2.10 PROJECTIONS

The projections for the Italian economy presented here update those prepared as part of the Eurosystem staff macroeconomic projections published on 17 December.[1] GDP growth in Italy is estimated at 3.8 per cent on average in 2022, 2.5 per cent in 2023 and 1.7 per cent in 2024. Inflation is projected to reach 3.5 per cent this year, primarily owing to the impact of rising energy prices, and 1.6 per cent on average in the two years 2023-24.

The recovery continues, despite the rise in the number of cases ...

The scenario presented here is based on the assumption that new COVID-19 cases peak in the first quarter of the year, without translating into a severe tightening of restrictions but with negative effects on mobility and consumption patterns in the short term. The spread of the epidemic is expected to lose momentum from the spring onwards, thanks to further progress in the vaccination campaign.

... supported by favourable financial conditions ...

The scenario further assumes that monetary and financial conditions remain favourable, notwithstanding a slight increase in nominal interest rates over the forecasting horizon. Based on the expectations that can be inferred from market prices in the ten days ending on 17 January, it is estimated that the yields on ten-year Italian government bonds will rise from 1.4 per cent on average this year to 1.9 per cent in 2024. Credit supply conditions are expected to stay relaxed: the cost of borrowing for firms is estimated at 1.4 per cent in 2022 and is projected to rise in the subsequent two years, while remaining at low levels by historical standards.

... and by the expansion in world trade

Finally, the projections are based on the assumption that world trade will continue to recover, after a temporary slump owing to the frictions in global value chains, which are expected to dissipate in the course of this year (see Section 1.1 and the box 'Supply chain bottlenecks: the impact on the global economy', Chapter 1). After a marked rebound in 2021, foreign demand for Italian products weighted by outlet markets is projected to expand by an average of 4.5 per cent each year over the forecasting period (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 by the European Central Bank.[1] The macroeconomic projections for Italy presented here update those released on 17 December and are based on the information available at 17 January.

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

a) foreign demand, weighted by the outlet markets for Italian exports, slows to 4.5 per cent on average in the three years 2022-24;

[1] For further information, 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', 17 December 2021.

b) the euro/dollar exchange rate, equal to 1.18 on average in 2021, falls to 1.14 in the three years 2022-24;[2]

c) the price of a barrel of Brent crude oil, based on the prices of futures contracts, rises to about $80 in 2022 (from $71 in 2021), and falls in the subsequent two years, reaching $70 in 2024; the projections take account of the administrative measures to limit increases in gas and electricity tariffs taken by the Italian Regulatory Authority for Energy, Networks and the Environment;

d) the three-month interest rate on the interbank market (EURIBOR), is equal to -0.4 per cent this year and rises to 0.1 per cent on average in the next two years;

Table

Assumptions for the main exogenous variables

	2021	2022	2023	2024
Potential foreign demand (1)	8.6	4.8	5.4	3.5
Dollar/euro (2)	1.18	1.14	1.14	1.14
Nominal effective exchange rate (1) (3)	-0.8	1.2	0.0	0.0
Crude oil prices (2) (4)	70.8	80.2	74.0	70.2
3-month Euribor (2)	-0.5	-0.4	0.0	0.2
1-year BOTs (2)	-0.5	-0.3	0.1	0.3
10-year BTPs (2)	0.8	1.4	1.7	1.9

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.

e) the yield on ten-year BTPs, equal to 1.4 per cent on average in 2022 (0.8 per cent in 2021), increases gradually to 1.9 per cent in 2024, in line with the values of forward rates implied by the term structure of interest rates on government bond yields;

f) the scenario incorporates the measures in the budget law for the three years 2022-24 and the information available on the implementation of the National Recovery and Resilience Plan (NRRP).

These assumptions are similar to those underpinning the projections released on 17 December. The most significant difference is linked to the gas and electricity tariffs in force since the first quarter of 2022, which have risen by 41.8 and 55 per cent, respectively. Small revisions have also been made to the interest rate projections, which are slightly higher for the next two years.

[2] The technical assumptions for interest rates, the exchange rate and oil prices are calculated based on the spot and forward prices observed in the markets in the ten working days ending on 17 January.

GDP is projected to rise sharply from the spring onwards

After weaker growth in the final part of 2021 (see the box 'Economic activity in the fourth quarter of 2021'), which is expected to continue in the early months of this year, it is estimated that GDP will return to steady growth from the spring, in concomitance with the anticipated improvement in the outlook for public health, regaining pre-pandemic levels sometime in mid-2022. The expansion in activity should then continue at a robust pace, though less markedly compared with the strong recovery that followed the reopenings in mid-2021. GDP is expected to increase by an annual average of 3.8 per cent in 2022, 2.5 per cent in 2023 and 1.7 per cent in 2024 (Table 18; Figure 50).

Fiscal policy support for growth in the three years will be substantial

In the scenario outlined here, considerable support for growth should come from the stimulus measures financed by the national budget and by European funds, especially those envisaged in the National Recovery and Resilience Plan (NRRP). In the projections, the measures introduced in 2021 and planned for the coming years, including those in the budget law for the three-years 2022-24, are expected to contribute about 5 percentage points in total to GDP over the four years 2021-24. A little less than half of this contribution is attributable to interventions under the NRRP, on the assumption that they are carried out effectively and without significant delays.

Table 18

Macroeconomic scenario

(percentage change on previous year unless otherwise indicated)

	2021	2022	2023	2024
GDP (1)	6.3	3.8	2.5	1.7
Household consumption	5.1	4.4	2.2	1.5
Government consumption	1.2	1.2	0.2	-0.5
Gross fixed investment	15.7	5.3	5.9	3.5
of which: in capital goods	11.4	7.2	6.9	5.3
Total exports	12.4	4.8	6.0	3.5
Total imports	12.7	5.1	6.3	3.4
Change in stocks (2)	0.0	-0.1	0.0	0.0
Memorandum item: GDP, raw data (3)	6.3	3.7	2.4	1.8
Prices (HICP)	1.9	3.5	1.6	1.7
HICP net of food and energy	0.8	1.0	1.4	1.6
GDP deflator	1.1	2.5	1.5	1.8
Employment (hours worked)	7.0	3.4	1.9	1.4
Employment (persons employed)	0.5	1.7	0.9	1.0
Unemployment rate (4)	9.4	9.0	8.9	8.7
Export competitiveness (5)	0.8	2.5	0.0	-0.2
Current account balance of the balance of payments (6)	3.8	3.1	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.

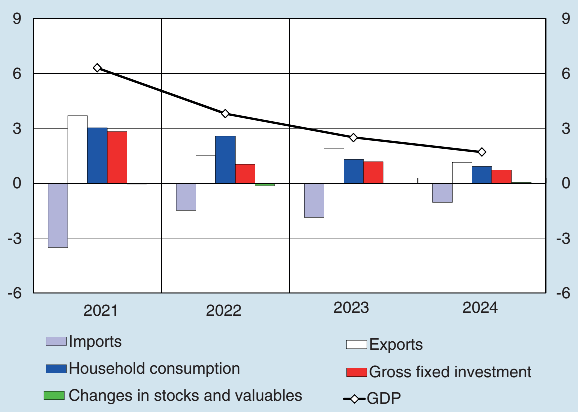
The number of persons employed will regain pre-pandemic levels by the end of this year

In the three years 2022-24, employment is expected to continue to expand, returning to pre-pandemic levels at the end of this year, both in terms of the number of persons employed and that of hours worked. The unemployment rate is projected to fall from 9.4 per cent on average in 2021 to 8.7 per cent in 2024.

Figure 50

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.

Consumption expenditure will continue to expand, despite the rise in the number of infections

While consumption is expected to continue to recover at a fast pace, its return to pre-pandemic levels is expected with a lag of around one year compared with that of GDP. In the early part of 2022, it is likely to be slowed by the ongoing caution in spending patterns, due to the course of the pandemic, and the impact of higher energy prices, which compresses the purchasing power of households. It is projected to return to rapid growth from the spring onwards, thanks to the improvement in the public health outlook, the gradual normalization of energy prices and the continued recovery in employment. Household expenditure is projected to grow by 4.4 per cent on average in 2022 before slowing to around 2 per cent in the following two years. The household saving rate, which rose to 15.6 per cent in 2020 (from 8.0 per cent in 2019), should fall gradually, returning to pre-crisis levels in 2024 (Figure 51).

Investment will continue to record vigorous growth ...

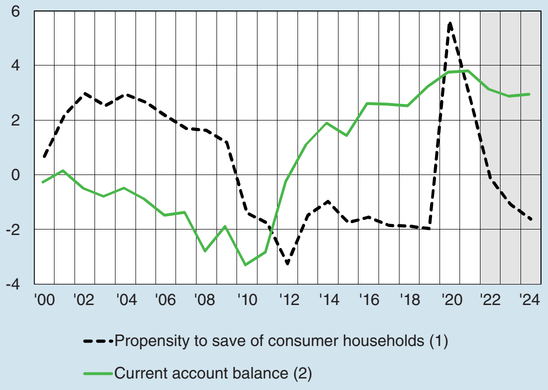
Capital formation, which already in the first quarter of 2021 had surpassed the average levels recorded in 2019, thanks above all to the marked expansion in the construction component, will continue to expand at a fast pace over the forecasting horizon. It is expected to benefit from the improvement in the growth outlook, favourable financing conditions and the funds to support public and private investments envisaged in the NRRP and the budget law. In the three years 2022-24, investment is projected to expand by almost 5 per cent on average each year, driven primarily by the machinery, equipment, and transport equipment component. The ratio of total investment to GDP should record a significant increase, reaching around 21 per cent in 2024 (just below the peak of 2007). For the construction sector, in 2024, the ratio is expected to remain a little over 9 per cent, still 2.5 percentage points below the highest levels recorded in 2007 (Figure 52).

... as will exports, in part thanks to the recovery of tourism

Foreign sales will continue to expand, thanks to the improvement in world trade and to competitiveness gains; services also look set to benefit from the recovery in international tourism flows. Exports are projected to grow by a little under 5 per cent on average in each of the three years 2022-24, a little more than foreign demand. Imports will expand at a slightly faster pace, driven by the performance of demand components with a high import content (exports and investment in capital goods). The current account surplus of the balance of payments, equal to 3.8 per cent in 2021, is projected to fall to 3.0 per cent on average in the three years 2022-24 (Figure 51).

Figure 51

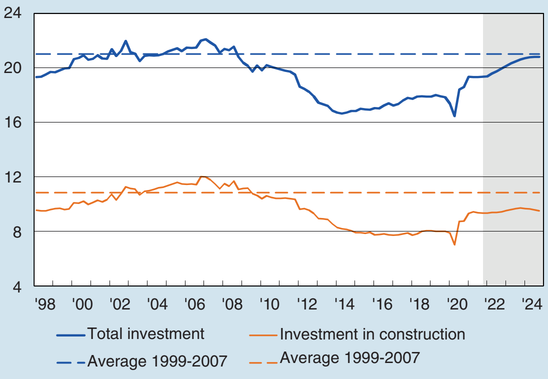
Propensity to save of consumer households and current account balance
(annual data; percentage points)



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

Figure 52

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



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

Inflation will moderate in the next two years

Consumer price inflation is expected to reach 3.5 per cent this year, mostly owing to the impact of higher energy prices and in particular of the unprecedented hikes in gas and electricity tariffs; however, these effects should moderate gradually over the course of 2022 and disappear entirely towards the end of the year. Inflation is projected to fall to 1.6 per cent on average in 2023, and to rise to 1.7 per cent in 2024 (Figure 53). The core component, equal to 1.0 per cent this year, is set to rise gradually, reaching 1.6 per cent at the end of the forecasting horizon, driven by the reduction in spare capacity margins and wage developments. Private sector wages, which rose by 0.8 per cent in 2021, are projected to accelerate gradually, to 1.3 per cent this year and to 1.8 per cent in both 2023 and 2024: this reflects the assumption that the current upward trend in price dynamics will have a limited bearing on the measures of inflation considered as the benchmark for future contractual renewals. Domestic inflation, measured by the change in the GDP deflator, equal to 1.1 per cent in 2021, is expected to rise to 2.5 per cent this year and to then come down to around 1.6 per cent in the two years 2023-24.

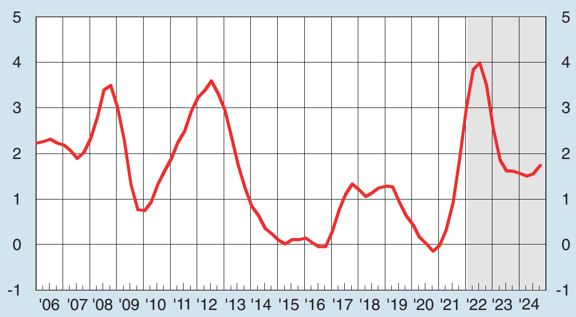
Compared with the July estimates, inflation has been revised upwards

Compared with the projections published in last July's *Economic Bulletin*, GDP growth is 1.2 percentage points higher in 2021, 0.6 points lower in 2022 and 0.2 points higher in 2023. The marked revision for 2021 is due to the higher than expected growth in GDP in the central part of the year.[2] The downward revision for 2022 mostly reflects the weaker performance of GDP in the winter months, due to the deterioration in the public health situation. The inflation profile has been revised upwards by 0.4 percentage points in 2021 and by 2.2 points in 2022, owing to the updating of data on energy commodity prices and assumptions regarding their future course, and by 0.3 points in 2023, mostly reflecting trends in core inflation.[3]

The growth projections for 2022 are below those released recently by the other main forecasters, made before the pandemic took another turn for the worse; for 2023, they are higher than those released in October by the International Monetary Fund and basically aligned with those of the other private and institutional forecasters (Table 19). Our inflation estimates are higher for 2022, insofar as they incorporate the higher prices of energy goods recorded in recent weeks and are aligned with those of the other forecasters for 2023.

Figure 53

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.

Table 19

Comparison with other organizations' forecasts for Italy
(percentage changes on previous year)

	GDP (1)		Inflation (2)	
	2022	2023	2022	2023
IMF (October)	4.2	1.6	1.8	1.2
OECD (December)	4.6	2.6	2.2	1.6
European Commission (November)	4.3	2.3	2.1	1.4
Consensus Economics (January)	4.2	2.2	2.7	1.3
Memorandum item: Bank of Italy (January)	3.8	2.5	3.5	1.6

Sources: IMF, *World Economic Outlook*, October 2021; OECD, *OECD Economic Outlook*, December 2021; European Commission, *European Economic Forecast. Autumn 2021*, November 2021; Consensus Economics, *Consensus Forecasts*, January 2022. Bank of Italy, *Economic Bulletin*, 1, 2022.
(1) The growth rate forecasts of the OECD are adjusted for calendar effects; those of the European Commission and IMF are not. – (2) HICP.

2 This revision had already been anticipated in last October's *Economic Bulletin*, which had projected growth of around 6 per cent.

3 Compared with the projections published on 17 December 2021, as part of the Eurosystem staff macroeconomic projections, the growth estimate is slightly lower in 2022 (by 0.2 percentage points); the revision mostly reflects the effect of the recent sharp rise in cases of COVID-19 that are estimated to have impacted mobility and consumption patterns in the early months of the year. The inflation estimates for 2022 are 0.7 points higher and basically unchanged for the subsequent two years; the revision is almost wholly attributable to the increase in gas and electricity tariffs announced by the Italian Regulatory Authority for Energy, Networks and the Environment for the first quarter of the year.

Considerable uncertainty remains, with downside risks to growth …

The growth projections are subject to multiple risks, mostly on the downside. In the short term, uncertainty is linked to the public health situation, any deterioration in which could lead to restrictions on mobility and impact consumer and business confidence to a greater extent than is currently incorporated in the estimates, further hindering the economic recovery. Risk factors are also linked to the possibility that tensions on the supply side become more persistent and are transmitted to the real economy to a greater extent, as well as to the eventuality of a more prolonged weakening of world trade. In the medium term, the projections are still conditioned by the full implementation of the spending programmes in the budget and the complete and timely realization of the interventions envisaged in the NRRP.

… and more balanced risks to inflation

In the short term, growth in prices could be higher than projected if energy prices remain at high levels for longer than assumed here and if tensions around supply were to lead to more persistent increases in the prices of intermediate goods. Over the longer term, another upside risk factor is the possibility of recent inflationary pressures being transmitted to a greater extent to medium term inflation expectations and wage growth. In the opposite direction, the materialization of the downside risk factors to the outlook for economic growth could lead to lower inflation.