# MACROECONOMIC PROJECTIONS FOR THE ITALIAN ECONOMY

## 13 October 2022

This note presents an update to the macroeconomic projections for the Italian economy for the three years 2022-24, which were published in the July Economic Bulletin.[1] This update is based on the data available at 30 September (for the technical assumptions) and at 11 October (for other data).

During the current phase of heightened uncertainty, projections such as those presented here, while reported as point estimates, are merely indicative and depend heavily on the assumptions made concerning changes in the prices and availability of commodities, which are largely dependent on geopolitical developments. This note presents a baseline scenario and a more adverse scenario. The baseline scenario assumes that the flows of gas from Russia to our country will remain at the levels observed in recent months and that commodity prices will be consistent with those inferred from recent futures contracts. In the more adverse scenario, it is assumed that energy supplies from Russia to Europe are completely shut off and that commodity prices are significantly higher, accompanied by a more marked slowdown in world trade and, in the short term, greater uncertainty.

Both scenarios take into account the measures included in the 2022 Budget Law, those adopted since the beginning of the year to counter the effects of rising energy prices, and the use of EU funds under the Next Generation EU programme, based on the latest information relating to the National Recovery and Resilience Plan (NRRP).

In the baseline scenario, the price of oil is around $103 a barrel on average in 2022, just under $80 in 2023 and $74 in 2024. Natural gas prices average about €150 per megawatt hour in 2022, almost €190 in 2023 and just under €120 in 2024 (see the box 'The assumptions').

GDP growth in Italy is projected to equal 3.3 per cent this year, 0.3 per cent in 2023 and 1.4 per cent in 2024 (see the table). A contraction in GDP in the second half of 2022 is expected to be followed by a modest recovery starting in the second quarter of 2023, which is projected to gradually gain momentum thereafter. The weakness in activity in the upcoming quarters will mainly reflect that of household consumption and firms' investment in machinery and equipment, reflecting the impact of high inflation on disposable income, heightened uncertainty and higher borrowing costs. The slowdown in international trade is also expected to play a role.

Compared with the projections published in last July's Economic Bulletin, GDP growth was revised slightly upwards for 2022 and downwards for the two years thereafter, specifically by 1 percentage point for 2023 and 0.3 points for 2024.

Household consumption is expected to contract in the first half of 2023, owing to the impact of the sharp rise in prices on disposable income, to then return to growth in the remainder of the year, thanks to the gradual decline in inflation and uncertainty. Overall, it is projected to fall by 0.4 per cent on average in 2023. Investment in machinery and equipment is expected to slow in the final part of this year and in the early months of the next due mainly to worsening investment conditions and heightened uncertainty and because of higher borrowing costs driven by increased interest rates. These latter will also likely have an impact on investment in construction, which is expected to slow as the building renovation incentives come to an end. Exports, after expanding strongly this year, driven in part by

[1] The projections reported in this note have been prepared by staff members of the Bank of Italy and do not reflect the Eurosystem's assessments.

the recovery in tourism flows, are expected to grow more slowly in the next two years, consistent with the assumption of a deceleration in international trade.

**Table 1– Macroeconomic projections for the Italian economy – baseline scenario**
*(year-on-year percentage changes unless otherwise indicated)*

| | October 2022 | | | | Economic Bulletin (July 2022) | | |
|---|---|---|---|---|---|---|---|
| | **2021** | **2022** | **2023** | **2024** | **2022** | **2023** | **2024** |
| GDP (1) | 6.7 | 3.3 | 0.3 | 1.4 | 3.2 | 1.3 | 1.7 |
| Household consumption | 5.1 | 2.9 | -0.4 | 1.2 | 2.3 | 0.5 | 1.6 |
| Government consumption | 1.5 | -0.4 | 0.2 | -0.4 | -0.6 | 1.3 | 0.4 |
| Gross fixed capital formation | 16.5 | 9.3 | 1.7 | 2.3 | 9.7 | 3.2 | 3.2 |
| *of which:* in capital goods | 12.1 | 6.3 | 2.0 | 3.4 | 6.2 | 3.5 | 5.7 |
| in construction | 21.8 | 12.6 | 1.4 | 1.2 | 13.5 | 2.8 | 0.7 |
| Total exports | 13.5 | 10.5 | 2.7 | 3.3 | 7.7 | 3.5 | 3.6 |
| Total imports | 14.8 | 12.8 | 2.2 | 2.9 | 11.2 | 3.3 | 3.4 |
| Consumer prices (HICP) | 1.9 | 8.5 | 6.5 | 2.3 | 7.8 | 4.0 | 2.0 |
| HICP net of energy and food | 0.8 | 3.2 | 3.1 | 2.5 | 2.9 | 2.1 | 2.1 |
| Household consumption deflator | 1.6 | 7.1 | 5.3 | 2.2 | 7.0 | 4.0 | 2.0 |
| Employment (hours worked) | 8.0 | 4.6 | 0.6 | 0.9 | 4.0 | 1.1 | 1.1 |
| Employment (persons employed) | 0.8 | 2.2 | 0.2 | 0.6 | 2.0 | 0.5 | 0.5 |
| Unemployment rate (2) | 9.5 | 8.1 | 8.3 | 8.3 | 8.3 | 8.1 | 8.0 |

Sources: Based on Bank of Italy and Istat data. The October 2022 update of the macroeconomic projections was prepared by Bank of Italy staff members based on information available at 30 September (for the technical assumptions) and at 11 October (for other data).
(1) For GDP and its components, changes estimated on the basis of quarterly data adjusted for seasonal and calendar effects. – (2) Annual averages, per cent.

In the labour market, the number of hours worked is projected to rise on average at a slightly slower pace than GDP in the two years 2023-24. The number of people employed is expected to rise even more slowly, reflecting a gradual recovery in the intensive margin of labour utilization. The unemployment rate is projected to rise slightly from 8.1 per cent on average in 2022 to 8.3 per cent in the next biennium.

Consumer price inflation, measured based on the change in the Harmonized Index of Consumer Prices (HICP), will likely equal 8.5 per cent on average in 2022, mainly driven by the effects of the strong rises in energy prices, which are reflected both directly and indirectly, through their impact on the other components, in the general price index ; the increase in food prices is also expected to contribute significantly.[2] Following this, a gradual stabilization of energy prices, albeit still high, and an easing of supply bottlenecks are projected to facilitate a gradual reduction in inflation, to 6.5 per cent on average in 2023 and to 2.3 per cent in 2024. For the latter year, the projections suggest that inflation would be

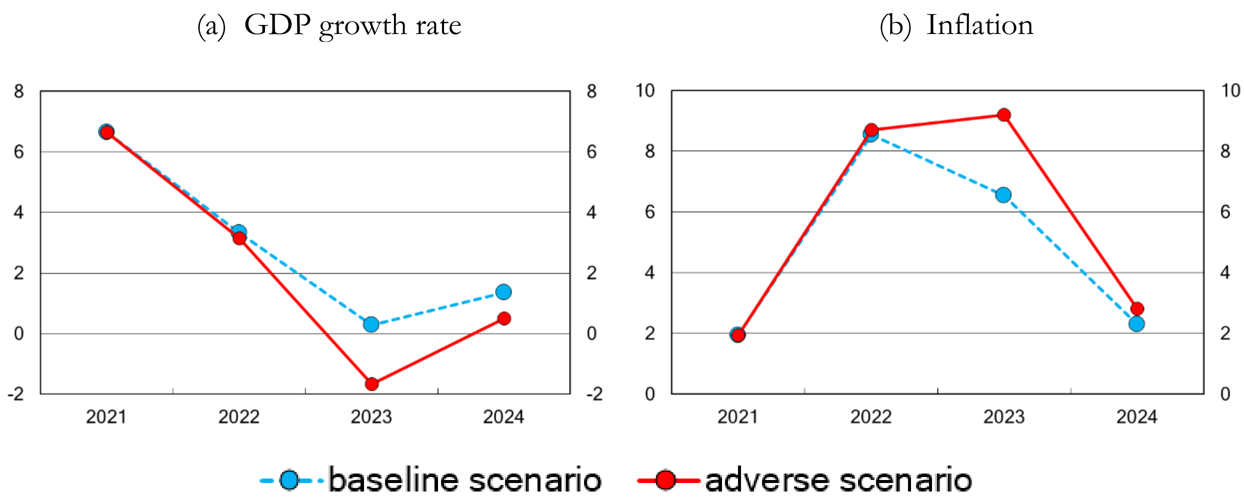
[2]When making comparisons with other projections, it should be remembered that the use of different indices could give rise to non-negligible differences in measuring inflation for this year and the next. Specifically, the national composition of the consumer price index leads for the current year to inflation estimates being about half a percentage point lower than that calculated using the HICP. Inflation measured based on the consumption deflator is more than 1 percentage point lower than that calculated using the HICP, largely because of the contribution of the imputed rents component - not included in the HICP - whose dynamic is very moderate.

driven mainly by the core component, which excludes food and energy. This component is expected to rise by 3.2 per cent on average this year and by 3.1 per cent in 2023 and 2.5 per cent in 2024.

Compared with the July Economic Bulletin, the inflation estimates are more than half a point higher for the current year, 2 points higher for next year and around 0.2 points higher for 2024. The revision reflects to a large extent the dynamic in the energy and food components, but is also affected by an acceleration in the core component, to which rising energy prices are transmitted with a time lag.

The outlook sketched out in the baseline scenario is surrounded by a high level of uncertainty, stemming mainly from the war in Ukraine and its effects on the prices and availability of commodities. In the more adverse alternative scenario, it is assumed that energy supplies from Russia to Europe are permanently shut off starting in the final quarter of this year and are gradually, albeit only partially, replaced with alternative sources next year, in a process that should be completed in 2024; oil and gas prices are projected to rise to around 50 per cent more than contemplated in the baseline scenario. These developments would be accompanied by a further slowdown in world trade and a sharp rise in uncertainty. GDP is expected to grow by 3 per cent this year and fall by more than 1.5 per cent in 2023, to then rise again moderately starting in 2024 (see the figure). Consumer price inflation, slightly higher this year compared with the baseline scenario, is projected to continue to rise next year too, to over 9 per cent, and then fall sharply in 2024.

**Figure - Baseline scenario and adverse scenario**
*(per cent)*




## THE ASSUMPTIONS

The underlying assumptions follow the methodology used in the Eurosystem staff macroeconomic projection exercises (see *A guide to the Eurosystem/ECB staff macroeconomic projection exercises*, available at https://www.ecb.europa.eu/pub/pdf/other/staffprojectionsguide201607.en.pdf). The technical assumptions for exchange rates, commodity prices and interest rates reflect the developments implied by the average market prices as at 30 September.

The scenario incorporates the measures included in the 2022 Budget Law, those adopted since the beginning of the year to counter the effects of rising energy prices, and the use of EU funds under the Next Generation EU programme, based on the latest data relating to the NRRP.

**Assumptions for the main exogenous variables in the baseline scenario**

| | | 2021 | 2022 | 2023 | 2024 |
|---|---|---|---|---|---|
| Weighted foreign demand | (1) | 9.6 | 4.6 | 2.4 | 3.4 |
| Dollar/Euro | (2) | 1.18 | 1.04 | 0.98 | 0.98 |
| Nominal effective exchange rate | (1), (3) | -0.8 | 2.7 | 1.1 | 0.0 |
| Prices of foreign manufactures | (1) | 5.7 | 9.8 | 3.3 | 1.9 |
| Crude oil prices | (4) | 70.7 | 102.9 | 79.7 | 74.2 |
| Natural gas prices | (5) | 47.1 | 149.9 | 187.2 | 118.0 |
| 3-month Euribor | (2) | -0.5 | 0.4 | 3.0 | 3.0 |
| Interest rate (10-year BTPs) | (2) | 0.8 | 3.1 | 4.3 | 4.5 |

(1) Percentage changes. – (2) Annual averages. – (3) Positive changes indicate a depreciation. – (4) Dollars per barrel of Brent crude oil. – (5) Euros per Megawatt hour.