## 2.10 PROJECTIONS

*The projections for the Italian economy presented here update – in light of the latest cyclical indicators – those prepared as part of the Eurosystem staff macroeconomic projections published on 16 December 2022.*[1] *In the baseline scenario, following growth of almost 4 per cent in 2022, GDP is projected to slow down over the next three years, with a 0.6-per cent uptick this year and a 1.2-per cent expansion in both 2024 and 2025. Inflation, which rose to almost 9 per cent on average in 2022, is projected to decline to 6.5 per cent this year and more strongly thereafter, to 2 per cent in 2025. The projections, though presented as point estimates, continue to be purely indicative, given the current exceptional uncertainty.*

**The macroeconomic outlook depends on how the conflict in Ukraine unfolds**

The war in Ukraine continues to be a major cause of instability for the macroeconomic outlook. In this baseline scenario, the tensions associated with the conflict are assumed to remain high in the first few months of this year, before easing gradually over the projection horizon. In an alternative scenario, we assess the economic repercussions of more adverse developments, associated with a permanent shutdown of Russian energy supplies.

In the assumptions underlying the baseline scenario, energy prices remain relatively high in 2023 and gradually abate in the following two years (see the box 'The assumptions underlying the macroeconomic scenario'). World trade slows down significantly this year, due to the impact of high inflation and of the uncertainty associated with the conflict in Ukraine on global economic activity, and picks up again in 2024-25. We assume nominal interest rates will move in line with market expectations, increasing further this year and stabilizing over the next two years.

### THE ASSUMPTIONS UNDERLYING THE MACROECONOMIC SCENARIO

The projections for the Italian economy presented here update those prepared as part of the Eurosystem staff macroeconomic projection exercise, published on 16 December 2022, and are based on the information available as at 13 January 2023.

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

a) following a 6.5 per cent increase in 2022, foreign demand, weighted by the outlet markets for Italian exports, slows down to 2 per cent in 2023; it expands by just over 3 per cent on average in the two years 2024-25;

b) the euro/dollar exchange rate, equal to 1.05 on average in 2022, stands at 1.06 this year and in 2024-25;

c) the price of a barrel of Brent crude oil, based on the prices of futures contracts, inches down over the forecast horizon to $73 in 2025 (from $102 in 2022); the gas price is around €77.5 per megawatt hour on average this year, down sharply from 2022, and gradually declines to €59 in 2025;

d) the three-month interest rate on the interbank market (Euribor), equal to 0.4 per cent in 2022, rises to 3.4 per cent in 2023 and edges down to 2.8 per cent on average over the next two years;

[1] For more information, see the Bank of Italy's website: 'Macroeconomic projections for the Italian economy (Eurosystem staff macroeconomic projections)', 16 December 2022.

e) the yield on ten-year BTPs rises to 4.7 per cent in 2025 (3.1 per cent in 2022), in line with the values of forward rates implied by the term structure of interest rates on government securities;

f) this scenario incorporates the provisions laid down in the Budget Law for the three years 2023-25 (see Section 2.9) and the information available on the implementation of the National Recovery and Resilience Plan (NRRP).

Table

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

| | 2022 | 2023 | 2024 | 2025 |
|---|---|---|---|---|
| Potential foreign demand (1) | 6.5 | 2.0 | 3.1 | 3.2 |
| Dollar/euro (2) | 1.05 | 1.06 | 1.06 | 1.06 |
| Nominal effective exchange rate (1) (3) | 1.7 | -0.6 | 0.0 | 0.0 |
| Crude oil prices (2) (4) | 101.7 | 80.7 | 76.8 | 73.5 |
| Natural gas prices (2) (5) | 130.4 | 77.5 | 74.1 | 59.3 |
| 3-month Euribor (2) | 0.4 | 3.4 | 3.0 | 2.6 |
| 1-year BOT yields (2) | 0.9 | 3.4 | 2.9 | 2.7 |
| 10-year BTP yields (2) | 3.1 | 4.4 | 4.6 | 4.7 |

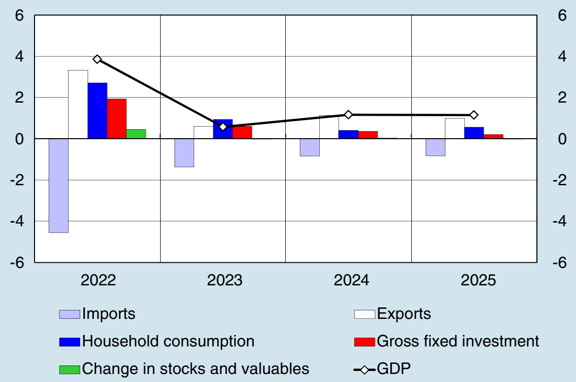
Sources: Based on Bank of Italy and Istat data.
(1) Percentage changes. – (2) Annual averages. – (3) Positive changes indicate a depreciation. – (4) Dollars per barrel of Brent crude oil. – (5) Euros per megawatt hour.

**GDP is projected to slow down this year, with growth to gain momentum over the next two years**

Economic activity, which was supported by robust consumption and investment growth for most of 2022, appears to have weakened in the last few months of the year (see Section 2.1). GDP growth should remain weak in the current quarter, before gradually picking up from the spring onwards; growth is projected to gain momentum from 2024, as inflationary pressures and uncertainty abate. GDP is expected to increase by an annual average of 0.6 per cent in 2023 and by 1.2 per cent in both 2024 and 2025 (Table 12; Figure 39).

Figure 39

**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.

**Inflation is projected to remain high in 2023 and to fall sharply in the following two years**

HICP inflation, which stood at 8.7 per cent in 2022, is projected to average 6.5 per cent this year, before declining more markedly, to 2.6 per cent in 2024 and 2.0 per cent in 2025 (Figure 40). This decline is highly dependent on the assumption of a gradual decrease in commodity prices, whose effects should only partially be offset by higher wage growth. Core inflation is projected to rise further to 3.8 per cent in 2023 and to fall close to 2 per cent in 2025. This trend reflects relatively strong growth in actual wages

Table 12

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

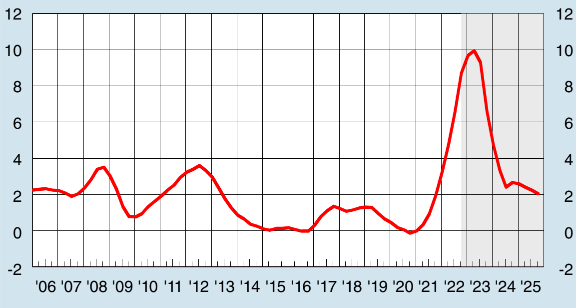
| | 2022 | 2023 | 2024 | 2025 |
|---|---|---|---|---|
| GDP (1) | 3.9 | 0.6 | 1.2 | 1.2 |
| Household consumption | 4.6 | 1.6 | 0.7 | 0.9 |
| Government consumption | 0.0 | -1.0 | 0.4 | 1.3 |
| Gross fixed investment | 9.6 | 2.9 | 1.6 | 1.0 |
| *of which:* in capital goods | 8.4 | 3.1 | 3.1 | 2.3 |
| Total exports | 10.4 | 1.8 | 3.3 | 2.8 |
| Total imports | 15.2 | 4.1 | 2.4 | 2.4 |
| Change in stocks (2) | 0.5 | 0.0 | 0.0 | 0.0 |
| *Memorandum item:* GDP, raw data (3) | 3.8 | 0.5 | 1.4 | 1.1 |
| Prices (HICP) | 8.7 | 6.5 | 2.6 | 2.0 |
| HICP net of food and energy | 3.3 | 3.8 | 2.6 | 2.2 |
| GDP deflator | 2.2 | 4.1 | 3.4 | 4.2 |
| Employment (hours worked) | 4.2 | 0.5 | 0.6 | 0.8 |
| Employment (headcount) | 2.2 | 0.4 | 0.5 | 0.7 |
| Unemployment rate (4) | 8.2 | 8.2 | 7.9 | 7.6 |
| Export competitiveness (5) | 2.7 | -2.2 | -1.6 | -0.2 |
| Current account balance of payments (6) | -0.9 | -1.2 | 0.5 | 1.6 |

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 (negative) value indicates a gain (loss) in competitiveness. – (6) Per cent of GDP.

in the private sector over the three-year forecast period, which in our assumptions should be supported by shorter delays than in the past in collective bargaining agreement renewals and by a narrowing gap between actual inflation and the benchmark inflation rate used for previous agreements. The GDP deflator is projected to grow at rates slightly below 4 per cent, on average, driven by rising labour costs and a partial recovery in profit margins.

Figure 40

**Consumer price inflation** (1)
*(quarterly data; year-on-year percentage changes; 4-term moving averages)*




Sources: Based on Bank of Italy and Istat data.
(1) HICP. The shaded area shows forecast data.

**Employment is expected to continue to gradually increase**

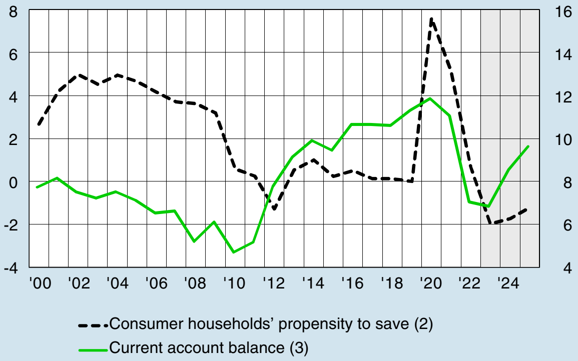
Hours worked are expected to continue to expand over the three-year period, at a slower pace than GDP. Headcount employment is projected to grow at even lower rates over the horizon, reflecting the gradual recovery in the intensive margin of labour supply. The unemployment rate is forecast to decline slightly over the three-year period.

**Consumption growth is likely hindered by inflation**

Household consumption – which reflected a return to pre-pandemic spending habits in 2022 – is expected to be more strongly affected by high inflation and flagging confidence this year. On average, consumption is projected to grow by approximately 1.5 per cent in 2023, mainly in the wake of strong growth in the previous year, and to slow down to just below 1 per cent on average in 2024-25. The saving rate, which fell to 7.1 per cent in the third quarter of 2022, is expected to decline further this year and recover only partially in the following two years (Figure 41).

Figure 41

**Propensity to save of consumer households and current account balance** (1)
*(annual data; percentage points)*



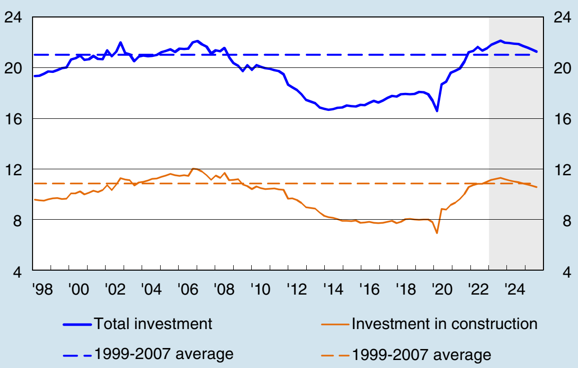

Sources: Based on Bank of Italy and Istat data.
(1) The shaded area shows forecast data. – (2) Right-hand scale. – (3) Per cent of GDP.

**Investment is poised for moderate growth**

Investment is projected to grow by almost 2 per cent on average over the three years 2023-25. The capital goods component is likely to be dampened by the worsening demand outlook and heightened uncertainty, especially in the early part of the forecast horizon. Thereafter, it will probably be affected by the higher funding costs associated with the rebound in interest rates, but these effects should be partially offset by fading uncertainty. Construction spending should continue to be supported by stimulus measures for most of this year, only to slow down later, partly on account of the increased cost of borrowing. NRRP funds should strongly support capital accumulation, mainly through a sharp increase in public investment. Overall, the total investment-to-GDP ratio is projected to stand above 20 per cent, just below its twenty-year highs (Figure 42).

Figure 42

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




Sources: Based on Bank of Italy and Istat data.
(1) Data seasonally and calendar adjusted. The shaded area shows forecast data.

**The deterioration in the energy balance is expected to weigh on the current account balance this year too**

Exports, which grew strongly in 2022 also thanks to the normalization of international tourism flows, are projected to slow down markedly this year, to below 2 per cent. Export growth should pick up again more strongly over the next two years, in line with foreign demand for Italian goods and services. Imports will likely expand at a similar pace, driven by the demand components with a high import content (exports and investment in capital goods). The sizeable energy deficit is expected to weigh on the current account balance of payments, which should remain negative this year.

**Growth projections are revised slightly down for 2024, inflation forecasts are revised upwards**

Compared with the scenario outlined in the October 2022 *Economic Bulletin*, growth projections for 2023 have been revised slightly upwards, due to the carryover effects of the trends observed in 2022. By contrast, the 2024 GDP growth estimate has been revised slightly downwards on account of lower consumption growth. Inflation estimates have been revised upwards by three tenths of a percentage point for 2024, incorporating the assumption of stronger wage increases.

Compared with those of the other leading forecasters, our projections for economic activity are slightly more favourable for 2023 and in line for 2024 (Table 13). Inflation estimates for the current year are comparable to those of other private and institutional forecasters. For 2024, they are higher than those of the European Commission and lower than those of the OECD.

Table 13

**Comparison with other organizations' forecasts for Italy**
*(percentage change on previous period)*

| | GDP (1) | | Inflation (2) | |
|---|---|---|---|---|
| | 2023 | 2024 | 2023 | 2024 |
| IMF (October) | -0.2 | 1.3 | 5.2 | 1.7 |
| OECD (November) | 0.2 | 1.0 | 6.5 | 3.0 |
| European Commission (November) | 0.3 | 1.1 | 6.6 | 2.3 |
| Consensus Economics (January) | 0.0 | 1.1 | 6.6 | 2.2 |
| *Memorandum item:* | | | | |
| Bank of Italy (October) | 0.3 | 1.4 | 6.5 | 2.3 |
| Bank of Italy (January) | 0.6 | 1.2 | 6.5 | 2.6 |

Sources: IMF, *World Economic Outlook*, October 2022; OECD, *OECD Economic Outlook*, November 2022; European Commission, European Economic Forecast. *Autumn 2022*, November 2022; Consensus Economics, *Consensus Forecasts*, January 2023; Banca d'Italia, *Economic Bulletin*, 4, 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. Forecasts of Consensus Economics refer to the consumer price index for the entire resident population.

**The risks to growth are on the downside while inflation risks are more balanced**

The projections presented under the baseline scenario are still surrounded by exceptionally high uncertainty, associated with developments in prices and in the availability of commodities, which are largely affected by the course of the conflict in Ukraine, trends in international trade and the repercussions of global monetary tightening. Overall, the risks to growth are skewed to the downside. The risks to inflation, on the other hand, are more balanced, as short-term upside risks essentially stemming from potential new energy price increases are offset by downside risks associated with a stronger and sustained deterioration in aggregate demand, particularly over the medium term.

**If energy supply from Russia were to shut down, GDP would likely fall and inflation would rise further**

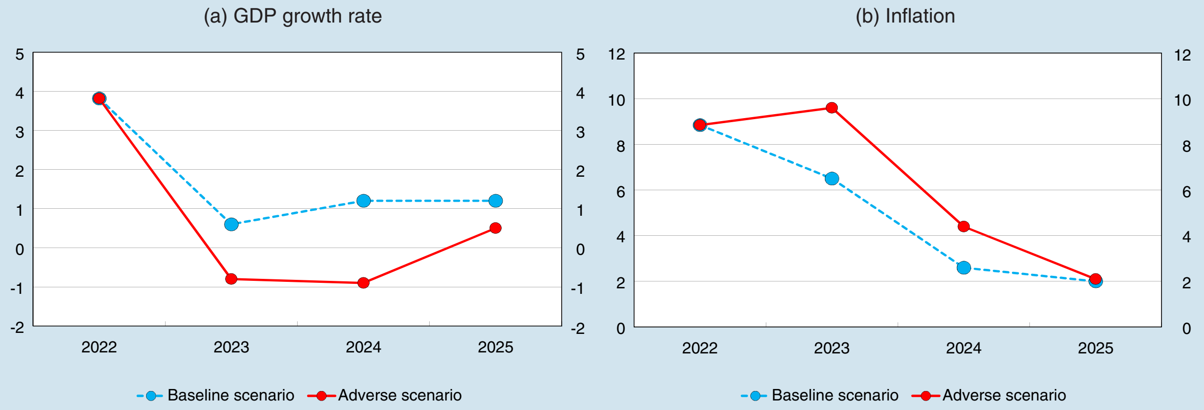
In a highly adverse scenario, we assess the consequences for our economy of a permanent disruption in European energy imports from Russia. A lower supply of natural gas on European markets would primarily result in a sharp increase in energy prices, associated with heightened uncertainty and significant weakness in global trade. In Italy, energy rationing for industrial use would be limited due to the high level of stocks, energy savings and the further gradual replacement of imports from Russia with other sources. These developments will likely result in slower economic activity and tighter financing conditions owing to the deterioration in credit quality. Under this scenario, GDP would fall by almost 1 per cent in both 2023 and 2024, and grow moderately in the following year (Figure 43.a). Consumer price inflation is forecast to rise further to close to 10 per cent this year, before declining to just above 4 per cent in 2024 and dropping towards 2 per cent in 2025 (Figure 43.b), when the direct and indirect impact of higher energy prices would be offset by the contrary effect of worsening cyclical conditions, which would weigh on price developments more persistently.

This scenario does not take into account any measures that may be introduced to mitigate the effects of more adverse developments. Nor does it take into account the possibility that, as a result of

Figure 43

**Baseline scenario and adverse scenario**

*(percentage changes)*




Sources: Based on Bank of Italy and Istat data.

significant weakness in economic activity and the labour market, wage adjustments for stronger consumer price growth will be smaller than expected based on past trends, helping to determine a lower level of inflation at the end of the forecast horizon.