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Summary[*]

Conflicts in Ukraine and the Middle East persist, causing volatility in energy commodity markets. Protectionism is also escalating in the United States, which increased customs duties on certain Asian countries, Brazil and the European Union (EU). A political agreement has been reached with the EU on 15 per cent tariffs, the specific details of which are yet to be clarified. The appreciation of the euro in the last six months is acting as an 'implicit tariff' on European exports. The latest forecasts from the International Monetary Fund (IMF) point to a slowdown in global trade, both this year and in 2026. In the euro area, inflation is gradually easing, reaching 2.0 per cent in June, in line with the European Central Bank (ECB) target. In light of the geopolitical uncertainty, central banks are becoming more cautious about monetary easing. In the first quarter of 2025 Italian GDP grew by 0.3 per cent respect to the previous quarter, while in spring, according to preliminary data from Istat, it recorded a slight decline (-0.1 per cent), the first in two years. Compared to the euro area, the pace of growth in the first quarters of the year was more subdued. Household spending continues to increase moderately, supported by employment but held back by the propensity to save. Investment recovered in the winter but the outlook appears uncertain, partly due to international tensions. Exports jumped in the first quarter, although this was temporary as it was aimed at bringing forward sales to the United States ahead of new tariffs. After recovering in the winter months, manufacturing weakened in the spring, but according to the Parliamentary Budget Office (PBO) indicator, the credit market is showing some signs of easing. In Italy, price dynamics are slightly below the European average, with wages accelerating but remaining well below 2021 levels in real terms.

Confidence among households and businesses deteriorated slightly in the second quarter and the PBO's uncertainty index worsened rapidly. The PBO estimates that Italy's GDP will grow by 0.5 per cent both this year and in 2026. Compared with the projections made for the endorsement of the Public Finance Document (DFP) 2025, the estimates have been revised downwards, this year due to the unexpected slowdown in the spring and in 2026 due to the strong appreciation of the euro. The Italian macroeconomic outlook remains surrounded by considerable uncertainty and downside risks, mainly attributable to US protectionism and the implementation of the National Recovery and Resilience Plan (NRRP).

[*] *Prepared by the Macroeconomic Analysis Service, coordinated by Libero Monteforte with contributions from Daniela Fantozzi, Cecilia Frale, Alessandro Girardi and Carmine Pappalardo; note completed with information available as of 30 July 2025.*

The international context

Despite geopolitical tensions, spreads on European bonds have narrowed

Conflicts in Ukraine and the Middle East continue, with devastating effects on the populations and economies of the affected countries, despite statements and diplomatic initiatives for a peaceful resolution. The air war between Iran and Israel, which broke out on 13th June and caused the subsequent intervention of the United States, has alerted investors to attacks in the Strait of Hormuz, through which approximately 20 million barrels of crude oil and fuel pass each day, accounting for almost a fifth of global consumption. During the 12 days of attacks, oil and gas prices rose by 9.2 per cent and 15.2 per cent respectively, compared to the average for May and early June, before falling back after the ceasefire between Iran and Israel.

The trade war also continues, with new announcements on US tariffs at the beginning of July and subsequent agreements. With the July announcements, US customs duties were increased mainly on some Asian countries, such as South Korea, as well as Brazil, for which 50 per cent tariffs on copper were announced. In the days leading up to the announcement, the price of copper had already begun to rise, as it had before April 2nd, as it is a strategic raw material for the production of components and for the construction of semiconductors, aircraft, ships, ammunition, data centers and missile defence systems used by the US defence industry.

Trade between the United States and European Union countries was initially expected to be subject to 30 per cent tariffs from August 1st; the political agreement reached with the European Commission provided for a 15 per cent rate for most products, with some exceptions to be clarified shortly; the agreement is expected to include significant investment and purchases in strategic sectors, such as energy and defence, by the EU in favour of the United States. The agreement did not have a major impact on the markets, partly because it had been anticipated. A quantitative assessment of the impact on the European economy is not possible at this stage due to the lack of details on the products involved, exemptions and investments and purchases to be made in the United States.

In addition to the risk factors for trade, the appreciation of the euro over the past six months acts as an "implicit tariff", making euro area products less competitive than those from the United States. The euro has weakened in recent days but remains at very high levels compared to last year, reflecting the diversification of portfolio strategies, with reduced exposure to US securities and increased purchases of securities from other countries.

The resilience of confidence in Europe is reflected in sovereign bond spreads, which are also benefiting from the ECB's accommodative monetary policy. Since last summer, the central bank has embarked on a cycle of easing that has helped improving financing conditions in the euro area, especially for countries with high public debt, by lowering the medium- and long-term yield curve.

In July, the spread between Italian 10-year BTPs and German Bunds reached its lowest level in about 15 years (below 85 basis points in the last few days of July), but remains higher than that of other euro area countries, including Greece, whose bonds since 2023 have lower yields than those of Italy (Figure 1). The decline in the spread on Italian bonds also reflects specific credit factors. Moody's recently raised its outlook on Italy's sovereign rating from 'stable' to 'positive', considenting better-than-expected public finances, political stability, a robust labour market, below-average private debt and a solid banking system. High public debt remains a major vulnerability, therefore economic growth and caution in public finance management are necessary to keep it on a sustainable path.

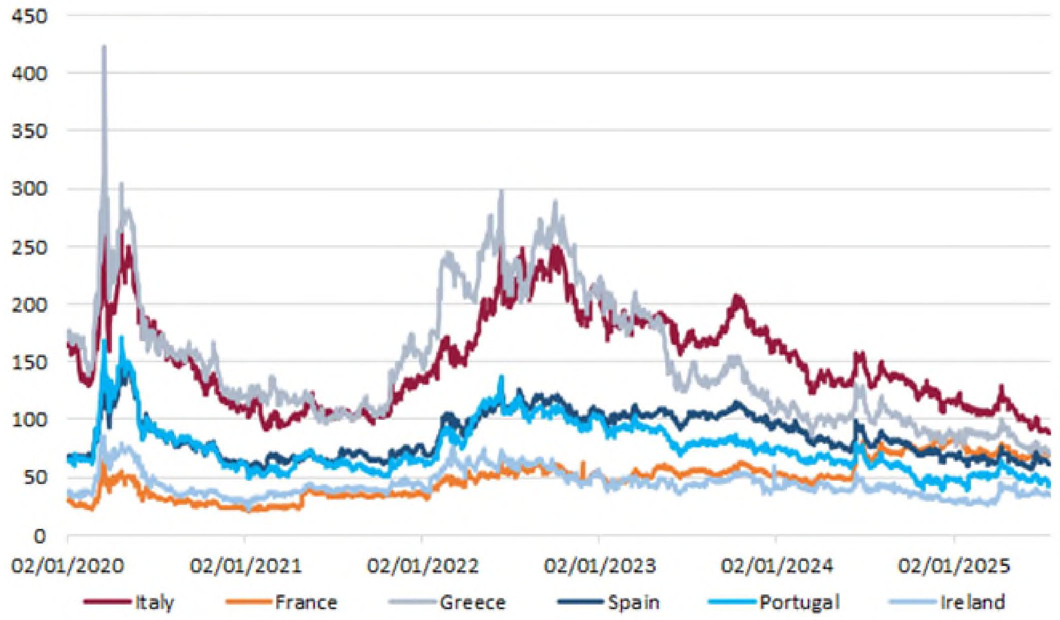
Despite persistent geopolitical tensions, the short-term global outlook is moderately optimistic. The global purchasing managers' index (PMI), which anticipates trends in international demand, increased slightly in June compared to the previous month (to 51.7 from 51.2). The improvement is attributable to manufacturing, where the indicator returned above the 50-point expansion threshold, rising by seven-tenths of a point, partially due to the recovery of the German manufacturing industry. Backlogs also showed a recovery, exceeding the 50-point threshold, thanks to the weak recovery in demand (Figure 2).

Among the high-frequency indicators, during the second quarter of 2025 a rise in the cost of transporting non-liquid raw materials and foodstuffs occurred (from 40.5 to 53 compared to the first quarter), as measured by the Baltic Dry Index. The increase in this indicator, which normally reflects international demand, could be affected at this stage by supply constraints, such as those on shipping in the Strait of Hormuz. The latest international trade data from the Dutch Central Plan Bureau show a modest cyclical decline for April and May, albeit at still relatively high levels (Figure 3). The cost of raw materials slightly decreased between the first and the second quarter of 2025 (75.0 from 76.6), due to demand expectations that incorporated announcements of higher tariffs.

In the United States, GDP resumed growth in the second quarter, expanding by 3.0 per cent on an annualised basis. After the decline in the first quarter, when the economy was affected by the announcement of tariffs and companies accumulated imported inventories in anticipation of the expected tariff increases; the rebound in output during spring was mainly driven by the normalisation of imports and domestic consumption. Conversely, activity in the euro area slowed in the second quarter (to 0.1 per cent from 0.6 per cent in annualised terms). Activity was affected by the slowdown in Germany and Italy (-0.1 per cent), France reported modest growth of 0.3 per cent, while Spain confirmed a faster pace of growth (0.7 per cent) than the area as a whole.

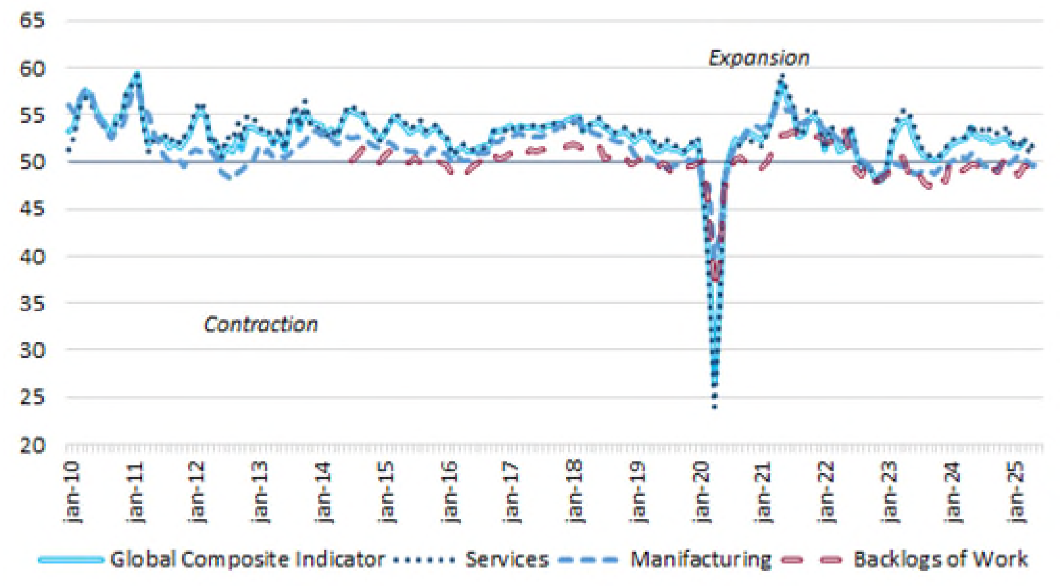
The Chinese economy also slowed in the second quarter, with GDP growth of 5.2 per cent, lower than in the first quarter (5.4 per cent) but higher than expected. In the 'pre-tariff rush', Chinese exporters accelerated shipments in winter in anticipation of the sharp tariff increases announced by the United States; in spring, flows then normalised downwards.

Figure 1 – Spreads of the main European countries with German Bunds
(basis points)



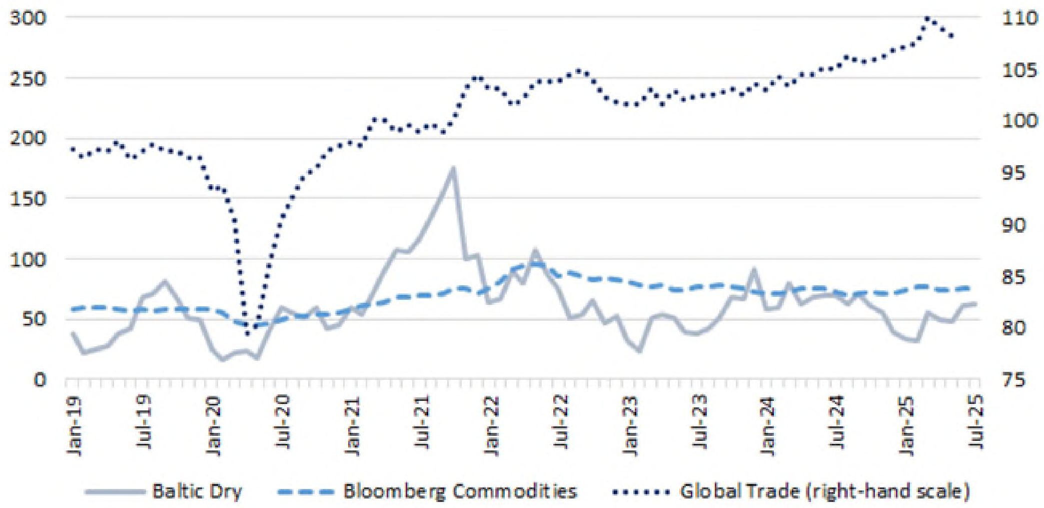
Source: LSEG.

Figure 2 – JP Morgan Global PMI Index



Source: S&P Global.

Figure 3 − Global activity indices
(index numbers, 2010 = 100)



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

International Monetary Fund forecasts

In its latest forecasts, the IMF revised upwards expectations for the major economies compared to April's report (Table 1). On the one hand, the IMF emphasized the marked advance in trade, and therefore in production, in the early months of the year in order to prevent subsequent tariff increases. On the other hand, it assumed trade policies that do not take into account the latest developments and are therefore better than those considered in previous forecasts. Global output is expected to grow by around three percentage points in both 2025 and 2026, slightly below last year's pace (Table 1). The United States is expected to grow by around two percentage points in both years, slightly more than expected in April; the GDP forecast for the euro area has also been slightly improved, but only for the current year. Among emerging countries, the outlook for China has been improved, especially for 2025, given the more favorable than expected developments in the first half of the year, also in conjunction with strong purchases from the United States before the new tariffs came into force. Global trade is expected to slow down both this year and next; expectations for trade in 2026 have been lowered accounting for the marked anticipations at the beginning of this year, before the new tariffs, which will consequently reduce stimulus in the coming quarters.

Table 1 − IMF forecasts

	WEO Update July 2025			Differences from WEO April 2025	
	2024	2025	2026	2025	2026
World product	3.3	3.0	3.1	0.2	0.1
Advanced economies	*1.8*	*1.5*	*1.6*	*0.1*	*0.1*
United States	*2.8*	*1.9*	*2.0*	*0.1*	*0.3*
Euro area	*0.9*	*1.0*	*1.2*	*0.2*	*0.0*
Emerging economies	*4.3*	*4.1*	*4.0*	*0.4*	*0.1*
China	*5.0*	*4.8*	*4.2*	*0.8*	*0.2*
World trade	3.5	2.6	1.9	0.9	-0.6

Source: International Monetary Fund, *World Economic Outlook update*, July 2025.

Volatility on energy commodity markets is growing

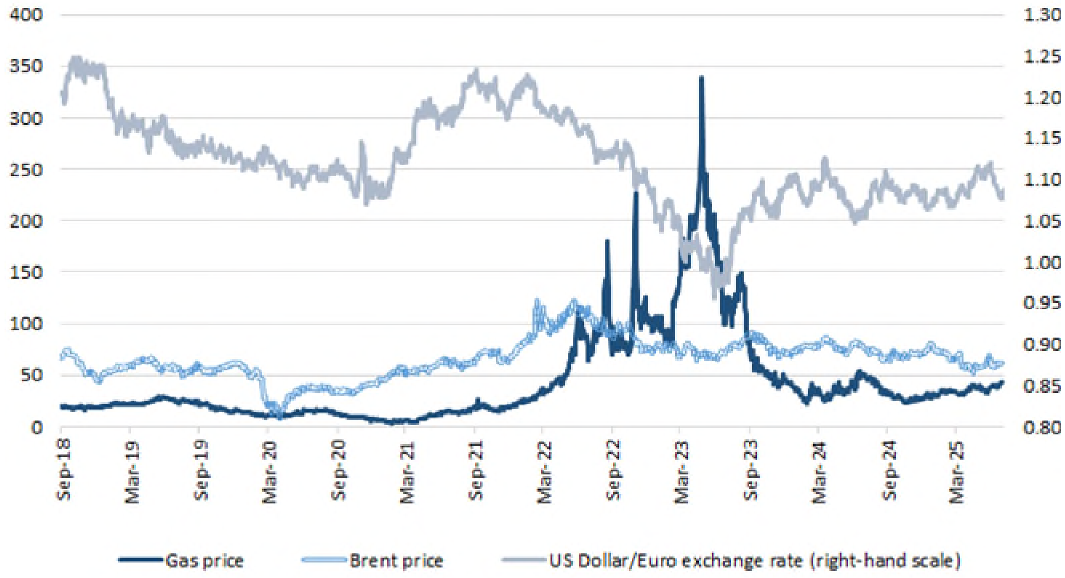
Israel's last June attack on Iran and the US administration's restrictive trade policy have changed operators' expectations and increased volatility on commodity markets. Inflationary pressures are expected in the upstream price formation process, increasing uncertainty about the timing and prices of oil. The commodity market rose sharply during the 12 days of bombing in Tehran (13 to 25 June); Brent prices rose from $68 per barrel (in line with the average for the previous three months) in the first few days of the month to $77 during the attacks, recording a monthly increase of around 11 per cent in June (Figure 4). In July, the price of crude oil fell marginally, despite new announcements on tariffs. The recent statement by OPEC+, whose countries (Saudi Arabia, Russia, Iraq, United Arab Emirates, Kuwait, Kazakhstan, Algeria and Oman) agreed to increase production by 548,000 barrels per day since August, also contributed to the stability of prices. This decision was taken 'consistently with the stable global economic outlook and current strong fundamentals'.

The price of natural gas on the Dutch market (TTF), which had fallen to around 35 euros per megawatt hour in April and May, followed a similar trend to Brent in the days of the attack on Iran, but recorded a moderate increase (to around 36.6 euros per megawatt hour) before falling to less than 34 euros in July.

The European currency has continued to appreciate against the dollar since the beginning of 2025, particularly in the second quarter (to 1.13 dollars per euro, from 1.05 in the previous period). Overall, since the beginning of the year, the euro has appreciated by 13.6 per cent, making goods exported outside the euro area and to the United States less competitive. Statements on US trade policy, with a series of announcements and denials combined with concerns about the sustainability of the budget measures contained in the One Big Beautiful Bill Act (OBBBA), fuelled investor mistrust, which contributed to disinvestment in US equities. In early July, the dollar-euro exchange rate peaked at 1.18, a level not recorded since September 2021, alerting the ECB to possible risks to growth.

In recent days, following the agreement on 15 per cent tariffs for the EU, the euro has weakened but remains at very high levels compared to last year.

Figure 4 – Oil and gas prices and exchange rates
(oil and gas prices in euros)



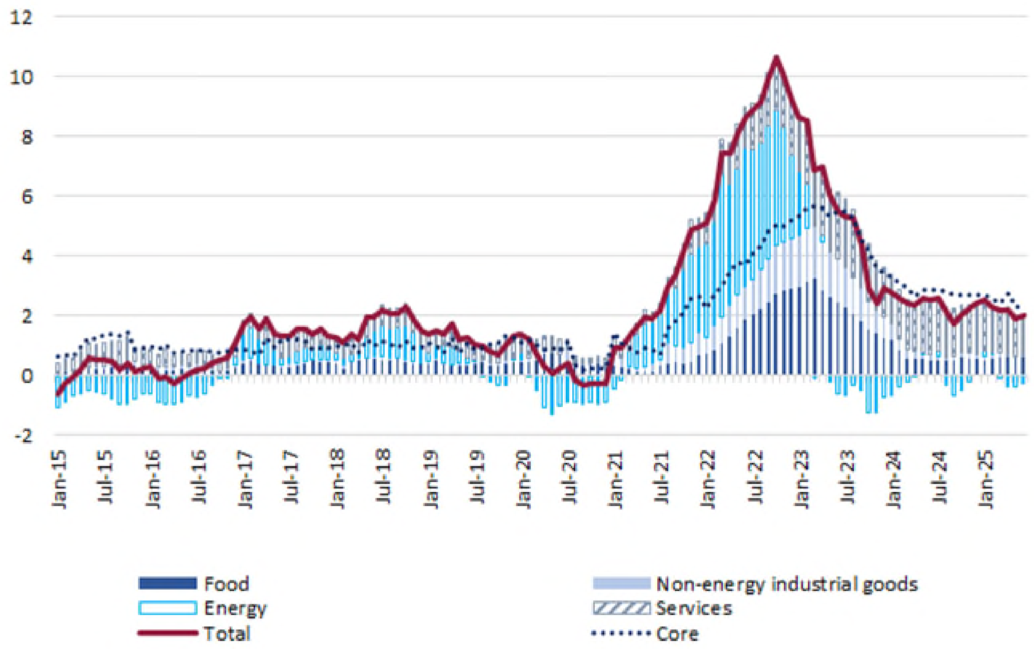
Source: S&P Global.

Inflation in the euro area is converging towards the central bank's target

Inflation in the United States picked up in June to 2.7 per cent, up three-tenths of a point from May; excluding the most volatile components, energy and food, the change in the index was slightly higher (2.9 per cent) but in line with expectations. The acceleration in consumer prices could indicate that companies are beginning to shift the costs of the new tariffs to consumers. PCE price dynamics, which are closely monitored by the Federal Reserve, declined in the second quarter to 2.1 per cent (from 3.6 per cent in the previous period); the change in the core component, which excludes food and energy, also declined in the second quarter to 2.5 per cent (from 3.6 per cent in the previous period).

In the euro area, inflation fell to 2.0 per cent in June, continuing the downward trend that began this year. Core inflation (excluding food, energy, alcohol and tobacco) remains slightly higher (2.3 per cent; Figure 5) than headline inflation, which incorporates the reduction in energy prices. The services component contributes more to inflation than food and non-energy industrial goods, but has shown signs of slowing in the last two months. Price dynamics in Germany and Spain are similar to those in the euro area, slightly lower in Italy (see the section on the Italian economy) and significantly lower in France.

Figure 5 – Euro area inflation (1)
(year-on-year percentage changes and contributions)

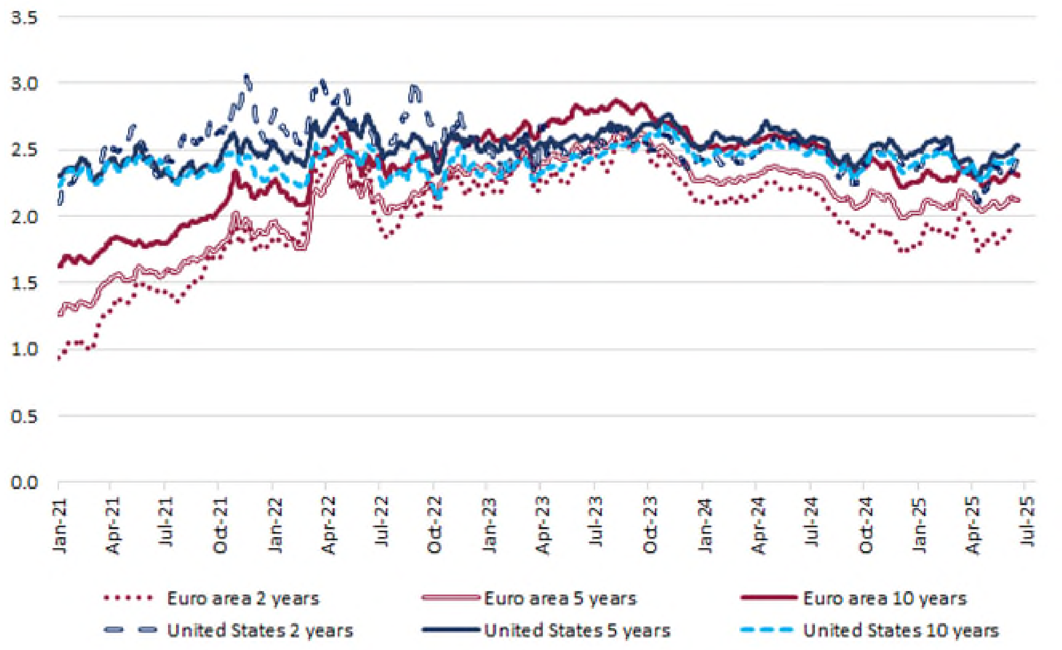


Source: calculations based on Eurostat data.
(1) The sum of the contributions may not correspond to the trend of the total index, as it is linked and processed in greater detail.

Inflation data, which are converging to the ECB's target values, and uncertainties about global tensions led the central bank to decide not to reduce official interest rates at its meeting on 24 July; further monetary policy easing is possible in the autumn, depending on price developments. The Federal Reserve (Fed) also decided in recent days to leave interest rates unchanged.

In the euro area, operators' inflation expectations are broadly stable, thanks to recent data in line with the central bank's inflation target. Compared with the first six months of the year, implicit expectations at various maturities rose slightly in July for the euro area and more markedly for the United States. The United States therefore continues to have higher inflation expectations than Europe for all maturities, particularly over a 10-year horizon (Figure 6); US bond yields are being driven by both restrictive trade policies and uncertainty about fiscal consolidation.

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



Source: LSEG.

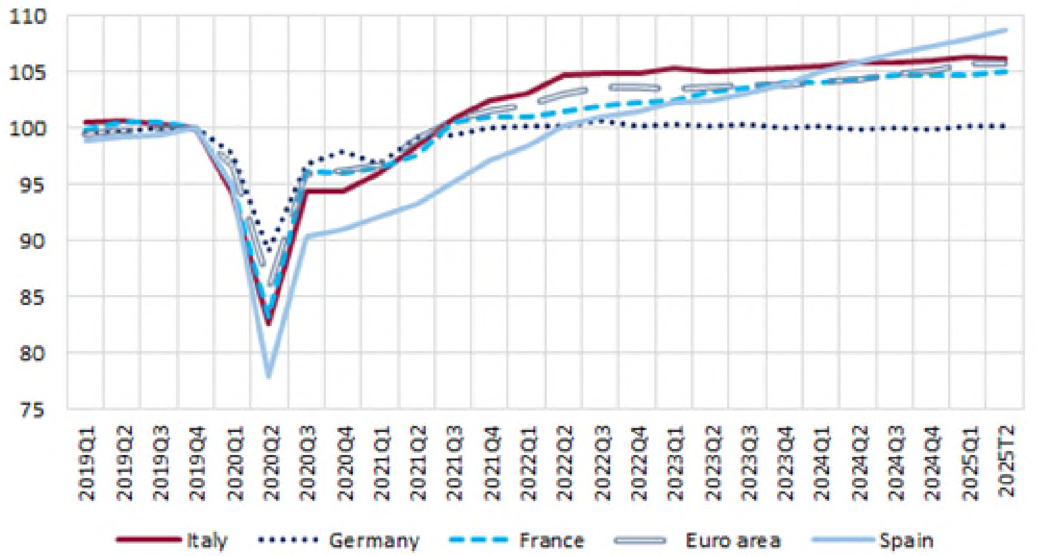
The Italian economy

GDP growth declined in the second quarter

In the first quarter of this year, GDP grew by 0.3 per cent on a quarterly basis. Economic expansion was driven by domestic demand rather than net foreign trade. On the supply side, value added increased in all major sectors except services, where it declined marginally.

In the second quarter, based on preliminary data released at the end of July, GDP fell slightly on a quarterly basis (-0.1 per cent), as had not happened since spring 2023; the change compared with the same quarter of last year narrowed to 0.4 per cent, from 0.7 per cent in the previous period. The statistical carry-over for 2025 growth is 0.5 per cent; however, after adjusting for working days (fewer in 2025 than in 2024), this should result in a reduction to the annual growth figure of about 0.1 percentage points. The contraction in economic activity in the spring months reflected a downturn in agriculture and industry (construction and manufacturing in the strict sense) against a stagnation in services. On the demand side, there was a positive contribution from the domestic component including inventories, which was more than offset by the clearly negative contribution from net foreign demand. Italy's GDP growth in the spring was in line with that of Germany and less favourable than that of the euro area (0.1 per cent) and France (0.3 per cent). Spain's good cyclical phase is confirmed, with the growth remaining at 0.7 per cent q-o-q. Compared with pre-pandemic levels, Italy's economic activity is about six percentage points higher, a gap that is smaller than that of Spain (over eight percentage points) but still larger than those of France and the euro area (about five per cent); in contrast, Germany's GDP level remains broadly in line with that at the end of 2019 (Figure 7).

Figure 7 – Euro area GDP and its largest economies
(index numbers, 2019Q4=100)



Source: calculations based on Eurostat data.

Household spending holds up amid caution

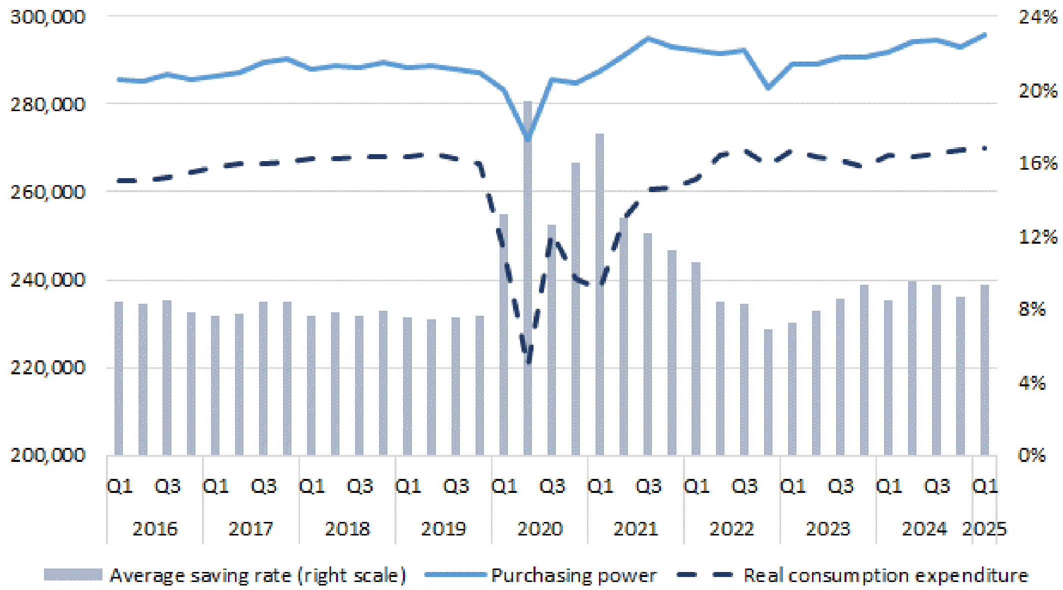
In the first few months of 2025, private spending continued to grow moderately, supported by improved household confidence and the consolidation of the labour market, despite a context marked by uncertainty and international tensions.

In the first quarter of the year, private consumption rose by 0.2 per cent on a quarterly basis, in line with the recovery that began in the second half of 2024. Household spending benefited from stronger purchasing power, which grew by 0.9 per cent compared with the previous quarter. The increase in nominal disposable income (1.8 per cent) more than offset the rise in consumer prices. Against this backdrop, the savings ratio rose by 0.6 percentage points to 9.3 per cent of disposable income, still higher than pre-pandemic levels (Figure 8).

Household spending appears to be continuing to expand, albeit at a moderate pace. According to PBO calculations, Confcommercio's seasonally adjusted consumption indicator (in volume) rose in the second quarter compared with the average for the first three months of the year, thanks to growth in the services component and, to a greater extent, in the goods component. Istat data on retail sales for April and May indicate stability for both food and non-food goods.

Less favourable signs emerge from consumer opinions, which, on average for the spring months, were revised downwards compared to the first quarter, both in terms of the personal and the general economic climate. The most recent surveys, referring to July, indicate a slight improvement in assessments of the personal, current and future situation, while the overall economic climate worsened.

Figure 8 – Purchasing power, consumption and household propensity to save *(millions of euros, values chained to 2020 and percentages)*



Source: Istat.

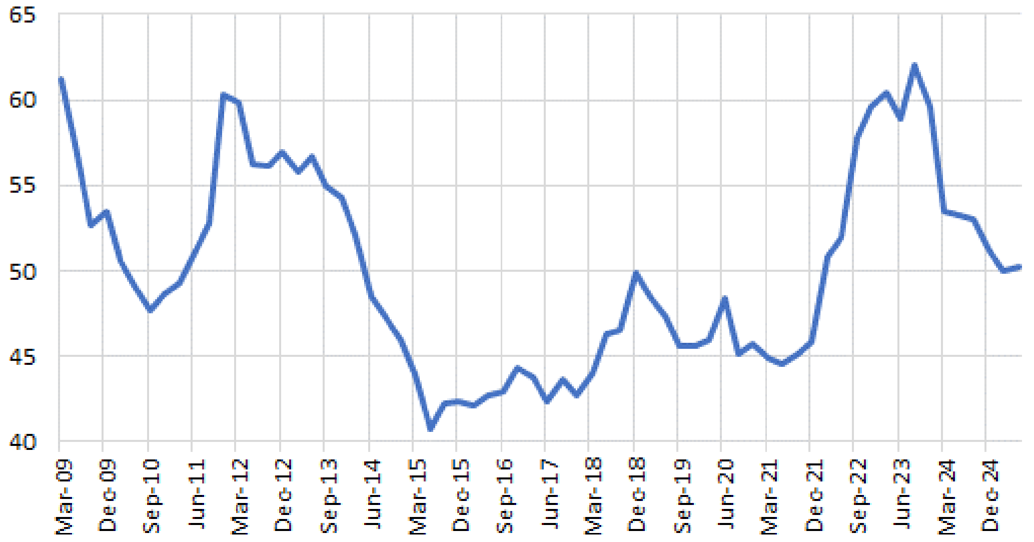
Capital accumulation remained buoyant but with uncertain prospects

In the first quarter of the year, investment increased by 1.6 per cent, confirming the sustained growth observed in the latter part of 2024. Accumulation grew in almost all components, housing (1.7 per cent), non-residential buildings (1.8 per cent), intellectual property products (1.7 per cent) and, to a lesser extent, plant and machinery (1.2 per cent). Over the same period, the profit share, measured as gross operating profit as a percentage of value added at basic prices of non-financial corporations, declined slightly compared with the previous quarter (to 42.1 per cent), in line with the trend observed since early 2023. Profit margins remained broadly unchanged in manufacturing and declined again in private services; they remain on average higher than pre-pandemic levels. The *mark-up* for the total economy remained broadly stable, in line with the average figure for the last two years and higher than pre-pandemic levels.

The outlook for capital accumulation appears uncertain. Qualitative surveys conducted in the spring point to unfavourable conditions for investment activity. The Bank of Italy's survey of inflation and growth expectations, conducted between May and June, also reports a negative assessment by industrial and service companies of the general economic situation and demand expectations, especially in manufacturing. Capacity utilisation in the second quarter continued the downward trend of recent years, standing at 72.2 per cent, just above the low recorded at the end of last year.

On the other hand, the share of companies reporting obstacles to production decreased compared with the first quarter (from 35.5 to 33.5), returning to a value close to the 2024 average; moreover, there are signs of easing in the credit market. According to the latest Bank of Italy survey on bank lending, credit demand remained subdued at the beginning of 2025, remaining virtually unchanged from the slight increase recorded in the fourth quarter of the previous year. The decline in interest rates was not sufficient to stimulate a recovery in demand, as businesses increasingly relied on self-financing. On the supply side, banks remained cautious in their lending conditions, reflecting increased risk perceptions amid a worsening economic and geopolitical environment. Surveys conducted among businesses confirm that access to credit remained broadly unchanged in the first quarter. In contrast, the PBO indicator of difficulties in accessing the credit market shows a gradual easing of tensions in recent quarters. compared with the peaks recorded at the beginning of last year (Figure 9).

Figure 9 – PBO indicator of difficulties in accessing credit (1)
(diffusion index; threshold between restrictive and expansionary conditions = 50)



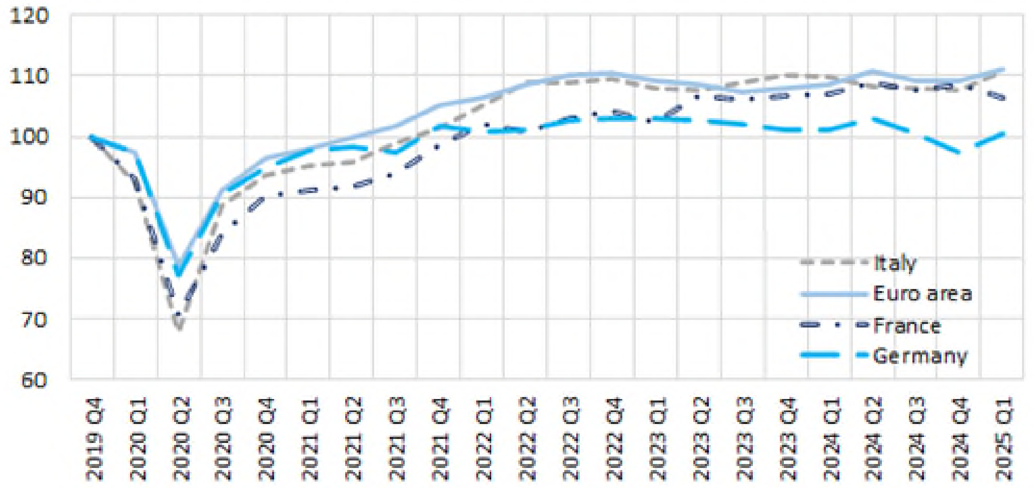
Source: calculations based on Istat data.
(1) For methodological details, please refer to PBO's Report on Recent Economic Developments- October 2023.

Exports are expected to be volatile due to tariffs

On average, in the first three months of this year, the volume of Italian exports of goods and services jumped by 2.8 per cent, against the contraction that had characterised the quarters of last year. Overall, exports in volume terms resumed growth, with positive contributions from the pharmaceutical sector, as well as from metallurgy, motor vehicles and the food industry. Exports of services also increased, supported in particular by business services. Italian export flows remain stronger than those of its main European trading *partners* and the euro area (Figure 10).

The recovery in foreign sales in the winter reflected the acceleration in sales to the United States, attributable to US importers anticipating higher tariffs. These tariffs were subsequently confirmed by the recent US-EU agreement, which sets a 15 per cent tariff on most exports, although with exemptions for strategic products to be specified in detail shortly. According to PBO estimates, in April-May, flows to the United States declined significantly, partly due to the gradual appreciation of the euro against the US currency. In the second quarter, foreign demand continued to show signs of weakness, as indicated by the Istat survey of manufacturing orders; even the PMI index, despite showing a partial recovery, remained below the expansion threshold.

Figure 10 – Export flows of the euro area and its three largest economies
(index numbers, 2019Q4=100)



Source: Eurostat.

In the first three months of 2025, the current account surplus, net of seasonal factors, declined slightly to 1.2 per cent of quarterly GDP, compared with 1.4 per cent in the previous period. The balance remains in line with the average levels of 2024, marking a period of stability after the reabsorption of the effects of the 2022 energy shock.

At the beginning of the year, imports rose sharply (2.6 per cent compared with the fourth quarter of 2024), driven by purchases of services from abroad. The expansion of imports also reflects the strengthening of the variables that usually drive them, in particular gross fixed investment and exports. Against a backdrop of increased purchases of goods from euro area partners, there was a sharp contraction in imports from non-EU countries, concentrated mainly on mechanical products and energy raw materials. Overall, slightly lower import growth than export growth resulted in a positive contribution of net foreign demand to GDP growth in the first quarter (0.1 percentage points), in contrast to the trend observed in 2024.

The recovery in manufacturing observed in winter appears to be temporary

After five consecutive quarters of decline, industrial production showed initial signs of recovery in winter, followed by a virtually flat trend in the second quarter. However, the latest turnover data for May paint a less favourable picture, with a negative change in the average for the spring months (-1.4 per cent) compared with the January-March period. Economic surveys point to a slowdown in the second quarter: in June, the PMI index fell to 48.4, reflecting the decline in domestic and foreign orders due to persistent weakness in demand and global uncertainty. The Istat index of manufacturing business confidence remained virtually unchanged compared with the first quarter, before recovering in July.

After the jump observed in April, the seasonally adjusted construction output index fell in May (-1.4 per cent); nevertheless, the change in the second quarter compared with the average for the first three months of the year remains positive (1.1 per cent). The assessments of construction companies appear mixed: the Istat confidence index fell in the second quarter of 2025, reflecting the decline in the buildings component, which was only partially offset by increases in civil engineering and specialised construction works. The construction sector, on the other hand, is holding up according to the PMI index, which stands just above the growth threshold in the second quarter (50.2); the trend in orders and employment points to favourable developments in the coming months.

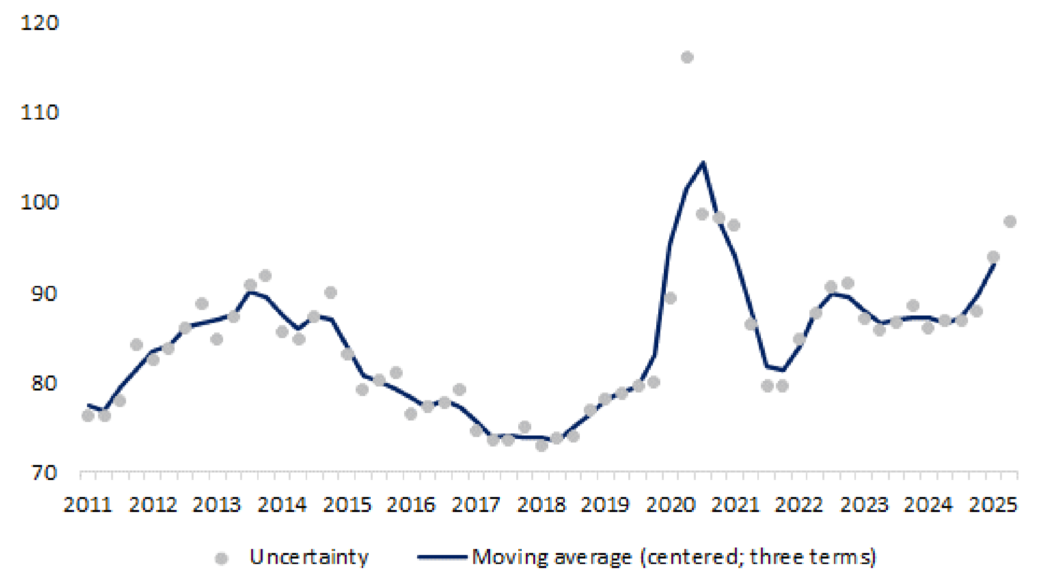
After the stagnation of last autumn, in the first three months of 2025, the value added of services recorded a marginal contraction (-0.1 per cent on a quarterly basis). In the second quarter the confidence index for the sector declined compared to the average for the first three months of the year, due to a widespread downward revision of the assessments of orders and business trends and expectations for orders. However, the PMI for the tertiary sector remained in expansionary territory in June at 52.1 (down from 53.2 in May, the highest level in almost twelve months). Based on Istat's preliminary national accounts for the second quarter, the added value of services is expected to have remained virtually unchanged, as in winter.

With regard to business start-ups, according to Movimprese data, in the first three months of 2025, the balance between registrations and closures was negative, by approximately 3,000 units, offsetting the positive balance of the last quarter of last year. The business demographic remains sluggish, with both registrations and closures showing a substantial downward trend over the last fifteen years. In terms of business type, limited companies were the only legal form with a positive balance. Central Italy was the only area with a favourable demographic trend. At the sectoral level, growth in professional and technical activities continued, while the decline in businesses in traditional sectors such as trade, agriculture and manufacturing continued.

According to data from the Bank of Italy's international tourism survey, in 2024 Italy's tourism balance of payments continued along the growth path already outlined in the previous three years: the surplus reached €21.2 billion, equal to 1.0 per cent of GDP, a level similar to that recorded in 2019, before the pandemic. Provisional data for the first quarter of 2025 point to a further improvement, with a surplus about one-sixth higher than in the same period of the previous year, supported by a 6.4 per cent increase in foreign tourist spending in Italy.

Overall, the composite business confidence index, calculated as the weighted average of sectoral climate indicators, fell by almost two points in the second quarter, reflecting declines in construction and services. In the most recent period, uncertainty among households and businesses, as measured by the PBO, has further increased, driven by both the business and household components (Figure 11).

Figure 11 – PBO indicator of uncertainty
(index number, 1993 Q1=100)



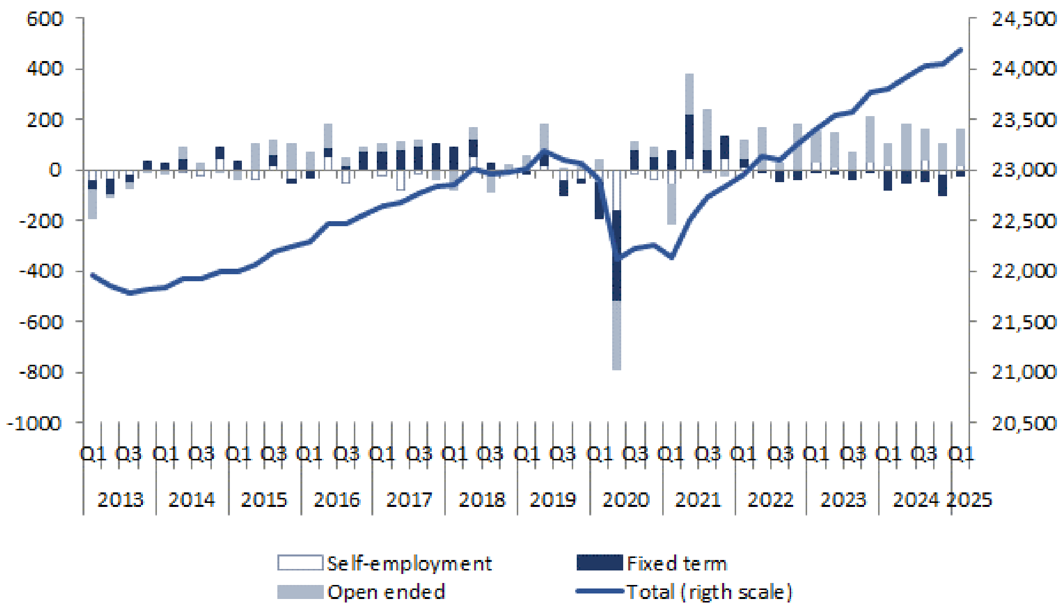
Source: calculations based on Istat data.

Employment returns to growth and wage dynamics recover

In winter employment resumed growth after the stagnation recorded in the final months of last year. The increase in employment levels (0.7 per cent on a quarterly basis) was driven by the recovery in services (0.9 per cent, from -0.3 per cent in the previous quarter) and the favourable performance in construction; by contrast, the number of employed remained unchanged for the second consecutive quarter in manufacturing and declined in agriculture. Labour input strengthened (1.0 per cent) more than employment, leading to an increase in average hours worked per employee, particularly in construction and, to a greater extent, in services, where tensions between labour supply and demand persist; by contrast, hours *per capita* remained unchanged in manufacturing for the third consecutive quarter, where there was greater use of wage supplementation instruments. Hourly productivity declined (-0.7 per cent), particularly in the tertiary sector, where output levels appeared to have stagnated since the second half of 2024.

In the first quarter employment benefited from the permanent component (0.9 per cent based on the Labour Force Survey) and a marginal increase in self-employment; by contrast, the long cycle of decline in fixed-term employment, which has been ongoing since the second quarter of 2022, continued (Figure 12). The increase in employment is mainly attributable to the older age group (50-64), which contributed significantly to the post-pandemic recovery. This phenomenon is driven by both demographic transition (the gradual ageing of the *baby boomer* cohort*)* and the raising of retirement requirements, which are keeping older workers in the labour force.

Figure 12 – Employed and self-employed
(absolute quarter-on-quarter variations; levels)



Source: Istat.

Preliminary data available for the second quarter point to a slight slowdown, due to a marginal decrease in employees, mainly reflecting a decline in temporary work; on the other hand, there was an acceleration in self-employment.

According to flow data from the INPS Labour Market Observatory for the non-agricultural private sector, permanent jobs, net of terminations, increased (5.6 per cent in the first quarter compared to the same period a year earlier), also supported by the increase in conversions of fixed-term contracts; fixed-term, seasonal and intermittent employment contracts, on the other hand, decreased. On a sectoral basis, the net change in jobs was driven by construction, against declines in trade and tourism services.

The use of wage supplementation measures, which had already been on the rise since last year, intensified in the winter months due to increased requests for authorized hours under the wage supplementation scheme (Cassa integrazione guadagni, CIG) in industry in the strict sense; applications were concentrated on the CIG used in cases of corporate reorganisation or restructuring (CIG straordinaria), which increased by more than two-thirds year-on-year. Wage growth slowed in construction and declined in trade.

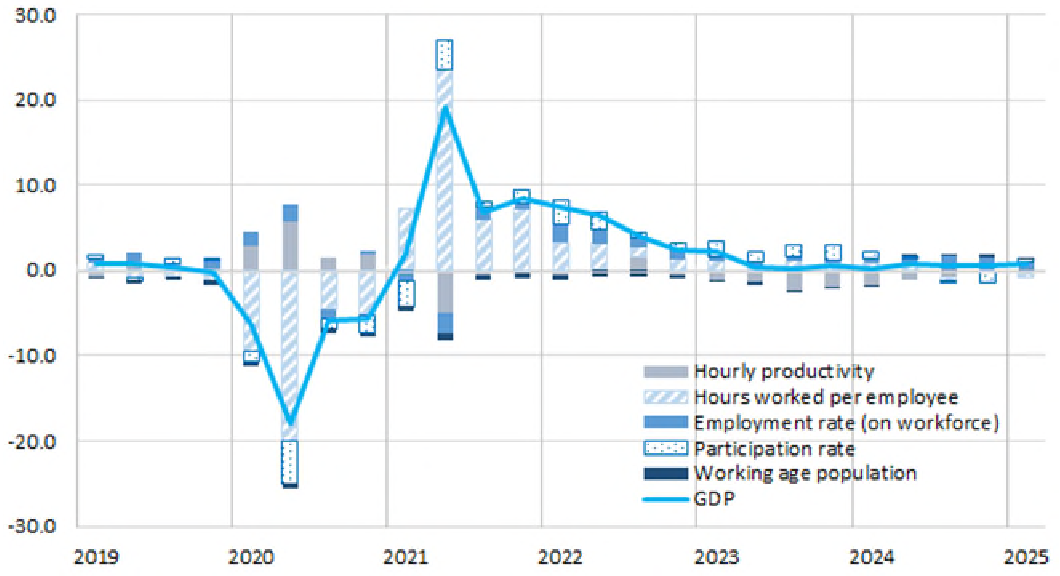
In the first quarter, the participation rate (15-64 years) rose again (to 66.9 per cent), reflecting increases in the older age groups. The expansion of the labour supply also incorporated the increase in the number of job seekers, after last year's decline, driven by the young individuals (15-34 years) and women. The unemployment rate (15-64 years) remained unchanged at 6.2 per cent and rose slightly in the spring months on average.

The number of inactive individuals, which grew throughout 2024, declined in the winter quarter, particularly among women and in all age groups except the youngest. The decline affected those closest to the labour market, i.e. those available to work but not actively looking for a job, who are more likely to enter the labour force when demand increases. The inactivity rate fell to low levels (33.1 per cent), similar to the degree of labour underutilization (15.3 per cent of the extended labour force).

The year-on-year change in GDP in the first quarter was mainly driven by the employment rate, as shown by the breakdown in terms of the main labour market variables, hourly productivity and demographics. This trend was also supported by labour market participation, which had been negative in the second half of 2024, and by slight growth in the working-age population, favoured by the larger share of older people (Figure 13). By contrast, the contribution of hourly productivity and hours worked per employee was negative.

Contract wage growth remained relatively high in the private sector (4.5 per cent year-on-year growth in the first quarter of the year), while it was moderate in the Public Administration sector. Wage pressures were driven by recent contract renewals in manufacturing (food), construction and services (logistics, social and welfare services, electricity), which provided for increases generally higher than the change in the HICP excluding imported energy (the HICP-NIE, estimated by Istat at around 2 per cent on average over the period 2025-27). The change in actual hourly wages in the economy as a whole increased marginally, to 3.3 per cent on an annual basis. The unit labour cost (ULC) trend appeared to be stronger than labour costs, reflecting the decline in productivity.

Figure 13 – Real GDP growth and labour market
(percentage changes; contributions to growth)



Source: calculations based on Istat data.

In the spring months, the change in contractual wages moderated in the private sector (3.3 per cent), partly due to the renewal of the trade contract, which provided for increases in line with the HICP-NIE. In the metalworking sector, the effectiveness of the national collective labour agreement, which expired in June 2024, has been extended until its renewal, ensuring that wage floors are adjusted in line with the previous year's HICP-NIE (1.3 per cent). By contrast, there was an acceleration in the public sector. Overall, contractual wage growth in the first half of the year (3.5 per cent) benefited from the negotiation process in the private sector, where the share of employees awaiting renewal fell compared to the second half of 2024 (to 33.3 per cent). Despite recent increases, real contractual wages in June were still well below (by around 9 per cent) 2021 levels, with a loss of purchasing power in private services (-10.7 per cent) almost double that of industry. Wage growth is expected to slow in the second half of the year, settling at 3.1 per cent on average for the year according to Istat, taking into account contracts in effect until June.

Inflation remains below two per cent, but is higher for services and food

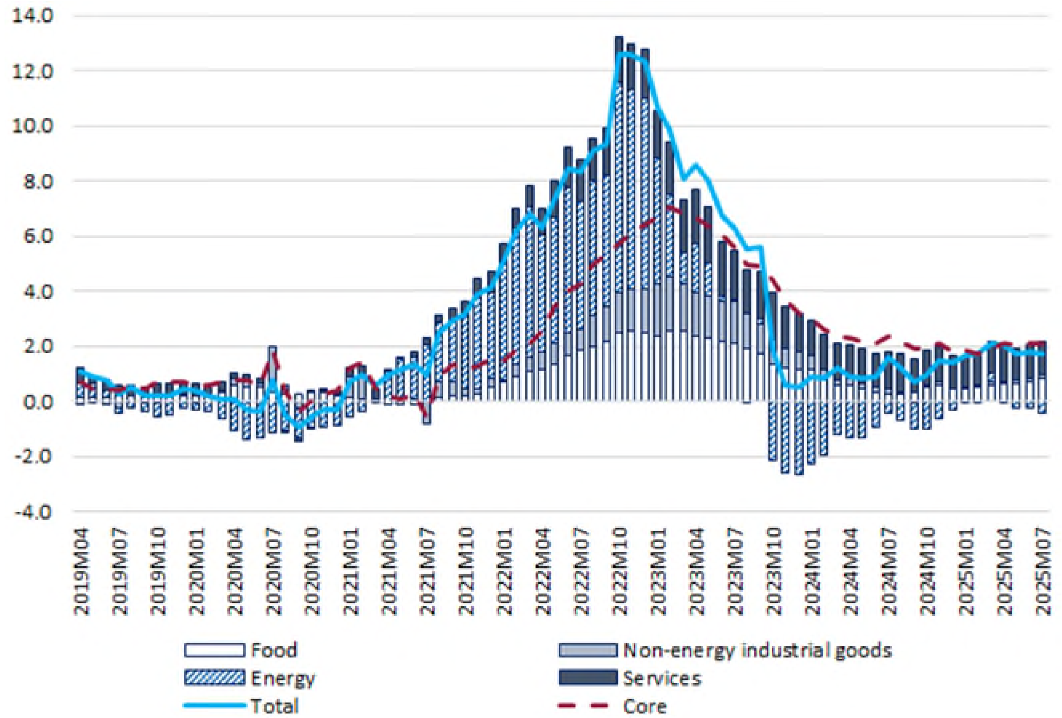
Italian inflation remains below two per cent, with the core component stable; food and service price dynamics remain higher than overall prices. Upstream pressures in the production chain are being absorbed and expectations are subdued, both in the short term and beyond.

In the second quarter of the year, the national consumer price index remained at 1.7 per cent, as in the previous three months. Energy prices fell (-1.6 per cent) due to lower international prices and adjustments to electricity tariffs[2] ; other components accelerated, however, especially food (to 3.1 per cent from 2.2 per cent in the first quarter) and, to some extent, services (to 2.8 per cent from 2.5 per cent) (Figure 14).

In the provisional data for July, inflation (measured by the NIC index) remained at 1.7 per cent, as a result of opposing forces: on the one hand, deflationary pressures in the energy sector intensified (-4.0 per cent from -2.1 per cent in June), but on the other hand, food prices accelerated (3.8 per cent from 3.3 per cent), especially unprocessed food (5.1 per cent from 4.2 per cent); as a result, inflation in the so-called shopping basket also rose (3.4 per cent in July). Overall price dynamics in services lost one-tenth of a point in July, but in some cases there were significant price increases (3.4 per cent year-on-year change for transport). In July, the acquired variation of the NIC index in 2025 reached 1.7 per cent (from 1.4 per cent in June), partly due to base effects.

[2] Decree Law 19/2025 (the so-called 'Bollette Decree') has led to a reduction in prices in the protected electricity market.

Figure 14 – Harmonised Index of Consumer Prices (HICP), contributions of components and core component (1)
(year-on-year percentage changes and contributions to growth)



Source: calculations based on Eurostat data.
(1) The chart shows the contributions to growth of the sectoral components of the harmonised index of consumer prices, as well as the change in the core component. The sum of the contributions may not correspond to the value of the total index, as it is linked and processed in greater detail.

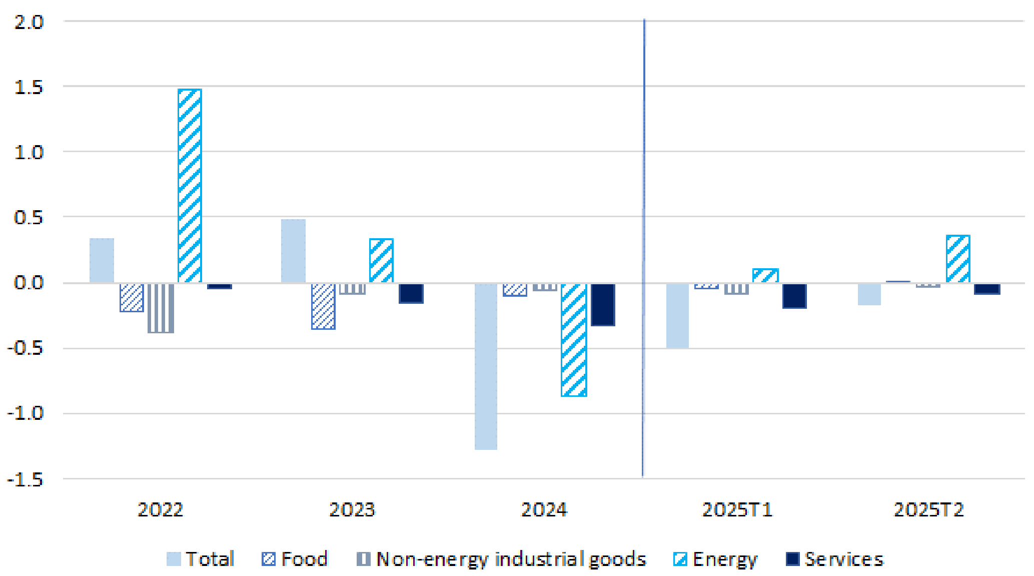
In the last quarter, the negative inflation differential between Italy and the euro area was almost completely absorbed; the gap, mainly attributable to services, narrowed to two-tenths of a percentage point in the spring, while in 2024 it had exceeded one percentage point (Figure 15).

Looking at individual items, the number of those recording subdued price dynamics remains predominant in Italy: in the last quarter, the share of goods and services with inflation below 2 per cent reached 54 per cent, remained at 15 per cent for the 2-3 per cent range, while the percentage of items with inflation between 3 and 5 per cent rose to 19 per cent, with very few others recording higher changes.

Upstream in the production chain, a new deflationary push seems to have returned in recent months, following the recoveries observed between the end of 2024 and the beginning of this year. Import prices have been falling for the third consecutive month and in May were 2.4 per cent lower than the 2024 average, due to lower energy prices in both the euro area and the non-euro area. The upward pressure observed at the beginning of the year also subsided in industry, where producer prices fell by almost 4 per cent on average in April-May compared with the previous three months, thanks to declines in the domestic energy sector. Producer prices in construction, both for buildings and roads, also slowed in recent months, but to a lesser extent. Producer prices in services (3.8 per cent year-on-year in the first quarter of 2025) remained in line with the average for 2024, with some peaks in professional, scientific and technical activities, maritime transport and accommodation.

Consumer and business expectations appear to be stable. The percentage of businesses surveyed by Istat that expect sales prices to remain unchanged is close to 90 per cent, and the share expecting possible increases is now negligible (8 per cent). The Bank of Italy's survey of business expectations also shows that in the second quarter of the year, expectations rose slightly across all horizons, standing at 2 per cent up to 24 months ahead. Purchasing managers surveyed for the PMI index reported that purchase prices fell for the second consecutive month in June, thanks to lower raw material prices and discounts offered by suppliers. As a result, some companies, given the weak demand conditions, sought to remain competitive by lowering their selling prices. At the same time, consumers are optimistic about price pressures: the share of households expecting prices to remain stable is high (almost 40 per cent in June), although lower than the share expecting price increases (58.5 per cent).

Figure 15 – Inflation differentials between Italy and the euro area (1)
(differences in percentage points)



Source: calculations based on Eurostat data.
(1) Differences between Italy and the euro area in terms of total harmonised inflation and the contributions of its components.

Macroeconomic forecasts for the Italian economy

The PBO's macroeconomic forecasts for the Italian economy in 2025-26 are reported below. Compared with the scenario outlined in April, for the endorsement of the Public Finance Document (DFP) 2025, the scenario has been updated to take account of the latest developments in international exogenous variables and on the business cycle. With regard to public finances, full use of the resources of the European *Next Generation EU* (NGEU) programme is assumed. With regard to international trade, the scenario assumes US tariffs on the European Union at 10 per cent, as defined prior to the recent political agreement (see the section on 'Risks to the forecast' at the end of this paragraph and the box on 'Assumptions underlying the forecast'). As with other economic policy measures, only measures that have been approved and fully defined in all their details are considered in the forecasts. The implications of the recent agreement will be assessed once the texts have been fully clarified and disclosed. Over the forecast horizon, it is therefore assumed that there will be no further tariff increases and that no new trade restrictions will be adopted, including by other countries.

Economic activity in 2025-26

The estimates incorporate second-quarter GDP data, which establishes a statistical carry-over for 2025 growth of 0.5 percentage points (adjusting for calendar effects, it could be 0.1 percentage point less in the annual data). According to the PBO's short-term forecast models, economic activity is expected to expand slightly in the third and fourth quarters. In the whole 2025, Italy's GDP is expected to grow by 0.5 per cent (Table 2), supported by good employment dynamics in a context of moderate, albeit slightly rising, inflation. In 2026 GDP growth is expected to remain at 0.5 per cent; stronger investment, driven by the NRRP, would be offset by a deterioration in net foreign demand due to continued protectionism.

Unlike those of other institutions (Table 3), the forecasts presented in this Note take into account the preliminary estimate of GDP for the last quarter (released by Istat on 30 July); the figure came as a negative surprise, as activity was expected to expand, albeit moderately. When comparing the projections for 2026, however, it is necessary to consider the heterogeneity of the assumptions for international exogenous factors, with particular reference to the trade war, for currency markets and for public finances.

Table 2 – Italian economic forecasts (1)

	2024	2025	2026
INTERNATIONAL EXOGENOUS VARIABLES			
World trade	3.3	2.6	1.9
Oil price (Brent, dollars per barrel)	80.6	70.0	66.4
Dollar/Euro exchange rate	1.08	1.13	1.19
Natural gas price (TTF, euro/MWh)	34.4	37.9	33.7
ITALIAN SCENARIO			
GDP	0.7	0.5	0.5
Imports of goods and services	-0.7	2.2	1.9
Final domestic consumption	0.6	0.7	0.6
- Household consumption and non-profit institutions	0.4	0.8	0.7
- General government expenditure	1.1	0.7	0.5
Investments	0.5	0.6	1.7
Exports of goods and services	0.4	1.5	0.7
CONTRIBUTIONS TO GDP GROWTH			
Net exports	0.4	-0.2	-0.3
Inventories	-0.2	0.0	0.0
Domestic demand net of inventories	0.5	0.7	0.8
PRICES AND NOMINAL GROWTH			
Import deflator	-1.8	0.6	-0.6
Export deflator	0.0	1.5	1.3
Consumption deflator	1.4	1.8	1.7
GDP deflator	2.1	2.2	2.0
Nominal GDP	2.9	2.7	2.6
LABOUR MARKET			
Labour cost per employee	2.8	3.2	3.1
Employment (FTEs)	2.2	0.6	0.4
Unemployment rate	6.5	6.0	5.9

(1) Percentage changes, except for contributions to GDP growth (percentage points), the unemployment rate (percentage), the exchange rate and the price of oil (levels). Due to rounding of growth rates to the first decimal place, the sum of the changes in volume and the related deflators may not coincide with the nominal dynamics.

Table 3 – Recent forecasts for Italy's GDP and consumer prices

		GDP		Inflation	
		2025	2026	2025	2026
International Monetary Found (1)	29 Jul	0.5	0.8		
Oxford Economics (2)	25 Jul	0.7	0.5	1.6	1.5
Consensus Economics: (2)	14 Jul				
- average		0.6	0.7	1.7	1.6
- min		0.4	0.3	1.1	1.1
- max		0.8	1.0	2.0	2.0
REF -Ricerche (2)	11 Jul	0.6	0.7	1.5	1.5
Prometeia (2)	25 Jun	0.6	0.7	1.7	1.8
Bank of Italy (1) (2)	13 Jun	0.6	0.8	1.5	1.5
OECD (2)	03 Jun	0.6	0.7		
European Commission (1)	19 May	0.7	0.9	1.8	1.5
MEF DFP 2025 (3)	11 Apr	0.6	0.8	2.1	1.9

(1) Harmonised price index. – (2) Data adjusted for working days. – (3) Consumption deflator.

Forecasts for expenditure components

In the two-year forecast period, economic activity is expected to be mainly supported by domestic demand, with household consumption contributing more than gross fixed investment. The contribution of changes in inventories, which last year subtracted two-tenths of a percentage point from GDP growth, would be virtually nil; on the other hand, the contribution of net foreign demand to GDP growth would be negative, particularly in 2026.

Consumption would benefit from rising employment and moderate inflation. Investment would be boosted by the implementation of the NGEU programme and monetary policy easing, while the negative contribution of net foreign demand would be affected by protectionist tensions arising from US trade policies.

In the two-year period 2025-26, household spending is estimated to grow by around 0.8 per cent, up from last year (0.4 per cent). The expansion of private consumption would be driven by household purchasing power, thanks to stronger disposable income (2.6 per cent in 2025 and 3.2 per cent in 2026) with modest inflationary pressures. The propensity to save, after rising in 2024, is expected to remain at high levels compared to the pre-pandemic period, reflecting a cautious attitude among households in a context of persistent economic uncertainty.

Gross fixed investment is expected to increase in 2025-26 by 0.6 per cent and 1.7 per cent respectively, driven mainly by the accumulation of machinery and equipment; the marked acceleration in 2026 reflects the concentration of resources through the NRRP. Capital accumulation will continue to benefit from favourable financing conditions, but could be affected by a possible postponement of spending beyond 2026 if the Plan is revised.

Overall, gross fixed investment as a percentage of GDP is expected to stand at around 22.0 per cent at the end of the forecast period, a high level by historical standards.

In 2025, exports are expected to grow by 1.5 per cent, a slower pace than global trade (2.6 per cent); the loss of foreign market shares already recorded in the last two years is expected to continue, exacerbated by the appreciation of the euro and protectionism. Imports, up by 2.2 per cent, would grow at a faster pace than foreign sales, partly due to the strengthening of the euro against the dollar. In 2026, exports are expected to slow to 0.7 per cent, compared with stronger global trade (1.9 per cent). By contrast, imports are expected to grow by 1.9 per cent, still supported by the appreciation of the exchange rate.

The current account balance, which returned to positive territory in 2023 largely due to the absorption of the energy deficit, is expected to reach 1.3 per cent of GDP in the two-year forecast period, marginally above last year's figure.

Labour market and inflation forecasts

Employment, measured in terms of full-time equivalent units (FTEs), is expected to increase on average over the two-year period 2025-26 by 0.5 per cent, broadly in line with output, incorporating a reduction in hours worked. Growth in employment, as defined by the Labour Force Survey, would be stronger than output growth this year, given the high demand for labour in some sectors, but is expected to halve in 2026. The employment rate (15-64 years) is expected to increase at a faster pace than the participation rate, particularly this year. Labour supply would expand moderately, mainly driven by the older segment of the labour force. The decline in the number of people seeking employment is expected to continue this year and slow in 2026. The unemployment rate is projected to fall to just below six per cent at the end of the forecast period (from 6.5 per cent in 2024).

Inflation, measured by the household consumption deflator, should rise moderately over the two-year forecast period (to 1.8 per cent on average), reflecting contrasting impulses mainly from external factors. Lower expectations for energy prices and the appreciation of the euro against the dollar are helping to contain price dynamics. The main upward pressures come from the costs of production factors, especially non-energy industrial goods, which would ultimately be reflected in consumer prices.

Wage growth in 2025-26 (slightly above three per cent on average) exceeds price growth, supporting household purchasing power, but real wages would remain more than three percentage points below 2021 levels at the end of the period. The growth of the GDP deflator, at around 2.1 per cent on average over the projection horizon, exceeds that of the private consumption deflator, as it is also driven by the terms of trade. On the supply side, the GDP deflator would be driven mainly by labour costs and, to a lesser extent, by corporate profit margins.

The main revisions compared with the spring forecasts

Compared with the macroeconomic scenario outlined by the PBO in April, when the 2025 DFP forecasts were endorsed, economic activity projections have been revised downwards slightly this year (by 0.1 percentage points), incorporating the unexpected decline in GDP in the second quarter. The lower GDP growth for 2026 (by 0.2 percentage points) is mainly affected by the sharp appreciation of the euro, which reduces price competitiveness and dampens net exports. With regard to price variables, the private consumption deflator has been revised downwards, by around 0.4 percentage points on average over the forecast period, due to lower import inflation pressures.

Risks to the forecast

The macroeconomic scenario for the Italian economy is exposed to risks that are overall on the downside, mainly because of international conflicts and the slow progress of the NRRP projects.

Geopolitical tensions are a primary source of uncertainty. The ongoing wars and the tightening of trade restrictions by the United States are having negative effects on economic activity, which are difficult to quantify at this stage. The overall impact of protectionism will depend on various factors, such as the duration of the restrictive measures, the retaliatory response by trading *partners* and the reactions of financial markets, central banks, businesses and consumers. In Europe the outlook for the German economy remains uncertain, as signalled by the decline in GDP in the second quarter, but significant stimulus for military spending and infrastructure is expected in the medium term. Expectations for world trade in 2026 are highly divergent, with several analysts forecasting expansion, albeit at a slower pace, while some predict a contraction.

Risks related to the timing of interventions financed by the NGEU programme over the next five quarters weigh on investment forecasts in Italy. This concentration could create bottlenecks on the supply side, slowing growth. Any rescheduling of planned spending would lead to a significant deterioration in the macroeconomic outlook for 2026.

The new phase of announcements in the first half of July by the United States on the introduction of new tariffs, followed by agreements such as the one with the EU (announced but not fully defined on 27 July), has contributed to heightening global uncertainty and volatility in financial markets; in response, central banks appear to be adopting a more cautious approach.

Last but not least, climate and environmental risks remain a structural vulnerability. Global warming continues to generate extreme weather events with direct impacts on prices – particularly for food and energy – and on production capacity. The increasing frequency and intensity of such events require governments and private operators to allocate resources for prevention and emergency management.

Box – Assumptions underlying the forecast

Assumptions about the international environment. − The forecast covers the two-year period 2025-26 and is based on updated international exogenous variables and technical assumptions applied to market prices available on 28 July. In particular, the following assumptions are made: 1) a slowdown in world trade in goods and services in 2025 (2.6 per cent compared with 3.3 per cent in 2024), which would continue in 2026 (1.9 per cent); global trade forecasts assume 10 per cent tariffs on Italian exports to the United States and do not take into account the recent agreement with the European Commission, as the details of the rates, exemptions and commitments on purchases and investments from the EU have not yet been defined; 2) a gradual easing of monetary and credit conditions, with the short-term interest rate in the euro area expected to be 2.1 per cent this year (down from 3.6 per cent in 2024) and falling further to 1.7 per cent in 2026; 3) an appreciation of the dollar against the euro to 1.16 on average over the period 2025-26 (from 1.08 in 2024); 4) a decline in the price of crude oil to 70 dollars per barrel, followed, according to *futures* market prices, by a further decline to around 66 dollars in 2026; 5) a temporary rise in euro gas prices this year to €37.9/MWh, followed by a decline to around €34/MWh in 2026. The public finance framework incorporates the measures contained in the 2025 budget and the full implementation of the projects financed under the NRRP.