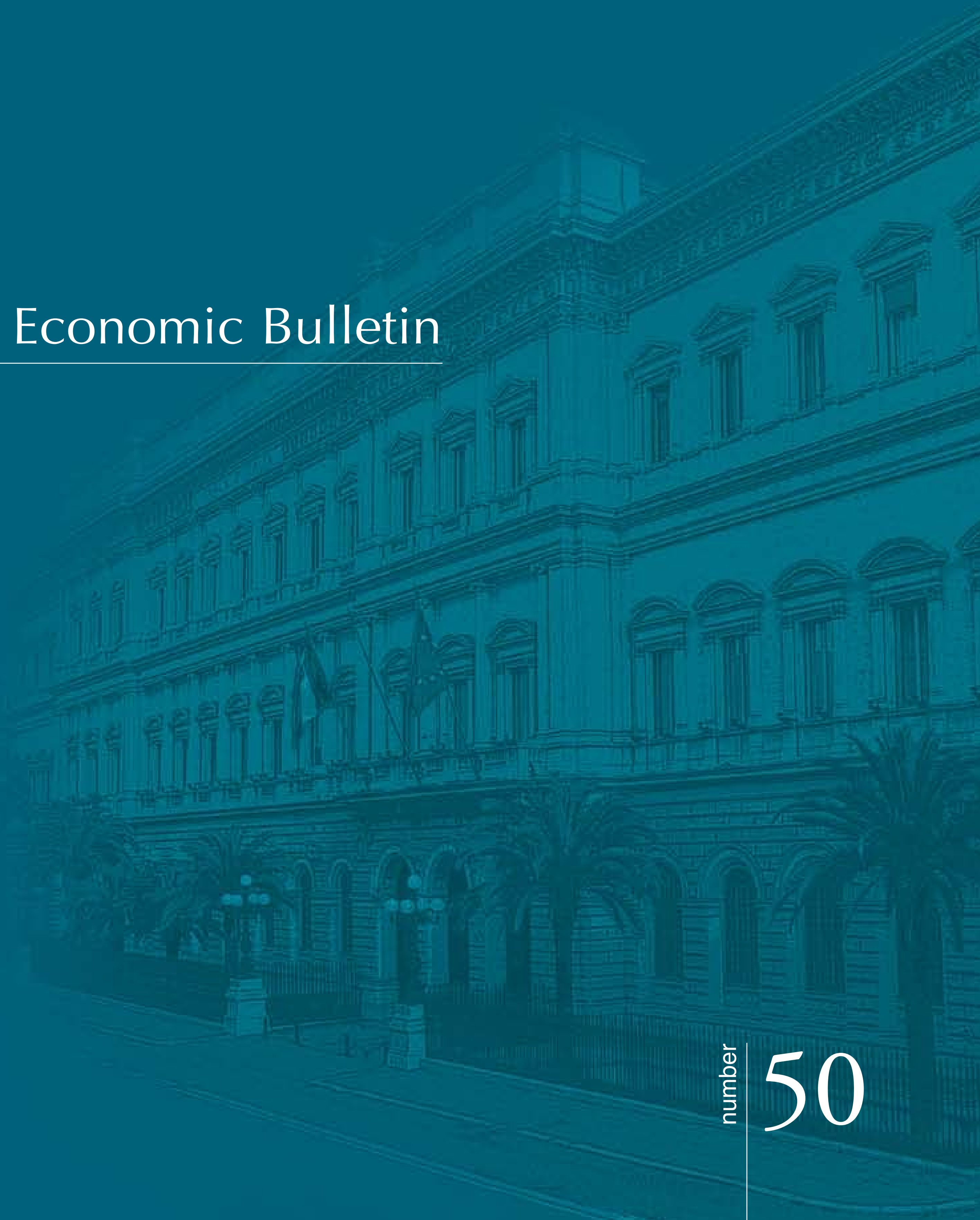
BANCA D'ITALIA

EUROSISTEMA

Economic Bulletin



October 2008

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SYMBOLS AND CONVENTIONS

Unless indicated otherwise, figures have been computed by the Bank of Italy.

In the following tables:

–	the phenomenon in question does not occur
....	the phenomenon occurs but its value is not known
..	the value is known but is nil or less than half the final digit shown
::	the value is not statistically significant
()	provisional; estimates are in italics

1 OVERVIEW

Massive, coordinated action to defend the stability of financial systems

The global financial crisis that began last year in the US subprime mortgage market worsened very sharply in September, bringing down several of the largest American and European financial institutions, causing stock markets to plummet and sparking fears of financial collapse and recession in the advanced economies. Widespread worries over possible counterparty insolvency following the failure of the Lehman Brothers investment bank blocked the wholesale markets where banks procure funds, first of all the interbank market. In the face of these grave events, governments and monetary authorities reacted with steadily increasing force and enhanced international coordination. Central banks countered the seizing-up of their national interbank markets with liquidity injections unprecedented both in magnitude and in mode. On 8 October the European Central Bank, the Federal Reserve, the Bank of England, the Bank of Canada, the Swedish Riksbank and the Swiss National Bank, with the support of the Bank of Japan, decided a concerted half-point reduction in interest rates – again, an unprecedented action. The United States and some European countries, including Italy, have prepared exceptional measures to recapitalize banks using public funds or to purchase hard-to-value, illiquid assets (as in the US, where up to $700 billion was made available to this end), while simultaneously extending and strengthening deposit guarantees. Specifically, on 8 October the UK Government unveiled a comprehensive plan to support the British financial system making provision, amongst other things, for State guarantee of new bank liabilities and direct public intervention in banks' capital; on 9 October the Italian Government, in addition to guaranteeing bank deposits, approved special procedures to intervene using public funds in banks' capital and to enable the Bank of Italy to more effectively support banks' liquidity in emergency situations. On 10 October the G7 finance ministers and central bank governors formally pledged to support financial institutions whose insolvency might have systemic repercussions and adopted all necessary measures to unfreeze the credit and money markets. On 12 October, the euro-area countries, acting in agreement with the EU Commission and the European Central Bank, approved a concerted action plan and urged the other EU countries to adopt its principles. The plan provides for individual national governments to take coordinated measures to facilitate bank funding (government guarantee for new medium-term debt issuance) and recapitalization (government subscription of preference shares or other instruments). In the days that followed, the competent authorities were called on to take measures to allow financial and non-financial institutions to value their assets in accordance with reasonable assumptions on default risk rather than immediate market value. On 13 October the Italian Government followed up on these Eurogroup decisions by adopting measures to enhance the liquidity of banks' securities portfolios and facilitate fund-raising in the market. For its part, the Bank of Italy took steps to facilitate Italian banks' recourse to Eurosystem refinancing. On 14 October the US Government, acting in agreement with the Federal Reserve, adopted further measures aimed at fostering the recapitalization of financial institutions with public funds, extending the federal government guarantee of their liabilities and assisting the financing of companies through Federal Reserve purchases of commercial paper. After falling some 30 per cent between 1 September and 10 October, in the days following the main world stock markets recouped part of the loss.

The growth forecasts for all the advanced countries are revised downwards

In early October the International Monetary Fund sharply lowered its growth forecasts for all the advanced countries. GDP growth rates over 2009 as a whole are expected to be close to zero and negative in some cases. The underlying assumption is that the efforts of the authorities to stabilize the markets and economies will succeed, so that activity will start recovering gradually in the course of 2009. This process is expected to benefit from the recent sharp declines in energy and commodity prices and the continuing growth of the main emerging economies. Inflation is expected to decline everywhere. On the other hand, the IMF lists a series of risks that, should they materialize, would make the recession deeper and longer; these risks have increased with the growing severity of the crisis on the financial and credit markets.

In Italy, the cyclical indicators are negative

In Italy, the rebound in economic activity in the first quarter was followed by a succession of signs of weakness. GDP contracted in the second quarter with respect to the first. The short-term picture indicates stagnation for the rest of the year. Productivity, which reflects the Italian economy's structural shortcomings, is being hurt by the cyclical downturn. Inflation is easing because of the fall in oil prices and the weakness of demand.

Consumption is contracting and the cost of household borrowing rising

The expenditure of Italian households fell by 0.3 per cent in the first six months of the year compared with the first half of 2007. Disposable income grew over the same period by a modest 0.5 per cent; despite the increase in nominal income due to the renewal of some contracts, this was half the figure in 2007 and reflected the rise in the prices of consumer goods caused by that in the international prices of raw materials. The deterioration in the economic cycle influences expectations, making spending decisions prudent and stimulating saving. Italian households remain among the least indebted in the advanced world, but the debt service burden has become heavier with the growth in households' exposure in the last few years and the rise in interest rates.

Employment continued to grow in the second quarter but was outpaced by the increase in labour market participation, which can perhaps be seen as a response to the threat to household incomes brought by economic stagnation. The cyclical difficulties are evident in the sharp increase in the number of persons who have recently lost their jobs among those in search of employment, especially in the Centre and North.

Corporate investment is declining

Corporate investment was virtually stagnant in the second quarter, while that in construction fell significantly. In the residential housing sector there appears to have been a drastic contraction in sales, and prices slowed, although they continued to rise, whereas in many other countries they fell, sometimes sharply. Exports contracted in the second quarter and are heading towards stagnation in the third, in response to the weakening of world demand and the unfavourable trend in competitiveness, at least through the first quarter of the year. The weakness of the cycle and the deterioration in lending conditions are reflected in a slowdown in firms' borrowing. That from banks grew but gross bond issues in the second quarter were nil, while redemptions amounted to €1.5 billion.

Lending conditions are tightened

According to the Bank Lending Survey carried out in July, in the second quarter of 2008 Italian banks continued to tighten their standards for lending to businesses. In the household lending segment, after almost two years of easier conditions, the restrictions already in being with respect to home mortgages were extended to consumer credit. Further limitations were expected in the second half of the year. The profitability of Italian banks is affected by the global financial crisis, but to a small extent, given their limited exposure to US subprime and Alt/A mortgages, related securities and other "vehicles" in the sector.

The public finance targets were confirmed in September

The budget for the years 2009-2011, which is designed to achieve the objectives set out in the Economic and Financial Planning Document in June, was approved in August. The 2009 Finance

Bill contains only some technical measures needed to implement the three-year programme. The Forecasting and Planning Report for 2009, confirming the objectives set out in the EFPD, projects a rise in general government net borrowing to 2.5 per cent of GDP in 2008; primary current expenditure is expected to increase by 0.5 percentage points with respect to 2007 and the incidence of taxation to decrease by 0.5 points. The debt-to-GDP ratio should fall slightly, to 103.7 per cent. According to the Forecasting and Planning Report net borrowing will fall to 2.1 per cent of GDP in 2009. This objective could be jeopardized by the worsening of the economic situation. The measures to support the financial system now decided by the Government are precautionary and will not necessarily affect the public finances. The State's guarantee of bank liabilities would increase expenditure only by the amount actually used. Any bank recapitalizations or exchanges of government securities for other instruments would have a temporary effect on the level of the gross debt, without changing net debt. The aim of the budget policy is to achieve balance and bring the public debt below 100 per cent of GDP in 2011. To a large extent these objectives will be achieved by containing expenditure; in this respect, the manner of implementing the measures decided in recent months will be crucial.

2 THE WORLD ECONOMY

2.1 ECONOMIC DEVELOPMENTS AND THE FINANCIAL MARKETS

In September conditions on the financial markets deteriorated; the authorities responded by coordinating exceptional measures

The financial market crisis, which has been under way, with ups and downs, since August 2007, took a turn for the worse in September, impacting on some of the leading financial institutions in Europe and the United States. A crisis of confidence has swept through the world financial markets, bringing trading on interbank markets to a virtual standstill, causing share prices to plummet, and creating serious financing problems for the institutions that rely most heavily on the money markets. The central banks have responded with large-scale, coordinated action to restore market liquidity. The US and European authorities have launched rescue operations to prevent major financial institutions from failing, judging that the systemic effects would have been unsustainable (see the box "The crisis of some US financial institutions and the support action of the authorities"). Some institutions in the US, including Lehman Brothers investment bank, have filed for bankruptcy; some have been taken over by other financial institutions. A comprehensive plan to bolster the financial system proposed by the US Administration was passed by Congress on 3 October. On 8 October the British Treasury announced a major rescue plan for the country's financial system; the banks will be recapitalized directly by the public sector. The authorities of some euro-area countries have also produced rescue packages, guaranteeing the liabilities of banking institutions and introduced a variety of safeguards. Also on 8 October, as the downside risk to economic growth increased and the upside risk to inflation simultaneously diminished – owing partly to the sharp fall in raw material prices in recent months – the central banks of the United States, the euro area, the United Kingdom, Canada, Sweden and Switzerland together cut their reference rates for monetary policy by 50 basis points. On 9 October the Italian Government introduced some important measures to guarantee the stability of the banking system and increase the safeguards for depositors. On 10 October the G7 finance ministers and central bank governors formally undertook to come to the support any financial institutions whose failure

Table 1

Selected macroeconomic projections
(percentage changes on the previous year)

	IMF			Private forecasters (1)	
	2007	2008	2009	2008	2009
GDP					
World	5.0	3.9	3.0	–	–
Advanced countries					
Euro area	2.6	1.3	0.2	1.1	0.4
Japan	2.1	0.7	0.5	0.5	0.1
United Kingdom	3.0	1.0	-0.1	1.0	0.1
United States	2.0	1.6	0.1	1.5	-0.5
Emerging countries					
Brazil	5.4	5.2	3.5	5.3	3.4
China	11.9	9.7	9.3	10.0	9.1
India	9.3	7.9	6.9	7.5	7.1
Russia	8.1	7.0	5.5	7.5	6.1
Consumer prices					
Advanced countries					
Euro area	2.1	3.5	1.9	3.5	2.3
Japan	0.1	1.6	0.9	1.6	0.9
United Kingdom	2.3	3.8	2.9	3.8	3.3
United States	2.9	4.2	1.8	4.5	2.3
Emerging countries					
Brazil	3.6	5.7	5.1	5.9	5.3
China	4.8	6.4	4.3	6.4	3.2
India	6.4	7.9	6.7	9.9	5.7
Russia	9.0	14.0	12.0	13.5	12.3
World trade (2)	7.2	4.9	4.1	–	–

Sources: National statistics; IMF, *World Economic Outlook*, October 2008. (1) Average of forecasts by Deutsche Bank, Goldman Sachs, JPMorgan, Merrill Lynch. Private analysts' forecasts refer to 10 October 2008. – (2) Goods and services.

might have systemic repercussions and to take all necessary steps to unfreeze the credit and money markets. They also declared they would guarantee the recapitalization of banks and other major financial intermediaries as needed and ensure that national deposit insurance programmes would provide full coverage if required. Finally, they announced that action could be taken to restart the secondary markets for mortgage and other securitized assets. [1] On 12 October the countries belonging to the euro area agreed on a coordinated plan, with national measures to implement it passed on the following day.

THE CRISIS OF SOME U.S. FINANCIAL INSTITUTIONS AND THE SUPPORT ACTION OF THE AUTHORITIES

During the summer the heavy losses incurred since the start of the mortgage crisis caused a pronounced worsening of the balance sheets of the two agencies specialized in the securitization of mortgage loans (Fannie Mae and Freddie Mac). By acquiring and guaranteeing mortgage loans so as to place them on the market again through the issue of mortgage-backed securities (MBSs), they provide important support to the availability of mortgage credit. In view of their increasing difficulty in raising new capital and in accessing the bond market, on 7 September the two companies were placed into conservatorship. In order to ensure the capital adequacy of the two agencies, the Treasury will provide them with fresh capital by buying equity interests of up to 80 per cent for up to $100 billion each. Maintaining their role was deemed crucial, especially in the present difficult conditions (the two companies had bought up no less than three quarters of the new residential mortgages granted in the first half of 2008). Indirectly, the Treasury's intervention was also aimed at avoiding an excessive fall in house prices; to that end the value of the MBSs held by the agencies can rise, within a given limit, until the end of 2009, even if it will subsequently have to be reduced by 10 per cent per year; in addition, the Treasury has announced that it will purchase MBSs newly-issued by the two agencies within the same time limit.

In the hours immediately following the failure of Lehman Brothers, which effectively caused funds to dry up on interbank markets, on 16 September the Federal Reserve intervened in support of the insurer American International Group (AIG), in the throes of a liquidity crisis, with a loan of $85 billion, against which the US Treasury will receive an 80 per cent equity interest in AIG; on 8 October a further loan of about $38 billion was granted. Here again the authorities' intervention was considered to be necessary in the light of the size of the company and its interconnectedness with the rest of the financial system both inside and outside the United States. In fact AIG, with assets amounting to nearly $1,000 billion, is the world's largest insurance operator and an important counterparty in the credit default swaps market.

The action of the US authorities also extended to the money market funds sector, hit in the days following the failure of Lehman Brothers by a wave of requests for redemptions after the value of some of them had fallen below par. On 19 September the Federal Reserve announced that it would provide banks with financing for the purchase of commercial paper secured by low risk assets held by the funds, so as to allow the latter to obtain greater liquidity. On the same day, moreover, to restore confidence in these markets the Treasury made $50 billion of resources available to supply a temporary guarantee on invested capital to funds that requested it.

In the second half of September, with the crisis of other important banks for which, as in the case of Lehman Brothers, the authorities did not consider it necessary to intervene directly, a consolidation of the US banking system took place: Merrill Lynch was acquired by Bank of America and Wachovia by Wells Fargo, while the assets of the bankrupt Washington Mutual were taken over by JPMorgan Chase, which in May had acquired the investment bank Bear Stearns. In addition, the investment banks Goldman Sachs and Morgan Stanley have begun their transformation into bank holding companies; in this way, becoming subject to more stringent supervision by the Federal Reserve, they will have access to the liquidity channels reserved to banks.

[1] The official press release of the G7 is available on the US Department of the Treasury website at www.treas.gov/press/releases/hp1195.htm.

On 3 October Congress approved a more far-reaching plan for supporting the financial system (the Troubled Assets Relief Program), which provides for the Treasury to buy or guarantee bad assets held by intermediaries and for which there is no current market. These transactions will mainly concern residential and commercial mortgage loans and related securities, may be carried out over a span of two years and will be financed through the issue of public securities for up to $350 billion, which may be increased up to $700 billion with a new authorization by Congress. The aim of the Program is to overcome the uncertainty weighing on the system as regards the size of the losses in financial institutions' balance sheets and thus to foster the recapitalization of those most exposed and the return to an orderly working of the money markets; it is intended to permit a recovery in credit activity and, consequently, in economic activity as a whole. The measure also contains a series of clauses designed to limit the potential adverse effects on the public finances. In the first place, the prices of the Treasury's purchases must take as full account as possible of the losses expected on financial assets and the premiums requested for the guarantees granted must be commensurate with the risks assumed. In addition, the Treasury will receive options to purchase shares of the companies participating in the Program, which will allow it to benefit if they should rise in price; alternatively, in the case of unlisted companies, the Treasury will receive senior debt instruments. Lastly, after five years have passed, the Administration must propose a law making it possible to recover any losses incurred from the financial sector.

On 14 October the Treasury announced it would recapitalize financial institutions up to a total of $250 billion against preferred stock as part of the Program. At the same time it authorized a temporary extension of the guarantee provided by the Federal Deposit Insurance Corporation to cover new senior debt instruments (which include interbank loans) and non-interest-bearing current accounts held for the most part by firms. Some of the leading institutions have already taken advantage of both possibilities.

The final effects of the initiatives of the US authorities on the federal budget are subject to wide margins of uncertainty, above all owing to the enormous size of the exposure assumed de facto by the Treasury vis-à-vis the mortgages held or guaranteed by Fannie Mae and Freddie Mac (about $5,300 billion). On the other hand, these assets consist mainly of low-risk claims, the losses on which, according to recent IMF estimates, should not exceed $100 billion. It is therefore likely that the final costs of the interventions will be only a small fraction of the total exposure, as was the case in the savings and loans bailout at the end of the 1980s.

The outlook for the advanced economies worsens

Against this background, there has been a marked deterioration in the advanced economies' growth prospects for the second half of 2008 and for 2009 (see the box "Downward revisions of the macroeconomic forecasts for the advanced countries"). The expansion of the US economy still under way in the second quarter could be followed by stagnation or decline. The pronounced weakening of the Japanese, euro-area and British economies in the second quarter could persist beyond, in some cases turning into recession. The emerging economies will slow, although growth will remain strong (Table 1).

DOWNWARD REVISIONS OF THE MACROECONOMIC FORECASTS FOR THE ADVANCED COUNTRIES

In the last three months both the International Monetary Fund and leading private analysts have significantly lowered their growth forecasts for the main industrial countries (see table). In particular, the IMF has cut its estimates of GDP growth in 2009 for the United States from 0.8 to 0.1 per cent, for Japan from 1.5 to 0.5 per cent, for the euro area from 1.2 to 0.2 per cent, and for the United Kingdom from 1.7 to -0.1 per cent. Compared with those of the IMF, private analysts' latest estimates are more pessimistic for the United States and Japan and slightly more optimistic for the euro area.

Table

Growth forecasts
(percentage changes on previous year)

Month forecast was made	IMF (1)				Private forecasters (2)			
	July		October		July		October	
	2008	2009	2008	2009	2008	2009	2008	2009
GDP								
United States	1.3	0.8	1.6	0.1	1.6	1.2	1.5	-0.5
Japan	1.5	1.5	0.7	0.5	1.2	1.3	0.5	0.1
Euro area	1.7	1.2	1.3	0.2	1.8	1.4	1.1	0.4
Germany	2.0	1.0	1.8	0.0	2.1	1.6	1.5	0.4
France	1.6	1.4	0.8	0.2	1.8	1.4	0.9	0.5
Italy	0.5	0.5	-0.1	-0.2	0.5	1.0	0.0	0.2
Spain	1.8	1.2	1.4	-0.2	1.8	1.5	1.3	0.0
United Kingdom	1.8	1.7	1.0	-0.1	1.5	1.3	1.0	0.1
Price of oil in dollars (3)								
percentage change	63.8	7.3	50.8	-6.3				
price per barrel	116.5	125	107.25	100.5				

(1) The IMF forecasts are from *World Economic Outlook Update*, 17 July 2008, and *World Economic Outlook*, October 2008. – (2) Average of the forecasts published by Deutsche Bank, Goldman Sachs, JPMorgan and Merrill Lynch. The forecasts refer to 3 July and 10 October 2008, respectively. – (3) Simple average of the prices of the three main grades of crude oil (Brent, Dubai and West Texas Intermediate).

The downward revision reflects the continuation, and in some countries the worsening, of the crisis in the real estate market and the increasing restriction of the supply of credit by banking systems. The tightening of lending conditions had begun to be felt in the first half of the year and it intensified during the summer as banks encountered increasing difficulty in proceeding with the recapitalization made necessary by huge realized and expected losses. In September the crisis of confidence in the international markets made banks' short-term funding difficult, suggesting that there would be a further, protracted restriction in the supply of credit. In particular, the higher cost and reduced availability of consumer credit and mortgage loans could adversely affect household consumption and also help to prolong the fall in property prices under way in the United States, the United Kingdom and some euro-area countries, thereby increasing the risk of mortgage defaults. Tighter lending conditions could also induce firms to cut back their investment plans. The slowdown forecast for Japan, less exposed to the risk of a contraction in lending, reflects the assessment of the consequences of a deceleration in exports, which would not only have a direct impact on output growth but would also prompt firms to scale down their planned investment.

Since the fall in the price of oil is due mainly to the deterioration in the prospects of growth, it is not likely to exert a significant anti-recessionary effect; it will attenuate the inflationary pressure.

Oil prices, which peaked in mid-July at $143 per barrel for the average of the three main grades, have since followed a clear downward trend. Recent weeks have seen wide swings, with prices falling as low as $75. On the basis of futures contracts, the price of WTI grade oil is expected to increase slowly but steadily during 2009, reaching $83 at the end of the year (Figure 1). The International Energy Agency has lowered its forecast of the growth in world demand for crude oil in 2009 to 0.8 per cent, bringing it into line with the IMF's scenario of a slowdown in the world economy. Non-fuel commodity prices have also fallen. The dollar prices of metals and food commodities in particular were around 18 and 14 per cent lower than the peaks recorded, respectively, in March and June. According to IMF estimates the dollar prices of both will tend to settle at their September levels towards the end of 2008 and in 2009.

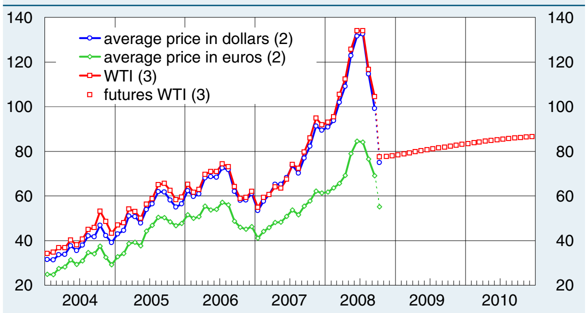
The crisis of confidence puts a heavy strain on the interbank markets…

Tension on the interbank markets of the advanced countries, which has been present for the past year, reached an unprecedented level in the second half of September, reflecting a much heightened perception of liquidity and counterparty risks following the collapse of Lehman Brothers. The yield differential between three-month unsecured dollar-denominated interbank deposits and three-month overnight index swaps, which is a measure of such risks, widened rapidly from about 80 basis points in the first half of September to 360 points on 10 October (Figure 2). The differentials in euro and in sterling have gone from 60 to 185 and from 75 to 215 basis points.

Figure 1

Crude oil: spot and futures prices (1)

(dollars and euros per barrel)



Sources: IMF and Thomson Financial Datastream.
(1) Monthly averages for spot prices; the last data refer to 10 October. – (2) Average price per barrel of the three main grades (Brent, Dubai and WTI). – (3) Dollars per barrel.

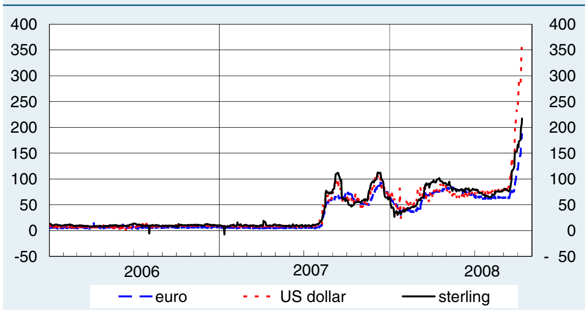
…prompting the central banks to take exceptional action to boost liquidity

The Federal Reserve responded to the crisis of confidence on the interbank market with action on several fronts. On 14 September it increased the supply of liquidity, extending the range of financial assets eligible as collateral for the Primary Dealer Credit Facility (which provides very-short-term loans at the discount rate) and the Term Security Lending Facility (providing Treasury securities in exchange for securities of private issuers) and raising the amount of financing available through the latter to $200 billion. On 29 September the Fed provided additional liquidity by raising the amount of funds available under the Term Auction Facility (which offers 28- and 84-day loans through an auction process) from $150 billion to $300 billion; on 6 October that figure was raised to $600 billion. The Fed also injected more dollars into foreign markets, notably increasing the swap lines with the European Central Bank and the Swiss central bank, and agreeing new lines with the central banks of Japan, Britain, Canada, Australia, Sweden, Denmark and Norway; overall, the value of the swap lines was raised from $70 billion to $620 billion. The ceiling on dollar swap lines between the Fed and the other central banks was removed on 13 October when the ECB and the British and Swiss central banks announced they would provide US dollar funding, at a fixed rate of interest, for the full amount required by the counterparties against appropriate collateral. On 7 October the Fed announced it would create a special purpose vehicle, financing it with secured credit lines, to buy three-month dollar-denominated US commercial paper rated A1 or better on the primary market.

Figure 2

Three-month LIBOR spread to overnight index swaps (1)

(basis points)



Sources: Thomson Financial Datastream and Bloomberg.
(1) Daily data.

The Bank of England has prolonged its Special Liquidity Scheme, which enables banks and building societies, through one-year asset swaps, to exchange mortgaged-backed securities for UK Treasury bills, from the original 21 October deadline to 30 January 2009; it has also raised the total amount of asset swaps envisaged under the Scheme from £50 billion to £200 billion. Other measures to increase liquidity have been taken by the European Central Bank (see ECB Monthly Bulletin for October 2008).

Share prices fell sharply in September and in the first ten days of October...

The US stock market, which had been gaining slightly from mid-July to the end of August, began to slip once more in the early days of September when it appeared that the government sponsored mortgage securitizers Fannie Mae and Freddie Mac were experiencing renewed difficulties. The fall gained impetus from the middle of September, as prices began to fluctuate more widely in response to uncertainty about the gist and timing of the Treasury Department's rescue plan announced on 18 September. By 10 October the Standard & Poor's 500 had dropped by around 30 per cent from the end of August (Figure 3). Share prices fell in all the main sectors. Stock markets in the euro area and the United Kingdom followed the US, also losing around 30 per cent in the same period; Japan fared worse, recording losses of close to 35 per cent. Implicit price volatility has increased in both the US and the euro area and is now at its greatest since the start of the financial crisis (Figure 4).

...and the spreads on bonds grew to the widest level since the crisis began

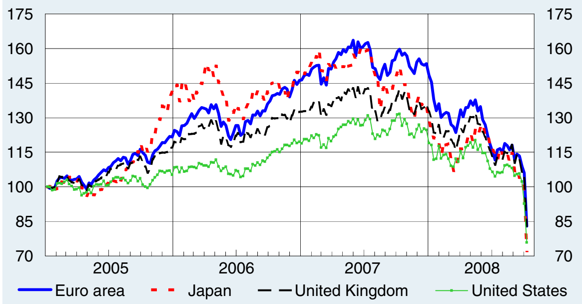
Risk premiums on high-yield corporate bonds have increased since the end of August by around 700 basis points in the United States and by over 800 points in the euro area; on 10 October they stood at just over 1,500 basis points in the US and just under 1,700 in the euro area. In September risk premiums on BBB-rated corporate bonds rose by more than 200 basis points in the US and by about 170 in the euro area, to around 540 and 375 basis points respectively on 10 October (Figure 5).

Yields on US government securities have been very volatile, reflecting the large portfolio adjustments in their direction that occur at times of considerable market tension. On 17 September the yields on three-month Treasuries were close to zero. The yields on 10-year Treasury bonds, fell from around 4 per cent in the second half of July and in August to a low of 3.4 per cent on the same date, before rising back to 3.8 per cent by 10 October. Interest rates on 10-year bonds in the euro area, United Kingdom and Japan recorded smaller fluctuations in September and on 10 October stood at 3.9, 4.4 and 1.5 per cent respectively (Figure 6).

Figure 3

Stock market indices (1)

(end-of-week data; first week of January 2005=100)

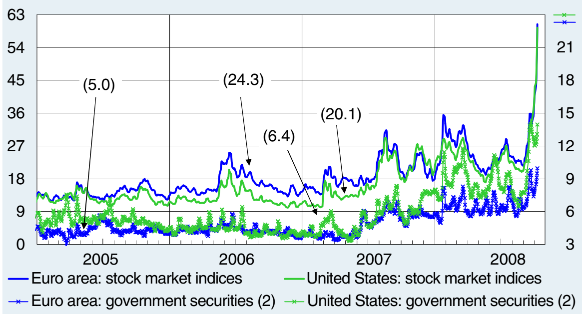


Source: Thomson Financial Datastream.
(1) Dow Jones Euro Stoxx for the euro area, Nikkei 225 for Japan, FTSE All Share for the United Kingdom and Standard & Poor's 500 for the United States.

Figure 4

Implicit volatility (1)

(percentage points; averages for the period 1999-2006 in brackets)

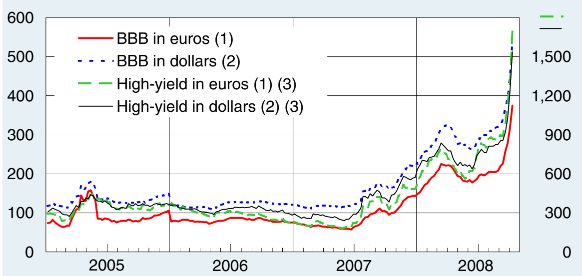


Source: Based on Bloomberg data.
(1) Moving averages over 5 days. Stock market indices: VSTOXX for the euro area and VIX for the United States. Government bonds: volatility implied by the prices of options on futures on the German Bund for the euro area and on futures on Treasury notes for the United States. – (2) Right-hand scale.

Figure 5

Yield differentials between dollar-denominated and euro-denominated bonds of non-financial corporations and government securities

(end-of-week data; basis points)



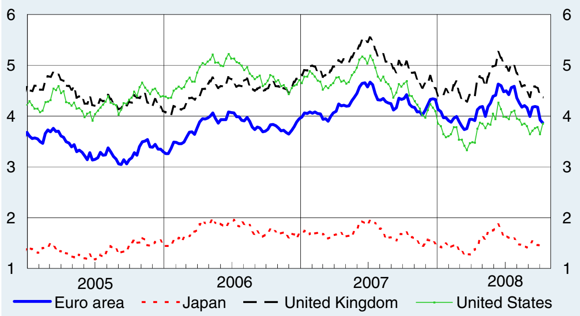
Source: Merrill Lynch.
(1) Yields on fixed-rate bonds denominated in euros with a residual term to maturity of not less than one year issued in the Euromarket; yield differentials are calculated with respect to French and German government securities. – (2) Yields on fixed-rate bonds denominated in dollars with a residual term to maturity of not less than one year issued in the US domestic market; yield differentials are calculated with respect to US Treasury securities. – (3) Right-hand scale.

In the emerging countries, risk premiums, measured by the difference between their long-term dollar-denominated government securities and US Treasury bonds, began to widen from mid-June. In September they became considerably more volatile, rising steeply when financial market tension was sharpest in the advanced economies. On 10 October they stood at around 670 basis points, some 400 points higher than in the middle of June. Since the end of August share prices have fallen by much the same amount as in the main advanced economies.

Figure 6

Yields on ten-year government bonds

(end-of-week data; percentages)

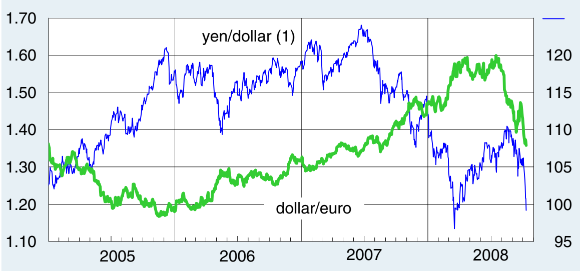


Source: National statistics.

Figure 7

Exchange rates

(daily data)



Source: ECB.
(1) Right-hand scale.

The dollar has appreciated, more than recouping the losses of the first half of the year

Since the end of June the US currency's effective exchange rate has risen by around 12 per cent, more than making up the fall of the first half of the year; by 10 October the dollar had gained 8 per cent with respect to the end of 2007. The improvement has been very marked against euro and sterling – which is difficult to understand since growth prospects have deteriorated in all three countries – with the exchange rate going from 1.58 to 1.36 to the euro and from 1.99 to 1.70 to the pound. After holding steady against the yen throughout the third quarter, the dollar depreciated by around 6 per cent in the first ten days of October (Figure 7). The depreciation against the Chinese currency has almost come to a halt, with a loss of around 6 per cent since the end of 2007.

The United Kingdom and several European countries have taken steps to bolster the markets

Under the rescue plan announced by the Government on 8 October, by the end of the year eight leading British banks and building societies will increase their tier 1 capital by a total of £25 billion, with the support of the Treasury, which has de facto guaranteed coverage. The Treasury has also allocated a further £25 billion to recapitalize all British financial institutions. Finally, it has announced that it will guarantee short- and medium-term debt securities issued in the coming months by financial institutions that are increasing their tier 1 capital at the same time, for a total figure of £250 billion (equal to around 18 per cent of the country's GDP). Other countries, Italy among them (see the box "The Italian Government's measures in support of banks"), have revised their regulatory framework along the lines agreed within the Ecofin Council, the G7 and the Eurogroup.

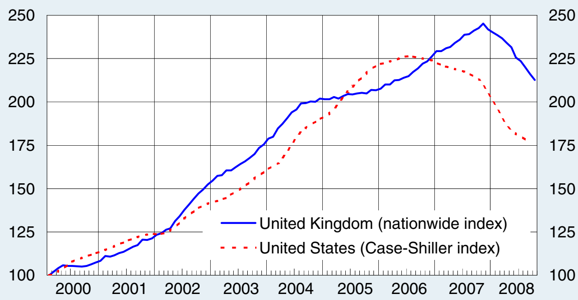
2.2 THE MAIN INDUSTRIAL AND EMERGING COUNTRIES

In the United States economic activity has weakened since the summer...

In the second quarter, the GDP of the United States increased by 2.8 per cent at an annual rate, faster than in the previous quarter and more than had been expected. Growth was driven by foreign demand: exports increased sharply and imports, of petroleum products in particular, declined. Private consumption increased very slightly while residential investment continued to fall, although less sharply than in the preceding quarters. In July and August consumption weakened, affected by the continued reduction in non-farm payroll employment (down by 300,000 jobs between June and September) and the significant decline in household net wealth – mainly housing wealth – under way for several quarters now. The effects of the support measures under the Economic Stimulus Act have been modest; it is estimated that tax rebates to households (about $100 billion, almost all paid between April and August) have mainly been put into savings. The most recent assessments of growth in 2008 by international organizations assume that GDP will basically remain stationary in the second half of the year.

Figure 8

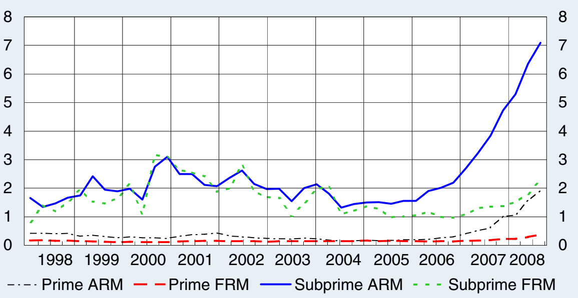
Real estate market: house prices index
(indices, January 2000=100)



Source: Thomson Financial Datastream.

Figura 9

Residential mortgages in the United States: foreclosures initiated as a proportion of outstanding mortgages, according to type of mortgage (1)
(quarterly data, seasonally adjusted; percentages)



Source: Thomson Financial Datastream.
(1) ARM: adjustable-rate mortgages; FRM: fixed-rate mortgages.

...given the persistence of the housing market crisis...

The crisis in the housing market has continued and is one of the crucial factors in the weakness of the US economy. In August the volume of sales of new houses was at about 9 per cent of the stock of unsold new houses, foreshadowing a fall in residential investment in the second half of the year as well. House prices continued to fall in the ten largest cities, as measured by the Case-Shiller index (Figure 8); from the mid-2006 peak, the decline reached 20 per cent and futures prices imply a further reduction of around 10 per cent by the end of 2009. The proportion of foreclosures initiated in relation to outstanding residential mortgages increased again in the second quarter, especially for those with an adjustable interest rate and not only in the subprime segment (Figure 9).

...and the emergence of signs of a tightening of the credit supply

In the second quarter the slowdown in lending from the banking system to non-financial firms became more marked. Lending to households, in the form of consumer credit as well as mortgages, continued to lose momentum. The Federal Reserve's Senior Loan Officer Opinion Survey, carried out in July, showed a further tightening of the supply of credit to both households and businesses. In the third quarter, there was also a considerable contraction in bond issues by non-financial corporations, which had remained strong until the second quarter, compensating for the slowdown in bank lending. The steady tightening of credit conditions for households and businesses, partly reflected in higher borrowing costs, constitutes the main risk for future economic growth.

Inflation expectations are falling...

The chain-type price index for personal consumption expenditures reached a peak of 4.6 per cent in July, falling to 4.5 per cent in August as a result of the substantial decline in energy prices; excluding food and energy items, inflation stabilized at 2.6 per cent in August. Since mid-July, inflation expectations over a ten-year timespan, which can be measured by the spread of yields on nominal Treasury securities over those on their inflation-protected counterparts, fell sharply; in the preceding months they had been affected by the large increases in raw material prices.

...markets expect a further slackening of monetary conditions

On 8 October the Fed, as part of a coordinated monetary policy action by the advanced economies' central banks, lowered its target for the federal funds rate by 50 basis points to 1.5 per cent. The latest futures prices indicate that markets expect a further 25 basis point reduction by the end of the year.

Net private capital inflows are declining

The current account deficit in the second quarter (5.1 per cent of GDP) remained virtually unchanged from the first. The deterioration in the terms of trade, mainly due to the soaring price of oil, offset a growth in export volumes and a reduction in imports; therefore the deficit in relation to transactions in goods and services remained the same at 5.1 per cent of GDP. The main contribution to financing the external deficit came from foreign official sources, but there were large outflows of private capital resulting from disposals of instruments issued by the US banking system. In July, there were further outflows of private capital.

In Japan economic activity weakened significantly

In Japan in the second quarter of 2008 GDP fell by 3.0 per cent on an annual basis, reflecting a decline in consumption and exports. The latter involved all the main outlet markets: East Asia, the United States and the European Union. The Bank of Japan's Tankan Survey, released on 1 October, showed a sharp deterioration in business conditions in the third quarter and expectations of a further worsening in the fourth. Recent estimates from the IMF indicate that economic activity will remain stagnant in the third and fourth quarters of 2008. Consumer price inflation increased to 2.3 per cent in July, falling back to 2.1 per cent in August (Figure 10). The rise in prices continues to be entirely attributable to food and energy goods, net of which, inflation is zero. While the Bank of Japan expressed its support for the coordinated action to reduce interest rates, it did not join in and maintained its monetary policy reference rate unchanged at 0.5 per cent. The markets think that any change in monetary conditions this year is unlikely.

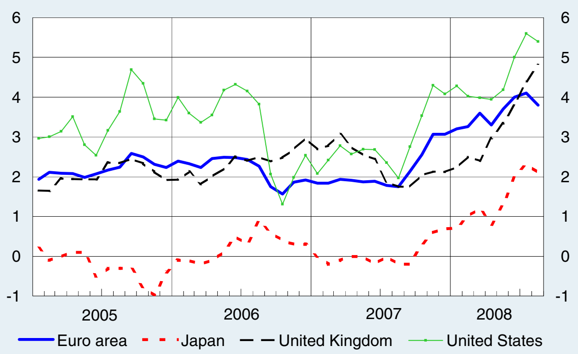
In the United Kingdom growth came to a halt and inflation is way above target

In the second quarter, economic activity in the United Kingdom was at a standstill, reflecting a sudden slowdown in consumption and exports and a further decline in both residential and other investment. The reduction in consumption reflected the growing difficulty of borrowing, as lending to households continued to slow down. The tightening of credit conditions resulting from the problems of the British banking system in raising new capital in the face of the losses suffered in the last few quarters affected both households and businesses. The impact on consumption was exacerbated by the concurrent reduction in wealth: between October 2007 and last September, house prices fell by about 13 per cent. The Bank of England's Credit Conditions Survey published on 2 October showed expectations of a further restriction in credit availability in the fourth quarter. Consumer price inflation rose to 4.7 per cent in August, almost three percentage points above the target. Nevertheless, there were no signs of increases in wages. Against this backdrop, the Bank of England joined in the coordinated reduction of monetary policy rates on 8 October, reducing its own reference rate by 50 basis points to 4.5 per cent. Markets are discounting a further cut of 50 basis points before the end of the year.

Figure 10

Consumer price inflation (1)

(monthly data; twelve-month percentage changes)



Source: Thomson Financial Datastream.
(1) For the United Kingdom, harmonized consumer prices.

In the main emerging economies, the slowdown is generally less severe

In the second quarter of 2008 the slight slowdown in production in the main emerging countries continued. The increase in GDP, compared with one year earlier, was 10.1

per cent in China, 7.9 per cent in India, 7.5 per cent in Russia, and 6.2 per cent in Brazil. Since July, the IMF has lowered its 2008 growth forecast for Russia from 7.7 per cent to 7.0 per cent, but its forecasts for China (9.7 per cent), India (7.9 per cent) and Brazil (5.2 per cent) remained virtually unchanged. Inflation in the emerging economies was a cause of strong concern in the first part of 2008 (see the box "Inflation in the emerging economies", in *Economic Bulletin*, No. 49, July 2008). In recent months, thanks to the fall in raw material prices, inflationary tensions generally eased. Inflation declined steadily in China (from 8.5 per cent in April to 4.9 per cent in August) and remained unchanged, but at very high levels, in Russia (around 15 per cent); there were small increases in Brazil (from 5.0 per cent to 6.2 per cent). In India, however, inflation continued to rise from 7.8 per cent in April to 9.0 per cent in August.

2.3 THE EURO AREA

European governments have taken extraordinary measures

On 7 October Ecofin approved a set of principles governing intervention to combat the financial crisis and member states pledged to raise their deposit guarantee protection for individuals to €50,000. On 12 October, the euro-area countries, acting in agreement with the EU Commission and the European Central Bank, approved a concerted action plan and urged the other EU countries to adopt its principles. The plan provides for individual national governments to take coordinated measures to facilitate bank funding (government guarantee for new medium-term debt issuance) and recapitalization (government subscription of preference shares or other instruments). On 13 October the Italian Government passed measures to implement it. In the days that followed, the competent authorities were called on to take measures to allow financial and non-financial institutions to value their assets in accordance with reasonable assumptions on default risk rather than immediate market value.

Following the slowdown in the first half of 2008…

In the first six months of 2008, euro-area growth decelerated further, to 0.8 per cent compared with the previous half year, confirming the downward trend under way for more than a year (in the first half of 2007 the economy had grown by 1.4 per cent). After recording an expansion of 0.7 per cent in the first quarter, which was mostly ascribable to temporary factors, in the spring GDP fell for the first time since the launch of European Monetary Union (-0.2 per cent). The decline was only partly due to the termination of the temporary factors that had supported the sharp increase recorded in the first three months of the year. In fact, all the components of demand and all of the euro area's main economies were affected by the slowdown. Household consumption fell on average by 0.2 per cent in the euro area and by 0.7 per cent in Germany, where it was constrained by the pessimism that continued to characterize consumer perceptions and by the low growth in disposable income; in France consumption remained stagnant. Investment fell everywhere and in particular in the construction sector, reflecting signs of a turnaround in the property cycle and of the adjustment that followed the investment in the first quarter. The global economic slowdown led to a 0.2 per cent decline in exports across the euro area and in Germany, with France recording a 2 per cent drop.

…economic activity remains weak in the second half of the year

Over the summer months, as tensions on financial markets worsened, the signs of weakness in the economic cycle grew stronger, based both on business and consumer surveys and on the performance of output and sales. In September the economic data deteriorated markedly; the €-coin indicator, which provides a snapshot of the economy's performance, fell sharply, dropping close to zero (Figure 11). The estimates obtained using the forecasting models devised by the Bank of Italy predict substantial stagnation of output in the third quarter of the year.

Inflation slows, both of consumer prices...

Twelve-month inflation as measured by the harmonized index of consumer prices dropped to 3.8 per cent in August (from 4 per cent in July), ending a long period of acceleration triggered by increases in the prices of food and energy products, which now appear to be slowing. According to provisional data published by Eurostat, the gradual decline of consumer price inflation continued in September (reaching 3.6 per cent on a twelve-month basis), driven by falling energy prices. The seasonally adjusted monthly data point to a more brusque inversion of the trend; based on partially estimated data, the annualized average rate of increase in prices in the third quarter fell to 1.1 per cent, from almost 5 per cent in the second quarter (Figure 12).

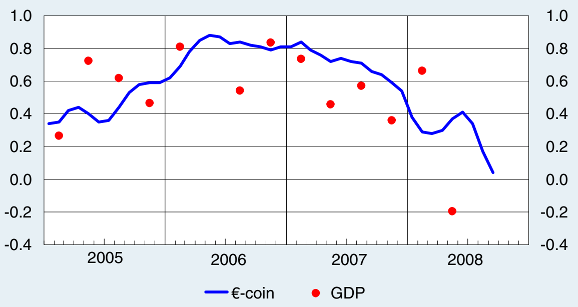
...and of producer prices...

The producer price index, which in the first seven months of the year had risen from 5.1 to 9.2 per cent, driven by the price increases in intermediate goods and energy products in particular, also slowed in August, reaching 8.5 per cent thanks to the easing of tensions in the raw materials markets. The upward pressures on consumer prices stemming from the earlier stages of production are weakening, as indicated by the moderate month-on-month growth in the prices of final consumer goods, including food products. Past increases in the prices of energy goods could still be transmitted to final prices; assessments by businesses of possible variations in their retail prices in the coming months, as surveyed by the European Commission, tend towards moderation, however.

Figure 11

€-coin coincident indicator of the euro-area business cycle and GDP (1)

(percentage changes)

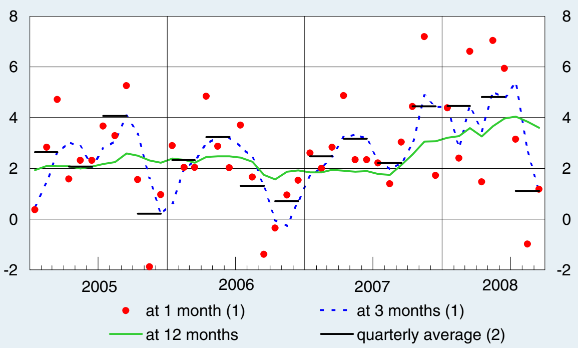


Sources: Eurostat and based on Thomson Financial Datastream data.
(1) For information on the construction of the indicator, see the box: "€-coin: a real-time estimate of growth in the euro area" in Economic Bulletin, No. 46. For GDP, quarterly data; changes with respect to previous quarter. For €-coin, monthly data; three-month changes.

Figure 12

Inflation in the euro area

(harmonized index of consumer prices)



Sources: Eurostat, ECB and Bank of Italy.
(1) On a seasonally adjusted and annual basis. – (2) Average, in the reference quarter, of monthly growth rates, on a seasonally adjusted and annual basis.

...and there is a slight decline in forecast inflation for 2008 and 2009

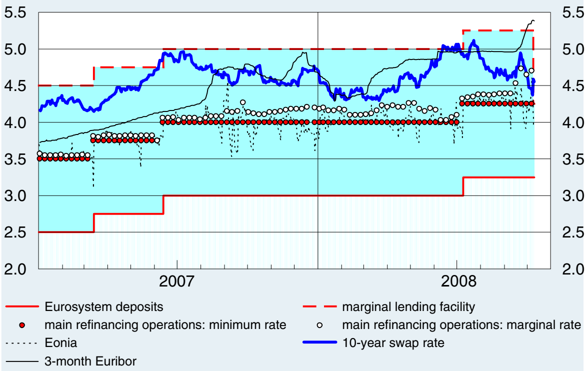
Consistent with falling oil prices and the easing of tensions over food commodity prices, in September the professional forecasters polled by Consensus Economics made a moderate downward revision to their inflation forecasts for 2008 and 2009, from 3.6 to 3.5 per cent, and from 2.5 to 2.4 per cent respectively. The heavy fluctuations in oil prices and the uncertainty surrounding their future movements were nonetheless reflected in the dispersion of forecasts for 2009, which has increased since the summer. Consumer expectations regarding prices, surveyed by the European Commission, signal a return to previous levels, following the peaks reached at the end of the spring.

Money and credit expansion slows

The growth in bank lending to the private sector is also slowing (although it was still 8.8 per cent over the twelve months ending in August), both in the corporate lending sector and, above all, in household loans; the slowdown in mortgages for home purchases partly reflected the accounting effect of massive securitizations aimed at obtaining securities eligible as collateral for Eurosystem refinancing operations. Looking ahead, the indications from the Bank Lending Survey conducted by the Eurosystem in July point to a further tightening of credit supply conditions; this possibility has increased in recent weeks due to the sharp acceleration in the international financial crisis. M3 money supply also slowed, by 8.8 per cent in August, owing to the slowdown in the more liquid components, in contrast with the brisk trend in short-term deposits, whose rising yields reflect the difficulties of the money market.

Figure 13

Official interest rates and money and financial market rates in the euro area
(daily data; percentages)



Sources: ECB and Reuters.

On the money market the ECB responded to the demand for liquidity

Since mid-September tensions on the euro money market have become increasingly acute due to the deepening international financial crisis. Trades on the interbank market dried up and interest rates rose significantly. Beginning on 12 Setpember the 1 and 3-month Euribor rates on unsecured loans increased by around 60 and 40 basis points respectively, reaching over 5 per cent (Figure 13). In the same period spreads with the corresponding rates on guaranteed loans (Eurepo) increased considerably (around 130 basis points over a 3-month horizon), due to the widening risk premium. The ECB addressed peaks in demand for liquidity by boosting supply; it also accommodated the demand for foreign currency liquidity from banks in the euro area by intensfiying dollar transactions, a move coordinated with the Federal Reserve and the other main central banks. As part of the coordinated intervention between the main central banks, on 8 October the Governing Council of the ECB reduced the rate on its main refinancing operations by 50 basis points, to 3.75 per cent. The decision reflects the fading of inflationary pressures associated with the fall in energy and commodity prices and the intensification of financial tensions, which led to a deterioration in prospects for growth and further reduced the risks to price stability. The ECB has also established that as of 15 October, all main refinancing operations will be conducted as fixed-rate tenders with full allotment of the amounts requested by the counterparties; finally, it reduced the corridor of standing facilities from 200 basis points to 100 basis points around the interest rate on the main refinancing operation for both the Eurosystem's marginal lending facility and the deposit facility (now equal to 4.25 and 3.25 per cent respectively). Both changes to the operational framework will remain in place at least until the end of the first maintenance period of 2009, on 20 January. An equivalent loosening of the criteria for granting liquidity was also adopted for foreign currency trades; the ECB and other major European central banks announced that, beginning in mid-October and at least until the end of January 2009, demand for dollars will be met through fixed-rate tenders with full allotment.

3 THE ITALIAN ECONOMY

3.1 THE CYCLICAL SITUATION

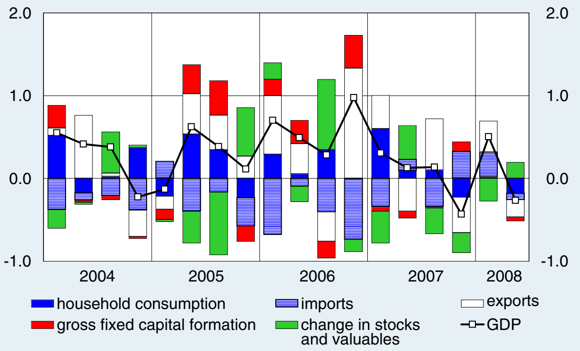
The Government has intervened to support the markets

The liquidity problems in the interbank market and the worsening of tensions in the financial and stock markets also affected Italy. In the last few days the Italian Government has approved a set of measures to ensure the stability of the Italian financial system (see the box "The Italian authorities' measures for the stability of the financial system").

Figure 14

Contributions of the main components of demand and imports to the growth in GDP (1)

(percentage points)



Source: Istat.
(1) The formula for calculating the contributions to real GDP growth in accordance with the new methodology for price deflation based on chain linking can be found at the Istat website: www.istat.it.

GDP fell in the second quarter...

In the second quarter of 2008 GDP fell by 0.3 per cent in relation to the preceding quarter, wiping out almost all of the recovery recorded in the first three months of the year. The fall reflected the sharp contraction of 0.7 per cent in exports, which had been the mainstay of the recent expansion; domestic demand remained weak, and only stock building kept it from detracting from growth, as consumption and investment in construction declined while investment in machinery, equipment and transport equipment stagnated (Figure 14). At the sectoral level the fall in output reflected the decrease in the value added of industry excluding construction and of the construction sector, where signs of recession are becoming ever plainer; the value added of the services sector remained unchanged. If one looks beyond the volatile quarterly data to examine semi-annual variations in GDP, the slowdown is clearly evident: the rate of growth of the Italian economy fell from about 1 per cent in the first half of 2007 to practically zero in the subsequent two periods (0.0 and 0.2 per cent respectively).

...and the indications for the next few quarters remain negative

There was no sign of a cyclical recovery during the summer: the most up-to-date indicators point essentially to stagnation in output in the third quarter. In August industrial production won back the ground lost in July, but according to our estimates it fell again in September, by approximately one percentage point, and therefore also declined in the third quarter as a whole. Surveys of economic conditions reveal widespread pessimism among firms and households. In September there were renewed falls both in the purchasing managers' index (PMI) and in ISAE's survey of business confidence, which is lower than at any time since October 2001; household confidence improved slightly but remained close to its lowest levels of the last ten years. Domestic demand appears to have remained flat: negative signals continued to come from retail sales and the car market, where new registrations in 2008 will probably be well below the average for the decade; spare capacity increased further.

THE ITALIAN AUTHORITIES' MEASURES FOR THE STABILITY OF THE FINANCIAL SYSTEM

On 9 October the Government issued Decree Law 155, entitled "Urgent measures to guarantee the stability of the credit system and the continued flow of credit to firms and consumers in the current state of crisis in world financial markets". The decree identified three specific areas for action: the recapitalization of Italian banks, support for operations designed to cope with the severe liquidity shortage, and a state guarantee for depositors.

The decree empowers the Ministry for the Economy and Finance to subscribe or guarantee capital increases decided by Italian banks whose capital the Bank of Italy judges to be inadequate. In the interests of taxpayers, the banks will have to adopt a plan for stabilization and strengthening and a consistent policy on dividends. Plan and policy will be assessed by the Bank of Italy. The shares subscribed by the Ministry will have priority in dividend distribution.

To facilitate intervention in support of liquidity, the decree simplifies the rules on collateral provided against financing from the Bank of Italy. In addition, in the event of severe liquidity crises, it authorizes the Ministry for the Economy and Finance to guarantee the loans granted by the Bank of Italy to Italian banks and the branches of foreign banks.

The scope for application of the procedures for special administration and provisional management of banks (Article 70 ff. of the Consolidated Law on Banking) is extended to cases of severe crisis, including liquidity crisis, that could jeopardize the stability of the financial system.

As regards depositor protection, the Ministry is empowered to issue a state guarantee to back up the Italian interbank deposit insurance scheme, which provides for coverage up to €103,191.38, considerably more than the EU minimum, recently raised to €50,000.

On 13 October the Government issued Decree Law 157 to increase the degree of liquidity of banks' assets and foster funding in the market, thereby implementing the measures agreed with the other euro-area countries. The decree authorizes the Ministry for the Economy and Finance, until 31 December 2009: i) to issue state guarantees for new Italian bank liabilities with maturity of less than five years; ii) to effect temporary exchanges of government securities with banks' portfolio assets or the liabilities of counterparty Italian banks; and iii) to issue state guarantees for contracts between Italian market participants and Italian banks making available to the latter, on a temporary basis, securities eligible for use in refinancing operations with the Eurosystem. The Bank of Italy is assigned to assess the conditions of the banks that request the activation of these facilities, which are granted for a fee.

The measures provided for in both decrees are precautionary and will not necessarily determine an increase in public expenditure. Any actual bank recapitalizations and temporary exchanges of securities would not change the figure for net borrowing, as these would be financial transactions. But there would be an increase in the public debt and in the borrowing requirement equal to the amount of resources raised in the financial markets, which would be reversed with the disposal of the assets so acquired. The extension of the guarantees on deposits and other liabilities and the guarantees on exchanges of securities will affect the accounts only if the guarantees are actually drawn on.

With a view to increasing the actual recourse by the banks operating in Italy to refinancing with the Eurosystem, on 13 October the Bank of Italy decided: i) to reduce the minimum size of loans eligible for refinancing operations from €1 million to €500,000; and ii) to activate a new facility, for up to a maximum of €40 billion, providing for temporary exchanges of government securities held by the Bank itself with assets held by Italian banks, for a 1 per cent commission. The assets exchanged by the banks can be debt instruments, denominated in various currencies, with ratings possibly below that of securities eligible for operations with the Eurosystem.

Labour market participation increased more than employment

After rising in the first quarter of 2008, employment continued to grow in the second, again reflecting mainly the contribution of women, foreigners and workers on fixed-term or part-time contracts. The present economic difficulties are reflected in an increase in the number of people previously in work but now seeking employment, especially in the Centre and North.

Inflation slowed

Thanks to an easing of imported inflationary pressures, in August the twelve-month rise in the index of consumer prices remained at the same level as in the preceding month (4.1 per cent) and in September it fell to 3.8 per cent. The slowdown in prices is likely to continue in the coming months, aided partly by the economic downturn.

Table 2

GDP and its main components

(chain-linked volumes; data adjusted for seasonal and calendar effects; percentage changes on preceding period)

	2007		2007(1)	2008	
	Q3	Q4		Q1	Q2
GDP	0.1	-0.4	1.5	0.5	-0.3
Total imports	1.2	-1.1	4.4	-1.0	0.3
National demand (2)	-0.1	-0.3	1.3	-0.2	..
National consumption	0.2	-0.3	1.4	0.1	-0.2
households	*0.2*	*-0.4*	*1.4*	*..*	*-0.3*
other (3)	*0.4*	*0.1*	*1.3*	*0.4*	*0.3*
Gross fixed capital formation	-0.1	0.6	1.2	..	-0.2
construction	*0.8*	*0.3*	*2.2*	*0.3*	*-0.9*
other goods	*-1.1*	*0.8*	*0.2*	*-0.3*	*0.5*
Changes in stocks and valuables (4)	-0.3	-0.2	..	-0.3	0.2
Total exports	2.2	-1.5	5.0	1.3	-0.7

Source: Istat.
(1) Data not adjusted for calendar effects. – (2) Including changes in stocks and valuables. – (3) Expenditure of general government and non-profit institutions serving households. – (4) Contribution to GDP growth over the preceding period, in percentage points.

3.2 FIRMS

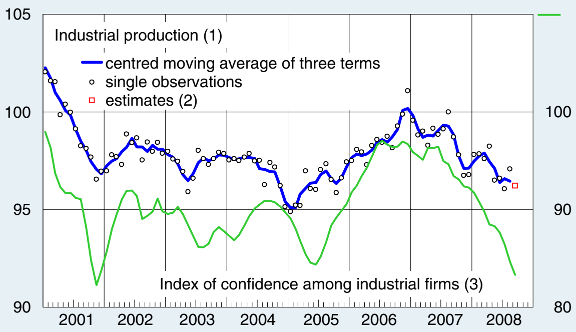
Industrial production fell in the summer

After falling in July and recovering in August, according to our estimates production in industry excluding construction declined again by about 1 per cent in September and therefore was also down in the third quarter as a whole (by more than 0.5 per cent on the preceding period; Figure 15). Industrial activity was affected mainly by the weakness of current demand and uncertainty about the short-term outlook. According to the most recent surveys of manufacturing firms by ISAE, expectations about production have been scaled down in line with the deterioration in assessments of the level of both domestic and export orders (Figure 16); the proportion of firms that consider the level of stocks to be higher than normal also increased. The indices compiled from interviews with purchasing managers (PMI) continued to fall during the summer, and in September reached their lowest level since 2001.

Figure 15

Industrial production and index of business confidence

(monthly data; indices, 2000=100)



Sources: Based on ISAE, Terna and Istat data.
(1) Adjusted for seasonal and calendar effects. – (2) Based on electricity consumption and the indicators of ISAE surveys of industrial firms. – (3) Average of the seasonally adjusted percentage balances of the responses to questions regarding the level of demand, production expectations and stocks of finished products; moving average of three terms (right-hand scale).

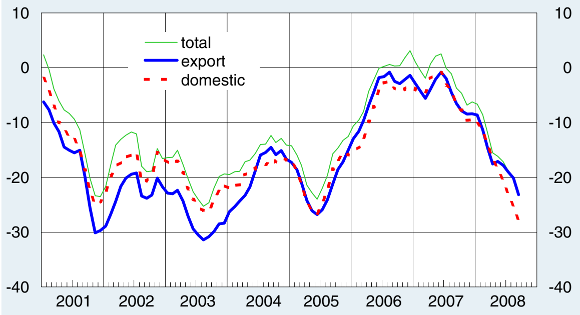
Investment activity is weakening...

Capital formation declined by 0.2 per cent in the second quarter as investment in construction fell sharply and that in machinery and equipment stagnated. The continuing decrease in the capacity utilization rate, the tightening of credit conditions and the contraction in order books are having an adverse effect on producers of capital goods. The survey of firms in industry and services carried out in September by the branches of the

Bank of Italy shows, by comparison with the 2007 survey, a slight increase in the proportion of firms that invested less than they had planned the previous year. Signs are emerging that investment plans will be reduced further in 2009, especially in the industrial sector. The survey conducted by the Bank of Italy in conjunction with *Il Sole 24 Ore* in the same month confirms the adverse cyclical picture; in addition, there was an increase in the percentage of firms stating that they had greater difficulty than in the past in obtaining loans from the credit system and faced more onerous conditions.

Figure 16

Industrial orders (1)
(monthly data)



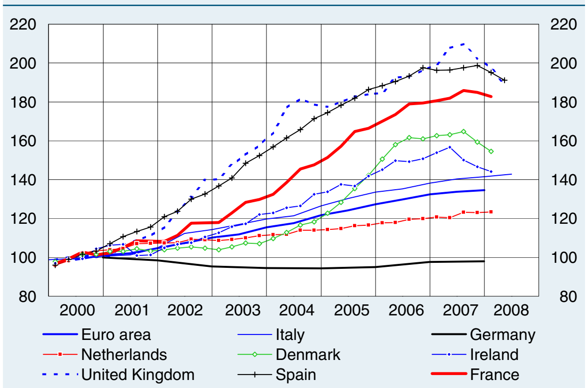
Source: Based on ISAE data.
(1) Moving average for the three months ending in the reference month of the difference between the percentage of positive replies ("high", "increasing") and that of negative replies ("low", "decreasing") to the request to assess the level of orders. Seasonally adjusted. The replies are weighted by size, sector and location of firm.

...especially in the construction sector

In the first half of the year the growth in the construction sector came to a halt: the modest rise in the first quarter was followed by a sharper fall in the second (0.9 per cent in relation to the previous quarter). The sector expects demand to weaken further and borrowing conditions to become less and less favourable. In keeping with the worsening of the general economic climate, confidence among building firms deteriorated in the course of the year, and more sharply during the summer, with an appreciable fall in the level of orders. The production and turnover data for companies supplying inputs to the sector (cement, plaster, tiles and bricks) and building firms' assessments of employment trends are consistent with a further fall in production in the most recent months. Available information on the residential sector shows that prices continued to slow during the year in conjunction with a dramatic contraction in sales. In the first two quarters of 2008 house prices rose by an average of 1.8 per cent (after adjustment for consumer price inflation), compared with about 3 per cent in the four quarters of 2007. The leading research institutes unanimously predict a fall in both the number of transactions and the rate of price increase in 2008 as a whole. Since the beginning of the year the slowdown in property prices has also become more pronounced in the other euro-area countries. On the basis of available data, which are affected by differences in the speed with which national data are released (Figure 17), house prices (adjusted for consumer price inflation) increased in France and the Netherlands (by 1 and 2 per cent respectively in the first quarter by comparison with the preceding period) but fell in Spain (by 2.5 per cent in the second quarter) and Ireland (by 6 per cent in the first quarter). Among the countries not participating in monetary union, the decline was even more pronounced in the United Kingdom (9 per cent in the second quarter) and Denmark (5 per cent in the first).

Figure 17

House prices in Europe
(inflation-adjusted prices per square metre; indices, 2000=100)



Sources: National statistics; for Italy, based on Bank of Italy, *Consulente Immobiliare* and Istat data.

The price competitiveness of manufacturing industry improved slightly

The stabilization of the euro vis-à-vis other leading currencies and the rapid acceleration in the producer prices of our non-European competitors led to an improvement in the competitiveness of Italian firms between March and July, amounting to more than 1 per cent on the basis of producer prices (Figure 18). This tendency, which was common to all the leading euro-area economies, is thought to have gathered pace in Italy in August and September. The indicator based on unit labour costs, which also takes account of differences in productivity performance, shows a less favourable trend: in the second quarter competitiveness deteriorated further in Italy and to a lesser extent in the other major euro-area countries as well.

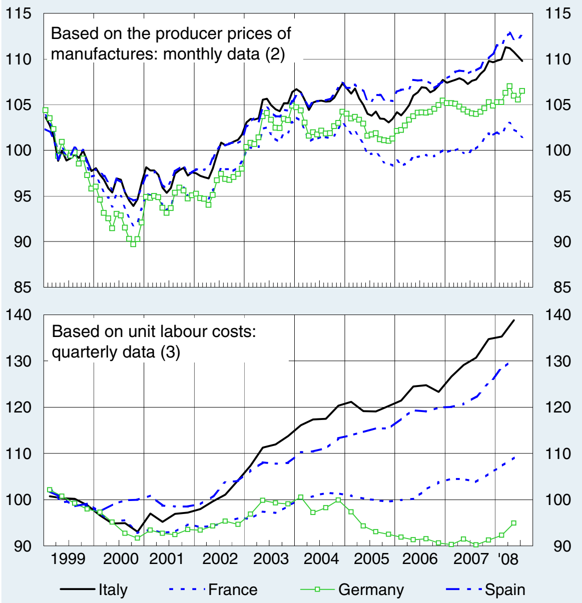
Productivity began to decline again

In Italy value added per employee fell for the third consecutive quarter in the context of a broadly unchanged level of activity and a rise in employment. In industry, where value added declined, productivity also fell, despite the contraction in employment in the sector. In the economy as a whole the rise in compensation per employee accelerated to 5.1 per cent (compared with 3.9 per cent in the first quarter) but in industry it remained unchanged at 4.5 per cent; the rate of increase in unit labour costs, on the other hand, quickened in both aggregates, to 6.1 and 5.2 per cent respectively (Figure 19 and Table 2.6 in the Statistical Appendix).

Figure 18

Indicators of competitiveness (1)

(indices, 1999=100)



Sources: Based on IMF, OECD and Eurostat data.
(1) An increase in the index indicates a loss of competitiveness. – (2) In relation to 61 competitor countries; latest available data refer to July 2008. – (3) In relation to 24 competitor countries; latest available data refer to the second quarter of 2008.

Corporate profitability is deteriorating...

Estimates based on national accounts data show that firms' operating profits continued to decline in the twelve months ending in June 2008, thus continuing a trend that has been under way intermittently since the first half of the decade. Self-financing decreased further to its lowest level of the past ten years in relation to value added, partly reflecting an increase in net interest expenses.

Figure 19

Labour costs and productivity in industry excluding construction

(annual data; percentage changes on preceding period)

Source: Based on Istat data.

...and their borrowing requirement is increasing

With investment virtually stagnating, the decline in self-financing has led to a slight increase in firms' borrowing requirement (the difference between gross investment and self-financing). At the end of June the financial debt of firms amounted to 74.7 per cent of GDP (Figure 20), 0.6 percentage points more than at the end of March.

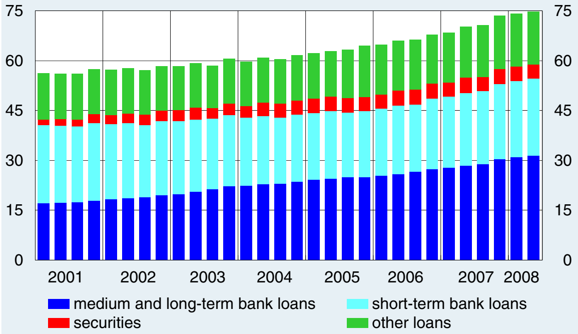
The growth in bank debt is slowing

Corporate debt towards the banking system continues to grow at a sustained pace (9.7 per cent in August), but it is showing signs of slowing for all sizes of firm and all geographical areas (Figure 21). The rate of growth reached a particularly low level for small firms (3.5 per cent, 5 per cent counting securitizations). In the second quarter of 2008 firms made net bond redemptions amounting to €1.5 billion; gross issues were virtually nil. According to Dealogic data on gross issues, placement activity remained very subdued in the third quarter as well. In addition, listed companies have raised almost no funds by means of capital increases since the beginning of the year. Mergers and acquisitions remained very limited; on the basis of data from *SDC Platinum*, eighteen operations amounting to €2 billion were announced in the first quarter and seventeen worth €4 billion in the second.

Figure 20

Corporate debt (1)

(as a percentage of GDP)

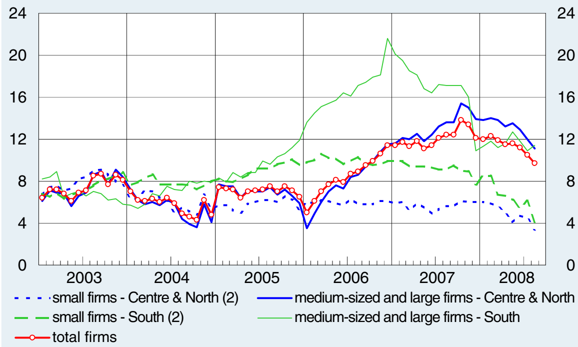


(1) The figures for the second quarter of 2008 are provisional.

Figure 21

Bank lending to firms by size and geographic location of firm (1)

(monthly data; twelve-month percentage changes)



(1) Loans exclude repos, bad debts and other minor items included in the Eurosystem harmonized definition of the aggregate. The breakdown by geographical area is based on customer residence. The percentage changes are calculated net of reclassifications, exchange rate variations and other changes not due to transactions. – (2) Limited partnerships, general partnerships, informal partnerships, de facto companies and sole proprietorships with up to 19 workers.

3.3 HOUSEHOLDS

Consumption fell in the first half...

After stagnating in the first quarter of 2008, household spending fell by 0.3 per cent in the second, and on average recorded a decrease of the same magnitude for the first six months of the year (Figure 22). The weakness of consumption reflected the modest growth in households' real disposable income, which rose by about 0.5 per cent in the first half of 2008 in relation to the corresponding period of last year. Nominal income rose by an estimated 4 per cent, owing mainly to an increase in compensation of employees as a result of a number of contract renewals, but households' purchasing power suffered because of the surge in consumer prices triggered by the rise in energy and food prices. Moreover, if adjustment is made for the monetary erosion of net financial assets due to the rise in inflation, in the first half of the year households' real disposable income contracted.

Growing concern about the economic situation sapped consumer confidence from the beginning of 2008 onwards, making households more cautious in their spending decisions and raising the saving rate. These developments had an impact on purchases of durable goods, which fell in the spring months for the fourth consecutive quarter (by 1.4 per cent on the preceding period) and were particularly conspicuous in the car market, with new registrations falling by about 2 per cent by comparison with the first three months of the year and by an average of 10.2 per cent in the first half in relation to the preceding period. Purchases of non-durable goods also fell, by an average of 0.8 per cent in the second quarter, owing mainly to the rapid acceleration in food prices, while spending on services stagnated, bringing to a close a long period of growth.

...and the outlook for the third quarter is also negative

The signs that can be deduced from the most recent economic indicators show that consumption remained weak during the summer. Car registrations continued to fall (by 3.8 per cent in the third quarter compared with the second, after seasonal adjustment), as did retail sales. The slight improvement in households' confidence in September, which was probably connected with the fall in oil prices, suggests that a further easing of consumer price pressures may at least attenuate the slowdown in household spending in the latter part of the year.

Household debt is declining relative to disposable income...

Household debt as a proportion of disposable income declined further in the second quarter, falling by 0.5 percentage points to 48.9 per cent, the same level as a year earlier; the decrease was mainly in medium and long-term debt (Figure 23). Since these data are obtained from the banks, they may have been affected by the volume of loans removed from their balance sheets by means of securitization operations, which have increased in recent months throughout the euro area. The ratio of Italian household debt to gross domestic product (33.7 per cent) remains very low by international standards, at around half the euro-area average and one third the level recorded in the United States and the United Kingdom.

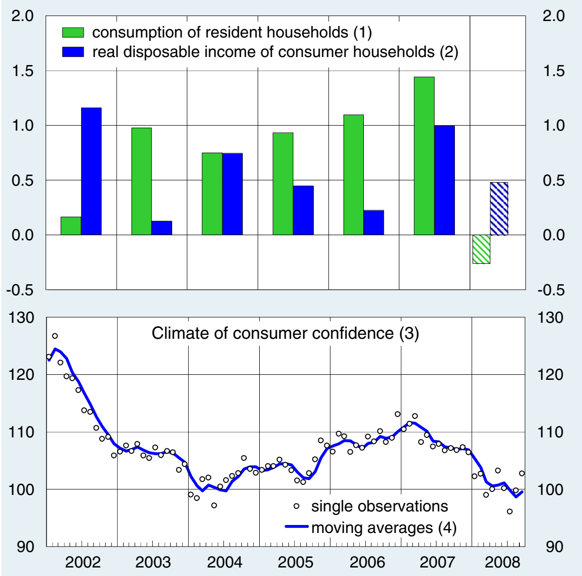
...but the cost of debt servicing is increasing

Households' debt servicing expenses (interest and repayments of principal) increased further; in the twelve months ending in June they amounted to 8.2 per cent of disposable income, one percentage point more than a year earlier. More than half of the increase was due to higher repayments of principal and the remainder to higher interest rates (Figure 24).

Figure 22

Household consumption and income and consumer confidence in Italy

(percentage rates of increase; indices)

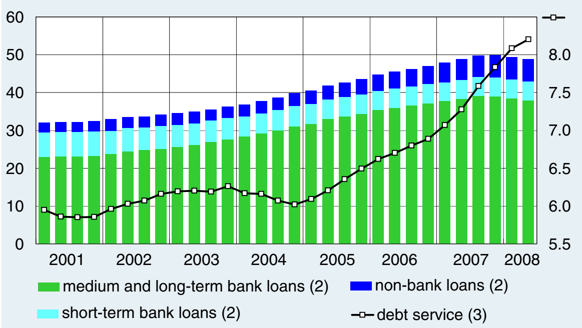


Sources: Based on ISAE and Istat data.
(1) Chain-linked volumes; percentage changes in relation to preceding year. Data for the first half of 2008 are adjusted for seasonal and calendar effects. – (2) Obtained using the deflator of consumption of resident households; our estimates for the first half of 2008. – (3) Indices: 1980=100, seasonally adjusted data. – (4) Moving average for the three months ending in the reference month.

Figure 23

Household debt (1)

(as a percentage of gross disposable income)



Sources: For gross disposable income, Istat and our estimates.
(1) Disposable income for 2008 is estimated on the basis of quarterly national accounts data. Data on loans in 2008 are provisional. – (2) End-of-period stocks. – (3) Right-hand scale. Refers only to consumer households and to the twelve months ending in the reference quarter. Debt service includes payment of interest and repayment of principal. Interest is calculated by multiplying the outstanding stocks in each period by an average rate that takes account of the composition of the stock according to maturity and type of intermediary; repayments of principal are estimated on the basis of supervisory reports.

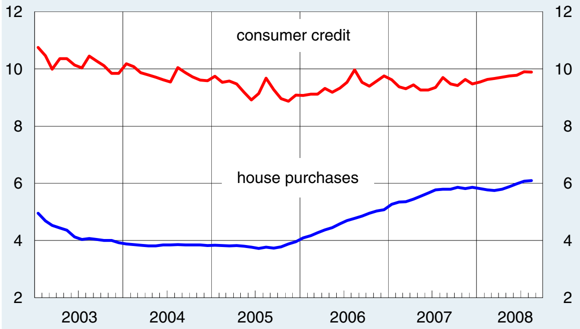
3.4 FOREIGN DEMAND AND THE BALANCE OF PAYMENTS

In the second quarter of 2008 exports declined...

After posting a good performance in the first three months of 2008, exports of goods and services declined by 0.7 per cent in volume terms in the second quarter by comparison with the preceding period, mirroring developments in France and Germany. The contraction of 1.3 per cent in exports of services, which account for around one fifth of the total, was twice as large as that in goods. Refined oil products, machinery, leather goods and transport equipment were the sectors worst affected. The fall in exports involved non-EU countries and especially the United States, where demand continues to be depressed by the cyclical slowdown and the depreciation of the dollar against the euro. In the last twelve months the pound sterling has also depreciated against the common European currency, but the adverse effect on exports to the United Kingdom has been smaller. Exports to other EU member states remained broadly stable: a modest reduction in sales to France offset an expansion in exports to Germany.

Figure 24

Interest rates on bank loans to households: APRC on new business (1)
(monthly data; percentages)



(1) The data on bank lending rates refer to euro transactions and are gathered and processed using the Eurosystem's harmonized method. "New business" means contracts concluded during the reference period or contracts renegotiating previous terms and conditions. The APRC (annual percentage rate of charge) includes ancillary expenses (administrative expenses, loan examination fees and insurance) and is calculated as the average rate across all maturities, weighted by loan amounts.

...and imports increased, owing to the recovery in services

The increase of 0.3 per cent in the overall volume of imports between the first and second quarters was the product of stagnation in merchandise exports and a recovery of 1.4 per cent in imports of services, offsetting part of the sharp fall in the first three months of the year. The overall result was strongly affected by the pronounced reduction in imports of energy products and transport equipment; the former were curbed by the large rise in the price of oil and the weakness of the business cycle and the latter by the appreciable fall in demand for motor vehicles.

Exports were checked by the weakness of world demand

Data for July on foreign trade in value terms appear to show that exports held up, especially those to non-EU countries, but not sufficiently to offset the sharp contraction they suffered in June. They continue to be affected by the uncertain cyclical situation of the world economy: information for August on trade with countries outside the European Union indicate a distinct fall in exports.

No change in the small surplus on merchandise trade

In the first seven months of 2008 the deficit on the current account of the balance of payments rose to €30.3 billion, compared with €20.3 billion in the corresponding period of 2007 (Table 3); it stood at 3.7 per cent of GDP in the second quarter of the year, against 4.2 per cent in the first. The modest surplus on merchandise trade improved only marginally; it now amounts to €2.4 billion. The relentless rise in the prices of crude oil and its derivatives drove the energy deficit up to €34.0 billion, around €9 billion more than in the first seven months of 2007. The deficit on services showed a further slight reduction, falling to €3.2 billion. The deficit on the income account, which has been steadily widening, increased to €20.8 billion, with most of the deterioration occurring in income on portfolio investment. Given that there was only a small net debtor position equal to 5.2 per cent of GDP at the end of 2007, the reason for the deterioration lay in the composition of gross assets and liabilities (equal to about 125 and 130 per cent of GDP respectively) according to currency and type of instrument. The appreciation of the euro curbed the growth in investment income from abroad, of which around 20 per cent is denominated in other currencies, with the US dollar accounting for almost half of that portion; substantial dividend payments concentrated in May and June contributed to the growth in income paid to non-residents.

Table 3

Italy's balance of payments (1)
(billions of euros)

	2006	2007	Jan.-July 2007	Jan.-July 2008
Current account	**-38.5**	**-37.4**	**-20.3**	**-30.3**
Goods	-10.2	2.9	2.0	2.4
non-energy products (2)	*37.5*	*47.7*	*26.9*	*36.4*
energy products (2)	*-47.7*	*-44.7*	*-24.9*	*-34.0*
Services	-1.3	-7.0	-4.1	-3.2
Income	-13.6	-19.7	-12.5	-20.8
Current transfers	-13.5	-13.7	-5.7	-8.8
Capital account	**1.9**	**2.7**	**1.1**	**1.4**
Financial account	**25.4**	**26.1**	**11.7**	**20.9**
Direct investment	-2.3	-37.0	-10.7	-18.6
Portfolio investment	44.3	18.1	-0.4	80.2
Financial derivates	-0.4	0.4	0.3	6.0
Other investment	-16.7	46.1	25.1	-44.2
Change in official reserves	0.4	-1.5	-2.6	-2.4
Errors and omissions	**11.2**	**8.6**	**7.5**	**8.0**

1) Provisional data for June and July 2008. – (2) Based on Istat data on foreign trade

The weight of debt securities in Italians' foreign portfolios continues to increase

In the first seven months of 2008 the financial account showed a net outflow of €18.6 billion in direct investment. Italian investment abroad (€16.6 billion) was accompanied by modest disinvestment by foreign investors, due to a large transaction between a resident bank and one abroad. Portfolio investment continued to show substantial net inflows (€80.2 billion), owing mainly to non-residents' purchases of Italian debt securities and residents' disposals of foreign equities and fund units. Since the onset of the financial crisis in August 2007 residents have steadily repatriated funds totalling €69.7 billion invested in riskier foreign assets, such as shares and fund units. Following moderate net disinvestment in the second half of 2007, in the first few months of this year non-residents resumed their large-scale purchases of Italian government securities, especially Treasury bills and bonds.

3.5 THE LABOUR MARKET

Employment is still growing...

In the second quarter of 2008 Istat's labour force survey shows a seasonally adjusted increase in employment of 0.4 per cent with respect to the preceding quarter (0.3 per cent according to the national accounts). This follows a rise of 0.5 per cent in the first three months of the year. The growth occurred in the South (0.9 per cent) and to a lesser extent in the North (0.5 per cent), while the Centre saw a decline of 0.4 per cent. The continued growth in employment in services was accompanied by a partial recovery in industry excluding construction, after three quarters of decline.

...especially among women, non-Italians and workers on fixed-term or part-time contracts

The increase in the number of people in employment by comparison with the second quarter of 2007 (Table 4) was due mainly to the growth in female employment (2.4 per cent, against 0.4 per cent for men). The share of non-Italian workers rose from 6.5 to 7.4 per cent, reflecting a large increase in registrations of citizens from new EU countries. Employees continued to represent a larger share of the total, rising from 73.6 to 74.2 per cent, owing largely to the growth in fixed-term jobs (from 13.4 to 14 per cent of total employees). The proportion of part-time employees rose by 1.1 percentage points to 15.1 per cent. The employment rate in the 15-64 age group rose by 0.3 points to 59.2 per cent, although there was a decline for men.

The large increase in participation...

The labour force increased again with respect to the preceding quarter, with seasonally adjusted growth of 0.6 per cent, compared with 0.8 per cent in the first three months of the year. The participation rate for the population aged between 15 and 64 was one percentage point higher than in the second quarter of 2007, reflecting mainly increased participation by women (Table 4). The participation rate of the 15-24 age group, which had begun to increase in the first quarter of this year after having been in decline since 2004, continued to rise.

...is reflected in a further rise in the unemployment rate

In a context of contrasting signals that it is difficult to attribute to a single factor, the expansion in the labour force was greater than that in employment, causing the seasonally adjusted unemployment rate to rise to 6.8 per cent, two tenths of a point more than in the preceding quarter. The rise occurred in the Centre and North (0.4 and 0.2 percentage points respectively), whereas in the South the rate fell by 0.1 point. The number of persons unemployed was almost 300,000 higher than in the second quarter of 2007; almost one third of these were persons who had been in work a year earlier, who were concentrated mainly in the Centre and North. Until the end of 2007 the contribution of this component to the rise in unemployment had been negative or nil (Figure 25).

Private sector earnings fall in real terms

According to the national accounts, the growth in de facto per capita earnings in the private non-farm sector, which had accelerated sharply to 6 per cent in the first quarter of 2008 with respect to a year earlier in connection with one-off payments under collective agreements in important sectors, came down to 3 per cent in the second quarter, almost one percentage point less than the rise in consumer prices. The increase was larger in industry than in private services (4.1 per cent compared with 1.9 per cent). Our estimates, which now take account of the renewal of the collective agreement in the distribution sector, confirm that the acceleration in de facto per

Table 4

Labour force status of the Italian population

(thousands of persons and percentages)

	H1 2007	H1 2008	Q2 2007	Q2 2008	Change Q2 2008/ Q2 2007 (1)
Total persons in work	**23,072**	**23,376**	**23,298**	**23,581**	**1.2**
Employees	**16,996**	**17,299**	**17,155**	**17,496**	**2.0**
of which: fixed-term contracts	*2,216*	*2,316*	*2,305*	*2,443*	*6.0*
part-time contracts	*2,355*	*2,573*	*2,397*	*2,639*	*10.1*
Self-employed	**6,076**	**6,076**	**6,143**	**6,085**	**-0.9**
Labour force	**24,556**	**25,108**	**24,710**	**25,285**	**2.3**
men	*14,701*	*14,874*	*14,797*	*14,987*	*1.3*
women	*9,855*	*10,234*	*9,914*	*10,298*	*3.9*
Population	**58,770**	**59,226**	**58,803**	**59,294**	**0.8**
Unemployment rate	**6.0**	**6.9**	**5.7**	**6.7**	**1.0**
men	*4.9*	*5.6*	*4.6*	*5.4*	*0.8*
women	*7.7*	*8.9*	*7.4*	*8.7*	*1.3*
Participation rate (age 15-64)	**62.2**	**63.1**	**62.5**	**63.5**	**1.0**
men	*74.2*	*74.5*	*74.5*	*74.9*	*0.4*
women	*50.3*	*51.8*	*50.6*	*52.1*	*1.5*
Employment rate (age15-64)	**58.4**	**58.7**	**58.9**	**59.2**	**0.3**
men	*70.5*	*70.3*	*71.1*	*70.8*	*-0.2*
women	*46.4*	*47.2*	*46.8*	*47.5*	*0.7*
North	*66.4*	*66.9*	*66.7*	*67.2*	*0.5*
Centre	*62.1*	*62.9*	*63.2*	*62.9*	*-0.3*
South	*46.2*	*46.1*	*46.7*	*47.0*	*0.3*

Source: Istat labour force surveys.
(1) Percentage change for persons and change in percentage points for rates.

Figure 25

Persons seeking work

(change on corresponding period of previous year)

Source: Based on data from Istat labour force surveys.

capita earnings in 2008 was due to one-off payments and that next year will see a return to a more moderate rate of growth.

Productivity performance remains disappointing

In the first half of the year value added per labour unit fell by 0.2 per cent in industry and by 1.9 per cent in private services with respect to the same period of 2007. In the economy as a whole it fell by 0.8 per cent, while compensation per employee increased by 4.5 per cent. As a result, unit labour costs rose by 5.3 per cent, well above the increase in France and Germany, where productivity continued to rise.

3.6 PRICE DEVELOPMENTS

The acceleration in inflation came to a halt in September

Consumer price inflation continued to rise during the summer. On the basis of the index for the entire resident population (CPI), it reached a twelve-month rate of 4.1 per cent in July and August, its highest level since the mid-1990s; the harmonized index (HICP) registered a similar rise, albeit with greater monthly volatility due to the different method of recording promotional sales (Table 5). Prices continued to be affected by the persistent increases in oil prices, which hit new peaks in July, and in food commodities, which rose continuously until the early summer before falling back. Inflation excluding food and energy products and items with regulated prices rose slightly, from around 2.4 per cent in the first half of the year to 2.7 per cent in August. One contributory factor was the half-point acceleration in the rate of increase of the prices of services (to 3.7 per cent in August), which was generated mainly by rises in the branches most directly affected by the pressures in commodity markets: air transport and restaurants and lodging services. Among the other components, the rate of increase in rents accelerated from 2.2 per cent at the beginning of the year to 2.7 per cent in August, responding with the customary lag of several months to the prolonged rise in average inflation. The rate of increase in the prices of goods other than food and energy, on the other hand, remained stable at around 1.5 per cent, helping to mitigate core inflation. According to provisional figures from Istat, in September the rise in the CPI slowed to a twelve-month rate of 3.8 per cent, thanks to the fall in crude oil prices and the easing of pressures in the market in food products. On the basis of available information, the rise in the prices of goods other than food and energy also slowed as a result of the deterioration in the economic climate and the weakening of overall demand. The easing of imported inflationary pressures was probably partly offset by an increase in domestic costs, in particular wages, owing primarily to one-off payments to cover periods of contract hiatus in both the private and public sectors; with the prospect of a further period of wage restraint, inflation should continue to head downwards in the next few quarters.

Table 5

Indicators of inflation in Italy
(twelve-month percentage changes)

		HICP (1)		CPI (2)			PPI (3)
		Overall index	Excl. energy and food	Overall index	1-month	Core component	Overall index
2006		2.2	1.6	2.1	–	1.8	5.6
2007		2.0	1.8	1.8	–	1.9	3.5
2007 –	Jan.	1.9	1.5	1.7	0.1	1.7	4.0
	Feb.	2.1	2.0	1.8	0.3	1.8	4.0
	Mar.	2.1	2.0	1.7	0.2	1.9	3.8
	Apr.	1.8	1.8	1.5	0.2	1.7	3.3
	May	1.9	1.8	1.5	0.3	1.9	3.0
	June	1.9	1.9	1.7	0.2	1.9	2.7
	July	1.7	1.7	1.6	0.2	2.0	2.0
	Aug.	1.7	1.8	1.6	0.2	2.1	2.1
	Sept.	1.7	1.7	1.7	0.0	1.8	3.5
	Oct.	2.3	1.9	2.1	0.3	2.0	3.7
	Nov.	2.6	1.9	2.4	0.4	2.1	4.8
	Dec.	2.8	2.0	2.6	0.3	2.2	4.7
2008	Jan.	3.1	2.1	3.0	0.4	2.4	5.4
	Feb.	3.1	2.0	2.9	0.2	2.2	5.9
	Mar.	3.6	2.4	3.3	0.5	2.4	6.4
	Apr.	3.6	2.1	3.3	0.2	2.4	6.3
	May	3.7	2.2	3.6	0.5	2.4	7.5
	June	4.0	2.3	3.8	0.4	2.5	8.2
	July	4.0	1.9	4.1	0.5	2.5	8.7
	Aug.	4.2	2.5	4.1	0.1	2.7	8.2
	Sept.	3.9	....	3.8	-0.3	....	....

Sources: Based on Istat and Eurostat data.
(1) Harmonized index of consumer prices. – (2) Index of consumer prices for the entire resident population; it differs from the harmonized index primarily on account of the different method of recording the prices of pharmaceutical products and promotional sales. – (3) Index of producer prices of industrial products sold on the domestic market.

Producer prices also slowed, thanks mainly to the fall in oil prices

The acceleration in producer prices (PPI), which had been under way for a year, came to an end in August; the twelve-month rate of increase in the overall index which had crept up to 8.7 per cent in July, fell by half of one percentage point, thanks to the marked slowdown in the rise in the prices of energy and food products, from 26.2 per cent in July to 23.7 per cent in the case of energy and from 9.6 to 8.1 per cent in that of food.

The slowdown in inflation should continue in the coming months

In the next few months the twelve-month rate of increase in consumer prices should slow, but it is likely to be affected by the adjustment in energy charges to take account, with the usual lag, of past increases in raw materials prices in international markets. According to professional forecasters surveyed by Consensus Economics in September, inflation will continue to decrease to just over 2 per cent in the second half of next year. These expectations take account of the initial effects of the weakening of economic activity both on the world prices of oil and other raw materials and on firms' pricing policies. The survey carried out in September by the Bank of Italy in collaboration with *Il Sole 24 Ore* revealed that firms are less inclined to raise their prices in the next few months, a finding that is in line with the responses recorded by the economic survey carried out by ISAE.

3.7 BANKS

The slowdown in bank lending continues...

In the twelve months ending in August 2008 the expansion in bank lending in Italy, although still substantial, slowed down to 7.7 per cent; it had been 10.1 per cent in December 2007 (Table 6). The slowdown, which began about two years ago as far as lending to households is concerned, has now spread to lending to non-financial companies. The recent developments are due mainly to a slackening of credit demand from firms and households. The slowdown in bank lending continued to be more pronounced in the South than in the Centre and North; in August the rates of growth were 6.4 and 7.5 per cent respectively (Selected statistics, Table A9).

Table 6

Main assets and liabilities of Italian banks (1)
(end-of-period data; 12-month percentage changes)

	2006	2007	August 2008	
				Stocks (2)
Assets				
Securities	5.3	7.3	42.6	311,258
Loans	11.5	10.1	7.7	1,719,116
up to 12 months	*10.8*	*7.5*	*7.6*	*588,369*
beyond 12 months	*11.9*	*11.3*	*7.7*	*1,130,747*
External assets	19.8	12.5	3.9	399,732
Liabilities				
Domestic funding (3)	9.9	7.3	12.6	1,770,295
Deposits	8.3	4.2	8.3	1,060,417
of which: (4)				
current accounts	*6.7*	*2.9*	*3.8*	*620,957*
with agreed maturity	*9.8*	*14.3*	*24.2*	*54,647*
redeemable at notice	*-0.8*	*-0.5*	*6.5*	*234,764*
repos	*29.4*	*12.1*	*27.0*	*136,183*
Bonds (3)	12.5	11.9	19.7	709,878
External liabilities	25.6	22.9	7.0	538,557

(1) The figures for August 2008 are provisional. From October 2007 onwards the data include Cassa Depositi e Prestiti S.p.A. The percentage changes are calculated net of reclassifications, exchange rate variations and other variations not due to transactions. – (2) Millions of euros. – (3) Includes bonds held by non-residents. – (4) Does not include those of central government.

...owing partly to the sustained pace of securitization

The slowdown in lending takes on a more gradual appearance if the assets securitized by banks are imputed to credit flows. If the figures are corrected for the effect of such operations, it can be estimated that credit grew by more than 10 per cent in Italy in August (Figure 26). Indeed, the slowdown in lending to households, particularly in the form of mortgage loans, can be ascribed in part to the recovery in securitization operations, aimed mainly at using the resulting securities as collateral in refinancing operations with the Eurosystem at a time of strains in the liquidity markets.

The gradual tightening of lending conditions continues

In the Bank Lending Survey carried out on 7 July with reference to the second quarter of this year, the participating Italian banks reported a further modest tightening of the criteria for lending to firms (see the box "Credit supply and demand in Italy"). As regards lending to households, after almost two years of easing, the signs of stricter conditions that had already emerged for mortgage loans spread to consumer credit. The banks foresee a further tightening of lending conditions. The quarterly survey of inflation expectations and growth in industry and services carried out in September by the Bank of Italy and *Il Sole 24 Ore* made similar findings: the proportion of firms reporting a deterioration in lending conditions was higher than in previous quarters, particularly among firms that had actually applied for a new loan or an increase in an existing one. The tightening of lending conditions will presumably have an impact on the volume of credit granted in the next few months. Average bank interest rates continued to adjust gradually to money-market rates (Figure 27).

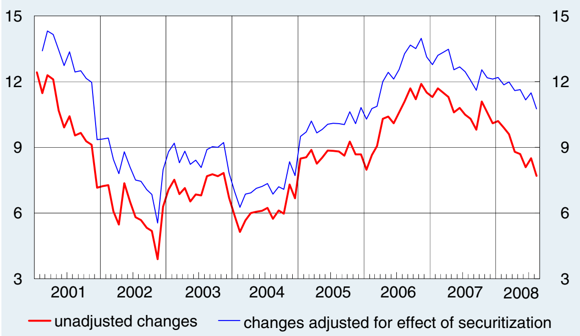
Credit quality, though still high, could be affected by the cyclical downturn

In the twelve months ending in June the ratio of new bad debts to total lending increased slightly, to 0.9 per cent. The volume of substandard loans (exposures to borrowers in temporary difficulties) in relation to total lending also increased to 1.6 per cent, compared with 1.5 per cent last December, indicating some signs that both households and firms are having difficulty repaying loans. As to the future, the deterioration in economic conditions and the rise in money-market rates could exacerbate difficulties in making payments on variable-rate mortgages, particularly those taken out when market rates were lowest. The rules on the early repayment and portability of mortgages and the recent agreement between the Italian Banking Association and the Ministry for the Economy and Finance aimed at permitting the revision of contractual terms or other agreements are designed to stabilize households' payment flows.

Figure 26

The effect of securitizations on bank lending in Italy (1)

(monthly data; 12-month percentage changes)

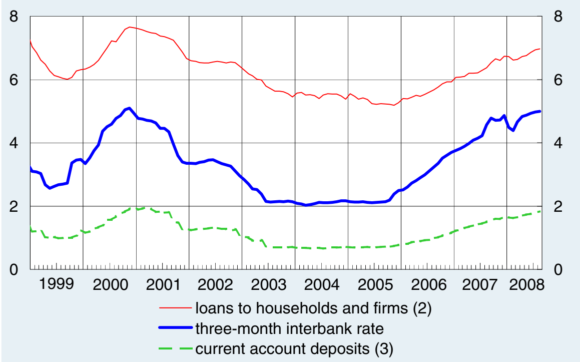


Source: Based on Bank of Italy data.
(1) Includes other loans to resident customers assigned without recourse to entities other than MFIs.

Figure 27

Short-term bank interest rates (1)

(monthly data; percentages)



Sources: Based on Bank of Italy and e-MID data.
(1) The data on lending and deposit rates refer to transactions in euros and are gathered and processed using the Eurosystem's harmonized method. – (2) Average rate on loans to households and firms with a maturity of up to one year. – (3) Average rate on current account deposits of households and firms.

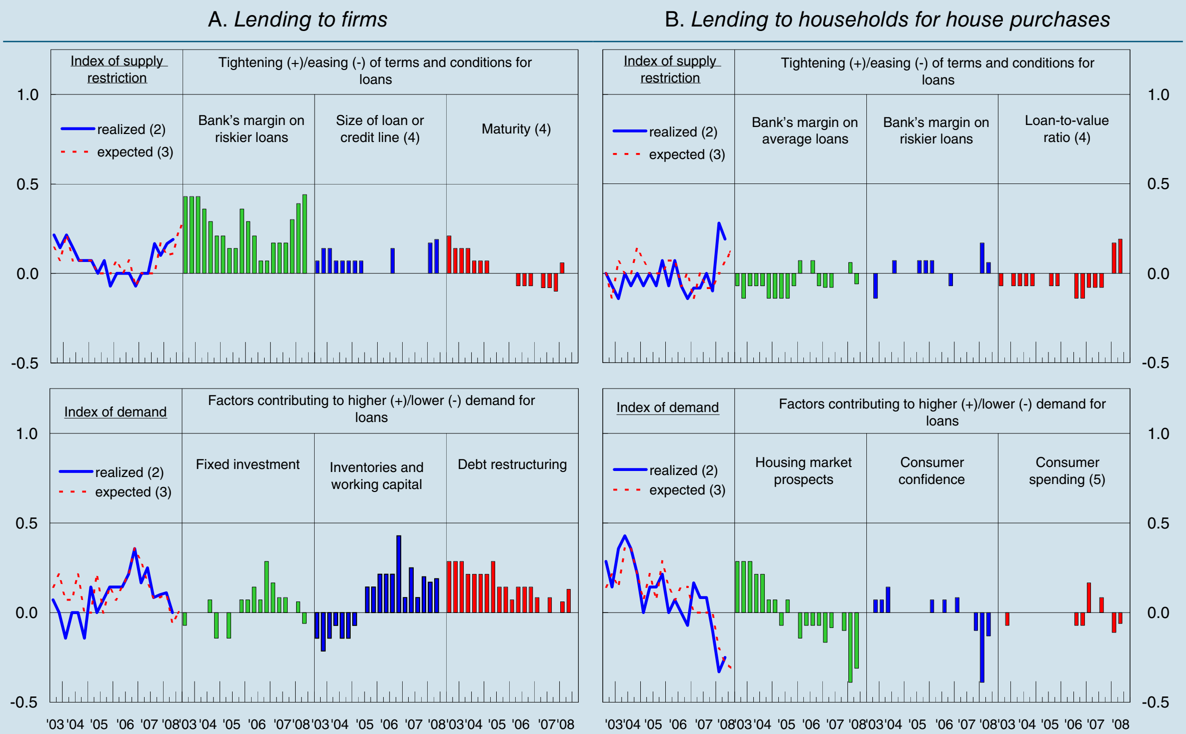
CREDIT SUPPLY AND DEMAND IN ITALY

As they had in the three previous surveys, the Italian banks participating in the euro-area Bank Lending Survey [1] for the second quarter reported that they had tightened credit standards for loans to firms moderately (Figure A). The tightening was more pronounced for long-term loans and those

[1] The survey, conducted in the first ten days of July, covered the eight leading Italian banking groups; the results for Italy are available at www.bancaditalia.it and those for the euro area at www.ecb.int. The results of the survey conducted in the first ten days of October, not yet available, will be released on 7 November.

Figure A

Trends in supply conditions and credit demand in Italy (1)



Source: Quarterly Bank Lending Survey for the euro area.
(1) Diffusion indices constructed by aggregating the qualitative replies from the groups participating in the survey, weighted as follows: for supply conditions, 1 = tightened considerably, 0.5 = tightened somewhat, 0 = remained basically unchanged, -0.5 = eased somewhat, -1 = eased considerably; for demand, 1 = increased considerably, 0.5 = increased somewhat, 0 = basically unchanged, -0.5 = decreased somewhat, -1 = decreased considerably. The range of variation of the index is from -1 to 1. – (2) Refers to the quarter ending at the moment of the survey. – (3) Forecasts made in the preceding quarter. – (4) Positive (negative) values indicate a greater (lesser) willingness of banks to grant large loans, long-term loans, or loans with high loan-to-value ratios. – (5) Positive (negative) values indicate that the trend in consumer spending other than for home purchases had an expansive (restrictive) effect on the demand for mortgages.

to larger firms and mainly reflected the deterioration of the economic situation and the persistence of financial strains (Figure B). For the first time since the onset of the crisis, the greater prudence of the banks surveyed was also reflected significantly in a shortening of loan maturities and in the use of particular clauses to contain risk. The banks reported a slowdown in credit demand from firms, especially the smaller ones. They indicated that for the third quarter they expected a further tightening of business lending standards and an unchanged rate of growth in credit demand.

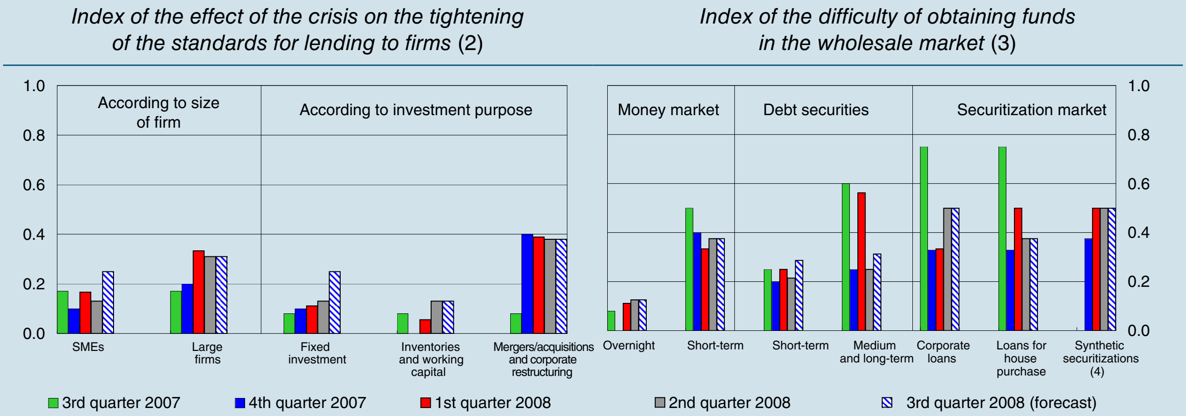
The tightening of lending conditions for households, under way since the start of the year as regards mortgages, was extended to consumer credit in the second quarter. The banks reduced their loan-to-value ratios on mortgage loans and increased their margins on consumer credit. Households' demand for mortgages continued to expand at roughly the same slow pace as in the preceding quarters. That for consumer credit apparently picked up in connection with the sluggish growth of disposable income.

On the funding side, the difficulties engendered by the financial market crisis persisted; they were attenuated only for issues of medium to long-term securities. Half the respondent banks reported that the subprime crisis had affected the cost of meeting capital adequacy requirements and consequently the supply of credit. The institutions surveyed expected the funding problems to continue in the third quarter.

The Italian banks' responses to the survey were broadly in line with those of their counterparts in the rest of the euro area. The only significant difference was the reported acceleration in consumer credit as estimated by the banks, while for the area as a whole it slowed down.

Figure B

Effects of the subprime mortgage crisis in Italy (1)



Source: Quarterly Bank Lending Survey for the euro area.
(1) Diffusion indices constructed by aggregating the qualitative replies to the special questions on the effects of the subprime mortgage crisis added to the quarterly Bank Lending Survey. – (2) Weighted as follows: 1 = tightened considerably, 0.5 = tightened somewhat, 0 = remained basically unchanged, -0.5 = eased somewhat, -1 = eased considerably. The range of variation of the index is from -1 to 1. – (3) Weighted as follows: 1 = considerable difficulty, 0.5 = some difficulty, 0 = basically no difficulty. The range of variation of the index is from 0 to 1. – (4) These imply recourse to credit derivatives. Data for the third quarter of 2007 are not available for this indicator.

Domestic funding accelerated, offsetting the fall in external liabilities

The growth in banks' domestic fund-raising rose to 12.6 per cent in August, with most of the additional expansion being in less liquid instruments: bonds, repos and time deposits. Current accounts, which had increased strongly in the first half of the year, slowed to a growth rate of 3.8 per cent. The increase in banks' external liabilities continued to slacken (see the box "The effects of the financial crisis on Italian banks' funding"). Since January the yield on fixed-rate bonds has risen by 0.5 percentage points to 4.8 per cent, and that on variable-rate issues by 0.1 percentage points to 5 per cent.

THE EFFECTS OF THE FINANCIAL CRISIS ON ITALIAN BANKS' FUNDING

The Italian banking system has a low exposure, either direct or indirect, to US subprime mortgages, and its operations in the structured finance market are relatively limited. Italian banking groups have made significantly smaller write-downs to structured credit products than the other main European banks. The exposure of the twenty largest banking groups to Lehman Brothers amounted in mid-September to 0.5 per cent of their regulatory capital at the end of 2007.

Since September 2007 the Bank of Italy has intensified its controls on the liquidity situation of the largest banking groups.

From the outbreak of the crisis, the strains in international capital markets have had a significant impact on the channels and the cost of Italian banks' funding. Funding from non-resident banks and money-market funds diminished by 0.9 per cent between the middle of 2007 and the middle of 2008, the latest date for which detailed data are available, whereas that channel had expanded by 43.4 per cent in the previous twelve months, when it had accounted for more than half of the growth of total funding. In particular, the stock of Italian bank bonds held by banks and money-market funds resident in the other euro-area countries contracted by 15 per cent (almost €20 billion).

Italian banks faced the decline in international demand for bank liabilities by increasing their funding from non-bank customers. Nevertheless, total fund-raising by the entire banking system slowed sharply to a growth rate of 6.7 per cent, half the pace of the previous twelve months.

The expansion in domestic funding was achieved mainly through an increase in bond sales to customers, in part the result of aggressive and costly issuance policies. The interest rate spread between fixed-rate bank bonds and BTPs, which had always been negative in the past, turned positive from the summer of 2007 onwards and averaged 20 basis points in the 12 months ending last June; that between floating-rate bonds and CCTs, which had been close to zero in the months preceding the crisis, averaged 36 basis points.

Large banks, more oriented to procuring funds on the international capital markets, have been affected more severely by the financial crisis. However, the expansion in volumes on the domestic interbank market allowed them to mitigate its repercussions. Total domestic interbank liabilities grew by more than 20 per cent between mid-2007 and mid-2008. Sight deposits accelerated from growth of 1.5 to 23.4 per cent despite the reduction in transactions on the e-MID interbank deposit market, reflecting the increasing propensity of banks to trade liquidity bilaterally. The stock of bank bonds held by other banks rose by more than 60 per cent, in part because securities remained on banks' balance sheets awaiting placement with the public.

The data, still incomplete, for the most recent months confirm the sharp slowdown in fund-raising abroad and the expansion in domestic funding.

Table

Bank funding (1)
(millions of euros and percentage points)

	Twelve-month absolute changes			Twelve-month percentage changes			Stocks at June 2008
	June 2008	June 2007	June 2006	June 2008	June 2007	June 2006	
Funding from resident non-bank customers (a)	123,332	67,812	63,993	10.0	5.8	5.8	1,534,093
Deposits	*46,249*	*46,857*	*53,758*	*5.4*	*5.8*	*7.1*	*1,072,270*
Bonds (2)	77,083	20,956	10,235	20.5	5.9	*3.0*	*461,823*
Deposits of non-resident non-bank customers (b)	6,599	-317	-549	11.5	-0.6	-0.9	64,305
Interbank funding from non-residents (c)	-5,270	172,000	62,746	-0.9	43.4	18.8	564,150
Deposits	13,169	132,782	37,918	3.0	42.4	*13.8*	*459,921*
Bonds (3)	*-18,439*	*39,218*	*24,828*	*-15.0*	*47.0*	*42.4*	*104,229*
Total funding (a+b+c)	124,661	239,495	126,190	6.7	14.8	8.5	2,162,548
Deposits	*66,017*	*179,322*	*91,126*	*4.9*	*15.2*	*8.4*	*1,596,496*
Bonds	58,644	60,174	35,063	11.8	13.7	*8.7*	*566,052*
Memorandum item:							
Domestic interbank funding	109,260	73,247	25,974	21.4	16.7	6.3	621,304
Deposits	*56,298*	*68,478*	*15,296*	*13.2*	*19.1*	*4.4*	*484,415*
Bonds	*52,962*	*4,769*	*10,678*	*63.1*	*6.0*	*15.6*	*136,889*

(1) Excludes funds raised from central banks. The data, except for those on stocks, do not include those reported by Cassa Depositi e Prestiti. – (2) Also includes bonds held by non-resident non-bank customers and by non-euro-area banks. – (3) Only includes bonds held by euro-area monetary and financial institutions.

Between July 2007 and August 2008 the average cost of Italian banks' total funding (non-bank customers and interbank sources, domestic and foreign) rose by 63 basis points, to 3.9 per cent.[1] The effects of the changes in the composition of liabilities were modest; nearly all of the increase can be ascribed to the rise in interest rates, due in part to the higher risk premiums on bank liabilities.

The difficulties in procuring funds are increasing in the light of recent international developments. The strains in the markets have grown since the middle of September, reflecting the crisis of major financial intermediaries in the United States (see the box "The crisis of some US financial institutions and the support action of the authorities"). The share prices of the main European banks have recorded large swings.

In September the average of the premiums on credit default swaps, which cover an issuer's securities from default risk, was equal to 87 basis points for the major Italian banking groups, a high level by historical standards but lower than the average of 141 basis points for large European intermediaries. The difference between the spreads for European and Italian banking groups widened after the failure of Lehman Brothers, suggesting less perception of risk for Italian than foreign banks. However, with the persistence of strains and the heightening of uncertainty, the premiums on credit default swaps have risen in Italy as well since the end of September; in the first ten days of October, the average premium was higher than in the previous month.

The surge in uncertainty has also caused a contraction in trading on the interbank market, a widening of the spreads between interbank rates and the reference rates set by the monetary authorities, and an expansion in overnight deposits with the European Central Bank. The strains persisted in the first few days of October, despite the coordinated reduction in interest rates by the monetary authorities and large infusions of liquidity into the system.

[1] The average cost of funds was calculated as the average of the interest rates on the different funding instruments, weighted by the respective quantities. The rates on the various forms of deposit from non-bank customers are drawn from ECB harmonized statistics, those on the stock of bonds outstanding from ten-day statistics. The rates on Italian and foreign interbank liabilities are the Eonia for current accounts, Eurepo rates for repos and Euribor rates for unsecured term deposits.

Banks' profitability declined in the first half of 2008

On the basis of data currently available, the relatively small exposure of the major Italian banks to the American subprime and Alt-A sectors, related securities and "vehicles" operating in the sector helped overall in containing the impact of the turmoil on bank profitability. According to their consolidated reports, in the first half of this year the profitability of the main Italian banking groups was down by comparison with the same period of 2007 but still in positive territory. Return on equity (ROE), calculated on an annual basis and excluding capital gains and extraordinary income, fell by almost three points to around 10 per cent. The growth in net interest income, although significant, was not sufficient to offset the decline in other income due to the contraction in income from trading and net commission income. Profit on ordinary activities fell by almost one fifth, owing partly to a slight increase in costs and higher write-downs on loans.

3.8 THE FINANCIAL MARKET

The stock market index continued to fall

Between the beginning of July and 10 October the Italian stock market index declined by 32 per cent in the wake of the international financial crisis, which caused comparable falls in the stock markets of all the euro-area countries; the loss since the beginning of 2008 amounted to 47 per cent, in line with the average for the area (Figure 28). The fall in share prices reflects a further deterioration in expectations about the profits of listed companies and an increase in the risk premium demanded by investors for holding shares. The largest declines were in the shares of companies in the oil and basic materials sectors (43 and 62 per cent respectively), which were affected by the sharp fall in the prices of oil and non-energy raw materials from mid-July onwards; more generally, the shares of non-financial corporations fell on average by more than the overall index (by 36 per cent) in reaction to the steady deterioration in the macroeconomic situation. On average, bank shares fell by less than the index as a whole (27 per cent).

Current earnings/price ratios continued to rise, reaching their highest levels of the last decade (Figure 29). As in the other world stock markets, the expected volatility of share prices increased dramatically at the end of August and is now at historical highs.

In the first nine months of the year there were seven new listings on the Italian stock exchange, compared with 25 in the corresponding period of the preceding year; the number of initial public offerings in the euro area was also significantly down: 47 against 153 a year earlier. At the end of September there were 299 Italian companies listed on Borsa Italiana, with a total market capitalization of €480 billion, equivalent to 30.2 per cent of GDP.

Figure 28

Share prices (1)

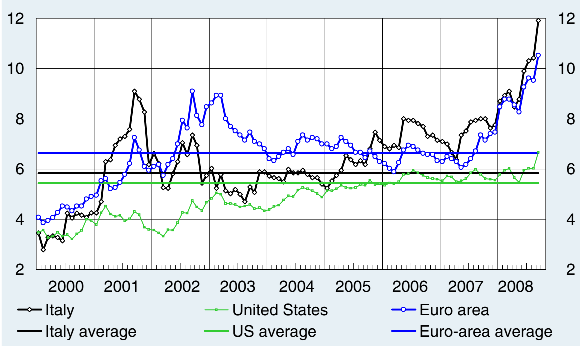
(end-of-week data; indices, 31 December 2004=100)

Source: Thomson Financial Datastream.
(1) MIB for Italy, Dow Jones Euro Stoxx for the euro area, Standard & Poor's 500 for the United States. The latest available figure refers to 10 October.

Figure 29

Current earnings/price ratios for the main stock exchanges (1)

(monthly data; percentages)



Sources: Thomson Financial Datastream and Bank of Italy data.
(1) Averages are calculated from January 1986.

Bond issues soared

In the second quarter of the year net bond issues by Italian companies amounted to €61 billion, substantially higher than in the preceding quarter (€37 billion) and in the comparable period of 2007 (€31 billion; Table 7). The increase reflects placements by banks and other financial corporations, the latter partly as a result of securitization operations. Italian non-financial corporations, by contrast, continued to make net redemptions of bonds, contrary to developments in the rest of the euro area.

Risk premiums increased on both private sector bonds...

Yield differentials between investment-grade bonds issued by non-financial corporations and government securities remained large but stable in July and August but increased from the beginning of September onwards as the crisis in financial markets deepened; the widening between the beginning of July and 10 October amounted to 1.8 percentage points, 0.5 points more than the differential for peer corporations in other euro-area countries. The premiums on credit default swaps on Italian banks rose by 0.3 percentage points, compared with 0.4 points for those on banks from the other countries in the area.

...and government securities

Investors' heightened risk aversion caused the yield differential between ten-year Italian government bonds and the corresponding German Bunds to widen, a phenomenon that could also be observed in the other euro-area countries. The differential increased rapidly in mid-September in connection with the collapse of the US investment bank Lehman Brothers and reached 90 basis points at the end of the month, its highest level since September 1997; it remained slightly below that level in the two subsequent weeks.

The net outflow of savings from investment funds continued

In the second quarter of 2008 net redemptions of investment fund units in Italy amounted to €31.8 billion (compared with €36.8 billion in the preceding quarter), of which €22.3 billion related to Italian funds and €9.4 billion to foreign funds. Among Italian harmonized funds, bond and equity funds recorded the greatest net outflows (€10.7 billion and €3.5 billion respectively). Hedge funds also reported net redemptions for the first time (€1.6 billion). By contrast, closed-end funds continued to benefit from an inflow of resources. The average return on harmonized investment funds was -1.0 per cent, the fourth consecutive quarter of negative returns. At the end of June the assets managed by Italian investment funds amounted to €297.1 billion, 20.7 per cent less than in June 2007. Individually managed portfolios also recorded substantial net redemptions of €40.1 billion; their average rate of return in the quarter is estimated at -0.8 per cent.

3.9 THE PUBLIC FINANCES

The budget objectives have been confirmed

Despite the deterioration in the economic situation, the Forecasting and Planning Report for 2009 published in September broadly confirmed the objectives for 2008 and subsequent years set out in the Economic and Financial Planning Document of June (Table 8). In 2008 general government net borrowing is expected to increase to 2.5 per cent of GDP, and the ratio of debt to GDP should fall slightly, to 103.7 per cent (Table 9). As in the Economic and Financial Planning Document, the objectives take account of the effects of the three-year budget measures launched during the summer (see the box "The budget for the years 2009-2011").

Table 7

Net bond issues (1)

(millions of euros)

	Banks	Other financial corporations	Non-financial corporations	Total
Italy				
2006	60,371	13,136	3,464	**76,971**
2007	63,928	15,166	10,125	**89,219**
2007 – Q1	21,619	2,342	-1,192	**22,769**
Q2	15,371	7,582	7,595	**30,548**
Q3	1,793	-2,444	-754	**-1,405**
Q4	25,145	7,686	4,476	**37,307**
2008 – Q1	39,930	-2,717	-144	**37,069**
Q2	45,023	17,664	-1,476	**61,211**
Euro area				
2006	346,467	236,865	27,043	**610,375**
2007	283,620	326,534	27,383	**637,537**
2007 – Q1	141,146	94,787	794	**236,728**
Q2	100,521	59,038	22,966	**182,524**
Q3	13,995	37,750	-4,421	**47,324**
Q4	27,958	134,959	8,044	**170,961**
2008 – Q1	34,386	12,342	-4,045	**42,682**
Q2	123,784	90,372	13,355	**227,511**

Sources: Bank of Italy and ECB.
(1) Bonds with a maturity at issue of more than one year, at face value, issued by resident companies belonging to the sector indicated. The nationality and sector refer to the issuer and not to the company that controls it. Net issues are equal to the difference between the face value of the securities issued and that of the securities redeemed.

Table 8

Public finance objectives and estimates for 2008

(billions of euros and percentages of GDP)

	General government			*Memo item:* GDP growth rate
	Net borrowing	Primary surplus	Debt	
Objectives				
June 2007 (1)	….	….	….	1.9
% of GDP	*2.2*	*2.7*	*103.2*	
September 2007 (2)	35.4	42.9	….	1.5
% of GDP	*2.2*	*2.7*	*103.5*	
November 2007 (3)	….	….	….	1.5
% of GDP	*2.2*	*2.6*	*103.5*	
Estimates				
March 2008 (4)	38.7	40.6	….	0.6
% of GDP	*2.4*	*2.6*	*103.0*	
June 2008 (1)	39.1	40.7	….	0.5
% of GDP	*2.5*	*2.6*	*103.9*	
September 2008 (5)	39.7	41.4	….	0.1
% of GDP	*2.5*	*2.6*	*103.7*	

(1) Economic and Financial Planning Document. – (2) Forecasting and Planning Report. The primary surplus is derived from Section II of the Report. – (3) Stability Programme. – (4) Combined Report on the Economy and the Public Finances. – (5) Forecasting and Planning Report.

For the purposes of the Notification of public finance data to the European Commission, the estimates of the net borrowing, debt and borrowing requirement of general government for the three years from 2005 to 2007 have been revised following the reclassification of Equitalia S.p.A. from the private to the public sector and the amendment of the statistical treatment of transactions in financial derivatives, on the basis of indications given by Eurostat in March. The revisions relate mainly to 2006 and 2007. The general government borrowing requirement and debt for 2006 have been revised upwards by 0.3 and 0.4 percentage points of GDP respectively. As regards the 2007 figures, debt was increased by 0.1 points and the borrowing requirement reduced by 0.3 points.[1] On the basis of quarterly data released by Istat, which take account of the new classification of Equitalia S.p.A. but not the effects of swap operations, net borrowing has also been revised downwards by about one third of a percentage point with respect to the estimate of 1.9 per cent of GDP published in February. The updated figures on the general government accounts will be published by Istat on 22 October.

Table 9

General government balances (1)
(millions of euros and percentages of GDP)

	2004	2005	2006	2007	2008
Net borrowing	48,312	60,428	49,634	29,179	39,703
% of GDP	*3.5*	*4.2*	*3.4*	*1.9*	*2.5*
Primary surplus	17,197	4,272	18,610	47,547	41,430
% of GDP	*1.2*	*0.3*	*1.3*	*3.1*	*2.6*
Interest payments	65,509	64,700	68,244	76,726	81,133
% of GDP	*4.7*	*4.5*	*4.6*	*5.0*	*5.1*
Debt	1,444,604	1,512,779	1,582,009	1,598,971	–
% of GDP	*103.8*	*105.9*	*106.9*	*104.1*	*103.7*

Sources: Based on Istat data for the general government accounts for 2004-07; for 2008, estimates set out in the Forecasting and Planning Report for 2009.
(1) Rounding may cause discrepancies in totals.

Structural net borrowing will deteriorate by 0.6 per cent of GDP in 2008

According to the estimates contained in the Forecasting and Planning Report, the structural deficit – that is to say net borrowing adjusted for the effects of the economic cycle and one-off measures – is set to deteriorate by 0.6 per cent of GDP with respect to 2007, rising to 2.5 per cent, owing mainly to the deficit-increasing measures in the budget for 2008. The revision associated with the reclassification of Equitalia S.p.A. has no effect on structural net borrowing, since it relates to a temporary component of the general government accounts.

THE BUDGET FOR THE YEARS 2009-2011

The budget for the next three years was set out in a measure adopted during the summer (Decree Law 112 of 25 June 2008, ratified by Law 133 of 6 August 2008) and the Finance Bill for 2009, presented at the end of September.

According to the official estimates, compared with the figures on a current legislation basis, Law 133/2008 reduces net borrowing by 0.6 percentage points of GDP in 2009, 1 point in 2010 and 1.8 points in 2011, thus achieving the objectives for net borrowing contained in the Economic and Financial Planning Document for 2009-2013 and basically confirmed in September's Forecasting and Planning Report.

The law in question also intervenes with regard to the accounts for 2008, increasing both revenue and expenditure but leaving net borrowing for the year unchanged.

The Finance Bill for 2009 does not change the expected public finance balances. Apart from some marginal interventions regarding revenue and expenditure, the bill details the extension for the three-year period of some tax reliefs granted in previous years, as provided for in Law 133/2008.

[1] For further details on the revision of the borrowing requirement and debt of general government, see *Finanza pubblica*, in *Supplementi al Bollettino Statistico*, year XVIII, no. 60, 14 October 2008.

Table

Effects on the general government consolidated accounts of the measures contained in Law 133/2008 (1)

(millions of euros)

	2008	2009	2010	2011
REVENUE				
Increase in revenue	**2,131**	**7,730**	**7,501**	**8,082**
Firms in the energy sector	0	2,395	1,323	1,331
Banks and insurance companies	1,710	1,877	2,623	2,484
Cooperatives	40	45	45	45
Increase in audit and control activity et al.	50	513	793	1,953
Payment on account of stamp duty and insurance tax	133	635	466	0
Stock options, household real estate funds and ban on accumulation	24	157	117	137
Effects of expenditure and other measures (2)	174	2,108	2,134	2,131
Decrease in revenue	**240**	**1,888**	**1,799**	**2,353**
Effects of expenditure cuts	20	785	1,244	1,773
Extension of tax reliefs	0	900	500	500
VAT deductibility of lodging and restaurant services	168	147	-80	-17
Other	52	56	135	97
NET INCREASE IN REVENUE	**1,890**	**5,842**	**5,702**	**5,729**
EXPENDITURE				
Decrease in expenditure	**348**	**12,117**	**18,931**	**32,789**
Rationalization and reorganization of general government	348	11,700	16,494	29,324
Local government	*0*	*3,787*	*5,831*	*9,824*
Public employment	*40*	*1,614*	*2,821*	*4,038*
Central government current expenditure	*202*	*3,881*	*4,173*	*6,887*
Central government capital expenditure	*107*	*2,419*	*3,670*	*8,574*
Health service	0	0	2,000	3,000
Social benefits	0	100	100	100
Other current expenditure	0	317	337	365
Increase in expenditure	**1,902**	**8,066**	**7,497**	**7,593**
Public employment	0	4,000	4,209	4,338
Health service	0	1,018	903	903
Social benefits	170	390	600	620
Transfers to public enterprises	300	0	0	0
Other current expenditure (3)	1,319	1,739	1,518	1,488
Other capital expenditure (3)	113	919	267	244
NET DECREASE IN EXPENDITURE	**-1,554**	**4,051**	**11,435**	**25,196**
DECREASE IN NET BORROWING	**337**	**9,893**	**17,137**	**30,925**

(1) Based on official estimates. – (2) In 2008 includes €170 million of additional tax revenue due by banks to supplement preferential tax regimes introduced in 2004 and removed by European Commission decision C(2008)869 of 11 March 2008. – (3) Compared with the text of Decree Law 112/2008, these items reflect the reclassification from current to capital expenditure of the increase in the employment fund (€0.7 billion in 2009) introduced during its ratification.

Whereas the budget for 2009 is based mainly on increases in revenue, in those for the two following years expenditure cuts play a predominant role. The net expenditure savings expected over the three years rise from just under €4.1 billion in 2009 to about €25.2 billion in 2011, while the net revenue increases remain basically unchanged at about €5.8 billion on average.

During the ratification of the June decree law (analyzed in the parliamentary testimony given by the Governor of the Bank of Italy on 2 July 2008[1]), changes were made to the measures but without altering the balances. The increases in expenditure (€1.4 billion in 2009, €1.3 billion in 2010 and €1.2 billion in 2011) concern, among other things, the extension of the abolition of the patient co-payment for specialist health services to the three years 2009-11 (€0.8 billion as of 2009), the creation of funds for public order needs and the financing of supplementary wage increases for general government (€0.3 billion in 2009 and €0.1 billion in 2010 and 2011). These increases are more than offset by additional reductions in expenditure (€1.8 billion in 2009, €1.7 billion in 2010 and €1.6 billion in 2011), achieved almost entirely through measures serving to rationalize and reorganize general government.

On the revenue side the changes made during the ratification of the decree law were of limited scope. As regards firms in the energy sector, the ratification law suppressed the articles providing for the extension of the rules on the payments on account of extraction royalties and those that provided for their increase. At the same time it slightly reduced the sectors to which the 5.5 percentage point Ires surtax applied and introduced specific rules for firms subject to consolidation of their accounts for tax purposes. Lastly, with effect from 2008, it increased the tax rate on life insurance mathematical provisions (€0.2 billion per year).

[1] Available on the Internet at www.bancaditalia.it/media/notizie/audizione_2009_2013

Taking account of the revisions to the 2007 budget balance and the forecast for this year contained in the Forecasting and Planning Report, the primary surplus is expected to fall from about 3.4 to 2.6 per cent of GDP in 2008. Primary current expenditure is likely to rise by half of a percentage point, exceeding 40 per cent of GDP for the first time; interest payments remain basically unchanged at 5.1 per cent of GDP. The ratio of tax and social security contributions to GDP is expected to fall by 0.5 points to 42.8 per cent.

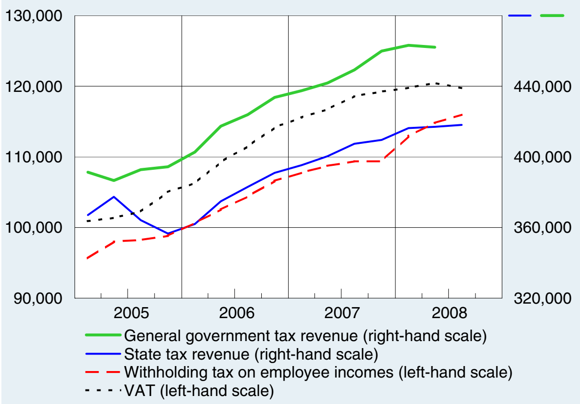
The data currently available on developments in the public accounts in the course of the year broadly confirm the assessments contained in the Forecasting and Planning Report.

Revenue increased, partly owing to exceptional factors

In the first nine months of the year revenue in the State budget increased by 3.2 per cent, buoyed by a number of exceptional factors, such as the abolition of the advance payment due at the end of the year from tax collection agents (Figure 30 and Table 10); excluding the effects of this measure and lottery receipts, revenue increased by about 2 per cent. The growth reflects the substantial rise in withholding tax on employee compensation (8 per cent), which benefited from the effects of a number of contract renewals and the payment of related arrears, the impact of which was magnified by the progressivity of personal income tax. The decline in receipts of corporate income tax worked in the opposite direction. Receipts of VAT remained broadly unchanged.

Figure 30

Tax revenue: rolling four-quarter totals
(millions of euros)



Sources: Istat for general government tax revenue; General Government Report and state sector budget for the other variables.

Table 10

State budget tax revenue on a cash basis (1)
(millions of euros and percentages)

	January-September			
			Percentage changes on	
	2007	2008	2006	2007
Direct taxes	**148,590**	**155,626**	**6.9**	**4.7**
Personal income tax	106,517	114,106	5.9	7.1
of which: withholding tax on employee incomes	*82,793*	*89,386*	*3.4*	*8.0*
balance	*5,852*	*5,928*	*33.5*	*1.3*
payment on account	*7,092*	*7,503*	*12.9*	*5.8*
Corporate income tax	27,469	26,074	35.0	-5.1
of which: balance	*11,625*	*10,341*	*47.1*	*-11.0*
payment on account	*15,546*	*15,204*	*27.3*	*-2.2*
Withholding taxes on interest income and capital gains	10,698	10,698	10.8	0.0
interest on bank deposits	*3,102*	*3,219*	*77.4*	*3.8*
interest on bonds	*4,875*	*5,543*	*0.4*	*13.7*
dividends	*394*	*569*	*-28.5*	*44.4*
capital gains	*986*	*610*	*12.2*	*-38.1*
managed assets	*1,341*	*757*	*-17.4*	*-43.5*
One-off taxes	1,112	1,868	-80.1	68.0
Taxes on insurance companies' mathematical reserves	1,105	1,090	5.7	-1.4
Other	1,689	1,790	-2.1	6.0
Indirect taxes	**125,025**	**126,640**	**5.8**	**1.3**
VAT	81,094	81,600	5.8	0.6
Other business taxes	11,505	14,452	20.9	25.6
Excise duties on mineral oils	14,865	15,143	-1.1	1.9
Other excise duties and sales taxes	5,141	3,991	-3.2	-22.4
Monopolies	7,363	7,498	3.7	1.8
Lotteries	5,057	3,956	11.6	-21.8
TOTAL TAX REVENUE	**273,615**	**282,266**	**6.4**	**3.2**

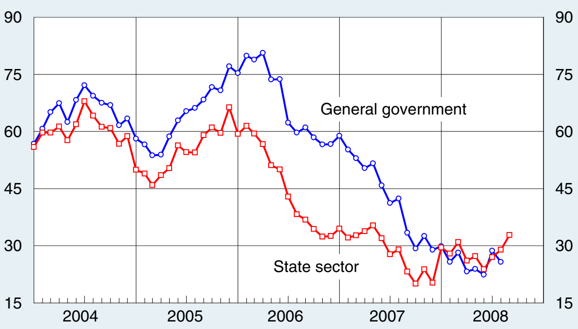
Source: Based on state budget data.
(1) For 2008, provisional data.

In the first seven months the borrowing requirement was lower than in the same period of 2007 owing to temporary factors

In the first seven months of the year the general government borrowing requirement, net of privatization receipts, amounted to €19.8 billion, €4.1 billion less than in the same period of 2007 (Figure 31 and Table 11). A number of exceptional factors contributed to the reduction, such as the abolition of the advance payment by tax collection agents mentioned above, the transfer to INPS of accumulated severance pay entitlements not assigned to private pension funds from January onwards, and the postponement of the due date for certain payments from taxpayers subject to sector studies. The effect

Figure 31

Rolling twelve-month borrowing requirement (1)
(billions of euros)



Source: Ministry of the Economy and Finance for the state sector borrowing requirement.
(1) Net of privatization receipts.

of most of these factors should cancel out in the second half of the year. On the basis of provisional data, in August the borrowing requirement was €3 billion higher than in the same month of 2007.

On the basis of estimates published by Istat, in the first half of 2008 net borrowing equalled 2.6 per cent of GDP, compared with 1.5 per cent a year earlier. The primary balance fell by one percentage point to 2.4 per cent, mirroring the increase in primary current expenditure, especially compensation of employees and social benefits in cash (Table 12). Revenue remained virtually unchanged at 42.7 per cent of GDP: the fall in indirect taxes was offset by increases in social security contributions and other current and capital revenue.

General government debt rose by €55.8 billion in the first seven months of the year. The increase reflects the overall borrowing requirement (€19.8 billion), the seasonal increase in assets held by the Treasury with the Bank of Italy (€32.1 billion), and the issue of bonds at below par (€4.1 billion). As regards the distribution of the debt among sub-sectors, central government debt increased by €57.4 billion and that of local authorities and social security institutions diminished by €1.4 billion and €0.2 billion respectively.

The Forecasting and Planning Report confirms the achievement of a balanced budget in 2011

The Forecasting and Planning Report essentially confirms the objectives for the period from 2009 to 2011 set out in the Economic and Financial Planning Document of June; it presents a unified forecasting framework, in that the planning estimates match the trend estimates, which already include the effects of the three-year budget measures adopted during the summer. Net borrowing will decline steadily until a broadly balanced budget is achieved in 2011, in line with the commitments made at European level: it should fall from 2.5 per cent of expected GDP in 2008 to 2.1 per cent in 2009, 1.2 per cent in 2010 and 0.3 per cent in 2011. The primary surplus is expected to rise from the figure of 2.6 per cent of GDP estimated for this year to 4.6 per cent in 2011, to a large extent reflecting the reduction in the ratio of expenditure to GDP. The public debt will gradually decrease, settling at less than GDP in 2011. Structural net borrowing is expected to rise this year, but the positive trend should then resume: according to the official estimates, it will shift from a deficit of 2.5 per cent of GDP in 2008 to a surplus of 0.2 per cent in 2011.

Table 11

General government borrowing requirement and debt

(millions of euros and percentages of GDP)

	2005	2006	2007	2008
	General government borrowing requirement net of privatization receipts			
Jan. – July	55,996	40,351	23,892	19,768
Year	75,284	58,862	29,855	–
% of GDP	*5.3*	*4.0*	*1.9*	–
	Privatization receipts			
Jan. – July	4,025	38	3,500	0
Year	4,618	38	3,500	–
	Memorandum item: settlements of past debts			
Jan. – July	363	89	135	50
Year	1,864	243	2,420	–
	Total general government borrowing requirement			
Jan. – July	51,971	40,313	20,392	19,768
Year	70,666	58,824	26,355	–
% of GDP	*4.9*	*4.0*	*1.7*	–
	Change in Treasury asset balances with the Bank of Italy			
Jan. – July	41,765	38,251	18,651	32,089
Year	-1,197	8,230	-13,142	–
	Issue discounts			
Jan. – July	-1,818	1,845	4,116	4,056
Year	-2,444	2,978	4,083	–
	Change in euro equivalent of foreign currency liabilities			
Jan. – July	1,147	-577	-137	-137
Year	1,150	-801	-333	–
	Change in debt			
Jan. – July	93,065	79,832	43,023	55,776
Year	68,175	69,230	16,963	–
% of GDP	*4.8*	*4.7*	*1.1*	–
	General government debt			
End July	1,537,668	1,592,611	1,625,031	1,654,747
End year	1,512,779	1,582,009	1,598,971	–
% of GDP	*105.9*	*106.9*	*104.1*	*103.7* (1)

(1) Estimate contained in the Forecasting and Planning Report for 2009.

The draft Finance Law for 2009 was presented to Parliament at the same time as the Forecasting and Planning Report; the three-year measures and the Finance Law for 2009 are expected to bring about a reduction in net borrowing by comparison with the baseline values estimated in June, namely 0.6 per cent of GDP in 2009, 1 per cent in 2010 and 1.8 per cent in 2011 (see the box "The budget for the years 2009-2011").

Around three fifths of the adjustment of net borrowing in 2009 is based on increases in revenue, while in subsequent years reliance is placed on reductions in expenditure. The revenue measures relate in particular to banks, insurance companies and firms in the energy sector; measures to curb tax evasion and avoidance are also expected to generate higher receipts. The provisions on the expenditure side are primarily financial constraints, the implementation of which will be dealt with in subsequent measures.

The objectives for 2009 could be more difficult to achieve if economic growth falls short of the rate of 0.5 per cent underlying the estimates contained in the Forecasting and Planning Report.

The estimates set out in the Forecasting and Planning Report show a large reduction in the ratio of expenditure to GDP between 2008 and 2011 (1.9 per cent of GDP). Capital expenditure should fall by almost one point to its lowest level in the last three decades in relation to GDP (excluding from the figure for 2000 the proceeds of sales of UMTS licences, which bear a negative sign in that aggregate); primary current expenditure should decrease by one point, owing mainly to a large contraction in compensation of employees and intermediate consumption. The ratio of tax and social security contributions to GDP should remain broadly unchanged: it is expected to decline by 0.5 per cent of GDP in 2008 (to 42.8 per cent), before increasing in the following two years and settling at 43.1 per cent in 2011.

Table 12

General government expenditure and revenue
(millions of euros)

	H1			
	2007	2008	Percentage change on first half of previous year	
			2007	2008
EXPENDITURE				
Compensation of employees	73,798	79,267	-3.0	7.4
Intermediate consumption	38,079	39,728	2.0	4.3
Social benefits in cash	123,301	129,118	4.5	4.7
Other current expenditure	40,899	43,601	0.8	6.6
Current expenditure, net of interest payments	**276,077**	**291,714**	**1.5**	**5.7**
% of GDP	*36.1*	*37.0*		
Interest payments	36,882	39,272	11.0	6.5
Current expenditure	**312,959**	**330,986**	**2.6**	**5.8**
% of GDP	*41.0*	*42.0*		
Gross fixed investment	15,750	15,381	-1.4	-2.3
Other capital expenditure	8,372	9,724	-13.5	16.1
Capital expenditure	**24,122**	**25,105**	**-6.0**	**4.1**
Total expenditure, net of interest payments	**300,199**	**316,819**	**0.9**	**5.5**
% of GDP	*39.3*	*40.2*		
TOTAL EXPENDITURE	**337,081**	**356,091**	**1.9**	**5.6**
% of GDP	*44.1*	*45.2*		
REVENUE				
Direct taxes	98,163	101,720	4.9	3.6
Indirect taxes	112,254	110,695	3.2	-1.4
Social security contributions	91,045	96,843	7.4	6.4
Other current revenue	22,274	23,504	0.5	5.5
Current revenue	**323,736**	**332,762**	**4.6**	**2.8**
% of GDP	*42.4*	*42.3*		
Capital taxes	126	243	5.9	92.9
Other capital revenue	1,972	2,898	3.0	47.0
Capital revenue	**2,098**	**3,141**	**3.1**	**49.7**
% of GDP	*0.3*	*0.4*		
TOTAL REVENUE	**325,834**	**335,903**	**4.6**	**3.1**
% of GDP	*42.6*	*42.7*		
NET BORROWING	**-11,247**	**-20,188**		
% of GDP	*-1.5*	*-2.6*		
Primary surplus	**25,635**	**19,084**		
% of GDP	*3.4*	*2.4*		
Memorandum item:				
GDP	764,142	787,456	3.9	3.1

Source: Istat, General government quarterly accounts.

SELECTED STATISTICS

Additional tables are contained in the Statistical Appendix of the *Economic Bulletin* available on the Internet at www.bancaditalia.it/pubblicazioni

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Table A1

Sources and uses of income: United States (1)

(seasonally adjusted data; percentage changes on the previous period and contribution to growth, on an annual basis)

	GDP	Resident households' expenditure		General government expenditure		Investment		Domestic demand (2)		Exports	Imports	Net exports	Stocks
	Change	Change	Contri-bution	Change	Contri-bution	Change	Contri-bution	Change	Contri-bution	Change	Change	Contri-bution	Contri-bution
2004	3.6	3.6	2.6	1.4	0.3	7.3	1.1	4.1	4.3	9.7	11.3	-0.7	0.4
2005	2.9	3.0	2.1	0.4	0.1	6.8	1.1	3.0	3.1	7.0	5.9	-0.2	-0.1
2006	2.8	3.0	2.1	1.7	0.3	1.9	0.3	2.6	2.8	9.1	6.0	..	..
2007	2.0	2.8	2.0	2.1	0.4	-3.1	-0.5	1.4	1.4	8.4	2.2	0.6	-0.4
2006 – Q1	4.8	4.3	2.9	3.9	0.7	8.3	1.4	4.5	4.7	16.7	10.3	0.1	-0.2
Q2	2.7	2.8	1.9	1.2	0.2	-2.5	-0.4	2.0	2.1	5.5	0.1	0.6	0.4
Q3	0.8	2.2	1.5	1.7	0.3	-4.8	-0.8	0.9	0.9	3.5	3.1	-0.1	-0.1
Q4	1.5	3.7	2.6	1.6	0.3	-7.6	-1.3	0.2	0.2	15.6	2.0	1.3	-1.4
2007 – Q1	0.1	3.9	2.7	0.9	0.2	-3.4	-0.6	1.2	1.3	0.6	7.7	-1.2	-1.1
Q2	4.8	2.0	1.4	3.9	0.8	3.0	0.5	2.9	3.1	8.8	-3.7	1.7	0.5
Q3	4.8	2.0	1.4	3.8	0.8	-0.9	-0.2	2.6	2.8	23.0	3.0	2.0	0.7
Q4	-0.2	1.0	0.7	0.8	0.2	-6.2	-1.0	-1.0	-1.1	4.4	-2.3	0.9	-1.0
2008 – Q1	0.9	0.9	0.6	1.9	0.4	-5.6	-0.9	0.1	0.1	5.1	-0.8	0.8	..
Q2	2.8	1.2	0.9	3.9	0.8	-1.7	-0.3	-0.1	-0.1	12.3	-7.3	2.9	-1.5

Source: National statistics.
(1) Chain-linked volumes. Public sector investment is included in government expenditure. – (2) Includes change in stocks.

Table A2

Sources and uses of income: Japan (1)

(seasonally adjusted data; percentage changes on the previous period and contribution to growth, on an annual basis)

	GDP	Resident households' expenditure		General government expenditure		Investment		Domestic demand (2)		Exports	Imports	Net exports	Stocks
	Change	Change	Contri-bution	Change	Contri-bution	Change	Contri-bution	Change	Contri-bution	Change	Change	Contri-bution	Contri-bution
2004	2.7	1.6	0.9	1.9	0.3	1.4	0.3	1.9	1.9	13.9	8.1	0.8	0.3
2005	1.9	1.3	0.7	1.6	0.3	3.1	0.7	1.7	1.6	7.0	5.8	0.3	-0.1
2006	2.4	2.0	1.1	-0.4	-0.1	1.3	0.3	1.6	1.5	9.7	4.2	0.9	0.2
2007	2.1	1.5	0.8	0.7	0.1	-0.6	-0.1	1.0	0.9	8.6	1.7	1.1	0.1
2006 – Q1	1.8	1.7	1.0	-1.5	-0.3	0.1	..	1.5	1.5	7.6	6.1	0.4	0.7
Q2	3.6	3.4	1.9	2.1	0.4	5.0	1.1	3.4	3.3	6.2	5.7	0.3	-0.1
Q3	0.8	-2.3	-1.3	1.3	0.2	-1.6	-0.4	-0.6	-0.6	8.8	-1.1	1.4	0.8
Q4	3.9	3.8	2.1	-1.3	-0.2	7.3	1.6	3.5	3.3	3.7	0.3	0.5	-0.2
2007 – Q1	3.8	2.3	1.3	1.1	0.2	1.7	0.4	2.3	2.2	11.5	2.0	1.4	0.3
Q2	-1.4	1.1	0.6	0.8	0.1	-9.3	-2.2	-2.0	-2.0	8.1	4.9	0.7	-0.5
Q3	1.0	..	..	0.2	..	-4.6	-1.0	-1.0	-1.0	10.9	-1.2	1.8	0.1
Q4	2.4	1.4	0.8	3.5	0.6	-2.6	-0.6	1.0	1.0	11.0	3.3	1.3	0.2
2008 – Q1	2.8	2.8	1.5	-1.9	-0.3	2.6	0.6	1.0	1.0	14.3	4.7	1.7	-0.8
Q2	-3.0	-1.9	-1.1	-0.2	..	-6.6	-1.5	-2.8	-2.7	-9.7	-9.9	-0.5	-0.1

Source: National statistics.
(1) Chain-linked volumes. Statistical discrepancies may cause differences between the sum of contributions and GDP growth. – (2) Includes change in stocks.

Table A3

Sources and uses of income: euro area (1)

(percentage changes on the previous period)

	Sources			Uses					
	GDP	Imports	Total	Gross fixed capital formation			Resident households' expenditure (2)	General government expenditure	Exports
				Construction	Machinery, equipment, sundry products & vehicles	Total			
	Chain-linked volumes								
2002	0.9	0.4	0.8	-0.6	-2.3	-1.4	0.9	2.4	1.8
2003	0.8	3.1	1.4	1.8	0.7	1.3	1.2	1.8	1.2
2004	2.1	7.0	3.4	1.1	3.5	2.2	1.6	1.6	7.3
2005	1.7	5.6	2.8	2.1	4.3	3.1	1.7	1.5	4.9
2006	2.9	8.1	4.4	4.4	6.7	5.5	1.9	1.9	8.2
2007	2.6	5.4	3.5	3.4	5.1	4.2	1.6	2.3	6.0
2006 – Q2	1.1	1.6	1.2	3.1	3.1	3.1	0.5	0.3	2.0
Q3	0.5	1.2	0.7	1.0	0.6	0.8	0.4	0.3	0.6
Q4	0.8	2.0	1.2	1.5	1.6	1.5	0.7	0.7	3.5
2007 – Q1	0.7	1.2	0.9	1.2	0.6	0.9	..	1.0	0.5
Q2	0.5	0.8	0.6	-1.0	1.5	0.2	0.7	0.2	1.3
Q3	0.6	2.2	1.1	0.7	1.2	0.9	0.4	0.5	1.8
Q4	0.4	-0.4	0.1	0.7	1.5	1.1	0.2	0.3	0.3
2008 – Q1	0.7	1.8	1.0	2.4	0.5	1.4	-0.1	0.3	1.8
Q2	-0.2	-0.5	-0.3	-1.6	-0.3	-1.0	-0.2	0.5	-0.2
	Implicit prices								
2002	2.6	-2.1	....	....	....	1.4	1.9	3.0	-0.4
2003	2.2	-1.8	....	....	....	1.1	2.1	2.4	-1.3
2004	1.9	1.5	....	....	....	2.5	2.0	2.0	1.0
2005	2.0	3.4	....	....	....	2.6	2.1	2.4	2.3
2006	1.9	3.8	....	....	....	2.9	2.2	2.0	2.7
2007	2.2	1.2	....	....	....	2.7	2.1	1.6	1.5
2006 – Q2	0.6	0.6	....	....	....	0.7	0.6	1.2	0.6
Q3	0.4	0.3	....	....	....	0.6	0.5	-0.2	0.7
Q4	0.4	-0.4	....	....	....	0.5	0.2	-0.1	0.1
2007 – Q1	0.8	0.2	....	....	....	1.0	0.6	0.7	0.3
Q2	0.6	0.7	....	....	....	0.7	0.6	0.4	0.6
Q3	0.5	0.5	....	....	....	0.2	0.7	0.5	0.3
Q4	0.4	1.3	....	....	....	0.6	0.9	0.7	0.3
2008 – Q1	0.7	1.4	....	....	....	0.7	0.8	0.4	1.0
Q2	0.7	1.4	....	....	....	0.7	0.9	1.4	0.7

Source: Eurostat.
(1) Quarterly data are seasonally and calendar adjusted. – (2) Includes expenditure of non-profit institutions serving households.

Table A4

Sources and uses of income: Italy (1)
(percentage changes on the previous period)

	Sources			Uses					
	GDP	Imports	Total	Gross fixed capital formation			Resident households' expenditure	General government expenditure (2)	Exports
				Construction	Machinery, equipment, sundry products & vehicles	Total			
	Chain-linked volumes								
2002	0.5	0.2	0.4	5.9	1.9	3.7	0.2	2.5	-2.9
2003	..	1.2	0.2	2.4	-4.6	-1.2	1.0	1.9	-2.0
2004	1.5	4.2	2.0	2.2	2.3	2.3	0.7	2.3	4.9
2005	0.6	2.2	0.9	0.5	0.9	0.7	0.9	1.9	1.0
2006	1.8	5.9	2.7	1.5	3.5	2.5	1.1	0.9	6.2
2007	1.5	4.4	2.1	2.2	0.2	1.2	1.4	1.3	5.0
2006 – Q2	0.5	0.4	0.5	1.2	1.5	1.4	0.1	0.4	1.3
Q3	0.3	1.5	0.5	-0.6	-1.3	-1.0	0.6	0.3	-1.3
Q4	1.0	2.7	1.3	2.9	0.9	1.9	..	0.6	5.0
2007 – Q1	0.3	1.2	0.5	0.4	-1.0	-0.3	1.0	0.4	1.4
Q2	0.1	-0.5	..	-1.3	0.6	-0.4	0.2	-0.1	-1.4
Q3	0.1	1.2	0.4	0.8	-1.1	-0.1	0.2	0.4	2.2
Q4	-0.4	-1.1	-0.6	0.3	0.8	0.6	-0.4	0.1	-1.5
2008 – Q1	0.5	-1.0	0.2	0.3	-0.3	..	..	0.4	1.3
Q2	-0.3	0.3	-0.1	-0.9	0.5	-0.2	-0.3	0.3	-0.7
	Implicit prices								
2002	3.3	-0.3	2.5	3.7	2.2	2.9	2.9	2.6	1.4
2003	3.1	-1.3	2.2	2.8	0.3	1.6	2.8	3.7	0.4
2004	2.6	2.7	2.6	4.0	1.4	2.7	2.6	2.7	2.6
2005	2.1	6.2	2.9	4.6	1.2	2.9	2.3	3.3	4.0
2006	1.7	7.6	3.0	3.2	2.0	2.6	2.7	2.0	4.5
2007	2.3	2.3	2.3	3.5	1.6	2.6	2.2	0.4	3.6
2006 – Q2	1.3	1.5	1.3	1.0	0.7	0.9	0.9	4.9	0.9
Q3	-0.3	1.2	..	0.9	0.3	0.6	0.7	-2.9	1.3
Q4	..	-1.0	-0.2	0.8	..	0.5	0.1	-2.3	0.2
2007 – Q1	1.3	0.1	1.0	1.2	0.8	1.0	0.4	1.2	1.2
Q2	0.7	1.5	0.9	0.6	0.3	0.5	0.6	0.9	1.2
Q3	0.5	1.4	0.7	0.7	0.4	0.6	0.9	0.2	0.5
Q4	0.3	0.4	0.3	0.7	..	0.4	0.8	1.9	0.9
2008 – Q1	0.7	2.6	1.1	0.8	1.5	1.1	0.8	-1.6	1.7
Q2	2.2	1.1	1.9	1.1	0.4	0.7	1.5	6.1	1.0

Source: Istat.
(1) Quarterly data are seasonally and calendar adjusted. – (2) Includes consumption of non-profit institutions serving households.

Table A5

Unit labour costs, per capita compensation and productivity: euro area (1)

(percentage changes on the year-earlier period)

	Per capita compensation	Productivity	of which: Value added (2)	of which: Employees	Unit labour costs
			Total industry excluding construction		
2004	2.9	4.2	2.8	-1.4	-1.2
2005	1.8	2.8	1.7	-1.1	-1.0
2006	3.6	3.9	3.5	-0.4	-0.4
2007	2.8	3.2	3.5	0.3	-0.4
2006 – Q1	3.7	4.6	3.7	-0.8	-0.9
Q2	3.6	4.0	3.6	-0.4	-0.4
Q3	3.9	4.0	3.8	-0.2	-0.1
Q4	3.3	4.3	4.2	-0.1	-1.0
2007 – Q1	2.4	3.3	3.6	0.3	-0.9
Q2	3.2	3.0	3.3	0.3	0.1
Q3	2.4	3.4	3.6	0.2	-1.0
Q4	3.2	2.9	3.2	0.3	0.2
2008 – Q1	3.5	2.2	2.6	0.4	1.3
Q2	3.2	0.8	1.0	0.3	2.4
			Services		
2004	1.9	0.4	2.0	1.5	1.5
2005	2.1	0.5	1.9	1.4	1.6
2006	1.8	0.5	2.7	2.2	1.3
2007	2.5	0.6	2.7	2.1	1.8
2006 – Q1	1.6	0.3	2.2	2.0	1.4
Q2	2.1	0.4	2.9	2.4	1.6
Q3	1.9	0.7	3.0	2.3	1.2
Q4	1.5	0.9	3.2	2.2	0.5
2007 – Q1	2.5	1.2	3.1	1.9	1.4
Q2	2.1	0.9	2.8	1.9	1.3
Q3	2.3	0.4	2.7	2.2	1.9
Q4	2.9	0.2	2.4	2.2	2.7
2008 – Q1	2.9	0.1	2.1	2.0	2.9
Q2	3.4	-0.1	1.7	1.8	3.5
			Total economy		
2004	2.1	1.5	2.3	0.8	0.6
2005	1.9	0.7	1.7	1.0	1.2
2006	2.2	1.2	2.8	1.6	1.0
2007	2.5	1.1	2.9	1.8	1.4
2006 – Q1	2.1	1.1	2.5	1.4	1.0
Q2	2.4	1.2	2.9	1.7	1.2
Q3	2.4	1.4	3.0	1.7	1.0
Q4	2.0	1.6	3.3	1.7	0.4
2007 – Q1	2.5	1.6	3.4	1.8	0.9
Q2	2.3	1.2	2.9	1.7	1.2
Q3	2.3	0.9	2.8	1.9	1.4
Q4	2.9	0.7	2.5	1.7	2.2
2008 – Q1	3.1	0.7	2.2	1.5	2.4
Q2	3.5	0.4	1.5	1.2	3.1

Source: Based on Eurostat.
(1) Euro-15. – (2) Value added at base prices, volumes at chain-linked prices – reference year 2000.

Table A6

Unit labour costs, per capita compensation and productivity: Italy

(percentage changes on the year-earlier period) (1)

	Per capita compensation (2)	Wages per employee (2)	Productivity	of which: Value added (3)	of which: Employees (2)	Unit labour costs
			Total industry excluding construction			
2003	4.0	3.9	1.9	0.9	-1.0	2.0
2004	2.7	3.1	0.7	-0.4	-1.0	2.0
2005	2.6	3.4	0.1	1.2	1.0	2.5
2006	2.4	2.8	-0.1	0.8	0.9	2.5
2007	3.7	4.6	2.2	2.4	0.2	1.5
2006 – Q1	2.4	3.1	-1.0	0.6	1.7	3.5
Q2	2.3	3.1	-0.9	0.3	1.2	3.3
Q3	2.0	2.8	1.5	2.5	1.0	0.4
Q4	1.0	1.2	-0.7	1.1	1.8	1.7
2007 – Q1	2.4	2.8	0.5	1.8	1.3	1.8
Q2	2.7	3.2	0.4	1.0	0.6	2.3
Q3	3.6	3.9	-2.5	-2.4	0.1	6.3
Q4	4.6	4.6	0.4	-0.8	-1.2	4.2
2008 – Q1	4.4	4.2	-0.8	-2.2	-1.4	5.2
Q2	2.2	2.6	0.5	1.8	1.3	1.7
			Services			
2003	3.1	3.4	0.9	1.6	0.7	2.3
2004	3.6	3.8	0.7	1.1	0.4	2.9
2005	2.5	2.9	0.1	2.1	2.1	2.5
2006	1.6	1.6	0.7	1.8	1.1	0.9
2007	3.4	3.7	0.1	1.5	1.4	3.4
2006 – Q1	5.6	6.0	-0.5	2.0	2.6	6.2
Q2	3.6	3.9	..	2.3	2.3	3.5
Q3	-2.2	-1.7	0.7	2.6	1.9	-2.9
Q4	1.6	1.9	1.6	2.4	0.7	-0.1
2007 – Q1	-0.3	-0.1	1.5	1.9	0.4	-1.7
Q2	1.1	0.9	..	1.9	1.9	1.0
Q3	3.9	3.9	-0.5	1.2	1.7	4.4
Q4	3.7	4.3	-1.0	0.9	1.9	4.8
2008 – Q1	5.4	5.5	-1.6	0.7	2.3	7.0
Q2	2.2	2.6	0.5	1.8	1.3	1.7
			Total economy			
2003	3.3	3.4	1.4	1.7	0.4	1.9
2004	3.2	3.4	0.6	0.7	0.2	2.6
2005	2.5	3.0	0.1	1.8	1.7	2.4
2006	1.9	2.1	0.6	1.6	1.0	1.4
2007	3.3	3.8	0.6	1.8	1.1	2.7
2006 – Q1	4.4	5.0	-0.4	1.6	2.1	4.9
Q2	3.1	3.6	-0.3	1.6	1.9	3.5
Q3	-0.9	-0.3	0.8	2.5	1.7	-1.7
Q4	1.6	1.9	1.3	2.2	0.8	0.3
2007 – Q1	0.6	0.8	1.2	1.8	0.6	-0.6
Q2	1.6	1.6	0.2	1.7	1.5	1.4
Q3	3.9	3.9	-0.8	0.3	1.1	4.8
Q4	3.9	4.3	-0.6	0.4	1.1	4.6
2008 – Q1	5.1	5.2	-1.0	0.1	1.1	6.1
Q2	2.2	2.6	0.5	1.8	1.3	1.7

Sources: Based on Istat and Eurostat data.
(1) There may be discrepancies between the sum of quarterly results and the annual accounts. – (2) Standard labour units. – (3) Value added at base prices, volumes at chain-linked prices – reference year 2000.

Harmonized index of consumer prices: main euro-area countries

(percentage changes on the year-earlier period)

	ITALY		GERMANY		FRANCE		SPAIN		EURO (1)	
	Total	Total excl. unproc-essed food and energy products	Total	Total excl. unproc-essed food and energy products	Total	Total excl. unproc-essed food and energy products	Total	Total excl. unproc-essed food and energy products	Total	Total excl. unproc-essed food and energy products
2003	2.8	2.7	1.0	0.9	2.2	2.2	3.1	3.0	2.1	2.0
2004	2.3	2.3	1.8	1.6	2.3	2.4	3.1	2.8	2.1	2.1
2005	2.2	2.0	1.9	1.0	1.9	1.2	3.4	2.7	2.2	1.5
2006	2.2	1.8	1.8	0.8	1.9	1.3	3.6	3.0	2.2	1.5
2007	2.0	1.9	2.3	2.1	1.6	1.5	2.8	2.7	2.1	2.0
2006 – Jan.	2.2	1.6	2.1	0.6	2.3	1.3	4.2	3.0	2.4	1.3
Feb.	2.2	1.6	2.1	0.7	2.0	1.1	4.1	3.0	2.3	1.3
Mar.	2.2	1.8	1.9	0.8	1.7	1.2	3.9	3.1	2.2	1.4
Apr.	2.3	1.9	2.3	1.0	2.0	1.3	3.9	3.2	2.5	1.6
May	2.3	1.8	2.1	0.6	2.4	1.3	4.1	3.1	2.5	1.5
June	2.4	1.8	2.0	0.8	2.2	1.4	4.0	3.1	2.5	1.6
July	2.3	1.7	2.1	1.0	2.2	1.5	4.0	3.2	2.4	1.6
Aug.	2.3	1.6	1.8	0.8	2.1	1.4	3.8	3.1	2.3	1.5
Sept.	2.4	2.0	1.0	0.8	1.5	1.2	2.9	3.0	1.7	1.5
Oct.	1.9	2.0	1.1	1.0	1.2	1.3	2.6	2.8	1.6	1.6
Nov.	2.0	1.8	1.5	1.1	1.6	1.4	2.7	2.7	1.9	1.6
Dec.	2.1	1.9	1.4	1.0	1.7	1.5	2.7	2.5	1.9	1.6
2007 – Jan.	1.9	1.6	1.8	1.7	1.4	1.4	2.4	2.8	1.8	1.8
Feb.	2.1	2.1	1.9	1.8	1.2	1.4	2.5	2.8	1.8	1.9
Mar.	2.1	2.0	2.0	1.7	1.2	1.3	2.5	2.5	1.9	1.9
Apr.	1.8	1.8	2.0	1.9	1.3	1.4	2.5	2.5	1.9	1.9
May	1.9	1.9	2.0	2.1	1.2	1.4	2.4	2.5	1.9	1.9
June	1.9	1.9	2.0	2.1	1.3	1.4	2.5	2.5	1.9	1.9
July	1.7	1.8	2.0	2.1	1.2	1.4	2.3	2.4	1.8	1.9
Aug.	1.7	1.9	2.0	2.2	1.3	1.6	2.2	2.5	1.7	2.0
Sept.	1.7	1.8	2.7	2.3	1.6	1.6	2.7	2.6	2.1	2.0
Oct.	2.3	2.1	2.7	2.2	2.1	1.7	3.6	3.1	2.6	2.1
Nov.	2.6	2.2	3.3	2.4	2.6	1.8	4.1	3.3	3.1	2.3
Dec.	2.8	2.3	3.1	2.4	2.8	1.9	4.3	3.4	3.1	2.3
2008 – Jan.	3.1	2.6	2.9	2.1	3.2	2.2	4.4	3.2	3.2	2.3
Feb.	3.1	2.5	3.0	2.2	3.2	2.3	4.4	3.3	3.3	2.4
Mar.	3.6	2.9	3.3	2.4	3.5	2.5	4.6	3.5	3.6	2.7
Apr.	3.6	2.7	2.6	1.8	3.4	2.5	4.2	3.2	3.3	2.4
May	3.7	2.8	3.1	1.8	3.7	2.4	4.7	3.3	3.7	2.5
June	4.0	3.0	3.4	1.8	4.0	2.5	5.1	3.4	4.0	2.5
July	4.0	2.7	3.5	1.8	4.0	2.4	5.3	3.5	4.0	2.5
Aug.	4.2	3.2	3.3	1.9	3.5	2.3	4.9	3.5	3.8	2.6

Source: Eurostat.
(1) Weighted average of the indices of the countries belonging to the euro area at the date indicated.

Table A8

Balance of payments (current account and capital account): Italy

(millions of euros)

	Current account						Capital account			
	Total	Goods	Services	Income	Current transfers		Total	Intangible assets	Capital transfers	
					Private	Public			Private	Public
2004	-13,077	8,854	1,179	-14,817	-1,477	-6,816	1,700	-38	-26	1,764
2005	-23,628	536	-541	-13,624	-1,676	-8,323	998	69	-66	995
2006	-38,506	-10,203	-1,272	-13,573	-5,473	-7,985	1,890	-100	-60	2,050
2007	-37,366	2,941	-6,978	-19,675	-6,762	-6,891	2,674	-69	71	2,671
2006 – Q3	-6,222	-1,464	217	-967	-1,515	-2,494	292	-2	1	293
Q4	-9,034	143	-1,732	-3,695	-1,549	-2,200	1,136	26	14	1,096
2007 – Q1	-12,471	-2,133	-3,345	-4,077	-1,278	-1,638	1,132	-1	29	1,104
Q2	-10,186	1,044	-1,091	-8,184	-1,742	-213	-32	-27	-15	10
Q3	-4,515	2,807	-871	-2,724	-1,620	-2,106	572	25	-30	577
Q4	-10,194	1,223	-1,671	-4,689	-2,123	-2,934	1,002	-65	87	980
2008 – Q1	-15,683	-1,482	-3,100	-6,135	-2,029	-2,936	1,224	23	-21	1,223
Q2	(-14,529)	(951)	(-662)	(-12,179)	….	….	(173)	….	….	….
2008 – July	52	1,264	658	-753	-554	-564	67	6	25	37
Aug.	-1,117	-862	-680	1,387	-382	-581	37	-1	2	37
Sept.	-5,156	-1,866	239	-1,601	-579	-1,349	187	-7	-26	219
Oct.	-3,238	168	-23	-2,205	-575	-603	106	23	2	81
Nov.	-2,813	-104	-748	-1,059	-524	-378	-83	2	-33	-52
Dec.	-2,983	79	-962	-431	-450	-1,219	1,114	2	44	1,068
2007 – Jan.	-5,505	-2,265	-1,444	-1,443	-524	170	259	-3	10	252
Feb.	-3,474	-892	-822	-1,209	-174	-377	266	-6	8	263
Mar.	-3,492	1,024	-1,079	-1,426	-579	-1,432	607	7	11	589
Apr.	-4,725	-635	-896	-2,095	-516	-584	-4	-8	..	5
May	-4,358	319	-209	-3,470	-541	-456	18	-18	-4	40
June	-1,103	1,360	14	-2,619	-685	827	-46	..	-10	-35
July	2,351	3,078	313	-230	-525	-285	35	21	-21	35
Aug.	-2,881	320	-1,053	-1,100	-459	-589	36	..	5	31
Sept.	-3,985	-591	-131	-1,394	-637	-1,232	500	3	-14	511
Oct.	-1,274	1,591	-82	-1,512	-797	-474	65	-47	1	111
Nov.	-3,884	693	-923	-2,502	-668	-485	153	-11	81	83
Dec.	-5,036	-1,061	-667	-675	-658	-1,975	784	-7	4	786
2008 – Jan.	-6,118	-2,753	-810	-1,675	-607	-273	322	9	23	290
Feb.	-3,416	771	-1,174	-2,228	-464	-321	275	17	-32	290
Mar.	-6,149	500	-1,116	-2,232	-958	-2,342	627	-4	-12	643
Apr.	-4,365	-347	-320	-2,310	-755	-633	22	-14	-6	43
May	-6,572	1,075	-562	-6,010	-557	-518	38	-4	1	41
June	(-3,592)	(223)	(220)	(-3,859)	….	….	(112)	….	….	….
July	(-114)	(2,921)	(561)	(-2,438)	….	….	(31)	….	….	….

Table A9

Lending by Italian banks by geographical area and sector (1)

(12-month percentage changes)

	General govern-ment	Finance and insurance companies	Non-financial corporations (a)		Households		Firms = (a) + (b)				Total
				under 20 employ-ees (2)	Producer (b) (3)	Consumer		Manufac-turing	Construc-tion	Services	
						Centre and North					
2007 – Mar.	4.8	13.7	11.1	4.1	6.3	8.6	10.7	4.7	14.4	12.1	10.3
June	4.8	9.8	11.5	4.2	5.5	8.1	10.9	5.7	14.7	10.5	9.8
Sept.	-0.1	7.7	12.7	5.5	5.7	8.5	12.1	7.1	15.3	12.1	10.1
Dec.	7.9	5.6	13.2	6.8	5.2	8.2	12.4	6.5	13.5	11.1	10.6
2008 – Mar.	6.0	14.2	13.1	7.1	3.9	5.3	12.3	8.6	13.3	10.6	11.0
June	8.7	5.7	12.3	6.9	2.3	3.1	11.4	7.5	11.5	11.3	9.0
Aug.	8.5	4.9	10.5	4.9	1.8	1.9	9.7	….	….	….	7.5
						South and Islands					
2007 – Mar.	-9.5	-1.7	17.2	9.0	9.6	12.7	15.8	13.8	21.2	18.1	12.9
June	2.5	4.4	15.4	9.4	9.2	12.0	14.3	11.3	20.9	16.2	12.6
Sept.	-3.8	-4.8	16.3	10.4	8.9	12.2	14.9	12.4	21.3	16.4	12.6
Dec.	-3.6	-7.0	10.8	9.8	6.6	10.5	10.1	7.3	18.5	9.7	9.2
2008 – Mar.	0.7	-3.8	11.0	9.7	5.0	6.0	9.9	6.1	17.5	9.5	7.9
June	-0.7	-0.8	11.4	8.6	3.6	2.9	10.0	4.5	15.2	11.4	6.7
Aug.	-0.2	7.6	10.9	7.5	2.1	3.2	9.4	….	….	….	6.4
						ITALY					
2007 – Mar.	2.5	13.2	11.8	4.8	7.1	9.4	11.3	5.8	15.5	12.8	10.7
June	4.4	9.7	12.0	5.0	6.4	9.0	11.4	6.4	15.7	11.2	10.2
Sept.	-0.7	7.4	13.1	6.1	6.5	9.3	12.4	7.7	16.3	12.7	10.4
Dec.	6.4	5.3	12.9	7.2	5.5	8.7	12.1	6.6	14.4	10.9	10.4
2008 – Mar.	5.4	13.7	12.8	7.5	4.2	5.5	11.9	8.3	14.0	10.5	10.5
June	7.4	5.6	12.2	7.1	2.6	3.0	11.2	7.2	12.1	11.4	8.7
Aug.	7.5	5.0	10.5	5.3	1.9	2.2	9.7	6.3	11.7	9.6	7.4

(1) Statistics for August 2008 are provisional; they include data for Cassa Depositi e Prestiti S.p.A. since October 2007. Loans do not include repurchase agreements, bad debts and some smaller items included in the Eurosystem harmonized definition. The breakdown by geographical area is according to customers' place of residence. Net of the effects of reclassification, exchange rate changes and other modifications not due to transactions. – (2) Limited partnerships and general partnerships with fewer than 20 employees. Informal associations, de facto companies and sole proprietorships with 6-19 employees. – (3) Informal associations, de facto companies and sole proprietorships with up to 5 employees.

Table A10

Financing of the general government borrowing requirement: Italy
(millions of euros)

	Currency and deposits		Short-term securities	Medium and long-term securities	MFI loans (1)	Other operations (1)		Borrowing requirement	
		of which: PO funds					*of which:* change in central bank current accounts		*of which:* financed abroad
2005	20,743	-4,177	-924	39,899	6,888	4,061	1,197	70,666	5,277
2006	7,476	-4,957	4,847	33,105	68,073	-54,677	-8,230	58,824	-7,013
2007	-13,977	-28,447	5,562	22,516	-2,525	14,779	13,142	26,355	-6,196
2005 – Q1	2,510	-516	11,204	45,886	1,198	-33,130	-34,293	27,666	1,288
Q2	12,725	149	9,287	20,745	1,952	-15,573	-14,842	29,136	3,536
Q3	2,758	-1,577	2,547	-19,414	346	29,464	28,813	15,701	424
Q4	2,751	-2,233	-23,963	-7,317	3,392	23,300	21,519	-1,837	29
2006 – Q1	10,657	-891	18,406	13,007	2,479	-11,612	-16,246	32,937	-19
Q2	1,162	-1,615	7,154	28,738	-627	-25,553	-26,568	10,872	724
Q3	232	-1,210	-7,819	5,993	56,493	-39,102	12,948	15,797	1,294
Q4	-4,575	-1,240	-12,893	-14,633	9,728	21,590	21,637	-783	-9,012
2007 – Q1	-1,537	-3,474	20,684	7,523	-256	-5,506	-5,753	20,907	-523
Q2	-16,496	-13,509	345	28,725	-2,077	-8,731	-8,936	1,766	2,499
Q3	-2,330	-8,550	3,074	-2,809	-1,121	7,061	5,459	3,875	-6,284
Q4	6,387	-2,914	-18,541	-10,923	930	21,955	22,372	-192	-1,888
2008 – Q1	1,313	-1,111	25,905	23,405	271	-33,145	-31,123	17,749	471
Q2	934	-1,266	8,186	-11,271	3,866	5,503	5,968	7,219	-5,659
2007 – Jan.	3,209	-263	12,347	-1,820	-96	-11,445	-11,383	2,195	-759
Feb.	-2,029	204	3,027	5,059	235	-3,549	-3,489	2,742	-291
Mar.	-2,718	-3,415	5,310	4,284	-395	9,488	9,120	15,970	528
Apr.	-4,256	-4,597	99	4,990	2,597	7,554	7,549	10,984	352
May	-3,081	-1,584	2,261	18,326	-2,704	-4,732	-5,066	10,069	506
June	-9,159	-7,329	-2,015	5,409	-1,971	-11,553	-11,419	-19,288	1,640
July	-203	-4,856	377	110	-301	-2,262	-3,963	-2,280	-2,647
Aug.	-1,558	-1,934	358	-728	-1,693	3,798	3,887	178	-448
Sept.	-569	-1,760	2,340	-2,191	872	5,526	5,534	5,977	-3,189
Oct.	-35	-580	5,213	5,095	385	-1,843	-1,859	8,817	70
Nov.	404	-1,152	-380	-5,344	1,635	8,634	8,860	4,949	460
Dec.	6,017	-1,182	-23,374	-10,674	-1,090	15,164	15,372	-13,958	-2,418
2008 – Jan.	3,013	-36	14,516	7,222	-125	-26,538	-26,389	-1,912	2,124
Feb.	-3,532	-659	4,821	1,657	-655	6,378	7,061	8,669	243
Mar.	1,833	-415	6,568	14,525	1,051	-12,986	-11,795	10,991	-1,896
Apr.	-1,102	-195	4,215	10,695	615	-2,738	-2,622	11,685	1,973
May	-1,248	-333	5,125	-19,457	1,016	23,157	23,334	8,592	-5,159
June	3,283	-738	-1,153	-2,508	2,235	-14,916	-14,744	-13,059	-2,472
July	-3,084	342	-2,111	11,941	-4,893	-7,052	-6,934	-5,199	-2,743

(1) As of September 2006 Cassa Depositi e Prestiti S.p.A. is included among MFIs; as of the same month its loans to general government bodies are included in the item “MFI loans”.

Table A11

General government debt: Italy

(millions of euros)

	Currency and deposits	*of which:* PO funds	Short-term securities	Medium and long-term securities	MFI loans (1)	Other liabilities (1)	General government debt	*of which:* in foreign currencies	*of which:* medium and long-term	*Memorandum item:* central bank current accounts
2005	149,530	70,578	117,460	1,129,206	61,393	55,190	1,512,779	27,255	1,259,069	14,634
2006	157,006	65,622	122,307	1,163,792	130,161	8,742	1,582,009	10,740	1,309,951	22,864
2007	143,029	37,175	127,869	1,190,060	127,635	10,379	1,598,971	3,465	1,333,206	9,721
2005 – Mar.	131,297	74,239	129,589	1,136,016	55,698	53,489	1,506,089	29,260	1,264,220	50,124
June	144,021	74,388	138,877	1,156,921	57,655	52,759	1,550,234	26,844	1,282,987	64,966
Sept.	146,779	72,811	141,424	1,136,390	58,000	53,409	1,536,003	26,634	1,261,537	36,153
Dec.	149,530	70,578	117,460	1,129,206	61,393	55,190	1,512,779	27,255	1,259,069	14,634
2006 – Mar.	160,186	69,687	135,868	1,142,223	63,869	59,824	1,561,971	22,314	1,276,935	30,880
June	161,349	68,072	143,025	1,172,123	63,240	60,839	1,600,577	18,375	1,303,923	57,449
Sept.	161,581	66,862	135,204	1,178,354	120,436	8,789	1,604,363	15,116	1,314,508	44,501
Dec.	157,006	65,622	122,307	1,163,792	130,161	8,742	1,582,009	10,740	1,309,951	22,864
2007 – Mar.	155,469	62,147	142,994	1,172,531	129,905	8,989	1,609,887	5,020	1,318,819	28,616
June	138,972	48,639	143,349	1,203,465	127,826	9,194	1,622,805	4,908	1,347,259	37,552
Sept.	136,642	40,089	146,422	1,200,306	126,705	10,796	1,620,871	4,678	1,344,939	32,094
Dec.	143,029	37,175	127,869	1,190,060	127,635	10,379	1,598,971	3,465	1,333,206	9,721
2008 – Mar.	144,342	36,064	153,806	1,214,012	127,906	8,357	1,648,423	3,236	1,354,915	40,845
June	145,276	34,799	161,980	1,204,704	131,771	7,892	1,651,623	3,214	1,345,624	34,877
2007 – Jan.	160,215	65,358	134,654	1,162,700	130,066	8,681	1,596,315	6,968	1,309,327	34,247
Feb.	158,186	65,562	137,682	1,168,341	130,300	8,620	1,603,129	6,845	1,314,355	37,736
Mar.	155,469	62,147	142,994	1,172,531	129,905	8,989	1,609,887	5,020	1,318,819	28,616
Apr.	151,213	57,551	143,094	1,177,513	132,501	8,993	1,613,314	4,907	1,323,782	21,067
May	148,131	55,967	145,358	1,196,808	129,797	9,327	1,629,422	4,960	1,342,998	26,133
June	138,972	48,639	143,349	1,203,465	127,826	9,194	1,622,805	4,908	1,347,259	37,552
July	138,769	43,782	143,726	1,204,116	127,525	10,894	1,625,031	4,837	1,349,253	41,515
Aug.	137,211	41,848	144,084	1,203,487	125,833	10,805	1,621,420	4,847	1,347,814	37,628
Sept.	136,642	40,089	146,422	1,200,306	126,705	10,796	1,620,871	4,678	1,344,939	32,094
Oct.	136,608	39,508	151,631	1,205,479	127,089	10,813	1,631,620	4,591	1,350,332	33,953
Nov.	137,012	38,357	151,251	1,200,385	128,725	10,587	1,627,959	3,490	1,344,929	25,093
Dec.	143,029	37,175	127,869	1,190,060	127,635	10,379	1,598,971	3,465	1,333,206	9,721
2008 – Jan.	146,042	37,139	142,390	1,198,086	127,511	10,230	1,624,259	3,431	1,341,429	36,111
Feb.	142,510	36,479	147,224	1,199,950	126,855	9,548	1,626,087	3,391	1,342,069	29,050
Mar.	144,342	36,064	153,806	1,214,012	127,906	8,357	1,648,423	3,236	1,354,915	40,845
Apr.	143,241	35,869	158,037	1,225,261	128,520	8,241	1,663,299	3,284	1,366,780	43,466
May	141,993	35,537	163,148	1,206,374	129,536	8,064	1,649,115	3,290	1,348,032	20,133
June	145,276	34,799	161,980	1,204,704	131,771	7,892	1,651,623	3,214	1,345,624	34,877
July	142,193	35,141	159,919	1,217,984	126,878	7,774	1,654,747	3,237	1,356,070	41,811

(1) As of September 2006 Cassa Depositi e Prestiti S.p.A. is included among MFIs; as of the same month its loans to general government bodies are included in the item “MFI loans”.