Summary[*]

The international context is fragile and unstable due to various conflicts on the EU's doorstep, as well as geopolitical tensions and trade wars. Lately the energy commodity markets have not experienced large fluctuations, but remain very volatile. The global economy is fragmented, the cyclical phase is stronger in the US than in Europe, held back by the stalemate in Germany. The International Monetary Fund (IMF) continues to foresee a marked acceleration in world trade this year, which however requires a quick recovery in elasticity to economic activity. Central banks of major countries have embarked on a path of easing monetary conditions; the next steps will depend on the development of prices and other economic indicators.

In recent quarters, Italian economy has recorded rates of change of a few tenths of a point, similar to those of the Euro area. In spring, our country's GDP grew by 0.2 per cent, driven by consumption (private and public) and inventories, while net foreign demand had a negative impact. Inflation fell below one percentage point in September and remains well below that of the euro area. Permanent employment continues to rise, the unemployment rate falls and real wages begin to recover some of the loss in purchasing power accumulated over the past two years.

The available timely economic indicators do not agree on a clear development of the cyclical phase. Based on the models of the Parliamentary Budget Office (PBO), GDP would have increased moderately in the third quarter, but there is also a non-negligible likelihood that it has essentially stagnated; activity remains held back by the weakness of the manufacturing sector. In 2024, the GDP would increase by 0.8 per cent, two-tenths of a point less than forecasted by the PBO at the time of the validation exercise of the Structural Budgetary Plan (MTFSP) forecasts; the revision is attributable to the worsening of the carry-over for 2024 from the quarterly data recently published by Istat.

Overall, the forecast risks are tilted to the downside. In the short term, the persistent weakness of industry and uncertainty about the outlook for the construction industry weigh heavily. For the coming years, the risks are mainly attributable to the economic fallout of the ongoing wars, as well as to the advancement of the works envisaged in the National Recovery and Resilience Plan (NRRP).

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[*] *Edited by the Macroeconomic Analysis Department, with co-ordination by Libero Monteforte and contributions by Giacomo Caterini, Daniela Fantozzi, Marco Fioramanti, Cecilia Frale, Alessandro Girardi and Carmine Pappalardo; note completed with information available as of 22 October 2024.*

The international context

The world economic outlook

The prolonged conflict in Ukraine and the widening clashes in the Middle East make the international environment more unstable than a few months ago, increasing risk factors and uncertainty about the global economic outlook. Repercussions are already evident in the volatility of oil and other commodity prices. The unstable international environment makes the actions of governments more uncertain, as also shown by the Economic Policy Uncertainty Index (EPU Index - Figure 1);[2] the indicator shows that in Europe there is more uncertainty about what institutions will do than the global average and the United States. The gap between the two areas widened starting in 2022 when the war in Ukraine broke out, and continued until recent months, when the Euro area index rose.

According to the latest estimates, the second half of 2024 will be characterised by a temporary interruption in the downward phase of inflation; for the Euro area, the latest forecasts of the European Central Bank (ECB) foresee a strengthening of price dynamics in the fourth quarter, still due to base effects on energy components. However, even in the core inflation, the downward trend in the headline inflation rate is confirmed in the medium term. Therefore, on October 17 the ECB Governing Council decided a further cut in key interest rates by 25 basis points (from 3.5 to 3.25 percent for deposit rate); this is the third consecutive cut, as expected by market analysts. Overseas, on September 18 the FED cut official interest rates by 50 basis points, ushering in monetary easing after the tightening of recent years. In the US, the labour market remains robust, financial markets welcomed the rate cut and expectations are for further easing by the end of 2024.

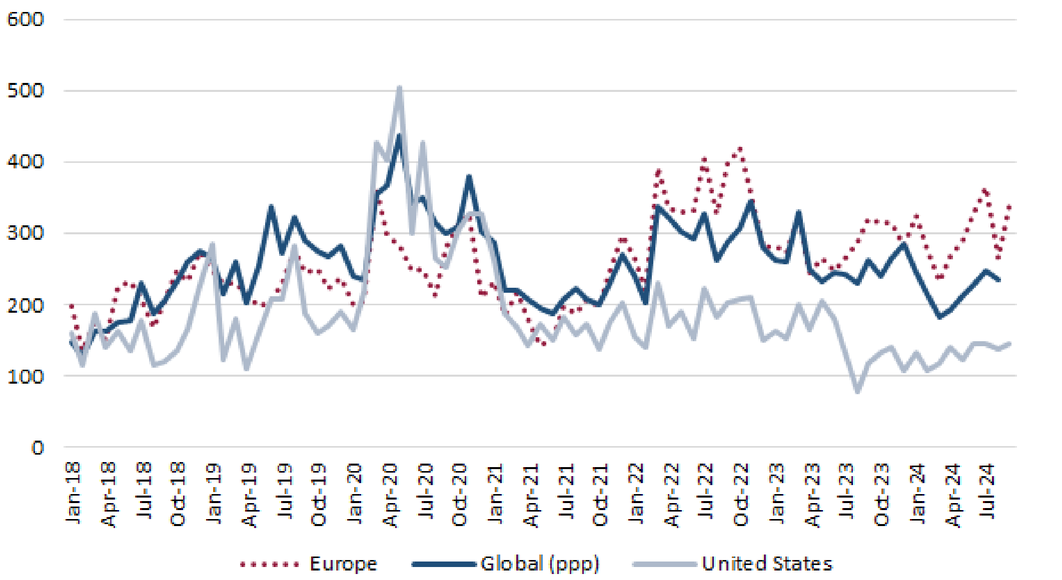
The short-term outlook is cautious. The Purchasing Managers' Index, the global PMI, showed a slight decline in the third quarter of the year, with the manufacturing component worsening, more than offsetting the weak recovery of the services component. Order backlogs showed stability in the first three quarters of the year, however below the 50 threshold, a symptom of a still weak external demand (Figure 2).

High-frequency indicators on global trade show a decline in the cost of transporting non-liquid commodities and foodstuffs in August, as measured by the Baltic Dry Index. The cuts reflect the weak international demand and the strong competition among exporters. International trade suffered from a sharp setback last year and now is slowly recovering, according to data from the Central Plan Bureau; in July, flows decreased slightly compared to the previous month (-0.3 percent), but the trend compared to the first half of 2023 is one of moderate growth (Figure 3). The cost of agricultural commodities has weakened

[2] The Economic Policy Uncertainty Index (EPU) is a monthly index edited by S. R. Baker, N. Bloom, S.J. Davis, and based on words derived from "uncertain" and "uncertainty" extrapolated from major newspapers by Country. The index is obtained by weighting the average between news volumes and other information. The global index is a monthly weighted average across major Countries. For more information on methodology, see https://www.policyuncertainty.com/global_monthly.html.

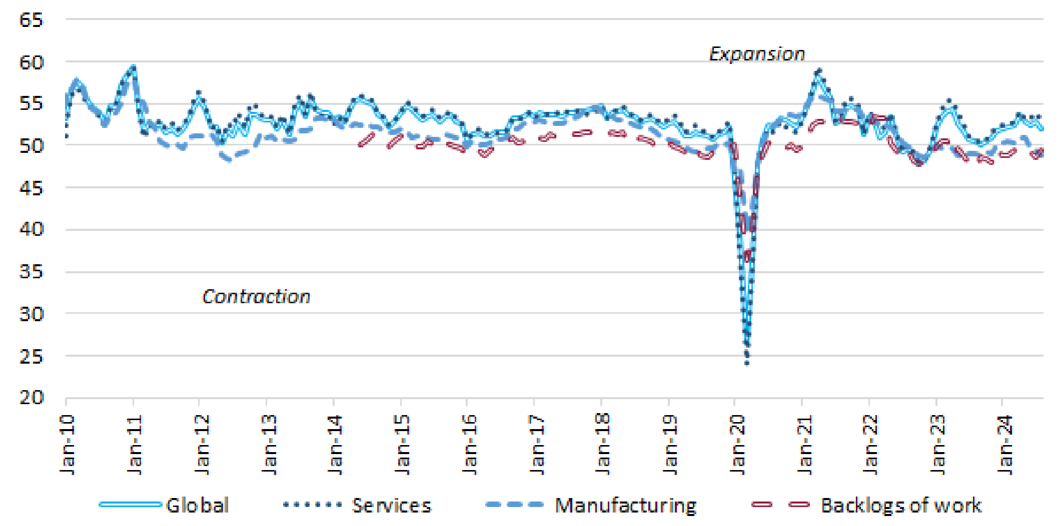
markedly over the past two quarters, falling by 3.3 per cent in August over previous month.

Figure 1 – Economic Policy Uncertainty Index (EPU Index) (1)



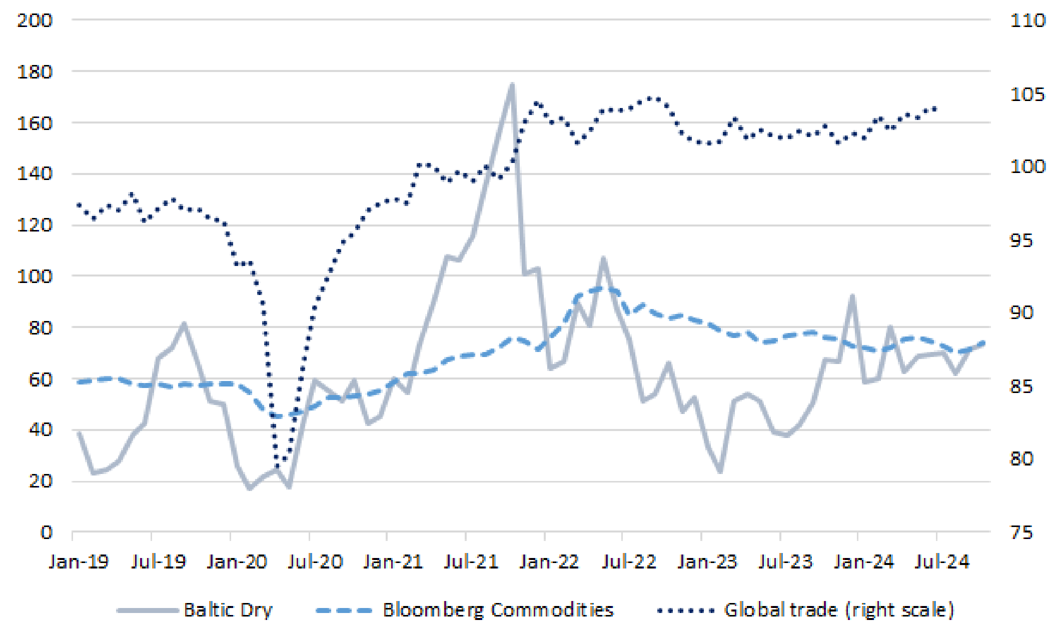
Source: https://www.policyuncertainty.com/index.html.
(1) The global index is computed by aggregating the indices of the different areas based on purchasing power parity.

Figure 2 – JP Morgan Global PMI Index



Source: S&P Global.

Figure 3 – Global economic activity indicators
(indicator numbers, 2010 = 100)



Source: elaborations based on CPB, Baltic Exchange and Bloomberg data.

As far as individual Countries or areas are concerned, the second quarter of the year showed heterogeneous dynamics among major economies. The US GDP grew more than expected (3.0 percent on quarterly basis and annualised terms), while the Euro area stagnated (0.2 percent economic change), suffering in particular from Germany slow down (-0.1 per cent). The China's GDP is slowing down, as the growth was from 5.3 per cent in the first three months of the year to 4.7 percent in the second quarter and 4.6 in third quarter.

International Monetary Fund's updated forecasts

In its October Report, IMF improved its growth forecast for the US by a couple of tenths of a point to 2024 and 2025 when GDP would, however, slow down to 2.2 per cent (Table 1). By contrast, IMF revised downwards the growth for the Euro area, where GDP is still expected to accelerate in both 2024 (to 0.8 percent from 0.4 percent last year) and 2025 (to 1.2 percent). On the other hand, in China real estate problems are expected to limit development in 2024-25 (4.8 and 4.5 percent GDP growth rates, respectively): the 5.0 per cent target for 2024 set by the government is at risk due to downward revisions of the estimates.

The world trade forecasts remain unchanged, foreseeing a recovery of elasticity with respect to global product, very pronounced in 2024 when it would approach the unit value; elasticity would continue to grow, but moderately so in 2025.

Table 1 – IMF forecasts

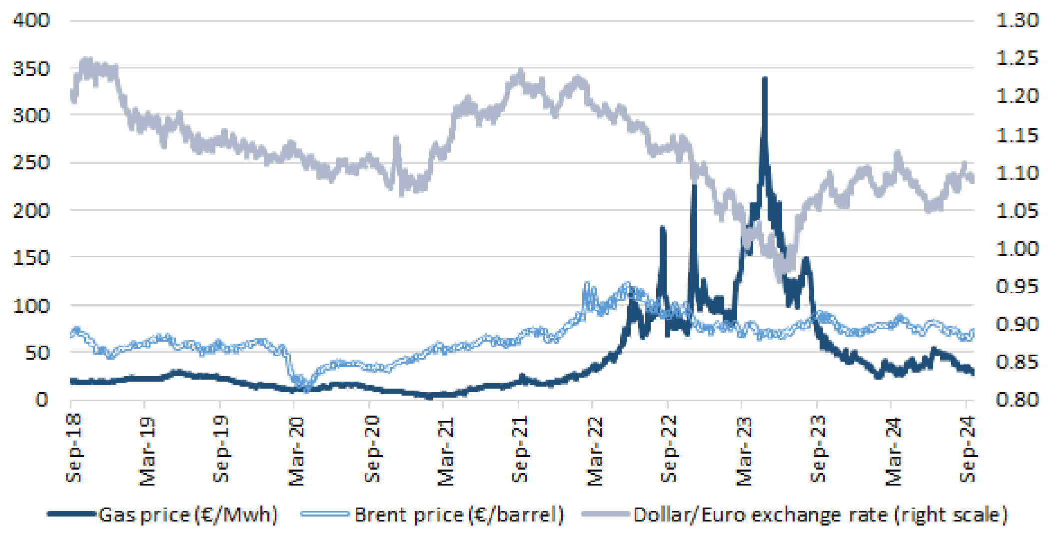
	WEO October 2024			Differences with WEO July 2024	
	2023	2024	2025	2024	2025
Global product	3.3	3.2	3.2	0.0	-0.1
Advanced economies	*1.7*	*1.8*	*1.8*	*0.1*	*0.0*
United States	*2.9*	*2.8*	*2.2*	*0.2*	0.3
Euro area	*0.4*	*0.8*	*1.2*	*-0.1*	*-0.3*
Emerging economies	*4.4*	*4.2*	*4.2*	*0.0*	*-0.1*
China	*5.2*	*4.8*	*4.5*	*-0.2*	*0.0*
Global trade	0.8	3.1	3.4	0.0	0.0

Source: IMF, *World Economic Outlook*, October 2024.

Tensions in energy commodity markets widen

Tensions in the Red Sea and conflicts in the Middle East keep oil price uncertainty high. Price of raw materials, that of Brent crude oil in particular, declined in summer months (Figure 4), mainly due to concerns about Chinese demand; Opec organization tried to support prices by postponing from October to December an additional 180,000 barrels per day. In the last few days, the extension of the conflicts in the Middle East forced prices to start rising again and volatility to increase; conflicts now involve Iran, which has a major influence on oil supply and energy production, so energy commodity prices could rise rapidly, depending on how the war scenarios evolve.

Figure 4 – Oil and gas price, and exchange rate
(oil and gas prices in Euro)



Source: S&P Global.

After the long downward phase that began last October, natural gas price on the Dutch market (TTF) started to rise again in August. The recent price increase reflects several factors; demand is rising as distribution companies are facing for the cold months, and ongoing conflicts increase the costs of raw material storage and transport on the supply side.

From the beginning of this year up to July, the exchange rate US currency to Euro almost stabilised and fluctuations were contained between USD 1.06 and USD 1.09 per Euro. The European currency also showed some volatility in the summer due to changes in inflation expectations and asynchronous monetary policy decisions between the two sides of the Atlantic. Euro started to appreciate in August, averaging over 1.10, influenced by the prospects of a slowdown in the US. Both Central banks have started their round of monetary easing, the speed and intensity with which they will continue is uncertain; several market participants expect the Federal Reserve to take a more aggressive approach in cutting rates, which could lead to a strengthening of the Euro. The outcome of the US presidential election may also have an impact on the exchange rate.

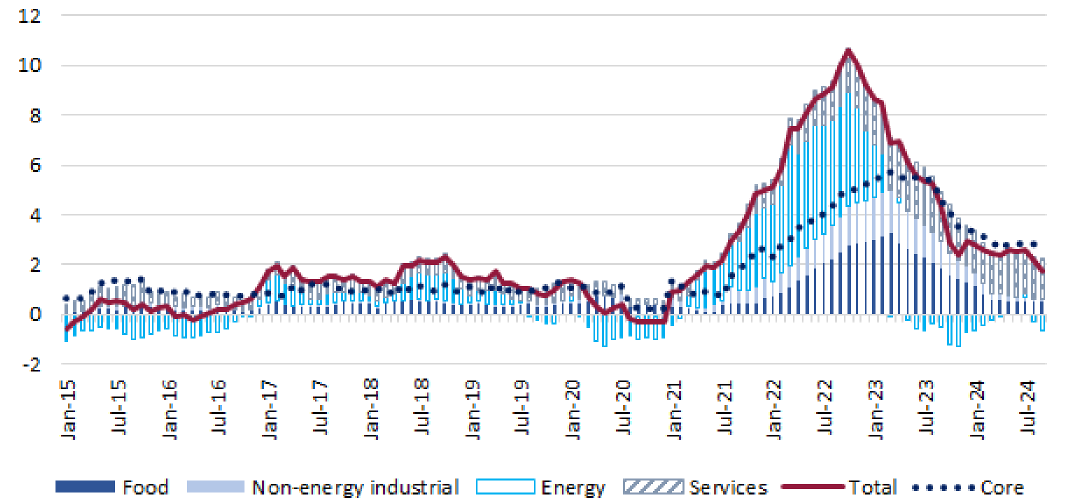
Inflation in the Euro area fell below two per cent

Inflation in the United States continued to fall, although less than expected: in September the headline inflation fell to 2.4 percent, the lowest since last February; net of the more volatile components, inflation continued to show some persistence, rising slightly in September. A similar dynamic can be seen in the development of the index on personal consumption expenditure in its core component (net of energy and food), an indicator highly regarded by the Federal Reserve for monetary policy decisions.

In September, inflation in the Euro area decreased to 1.7 per cent (from 2.2 in August; Figure 5), the lowest value in more than three years. The core component is continuing to decline slowly, with service prices showing persistence. In September, main Countries in the area recorded similar inflation figures: in particular, Germany showed a rate of 1.8 percent, just above the area average, Spain 1.7 per cent and France 1.4 percent; Italy continued to stand out, as harmonised inflation in the same month fell to 0.7 percent (see Figure 17 in the “The Italian economy” section), well below the area average.

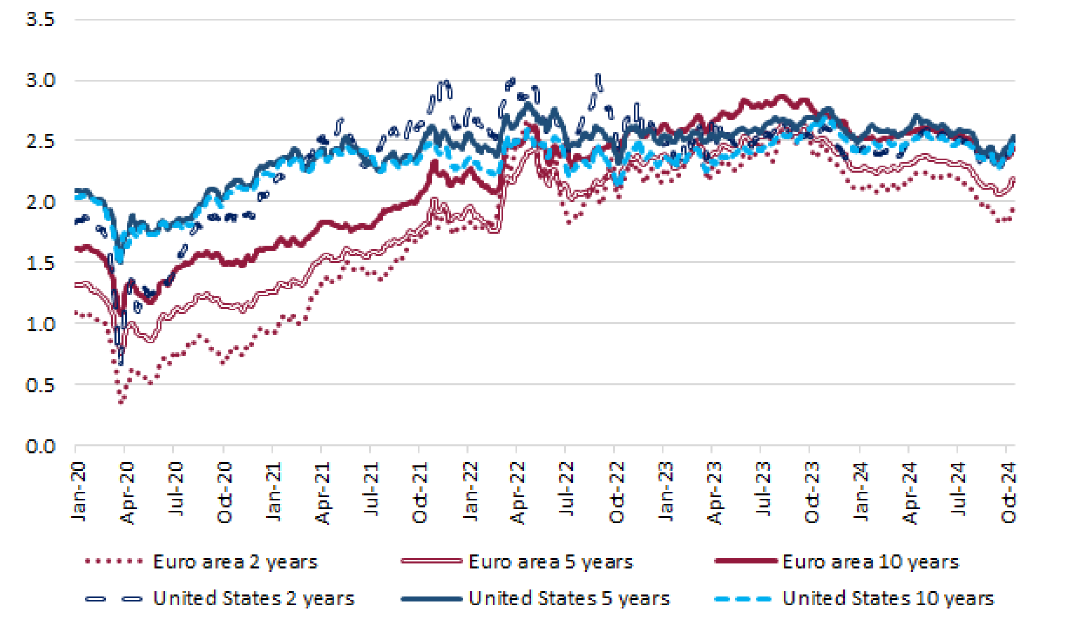
In the Euro area, traders’ inflation expectations continue to fall and expectations for the 10-year Euro inflation swap rate appear to be converging around 2.4 per cent (July-September average), compared to 2.6 percent on average in April-June; the United States has higher expectations than Europe for each maturity (2, 5 and 10 years), driven in part by uncertainty over the outcome of the US elections at the end of the year (Figure 6). The inflation curve inferred from price-indexed swaps continues to be rather flat; in fact, the spread between ten- and two-year expectations in the summer is about 40 basis points for the Euro area and zero for the US.

Figure 5 – Consumer inflation in the Euro area (1)
(percentage variations and contributions)



Source: elaborations on Eurostat data regarding the Harmonised Index of Consumer Prices (HICP).
(1) The graph shows the contributions to growth of the sectoral components of the overall consumer price, as well as the change in core inflation. The sum of the contributions may not correspond with the dynamics of the total index, as it is chain-linked and processed at a higher detail.

Figure 6 – Inflation expectations implied in inflation-linked swaps in the euro zone and the United States
(percentage points)



Source: S&P.

The Italian economy

Revisions to quarterly data worsened the acquired growth for 2024

In recent weeks, Istat conducted a major revision of national accounts, carried out according to the standards agreed upon in the European Union and adopting 2021 as the new benchmark year (i.e. the period used to estimate the levels of the national accounts aggregates).[3] On 23 September, the new annual accounts were released, in which the time series were revised from 1995, which now allows a new interpretation of growth accounting (see box "Growth accounting for Italy: a first assessment in the light of the new national accounts"). The nominal GDP level was revised upwards for the three-year period 2021-23 (Figure 7), following earlier revisions that had already raised the years between 2020 and 2022.

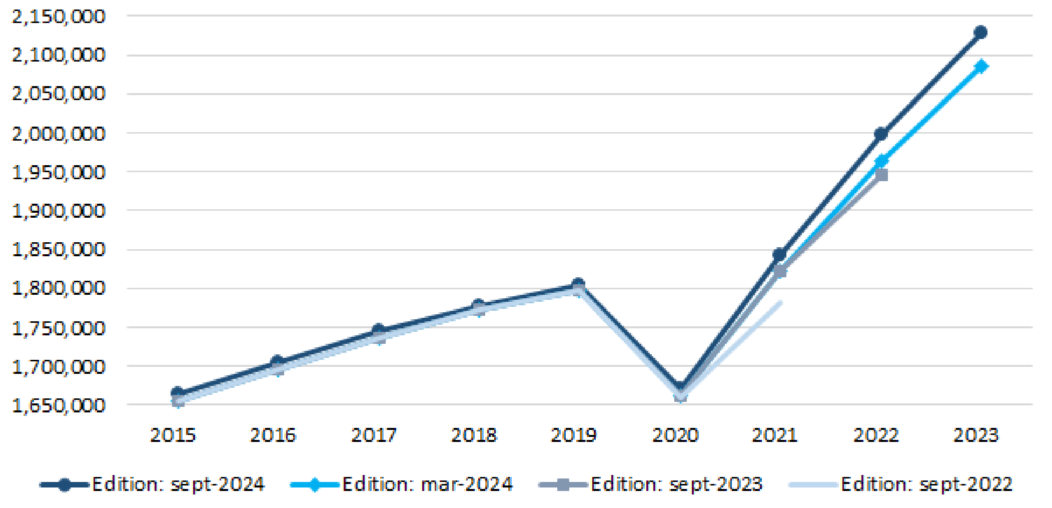
The dynamics of GDP in volume (chained values with base 2020) of the Italian economy was revised to 8.9 per cent for 2021 (from 8.3) and to 4.7 for 2022 (from 4.0). By contrast, last year's GDP change was limited to 0.7 per cent (from an estimated 0.9 per cent in March) but remained above the Euro area for the third year in a row. The GDP growth rate for 2023 indicates the end of the strong recoveries that followed the pandemic crisis, showing a value in line with the pre-pandemic averages for Italy.

On 4 October, Istat released the quarterly accounts, which were consistent with the new annual series. The economic change in GDP in the first and second quarter was confirmed at 0.3 and 0.2 per cent respectively, while it decreased for all quarters of 2023 except the first. The growth acquired in 2024 was reduced to 0.4 per cent from the 0.6 previously estimated by Istat; consequently, the GDP forecast for this year would be mechanically reduced by two-tenths of a percentage point.

For domestic final consumption, after the winter setback there was a recovery in spring, with a slight expansion in household consumption (0.3 per cent) and a strong acceleration in PA spending (1.0 per cent). Gross fixed capital formation in the second quarter just shrank (whereas the previous data showed a positive change, by three-tenths of a point) for the second consecutive period. Foreign flows also contracted overall in the first half of this year, with exports declining (-0.6 per cent in winter and -1.2 in spring) and a negative contribution to growth from net foreign demand of about half a percentage point. Domestic demand net of inventories provided a positive contribution to GDP growth in the second quarter (0.4 percentage points, attributable equally to public and private consumption), slightly above that of the change in inventories (0.3 percentage points; Figure 8).

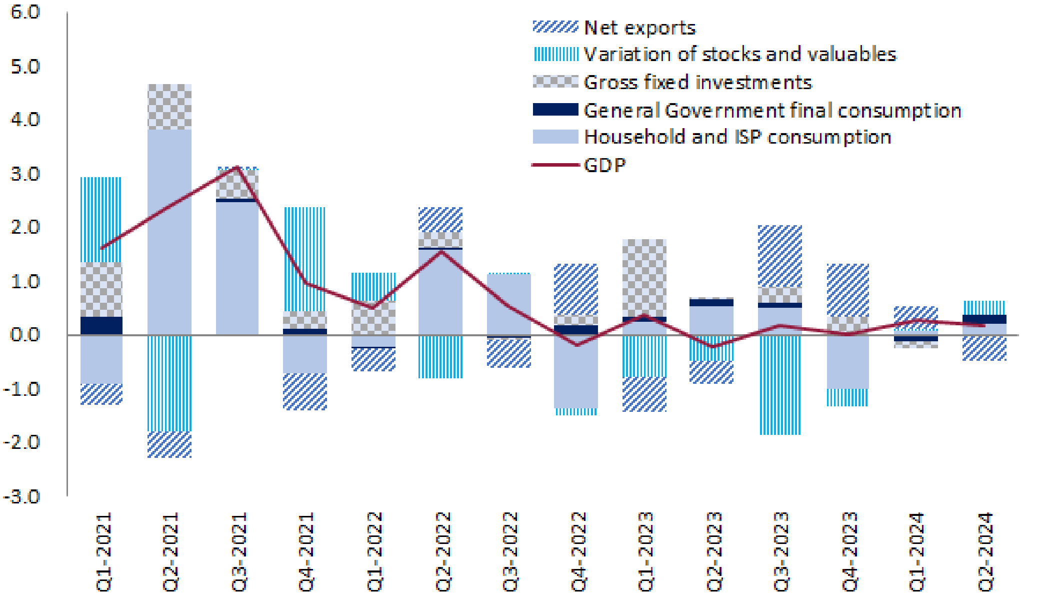
[3] A more recent base year (2020) was also adopted for volume estimates of national accounts aggregates at chain-linked values.

Figure 7 – Italy's nominal GDP in various Istat publications
(millions of Euro)



Source: Istat.

Figure 8 – GDP change compared to previous quarter and contributions of demand components to GDP
(quarterly percentage changes and contributions in percentage points)



Source: Istat.

On the supply side, there was a non-negligible growth in the value added of services in the spring (0.4 per cent, slightly less than in the first quarter), while industry in the strict sense of the word continued to decline (-0.5 per cent) and construction sector recorded its biggest setback (-0.6 per cent) for more than a year.

The slowdown observed in the spring also affected the other major Euro area economies, except for Spain, whose growth stood at 0.8 per cent.

However, for the second quarter in a row the economic trend of Italian GDP remained in line with that of France and the Euro area (0.2 per cent) and higher than that of Germany, which was still contracting (-0.1 per cent).

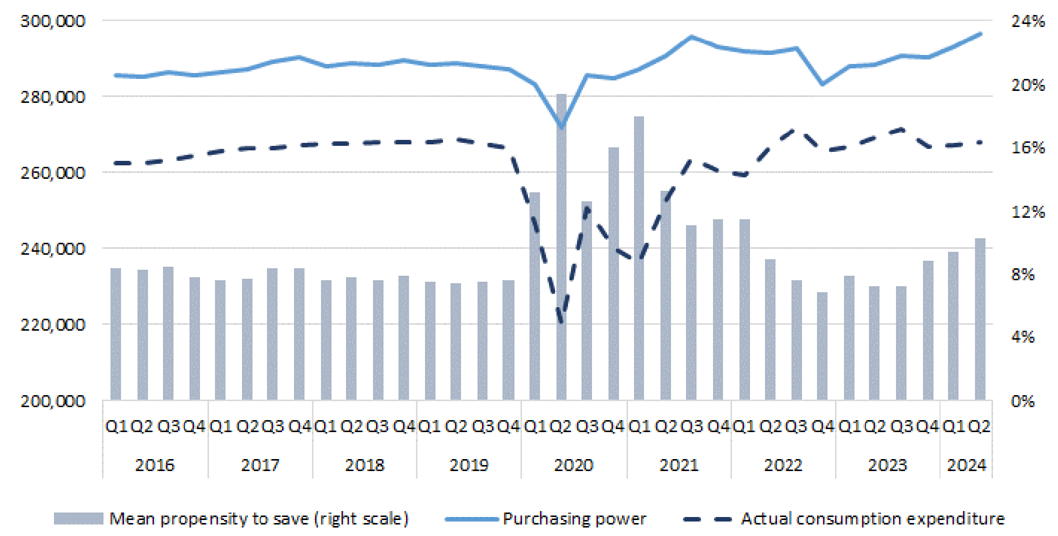
Consumer spending recovers slowly as savings increase

In the spring, household spending in real terms came close to average levels observed in 2019, the last pre-pandemic year; in the second quarter, private consumption increased by 0.3 per cent on an economic basis, driven by the services component (1.1 per cent), which more than offset the decline in that of goods, particularly for non-durables.

Household purchases remained moderate: in the first two quarters of the year, growth in consumer spending at current prices (0.4 per cent in the spring) was lower than growth in disposable income and purchasing power (1.2 per cent for both), resulting in a greater propensity to save, which exceeded the 10 per cent threshold in the spring, well above the average of the pre-pandemic decade (Figure 9).

During the summer there were mixed signals on consumer spending orientations. Based on PBO calculations, the seasonally adjusted consumption indicator (in volume) of Confcommercio would have grown slightly in the third quarter, driven by the goods component. However, less favourable indications come from retail sales (in volume), whose change over the summer is almost zero.

Figure 9 – Household purchasing power, consumption and savings
(millions of Euro, chain-linked volumes and percentage shares)



Source: Istat.

Household confidence improved slightly in the third quarter, confirming a trend that had been underway since the early months of 2024, a period in which, however, some caution was observed in spending orientations, which favoured durable goods and services.

Housing investment slows down, but other components of accumulation increase

Based on quarterly data revised by Istat in October, gross fixed capital formation in the second quarter just shrank, registering the second consecutive economic decline in both the total (-0.1 per cent) and the housing component (-2.0 per cent); by contrast, accumulation in non-residential construction remained on the rise (0.7 per cent on a quarterly basis), as did investment in plant and machinery (0.9 per cent).

Despite these weak economic developments, gross fixed capital formation in the first half of the year 2024 exceeded the average of 2023, also because of the revisions to the national accounts released by Istat in recent weeks. The investment rate of non-financial companies (the ratio of gross fixed capital formation to added value) barely declined in the second quarter to 22.2 per cent, a value consistent with the average of the decade before the pandemic; the profit share (measured as the gross operating surplus on the value added of non-financial companies) fell to 42.6 per cent, the lowest observed in the last four years. The mark-up for the total economy also recorded its fourth consecutive economic decline in the April-June period, reflecting the contraction observed in all sectors except for agriculture.

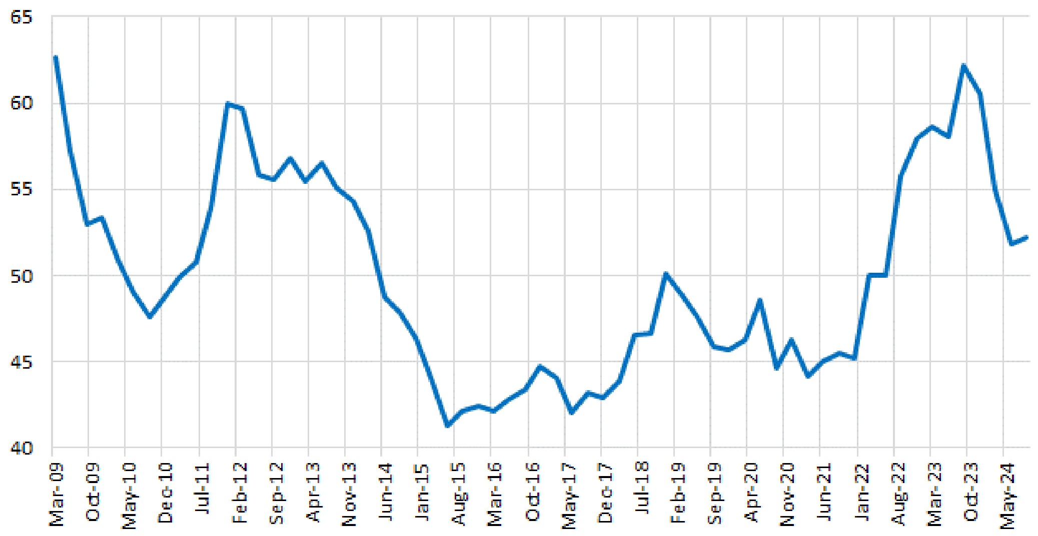
Qualitative surveys conducted at summer end report negative assessments of demand and conditions for investment. According to Bank of Italy's August-September survey on inflation and growth expectations, investment spending will expand this year in services and construction sector, but at a slower pace than in the spring; the scenario remains unfavourable for industry. The same survey points to cautious opinions on the general economic situation in all sectors, and assessments of demand appear to be clearly deteriorating, especially in industry in the strict sense of the word.

Based on the imbalance between supply and demand, the PBO's indicator[4] on tensions in the credit market remained essentially stable in the spring and summer quarters, after the strong improvement observed in the previous months (Figure 10). A stabilisation is also emerging for the mortgage market: real estate agents interviewed between June and July for Bank of Italy's economic survey on the housing market, report unchanged difficulties in accessing mortgages after the improvements observed in the final part of 2023. The less unfavourable opinions noted in the surveys are reflected in the trends in

[4] The PBO indicator on tensions in the credit market is estimated using qualitative information, which also takes into account the judgments expressed in the Istat survey on manufacturing business confidence. When the value rises, tensions in the credit market are estimated to increase.

household mortgages, which recovered slightly in the spring and summer quarters according to Bank of Italy's October Economic Bulletin.

Figure 10 – PBO index on credit conditions for businesses (1)
(diffusion index; threshold between restrictive and expansive conditions = 50)



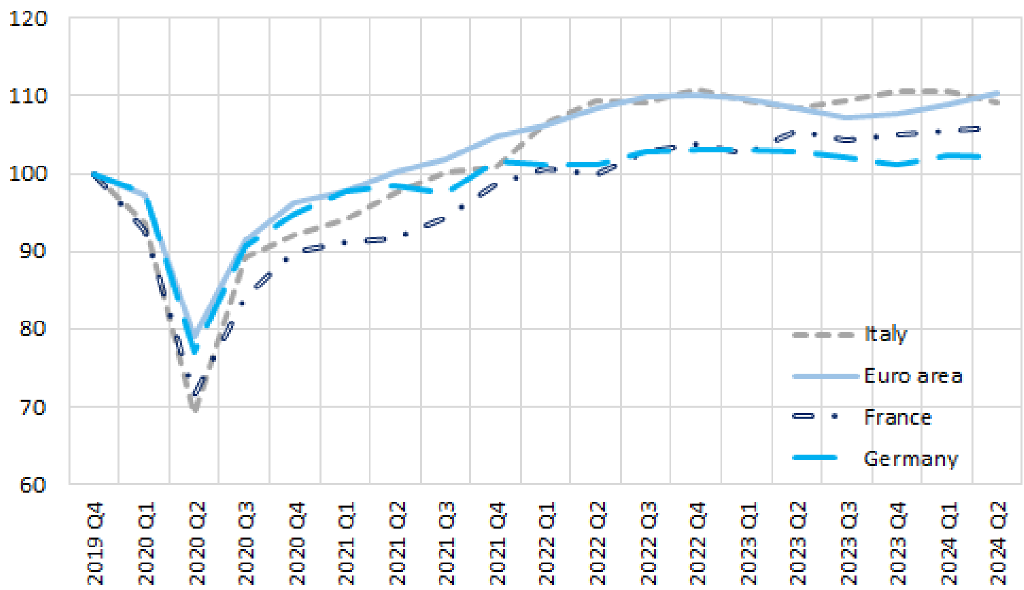
Source: calculations based on data from Istat.
(1) For methodological details see the PBO's Report on recent economic developments - October 2023.

Exports weakened in the first half of the year

In the second quarter of this year the volume of Italian exports of goods and services contracted by 1.2 per cent, continuing the weakness also observed in the previous period. The increase in service exports, also favoured by copious tourist flows, was counterbalanced by an economic decline in exports of goods, particularly in the mechanical engineering and automotive sectors. Geographically, sales decreased in markets outside the Euro area (mainly in the US) and, to a lesser extent, within the currency area. Despite this, Italy's export performance remained solid compared to that of its main European trading partners, with an increase compared to pre-pandemic values still higher than that of the two largest Euro area countries (Figure 11).

The current account surplus, adjusted for seasonal effects, increased in the second quarter compared to the previous period, reaching 2.0 per cent of GDP. This improvement was supported by the narrowing of the primary income deficit, while the energy deficit remained stable, and the surplus of non-energy goods deteriorated.

Figure 11 – Export volumes of the Euro area and its three largest economies
(index numbers, 2019Q4=100)



Source: Eurostat.

In the July-August two-month period, foreign sales of goods (in value) declined by about one percentage point compared to the first quarter average, reflecting a slowdown that affected non-EU markets more than domestic EU markets. Istat qualitative surveys on foreign orders and the corresponding PMI index seem to outline a weak phase for foreign trade in the short term.

Imports in the second quarter increased slightly (0.2 per cent compared to the first quarter), mainly driven by services. The decline in purchases of goods from Euro area Countries, especially Germany, was more than offset by the increase in imports from non-European markets, especially from Asian countries. At industry level, the most pronounced reduction was in energy products and motor vehicles.

The resilience of imports in volume, together with the decline in exports, resulted in a negative contribution of net foreign demand to GDP growth in the second quarter (-0.3 percentage points).

Industrial activity is not expected to recover in the short term

In the first eight months of 2024, industrial production fell by almost three points compared to the average of 2023, only showing a slight positive sign in August (a tenth of a point on a monthly basis, attributable to consumer goods and the energy component), which was however insufficient to compensate for the average drop in the first two summer months; manufacturing was mainly affected by the weakness in the production of consumer durables and capital goods, which also included motor vehicles. The outlook remains unfavourable, and the manufacturing PMI index remains below the threshold of 50 that demarcates expansion and contraction phases; the indicator on the climate of confidence surveyed by Istat among manufacturing companies is at its lowest level in three years.

The degree of capacity utilisation of manufacturing companies over the past four quarters has remained broadly stable, hovering around 76 per cent in the spring, a percentage close to that of the pre-pandemic period; the share of companies facing production bottlenecks is significantly reduced, but the share of companies reporting labour shortages is increasing.

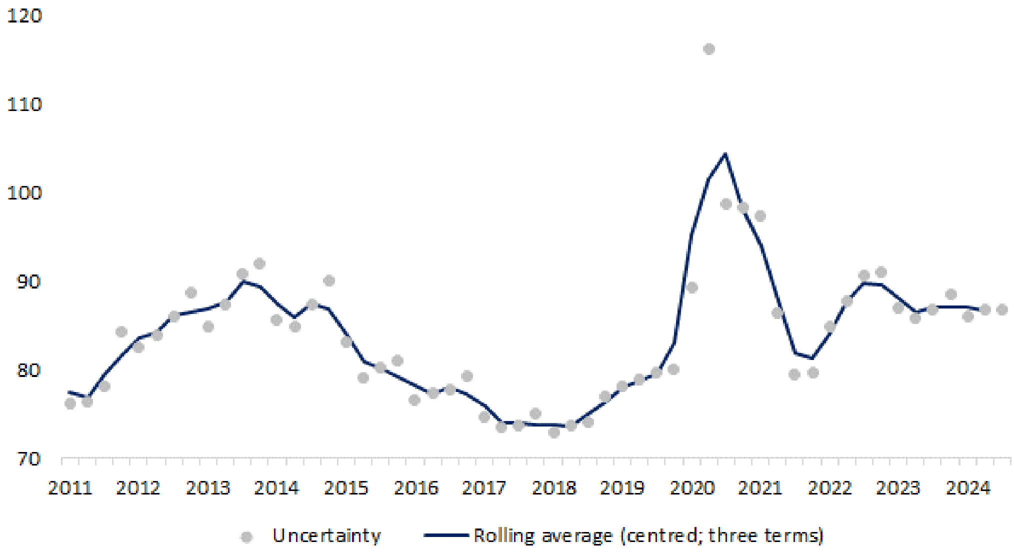
Since the spring, the construction sector PMI index has also moved into restrictive territory, although the sector's output grew in the first eight months of the year, by five per cent compared to the average of 2023. The latest data on production in construction sector show a marked drop in summer, by 1.8 per cent in August compared to July.

During summer, the business confidence climate recorded by Istat weakened in all sectors except services. The services PMI indicator has also been in an expansionary phase since spring, supported by views on new customer acquisition and favourable expectations. The data on tertiary sector activity are consistent with the surveys; added value grew by 0.4 per cent in the spring, thanks to increases in almost all sectors with the exception of those attributable to the public sector (General Government, defence, education and health), for which it has been contracting for over a year. Similarly, in the May-July period turnover in services grew by 0.4 per cent compared to the previous three months, driven by the sectors related to tourism and catering and information and communication services.

Regarding the birth-mortality rate of enterprises, after a first quarter in which terminations had exceeded activations (-10,951 the balance), Unioncamere's Movimprese survey recorded a positive balance of over 29,000 units in the spring, with a trend growth of 4.0 per cent. All major sectors contributed to this result, particularly accommodation and food services. The balance was also broadly positive in the third quarter, and the number of active enterprises increased slightly.

During summer, uncertainty measured by the PBO index remained almost unchanged (Figure 12), with a slight deterioration for businesses and a slight improvement for households.

Figure 12 – PBO indicator of uncertainty (1)
(index number, 1993Q1=100)



Source: calculations based on data from Istat.
(1) For more details on the indicator, please refer to PBO's Report on recent economic developments - April 2017.

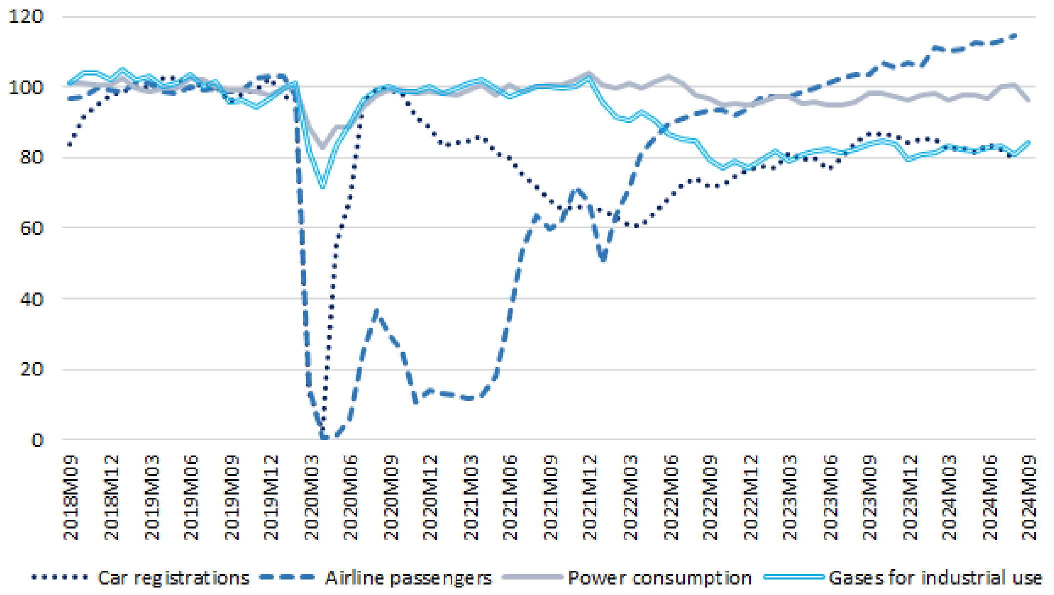
Latest indications and short-term forecasts

Timely monthly quantitative variables signal a cyclical phase that is little more than stagnant. At the end of the summer, electricity consumption showed a setback, probably also as a result of the below-average temperatures for the period; on the contrary, gas consumption for industrial use in September recovered the previous month's drop, but still remains well below the pre-crisis level, also due to the efficiency gains after the 2022 energy crisis. The upward trend in air passenger traffic is confirmed, which continues to benefit from large tourist flows, while new car registrations have not yet recovered the values of 2019 (Figure 13).

According to PBO estimates, during summer GDP changed very little compared to the previous quarter, within a range of -0.1 to 0.2 per cent (Figure 14). The downturn in manufacturing production has been holding back activity almost uninterruptedly for two years. Construction sector is currently in an uncertain, but overall weak phase. By contrast, the tertiary sector, which accounts for a large part of the value added for the entire economy, continues to make a positive contribution to GDP, driven by international tourism flows.

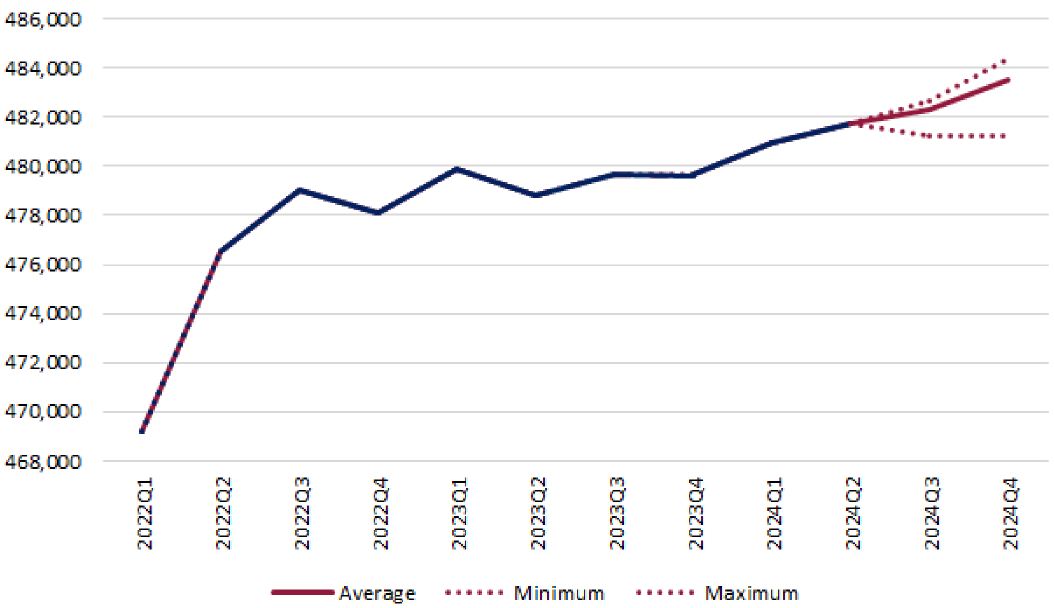
In the final part of 2024, the production dynamics would gradually strengthen. Overall, in 2024 the GDP growth forecast is now around 0.8 per cent in the annual series, that are not adjusted for calendar effects. This value is two-tenths of a percentage point lower than the forecast produced last month by the PBO for the validation of the MTFSP 2024 macroeconomic scenario. The slight downward revision is mainly attributable to the lower statistical drag that the new quarterly national accounts series (released on 4 October) shows compared to the previous data (released on 2 September).

Figure 13 – Real-time indicators of economic activity
(index number, 2019 average = 100; seasonally adjusted data)



Source: Terna, Snam, Assareoporti, Anfia.

Figure 14 – Short-term GDP forecast (1)
(millions of Euro and concatenated values; referenced year 2020)



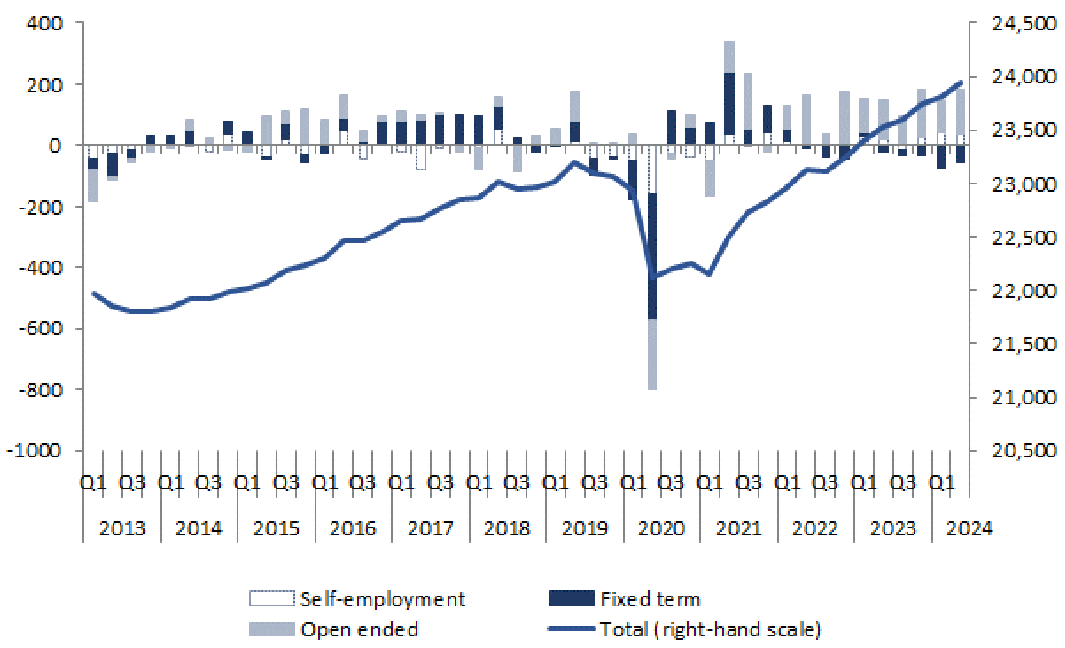
(1) GDP forecasts are obtained using PBO's short-term models (for more details see the technical note "The PBO's macroeconomic forecasting tools").

Unemployment rate falls and wages recover in real terms

During the spring, the expansion in the number of employed persons continued, but labour input contracted slightly (-0.2 per cent compared to the previous quarter). Hours worked declined in industry excluding construction, to a greater extent than the decrease in output, declined moderately in construction sector and grew slightly in services. After a year and a half of contractions, productivity per hour returned to growth, albeit marginally. The reduction in hours worked reflected a significant decline in hours per capita, probably due to labour hoarding, particularly in services; in construction sector, employment was reportedly driven by good labour demand conditions, as measured by the high vacancy rate.

The number of employed persons grew in the second quarter (0.5 per cent on the basis of the Quarterly Labour Force Survey, up from 0.3 in the first three months), primarily due to the boost in permanent employment; the increase in self-employment also contributed to this, while the ongoing decline in the number of fixed-term employees, which had persisted for over a year, continued (Figure 15). The increase in employment in the spring was mainly driven by the female component and affected the middle (35-49 years) and older age groups. According to provisional data, the number of employees would continue to expand over the summer months at a pace like that of the second quarter. The employment rate rose slightly, reaching a new all-time high (62.3 per cent on average in July-August).

Figure 15 – Employees and self-employed
(absolute economic changes; levels)



Source: Istat.

Administrative data from the INPS Observatory on the labour market, relating to the private non-agricultural sector, confirm the driving role of permanent employment. Job creation was mainly in tourism-related services (accommodation and catering, trade), professional services and the construction sector. However, in the first half of this year the net activation of permanent contracts slowed due to lower recruitment and a decrease in the transformation of fixed-term employment relationships into permanent contracts.

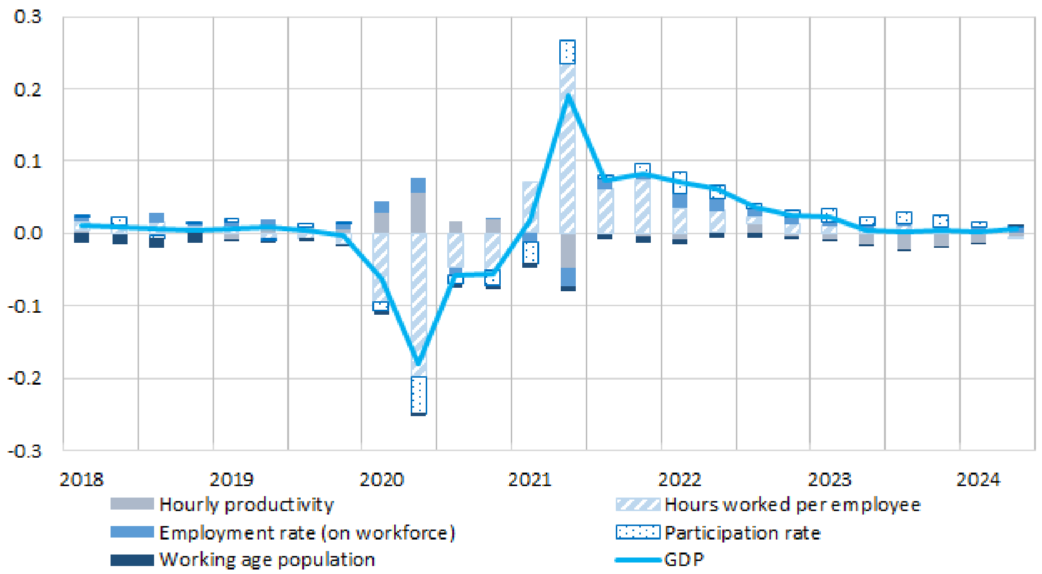
The use of wage subsidies, which started to increase again in the first three months of this year after an extended period of decline following the pandemic, intensified further in the second quarter (36.3 per cent compared to previous year). The majority of requests for intervention since the beginning of the year entirely concerned the authorised hours of the Wages Guarantee Fund (Cassa Integrazione Guadagni, CIG) in industry excluding construction, particularly in manufacturing industries experiencing a marked weakening of the cyclical phase (textiles, clothing and leather, mechanics, metallurgy). In contrast, the use of supplementary wage schemes decreased in construction and trade sectors.

After a slight decrease in the winter months, the participation rate (15-64 years) was stationary at high values in the second quarter. Supported by favourable employment trends, the unemployment rate continued to fall during the spring (6.8 per cent), especially among women. The number of job seekers decreased and this pattern intensified in the summer months, particularly among female, alongside a moderate employment growth. In July-August, the sharp fall in the unemployment rate (to 6.3 per cent) mainly implied a weakening of the labour supply; the participation rate thus decreased (to 66.6 per cent, -0.2 percentage points compared to the second quarter).

Since the beginning of the year, the number of inactive individuals has increased, predominantly among the younger population (15-34 years), mainly for reasons of study or awaiting the outcome of previous job search searches. More transitions from unemployment to inactivity are observed, which explains the increase in the already large group of inactive people furthest from the labour market (those who do not seek and are not available for work). The inactivity rate stopped its decline (to 33.1 per cent in the second quarter) and rose again in the summer.

Breaking down the year-on-year change in GDP into the contributions of the main labour market variables, labour productivity and demographics, growth in the second quarter was mainly driven by the employment rate and marginally by the activity rate (Figure 16). The contribution of hourly productivity remained unfavourable, as did the contribution of hours worked per employee, which turned negative for the first time since the end of 2020.

Figure 16 – Real GDP growth and labour market
(year-on-year percentage changes; contributions to growth)



Source: elaborations on Istat data.

In the second quarter the dynamic of contractual wages in overall economy (3.5 per cent year-on-year) was supported by the recovery of the bargaining process. In the private sector, the increase in hourly wages (4.1 per cent) was mainly driven by the April pay increases in trade and the June adjustment of hourly earnings in the metal sector. In General Government sector, wage growth remained at the same level as in the first quarter (1.6 per cent). During the summer months the growth of contractual wages in the private sector stabilised at the levels of the previous quarter, as in the overall economy (3.5 per cent year on year in July-August). This dynamic is expected to continue in the second half of the year, driven by the recent contract renewals, so it would remain higher than the 2024 expected value of the reference index for collective bargaining (1.9 per cent according to the HICP net of imported energy). The change in actual hourly wages strengthened in the second quarter to 4.7 per cent year-on-year, up from 2.9 per cent in the first quarter. The loss of real wages in recent years is thus shrinking, but remains significant (almost four per cent compared to the second quarter of 2021). Unit labour costs (ULC) accelerated, reflecting the increase in hourly labour costs, as well as the continuing, albeit moderating, downward trend in productivity.

Italian consumer inflation remains lower than in the Euro area

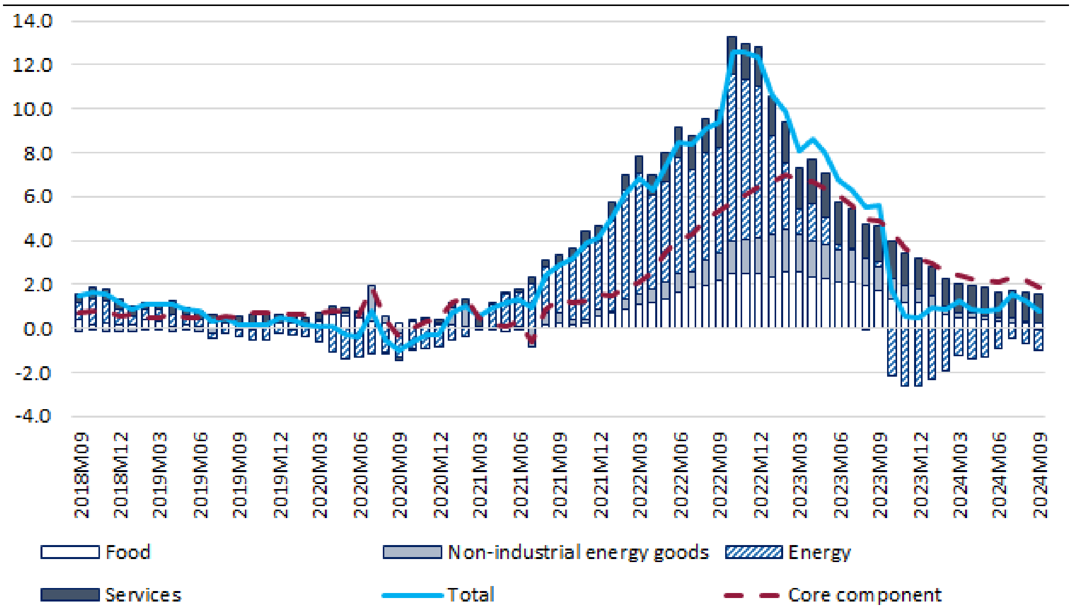
Inflation continued to fall, thanks to price reductions observed in the energy sector and some services, which outweighed weak price increases in the food sector. The underlying component stabilised below the ECB target and expectations remained subdued. However, foreign pressures upstream are reactivating, also in connection with geopolitical tensions outside the Euro area.

Consumer inflation (NIC) stood at 1.0 per cent in the third quarter, slightly up from previous period (0.8 per cent) due to a lower negative effect of the energy component. In September price dynamics started to fall again, to 0.7 per cent, the lowest value since the beginning of the year. The decline in the prices of energy goods intensified (-8.7 on annual basis in September from -6.1) and inflation for some services, especially transport, recreational, cultural and personal care services decreased (Figure 17); however, the growth in food prices increased, which supported the dynamics of the so-called "shopping trolley" (to 1.0 per cent from 0.6). The underlying component remained just below the ECB target, falling to 1.8 per cent in September. The carry-over price growth for 2024 is 1.0 per cent for the overall index and 2.1 for the core component.

Inflation in Italy is still lower than in the Euro area, but the negative differential (equal to one percentage point in the third quarter of the year from 1.6 in the first two), which opened up at the end of 2023 with the start of the deflationary phase for energy goods (Figure 18), is narrowing; the negative differential for the food sector is increasing and that for services is persisting. Italian core inflation is lower than in Europe (2.2 per cent in the third quarter in Italy compared to 2.8 per cent in the Euro area), where it remains more persistent.

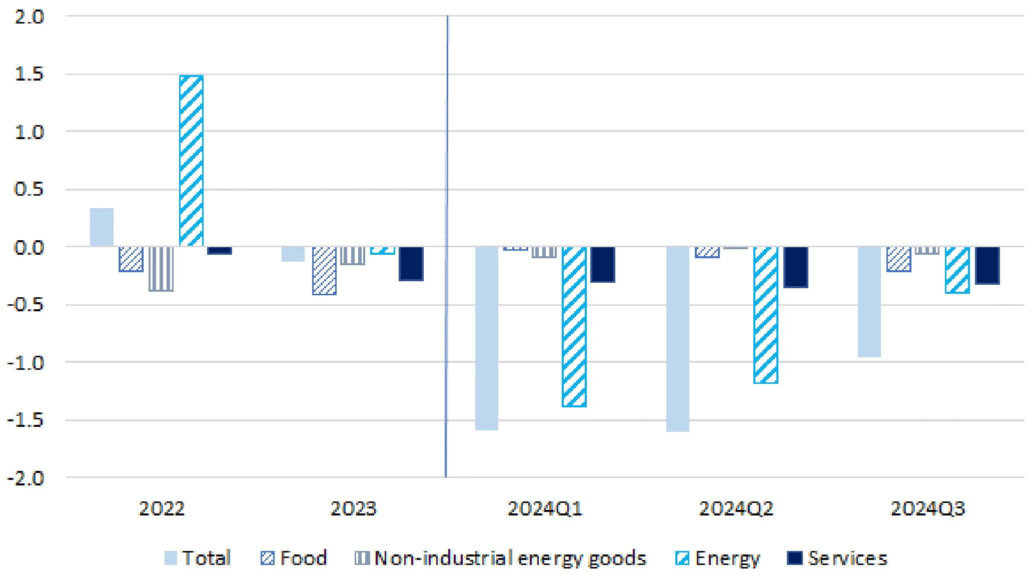
In Italy, the number of basket items with low price dynamics continues to grow; now almost 60 per cent of goods and services show inflation below 2.0 per cent.

Figure 17 – Consumer inflation in Italy (1)
(percentage variations and contributions)



Source: elaborations on Eurostat data regarding the Harmonised Index of Consumer Prices (HICP).
(1) The graph shows the contributions to growth of the sectoral components of the overall consumer price, as well as the variation in core inflation. The sum of the contributions may not correspond with the dynamics of the total index, as it is chain-linked and computed at a higher detail.

Figure 18 – Italy's inflation differentials with the Euro area (1)
(differences in percentage points)



Source: elaborations on Eurostat data.
(1) Differences in harmonised inflation between Italy and the Euro area.

However, the deflationary dynamic upstream in the production chain seems to be coming to an end, due to renewed tensions in energy commodity prices. Imported prices in August rose for the third consecutive month (1.0 per cent from 1.3 per cent in July) compared to the previous year, mainly reflecting fluctuations in the prices of energy goods such as crude oil and electricity. At the same time, production price deflation in industry was softening (-0.8 per cent in August, down from -1.1 per cent in July), again due to the exhaustion of the cuts phase of declines in the energy sector. In services, growth in producer prices strengthened slightly (3.1 per cent in the second quarter of 2024 from 2.8 per cent in the first quarter), particularly in real estate and rental activities, travel agencies and business support.

Consumer and business expectations are consistent with price dynamics stabilising at low values. The percentage of companies interviewed in the Istat surveys expecting a possible upturn in inflation is now residual since the spring (around 8 per cent) and the percentage of those expecting a reduction is also stable (around 5 per cent); at the same time, consumers mostly expect stable prices (46.8 in the average of the last three months) or softening increases (just under 20 per cent of those interviewed in recent months). The Bank of Italy's survey on business expectations shows expectations for inflation, in the third quarter, to be low although slightly rising; at a sectoral level, no tensions are foreseen in services and manufacturing, while the trend is slightly more pronounced in the construction sector. Purchasing managers surveyed for the PMI index reported in September that cost pressures were easing and sales prices were falling slightly.

Box – Growth accounting for Italy: an initial assessment in the light of the new national accounts

The recent revision of Istat's national accounts time series changed the picture of Italy's macroeconomic dynamics from 1995 to 2023[5]. Compared to the annual series released last March, nominal GDP was raised, in particular in the years 2021-23, and at the end of the period was above the previous March estimate by approximately EUR 43 billion (see Figure 7 in the "The Italian economy" section); in 2023, GDP in volume was for the first time above the all-time high of 2008 reached before the financial crisis. A further major revision was made in the construction sector. The generous incentive measures of the past few years, first and foremost the Superbonus, have fostered a significant growth in the volume of construction investments, whose level of 2023 has been revised by about fifteen percentage points compared to previous estimates. At the same time, employment increased significantly, albeit accompanied by a contraction of real wages. Compared to the picture that emerged from previous national accounts, labour productivity in recent years has improved, leading to an increasing gap between productivity growth and the reduction of real wages, one of the most intense downturns in the recent history of the Italian economy.

The Value Added (VA) has been revised in the new annual data in both nominal and volume terms. Focusing on the last three years for the total economy, the level of VA (at basic prices and chain-linked values) was revised upwards in 2021 and 2022 and downwards in 2023. At sectors level, average downward revisions were observed for agriculture and manufacturing, and upward revisions for services and construction sector, whose VA over the three years 2021-23 as a whole rose by almost 13 percentage points compared to previous accounts.

VA is central to the assessment of a country's economic activity, as it measures the increase in value generated throughout the various stages of the production process. It represents the difference between the total value of the production of goods and services and the cost of the intermediate inputs used. Thus, VA reflects not only net output, which is then allocated to the demand components, but also the income produced by enterprises, which includes workers' compensation and profits for the owners of capital. This dual function makes it a fundamental tool for analysing the distribution of wealth and the dynamics of production supply and hence the labour market. In growth accounting, VA allows the determinants of economic expansion to be identified, distinguishing between productivity, capital accumulation and labour force.

This box analyses the effects of the new accounting estimates on VA for the total economy and the four main sectors (agriculture, industry in the strict sense of the word, construction sector and services), focusing on the decomposition of the growth contributions of labour, capital and total factor productivity (TFP). The analysis covers the period 1995-2023 and is carried out starting from the generic production function:

$$VA = f(TFP, K, L)$$

in which TFP is the total productivity of factors, K capital and L labour. To proceed algebraically with the decomposition of contributions, certain assumptions about the structure of the economy must be made, such as perfect market competition, constant returns to scale of production technology, Hicksian neutrality, and the absence of adjustment costs[6]. With these assumptions, the formula becomes[7]:

[5] See Istat "National Economic Accounts - Year 2023", https://www.istat.it/comunicato-stampa/conti-economici-nazionali-anno-2023/.

[6] For more details see the Istat methodological note in "Measures of Productivity - Years 1995-2022".

[7] From a theoretical point of view, the correct formula should be expressed in terms of logarithms of differences rather than rates of change. While the two measures are very similar in times of moderate growth, they differ significantly in times of strong variability, as has been the case in recent years. In order to reconcile the rate of change of VA obtained from the calculations reported here with the official Istat rate of change,

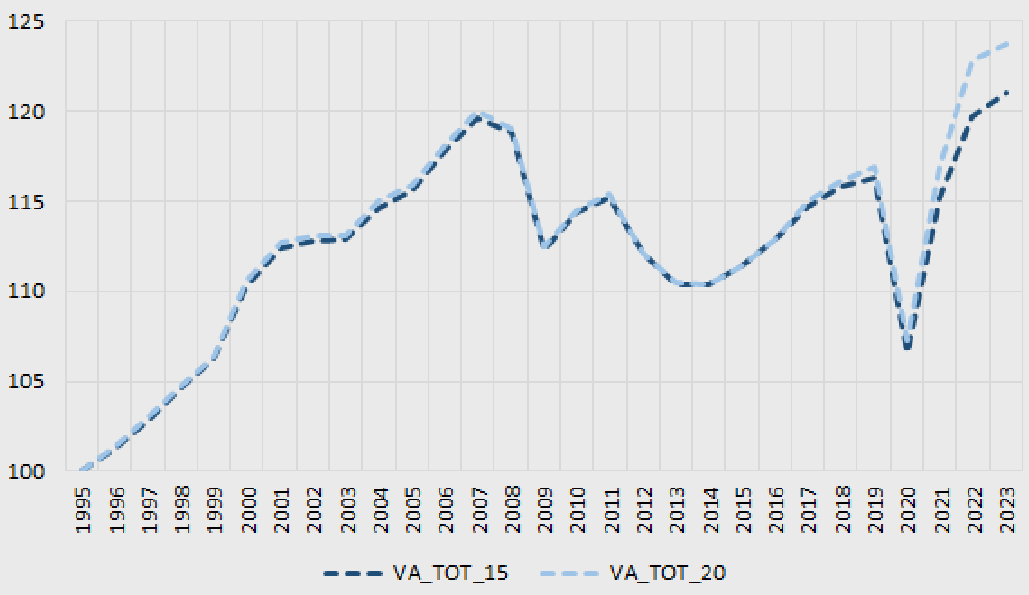
$$\frac{\Delta VA}{VA} = \xi_K^{VA} \cdot \frac{\Delta K}{K} + \xi_L^{VA} \cdot \frac{\Delta L}{L} + \frac{\Delta TFP}{TFP}$$

Variables ξ_K^{VA} *e* ξ_L^{VA} represent the elasticity of VA to capital and labour, respectively; the assumptions imply that each is equal to the share of remuneration of that factor in the *output* value. Given the VA, elasticities and the capital and labour factors of production, TFP is obtained as a residual, the so-called Solow residual[8].

Figure B.1 shows that the effect of the revisions is mainly concentrated in the period 2021-2023. At the end of this interval, the level of VA for the total economy in real terms is about three percentage points higher than the level reported by Istat with the previous accounts. This translates into a higher average annual growth rate of about one-tenth of a percentage point for the entire period covered by the revision of national accounts (Table R.1a). This result was largely driven by the improved dynamics of services and construction sector, which remained the sectors with the strongest growth trajectory.

Breaking down the change in VA by production factors, it emerges that in the new series the increase for the Italian total economy over the period 1996-2023 is attributable to capital and labour to a similar extent and, slightly less, also to TFP (Table B.1a); by contrast, on the basis of the previous national accounts, the contribution of productivity appeared modest. At sector level, services and construction sector recorded the most significant upward revisions in productivity. In construction sector, a higher contribution of the labour factor was observed compared to the previous version of national accounts; in agriculture, a reshuffling between the contributions of the production factors is noted, with a worsening for labour and an improvement for capital.

Figure B1 – VA total economy: accounting with base year 2015 and 2020
(index numbers, 1995Q1=100)



the formulation in rates of change was chosen, which, while producing differences in the results, does not change the order of importance of the contributions of the various components to the final result.

[8] It should be noted that the new accounting estimates, although they report the update for VA, capital and labour, still do not report the new information on labour and capital remuneration shares consistent with the new accounting. Therefore, the most recent available quotas were used to perform the breakdown, i.e. those for April 2024.

Table B1a – VA and contributions total economy and main sectors (1996-2023) (1)
(percentage variations and contributions)

		Averages 1996-2023				
		VA		K	L	TFP
Economy total	2020	0.76%		0.33%	0.23%	0.20%
	2015	0.68%		0.36%	0.23%	0.09%
Agriculture	2020	-0.01%	(0,00)	-0.66%	-1.07%	1.26%
	2015	0.04%	(0,00)	-0.74%	-0.87%	1.28%
Industry	2020	-0.05%	(-0,01)	0.34%	-0.45%	0.05%
	2015	-0.02%	(0,00)	0.38%	-0.47%	0.07%
Construction sect	2020	0.39%	(0,02)	0.13%	0.66%	-0.39%
	2015	0.11%	(0,01)	0.15%	0.55%	-0.59%
Services	2020	1.04%	(0,75)	0.36%	0.49%	0.19%
	2015	0.95%	(0,69)	0.39%	0.51%	0.05%

(1) The year shown in first column is the referenced year of the chaining of the new (2020) and old (2015) accounts. The values in brackets are the sectoral contributions to total VA growth. Their sum may not exactly coincide with VA due to rounding and the properties of chaining.

Since data revisions mainly concerned the period after the outbreak of the pandemic, it is appropriate to focus on the last three years (Table B.1b). In 2021-23 there was a significant increase in the level of overall economic activity, with an average annual growth rate of almost five per cent on a new accounting basis; the average annual increase in VA would have been driven largely by the boost of the labour factor, which contributed more than 3.5 percentage points, as well as by the substantial improvement in TFP, which contributed just under one percentage point. At a sector level, the strongest increase was in the construction sector, where in addition to labour, TFP and capital, in that order, were also important growth drivers. Agriculture is the only sector that recorded a decrease in VA, which is only slightly more pronounced than estimated in previous accounts. Considering the relative weight of the sectors, the largest contribution to growth certainly came from services.

In conclusion, the most recent national accounts series paint an overall favourable scenario for the Italian economy in the post-pandemic period, with growth revised upwards mainly for the construction sector and total factor productivity.

Table B1b – VA and contributions total economy and main sectors (2021-23) (1)
(percentage variations and contributions)

		Averages 2021-2023				
		VA		K	L	TFP
Economy total	2020	4.76%		0.32%	3.63%	0.82%
	2015	4.22%		0.33%	3.59%	0.30%
Agriculture	2020	-0.41%	(-0,01)	0.33%	-0.64%	-0.39%
	2015	-0.30%	(-0,01)	-0.01%	-0.44%	-0.05%
Industry	2020	4.00%	(0,77)	0.24%	2.68%	1.07%
	2015	3.72%	(0,76)	0.33%	2.59%	0.80%
Construction sect	2020	13.81%	(0,75)	1.21%	7.90%	4.70%
	2015	10.94%	(0,61)	0.55%	7.58%	2.80%
Services	2020	4.48%	(3,29)	0.30%	3.86%	0.32%
	2015	4.05%	(3,14)	0.31%	3.90%	-0.16%

(1) The year shown in first column is the referenced year of the chaining of the new (2020) and old (2015) accounts. The values in brackets are the sectoral contributions to total VA growth. Their sum may not exactly coincide with VA due to rounding and the properties of chaining.