## 2.10 PROJECTIONS

The projections for the Italian economy presented in this *Economic Bulletin* update those prepared as part of the Eurosystem coordinated exercise and published on 11 June.[1]

**Demand is buoyed by the progress in vaccinations ...**

The scenario outlined here assumes that the public health situation will continue to improve at both national and global level, also thanks to the vaccination campaigns, and that this will confirm the easing of the restrictions on mobility, which would be lifted at the beginning of 2022.

**... economic policies ...**

It is also assumed that there will be strong support from fiscal policy, with the use of both national and EU funds, and that favourable monetary and financial conditions will be maintained. Under the technical assumptions, Italian ten-year government securities will remain stable at 0.9 per cent this year and increase only gradually in the subsequent two years, in line with the expectations implied in market prices, which reflect the intention expressed by the Eurosystem to maintain a very expansionary monetary stance for a prolonged period of time.

Credit conditions are assumed to remain relaxed: thanks to the recovery in economic activity and to the very gradual withdrawal of the support measures, the repercussions of the pandemic crisis on firms' indebtedness and on the quality of bank credit have remained limited and are not translating into a significant tightening of financial conditions. The cost of borrowing for firms is assumed to be 1.5 per cent in 2021 on average and to rise only slightly afterwards.

**... and the recovery in world trade**

The projections also incorporate favourable developments in global trade, in line with the most recent assessments of international institutions (see Section 1.1). After falling by about 10 percentage points in 2020, Italy's foreign demand, weighted by the outlet markets, is forecast to increase by 8.8 per cent in 2021 and by 4.7 per cent on average in each of the next two years (see the box 'The assumptions underlying the macroeconomic scenario').

### THE ASSUMPTIONS UNDERLYING THE MACROECONOMIC SCENARIO

The forecasting scenario for the Italian economy prepared by the Bank of Italy experts as part of the Eurosystem staff macroeconomic projection exercise is published each June and December, following the release of the euro-area projections[1] by the European Central Bank. The macroeconomic projections for Italy presented here update those released on 11 June and are based on the information available at 9 July.

The main assumptions underlying the scenario are as follows (see the table):

a) foreign demand, weighted by the outlet markets for Italian exports, which decreased by 10 per cent in 2020, expands by 8.8 per cent this year and by 4.7 per cent on average in the two years 2022-23;

[1] See the Bank of Italy's website, 'Macroeconomic projections for Italy', containing the projections published to date as part of the Eurosystem coordinated exercise.

[1] See the Bank of Italy's website, 'Macroeconomic projections for the Italian economy', 11 June 2021.

b) the euro/dollar exchange rate, equal to 1.14 in 2020, rises to 1.20 in 2021 and settles at 1.19 in the two years 2022-23;[2]

c) the price of a barrel of Brent crude oil, fixed on the basis of the prices of futures contracts, averages $69.2 this year ($42.3 in 2020), remains at similar levels in 2022, and declines slightly afterwards, to around $65 in 2023;

d) the three-month interest rates on the interbank market (Euribor) averages -0.5 per cent in the two years 2021-22 and is equal to -0.4 per cent in 2023;

e) the yield on ten-year BTPs, equal to 1.1 per cent on average in 2020, falls to 0.9 per cent in 2021, and then increases gradually to 1.4 per cent in 2023, in line with the values of forward rates implied by the term structure of interest rates on government bond yields.

Table

**Assumptions for the main exogenous variables**

| | 2020 | 2021 | 2022 | 2023 |
|---|---|---|---|---|
| Potential foreign demand (1) | -10.0 | 8.8 | 5.9 | 3.4 |
| Dollar/euro (2) | 1.14 | 1.20 | 1.19 | 1.19 |
| Nominal effective exchange rate (1) (3) | -1.5 | -1.0 | 0.2 | 0.0 |
| Crude oil prices (2) (4) | 42.3 | 69.2 | 69.0 | 64.8 |
| 3-month Euribor (2) | -0.4 | -0.5 | -0.5 | -0.4 |
| 1-year BOTs (2) | -0.1 | -0.5 | -0.4 | -0.3 |
| 10-year BTPs (2) | 1.1 | 0.9 | 1.1 | 1.4 |

Sources: Based on Bank of Italy and Istat data.
(1) Percentage changes. – (2) Annual averages. – (3) Positive changes indicate a depreciation. – (4) Dollars per barrel of Brent crude oil.

f) the scenario incorporates the measures included in the 2021 Budget Law and in Decree Laws 41/2021 ('Support Decree'), 59/2021 ('Complementary Fund to the National Recovery and Resilience Plan'),[3] and 73/2021 ('Support-*bis*' decree), as well as an assumption on the use of EU funds under the Next Generation EU programme, based on the guidance provided by the NRRP.

[2] The technical assumptions on interest rates, exchange rates and oil prices are calculated on the basis of the spot and forward prices observed in the markets in the ten working days to 12 July.

[3] Containing urgent measures relating to the Complementary Fund to the National Recovery and Resilience Plan and other urgent measures regarding investment.

**GDP is set to accelerate markedly starting from the summer ...**

Based on these assumptions, following the recovery in the first half of 2021, GDP is projected to accelerate significantly starting from the third quarter. Looking at the year as a whole, GDP growth is currently estimated at 5.1 per cent in 2021 and is forecast to remain high in the following two years (with point estimates of 4.4 per cent in 2022 and 2.3 per cent in 2023). Starting from the second half of 2022, GDP is expected to return to pre-pandemic levels (Table 16; Figures 48 and 49).

**... thanks to the key role played by the NRRP**

The scenario presented here is heavily dependent on the effectiveness and timeliness of the measures introduced to support and relaunch the economy. In the projections, the interventions financed by the national budget and by EU funding, including those set out in the NRRP,[2] provide a significant boost to economic activity, raising GDP by about 4 percentage points cumulatively over the three-year

[2] The projections take into account the interventions provided for in the 2021 Budget Law and in Decree Laws 41/2021 ('Support Decree'), 59/2021 ('Complementary Fund to the National Recovery and Resilience Plan'), and 73/2021 ('Support-*bis*' decree). They also assume that the EU funding under the NGEU programme will be used in a way that is consistent with the indications of the NRRP.

**Table 16**

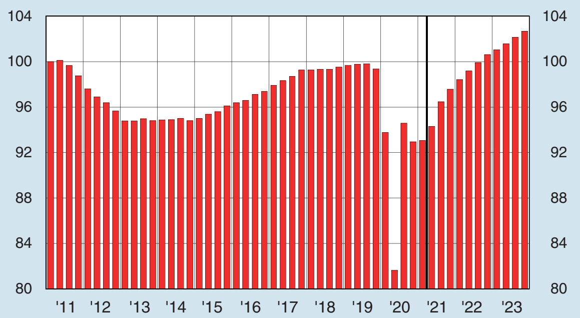
## Macroeconomic scenario
*(percentage changes on previous year unless otherwise indicated)*

| | 2020 | 2021 | 2022 | 2023 |
|---|---|---|---|---|
| GDP (1) | -8.9 | 5.1 | 4.4 | 2.3 |
| Household consumption | -10.7 | 3.3 | 5.6 | 2.2 |
| Government consumption | 1.6 | 2.2 | -1.9 | 0.6 |
| Gross fixed investment | -9.6 | 15.2 | 8.7 | 5.0 |
| *of which:* in capital goods | -11.5 | 11.6 | 8.2 | 7.6 |
| Total exports | -14.7 | 11.0 | 6.5 | 3.2 |
| Total imports | -13.2 | 12.9 | 7.7 | 3.7 |
| Changes in stocks (2) | -0.1 | 0.3 | 0.0 | 0.0 |
| *Memorandum item:* GDP, raw data (3) | -8.9 | 5.1 | 4.3 | 2.2 |
| Prices (HICP) | -0.1 | 1.5 | 1.3 | 1.3 |
| HICP net of food and energy | 0.5 | 0.5 | 0.6 | 1.1 |
| GDP deflator | 1.2 | 1.3 | 1.6 | 1.4 |
| Employment (hours worked) | -11.2 | 5.0 | 4.1 | 2.5 |
| Employment (persons employed) | -2.8 | -0.7 | 1.6 | 1.8 |
| Unemployment rate (4) | 9.3 | 10.5 | 10.3 | 9.9 |
| Export competitiveness (5) | -2.2 | 0.4 | 0.3 | -0.7 |
| Current account balance of the balance of payments (6) | 3.5 | 3.3 | 2.9 | 2.9 |

Sources: Based on Bank of Italy and Istat data.
(1) For GDP and its components: chain-linked volumes; changes estimated on the basis of quarterly data adjusted for seasonal and calendar effects. – (2) Includes valuables. Contributions to GDP growth; per cent. – (3) Not calendar adjusted. – (4) Annual averages; per cent. – (5) Calculated by comparing the price of foreign manufactures with the deflator of Italian merchandise exports (excluding energy and agricultural products); a positive value indicates a gain in competitiveness. – (6) Per cent of GDP.

**Figure 48**

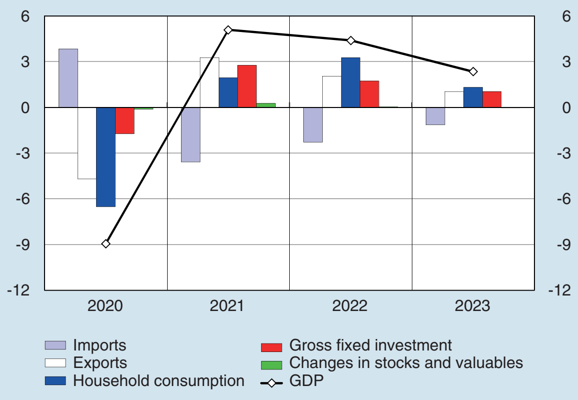
### GDP projections: quarterly profile (1)
*(quarterly data; indices: Q1 2011=100)*




Sources: Based on Bank of Italy and Istat data.
(1) Data seasonally and calendar adjusted. Observed data up to Q1 2021. Projections for the subsequent quarters.

**Figure 49**

### GDP growth and contributions of the main demand components and of imports (1)
*(annual data; percentage changes and percentage points)*



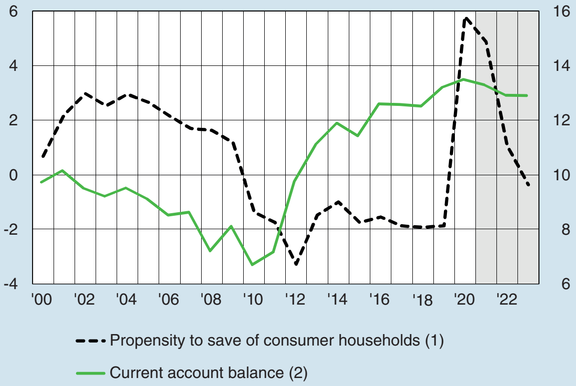

Sources: Based on Bank of Italy and Istat data.
(1) Data seasonally and calendar adjusted.

forecasting horizon. About half of this effect is attributable to interventions under the NRRP, with the assumption that they will be carried out effectively and without significant delays.

These assessments incorporate the demand effects of the interventions carried out under the NRRP, which are associated with an average multiplier of just over one, in keeping with the assumptions that such interventions are to a large extent concentrated in public investments. Further effects playing out in the years beyond the forecasting horizon could be obtained if the execution of public investments were done in such a way as to raise the profitability of private capital, through the reforms laid out in the NRRP and the plans to incentivize research and innovation.[3]

Figure 50

**Propensity to save of consumer households and current account balance**
*(monthly data; percentage points)*




Sources: Based on Bank of Italy and Istat data.
(1) Right-hand scale. – (2) Per cent of GDP.

**In the projection scenario, employment picks up again ...**

Over the next three years, the number of hours worked is projected to increase by over 11 per cent, returning to pre-pandemic levels at the end of 2022. The number of people in employment is also expected to expand further in the coming quarters, exceeding pre-crisis levels by the first half of 2023. In the projections, the impact on total employment of the lifting of the freeze on dismissals is largely offset by new hires. The unemployment rate is expected to rise in 2021, to 10.5 per cent, and to subsequently fall, to 9.9 per cent in 2023.

**... consumption grows gradually ...**

Consumption, which at the beginning of 2021 was affected by the restrictions on mobility and the fears of contagion, is projected to return to growth in the summer months (see Section 2.3), with a partial recovery in purchases that were not made in 2020 (see the box 'Savings accumulated during the pandemic and consumption projections'). The saving rate is expected to decrease in the next two years, as the health-related crisis is overcome and the uncertainty around the outlook for income is gradually dispelled, but will likely remain above pre-crisis levels (Figure 50). Household spending is projected to grow by 3.3 per cent on average this year, by 5.6 per cent in 2022 and by 2.2 per cent in 2023.

## SAVINGS ACCUMULATED DURING THE PANDEMIC AND CONSUMPTION PROJECTIONS

In 2020, the fall in household consumption, equal to 10.7 per cent in real terms, was much more pronounced than that in disposable income, which decreased by only 2.6 per cent thanks to the mostly temporary public support measures. This resulted in an exceptional increase in households' aggregate saving rate, which – though concentrated among the wealthiest households – rose to 15.8 per cent,[1] almost twice the average level recorded in the previous decade.

[1] Adjusted to take account of changes in the net equity of households in pension fund technical reserves; net of that component, the saving rate rose to 15.3 per cent.

[3] See the box 'The National Recovery and Resilience Plan', Chapter 4, *Annual Report for 2020*, 2021.

Therefore, in the formulation of macroeconomic projections for the next three years, a key role is played by the assumptions on the share of savings accumulated in 2020 that households could use for consumption purposes in the current year. The plausibility and implications of these assumptions are to be assessed.

According to the Bank of Italy's Special Survey of Italian Households, the increase in savings in 2020 was attributable in almost equal measure to the restrictions on mobility and on access to certain services (e.g. leisure and restaurants), to fears of contagion, and to precautionary motives of a financial nature.[2] Going forward, based on the surveys available so far, and even assuming a progressive lifting of the restrictions, households expect that they will use part of their greater wealth for future spending, but will still exercise considerable caution. In particular, the respondent households indicated that this year they plan to use about one third of the savings accumulated in 2020 for consumption purposes.

These findings suggest that, also taking account of cyclical conditions, this year the response of consumption to the increase in financial wealth, held above all in the form of deposits, could be stronger than what was observed on average for the Italian economy based on past patterns.[3]

A stronger response of consumption to the increase in wealth could be motivated by the desire to make purchases in 2021 that had been postponed owing to the pandemic. As observed in past recessions,[4] it is likely that at least part of the spending on durable and semi-durable goods not made in 2020 was

**Figure**

**Breakdown of the contraction in the final consumption of households in 2020**

*(changes on 2019; millions of euros)*


Source: Based on Istat data.

2 C. Rondinelli and F. Zanichelli, 'The main results of the fourth wave of the Special Survey of Italian Households', Banca d'Italia, *Note Covid-19*, 21 May 2021.

3 R. De Bonis, D. Liberati, J. Muellbauer and C. Rondinelli, 'Consumption and wealth: new evidence from Italy', Banca d'Italia, Temi di Discussione (Working Papers), 1304, 2020; R. De Bonis and A. Silvestrini, 'The effects of financial and real wealth on consumption: new evidence from OECD countries', Banca d'Italia, Temi di Discussione (Working Papers), 837, 2011; M. Paiella, 'Does wealth affect consumption? Evidence for Italy', Banca d'Italia, Temi di Discussione (Working Papers), 510, 2004. These authors estimate that for Italy an increase in financial wealth equal to one euro would generate greater consumption ranging between 4 and 9 euro cents. These estimates are in line with those implied by the Bank of Italy's quarterly econometric model; see G. Bulligan, F. Busetti, M. Caivano, P. Cova, D. Fantino, A. Locarno and L. Rodano, 'The Bank of Italy econometric model: an update of the main equations and model elasticities', Banca d'Italia, Temi di Discussione (Working Papers), 1130, 2017.

4 A. Bassanetti, M. Cecioni, A. Nobili and G. Zevi, 'The main recessions in Italy: a retrospective comparison', Banca d'Italia, Questioni di Economia e Finanza (Occasional Papers), 46, 2009.

postponed to 2021.[5] It is instead less plausible that this is also true of services and non-durable goods. In 2020 on average, lower purchases of durable and semi-durable goods contributed less than 20 per cent (about €25 billion) to the fall in domestic consumption (down by 11.8 per cent, or almost €125 billion). The remaining portion of the fall in consumption (about 80 per cent, or just under €100 billion) was instead ascribable to spending on services and non-durable goods (see the figure).

These considerations are incorporated in the macroeconomic projections, where household consumption includes an upward revision compared with the estimate that would be obtained by considering the elasticities by which consumption typically reacts to increases in income and wealth in the Bank of Italy's quarterly econometric model. The assumption is that this revision, amounting to about €20 billion by the first half of 2022, will lead to a full recovery in non-durable goods purchases that were not made in 2020 (about €8 billion) and a partial recovery in the purchases of semi-durable goods that were put off in that same period.

While the growth in household consumption in 2021 exceeds that which may be inferred from the standard elasticities of the model, the saving rate declines only gradually in the three-year forecasting horizon, remaining above pre-pandemic levels. This is due to consumers' tendency to smooth over time the impact on consumption of one-off increases in the financial resources at their disposal, such as those associated with the greater savings accumulated during the health-related crisis. Moreover, a gradual fall in the saving rate is consistent with the indications of cautious spending that our surveys found.

However, this assessment is marked by considerable uncertainty, given the unprecedented contraction in consumption during the pandemic and its determinants.

In a more pessimistic scenario, households' fears regarding the outlook for employment and income could be more persistent. This would result in a slower recovery in consumption compared with that presented in the forecasting scenario. To quantify the consequences of this eventuality, it may be assumed that households will decide to postpone further the purchases of non-durable goods not made so far.[6] Should this occur, the growth in GDP in 2021 would decline by around half a percentage point, to 4.6 per cent. In the subsequent two-year period, both GDP and consumption would make up practically in full for the slower growth (see the table).

**Table**

**Effects of possible alternative assumptions on consumption**
*(differences in the rates of change compared with the forecasting scenario; percentage points)*

| | Recovery in consumption occurs later | | | Recovery in consumption occurs earlier | | |
|---|---|---|---|---|---|---|
| | 2021 | 2022 | 2023 | 2021 | 2022 | 2023 |
| Final domestic consumption of households | -0.9 | 0.5 | 0.4 | 1.3 | -0.3 | 0.0 |
| Gross domestic product (GDP) | -0.5 | 0.2 | 0.2 | 0.7 | -0.1 | 0.0 |

Source: Based on Istat data.

5 Durable goods include, in particular, cars, motorcycles, boats, furnishings, household appliances, jewellery, and clocks and watches. Semi-durable goods include above all clothing, footwear, glasses, books and various household items (linen, furnishing fabrics, glassware, crockery, etc.).

6 The upward revision included in the forecasting scenario would therefore be reduced over the course of this year for the part attributable to durable goods (about €8 billion), and correspondingly increased in the following two-year period.

A more favourable scenario, stemming from a rapid improvement in the COVID-19 situation and a recovery in confidence, could lead households to increase spending by more than what is hypothesized in the forecasting scenario. Assuming that the saving rate will return to the average levels recorded in the decade before the pandemic crisis by 2023, this would result in higher consumption spending of about €10 billion starting from this year. This, in turn, would entail higher GDP growth of more than half a percentage point compared with the central projection in 2021, and only slightly lower than that in 2022 (see the table).

**... capital accumulation is very rapid ...**

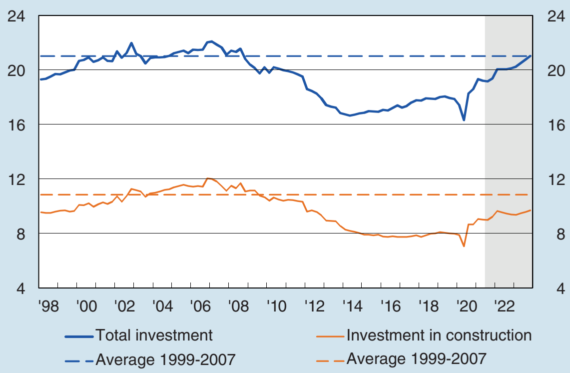
The recovery will likely be marked by a strong contribution of investment, contrary to what was observed after the two previous recessions.[4] Capital accumulation, which already in the first quarter of the year had surpassed the average levels recorded in 2019, will continue to expand thanks to the improved outlook for demand, the favourable financing conditions, and the support envisaged under the NRRP. Investment is expected to rise by 15.2 per cent on average in 2021, by 8.7 per cent in 2022 per cent and by 5 per cent in 2023. At the end of the three-year period, the ratio of investment to GDP is projected to regain, after more than a decade, the levels prevailing before the global financial crisis of 2008-09 (Figure 51). The public component looks set to play a key part in this, returning, as a share of GDP, to levels in line with the European average after more than a decade.

**... and exports are in line with developments in world trade**

Foreign sales, especially of goods, are projected to be driven by the recovery in world trade. Those of services will likely be affected by the more gradual recovery in tourist flows, which are assumed to regain pre-crisis levels only in 2023. Exports are expected to grow by 11 per cent this year and by about 5 per cent on average in each of the next two years, in line with foreign demand. Imports, also in part activated by investments, are projected to grow at a higher rate. The current account surplus of the balance of payments should decline slightly over the forecasting horizon, to just under 3 per cent (Figure 50).

Figure 51

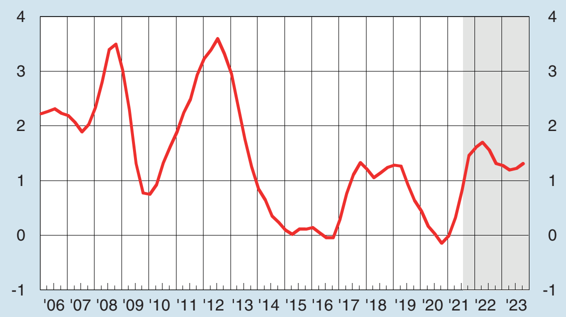
**Investment as a percentage of GDP** (1)
*(quarterly data)*




Sources: Based on Bank of Italy and Istat data.
(1) Data seasonally and calendar adjusted.

Figure 52

**Consumer price inflation** (1)
*(quarterly data; year-on-year percentage changes)*




Sources: Based on Bank of Italy and Istat data.
(1) HICP; 4-term moving averages.

[4] See Chapter 6, 'Firms', *Annual Report for 2020*, 2021.

**The rise in inflation reflects the increases in energy prices**

Consumer price inflation, driven above all by the impact of the increase in commodity prices, is projected to reach 1.5 per cent this year and to slow to 1.3 per cent in the next two years (Figure 52). Also considering the low level of inflation expectations reported so far by households and firms (see Section 2.6), at the moment there are no signs of a stronger transmission to domestic prices or of an acceleration in wages, a necessary condition for a more persistent rise in inflation. The core component is expected to rise from 0.5 per cent in 2021 to up to 1.1 per cent in 2023. This would be supported by a reduction in spare capacity margins and an only gradual acceleration in wages: in the private sector, they are assumed to rise by about 0.7 per cent this year and by around 1.2 per cent on average in each of the next two years. Domestic inflation, measured by the GDP deflator, is projected to average 1.4 per cent over the three-year period.

Table 17

**Other organizations' forecasts for Italy**
*(percentage changes on previous period)*

| | GDP (1) | | Inflation (2) | |
|---|---|---|---|---|
| | 2021 | 2022 | 2021 | 2022 |
| IMF (June) | 4.3 | 4.0 | 0.8 | 1.0 |
| OECD (May) | 4.5 | 4.4 | 1.3 | 1.0 |
| European Commission (July) | 5.0 | 4.2 | 1.4 | 1.2 |
| Consensus Economics (June) | 4.5 | 4.2 | 1.2 | 1.1 |

Sources: IMF, *Italy. 2021 Article IV consultation-press release; staff report; and statement by the Executive Director for Italy*, IMF Country Report, 21/101, June 2021; OECD, *OECD Economic Outlook*, May 2021; European Commission, *European Economic Forecast Summer 2021*, July 2021; Consensus Economics, *Consensus Forecasts*, June 2021.
(1) The growth rate forecasts of the OECD are adjusted for calendar effects; those of the European Commission and IMF are not. – (2) HICP.

**GDP projections are revised upwards ...**

Compared with the projections published in January's *Economic Bulletin,* GDP growth was revised upwards by 1.6 percentage points for 2021 and 0.6 points for 2022. The revision is due above all to the impact of the additional support measures introduced by the Government and new information on the time frame and implementation of the interventions set out in the NRRP. The inflation forecasts were revised upwards by about 0.8 percentage points this year and around 0.3 points on average in the two-year period 2022-23, reflecting the higher commodity prices.[5]

Our growth projections for the two-year period 2021-22 are in line with those released by the European Commission in July. They are instead slightly more favourable than those formulated in May by the OECD and in June by the IMF and by Consensus Economics (Table 17), which were prepared before the release of the upward revision regarding the GDP estimate for the first quarter. The inflation forecasts for this year and the next do not deviate significantly from those formulated by the European Commission, the OECD and Consensus Economics, while they are higher than those prepared by the IMF.

**The pandemic and the effectiveness of the policies adopted are factors of uncertainty**

The main elements of uncertainty surrounding the outlook for growth are linked to the course of the pandemic and the effectiveness of the support policies. Over the course of this year, trends in the number of COVID-19 cases may affect confidence as well as consumption and investment decisions. In the following years, the intensity of the recovery will mostly depend on how the projects connected with the NRRP will be implemented. A delayed or less effective execution of those projects and, more broadly, a premature lifting of economic policy support could weaken the recovery. Conversely, growth could benefit from a swifter execution of the intervention – which could positively affect confidence, capital accumulation and the propensity to spend – as well from an impact of the

[5] Compared with the projections published on 11 June as part of the Eurosystem staff macroeconomic projections, GDP growth was revised upwards by 0.7 percentage points in 2021, above all owing to the revision of the GDP estimate for the first quarter that was released by Istat on 1 June.

NRRP projects and reforms on potential growth even before the end of the three-year forecasting horizon. The pace of the recovery in economic activity will also depend on how consumption behaviour responds to the re-opening of the economy.

Risks to inflation are balanced. The persistence of ample margins of spare capacity could delay the recovery in wages compared with the projection scenario. Conversely, targeted and lasting support to the economy could translate into a more rapid return of inflation expectations and wage growth in Italy and in the euro area towards levels consistent with the definition of price stability.