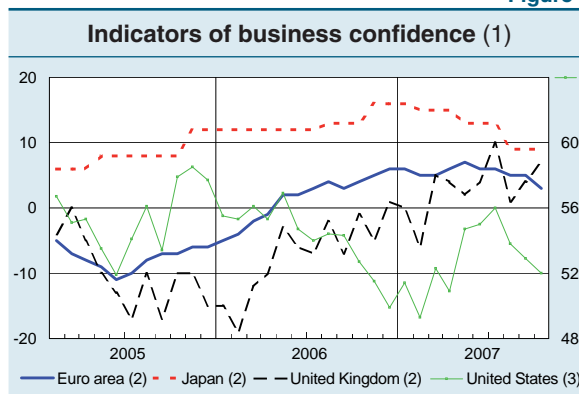
Source: National statistics.
(1) Updated to 10 October 2007.

Figure 6



Source: ECB.
(1) Updated to 10 October 2007. – (2) Right-hand scale. – (3) Left-hand scale.

Figure 7



Sources: National statistics and European Commission.
(1) Manufacturing sector. Percentage balance of firms' responses. – (2) Left-hand scale. – (3) Right-hand scale.

The expansion in Japan continues, albeit at an uneven pace

Growth in Japan remained erratic, making it difficult to identify underlying trends. An annualized 3 per cent increase in GDP in the first quarter of this year was followed by a contraction of 1.2 per cent. Available data on the third quarter provide conflicting indications. Industrial output rose strongly in August, but business confidence has shown a tendency to deteriorate for some months. The slowdown in employment growth in recent months and enduring wage stagnation could continue to hold back consumption growth. According to the forecasts of private analysts (Table 1), the Japanese economy should continue to grow this year and next at an average rate slightly slower than in 2006.

Consumer price inflation remained essentially nil, even in the measure excluding the most volatile components. The Bank of Japan kept its reference interest rate unchanged at 0.5 per cent. Yields on ten-year government bonds, which had risen by about 30 basis points in the first half of the year, came back down to 1.6 per cent during the summer, reflecting the waning of expectations of an increase in official rates.

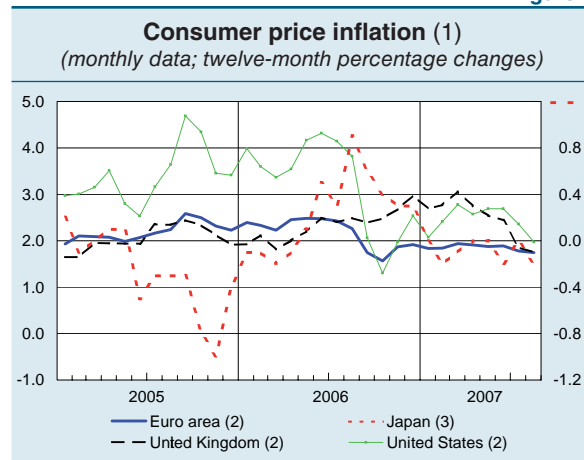
Growth in the United Kingdom remained strong

In the second quarter the UK economy continued to grow at an annual rate of 3.3 per cent, close to the rates recorded in preceding quarters. Business confidence does not appear to have been adversely affected by the turmoil in the financial markets (Figure 7), even though a survey carried out by the Bank of England indicated that the availability of credit to companies has declined in the last few months. Inflation, as measured by the harmonized consumer price index, continued to fall rapidly from the high level touched in the first half of this year, falling to 1.8 per cent in August. The Bank of England kept its reference rate unchanged at 5.75 per cent, after having increased it at the beginning of July. Until August the markets had expected a further increase, but in September they began to anticipate a possible reduction before the beginning of 2008.

The rapid expansion of the emerging economies continues

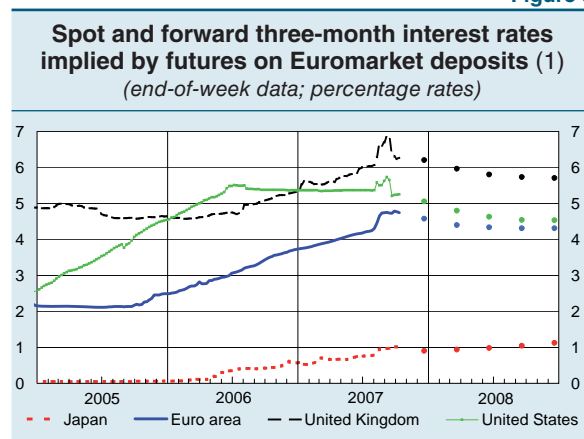
In the first half of the year the expansion in economic activity in the leading emerging countries remained strong and in some cases was more rapid than last year. As in 2006, China, India, Russia and Brazil together accounted for around half of the growth in world GDP. The financial turmoil during the summer had a limited impact on their rates of growth, which according to private analysts were only slightly lower in the second half of the year.

Figure 8



Sources: Thomson Financial Datastream and Bloomberg.
(1) General price index. For the United Kingdom, harmonized consumer prices. – (2) Left-hand scale. – (3) Right-hand scale.

Figure 9



Source: Thomson Financial Datastream.
(1) Spot interest rates updated to 10 October 2007; prices of futures on 10 October.

In China GDP increased at an annual rate of 11.5 per cent in the first half of 2007 (compared with 11.1 per cent in 2006), and continued to be powered to a large extent by the strong growth in investment and exports. The current account surplus widened further and could amount to almost 12 per cent of GDP in 2007 (9.5 per cent in 2006). Measures were recently introduced to reduce the tax incentives for exports, but so far they have been of limited effectiveness. The renminbi continued to appreciate gradually against the dollar; the effective appreciation since July 2005, when the new exchange rate regime was introduced, is around 4 per cent. In order to absorb excess liquidity, the Chinese central bank raised interest rates and increased the level of compulsory reserves, but these measures have had a very small effect so far. The strong acceleration in inflation, to 6.5 per cent in August, is attributable entirely to increases in food prices, owing to supply bottlenecks.

THE EURO AREA

Growth slows slightly In the second quarter of 2007 euro-area GDP increased at 1.3 per cent on an annual basis, well below the rate of the preceding quarters. The slowdown reflects mainly the fall in investment in construction, by 6.2 per cent at an annual rate. Household consumption grew by 2.2 per cent, sustained by the increase in disposable income. Net foreign demand made a small positive contribution.

More recently, industrial production has remained positive (Figure 10) while the other economic indicators have deteriorated slightly, although staying at a level consistent with continued cyclical expansion. In September the €-coin indicator, which provides a real-time estimate of the rate of GDP growth adjusted for short-term fluctuations, signalled a further decline, while projecting that growth would improve in the third quarter compared with the second (Figure 11; see the box “€-coin, a real-time estimate of growth in the euro area”).

An examination of the main euro-area economies reveals a mixed cyclical picture. In Germany industrial production increased by around 1 per cent in the two months from June to August with respect to the previous period. Business confidence, as captured by the IFO survey, remains historically high, but has been falling steadily since the spring. In France the rise in industrial activity and retail sales of manufactured goods has been accompanied by less positive indications about business confidence in the industrial sector.

Figure 10

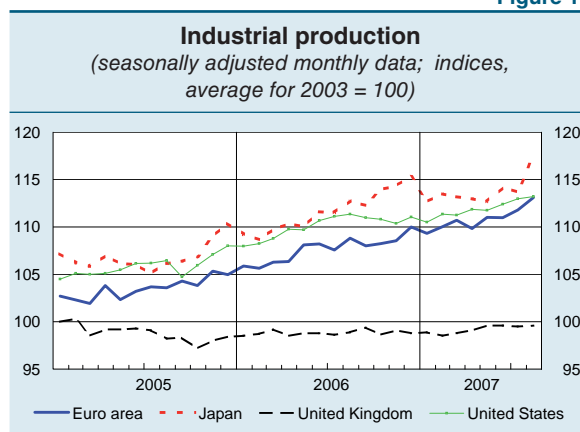
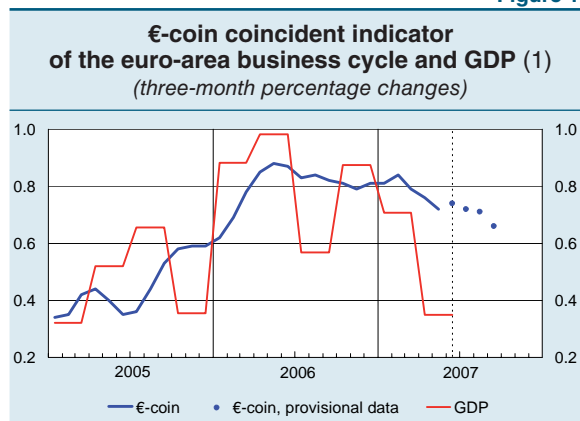


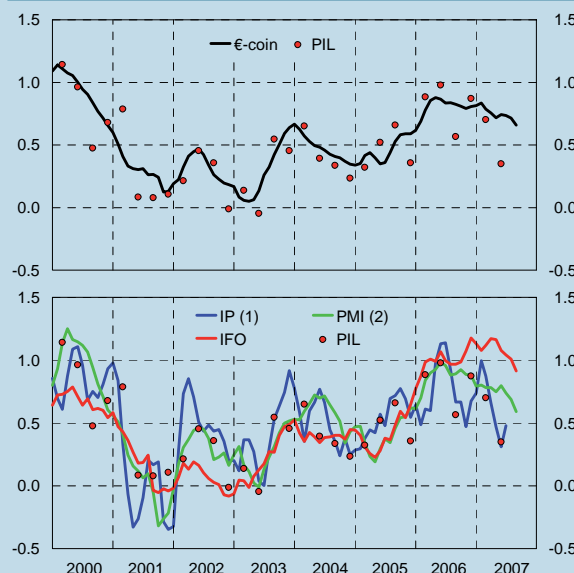
Figure 11



€-COIN: A REAL-TIME ESTIMATE OF GROWTH IN THE EURO AREA

Official figures on euro-area GDP are available only at quarterly intervals and not until about 45 days after the reference period; moreover, the data are subject to revision and short-term volatility that complicate interpretation. For a comprehensive assessment of the current outlook for the economy, many statistics are available on an almost daily basis, but the problems posed by their different frequency, timeliness and reliability have to be resolved. The composite indicators currently available suffer from high volatility, often relate to a single country or sector and are difficult to use for the euro area as a whole. In order to overcome at least some of these problems, the Economic Research Department of the Bank of Italy has devised €-coin, a monthly indicator (see the Figure; for further information on the method of calculating the indicator, see F. Altissimo, R. Cristadoro, M. Forni, M. Lippi and G. Veronese, “Eurocoin: Tracking Economic Growth in Real Time”, in Banca d’Italia, Tema di Discussione No. 631).

€-coin compared with other indicators



Sources: Bank of Italy, Eurostat IFO and Reuters.
(1) Index of euro-area industrial production. – (2) Purchasing managers’ index for manufacturing industry in the euro area.

€-coin is a composite, timely measure that gives an immediate reading of growth in the euro area; using multivariate statistical analysis, it provides a real-time estimate of GDP growth in the area, cleansed of the more erratic and volatile components. In other words, €-coin “captures” the trend-cycle component of growth, highlighting cyclical turning points more clearly than other indicators. In the new version published in September (for a more detailed presentation of the indicator, see the website <http://eurocoin.bancaditalia.it>), the indicator is based on a revised and extended dataset, uses an estimation technique better suited to extracting the underlying components of growth and produces a more timely estimate (the figure for each month is now published at the end of the month itself, thirty days earlier than with the previous version).

Inflation expectations remain stable

Inflation in the area as a whole fell from 1.9 per cent to 1.8 per cent in July and 1.7 per cent in August. Core inflation accelerated slightly in the latter month, to 2 per cent, mainly owing to sharp increases in the prices of processed food (from 1.9 per cent in July to 2.5 per cent). According to the flash estimate published by Eurostat, euro-area inflation accelerated to 2.1 per cent in September, owing partly to the base effect of the statistical comparison with the preceding year, when energy prices had fallen substantially. The main private forecasters kept their expectations of average inflation in the area virtually unchanged (around 2 per cent for both 2007 and 2008).

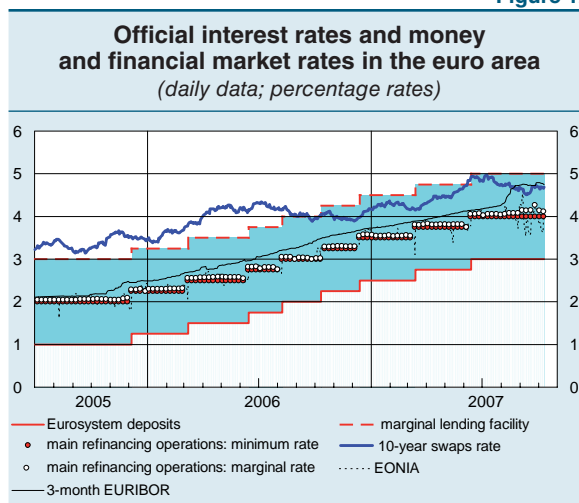
The ECB keeps its reference rates unchanged

At its meetings in August and September the European Central Bank kept the minimum rate on main refinancing operations unchanged at 4 per cent (Figure 12). The ECB provided the market with additional funds on several occasions by means of both main refinancing and three-month operations in order to meet the high demand for liquidity from banks and to stabilize short-term money-market

rates. Incorporating the rise in the risk premium associated with high uncertainty about the outcome of the crisis, three-month Euribor nevertheless rose sharply from its July level (by 60 basis points, to 4.8 per cent at the beginning of October).

The growth in bank lending to the private sector continued to accelerate (to 11.2 per cent in August), reflecting the rapid expansion in lending to firms in contrast with a slowdown in lending to households, particularly for house purchases. However, according to information obtained in September from banks participating in the Bank Lending Survey, lending criteria are tightening following the turmoil in the financial markets. Liquidity conditions remain expansionary, as indicated by the rate of growth in the M3 money supply, which was running at a record 11.6 per cent in August. The rapid growth in money continues to be driven by the strong expansion in less liquid monetary assets due to the narrow differential between long-term and short-term yields.

Figure 12



Sources: ECB, Reuters and Telerate.

3 RECENT DEVELOPMENTS IN ITALY

THE CYCLICAL SITUATION

In 2007 GDP growth has slowed, held back by a fall in exports

Since the end of 2006, there has been a slowdown in economic activity in Italy (Table 2). Following an essentially flat second quarter, our most recent figures indicate a slight acceleration in GDP last summer, to close to the estimated potential growth rate of the economy.

The slowdown in output growth in the first half of the year was partly due to the fall in exports, which were adversely affected by weakened growth in the euro area, in particular in Germany. Household consumption, buoyed by an upturn in available income, began to rise appreciably, at an annualized rate of about 2.5 per cent, with a steeper improvement in durable goods. Investment grew in line with GDP. Taking account of the slower build-up in stocks, the overall contribution of national demand to GDP growth was still fairly limited (Figure 13) and not enough to ensure a more solid expansion.

Employment is once again following the positive trend that was temporarily interrupted last year. The increase in the number of jobs in the first half of the year mainly concerned the Centre and North, where the unemployment rate fell to historically low levels.

Price increases over the first nine months of 2007 remained below the trend rate of 2 per cent, curbed by the small growth of internal costs, low pressure on the demand side, and the strengthening of the euro.

The turmoil in the international financial markets may affect growth but only slightly

The turmoil in the international financial markets that began last August has not so far had any significant effect on

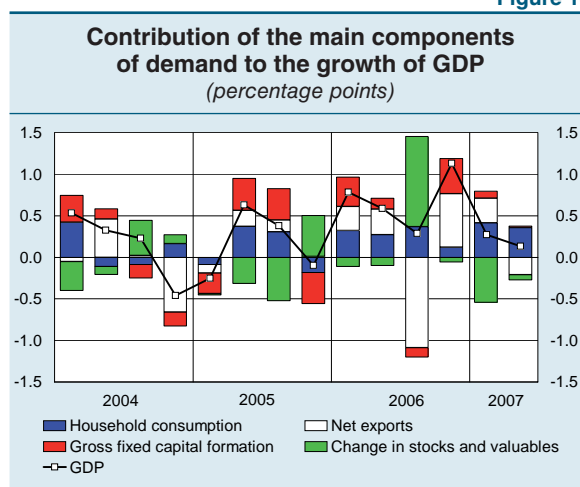
Table 2

	GDP and its main components				
	<i>(chain-linked volumes; adjusted for seasonal and calendar effects; percentage changes on previous period)</i>				
	2006		2006	2007	
	Q3	Q4	(1)	Q1	Q2
GDP	0.3	1.1	1.9	0.3	0.1
Total imports	2.2	1.8	4.3	-1.1	-0.3
National demand (2)	1.4	0.5	1.6	..	0.3
National consumption	0.5	0.2	1.0	0.6	0.5
<i>households</i>	0.6	0.2	1.5	0.7	0.6
<i>other (3)</i>	0.2	..	-0.3	0.1	0.1
Gross fixed investment	-0.6	2.1	2.3	0.4	0.1
<i>construction</i>	0.3	2.8	2.1	1.5	-1.3
<i>other goods</i>	-1.4	1.4	2.6	-0.6	1.4
Change in stocks and valuables (4)	1.1	-0.1	0.3	-0.5	-0.1
Total exports	-1.9	4.2	5.3	-0.1	-1.0
Net external demand (4)	-1.1	0.6	0.3	0.3	-0.2

Source: Istat.

(1) 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 previous period in percentage points.

Figure 13



Source: Istat.

economic activity, but the most recent qualitative surveys report growing concern on the part of businesses. Compared with last July's forecasts, the macroeconomic scenarios for 2008 could be affected by this, even if only slightly. According to the available estimates, the appreciation of the euro since the start of 2006 – about 5 per cent in real terms – curbed GDP growth in Italy only modestly.

FIRMS

Industrial production has risen, but demand weakens

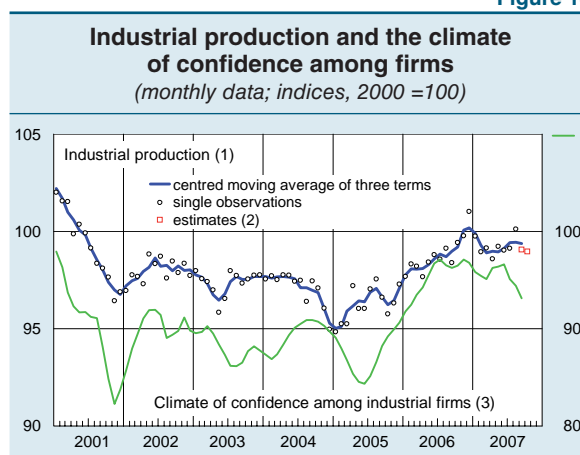
Industrial production appears to have followed its decline in the first half of the year with a partial recovery in the third quarter, rising back close to the level at which it began the year (Figure 14). After the strong growth recorded in August, estimates for the two months September-October, based on electricity consumption, indicate that the pace of production slowed down along with orders (Figure 15). According to the data now available, the cyclical situation will not change in the fourth quarter, with production likely to fluctuate around its levels of the summer. The business outlook survey carried out by the Bank of Italy's branches at the end of September (see the box "The state of the economy: findings of the survey of a sample of Italian firms in industry and services"), the ISAE surveys and the poll conducted by the Bank of Italy together with *Il Sole 24ore* registered signs of a weakening of demand in connection with the international financial turbulence and with the exchange rate of the euro.

In the first half of 2007 investment grew at a similar rate to GDP.

Gross fixed investment is in line with the GDP cycle. It is flat in machinery and equipment ...

Investment in machinery and equipment remained virtually unchanged around the high level it had reached at the end of 2006. In a context of favourable financial conditions, the propensity to invest is undermined by uncertainty engendered by the softness of demand. However, the firms interviewed in the survey conducted by the Bank's branches broadly confirmed the investment plans they had prepared at the start of the year.

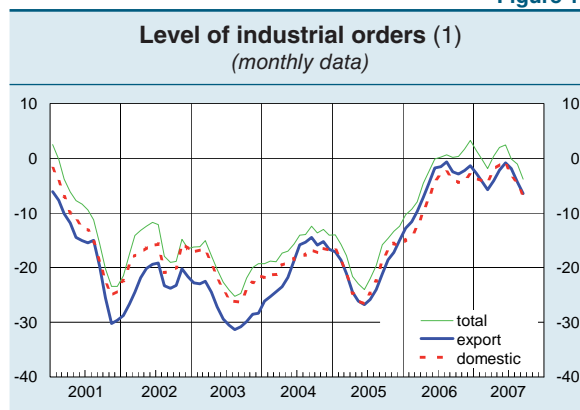
Figure 14



Sources: Based on ISAE, Enel and Istat data.

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

Figure 15



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 ISAE surveys, weighted by size, sector and location of firm. The trend figures refer to the responses for three months ahead. Seasonally adjusted data.

THE STATE OF THE ECONOMY: FINDINGS OF THE SURVEY OF A SAMPLE OF ITALIAN FIRMS IN INDUSTRY AND SERVICES

Between 20 September and 10 October the branches of the Bank of Italy carried out the Fifteenth Cyclical Survey of a sample of firms with 20 or more employees in industry excluding construction and in services. The overall picture that emerges from the firms' assessments is one of a continuation of the expansion that began in mid-2005, albeit at a slower pace.

For 2007 the majority of the firms expect their nominal expenditure on fixed investment to be in line with their plans made at the beginning of the year (see Table) and to be an estimated 2.5 per cent higher in real terms than in 2006. Firms expecting their investment to be higher than planned slightly outnumber those expecting it to be lower. The number of firms indicating an expected increase in capital formation in 2008 also has the upper hand by a small margin.

**Main results of the cyclical survey of Italian firms
in industry excluding construction and in services (1)**
(percentage composition of replies, excluding replies of "don't know")

RESPONSE	2006			2007		
	Industry excl. construction	Services	Total	Industry excl. construction	Services	Total
<i>Investment spending during the year in relation to initial planned investment</i>						
Lower	16.8	15.3	16.2	17.3	12.8	15.4
Practically the same	62.3	63.0	62.6	62.0	66.0	63.7
Higher	20.9	21.7	21.2	20.7	21.3	20.9
<i>Investment spending planned for the following year</i>						
Lower	18.0	19.9	18.8	20.0	17.0	18.7
Stable	53.4	56.6	54.7	52.4	57.6	54.6
Higher	28.6	23.5	26.5	27.6	25.4	26.7
<i>Employment during the year (2)</i>						
Lower	23.3	23.4	23.3	19.1	13.6	16.4
Practically the same	51.2	45.5	48.5	50.9	48.0	49.5
Higher	25.6	31.0	28.2	30.0	38.4	34.1
<i>Expected trend in orders over next six months</i>						
Lower	9.6	11.1	10.2	13.2	11.3	12.4
Stable	41.7	48.5	44.5	43.2	50.4	46.2
Higher	48.7	40.4	45.3	43.6	38.3	41.4
<i>Industrial production in fourth quarter with respect to third quarter</i>						
Lower	10.2		10.2	12.3		12.3
Practically the same	44.0		44.0	45.6		45.6
Higher	45.8		45.8	42.1		42.1

(1) Survey conducted by means of telephone interviews. Sample of firms with 20 or more employees in industry excluding construction (3,058 firms) and in services (wholesale and retail trade, hotels and restaurants, transport and communications, other professional services: 1,138 firms). Percentages are estimated using a weight for each firm which takes account – for the total distributions by geographical area, size of firm and branch of activity – of the ratio between the sample size and the population of firms. Standard errors of the estimated percentages are not greater than 0.7 per cent. – (2) Weighted according to the number of employees. Changes in average employment in 2007.

One third of the firms interviewed considered that their reference market had expanded during the previous six months, while 11 per cent thought it had been in recession. Among those not noticing significant changes (54 per cent of the sample), fewer than one fifth expect an expansion during the next half-year. According to the respondents, signs of a mild slowdown in demand appeared during the summer: orders stagnated at their June level for almost half of the firms and rose for just under 40 per cent of them. For the remainder of the year, more than four fifths of the sample expect both orders and industrial production to increase or remain static. As in past surveys, a large majority of firms expect to end the current year with a post-tax profit (70 per cent); only one tenth expect to record a loss.

In 2007 the average level of employment should be higher than last year, especially in services, among firms in the North and among larger companies. Among the firms in the sample, wage increases over and above those granted under national collective agreements affected 37 per cent of employees in industry and 30 per cent of those in services (compared with 45 and 40 per cent respectively in 2006). The increases, which were more common in larger firms, exceeded 2 per cent for only about one quarter of the employees involved.

... decreasing in construction ...

The growth of investment in construction, which had been gradually decelerating, turned negative in the spring. Residential building activity contracted for the first time since 2004, confirming the signs of a cyclical downturn in real estate that had emerged in 2006 with the slowdown in house sales and prices following the increase in the cost of mortgage loans. In August the climate of confidence among construction firms held steady at levels above the lows reached in the spring; it is likely that activity will recover to some extent in the coming months.

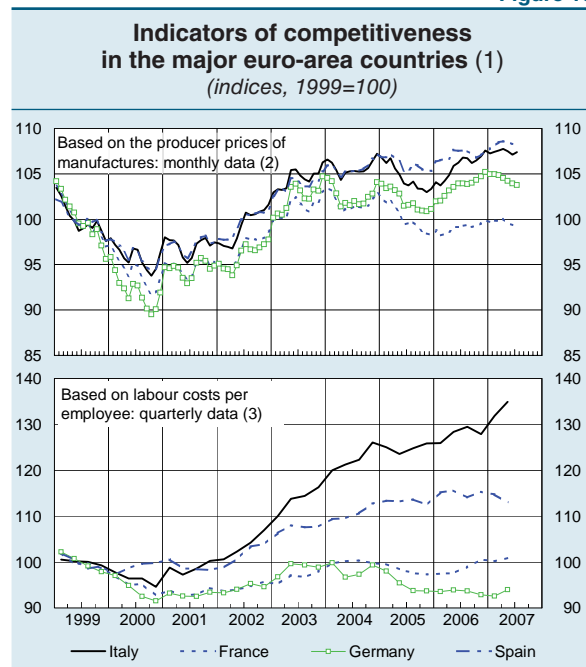
... and increasing in transport equipment

After the steep decline in the first quarter, investment in transport equipment accelerated sharply in the second, growing by 9 per cent quarter on quarter, thanks to the stimulus of the tax incentives that took effect in the spring.

Price competitiveness worsens slightly owing to the appreciation of the euro

In the first half of 2007, firms' competitiveness, measured by the real effective exchange rate calculated on the basis of producer prices, remained virtually unchanged with respect to the second half of 2006 (Figure 16). The slowdown in producer prices enabled the index of competitiveness to regain its end-2006 level during the summer; this recovery was halted in September by the rapid appreciation of the euro. Measured on the basis of unit labour costs, competitiveness deteriorated plainly in the first six months of the year, especially vis-à-vis the other major euro-area countries (Figure 16).

Figure 16



Sources: Based on IMF, OECD and Eurostat data.
(1) An increase in an index signals a loss of competitiveness. – (2) In relation to 61 competitor countries; latest available data refer to July 2007. – (3) In relation to 24 competitor countries; latest available data refer to the second quarter of 2007.

**Productivity slows,
unit labour costs
accelerate**

The weakness of industrial activity in the first half was reflected in a productivity slowdown (of about half a percentage point with respect to the previous period), due in part to the increase in employment. Labour costs per full-time employee rose by 2.2 per cent, while unit labour costs increased by 2.8 per cent (Figure 17). With unit labour costs declining in the service sector, unit labour costs for the whole economy remained practically unchanged compared with the second half of 2006.

Firms' profitability rises...

According to estimates based on the national accounts, firms' operating profitability rose slightly in the twelve months to June 2007 compared with 2006. The improvement in gross operating profit more than offset the increase in net financial charges (due mainly to the rise in interest rates). Self-financing grew.

...as does their debt...

Firms' borrowing requirement, defined as the difference between gross investment (including stocks) and self-financing, remained about the same. Financial debt has continued to grow and is now equal to 69 per cent of GDP, nearly 2 percentage points higher than in December (Figure 18).

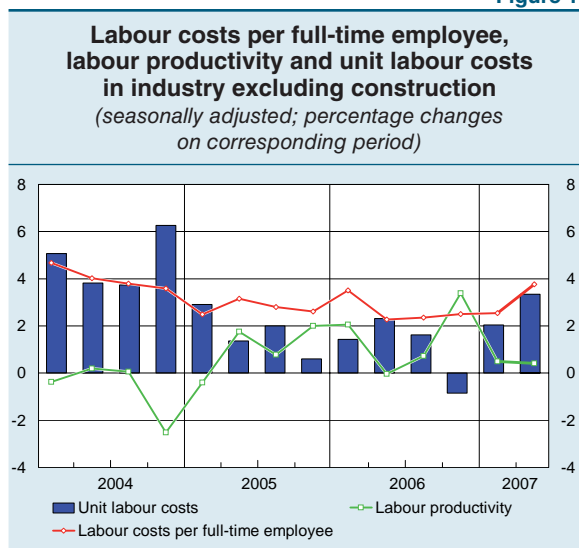
After not tapping the bond market in any significant way the second half of 2006, firms made net bond issues amounting to more than €6 billion in the first half of this year. There were no large capital increases by listed companies, but there was a rise in the number of new listings. Lending to firms continues to accelerate, expanding by 13.1 per cent in the twelve months to August; the increase was very substantial for medium-sized and large firms and for those in the South (Figure 19).

...without particular financial strains

Despite adjusting to the increase in official rates, the cost of bank credit for firms is still low by historical standards. The risk indicators on corporate debt have come down slightly and remain at low levels compared with the past. Substandard loans – i.e. loans to firms in temporary difficulty – have also diminished.

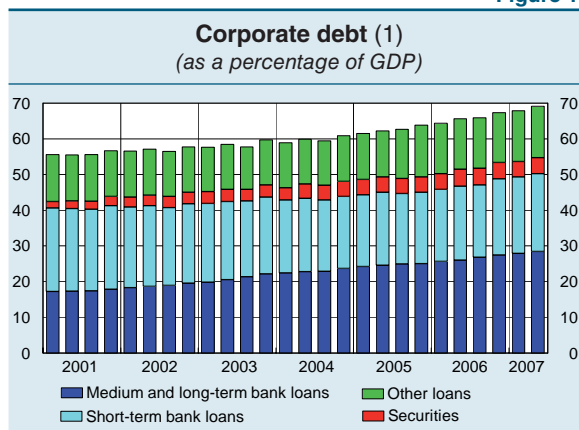
In the second quarter of 2007 Italian companies announced 63 acquisitions of significant shareholdings amounting to €18.4 billion, of which €11.5 billion for minority interests. Prominent among the latter were the acquisition by an Eni-Enel consortium of some assets of Yukos (€4.4 billion) and the acquisition by Eni of €3.5 billion of oil and gas assets from Dominion, one of the largest American energy companies.

Figure 17



Source: Istat.

Figure 18



(1) The figures for the fourth quarter of 2007 are provisional.

HOUSEHOLDS

Consumer spending has so far remained strong...

In the first six months of 2007 household consumption accelerated to annual growth of over 2 per cent with respect to the last half of 2006.

The strong expansion in spending on services and durable goods continued (at an annualized rate of about 3.5 per cent in the first six months). Almost two fifths of spending on durables was on automobiles, boosted by the 2007 Finance Law's incentives to replace old vehicles and by the wider choice of new models. By contrast, spending on food products continued on the downward trend underway for the past year.

According to our preliminary estimates, in the first six months of 2007 households' real disposable income accelerated to growth of 1.1 per cent on the year-earlier period (about 0.5 per cent more than in the last half of 2006; Figure 20). The chief contributory factor to this increase was growth in employees' compensation, thanks in particular to an increase in employment.

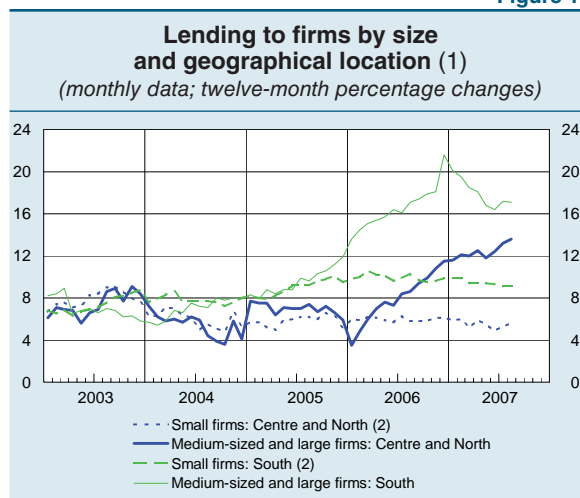
... but there are increasing signs of a slowdown

As shown by the fall and subsequent flatness of the ISAE consumer confidence index (Figure 20), on the whole households continue to be prudent. Recent data on retail sales in small and large outlets suggest that consumption of food products continued to fall in the third quarter. Following the removal of state incentives for scrapping, new vehicle registrations, which had experienced lively growth in the first six months of 2007, fell in the third quarter (-2.9 per cent compared with the previous period) and almost came to a complete standstill in September. Car dealers reported a drop in new orders, making continued modest performance likely for the rest of the year.

Growth in household debt also slows

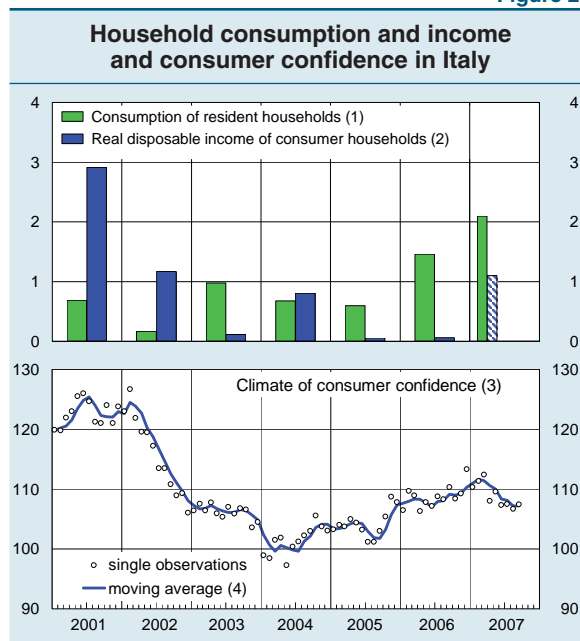
While continuing to expand at a rapid pace household debt slowed (to 10.3 per cent in the twelve months to June 2007). This was partly due to higher short-term interest rates, increasing since the beginning of 2006. Bank loans

Figure 19



(1) Loans exclude repos, bad debts and other, minor items included in the Eurosystem harmonized definition of the aggregate. The breakdown by geographical area is based on customer residence. The percentage changes are calculated net 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.

Figure 20



Sources: Based on Istat and ISAE data.

(1) Chain-linked volumes; percentages changes. In the first six months of 2007; data seasonally adjusted and adjusted for number of working days in month. – (2) Deflated using the deflator of consumption of resident households; our estimates for the first half of 2007. – (3) Index: 1980=100, seasonally adjusted data. – (4) Moving average for the three months ending in the reference month.

for house purchases have slowed (to a 12-month rate of 9.5 per cent in June against 12.6 per cent in December 2006) as has consumer credit (9.9 per cent against 13 per cent). Last June the ratio of financial debt to disposable income climbed to almost 49 per cent, almost two percentage points more than at the end of June 2006 (Figure 21). The most recent data signal a slight acceleration in loans (9.8 per cent in August). Consumer credit, by contrast, recorded a further slowdown (to 6.8 per cent), confirming the indications of the *Bank Lending Survey* (see the box “Credit supply and demand in Italy: the effects of the recent turmoil in the financial markets”).

The cost of debt-service (payment of interest and repayment of capital) rose to 7.3 per cent of disposable income in the twelve months ending June 2007, almost half a point more than it was at end December 2006. The increase is partly due to interest rate rises in the current year (Figure 22).

FOREIGN DEMAND AND THE BALANCE OF PAYMENTS

Italy's exports decrease in the second quarter of 2007

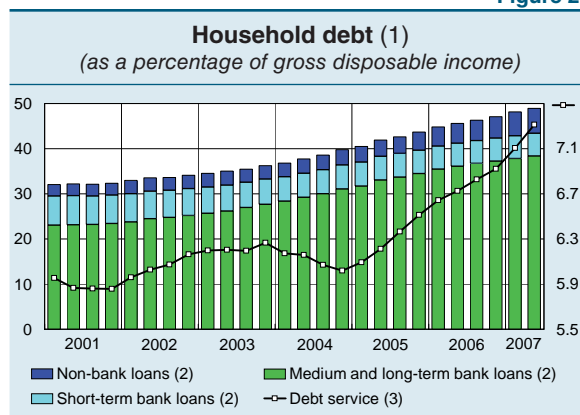
In the second quarter of 2007 Italian exports of goods and services, measured by the national accounts, contracted by 1 per cent quarter-on-quarter, after remaining stationary in the first three months (Table 2). This contrasts with the trend of exports in the other euro-area countries, which recorded an increase in both the first and second quarters. Italy's share of world trade, in nominal terms, is likely to grow to the same values as in 2004, while at constant prices it should remain broadly unchanged.

CREDIT SUPPLY AND DEMAND IN ITALY: THE EFFECTS OF THE RECENT TURMOIL IN THE FINANCIAL MARKETS

In order to gain an insight into the repercussions that the crisis over the summer may have had on conditions for lending to households and firms, a number of specific questions were added to the standard questionnaire for the latest Bank Lending Survey, which was conducted in the last ten days of September. According to the replies from the Italian banks interviewed,¹ the

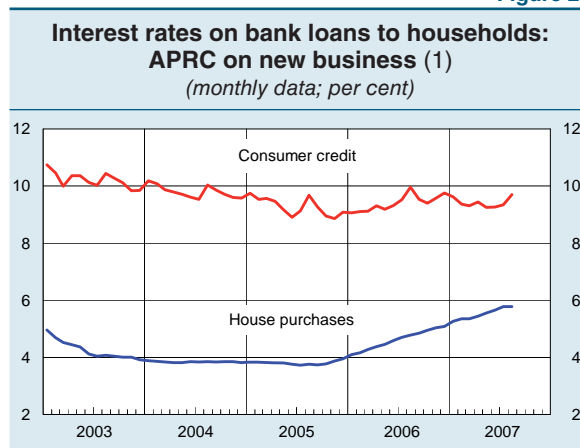
¹ The results of the survey for the euro area are available on the website www.ecb.int and those for Italy on the website www.bancaditalia.it.

Figure 21



Sources: Istat and our estimates for gross disposable income. (1) Consumer households, non-profit institutions serving households and sole proprietorships with up to 5 workers. Disposable income and debt service are for the twelve months ending in the reference quarter. For quarterly data on disposable income, our estimates; 2006 data, estimates. – (2) Left-hand scale. End-of-period stocks. – (3) Right-hand scale. Refers only to consumer households. Debt service includes payment of interest and repayment of principal.

Figure 22

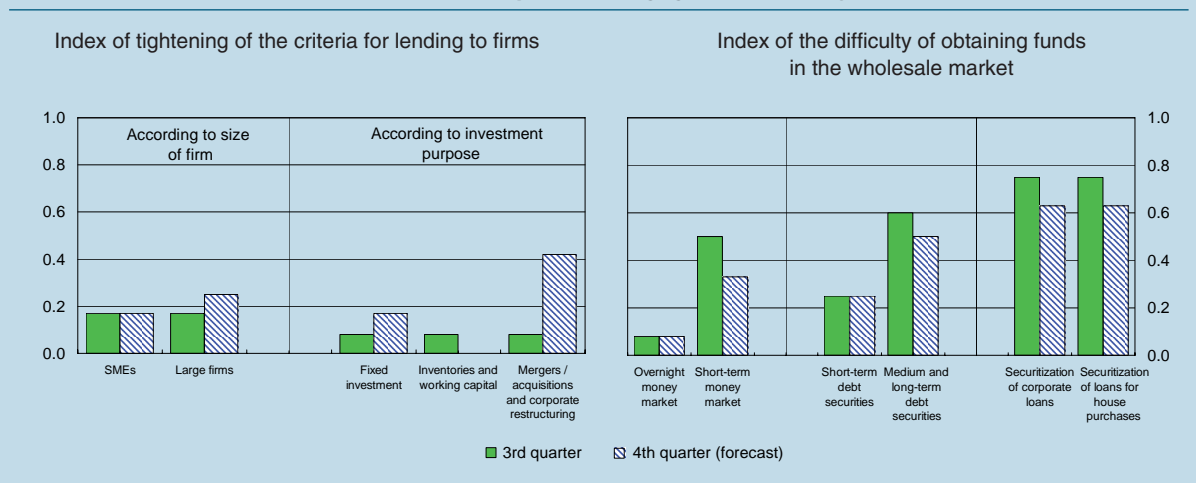


(1) The data on bank lending rates refer to euro transactions and are gathered and processed using the Eurosystem's harmonized method. New contracts concluded during the reference period or contracts renegotiating previous terms and conditions. The annual percentage rate of charge (APRC) includes accessory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

recent turmoil in the financial markets led to a moderate tightening of the criteria for lending to firms (Figure 1), which was reflected in an increase in the interest rates charged for more risky loans; the credit institutions foresee a further moderate tightening in the fourth quarter of 2007. When lending is broken down according to purpose, more pronounced restrictive effects emerge for loans in connection with corporate restructuring, especially looking forward to the last part of the year. However, the banks report that the criteria for lending to families, both for house purchases and for other purposes, have not changed significantly as a result of the sub-prime mortgage crisis, nor should they in the next quarter.

Figure 1

Effects of the sub-prime mortgage crisis in Italy (1)



Source: Bank Lending Survey for the euro area.

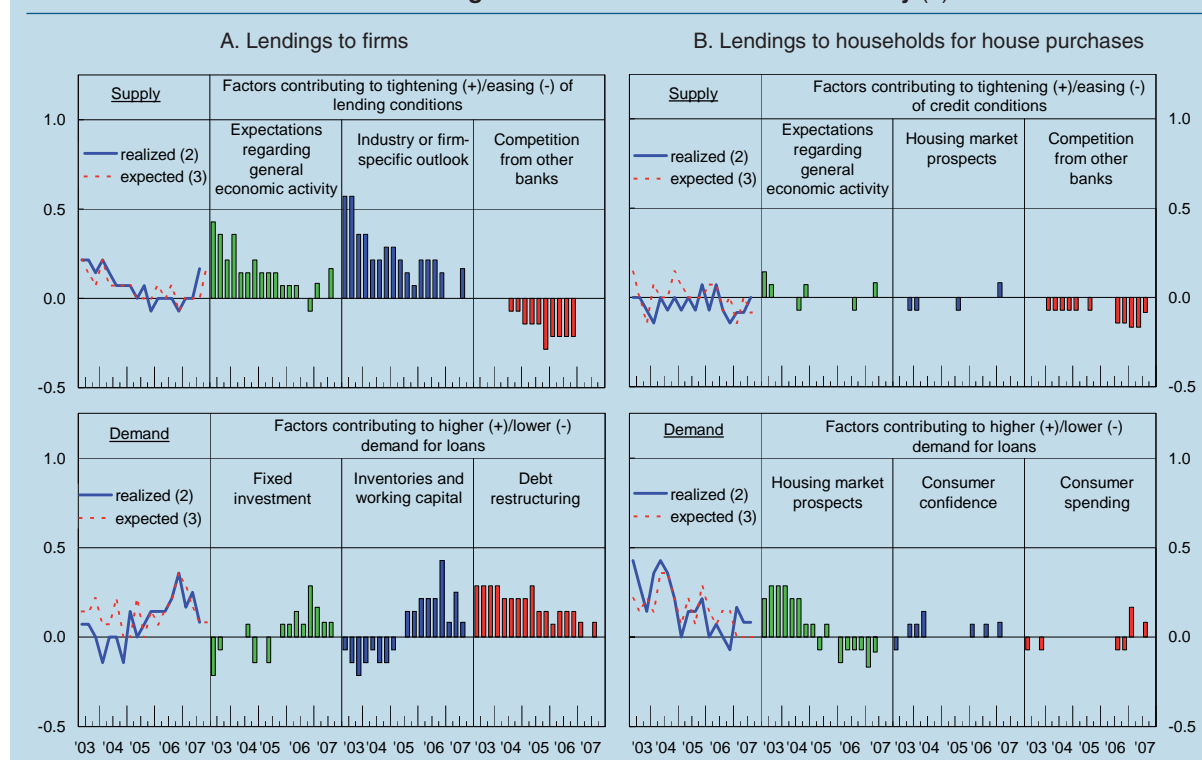
(1) Diffusion indices constructed by aggregating the qualitative replies from the groups participating in the quarterly Bank Lending Survey, weighted as follows: 1 = tightened considerably, 0.5 = tightened somewhat, 0 = remained basically unchanged. The range of variation of the index is from 0 to 1.

The banks report more obvious consequences on the funding side. They indicate that they encountered difficulties in the last three months in obtaining funds both in the money market (for medium-term funds) and in the bond market. The greatest difficulties related to the securitization of both corporate loans and mortgage loans to households. The participating banks expect the funding difficulties to persist into the next quarter, albeit easing slightly, and to affect both interest rate spreads and the volume of lending. At the same time, they consider that the sub-prime crisis will have only a moderate effect on their capital costs and, by this path, on the supply of credit.

The information from the banks in the standard part of the questionnaire confirms the picture of a slight restriction of the supply of credit to firms (Figure 2). It also shows a modest slowdown in loan demand in the third quarter, especially for financing inventories and working capital. Household demand for mortgages continued to increase at a rate similar to that of the last quarter, while consumer credit and other lending was marginally slower, mainly on account of the increase in household saving. The banks forecast that corporate loan demand will continue to grow in the final part of 2007 at a rate similar to that observed in the third quarter. Household demand for mortgages is likely to slow somewhat, while consumer credit will increase more rapidly.

Figure 2

Trends in lending conditions and credit demand in Italy (1)



Source: Bank Lending Survey for the euro area.

(1) Diffusion indices constructed by aggregating the qualitative replies from the groups participating in the quarterly Bank Lending Survey, weighted as follows: for supply, 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) In the quarter in which the survey was conducted. – (3) Forecasts made in the preceding quarter.

Exports of goods fell by 0.7 per cent in the second quarter, cancelling out the first quarter's increase. Exports of services, meanwhile continued their steady decline, falling by 2.4 per cent in both quarters. Since the real effective exchange rate appreciated by only a small amount, Italian exports were presumably curbed by the slowing of economic activity in the country's main outlet markets. The majority of goods sectors were affected by this situation, in particular chemicals and transport equipment.

Imports of goods and services fell by 0.4 per cent in the first half of 2007 with respect to the year-earlier period, led downwards by the 1.6 per cent contraction in the goods component. By contrast, imports of services continued to accelerate rapidly, to growth of 4.7 per cent on the previous period.

The current account deficit is stable

In the first seven months of 2007 the current account deficit (€20.6 billion, or about 2.3 per cent of GDP) remained roughly unchanged at the high level recorded in 2006 (Table 3). The marked improvement in the balance on goods, partly due to the reduction in the deficit on energy, was offset by the increase in the deficit on services and income. The deterioration in the latter item, which is the main component of the deficit on current account, was due to the decrease in income in euros on dollar-denominated assets and the rise in interest payments on the banks' larger Euromarket debtor position. As to the balance of trade, the main sectors

that contributed to the improvement were machinery and mechanical equipment, which recorded a further increase in the value of exports, and refined petroleum products. The deterioration in the balance on services was due mainly to the item “other business services” and to a lesser extent to the foreign travel component, whose surplus contracted slightly in the first six months of 2007 compared with the same period a year earlier.

The financial account recorded net direct and portfolio investment outflows of €10.2 billion in the first seven months of the year, compared with net inflows of €70.6 billion in the corresponding period of 2006. Direct investment net outflows increased from €12.6 billion to €27.8 billion following a major operation in the banking sector; inward direct investment returned to the level recorded before it doubled in 2006. Portfolio investment outflows declined, as did inflows but by a much larger amount. The reduction in outflows was due to the equity component, in contrast with the moderate increase in purchases of foreign non-equity securities. On the side of inflows, there was a sharp contraction in investment in debt securities, along with disposals of equity securities. The figures on investment by non-residents in Italian debt securities continued to reflect the sharp drop in net investment in BTPs and other Italian government securities.

Table 3

Italy's balance of payments (1) (millions of euros)			
	2006	Jan.-July 2006	Jan.-July 2007
Current account	-37,869	-21,678	-22,136
Goods	-9,532	-6,176	2,200
<i>non-energy products (2)</i>	38,847	22,763	27,915
<i>energy products (2)</i>	-48,379	-28,939	-24,824
Services	-1,474	876	-3,791
Income	-13,607	-9,682	-14,105
Current transfers	-13,256	-6,695	-6,440
Capital account	1,891	529	1,441
Financial account	35,526	21,057	20,689
Direct investment	-2,296	11,151	-11,614
Portfolio investment	54,829	59,399	-108
Financial derivatives	-416	439	2,334
Other investment	-17,034	-50,255	32,707
Reserve assets	443	323	-2,630
Errors and omissions	452	92	6

(1) Provisional data for July 2007. – (2) Based on Istat data on foreign trade.

THE LABOUR MARKET

Employment continues to grow ... In the first half of 2007 employment expanded on a seasonally adjusted basis by 0.8 per cent with respect to the second half of 2006 according to the national accounts and by 0.3 per cent according to Istat's labour force survey. The survey found an increase of 0.5 per cent or 105,000 jobs compared with the first half of 2006 (Table 4). With the release of the national accounts data for the second quarter Istat revised the employment figure for the first quarter upwards. Employment increased in industry and private-sector services, held steady in the public sector and declined in agriculture. The share of total payroll employment accounted for by fixed-term employees remained the same as in the first half of 2006, as did the share of total employment consisting in coordinated and continuous collaboration and occasional contracts (2.1 per cent).

In all parts of Italy the employment expansion came mostly in the second quarter. It outpaced the growth in output, owing in part to the annual revision of the number of resident foreigners, which resulted in a corresponding increase in the official count of persons employed.

... reflecting slow wage growth Wage moderation continued. According to the national accounts, gross earnings per employee for the entire economy rose by just over 1 per cent in the first six

months compared with the year-earlier period. The increase was larger in the private sector (2.5 per cent), driven up by that in industry excluding construction (3.2 per cent, owing to the payment of several contract instalments in the engineering and energy sectors). In the other sectors earnings were practically stationary, mainly as a result of the postponed renewal of the collective bargaining agreement covering public sector employees.

The participation rate declines, mainly among young people

The participation rate for the population aged 15-64 came down to 62.5 per cent, half a point lower than a year earlier. The main factor was the fall in the rate for the youngest age-group (15-24) from 32.5 to 31 per cent. Since the first quarter of 2004, when the revised statistical series was introduced, the participation rate of this group has fallen by 5 percentage points. The decline in the overall rate appears to be correlated with the increasing share of young people attending school or training programmes (up from 55 to 60 per cent in the three years).

The unemployment rate falls further despite labour force expansion

The labour force returned to growth in the second quarter after falling continuously for a year, with a seasonally adjusted increase of 0.2 per cent, or 48,000 persons, vis-à-vis the first quarter. The increase came essentially in the Centre and North, while in the South the decline under way since the second quarter of 2006 was halted. The faster expansion of employment than of the labour force caused the unemployment rate to decline by a further 0.2 percentage points in the second quarter to 6 per cent on a seasonally adjusted basis; it fell to 4 per cent in the Centre and North and to 10.8 per cent in the South.

Table 4

Labour force status of the Italian population (percentage)					
	Average 2006	H1 2006	Q2 2006	H1 2007	Q2 2007
Thousands of persons					
Employees	16,915	16,853	17,015	16,996	17,155
open-ended contracts	14,693	14,690	14,801	14,781	14,850
fixed-term contracts	2,222	2,163	2,214	2,216	2,305
Self-employed	6,073	6,114	6,172	6,076	6,143
Total persons in work	22,988	22,967	23,187	23,072	23,298
Labour force	24,662	24,715	24,808	24,556	24,710
men	14,740	14,773	14,846	14,701	14,797
women	9,922	9,942	9,962	9,855	9,914
Population	58,333	58,376	58,496	58,436	58,736
Per cent					
Unemployment rate	6.8	7.1	6.5	6.0	5.7
men	5.4	5.6	5.2	4.9	4.6
women	8.8	9.2	8.5	7.7	7.4
Participation rate (age 15-64)	62.7	62.9	63.0	62.2	62.5
men	74.6	74.8	75.1	53.9	74.5
women	50.8	50.9	51	50.3	50.6
Employment rate (age 15-64)	58.4	58.4	58.9	58.4	58.9
men	70.5	70.5	71.1	51.1	71.1
women	46.3	46.2	46.7	46.4	46.8

Source: Istat, labour force surveys.

PRICE DEVELOPMENTS

Consumer inflation holds steady ...

The rise in prices has continued to be subdued this year, reflecting wage moderation, the appreciation of the euro and weak domestic demand. The twelve-month rise in the consumer price index for the entire resident population averaged 1.6 per cent in the third quarter, the same as in the second. The increase was 1.6 per cent in July and in August (1.7 per cent for the harmonized index) and, according to preliminary estimates, 1.7 per cent in September (1.6 per cent for the harmonized index; Table 5).

A contributing factor in the curbing of consumer inflation was the slowdown in regulated energy and fresh food prices. This was offset by a sudden acceleration in service prices from a twelve-month rise

of 2.5 per cent in the second quarter to 2.8 per cent in July and in August, owing to increments for tourist facilities. The pick-up affected core inflation, which rose from an average annual rate of 1.8 per cent to 2.1 per cent.

producer price inflation slows ...

As in the second quarter, the slowdown in the prices of energy inputs lowered the rate of producer price inflation. The twelve-month rise in the overall producer price index eased to 2.0 per cent in July and 1.9 per cent in August. Net of food and energy products, producer price inflation continued the deceleration under way since the start of the year, led by intermediate goods and, to a lesser extent, consumer goods. In line with trends in the rest of the euro area, producer prices of consumer food products accelerated from an average rate of 3.0 per cent in the second quarter to 3.9 per cent in July and August, owing above all to sharp rises for meat and dairy products.

and inflation expectations remain stable

Since June the expectations of the forecasters polled by Consensus Economics for average consumer price inflation in Italy have remained unchanged at 1.8 per cent for 2007 and 1.9 per cent for 2008.

BANKS

Bank lending continues to grow rapidly

Bank lending continues to expand at a good pace (10.2 per cent in the twelve months ending in August; Table 6). Short-term lending has slowed, especially to financial companies; medium and long-term lending has been driven by the demand for funds for house purchases. The growth in loans granted by “small” and “minor” banks came to outpace that of larger banks again (by nearly 5 percentage points in August). The value of securitized lending, which was very high in the first seven months of the year, contracted sharply in August in conjunction with the sub-prime mortgage crisis in the United States. If the flow of credit disbursed is taken to include the assets that banks securitized (which continue to finance the economy, although they no longer appear on banks’ balance sheets), the expansion in lending in the twelve months ending in August rises to 12.2 per cent.

Some signs of strain on the supply side

The recent turbulence in financial markets has been reflected in a slight tightening of the selection criteria used by banks in their lending to firms (see the box “Credit supply and demand in Italy: the effects of the recent turmoil in the financial markets”). The difficulty intermediaries encountered in raising funds on the interbank market in August led to a sharp rise in money market rates for longer maturities, while bank lending and deposit rates continued to rise gradually, as in earlier periods of rising official rates (Figure 23).

Table 5

Indicators of inflation in Italy				
<i>(twelve-month percentage change, except as indicated)</i>				
	HICP (1)	CPI (2)		PPI (3)
	Overall index	Overall index	Core component	Overall index
		1-month		
2005	2.2	1.9		2.0
2006	2.2	2.1		1.8
2006 – Jan.	2.2	2.2	0.2	1.7
Feb.	2.2	2.1	0.2	1.8
Mar.	2.2	2.1	0.2	1.8
Apr.	2.3	2.2	0.3	1.9
May	2.3	2.2	0.3	1.8
June	2.4	2.3	0.1	1.8
July	2.3	2.2	0.3	1.7
Aug.	2.3	2.2	0.2	1.6
Sept.	2.4	2.1	-0.1	1.8
Oct.	1.9	1.8	-0.1	1.9
Nov.	2.0	1.8	0.1	1.8
Dec.	2.1	1.9	0.1	1.8
2007 – Jan.	1.9	1.7	0.1	1.7
Feb.	2.1	1.8	0.3	1.8
Mar.	2.1	1.7	0.2	1.9
Apr.	1.8	1.5	0.2	1.7
May	1.9	1.5	0.3	1.9
June	1.9	1.7	0.2	1.9
July	1.7	1.6	0.2	2.0
Aug.	1.7	1.6	0.2	2.1
Sept. (4)	1.6	1.7	0.0	1.9

Sources: Based on Istat and Eurostat data.

(1) Harmonized index of consumer prices. – (2) Index of consumer prices for the entire resident population. The core component is defined as the change in the index excluding food and energy and products whose prices are regulated. – (3) Index of producer prices of industrial products sold on the domestic market. – (4) Provisional.

Loan quality remains high

The indicators of loan riskiness have declined slightly and remain at a very low level compared with the past. The loans classified as bad debts in the twelve months ending in June amounted to 0.8 per cent of the total, compared with 0.9 per cent in December; decreases occurred throughout the country. There was also a reduction in the volume of substandard assets, i.e. loans to customers in temporary difficulty.

Fund-raising is slowing, while rates on bonds are rising

Banks' domestic fund-raising slowed to 7.8 per cent in the twelve months ending in August, reflecting the trend of less liquid deposits and repos. By contrast, consumer households' current accounts recorded a slight acceleration, to which the increased uncertainty concerning the financial markets may have contributed. Growth in sales of bonds slowed to 12.4 per cent. The yield on bank bonds rose to 4.4 per cent for fixed-rate bonds and to 4.5 per cent for variable-rate bonds.

Italian banks increase their foreign borrowing

In order to finance the growth in their lending, which has outpaced that in their domestic fund-raising, banks have progressively increased their net external liabilities (from €91 billion at the end of 2006 to €126 billion in August). The increase has been primarily in euros on the interbank market. Over the same period the component denominated in other currencies declined from 58 to 46 per cent.

Banks' profitability rose in the first half-year

In the first half-year banks' profits rose by more than 50 per cent compared with the corresponding period of 2006. This result was due to rapid growth in revenues (7 per cent), the near stability of operating costs, and the very substantial extraordinary profits deriving mainly from the capital gains realized in mergers. The growth in revenues was fueled by net interest income, thanks both to an increase in volumes and to a widening of spreads, while the expansion in fee income was much smaller. The moderate increase in operating costs was primarily in connection with staff costs,

Table 6

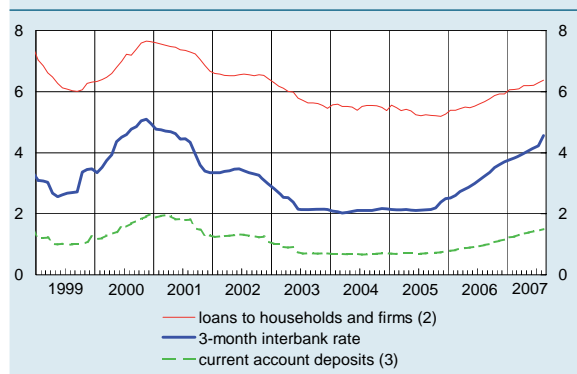
Main assets and liabilities of Italian banks (1)
(end-of-period data; 12-month percentage changes)

	2005	2006	August 2007	
			Stocks (2)	
Assets				
Securities	19.4	5.3	2.3	220,499
Loans	8.7	11.5	10.2	1,452,243
of which: (3)				
short-term (a)	2.0	10.5	9.6	499,385
medium and long-term (b)	13.0	11.6	11.2	894,202
(a)+(b)	8.6	11.2	10.6	1,393,586
External assets	11.0	19.8	26.9	382,630
Liabilities				
Domestic funding (4)	7.8	9.9	7.8	1,411,294
Deposits	6.9	8.3	4.8	825,287
of which: (5)				
current accounts	8.0	6.7	4.9	598,115
with agreed maturity	2.7	9.8	3.9	44,742
redeemable at notice	2.5	-0.8	-3.6	66,459
repos	4.9	29.4	9.7	107,245
Bonds (4)	9.3	12.5	12.4	586,006
External liabilities	11.8	25.6	30.0	508,826

(1) The figures for August 2007 are provisional. The percentage changes are calculated net of reclassifications, exchange rate variations and other variations not due to transactions. – (2) Bad debts, repos and some minor items are not shown in the breakdown. – (3) Includes bonds held by non-residents. – (5) Excludes those of central government.

Figure 23

Short-term bank interest rates (1)
(monthly data; percentages)



Sources: Based on Bank of Italy and Interbank Deposit Market data. (1) The data on bank 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 not more than one year. – (3) Average rate on current account deposits of households and firms.

which were also influenced by the new methods of calculating severance pay introduced by the reform of supplementary retirement provision.

Italian banks' exposure to subprime risk appears small

According to a survey carried out by the Bank of Italy in collaboration with the European supervisory authorities, the exposure of the leading Italian banking groups to the American sub-prime and Alt-A mortgage sectors appears limited. None of the groups surveyed indicated that it had granted such loans to US counterparties. On the basis of the data currently available, the value of the investments that include securities linked to such loans is about €1.3 billion (less than 1.5 per cent of the average core capital of the groups in the sample). The lines of credit granted to "vehicle companies" operating in the sector – which in any case have invested very little in such assets – total €1.6 billion (on average less than 2 per cent of the groups' core capital). Of this amount, only a small portion has been drawn down to date.

If the difficulties should spread to other vehicles not directly involved in investing with sub-prime risk, the potential risks facing Italian and international banks could grow in size. Repercussions on profitability may also be caused by the illiquidity of the market in structured securities, which has adversely affected their value.

THE FINANCIAL MARKET

Shares partially recoup losses due to financial turbulence

The general Italian share index fell by 5 per cent in the third quarter, broadly in line with the Dow Jones

Euro Stoxx index, which lost 3 per cent (Figure 24). Prices began their decline in late July in the wake of the crisis in the structured loan market and started to recover in the first week of September. Telecommunications and raw materials shares recorded moderate rises, while industrial, technology and banking shares declined (the latter less sharply than in the other euro-area countries).

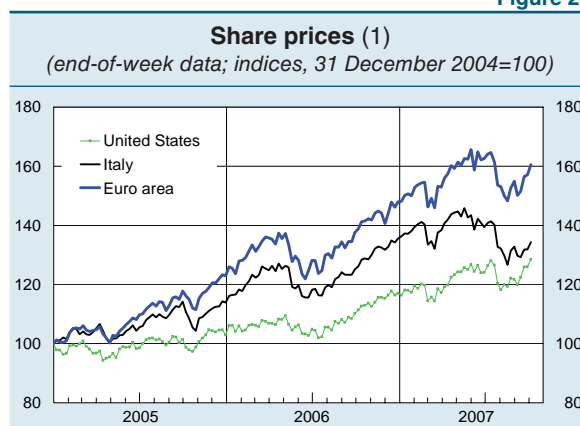
Reflecting the market downswing, the ratio of current earnings to market price rose further to stand slightly above its long-term average (Figure 25). The expected volatility of share prices is in line with the other main international markets; at the start of October it returned to values slightly above those recorded before the summer.

New listings picked up to 25 in the first nine months, compared with 13 in the same period of 2006. The number of Italian companies listed rose to 297 at the end of September, with total market value of €772 billion (equal to 50.5 per cent of GDP). In September trading was launched on the Alternative Capital Market, the exchange for small-cap shares with simplified listing requirements and reserved to professional investors. At the end of September there was one firm listed.

Non-financial corporate bond issues resume

Net bond issues by Italian firms on the Euromarket rose from €24 billion in the first quarter to €33 billion in the second (Table 7). Against a slight reduction in bank issues, there were substantial issues by other financial corporations and by

Figure 24



Source: Bloomberg.
(1) MIB for Italy, Dow Jones Euro Stoxx for the euro area, Standard & Poor's 500 for the United States.

non-financial corporations. The yield differential between euro-denominated Italian corporate issues and government securities widened slightly during the quarter, remaining in line with those for their euro-area counterparts. The only exception was Fiat, yields on whose paper diminished significantly in September as the result of a rating upgrade.

The yield differential between the benchmark ten-year BTP and the corresponding German Bund is now about 25 basis points, slightly more than the average for the first half.

Investment fund net outflows continue

Net redemptions of the investment funds controlled by Italian intermediaries remained substantial in the second quarter (€12 billion). Essentially, this reflected the performance of Italian funds, in particular harmonized funds, which recorded net redemptions of €15 billion, while hedge funds had net fund-raising of €2 billion.

The outflow, which has been underway for some time, has a number of causes (see the *Annual Report for 2006*, Chapter 13). One factor may have been the increasing market penetration of funds controlled by foreign intermediaries, which recorded net fund-raising of €11 billion in the first half of the year (€6 billion in the second quarter).

Initial inquiries by the Bank of Italy have not found any indication that Italian open-end securities funds have invested in securities that have been downgraded or that are exposed to a risk of downgrading as a result of the recent financial crisis.

In the second quarter the average rate of return of harmonized funds set up in Italy was 1.7 per cent. The good performance of stock markets internationally favoured equity funds, which produced an average return of 4.4 per cent; bond funds were penalized by the rise in interest rates and suffered average losses of 0.3 per cent.

Individual portfolio management accounts returned to net fund-raising, with an inflow of €3 billion. Their average yield for the quarter is estimated at 0.3 per cent.

Figure 25

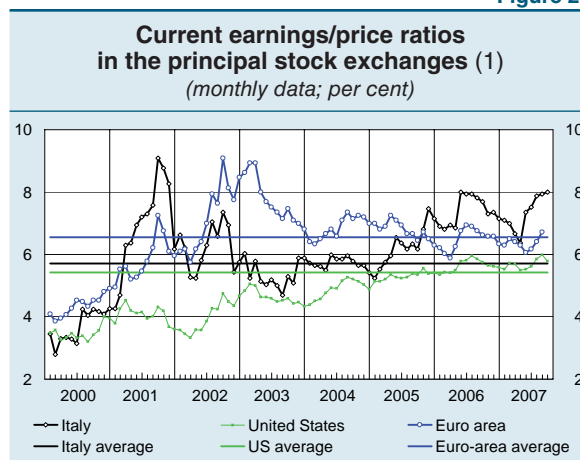


Table 7

Net bond issues by banks and firms in Italy and the euro area (1)

(millions of euros)

	Banks	Other financial corporations	Non-financial corporations	Total
Italy				
2005	41,502	35,471	1,434	78,407
2006	60,371	15,551	4,473	80,395
2006 – Q1	20,039	1,328	516	21,883
Q2	12,310	1,753	3,750	17,813
Q3	7,155	4,314	356	11,825
Q4	20,867	8,156	-149	28,874
2007 – Q1	21,619	3,442	-1,229	23,832
Q2	15,371	10,326	7,606	33,303
Euro area				
2005	292,670	176,227	22,250	491,147
2006	346,456	231,698	33,056	611,207
2006 – Q1	100,624	45,604	1,752	147,980
Q2	87,157	57,277	16,506	160,940
Q3	62,332	33,505	2,620	98,457
Q4	96,340	95,312	12,178	203,830
2007 – Q1	141,879	81,922	981	224,781
Q2	100,456	57,573	21,505	179,534

Sources: Bank of Italy and ECB.

(1) Bonds with a maturity at issue of more than one year, valued at par, issued by resident companies belonging to the sector indicated. The nationality and the 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.

THE PUBLIC FINANCES

The projected deficit for 2007 improves to 2.4% from 2.5% estimated in June

The Forecasting and Planning Report for 2008, submitted by the Government at the end of September together with the budget, estimates that general government net borrowing will amount to 2.4 per cent of GDP this year, compared with 4.4 per cent in 2006 (which, excluding extraordinary expenditure in relation to high-speed railway construction and the European Court of Justice decision on VAT reimbursements, falls to 2.5 per cent).

In 2007 the Government expects to achieve an improvement in structural net borrowing of 0.5 percentage points of GDP with respect to 2006; the structural balance is calculated excluding the extraordinary expenditure referred to above and the effects of temporary measures and the economic cycle. The improvement would be smaller if contributions in respect of severance pay were included among the temporary components.

The ratio of the debt to GDP has begun to decline once more, from 106.8 to 105.0 per cent (Table 8).

Two thirds of the increase in revenues during the year has been used to finance additional spending

As in 2006, the projections for tax revenue have been revised progressively upwards in the course of the year. About two thirds of the extra revenue was earmarked in June and September to finance additional spending (see the box "The measures decided at the end of June and September").

The net borrowing target for 2007 had been set at 2.8 per cent of GDP in September 2006 by the Forecasting and Planning Report for 2007 (Table 9).

In June, the Economic and Financial Planning Document revised the estimate for the deficit on a current programmes basis down to 2.1 per cent of GDP, mainly in consequence of the higher estimate for revenues. At the same time measures were approved entailing additional expenditure equal to 0.4 per cent of GDP; the deficit for 2007 was accordingly projected at 2.5 per cent.

Table 8

General government balances (1) (millions of euros and percentages of GDP)					
	2003	2004	2005	2006	2007
Net borrowing	46,614	48,066	59,523	65,504	36,361
% of GDP	3.5	3.5	4.2	4.4	2.4
Primary surplus	21,736	17,628	4,690	2,048	38,173
% of GDP	1.6	1.3	0.3	0.1	2.5
Interest payments	68,350	65,694	64,213	67,552	74,534
% of GDP	5.1	4.7	4.5	4.6	4.8
Debt	1,392,388	1,443,395	1,511,198	1,575,441	
% of GDP	104.3	103.8	106.2	106.8	105.0

Sources: Based on Istat for the accounts of general government for 2003-06; for 2007, estimates of the Forecasting and Planning Report for 2008.

(1) Rounding may cause discrepancies in totals.

Table 9

Public finance objectives and estimates for 2007
(billions of euros and percentages of GDP)

	General government			Memo. item
	Net borrowing	Primary surplus	Debt	GDP growth rate
Objectives				
July 2006 (1)	....	....	....	1.2
% of GDP	2.8	2.1	107.5	
September 2006 (2)	42.1	30.7	....	1.3
% of GDP	2.8	2.0	106.9	
December 2006 (3)	....	....	....	1.3
% of GDP	2.8	2.2	106.9	
Estimates				
March 2007 (4)	34.6	39.4	....	2.0
% of GDP	2.3	2.6	105.4	
June 2007 (1) (5)	38.3	35.5	....	2.0
% of GDP	2.5	2.3	105.1	
September 2007 (6) (7)	36.4	38.2	....	1.9
% of GDP	2.4	2.5	105.0	

(1) Economic and Financial Planning Document. – (2) Forecasting and Planning Report. – (3) Stability Programme. – (4) Combined Report on the Economy and Public Finances. – (5) Including the effects of Decree Law 81/2007. – (6) Update to Economic and Financial Planning Document for 2008-11. – (7) Including the effects of Decree Law 159/2007.

THE MEASURES DECIDED AT THE END OF JUNE AND SEPTEMBER

Decree Law 81 of 2 July 2007, the simultaneous mid-year budget revision and Decree Law 159 of 1 October 2007 provide for increased expenditure of €11.8 billion (net of savings of €0.5 billion) and assistance for more needy households (€1.9 billion, treated in the official estimates as a reduction in revenue) in 2007. More than half of the increased expenditure is on the current account. The July decree has effects in 2008 and 2009 as well, the additional costs being estimated at €1.6 billion in each of those years. The October decree, by contrast, has only negligible effects in the two years.

Decree Law 81. – The decree gives rise to increases in expenditure of €5.6 billion in 2007 (further costs amounting to €0.8 billion stem from the simultaneous mid-year budget revision). A large part of the increased expenditure (around €4.2 billion) is due to an adjustment of resources to the needs of existing policies. The topping-up of the budget allocations of central departments or the easing of limits on the growth in their expenditure account for €2.5 billion. A further €0.9 billion is due to: an enhancement of the indexation of old-age pensions to prices in the three years from 2008 to 2010; the award of an additional payment to pensioners aged 64 or over on modest incomes; an increase in pensions for persons in need. Resources are also provided for international peace missions and humanitarian aid (€0.3 billion), current transfers to public enterprises (€0.3 billion), investment to modernize the traditional road and rail networks (€0.5 billion and €0.7 billion). Other increases in expenditure are due to allocations for short-term supply teachers in schools (€0.2 billion) and changes to the domestic Stability Pact (€0.3 billion).

The increased outlays estimated for 2008 and 2009 are due almost entirely to the creation of a fund aimed primarily at supplementing modest pensions.

A number of provisions introduced in 2006 were revised during ratification in Parliament. The deterioration in the net budgetary position due to part of the amendments (easing of the constraints imposed by the domestic Stability Pact; extension of the reduction in the Regional Tax on Productive Activities on labour costs to banks, financial companies and insurance companies; relaxation of the rules on sector studies) was offset by changes to the deductibility of the cost of company motor vehicles and reductions in current and capital expenditure.

Decree Law 159. – On the basis of the assessments contained in the accompanying Technical Report, the decree gives rise to higher expenditure in 2007 on the current account (€2.1 billion, net of the indirect effects on revenue) and on the capital account (€3.8 billion). Around half of the increased disbursements consist of the bringing forward of expenditure deriving from previous commitments or established practice. In addition, it provides for savings worth €0.5 billion and a one-off payment of €150 to personal taxpayers whose net liability for 2006 was zero and a further €150 for each dependent family member (€1.9 billion). In the official estimates the cost of the latter measure is treated as a reduction in revenue.

Additional resources are provided to cover the renewal of public sector labour agreements in the two years 2006-07: net of the indirect effects on revenue (€0.5 billion), the impact of this measure on the deficit is around €0.5 billion. Furthermore, the decree brings forward to 2007 a number of transfers to the Railways (€1 billion) and to the National Road Agency ANAS (€0.2 billion), and aid for cooperation and development (€0.9 billion).

It also provides for the launch of a programme of public residential construction (€0.6 billion), aimed partly at the renovation of existing accommodation. A further sum of €1.5 billion is set aside for other capital spending, mainly for the underground railway systems in Rome, Naples and Milan (€0.8 billion) and measures relating to the MOSE project to safeguard Venice from rising sea levels (€0.2 billion).

The Forecasting and Planning Report for 2008 further improved the public finance estimates, chiefly by revising the revenue estimate upwards. A decree law approved together with the Report earmarks part of the improvement to finance measures that will raise the deficit in 2007 by 0.5 per cent of GDP.

With respect to the forecasts made in the autumn of 2006, revenue has been revised upwards by a total of €16.4 billion (1.1 per cent of GDP). Excluding the measure decided in September affecting revenues (in favour of persons with incomes too low to benefit from tax relief), the increase amounts to over €18 billion. More than half of the revision (€9.3 billion) was made in March 2007 on the basis of the definitive 2006 outturn for receipts. The subsequent revisions have mainly involved direct taxes (€6.4 billion), in connection with the unexpected sharp increase in receipts of self-assessed taxes in the summer (see the box “State budget tax revenue”).

STATE BUDGET TAX REVENUE

In the first nine months of the year State budget tax revenue increased by 6.4 per cent (€16.5 billion) with respect to the corresponding period of 2006. The dropping out of receipts from the one-off withholding taxes that were not extended to 2007 was more than offset by the growth in those from other taxes. In particular, corporate income tax receipts rose substantially (35 per cent, or €7.1

State budget tax revenue on a cash basis (1) (amounts in millions of euros; per cent)

	January-September			Contribution to growth in 2007
	2006	2007	% change on 2006	
Direct taxes	138,953	148,590	6.9	3.7
Personal income tax	100,584	106,517	5.9	2.3
<i>of which: withholdings from employee incomes</i>	80,060	82,793	3.4	
<i>balances</i>	4,385	5,852	33.5	
<i>payments on account</i>	6,281	7,092	12.9	
Corporate income tax	20,340	27,469	35.0	2.8
<i>of which: balances</i>	7,902	11,625	47.1	
<i>payments on account</i>	12,216	15,546	27.3	
Taxes on interest income and capital gains	9,657	10,698	10.8	0.4
<i>interest on bank deposits</i>	1,749	3,102	77.4	
<i>interest on bonds</i>	4,855	4,875	0.4	
<i>dividends</i>	551	394	-28.5	
<i>capital gains</i>	879	986	12.2	
<i>managed assets</i>	1,623	1,340	-17.4	
One-off taxes	5,602	1,112	-80.1	-1.7
Taxes on insurance companies' mathematical reserves	1,045	1,105	5.7	0.0
Other	1,725	1,689	-2.1	0.0
Indirect taxes	118,134	125,025	5.8	2.7
VAT	76,652	81,094	5.8	1.7
Other business taxes	9,517	11,505	20.9	0.8
Excise duties on mineral oils	15,023	14,865	-1.1	-0.1
Other excise duties and sales taxes	5,311	5,141	-3.2	-0.1
Monopolies	7,098	7,363	3.7	0.1
Lotteries	4,533	5,057	11.6	0.2
TOTAL TAX REVENUE	257,087	273,615	6.4	6.4

Source: Based on State budget.
(1) For 2007, provisional data.

billion); the sharp growth, greater than expected, involved both payments on account and those of balances. The revenue gain reflects the recovery of economic activity in 2006, the policy of combating evasion and avoidance, and the measures adopted to broaden the tax base in order to compensate for the effects of the 2006 European Court of Justice decision on VAT. The very substantial rise in payments on account is also tied to payments of substantial amounts by some large companies.

As regards other direct taxes, personal income tax receipts grew by 5.9 per cent (€5.9 billion). The smallness of the increase in payroll withholdings (3.4 per cent or €2.7 billion) was partly a reflection of the large amounts collected at the beginning of 2006 in respect of back pay following the renewal of labour contracts. After years of slow growth, self-assessed personal income tax, paid mainly by self-employed individuals and small firms, rose by 21.4 per cent (€2.3 billion). Some measures relating to sector studies influenced this result.

Receipts from withholding taxes in settlement of income from financial assets grew by a total of 10.8 per cent (€1 billion). The reallocation of investors' portfolios led to a reduction in receipts from the tax on managed assets and a simultaneous increase of 20.8 per cent (€1.4 billion) in those from taxes on interest income, which also benefited from the rise in interest rates.

Turning to indirect taxes, VAT receipts grew by 5.8 per cent (€4.4 billion), outpacing the rise in consumption. This reflects a shift in the composition of demand towards goods taxed at higher rates – while consumption of food products declined, there was a significant increase in purchases of durable goods – and the steps taken to bring areas of evasion and avoidance into the net. Receipts from other business taxes grew by 20.9 per cent (€2 billion); an important factor was the growth of 33.4 per cent (€0.8 billion) in those from the registration tax, which reflected the measures introduced with Decree Law 223 of July 2006 to expand and recoup the tax base.

According to official estimates, taken together the June and September measures increased the deficit for 2007 by 0.9 per cent of GDP.

Revenues rise by 0.6 points in proportion to GDP, primary current expenditure falls by 0.1 point

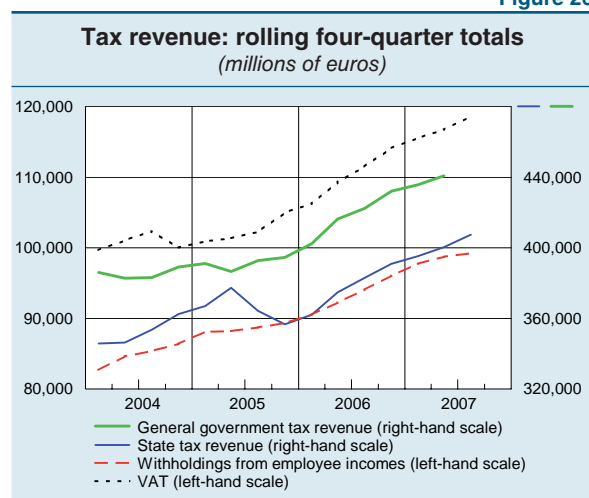
The Forecasting and Planning Report estimates an increase of 5.9 per cent in total general government revenues in 2007; the ratio to GDP will rise by 0.6 percentage points, to 46.7 per cent. In part the increase reflects the transfer to INPS of the portions of severance pay accruing to workers in firms with staff of at least 50 that the employees have not assigned to private pension funds. The

GDP ratio of primary current expenditure falls by 0.1 percentage points, to 39.8 per cent. In real terms, deflated by the consumer price index, expenditure rises by about 2.5 per cent, comparable to the average over the last decade of about 2.3 per cent.

Excluding the extraordinary items recorded in 2006 to take account of the European Court of Justice decision on VAT and the cancellation of the high-speed train company's debt to the State, capital expenditure will increase by 0.3 percentage points in relation to GDP, reflecting the measures passed during the year to increase and bring forward expenditure.

The data now available on the public accounts basically corroborate the estimates of the Forecasting and Planning Report.

Figure 26



Sources: Istat for general government tax revenue; General Government Report and state budget for the other variables.

In the first nine months of the year State budget tax revenues grew by 6.4 per cent (Figure 26).

The borrowing requirement declines sharply

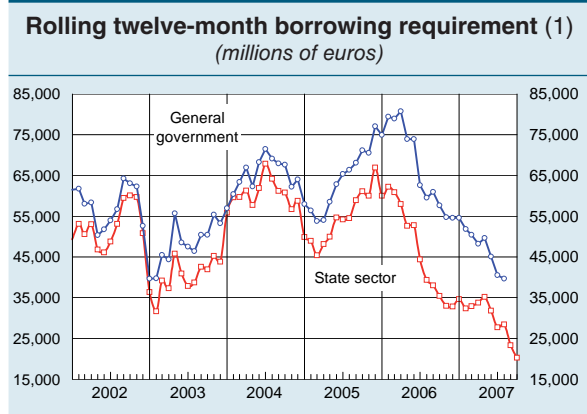
Through July the general government borrowing requirement, net of privatization receipts, was €25.8 billion, nearly €15 billion less than a year earlier. Its ratio to GDP in 2007 is the lowest of the last ten years (Figure 27 and Table 10).

According to the estimates released by Istat, in the first half of the year net borrowing amounted to 1.9 per cent of GDP, compared with 2.7 per cent a year earlier. The primary balance was in surplus by 2.9 per cent of GDP, against 1.8 per cent in the first half of 2006 (Table 11). Tax receipts increased by 4.2 per cent, led by the revenue from company income tax, the substitute tax on income from financial assets, and social security contributions. The slow growth in primary spending (1.2 per cent) reflected the contraction in employee compensation and capital expenditure. The performance of both these components is expected to be positive over the year as a whole. Compensation of employees will reflect the payment of the increases in contractual pay agreed to date, which involve about a third of all public employees. Capital expenditure will be influenced by the measures adopted in the second half of the year, which will push outlays up by more than €5 billion.

In the first seven months of the year the general government debt increased by €44.9 billion. This breaks down into an increase of €22.3 billion in the total borrowing requirement (held down by the reduction in the share capital of the Export Credit Insurance Agency, SACI S.p.A., which brought receipts of €3.5 billion to the Treasury); a seasonal increase of €18.7 billion in the assets that the Treasury holds with the Bank of Italy; and the issue of securities below par for €4.1 billion. In August and September the Treasury assets were run down by around €9 billion, diminishing the increase in the debt by an equivalent amount. A further decrease is expected in the fourth quarter; at the end of September the assets amounted to over €32 billion (the minimum balance set by law is €10 billion).

By sub-sector, central government debt increased by €41.9 billion and that of local authorities by €3 billion.

Figure 27



Source: Ministry of the Economy and Finance for the state sector borrowing requirement.

(1) Net of privatization receipts.

Table 10

General government borrowing requirement and debt (millions of euros)				
	2004	2005	2006	2007
<i>General government borrowing requirement net of privatization receipts</i>				
Jan.-July	47,686	56,063	40,699	25,825
Year	57,991	74,912	54,579	-
% of GDP	4.2	5.3	3.7	-
<i>Privatization receipts</i>				
Jan.-July	15	4,025	38	3,500
Year	8,316	4,618	38	-
<i>Memorandum item: settlements of past debts</i>				
Jan.-July	225	363	89	299
Year	529	1,864	243	-
<i>Total general government borrowing requirement</i>				
Jan.-July	47,671	52,038	40,661	22,325
Year	49,675	70,294	54,541	-
% of GDP	3.6	4.9	3.7	-
<i>Change in Treasury asset balances with the Bank of Italy</i>				
Jan.-July	34,446	41,765	38,251	18,651
Year	2,578	-1,197	8,230	-
<i>Issue discounts</i>				
Jan.-July	197	-1,818	1,845	4,116
Year	-227	-2,444	2,274	-
<i>Change in euro equivalent of foreign currency liabilities</i>				
Jan.-July	496	1,147	-577	-161
Year	-1,021	1,150	-801	-
<i>Change in debt</i>				
Jan.-July	82,810	93,132	80,179	44,932
Year	51,006	67,803	64,243	-
% of GDP	3.7	4.8	4.4	-
<i>General government debt</i>				
End July	1,475,199	1,536,527	1,591,377	1,620,373
End year	1,443,395	1,511,198	1,575,441	-
% of GDP	103.8	106.2	106.8	105.0 (1)

(1) Estimate contained in the Forecasting and Planning Report for 2008.

The objective for 2008 announced at the end of 2007 is confirmed

In September the Forecasting and Planning Report estimated net borrowing on a current programmes basis for 2008 at 1.8 per cent of GDP, compared with 2.2 per cent projected in June and 2.9 per cent in last year's Report. The budget presented by the Government raises the deficit by €6.5 billion (0.4 per cent of GDP) and confirms the 2.2 per cent target for net borrowing set in last year's Report (see the box "The budget for 2008"). According to the official estimates, structural net borrowing will improve by 0.2 percentage points of GDP compared with 2007.

In the scenario outlined in the Report for 2008 the fiscal burden remains unchanged at the level forecast for 2007 (43 per cent of GDP). Primary current spending rises by 0.2 percentage points to 40 per cent, the peak registered in 2005, while capital expenditure declines by almost 0.4 points to around the same proportion recorded in 2006.

The objectives for net borrowing in 2009-11 set out in the Planning Document last June are largely confirmed (Table 12). Budget balance should be achieved in 2011, when the primary surplus is projected to reach 4.9 per cent of GDP. In order to achieve these objective it will be necessary to adopt corrective measures of the order of 0.4 per cent of GDP in each of the three years. This calculation is based on current-programmes projections that do not take account of the effects of expenditure appropriations which, although recurrent, nevertheless require formal legislative enactment (such as outlays in connection with the renewal of the national labour contracts for public employees).

The budget for 2008 is examined in the Governor's testimony to Parliament on 10 October 2007. (http://www.bancaditalia.it/interventi/integov/2007/10102007/en_draghi_10_10_07.pdf).

Table 11

General government expenditure and revenue (millions of euros)				
	H1		Percentage change on first half of previous year	
	2006	2007	2006	2007
EXPENDITURE				
Compensation of employees	76,443	74,375	9.8	-2.7
Intermediate consumption	37,338	38,546	-0.9	3.2
Social benefits in cash	118,295	123,673	4.6	4.5
Other current expenditure	40,734	40,946	0.0	0.5
Current expenditure, net of interest payments	272,810	277,540	4.5	1.7
% of GDP	37.3	36.3		
Interest payments	32,953	36,787	-1.0	11.6
Current expenditure	305,763	314,327	3.8	2.8
% of GDP	41.9	41.1		
Gross fixed investment	15,669	15,465	2.3	-1.3
Other capital expenditure	9,851	9,014	-7.2	-8.5
Capital expenditure	25,520	24,479	-1.6	-4.1
Total expenditure, net of interest payments	298,330	302,019	3.9	1.2
% of GDP	40.8	39.5		
TOTAL EXPENDITURE	331,283	338,806	3.4	2.3
% of GDP	45.4	44.3		
REVENUE				
Direct taxes	93,674	98,447	16.6	5.1
Indirect taxes	107,540	111,473	8.7	3.7
Social security contributions	86,119	90,519	4.8	5.1
Other current revenue	21,869	21,909	3.3	0.2
Current revenue	309,202	322,348	9.4	4.3
% of GDP	42.3	42.2		
Capital taxes	118	144	-42.7	22.0
Other capital revenue	1,936	1,903	10.0	-1.7
Capital revenue	2,054	2,047	4.5	-0.3
% of GDP	0.3	0.3		
TOTAL REVENUE	311,256	324,395	9.4	4.2
% of GDP	42.6	42.4		
NET BORROWING	-20,027	-14,411	-44.2	-28.0
% of GDP	-2.7	-1.9		
Primary surplus	12,926	22,376	601.0	73.1
% of GDP	1.8	2.9		
<i>Memorandum item:</i>				
GDP	730,440	764,190	3.6	4.6

Source: Istat, general government expenditure and revenue.

Table 12

Fiscal objectives included in the Economic and Financial Planning Document (June 2007) and update (September) (percentage of GDP)												
	2006		2007		2008		2009		2010		2011	
	outturn	June	Sept.	June	Sept.	June	Sept.	June	Sept.	June	Sept.	
Net borrowing	4.4	2.5	2.4	2.2	2.2	1.5	1.5	0.7	0.7	-0.1	0.0	
Primary surplus	0.1	2.3	2.5	2.7	2.6	3.4	3.4	4.2	4.2	4.9	4.9	
Interest payments	4.6	4.8	4.8	4.9	4.9	4.9	4.9	4.9	4.9	4.8	4.8	
Debt	106.8	105.1	105.0	103.2	103.5	101.2	101.5	98.3	98.5	95.0	95.1	

THE BUDGET FOR 2008

The budget increases net borrowing in 2008 by €6.5 billion (0.4 percentage points of GDP). It raises resources amounting to about €5.4 billion and provides for expenditure increases and tax reliefs amounting to €12 billion.

Decrease in revenue. – Tax relief of €2.8 billion is granted to households, mainly in relation to first homes (€2.5 billion). In particular, for taxpayers with an annual income up to €50,000 there is a reduction in the municipal tax on first homes of up to €200, or 1.33 per mille of the tax base. The decrease in municipalities' revenue as a result of this measure (€0.8 billion) will be made good by additional central government transfers. Tenants with a registered lease for their first home are allowed a personal income tax credit of €300 if their income does not exceed €15,493.71 and of €150 if it is between that figure and €30,987.41. There is an alternative tax credit for young people aged 20 to 30 for the first three years of a registered lease for their first home. The amount is €991.60 for incomes up to €15,493.71 and €495.80 for incomes between that amount and €30,987.41. Persons with low incomes who are unable to exploit all the personal income tax reliefs will receive an amount equal to the portion of the reliefs they are unable to benefit from; the procedures have yet to be determined.

Taxpayers with only income from real estate up to €500 are exempt from income tax and the imputed income from first home ownership will no longer count in calculating tax credits for dependents and labour income (€0.4 billion).

Some other tax reliefs for households are extended (for housing renovation expenses and for upgrading the energy-efficiency of buildings) and new Irpef tax credits are introduced (for teacher training expenses and transit passes for local public transport).

Taxes on companies are reorganized on a large scale, with essentially no net impact on the public finances. The reductions in tax rates – from 33 to 27.5 per cent for corporate income tax (Ires) and from 4.25 to 3.9 per cent for the

Estimated effects of the budget on the general government consolidated accounts (1)

(millions of euros)

REVENUE	
Increase in revenue	710
Limitation of group setoffs of VAT	450
Other measures	260
Decrease in revenue	3,310
Tax relief for households	2,830
<i>Irpef – deduction for first home rent</i>	1,300
<i>ICI – deduction for first home</i>	820
<i>Irpef – deduction for first home</i>	380
<i>Other</i>	330
Tax relief for companies (2)	480
<i>of which: tax regime for small and marginal taxpayers</i>	210
NET DECREASE IN REVENUE	2,600
EXPENDITURE	
Decrease in expenditure	4,730
Current expenditure	1,760
<i>Intermediate consumption</i>	820
<i>Reorganization of government and improved quality of expenditure (3)</i>	440
<i>Cap on tax credit offsets</i>	320
<i>Public employment</i>	90
<i>Ministry transfer payments</i>	90
Capital expenditure	2,970
<i>Lapsing of expenditure carryovers</i>	1,640
<i>Building maintenance</i>	450
<i>Investments of social security institutions</i>	400
<i>Territorial protection</i>	260
<i>Investment subsidies</i>	100
<i>Other</i>	120
Increase in expenditure	8,650
Current expenditure	5,900
<i>Public employment</i>	2,200
<i>Social security (4)</i>	1,280
<i>Intermediate consumption and expenditure of ministries (5)</i>	1,000
<i>Armed forces</i>	310
<i>Stability pact</i>	280
<i>Social and development policies</i>	180
<i>Other</i>	650
Capital expenditure	2,450
<i>Expenditure of ministries and refinancing of measures to support the economy (6)</i>	1,170
<i>Territorial protection</i>	360
<i>Local transport</i>	350
<i>Infrastructure</i>	110
<i>Other</i>	460
Other net effects (7)	300
NET INCREASE IN EXPENDITURE	3,920
TOTAL INCREASE IN NET BORROWING	6,520

(1) Based on official estimates contained in the technical reports and annexes to the finance bill for 2008 (Parliamentary Act No. 1817). – (2) Excluding the initial effects of the changes to corporate income tax (Ires) and the regional tax on productive activities (Irap). – (3) Includes the reassignment of €300 million of revenue under Article 79(1) of the finance bill. – (4) Concerns the appropriations to finance last July's Social Security, Labour and Competitiveness Agreement. – (5) Of which €900 million deriving from changes to Table A. – (6) Changes to Tables B and D. – (7) Effects of the changes introduced with Tables C, E and F.

regional tax on productive activities (IRAP) – will be offset by the broadening of the tax bases, the limits placed on the use of reliefs granted via tax credits, and the reintroduction of a substitute tax on transactions involved in corporate reorganizations.

The Ires tax base is broadened mainly by setting new limits to the deductibility of interest expenses (with the simultaneous repeal of the provisions on thin capitalization and the pro rata capital tax) and abolishing accelerated depreciation. The tax treatment of consolidated reporting is also revised. Lastly, the tax base is reduced by raising the portion of capital gains enjoying the participation exemption to 95 per cent.

The tax base for IRAP can now be drawn directly from the company's income statement without the adjustments required for business income, independently of the rules followed in drawing up the account (Italian Civil Code or international accounting standards).

Provision is made for sole proprietorships and partnerships to be able to opt, in place of personal income tax, for separate taxation of retained earnings, at the same rate as corporate income tax. For self-employed workers and small enterprises that satisfy certain requirements (in particular revenues of less than €30,000) a substitute tax regime is introduced with a tax rate of 20 per cent, exemption from VAT and IRAP, and documentation and accounting simplifications.

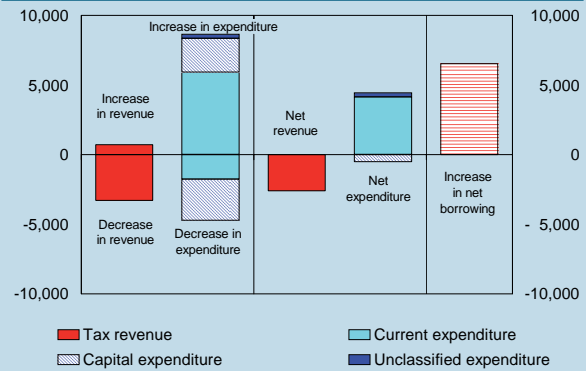
Increase in revenue. – The budget provides for an increase in revenue amounting to €0.7 billion, deriving mainly from restrictions on offsetting VAT credits in the case of companies that have been involved in group liquidation procedures.

Increase in expenditure. – Additional expenditure is set to amount to €8.7 billion, of which €5.9 billion of current revenue. Resources amounting to €2.2 billion are allocated for public employment, to be used almost entirely for the renewal of the 2006-07 national contract. A Fund is to be created to finance the Social Security, Labour and Competitiveness Agreement signed by the Government and the two sides of industry in July (€1.3 billion). The measures regarding the domestic stability pact, which are intended to correct problems that emerged in the application of the new rules, are expected to give rise to costs amounting to €0.3 billion. Greater resources are allocated for social policies and development (€0.2 billion); they will be used to finance numerous measures aimed primarily at countering social exclusion. Other increases in current expenditure regard the ministries (€1 billion) and the armed forces (€0.3 billion).

The increase in capital expenditure comes mainly from measures concerning territorial protection (€0.4 billion) and local public transport (€0.4 billion).

Decrease in expenditure. – Current expenditure is expected to produce savings amounting to €1.8 billion and capital expenditure about €3 billion. The reduction in central government intermediate consumption derives from the rationalization of purchases of goods and services (€0.5 billion) and the introduction of limits on spending for the ordinary maintenance of public buildings and on rentals (€0.3 billion). Measures to improve public spending and reorganize general government are

The budget for 2008: composition and effects on net borrowing
(millions of euros)



expected to yield savings of €0.4 billion. The provisions setting limits on the utilization of some types of tax credit will reduce outlays by €0.3 billion.

Reductions of €2.1 billion in capital expenditure are to come from the shortening from 7 to 3 years of the time limit before extinction of expenditure arrears and from ceilings on extraordinary maintenance expenditure for public buildings, while the requirement that social security institutions' real estate investments consist exclusively of units of real estate investment funds or shareholdings in real estate firms should save €0.4 billion.

STATISTICAL APPENDIX

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	Contribution	Change	Contribution	Change	Contribution	Change	Contribution	Change	Change	Contribution	Contribution	
2003	2.5	2.8	1.9	2.5	0.5	3.4	0.5	2.8	2.9	1.3	4.1	-0.4	..	
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	3.1	3.2	2.2	0.7	0.1	6.9	1.1	3.1	3.3	6.9	5.9	-0.2	-0.2	
2006	2.9	3.1	2.2	1.8	0.4	2.4	0.4	2.8	3.0	8.4	5.9	-0.1	0.1	
2005 – Q1	3.1	2.4	1.7	1.3	0.3	4.0	0.7	2.6	2.8	6.0	2.1	0.3	0.2	
Q2	2.8	3.5	2.4	1.2	0.2	7.9	1.3	1.9	2.0	9.5	0.8	0.8	-1.9	
Q3	4.5	4.1	2.8	3.2	0.6	8.0	1.3	4.3	4.6	2.1	2.1	-0.1	-0.1	
Q4	1.2	1.2	0.8	-1.9	-0.4	2.3	0.4	2.5	2.6	10.6	16.2	-1.4	1.7	
2006 – Q1	4.8	4.4	3.0	4.9	0.9	7.9	1.3	4.5	4.7	11.5	6.9	0.1	-0.5	
Q2	2.4	2.4	1.6	1.0	0.2	-1.9	-0.3	1.9	1.9	5.7	0.9	0.5	0.5	
Q3	1.1	2.8	1.9	0.8	0.1	-4.7	-0.8	1.3	1.4	5.7	5.4	-0.3	0.1	
Q4	2.1	3.9	2.7	3.5	0.7	-7.1	-1.2	0.8	0.9	14.3	1.6	1.3	-1.3	
2007 – Q1	0.6	3.7	2.6	-0.5	-0.1	-4.4	-0.7	1.1	1.1	1.1	3.9	-0.5	-0.7	
Q2	3.8	1.4	1.0	4.1	0.8	3.2	0.5	2.4	2.5	7.5	-2.7	1.3	0.2	

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	Contribution	Change	Contribution	Change	Contribution	Change	Contribution	Change	Change	Contribution	Contribution	
2003	1.4	0.4	0.2	2.3	0.4	-0.5	-0.1	0.8	0.7	9.2	3.9	0.6	0.2	
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	1.6	0.9	1.7	0.3	2.4	0.5	1.7	1.6	7.0	5.8	0.3	-0.1	
2006	2.2	0.9	0.5	0.4	0.1	3.4	0.8	1.4	1.3	9.6	4.5	0.8	0.1	
2005 – Q1	3.0	3.1	1.7	5.7	1.0	4.1	0.9	3.2	3.0	-1.1	-1.1	..	-0.6	
Q2	4.1	3.6	2.0	-2.6	-0.5	3.8	0.9	2.9	2.8	14.3	5.0	1.3	0.4	
Q3	2.6	2.7	1.5	4.3	0.7	5.2	1.2	2.7	2.6	12.2	14.5	0.1	-0.8	
Q4	1.5	1.3	0.7	-4.4	-0.8	-3.0	-0.7	-0.8	-0.8	16.0	-0.9	2.2	..	
2006 – Q1	2.4	-0.2	-0.1	-0.2	..	7.7	1.7	2.0	1.9	9.7	7.9	0.5	0.4	
Q2	2.4	1.8	1.0	3.3	0.6	5.2	1.2	2.7	2.6	3.1	5.2	-0.1	-0.1	
Q3	-0.5	-3.7	-2.1	2.2	0.4	-3.8	-0.9	-2.1	-2.0	9.1	-1.5	1.5	0.6	
Q4	5.6	4.3	2.3	0.3	..	12.3	2.7	5.1	4.7	3.5	-0.3	0.6	-0.3	
2007 – Q1	3.0	3.4	1.8	-0.8	-0.1	-1.9	-0.4	1.3	1.2	14.2	3.6	1.6	..	
Q2	-1.2	1.0	0.6	1.4	0.2	-7.0	-1.7	-1.4	-1.3	3.1	2.4	0.2	-0.5	

Source: National statistics.

(1) Chain-linked volumes. – (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' expenditure	General government expenditure (2)	Exports
				Construction	Machinery, equipment, sundry products & vehicles	Total			
Chain-linked volumes									
2001	1.9	1.8	1.9	0.4	0.7	0.5	2.0	2.0	3.7
2002	0.9	0.3	0.7	-1.0	-2.0	-1.5	0.8	2.4	1.7
2003	0.8	3.1	1.4	1.2	1.0	1.2	1.2	1.8	1.1
2004	2.0	6.7	3.3	1.2	3.1	2.3	1.6	1.3	6.9
2005	1.5	5.2	2.5	1.6	3.9	2.6	1.5	1.4	4.4
2006	2.8	7.7	4.2	4.1	5.2	5.1	1.8	2.0	7.9
2005 – Q2	0.6	2.9	1.2	1.9	1.4	1.6	0.4	0.7	2.2
Q3	0.6	1.9	1.0	0.9	1.8	1.3	0.6	0.3	2.2
Q4	0.4	1.9	0.8	0.6	1.1	0.9	0.1	0.1	0.9
2006 – Q1	0.9	2.1	1.2	-0.1	1.4	0.7	0.7	1.1	3.0
Q2	1.0	1.3	1.1	2.6	2.9	2.7	0.4	0.2	1.6
Q3	0.6	1.9	1.0	1.2	0.5	0.8	0.5	0.6	1.1
Q4	0.8	1.7	1.1	1.6	1.9	1.7	0.4	0.4	3.1
2007 – Q1	0.8	1.0	0.8	2.7	1.1	1.9	..	0.8	0.8
Q2	0.3	0.5	0.4	-1.6	1.2	-0.2	0.5	0.1	0.8
Implicit prices									
2001	2.4	0.7	....	....	....	1.4	2.4	2.8	1.3
2002	2.6	-2.0	....	....	....	1.4	1.9	3.1	-0.2
2003	2.2	-1.7	....	....	....	1.2	2.1	2.4	-1.2
2004	2.0	1.6	....	....	....	2.5	2.1	2.3	1.1
2005	1.9	3.8	....	....	....	2.3	2.1	2.6	2.7
2006	1.9	4.0	....	....	....	2.7	2.2	2.1	2.6
2005 – Q2	0.5	0.7	....	....	....	0.6	0.6	0.6	0.6
Q3	0.4	1.7	....	....	....	0.6	0.7	0.6	0.9
Q4	0.7	0.9	....	....	....	0.6	0.5	1.6	0.9
2006 – Q1	0.2	1.9	....	....	....	0.6	0.6	-0.3	0.7
Q2	0.5	0.4	....	....	....	0.7	0.6	1.1	0.6
Q3	0.5	0.3	....	....	....	0.8	0.5	-0.2	0.5
Q4	0.4	-0.6	....	....	....	0.6	0.2	..	0.2
2007 – Q1	0.7	0.6	....	....	....	0.9	0.4	0.6	0.3
Q2	0.6	0.6	....	....	....	0.6	0.6	0.3	0.6

Source: Based on Eurostat data.

(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' expenditure	General government expenditure (2)	Exports
				Building	Machinery & equipment, sundry products & vehicles	Total			
Chain-linked volumes									
2001	1.8	-0.2	1.4	4.1	1.3	2.5	0.7	3.6	0.5
2002	0.3	-0.5	0.2	4.8	3.4	4.0	0.2	2.2	-4.0
2003	..	0.8	0.2	1.4	-4.1	-1.7	1.0	2.1	-2.4
2004	1.2	2.7	1.5	1.5	1.8	1.6	0.7	1.6	3.3
2005	0.1	0.5	0.2	0.3	-1.2	-0.5	0.6	1.5	-0.5
2006	1.9	4.3	2.4	2.1	2.6	2.3	1.5	-0.3	5.3
2005 – Q2	0.6	1.8	0.9	2.8	1.2	1.9	0.6	..	2.5
Q3	0.4	..	0.3	1.1	2.5	1.8	0.5	0.4	0.6
Q4	-0.1	1.4	0.2	-1.4	-2.2	-1.8	-0.3	-0.2	1.4
2006 – Q1	0.8	1.2	0.9	0.4	2.9	1.7	0.6	-0.3	2.3
Q2	0.6	0.3	0.5	1.0	0.3	0.6	0.5	-0.1	1.4
Q3	0.3	2.2	0.7	0.3	-1.4	-0.6	0.6	0.2	-1.9
Q4	1.1	1.8	1.3	2.8	1.4	2.1	0.2	..	4.2
2007 – Q1	0.3	-1.1	..	1.5	-0.6	0.4	0.7	0.1	-0.1
Q2	0.1	-0.3	..	-1.3	1.4	0.1	0.6	0.1	-1.0
Implicit prices									
2001	3.0	3.4	3.1	2.6	2.1	2.3	2.6	4.0	4.5
2002	3.4	0.4	2.8	3.8	1.8	2.6	2.9	2.8	2.6
2003	3.1	-0.9	2.3	3.3	1.0	2.0	2.8	3.6	0.9
2004	2.9	4.2	3.1	4.6	2.0	3.2	2.6	3.4	4.2
2005	2.2	7.9	3.4	3.9	2.4	3.1	2.4	3.6	5.6
2006	1.8	9.1	3.3	3.1	1.8	2.4	2.7	3.4	5.2
2005 – Q2	0.6	1.7	0.8	0.8	0.4	0.6	0.8	0.5	1.0
Q3	0.2	4.0	1.0	0.7	0.6	0.7	0.8	0.6	2.0
Q4	1.4	1.1	1.3	0.7	0.3	0.5	0.5	7.0	1.4
2006 – Q1	-0.6	4.2	0.4	0.5	0.1	0.3	0.7	-3.8	0.8
Q2	1.1	1.5	1.2	1.0	0.8	0.9	0.8	4.5	1.3
Q3	0.2	1.3	0.5	0.9	0.3	0.6	0.7	-2.5	1.5
Q4	0.4	-1.1	0.1	0.9	1.2	1.0	..	-1.1	1.4
2007 – Q1	0.9	2.7	1.3	1.2	1.3	1.3	0.4	1.0	2.5
Q2	0.7	0.8	0.8	0.9	0.4	0.6	0.6	0.3	1.5

Source: Based on Istat data.

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

Table A5

Unit labour costs, per capita compensation and productivity: euro area (1)
(percentage changes on the year-earlier period)

	Per capita compensation	Productivity			Unit labour costs
		of which:			
		Value added (2)	Employees (1)		
Total industry excluding construction					
2002	2.2	1.1	-0.1	-1.1	1.0
2003	2.1	1.8	0.3	-1.4	0.4
2004	2.7	2.9	2.4	-1.1	-0.2
2005	1.5	2.2	0.6	-1.3	-0.7
2006	3.2	4.2	3.7	-0.2	-1.0
2005 – Q1	1.2	1.5	0.3	-1.2	-0.3
Q2	1.6	1.9	0.4	-1.5	-0.3
Q3	1.5	2.1	1.0	-1.2	-0.6
Q4	1.7	3.1	1.9	-1.2	-1.4
2006 – Q1	3.1	4.1	3.5	-0.6	-1.0
Q2	3.1	3.9	3.7	-0.2	-0.8
Q3	3.4	4.2	4.2	..	-0.7
Q4	3.0	4.6	4.5	-0.1	-1.5
2007 – Q1	1.7	3.1	4.4	1.3	-1.3
Q2	2.7	2.7	4.1	1.3	-0.1
Services					
2002	2.8	0.0	1.4	1.4	2.8
2003	2.3	-0.1	1.1	1.1	2.3
2004	2.0	0.2	1.8	1.5	1.8
2005	1.9	0.6	1.9	1.4	1.3
2006	1.9	0.5	2.4	2.0	1.4
2005 – Q1	1.9	0.7	2.1	1.4	1.1
Q2	1.7	0.6	2.0	1.3	1.0
Q3	1.7	0.6	2.0	1.4	1.1
Q4	2.4	0.6	2.0	1.3	1.8
2006 – Q1	1.9	0.3	2.0	1.7	1.6
Q2	2.2	0.3	2.5	2.2	1.9
Q3	2.0	0.4	2.5	2.1	1.5
Q4	1.3	0.8	2.8	2.0	0.5
2007 – Q1	1.9	0.5	3.0	2.5	1.3
Q2	1.1	0.3	2.7	2.4	0.9
Total economy					
2002	2.6	0.3	0.9	0.6	2.3
2003	2.3	0.3	0.7	0.4	2.0
2004	2.1	0.9	2.1	0.9	1.2
2005	1.8	0.7	1.5	0.9	1.0
2006	2.2	1.3	2.7	1.5	0.9
2005 – Q1	1.6	0.5	1.5	1.0	1.2
Q2	1.6	0.5	1.4	0.9	1.1
Q3	1.6	0.9	1.7	0.8	0.7
Q4	2.2	0.9	1.8	0.8	1.2
2006 – Q1	2.2	1.1	2.3	1.2	1.1
Q2	2.4	1.2	2.8	1.6	1.2
Q3	2.4	1.3	2.9	1.6	1.1
Q4	1.8	1.6	3.2	1.6	0.2
2007 – Q1	1.9	1.1	3.6	2.5	0.8
Q2	1.6	0.5	3.0	2.4	1.0

Source: Based on Eurostat.

(1) Averages for the countries belonging to the euro area at the date shown. – (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)

	Per capita compensation (1)	Wages per employee (1)	Productivity			Unit labour costs
			of which:			
			Value added (2)	Employees (1)		
Total industry excluding construction						
2002	2.5	2.7	-1.4	-0.8	0.7	4.0
2003	2.8	2.6	-2.2	-2.3	0.0	5.2
2004	4.0	3.9	0.2	-0.8	-1.0	3.9
2005	2.8	2.8	0.3	-1.8	-2.1	2.4
2006	2.7	3.2	1.2	2.5	1.3	1.4
2005 – Q1	2.5	2.5	-0.4	-2.7	-2.3	2.9
Q2	3.2	3.3	1.8	-1.5	-3.2	1.4
Q3	2.8	2.9	0.8	-0.7	-1.4	2.0
Q4	2.6	2.7	2.0	0.2	-1.7	0.6
2006 – Q1	3.5	4.0	2.1	2.9	0.8	1.4
Q2	2.3	2.7	0.0	2.0	2.0	2.3
Q3	2.4	2.8	0.7	2.3	1.5	1.6
Q4	2.5	3.1	3.4	4.2	0.8	-0.9
2007 – Q1	2.5	2.6	0.5	1.3	0.8	2.0
Q2	3.8	4.0	0.4	0.9	0.5	3.3
Services						
2002	2.8	2.6	-0.9	1.0	1.8	3.7
2003	3.8	3.3	-0.8	0.3	1.1	4.6
2004	3.1	3.4	0.4	1.1	0.7	2.7
2005	3.5	3.6	0.5	1.0	0.5	3.0
2006	2.5	2.7	-0.3	1.6	1.9	2.9
2005 – Q1	2.6	2.8	0.2	1.1	0.9	2.4
Q2	1.3	1.4	0.2	1.0	0.7	1.1
Q3	2.9	3.2	0.5	0.8	0.2	2.4
Q4	7.0	7.0	1.0	1.1	0.1	5.9
2006 – Q1	3.6	3.7	-0.1	1.2	1.3	3.7
Q2	5.3	5.5	-0.9	1.5	2.5	6.3
Q3	3.6	3.7	-0.8	1.4	2.2	4.5
Q4	-2.2	-1.9	0.6	2.3	1.7	-2.7
2007 – Q1	1.5	1.6	1.3	2.3	0.9	0.1
Q2	-0.8	-0.7	1.3	2.0	0.6	-2.0
Total economy						
2002	2.7	2.6	-0.7	0.5	1.3	3.5
2003	3.7	3.2	-0.9	-0.3	0.6	4.6
2004	3.3	3.4	0.6	1.0	0.4	2.7
2005	3.1	3.3	0.4	0.2	-0.2	2.7
2006	2.5	2.8	0.1	1.7	1.6	2.5
2005 – Q1	2.3	2.5	-0.4	0.1	0.4	2.7
Q2	1.7	1.8	0.3	0.3	0.1	1.4
Q3	2.8	3.1	1.2	0.5	-0.7	1.6
Q4	5.4	5.5	1.1	0.6	-0.5	4.2
2006 – Q1	3.4	3.6	0.5	1.6	1.1	2.9
Q2	4.3	4.6	-0.5	1.5	2.0	4.8
Q3	3.2	3.4	-0.6	1.3	1.9	3.8
Q4	-0.7	-0.3	1.0	2.6	1.5	-1.7
2007 – Q1	2.0	2.1	1.5	2.2	0.7	0.5
Q2	0.7	0.8	1.2	1.8	0.5	-0.5

Source: Based on Istat data.

(1) Standard labour units. – (2) 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. unprocessed food and energy products	Total	Total excl. unprocessed food and energy products	Total	Total excl. unprocessed food and energy products	Total	Total excl. unprocessed food and energy products	Total	Total excl. unprocessed food and energy products
2002	2.6	2.8	1.4	1.6	1.9	2.2	3.6	3.9	2.2	2.5
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
2005 – Jan.	2.0	2.2	1.6	1.4	1.6	1.4	3.1	2.8	1.9	1.8
Feb.	2.0	2.1	1.9	1.3	1.9	1.2	3.3	2.8	2.1	1.6
Mar.	2.2	2.1	1.6	1.0	2.1	1.4	3.4	2.9	2.1	1.6
Apr.	2.1	2.0	1.4	0.7	2.0	1.3	3.5	2.7	2.1	1.4
May	2.3	2.1	1.6	1.1	1.7	1.3	3.0	2.6	2.0	1.6
June	2.1	2.0	1.8	0.8	1.8	1.2	3.2	2.5	2.1	1.4
July	2.1	1.8	1.8	0.8	1.8	0.9	3.3	2.5	2.2	1.3
Aug.	2.1	1.9	1.9	0.8	2.0	1.0	3.3	2.5	2.2	1.3
Sept.	2.2	1.8	2.5	1.1	2.4	1.2	3.8	2.6	2.6	1.4
Oct.	2.6	1.8	2.3	1.3	2.0	1.1	3.5	2.7	2.5	1.5
Nov.	2.4	1.9	2.2	1.2	1.8	1.1	3.4	2.8	2.3	1.5
Dec.	2.1	1.6	2.1	0.9	1.8	1.2	3.7	3.0	2.2	1.4
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	2.6	1.7	2.0

Source: Eurostat.

(1) Weighted average of the harmonized indices of the countries belonging to the euro area at the date shown.

Table A8

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	-13,057	8,854	1,179	-14,817	-1,477	-6,796	1,700	-38	-26	1,764
2005	-23,403	536	-523	-13,643	-1,451	-8,323	998	69	-66	994
2006	-37,869	-9,532	-1,474	-13,607	-5,251	-8,004	1,891	-100	-60	2,051
2005 – Q3	-773	1,887	1,632	-1,640	-324	-2,328	129	2	-44	171
Q4	-6,680	-729	-234	-2,420	-1,091	-2,207	396	62	-14	348
2006 – Q1	-12,577	-5,924	-1,470	-2,125	-1,274	-1,784	488	-106	65	529
Q2	-9,365	-1,714	1,688	-6,803	-1,014	-1,522	-26	-19	-139	132
Q3	-6,484	-1,675	130	-970	-1,468	-2,501	293	-2	1	294
Q4	-9,444	-219	-1,822	-3,709	-1,496	-2,197	1,136	26	14	1,096
2007 – Q1	-12,354	-2,094	-3,144	-4,149	-1,247	-1,720	1,212	-1	29	1,184
Q2	-9,136	2,169	-1,033	-8,263	-1,728	-282	33	-27	-15	75
2005 – July	2,637	3,527	991	-1,291	-77	-513	36	1	-3	37
Aug.	-2,063	-306	-707	-360	-56	-635	23	2	-21	42
Sept.	-1,346	-1,334	1,348	10	-191	-1,180	70	-1	-21	92
Oct.	-556	455	349	-538	-328	-494	59	-2	-31	92
Nov.	-2,781	-635	-210	-1,293	-254	-389	116	38	-2	80
Dec.	-3,343	-549	-373	-589	-508	-1,324	222	26	20	176
2006 – Jan.	-4,213	-3,070	-377	-605	-196	35	76	5	-42	113
Feb.	-3,257	-2,075	-338	-522	-239	-84	147	-8	101	55
Mar.	-5,107	-779	-755	-998	-839	-1,735	265	-103	7	361
Apr.	-3,532	-1,010	752	-2,367	-216	-691	-48	-9	-82	43
May	-3,466	-343	179	-2,183	-485	-634	65	3	19	42
June	-2,367	-361	756	-2,252	-313	-197	-43	-14	-76	47
July	264	1,462	658	-755	-537	-564	67	6	25	37
Aug.	-1,679	-1,366	-750	1,384	-367	-581	37	-1	2	37
Sept.	-5,068	-1,771	222	-1,599	-564	-1,356	188	-7	-26	220
Oct.	-3,315	107	-53	-2,209	-558	-603	106	23	2	81
Nov.	-3,183	-473	-761	-1,063	-507	-378	-83	2	-33	-52
Dec.	-2,945	147	-1,009	-437	-431	-1,216	1,114	2	44	1,068
2007 – Jan.	-5,454	-2,324	-1,291	-1,494	-515	170	259	-3	10	252
Feb.	-3,302	-751	-736	-1,271	-167	-377	266	-6	8	264
Mar.	-3,599	981	-1,116	-1,385	-565	-1,514	687	7	11	669
Apr.	-4,275	-217	-856	-2,115	-502	-584	37	-8	..	46
May	-3,984	747	-232	-3,502	-541	-456	19	-18	-4	41
June	-878	1,639	55	-2,645	-684	758	-22	..	-10	-12
July	(896)	(3,016)	(481)	(-1,985)	....	....	(42)	....	....	....

Table A9

Lending by Italian banks by geographical area and sector (1)											
	General government	Finance and insurance companies	Non-financial corporations (a)		Households		Firms = (a) + (b)			Total	
			under 20 employees (2)		Producer (b) (3)	Consumer	Manufacturing	Construction	Services		
12-month percentage changes (4)											
<i>Centre and North</i>											
2006 – Mar.	9.0	4.5	5.8	4.7	7.8	15.5	6.0	1.7	14.6	6.2	8.0
June	6.2	15.0	7.0	4.3	7.4	13.3	7.0	2.6	12.9	7.8	9.5
Sept.	9.0	13.7	8.8	4.5	7.3	12.8	8.7	4.1	13.5	10.2	10.3
Dec.	4.9	15.4	10.7	5.1	7.2	10.0	10.4	5.7	14.3	12.4	10.7
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
Aug.	1.4	7.5	12.7	5.4	5.8	8.7	12.1	....	....	....	10.2
<i>South and Islands</i>											
2006 – Mar.	14.8	13.2	14.3	9.0	11.5	18.3	13.8	10.6	15.8	15.0	15.5
June	1.6	14.3	15.3	8.5	10.3	16.4	14.4	12.5	17.6	15.3	14.5
Sept.	-3.8	12.4	16.3	9.4	9.9	15.6	15.1	11.9	20.3	16.5	14.2
Dec.	-3.0	-22.3	19.9	9.6	10.1	13.1	18.1	12.5	20.5	22.2	13.9
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
Aug.	1.6	2.9	16.1	9.7	8.8	12.3	14.8	....	....	....	13.0
<i>ITALY</i>											
2006 – Mar.	9.9	4.7	6.8	5.3	8.6	16.1	7.0	2.6	14.8	7.3	9.0
June	5.5	15.0	7.9	4.8	8.0	14.0	7.9	3.7	13.6	8.7	10.2
Sept.	7.0	13.7	9.7	5.2	7.9	13.4	9.5	5.0	14.6	11.0	10.9
Dec.	3.7	14.1	11.8	5.7	7.9	10.7	11.4	6.5	15.3	13.7	11.2
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
Aug.	1.4	7.4	13.1	6.0	6.5	9.5	12.4	7.4	15.8	12.3	10.6
Stock of loans in June 2007 (5) (6)											
<i>(millions of euros)</i>											
Centre and North	49,040	164,943	638,150	66,037	61,530	273,098	699,680	183,607	90,472	357,094	1,186,760
South and Islands	8,373	3,870	90,468	11,283	19,226	77,182	109,694	25,143	18,364	55,030	199,119
ITALY	57,413	168,813	728,618	77,320	80,756	350,279	809,373	208,743	108,836	412,129	1,385,879
Percentage breakdown of lending in June 2007 (6)											
Centre and North	4.1	13.9	53.8	5.6	5.2	23.0	59.0	15.5	7.6	30.1	100.0
South and Islands	4.2	1.9	45.4	5.7	9.7	38.8	55.1	12.6	9.2	27.6	100.0
ITALY	4.1	12.2	52.6	5.6	5.8	25.3	58.4	15.1	7.9	29.7	100.0

(1) 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. Data for August 2007 are provisional. – (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. – (4) Net of the effects of reclassification, exchange rate changes and other modifications not due to transactions. – (5) Stocks by geographical area may not add to the total because the figures are taken from different items of the accounting supervisory reports. – (6) Rounding may cause discrepancies.

Table A10

Financing of the general government borrowing requirement
(millions of euros)

	Currency and deposits		Short-term securities	Medium and long-term securities	MFI loans (1)	Other operations (1)		Borrowing requirement	
		<i>of which:</i> PO funds					<i>of which:</i> change in central bank current accounts		<i>of which:</i> financed abroad
2004	16,364	-1,187	-998	41,609	-1,409	-5,890	-2,578	49,675	4,904
2005	21,574	-4,177	-924	39,989	5,593	4,061	1,197	70,294	4,007
2006	7,601	-4,957	4,867	33,156	63,594	-54,677	-8,230	54,541	-7,104
2004 – Q1	6,509	-384	25,031	19,787	-513	-19,458	-19,890	31,356	4,958
Q2	12,048	2,646	3,107	26,273	144	-23,785	-22,221	17,787	1,077
Q3	-506	-2,826	-2,200	8,372	187	8,526	8,251	14,379	-1,028
Q4	-1,687	-623	-26,936	-12,823	-1,227	28,826	31,282	-13,847	-104
2005 – Q1	2,207	-516	11,204	45,940	1,198	-33,130	-34,293	27,418	1,293
Q2	12,648	149	9,287	20,756	1,952	-15,573	-14,842	29,071	3,546
Q3	3,238	-1,577	2,547	-19,414	346	29,464	28,813	16,181	424
Q4	3,481	-2,233	-23,963	-7,292	2,097	23,300	21,519	-2,377	-1,256
2006 – Q1	10,908	-891	18,406	13,053	2,479	-11,612	-16,246	33,234	-259
Q2	1,187	-1,615	7,154	28,768	-630	-25,553	-26,568	10,926	732
Q3	232	-1,210	-7,799	5,973	55,958	-39,101	12,948	15,263	1,294
Q4	-4,726	-1,240	-12,893	-14,639	5,787	21,590	21,637	-4,882	-8,871
2007 – Q1	-1,459	-3,474	20,664	7,523	2,261	-5,624	-5,753	23,365	-519
Q2	-16,435	-13,509	345	28,700	-587	-8,724	-8,936	3,298	2,499
2006 – Jan.	7,139	-844	9,294	20,225	615	-31,497	-31,955	5,775	-308
Feb.	1,999	370	2,388	-1,681	319	5,547	2,941	8,572	-39
Mar.	1,770	-417	6,725	-5,491	1,545	14,338	12,768	18,887	88
Apr.	-618	-370	4,549	4,722	398	681	47	9,732	-1,834
May	550	-56	2,139	4,834	-1,129	9,452	8,401	15,846	1,187
June	1,256	-1,188	465	19,212	101	-35,686	-35,016	-14,653	1,379
July	-1,482	-601	-2,755	-4,529	-935	6,202	4,564	-3,499	-190
Aug.	1,440	-28	-2,960	7,915	-475	3,237	1,153	9,157	-1,225
Sept.	274	-582	-2,084	2,587	57,367	-48,540	7,232	9,604	2,709
Oct.	-455	-216	-571	3,047	719	1,949	1,870	4,687	-7,105
Nov.	-1,880	-553	2,898	2,108	10	5,602	5,765	8,737	2,052
Dec.	-2,391	-471	-15,220	-19,793	5,058	14,039	14,002	-18,306	-3,819
2007 – Jan.	3,287	-263	12,347	-1,824	815	-11,562	-11,383	3,063	-756
Feb.	-2,029	204	3,027	5,059	1,118	-3,550	-3,489	3,624	-291
Mar.	-2,717	-3,415	5,290	4,289	328	9,488	9,120	16,678	528
Apr.	-4,256	-4,597	99	4,960	2,811	7,560	7,549	11,175	352
May	-3,092	-1,584	2,261	18,325	-1,488	-4,732	-5,066	11,274	505
June	-9,087	-7,329	-2,015	5,415	-1,910	-11,553	-11,419	-19,150	1,643
July	-810	-4,856	377	110	-205	-3,809	-3,963	-4,338	-2,645

(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
(millions of euros)

	Currency and deposits		Short-term securities	Medium and long-term securities	MFI loans (1)	Other liabilities (1)	General government debt			Memorandum item: central bank current accounts
		of which: PO funds					of which: in foreign currencies	of which: medium and long-term		
2004	127,562	74,755	118,384	1,090,626	54,496	52,327	1,443,395	26,630	1,218,564	15,831
2005	149,137	70,578	117,460	1,129,313	60,098	55,190	1,511,198	27,255	1,257,881	14,634
2006	156,737	65,622	122,327	1,163,949	123,684	8,743	1,575,441	10,740	1,303,632	22,864
2004 – Mar.	117,707	75,559	144,444	1,070,717	55,408	56,071	1,444,347	29,614	1,206,025	33,143
June	129,756	78,204	147,554	1,096,958	55,549	54,507	1,484,324	31,649	1,228,711	55,364
Sept.	129,250	75,378	145,334	1,104,692	55,730	54,782	1,489,787	30,998	1,236,028	47,113
Dec.	127,562	74,755	118,384	1,090,626	54,496	52,327	1,443,395	26,630	1,218,564	15,831
2005 – Mar.	129,770	74,239	129,589	1,136,087	55,698	53,489	1,504,632	29,260	1,264,291	50,124
June	142,418	74,388	138,877	1,157,003	57,655	52,759	1,548,712	26,844	1,283,069	64,966
Sept.	145,656	72,811	141,424	1,136,472	58,000	53,409	1,534,962	26,634	1,261,619	36,153
Dec.	149,137	70,578	117,460	1,129,313	60,098	55,190	1,511,198	27,255	1,257,881	14,634
2006 – Mar.	160,045	69,687	135,868	1,142,375	62,574	59,824	1,560,687	22,314	1,275,813	30,880
June	161,232	68,072	143,025	1,172,307	61,943	60,839	1,599,346	18,375	1,302,829	57,449
Sept.	161,464	66,862	135,224	1,178,518	117,899	8,790	1,601,895	15,116	1,312,136	44,501
Dec.	156,737	65,622	122,327	1,163,949	123,684	8,743	1,575,441	10,740	1,303,632	22,864
2007 – Mar.	155,278	62,147	142,994	1,172,660	125,945	8,871	1,605,750	5,020	1,314,872	28,616
June	138,843	48,639	143,349	1,203,569	125,358	9,083	1,620,201	4,908	1,344,784	37,552
2006 – Jan.	156,276	69,734	126,753	1,149,245	60,711	55,649	1,548,633	26,360	1,278,266	46,589
Feb.	158,275	70,104	129,141	1,148,371	61,032	58,254	1,555,073	23,446	1,279,406	43,648
Mar.	160,045	69,687	135,868	1,142,375	62,574	59,824	1,560,687	22,314	1,275,813	30,880
Apr.	159,426	69,317	140,421	1,146,862	62,971	60,459	1,570,139	19,509	1,280,240	30,834
May	159,976	69,261	142,561	1,152,379	61,842	61,510	1,578,269	17,673	1,285,927	22,433
June	161,232	68,072	143,025	1,172,307	61,943	60,839	1,599,346	18,375	1,302,829	57,449
July	159,750	67,471	140,268	1,167,874	61,008	62,477	1,591,377	18,101	1,299,198	52,885
Aug.	161,190	67,444	137,306	1,175,937	60,532	64,562	1,599,526	17,379	1,308,744	51,732
Sept.	161,464	66,862	135,224	1,178,518	117,899	8,790	1,601,895	15,116	1,312,136	44,501
Oct.	161,008	66,646	134,652	1,181,733	118,618	8,869	1,604,881	12,370	1,314,917	42,631
Nov.	159,128	66,093	137,550	1,183,694	118,627	8,706	1,607,705	10,813	1,319,583	36,866
Dec.	156,737	65,622	122,327	1,163,949	123,684	8,743	1,575,441	10,740	1,303,632	22,864
2007 – Jan.	160,025	65,358	134,674	1,162,829	124,500	8,564	1,590,591	6,968	1,303,774	34,247
Feb.	157,996	65,562	137,702	1,168,470	125,617	8,502	1,598,288	6,845	1,309,684	37,736
Mar.	155,278	62,147	142,994	1,172,660	125,945	8,871	1,605,750	5,020	1,314,872	28,616
Apr.	151,022	57,551	143,094	1,177,613	128,756	8,882	1,609,367	4,907	1,320,459	21,067
May	147,930	55,967	145,358	1,196,907	127,268	9,216	1,626,679	4,960	1,340,457	26,133
June	138,843	48,639	143,349	1,203,569	125,358	9,083	1,620,201	4,908	1,344,784	37,552
July	138,032	43,782	143,731	1,204,220	125,153	9,236	1,620,373	4,837	1,345,328	41,515

(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".

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